

STATE OF TENNESSEE  
TREASURER'S REPORT



Dale Sims, State Treasurer  
Fiscal Year Ended June 30, 2008

# 2008 TREASURER'S REPORT



Dale Sims, Treasurer  
State of Tennessee

Prepared by:

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# 2008

# Treasurer's Report

*The cover features the colors of the official flag of the State of Tennessee. The flag features three stars of pure white, representing the grand divisions of the state: East, Middle and West. They are bound together by the endless circle of the blue field, the symbol being three bound together in an indissoluble trinity. This flag was adopted as the official flag of the state of Tennessee by an act of the General Assembly passed and approved April 17, 1905.*

**This report is available in its entirety on the Internet at:  
[www.tn.gov/treasury/TreasurersAnnualReport.pdf](http://www.tn.gov/treasury/TreasurersAnnualReport.pdf)**



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LETTER OF TRANSMITTAL



State of Tennessee  
Treasury Department  
State Capitol  
Nashville, Tennessee 37243

December 31, 2008

The Honorable Phil Bredesen, Governor  
The Honorable Ron Ramsey, Speaker of the Senate  
The Honorable Jimmy Naifeh, Speaker of the House of Representatives  
Members of the General Assembly  
Citizens of the State of Tennessee

Ladies and Gentlemen:

Pursuant to the requirements of Section 4-4-114, *Tennessee Code Annotated*, I am pleased to transmit a report of the activity of the Treasury Department for the fiscal year ending June 30, 2008.

My staff and I appreciate your support and interest in the programs we administer and our efforts to serve all Tennesseans. We look forward to working with you to meet the challenges ahead in this new year.

Sincerely,

A handwritten signature in black ink that reads "Dale Sims".

Dale Sims

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## MISSION OF THE TREASURY DEPARTMENT

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### **Vision Statement**

To be faithful stewards of the state's financial and human resources. To be passionate about achieving our mission and living by our core values.

### **Mission Statement**

We will be a leader by providing exceptional service to our customers honestly, efficiently, and effectively.

### **Treasury Team Commitment**

In order for us to provide exceptional service, both management and employees will foster an environment that respects, challenges, motivates, and rewards each team member. Each of us has a responsibility to develop and maintain this environment so that, together, we can achieve our mission and live by our core values.

### **Department Core Values**

*Impeccable Honesty:* We will develop relationships and interact with one another and with our customers in a manner that fosters and encourages trust. We will maintain the highest ethical and professional standards in everything that we do.

*Mutual Respect:* We will treat everyone equitably and with honor. We will communicate in a manner that promotes open dialogue with our customers, within the department, and with our peers in state government.

*Continuous Improvement:* We will continually challenge ourselves to improve the level of service that we provide by being innovative, collaborative, creative, and efficient. We will work to be the best at what we do.

*Shared Accountability:* We will work as a team and will purposely strive to leverage the strengths and overcome the weaknesses of each team member. We will accept responsibility individually and collectively for the service that we provide to our customers.

*Exceptional Service:* We will be innovative in how we provide services to our customers and in how we do our work. We will be relentless in our pursuit of quality and excellence in everything that we do. We will focus not only on solving customers' problems, but also anticipating their needs.

*Exemplary Leadership:* We will be visionary leaders and positive role models for our peers. We strive to be highly respected both inside and outside state government.

## EXECUTIVE SUMMARY

The 2008 Treasurer's Report contains reports on various programs administered by the Treasury Department, including the Baccalaureate Education System Trust, the Careers Now Program, the Chairs of Excellence Program, Claims Administration, the Tennessee Claims Commission, the Deferred Compensation Program, the Flexible Benefits Plan, Investments, Risk Management, the Small and Minority Owned Business Assistance Program, the Tennessee Consolidated Retirement System, and the Unclaimed Property Program. The following comments represent a brief statement of the purpose and operations of programs administered by the department. The remainder of this report gives detailed data regarding the activities of these programs during the 2008 fiscal year.

The Baccalaureate Education System Trust, BEST, is a Section 529 qualified tuition program that allows anyone to pay for higher education costs in advance on behalf of a beneficiary. BEST provides two tax-favored savings vehicles: The Prepaid College Tuition Plan and the Savings Plan. The Prepaid College Tuition Plan (Educational Services Plan), introduced in 1997, is based on the weighted average tuition inflation increases at Tennessee's four-year public universities. Through the purchase of affordable tuition units, Tennesseans can pay for future tuition at today's price and ease their concerns about whether they will have enough funds to pay for their children's higher education. At June 30, 2008, BEST held 8,941 contracts with net assets totaling \$90.1 million. Tennessee endorses the Path2College 529 Savings Plan through a contractual agreement with the State of Georgia. The Path2College 529 Savings Plan offers seven investment options, and fees ranging from 50-76 basis points.

The Careers NOW Program provides Tennessee college students the opportunity to learn more about the operations of state government and career opportunities by working in one of the three constitutional offices for a semester. Since the inception of the program in 1996, over 255 students have participated in the program.

The University of Tennessee Institute for Public Service administers the "County Official's Certificate Training Program Act." Certain full-time county officers are eligible for an educational incentive payment if the officers have completed the continuing education requirements of the program. The UT Institute for Public Service is required to provide the Treasurer's office a listing of those officers who have successfully completed all levels of the County Officials Certificate Training Program.

The Chairs of Excellence Trust is a permanent trust fund authorized in 1984 to further the cause of higher education in Tennessee. The funding of the program is provided through contributions made by a private donor and a matching amount by the state, thus, creating a chair. Income from the chair is used to offset the cost of retaining a nationally or regionally recognized scholar at a state college or university who teaches in a specified academic area. Since 1984, a total of 99 chairs have been created. The Trust totaled \$236.9 million fair value of net assets at June 30, 2008.

The Division of Claims Administration is responsible for investigating and making determinations on claims made against the state for workers' compensation by state employees, employee property damage, tort liability and criminal injury compensation. Staff support from the Division of Claims Administration also assists the Board of Claims. The Division of Claims Administration received 4,710 claims for tort, employee property damage and workers' compensation. Payments made during the year for workers' compensation, tort, and employee property damage claims totaled \$27.5 million. The division received 4,282 criminal injury, drunk driver, and sexual

**INTRODUCTION****BACCALAUREATE  
EDUCATION  
SYSTEM TRUST  
(BEST)****CAREERS NOW  
PROGRAM****CERTIFIED PUBLIC  
ADMINISTRATOR****CHAIRS OF  
EXCELLENCE****CLAIMS  
ADMINISTRATION**

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**EXECUTIVE SUMMARY**

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assault forensic exam claims. Payments made totaled \$13.6 million. Since the first payments were issued in 1982, more than \$189 million has been paid to crime victims.

**CLAIMS  
COMMISSION**

The Tennessee Claims Commission is an administrative tribunal created to determine monetary claims against the State of Tennessee. There are three commissioners, one from each grand division of the state. At June 30, 2008, the commission had 596 open claims (including claims transferred to administrative law judges).

**DEFERRED  
COMPENSATION  
PROGRAM**

The State of Tennessee Deferred Compensation Program offers state employees the opportunity to accumulate supplemental retirement income on a tax advantaged basis. Participants may direct the investment of their deferred salary into a variety of investment products contracted for the program. During the fiscal year, the state, the University of Tennessee and Board of Regents each matched their employees' contributions to the 401(k) plan at \$50 per month. As of June 30, 2008, a total of 81,033 state and higher education employee accounts were held in the program. The market value of accumulated account balances totaled \$1.2 billion.

**FLEXIBLE  
BENEFITS PLAN**

The State of Tennessee Flexible Benefits Plan is an optional benefit plan which enables state employees to pay for certain expenses with before-tax dollars. At June 30, 2008, 44,542 state employees were using the plan: 43,398 paid group medical premiums, 26,914 paid group dental premiums, 4,767 used the medical expense reimbursement account and 418 used the dependent care reimbursement account. The plan generated over \$6.9 million in F.I.C.A. savings for the state during the 2008 fiscal year. Employees realized similar savings. The state's F.I.C.A. savings are used to fund the state wellness program and to help fund a portion of the 401(k) match for state employees.

**INVESTMENTS**

The Investment Division has the responsibility for investing all funds under management of the Treasury Department.

State Cash Management - This division manages the State Pooled Investment Fund which includes the state's cash, the various dedicated reserves and trust funds of the state, and the Local Government Investment Pool. During 2008, investments averaged \$8.1 billion, producing \$326.2 million in income for an average rate of return of 4.13%. The State Trust of Tennessee allows the department to use the Federal Reserve Wire Transfer System to transfer funds on a limited basis.

Pension Fund Investments - This division manages the investments of the Tennessee Consolidated Retirement System (TCRS) which, at June 30, 2008, totaled \$31.6 billion at fair market value. For the year, investment losses of (\$430) million were recognized, for a rate of return of (1.21%) on a fair value basis. The Investment Division also manages investments for the Chairs of Excellence Trust and the Baccalaureate Education System Trust which, at June 30, 2008, had market values of \$236.9 million and \$90.1 million, respectively.

**RISK  
MANAGEMENT**

The Division of Risk Management is responsible for identifying the state's exposure to property and casualty risks, and determining the appropriate risk control methods to protect the state against monetary loss due to unforeseen events. The division administers the state's Property/Casualty Insurance Program, including the procurement of all-risk, replacement cost property insurance for all state-owned buildings and contents, builders' risk insurance for new construction, fire

## EXECUTIVE SUMMARY

arts insurance to protect all types of valuable artwork and items of antiquity, boiler insurance and inspection services for all state-owned boiler objects, and fidelity and crime coverage to protect against employee dishonesty. The State procures its insurance with the aid of a qualified property/casualty insurance broker. This year, an RFP was issued for an Aviation Insurance Broker to procure insurance for the State's 51 aircraft. The new broker will obtain the proper coverages for the current policy year beginning November 1, 2008. Loss prevention and control services are also provided for workers' compensation and tort liability. As of July 1, 2008, the State's total insured property values were \$16.5 billion. A total of \$11 million in annual aggregate deductible retentions were funded through the Risk Management Fund. The State's property insurance carrier will indemnify the State for every covered loss that exceeds the annual aggregate deductible, after the per occurrence, or working deductible, has been assumed by the agency that suffered the loss.

The Small and Minority-Owned Business Assistance Program is responsible for supporting outreach to new, expanding and existing businesses unable to derive benefit from conventional means of monetary resources and insight provided by traditional lenders and financial advisors. The Program consists of two components: Loans and Program Services. The loans provided must be for a specific project, however, acceptable purposes for loan proceeds can include acquisition of machinery and equipment; working capital; supplies and materials; inventory and certain other business-related activity. Program Services include technical assistance, education and consulting services to facilitate support in the areas of strategy, planning and financial management. These Program components are deemed essential resources that will enable and enhance growth of the State's small business segment. The principle function of the Small and Minority-Owned Business Assistance Program is to provide a significant statewide platform through a support structure that fosters the expansion of small and minority-owned businesses.

**SMALL AND  
MINORITY-OWNED  
BUSINESS  
ASSISTANCE  
PROGRAM**

The Tennessee Consolidated Retirement System provides retirement coverage to state employees, higher education employees, teachers, and employees of political subdivisions that have elected to participate in the plan. As of June 30, 2008, there were 215,645 active TCRS members: 48,214 state employees; 72,140 K-12 teachers; 77,878 political subdivision employees; and 17,413 higher education employees. As of June 30, 2008, there were 102,306 retirees. TCRS paid \$1.33 billion in benefits during fiscal year 2008. The state of Tennessee is responsible for the pension liability for state employees and higher education employees and funds a significant portion of the retirement liability for teachers through the BEP. Each participating political subdivision is responsible for the liability of its employees.

**TENNESSEE  
CONSOLIDATED  
RETIREMENT  
SYSTEM**

The Unclaimed Property Division administers the state's Uniform Disposition of Unclaimed Property Act. Under this act, the state provides one centralized location for the owners of abandoned property, or their heirs, to turn to when searching for checking accounts, savings accounts, insurance policies, utility deposits and securities. During the fiscal year, \$80.4 million of unclaimed property was collected, which consisted of \$52.3 million that was remitted to Treasury and \$28.1 million in the sale of securities. In addition, \$22.4 million was returned to owners or their heirs, local governments and other states. Since the program's inception in 1979, \$552.2 million in unclaimed property has been reported to the Treasury and \$175.6 million of that property has been returned to claimants.

**UNCLAIMED  
PROPERTY  
DIVISION**

**TREASURY NUMBERS AT A GLANCE**  
**FISCAL YEAR 2008**

<b>ADMINISTRATIVE</b>	Number of Filled Positions	211
	Payroll Expenditures	\$ 14,467,383
	Other Expenditures	\$ 5,598,637
	Total Administrative Expenditures	\$ 20,066,020
<b>CASH MANAGEMENT PROGRAM</b>	General Fund Earnings	\$ 106,649,405
	LGIP Earnings	\$ 128,770,186
	Restricted Fund Earnings	\$ 90,758,041
	Total Cash Management Earnings	\$ 326,177,632
<b>RETIREMENT PROGRAM</b>	Retirement Benefits	\$ 1,332,715,640
	Number of Retirees	102,306
	Number of Active Members	215,645
	Retirement Contributions	\$ 1,084,112,872
	Retirement Net Investment Income	\$ (430,058,924)
<b>CLAIMS ADMINISTRATION PROGRAM</b>	Workers' Compensation Payments	\$ 20,942,899
	Workers' Compensation Claims Filed	3,250
	Employee Property Damage Payments	\$ 28,266
	Employee Property Damage Claims Filed	141
	Tort Payments	\$ 6,509,611
	Tort Claims Filed	1,319
	Criminal Injury Fund Payments	\$ 13,631,241
Criminal Injury Fund Claims Filed	4,282	
<b>RISK MANAGEMENT PROGRAM</b>	Estimated Gross Property Losses Incurred	\$ 9,325,200
	Total Property Values Insured	\$ 16,500,000,000
<b>CHAIRS OF EXCELLENCE PROGRAM</b>	Chairs of Excellence Investment Income	\$ (7,631,048)
	Chairs of Excellence Expenditures	\$ 7,861,506
	Number of Chairs of Excellence	99
<b>OTHER PROGRAMS</b>	Deferred Compensation Contributions	\$ 143,000,801
	Deferred Compensation Accounts	81,033
	Flexible Benefits Plan Payments	\$ 8,083,852
	Unclaimed Property Revenues	\$ 80,471,524
	Unclaimed Property Payments	\$ 22,428,973
	BEST Prepaid Accounts	8,941
BEST Prepaid Contributions (net of fees)	\$ 4,933,806	
<b>FAIR VALUE OF ASSETS UNDER MANAGEMENT AT JUNE 30, 2008</b>	Retirement Trust Fund	\$ 31,634,129,482
	Chairs of Excellence Trust Fund	\$ 236,954,830
	State Pooled Investment Fund	\$ 8,684,378,183
	Deferred Compensation (outside managers)	\$ 1,217,853,524
	Best Educational Services Plan	\$ 90,054,949
	Total Assets Under Management	\$ 41,863,370,968

# TREASURER'S REPORT

*Employee Benefits*

TENNESSEE CONSOLIDATED RETIREMENT SYSTEM

TENNESSEE CONSOLIDATED RETIREMENT SYSTEM

The Tennessee Consolidated Retirement System (TCRS) was established July 1, 1972. Prior to this date, there were seven different public employee retirement systems. The TCRS, a defined benefit plan which is qualified under 401(a) of the Internal Revenue Code, is a retirement system for state employees, higher education employees, teachers, and local government employees.

MEMBERSHIP

Membership in the retirement system is a condition of employment for full-time state employees, teachers, general employees in higher education, and the employees of local governments that participate in TCRS. Membership is optional for certain part-time employees. Faculty employees in higher education may participate in either TCRS or an Optional Retirement Program (ORP), which is a defined contribution plan designed for faculty employees in institutions of higher education. When an employee joins TCRS, he receives an introductory letter and

membership pamphlet outlining various aspects of retirement membership.

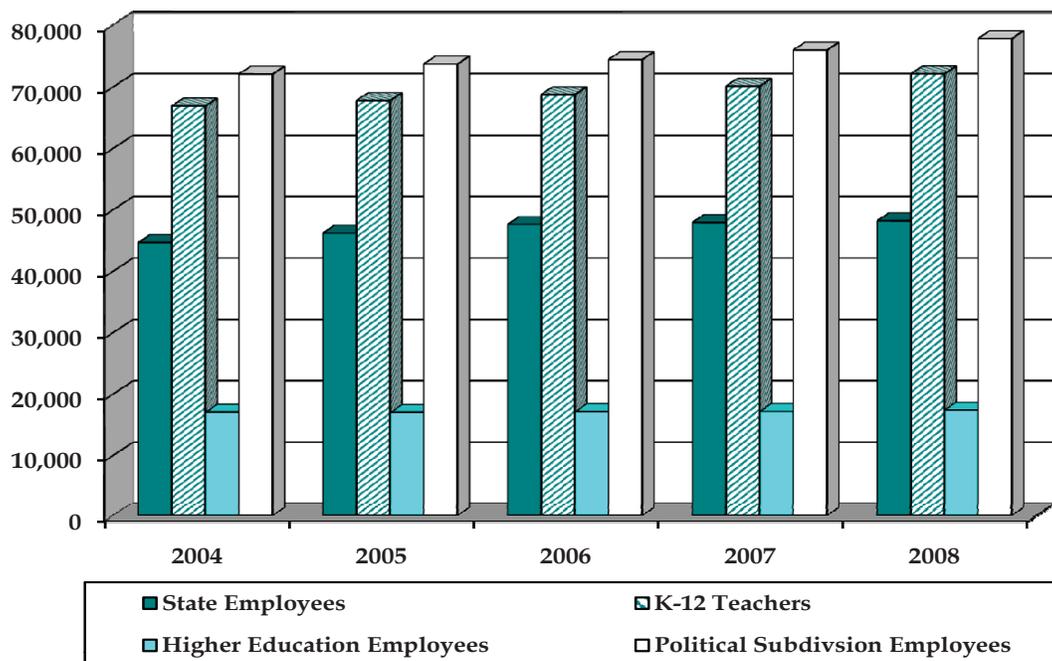
State employees and teachers become vested after five years of service. Political subdivision members attain vested status upon completion of 10 years unless five year vesting has been authorized. A vested member is guaranteed a retirement benefit once the age requirements are met.

As of June 30, 2008, there were 215,645 active members of TCRS and 11,167 higher education employees participating in the ORP.

Since July 1, 1976, all new members of the TCRS except state judges have been classified as Group I members. State judges have been permitted to enroll in Group IV since September 1, 1990. From July 1, 1972 to June 30, 1976, all employees were classified as Group I, with the exception of state policemen, wildlife officers, firemen and policemen who were classified as Group II, and judges and elected officials who were classified as Group III. Members of seven superseded systems are permitted to retain their original rights and benefits.

ACTIVE MEMBERS

Fiscal Years 2004-2008



## TENNESSEE CONSOLIDATED RETIREMENT SYSTEM

### CONTRIBUTIONS

The funding of retirement benefits is financed by member contributions, employer contributions, and the earnings of the invested assets. Effective July 1, 1981, the employee contributions of certain state employees and higher education employees were assumed by the state. Local governments can also adopt these noncontributory provisions for their employees. Group I K-12 teachers and contributory local government employees contribute to TCRS at the rate of 5% of gross salary. Employee contribution rates vary for superseded classifications.

Effective January 1, 1987, all state employees and teachers who contribute a portion of their income to the retirement system became covered by Section 414(h) of the Internal Revenue Code. Under 414(h), payment of federal income tax on an employee's retirement contributions is deferred until these contributions are withdrawn in the form of a refund or monthly benefit payments. Political subdivisions may pass a resolution adopting Section 414(h) coverage for their employees.

Upon termination of employment, a member may elect to withdraw his contributions and accumulated interest from the retirement system in a lump sum.

By obtaining a lump sum refund, a member waives all rights and benefits in the retirement system. A vested member may leave his account balance in TCRS and apply for benefits upon meeting the age requirements. A non-vested member who terminates employment may only leave his account balance in TCRS for up to seven years. During the 2008 fiscal year, 6,569 refunds totaling \$37.7 million were issued.

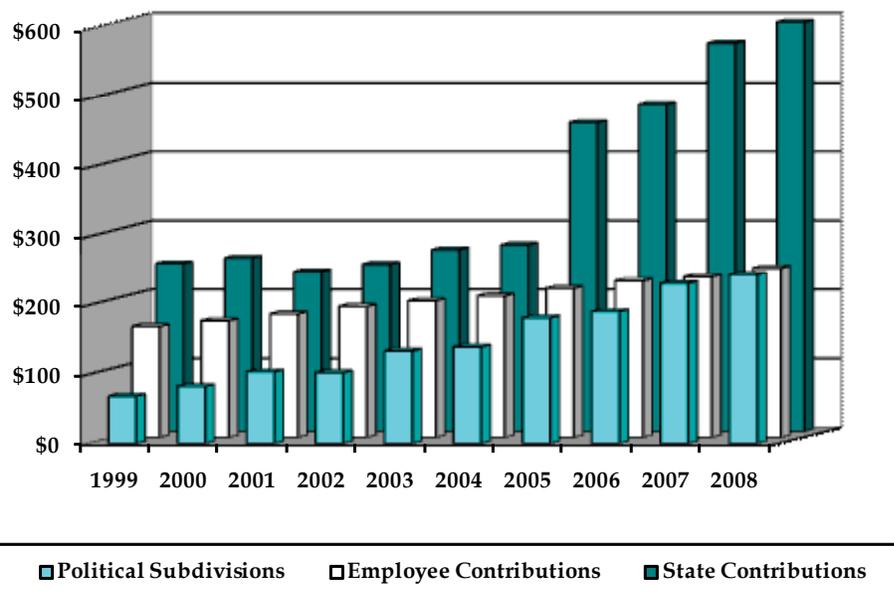
The contribution rate for the employers participating in the retirement system is determined by a biennial actuarial valuation performed by an independent actuarial firm. The contribution rates include funding for the basic benefit, the cost-of-living increase provisions, and amortization of the accrued liability over a 40 year period which began in July of 1975. The employer contribution rates for the year ending June 30, 2008 were as follows:

Noncontributory State and Higher Education Employees	13.62%
K-12 Teachers	6.24%
Political Subdivisions Individually Determined Faculty Members Electing to Participate in the ORP	10.0%*

\*11% for salary above the social security wage base.

### RETIREMENT CONTRIBUTIONS

*Fiscal Years 1999-2008  
Expressed in Millions*



TENNESSEE CONSOLIDATED RETIREMENT SYSTEM

**RETIREMENT BENEFITS**

The benefits provided by TCRS are designed, when combined with the benefit payable from social security, to allow career employees to maintain their standard of living at retirement.

As of June 30, 2008, 102,306 retirees were receiving monthly benefit payments. This represents a 4% increase over the previous year.

Group I state employees and teachers become eligible to retire from the TCRS at age 60 with five years of service or at any age with 30 years of service. State employees and teachers become vested after five years of service. Political subdivision members attain vested status upon completion of 10 years unless five year vesting has been authorized. Retirement benefits are based on the average of the member's five highest consecutive years of salary and the years of creditable service. A reduced retirement benefit is available to vested members at age 55 or upon completion of 25 years of service.

A Group I Benefits calculator is available on the program's Internet site: <http://www.tn.gov/treasury/tcrs>.

Disability benefits are available to active members with five years of service who become disabled and can not engage in gainful employment. There is no service requirement for disability benefits paid to active members whose disability is a result of an accident or injury occurring while the member was in the performance of duty.

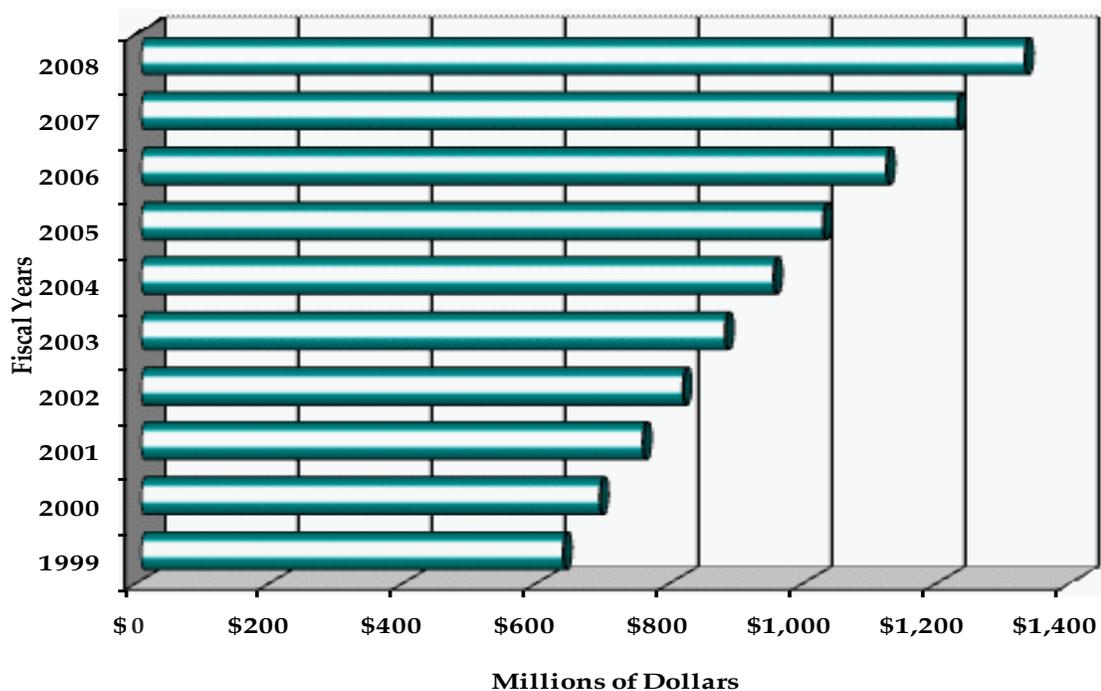
Cost-of-living adjustments after retirement are based on the Consumer Price Index (CPI). If there is an increase in the CPI of as much as .5% in any calendar year, the retired member's benefit will be adjusted by an amount equal to the increase in the CPI, not to exceed 3% nor be less than 1%.

Certain death benefits are available to the beneficiary(s) of a member who dies prior to retirement. At retirement, a member may select an optional benefit that is actuarially reduced so that his beneficiary may continue to receive a benefit after his death.

Benefits paid in fiscal year 2008 totaled \$1.33 billion, an increase of \$100 million over 2007 benefit payments.

**ANNUAL BENEFIT PAYMENTS**

*Fiscal Years 1999-2008  
Expressed in Millions*



TENNESSEE CONSOLIDATED RETIREMENT SYSTEM

TENNESSEE'S RETIREMENT PROGRAM, TCRS AND SOCIAL SECURITY BENEFITS  
for Calendar Year 2008

Five-Year AFC*	Projected Annual Retirement Income	15 Years Service	% of AFC	20 Years Service	% of AFC	25 Years Service	% of AFC	30 Years Service	% of AFC	35 Years Service	% of AFC
\$15,000	TCRS	\$ 3,544		\$ 4,725		\$ 5,906		\$ 7,088		\$ 8,269	
	Social Security	9,048		9,048		9,048		9,048		9,048	
	Total	\$ 12,592	83.9%	\$ 13,773	91.8%	\$ 14,954	99.7%	\$ 16,136	107.6%	\$ 17,317	115.4%
\$20,000	TCRS	\$ 4,725		\$ 6,300		\$ 7,875		\$ 9,450		\$ 11,025	
	Social Security	10,572		10,572		10,572		10,572		10,572	
	Total	\$ 15,297	76.5%	\$ 16,872	84.4%	\$ 18,447	92.2%	\$ 20,022	100.1%	\$ 21,597	108.0%
\$25,000	TCRS	\$ 5,906		\$ 7,875		\$ 9,844		\$ 11,813		\$ 13,781	
	Social Security	12,096		12,096		12,096		12,096		12,096	
	Total	\$ 18,002	72.0%	\$ 19,971	79.9%	\$ 21,940	87.8%	\$ 23,909	95.6%	\$ 25,877	103.5%
\$30,000	TCRS	\$ 7,088		\$ 9,450		\$ 11,813		\$ 14,175		\$ 16,538	
	Social Security	13,632		13,632		13,632		13,632		13,632	
	Total	\$ 20,720	69.1%	\$ 23,082	76.9%	\$ 25,445	84.8%	\$ 27,807	92.7%	\$ 30,170	100.6%
\$35,000	TCRS	\$ 8,269		\$ 11,025		\$ 13,781		\$ 16,538		\$ 19,294	
	Social Security	15,156		15,156		15,156		15,156		15,156	
	Total	\$ 23,425	66.9%	\$ 26,181	74.8%	\$ 28,937	82.7%	\$ 31,694	90.6%	\$ 34,450	98.4%
\$40,000	TCRS	\$ 9,450		\$ 12,600		\$ 15,750		\$ 18,900		\$ 22,050	
	Social Security	16,680		16,680		16,680		16,680		16,680	
	Total	\$ 26,130	65.3%	\$ 29,280	73.2%	\$ 32,430	81.1%	\$ 35,580	89.0%	\$ 38,730	96.8%
\$45,000	TCRS	\$ 10,631		\$ 14,175		\$ 17,719		\$ 21,263		\$ 24,806	
	Social Security	18,204		18,204		18,204		18,204		18,204	
	Total	\$ 28,835	64.1%	\$ 32,379	72.0%	\$ 35,923	79.8%	\$ 39,467	87.7%	\$ 43,010	95.6%
\$50,000	TCRS	\$11,813		\$ 15,750		\$ 19,688		\$ 23,625		\$ 27,563	
	Social Security	19,536		19,536		19,536		19,536		19,536	
	Total	\$31,349	62.7%	\$ 35,286	70.6%	\$ 39,224	78.4%	\$ 43,161	86.3%	\$ 47,099	94.2%
\$55,000	TCRS	\$ 13,128		\$ 17,504		\$ 21,879		\$ 26,255		\$ 30,631	
	Social Security	20,244		20,244		20,244		20,244		20,244	
	Total	\$ 33,372	60.7%	\$ 37,748	68.6%	\$ 42,123	76.6%	\$ 46,499	84.5%	\$ 50,875	92.5%
\$60,000	TCRS	\$ 14,506		\$ 19,341		\$ 24,176		\$ 29,012		\$ 33,847	
	Social Security	20,940		20,940		20,940		20,940		20,940	
	Total	\$ 35,446	59.1%	\$ 40,281	67.1%	\$ 45,116	75.2%	\$ 49,952	83.3%	\$ 54,787	91.3%
\$65,000	TCRS	\$ 15,884		\$ 21,179		\$ 26,473		\$ 31,768		\$ 37,062	
	Social Security	21,564		21,564		21,564		21,564		21,564	
	Total	\$ 37,448	57.6%	\$ 42,743	65.8%	\$ 48,037	73.9%	\$ 53,332	82.0%	\$ 58,626	90.2%
\$70,000	TCRS	\$ 17,262		\$ 23,016		\$ 28,770		\$ 34,524		\$ 40,278	
	Social Security	22,164		22,164		22,164		22,164		22,164	
	Total	\$ 39,426	56.3%	\$ 45,180	64.5%	\$ 50,934	72.8%	\$ 56,688	81.0%	\$ 62,442	89.2%

\* Average Final Compensation (AFC)

This chart is based on a date of retirement in 2008. Social security benefits have been calculated by Bryan, Pendleton, Swats & McAllister, actuarial consultants for the TCRS, utilizing the following assumptions:

- (1) retirement is taking place at age 65 in 2008;
- (2) the retiree has worked a full career (TCRS plus other employers, if necessary) of 35 years or more; and
- (3) salary increases throughout the retiree's career have followed the same pattern as National Average Earnings.

The department's Internet benefits calculator allows members to receive an immediate estimate: [www.tn.gov/treasury/tcrs](http://www.tn.gov/treasury/tcrs)

## TENNESSEE CONSOLIDATED RETIREMENT SYSTEM

**ACTUARIAL VALUATION**

An actuarial valuation of the TCRS is performed by an independent actuarial firm every two years. The purpose of the valuation is to determine the funding requirements for the employers participating in the TCRS. The latest valuation was performed July 1, 2007 to establish the employer contribution rates for July 1, 2008. The system's accrued liability at July 1, 2007 was \$1.6 billion. The state and teacher accrued liability is being amortized over a 20 year period. The amortization period for local governments varies by entity.

In addition to the biennial actuarial valuation, an experience study is conducted every four years for the purpose of establishing actuarial and economic assumptions to be used in the actuarial valuation process. Following are the assumptions used in the July 1, 2007 actuarial valuation of the plan:

***Economic Assumptions***

- (1) 7.5% annual return on investments
- (2) Graded salary scale reflecting plan experience
- (3) 3.5% annual increase in social security wage base

***Actuarial Assumptions***

- (1) Pre-Retirement mortality based on age and sex
- (2) Post-Retirement mortality based on age
- (3) Disability rate based on age
- (4) Turnover rate based on age and length of service
- (5) Retirement age distribution based on age and service

**POLITICAL SUBDIVISIONS**

Political subdivisions may participate in the TCRS if the chief governing body passes a resolution authorizing coverage and accepting the liability associated with the coverage. Each political subdivision is responsible for the retirement cost of its employees and, in addition to employer contributions, pays the TCRS a fee for TCRS administration.

**POLITICAL SUBDIVISION PARTICIPATION**

Participation as of June 30, 2008:

Cities	177
Counties	89
Utility Districts	59
Special School Districts	19
Joint Ventures	23
Housing Authorities	11
911 Emergency Communication Districts	41
Miscellaneous Authorities	<u>54</u>
Total	<u>473</u>

**TENNESSEE CONSOLIDATED RETIREMENT SYSTEM**

**MAJOR LEGISLATIVE IMPROVEMENTS**

- 1972** Benefit formula improved from 1.12% of salary up to the SSIL to 1.5% of salary up to the SSIL.
- 1973** Annual cost-of-living increase based on the CPI with a cap of 1.5% adopted for retirees.
- 1974** Disability retirement eligibility requirement reduced from 10 years to 5 years of service.  
  
Maximum annual cost-of-living increase raised to 3%.  
  
Provision to increase retirees' benefits whenever the benefit formula is improved.  
  
Service credit authorized for unused accumulated sick leave.
- 1976** Service retirement eligibility requirements reduced from age 65 or 35 years of service to age 60 or 30 years of service.  
  
Early retirement eligibility requirements reduced from age 60 or 30 years of service to age 55.
- 1978** A bonus cost-of-living increase granted to retirees at a lump-sum cost of \$15.3 million.  
  
An optional retirement plan established for teachers in the Board of Regents system.
- 1980** Death benefits for members dying in-service with 10 years of service improved by offering a 100% joint and survivor annuity of the member's accrued benefit for the spouse.
- 1981** Noncontributory retirement for state employees and higher education employees adopted. Employees' contributions, up to 5%, were assumed by the state.
- 1983** An actuarially reduced retirement benefit at any age with 25 years of service authorized.
- 1984** Credit for out-of-state service for the purpose of determining retirement eligibility authorized.  
  
Retirement credit for armed conflict approved.  
  
Part-time employees permitted to participate in TCRS and members allowed to establish credit for previous part-time employment.
- 1985** \$22 million ad-hoc increase granted to retirees.

- 1987** Service credit for half of peacetime military service made available.  
  
\$17 million ad-hoc increase granted to retirees.  
  
Retirement incentive for state employees.  
  
Section 414(h) of the IRC adopted, allowing employee contributions to be made on a tax-deferred basis.
- 1990** Retirement incentive for state employees.
- 1991** 3.6% indexing of salaries for noncontributory employees extended one year. Each succeeding year up to 1997, the 3.6% indexing was extended. In 1997, it was extended indefinitely.
- 1992** Minimum number of years required to qualify for retirement was reduced from 10 to 5 years.
- 1993** Salary portability for service in different classifications authorized effective January 1, 1994.  
  
Benefit improvement up to 5% authorized.
- 1997** Compounded COLA for retirees approved.
- 1998** Group 2 and 3 service requirements amended to permit service retirement with 30 years of service, regardless of age.  
  
Group 1 and Prior Class C benefit limitations increased to 80%.  
  
Mandatory retirement established with supplemental bridge benefit for all state public safety officers.
- 1999** Group 1 benefit maximum increased to 90%.
- 2000** Group 2 benefit maximum increased to 80%.
- 2001** Line of Duty Death Benefits adopted to guarantee a minimum \$50,000 death benefit.
- 2005** Return to work statutes were reformed, including a temporary employment increase to 120 days.
- 2006** Ad-hoc increase granted to members retired prior to 1989.
- 2007** Public Safety Officer benefits were enhanced.

## TENNESSEE CONSOLIDATED RETIREMENT SYSTEM

**SOCIAL SECURITY**

The Old Age & Survivors Insurance Agency (OASI) administers Section 218 of the federal Social Security Act for Tennessee public employees. This section relates to coverage agreements and modifications as well as to coverage determinations.

Prior to 1951, social security coverage was not available to public employees. Amendments to the Social Security Act made in 1950 allowed certain groups of state and local government employees who were not covered by an employer-sponsored retirement plan to voluntarily participate in social security. Amendments made in 1954 allowed coverage for public employees who were covered by an employer-sponsored retirement plan if federal referendum requirements are met.

The Tennessee Master Agreement was executed on August 16, 1951. It provided full social security coverage (retirement, survivors, disability, and hospital insurance) to public employees who were not

covered by an employer-sponsored retirement plan. A modification to the agreement, effective January 1, 1956, provided social security coverage to employees serving in positions which were then covered by the Tennessee State Retirement System and the Tennessee Teachers' Retirement System. After the Tennessee Consolidated Retirement System was established July 1, 1972, a statewide social security coverage referendum was held among eligible employees.

The 1985 Budget Reconciliation Act mandated Medicare hospital insurance coverage for public employees hired after March 31, 1986 who do not have full social security coverage. The Omnibus Budget Reconciliation Act of 1990 (OBRA) generally mandated full social security coverage for state and local government employees who are not covered by an employer-sponsored retirement plan.

Effective in 1991, separate wage bases were implemented for social security and Medicare and separate reporting of withholding was required.

**SCHEDULE OF HISTORICAL SOCIAL SECURITY CONTRIBUTION RATES**

Calendar Year	Employee Rate	Employer Rate	Social Security Wage Base	Medicare Wage Base
2008	7.65%	7.65%	\$ 102,000	No Limit
2007	7.65	7.65	97,500	No Limit
2006	7.65	7.65	94,200	No Limit
2005	7.65	7.65	90,000	No Limit
2004	7.65	7.65	87,900	No Limit
2003	7.65	7.65	87,000	No Limit
2002	7.65	7.65	84,900	No Limit
2001	7.65	7.65	80,400	No Limit
2000	7.65	7.65	76,200	No Limit
1999	7.65	7.65	72,600	No Limit

## DEFERRED COMPENSATION PROGRAM

### DEFERRED COMPENSATION PROGRAM

The Deferred Compensation Program is a voluntary program designed to provide state employees with the opportunity to accumulate supplemental retirement income on a tax advantaged basis. Participants may postpone income taxes on contributions and earnings by agreeing to defer receipt of a portion of their current income until retirement. For fiscal year 2007 the 401(k) Plan began offering employees a designated Roth 401(k) after tax contribution option as payroll systems accommodate this change. The contributions are made after tax and the distributions are tax advantaged subject to timing restrictions. The University of Tennessee is the first payroll system to accommodate the Roth contributions.

This program offers employees two plans. The 457 plan was implemented in the 1981-82 fiscal year and the 401(k) plan was implemented in the 1983-84 fiscal year. In accordance with changes to *Internal Revenue Code Section 457*, the state's 457 plan was converted to a trust effective January 1, 1999.

As of June 30, 2008, accounts were held by 75,393 individuals in the 401(k) plan and 5,640 individuals in the 457 plan. At fiscal year end, 35,019 state employees, 10,008 University of Tennessee employees, and 11,716 Tennessee Board of Regents employees were actively contributing to the 401(k) plan and 2,391 state employees, 503 University of Tennessee employees, and 371 Tennessee Board of Regents employees were actively contributing to the 457 plan.

The program is used by state employees of all ages and salary levels. The majority of active contributors are under age 50 and earn below \$36,000 per year.

IRS regulations for 2008 allow a maximum deferral in the 457 plan of 100% of compensation up to the maximum annual contribution of \$15,500. The maximum deferral in the 401(k) plan is 100% of compensation up to the maximum annual contribution of \$15,500. Participants who also use a 403(b) plan are subject to additional limits. Participants age 50 and older are eligible to make additional deferrals.

During the 2008 fiscal year, the state, the Tennessee Board of Regents and the University of Tennessee

each matched their employees' contributions to the 401(k) plan at \$50 per month as authorized by the General Assembly. The amount contributed by the state during the year was \$30.8 million. Employees contributed \$111.7 million.

Participants in the program at June 30, 2008 directed the investment of their deferred salary to the Regions Bank Time Deposit Account, ING's Fixed Account, Calvert's Income Fund, State Street Bank & Trust's S&P 500 Index Fund, Fidelity Investments' Magellan Fund, Puritan Fund, OTC Portfolio, Contrafund, International Growth and Income Fund, and Government Money Market Portfolio. Investment options added in 2008 include: Dimensional Fund Advisors (DFA) International Fund, Fidelity Small Cap Independence Fund, a series of Vanguard Target Date Funds, Vanguard Total Bond Market Index Signal, and several options through the ING variable annuity. A self directed brokerage account option provides access to additional mutual funds.

Enrollment and record keeping services for the program are provided by Great-West Retirement Services. The use of an unbundled arrangement enables participants to receive an objective presentation of the investment products, to avoid the sales fees traditionally associated with bundled products, and to receive consolidated account statements and benefit estimates. All of the products available for new enrollment are offered without sales fees, surrender fees, mortality and expense risk fees, or minimum deposit requirements.

Participants receive a quarterly statement showing their contributions and earnings during the quarter. In addition, once a year, participants receive a special statement projecting their account balance to a variety of retirement ages and showing the monthly income those account balances might provide. The program provides a variety of communication and education materials and services, including a comprehensive Internet site, a handbook for participants, several booklets on special topics, investment seminars around the state, plus a voice response telephone system and an Internet account access system which provide participants with immediate access to account balances and account transactions 24 hours a day.

**DEFERRED COMPENSATION PROGRAM**

Online statements are available upon request.

The Internet site, [www.tn.gov/treasury/dc](http://www.tn.gov/treasury/dc), provides full information about the program. Information available through the site includes forms, participation information and illustrations, descriptions of the investment choices and historical performance figures, an interactive benefit calculator, complete information for participants who may be approaching retirement age or considering withdrawing funds from the program, an e-mail address for participants to request additional personalized information and full account activity access.

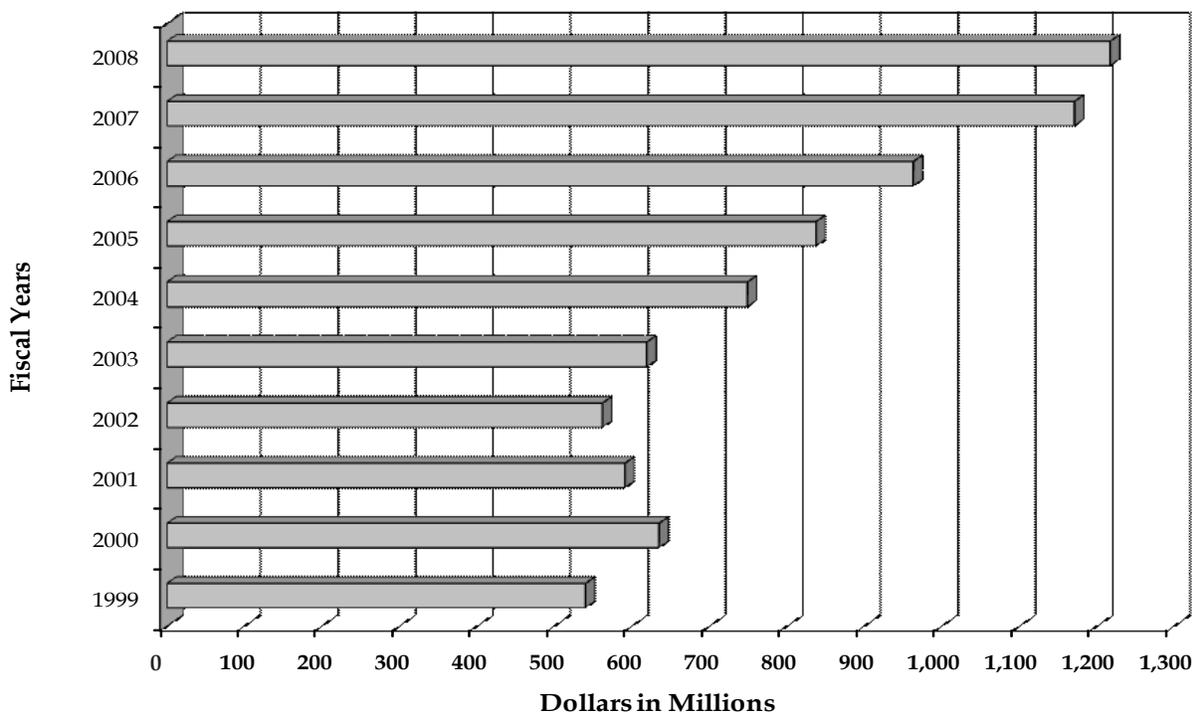
For the year ending June 30, 2008, contributions to the program totaled \$143 million. Contributions are wired for immediate crediting. At June 30, 2008, accumulated account balances totaled \$1.2 billion.

Under the loan program offered in the 401(k) plan, active employees who have accumulated \$4,000 or more in their 401(k) account may borrow up to half of their account value. Participants repay principal and interest to their 401(k) account through salary deduction. Taxes continue to be deferred while funds accumulated in the plan are in loan status. As of June 30, 2008, there were 4,243 loans outstanding from the 401(k) plan. Outstanding loan balances totaled \$13.6 million.

Benefits from the program may be distributed in periodic payments, in an annuity, or in a lump sum. During the year ended June 30, 2008, there were 3,323 periodic payments made from the program. In addition, 3,704 lump sum distributions and 3,327 partial lump sum distributions were issued during fiscal year 2008.

**DEFERRED COMPENSATION PROGRAM ASSETS**

*Expressed in Millions  
Fiscal Years 1999-2008*



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**DEFERRED COMPENSATION PROGRAM**


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**DEFERRED COMPENSATION CONTRIBUTIONS AND MARKET VALUE**

	<b>Contributions Fiscal Year 2008</b>	<b>Market Value June 30, 2008</b>
<b>Plan I (457)</b>		
ING	\$ 1,659,274	\$ 34,562,342
American General	15,870	630,733
Calvert	1,023,877	6,921,299
Fidelity	10,880,767	106,586,900
State Street	1,234,991	5,560,875
Regions	1,047,670	16,701,077
Ameritrade	-	162,943
Vanguard	23,288	1,140,721
Dimensional	5,928	199,877
	<u>\$ 15,891,665</u>	<u>\$ 172,466,767</u>
<b>Plan II (401K)</b>		
ING	\$ 15,353,069	\$ 135,262,270
Calvert	5,252,904	37,005,087
Fidelity	89,836,463	759,779,375
State Street	6,187,294	32,456,451
Regions	10,387,336	74,192,792
Ameritrade	-	1,311,998
Vanguard	85,847	5,015,818
Dimensional	6,223	362,966
	<u>\$ 127,109,136</u>	<u>\$ 1,045,386,757</u>
<b>Total for both plans</b>	<u>\$ 143,000,801</u>	<u>\$ 1,217,853,524</u>

## FLEXIBLE BENEFITS PLAN

### FLEXIBLE BENEFITS PLAN

The Flexible Benefits Plan is an optional benefit plan that enables state employees to pay for certain expenses with tax-free salary. Authorized under Section 125 of the Internal Revenue Code, this plan allows employees to avoid income tax and social security tax on the portion of the upcoming year's salary they agree to set aside for that year's (1) group medical insurance premiums, (2) group dental insurance premiums, (3) out-of-pocket medical expenses, and (4) dependent care expenses.

In exchange for its favorable tax treatment, the plan must comply with specific rules set forth by the Internal Revenue Code and Regulations. Employees must decide what they will purchase through the plan and how much they will spend before the year begins. State employees enrolled in a group health or dental insurance program are automatically enrolled in the insurance premium portion of the plan unless they elect not to participate. Use of the other benefit options requires a new election each year.

Enrollment in the plan is for a full calendar year. Enrollments may not be changed after the year has begun unless the employee experiences a change in family status and reports that change promptly. Employees must use the amounts set aside in each

category for corresponding expenses incurred during the year and any amount not used by the employee must be subject to forfeiture.

At June 30, 2008, a total of 44,542 state employees were enrolled in one or more of the plan's four options: 43,398 employees used the plan to pay medical insurance premiums, 26,914 paid dental insurance premiums, 4,767 used the medical expense reimbursement account, and 418 used the dependent care reimbursement account.

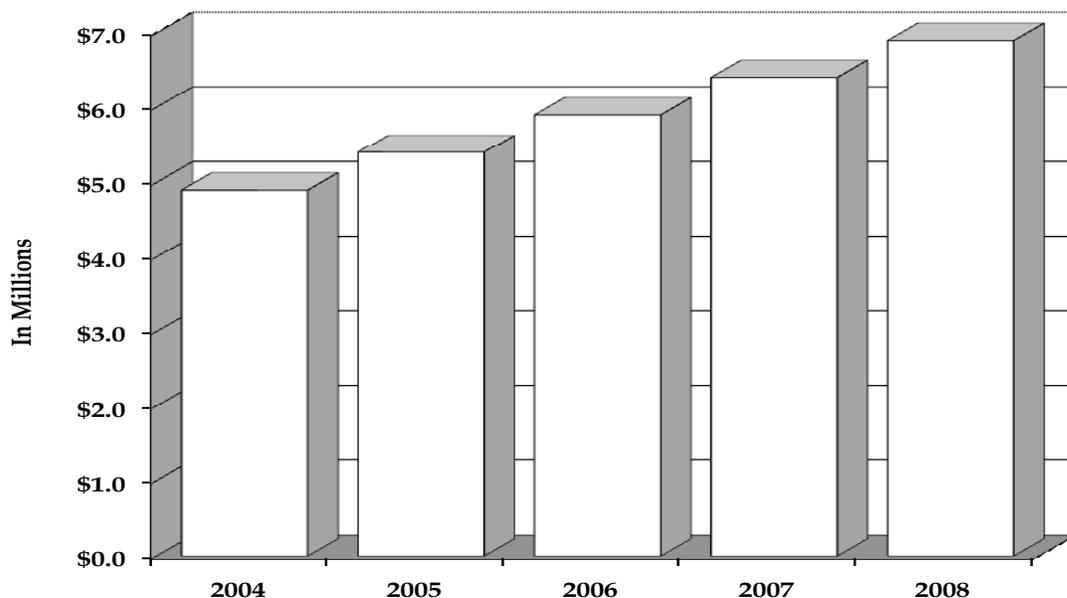
Since contributions to the plan are exempt from both employee and employer F.I.C.A. (social security) tax, employees' use of the plan creates F.I.C.A. savings for the state. In fiscal year 2008, the state's F.I.C.A. savings totaled \$6.9 million. Employees realize similar savings.

Since the program began operation in January 1989, the state's F.I.C.A. savings have totaled \$61.8 million. Savings exceeding the costs of administering the plan have been designated for offsetting costs of the state's wellness program, providing assistance for day care programs, funding for employee sick leave bank administration and funding matching contributions to the 401(k) plan. As of June 30, 2008, \$55.2 million had been transferred to offset costs of other benefit programs.

### F.I.C.A. SAVINGS TO STATE

*Fiscal Years 2004-2008*

*Expressed in Millions*



# TREASURER'S REPORT

*Investments*

**TCRS INVESTMENTS****TCRS INVESTMENTS**

Investment objectives for the TCRS Investment Division are to obtain the highest available return on investments consistent with the preservation of principal, while maintaining sufficient liquidity to react to the changing environment and to pay beneficiaries in a timely manner.

TCRS Investment Division's policies and strategies serve to benefit plan members in several ways. The emphasis on a conservative asset allocation and high quality securities helps to ensure the soundness of the system and the ability to provide the needed funds upon a member's retirement.

Funds in the retirement system are actively managed with a diversified portfolio of high-quality domestic and international bonds, domestic and international stocks, real estate and money market instruments.

The investment authority for TCRS is set out in *Tennessee Code Annotated*, Section 8-37-104(a), which provides that, with certain specific exceptions, investments of TCRS assets are subject to the same terms, conditions, and limitations imposed on domestic life insurance companies. It further provides that investment policy for TCRS funds is subject to the approval of the Board of Trustees.

The Investment Advisory Council established in *Tennessee Code Annotated*, Section 8-37-108 provides policy guidance to the Board of Trustees and the investment staff. The current Advisory Council is comprised of senior investment professionals from within the State of Tennessee.

To assist in the fiduciary responsibility for managing the TCRS portfolio, Strategic Investment Solutions, Inc. serves as the general investment consultant for TCRS. The Townsend Group serves as the real estate investment consultant.

Northern Trust Company is the Master Trust Bank for TCRS which provides safekeeping and accounting services for the investment portfolio.

**COST OF INVESTMENT OPERATION**

The administrative cost to operate the investment program for TCRS is less than 4 basis points (.04%) of assets. The Wall Street Journal reported on August 27, 2001 that the average mutual fund fee was 56 basis points and that the average fee for large public pension funds was 28 basis points. The cost of 4 basis points includes the cost of personnel, operational cost, master bank custodian cost, record keeping, and the cost of external management for international equities. Commission cost for trades are capitalized.

**PERFORMANCE MEASUREMENT**

An independent external investment consultant, Strategic Investment Solutions, Inc., provides performance measurement for TCRS. During the 2008 fiscal year, TCRS had a total return of (1.21%). Domestic stocks lost 11.93%, while the S&P 1500 Index lost 12.72%. Domestic Bonds earned 5.98% versus the bond index of 7.78%, while international stocks lost 6.38% versus (10.61%) for the EAFE Index. Real estate earned 12.53%.

## TCRS INVESTMENTS

## INVESTMENT SUMMARY

As of June 30, 2008

	Domestic		International		Total	
	Fair Value	%	Fair Value	%	Fair Value	%
<b>Fixed Income</b>						
Government Bonds	\$ 6,449,045,051	20.52%	\$ 975,890,473	3.11%	\$ 7,424,935,524	23.63%
Corporate Bonds	6,462,234,763	20.57%	19,614,062	0.06%	6,481,848,825	20.63%
Total Bonds	12,911,279,814	41.09%	995,504,535	3.17%	13,906,784,349	44.26%
Preferred Stock	93,047,000	0.30%	28,754	0.00%	93,075,754	0.30%
Total Fixed Income	13,004,326,814	41.39%	995,533,289	3.17%	13,999,860,103	44.56%
<b>Common Stock</b>						
Consumer Discretionary	921,131,217	2.93%	657,514,060	2.09%	1,578,645,277	5.02%
Consumer Staples	1,098,438,746	3.50%	564,692,306	1.78%	1,663,131,052	5.28%
Energy	1,663,217,207	5.29%	436,681,646	1.39%	2,099,898,853	6.68%
Financials	1,519,212,775	4.83%	729,787,494	2.33%	2,249,000,269	7.16%
Healthcare	1,293,915,800	4.12%	447,747,082	1.42%	1,741,662,882	5.54%
Industrials	1,308,817,646	4.16%	839,630,804	2.68%	2,148,448,450	6.84%
Information Technology	1,845,403,991	5.87%	318,671,214	1.02%	2,164,075,205	6.89%
Materials	465,231,152	1.48%	429,396,138	1.37%	894,627,290	2.85%
Rights/Warrants	-	0.00%	104,124	0.00%	104,124	0.00%
Telecommunication Services	309,961,980	0.99%	213,568,217	0.68%	523,530,197	1.67%
Unit	-	0.00%	13,458,330	0.04%	13,458,330	0.04%
Utilities	458,045,425	1.46%	150,550,161	0.48%	608,595,586	1.94%
Total Common Stock	10,883,375,939	34.63%	4,801,801,576	15.28%	15,685,177,515	49.91%
<b>Short-Term Investments</b>						
Commercial Paper	287,351,391	0.91%	-	0.00%	287,351,391	0.91%
U.S. Government Securities	121,968,950	0.39%	-	0.00%	121,968,950	0.39%
Total Short-Term Investments	409,320,341	1.30%	-	0.00%	409,320,341	1.30%
<b>Real Estate</b>	1,330,171,187	4.23%	-	0.00%	1,330,171,187	4.23%
<b>Total Investments</b>	25,627,194,281	81.55%	5,797,334,865	18.45%	31,424,529,146	100.00%
<b>Short Term Investments Classified as Cash Equivalents</b>	(359,322,591)				(359,322,591)	
<b>Total Investments as Shown on the Statement of Plan Net Assets</b>	\$ 25,267,871,690		\$ 5,797,334,865		\$ 31,065,206,555	

This schedule classifies Canadian investments as domestic securities, convertible bonds as fixed income securities, and preferred stock as fixed income securities. For investment purposes convertible bonds and preferred stock are considered equity securities. Accordingly, the asset allocation percentages in this schedule will vary from the investment consultant's asset allocation percentages.

## TCRS INVESTMENTS

## TCRS INVESTMENTS BENCHMARK ANALYSIS

<b>Fiscal Year</b>	<b><sup>1</sup>Public Fund Index Median Total Return</b>	<b><sup>2</sup>TCRS Total Return</b>
2008	(4.7%)	(1.2%)
2007	14.1	13.2
2006	6.9	6.9
2005	9.4	7.3
2004	15.0	9.3
2003	3.7	4.9
2002	(5.2)	(1.9)
2001	(4.1)	(1.6)
2000	9.5	7.9
1999	10.0	9.5

<sup>1</sup>This index most closely resembles the structure and objectives of TCRS.

<sup>2</sup>This is the time weighted method used to calculate returns and is the most accurate way to measure performance.

## SUMMARY OF TCRS EARNINGS

*Fiscal Years 2004-2008*

<b>Fiscal Year</b>	<b>TCRS Portfolio Earnings</b>
2008	\$ (430,058,924)
2007	3,791,403,651
2006	1,877,298,490
2005	1,850,367,215
2004	2,181,853,628
2003	1,112,478,748

## STATE CASH MANAGEMENT

### STATE CASH MANAGEMENT

The State of Tennessee receives revenues from many sources such as taxes, licenses, fees, and the federal government. As these monies are collected, they are deposited into one of the more than 60 financial institutions in Tennessee that have contracted with the state to serve as depositories. Under the state Constitution, the state may not spend more money on its programs than it has collected in revenues. Consequently, at any point in time the state has a sizable sum of money collected but not yet spent. These monies are invested by the Treasury Department until needed to pay for state expenses, payroll, or benefit program disbursements.

During the 2008 fiscal year, the average balance of short term investments in the Treasurer's Cash Management program was \$8,098,482,824 per month and interest income of \$326,177,632 was earned. This includes deposits in the Local Government Investment Pool administered by the Treasury Department.

The State Funding Board sets the investment policy for the state. The State Funding Board is composed of the Governor, Commissioner of Finance and Administration, Comptroller, Secretary of State, and Treasurer. The foremost investment objective of the State Pooled Investment Fund is safety of principal, followed by liquidity and then yield.

The current investment policy for the State Pooled Investment Fund was established to follow SEC Rule 2a-7-like guidelines for a money market fund. The maximum maturity of any security can not exceed 397 days and the weighted average maturity must be 90 days or less.

Funds may be invested in collateralized certificates of deposit with authorized Tennessee financial institutions; bills, notes and bonds of the U.S. Treasury; other obligations guaranteed as to principal and interest by the U.S. or any of its agencies; and repurchase agreements against obligations of the U.S. or its agencies. Securities underlying repurchase agreements must be book-entry and delivered to the State Trust of Tennessee. Funds may also be invested in prime commercial paper and prime banker's acceptances.

At June 30, 2008, investments had an average maturity of 85 days, and an average weighted yield of 2.34%. The total balance in the State Pooled Investment Fund at June 30, 2008, \$8,684,378,183 fair value, was allocated as follows: U.S. Treasury government and agency securities, 35.78%; repurchase agreements and overnight deposits, 4.80%; collateralized certificates of deposit, 28.73%; and commercial paper, 30.69%.

### ADMINISTRATION OF AUTHORIZED STATE DEPOSITORY ACCOUNTS

The Cash Management Division is responsible for the administration of the state's bank accounts in Tennessee financial institutions designated as authorized state depositories. Taxpayers and state agencies can deposit certain tax funds due to the state directly to any Treasurer's account at any authorized state depository.

The four most significant functions of administering the accounts are: (1) authorizing the state depository to accept state funds; (2) cash concentration; (3) collateralizing deposits; and (4) monitoring collateral and deposits. Financial institutions' requests to become authorized state depositories are received in Cash Management, reviewed, and forwarded to the appropriate state officials for consideration and approval.

The Cash Management Division is responsible for the cash concentration and management of all state depository accounts. Cash Management staff inquire on the balances of bank accounts and concentrate available funds into the State Trust to meet liquidity and investment needs. Account balances are drawn to the floor and concentrated by Fed wire or Automated Clearinghouse (ACH) transactions. The account floor is the minimum amount required by the financial institution for that particular account to earn interest. All of these state accounts are interest bearing.

Changes in branch banking laws and bank ownership due to mergers and acquisitions have brought about a need to quickly identify the parent bank, holding company and affiliate trustee custodians for state depositories. The ability to access and update this

## STATE CASH MANAGEMENT

information on a database enhances the ability to monitor deposits and collateral based on appropriate bank ownership.

This same database is accessed for current account information, for balance inquiry, and cash concentration. It automates the link from balance inquiry to cash concentration by generating an ACH transaction. This automation provides more time to inquire on more accounts. The account balance floors are automatically compared to the balances entered to calculate ACH transaction amounts.

### STATE COLLATERAL PROGRAM

Collateral is required to secure state deposits held in authorized state depository institutions. Statute sets the required collateral level at a market value of 105 percent of the value of the deposit secured, less the amount secured by the Federal Deposit Insurance Corporation. However, if the state depository is operating with a capital-to-asset ratio of less than five percent, additional collateral with a market value of \$100,000 is required. Alternatively, a financial institution may pledge collateral via the collateral pool. The types of investment instruments which are eligible to be pledged as collateral are listed in this report.

The state of the economy and the financial environment have increased the importance of monitoring collateral. Cash Management staff review collateral daily, weekly, and monthly. Any collateral deficiencies at authorized state depository institutions are reported to the Funding Board monthly. Reasons for under-collateralization include market price volatility of the security pledged, unexpected high deposits to an account, interest accruals, capital-to-asset ratios falling below five percent, and principal paydowns on asset backed securities that have been pledged as collateral.

Collateral is held by an authorized trustee custodian in the name of the State of Tennessee. Treasury staff must authorize the receipt, release, and substitution of all collateral.

### COLLATERAL POOL

The operation of a collateral pool for banks is authorized by *Tennessee Code Annotated*, Section 9-4-501, et seq. The Collateral Pool operates under the jurisdiction of the Collateral Pool Board, which is comprised of four bankers and three government members representing state and local government divisions. The Collateral Pool Board has established rules and procedures that provide a low amount of risk and a high degree of efficiency for participating institutions.

While participation in the Collateral Pool is voluntary, participation is subject to application to and approval by the Collateral Pool Board. The Board has established minimum financial performance levels for applicants which must be met to ensure that only healthy institutions are permitted to participate.

All public funds held by a pool participant are collateralized based on a collateral target calculated each month by the participant. The collateral target is based on the aggregate average balance of all public funds for the month multiplied by the pledge percentage level assigned to the participant by the Board.

The Board has established three different collateral pledge levels: 115 percent, 100 percent and 90 percent. The pledge level is based on financial criteria set by the Collateral Pool Board with the financially strongest institutions being eligible for the lowest pledge level. Under the Collateral Pool, should a financial institution default with insufficient collateral to cover public deposits, then the other financial institutions must make up the difference on a pro rata basis. Accordingly, public funds are not at risk in the Collateral Pool.

All collateral transactions for the pool are monitored and processed through the Treasury Department using uniform statewide procedures. In addition, Treasury Department staff monitors all pool activity through the monthly, quarterly, and annual reports required to be submitted by pool participants.

The Collateral Pool provides collateral for both state funds and local government funds for those

**STATE CASH MANAGEMENT**

institutions participating in the pool. The Collateral Pool serves as a significant administrative advantage for local governments. Under the Collateral Pool, the Treasurer, rather than the local government, is responsible for monitoring the pledge level; pricing collateral; reconciling collateral monthly with the trustee custodian; monitoring collateral; pledging, releasing and substituting collateral; and maintaining a trustee custodian relationship.

Currently, the Collateral Pool has 89 participant institutions collateralizing public funds in excess of \$8.0 billion.

**8-5-110 COLLATERAL**

*Tennessee Code Annotated*, Section 8-5-110 designates the Treasurer as the custodian of all negotiable instruments deposited with the state or any department thereof, and requires the Treasurer to be exclusively responsible for the safekeeping thereof.

Cash Management personnel work directly with the personnel of the state agencies to accept and release collateral held in accordance with their specific instructions. Other state agencies cooperating with the Treasurer in this regard include the Department of Health, the Department of Environment and Conservation, the Department of Commerce and Insurance, the Department of Transportation, and the Department of Financial Institutions.

**STATE CASH MANAGEMENT COMPARATIVE RETURNS**

In order to ensure that state investment returns reflect current market conditions, several market indicators are carefully monitored. Among these are rates reported daily in the Wall Street Journal, rates on U.S. Treasury securities and institutional money market funds. The following table illustrates state returns compared with two of these indicators.

<b>Fiscal Year</b>	<b><sup>1</sup>Total Pool Funds</b>	<b><sup>2</sup>Merrill Lynch Institutional Fund</b>	<b><sup>3</sup>Standard &amp; Poor's 7-Day LGIP Yield Index</b>	<b><sup>4</sup>90-Day Treasury (CD Equivalent Yield)</b>
2008	4.13%	4.23%	2.60%	2.75%
2007	5.30	5.11	4.50	5.02
2006	4.11	4.00	4.00	4.18
2005	2.12	2.00	1.89	2.25
2004	1.11	.93	.84	.97

<sup>1</sup>Investment return on total portfolio.

<sup>2</sup>This index most closely resembles the structures and objectives of the total cash portfolio.

<sup>3</sup>Index is for LGIP benchmark pools rated AAAM & AAM by S&P.

<sup>4</sup>This approximates the reinvestment period for new funds for the period.

## STATE CASH MANAGEMENT

## SECURITIES ACCEPTABLE AS COLLATERAL FOR STATE DEPOSITS

1. U.S. Treasury Bills
2. U.S. Treasury Notes & Bonds
3. Federal Housing Administration (FHA) debentures
4. Government National Mortgage Associations (GNMA)\*
5. Farm Credit System (FCS)
  - a. Federal Land Bank Bond (FLBB)
  - b. Farm Credit Systemwide Bonds (FCSB)
  - c. Farm Credit Systemwide Discount Notes (FCDN)
  - d. Farm Credit Systemwide Floating Rate Notes (FCFR)
6. Federal Home Loan Banks
  - a. Bonds (FHLB)
  - b. Discount Notes (FHDN)
  - c. Floating Rate Notes (FHFR)
7. Federal Home Loan Mortgage Corporation (FHLMC)\*
  - a. Mortgage-Backed Participation Certificates and Adjustable Rate Securities (FMPC, FMAR)
  - b. Discount Notes (FMDN)
8. Federal National Mortgage Association (FNMA)\*
  - a. Bonds, Debentures, Secondary Market Debt Obligations (FNSM)
  - b. Discount Notes (FNDN)
  - c. Floating Rate Notes (FNFR)
  - d. Mortgage-Backed Pass-Through Certificates (FNRF)
  - e. Residential Financing Securities (FNRF)
  - f. Adjustable Rate Mortgage-Backed Bonds (FNAR)
9. Student Loan Marketing Association (SLMA)
  - a. Discount Notes (SLDN)
  - b. Fixed Rate Notes (SLMN)
  - c. Floating Rate Notes (SLFR)
  - d. Bonds (SLBD)
10. Tennessee Valley Authority Bonds and Notes (TVA)
11. Collateralized Mortgage Obligations (CMOs) and Real Estate Mortgage Investment Conduits (REMICs) that are direct obligations of a U.S. agency or FNMA/FHLMC, except that the "residual" class/tranche of such securities will not be acceptable. Sufficient excess securities should be pledged to allow for the periodic reduction of principal.
12. Certain Tennessee Municipal Bonds as specified in T.C.A. Section 9-4-103.
13. Surety Bonds issued by insurance companies meeting certain requirements, including licensure under the laws of Tennessee.
14. Standby Letters of Credit from approved Federal Home Loan Banks.

\* Pass through securities must reflect current paid down values and be kept up to date.

## STATE CASH MANAGEMENT

## HISTORICAL ANALYSIS OF STATE CASH INVESTMENTS

*Collateralized Time Deposits*

<b>Fiscal Year</b>	<b>Average Amount Invested</b>	<b>Amount Earned</b>	<b>Rate of Return</b>
2008	\$ 2,455,349,750	\$ 107,899,521	4.35%
2007	2,124,406,667	112,695,354	5.30%
2006	1,759,051,167	72,963,609	4.08%
2005	1,888,126,667	38,198,848	2.00%
2004	1,932,058,417	20,858,498	1.11%

*Repurchase Agreements and Overnight Deposit Accounts*

<b>Fiscal Year</b>	<b>Average Amount Invested</b>	<b>Amount Earned</b>	<b>Rate of Return</b>
2008	\$ 387,890,324	\$ 12,631,202	3.93%
2007	398,534,694	17,529,090	5.45%
2006	384,561,576	13,866,064	4.37%
2005	493,189,109	9,740,888	2.37%
2004	293,922,333	3,408,318	1.05%

*Commercial Paper*

<b>Fiscal Year</b>	<b>Average Amount Invested</b>	<b>Amount Earned</b>	<b>Rate of Return</b>
2008	\$ 2,481,205,417	\$ 92,953,120	3.87%
2007	2,002,307,667	106,634,748	5.34%
2006	1,506,052,417	64,594,383	4.24%
2005	795,684,167	18,853,258	2.37%
2004	894,287,583	9,195,815	1.02%

*U.S. Government Securities*

<b>Fiscal Year</b>	<b>Average Amount Invested</b>	<b>Amount Earned</b>	<b>Rate of Return</b>
2008	\$ 2,774,037,333	\$ 112,693,789	4.22%
2007	2,210,772,500	115,043,989	5.26%
2006	1,747,103,333	69,817,959	3.99%
2005	1,254,517,917	25,938,244	2.07%
2004	906,027,583	10,863,449	1.19%

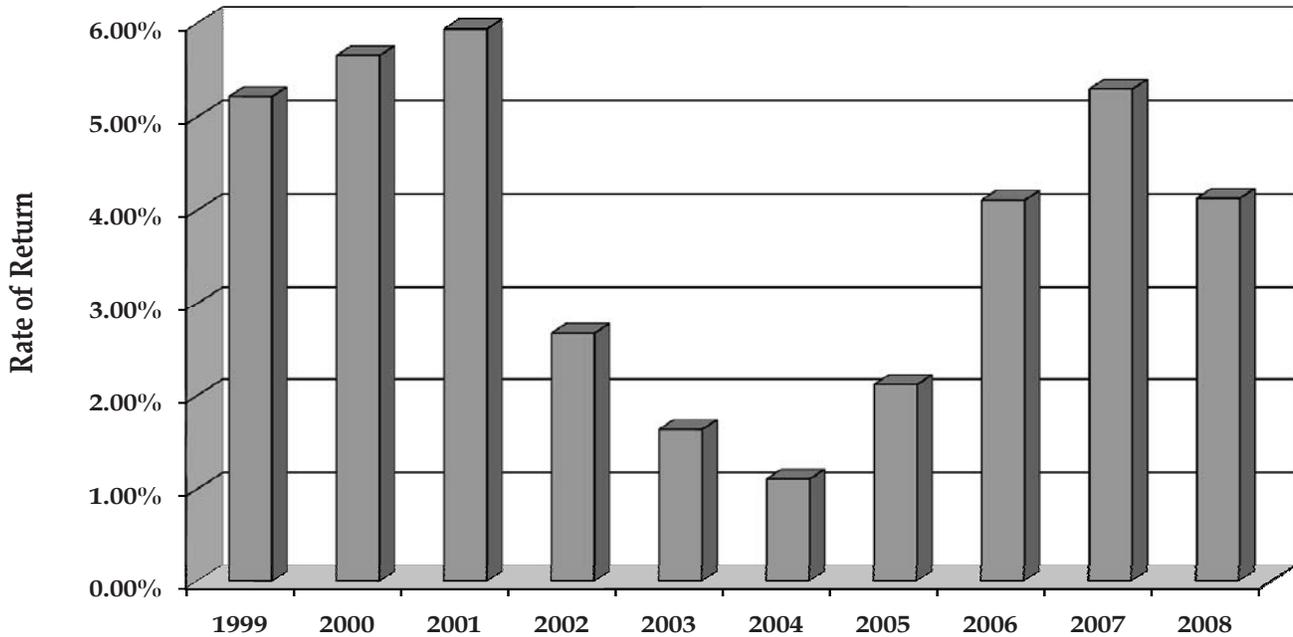
*Total Funds*

<b>Fiscal Year</b>	<b>Average Total Funds Invested</b>	<b>Cash Management Investment Earnings</b>	<b>Composite Weighted Average Rate of Return</b>
2008	\$ 8,098,482,824	\$ 326,177,632	4.13%
2007	6,736,021,528	351,903,181	5.30%
2006	5,396,768,493	221,242,015	4.11%
2005	4,431,517,860	92,731,238	2.12%
2004	4,026,295,916	44,326,080	1.11%

STATE CASH MANAGEMENT

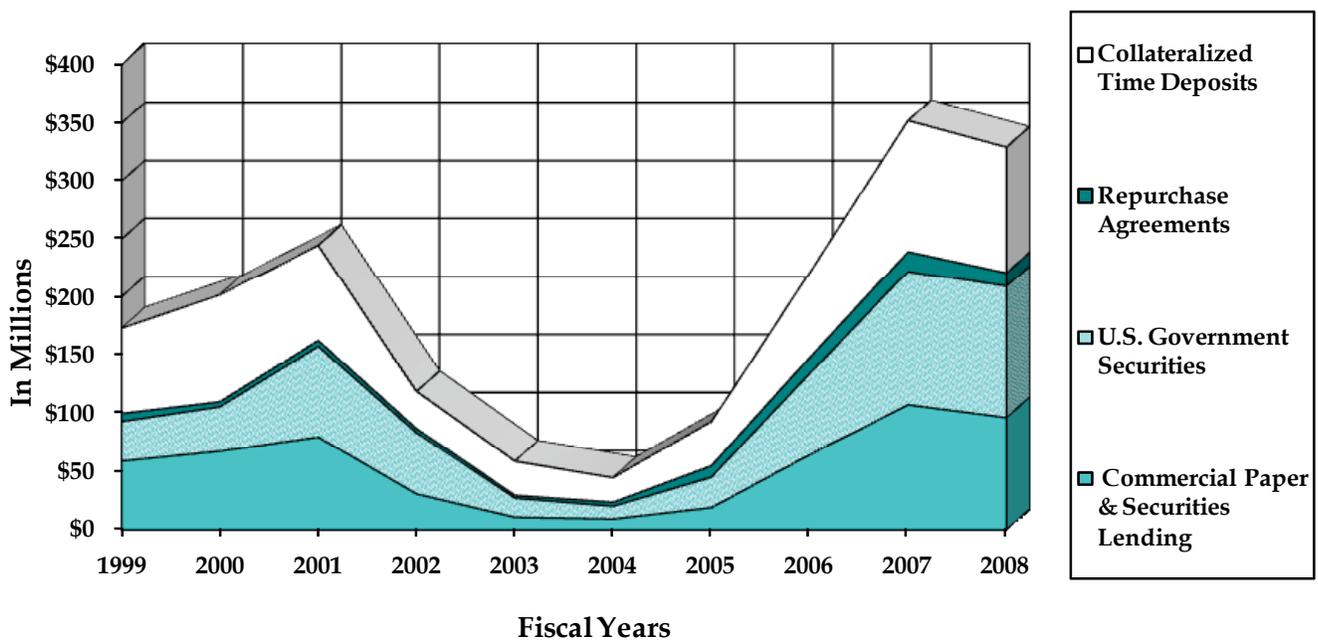
CASH MANAGEMENT INVESTMENTS COMPOSITE WEIGHTED AVERAGE RATE OF RETURN

Fiscal Years 1999-2008



ANALYSIS OF STATE CASH EARNINGS

Fiscal Years 1999-2008



STATE CASH MANAGEMENT

CASH MANAGEMENT PORTFOLIO ANALYSIS

Fiscal Year Ended June 30, 2008

Date	Current Investment Yield	Total Portfolio Yield	Avg. Days to Maturity	Portfolio Composition			
				Certificates of Deposit	Repurchase Agreements	U.S. Agency	Commercial Paper
July 2007	5.26%	5.34%	72	27.80%	3.89%	33.10%	35.22%
August 2007	3.51%	5.34%	77	30.03%	4.07%	35.94%	29.96%
September 2007	4.92%	5.25%	73	32.90%	3.98%	35.88%	27.23%
October 2007	4.76%	5.08%	75	36.15%	4.15%	34.69%	25.01%
November 2007	4.53%	4.88%	70	39.25%	4.24%	29.31%	27.20%
December 2007	4.31%	4.68%	89	38.42%	4.47%	31.32%	25.79%
January 2008	3.78%	4.42%	86	34.87%	4.06%	31.99%	29.09%
February 2008	2.97%	3.69%	74	24.46%	3.93%	33.97%	37.65%
March 2008	2.61%	3.23%	80	24.79%	3.73%	34.01%	37.47%
April 2008	2.20%	2.77%	89	26.21%	3.63%	39.58%	30.58%
May 2008	2.04%	2.52%	89	27.00%	3.49%	37.09%	32.42%
June 2008	2.05%	2.30%	90	28.13%	3.70%	36.45%	31.73%
<b>Average</b>	3.57%	4.13%	80	30.83%	3.94%	34.44%	30.78%

MONTH	General Fund		LGIP		Other Restricted		Total Average Invested
	Average	Percent	Average	Percent	Average	Percent	
July 2007	\$ 3,149,160,845	39.36%	\$ 2,727,492,889	34.09%	\$ 2,123,648,461	26.54%	\$ 8,000,302,195
August 2007	3,137,173,281	39.44%	2,685,797,251	33.77%	2,130,933,051	26.79%	7,953,903,583
September 2007	2,986,715,766	38.45%	2,663,732,523	34.29%	2,117,307,052	27.26%	7,767,755,341
October 2007	2,928,063,688	38.34%	2,584,745,359	33.84%	2,125,148,935	27.82%	7,637,957,982
November 2007	2,692,724,975	36.03%	2,707,576,214	36.23%	2,073,093,114	27.74%	7,473,394,303
December 2007	2,492,332,248	33.16%	2,929,395,422	38.97%	2,093,590,163	27.86%	7,515,317,833
January 2008	2,450,888,685	30.93%	3,337,515,470	42.13%	2,134,443,519	26.94%	7,922,847,674
February 2008	2,266,177,384	28.32%	3,564,674,800	44.53%	2,171,650,139	27.14%	8,002,502,323
March 2008	2,154,046,462	25.30%	4,218,083,424	49.53%	2,142,565,067	25.16%	8,514,694,953
April 2008	2,345,603,591	27.14%	4,085,296,156	47.26%	2,212,658,794	25.60%	8,643,558,541
May 2008	2,747,933,923	30.91%	3,918,695,531	44.08%	2,224,107,653	25.02%	8,890,737,107
June 2008	3,005,158,825	33.92%	3,612,919,494	40.78%	2,240,737,731	25.29%	8,858,816,050
<b>Average</b>	\$ 2,696,331,639	33.29%	\$ 3,252,993,711	40.17%	\$ 2,149,156,974	26.54%	\$ 8,098,482,324

**STATE CASH MANAGEMENT**

**LOCAL GOVERNMENT INVESTMENT POOL**

Tennessee municipalities, counties, school districts, utility districts, community service agencies, local government units, and political subdivisions can deposit monies with the Treasurer to be invested in the state cash management investment pool. Of course, these local governments can invest their monies directly in the money market if they so desire. However, by allowing their dollars to be invested by the state they eliminate the complexities of managing day-to-day investment and collateral relationships with banks and/or securities dealers. This allows cash managers who have previously been limited either by the relatively small amount of funds available for investment or the complexities of today's investment environment to take advantage of the volume and expertise of the Treasurer's cash management program.

The Local Government Investment Pool began operations in November of 1980. Participation in the LGIP program currently stands in excess of 1,800 accounts. The Department of Transportation (DOT) program has more than 600 active accounts.

Local governments which enter into agreements with the DOT often establish an LGIP account to fund the local matching portion of a highway project grant. These DOT accounts are available to provide the local match to the specific highway project in a timely manner while earning interest for the local government. In a similar fashion, the Tennessee Board of Regents schools provide their matching portion of

Capital Projects funds while earning interest for the benefit of the Board of Regents school.

An electronic banking system allows participants to access their accounts in a secure Internet application. Thus, participants are able to communicate their instructions by telephone, telefax, or the Internet.

In addition, voice mail telephone service has been provided to permit LGIP participants to give telephone transaction instructions while staff is busy on other telephone lines. Voice mail permits an increase in productivity while holding costs constant.

LGIP reports mailed to participants include monthly statements and transaction confirmations. Monthly statements detail all debits and credits to the account during the month, the account's average daily balance, and interest credited. A transaction confirmation is mailed to the participant each time a deposit or withdrawal is made. Many participants rely on this documentation for daily and weekly reconciliations.

Participants earn interest on LGIP deposits based on the total portfolio return of the cash management pool, less a monthly administrative fee of five one hundredths of one percent (.05%). During the 2008 fiscal year, the average rate participants earned on their deposits after the fee reduction was 4.08%. Other activity is shown on the following schedule by participant group.

**LOCAL GOVERNMENT INVESTMENT POOL SCHEDULE OF ACTIVITY BY ENTITY TYPE**

*Fiscal Year Ended June 30, 2008*

	Account Balance 7/1/2007	Net Deposits/(Withdrawals) FY 2008	Interest Credited FY 2008	Account Balance 6/30/2008
Cities	\$ 884,942,065	\$ 103,136,368	\$ 36,693,674	\$ 1,024,772,107
Counties	728,362,524	176,053,474	36,273,221	940,689,219
Commitments to D.O.T.	43,337,929	(7,045,408)	1,734,535	38,027,056
Educational Institutions	691,296,434	89,140,707	34,218,768	814,655,909
Community Health Agencies	6,798,535	(5,032,629)	187,667	1,953,573
Other	363,192,149	41,042,667	19,662,321	423,897,137
	<u>\$ 2,717,929,636</u>	<u>\$ 397,295,179</u>	<u>\$ 128,770,186</u>	<u>\$ 3,243,995,001</u>

**STATE CASH MANAGEMENT**

**STATE TRUST OF TENNESSEE**

The State Trust of Tennessee, a not-for-profit corporation chartered in the State of Tennessee in 1979, enables the Treasury Department to hold limited membership in the Federal Reserve Bank System. Being a limited member of the Federal Reserve gives the Treasury Department access to the Federal Reserve Wire System, which is used to send, receive, transfer and control funds movement expediently under the Treasurer's management.

Due to restrictions imposed upon state-owned trust companies by the Federal Reserve Board, the State Trust of Tennessee is limited in the number

of daily outgoing wire transfers and may not settle ACH transactions through its account at the Federal Reserve.

The restrictions require the State Trust of Tennessee to contract with an agent bank to execute these transactions. Regions Bank in Nashville serves as the Trust's agent for the period July 1, 2004 through June 30, 2009.

The State Trust is an associate member of the Regional Check Clearinghouse. Approximately 85% of all check items presented for redemption are processed through the clearinghouse .

**STATE TRUST OF TENNESSEE FEDERAL RESERVE BANK TRANSACTIONS**

*Fiscal Year 2008*

	<u>Transaction Type</u>	<u>Number</u>	<u>Amount</u>
(1)	Wire Disbursements	1,010	\$ 20,809,974,051
(2)	Wire Receipts	5,829	21,859,537,938
(3)	Security Disbursements	177	5,159,333,673
(4)	Security Receipts	125	4,104,301,133
(5)	Check Redemptions	<u>3,734,149</u>	<u>4,615,260,063</u>
	<b>Total</b>	<b><u>3,741,290</u></b>	<b><u>\$ 56,548,406,858</u></b>

Explanation of Transaction Types:

- (1) Disbursements of cash for the purpose of non-Fed eligible securities, settlement wires to agent bank, and other nonrecurring wires.
- (2) Receipt of cash for payment of interest and principal for non-Fed eligible securities, concentration of cash deposited in local banks, drawdown of Federal funds, and Local Government Investment Pool (LGIP) deposits.
- (3) Disbursement of cash against the receipt of Fed eligible securities (U.S. Government securities held in book-entry form by the Federal Reserve Bank).
- (4) Receipt of cash against the disbursement of Fed eligible securities.
- (5) Redemption of warrants, drafts, and checks issued by the state.

**TENNESSEE CONSOLIDATED RETIREMENT SYSTEM  
LARGEST HOLDINGS**

**LARGEST STOCK HOLDINGS***as of June 30, 2008**by Fair Value*

Shares	Security Name	Fair Value
4,974,794	Exxon Mobil Corporation	\$ 438,428,595
7,921,000	Microsoft Corporation	217,906,710
1,990,530	Chevron Corporation	197,321,239
3,221,900	Procter & Gamble Company	195,923,739
7,279,000	General Electric Company	194,276,510
1,362,800	International Business Machines Corporation	161,532,684
2,506,900	Johnson & Johnson	161,293,946
4,700,745	AT&T Incorporated	158,368,099
6,169,700	CISCO Systems	143,507,222
6,357,500	Intel Corporation	136,559,100

**LARGEST BOND HOLDINGS***as of June 30, 2008**by Fair Value*

Par Value	Security Name	Yield	Maturity	Moody's Quality Rating	Fair Value
\$200,000,000	FNMA	4.82%	03/05/14	NR	\$ 204,562,000
178,200,000	United States Treasury Infl Index Bond	5.69	01/15/26	Aaa	190,984,373
180,000,000	United States Treasury Note	4.71	04/15/13	Aaa	182,335,415
155,000,000	United States Treasury Infl Index Note	4.37	01/15/16	Aaa	176,747,278
130,000,000	United States Treasury Infl Index Note	3.11	01/15/11	Aaa	174,676,865
157,500,000	United States Treasury Note	3.25	05/31/13	Aaa	158,668,965
125,000,000	United States Treasury Infl Index Note	3.11	01/15/14	Aaa	154,323,110
117,000,000	United States Treasury Infl Index Note	3.11	07/15/12	Aaa	153,509,234
100,000,000	United States Treasury Infl Index Bond	5.11	04/15/32	Aaa	151,924,953
142,626,275	GNMA Pool #782222	5.68	11/15/37	Aaa	142,057,196

*A complete portfolio listing is available upon request*

*Key to Ratings: All ratings presented are from Moody's Investors Service with the exception of some of the government agency securities. Moody's does not rate these securities. Standard & Poor's does provide ratings for the securities (AAA is Standard & Poor's highest rating.) Government Securities are not rated per se' but are considered the best quality securities.*

*Moody's rates securities as follows:*

<i>Aaa</i>	<i>Best Quality</i>
<i>Aa</i>	<i>High Quality</i>
<i>A</i>	<i>Upper Medium Quality</i>
<i>Baa</i>	<i>Medium Quality</i>
<i>NR</i>	<i>Not Rated</i>

## STATE CASH PORTFOLIO AS OF JUNE 30, 2008

	Maturity	Yield to Maturity	Par Value	Fair Value
<b>U.S. TREASURY AND AGENCY OBLIGATIONS</b>				
Farmer Mac	04/01/09	2.50 %	\$ 147,000,000	\$ 146,620,740
Farmer Mac	04/01/09	2.37	116,240,000	115,765,741
Farmer Mac	01/30/09	2.90	75,000,000	75,016,500
Farmer Mac	03/13/09	2.83	90,000,000	89,987,400
Federal Home Loan Bank	04/02/09	2.44	34,765,000	34,580,398
Federal Home Loan Bank	05/06/09	2.80	44,500,000	44,458,170
Federal Home Loan Bank	05/06/09	2.66	35,550,000	35,483,522
Federal Home Loan Bank	05/14/09	2.51	42,900,000	42,806,049
Federal Home Loan Bank	06/30/09	2.74	50,000,000	49,906,500
Federal Home Loan Bank	08/01/08	2.06	10,000,000	9,981,000
Federal Home Loan Bank	11/14/08	2.33	100,000,000	99,060,000
Federal Home Loan Bank	11/14/08	2.27	100,000,000	99,060,000
Federal Home Loan Bank	07/01/08	2.00	75,000,000	75,000,000
Federal Home Loan Bank	07/23/08	2.14	50,000,000	49,935,000
Federal Home Loan Bank	11/14/08	2.32	40,000,000	40,162,400
Federal Home Loan Bank	04/01/09	2.40	30,000,000	29,878,200
Federal Home Loan Bank	05/05/09	2.40	50,000,000	49,875,000
FHLMC Note 2.050	08/15/08	2.07	225,000,000	224,370,000
FHLMC Note 2.090	09/12/08	2.11	100,000,000	99,530,000
FHLMC Note 2.140	11/10/08	2.16	31,452,000	31,165,787
FHLMC Note 2.210	09/15/08	2.22	100,000,000	99,510,000
FHLMC Note 2.400	04/02/09	2.40	50,000,000	49,836,000
FHLMC Note 2.500	05/15/09	2.52	44,000,000	43,855,240
FHLMC Note 2.500	04/21/09	2.53	56,300,000	56,135,604
FHLMC Note 2.500	05/28/09	2.50	50,000,000	49,814,000
FHLMC Note 2.600	06/04/09	2.60	25,000,000	24,925,750
FHLMC Note 2.850	06/16/09	2.85	46,950,000	46,901,173
FHLMC Note 5.750	03/15/09	2.25	4,002,000	4,083,280
FNMA Discount Notes	09/10/08	2.09	25,000,000	24,885,000
FNMA Discount Notes	07/01/08	2.72	2,500,000	2,500,000
FNMA Discount Notes	08/15/08	1.65	100,000,000	99,720,000
FNMA Discount Notes	10/15/08	2.14	50,000,000	49,645,000
FNMA Discount Notes	12/15/08	2.06	100,000,000	98,840,000
FNMA Discount Notes	12/15/08	2.06	100,000,000	98,840,000
FNMA Discount Notes	10/15/08	2.13	100,000,000	99,290,000
FNMA Discount Notes	10/15/08	2.24	100,000,000	99,290,000
FNMA Discount Notes	10/15/08	2.10	12,776,000	12,685,290
FNMA Discount Notes	11/12/08	2.18	50,000,000	49,540,000
FNMA Discount Notes	07/15/08	2.04	50,000,000	49,960,000
FNMA Discount Notes	07/15/08	2.10	65,000,000	64,948,000

(continued)

**STATE CASH PORTFOLIO  
AS OF JUNE 30, 2008**

	Maturity	Yield to Maturity	Par Value	Fair Value
FNMA Discount Notes	07/21/08	1.66	100,000,000	99,880,000
FNMA Discount Notes	07/01/08	1.96	40,549,000	40,549,000
FNMA Discount Notes	07/01/08	1.96	18,688,000	18,688,000
FNMA Discount Notes	10/01/08	2.17	61,500,000	61,162,092
FNMA Discount Notes	09/02/08	2.16	47,138,500	46,961,141
Freddie Mac Discount Note	09/15/08	2.08	100,000,000	99,510,000
Freddie Mac Discount Note	09/15/08	2.10	78,542,000	78,157,144
Freddie Mac Discount Note	09/15/08	2.08	35,000,000	34,828,500
Freddie Mac Discount Note	11/10/08	3.63	13,184,000	13,064,025
Freddie Mac Discount Note	10/14/08	2.11	50,000,000	49,645,000
<b>TOTAL U.S. TREASURY AND AGENCY OBLIGATIONS</b>			<b>\$ 3,123,536,500</b>	<b>\$ 3,110,291,646</b>

	Maturity	Yield to Maturity	Par Value	Fair Value
<b>CERTIFICATES OF DEPOSIT</b>				
Community Bank & Trust, Ashland City	07/30/08	2.00 %	\$ 3,000,000	\$ 3,000,000
Community Bank & Trust, Ashland City	08/06/08	2.00	1,000,000	1,000,000
Community Bank & Trust, Ashland City	10/03/08	2.25	1,000,000	1,000,000
Community Bank & Trust, Ashland City	10/28/08	2.10	4,000,000	4,000,000
Community Bank & Trust, Ashland City	10/28/08	2.10	1,500,000	1,500,000
Community Bank & Trust, Ashland City	12/05/08	2.15	1,000,000	1,000,000
Community Bank & Trust, Ashland City	12/05/08	2.15	3,000,000	3,000,000
Community Bank & Trust, Ashland City	12/19/08	2.75	2,000,000	2,000,000
Bank of Crockett, Bells	10/24/08	2.25	200,000	200,000
Bank of Crockett, Bells	11/14/08	2.10	300,000	300,000
Bank of Crockett, Bells	12/19/08	2.75	1,000,000	1,000,000
Bank of Bradford	11/14/08	2.10	90,000	90,000
People's Bank and Trust Company, Byrdstown	07/22/08	3.44	100,000	100,000
People's Bank and Trust Company, Byrdstown	11/28/08	2.10	100,000	100,000
Citizens Bank, Carthage	09/30/08	2.10	4,000,000	4,000,000
First State Bank, Chapel Hill	11/25/08	2.10	200,000	200,000
CapitalMark Bank & Trust, Chattanooga	08/12/08	3.00	4,000,000	4,000,000
CapitalMark Bank & Trust, Chattanooga	09/12/08	2.85	2,000,000	2,000,000
CapitalMark Bank & Trust, Chattanooga	09/15/08	2.25	3,000,000	3,000,000
CapitalMark Bank & Trust, Chattanooga	11/04/08	2.10	4,000,000	4,000,000
CapitalMark Bank & Trust, Chattanooga	11/10/08	2.10	2,000,000	2,000,000
Legends Bank, Clarksville	09/11/08	2.25	1,000,000	1,000,000
Legends Bank, Clarksville	10/03/08	2.25	1,000,000	1,000,000
Legends Bank, Clarksville	10/27/08	2.10	1,000,000	1,000,000

(continued)

## STATE CASH PORTFOLIO AS OF JUNE 30, 2008

	Maturity	Yield to Maturity	Par Value	Fair Value
Legends Bank, Clarksville	12/04/08	2.75	1,000,000	1,000,000
Legends Bank, Clarksville	12/22/08	2.75	1,000,000	1,000,000
Bank of Cleveland	07/15/08	4.25	5,000,000	5,000,000
Bank of Cleveland	12/12/08	2.75	5,000,000	5,000,000
Bank of Cleveland	12/19/08	2.75	5,000,000	5,000,000
Community First Bank & Trust, Columbia	08/22/08	3.00	2,000,000	2,000,000
Community First Bank & Trust, Columbia	09/05/08	2.85	2,000,000	2,000,000
Community First Bank & Trust, Columbia	12/05/08	2.15	3,000,000	3,000,000
Community First Bank & Trust, Columbia	08/22/08	3.00	1,000,000	1,000,000
Putnam 1st Mercantile Bank, Cookeville	11/04/08	2.10	1,000,000	1,000,000
Community National Bank, Dayton	11/10/08	2.10	2,000,000	2,000,000
Community National Bank, Dayton	12/19/08	2.75	1,000,000	1,000,000
The Farmers & Merchant Bank, Dyer	07/25/08	2.00	2,500,000	2,500,000
The Farmers & Merchant Bank, Dyer	07/25/08	2.00	2,000,000	2,000,000
First Citizens National Bank, Dyersburg	11/14/08	2.10	3,000,000	3,000,000
First Citizens National Bank, Dyersburg	11/14/08	2.10	20,000,000	20,000,000
Security Bank, Dyersburg	09/19/08	2.25	300,000	300,000
Security Bank, Dyersburg	09/19/08	2.25	500,000	500,000
Security Bank, Dyersburg	09/19/08	2.25	450,000	450,000
Tennessee Commerce Bank, Franklin	07/08/08	4.25	500,000	500,000
Tennessee Commerce Bank, Franklin	08/22/08	3.00	2,500,000	2,500,000
Tennessee Commerce Bank, Franklin	08/22/08	3.00	2,000,000	2,000,000
Tennessee Commerce Bank, Franklin	08/26/08	2.85	1,750,000	1,750,000
Tennessee Commerce Bank, Franklin	09/08/08	2.85	3,500,000	3,500,000
Tennessee Commerce Bank, Franklin	09/08/08	2.25	2,500,000	2,500,000
Tennessee Commerce Bank, Franklin	09/11/08	2.25	3,500,000	3,500,000
Tennessee Commerce Bank, Franklin	09/12/08	2.85	3,000,000	3,000,000
Tennessee Commerce Bank, Franklin	09/12/08	2.85	3,000,000	3,000,000
Tennessee Commerce Bank, Franklin	09/12/08	2.85	500,000	500,000
Tennessee Commerce Bank, Franklin	09/12/08	2.85	500,000	500,000
Tennessee Commerce Bank, Franklin	09/12/08	2.85	1,000,000	1,000,000
Tennessee Commerce Bank, Franklin	10/03/08	2.25	2,500,000	2,500,000
Tennessee Commerce Bank, Franklin	10/20/08	2.25	3,500,000	3,500,000
Tennessee Commerce Bank, Franklin	10/27/08	2.10	1,500,000	1,500,000
Tennessee Commerce Bank, Franklin	12/09/08	2.15	750,000	750,000
Tennessee Commerce Bank, Franklin	12/09/08	2.15	200,000	200,000
Friendship Bank	11/28/08	2.10	50,000	50,000
Friendship Bank	11/28/08	2.10	525,000	525,000
Friendship Bank	11/28/08	2.10	1,550,000	1,550,000
Friendship Bank	12/12/08	2.75	375,000	375,000
Gates Banking and Trust Company	08/08/08	3.00	450,000	450,000
Gates Banking and Trust Company	08/19/08	3.00	500,000	500,000

(continued)

**STATE CASH PORTFOLIO  
AS OF JUNE 30, 2008**

	<b>Maturity</b>	<b>Yield to Maturity</b>	<b>Par Value</b>	<b>Fair Value</b>
Gates Banking and Trust Company	09/19/08	2.25	500,000	500,000
Gates Banking and Trust Company	09/19/08	2.25	500,000	500,000
Gates Banking and Trust Company	10/21/08	2.25	350,000	350,000
Trust One Bank, Germantown	07/14/08	2.85	3,000,000	3,000,000
Trust One Bank, Germantown	07/14/08	2.85	4,000,000	4,000,000
Trust One Bank, Germantown	08/15/08	2.25	2,000,000	2,000,000
Trust One Bank, Germantown	08/15/08	2.25	2,000,000	2,000,000
Trust One Bank, Germantown	08/15/08	2.25	2,000,000	2,000,000
Trust One Bank, Germantown	08/15/08	2.25	1,000,000	1,000,000
Trust One Bank, Germantown	11/07/08	2.10	6,000,000	6,000,000
Trust One Bank, Germantown	12/12/08	2.15	3,000,000	3,000,000
Trust One Bank, Germantown	12/12/08	2.15	1,000,000	1,000,000
Trust One Bank, Germantown	12/12/08	2.15	1,000,000	1,000,000
Trust One Bank, Germantown	12/12/08	2.15	3,000,000	3,000,000
Bank of Gleason	07/25/08	3.50	1,000,000	1,000,000
Bank of Gleason	07/25/08	3.50	1,000,000	1,000,000
Bank of Gleason	09/09/08	2.81	300,000	300,000
Bank of Gleason	11/18/08	2.10	750,000	750,000
Bank of Gleason	11/28/08	2.10	350,000	350,000
Bank of Halls	09/19/08	2.25	200,000	200,000
Bank of Halls	09/26/08	2.25	300,000	300,000
Bank of Halls	11/10/08	2.10	500,000	500,000
Bank of Halls	12/05/08	2.15	1,000,000	1,000,000
Bank of Halls	12/05/08	2.15	200,000	200,000
Bank of Halls	12/05/08	2.15	400,000	400,000
Bank of Halls	12/09/08	2.15	1,000,000	1,000,000
Bank of Halls	12/19/08	2.75	700,000	700,000
First State Bank, Henderson	07/21/08	3.50	1,000,000	1,000,000
American Security Bank and Trust Company, Hendersonville	07/07/08	2.00	500,000	500,000
American Security Bank and Trust Company, Hendersonville	11/14/08	2.10	2,000,000	2,000,000
American Security Bank and Trust Company, Hendersonville	12/09/08	2.15	500,000	500,000
American Security Bank and Trust Company, Hendersonville	12/09/08	2.15	200,000	200,000
American Security Bank and Trust Company, Hendersonville	12/09/08	2.15	200,000	200,000
American Security Bank and Trust Company, Hendersonville	12/22/08	2.75	2,500,000	2,500,000
Bank of Jackson	09/18/08	2.25	1,000,000	1,000,000
Bank of Jackson	09/19/08	2.25	1,000,000	1,000,000
Bank of Jackson	09/19/08	2.25	500,000	500,000
First Volunteer Bank, Jamestown	08/15/08	2.00	500,000	500,000
First Volunteer Bank, Jamestown	08/15/08	2.00	500,000	500,000
First Volunteer Bank, Jamestown	08/15/08	2.00	300,000	300,000
First Volunteer Bank, Jamestown	08/15/08	2.00	200,000	200,000
First Volunteer Bank, Jamestown	08/15/08	2.00	500,000	500,000

*(continued)*

## STATE CASH PORTFOLIO AS OF JUNE 30, 2008

	Maturity	Yield to Maturity	Par Value	Fair Value
First Volunteer Bank, Jamestown	08/15/08	2.00	450,000	450,000
Citizens State Bank, Jasper	08/01/08	3.00	200,000	200,000
Citizens State Bank, Jasper	08/19/08	3.00	100,000	100,000
Citizens State Bank, Jasper	08/19/08	3.00	200,000	200,000
BankEast, Knoxville	07/07/08	2.00	5,000,000	5,000,000
BankEast, Knoxville	07/07/08	2.00	2,000,000	2,000,000
BankEast, Knoxville	07/07/08	2.00	8,000,000	8,000,000
BankEast, Knoxville	07/07/08	2.00	5,000,000	5,000,000
BankEast, Knoxville	07/07/08	2.00	5,000,000	5,000,000
BB& T, Knoxville	08/08/08	2.25	20,000,000	20,000,000
BB& T, Knoxville	09/16/08	2.25	75,000,000	75,000,000
BB& T, Knoxville	10/31/08	2.10	40,000,000	40,000,000
BB& T, Knoxville	12/05/08	2.15	100,000,000	100,000,000
BB& T, Knoxville	07/03/08	4.25	100,000,000	100,000,000
BB& T, Knoxville	10/03/08	2.25	100,000,000	100,000,000
Citizens Bank of Lafayette	07/15/08	4.25	250,000	250,000
Citizens Bank of Lafayette	12/19/08	2.75	100,000	100,000
United Community Bank, Lenior City	07/25/08	3.50	500,000	500,000
United Community Bank, Lenior City	12/02/08	2.15	500,000	500,000
The Coffee County Bank, Manchester	09/27/08	2.25	95,000	95,000
Planters Bank of Tennessee, Maury City	10/28/08	2.10	200,000	200,000
The First National Bank of McMinnville	07/17/08	2.00	9,000,000	9,000,000
Cadence Bank, Memphis	10/28/08	2.10	3,000,000	3,000,000
Cadence Bank, Memphis	10/28/08	2.10	2,000,000	2,000,000
Cadence Bank, Memphis	10/28/08	2.10	2,000,000	2,000,000
Cadence Bank, Memphis	10/28/08	2.10	3,000,000	3,000,000
Cadence Bank, Memphis	10/28/08	2.10	2,000,000	2,000,000
Cadence Bank, Memphis	10/28/08	2.10	5,000,000	5,000,000
Cadence Bank, Memphis	10/28/08	2.10	5,000,000	5,000,000
Cadence Bank, Memphis	10/28/08	2.10	5,000,000	5,000,000
Cadence Bank, Memphis	10/28/08	2.10	5,000,000	5,000,000
Cadence Bank, Memphis	10/28/08	2.10	2,500,000	2,500,000
Cadence Bank, Memphis	10/28/08	2.10	1,000,000	1,000,000
Landmark Community Bank, Memphis	10/28/08	2.10	2,000,000	2,000,000
Independent Bank, Memphis	09/19/08	2.25	10,000,000	10,000,000
Independent Bank, Memphis	09/19/08	2.25	1,000,000	1,000,000
Independent Bank, Memphis	09/19/08	2.25	3,000,000	3,000,000
Independent Bank, Memphis	09/19/08	2.25	3,000,000	3,000,000
Independent Bank, Memphis	09/19/08	2.25	4,000,000	4,000,000
Independent Bank, Memphis	09/29/08	2.25	5,000,000	5,000,000
Paragon National Bank, Memphis	08/08/08	3.00	5,000,000	5,000,000
Paragon National Bank, Memphis	11/18/08	2.10	5,000,000	5,000,000

(continued)

**STATE CASH PORTFOLIO  
AS OF JUNE 30, 2008**

	<b>Maturity</b>	<b>Yield to Maturity</b>	<b>Par Value</b>	<b>Fair Value</b>
Paragon National Bank, Memphis	11/25/08	2.10	3,000,000	3,000,000
Paragon National Bank, Memphis	12/02/08	2.15	1,000,000	1,000,000
Renasant Bank, Memphis	07/08/08	2.00	4,000,000	4,000,000
Renasant Bank, Memphis	07/11/08	2.00	2,500,000	2,500,000
Renasant Bank, Memphis	07/14/08	2.00	1,000,000	1,000,000
Renasant Bank, Memphis	07/14/08	2.00	3,000,000	3,000,000
Renasant Bank, Memphis	07/15/08	2.00	2,000,000	2,000,000
Renasant Bank, Memphis	07/15/08	2.00	5,000,000	5,000,000
Renasant Bank, Memphis	07/15/08	2.00	1,000,000	1,000,000
Renasant Bank, Memphis	07/18/08	2.00	4,000,000	4,000,000
Renasant Bank, Memphis	07/18/08	2.00	5,000,000	5,000,000
Renasant Bank, Memphis	07/21/08	2.00	3,000,000	3,000,000
Renasant Bank, Memphis	07/22/08	2.00	3,000,000	3,000,000
Renasant Bank, Memphis	07/28/08	2.00	1,000,000	1,000,000
Renasant Bank, Memphis	07/31/08	2.00	3,500,000	3,500,000
Patriot Bank, Millington	10/31/08	2.10	1,500,000	1,500,000
Regions, Nashville	08/06/08	2.39	100,000,000	100,000,000
Regions, Nashville	09/03/08	2.10	50,000,000	50,000,000
Regions, Nashville	12/05/08	2.15	50,000,000	50,000,000
Regions, Nashville	12/05/08	2.15	100,000,000	100,000,000
Regions, Nashville	12/05/08	2.15	50,000,000	50,000,000
Regions, Nashville	12/05/08	2.15	100,000,000	100,000,000
Bank of Nashville	10/31/08	2.10	5,000,000	5,000,000
Bank of Nashville	10/31/08	2.10	20,000,000	20,000,000
Bank of Nashville	11/04/08	2.10	5,000,000	5,000,000
Civic Bank & Trust, Nashville	10/24/08	2.25	1,000,000	1,000,000
Fifth Third Bank, Nashville	07/14/08	2.25	25,000,000	25,000,000
Fifth Third Bank, Nashville	07/14/08	2.25	30,000,000	30,000,000
Fifth Third Bank, Nashville	09/15/08	2.25	50,000,000	50,000,000
Fifth Third Bank, Nashville	10/31/08	2.10	25,000,000	25,000,000
Fifth Third Bank, Nashville	11/07/08	2.10	25,000,000	25,000,000
Fifth Third Bank, Nashville	11/07/08	2.10	25,000,000	25,000,000
Fifth Third Bank, Nashville	11/07/08	2.10	25,000,000	25,000,000
Fifth Third Bank, Nashville	12/12/08	2.15	50,000,000	50,000,000
Pinnacle National Bank, Nashville	07/23/08	2.00	15,000,000	15,000,000
Pinnacle National Bank, Nashville	08/20/08	2.00	25,000,000	25,000,000
Pinnacle National Bank, Nashville	08/20/08	2.00	25,000,000	25,000,000
Pinnacle National Bank, Nashville	08/22/08	2.25	10,000,000	10,000,000
Pinnacle National Bank, Nashville	10/27/08	2.10	5,000,000	5,000,000
Pinnacle National Bank, Nashville	10/27/08	2.10	10,000,000	10,000,000
Pinnacle National Bank, Nashville	10/27/08	2.10	5,000,000	5,000,000
Pinnacle National Bank, Nashville	10/27/08	2.10	20,000,000	20,000,000

(continued)

## STATE CASH PORTFOLIO AS OF JUNE 30, 2008

	Maturity	Yield to Maturity	Par Value	Fair Value
Pinnacle National Bank, Nashville	10/27/08	2.10	20,000,000	20,000,000
Pinnacle National Bank, Nashville	10/27/08	2.10	5,000,000	5,000,000
Pinnacle National Bank, Nashville	10/27/08	2.10	10,000,000	10,000,000
Pinnacle National Bank, Nashville	10/27/08	2.10	5,000,000	5,000,000
Pinnacle National Bank, Nashville	11/28/08	2.10	10,000,000	10,000,000
Pinnacle National Bank, Nashville	12/01/08	2.15	10,000,000	10,000,000
US Bank, Nashville	09/26/08	2.25	150,000,000	150,000,000
US Bank, Nashville	10/03/08	2.25	100,000,000	100,000,000
US Bank, Nashville	11/18/08	2.10	100,000,000	100,000,000
US Bank, Nashville	11/18/08	2.10	250,000,000	250,000,000
US Bank, Nashville	12/09/08	2.15	50,000,000	50,000,000
US Bank, Nashville	12/12/08	2.15	50,000,000	50,000,000
Newport Federal Bank	07/14/08	4.25	500,000	500,000
Newport Federal Bank	07/14/08	4.25	500,000	500,000
Newport Federal Bank	09/22/08	2.25	95,000	95,000
Newport Federal Bank	09/22/08	2.25	300,000	300,000
Community Trust & Banking Company, Ooltewah	07/11/08	4.25	500,000	500,000
Community Trust & Banking Company, Ooltewah	10/28/08	2.10	500,000	500,000
Community Trust & Banking Company, Ooltewah	12/12/08	2.75	500,000	500,000
Tennessee State Bank, Pigeon Forge	10/27/08	2.10	10,000,000	10,000,000
Tennessee State Bank, Pigeon Forge	10/27/08	2.10	20,000,000	20,000,000
Tennessee State Bank, Pigeon Forge	10/27/08	2.10	10,000,000	10,000,000
Tennessee State Bank, Pigeon Forge	10/27/08	2.10	15,000,000	15,000,000
First National Bank of Pulaski	11/14/08	2.10	2,000,000	2,000,000
First National Bank of Pulaski	11/18/08	2.10	300,000	300,000
First National Bank of Pulaski	11/18/08	2.10	700,000	700,000
First National Bank of Pulaski	11/18/08	2.10	500,000	500,000
First National Bank of Pulaski	11/21/08	2.10	500,000	500,000
First National Bank of Pulaski	11/21/08	2.10	300,000	300,000
First National Bank of Pulaski	11/25/08	2.10	300,000	300,000
First National Bank of Pulaski	11/25/08	2.10	1,000,000	1,000,000
First National Bank of Pulaski	11/28/08	2.10	1,000,000	1,000,000
First National Bank of Pulaski	11/28/08	2.10	1,000,000	1,000,000
First National Bank of Pulaski	12/12/08	2.15	2,000,000	2,000,000
First National Bank of Pulaski	12/19/08	2.75	6,000,000	6,000,000
First National Bank of Pulaski	12/23/08	2.75	10,000,000	10,000,000
Bank of Ripley	08/01/08	2.00	400,000	400,000
The People's Bank, Sardis	11/25/08	2.10	2,000,000	2,000,000
The Hardin County Bank, Savannah	07/15/08	4.25	1,000,000	1,000,000
Commerce Union Bank, Springfield	10/23/08	2.50	3,000,000	3,000,000
Citizens City & County Bank, Trenton	11/18/08	2.10	95,000	95,000

(continued)

**STATE CASH PORTFOLIO  
AS OF JUNE 30, 2008**

	Maturity	Yield to Maturity	Par Value	Fair Value
First State Bank, Union City	08/20/08	2.00	2,000,000	2,000,000
First State Bank, Union City	10/27/08	2.10	2,500,000	2,500,000
First State Bank, Union City	10/28/08	2.10	5,000,000	5,000,000
First State Bank, Union City	10/28/08	2.10	1,000,000	1,000,000
First State Bank, Union City	10/31/08	2.10	3,000,000	3,000,000
First State Bank, Union City	11/18/08	2.10	2,000,000	2,000,000
First State Bank, Union City	12/22/08	2.75	3,000,000	3,000,000
First State Bank, Union City	12/22/08	2.75	3,000,000	3,000,000
Wayne County Bank, Waynesboro	10/10/08	2.25	500,000	500,000
Wayne County Bank, Waynesboro	11/10/08	2.10	900,000	900,000
<b>TOTAL CERTIFICATES OF DEPOSIT</b>			<b>\$ 2,495,325,000</b>	<b>\$ 2,495,325,000</b>

**OVERNIGHT DEPOSIT ACCOUNTS**

Regions Bank - Overnight Deposit Account	07/01/08	2.13%	\$ 417,127,384	\$ 417,127,384
<b>TOTAL OVERNIGHT DEPOSIT ACCOUNTS</b>			<b>\$ 417,127,384</b>	<b>\$ 417,127,384</b>

	Rating	Maturity	Par Value	Fair Value
<b>COMMERCIAL PAPER</b>				
American Express	A1	07/01/08	\$ 50,000,000	\$ 50,000,000
American General	A1	07/01/08	350,000,000	350,000,000
B A S F	A1	07/14/08	50,000,000	49,962,445
B A S F	A1	07/17/08	50,000,000	49,953,333
B M W	A1	07/01/08	150,000,000	150,000,000
B M W	A1	07/01/08	25,000,000	25,000,000
Cargill Global	A1	07/01/08	40,000,000	40,000,000
Cargill Global	A1	07/01/08	50,000,000	50,000,000
Cargill Global	A1	07/01/08	50,000,000	50,000,000
DuPont	A1	07/11/08	50,000,000	49,971,528
G E	A1	07/01/08	35,000,000	35,000,000
G E	A1	07/09/08	100,000,000	99,949,333
H S B C	A1	07/01/08	300,000,000	300,000,000
Merrill Lynch	A1	07/01/08	450,000,000	450,000,000
Metlife	A1	07/09/08	16,000,000	15,992,533
Nestle	A1	07/01/08	350,000,000	350,000,000
Nestle	A1	07/10/08	50,000,000	49,973,375
Nestle	A1	07/16/08	50,000,000	49,955,625
Toyota	A1	07/01/08	450,000,000	450,000,000
<b>TOTAL COMMERCIAL PAPER</b>			<b>\$ 2,666,000,000</b>	<b>\$ 2,665,758,172</b>

<b>TOTAL STATE CASH PORTFOLIO</b>			<b>\$ 8,701,988,884</b>	<b>\$ 8,688,502,202</b>
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**BACCALAUREATE EDUCATION SYSTEM TRUST PORTFOLIO**


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**BACCALAUREATE EDUCATION SYSTEM TRUST PORTFOLIO**
*as of June 30, 2008*

<b>Fixed Mutual Funds</b>	<b>Units</b>	<b>Fair Value</b>
State Street Lehman Aggregate Index	3,337,650	\$ <u>41,233,334</u>
<b>TOTAL FIXED INCOME MUTUAL FUNDS</b>		\$ <u>41,233,334</u>

<b>Equity Mutual Funds</b>	<b>Units</b>	<b>Fair Value</b>
State Street S&P 500 Index Fund	549,749	\$ 30,423,660
State Street MSCI EAFE Index Fund	980,181	16,640,536
Northern Institutional Fund	2,040,325	<u>2,040,325</u>
<b>TOTAL EQUITY MUTUAL FUNDS</b>		\$ <u>49,104,521</u>

**TOTAL PORTFOLIO** \$ 90,337,855

## CHAIRS OF EXCELLENCE LARGEST HOLDINGS

## LARGEST BOND HOLDINGS

as of June 30, 2008

by Fair Value

Par Value	Security Name	Yield at Market	Maturity	Moody's Quality Rating	Fair Value
\$ 9,200,000	US Treasury Notes Index Linked	4.37%	01/15/16	Aaa	\$ 10,490,806
5,000,000	US Treasury Notes Inflation Indexed	3.11	01/15/12	Aaa	6,679,205
4,770,000	US Treasury Bonds Infl IX Bond	5.69	01/15/26	Aaa	5,112,208
4,500,000	Pvtpl CMO Bear Stearns Coml Mtg Inc	3.37	05/14/16	Aaa	4,574,911
3,500,000	US Treasury Bonds DTD	4.65	05/15/30	Aaa	4,308,006
3,941,223	FNMA Pool #745250	5.30	01/01/21	NR	3,916,551
3,772,403	FNMA Pool #867662	5.50	05/01/36	NR	3,889,046
3,310,051	FNMA Pool #839272	5.91	09/01/35	NR	3,272,747
2,500,000	US Treasury Notes DTD	3.59	11/15/15	Aaa	2,632,812
2,676,044	FNMA Pool #829070	5.34	09/01/20	NR	2,603,630

A complete portfolio listing is available upon request

Mutual Funds	Units	Fair Value
State Street S&P 500 Index Fund	1,500,424	\$ 83,034,997
State Street MCSI EAFE Index Fund	2,310,936	39,232,762
Northern Institutional Fund	6,880,110	6,880,110
<b>TOTAL MUTUAL FUNDS</b>		<b>\$ 129,147,869</b>

Key to Ratings: All ratings presented are from Moody's Investors Service with the exception of some of the government agency securities. Moody's does not rate these securities. Standard & Poor's does provide ratings for the securities (AAA is Standard & Poor's highest rating.) Government Securities are not rated per se<sup>1</sup> but are considered the best quality securities.

Moody's rates securities as follows:

Aaa	Best Quality
Aa	High Quality
A	Upper Medium Quality
Baa	Medium Quality
NR	Not Rated

# TREASURER'S REPORT

*Programs*

**BACCALAUREATE EDUCATION SYSTEM TRUST****BACCALAUREATE EDUCATION SYSTEM TRUST**

*Tennessee Code Annotated*, Title 49, Chapter 7, Part 8 sets forth the Tennessee Baccalaureate Education System Trust (BEST) Act. The Act creates a tuition program, as an agency and instrumentality of the State of Tennessee, under which parents and other interested persons may assist students in saving for tuition cost of attending colleges and universities. The tuition program is known as the BEST Program and is comprised of two types of tuition plans: The BEST Savings Plan and the BEST Prepaid College Tuition Plan. On May 30, 2008, the BEST Savings Plan was closed in an effort to provide customers in the plan a wider range of investment options and lower fees. Effective June 1, 2008, BEST contracted with the Georgia Higher Education Savings Plan to offer the Path2College 529 Plan to Tennesseans.

The federal guidelines for both 529 plans are contained in Section 529 of the *Internal Revenue Code*. The requirements for participation and administration of the Prepaid College Tuition Plan are contained in *Chapter 1700-5-1 of the Official Compilation of the Rules and Regulations of the State of Tennessee*.

The BEST program offers several favorable tax benefits to its participants. BEST contracts are exempt from all federal, state and local taxes if used for qualified education expenses. In addition, earnings on any distribution used to pay for qualified higher education expenses are exempt from taxation. The maximum account limit for a beneficiary in the BEST Prepaid program is \$235,000. Additionally, the maximum account balance limit for the Path2College 529 Plan is \$235,000.

**BEST PREPAID COLLEGE TUITION PLAN**

The BEST Prepaid College Tuition Plan allows anyone to pay for higher education tuition in advance on behalf of a beneficiary. Tuition and mandatory fees may be purchased in increments known as tuition

units. One tuition unit represents a value of one percent of the weighted average undergraduate tuition at Tennessee's four-year public universities plus an amount to cover administration and actuarial soundness of the program. The cost for one academic year of tuition at the average-priced, four-year undergraduate Tennessee public university will be covered by approximately 100 tuition units. Higher education institutions that cost more than the average Tennessee four-year public university will require more units; those that cost less will require fewer units.

The person who opens the account or the child must be a resident of Tennessee when the tuition account is opened, and enrollment is open to anyone who meets the residency requirement. There is no age limit for enrollment; however, the beneficiary must be born, and tuition units must be on account with BEST for at least two years prior to use. The purchase of one unit is required at the time of enrollment; however, flexibility is a key component of the program by allowing participants to determine when and how much to save. Participants have several payment options including cash, check, payroll deduction and automatic bank withdrawal.

Qualified expenses include tuition, fees, supplies, books, room and board, and supplies and equipment required for enrollment or attendance. The units may be used at any accredited higher education institution -- in-state or out-of-state, public or private. They may also be used at vocational and technical schools or professional and graduate schools. Participants do not have to choose a specific school when they enroll in the program.

Interested parties and participants may utilize BEST's website for program information, located at [www.tn.gov/treasury/best](http://www.tn.gov/treasury/best), to learn about the program. The site features the contract application, which can be downloaded, completed, and mailed to the BEST office. Questions or comments to BEST staff can be e-mailed through this site.

**BACCALAUREATE EDUCATION SYSTEM TRUST**

The Baccalaureate Education System Trust prepaid program began accepting contracts and contributions in June 1997. At June 30, 2008, BEST had 8,941 contracts with net assets totaling \$90.1 million. The unit price for the August 1, 2007 – December 31, 2007 enrollment period was \$61.48 per unit. The unit price increased to \$63.63 per unit for the January 1, 2008 – July 31, 2008 enrollment period. The BEST Board annually adjusts the unit purchase price and unit payout price to reflect the current weighted average tuition of Tennessee’s public colleges and universities.

From the first payout in Fall 1999, the BEST Prepaid program has issued \$13.4 million in payments to colleges and universities.

**Path2College 529 Plan**

Anyone interested in investing for a college education can open an account on a child’s behalf in the Path2College 529 College Savings Plan. There are

no residency requirements. The account can be used to pay for qualified higher education expenses at any eligible college, university, trade or vocational school, or other post-secondary institution in the State of Tennessee or anywhere in the country, and at certain schools abroad. Qualified expenses include tuition, fees, supplies, books, certain room and board expenses, and equipment required for enrollment or attendance.

The Path2College 529 Plan, established by the Georgia Higher Education Saving Plan, offers seven investment options: The Managed Allocation Option, the Aggressive Managed Allocation Option, the 100% Equity Option, the Balance Fund Option, the Fixed Income Option, the Guaranteed Option and the Money Market Option. There are no enrollment or administrative fees. Annual asset-based fees range from 50-76 basis points.

**PREPAID TUITION PLAN**

*History of Per Unit Payout, Prices and Fees*

<u>Enrollment Fiscal Year</u>	<u>Unit Payout</u>	<u>Administrative Fee</u>	<u>Actuarial Soundness</u>	<u>Unit Price (Aug. 1-Dec. 31)</u>	<u>Adjustment for Purchases after Dec. 31*</u>	<u>Unit Price (Jan. 1-July 31)</u>
1998	\$ 21.64	\$ 2.11	\$ 0.00	\$ 23.75	\$ 0.00	\$ 23.75
1999	25.00	1.75	0.00	26.75	1.25	28.00
2000	27.08	1.92	0.00	29.00	1.25	30.25
2001	29.58	1.92	0.00	31.50	1.50	33.00
2002	33.51	0.99	0.00	34.50	2.35	36.85
2003	35.98	1.02	0.00	37.00	1.40	38.40
2004	40.70	1.30	0.00	42.00	1.60	43.60
2005	43.15	2.10	3.71	48.96	1.84	50.80
2006	47.71	2.28	4.07	54.06	2.03	56.09
2007	49.72	2.98	4.24	56.94	2.14	59.08
2008	53.79	3.13	4.56	61.48	2.15	63.63
2009	56.93	3.87	4.86	65.66	2.05	67.71

\* Adjustment equal to 1/2 earnings rate assumption.

**CAREERS NOW PROGRAM****CAREERS NOW PROGRAM**

College students in Tennessee have the opportunity to learn more about the operation of state government and the various career opportunities in state government through the Careers NOW Program. Students in the program work in one of the three constitutional offices for a semester. The Treasurer, the Comptroller of the Treasury, and the Secretary of State work together to match opportunities with students' interests.

Since the program's inception in 1996, over 255 students have been selected to participate. New classes begin each spring and summer semester.

The goal of the program is to develop a pool of students who, upon graduation, will be candidates for career positions in one of the three constitutional offices. Twenty-two percent of our students have been hired in full time positions in the three constitutional offices and throughout state government. The students receive hands on work experience and the participating institutions and constitutional offices jointly facilitate the development of a detailed curriculum to meet the academic commitment made to higher education institutions.

Careers NOW is designed to offer students a combination of practical work experience and formal training, while giving them the opportunity to see the challenges of public service. In addition to their daily work responsibilities, students attend seminars, visit state agencies, complete written work assignments, engage in opportunities to increase their overall understanding and knowledge of Tennessee state government, and research a current government issue for their special project. Past projects selected by students have included voter registration and election issues, Internet voting, prisons and capital punishment, and higher education issues.

To be eligible for the program, students must be classified as juniors, seniors, or graduate students and have a "B" average or better. Major fields of study may include Accounting, Business Administration, Computer Science, Economics, English, Finance,

Geoscience, History, Journalism, Law, Library Science, Management Information Systems, Marketing, Math, Political Science, Public Administration, Public Relations, Social Science, and related fields. Previously, students have been required to be enrolled in a college or university located within Tennessee.

Applicants have come from Austin Peay State University, East Tennessee State University, Fisk University, David Lipscomb University, Middle Tennessee State University, Rhodes College, Tennessee State University, Tennessee Technological University, University of Memphis, University of Tennessee at Martin, University of Tennessee at Knoxville, University of the South, Carson Newman College and Vanderbilt University. The majority of the participants have been Business or Accounting majors and have come from Middle Tennessee State University, Tennessee State University and Tennessee Technological University. Approximately 40 percent of the student participants have been minorities and 38 percent of the students have come from Tennessee State University.

The Careers NOW Program accepts Tennessee residents who are attending out-of-state colleges and universities including University of North Alabama, St. Louis University, Furman University, Centre College, College of William and Mary, University of Washington and Samford University. The expectation is that the program will benefit from a broadened base of experience and that the students will benefit from the opportunity to gain experience in state government leading to permanent employment opportunities in their home state of Tennessee.

Current program information, assignment descriptions, and program application forms are available on the Internet at [www.tn.gov/treasury/now](http://www.tn.gov/treasury/now).

**CERTIFIED PUBLIC ADMINISTRATOR  
EDUCATIONAL INCENTIVE PAYMENT PROGRAM**

**CERTIFIED PUBLIC ADMINISTRATOR**

The University of Tennessee Institute for Public Service administers the "County Official's Certificate Training Program Act." Certain full-time county officers are eligible for an educational incentive payment if the officers have completed the continuing education requirements of the program. The UT Institute for Public Service is required to provide the Treasurer's office a listing of those officers who have successfully completed all levels of the County Officials Certificate Training Program. The educational incentive payments are issued by the State Treasurer. The State

Treasurer must issue such payments no later than October 31 of each year. The program began in 1998.

For the 2007-08 fiscal year, there were 287 officers that received the \$1,500 educational incentive payment. The total paid to all officers was \$ 430,500. The following table represents the number of payments by position.

<b>Officer</b>	<b>Number Receiving Payment</b>
Assessor of Property	31
Circuit Court Clerk	37
Clerk & Master	45
County Clerk	36
County Mayor/County Executive	24
Criminal Court Clerk	2
General Sessions Court Clerk	2
Chief Administrative Officer of Highways	9
Juvenile Court Clerk	3
Probate Court Clerk	1
Register of Deeds	44
Sheriff	2
Trustee	<u>51</u>
<b>TOTAL</b>	<b><u>287</u></b>

**CERTIFIED PUBLIC ADMINISTRATOR  
EDUCATIONAL INCENTIVE PAYMENT PROGRAM**

**FIVE YEAR INCENTIVE PAYMENT HISTORY**  
*Fiscal Years 2004-2008*

Fiscal Year Ended June 30	Recipients
2008	287
2007	282
2006	288
2005	274
2004	265

**COUNTY PROVIDED INCENTIVE PAYMENT**

Each county is encouraged and authorized to provide in its annual budget for payment of an annual educational incentive to certain employees who attain the designation of a "certified public administrator" in an amount not to exceed \$3,000 less any incentive payment made by the State Treasurer. Such payments

shall be paid by the county by October 31 of each year. The County Mayors shall provide to the State Treasurer the amount of any educational incentive paid by the county and the number of persons receiving such incentive.

Summary information is provided below:

Number of counties that provided an incentive	15
Number of counties that did not provide an incentive	58
Number of counties that did not provide information	<u>22</u>
Total	<u>95</u>
Total amount of incentives paid	\$ 198,645
Total number of recipients	184
Average amount of incentive that was paid	\$ 1,080

**CHAIRS OF EXCELLENCE TRUST**

**CHAIRS OF EXCELLENCE TRUST**

The Chairs of Excellence (COE) Trust provides funds with which state colleges and universities are able to contract with persons of regional or national prominence to teach in specified academic areas. The program is open to all state four-year colleges and universities, and the UT Space Institute.

The funding of the program is provided through

contributions (corpus) made by a private donor and a matching amount by the state, thus, creating a chair. A chair is authorized to spend 4% of the 3-year average market value of the chair. However, the corpus can not be spent.

Since the beginning of the program in 1984, there have been 99 chairs created, with state appropriations totaling \$44 million and matching contributions totaling \$55.9 million.

**FIVE YEAR HISTORY**

*Fiscal Years 2004-2008*

<b>Fiscal Year</b>	<b>Investment Income</b>	<b>Total Spending of the Chairs</b>	<b>Asset Balance</b>
2008	\$ (7,631,048)	\$ 7,368,032	\$ 236,954,830
2007	33,163,435	6,515,606	252,447,384
2006	12,471,255	6,689,303	226,159,791
2005	11,749,363	6,032,346	220,507,071
2004	16,953,010	6,862,657	214,975,481

**ANNUALIZED INVESTMENT RETURN**

	<b>1 Year</b>	<b>5 Years</b>	<b>10 Years</b>
Domestic Equity	(13.10%)	7.60%	2.58%
International Equity	(10.59 )	-	-
Fixed Income	9.21	3.58	5.61
Short-Term	4.92	3.49	3.86
Total Portfolio	(3.08 )	6.00	4.45

## CHAIRS OF EXCELLENCE TRUST

## AUTHORIZED CHAIRS OF EXCELLENCE

## THE UNIVERSITY OF TENNESSEE

*Chattanooga*

Miller COE in Management & Technology  
 Sun Trust Bank COE in the Humanities  
 Provident Life & Accident Ins. Co. COE in  
 Applied Math  
 West COE in Communications & Public Affairs  
 COE in Judaic Studies  
 Cline COE in Rehabilitation Technology  
 Frierson COE in Business Leadership  
 Harris COE in Business  
 Lyndhurst COE in Arts Education  
 McKee COE in Dyslexic Research & Exceptional In-  
 struction

*Knoxville*

Racheff Chair of Ornamental Horticulture  
 Racheff Chair of Material Science & Engineering  
 COE in English  
 Condra COE in Computer Integrated  
 Engineering & Manufacturing  
 Condra COE in Power Electronics Applications  
 Pilot COE in Management  
 Holly COE in Political Economy  
 Schmitt COE in History  
 COE in Science, Technology & Medical Writing  
 Shumway COE in Romance Languages  
 Goodrich COE in Civil Engineering  
 Clayton Homes COE in Finance  
 COE in Policy Studies  
 Blasingame COE in Agricultural Policy Studies  
 Lincoln COE in Physics  
 Hunger COE in Environmental Studies

*Martin*

Hendrix COE in Free Enterprise & Economics  
 Dunagan COE in Banking  
 Parker COE in Food & Fiber Industries

*Memphis*

Van Vleet COE in Microbiology & Immunology  
 Van Vleet COE in Pharmacology  
 Van Vleet COE in Biochemistry  
 Van Vleet COE in Virology  
 Muirhead COE in Pathology  
 COE in Obstetrics & Gynecology  
 LeBonheur COE in Pediatrics  
 Crippled Children's Hospital COE in  
 Biomedical Engineering  
 Plough COE in Pediatrics  
 Gerwin COE in Physiology  
 Hyde COE in Rehabilitation

Dunavant COE in Pediatrics  
 First Tennessee Bank COE in Pediatrics  
 Federal Express COE in Pediatrics  
 Semmes-Murphey COE in Neurology  
 Bronstein COE in Cardiovascular Physiology  
 Goodman COE in Medicine  
 LeBonheur COE in Pediatrics (II)  
 Soloway COE in Urology

*Space Institute*

Boling COE in Space Propulsion  
 H. H. Arnold COE in Computational Mechanics

## TENNESSEE BOARD OF REGENTS

*Austin Peay State University*

Acuff COE in Creative Arts  
 Harper/James and Bourne COE in Business  
 The Foundation Chair of Free Enterprise  
 Reuther COE in Nursing

*East Tennessee State University*

Quillen COE of Medicine in Geriatrics  
 & Gerontology  
 AFG Industries COE in Business & Technology  
 Harris COE in Business  
 Long Chair of Surgical Research  
 Dishner COE in Medicine  
 Quillen COE in Teaching and Learning  
 Basler COE for Integration of Arts, Rhetoric, and Sci-  
 ences  
 Leeanne Brown and Universities Physicians  
 Group COE in General Pediatrics

*Middle Tennessee State University*

Seigenthaler Chair of First Amendment Studies  
 Jones Chair of Free Enterprise  
 Adams COE in Health Care Services  
 National Healthcorp COE in Nursing  
 Russell COE in Manufacturing Excellence  
 Murfree Chair of Dyslexic Studies  
 Miller COE in Equine Health  
 Miller COE in Equine Reproductive Physiology  
 Jones COE in Urban & Regional Planning

*Tennessee State University*

Frist COE in Business Administration  
 COE in Banking & Finance

*Tennessee Technological University*

Owen Chair of Business Administration  
 Mayberry Chair of Business Administration

*University of Memphis*

COE in Molecular Biology  
 Herff COE in Law

## CHAIRS OF EXCELLENCE TRUST

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Fogelman COE in Real Estate  
Sales & Marketing Executives of Memphis  
COE in Sales  
COE in Accounting  
Arthur Andersen Company Alumni COE in  
Accounting  
Moss COE in Philosophy  
Wunderlich COE in Finance  
Herff COE in Biomedical Engineering  
Bornblum COE in Judaic Studies  
Shelby County Government COE in  
International Economics  
Wang COE in International Business  
COE in Free Enterprise Management  
COE in English Poetry

Herff COE in Computer Engineering  
Lowenberg COE in Nursing  
COE in Art History  
Federal Express COE in Management  
Information Systems  
Moss COE in Psychology  
Moss COE in Education  
Hardin COE in Combinatorics  
Hardin COE in Economics/Managerial  
Journalism  
Sparks COE in International Relations  
Plough COE in Audiology & Speech Language  
Pathology

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## CLAIMS AGAINST THE STATE

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### CLAIMS AGAINST THE STATE

The primary function of the Division of Claims Administration, Board of Claims, and Tennessee Claims Commission is to provide an avenue for persons who have been damaged by the state to be heard and, if appropriate, compensated for their loss or damage. All claims are paid through the Risk Management Fund. This fund is supported by premiums paid by each state department, agency and institution. The required funding is based upon an actuarial study which reflects risk assessment and estimated losses.

The Division of Claims Administration processes claims filed against the state for the negligent operation of motor vehicles or machinery; negligent care, custody and control of persons or property; professional malpractice; workers' compensation claims by state employees; dangerous conditions on state maintained highways and bridges; and nuisances created or maintained by the state. The Division of Claims Administration operates in conjunction with the Attorney General's Office and the Tennessee Claims Commission in this claims process.

The Division of Claims Administration contracts with a third party administrator for the processing of workers' compensation claims. The division's staff monitors the work done by the third party administrator and acts as a liaison between state employees and the third party administrator. For claims occurring on or after July 1, 2005, worker's compensation claim disputes are filed with the Department of Labor and Workforce Development's Benefit Review Conference program for possible resolution without litigation.

The division contracts with a managed care organization which has established a workers' compensation preferred provider network for medical treatment for injured state employees. Currently, all state employees have access to this network.

The managed care organization also provides case management services such as pre-certification for inpatient hospital care, bill review, large case management and other services to manage the costs of workers' compensation claims. The use of a preferred provider network allows the state to negotiate further savings off workers' compensation medical bills after the mandated fee schedule reduction, which became required on January 1, 2006. Currently, the state has obtained approximately 48% savings off billed charges as a result of the fee schedule, plus an additional 3% savings (after fee schedule reduction) as a result of the preferred provider arrangement.

The Division of Claims Administration also handles all employee property damage claims and tort claims.

During fiscal year 2008, the Division of Claims Administration received 4,710 claims falling within these categories (including workers' compensation claims filed with the third party administrator). In order for a claim to be acted upon by the Division of Claims Administration, notice must be filed with the division. The division then has 90 days to make a determination on the claim. If the division is unable to act, the claim is automatically referred to the Tennessee Claims Commission. This process ensures that claims will be processed in a timely fashion.

This division also provides staff support to the Board of Claims. The Board of Claims has the authority to hear claims which do not fall within the jurisdiction of the Tennessee Claims Commission. During the 2008 fiscal year, the Board took action on a total of two claims. The Board also reviews and approves the purchase of insurance policies by the state and makes recommendations to the Commissioner of Finance and Administration and the General Assembly regarding the required funding for the Risk Management Fund.

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**CLAIMS AGAINST THE STATE**


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**CLAIMS AND PAYMENT ACTIVITY***Fiscal Year 2008*

<b>Claims Activity</b>	<b>Claims Filed</b>	<b>Payments Made</b>
Worker's Compensation Claims	3,250	
Death Payments		\$ 275,251
Medical Payments		11,117,290
Temporary Disability		2,768,288
Permanent Disability		6,782,070
Subtotal		<u>20,942,899</u>
Employee Property Damage	141	<u>28,266</u>
Tort Claims	1,319	
Death Payments		1,742,145
Bodily Injury Payments		3,972,936
Property Damage Payments		794,530
Subtotal		<u>6,509,611</u>
<b>Total Claims Against the State</b>	<u><b>4,710</b></u>	<u><b>\$ 27,480,776</b></u>

**FIVE YEAR CLAIMS HISTORY***Fiscal Years 2004-2008*

<b>Fiscal Year</b>	<b>Claims Filed</b>	<b>Amount of Claims Paid</b>
2008	4,710	\$ 27,480,776
2007	4,856	25,997,535
2006	4,906	24,420,318
2005	5,409	28,975,152
2004	5,825	27,705,099

**CRIMINAL INJURIES COMPENSATION FUND**

**CRIMINAL INJURIES COMPENSATION FUND**

The Criminal Injuries Compensation Fund ("Fund") provides financial assistance to crime victims through two types of programs. The funding for the programs includes privilege taxes assessed in courts against criminal defendants and other offenders upon conviction, fees levied against parolees and probationers, the proceeds of bond forfeitures in felony cases, and a federal grant. Jurors may also elect to donate their jury service reimbursement to the Fund.

**Criminal Injuries Compensation Program**

Payments made under the Criminal Injuries Compensation Program are intended to defray the costs of medical services, loss of earnings, burial costs, and other pecuniary losses to either an innocent victim of a crime or to the dependents of a deceased victim. Applications for Criminal Injuries Compensation are filed with the Division of Claims Administration. During the 2008 fiscal year, 2,814 new claims were filed.

The division's staff reviews the application and obtains supporting information from the appropriate District Attorney's Office to determine eligibility for payment from the Criminal Injuries Compensation Fund. If the division cannot process a claim within 90 days, then the claim is transferred to the Tennessee Claims Commission. Eligible payments are issued promptly and are payable directly to the service provider if the bill is unpaid, to the victim for out-of-pocket expenses and, if appropriate, his or her attorney. On average, the division renders a decision on claims within 41 days.

During the 2008 fiscal year, the Division of Claims Administration made payments to victims of crime totaling \$13.6 million.

Victims of drunk drivers are also paid from the Criminal Injuries Compensation Fund. When the proximate cause of a death or injury is the operator's intoxication as prohibited by T.C.A. Section 55-10-401, the victim's death or injury is eligible for compensation, not to exceed a maximum award of \$30,000 plus attorney's fees.

Since the first claims were paid in 1982, the program has awarded a total of more than \$189 million to crime victims.

The Division of Claims Administration has made an effort to educate members of the public of the existence and benefits of the Criminal Injuries Compensation Program by printing and distributing informative brochures explaining the program. Public awareness efforts and the use of victim assistance coordinators in each judicial district have also aided in providing the public with information about the benefits provided through the Criminal Injuries Compensation Fund.

**Sexual Assault Forensic Exam Reimbursement**

In 2007, the General Assembly amended the Criminal Injuries Compensation Act to provide payment for services related to sexual assault forensic examinations. The Fund provides reimbursement to a facility that performs sexual assault forensic exams on victims of certain sexually-oriented crimes. Facilities must bill the Fund (not the victim) and cannot seek any additional payment from the victim after payment by the Fund. Payment is up to \$750 for such services for crimes occurring on or after July 1, 2007. During the 2008 fiscal year, 1,468 forensic claims were filed.

**SOURCES OF FUNDS**

*Fiscal Years 2006-2008*

Source	2006		2007		2008	
	Amount	Percentage	Amount	Percentage	Amount	Percentage
Fines	\$ 4,351,199	39%	\$ 4,718,062	39%	\$ 7,038,358	44%
Federal Funds	3,177,000	29%	3,411,000	28%	5,253,000	32%
Probation Fees	2,107,481	19%	2,183,494	18%	2,852,637	18%
Parole Fees	764,503	7%	833,820	7%	325,936	2%
Bond Forfeitures	339,176	3%	536,720	5%	397,807	2%
Other	365,429	3%	333,891	3%	272,009	2%
<b>Total</b>	<b>\$ 11,104,788</b>	<b>100%</b>	<b>\$ 12,016,987</b>	<b>100%</b>	<b>\$ 16,139,747</b>	<b>100%</b>

**CRIMINAL INJURIES COMPENSATION FUND**

**CLAIMS PAID BY CRIME TYPE**

*Fiscal Year 2008*

Crime Type	Number Paid	Percentage of Total Claims	Amount Paid	Percentage of Total Paid
Assault	810	24.9%	\$ 6,193,824	45.4%
Homicide	310	9.5%	2,807,706	20.6%
Robbery by Force	197	6.1%	1,598,928	11.7%
Child Sexual Abuse	1,253	38.6%	1,447,992	10.5%
Adult Sexual Assault	579	17.8%	675,323	5.0%
DUI	79	2.4%	639,879	4.7%
Vehicular (non DUI)	18	0.6%	118,977	0.9%
Child Physical Abuse	2	0.1%	117,441	0.9%
Kidnapping	1	0.0%	23,242	0.2%
Arson	1	0.0%	7,929	0.1%
<b>Total</b>	<b>3,250</b>	<b>100.0%</b>	<b>\$ 13,631,241</b>	<b>100.0%</b>

These numbers include reimbursement of sexual assault forensic examinations on 1,354 claims totaling \$929,425

**NEW CLAIMS FILED**

*Fiscal Year 2008*

Crime Type	Number Filed
Child Sexual Abuse	1,527
Assault	1,201
Adult Sexual Assault	670
Homicide	407
Robbery by Force	211
DUI	142
Vehicular (Non DUI)	83
Other	26
Child Physical Abuse	9
Stalking	3
Kidnapping	3
<b>Total</b>	<b>4,282</b>

These numbers include 1,468 claims filed for sexual assault forensic exam reimbursement.

**CLAIMS DENIED BY REASON**

*Fiscal Year 2008*

Reason Type	Number Denied	Percentage
Contributory Behavior	273	19.9%
Failure to Cooperate/Prosecute	240	17.5%
Ineligible Crime	206	15.0%
Insufficient Documentation	171	12.5%
Collateral Resource Covered Loss(es)	137	10.0%
Insufficient Proof of a Crime	63	4.6%
Late Filing of Claim	60	4.4%
Ineligible Claimant	58	4.2%
Other	43	3.0%
Ineligible Loss(es)	32	2.3%
Loss(es) Less than \$100	28	2.0%
Late Reporting of Crime	25	1.8%
No Collateral Resource Information	22	1.6%
Passenger with Drunk Driver	9	0.7%
No Report of Crime	5	0.4%
Lack of Proper Signature	1	0.1%
<b>Total</b>	<b>1,373</b>	<b>100.0%</b>

In fiscal year 2008, 1,137 claims were denied, including claims for sexual assault forensic examinations. Some claims are denied for more than one reason.

## CLAIMS COMMISSION

**CLAIMS COMMISSION**

Section 9-8-301 of Tennessee Code Annotated establishes the Tennessee Claims Commission as the administrative tribunal to determine monetary claims against the state. The commission has three commissioners, one from each grand division of the state. The three commissioners, who are appointed by the Governor and confirmed by the General Assembly, serve staggered eight-year terms.

The commission has a central office in Nashville with an administrative clerk and administrative services assistant. The commission is attached to the Treasury Department of administrative purposes.

The commission adjudicates claims involving tax recovery, state workers' compensation, and alleged negligence by state officials or agencies (e.g., negligent care, custody, or control of persons, property, or animals; professional malpractice; negligent operation or maintenance of a motor vehicle; and dangerous conditions on state-maintained highways or state controlled real property). The claims are payable from the Risk Management Fund. Damages are limited to \$300,000 per claimant and \$1,000,000 per occurrence. In addition, the commission awards compensation to victims of crime through the Criminal Injury Compensation Fund, and the Claims Commission has jurisdiction to review final decisions of the Secretary of State, denying a charitable gaming annual application as provided for under Tennessee Code Annotated, Section 3-17-104(h)(1). The Treasury Department's Division of Claims Administration is responsible for paying all claims.

**CLAIMS PROCESSING**

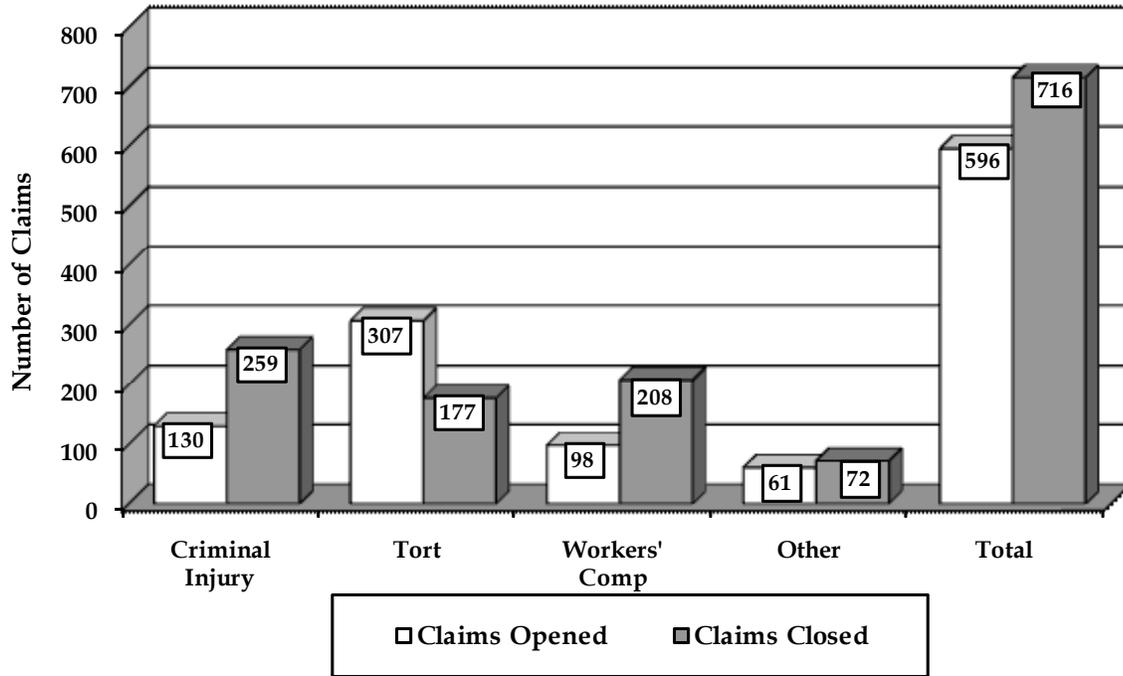
The vast majority of claims are first filed with the Division of Claims Administration. Claims involving taxes are filed directly with the Claims Commission, and claims involving workers' compensation are filed directly with the third party administrator.

Both the Division of Claims Administration and the third party administrator have 90 days to accept or deny a claim before the claim is automatically transferred to the commission. Claimant's can appeal both entities' decisions to the commission.

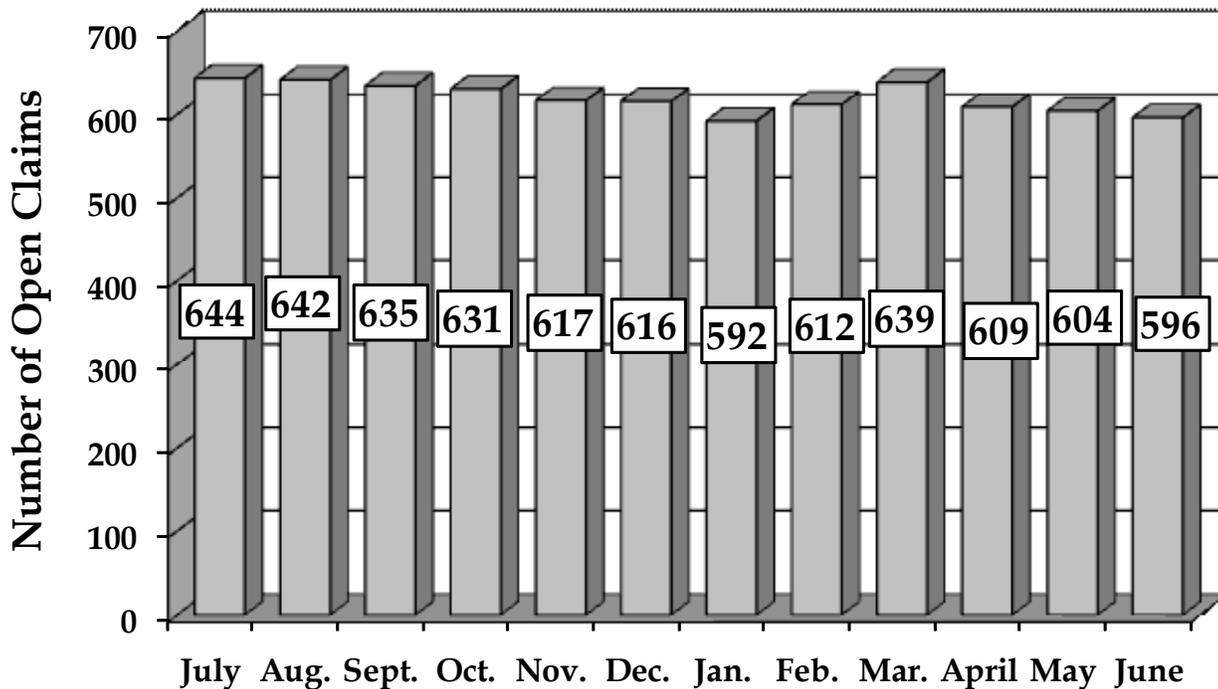
The commission has two separate dockets: a regular docket for claims greater than \$15,000 and a small docket for claims under that amount. Commission decision regular docket claims can be appealed to the Tennessee Court of Appeals or, in the case of tax or workers' compensation, to the Tennessee Supreme Court. Small docket claims can not be appealed, but such can be removed to the regular docket (at the discretion of either party) before a hearing is held.

CLAIMS COMMISSION

NUMBER OF CLAIMS OPENED AND NUMBER OF DISPOSITIONS BY CLAIM TYPE  
 (Including Dispositions by Administrative Law Judges)  
 Fiscal Year 2008



CLAIMS COMMISSION OPEN CLAIMS  
 Fiscal Year 2008



**RISK MANAGEMENT****DIVISION OF RISK MANAGEMENT**

The Division of Risk Management identifies and analyzes the state's exposure to property and casualty risks, and implements certain risk management techniques to mitigate the state's exposure to loss. The state funds various levels of risk retention through the Risk Management Fund.

The state contracts with a private insurance broker to research the insurance marketplace, and target only those insurance carriers, with the highest A.M. Best ratings, which are capable and willing to provide competitive insurance quotes for the State's various lines of coverage. An RFP process is used to select a broker, which provides the best overall proposal based on independent technical and cost ratings.

Fiscal year 2008 continued to show signs of a soft market within the insurance industry. Underwriting guidelines remained consistent with the goal of achieving continued written premium growth and underwriting profitability. In turn, this allowed significant capacity in the marketplace for most lines of coverage. Catastrophic risks, however, continued to be a major underwriting issue. The state's primary level of property insurance limits remained at \$250 million, but an additional \$250 million in excess coverage was negotiated, providing total coverage of \$500 million (excluding flood and earthquake). Flood coverage remained at \$50 million, with the exception of properties in 100 year flood zones, which were limited to \$10 million per occurrence. Earthquake limits, once again, remained at \$50 million, except for properties in the New Madrid area, where the limits were \$40 million. The state's annual aggregate deductibles were once again negotiated at \$5 million for property, and \$5 million for earthquake and flood combined. As of July 1, 2008, total insured property values were \$16.6 billion. Fiscal year 2008 premium costs for all lines of property and fidelity coverages amounted to \$2.7 million.

The Builders' Risk Insurance Program provides coverage for building construction projects approved by the State Building Commission. The policy provides all-risk coverage for the state agency, general

contractor and all subcontractors for the duration of the construction project. In fiscal year 2008, 189 insurance certificates were issued for new construction projects approved by the State Building Commission. Certificates are renewed annually on July 1, for projects continuing from one fiscal year to the next, to ensure continuity of coverage. Coverage limits remained at \$25 million per location and \$30 million per occurrence. The contractor is responsible for providing builders' risk coverage for projects exceeding these limits. Evidence of such coverage must be provided to the state, prior to beginning the construction project.

Boiler insurance is procured to protect the state's 2,484 boiler objects. This policy performs two major functions: (1) provides boiler breakdown coverage; and (2) assumes the responsibility for jurisdictional inspections for all pressure vessels. Certified inspectors evaluate all boiler objects on a scheduled basis to ensure the safe operation of the objects, which in turn, will prevent loss to human life and property. This loss prevention program has proven very effective with results showing no major incidents within the past five years.

To protect the state from financial loss due to employee dishonesty, a fidelity and crime policy is obtained. Coverage limits are provided in the amount of \$1 million per occurrence. A policy endorsement is added to extend coverage to Treasurers and Tax Collectors.

During 2008, an RFP was issued for an aviation insurance broker. The broker assists the state in obtaining aviation coverage for the state's fleet of 51 aircraft.

Risk Management administers the claims process for all lines of coverage. The Division coordinates the activities of the insurance carrier, independent adjusters, state facility managers, and state agency contacts. For emergency situations, a restoration company is under state contract to provide immediate response to prevent costly damages. A detailed property inventory (schedule) provides the current insurable values for both buildings and contents.

**RISK MANAGEMENT**

<p>Agency deductibles vary according to the type of claim: (1) Property-\$25,000; (2) Builders' Risk-\$10,000; (3) Boiler-\$10,000; (4) Fine Arts-\$0; (5) Fidelity &amp; Crime-\$100,000. If a loss exceeds the agency deductible, then loss costs are paid from the Risk Management Fund, until the State's annual aggregate deductibles are satisfied. Any remaining costs are the responsibility of the insurance carrier, until the end of the fiscal year. In fiscal year 2008, Treasury successfully applied for FEMA reimbursement of the state's aggregate deductible applicable to the tornado loss of February 5, 2008. The estimated amount of recovery is \$3.4 million.</p>	<p>The prevention and control of losses is an important part of managing the state's risks. In fiscal year 2008, risk management staff conducted loss prevention surveys at 73 locations. A total of 143 buildings were inspected for fire/life safety hazards. During these inspections, safety violations were recorded and corrective action reports were submitted to the agencies with recommendations for safety code compliance. Three ergonomics training/education sessions were conducted for 100 state employees. Workers' compensation claims frequency decreased 8.3%.</p>
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**STATE PROPERTY**  
**Summary of Key Points**  
*Fiscal Year 2008*

Insurance Coverage Information

Insured Property Values	\$ 16,500,000,000
Primary Property Limits Per Occurrence	\$ 250,000,000
Excess Property Limits Per Occurrence	\$ 250,000,000

Annual Aggregate Deductibles:

Property	\$ 5,000,000
Earthquake & Flood Combined	\$ 5,000,000
Builders' Risk	\$ 1,000,000

Financing of Estimated Property Losses:

Cumulative Agency Deductibles (Agency Obligation)	\$ 350,000
Insurance Carrier Obligation	3,975,200
Risk Management Fund Obligation	<u>5,000,000</u>
 Total Property Losses	 <u><u>\$ 9,325,200</u></u>

The amount of coverage, the level of the deductibles, the selection of the insurance companies to provide coverage, and the amount of the insurance premium, are reviewed and approved annually by the Board of Claims.

## SMALL AND MINORITY-OWNED BUSINESS ASSISTANCE PROGRAM

### SMALL AND MINORITY-OWNED BUSINESS ASSISTANCE PROGRAM

Chapter 830 of the Tennessee Public Acts of 2004 created within the Treasury Department the Small and Minority-Owned Business Assistance Program. Chapter 830 required the Department by rule to develop an assistance program for small and minority-owned businesses, as defined in TCA 65-5-113, which will include loans, technical assistance, consulting and educational services. The legislative intent is for the Department to use the assistance provided by this program to support outreach to new, expanding and existing businesses in Tennessee that do not have reasonable access to capital markets and traditional commercial lending facilities.

The Small and Minority-Owned Business Assistance Program (SMOB) replaced the Small and Minority-Owned Telecommunications Business Assistance Program that was administered by the Department of Economic and Community Development. The Telecommunications Program provided loan guarantees to qualifying businesses. With all program obligations met, the program has been phased out. Whereas the Telecommunications Program focused on a specific facet of industry, the Small and Minority-Owned Business Assistance Program (SMOB) was designed to perpetuate growth on a less restrictive continuum.

In addition to the provision of loan proceeds and technical assistance, this program is inclusive of program services such as financial counseling, assistance with the packaging of loan proposals, developing strategies for improved cash flow management, implementing internal financial management systems, strategic planning and identifying procurement opportunities with state, federal and local government systems. Another component of the Program is the educational aspect whereby various workshops and seminars will be conducted throughout the state geared toward small and minority-owned businesses.

The principle function of the Small and Minority-Owned Business Assistance Program (SMOB) is to provide a significant statewide platform through a support structure that fosters the expansion of small and minority-owned businesses in Tennessee. SMOB

consists of two components: loans (including lines of credit) and program services. The loans provided must be for a specific project. Acceptable purposes for loan proceeds include:

- acquisition of machinery and equipment
- working capital
- supplies and materials
- inventory
- certain other business-related activity

Note: A line of credit shall be considered a Loan under the Program. There are certain types of businesses that are deemed ineligible to receive assistance from the SMOB Program. Ineligible businesses include:

- o churches
- o non-profit organizations
- o insurance companies
- o real estate contractors
- o real estate developers
- o night clubs and any similar entertainment-oriented business
- o businesses that do not create or provide jobs
- o businesses not incorporated or located in Tennessee.

The infrastructure of the Small and Minority-Owned Business Assistance Program (SMOB) consist of a program administrative team, lenders and a service provider network. In a capsule, the Program Administrator for SMOB is Southeast Tennessee Development District who handles the daily operation of the Program by overseeing activities of the lenders who make the loans and by overseeing the activities of the service provider network who give technical assistance to the businesses that qualify for participation in the Program.

Lenders for SMOB are:

- o East Tennessee Development District
- o Nashville Minority Business Development Loan Fund
- o Northeast Tennessee Economic Development Corporation
- o South Central Tennessee Development District
- o Southeast Capital Corporation
- o Southwest Tennessee Development District

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**SMALL AND MINORITY-OWNED BUSINESS ASSISTANCE PROGRAM**


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The primary service provider of technical assistance for SMOB is:

- o Tennessee Small Business Development Center Network

The SMOB Program was officially launched in February 2008 with results for the first four months of operation depicted below as of June 2008:

Race	Male	Female	Number of Loans	Total Loans by Race
African-American	\$ 483,443	\$ 546,500	16	\$ 1,029,943
White	585,000	554,000	15	1,139,000
Total Loans by Sex	<u>\$ 1,068,443</u>	<u>\$ 1,100,500</u>	<u>31</u>	<u>\$ 2,168,943</u>

Interested parties may utilize SMOB's website, located at [www.tn.gov/treasury/smob](http://www.tn.gov/treasury/smob), to learn about the program.

## UNCLAIMED PROPERTY DIVISION

## UNCLAIMED PROPERTY DIVISION

The Treasury Department has administered the Uniform Disposition of Unclaimed Property Act since it was enacted in 1978. Administration is carried out by the Unclaimed Property Division, which operates the program in a manner designed to return unclaimed property to the rightful owner.

The Unclaimed Property Act provides that property that an organization or individual is holding for another person will be delivered to the Treasurer for custody if the holder of the property has had no contact with the owner for a period of time, normally five years, and if the holder cannot locate the owner. Once property is delivered, the Treasurer utilizes various techniques to locate the owners. There is no time limit on claiming this property.

During the period July 1, 2007 through June 30, 2008, \$52.3 million of cash property was turned over to the Treasurer. This includes \$5.5 million remitted by third party audit organizations from out-of-state non-reporting holders for Tennessee residents. An additional \$28.1 million in proceeds from stock sales was recognized as revenue.

Entities with property to report to Tennessee's Unclaimed Property Division obtain forms, instructions, free software, and other valuable data from the Internet web site. Many entities have expressed their appreciation for this easy access to reporting tools.

The Treasurer utilizes various methods to locate owners of unclaimed property. Initially notification to the last known address of each owner is sent. If no response is received, additional search efforts are made through Department of Labor and Workforce Development records, telephone directories, drivers' license records, external locate research tool, and other sources. Finally the names of owners and last known addresses are advertised in newspapers throughout the state.

In addition, a searchable database of the owners' names is available on the division's Internet site: [www.tn.gov/treasury/unclaim](http://www.tn.gov/treasury/unclaim). This site logged 3.2 million visitors at June 30, 2008, an increase of 314,000 for the fiscal year. In additions the owners' names are available on the national website Missing Money at: [www.missingmoney.com](http://www.missingmoney.com). The records of unclaimed property owners are also available for viewing by the public in the Unclaimed Property Division office.

During the period July 1, 2007 through June 30, 2008, \$22.4 million of cash property was returned by the Unclaimed Property Division to the owners or their heirs, local governments and reciprocal states.

Any local government in Tennessee that turns over unclaimed property to the state may request that the property be returned to the local government for safekeeping after it has been held by the state for 18 months. This fiscal year, \$1,520,180 was refunded to 26 local governments.

Tennessee has reciprocal agreements with other unclaimed property programs in other states to exchange property held by one state for owners with a last known address in the other state. Tennessee received \$1.6 million for residents or former residents in exchange for \$1.2 million paid to other states' unclaimed property offices.

Since the program began operations in 1979, \$552.2 million in unclaimed property has been reported to the Treasurer and \$175.6 million has been returned to owners, heirs, local governments and reciprocal states.

**After all location techniques are employed, the Unclaimed Property Division is able to return approximately 59% of property that is turned over with an owner's name.**

## UNCLAIMED PROPERTY DIVISION

## METHODS USED TO RETURN PROPERTY

Fiscal Year 2008

Location Method	Number of Accounts	Value of Claims	Average Claim Value
Website Inquiries	8,833	\$ 7,979,299	\$ 903
Staff or Other Outreach	945	6,397,311	6,770
Mailings to Last Known Address	2,972	1,532,086	516
Holder Referral or Reimbursement	487	1,508,830	3,098
Advertisement and Television	1,586	917,132	578
Match with Dept. of Labor and Workforce Records	2,045	728,643	356
Independent Locator	43	668,736	15,552
<b>Total Claim Payments</b>	<b>16,911</b>	<b>\$ 19,732,037</b>	<b>\$ 1,167</b>
Refunds to Local Governments	26	1,520,180	
Interstate Exchanges	45	1,176,756	
<b>Total Payments</b>	<b>16,982</b>	<b>\$ 22,428,973</b>	

## SOURCES OF UNCLAIMED PROPERTY

Fiscal Years 2004-2008

	2008	2007	2006	2005	2004
Corporations, Transportation, Colleges, Retailers	26%	22%	19%	11%	19%
Financial Institutions	24%	28%	29%	37%	28%
Insurance Companies	22%	20%	21%	20%	29%
Escheat and Other	7%	7%	6%	7%	7%
Cities and Counties	6%	4%	8%	5%	5%
Securities and Brokerage Firms	5%	5%	4%	8%	1%
Utilities	4%	5%	6%	5%	6%
Hospitals and Health Care	3%	6%	4%	3%	2%
Other States	3%	3%	3%	4%	3%
<b>Total</b>	<b>100%</b>	<b>100%</b>	<b>100%</b>	<b>100%</b>	<b>100%</b>

## ACTIVITY

Fiscal Years 2004-2008

	2008	2007	2006	2005	2004
Number of Holders Reporting	5,891	5,531	5,251	5,228	4,784
Number of Properties Received	371,527	223,703	290,254	226,918	294,446
Cash Received (Not including Shares Sold)	\$52,314,382	\$45,016,106	\$40,233,068	\$40,397,209	\$37,425,232
Number of Shares Received	2,257,769	1,364,190	1,685,649	489,767	830,379
Value of Shares Sold	\$28,157,142	\$ 6,021,856	\$23,277,122	\$ 8,908,304	\$ 3,455,735
Number of Claims Paid	16,982	15,430	15,245	16,504	14,742
Cash Paid	\$22,428,973	\$17,459,932	\$20,727,999	\$17,560,719	\$13,043,762
Shares Paid	223,892	148,952	348,525	265,790	308,569

# TREASURER'S REPORT

*Administration*

## STATUTORY DUTIES OF THE STATE TREASURER

### BOARDS AND COMMISSIONS

	<u>Tennessee Code Annotated Section</u>
Advisory Council on Workers' Compensation	50-6-121
Baccalaureate Education System Trust Board	49-7-804
Collateral Pool Board	9-4-506
Board of Claims	9-8-101
State Board of Equalization	4-3-5101
Tennessee Consolidated Retirement System Board of Trustees	8-34-302
Chairs of Excellence Endowment Trust	49-7-501
Commission on Crime Victims Assistance	Ex. Order 10 of 2003
Commission to Purchase Surplus Federal Property	12-1-103
Council on Pensions & Insurance	3-9-101
State Funding Board	9-9-101
Public Records Commission	10-7-302
Sick Leave Bank Board	8-50-903
State Building Commission	4-15-101
State Capitol Commission	4-8-301
State Insurance Committee	8-27-101
Local Government Insurance Committee	8-27-207
Local Education Insurance Committee	8-27-301
Tennessee State School Bond Authority	49-3-1204
State Trust of Tennessee	9-4-806
Tennessee Child Care Facilities Corporation Board	4-37-103
Tennessee Higher Education Commission	49-7-204
Tennessee Housing Development Agency	13-23-106
Tennessee Local Development Authority	4-31-103
Tennessee Sports Hall of Fame	4-3-5403
Tennessee Student Assistance Corporation	49-4-202
Tuition Guaranty Fund Board	49-7-2018
Workers Compensation Insurance Fund Board	50-6-604
Catastrophic Injuries Fund Commission	29-20-408
Industrial Finance Corporation Board	4-17-405
Tennessee Industrial Development Authority	13-16-301
Advisory Committee to the Trustees of the Fisk University Stieglitz Collection Art Endowment Fund	4-20-201
Access Improvement Project Committee	54-2-207
Advisory Board to Establish Compensation for the Use of the Right-of-Way for Underground Fiber Optic Cable Facilities	54-16-112
Appeals from Gift Tax Appraisals Board	67-8-116

### ADMINISTRATION

Baccalaureate Education System Trust	49-7-801, et seq.
Board of Claims	9-8-101, et seq.
Chairs of Excellence Trust	49-7-501 – 49-7-502
Collateral Pool	9-4-501 – 9-4-523
Collateral Program	9-4-101 – 9-4-105
Council on Pensions and Insurance	3-9-101
Criminal Injury Compensation Fund	29-13-101, et seq.
Deferred Compensation	8-25-101, et seq.
Escheat	31-6-101, et seq.
Flexible Benefits Plan	8-25-501
Investment Advisory Council	8-37-108
Investment of State Idle Cash Funds	9-4-602
Local Government Investment Pool	9-4-704
Old Age and Survivors Insurance Agency	8-38-101, et seq.
Pooled Investment Fund	9-4-704
Receipt and Disbursement of Public Funds	8-5-106 – 8-5-111; 9-4-301, et seq.
Small and Minority-Owned Business Assistance Program	65-5-213
State Cash Management	9-4-106 – 9-4-108; 9-4-401 – 9-4-409
State Treasurer's Office	8-5-101, et seq.
State Trust of Tennessee	9-4-801, et seq.
Tennessee Claims Commission	9-8-301, et seq.
Tennessee Consolidated Retirement System and Miscellaneous Systems	Title 8, Chptrs. 34, 35, 36, 37 & 39
Unclaimed Property	66-29-101, et seq.
Victims of Drunk Drivers Compensation Fund	40-24-107

## EXECUTIVE STAFF DIRECTORY

*Treasurer's Office*

Treasurer	Dale Sims	(615) 741-2956
Executive Assistant	Janice H. Cunningham	(615) 741-2956
General Counsel	Mary Roberts-Krause, JD	(615) 253-3855
Counsel	Doug Connell	(615) 741-2956
Human Resource Director	Ann Taylor-Tharpe	(615) 253-4111
Director of Internal Audit	Elizabeth Wood, CPA	(615) 253-2018

*Investments*

Assistant to the Treasurer	Ed Hennessee, CFP	(615) 532-1167
Chief Investment Officer	Michael Brakebill, CFA	(615) 532-1157
Deputy CIO Fixed Income Director	Andy Palmer, CFA	(615) 532-1183
Equity Director	Michael Keeler, CFA	(615) 532-1165
Senior Equity Portfolio Manager	Jeremy Conlin, CLU, ChFC, CFA	(615) 532-1152
Senior Equity Portfolio Manager	Jim Robinson, CFA	(615) 532-1177
Senior Equity Portfolio Manager	Roy Wellington, CFA	(615) 532-1151
Senior Fixed Income Portfolio Manager	Terry Davis, CFA	(615) 253-5416
Real Estate Director	Peter Katseff	(615) 532-1160
Cash Management and Short-Term Investments Manager	Tim McClure, CCM	(615) 532-1166

*Retirement Administration*

TCRS Director	Jill Bachus, CPA	(615) 741-7063
TCRS Assistant Director	Jamie Wayman, CPA	(615) 741-7063
TCRS Director of Deferred Compensation	Beth Chapman, CPA	(615) 741-7063
Director of Old Age and Survivors Insurance	Vernon Bush, JD	(615) 741-7902
Counseling Services Manager	Sandra Sewell	(615) 741-1971
Member Benefits Manager	Erica Nale	(615) 741-4868
Financial Services Manager	Keevia Battle, CPA	(615) 741-4913
Customer Services Manager	Jennifer Wooten	(615) 741-1971

*Support Services*

Assistant to the Treasurer	Rick DuBray, CPA	(615) 253-5764
Director of Accounting	Kim Morrow, CPA	(615) 532-3840
Assistant Director of Accounting	Connie Gibson, CPA	(615) 532-8051
Director of Management Services	Kerry Hartley, CPA	(615) 532-8552
Assistant Director of Management Services	Mary Alexander	(615) 253-8771
Director of Information Systems	Gary Ridner CPA, CISSP	(615) 532-8035
Assistant Director of Information Systems	Nathan Burton	(615) 253-4164

*Program Services*

Assistant to the Treasurer	Steven Curry, CPA-inactive, CEBS, CCM	(615) 532-8045
Director of Risk Management	Steve Gregory	(615) 741-1009
Manager Small Minority Business Program	Jaye Chavis	(615) 253-2265
Manager BEST Program	LaKeshia Page	(615) 532-5888
Director of Unclaimed Property	John Gabriel	(615) 253-5354
Assistant Director Unclaimed Property	Kellie Williamson	(615) 253-5356
Director of Claims Administration	Anne Adams	(615) 741-9957
Manager Criminal Injury Program	Amy Dunlap	(615) 741-9962
East Tennessee Claims Commissioner	William O. Shults, JD	(423) 623-9270
Middle Tennessee Claims Commissioner	Stephanie Reevers, JD	(615) 253-1626
West Tennessee Claims Commissioner	Nancy Miller-Herron, JD	(731) 364-2440
Administrative Clerk, Claims Commission	Marsha Richeson	(615) 532-5385

*The Treasurer is housed on the 1st floor of the State Capitol Building.  
Divisions are housed on the 9th, 10th, and 11th floors of the Andrew Jackson Building.*

## TREASURY STAFF

Adams, Anne	DuBray, Rick	McDade, Joshua	Sabin, Stephanie <sup>15</sup>
Alexander, Mary <sup>25</sup>	Dunlap, Amy <sup>15</sup>	McKenzie, Amanda	Sanders, Sharon
Anderson, Sandra <sup>10</sup>	Edmundson, Ray	Mercier, Brenda <sup>20</sup>	Sanders, Teresa
Arnett, Ron	Esaka, Cassandra	Miller, Henry	Sanford, Letha <sup>5</sup>
Arnold, Sandra <sup>25</sup>	Esters, Adrienne	Miller-Herron, Nancy	Scott, Tammie
Atkins, Janice	Faehr, Karen <sup>5</sup>	Moore, Crystal	Sewell, Sandra
Aymett, Ron	Farmer, Sharon	Morgan, Prentice	Sharp, Ryan
Bachus, Jill	Fisher, Peggy <sup>30</sup>	Morrow, Kim <sup>25</sup>	Sholders, Nikki
Baker, Linda <sup>35</sup>	Fohl, Jamie <sup>20</sup>	Moses, Gail	Shults, William O.
Baker, Sam	Fredin, Cort	Moulder, Mike	Simpson, Ben
Baker, Sherry	Freeman, Jerry	Murphy, Aimee	Sims, Dale
Bandy, Gregory	Fuqua, Monica	Murphy, RJ	Singleton, David <sup>10</sup>
Barrett, Billy	Gabriel, John	Myers, Barbara	Smith, Anita
Battle, Keevia <sup>5</sup>	Gaines, Doug	Myers, Rhonda	Smith, Brett
Bauer, David	Gatewood, Ann <sup>35</sup>	Nelson, Dana	Smith, Kimberly <sup>5</sup>
Baumgartel, Karen	Gibson, Connie	Newberry, Lori	Smith, Robert
Binion, Ashley	Graves, Randy	Nguyen, Tien	Smotherman, Suzanne
Brakebill, Michael	Gray, Tammy	Nichols, Amycity	Staggs, Amanda
Brown, Buffy	Green, Carrie	Norment, Christy	Sundell, Tim
Burcham, Janet	Green, Janice	O'Connell, Heather	Swadley, Breeanna
Burns, Bobby	Greene, Barbara	O'Leary, Candy <sup>20</sup>	Taylor-Tharpe, Ann
Burton, Nathan	Gregory, Steve	O'Saile, Mandy <sup>5</sup>	Thomas, Issac
Bush, Vernon	Griffin, Delores	Oliphant, Sarah	Thompson, Jamie Lynn
Butterfield, Keith <sup>5</sup>	Hadley, Cris	Otts, Kimberly	Thorne, Paul
Campbell, Heath <sup>5</sup>	Hall, Sherry	Oyster, David	Tucker, Anthonio
Carr, Brenda <sup>30</sup>	Hargrove, Kathy	Padgett, Wendy	Veach, Johnny <sup>25</sup>
Cavender, William	Hartley, Kerry	Page, LaKeshia	Vinson, Maxine
Chandler, Joseph	Hedges, Matthew	Palmer, Andy	Wagner, Malinda
Chapman, Beth	Hennessee, Ed	Parlow, Yvonne	Wakefield, Gayle
Chatman, Shirley	Hudgins, Terry	Parton, Floyd	Wakefield, Mark
Chavis III, Jordan	Hurt, Sandra <sup>5</sup>	Patton, Janice	Washington, Tracey
Coleman, Kanika	Hyder, Patti <sup>25</sup>	Payne, Jana	Wayman, Jamie
Conlin, Jeremy <sup>20</sup>	Ingle, Harry	Pirtle, Karen	Wellington, Roy
Connell, Doug	Jackson, Stacey	Picunko, Jesse	Whitworth, Deborah
Costa, Delcinia <sup>10</sup>	Jacobsen, Mark	Pinson, Marian	Wilkins, Natasha
Cotter, Liddye	Javner, Donnie	Pritchett, Brad <sup>5</sup>	Williams, Teresa
Couch, Janie	Jefferies, Brian	Rafn, Sonya	Williamson, Kellie
Crews, Daniel	Jennette, Angela <sup>5</sup>	Redmond, William <sup>10</sup>	Willocks, Dianne <sup>40</sup>
Crosby, Cindy	Johnson, Roxanne	Reevers, Stephanie	Wilson, Martha
Culberson, Cavandrea <sup>5</sup>	Johnson, Tawana <sup>5</sup>	Reynolds, Ian	Wilson, Shirley
Cunningham, Janice <sup>30</sup>	Jones, Chris	Richeson, Marsha	Wimmer, Genera <sup>20</sup>
Curry, Steve	Jorgensen, Chelsea	Riley, Carla	Wood, Britt
Curtis, Karen	Katseff, Peter <sup>10</sup>	Roberts-Krause, Mary	Woodard, Vivian
Curtis, Shawn <sup>10</sup>	Keeler, Mike <sup>15</sup>	Roberts, Rachel	Woodrum, Angela <sup>10</sup>
Daniel, Ted	King, Jenny	Robinson, Jim	Wooten, Jennifer
Daniels, Ruth <sup>30</sup>	Klar, Markus	Robinson, Mia <sup>5</sup>	Younglove, Sigourney
Darrell, Pat	Ladd, George	Rochelle, Dawn <sup>5</sup>	
Davis, Amanda <sup>5</sup>	Lantz, Kaci		
Davis, Jason	Lee, Andrea		
Davis, Melissa	Li, Liren		
Davis, Terry	Mackey, Wanda		
Denney, Pam	Maddox, Teresa		
Derrick, Brian <sup>10</sup>	Majors, Vallie		
Dickens, Sarah	Manson, Cathy		
Dills, Larissa	Marshall, Fred		
Dineen, Amy	Martin, Alfredia		
Dodson, Marcus	Mason, Justin <sup>5</sup>		
Dorse, Bridget <sup>10</sup>	McBee, Johnny		
Doss, Gail	McClure, Tim <sup>20</sup>		

<sup>5</sup> Received 5-year service award in 2008  
<sup>10</sup> Received 10-year service award in 2008  
<sup>15</sup> Received 15-year service award in 2008  
<sup>20</sup> Received 20-year service award in 2008  
<sup>25</sup> Received 25-year service award in 2008  
<sup>30</sup> Received 30-year service award in 2008  
<sup>35</sup> Received 35-year service award in 2008  
<sup>40</sup> Received 40-year service award in 2008

## TREASURY INTERNET SERVICES

Program	Internet Site Features	Internet Address
<i>Services to the Public</i>		
BEST	Program information, rate information, contracts, forms and newsletters	<a href="http://www.tn.gov/treasury/best">www.tn.gov/treasury/best</a>
Careers NOW	Program information, calendar, campus contacts, job descriptions and applications	<a href="http://www.tn.gov/treasury/now">www.tn.gov/treasury/now</a>
Criminal Injury Compensation Program	Frequently asked questions, application and forms, links to victims' programs nationwide and victims' organizations	<a href="http://www.tn.gov/treasury/injury">www.tn.gov/treasury/injury</a>
Unclaimed Property Program	Search for unclaimed property, claim forms, program information, links to other states' programs, holder reporting information, forms, instructions and free software	<a href="http://www.tn.gov/treasury/unclaim">www.tn.gov/treasury/unclaim</a>
TN Claims Commission	Information, contacts, rules and statutes	<a href="http://www.tn.gov/treasury/claims">www.tn.gov/treasury/claims</a>
<i>Government Services</i>		
Local Government Investment Pool	Information, forms, operations manual, newsletters, past rates, portfolio and investment policy	<a href="http://www.tn.gov/treasury/lqip">www.tn.gov/treasury/lqip</a>
OASI/Social Security	Information, FICA rates, law and forms	<a href="http://www.tn.gov/treasury/oasi">www.tn.gov/treasury/oasi</a>
Risk Management Program	Program and claim process information, frequently asked questions, property insurance report search, safety check lists, agency loss control reports and employee safety information	<a href="http://www.tn.gov/treasury/risk">www.tn.gov/treasury/risk</a>
Workers' Compensation Program	Information on reporting accidents and filing claims, eligibility criteria, glossary, explanation of benefits and provider directory	<a href="http://www.tn.gov/treasury/wc">www.tn.gov/treasury/wc</a>
<i>Public Employee Benefit Programs</i>		
Deferred Compensation Program	Account access (inquiry, transfers, allocation changes), participation and investment information, benefit projection calculator, withdrawal information and forms	<a href="http://www.tn.gov/treasury/dc">www.tn.gov/treasury/dc</a>
Flexible Benefits Plan	Program information and forms	<a href="http://www.tn.gov/treasury/flex">www.tn.gov/treasury/flex</a>
Optional Retirement Program	Program information, forms, company contacts and product information	<a href="http://www.tn.gov/treasury/orp">www.tn.gov/treasury/orp</a>
Tennessee Consolidated Retirement System	Program information, benefits calculator, publications, newsletters, forms, annual report, frequently asked questions, political subdivision option search and retirement planning information	<a href="http://www.tn.gov/treasury/tcrs">www.tn.gov/treasury/tcrs</a>
<i>Other</i>		
About the Treasurer	Statutory duties and biographical information	<a href="http://www.tn.gov/treasury/about.html">www.tn.gov/treasury/about.html</a>
Annual Report	Treasurer's Report on-line	<a href="http://www.tn.gov/treasury/TreasurersAnnualReport">www.tn.gov/treasury/TreasurersAnnualReport</a>
Bank Collateral Pool	Program information, forms and participants	<a href="http://www.tn.gov/treasury/bank">www.tn.gov/treasury/bank</a>
Map to Treasury Offices	Directions to Treasury offices	<a href="http://www.tn.gov/treasury/map.gif">www.tn.gov/treasury/map.gif</a>

# TREASURER'S REPORT

*Financial Statements*

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**BACCALAUREATE EDUCATION SYSTEM TRUST, EDUCATIONAL SERVICES PLAN  
INDEPENDENT AUDITOR'S REPORT**

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STATE OF TENNESSEE  
**COMPTROLLER OF THE TREASURY**  
DEPARTMENT OF AUDIT / DIVISION OF STATE AUDIT  
SUITE 1500, JAMES K. POLK STATE OFFICE BUILDING  
NASHVILLE, TENNESSEE 37243-0264  
PHONE (615) 401-7897 / FAX (615) 532-2765

December 4, 2008

Members of the General Assembly  
and  
Members of the Board of Trustees  
Baccalaureate Education System Trust  
and  
The Honorable Dale Sims, Treasurer  
State Capitol  
Nashville, Tennessee 37243

Ladies and Gentlemen:

We have audited the accompanying fiduciary net assets of the Baccalaureate Education System Trust, Educational Services Plan, a private-purpose trust fund of the State of Tennessee, as of June 30, 2008, and June 30, 2007, and the related statements of changes in fiduciary net assets for the years then ended. These financial statements are the responsibility of management. Our responsibility is to express an opinion on these financial statements, based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion. Tennessee statutes, in addition to audit responsibilities, entrust certain other responsibilities to the Comptroller of the Treasury. Those responsibilities include serving as a member of the board of the Baccalaureate Education System Trust.

As discussed in Note A.1., the financial statements referred to above present only the Baccalaureate Education System Trust, Educational Services Plan, a private-purpose trust fund, and do not purport to, and do not, present fairly the financial position of the State of Tennessee as of June 30, 2008, and June 30, 2007, and the changes in its financial position for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to above present fairly, in all material respects, the fiduciary net assets of the Baccalaureate Education System Trust, Educational Services Plan, of the State of Tennessee as of June 30, 2008, and June 30, 2007, and the changes in its fiduciary net assets for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with generally accepted government auditing standards, we have also issued our report dated December 4, 2008, on our consideration of the Baccalaureate Education System Trust, Educational Services Plan's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, and contracts and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with generally accepted government auditing standards and should be read in conjunction with this report in considering the results of our audit.

Sincerely,

A handwritten signature in cursive script that reads "Arthur A. Hayes, Jr.".

Arthur A. Hayes, Jr., CPA  
Director

**BACCALAUREATE EDUCATION SYSTEM TRUST, EDUCATIONAL SERVICES PLAN  
COMPARATIVE STATEMENTS OF FIDUCIARY NET ASSETS  
JUNE 30, 2008 AND JUNE 30, 2007**

ASSETS	June 30, 2008	June 30, 2007
Cash and cash equivalents	\$ 1,756,131	\$ 27,312,565
Receivables		
Contributions receivable	8,651	8,362
Investment income receivable	855,069	5,297
Investments, at fair value		
Investment in fixed income index fund	41,233,334	30,727,757
Investment in equity index fund	47,064,196	37,505,487
<b>TOTAL ASSETS</b>	<u>90,917,381</u>	<u>95,559,468</u>
<b>LIABILITIES</b>		
Investments purchased	852,163	0
Other investment payable	10,269	7,810
<b>TOTAL LIABILITIES</b>	<u>862,432</u>	<u>7,810</u>
<b>NET ASSETS HELD IN TRUST FOR PLAN PARTICIPANTS</b>	<u>\$ 90,054,949</u>	<u>\$ 95,551,658</u>

*See accompanying Notes to the Financial Statements*

**BACCALAUREATE EDUCATION SYSTEM TRUST, EDUCATIONAL SERVICES PLAN  
COMPARATIVE STATEMENTS OF CHANGES IN FIDUCIARY NET ASSETS  
FOR THE YEARS ENDED JUNE 30, 2008 AND JUNE 30, 2007**

ADDITIONS	For the Year Ended June 30, 2008	For the Year Ended June 30, 2007
Contributions	\$ 4,933,806	\$ 5,578,640
Investment income		
Net increase (decrease) in fair value of investments	(7,464,949)	6,559,337
Interest and dividend income	3,559,556	2,398,731
Less: Investment expense	(38,507)	(27,420)
Net investment income	<u>(3,943,900)</u>	<u>8,930,648</u>
Administrative fees	322,684	351,988
Transfer from general fund	0	25,950,000
<b>TOTAL ADDITIONS</b>	<u>1,312,590</u>	<u>40,811,276</u>
<b>DEDUCTIONS</b>		
Refunds	832,858	731,244
Payments	5,551,813	4,939,836
Administrative cost	424,628	372,041
<b>TOTAL DEDUCTIONS</b>	<u>6,809,299</u>	<u>6,043,121</u>
<b>CHANGE IN NET ASSETS</b>	(5,496,709)	34,768,155
<b>NET ASSETS HELD IN TRUST FOR PLAN PARTICIPANTS</b>		
<b>BEGINNING OF YEAR</b>	<u>95,551,658</u>	<u>60,783,503</u>
<b>END OF YEAR</b>	<u>\$ 90,054,949</u>	<u>\$ 95,551,658</u>

*See accompanying Notes to the Financial Statements*

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**BACCALAUREATE EDUCATION SYSTEM TRUST, EDUCATIONAL SERVICES PLAN**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**JUNE 30, 2008 AND JUNE 30, 2007**

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**A. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

**1. Reporting Entity**

The Tennessee Baccalaureate Education System Trust Fund (BEST), Educational Services Plan (ESEP) is an integral part of the primary government and has been included in the *Tennessee Comprehensive Annual Financial Report* as a private-purpose trust fund.

**2. Measurement Focus and Basis of Accounting**

The accompanying financial statements have been prepared in conformity with generally accepted accounting principles as prescribed by the Governmental Accounting Standards Board (GASB). The financial statements have been prepared using the flow of economic resources measurement focus and the accrual basis of accounting. Under this basis, revenues are recorded when earned and expenses are recorded at the time liabilities are incurred.

**3. Cash and Cash Equivalents**

Cash and Cash Equivalents, by definition, includes cash and short-term investments with a maturity date within three months of the acquisition date. The state's accounting policy regarding the definition of cash and cash equivalents includes cash management pools as cash. Cash received by the ESEP that cannot be invested immediately in securities, or that is needed for operations, is invested in the State Pooled Investment Fund administered by the State Treasurer or a short-term, open-end mutual fund, Northern Institutional Government Portfolio, under the contractual arrangements for master custody services during the fiscal year ended June 30, 2008. During the fiscal year ended June 30, 2007, cash that could not be invested immediately in securities, or that was needed for operations, was invested in the State Pooled Investment Fund administered by the State Treasurer or a short-term, open-end mutual fund, J P Morgan Prime Money Market fund, under the contractual arrangements for master custody services at that time.

**4. Method Used to Value Investments**

Investments are reported at fair value. Securities traded on a national exchange are valued at the last reported sales price. The fair value of investments in open-end mutual funds is based on the share price. Investment income consists of realized and unrealized appreciation (depreciation) in the fair value of investments and interest and dividend income. Interest income is recognized when earned. Securities and securities transactions are recorded in the financial statements on trade-date basis.

**B. DEPOSITS AND INVESTMENTS**

In accordance with State statute, the ESEP assets may be invested in any instrument, obligation, security or property that constitutes a legal investment for assets of the Tennessee Consolidated Retirement System (TCRS). In addition, the assets of the ESEP may be pooled for investment purposes with the assets of the TCRS or any other assets under the custody of the State Treasurer.

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**BACCALAUREATE EDUCATION SYSTEM TRUST, EDUCATIONAL SERVICES PLAN**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**JUNE 30, 2008 AND JUNE 30, 2007**

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The authority for investing the assets of the ESEP is vested in its Board of Trustees and the responsibility for implementing the investment policy established by the Board is delegated to the State Treasurer. The ESEP does not maintain its own bank accounts but utilizes the State Pooled Investment Fund for its operating cash needs. The State Pooled Investment Fund is authorized by state statute to invest funds in accordance with policy guidelines approved by the Funding Board of the State of Tennessee. The current resolution of that board gives the Treasurer authority to invest in collateralized certificates of deposit in authorized state depositories, prime commercial paper, prime bankers' acceptances, certain repurchase agreements, and various U.S. Treasury and Agency obligations. The State Pooled Investment Fund is also authorized to enter into securities lending agreements in which U.S. Government Securities may be loaned for a fee. The loaned securities are transferred to the borrower by the custodial agent upon simultaneous receipt of collateral securities. Required risk disclosures relative to the State Pooled Investment Fund are presented in the *Tennessee Comprehensive Annual Financial Report*. That report may be obtained by writing to the Tennessee Department of Finance and Administration, Division of Accounts, 14th Floor William R. Snodgrass Tennessee Tower, 312 Rosa L. Parks Avenue, Nashville, Tennessee 37243-0298.

**Credit Risk**

The ESEP does not currently own specific fixed income securities, but chooses to invest in a Lehman Government Aggregate Index Fund. At June 30, 2008 and June 30, 2007, the ESEP had \$41,233,334 and \$30,727,757 respectively, invested in the Lehman Government Aggregate Index Fund.

Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. Credit quality ratings for the ESEP's investments in fixed income securities as of June 30, 2008 and June 30, 2007 are not available since the Lehman Government Aggregate Index Fund is not traded on an exchange and is unrated; however the average rating for the securities in the fund is AA1/AA2 for June 30, 2008 and AA2 for June 30, 2007. Neither the State Pooled Investment Fund nor the J P Morgan Prime Money Market Fund has obtained a credit quality rating from a nationally recognized credit ratings agency. The Northern Institutional Government Portfolio has a credit quality rating of AAA at June 30, 2008.

The ESEP's investment policy states that the trust may acquire securities which are rated within the four highest grades at the time of acquisition by any of the recognized rating agencies. In addition, the policy requires that only the highest quality short-term debt issues, including commercial paper with ratings of A1 or P1, may be purchased. The policy further states that index funds may be utilized as an alternative to selecting individual securities.

**Interest Rate Risk**

Interest rate risk is the risk that future changes in prevailing market rates of interest will have an adverse effect on the fair value of debt investments. The fair values of securities with long terms to maturity may be highly sensitive to interest rate changes. The investment policy for the ESEP states that bonds generally will be purchased and held to maturity, but when necessary, the portfolio will be actively managed in times of volatile interest rate swings to shorten the average maturity and protect principal value. The effective duration for the Lehman Government Aggregate Index fund that ESEP utilizes was 4.68 at June 30, 2008 and 4.72 at June

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**BACCALAUREATE EDUCATION SYSTEM TRUST, EDUCATIONAL SERVICES PLAN**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**JUNE 30, 2008 AND JUNE 30, 2007**

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30, 2007. Duration is a measure of a debt investment's exposure to fair value changes arising from changing interest rates. It uses the present value of cash flows weighted for those cash flows as a percentage of the investment's full price.

**C. DESCRIPTION OF THE EDUCATIONAL SERVICES PLAN**

The Tennessee Baccalaureate Education System Trust, Educational Services Plan, administered by the State Treasurer, was created under *Tennessee Code Annotated*, Title 49, Chapter 7, Part 8 for the purpose of improving higher education in the State of Tennessee by assisting students or their families to pay in advance, a portion of the tuition and other costs of attending colleges and universities. Under the program, a purchaser may enter into a contract with the BEST Board of Trustees to purchase tuition units on behalf of a beneficiary. Each tuition unit purchased entitles the beneficiary to an amount no greater than one percent of the weighted average tuition of Tennessee's four-year public universities during the academic term in which it is used; however, the tuition unit or equivalent funds may be used at any accredited public or private, in-state or out-of-state institution. The purchase price of the tuition unit is determined annually by the BEST Board of Trustees with the assistance of an actuary to maintain the plan's financial soundness. Refunds and tuition payments are guaranteed only to the extent that ESEP program funds are available and neither the State of Tennessee nor the BEST Board of Trustees is liable for any amount in excess of available program funds. The net assets held in trust for plan participants were \$3,572,373 more at June 30, 2008, and \$13,856,044 more at June 30, 2007, than the amounts needed to fund the outstanding tuition units at their weighted average tuition unit prices in effect at the respective dates.

**D. OTHER ACCOUNTING DISCLOSURES**

In accordance with *Public Chapter 603, Acts of 2007*, a transfer of \$25,950,000 from the general fund was made June 30, 2007 to meet the obligations of the ESEP program.

**E. SUBSEQUENT EVENTS**

Continued disruption in the credit markets and overall declines in economic conditions in markets in the United States of America and internationally have resulted in significant declines in the fair market value of the ESEP's investments subsequent to June 30, 2008. As of October 31, 2008, the ESEP estimates that the value of investments has declined approximately \$15 million compared to the value as of June 30, 2008.

**CHAIRS OF EXCELLENCE  
INDEPENDENT AUDITOR'S REPORT**



STATE OF TENNESSEE  
**COMPTROLLER OF THE TREASURY**  
DEPARTMENT OF AUDIT / DIVISION OF STATE AUDIT  
SUITE 1500, JAMES K. POLK STATE OFFICE BUILDING  
NASHVILLE, TENNESSEE 37243-0264  
PHONE (615) 401-7897 / FAX (615) 532-2765

December 4, 2008

Members of the General Assembly  
and  
Members of the Board of Trustees  
Chairs of Excellence Trust  
and  
The Honorable Dale Sims, Treasurer  
State Capitol  
Nashville, Tennessee 37243

Ladies and Gentlemen:

We have audited the accompanying balance sheets of the Chairs of Excellence, a permanent fund of the State of Tennessee, as of June 30, 2008, and June 30, 2007, and the related statements of revenues, expenditures, and changes in fund balances for the years then ended. These financial statements are the responsibility of management. Our responsibility is to express an opinion on these financial statements, based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion. Tennessee statutes, in addition to audit responsibilities, entrust certain other responsibilities to the Comptroller of the Treasury. Those responsibilities include serving as a member of the board of the Chairs of Excellence.

As discussed in Note A.1., the financial statements referred to above present only the Chairs of Excellence, a permanent fund, and do not purport to, and do not, present fairly the financial position of the State of Tennessee as of June 30, 2008, and June 30, 2007, and the changes in its financial position for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Chairs of Excellence of the State of Tennessee as of June 30, 2008, and June 30, 2007, and the changes in its financial position for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with generally accepted government auditing standards, we have also issued our report dated December 4, 2008, on our consideration of the Chairs of Excellence's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, and contracts and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with generally accepted government auditing standards and should be read in conjunction with this report in considering the results of our audit.

Sincerely,

A handwritten signature in black ink that reads 'Arthur A. Hayes, Jr.'.

Arthur A. Hayes, Jr., CPA  
Director

**CHAIRS OF EXCELLENCE  
COMPARATIVE BALANCE SHEETS  
JUNE 30, 2008 AND JUNE 30, 2007**

	June 30, 2008	June 30, 2007
<b>ASSETS</b>		
Cash and cash equivalents	\$ 6,829,613	\$ 4,892,461
Investments, at fair value		
Government securities	65,101,130	78,964,587
Corporate securities	45,812,422	25,128,948
Investment in equity mutual fund	122,267,759	145,870,688
Total investments	<u>233,181,311</u>	<u>249,964,223</u>
Receivables		
Due from colleges and universities	417,000	698,000
Investment income receivable	1,868,609	1,998,280
Total receivables	<u>2,285,609</u>	<u>2,696,280</u>
<b>TOTAL ASSETS</b>	<u>\$ 242,296,533</u>	<u>\$ 257,552,964</u>
 <b>LIABILITIES AND FUND BALANCES</b>		
<b>LIABILITIES</b>		
Due to colleges and universities	\$ 1,825,705	\$ 1,861,610
Due to the Academic Scholars Fund	3,515,998	3,227,367
Other investment payable	0	16,603
<b>TOTAL LIABILITIES</b>	<u>5,341,703</u>	<u>5,105,580</u>
 <b>FUND BALANCES</b>		
Reserved for non-expendable corpus	99,929,963	99,929,963
Unreserved	137,024,867	152,517,421
<b>TOTAL FUND BALANCES</b>	<u>236,954,830</u>	<u>252,447,384</u>
<b>TOTAL LIABILITIES AND FUND BALANCES</b>	<u>\$ 242,296,533</u>	<u>\$ 257,552,964</u>

*See accompanying Notes to the Financial Statements*

**CHAIRS OF EXCELLENCE  
COMPARATIVE STATEMENTS OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCES  
FOR THE YEARS ENDED JUNE 30, 2008 AND JUNE 30, 2007**

	For the Year Ended June 30, 2008	For the Year Ended June 30, 2007
<b>REVENUES</b>		
Investment income (loss)	\$ (7,631,048)	\$ 33,163,435
<b>TOTAL REVENUES</b>	<u>(7,631,048)</u>	<u>33,163,435</u>
<b>EXPENDITURES</b>		
University of Tennessee	3,541,606	3,180,266
Tennessee Board of Regents	3,826,426	3,335,341
Academic Scholars Fund	288,632	164,790
Administrative cost	204,842	195,445
<b>TOTAL EXPENDITURES</b>	<u>7,861,506</u>	<u>6,875,842</u>
<b>EXCESS (DEFICIENCY) OF REVENUES OVER (UNDER) EXPENDITURES</b>	(15,492,554)	26,287,593
<b>FUND BALANCES, BEGINNING OF YEAR</b>	<u>252,447,384</u>	<u>226,159,791</u>
<b>FUND BALANCES, END OF YEAR</b>	<u>\$ 236,954,830</u>	<u>\$ 252,447,384</u>

*See accompanying Notes to the Financial Statements*

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**CHAIRS OF EXCELLENCE**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**JUNE 30, 2008 AND JUNE 30, 2007**

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**A. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

1. **Reporting Entity** - The Chairs of Excellence (COE) Trust forms an integral part of the primary government and has been included as a permanent fund in the *Tennessee Comprehensive Annual Financial Report*.
2. **Measurement Focus and Basis of Accounting** - The accompanying financial statements have been prepared in conformity with generally accepted accounting principles as prescribed by the Governmental Accounting Standards Board (GASB), using the flow of current financial resources measurement focus and the modified accrual basis of accounting. Under this basis, revenues are recorded when they become both measurable and available, and expenditures are recognized when the related fund liability is incurred. The COE Trust follows the State of Tennessee's revenue recognition period, in which taxes and fees are considered to be available if received in the first sixty days of the new fiscal year. Federal grants, departmental services, and interest associated with the current fiscal year are all considered to be available if received in twelve months. All other revenue items are considered to be measurable and available only when cash is received by the COE Trust.
3. **Cash and Cash Equivalents** - Cash and cash equivalents by definition, includes cash and short term investments with a maturity date within three months of the acquisition date. The state's accounting policy regarding the definition of cash and cash equivalents includes cash management pools as cash. Cash received by the COE Trust that cannot be immediately invested in securities, or that is needed for operations, is invested in either the State Pooled Investment Fund sponsored by the State of Tennessee and administered by the State Treasurer or a short-term, open-end mutual fund, Northern Institutional Government Portfolio, under the contractual arrangement for master custody services during the fiscal year ended June 30, 2008. During the fiscal year ended June 30, 2007, cash that could not be invested immediately in securities, or that was needed for operations, was invested in the State Pooled Investment Fund administered by the State Treasurer or a short-term, open-end mutual fund, J P Morgan Prime Money Market fund, under the contractual arrangements for master custody services at that time.
4. **Method Used to Value Investments** - Investments are reported at fair value. For fair value reporting, securities traded on a national or international exchange are valued at the last reported sales price at current exchange rates. The fair value of investments in open-end mutual funds is based on the share price. Investment income includes realized and unrealized appreciation (depreciation) in the fair value of investments, and interest and dividend income. Interest income is recognized when earned. Securities and securities transactions are recorded in the financial statements on trade date basis.
5. **Fund Balances** - The reserve for non-expendable corpus includes funds provided by contributions from the state, colleges and universities and private sources.

*(continued)*

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**CHAIRS OF EXCELLENCE**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**JUNE 30, 2008 AND JUNE 30, 2007**

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**B. DEPOSITS AND INVESTMENTS**

State statute authorizes the funds of the COE Trust to be commingled for investment with other trust funds and other funds subject to investment by the State Treasurer. The COE Trust does not maintain its own bank accounts but utilizes the State Pooled Investment Fund for its operating cash needs. As of June 30, 2007, the COE Trust also invested idle cash in a short term investment with the master custodian, JP Morgan Prime Money Market Fund. The State Pooled Investment Fund is authorized by state statute to invest funds in accordance with policy guidelines approved by the Funding Board of the State of Tennessee. The current resolution of that board gives the Treasurer authority to invest in collateralized certificates of deposit in authorized state depositories, prime commercial paper, prime bank-ers' acceptances, certain repurchase agreements and various U.S. Treasury and Agency obligations. The State Pooled Investment Fund is also authorized to enter into securities lending agreements in which U.S. Government Securities may be loaned for a fee. The loaned securities are transferred to the borrower by the custodial agent upon simultaneous receipt of collateral securities.

State statute also authorizes the Board of Trustees of the COE Trust to adopt an investment policy for the trust in accordance with the laws, guidelines and policies that govern investments by the Tennessee Consolidated Retirement System. The State Treasurer is responsible for the investment of trust funds in accordance with the policy established by the trustees. The investment policy of the COE Trust requires that public funds, capital gains on public funds, and all current income exceeding withdrawals be invested in fixed income securities. Private contributions may be invested in equity securities, including domestic and foreign common stocks, preferred stocks and convertible bonds. Subsequent to the initial funding of a chair, funds may be transferred from the equity corpus to the fixed income corpus but not from the fixed income corpus to the equity corpus.

*(continued)*

**CHAIRS OF EXCELLENCE  
NOTES TO THE FINANCIAL STATEMENTS  
JUNE 30, 2008 AND JUNE 30, 2007**

As of June 30, 2008 and June 30, 2007, the COE Trust had the following investments:

<i>Expressed in Thousands</i> Investment Type	Fair Value As of June 30, 2008	United States Treasury/Agency	Credit Quality Ratings				
			AAA	AA	A	BBB	Not Rated
<b>Debt Investments</b>							
U.S. Government							
U.S. Treasuries	\$ 9,894	\$ 9,894					
U.S. Government TIPS	23,658	23,658					
U.S. Agencies	0						
Mortgage Backed							
Government	31,549	3,848					\$ 27,701
Corporate	18,142		\$ 18,142				
Corporate							
Corporate Bonds	22,538		2,067	\$ 2,925	\$ 10,241	\$ 7,305	
Corporate Asset Backed	5,133		4,583		60	490	
Private Placements	0						
<b>Total Debt Investments</b>	<b>\$ 110,914</b>	<b>\$ 37,400</b>	<b>\$ 24,792</b>	<b>\$ 2,925</b>	<b>\$ 10,301</b>	<b>\$ 7,795</b>	<b>\$ 27,701</b>
<b>Other Investments</b>							
Commingled Funds							
U.S. Equity	\$ 83,034						
Non - U.S. Equity	39,233						
Money Market Funds	6,880						
<b>Total Other Investments</b>	<b>\$ 129,147</b>						
<b>Total Investments</b>	<b>\$ 240,061</b>						
Less: Investments Classified as Cash Equivalents on Balance Sheet (Rated AAA)	(6,880)						
<b>Total Investments as Shown on Balance Sheet</b>	<b>\$ 233,181</b>						

*Note: Securities included in the United States Treasury/Agency categories above consist of obligations of the U.S. government, or obligations explicitly guaranteed by the U.S. government and are not considered to have credit risk. Securities that are in the Not Rated categories are implicitly guaranteed by the U.S. government but are not rated by Standard and Poor's or Moody's.*

<i>Expressed in Thousands</i> Investment Type	Fair Value As of June 30, 2007	United States Treasury/Agency	Credit Quality Ratings				
			AAA	AA	A	BBB	Not Rated
<b>Debt Investments</b>							
U.S. Government							
U.S. Treasuries	\$ 17,422	\$ 17,422					
U.S. Government TIPS	21,193	21,193					
U.S. Agencies	7,520		\$ 7,520				
Mortgage Backed							
Corporate	5,321		5,321				
Government Pass-through	32,830	3,867					\$ 28,963
Corporate							
Corporate Bonds	16,486		2,036	\$ 5,398	\$ 6,402	\$ 2,650	
Corporate Asset Backed	2,005		1,003		1,002		
Private Placements	1,317			493		824	
<b>Total Debt Investments</b>	<b>\$ 104,094</b>	<b>\$ 42,482</b>	<b>\$ 15,880</b>	<b>\$ 5,891</b>	<b>\$ 7,404</b>	<b>\$ 3,474</b>	<b>\$ 28,963</b>
<b>Other Investments</b>							
Commingled Funds							
U.S. Equity	\$ 101,720						
Non - U.S. Equity	44,151						
Money Market Funds	5,066						
<b>Total Other Investments</b>	<b>\$ 150,937</b>						
<b>Total Investments</b>	<b>\$ 255,031</b>						
Less: Investments Classified as Cash Equivalents on Balance Sheet	(5,066)						
<b>Total Investments as Shown on Balance Sheet</b>	<b>\$ 249,965</b>						

*Note: Securities included in the United States Treasury/Agency categories above consist of obligations of the U.S. government, or obligations explicitly guaranteed by the U.S. government and are not considered to have credit risk. Securities that are in the Not Rated categories are implicitly guaranteed by the U.S. government but are not rated by Standard and Poor's or Moody's.*

(continued)

**CHAIRS OF EXCELLENCE  
NOTES TO THE FINANCIAL STATEMENTS  
JUNE 30, 2008 AND JUNE 30, 2007**

**Credit Risk**

Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. Credit quality ratings for the COE Trust's investments in fixed income securities as of June 30, 2008 and June 30, 2007 are included in the above schedule. Securities are rated using Standard and Poor's and/or Moody's and are presented above using the Standard and Poor's rating scale. Neither the State Pooled Investment Fund nor the J P Morgan Prime Money Market Fund has obtained a credit quality rating from a nationally recognized credit ratings agency. The Northern Institutional Government Portfolio has a credit quality rating of AAA at June 30, 2008.

The COE Trust's investment policy states that the majority of investments should be placed in high quality debt securities to produce adequate income with minimal risk. In addition, for short-term investments, the investment policy states that only the highest quality short-term debt issues should be purchased.

As noted above, the COE Trust does not maintain its own bank accounts but utilizes the State Pooled Investment Fund for its operating cash purposes. Required risk disclosures relative to the State Pooled Investment Fund are presented in the *Tennessee Comprehensive Annual Financial Report*. That report may be obtained by writing to the Tennessee Department of Finance and Administration, Division of Accounts, 14th Floor William R. Snodgrass Tennessee Tower, 312 Rosa L. Parks Avenue, Nashville, Tennessee 37243-0298.

**Concentration of Credit Risk**

A concentration of investments in any one single issuer of debt securities presents a greater risk for loss in the event that the issuer fails on its obligations. The COE Trust had the following investment amounts and percentages of total investments, in organizations representing five percent or more of total investments, excluding those organizations whose issues are explicitly guaranteed by the United States government, and investments in mutual funds, external investment pools, and other pooled investments:

<u>Issuer Organization</u>	<u>June 30, 2008</u>		<u>June 30, 2007</u>	
	<u>Fair Value</u>	<u>Percentage</u>	<u>Fair Value</u>	<u>Percentage</u>
Federal National Mortgage Association	\$24,110,196	10.04%	\$30,023,756	11.78%

The COE Trust's investment policy does not specifically address limitations on investing in any one issuer.

**Interest Rate Risk**

Interest rate risk is the risk that future changes in prevailing market rates of interest will have an adverse effect on the fair value of debt investments. The fair values of securities with long terms to maturity may be highly sensitive to interest rate changes. The investment policy for the COE Trust states that the maturity of its debt securities may range from short-term instruments, including investments in the State Pooled Investment Fund, to long-term bonds, with consideration of liquidity needs. However, the policy does not specifically address limits on investment maturities. The fixed income portfolio is benchmarked against the Lehman Government/Corporate Intermediate Index and tends to have a duration within a tight range around that index. Duration is a measure of a debt investment's exposure to fair value changes arising from changing interest rates. It uses the present value of cash flows weighted for those cash flows as a percentage of the investment's full price. The COE Trust had the following investments and effective duration at June 30, 2008 and June 30, 2007.

(continued)

**CHAIRS OF EXCELLENCE**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**JUNE 30, 2008 AND JUNE 30, 2007**

**Chairs of Excellence**  
**Debt Investments**  
*(Expressed in Thousands)*

Investment Type	Fair Value As of June 30, 2008	Effective Duration (years)
<b>Debt Investments</b>		
U.S. Government		
U.S. Treasuries	\$ 9,894	10.63
U.S. TIPS	23,658	7.00
Mortgage Backed		
Government	31,549	4.21
Corporate	18,142	3.40
Corporate		
Corporate Bonds	22,538	4.84
Corporate Asset Backed	5,133	3.70
<b>Total Debt Investments</b>	<b>\$ 110,914</b>	<b>5.35</b>

Investment Type	Fair Value As of June 30, 2007	Effective Duration (years)
<b>Debt Investments</b>		
U.S. Government		
U.S. Treasuries	\$ 17,422	9.17
U.S. TIPS		
Inflation Indexed Bonds	4,026	7.03
Inflation Indexed Notes	17,167	2.21
U.S. Agencies	7,520	1.67
Mortgage Backed		
Corporate	5,321	6.31
Government		
GNMA	3,867	5.32
FHLMC	3,964	4.83
FNMA	24,999	4.49
Corporate		
Corporate Bonds	16,486	3.22
Corporate Asset Backed	2,005	4.21
Private Placements	1,317	5.00
<b>Total Debt Investments</b>	<b>\$ 104,094</b>	<b>4.80</b>

*(continued)*

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**CHAIRS OF EXCELLENCE**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**JUNE 30, 2008 AND JUNE 30, 2007**

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**Asset Backed Securities**

The COE Trust invests in collateralized mortgage obligations (CMOs) which are mortgage backed securities. These securities are based on cash flows from interest and principal payments on underlying mortgages. Therefore, they are sensitive to prepayments by mortgagees, which may result from a decline in interest rates. The fair value of CMOs at June 30, 2008 was \$18,141,180 of which \$10,551,422 were CMOs that are generally more sensitive to interest rate changes. The fair value of CMOs at June 30, 2007 which was originally reported as zero has been reclassified to \$5,320,551 due to securities classified as asset backed securities being more accurately stated as CMOs. Of this amount at June 30, 2007, \$2,489,229 were CMOs that are generally more sensitive to changes in interest rates.

**C. OTHER ACCOUNTING DISCLOSURES**

1. **Chairs of Excellence Endowment Trust** - The COE Trust is authorized by the 94th General Assembly to further the cause of education in Tennessee. The COE Trust is administered by the State Treasurer. The Trust is set up into two general accounts which equally divide any state appropriations: one for the University of Tennessee and one for the Tennessee Board of Regents. As each Chair is designated, a portion of the appropriation is transferred to a sub account for that Chair. The awarding college or university must provide matching contributions, of which at least 50 percent of the funds are from private contributions.

As of June 30, 2008, 99 Chairs have been established with matching contributions received totaling \$55,929,963. Total contributions to the COE Trust totaled \$99,929,963 as of June 30, 2008. This includes \$44,000,000 from the State, \$10,321,300 from Colleges and Universities, and \$45,608,663 from private contributions.

2. **Academic Scholars Fund** - Funds from the Academic Scholars Fund are combined with the COE Trust for investment purposes only. The Academic Scholars Fund general account receives only the income earned on its principal and does not receive any COE Trust state contributions or appropriations. These funds are invested in domestic fixed income securities.

**D. SUBSEQUENT EVENTS**

1. **Market Decline** - Continued disruption in the credit markets and overall declines in economic conditions in markets in the United States of America and internationally have resulted in significant declines in the fair value of COE Trust's investments subsequent to June 30, 2008. As of October 31, 2008, the COE Trust estimates that the value of investments has declined approximately \$42 million compared to the value of June 30, 2008.

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**CRIMINAL INJURIES COMPENSATION FUND  
INDEPENDENT AUDITOR'S REPORT**

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STATE OF TENNESSEE  
**COMPTROLLER OF THE TREASURY**  
DEPARTMENT OF AUDIT / DIVISION OF STATE AUDIT  
SUITE 1500, JAMES K. POLK STATE OFFICE BUILDING  
NASHVILLE, TENNESSEE 37243-0264  
PHONE (615) 401-7897 / FAX (615) 532-2765

December 4, 2008

Members of the General Assembly  
and  
The Honorable Dale Sims, Treasurer  
State Capitol  
Nashville, Tennessee 37243

Ladies and Gentlemen:

We have audited the accompanying balance sheets of the Criminal Injuries Compensation Fund, a special revenue fund of the State of Tennessee, as of June 30, 2008, and June 30, 2007, and the related statements of revenues, expenditures, and changes in fund balances and revenues, expenditures, and changes in fund balances (budget and actual) for the years then ended. These financial statements are the responsibility of management. Our responsibility is to express an opinion on these financial statements, based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

As discussed in Note A.1., the financial statements referred to above present only the Criminal Injuries Compensation Fund, a special revenue fund, and do not purport to, and do not, present fairly the financial position of the State of Tennessee as of June 30, 2008, and June 30, 2007, and the changes in its financial position and budgetary comparisons for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Criminal Injuries Compensation Fund of the State of Tennessee as of June 30, 2008, and June 30, 2007, and the changes in its financial position and budgetary comparisons for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with generally accepted government auditing standards, we have also issued our report dated December 4, 2008, on our consideration of the Criminal Injuries Compensation Fund's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, and contracts and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with generally accepted government auditing standards and should be read in conjunction with this report in considering the results of our audit.

Sincerely,

A handwritten signature in cursive script that reads 'Arthur A. Hayes, Jr.'.

Arthur A. Hayes, Jr., CPA  
Director

**CRIMINAL INJURIES COMPENSATION FUND  
COMPARATIVE BALANCE SHEETS  
JUNE 30, 2008 AND JUNE 30, 2007**

	June 30, 2008	June 30, 2007
<b>ASSETS</b>		
Cash	\$ 7,964,318	\$ 8,266,771
Accounts receivable	591,921	450,120
Due from federal government	<u>5,253,000</u>	<u>0</u>
<b>TOTAL ASSETS</b>	<u>\$ 13,809,239</u>	<u>\$ 8,716,891</u>
 <b>LIABILITIES AND FUND BALANCES</b>		
<b>LIABILITIES</b>		
Accounts payable	\$ 136,211	\$ 104,878
Claims liability	<u>6,694,308</u>	<u>6,748,933</u>
<b>TOTAL LIABILITIES</b>	<u>6,830,519</u>	<u>6,853,811</u>
 <b>FUND BALANCES</b>		
Reserved for victims of drunk drivers (see Note B.1)	1,919,987	1,862,436
Unreserved	<u>5,058,733</u>	<u>644</u>
<b>TOTAL FUND BALANCES</b>	<u>6,978,720</u>	<u>1,863,080</u>
<b>TOTAL LIABILITIES AND FUND BALANCES</b>	<u>\$ 13,809,239</u>	<u>\$ 8,716,891</u>

*See accompanying Notes to the Financial Statements*

**CRIMINAL INJURIES COMPENSATION FUND**  
**COMPARATIVE STATEMENTS OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCES**  
**FOR THE YEARS ENDED JUNE 30, 2008 AND JUNE 30, 2007**

	For the Year Ended June 30, 2008	For the Year Ended June 30, 2007
<b>REVENUES</b>		
State		
Fines	\$ 7,038,358	\$ 4,718,062
Fees	3,178,573	3,017,314
Federal	5,253,000	3,411,000
Interest income	270,119	331,847
Other	<u>399,697</u>	<u>538,764</u>
<b>TOTAL REVENUES</b>	<u>16,139,747</u>	<u>12,016,987</u>
<b>EXPENDITURES</b>		
Claim payments	13,576,616	12,907,574
Victims' coalition grant	100,000	100,000
District Attorneys General grant	204,400	197,591
Administrative cost	<u>843,091</u>	<u>686,652</u>
<b>TOTAL EXPENDITURES</b>	<u>14,724,107</u>	<u>13,891,817</u>
<b>EXCESS (DEFICIENCY) OF REVENUES OVER (UNDER) EXPENDITURES</b>	1,415,640	(1,874,830)
<b>OTHER FINANCING SOURCES</b>		
Transfer from general fund	<u>3,700,000</u>	<u>602,000</u>
<b>TOTAL OTHER FINANCING SOURCES</b>	<u>3,700,000</u>	<u>602,000</u>
<b>NET CHANGE IN FUND BALANCES</b>	5,115,640	(1,272,830)
<b>FUND BALANCES, BEGINNING OF YEAR</b>	<u>1,863,080</u>	<u>3,135,910</u>
<b>FUND BALANCES, END OF YEAR</b>	<u>\$ 6,978,720</u>	<u>\$ 1,863,080</u>

*See accompanying Notes to the Financial Statements*

**CRIMINAL INJURIES COMPENSATION FUND**  
**COMPARATIVE STATEMENTS OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCES**  
**BUDGET AND ACTUAL (BUDGETARY BASIS) FOR THE YEARS ENDED JUNE 30, 2008 AND JUNE 30, 2007**

	For the Year Ended June 30, 2008			For the Year Ended June 30, 2007		
	Original Budget	Final Budget	Actual (Budgetary Basis)	Original Budget	Final Budget	Actual (Budgetary Basis)
<b>SOURCES OF FINANCIAL RESOURCES</b>						
<b>FUND BALANCES, BEGINNING OF YEAR</b>	\$ 1,863,080	\$ 1,863,080	\$ 1,863,080	\$ 3,135,910	\$ 3,135,910	\$ 3,135,910
<b>REVENUES</b>						
Taxes	5,000,000	5,000,000	7,038,358	5,900,000	5,900,000	4,718,062
Fees	3,167,000	3,167,000	3,178,573	3,406,900	3,406,900	3,017,314
Federal	5,055,000	5,055,000	5,253,000	3,415,100	3,415,100	3,411,000
Interest income	0	0	270,119	0	0	331,847
Other	603,000	603,000	399,697	603,000	603,000	538,764
<b>OTHER FINANCIAL SOURCES</b>						
Transfer in	1,900,000	3,700,000	3,700,000	0	602,000	602,000
<b>TOTAL SOURCES OF FINANCIAL RESOURCES</b>	<b>17,588,080</b>	<b>19,388,080</b>	<b>21,702,827</b>	<b>16,460,910</b>	<b>17,062,910</b>	<b>15,754,897</b>
<b>USES OF FINANCIAL RESOURCES</b>						
<b>EXPENDITURES</b>						
Claim payments	15,000,000	18,425,600	13,576,616	12,500,000	13,397,600	12,907,574
Victims' coalition grant	0	100,000	100,000	0	100,000	100,000
District Attorneys General grant	0	204,400	204,400	0	204,400	197,591
Administrative cost	825,000	825,000	843,091	825,000	825,000	686,652
<b>TOTAL USES OF FINANCIAL RESOURCES</b>	<b>15,825,000</b>	<b>19,555,000</b>	<b>14,724,107</b>	<b>13,325,000</b>	<b>14,527,000</b>	<b>13,891,817</b>
<b>FUND BALANCES, END OF YEAR</b>	<b>\$ 1,763,080</b>	<b>\$ (166,920)</b>	<b>\$ 6,978,720</b>	<b>\$ 3,135,910</b>	<b>\$ 2,535,910</b>	<b>\$ 1,863,080</b>

See accompanying Notes to the Financial Statements

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**CRIMINAL INJURIES COMPENSATION FUND**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**JUNE 30, 2008 AND JUNE 30, 2007**

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**A. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES****1. Reporting Entity**

The Criminal Injuries Compensation Fund is part of the primary government and has been included in the *Tennessee Comprehensive Annual Financial Report* as a special revenue fund. The Criminal Injuries Compensation Program (CIC) is funded through privilege and litigation taxes assessed in courts against certain criminal defendants upon conviction, fees levied against parolees, probationers and employed releasees, proceeds from sales of illegal contraband and bond forfeitures in felony cases, donations from individuals serving as jurors, interest income and a federal grant. Payments made under the CIC program are intended to defray the costs of medical services, loss of earnings, burial costs, and other pecuniary losses to either the victim of a crime or to the dependents of deceased victims.

**2. Measurement Focus and Basis of Accounting**

The accompanying financial statements have been prepared in conformity with generally accepted accounting principles as prescribed by the Governmental Accounting Standards Board (GASB) using the flow of current financial resources measurement focus and the modified accrual basis of accounting. Under this method, revenues are recorded when they become both measurable and available, and expenditures are recognized at the time the fund liabilities are incurred. For revenue recognition purposes, taxes and fees are considered to be available if received in the first sixty days of the new year. Federal grants, departmental services, and interest associated with the current fiscal year are all considered to be available if received in twelve months. All other revenue items are considered to be measurable and available only when cash is received by the Criminal Injuries Compensation Fund.

**3. Cash**

The primary government's policy regarding the definition of Cash and Cash Equivalents includes cash management pools as cash. Cash deposited in the Criminal Injuries Compensation Fund is pooled with the State Pooled Investment Fund (SPIF), administered by the State Treasurer, which is authorized by statute to invest funds in accordance with policy guidelines approved by the Funding Board of the State of Tennessee. The current resolution of that board gives the Treasurer authority to invest in collateralized certificates of deposit in authorized state depositories, prime commercial paper, prime bankers' acceptances, certain repurchase agreements, and various U.S. Treasury and Agency obligations. The SPIF is also authorized to enter into securities lending agreements in which U.S. Government securities may be loaned for a fee. The loaned securities are transferred to the borrower by the custodial agent upon simultaneous receipt of collateral securities. The SPIF has not obtained a credit quality rating from a nationally recognized ratings agency. Required risk disclosures relative to the SPIF are presented in the *Tennessee Comprehensive Annual Financial Report*. That report may be obtained by writing to the Tennessee Department of Finance and Administration, Division of Accounts, 14th Floor William R. Snodgrass Tennessee Tower, 312 Rosa L Parks Avenue, Nashville, Tennessee 37243-0298.

**4. Budgetary Process**

Legislation requires that annual budgets be adopted for special revenue funds. The CIC budget is included in the budget presented by the Governor to the General Assembly at the beginning of each annual legislative session. The CIC annual budget is prepared on the modified accrual basis of accounting. Budgetary control is maintained at the departmental level. Budget revisions during the year, reflecting program changes or administrative intradepartmental transfers, may be affected with certain executive and legislative branch approval. Only the legislature may transfer appropriations between departments.

*(continued)*

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**CRIMINAL INJURIES COMPENSATION FUND**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**JUNE 30, 2008 AND JUNE 30, 2007**

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**5. Reclassification**

Funds classified as revenue from state taxes on the June 30, 2007 financial statements have been reclassified as revenue from state fines.

**B. OTHER ACCOUNTING DISCLOSURES****1. Reserves**

A reserve has been established for the Victims of Drunk Drivers Compensation Fund (VDDC) which is included in the Criminal Injuries Compensation Fund. A requirement of the CIC and VDDC combination is that a reserve be established annually for an amount equal to three times the awards paid for VDDC during the fiscal year. *Chapter 761 of the Public Acts of 1992* discusses the fund combination as well as the VDDC reserve requirement.

**2. Receivable**

The receivable shown on the Comparative Balance Sheets as due from federal government includes funds for a grant awarded to the CICF under the Victims of Crime Act Formula Grant Program by the Department of Justice, Office of Justice Programs.

**3. Other Financing Sources**

During fiscal year 2008, two transfers totaling \$3,700,000 were made from the State's general fund. *Chapter 603 of the Public Acts of 2007* authorized a transfer from the general fund of \$1,900,000. *Chapter 1203 of the Public Acts of 2008* authorized a transfer from the general fund of \$1,800,000. During fiscal year 2007, \$602,000 was transferred from the State's general fund in accordance with *Chapter 963 of the Public Acts of 2006*.

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**FLEXIBLE BENEFITS PLAN  
INDEPENDENT AUDITOR'S REPORT**

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STATE OF TENNESSEE  
**COMPTROLLER OF THE TREASURY**  
DEPARTMENT OF AUDIT / DIVISION OF STATE AUDIT  
SUITE 1500, JAMES K. POLK STATE OFFICE BUILDING  
NASHVILLE, TENNESSEE 37243-0264  
PHONE (615) 401-7897 / FAX (615) 532-2765

December 4, 2008

Members of the General Assembly  
and  
The Honorable Dale Sims, Treasurer  
State Capitol  
Nashville, Tennessee 37243

Ladies and Gentlemen:

We have audited the accompanying statements of fiduciary net assets of the Flexible Benefits Plan, an employee benefit trust fund of the State of Tennessee, as of June 30, 2008, and June 30, 2007, and the related statements of changes in fiduciary net assets for the years then ended. These financial statements are the responsibility of management. Our responsibility is to express an opinion on these financial statements, based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

As discussed in Note A.1., the financial statements referred to above present only the Flexible Benefits Plan, an employee benefit trust fund, and do not purport to, and do not, present fairly the financial position of the State of Tennessee as of June 30, 2008, and June 30, 2007, and the changes in its financial position for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to above present fairly, in all material respects, the fiduciary net assets of the Flexible Benefits Plan of the State of Tennessee as of June 30, 2008, and June 30, 2007, and the changes in its fiduciary net assets for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with generally accepted government auditing standards, we have also issued our report dated December 4, 2008, on our consideration of the Flexible Benefits Plan's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, and contracts and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with generally accepted government auditing standards and should be read in conjunction with this report in considering the results of our audit.

Sincerely,

A handwritten signature in cursive script that reads "Arthur A. Hayes, Jr.".

Arthur A. Hayes, Jr., CPA  
Director

**FLEXIBLE BENEFITS PLAN**  
**COMPARATIVE STATEMENTS OF FIDUCIARY NET ASSETS**  
**JUNE 30, 2008 AND JUNE 30, 2007**

	June 30, 2008	June 30, 2007
<b>ASSETS</b>		
Cash	\$ 1,664,270	\$ 1,891,250
Due from other funds	289,628	286,025
<b>TOTAL ASSETS</b>	<u>1,953,898</u>	<u>2,177,275</u>
<b>LIABILITIES</b>		
Accounts payable	99,108	118,442
Due to other funds	356,138	274,354
<b>TOTAL LIABILITIES</b>	<u>464,246</u>	<u>392,796</u>
<b>NET ASSETS</b>		
Held in trust for employee benefit programs	<u>\$ 1,489,652</u>	<u>\$ 1,784,479</u>

*See accompanying Notes to the Financial Statements*

**FLEXIBLE BENEFITS PLAN**  
**COMPARATIVE STATEMENTS OF CHANGES IN FIDUCIARY NET ASSETS**  
**FOR THE YEARS ENDED JUNE 30, 2008 AND JUNE 30, 2007**

	For the Year Ended June 30, 2008	For the Year Ended June 30, 2007
<b>ADDITIONS</b>		
Employee contributions	\$ 8,192,241	\$ 7,677,605
FICA savings	6,903,857	6,371,652
<b>TOTAL ADDITIONS</b>	<u>15,096,098</u>	<u>14,049,257</u>
<b>DEDUCTIONS</b>		
Employee reimbursements	8,083,852	7,338,354
Employee benefit programs		
Deferred compensation match	6,320,553	7,175,371
Wellness program	455,311	499,387
Employee daycare assistance	34,107	48,895
Sick leave bank administration	101,641	101,377
Total employee benefit programs	<u>6,911,612</u>	<u>7,825,030</u>
Administrative fees	395,461	438,319
<b>TOTAL DEDUCTIONS</b>	<u>15,390,925</u>	<u>15,601,703</u>
<b>CHANGE IN NET ASSETS</b>	(294,827)	(1,552,446)
<b>NET ASSETS, BEGINNING OF YEAR</b>	<u>1,784,479</u>	<u>3,336,925</u>
<b>NET ASSETS, END OF YEAR</b>	<u>\$ 1,489,652</u>	<u>\$ 1,784,479</u>

*See accompanying Notes to the Financial Statements*

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**FLEXIBLE BENEFITS PLAN**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**JUNE 30, 2008 AND JUNE 30, 2007**

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**A. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

**1. Reporting Entity**

The Flexible Benefits Plan is part of the primary government and has been included in the *Tennessee Comprehensive Annual Financial Report* as an employee benefit trust fund. The state offers its employees a cafeteria plan created in accordance with *Internal Revenue Code Section 125*. The plan is available on an optional basis to all state employees. Through the plan, employees may elect to direct a portion of their salary to pay for certain benefits. Benefits which may be purchased through the plan include state group medical insurance, state group dental insurance, out-of-pocket medical expenses and/or dependent care expenses. Because elections must be filed before the salary or the benefits are received and because salary directed to the plan may not be withdrawn by participants for any other purpose, salary directed to the plan is exempt from federal income tax and social security tax. Elections made by employees may not be changed during the calendar plan year except in the event of a corresponding change in the participant's family status. Participants may claim expenses incurred through March 15th following the end of the plan year. Any contributions to the plan not withdrawn are forfeited to the state and are used for defraying administrative costs, in accordance with *IRS Proposed Regulation 1.125-2 (Q7)*.

**2. Measurement Focus and Basis of Accounting**

The accompanying financial statements have been prepared in conformity with generally accepted accounting principles as prescribed by the Governmental Accounting Standards Board (GASB). The financial statements have been prepared using the flow of economic resources measurement focus and the accrual basis of accounting. Under this method, revenues are recorded when earned, and expenses are recorded at the time liabilities are incurred.

**3. Cash**

The primary government's policy regarding the definition of Cash and Cash Equivalents includes cash management pools as cash. Cash deposited in the Flexible Benefits Plan is pooled with the State Pooled Investment Fund (SPIF), administered by the State Treasurer, which is authorized by statute to invest funds in accordance with policy guidelines approved by the Funding Board of the State of Tennessee. The current resolution of that board gives the Treasurer authority to invest in collateralized certificates of deposit in authorized state depositories, prime commercial paper, prime bankers' acceptances, certain repurchase agreements, and various U.S. Treasury and Agency obligations. The SPIF is also authorized to enter into securities lending agreements in which U.S. Government securities may be loaned for a fee. The loaned securities are transferred to the borrower by the custodial agent upon simultaneous receipt of collateral securities. The SPIF has not obtained a credit quality rating from a nationally recognized ratings agency. Required risk disclosures relative to the SPIF are presented in the *Tennessee Comprehensive Annual Financial Report*. That report may be obtained by writing to the Tennessee Department of Finance and Administration, Division of Accounts, 14th Floor William R. Snodgrass Tennessee Tower, 312 Rosa L. Parks Avenue, Nashville, Tennessee 37243-0298.

*(continued)*

**FLEXIBLE BENEFITS PLAN**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**JUNE 30, 2008 AND JUNE 30, 2007**

**B. OTHER ACCOUNTING DISCLOSURES**

1. The FICA savings and forfeitures of reimbursement accounts generated by the Flexible Benefits Plan are used by the State for other employee benefit programs. During the years ended June 30, 2008 and June 30, 2007 the following amounts were paid or transferred to other State funds for these employee benefit programs:

<b>Program</b>	<b>FY 2008</b>	<b>FY 2007</b>
Deferred Compensation Contribution Match	\$ 6,320,553	\$ 7,175,371
State Wellness Program	455,311	499,387
State Day Care Assistance	34,107	48,895
Sick Leave Bank	101,641	101,377

2. Due from other funds consists of dependent care and medical reimbursement deposits from the accrued payroll at June 30 for the following funds:

	<b>FY 2008</b>	<b>FY 2007</b>
Due from General Fund	\$ 232,756	\$ 230,432
Due from Internal Service Fund	11,149	11,170
Due from Enterprise Fund	5,445	4,684
Due from Special Revenue Fund	10,532	11,128
Due from Highway Fund	18,278	17,578
Due from Education Trust Fund	11,468	11,033

3. Due to other funds consists of deferred compensation match payments from the accrued payroll at June 30 for the following funds:

	<b>FY 2008</b>	<b>FY 2007</b>
Due to General Fund	\$ 298,032	\$ 223,665
Due to Internal Service Fund	7,358	5,798
Due to Enterprise Fund	2,107	1,570
Due to Special Revenue Fund	9,300	7,300
Due to Highway Fund	38,839	30,003
Due to Education Trust Fund	9,502	6,018

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**RISK MANAGEMENT FUND  
INDEPENDENT AUDITOR'S REPORT**

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**STATE OF TENNESSEE  
COMPTROLLER OF THE TREASURY  
DEPARTMENT OF AUDIT / DIVISION OF STATE AUDIT  
SUITE 1500, JAMES K. POLK STATE OFFICE BUILDING  
NASHVILLE, TENNESSEE 37243-0264  
PHONE (615) 401-7897 / FAX (615) 532-2765**

December 4, 2008

Members of the General Assembly  
and  
Members of the Board of Claims  
and  
The Honorable Dale Sims, Treasurer  
State Capitol  
Nashville, Tennessee 37243

Ladies and Gentlemen:

We have audited the accompanying statements of net assets of the Risk Management Fund, an internal service fund of the State of Tennessee, as of June 30, 2008, and June 30, 2007, and the related statements of revenues, expenses, and changes in fund net assets and cash flows for the years then ended. These financial statements are the responsibility of management. Our responsibility is to express an opinion on these financial statements, based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion. Tennessee statutes, in addition to audit responsibilities, entrust certain other responsibilities to the Comptroller of the Treasury. Those responsibilities include serving as a member of the Board of Claims.

As discussed in Note A.1., the financial statements referred to above present only the Risk Management Fund, an internal service fund, and do not purport to, and do not, present fairly the financial position of the State of Tennessee as of June 30, 2008, and June 30, 2007, and the changes in its financial position and cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Risk Management Fund of the State of Tennessee as of June 30, 2008, and June 30, 2007, and the changes in its financial position and cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with generally accepted government auditing standards, we have also issued our report dated December 4, 2008, on our consideration of the Risk Management Fund's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, and contracts and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with generally accepted government auditing standards and should be read in conjunction with this report in considering the results of our audit.

Sincerely,

A handwritten signature in black ink that reads "Arthur A. Hayes, Jr." with a stylized flourish at the end.

Arthur A. Hayes, Jr., CPA  
Director

**RISK MANAGEMENT FUND**  
**COMPARATIVE STATEMENTS OF NET ASSETS**  
**JUNE 30, 2008 AND JUNE 30, 2007**

	June 30, 2008	June 30, 2007
<b>ASSETS</b>		
Current assets		
Cash	\$ 123,966,156	\$ 116,768,941
Due from federal government	3,340,676	3,332,653
Accounts receivable	0	12,100
Total current assets	<u>127,306,832</u>	<u>120,113,694</u>
Noncurrent assets		
Due from federal government	<u>3,294,074</u>	<u>0</u>
<b>TOTAL ASSETS</b>	<u>130,600,906</u>	<u>120,113,694</u>
<b>LIABILITIES</b>		
Current liabilities		
Accounts payable	482,934	684,502
Deferred revenue	7,000	6,000
Claims liability	28,389,349	28,934,275
Total current liabilities	<u>28,879,283</u>	<u>29,624,777</u>
Noncurrent liabilities		
Claims liability	<u>64,488,551</u>	<u>59,525,524</u>
<b>TOTAL LIABILITIES</b>	<u>93,367,834</u>	<u>89,150,301</u>
<b>NET ASSETS - UNRESTRICTED</b>	<u>\$ 37,233,072</u>	<u>\$ 30,963,393</u>

*See accompanying Notes to the Financial Statements*

**RISK MANAGEMENT FUND**  
**COMPARATIVE STATEMENTS OF REVENUES, EXPENSES, AND CHANGES IN FUND NET ASSETS**  
**FOR THE YEARS ENDED JUNE 30, 2008 AND JUNE 30, 2007**

	For the Year Ended June 30, 2008	For the Year Ended June 30, 2007
<b>OPERATING REVENUES</b>		
Casualty premiums	\$ 38,893,900	\$ 15,017,600
Property premiums	5,491,000	5,450,320
<b>TOTAL OPERATING REVENUES</b>	<b>44,384,900</b>	<b>20,467,920</b>
<b>OPERATING EXPENSES</b>		
Torts		
Death	1,742,145	1,957,966
Bodily injury	3,972,936	3,667,255
Property damage	794,530	827,155
Total Torts	6,509,611	6,452,376
Workers' Compensation		
Death	275,251	431,084
Medical	11,117,290	10,587,088
Temporary disability	2,768,288	2,066,577
Permanent disability	6,782,070	6,441,543
Total Workers' Compensation	20,942,899	19,526,292
Property Damage		
Employee property	28,266	18,867
State owned property	1,814,435	5,831,067
Total Property Damage	1,842,701	5,849,934
Property insurance premiums	2,748,524	2,482,031
Professional/ Administrative	9,398,779	9,134,944
Addition to accrued liability	4,418,101	4,993,441
<b>TOTAL OPERATING EXPENSES</b>	<b>45,860,615</b>	<b>48,439,018</b>
<b>OPERATING LOSS</b>	<b>(1,475,715)</b>	<b>(27,971,098)</b>
<b>NON-OPERATING REVENUES</b>		
Grant revenue	3,302,097	3,332,653
Interest income	4,441,672	6,352,648
Taxes	1,625	1,775
<b>TOTAL NON-OPERATING REVENUES</b>	<b>7,745,394</b>	<b>9,687,076</b>
<b>CHANGE IN NET ASSETS</b>	<b>6,269,679</b>	<b>(18,284,022)</b>
<b>NET ASSETS, BEGINNING OF YEAR</b>	<b>30,963,393</b>	<b>49,247,415</b>
<b>NET ASSETS, END OF YEAR</b>	<b>\$ 37,233,072</b>	<b>\$ 30,963,393</b>

*See accompanying Notes to the Financial Statements*

**RISK MANAGEMENT FUND**  
**COMPARATIVE STATEMENTS OF CASH FLOWS**  
**FOR THE YEARS ENDED JUNE 30, 2008 AND JUNE 30, 2007**

	For the Year Ended June 30, 2008	For the Year Ended June 30, 2007
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>		
Receipts from premiums	\$ 44,397,000	\$ 20,455,820
Payments for claims	(29,313,846)	(31,687,655)
Payments for administrative expenses	(9,392,759)	(9,223,185)
Payments for insurance premiums	(2,936,477)	(2,385,863)
	<u>2,753,918</u>	<u>(22,840,883)</u>
<b>NET CASH FROM OPERATING ACTIVITIES</b>		
<b>CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES</b>		
Taxes received	1,625	1,775
	<u>1,625</u>	<u>1,775</u>
<b>NET CASH FROM NONCAPITAL FINANCING ACTIVITIES</b>		
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>		
Interest received	4,441,672	6,352,648
	<u>4,441,672</u>	<u>6,352,648</u>
<b>NET CASH FROM INVESTING ACTIVITIES</b>		
<b>NET INCREASE (DECREASE) IN CASH</b>	7,197,215	(16,486,460)
<b>CASH, BEGINNING OF YEAR</b>	<u>116,768,941</u>	<u>133,255,401</u>
<b>CASH, END OF YEAR</b>	<u>\$ 123,966,156</u>	<u>\$ 116,768,941</u>
<b>RECONCILIATION OF OPERATING INCOME TO NET CASH FROM OPERATING ACTIVITIES</b>		
<b>OPERATING LOSS</b>	\$ (1,475,715)	\$ (27,971,098)
<b>ADJUSTMENTS TO RECONCILE OPERATING LOSS TO NET CASH FROM OPERATING ACTIVITIES</b>		
Changes in assets and liabilities		
(Increase) decrease in accounts receivable	12,100	(12,100)
Increase (decrease) in accounts payable	(201,568)	148,874
Increase in deferred revenue	1,000	0
Increase in claims liability	4,418,101	4,993,441
	<u>4,229,633</u>	<u>5,130,215</u>
<b>TOTAL ADJUSTMENTS</b>		
<b>NET CASH FROM OPERATING ACTIVITIES</b>	<u>\$ 2,753,918</u>	<u>\$ (22,840,883)</u>

*See accompanying Notes to the Financial Statements*

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**RISK MANAGEMENT FUND**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**JUNE 30, 2008 AND JUNE 30, 2007**

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**A. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

**1. Reporting Entity**

The Risk Management Fund (RMF) is part of the primary government and has been included in the *Tennessee Comprehensive Annual Financial Report* as an internal service fund.

**2. Measurement Focus and Basis of Accounting**

The accompanying financial statements have been prepared in conformity with generally accepted accounting principles as prescribed by the Governmental Accounting Standards Board (GASB). The RMF generally follows private sector standards of accounting and financial reporting issued prior to December 1, 1989, to the extent that these standards do not conflict with or contradict guidance of the Governmental Accounting Standards Board. The financial statements have been prepared using the flow of economic resources measurement focus and the accrual basis of accounting. Under this method, revenues are recorded when earned and expenses are recorded at the time liabilities are incurred. The RMF distinguishes operating revenues and expenses from nonoperating items. Operating revenues and expenses generally result from the services provided by the RMF. The principal operating revenue of the RMF consists of charges to its customers for insurance premiums. Operating expenses include claims expenses, insurance premiums, administrative expenses and the current charge to the accrued liability. Revenues and expenses not resulting from the services provided by the RMF are reported as nonoperating revenues and expenses.

**3. Cash**

The primary government's policy regarding the definition of Cash and Cash Equivalents includes cash management pools as cash. Cash deposited in the RMF is pooled with the State Pooled Investment Fund (SPIF), administered by the State Treasurer, which is authorized by statute to invest funds in accordance with policy guidelines approved by the Funding Board of the State of Tennessee. The current resolution of that board gives the Treasurer authority to invest in collateralized certificates of deposit in authorized state depositories, prime commercial paper, prime bankers' acceptances, certain repurchase agreements, and various U.S. Treasury and Agency obligations. The SPIF is also authorized to enter into securities lending agreements in which U.S. Government securities may be loaned for a fee. The loaned securities are transferred to the borrower by the custodial agent upon simultaneous receipt of collateral securities. The SPIF has not obtained a credit quality rating from a nationally recognized ratings agency. Required risk disclosures relative to the SPIF are presented in the *Tennessee Comprehensive Annual Financial Report*. That report may be obtained by writing to the Tennessee Department of Finance and Administration, Division of Accounts, 14th Floor William R. Snodgrass Tennessee Tower, 312 Rosa L Parks Avenue, Nashville, Tennessee 37243-0298.

**B. OTHER ACCOUNTING DISCLOSURES**

**1. Risk Management**

It is the policy of the state not to purchase commercial insurance for the risks of casualty losses for general liability, automobile liability, professional malpractice, and workers' compensation. The state's management believes it is more economical to manage these risks internally and set aside assets for claim settlement in its internal service fund, the RMF. The state purchases commercial insurance for real property, flood, earthquake, and builder's risk losses and surety bond coverage on the state's officials and employees. The RMF is also responsible for claims

*(continued)*

**RISK MANAGEMENT FUND**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**JUNE 30, 2008 AND JUNE 30, 2007**

for damages to state owned property up to the amount of the property insurance aggregate deductible amount. The insurance policy deductibles vary from \$25,000 per occurrence, depending on the type of coverage, to an aggregate of \$5 million. Settled claims resulting from these risks have not exceeded commercial insurance coverage in any of the past three fiscal years. All agencies and authorities of the state participate in the RMF, except for the Dairy Promotion Board and the Certified Cotton Growers' Organization. The Tennessee Education Lottery Corporation participates in the RMF for general liability purposes but is responsible for its own worker's compensation coverage.

The RMF liabilities are reported when it is probable that a loss has occurred and the amount of that loss can be reasonably estimated. Liabilities include an amount for claims that have been incurred but not reported. Because actual claims liabilities depend on such complex factors as inflation, changes in legal doctrines, and damage awards, the process used in computing claims liability does not necessarily result in an exact amount. Claims liabilities are reevaluated annually to take into consideration recently settled claims, the frequency of claims, and other economic and social factors. The present value of the casualty liability as actuarially determined was \$84,622,437 (discounted at 3.50%) at June 30, 2008 and \$83,836,098 (discounted at 3.50%) at June 30, 2007. An additional \$300,000 was added to the casualty liability for 2008 for a general liability claim ordered to be paid by the courts. The order occurred prior to June 30, 2008 but had not yet been paid at that date. The data for this claim was not provided to the actuary and thus was not included in the actuarial calculation. The accrued liability for incurred property losses was \$7,955,463 at June 30, 2008 and \$4,623,701 at June 30, 2007. The changes in the balances of the claims liabilities during fiscal years 2007 and 2008 were as follows:

Fiscal Year	Beginning Claims Liability	Current Year Claims and Changes in Estimates	Claim Payments	Ending Claims Liability
2008	\$88,459,799	\$33,713,312	\$(29,295,211)	\$92,877,900
2007	\$83,466,358	\$36,822,043	\$(31,828,602)	\$88,459,799

The RMF held \$123.9 million in cash at June 30, 2008 and \$116.8 million in cash at June 30, 2007 that is designated for payment of these claims.

The RMF allocates the cost of providing claims servicing and claims payment by charging a premium to each agency based on a percentage of each organization's expected loss costs which include both experience and exposures. This charge considers recent trends in actual claims experience of the state as a whole.

**2. Receivable**

The receivables shown on the Statement of Net Assets as due from federal government includes funds to be received from the Federal Emergency Management Agency for property losses that were classified as a disaster. The portion of these funds expected to be received in the next fiscal year is classified as a current asset.

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**SMALL AND MINORITY-OWNED BUSINESS ASSISTANCE PROGRAM FUND  
INDEPENDENT AUDITOR'S REPORT**

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STATE OF TENNESSEE  
**COMPTROLLER OF THE TREASURY**  
DEPARTMENT OF AUDIT / DIVISION OF STATE AUDIT  
SUITE 1500, JAMES K. POLK STATE OFFICE BUILDING  
NASHVILLE, TENNESSEE 37243-0264  
PHONE (615) 401-7897 / FAX (615) 532-2765

December 4, 2008

Members of the General Assembly  
and  
The Honorable Dale Sims, Treasurer  
State Capitol  
Nashville, Tennessee 37243

Ladies and Gentlemen:

We have audited the accompanying balance sheets of the Small and Minority-Owned Business Assistance Program, a special revenue fund of the State of Tennessee, as of June 30, 2008, and June 30, 2007, and the related statements of revenues, expenditures, and changes in fund balance and revenues, expenditures, and changes in fund balance (budget and actual) for the years then ended. These financial statements are the responsibility of management. Our responsibility is to express an opinion on these financial statements, based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

As discussed in Note A.1., the financial statements referred to above present only the Small and Minority-Owned Business Assistance Program, a special revenue fund, and do not purport to, and do not, present fairly the financial position of the State of Tennessee as of June 30, 2008, and June 30, 2007, and the changes in its financial position and budgetary comparisons for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Small and Minority-Owned Business Assistance Program of the State of Tennessee as of June 30, 2008, and June 30, 2007, and the changes in its financial position and budgetary comparisons for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with generally accepted government auditing standards, we have also issued our report dated December 4, 2008, on our consideration of the Small and Minority-Owned Business Assistance Program's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, and contracts and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with generally accepted government auditing standards and should be read in conjunction with this report in considering the results of our audit.

Sincerely,

A handwritten signature in cursive script that reads "Arthur A. Hayes, Jr.".

Arthur A. Hayes, Jr., CPA  
Director

**SMALL AND MINORITY-OWNED BUSINESS ASSISTANCE PROGRAM FUND  
COMPARATIVE BALANCE SHEETS  
JUNE 30, 2008 AND JUNE 30, 2007**

	June 30, 2008	June 30, 2007
<b>ASSETS</b>		
Cash	\$ 10,305,873	\$ 12,117,094
Long-term loan receivables	1,400,000	0
<b>TOTAL ASSETS</b>	<u>\$ 11,705,873</u>	<u>\$ 12,117,094</u>
<b>LIABILITIES AND FUND BALANCES</b>		
<b>LIABILITIES</b>		
Accounts payable	\$ 19,375	\$ 0
<b>TOTAL LIABILITIES</b>	<u>19,375</u>	<u>0</u>
<b>FUND BALANCES</b>		
Reserved for loans	1,400,000	0
Unreserved	10,286,498	12,117,094
<b>TOTAL FUND BALANCES</b>	<u>11,686,498</u>	<u>12,117,094</u>
<b>TOTAL LIABILITIES AND FUND BALANCES</b>	<u>\$ 11,705,873</u>	<u>\$ 12,117,094</u>

*See accompanying Notes to the Financial Statements*

**SMALL AND MINORITY-OWNED BUSINESS ASSISTANCE PROGRAM FUND  
COMPARATIVE STATEMENTS OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCE  
FOR THE YEARS ENDED JUNE 30, 2008 AND JUNE 30, 2007**

	For the Year Ended June 30, 2008	For the Year Ended June 30, 2007
<b>REVENUES</b>		
Interest income	\$ 490,212	\$ 630,066
<b>TOTAL REVENUES</b>	<u>490,212</u>	<u>630,066</u>
<b>EXPENDITURES</b>		
Loan guarantee payments	0	201,946
Disparity study	464,000	0
Administrative cost	456,808	105,603
<b>TOTAL EXPENDITURES</b>	<u>920,808</u>	<u>307,549</u>
<b>EXCESS (DEFICIENCY) OF REVENUES OVER (UNDER) EXPENDITURES</b>	(430,596)	322,517
<b>FUND BALANCES, BEGINNING OF YEAR</b>	<u>12,117,094</u>	<u>11,794,577</u>
<b>FUND BALANCES, END OF YEAR</b>	<u>\$ 11,686,498</u>	<u>\$ 12,117,094</u>

*See accompanying Notes to the Financial Statements*

**SMALL AND MINORITY-OWNED BUSINESS ASSISTANCE PROGRAM FUND  
STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCE BUDGET  
AND ACTUAL (BUDGETARY BASIS) FOR THE YEARS ENDED JUNE 30, 2008 AND JUNE 30, 2007**

	For the Year Ended June 30, 2008			For the Year Ended June 30, 2007		
	Original Budget	Final Budget	Actual (Budgetary Basis)	Original Budget	Final Budget	Actual (Budgetary Basis)
<b>SOURCES OF FINANCIAL RESOURCES</b>						
<b>FUND BALANCES, BEGINNING OF YEAR</b>	\$ 12,117,094	\$ 12,117,094	\$ 12,117,094	\$ 11,794,577	\$ 11,794,577	\$ 11,794,577
<b>REVENUES</b>						
Interest income	80,100	151,800	490,212	80,100	80,100	630,066
<b>TOTAL SOURCES OF FINANCIAL RESOURCES</b>	<u>12,197,194</u>	<u>12,268,894</u>	<u>12,607,306</u>	<u>11,874,677</u>	<u>11,874,677</u>	<u>12,424,643</u>
<b>USES OF FINANCIAL RESOURCES</b>						
<b>EXPENDITURES</b>						
Loan guarantee payments	68,100	151,800	0	80,100	140,100	201,946
Disparity study	0	2,100,000	464,000	0	2,000,000	0
Administrative cost	0	0	456,808	0	0	105,603
<b>TOTAL USES OF FINANCIAL RESOURCES</b>	<u>68,100</u>	<u>2,251,800</u>	<u>920,808</u>	<u>80,100</u>	<u>2,140,100</u>	<u>307,549</u>
<b>FUND BALANCES, END OF YEAR</b>	<u>\$ 12,129,094</u>	<u>\$ 10,017,094</u>	<u>\$ 11,686,498</u>	<u>\$ 11,794,577</u>	<u>\$ 9,734,577</u>	<u>\$ 12,117,094</u>

See accompanying Notes to the Financial Statements

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**SMALL AND MINORITY-OWNED BUSINESS ASSISTANCE PROGRAM FUND**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**JUNE 30, 2008 AND JUNE 30, 2007**

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**A. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES****1. Reporting Entity**

The Small and Minority-owned Business Assistance Program Fund (the Fund) is part of the primary government and has been included in the *Tennessee Comprehensive Annual Financial Report* as a special revenue fund.

**2. Measurement Focus and Basis of Accounting**

The accompanying financial statements have been prepared in conformity with generally accepted accounting principles as prescribed by the Governmental Accounting Standards Board (GASB) using the flow of current financial resources measurement focus and the modified accrual basis of accounting. Under this method, revenues are recorded when they become both measurable and available, and expenditures are recognized at the time the fund liabilities are incurred. For revenue recognition purposes, interest income associated with the current fiscal year is considered to be available if received in twelve months.

**3. Cash**

The state's accounting policy regarding the definition of Cash and Cash Equivalents includes cash management pools as cash. Cash deposited in the Small and Minority-owned Business Assistance Program is pooled with the State Pooled Investment Fund (SPIF), administered by the State Treasurer, which is authorized by statute to invest funds in accordance with policy guidelines approved by the Funding Board of the State of Tennessee. The current resolution of that board gives the Treasurer authority to invest in collateralized certificates of deposit in authorized state depositories, prime commercial paper, prime bankers' acceptances, certain repurchase agreements and various U.S. Treasury and Agency obligations. The SPIF is also authorized to enter into securities lending agreements in which U.S. Government securities may be loaned for a fee. The loaned securities are transferred to the borrower by the custodial agent upon simultaneous receipt of collateral securities. The SPIF has not obtained a credit quality rating from a nationally recognized ratings agency. Required risk disclosures relative to the State Pooled Investment Fund are presented in the *Tennessee Comprehensive Annual Financial Report*. That report may be obtained by writing to the Tennessee Department of Finance and Administration, Division of Accounts, 14th Floor William R. Snodgrass Tennessee Tower, 312 Rosa L. Parks Avenue, Nashville, Tennessee 37243-0298.

**4. Budgetary Process**

Legislation requires that annual budgets be adopted for special revenue funds. The Small and Minority-owned Business Assistance Program Fund's budget is included in the budget presented by the Governor to the General Assembly at the beginning of each annual legislative session. The Fund's annual budget is prepared on the modified accrual basis of accounting. Budgetary control is maintained at the departmental level. Budget revisions during the year, reflecting program changes or administrative intradepartmental transfers, may be affected with certain executive and legislative branch approval. Only the legislature may transfer appropriations between departments.

**5. Reclassification**

Expenditures classified on the June 30, 2007 financial statements as contract payments have been reclassified as administrative cost.

(continued)

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**SMALL AND MINORITY-OWNED BUSINESS ASSISTANCE PROGRAM FUND**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**JUNE 30, 2008 AND JUNE 30, 2007**

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**B. OTHER ACCOUNTING DISCLOSURES**

- 1. Small and Minority-Owned Business Assistance Program** - The Small and Minority-owned Business Assistance Program, administered by the State Treasurer, was established by *Chapter 830 of the Public Acts of 2004* to support the outreach to new, expanding, and existing businesses in Tennessee that do not have reasonable access to capital markets and traditional commercial lending facilities. The Fund is supported from funds remaining in the former Small and Minority-owned Telecommunications Business Assistance Program Fund, and interest income earned on the Fund. Payments are made in support of the assistance program for small and minority-owned businesses, and may include loans and loan guarantees, technical assistance and services, and consulting and educational services.
- 2. Commitments** - The Fund did not have any loan guarantees outstanding at June 30, 2008. As of June 30, 2007, the Fund was under loan guarantee obligations in the amount of \$58,979 in the event of loan defaults.
- 3. Receivables** - The long-term loan receivables on the Comparative Balance Sheets represent outstanding loans made to qualified organizations under the provisions of the Small and Minority-Owned Business Assistance Program.
- 4. Reserves** - The reserve for loans includes funds on loan to qualified organizations under the provisions of the program.

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**STATE POOLED INVESTMENT FUND  
INDEPENDENT AUDITOR'S REPORT**

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STATE OF TENNESSEE  
**COMPTROLLER OF THE TREASURY**  
DEPARTMENT OF AUDIT / DIVISION OF STATE AUDIT  
SUITE 1500, JAMES K. POLK STATE OFFICE BUILDING  
NASHVILLE, TENNESSEE 37243-0264  
PHONE (615) 401-7897 / FAX (615) 532-2765

December 4, 2008

Members of the General Assembly  
and  
Members of the State Funding Board  
and  
The Honorable Dale Sims, Treasurer  
State Capitol  
Nashville, Tennessee 37243

Ladies and Gentlemen:

We have audited the accompanying statements of fiduciary net assets of the State Pooled Investment Fund as of June 30, 2008, and June 30, 2007, and the related statements of changes in fiduciary net assets for the years then ended. These financial statements are the responsibility of management. Our responsibility is to express an opinion on these financial statements, based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion. Tennessee statutes, in addition to audit responsibilities, entrust certain other responsibilities to the Comptroller of the Treasury. Those responsibilities include serving as a member of the State Funding Board.

As discussed in Note A.1., the financial statements referred to above present only the State Pooled Investment Fund of the State of Tennessee and do not purport to, and do not, present fairly the financial position of the State of Tennessee as of June 30, 2008, and June 30, 2007, and the changes in its financial position for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to above present fairly, in all material respects, the fiduciary net assets of the State Pooled Investment Fund of the State of Tennessee as of June 30, 2008, and June 30, 2007, and the changes in its fiduciary net assets for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with generally accepted government auditing standards, we have also issued our report dated December 4, 2008, on our consideration of the State Pooled Investment Fund's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, and contracts and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with generally accepted government auditing standards and should be read in conjunction with this report in considering the results of our audit.

Sincerely,

A handwritten signature in cursive script that reads 'Arthur A. Hayes, Jr.'.

Arthur A. Hayes, Jr., CPA  
Director

**STATE POOLED INVESTMENT FUND  
COMPARATIVE STATEMENTS OF FIDUCIARY NET ASSETS  
JUNE 30, 2008 AND JUNE 30, 2007**

	June 30, 2008	June 30, 2007
<b>ASSETS</b>		
Cash and cash equivalents	\$ 3,573,096,697	\$ 4,867,617,896
Short-term investments, at amortized cost	5,008,478,537	2,860,015,701
Accrued income receivable	15,238,704	51,184,845
<b>TOTAL ASSETS</b>	8,596,813,938	7,778,818,442

**LIABILITIES AND NET ASSETS**

NET ASSETS HELD IN TRUST FOR POOL PARTICIPANTS	\$ 8,596,813,938	\$ 7,778,818,442
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*See accompanying Notes to the Financial Statements*

**STATE POOLED INVESTMENT FUND  
COMPARATIVE STATEMENTS OF CHANGES IN FIDUCIARY NET ASSETS  
FOR THE YEARS ENDED JUNE 30, 2008 AND JUNE 30, 2007**

	For the Year Ended June 30, 2008	For the Year Ended June 30, 2007
<b>OPERATIONS</b>		
Investment income	\$ 326,177,632	\$ 351,903,181
Expenses		
Administrative fee	4,026,688	3,330,233
Custodian and banking services fees	60,664	32,549
Total expenses	4,087,352	3,362,782
<b>NET INVESTMENT INCOME</b>	322,090,280	348,540,399
<b>CAPITAL SHARE TRANSACTIONS (DOLLAR AMOUNTS AND NUMBER OF SHARES ARE THE SAME)</b>		
Shares sold	36,424,289,408	34,691,661,275
Less shares redeemed	35,928,384,192	33,720,095,902
<b>INCREASE FROM CAPITAL SHARE TRANSACTIONS</b>	495,905,216	971,565,373
<b>TOTAL INCREASE IN NET ASSETS</b>	817,995,496	1,320,105,772.60
<b>NET ASSETS HELD IN TRUST FOR POOL PARTICIPANTS</b>		
BEGINNING OF YEAR	7,778,818,442	6,458,712,670
END OF YEAR	\$ 8,596,813,938	\$ 7,778,818,442

*See accompanying Notes to the Financial Statements*

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**STATE POOLED INVESTMENT FUND**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**JUNE 30, 2008 AND JUNE 30, 2007**

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**A. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES****1. Reporting Entity**

The State Pooled Investment Fund (SPIF) is an external investment pool sponsored by the State of Tennessee. The external portion of the State Pooled Investment Fund, consisting of funds belonging to entities outside of the State of Tennessee Financial Reporting Entity, has been included as a separate investment trust fund in the *Tennessee Comprehensive Annual Financial Report*. The internal portion, consisting of funds belonging to the State and its component units, has been included in the various participating funds and component units in the *Tennessee Comprehensive Annual Financial Report*.

**2. Measurement Focus and Basis of Accounting**

The accompanying financial statements have been prepared in conformity with generally accepted accounting principles as prescribed by the Governmental Accounting Standards Board (GASB) using the flow of economic resources measurement focus and the accrual basis of accounting. Under this basis, revenues are recorded when earned and expenses are recorded at the time liabilities are incurred.

**3. Cash and Cash Equivalents**

This classification includes deposits in demand accounts as well as short-term investments with a maturity date within three months of the date acquired by the State.

**4. Method Used to Report Investments and Participant Shares**

The SPIF is not registered with the Securities and Exchange Commission (SEC) as an investment company but, through its investment policy adopted by the Funding Board of the State of Tennessee (Funding Board), operates in a manner consistent with the SEC's Rule 2a7 of the *Investment Company Act of 1940*. Rule 2a7 allows SEC registered mutual funds to use amortized cost to report net assets in computing share prices. Likewise, the SPIF uses amortized cost accounting measures to report investments and share prices. During the fiscal years ended June 30, 2008 and June 30, 2007, the State had not obtained or provided any legally binding guarantees to support the value of participant shares. The State of Tennessee has not obtained a credit quality rating for the SPIF from a nationally recognized credit ratings agency.

**B. DEPOSITS AND INVESTMENTS**

The State Pooled Investment Fund is authorized by statute to invest funds in accordance with policy guidelines approved by the Funding Board. The current resolution of the Funding Board gives the Treasurer approval to invest in collateralized certificates of deposit in authorized state depositories, prime commercial paper, prime bankers' acceptances, bonds, notes, and treasury bills of the United States or other obligations guaranteed as to principal and interest by the United States or any of its agencies, repurchase agreements for obligations of the United States or its agencies, and securities lending agreements whereby securities may be loaned for a fee. Investments in derivative type securities and investments of high risk are prohibited.

*(continued)*

**STATE POOLED INVESTMENT FUND**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**JUNE 30, 2008 AND JUNE 30, 2007**

At June 30, 2008 and June 30, 2007, the principal amount of certificates of deposit in state depositories was \$2,495,325,000 and \$2,233,085,000 respectively. Interest rates on certificates of deposit held at June 30, 2008 ranged from 2.0% to 5.25% and at June 30, 2007 ranged from 5.25% to 5.3%. The days to maturity on certificates of deposit ranged from 22 to 239 days at June 30, 2008 and 29 to 357 days at June 30, 2007.

As of June 30, 2008 and June 30, 2007, the SPIF had the following investments:

June 30, 2008 Investment Type	Carrying Amount	Fair Value	Par Value	Interest Rate Range	Days to Maturity	Carrying Amount Credit Quality Ratings		
						AAA	A1(1)	Not Rated (2)
Cash Equivalents and Short-term Investments:								
U.S. Government Agencies	\$ 3,113,841,984	\$ 3,110,291,646	\$ 3,123,536,500	1.64% to 5.75%	1 to 389 days	\$ 557,228,731		\$ 2,556,613,253
Commercial Paper	2,665,600,874	2,665,600,874	2,666,000,000	2.05% to 2.55%	1 to 44 days		2,665,600,874	
<b>Total Cash Equivalents and Short-term Investments</b>	<b>5,779,442,858</b>	<b>\$ 5,775,892,520</b>	<b>\$ 5,789,536,500</b>			<b>\$ 557,228,731</b>	<b>\$ 2,665,600,874</b>	<b>\$ 2,556,613,253</b>
Less: short-term investments classified as cash equivalents on Statement of Fiduciary Net Assets	(2,905,439,321)							
Add: certificates of deposit classified as short-term investments on Statement of Fiduciary Net Assets	2,134,475,000							
<b>Short-term investments as shown on Statement of Fiduciary Net Assets</b>	<b>\$ 5,008,478,537</b>							

Footnotes

- 1 A1 is the highest rating category for commercial paper
- 2 Includes securities that are implicitly guaranteed by the U.S. government but are not rated by Standard and Poor's or Moody's.

June 30, 2007 Investment Type	Carrying Amount	Fair Value	Par Value	Interest Rate Range	Days to Maturity	Carrying Amount Credit Quality Ratings		
						AAA	A1(1)	Not Rated (2)
Cash Equivalents and Short-term Investments:								
U.S. Government Agencies	\$ 2,564,259,618	\$ 2,562,261,251	\$ 2,566,367,000	2.88% to 5.38%	72 to 391 days	\$ 2,065,461,749		\$ 498,797,869
Commercial Paper	2,723,847,582	2,723,847,582	2,725,240,000	5.21% to 5.37%	3 to 45 days		\$ 2,723,847,582	
<b>Total Cash Equivalents and Short-term Investments</b>	<b>5,288,107,200</b>	<b>\$ 5,286,108,833</b>	<b>\$ 5,291,607,000</b>			<b>\$ 2,065,461,749</b>	<b>\$ 2,723,847,582</b>	<b>\$ 498,797,869</b>
Less: short-term investments classified as cash equivalents on Statement of Fiduciary Net Assets	(2,922,531,500)							
Add: certificates of deposit classified as short-term investments on Statement of Fiduciary Net Assets	494,440,000							
<b>Short-term investments as shown on Statement of Fiduciary Net Assets</b>	<b>\$ 2,860,015,700</b>							

Footnotes

- 1 A1 is the highest rating category for commercial paper
- 2 Includes securities that are implicitly guaranteed by the U.S. government but are not rated by Standard and Poor's or Moody's.

(continued)

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**STATE POOLED INVESTMENT FUND**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**JUNE 30, 2008 AND JUNE 30, 2007**

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**Credit Risk**

Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. Credit quality ratings for the SPIF's investments in debt securities as of June 30, 2008 and June 30, 2007 are included in the above schedule. Securities are rated using Standard and Poor's and/or Moody's and are presented above using the Standard and Poor's rating scale. State statutes provide a process for financial institutions desiring to act as state depositories to be approved by the State Treasurer. Statutes also provide for the Commissioner of Financial Institutions to advise, on a timely basis, the Treasurer and the Commissioner of Finance and Administration of the condition of each state bank and state chartered savings and loan association, including his recommendations regarding its condition and safety as a state depository. Similar provisions apply to federally chartered banks and savings and loan associations designated as state depositories. This process ensures that institutions whose financial status is uncertain are monitored for collateral sufficiency. All certificates of deposit are required by policy to be placed directly with state depositories. All repurchase agreements are done with primary dealers in government securities which have executed a master repurchase agreement with the State. The SPIF's investment policy requires a AAA credit quality rating for the purchase of obligations of instrumentalities that are not fully guaranteed by the United States government. Prime banker's acceptances must be issued by domestic banks with a minimum AA long-term debt rating or foreign banks with a AAA long-term debt rating by a majority of the rating services that have rated the issuer. The short-term debt rating must be at least A1 or the equivalent by all of the rating services that rate the issuer. Commercial paper should be rated in the highest tier by all rating agencies that rate the paper. Commercial paper on a credit rating agency's negative credit watch list cannot be purchased under the investment policy. The policy requires that a credit analysis report on the corporation be prepared prior to acquisition of the commercial paper.

**Concentration of Credit Risk**

A concentration of investments in any one single issuer of debt securities presents a greater risk for loss in the event that the issuer fails on its obligations. An objective stated in the SPIF's investment policy is that the investment portfolio will be diversified to avoid incurring unreasonable and avoidable risks regarding specific security types or individual financial institutions. Acquisitions are monitored by policy to assure that no more than twenty percent (20%) of the book value of the pool, at the date of acquisition, is invested in a single United States government agency security and that such acquisition does not cause the SPIF's aggregate United States government agency holdings to exceed forty percent (40%) of the total book value of the pool on such date. In addition, the SPIF's investment policy limits the book value of prime banker's acceptances to five percent (5%) of the total book value of the pool and limits such investments in any one commercial bank to the lesser of five percent (5%) of the portfolio's book value or \$25 million. Prime commercial paper investments are limited to five percent (5%) of the total portfolio book value invested in any one single issuing corporation and the total holdings of an issuer's paper should not represent more than five percent (5%) of the issuing corporation's total outstanding commercial paper, with the maximum amount of a specific corporation's commercial paper limited to \$100 million, not including commercial paper maturing on the next business day. Prime commercial paper shall not exceed forty percent (40%) of the total pool's book value. The SPIF had the following investment amounts and percentages of total investments, in organizations representing five percent (5%) or more of total investments, excluding those organizations whose issues are explicitly guaranteed by the United States government, and investments in mutual funds, external investment pools, and other pooled investments:

*(continued)*

**STATE POOLED INVESTMENT FUND  
NOTES TO THE FINANCIAL STATEMENTS  
JUNE 30, 2008 AND JUNE 30, 2007**

Issuer Organization	June 30, 2008	
	Carrying Amount	Percentage of Total Investments
Federal National Mortgage Association	\$ 1,018,192,043	17.62 %
Federal Home Loan Mortgage Corporation	1,006,383,112	17.41
Federal Home Loan Banks	661,047,171	11.44
Merrill Lynch	449,968,750	7.79
Toyota	449,968,750	7.79
Nestle	449,904,403	7.78
Federal Farmers Credit Banks	428,219,658	7.41
American General	349,975,208	6.06
HSBC	299,981,250	5.19

Issuer Organization	June 30, 2007	
	Carrying Amount	Percentage of Total Investments
Federal Home Loan Banks	\$ 1,291,383,217	24.42 %
Federal Home Loan Mortgage Corporation	734,889,721	13.90
Federal National Mortgage Association	429,817,869	8.13
General Electric	374,944,479	7.09
Citigroup	374,842,382	7.09
HSBC	374,812,847	7.09
Toyota	349,948,333	6.62
Prudential Funding	299,955,667	5.67

**Interest Rate Risk**

Interest rate risk is the risk that future changes in prevailing market rates of interest will have an adverse effect on the fair value of debt investments. The fair values of securities with long terms to maturity may be highly sensitive to interest rate changes. The SPIF's investment policy with respect to maturity states that the dollar weighted average maturity of the pool shall not exceed ninety (90) days and that no investment may be purchased with a remaining maturity of greater than three hundred ninety seven (397) calendar days. In addition, it is the intent of the Funding Board that the market value of the SPIF not deviate more than 0.5 percent from amortized cost. If it does, actions may include, but not be limited to, selling securities whose market value substantially deviates from amortized cost, and investing in securities with ninety (90) days or less to maturity. Agency variable rate notes are permitted by investment policy provided they are indexed to treasury bill, commercial paper, federal funds, LIBOR or the prime rates. It is the intent of the Funding Board that variable rate notes must move in the same direction as general money market rates. Prime banker's acceptances must have an original maturity of not more than two hundred seventy (270) days to be eligible for purchase, with the intent to hold to maturity. Prime commercial paper shall not have a maturity that exceeds one hundred eighty (180) days, and individual repurchase agreement transactions shall not have a maturity that exceeds ninety (90) days.

*(continued)*

**STATE POOLED INVESTMENT FUND  
 NOTES TO THE FINANCIAL STATEMENTS  
 JUNE 30, 2008 AND JUNE 30, 2007**

As of June 30, 2008 and June 30, 2007, the SPIF portfolio had the following weighted average maturities on debt investments:

June 30, 2008		
Investment Type	Carrying Amount	Weighted Average Maturity (Months)
U.S. Government Agencies	\$ 3,113,841,984	4.97
Commercial Paper	2,665,600,874	0.10
Aggregate Portfolio	\$ 5,779,442,858	2.72

June 30, 2007		
Investment Type	Carrying Amount	Weighted Average Maturity (Months)
U.S. Government Agencies	\$ 2,564,259,618	6.27
Commercial Paper	2,723,847,582	0.17
Aggregate Portfolio	\$ 5,288,107,200	3.13

**C. OTHER ACCOUNTING DISCLOSURES**

**Description of the State Pooled Investment Fund**

The State Pooled Investment Fund is established by *Tennessee Code Annotated*, Section 9-4-603 “for the purpose of receiving and investing any money in the custody of any officer or officers of the state unless prohibited by statute to be invested.” Participants in the SPIF include the general fund of the State and any department or agency of the State which is required by court order, contract, state or federal law or federal regulation to receive interest on invested funds and which are authorized by the State Treasurer to participate in the SPIF. In addition, funds in the State of Tennessee Local Government Investment Pool (LGIP) are consolidated with the SPIF for investment purposes only. The SPIF, as noted in A.4 above, is not registered as an investment company with the SEC. The primary oversight responsibility for the investment and operations of the SPIF rests with the Funding Board.

Investment in the SPIF by local governments and certain state agencies is optional and participants may invest any amount for any length of time in the SPIF. However, some deposits made to the LGIP are contractually required and committed to the State Department of Transportation (DOT). The only withdrawals allowed from these accounts are to pay the DOT in accordance with progress billings for construction projects contracted between the entity and the DOT.

An average rate of return is calculated on the investments made each month in the SPIF and is used to credit earnings to LGIP participants and the State departments and agencies required to earn interest. The State’s general fund is credited with the residual earnings. Accordingly, participants’ shares are sold and redeemed at a value equal to the amount of the principal plus accrued earnings while investments are reported at amortized cost. For the fiscal years ending June 30, 2008 and June 30, 2007, an administrative fee of .05 percent was charged against each participant’s average daily balance to provide funding for administrative expenses to operate the SPIF.

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**TENNESSEE CONSOLIDATED RETIREMENT SYSTEM  
INDEPENDENT AUDITOR'S REPORT**


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**STATE OF TENNESSEE  
COMPTROLLER OF THE TREASURY  
DEPARTMENT OF AUDIT  
DIVISION OF STATE AUDIT**

SUITE 1500  
JAMES K. POLK STATE OFFICE BUILDING  
NASHVILLE, TENNESSEE 37243-0264  
PHONE (615) 401-7897  
FAX (615) 532-2765

December 3, 2008

Members of the General Assembly  
and  
Members of the Board of Trustees  
Tennessee Consolidated Retirement System  
and  
The Honorable Dale Sims, Treasurer  
State Capitol  
Nashville, Tennessee 37243

Ladies and Gentlemen:

We have audited the accompanying statements of plan net assets of the Tennessee Consolidated Retirement System as of June 30, 2008, and June 30, 2007, and the related statements of changes in plan net assets for the years then ended. These financial statements are the responsibility of the Tennessee Consolidated Retirement System's management. Our responsibility is to express an opinion on these financial statements, based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion. Tennessee statutes, in addition to audit responsibilities, entrust certain other responsibilities to the Comptroller of the Treasury. Those responsibilities include serving as a member of the board of trustees of the Tennessee Consolidated Retirement System.

As discussed in Note A.1., the financial statements present only the Tennessee Consolidated Retirement System, pension trust funds of the State of Tennessee, and do not purport to, and do not, present fairly the financial position of the State of Tennessee as of June 30, 2008, and June 30, 2007, and the changes in its financial position for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to above present fairly, in all material respects, the plan net assets of the Tennessee Consolidated Retirement System as of June 30, 2008, and June 30, 2007, and the changes in its plan net assets for the years then ended in conformity with accounting principles generally accepted in the United States of America.

The management's discussion and analysis and the schedules of funding progress and employer contributions on pages 111 through 115 and 130 through 131 are not required parts of the basic financial statements but are supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary

*(continued)*

**TENNESSEE CONSOLIDATED RETIREMENT SYSTEM  
INDEPENDENT AUDITOR'S REPORT**

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December 3, 2008

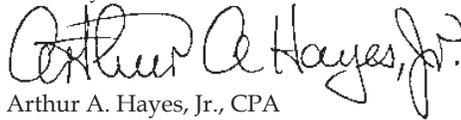
Page 2

information. However, we did not audit the information and express no opinion on it.

Our audits were conducted for the purpose of forming an opinion on the basic financial statements. The actuarial balance sheet on page 132 is presented for purposes of additional analysis and is not a required part of the basic financial statements. Such information has not been subjected to the auditing procedures applied in the audit of the basic financial statements and, accordingly, we express no opinion on it.

In accordance with generally accepted government auditing standards, we have also issued our report dated December 3, 2008, on our consideration of the Tennessee Consolidated Retirement System's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, and contracts and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with generally accepted government auditing standards and should be read in conjunction with this report in considering the results of our audit.

Sincerely,



Arthur A. Hayes, Jr., CPA  
Director

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**TENNESSEE CONSOLIDATED RETIREMENT SYSTEM  
MANAGEMENT'S DISCUSSION AND ANALYSIS  
FOR THE YEARS ENDED JUNE 30, 2008 AND JUNE 30, 2007**

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The Management of the Tennessee Consolidated Retirement System (TCRS) provides this discussion and analysis as an overview of the TCRS' financial activities for the fiscal years ended June 30, 2008 and June 30, 2007. This section should be read in conjunction with the Independent Auditor's Report, the audited financial statements, and the accompanying notes.

### FINANCIAL HIGHLIGHTS

- The plan net assets (total assets minus total liabilities) of the TCRS at June 30, 2008 were \$31.6 billion, decreasing over \$731.8 million (2.3 percent) from the plan net assets at June 30, 2007. The net assets are held in trust to meet future benefit obligations.
- The TCRS relies upon contributions from employees and employers, along with investment income, to meet the funding requirements of an actuarially determined accrued liability. As of July 1, 2007, the date of the latest actuarial valuation, the TCRS' funded ratio was 96.2 percent for the SETHEEPP group and 89.4 percent for the PSPP group.
- Contribution revenue for fiscal year 2008 totaled \$1,084,112,872 an increase of 5.5 percent compared to fiscal year 2007.
- Net investment income for fiscal year 2008 was \$(430,058,924). During fiscal year 2008, the TCRS received an investment return on its portfolio of (1.21) percent, compared to 13.1 percent for fiscal year 2007.
- Total benefits and refunds paid for fiscal year 2008 were \$1,378,691,525 – an increase of 8.8 percent over fiscal year 2007 total benefits and refunds paid of \$1,266,775,568.
- Total administrative expenses for fiscal year 2008 were \$7,201,911 – an increase of 11.3 percent over fiscal year 2007 administrative expenses of \$6,468,558.

### OVERVIEW OF THE FINANCIAL STATEMENTS

The TCRS financial statements consist of the Statement of Plan Net Assets (on pages 116 through 117), the Statement of Changes in Plan Net Assets (on pages 118 through 119), and the Notes to the Financial Statements (on pages 120 through 129). In addition, Required Supplementary Information is presented, which includes this Management's Discussion and Analysis, as well as the schedules on pages 130 through 131.

The Statement of Plan Net Assets and the Statement of Changes in Plan Net Assets report information about the plan net assets (total assets in excess of total liabilities) as of the end of the fiscal year and the changes in those plan net assets during the fiscal year. These statements include all assets and liabilities using the accrual basis of accounting. Under the accrual basis of accounting, the current year's revenues and expenses are included in the financial activity, regardless of when cash is received or paid. The difference between the total assets and total liabilities on the Statement of Plan Net Assets, or net assets held in trust for pension benefits, provides a measurement of the financial position of the TCRS as of the end of the fiscal year. The Statement of Changes in Plan Net Assets provides information on the activities that caused the financial position to change during the fiscal year. Over time, increases or decreases in the plan net assets of the TCRS are one indicator of whether the system's financial health is improving or deteriorating.

In addition to the two basic financial statements, the reader should also review the Schedules of Funding Progress and the Schedules of Employer Contributions to gain an understanding of the funded status of the TCRS over time. This information provides an indication of the TCRS' ability to meet both current and future benefit payment obligations. The Notes to the Financial Statements are also important to the reader's understanding of the financial statements and provide additional information regarding the TCRS, such as descriptions of the plans administered by the TCRS, including contribution and benefit provisions, and information about the accounting policies and investment activities.

*(continued)*

**TENNESSEE CONSOLIDATED RETIREMENT SYSTEM  
MANAGEMENT'S DISCUSSION AND ANALYSIS  
FOR THE YEARS ENDED JUNE 30, 2008 AND JUNE 30, 2007**

**ANALYSIS OF ASSETS, LIABILITIES AND PLAN NET ASSETS**

At June 30, 2008, the TCRS had plan net assets (total assets in excess of total liabilities) of \$31.6 billion, a decrease of over \$731.8 million (2.3 percent) from \$32.4 billion at June 30, 2007. The assets of the TCRS consist primarily of investments. The decrease in plan net assets is primarily the result of negative investment income caused by unfavorable equity market conditions. Condensed financial information comparing the TCRS' plan net assets for the past three fiscal years follows.

**PLAN NET ASSETS**

	June 30, 2008	June 30, 2007	FY08 - FY07 Percentage Change	June 30, 2006	FY07 - FY06 Percentage Change
<b>ASSETS</b>					
Cash and cash equivalents	\$ 358,321,692	\$ 569,035,627	(37.0)%	\$ 826,611,111	(31.2)%
Member and employer receivables	86,041,851	86,352,774	(0.4)%	71,671,617	20.5%
Investment income receivables	159,667,086	169,973,211	(6.1)%	172,541,678	(1.5)%
Investments sold	62,828,189	16,256,391	286.5%	33,287,736	(51.2)%
Foreign currency receivable	153,933,265	5,796,800	2,555.5%	19,732,929	(70.6)%
Short-term securities	49,997,750	527,594,750	(90.5)%	503,846,988	4.7%
Long-term investments	31,015,208,805	31,014,634,498	0.0%	27,255,904,731	13.8%
<b>TOTAL ASSETS</b>	<u>31,885,998,638</u>	<u>32,389,644,051</u>	(1.6)%	<u>28,883,596,790</u>	12.1%
<b>LIABILITIES</b>					
Death benefits, refunds and other payables	1,591,252	\$2,750,418	(42.1)%	2,319,549	18.6%
Investments purchased	85,807,691	10,520,944	715.6 %	38,344,946	(72.6)%
Other investment payables	9,367,826	4,606,919	103.3%	2,563,959	79.7%
Foreign currency payable	155,102,387	5,796,800	2,575.7%	19,732,929	(70.6)%
<b>TOTAL LIABILITIES</b>	<u>251,869,156</u>	<u>23,675,081</u>	963.9%	<u>62,961,383</u>	(62.4)%
<b>NET ASSETS HELD IN TRUST FOR PENSION BENEFITS</b>	<u>\$ 31,634,129,482</u>	<u>\$ 32,365,968,970</u>	(2.3)%	<u>\$28,820,635,407</u>	12.3%

**ANALYSIS OF REVENUES AND EXPENSES**

While contributions to TCRS for fiscal year 2008 increased by \$57 million (5.5 percent) over contributions for fiscal year 2007, a significant decrease in investment income resulted in an overall decline in revenues for 2008 of 86.4 percent compared to revenues for fiscal year 2007. Although employer contribution rates did not change during fiscal year 2008, the increase in contributions can be attributed to new employers joining TCRS and increased salaries. Market conditions resulted in an overall loss to the TCRS investment portfolio of 1.2 percent and negative investment income of \$430.1 million.

Total benefits and refunds paid during the year ended June 30, 2008 were \$1,378,691,525 an increase of 8.8 percent over fiscal year 2007 total benefits and refunds paid. Total benefits and refunds paid during the year ended June 30, 2007 were \$1,266,775,568 an increase of 9.3 percent over fiscal year 2006 total benefits and refunds paid. The increase in benefit expenses can be attributed to 3.0 percent in cost of living adjustments awarded to retirees on both July 1, 2007 and July 1, 2006 respectively. In addition, more retirees were added to payroll than removed during these fiscal years.

(continued)

**TENNESSEE CONSOLIDATED RETIREMENT SYSTEM  
MANAGEMENT'S DISCUSSION AND ANALYSIS  
FOR THE YEARS ENDED JUNE 30, 2008 AND JUNE 30, 2007**

In addition, administrative expenses for the year ended June 30, 2008 were \$7,201,911, an increase of 11.3 percent over fiscal year 2007 administrative expenses. This increase was primarily due to the additional expense of the biennial actuarial study performed in fiscal year 2008. Administrative expenses for the year ended June 30, 2007 were \$6,468,558, an increase of 4.1 percent over fiscal year 2006 administrative expenses.

Condensed financial information comparing the TCRS' revenues and expenses for the past three fiscal years follows.

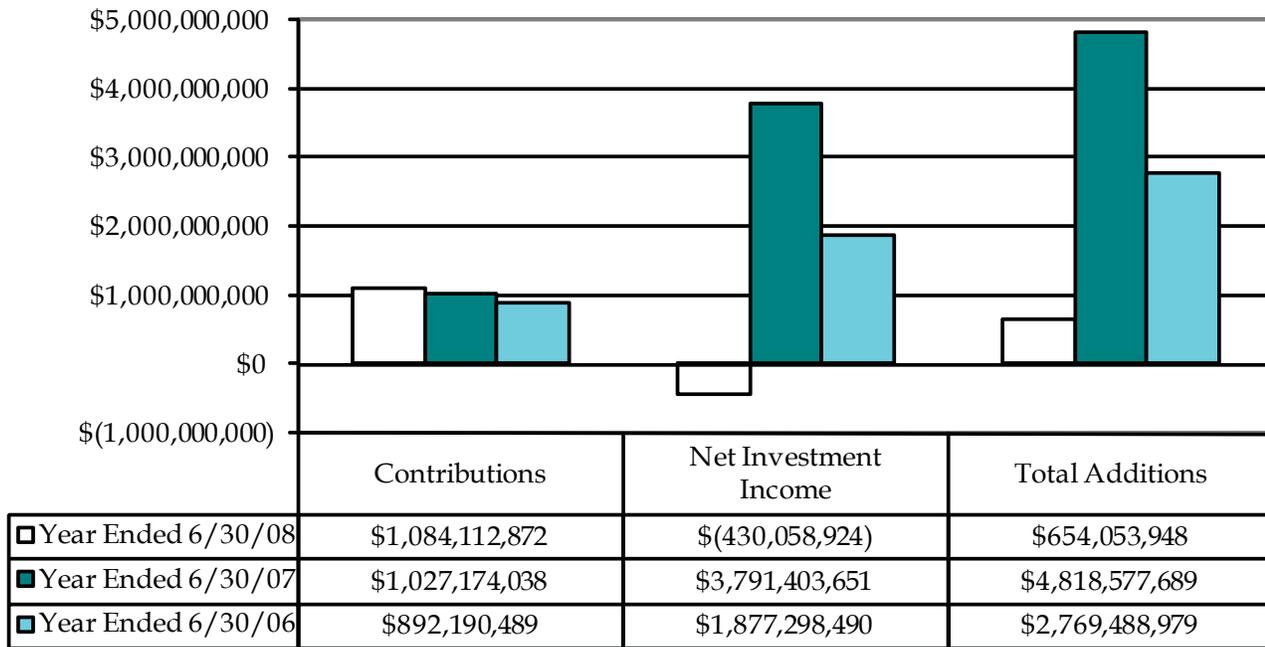
**CHANGES IN PLAN NET ASSETS**

	For the Year Ended June 30, 2008	For the Year Ended June 30, 2007	FY08 - FY07 Percentage Change	For the Year Ended June 30, 2006	FY07 - FY06 Percentage Change
<b>ADDITIONS</b>					
Contributions	<u>\$1,084,112,872</u>	<u>\$1,027,174,038</u>	5.5 %	<u>\$892,190,489</u>	15.1%
Investment income					
Net appreciation (depreciation) in fair value of investments	(1,574,090,230)	2,717,644,583	(157.9)%	893,530,576	204.1%
Interest, dividends and other investment income	1,168,574,283	1,097,511,473	6.5%	1,002,725,069	9.5%
Less: Investment expense	<u>(24,542,977)</u>	<u>(23,752,405)</u>	3.3 %	<u>(18,957,155)</u>	25.3%
Net investment income	<u>(430,058,924)</u>	<u>3,791,403,651</u>	(111.3)%	<u>1,877,298,490</u>	102.0%
<b>TOTAL ADDITIONS</b>	<u>654,053,948</u>	<u>4,818,577,689</u>	(86.4)%	<u>2,769,488,979</u>	74.0%
<b>DEDUCTIONS</b>					
Annuity benefits					
Retirement benefits	993,293,429	918,540,446	8.1 %	843,183,130	8.9 %
Survivor benefits	62,811,272	58,202,209	7.9 %	53,991,908	7.8 %
Disability benefits	28,128,249	26,722,134	5.3 %	25,808,859	3.5%
Cost of living	243,575,211	221,463,825	10.0 %	195,538,793	13.3%
Death benefits	4,907,479	5,502,982	(10.8)%	5,668,204	(2.9)%
Refunds	45,975,885	36,343,972	26.5%	34,710,966	4.7%
Administrative expenses	<u>7,201,911</u>	<u>6,468,558</u>	11.3 %	<u>6,213,597</u>	4.1%
<b>TOTAL DEDUCTIONS</b>	<u>1,385,893,436</u>	<u>1,273,244,126</u>	8.8 %	<u>1,165,115,457</u>	9.3%
<b>NET INCREASE (DECREASE)</b>	(731,839,488)	3,545,333,563	(120.6)%	1,604,373,522	121.0%
<b>NET ASSETS HELD IN TRUST FOR PENSION BENEFITS</b>					
BEGINNING OF YEAR	<u>32,365,968,970</u>	<u>28,820,635,407</u>	12.3 %	<u>27,216,261,885</u>	5.9%
END OF YEAR	<u>\$31,634,129,482</u>	<u>\$32,365,968,970</u>	(2.3)%	<u>\$28,820,635,407</u>	12.3%

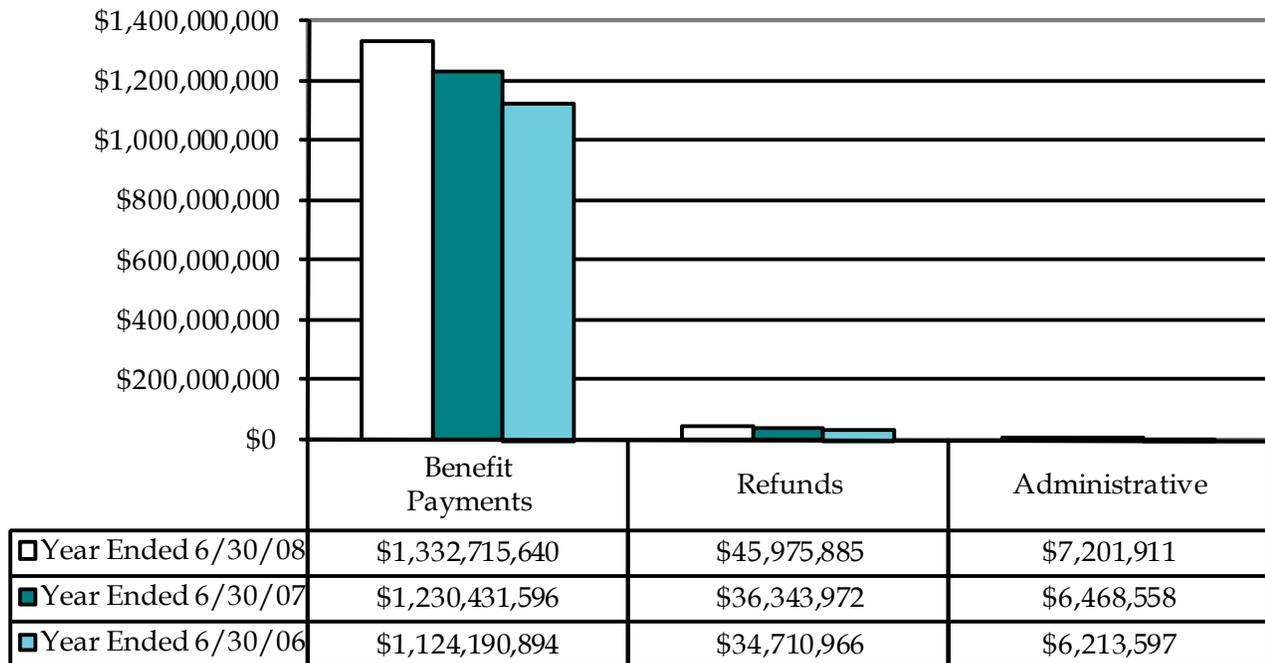
(continued)

**TENNESSEE CONSOLIDATED RETIREMENT SYSTEM  
MANAGEMENT'S DISCUSSION AND ANALYSIS  
FOR THE YEARS ENDED JUNE 30, 2008 AND JUNE 30, 2007**

**REVENUES BY TYPE**



**EXPENSES BY TYPE**



(continued)

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**TENNESSEE CONSOLIDATED RETIREMENT SYSTEM  
MANAGEMENT'S DISCUSSION AND ANALYSIS  
FOR THE YEARS ENDED JUNE 30, 2008 AND JUNE 30, 2007**

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**ECONOMIC FACTORS, FUTURE FUNDING PROVISIONS, OVERALL OUTLOOK**

For the year ended June 30, 2008, the domestic portfolios weakened considerably with a loss of 11.93% following a strong 20.58% return the prior fiscal year. The S&P 1500 index, TCRS' domestic equity benchmark, reported a loss of 12.72% for the fiscal year ended June 30, 2008. Likewise, the international stock portfolios followed a 27.19% return for the year ended June 30, 2007 with a negative return of 6.38% for 2008. The international equity market, as represented by the EAFE index, reported growth of 27% in fiscal year 2007 contrasting with a 10.61% loss in the fiscal year ended June 30, 2008. The domestic bond market, as measured by the Citigroup Broad Investment Grade index, had a positive return of 6.06% for the year ended June 30, 2007, followed by 7.78% return for the 2008 fiscal year. The domestic fixed income portfolio earned 6.17% and 5.98% respectively. Fixed income relative performance began to suffer in the 2008 fiscal year due to the poor performance of asset backed securities. The real estate portfolio earned 12.53% for the year ended June 30, 2008 as compared to the NCREIF index benchmark of 13.58%.

The initial stages of broad equity and fixed income market weakness began during the 2008 fiscal year. The outlook for domestic and international markets is unsettled at best.

The employer contribution rates changed on July 1, 2008 for most of the employers participating in TCRS. The contribution levels did not change significantly because of the overall positive experience of the plan.

**CONTACTING THE TCRS**

This report is designed to provide a financial overview of the TCRS to state legislators, members of the Board of Trustees of the TCRS, state officials, participating employers and any other interested parties. Questions or requests for additional information regarding the financial information presented in this report may be addressed in writing to the Tennessee Treasury Department, Consolidated Retirement System, 10th Floor Andrew Jackson Building, Nashville, TN 37243-0230.

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**TENNESSEE CONSOLIDATED RETIREMENT SYSTEM**  
**COMPARATIVE STATEMENTS OF PLAN NET ASSETS**  
**AS OF JUNE 30, 2008 AND JUNE 30, 2007**


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Expressed in thousands

	<b>State Employees, Teachers, Higher Education Employees Pension Plan (SETHEPP)</b>	<b>Political Subdivisions Pension Plan (PSPP)</b>
<b>ASSETS</b>		
Cash and cash equivalents	\$ 300,422	\$ 57,899
Receivables		
Member receivable	20,835	4,794
Employer receivable	41,864	18,549
Accrued interest receivable	104,184	20,079
Accrued dividends receivable	28,482	5,489
Real estate income receivable	1,202	232
Foreign currency receivable	129,060	24,873
Investments sold	52,676	10,152
Total receivables	<u>378,303</u>	<u>84,168</u>
Investments, at fair value		
Short-term securities	41,919	8,079
Government securities	6,225,179	1,199,756
Corporate securities	5,512,517	1,062,408
Corporate stocks	13,150,692	2,534,486
Real estate	1,115,236	214,935
Total investments	<u>26,045,543</u>	<u>5,019,664</u>
<b>TOTAL ASSETS</b>	<u>26,724,268</u>	<u>5,161,731</u>
<b>LIABILITIES</b>		
Accounts payable		
Death benefits and refunds payable	1,195	212
Other	52	133
Investments purchased	71,943	13,865
Foreign currency payable	130,040	25,062
Other investment payables	7,854	1,514
<b>TOTAL LIABILITIES</b>	<u>211,084</u>	<u>40,786</u>
<b>NET ASSETS HELD IN TRUST FOR PENSION BENEFITS</b>	<u>\$ 26,513,184</u>	<u>\$ 5,120,945</u>

See accompanying Notes to the Financial Statements

(continued)

(CONTINUED)

June 30, 2008 Total	State Employees, Teachers, Higher Education Employees Pension Plan (SETHEPP)	Political Subdivisions Pension Plan (PSPP)	For the Year Ended June 30, 2007 Total
\$ 358,321	\$ 479,656	\$ 89,379	\$ 569,035
25,629	20,405	5,023	25,428
60,413	40,814	20,111	60,925
124,263	122,665	22,857	145,522
33,971	19,480	3,630	23,110
1,434	1,131	211	1,342
153,933	4,886	910	5,796
62,828	13,703	2,553	16,256
<u>462,471</u>	<u>223,084</u>	<u>55,295</u>	<u>278,379</u>
49,998	444,725	82,870	527,595
7,424,935	7,643,081	1,424,212	9,067,293
6,574,925	4,476,732	834,194	5,310,926
15,685,178	13,110,008	2,442,920	15,552,928
1,330,171	913,303	170,185	1,083,488
<u>31,065,207</u>	<u>26,587,849</u>	<u>4,954,381</u>	<u>31,542,230</u>
<u>31,885,999</u>	<u>27,290,589</u>	<u>5,099,055</u>	<u>32,389,644</u>
1,407	1,396	1,063	2,459
185	291	0	291
85,808	8,869	1,653	10,522
155,102	4,886	910	5,796
9,368	3,883	724	4,607
<u>251,870</u>	<u>19,325</u>	<u>4,350</u>	<u>23,675</u>
<u>\$ 31,634,129</u>	<u>\$ 27,271,264</u>	<u>\$ 5,094,705</u>	<u>\$ 32,365,969</u>

**TENNESSEE CONSOLIDATED RETIREMENT SYSTEM  
COMPARATIVE STATEMENTS OF CHANGES IN PLAN NET ASSETS  
FOR THE YEARS ENDED JUNE 30, 2008 AND JUNE 30, 2007**

*Expressed in Thousands*

	<b>State Employees, Teachers, Higher Education Employees Pension Plan (SETHEPP)</b>	<b>Political Subdivisions Pension Plan</b>
<b>ADDITIONS</b>		
Contributions		
Member contributions	\$ 181,236	\$ 64,617
Employer contributions	593,412	244,847
Total contributions	<u>774,648</u>	<u>309,464</u>
Investment income		
Net appreciation (depreciation) in fair value of investments	(1,322,815)	(251,275)
Interest	631,028	119,867
Dividends	297,009	56,418
Real estate income, net of operating expenses	53,995	10,257
Total investment income	<u>(340,783)</u>	<u>(64,733)</u>
Less: Investment expense	<u>(20,625)</u>	<u>(3,918)</u>
Net investment income	<u>(361,408)</u>	<u>(68,651)</u>
<b>TOTAL ADDITIONS</b>	<u>413,240</u>	<u>240,813</u>
<b>DEDUCTIONS</b>		
Annuity benefits		
Retirement benefits	851,426	141,867
Survivor benefits	53,840	8,971
Disability benefits	24,111	4,017
Cost of living	215,810	27,765
Death benefits	3,309	1,599
Refunds	19,113	26,863
Administrative expense	3,711	3,491
<b>TOTAL DEDUCTIONS</b>	<u>1,171,320</u>	<u>214,573</u>
<b>NET INCREASE</b>	(758,080)	26,240
<b>NET ASSETS HELD IN TRUST FOR PENSION BENEFITS</b>		
<b>BEGINNING OF YEAR</b>	27,271,264	5,094,705
<b>END OF YEAR</b>	<u>\$ 26,513,184</u>	<u>\$ 5,120,945</u>

*See accompanying Notes to the Financial Statements*

*(continued)*

(CONTINUED)

For the Year Ended June 30, 2008 TOTAL	State Employees, Teachers, Higher Education Employees Pension Plan (SETHEPP)	Political Subdivisions Pension Plan (PSPP)	For the Year Ended June 30, 2007 TOTAL
\$ 245,853	\$ 175,743	\$ 57,003	\$ 232,746
838,259	562,729	231,699	794,428
<u>1,084,112</u>	<u>738,472</u>	<u>288,702</u>	<u>1,027,174</u>
(1,574,090)	2,295,671	421,974	2,717,645
750,895	618,197	113,632	731,829
353,427	258,925	47,594	306,519
64,252	49,977	9,186	59,163
<u>(405,516)</u>	<u>3,222,770</u>	<u>592,386</u>	<u>3,815,156</u>
(24,543)	(20,064)	(3,688)	(23,752)
<u>(430,059)</u>	<u>3,202,706</u>	<u>588,698</u>	<u>3,791,404</u>
<u>654,053</u>	<u>3,941,178</u>	<u>877,400</u>	<u>4,818,578</u>
993,293	789,603	128,937	918,540
62,811	50,032	8,170	58,202
28,128	22,971	3,751	26,722
243,575	196,439	25,025	221,464
4,908	3,719	1,784	5,503
45,976	19,231	17,113	36,344
7,202	3,385	3,084	6,469
<u>1,385,893</u>	<u>1,085,380</u>	<u>187,864</u>	<u>1,273,244</u>
(731,840)	2,855,798	689,536	3,545,334
32,365,969	24,415,466	4,405,169	28,820,635
<u>\$ 31,634,129</u>	<u>\$ 27,271,264</u>	<u>\$ 5,094,705</u>	<u>\$ 32,365,969</u>

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**TENNESSEE CONSOLIDATED RETIREMENT SYSTEM**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**JUNE 30, 2008 AND JUNE 30, 2007**

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The Tennessee Consolidated Retirement System (TCRS) administers two defined benefit pension plans - State Employees, Teachers and Higher Education Employees Pension Plan (SETHEEPP) and Political Subdivisions Pension Plan (PSPP). Although the assets of the plans are commingled for investment purposes, each plan's assets may be used only for the payment of benefits to members of that plan, in accordance with the terms of the plan.

**A. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

1. **Reporting Entity** - The TCRS is included in the State of Tennessee Financial Reporting Entity. Because of the state's fiduciary responsibility, the TCRS has been included as pension trust funds in the *Tennessee Comprehensive Annual Financial Report*.
2. **Measurement Focus and Basis of Accounting** - The accompanying financial statements have been prepared in conformity with generally accepted accounting principles as prescribed by the Governmental Accounting Standards Board (GASB). The financial statements have been prepared using the flow of economic resources measurement focus and the accrual basis of accounting. Under this method, revenues are recorded when earned and expenses are recorded at the time liabilities are incurred.  
  
Plan member contributions are recognized in the period of time for which the contributions are assessed. Plan employer contributions are recognized when due and the employer has made a formal commitment to provide the contributions. Benefits and refunds are recognized when due and payable in accordance with the terms of each plan.
3. **Cash and Cash Equivalents** - Cash and cash equivalents by definition, includes cash and short-term investments with a maturity date within three months of the acquisition date. The state's accounting policy regarding the definition of cash and cash equivalents includes cash management pools as cash. Cash received by the TCRS that cannot be invested immediately in securities, or that is needed for operations, is invested in the State Pooled Investment Fund sponsored by the State of Tennessee and administered by the State Treasurer. The classification of cash and cash equivalents also includes cash invested in a short-term, open-end mutual fund under the contractual arrangement for master custody services.
4. **Method Used to Value Investments** - Investments are reported at fair value. Securities traded on a national or international exchange are valued at the last reported sales price at current exchange rates. The fair value of real estate investments is determined at least every three years by qualified independent appraisers who are members of the Appraisal Institute and internally by real estate advisors for those years when independent appraisals are not performed. Investment income includes realized and unrealized appreciation (depreciation) in the fair value of investments. Interest income is recognized when earned. Securities and securities transactions are recorded in the financial statements on trade-date basis. Real estate transactions are recorded in the financial statements at the time of closing.
5. **Reclassification** - The fair value of collateralized mortgage obligations at June 30, 2007 which was originally reported in Note C as \$141,501,440 has been reclassified to \$1,665,827,439 due to securities previously classified as mortgage-backed securities being more accurately classified as CMOs.

(continued)

**TENNESSEE CONSOLIDATED RETIREMENT SYSTEM  
NOTES TO THE FINANCIAL STATEMENTS  
JUNE 30, 2008 AND JUNE 30, 2007**

**B. PLAN DESCRIPTIONS AND CONTRIBUTION INFORMATION**

At July 1, 2007, the date of the latest actuarial valuation, the membership of each plan consisted of the following:

	<b>SETHEEPP</b>	<b>PSPP</b>
Retirees and beneficiaries currently receiving benefits	70,598	27,632
Terminated members entitled to but not receiving benefits	21,032	9,732
Current active members	<u>136,329</u>	<u>76,396</u>
Total	227,959	113,760
Number of participating employers	140	488

**State Employees, Teachers and Higher Education Employees Pension Plan**

*Plan Description* - SETHEEPP is a cost-sharing, multiple employer defined benefit pension plan that covers the employees of the state, teachers with Local Education Agencies (LEA's) and higher education employees. The TCRS provides retirement benefits as well as death and disability benefits to plan members and their beneficiaries. Benefits are determined by a formula using the member's high five-year average salary and years of service. Members become eligible to retire at the age of 60 with five years of service or at any age with 30 years of service. A reduced retirement benefit is available to vested members who are at least 55 years of age or have 25 years of service. Disability benefits are available to active members with five years of service who become disabled and cannot engage in gainful employment. There is no service requirement for disability that is the result of an accident or injury occurring while the member was in the performance of duty. Members joining the plan on or after July 1, 1979 are vested after five years of service. Members joining prior to July 1, 1979 are vested after four years of service. Compounded cost of living adjustments (COLA) are provided each July based on the percentage change in the Consumer Price Index (CPI) during the previous calendar year except that (a) no COLA is granted if the CPI is less than one-half percent; (b) a COLA of 1 percent will be granted if the CPI increases between one-half percent and one percent; (c) the maximum annual COLA is capped at three percent. Benefit provisions are established by state statute found in Title Eight, Chapters 34 through 37 of the *Tennessee Code Annotated*. State statutes are amended by the Tennessee General Assembly. Ad hoc increases may only be authorized by the General Assembly. Public safety officers receive an additional supplemental benefit that is paid from age 60 to age 62.

*Superseded Systems and Certain Employment Classifications* - Members of superseded systems that became members of the TCRS at consolidation in 1972, have their rights preserved to the benefits of the superseded system, if the benefit from the superseded plan exceeds that provided by the Group 1 (teachers and general employees) TCRS formula. Likewise, public safety employees and officials of TCRS Groups 2, 3 and 4 are entitled to the benefits of those formulas, if better than the Group 1 benefits.

*Contributions and Reserves* - Effective July 1, 1981, the plan became noncontributory for most state and higher education employees. The contribution rate for teachers is five percent of gross salary. The employers contribute a set percentage of their payrolls, determined by an actuarial valuation. *Tennessee Code Annotated* Title Eight, Chapter 37 provides that the contribution rates be established and may be amended by the Board of Trustees of the TCRS. The administrative budget for the plan is approved through the state of Tennessee's annual budget process. Funding for the administrative budget is included in employer contributions.

The net assets of the plan are legally required to be reserved in two accounts, the Member Reserve and the Employer Reserve. The Member Reserve represents the accumulation of employee contributions plus interest. The Employer Reserve represents the accumulation of employer contributions, investment income and transfers from the Member Reserve for retiring members. Benefit payments and interest credited

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**TENNESSEE CONSOLIDATED RETIREMENT SYSTEM**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**JUNE 30, 2008 AND JUNE 30, 2007**

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to the members' accounts are reductions to the Employer Reserve. At June 30, 2008, the plan's Member Reserve and Employer Reserve were fully funded with balances of \$3,495.6 million and \$23,017.6 million, respectively. At June 30, 2007, the plan's Member Reserve and Employer Reserve were fully funded with balances of \$3,386.5 million and \$23,884.7 million, respectively.

**Political Subdivisions Pension Plan**

*Plan Description* - PSPP is an agent multiple-employer defined benefit pension plan that covers the employees of participating political subdivisions of the state of Tennessee. Employee class differentiations are not made under PSPP. The TCRS provides retirement benefits as well as death and disability benefits to plan members and their beneficiaries. Benefits are determined by a formula using the member's high five-year average salary and years of service. Members become eligible to retire at the age of 60 with five years of service or at any age with 30 years of service. A reduced retirement benefit is available to vested members who are at least 55 years of age or have 25 years of service. Disability benefits are available to active members with five years of service who become disabled and cannot engage in gainful employment. There is no service requirement for disability that is the result of an accident or injury occurring while the member was in the performance of duty. Members joining the plan prior to July 1, 1979 are vested after four years of service. Members joining on or after July 1, 1979 are vested upon completion of 10 years of service, unless five years vesting is authorized by resolution of the chief governing body. Cost of living adjustments (COLA) are the same as provided by SETHEPP except that the local government may elect (a) to provide no COLA benefits or (b) to provide COLA benefits under a non-compounding basis rather than the compounded basis applicable under SETHEPP. Benefit provisions are established and amended by state statute. Pursuant to Article Two, Section 24 of the *Constitution of the State of Tennessee*, the state cannot mandate costs on local governments. Any benefit improvement may be adopted by the governing body of a governmental entity participating in the TCRS.

*Contributions and Reserves* - Political subdivisions may elect contributory or noncontributory retirement for their employees. The contribution rate for contributory employees of political subdivisions is five percent of gross salary. The employers contribute a set percentage of their payrolls, equal to at least, the percentage determined by an actuarial valuation. State statute provides that the contribution rates be established and may be amended by the Board of Trustees of the TCRS. The administrative budget for the plan is approved through the state's annual budget process. Funding for the administrative budget is included in employer contributions.

The net assets of the plan are legally required to be reserved in two accounts, the Member Reserve and the Employer Reserve. The Member Reserve represents the accumulation of employee contributions plus interest. The Employer Reserve represents the accumulation of employer contributions, investment income and transfers from the Member Reserve for retiring members. Benefit payments and interest credited to the members' accounts are reductions to the Employer Reserve. At June 30, 2008, the plan's Member Reserve and Employer Reserve were fully funded with balances of \$951.5 million and \$4,169.5 million, respectively. At June 30, 2007, the plan's Member Reserve and Employer Reserve were fully funded with balances of \$896.1 million and \$4,198.6 million, respectively.

**C. DEPOSITS AND INVESTMENTS**

State statute authorizes the TCRS to maintain cash, not exceeding ten percent of the total amount of funds in the retirement system, on deposit in one or more banks, savings and loan associations or trust companies that are qualified as state depositories. The TCRS does not utilize its own bank accounts but invests in the State Pooled Investment Fund for the initial deposit of funds and for its operating cash needs. The State Pooled Investment Fund is authorized by state statute to invest funds in accordance with policy guidelines approved by the Funding Board of the State of Tennessee. The current resolution

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**TENNESSEE CONSOLIDATED RETIREMENT SYSTEM**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**JUNE 30, 2008 AND JUNE 30, 2007**

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of that board gives the Treasurer authority to invest in collateralized certificates of deposit in authorized state depositories, prime commercial paper, prime bankers' acceptances, certain repurchase agreements and various U.S. Treasury and Agency obligations. The State Pooled Investment Fund is also authorized to enter into securities lending agreements in which U.S. Government Securities may be loaned for a fee. The loaned securities are transferred to the borrower by the custodial agent upon simultaneous receipt of collateral securities.

State statute also authorizes the TCRS to invest in bonds, debentures, preferred stock and common stock, real estate and in other good and solvent securities subject to the approval of the Board of Trustees, but further subject to the following statutory restrictions and provisions:

- a. The total sum invested in common and preferred stocks shall not exceed seventy-five percent (75 percent) of the total of the funds of the retirement system.
- b. The total sum invested in notes and bonds or other fixed income securities exceeding one year in maturity shall not exceed seventy-five percent (75 percent) of the total funds of the retirement system.
- c. Within the restrictions in (a) and (b) above, an amount not to exceed fifteen percent (15 percent) of the total of the funds of the retirement system may be invested in securities of the same kinds, classes, and investment grades as those otherwise eligible for investment in various approved foreign countries, provided that such percentage may be increased by the board with the subsequent approval of the council on pensions and insurance.
- d. Within the restrictions in (a) and (b) above, funds may be invested in Canadian securities which are substantially of the same kinds, classes and investment grades as those otherwise eligible for investment.
- e. The total amount of securities loaned under a securities lending program cannot exceed thirty percent (30 percent) of total assets.
- f. The total sum invested in real estate shall not exceed five percent (5 percent) of the market value of total assets.

State statute also authorizes the TCRS to invest in forward contracts to hedge its foreign currency exposure and to purchase or sell domestic equity index futures contracts for the purpose of asset allocation relating to the domestic equity portfolio. The total amount of the financial futures contract obligation shall not exceed five percent (5 percent) of the market value of total assets.

Changes were made to the statute relative to the investment guidelines for the TCRS during the 2008 legislative session. These changes include increasing the allowable real estate allocation from five percent (5 percent) to ten percent (10 percent) and allowing investment in private equities not to exceed five percent (5 percent) of the market value of total assets. The Board of Trustees approved these revisions to the investment policy after June 30, 2008 and therefore, the changes were not in effect at year end.

Title to real property invested in by the TCRS is held by real estate investment holding companies.

*(continued)*

**TENNESSEE CONSOLIDATED RETIREMENT SYSTEM**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**JUNE 30, 2008 AND JUNE 30, 2007**

As of June 30, 2008 and June 30, 2007, the TCRS had the following investments:

**Investments**  
*(Expressed in Thousands)*

Investment Type	Fair Value as of June 30, 2008	U.S. Treasury/ Agency (1)	Credit Quality Ratings							(2)	(3)
			AAA	AA	A	BBB	BB	B	A1		
<b>Debt Investments</b>											
U.S. Govt. Treasuries, Notes, Bonds	\$ 859,779	\$ 859,779									
U.S. Govt. Inflation Indexed	1,617,494	1,617,494									
U.S. Govt. Agencies	489,958		\$ 489,958								
Mortg.-Backed Govt.	3,481,814	463,141									\$ 3,018,673
Corporate CMO's	2,186,147		2,133,824	\$ 33,463							18,860
Corporate Bonds	3,045,230		12,142	220,368	\$ 981,941	\$ 1,767,224	\$ 45,258	\$ 18,297			
Corporate Asset-Backed	1,230,858		1,112,036	62,183	19,641	36,998					
Non-U.S. Govt./Sovereign	975,890	767,765	208,125								
Non-U.S. Corporate	19,614		19,614								
Short-Term Commercial Paper	287,352										287,352
Short-Term Agencies	121,969	121,969									
<b>Total Debt Investments</b>	<b>\$ 14,316,105</b>	<b>\$ 3,830,148</b>	<b>\$ 3,975,699</b>	<b>\$ 316,014</b>	<b>\$ 1,001,582</b>	<b>\$ 1,804,222</b>	<b>\$ 45,258</b>	<b>\$ 18,297</b>	<b>\$ -</b>	<b>\$ 3,324,885</b>	
<b>Other Investments</b>											
U.S. Equity	\$ 10,937,097		(1) Includes obligations of the U.S. government or obligations explicitly guaranteed by the U.S. government and are not considered to have credit risk.								
Non-U.S. Equity	4,841,156										
Real Estate	1,330,171										
<b>Total Other Investments</b>	<b>\$ 17,108,424</b>		(2) A1 is the highest rating category for commercial paper								
<b>Total Investments</b>	<b>\$ 31,424,529</b>										
Less: Short-Term Investments Classified as Cash Equivalents on the Statements of Plan Net Assets	(359,322)		(3) Includes securities that are implicitly guaranteed by the U.S. government, but are not rated by Standard and Poor's or Moody's.								
<b>Total Investments as Shown on Statements of Plan Net Assets</b>	<b>\$ 31,065,207</b>										

Investment Type	Fair Value as of June 30, 2007	U.S. Treasury/ Agency (1)	Credit Quality Ratings							(2)	(3)
			AAA	AA	A	BBB	BB	B	A1		
<b>Debt Investments</b>											
U.S. Govt. Treasuries, Notes, Bonds	\$ 825,413	\$ 825,413									
U.S. Govt. STRIPS	264,838	264,838									
U.S. Govt. TIPS	1,959,797	1,959,797									
U.S. Govt. Agencies	1,252,600		\$ 1,252,600								
Mortg.-Backed Govt. Pass-Through Govt. CMO's	3,923,008	217,693									\$ 3,705,315
Corporate CMO's	117,568		117,568								
Corporate CMO's	1,548,259		1,528,268	\$ 19,991							
Corporate Bonds	2,294,723		49,523	300,677	\$ 818,312	\$ 1,097,950	\$ 9,782	\$ 18,479			
Corporate Asset-Backed	772,069		652,730	20,035	9,019	90,285					
Private Placements	399,024		77,963	108,899	69,798	142,364					
Yankee Bonds	18,369				9,122	9,247					
Supranationals	41,217		41,217								
Non-U.S. Govt./Sovereign	724,069		359,185	100,506	264,378						
Non-U.S. Corporate	237,265		237,265								
Short-Term Commercial Paper	566,543								\$ 566,543		
Short-Term Certificate of Deposit	9,982										
Short-Term Agencies	517,613				9,982						517,613
<b>Total Debt Investments</b>	<b>\$ 15,472,357</b>	<b>\$ 3,267,741</b>	<b>\$ 4,316,319</b>	<b>\$ 560,090</b>	<b>\$ 1,170,629</b>	<b>\$ 1,339,846</b>	<b>\$ 9,782</b>	<b>\$ 18,479</b>	<b>\$ 566,543</b>	<b>\$ 4,222,928</b>	
<b>Other Investments</b>											
U.S. Equity	\$ 10,765,940		(1) Includes obligations of the U.S. government or obligations explicitly guaranteed by the U.S. government and are not considered to have credit risk.								
Non-U.S. Equity	4,786,988										
Real Estate	1,083,488										
Commingled Money Market Funds	9		(2) A1 is the highest rating category for commercial paper								
<b>Total Other Investments</b>	<b>\$ 16,636,425</b>										
<b>Total Investments</b>	<b>\$ 32,108,782</b>		(3) Includes securities that are implicitly guaranteed by the U.S. government, but are not rated by Standard and Poor's or Moody's.								
Less: Short-Term Investments Classified as Cash Equivalents on the Statements of Plan Net Assets	(566,552)										
<b>Total Investments as Shown on Statements of Plan Net Assets</b>	<b>\$ 31,542,230</b>										

(continued)

**TENNESSEE CONSOLIDATED RETIREMENT SYSTEM  
NOTES TO THE FINANCIAL STATEMENTS  
JUNE 30, 2008 AND JUNE 30, 2007**

**Credit Risk** - Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. Credit quality ratings for the TCRS' investments in fixed income securities as of June 30, 2008 and June 30, 2007 are included in the above schedule. Securities are rated using Standard and Poor's and/or Moody's and are presented above using the Standard and Poor's rating scale. The State Pooled Investment Fund has not obtained a credit quality rating from a nationally recognized credit ratings agency.

The TCRS' investment policy specifies that bond issues subject for purchase are investment grade bonds rated in the four highest ratings by one of the recognized rating agencies. In addition, the policy states that private placements that do not have an active secondary market shall be thoroughly researched from a credit standpoint and shall be viewed by TCRS' investment staff as having the credit quality rating equivalent of an AA rating on a publicly traded issue. For short-term investments, the TCRS' investment policy provides for the purchase of only the highest quality debt issues. Commercial paper should be rated in the highest tier by all rating agencies which rate the paper, with a minimum of two ratings required. Commercial paper cannot be purchased if a rating agency has the commercial paper on a negative credit watch. The investment policy also requires preparation of a credit analysis report on the corporation prior to purchasing commercial paper.

As noted above, the TCRS does not utilize its own bank accounts but invests in the State Pooled Investment Fund for its operating cash purposes. Required risk disclosures relative to the State Pooled Investment Fund are presented in the *Tennessee Comprehensive Annual Financial Report*. That report may be obtained by writing to the Tennessee Department of Finance and Administration, Division of Accounts, 14th Floor William R. Snodgrass Tennessee Tower, 312 Rosa Parks Avenue, Nashville, Tennessee 37243-0298.

**Concentration of Credit Risk** - A concentration of investments in any one single issuer of debt securities presents a greater risk for loss in the event that the issuer fails on its obligations. The TCRS had the following investment amounts and percentages of plan net assets, in organizations representing five percent or more of plan net assets, excluding those organizations whose issues are explicitly guaranteed by the United States government, and investments in mutual funds, external investment pools, and other pooled investments:

Issuer Organization	June 30, 2008		June 30, 2007	
	Fair Value	Percentage	Fair Value	Percentage
Federal Home Loan Mortgage Corp.	\$1,373,411,585	4.34%	\$2,043,123,831	6.31%
Federal National Mortgage Assoc.	2,214,699,793	7.00%	2,865,385,846	8.85%

The TCRS' investment policy limits the maximum amount of a specific corporation's commercial paper that can be purchased to \$100 million. There are no specific investment policies that limit investment in any one issuer.

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**TENNESSEE CONSOLIDATED RETIREMENT SYSTEM**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**JUNE 30, 2008 AND JUNE 30, 2007**

**Interest Rate Risk** - Interest rate risk is the risk that future changes in prevailing market rates of interest will have an adverse effect on the fair value of debt investments. The fair values of securities with long terms to maturity may be highly sensitive to interest rate changes. The TCRS' investment policy does not specifically address limits on investment maturities. The fixed income portfolio, however, is benchmarked against the Citigroup Broad Investment Grade Index and tends to have a duration within a range around that index. Duration is a measure of a debt investment's exposure to fair value changes arising from changing interest rates. It uses the present value of cash flows weighted for those cash flows as a percentage of the investment's full price. The TCRS had the following investments and effective duration at June 30, 2008 and June 30, 2007.

**Debt Investments**  
*(Expressed in Thousands)*

Investment Type	Fair Value as of June 30, 2008	Effective Duration (years)
<u>Debt Investments</u>		
Government Agencies	\$ 698,083	4.54
Government Bonds	1,627,544	7.30
Government Inflation Indexed	1,617,494	7.29
Government Mortgage-Backed	3,481,814	4.39
Corporate Collateralized Mortgage Obligations (CMO)	2,186,148	3.94
Corporate Asset Backed Securities	1,230,857	2.94
Corporate Bonds	3,064,844	6.42
Short-Term Commercial Paper	287,352	0.00
Short-Term Agencies	121,969	0.13
Total Debt Investments	\$ 14,316,105	5.17

Investment Type	Fair Value as of June 30, 2007	Effective Duration (years)
<u>Debt Investments</u>		
Government Agencies	\$ 1,256,788	2.87
Government Bonds	1,500,391	8.04
Government STRIPS	264,838	12.77
Government Notes	40,648	0.27
Government Inflation Indexed	1,959,797	3.57
Government State and Local Obligations	4,255	0.19
Government National Mortgage Association (GNMA)	217,693	3.47
Federal Home Loan Mortgage Corporation (FHLMC)	1,390,664	4.69
Federal National Mortgage Association (FNMA)	2,314,651	4.60
Government Collateralized Mortgage Obligations (CMO)	117,568	7.49
Corporate Collateralized Mortgage Obligations (CMO)	1,548,259	5.90
Asset Backed Securities	772,069	3.85
Corporate Bonds	2,586,646	6.13
Private Placements	399,024	7.38
Miscellaneous Other Fixed Income	4,928	6.93
Short-Term Commercial Paper	566,543	0.03
Short-Term Certificate of Deposit	9,982	0.00
Short-Term Agencies	517,613	0.43
Total Debt Investments	\$ 15,472,357	4.99

(continued)

**TENNESSEE CONSOLIDATED RETIREMENT SYSTEM**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**JUNE 30, 2008 AND JUNE 30, 2007**

**Asset-Backed Securities** – The TCRS invests in various collateralized mortgage obligations (CMOs) which are mortgage-backed securities. These securities are based on cash flows from interest and principal payments on underlying mortgages and could therefore be more sensitive to prepayments by mortgagees as a result of a decline in interest rates. The fair value of CMOs at June 30, 2008 was \$2,186,147,672 of which \$1,223,407,319 were CMOs that are generally more sensitive to interest rate changes. The fair value of CMOs at June 30, 2007 was \$1,665,827,439 of which \$899,811,328 were CMOs that are generally more sensitive to changes in interest rates.

**Foreign Currency Risk** - Foreign currency risk is the risk that changes in exchange rates will adversely affect the fair value of an investment or deposit. The TCRS' investment policy limits the asset allocation for international investments to twenty-five percent of total assets. The TCRS' exposure to foreign currency risk at June 30, 2008 and June 30, 2007 was as follows:

**Foreign Currency-Denominated Investments**  
*(Expressed in Thousands)*

Currency	Total Fair Value June 30, 2008	Fixed Income	Equity	Cash
Australian Dollar	\$ 262,220		\$ 262,220	
British Pound Sterling	1,256,316	\$ 128,214	1,128,102	
Canadian Dollar	47,193		47,193	
Danish Krone	93,241		93,220	\$ 21
Euro Currency	1,779,678	332,656	1,445,990	1,032
Hong Kong Dollar	141,112		141,020	92
Japanese Yen	1,554,682	534,634	1,016,364	3,684
New Zealand Dollar	4,900		4,819	81
Norwegian Krone	63,305		63,305	
Singapore Dollar	79,452		79,106	346
Swedish Krona	117,084		116,720	364
Swiss Franc	326,064		325,978	86
Total	\$ 5,725,247	\$ 995,504	\$ 4,724,037	\$ 5,706

Currency	Total Fair Value June 30, 2007	Fixed Income	Equity	Cash
Australian Dollar	\$ 259,144	\$ 8,443	\$ 250,425	\$ 276
British Pound Sterling	1,263,570	77,543	1,183,999	2,028
Canadian Dollar	49,779	67	49,571	141
Danish Krone	62,477		62,475	2
Euro Currency	1,806,669	312,885	1,493,692	92
Hong Kong Dollar	134,801		134,750	51
Japanese Yen	1,569,152	569,953	995,983	3,216
New Zealand Dollar	10,640		10,606	34
Norwegian Krone	82,993	33,727	49,171	95
Singapore Dollar	84,307		84,119	188
Swedish Krona	164,588		164,150	438
Swiss Franc	302,380		302,334	46
Total	\$ 5,790,500	\$ 1,002,618	\$ 4,781,275	\$ 6,607

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**TENNESSEE CONSOLIDATED RETIREMENT SYSTEM**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**JUNE 30, 2008 AND JUNE 30, 2007**

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**Derivatives** - The TCRS may buy or sell equity index futures contracts for the purposes of making asset allocation changes in an efficient and cost effective manner and to improve liquidity. The futures contracts are limited to the S&P 500 Index, the S&P Midcap 400 Index and the Russell 2000 Index. The TCRS can increase (decrease) equity market exposure by buying (selling) the equity index future to obtain its target domestic equity allocation. Gains (losses) on equity index futures hedge losses (gains) produced by any deviation from the TCRS' target equity allocation. The gains and losses resulting from daily fluctuations in the fair value of the outstanding futures contract are settled daily, on the following day, and a receivable or payable is established for any unsettled gain or loss as of the financial statement date. As of June 30, 2008, the TCRS was under contract for equity index futures and the resulting payable is reflected in the financial statements at fair value. The TCRS was not under any futures contracts at June 30, 2007.

The international securities expose the TCRS to potential losses due to a possible rise in the value of the US dollar. The TCRS investment managers can reduce foreign currency exposure by selling foreign currency forward contracts, at agreed terms and for future settlement, usually within a year. The manager will reverse the contract by buying the foreign currency before the settlement date. A gain (loss) on this transaction pair will hedge a loss (gain) on the currency movement of the international security. The TCRS can sell up to 80% of its foreign currency exposure into US dollars. The fair value of foreign currency forward contracts outstanding as of June 30, 2008 and June 30, 2007 has been reflected in the financial statements.

**D. COMMITMENTS**

**Standby Commercial Paper Purchase Agreement** - The TCRS has agreed to serve as standby commercial paper purchaser for commercial paper issued by the Funding Board of the State of Tennessee. By serving as a standby commercial paper purchaser, the TCRS receives an annual fee of 7.5 basis points on the \$250 million maximum issuance under this agreement during times when both Moody's and Standard and Poor's investment ratings assigned to the State of Tennessee's general obligation bonds are Aaa and AAA respectively, and 12 basis points during times when either Moody's or Standard and Poor's has assigned ratings other than Aaa and AAA respectively. In the unlikely event that the TCRS would be called upon to purchase the commercial paper, the TCRS would receive interest at a rate equal to prime plus 75 basis points during the first 30 consecutive days, plus an additional 50 basis points for each consecutive 30 days thereafter, up to a maximum rate allowed by state law.

**Pending Real Estate Items** - At June 30, 2008 the TCRS had unfunded commitments of \$18,476,000 for pending real estate purchases. At June 30, 2007 the TCRS had unfunded commitments of \$32,777,459 for pending real estate purchases.

**E. SUBSEQUENT EVENT**

**Market Decline** - Continued disruption in the credit markets and overall declines in economic conditions in markets in the United States of America and internationally have resulted in significant declines in the fair market value of the TCRS' investments subsequent to June 30, 2008. As of October 31, 2008, the TCRS estimates that the value of investments excluding the real estate portfolio has declined approximately \$5.5 billion compared to the value as of June 30, 2008.

*(continued)*

**TENNESSEE CONSOLIDATED RETIREMENT SYSTEM  
NOTES TO THE FINANCIAL STATEMENTS  
JUNE 30, 2008 AND JUNE 30, 2007**

**F. FUNDED STATUS AND FUNDING PROGRESS**

The funded status of each plan as of July 1, 2007, the most recent actuarial valuation date, is as follows:

<b>SCHEDULES OF FUNDING PROGRESS</b> <i>(Expressed in Thousands)</i>								
	Actuarial Valuation Date	Actuarial Value of Plan Assets (a)	Actuarial Liability Frozen Entry Age (b)	Accrued Entry Age (b)	Unfunded AAL (UAAL) (b-a)	Funded Ratio (a/b)	Annual Covered Payroll (c)	UAAL as a Percentage of Covered Payroll ((b-a)/c)
<b>SETHEEPP</b>	07/01/07	\$ 26,214,995	\$ 27,240,151		\$1,025,156	96.24%	\$ 5,742,866	17.85%
<b>PSPP</b>	07/01/07	\$ 4,897,974	\$ 5,475,620		\$ 577,646	89.45%	\$ 2,081,964	27.75%

The TCRS uses the Frozen Entry Age actuarial cost method to calculate the annual required contribution (ARC). Effective July 1, 2007, the TCRS reestablished unfunded accrued liabilities for all groups. For the year ended June 30, 2008, information regarding the funded status and funding progress is required to be presented using the entry age actuarial cost method. In the actuarial valuation in which unfunded accrued liabilities are reestablished, the Frozen Entry Age actuarial cost method and the entry age normal actuarial cost method produce the same results.

The required schedule of funding progress immediately following the notes to the financial statements is intended to present multiyear trend information about whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liability for benefits. Since the requirement to present the Schedule of Funding Progress using the entry age actuarial cost method is effective beginning for the year ended June 30, 2008, only the funded status information relating to the most recent actuarial valuation date is provided in the required supplemental information. Additional required historical information will be provided in subsequent years once available.

Additional information as of the latest actuarial valuation follows:

	<b>SETHEEPP</b>	<b>PSPP</b>
Valuation Date	July 1, 2007	July 1, 2007
Actuarial cost method	Frozen Entry Age	Frozen Entry Age
Amortization method	Level Dollar	Level Dollar
Remaining amortization period	20 years closed period	(1) closed period
Asset valuation method	5-year Moving Market Average	5-year Moving Market Average
Actuarial assumptions:		
Investment rate of return	7.50%	7.50%
Projected salary increases	4.75% (2)	4.75% (2)
Included inflation at	3.00%	3.00%
Cost-of-living adjustments	3.00%	3.00%
Increase in Social Security wage base	3.50%	3.50%

(1) The length of the amortization period varies by political subdivision, not to exceed 30 years.  
 (2) Uniform rate that approximates the effect of a graded salary scale.

**TENNESSEE CONSOLIDATED RETIREMENT SYSTEM  
 REQUIRED SUPPLEMENTARY INFORMATION  
 SCHEDULES OF FUNDING PROGRESS**

**SCHEDULES OF FUNDING PROGRESS**  
*(Expressed in Thousands)*

	Actuarial	Actuarial	Actuarial	Unfunded	Funded	Annual	UAAL as a
	Valuation	Value of	Liability (AAL)	AAL	Ratio	Covered	Percentage of
	Date	Plan Assets	Frozen Entry Age	(UAAL)	(a/b)	Payroll	Covered Payroll
		(a)	(b)	(b-a)		(c)	((b-a)/c)
<b>SETHEEPP</b>	07/01/07	\$ 26,214,995	\$ 27,240,151	\$1,025,156	96.24%	\$ 5,742,866	17.85%
<b>PSPP</b>	07/01/07	\$ 4,897,974	\$ 5,475,620	\$ 577,646	89.45%	\$ 2,081,964	27.75%

The schedule of funding progress is intended to present multiyear trend information about whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liability for benefits. Since the TCRS has previously calculated the annual required contribution (ARC) using the aggregate actuarial cost method and the requirement to present the Schedule of Funding Progress using the entry age actuarial cost method is effective beginning for the year ended June 30, 2008, only the funded status information relating to the most recent actuarial valuation date is provided. Additional required historical information will be provided in subsequent years once available.

**TENNESSEE CONSOLIDATED RETIREMENT SYSTEM  
REQUIRED SUPPLEMENTARY INFORMATION  
SCHEDULES OF EMPLOYER CONTRIBUTIONS**

**SCHEDULES OF EMPLOYER CONTRIBUTIONS**

*Expressed in Thousands*

Year Ended June 30	SETHEEPP		PSPP	
	Annual Required Contribution	Percentage Contributed	Annual Required Contribution	Percentage Contributed
2008	\$593,412	100.00%	\$244,847	100.00%
2007	\$562,729	100.00%	\$231,699	100.00%
2006	\$474,879	100.00%	\$191,000	100.00%
2005	\$448,154	100.00%	\$181,096	100.00%
2004	\$271,298	100.00%	\$139,808	100.00%
2003	\$264,320	100.00%	\$134,014	100.00%

An actuarial valuation of the TCRS is performed every two years with the next valuation scheduled to be effective July 1, 2009.

TENNESSEE CONSOLIDATED RETIREMENT SYSTEM  
ACTUARIAL BALANCE SHEET

ACTUARIAL BALANCE SHEET  
as of July 1, 2007

	State Employees, Teachers, Higher Ed. Employees Pension Plan (SETHEEPP)	Political Subdivision Pension Plan (PSPP)	Total
<b>ASSETS</b>			
<b>Present assets creditable to</b>			
Employer accumulation fund	\$ 22,828,158,274	\$ 4,001,181,918	\$ 26,829,340,192
Members' accumulation fund	3,386,836,344	896,792,065	4,283,628,409
<b>Total present assets</b>	<u>26,214,994,618</u>	<u>4,897,973,983</u>	<u>31,112,968,601</u>
<b>Present value of prospective contributions payable to</b>			
Employe accumulation fund			
Normal	3,822,067,457	1,321,097,983	5,143,165,440
Accrued liability	1,025,156,148	577,645,568	1,602,801,716
<b>Total employer accumulation</b>	<u>4,847,223,605</u>	<u>1,898,743,551</u>	<u>6,745,967,156</u>
<b>Member's accumulation fund</b>	<u>1,559,379,148</u>	<u>515,995,791</u>	<u>2,075,374,939</u>
<b>Total prospective contributions</b>	<u>6,406,602,753</u>	<u>2,414,739,342</u>	<u>8,821,342,095</u>
<b>TOTAL ASSETS</b>	<u>\$ 32,621,597,371</u>	<u>\$ 7,312,713,325</u>	<u>\$ 39,934,310,696</u>
<b>LIABILITIES</b>			
<b>Present value of prospective benefits payable on account of</b>			
Present retired members and beneficiaries	\$ 12,544,677,397	\$ 1,902,875,092	\$ 14,447,552,489
Present active members	19,503,069,132	5,234,527,606	24,737,596,738
Former members	573,850,842	175,310,627	749,161,469
<b>TOTAL LIABILITIES</b>	<u>\$ 32,621,597,371</u>	<u>\$ 7,312,713,325</u>	<u>\$ 39,934,310,696</u>

UNAUDITED