# Virginia529
# Annual Report

For the period ended on June 30, 2013

Virginia529 College Savings Plan℠

COMMONWEALTH of VIRGINIA

VIRGINIA COLLEGE SAVINGS PLAN
9001 Arboretum Parkway, North Chesterfield, VA 23236

Mary G. Morris
Chief Executive Officer

(804) 371-0766

## LETTER OF TRANSMITTAL

October 1, 2013

Board of the Virginia College Savings Plan
9001 Arboretum Parkway
North Chesterfield, Virginia 23236

To the Members of the Board:

It is our pleasure to present the Annual Financial Report (the Report) of the Virginia College Savings Plan (VA529) for the fiscal year ended June 30, 2013, as required by Section 23-38.84 of the Code of Virginia. This Report will be presented to the Governor, the Senate Committee on Finance, the House Committees on Appropriations and Finance, and the Joint Legislative and Audit Review Commission. The Report also will be available on our web site at Virginia529.com.

### MISSION AND PROGRAMS

VA529's mission is to continue to be a national leader in 529 programs by providing superior, affordable, innovative, tax-advantaged college savings options to assist families and others in achieving their higher education goals, all as part of our statutory mandate to help make college more affordable and accessible. We accomplish our mission primarily through four college savings programs, Virginia529 prePAID℠ (prePAID), Virginia529 inVEST℠ (inVEST), CollegeAmerica® and CollegeWealth®.

### ACCOUNTING SYSTEM AND INTERNAL CONTROL

VA529's management assumes full responsibility for the accuracy, completeness and reliability of the information presented. The financial statements are presented in accordance with accounting principles generally accepted in the United States of America (GAAP) as established by the Governmental Accounting Standards Board (GASB). The financial statements contain a description of the accounting principles used in the preparation of the statements. In accordance with GASB principles per the Codification of Governmental Accounting and Financial Reporting Standards, the financial statements include Management's

Discussion and Analysis (MD&A). This Letter of Transmittal is designed to complement the MD&A and should be read in conjunction with it.

VA529's management is responsible for maintaining a system of adequate internal accounting controls designed to provide reasonable assurance that transactions are executed in accordance with management's general or specific authorization, and are recorded as necessary to maintain accountability for assets and to permit preparation of financial statements in accordance with GAAP. The internal control system includes the organization plan, the appropriate segregation of duties and responsibilities and sound practices in the performance of duties, data security, and personnel with capabilities commensurate with their responsibilities.

**VIRGINIA529 PREPAID ACTUARIAL VALUATION AND OUTLOOK**

VA529's most recent actuarial valuation report for the Virginia529 prePAID program was prepared by Milliman, Inc. as of June 30, 2013 and compares the value of the current and projected assets of prePAID to the value of expected future disbursements and program costs. The actuarial valuation was performed based upon generally accepted actuarial principles. The two most significant assumptions used to prepare prePAID's actuarial valuation report are the long-term rates of investment return and future tuition growth. The report indicated an improvement in prePAID's actuarially determined funded position from the position as of June 30, 2012 primarily due to lower than expected tuition increases and higher than expected investment returns. We are pleased to report that prePAID was 110 percent funded on an actuarial basis as of June 30, 2013.

The Plan continues to remain optimistic that its asset allocation and investment strategies will result in the prePAID portfolio meeting or exceeding performance expectations over the long-term. The Plan has assumed a long-term rate of return of 6.75 percent on prePAID investments. As of June 30, 2013, the total return since inception was 6.4 percent, net of fees, and reflected the higher than expected 8.4 percent overall performance during fiscal 2013. In June 2009, the Plan adopted a new target asset allocation strategy designed to improve returns with a slightly lower expected volatility of returns versus the prior allocation strategy. Plan staff and the Investment Advisory Committee continued to work diligently during fiscal year 2013 to implement the new target allocation strategy. As of June 30, 2013, the prePAID portfolio was within about 3.0 percent of its target allocation in the four major categories.

In aggregate, market movements had a positive net effect on the prePAID portfolio in fiscal 2013. In mid-September 2012, the Federal Reserve (Fed) announced a third round of quantitative easing under which it may purchase additional agency mortgage-backed securities at a pace of $40 billion per month and longer-term Treasury securities at a pace of $45 billion per month, with no end-date or total purchase limit specified in advance. The Fed also announced that it would maintain its existing policy of reinvesting principal payments from its holdings of agency debt and agency mortgage-backed securities in additional agency mortgage-backed securities for the foreseeable future. Finally, the Fed announced its decision to retain the target range for the federal funds rate at 0 to 1/4 percent at least through mid-2015, absent changes in inflation. The Fed's goal was to place downward pressure on longer-term interest rates and the unemployment rate, support mortgage markets, and help make broader financial conditions more accommodative.

In December 2012, the Fed announced its intention to keep the target range for the federal funds rate at 0 to 1/4 percent as long as the unemployment rate remained above 6-1/2 percent and inflation remained in check. The Fed's moves through calendar year-end signaled a shift in which the Fed was making monetary policy conditional on explicit economic goals. At year-end, all G7 central banks were continuing their interest rate easing or were on hold at low levels. In the U.S., all eyes were on Congress and the White House as we headed towards the "fiscal cliff" of tax increases and budget cuts in January 2013.

A last minute deal avoided the fiscal cliff but increases in tax rates for upper-income taxpayers and an expiration of the payroll tax cut went into effect in January 2013. In February and March Congress avoided a federal government shutdown and raised the debt ceiling but failed to avoid the sequestration which forcibly reduced federal spending by $85 billion through calendar 2013. During this time, the domestic equity markets soared with the Dow Jones Industrial Average and the S&P 500 Index reaching record highs. In April, commodities fell sharply in global trading and the domestic equity markets followed. In May, Fed Chairman Ben Bernanke indicated during Congressional testimony that the Fed was prepared to reduce its Treasury and agency mortgage-backed security purchases if the economy continued to improve. That along with a formal statement to that effect from the Fed following its June meeting, led to a significant sell-off in U.S. Treasuries in late May and June. The yield on the ten-year Treasury bond soared from 1.85 percent on March 31st to 2.49 percent on June 30th. However, domestic stocks continued to rally through fiscal year-end as economic data remained positive.

U.S. equities continued to climb in the first quarter of fiscal 2014 and the fixed income markets moderated as the Fed decided to await more evidence that economic progress will be sustained before adjusting the pace of its purchases. As of September 2013, the U.S. unemployment rate was 7.3 percent down from 8.1 percent a year earlier. Although the trend in the unemployment numbers was positive during fiscal 2013 and into fiscal 2014, the underlying numbers reflect sluggish job creation and a lagging recovery. GDP is growing at about 2 percent. Despite the aforementioned increases, interest rates remained low both domestically and globally, helping the fixed income market. It is difficult to estimate how these and other factors may impact the performance of prePAID during the remainder of fiscal 2014.

The other significant factor in prePAID's ability to meet its future obligations is the future growth in tuition. As a result of additional funding in recent years, and a concerted effort on the part of the colleges and universities to contain tuition growth, full time undergraduate tuition and all mandatory fees at public higher education institutions in Virginia increased by an average of 4.3 percent for the 2013-14 academic year. This increase was just slightly more than last year's 4.1 percent increase.

The 2013 General Assembly provided approximately $25.1 million in additional general fund support to higher education institutions in fiscal 2014. According to the State Council of Higher Education for Virginia (SCHEV), notwithstanding this additional funding, for the first time, the State's contribution to the cost of higher education is estimated to be 49 percent, which means that on average, in-state undergraduate students are paying more than half of the cost of their education in fiscal 2014. That is 18 percent lower than the target of 67 percent identified in the Commonwealth's tuition policy.

There is an inverse relationship between state funding and the rate at which tuition increases at public higher education institutions. For the fourth consecutive year, general fund revenue growth surpassed the revenue forecast and the Commonwealth ended fiscal 2012 with a surplus. According to the Governor's Office, the main drivers of the revenue surplus were growth in individual income tax nonwithholding, lower individual income tax refunds and higher than expected recordation tax receipts. While the Commonwealth's economy and general fund revenue are recovering, it is unknown when and to what extent additional resources may become available to restore support to public higher education and mitigate pressure on tuition. The full impact of federal spending reductions that went into effect in March 2013 – sequestration – on Virginia's economy has yet to be known. Virginia is considered to be one of the most vulnerable states to federal spending reductions because of its dependence on defense spending and the large number of federal employees who live and work in Virginia.

In assessing prePAID's financial condition and in pricing prePAID contracts, VA529 has projected that tuition and fee increases at Virginia's public higher education institutions will increase annually by approximately 7.5 percent for four-year and two-year institutions for fiscal years 2015 and thereafter. Changes in public education funding or changes in tuition models that result in tuition increases above VA529's projections would have an immediate, detrimental impact on VA529's outstanding long-term prePAID obligations. However, with the statutory requirement that institutions provide updated, long-term tuition projections, the Plan remains in a favorable position to prepare for future tuition and fee increases.

## 2013 PROGRAM HIGHLIGHTS

- **Account Growth and Transaction Volume**

During fiscal 2013, the Plan continued to experience positive growth in accounts as shown in the table below. CollegeWealth's 41.2 percent growth rate demonstrates the success of the program with BB&T and Union First Market Bank. This figure will continue to normalize in the future as the program's account base continues to increase following its 2009 re-launch. The inVEST Program's 12.7 percent growth rate depicts continued strong growth and corresponds to an additional 19,787 accounts opened during the fiscal year.

| Fiscal 2013 Growth in Accounts[1] | |
|---|---|
| **prePAID** | 4.6% |
| **inVEST** | 12.7% |
| **CollegeAmerica** | 3.2% |
| **CollegeWealth** | 41.2% |

*[1]Gross accounts opened during fiscal year, except for CollegeAmerica (net)*

Transaction volume also continued to increase as participants utilized their college savings accounts. During fiscal year 2013, the Plan processed 24,221 inVEST distribution requests and 26,462 prePAID payments to institutions, representing a 9.7 percent and .6 percent increase over the prior fiscal year, respectively.

- **Plan and Program Rebranding**

On November 13, 2012, VA529 announced program name changes to two of its four programs. The Virginia Prepaid Education Program was renamed Virginia529 prePAID and the Virginia Education Savings Trust was renamed Virginia529 inVEST. New logos were also introduced. The change will further help reinforce the Virginia529 brand and help promote awareness and recognition of Virginia529's college savings programs. Using the 529 in the name will also further enhance and popularize the 529 brand in the minds of current and prospective investors.

- **prePAID Semester Contracts**

In addition to the name changes described above, VA529 also modified the prePAID program to allow customers to purchase contracts in semester increments instead of full years, effectively cutting the cost of getting started in prePAID in half. In addition, VA529 refined the pricing for contracts with Tier I (university) and Tier II (community college) pricing at a definite conversion factor to attract purchasers at multiple affordability levels. These were significant changes in the prePAID program and included the introduction of a Virginia529 prePAID web calculator to assist customers in determining which price, contract or combination best suited their situation. The introduction of semester contracts was a success with over 11 percent of the new contracts sold during the 2012-13 enrollment period being single-semester contracts.

- **Operational and System Improvements**

During fiscal 2013 the Plan continued to make improvements to better serve our customers. While too numerous to list them all, we offer some examples. In June 2013, VA529 implemented a new customer contact center phone system. This new system will provide improved customer service via customized phone queues, intra-day phone queue management, messaging and voice mail, internal reporting, and improvements to hardware and software. VA529 is also adding staff to its customer service area to handle increasing call volume. We are also making improvements to the Virginia529.com web site to provide more information in order to reduce customer calls. In the next fiscal year, we plan on further developing customer access to on-line forms in order to improve efficiency, reduce paper and improve the customer experience.

VA529 successfully converted its general ledger accounting systems to Banner Finance as of July 1, 2010. This project has resulted in process efficiencies, reduced data entry and improved reporting. During fiscal 2013 we continued to modify financial processes to improve efficiencies between the Banner College Savings System module (participant recordkeeping) and Banner Finance (transaction accounting and reporting). In fiscal 2013, VA529's Information Technology Division completed development of the Banner College Savings System 8.0 Release. Banner 8.0 was released for testing on July 2, 2013. VA529 staff and other Banner College Savings System users began testing Banner 8.0 during the first quarter of fiscal 2014. Once this new release is in production, it will allow VA529 to utilize some of the workflow features in Banner Finance and will improve operational productivity and efficiency.

The Department of Accounts is replacing CARS with a new, more robust accounting system (Cardinal Project). During fiscal 2013, VA529 volunteered and was selected as a Wave 1 pilot interfacing agency to help test and validate Cardinal and related processes prior to state-wide release to all interfacing agencies. VA529's participation will help ensure that our unique transaction processing and interfacing needs are addressed prior to the roll out to remaining agencies in fiscal 2017. Cardinal's targeted go-live date for Wave 1 agencies is October 2014. VA529 accounting and IT staff will be working through fiscal 2014 on this project.

- **Virginia529 inVEST Program Investment Changes**

VA529 closed the money market portfolio for inVEST participants on December 31, 2012. This change was required in order to retain our ability to offer a stable value investment option to inVEST participants. In order to attract companies to provide wrap coverage for inVEST's stable value portfolio, either the money market portfolio had to be eliminated or restrictions on participants' ability to transfer funds from the money market portfolio to other investment options had to be added. The Board weighed the availability of other low-risk strategies, including the existing stable value portfolio and the CollegeWealth FDIC insured option in deciding to eliminate the money market portfolio. Participants were notified in advance and those remaining in the money market portfolio were transferred automatically into the inVEST stable value portfolio on December 31st.

Stable value comprised over 20 percent of the inVEST program's assets under management as of June 30, 2013. The age-based evolving portfolios continue to be the most popular of the diversified inVEST program investment options.

- **Joint Legislative Audit and Review Commission (JLARC) Oversight.**

During its 2012 Session, the General Assembly passed, and the Governor signed, the Virginia College Savings Plan Oversight Act, which provided for oversight and evaluation on a continuing basis by JLARC. Although the legislation was not the result of a problem or deficiency, JLARC oversight resulted in the dedication of VA529 staff and financial resources in fiscal 2013 as the Oversight Act was implemented.

During fiscal 2013 VA529 staff worked to familiarize JLARC with our operations. Also during the year, JLARC's actuary, Gabriel Roeder Smith & Company (GRS) completed its initial quadrennial actuarial audit of the prePAID program, which included a non-replication actuarial audit of prePAID's actuarial policy and practices, focusing on VA529 actuary's (Milliman, Inc.) June 30, 2012 actuarial valuation report. In their report, GRS agreed with Milliman's conclusion that prePAID was actuarially sound, that data used in their 2012 valuation report was reasonable and appropriate, that Milliman followed generally accepted actuarial principles and practices, and that the pricing methodology was actuarially sound. The full report may be found on JLARC's website at http://jlarc.virginia.gov/vcsp. We look forward to continuing our relationship with JLARC.

**ACKNOWLEDGEMENTS**

We remain committed to providing the best possible customer service to our program participants and to the citizens of the Commonwealth, and to be responsible stewards of the funds in our care. We express our sincere thanks and appreciation to our outstanding staff, our business partners and the guidance and dedication of our Board and Committee members.

Respectfully submitted,

Mary G. Morris
Chief Executive Officer

Gary Ometer, CPA, CGMA
Chief Financial Officer

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**Commonwealth of Virginia**

*Auditor of Public Accounts*

Martha S. Mavredes, CPA
Auditor of Public Accounts

P.O. Box 1295
Richmond, Virginia 23218

November 14, 2013

The Honorable Robert F. McDonnell
Governor of Virginia

The Honorable John M. O'Bannon, III
Chairman, Joint Legislative Audit
And Review Commission

Board Members
Virginia College Savings Plan

INDEPENDENT AUDITOR'S REPORT

**Report on Financial Statements**

We have audited the accompanying financial statements of the business-type activities (the Enterprise Fund) and remaining fund information (the Private-Purpose Trust Fund) of the **Virginia College Savings Plan** (Plan), as of and for the year ended June 30, 2013, and the related notes to the financial statements, which collectively comprise the Plan's basic financial statements as listed in the table of contents.

***Management's Responsibility for the Financial Statements***

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

***Auditor's Responsibility***

Our responsibility is to express opinions on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States. 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 involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall financial statement presentation.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a reasonable basis for our audit opinion.

***Opinion***

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the business-type activities and remaining fund information of the Virginia College Savings Plan as of June 30, 2013, and the changes in financial position and, where applicable, cash flows, for the year then ended, in accordance with accounting principles generally accepted in the United States of America.

***Emphasis of Matter***

*Correction of 2012 Financial Statements*

As discussed in Note 2, the fiscal year 2012 financial statements of the Private-Purpose Trust Fund have been restated to correct a misstatement pertaining to unapplied payments for program participants. Our opinion is not modified with respect to this matter.

*Relationship to the Commonwealth of Virginia*

As discussed in Note 1, the basic financial statements of the Plan are intended to present the financial position, the changes in financial position and cash flows of only that portion of the business-type activities, the major enterprise fund, and aggregate remaining fund information of the Commonwealth of Virginia that is attributable to the transactions of the Plan. They do not purport to, and do not, present fairly the Commonwealth of Virginia's overall financial position as of June 30, 2013, and the changes in its financial position and its cash flows, where applicable, for the year then ended in conformity with accounting principles generally accepted in the United States of America. Our opinion is not modified with respect to this matter.

***Other Matters***

*Required Supplementary Information*

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 7 through 19 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of the financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to management's discussion and analysis in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on management's discussion and analysis because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

*Supplementary and Other Information*

Our audit was conducted for the purpose of forming an opinion on the financial statements that collectively comprise the Virginia College Savings Plan's basic financial statements. The accompanying supplementary information, such as Appendix A, Appendix B, and Appendix C, and the other information, such as the letter of transmittal and program information for CollegeAmerica and CollegeWealth, are presented for the purpose of additional analysis and are not a required part of the basic financial statements.

Appendix A, Appendix B, and Appendix C are the responsibility of management and were derived from and relate directly to the underlying accounting and other records used to prepare the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the basic financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, Appendix A, Appendix B, and Appendix C are fairly stated, in all material respects, in relation to the basic financial statements taken as a whole.

The letter of transmittal and program information for CollegeAmerica and CollegeWealth have not been subjected to the auditing procedures applied in the audit of the basic financial statements and, accordingly, we do not express an opinion or provide any assurance on them.

**Other Reporting Required by Government Auditing Standards**

In accordance with Government Auditing Standards, we have also issued our report dated November 14, 2013 on our consideration of the Virginia College Savings Plan's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, 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 Government Auditing Standards in considering the Virginia College Savings Plan's internal control over financial reporting and compliance.

Staci A. Henshaw

DEPUTY AUDITOR OF PUBLIC ACCOUNTS

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# Management's Discussion
## & Analysis

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# VIRGINIA COLLEGE SAVINGS PLAN'S
# MANAGEMENT'S DISCUSSION AND ANALYSIS
# Unaudited

The Virginia College Savings Plan's (VA529) Management's Discussion and Analysis is designed to assist the reader in focusing on significant financial issues and provides an overview of financial activity. This discussion includes an analysis of the VA529's financial condition and results of operations for the fiscal year ended June 30, 2013. This presentation includes summarized data and should be read in conjunction with the accompanying financial statements and notes.

VA529 operates the Commonwealth's Internal Revenue Code (IRC) Section 529 qualified tuition plan, which offers four programs, Virginia529 prePAID℠ (prePAID), Virginia529 inVEST℠ (inVEST), CollegeAmerica® and CollegeWealth®. prePAID is considered a defined benefit program which offers contracts, at actuarially determined prices, that provide the future payment of undergraduate tuition for the normal full-time course load for students enrolled in a general course of study at any Virginia public higher educational institution and all mandatory fees required as a condition of enrollment of all students and differing payouts at private or out-of-state institutions. Annually, VA529's actuary determines the actuarial soundness of prePAID. Key factors used in the actuarial analysis include anticipated tuition increases (both short and long-term) as well as anticipated long-term investment performance. inVEST is a defined contribution savings program, which allows participants to make contributions into their selected investment portfolio(s). inVEST accounts are subject to market investment risks, including the possible loss of principal.

CollegeAmerica and CollegeWealth are also defined contribution savings programs. CollegeAmerica, a broker-sold program, offers 38 different American Funds mutual fund products as investment options. CollegeAmerica participants bear all market risk for their investment, including the potential loss of principal. The American Funds acts as program manager for CollegeAmerica and provides all back office and operational services for the program. CollegeWealth participants invest in FDIC-insured savings products offered through two participating banks BB&T and Union First Market Bank.

## Overview of Financial Statements

This discussion and analysis is an introduction to VA529's basic financial statements, which include VA529's business-type activity or enterprise fund, the fiduciary or private purpose trust funds, and notes to the financial statements.

### Business Type Activities – Enterprise Fund

All prePAID activities and VA529's operating activities are accounted for in an enterprise fund, which is typically used to account for governmental operations that are financed and operated in a manner similar to a private sector business. Enterprise funds typically report activities that charge fees for supplies or services to the general public. This activity is reported on the full accrual basis of accounting. This means that all revenue and expenses are reflected in the financial statements even if the related cash has not been received or paid as of June 30th.

The Statement of Net Position presents information on all prePAID assets and liabilities, with the difference between the two reported as total net position. Over time, increases and decreases in net position along with the information contained in the annual actuarial soundness report indicate prePAID's financial position.

The Statement of Revenues, Expenses, and Changes in Net Position presents the revenues earned and expenses incurred during the year, including both actual as well as actuarially determined contract payments from participants and distributions for higher education expenses.

The Statement of Cash Flows presents information related to cash inflows and outflows summarized by operating, financing, and investing activities.

### Fiduciary Fund

inVEST is reported as a private purpose trust fund. A private purpose trust fund accounts for transactions of trust arrangements in which the principal and income benefit individuals, private organizations or other governments, and uses the full accrual basis of accounting.

inVEST activities are reported in the Statement of Fiduciary Net Position and the Statement of Changes in Fiduciary Net Position. The Statement of Fiduciary Net Position presents information on all inVEST assets and liabilities, with the difference between the two reported as total net position. The Statement of Changes in Fiduciary Net Position presents the revenues earned and expenses incurred during the year.

CollegeAmerica and CollegeWealth are also defined contribution savings programs and are presented as Other Information.

### Notes to the Financial Statements

The Notes to the Financial Statements provide additional information that is essential to a full understanding of the data provided in the financial statements.

## Fiscal 2013 Financial Highlights

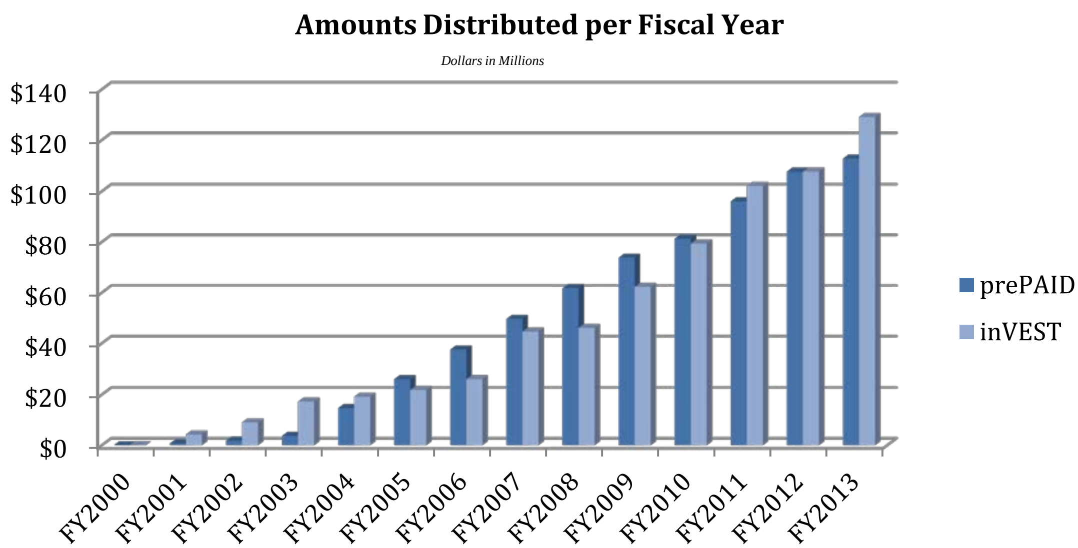
VA529 collects, holds, invests and distributes monies held in trust for program participants. VA529 invests its funds pursuant to statute and Investment Policies and Guidelines under the direction of its Board and Investment Advisory Committee in a mix of equity, fixed income and alternative investments. During the fiscal year ended June 30, 2013, the domestic and international equity markets performed very well with moderate volatility as compared to recent years. The United States domestic equity market, as measured by the Standard & Poor's 500 Index, ended the year up 20.6 percent from June 30, 2012 while international equity markets as measured by the MSCI EAFE Index, were up 19.1 percent. The fixed income markets provided consistent performance through the third quarter but slid in the fourth quarter as interest rates rose sharply. The Barclays Capital US Aggregate Bond Index returned -0.7 percent for the year ended June 30, 2013. However, certain fixed income classes such as high yield bonds performed well as demonstrated by the Barclays Capital High Yield Index returning 9.5 percent for the year ended June 30, 2013.

In aggregate, market movements had an overall net positive effect on fixed income and equity security prices in the prePAID, inVEST and CollegeAmerica portfolios for the fiscal year ended June 30, 2013.

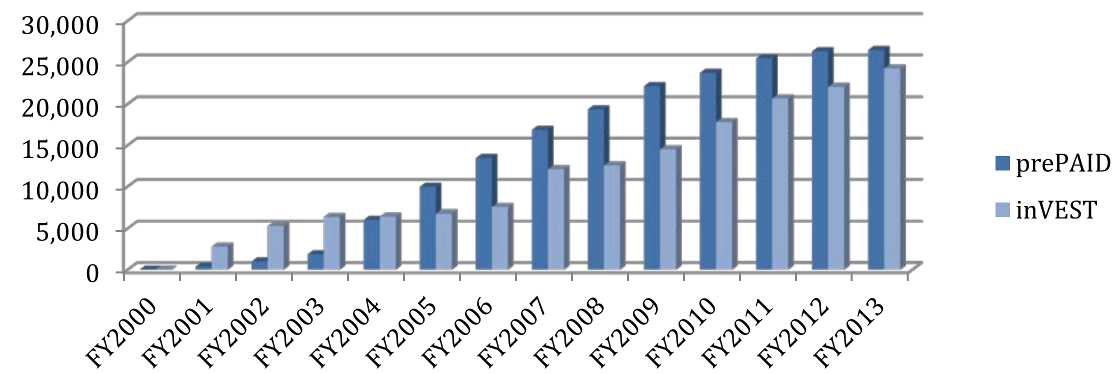
- The Enterprise Fund's total cash, cash equivalents, and investments held in trust for program participants increased by $171.6 million, or about 8.6 percent from fiscal year-end 2012 .
- prePAID's actual return on investments for the fiscal year ended June 30, 2013 was 8.4 percent on a time-weighted and 8.1 percent on a dollar-weighted basis reflecting the equity and fixed income market performance during the fiscal year.
- The Enterprise Fund's net position increased by $145.3 million to an actuarially determined surplus of $219.5 million from an actuarial surplus of $74.2 million in the prior year, which was primarily due to lower than expected tuition increases and higher than expected investment returns.

- prePAID's actuarially determined obligations for future payments increased by $13.8 million, or approximately .63 percent, which was primarily due to the additional obligation of 3,235 new contracts opened during the 2012 – 2013 enrollment period.
- inVEST net position held in trust for program participants increased by $339.4 million or about 17.3 percent due to growth in accounts and improved capital markets performance.
- Both prePAID and inVEST applicants continued to increase utilization of on-line applications with more than 93.8 and 90.6 percent, respectively, of applications being filed on-line.
- VA529 continued to experience positive growth in accounts, particularly in inVEST and CollegeWealth with 13 percent and 41 percent gross account growth, respectively. CollegeAmerica also experienced positive net account growth in 2013 at 3.2 percent. More information on CollegeAmerica and CollegeWealth is provided in Other Information.
- Distributions as measured by dollars and number of transactions continued to increase for both prePAID and inVEST as participants utilized their college savings accounts. Transactional activity for both prePAID and inVEST is depicted in the graphs below.

The two graphs below represent inVEST and prePAID distributions since fiscal year 2000.



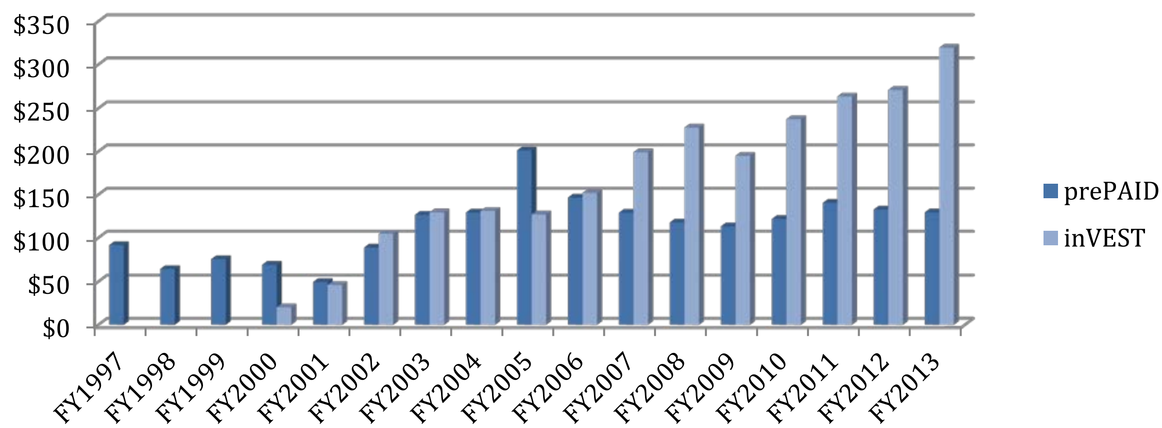
**Number of Distributions on Behalf of Beneficiaries per Fiscal Year**



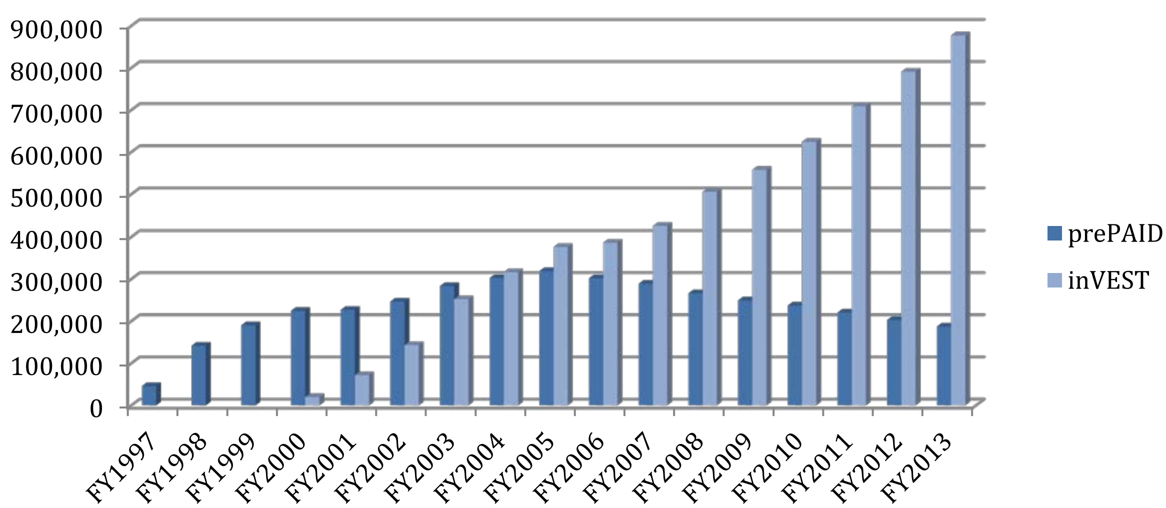

The two graphs below represent prePAID contract payments and inVEST contributions received since fiscal year 1997 – inVEST being introduced in fiscal 2000.

**Amounts Received per Fiscal Year**

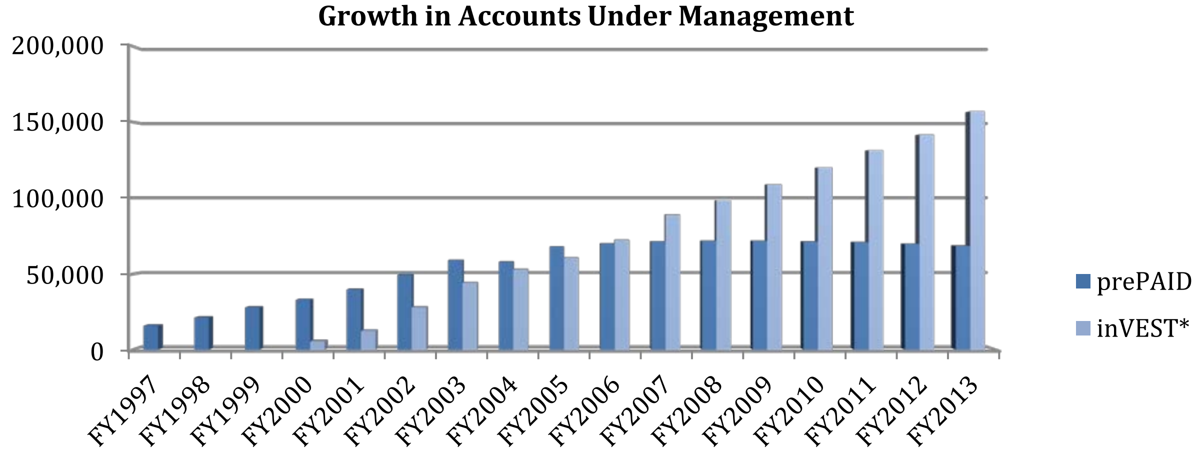
*Dollars in Millions*




**Number of Payments/Contributions Received per Fiscal Year**



The graph below represents inVEST and prePAID accounts under management since fiscal year 1997 – inVEST being introduced in fiscal 2000.




*In fiscal 2013, VA529 instituted a policy to close zero balance inVEST accounts that had no activity for the trailing 18 months. On June 27, 2013 VA529 closed 13,134 zero balance inVEST accounts and will continue to close such accounts on a monthly basis in the future. For reporting purposes, inVEST accounts reported for fiscal years prior to 2013 have been adjusted retroactively as if the zero balance account policy had been in effect since inception of the inVEST program.

## Analysis of Enterprise Fund Financial Activities

The Enterprise Fund includes the activities of prePAID as well as VA529's general operating activities. The Enterprise Fund ended the year with net position of $219.5 million.

Table 1 is a summary comparison of the prePAID's Statement of Revenues, Expenses, and Changes in Net Position for fiscal year 2013 as compared to the prior year.

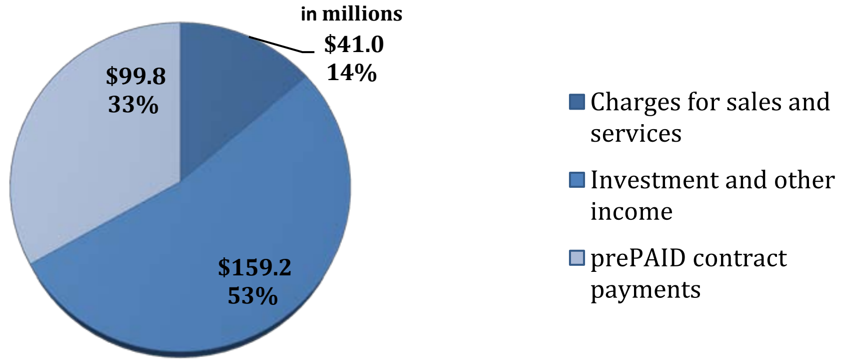
### Table 1 – Enterprise Fund – Changes in Net Position (in millions)

| YEARS ENDED JUNE 30, | 2013 | 2012 | CHANGE |
|---|---|---|---|
| Operating revenues | | | |
| Charges for sales and services | $ 41.0 | $ 35.9 | $ 5.1 |
| Interest and dividends | 103.2 | 60.7 | 42.5 |
| Net increase (decrease) in fair value of investments | 56.0 | (44.0) | 100.0 |
| prePAID contract payments | 99.8 | 107.4 | (7.6) |
| Other | 0.8 | 0.0 | 0.8 |
| Net operating revenues | 300.8 | 160.0 | 140.8 |
| Operating expenses | | | |
| Tuition benefits expense | 137.9 | 78.4 | 59.5 |
| Other operating expenses | 17.1 | 17.2 | ( 0.1) |
| Net operating expenses | 155.0 | $95.6 | 59.4 |
| Transfer to the Commonwealth | (0.3) | (0.4) | 0.1 |
| Non operating interest expense | (0.1) | (0.1) | - |
| Change in net position | $ 145.3 | $ 63.9 | $ 81.5 |

Amounts may not sum due to rounding

Capital markets performed well during the fiscal year. The prePAID Portfolio's allocation to domestic equities posted the strongest returns, however nearly all of the portfolio's investments posted positive returns for the fiscal year. For the fiscal year ended June 30, 2013, there was a net increase in the fair value of investments of approximately $56 million, versus the decrease in the prior fiscal year of $44 million. The fair market value of investment securities changes on a daily basis depending upon market conditions. This number will fluctuate from year to year, depending upon market conditions on June 30th, or the last business day of the fiscal year. Investment income represents about 53 percent of enterprise fund revenue, as shown in Chart 1.

**Chart 1**
**2013 Enterprise Fund Revenue**




VA529 prePAID contract payment revenue includes actual and actuarially estimated contributions, and represents approximately 33 percent of enterprise fund revenue. Actual contract payments from participants decreased by $3.8 million over prior year receipts. In addition, actuarially determined prePAID contract payment revenue decreased by $3.9 million. Receipts for charges for sales and services totaled $41 million in fiscal year 2013. This is a $5.1 million increase over the prior year. The increase is attributable to the growth in assets in the CollegeAmerica and CollegeWealth programs.

Table 1 reflects tuition benefits expense, which is comprised of two components; actuarially determined and actual tuition benefits expenses. The actuarial tuition benefit expense is accrued for estimated expenses, as determined by VA529's actuary, and it represents the net change in tuition benefits payable over the prior fiscal year end. This actuarially determined amount increased from the previous fiscal year end accrual by $53.7 million.

Actual tuition benefit expense represents actual distributions made during the fiscal year. This actual amount increased over the prior year by $5.8 million, or 4.9 percent. The increase in actual distributions is attributable to an increase in the number of students using benefits and increases in tuition and mandatory fees at the higher education institutions. The net change in tuition benefits expense from fiscal year 2012 is $59.5 million.

Table 2 demonstrates the numbers of students served and the amounts paid from prePAID directly to Virginia public universities and community colleges during fiscal year 2013. Virginia's colleges received approximately $95.2 million in prePAID tuition and mandatory fee payments for 11,133 students in fiscal year 2013.

**Table 2**
**prePAID Payments to Virginia Public Universities and Community Colleges**
**Fiscal Year 2013**

| PUBLIC COLLEGES | STUDENTS WITH prePAID CONTRACTS | prePAID PAYMENTS TO COLLEGES |
|---|---|---|
| Virginia Tech | 1,928 | $20.0 million |
| University of Virginia | 1,394 | $16.3 million |
| Virginia Commonwealth University | 1,144 | $9.9 million |
| James Madison University | 1,095 | $9.1 million |
| College of William & Mary | 633 | $8.3 million |
| George Mason University | 817 | $6.9 million |
| Christopher Newport University | 480 | $4.8 million |
| Longwood University | 428 | $4.0 million |
| Old Dominion University | 540 | $3.6 million |
| Radford University | 437 | $3.4 million |
| University of Mary Washington | 374 | $3.2 million |
| Virginia Military Institute | 79 | $1.0 million |
| University of Virginia at Wise | 28 | $0.2 million |
| Virginia State University | 29 | $0.2 million |
| Norfolk State University | 14 | $0.1 million |
| Community Colleges * | 1,713 | $4.2 million |

*Includes Richard Bland College; Virginia's only 2-year junior college.

As shown in Chart 2, tuition benefit payments represent 88 percent of actual expenses of the Enterprise Fund. Actual tuition benefits expenses increased by $5.8 million over the prior fiscal year. Of the $17.1 million expended for administrative and operating services, 82 percent were for personal and contractual services.

**Chart 2**
**2013 Enterprise Fund Expenses**
**in millions**

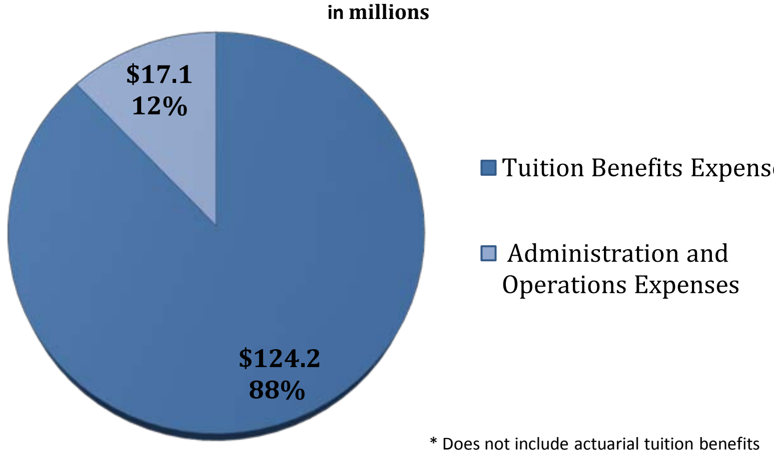


Table 3 provides a comparison of administrative and operating expenses between fiscal years 2013 and 2012.

### Table 3 – Enterprise Fund
### Plan Administration and Operations Expenses (in thousands)

| YEARS ENDED JUNE 30, | 2013 | 2012 | CHANGE |
|---|---|---|---|
| Personal Services | $ 7,929 | $ 7,375 | $ 554 |
| Contractual Services | 6,117 | 6,911 | (794) |
| Supplies & Materials | 47 | 57 | (10) |
| Depreciation | 498 | 290 | 208 |
| Rent, insurance, and other related charges | 122 | 103 | 19 |
| Expendable equipment | 397 | 446 | (49) |
| SOAR Virginia | 2,000 | 2,000 | - |
| Other | 19 | 6 | 13 |
| Admin. and Operating Expenses | $ 17,129 | $ 17,188 | $ (59) |

The 7.5 percent increase in personal services expense, is attributable in part to VA529 employees receiving a 3 percent salary bonus provided to all state employees in December 2012, as well as an increase in the number of VA529 employees in fiscal 2013. The 11.5 percent decrease in contractual services is primarily attributable to an operating transfer made to inVEST in the previous fiscal year. The operating transfer was reimbursed in this fiscal year and is reported in Other Revenue. The increase in other expenses is due an increase in promotional award expenses.

### Table 4 – Enterprise Fund
### prePAID Financial Position (in millions)

| As of JUNE 30, | 2013 | 2012 | CHANGE |
|---|---|---|---|
| **Assets**: | | | |
| Current assets | $ 131.2 | $ 114.3 | $ 16.9 |
| Investments | 2,089.3 | 1,935.4 | 153.9 |
| Other noncurrent assets | 174.1 | 188.1 | (14.0) |
| Total prePAID Assets | $ 2,394.6 | $ 2,237.8 | $156.8 |
| **Liabilities:** | | | |
| Current liabilities | $ 209.7 | $ 192.6 | $ 17.1 |
| Noncurrent liabilities | 1,980.0 | 1,982.8 | (2.8) |
| Total prePAID liabilities | $ 2,189.7 | $ 2,175.4 | $ 14.3 |
| **Change in prePAID net position** | $ 204.9 | $ 62.4 | $142.5 |

## Assets

Current assets increased by approximately $16.9 million from the previous year. The increase was primarily the result of several investment managers increasing their cash positions during the year.

Long-term investments increased by $153.9 million, or 8 percent. This increase was partially due to market conditions that positively impacted investment performance as well as the purchase of long-term investments. Other noncurrent assets decreased by $14.0 million, which was due to the decrease in the noncurrent portion of the tuition contributions receivable. This represents the decrease in the actuarially determined amount expected to be collected from contract holders of record in future years.

## Liabilities

Total tuition benefits payable, reflected in both current and noncurrent liabilities above, increased by $13.8 million, or approximately .63 percent. The total increase represents the change in the actuarial present value of the future tuition obligation. Changes in the present value of the future tuition benefit obligation can be attributed to the changes in the present value discount due to the passage of time, differences between actual experience and the actuarial assumptions used, and any modification of the actuarial assumptions. However, this increase is primarily due to new contracts sold.

## Actuarial Soundness

VA529's statute requires that it annually determine the actuarial soundness of prePAID. The purpose of the actuarial valuation is to assess the future value of VA529's assets and liabilities, which are discounted to reflect their present value.

During fiscal year 2013, prePAID's actuarial position, as calculated by VA529's actuary and reported in the 2013 Actuarial Valuation Report, improved from an actuarial surplus of $74.2 million to a surplus of $219.5 million. This improvement is mostly attributable to lower than expected tuition increases and higher than expected investment returns. Actuarial assumptions are discussed in Note 8 in the Notes to the Financial Statements.

The overall effect of the changes on the actuarial reserve is summarized in Table 5. A copy of the 2013 Actuarial Valuation Report may be obtained from VA529.

### Table 5
### prePAID Statement of Changes in Actuarial Reserve (dollars in millions)

| | | |
|---|---|---|
| Actuarial reserve at June 30, 2012 | $ | 74.2 |
| Interest on the reserve at 6.75% | | 5.0 |
| Investment gain (loss) | | 27.5 |
| Tuition gain (loss) | | 61.5 |
| Higher than expected actual account balances | | (7.3) |
| Sales of new contracts | | 10.5 |
| Administrative fee revenue from VA529 programs | | 25.9 |
| Change in expense assumptions | | 0.5 |
| Change in other assumptions | | 13.7 |
| Other gains | | 8.0 |
| Actuarial reserve at June 30, 2013 | $ | 219.5 |

VA529 prePAID's overall funded status, as calculated by the actuary, as of June 30, 2013 was 110%. Chart 3 provides prePAID's funded status since 2001.

**Chart 3**
**prePAID Actuarially Funded Percentage as of June 30th**

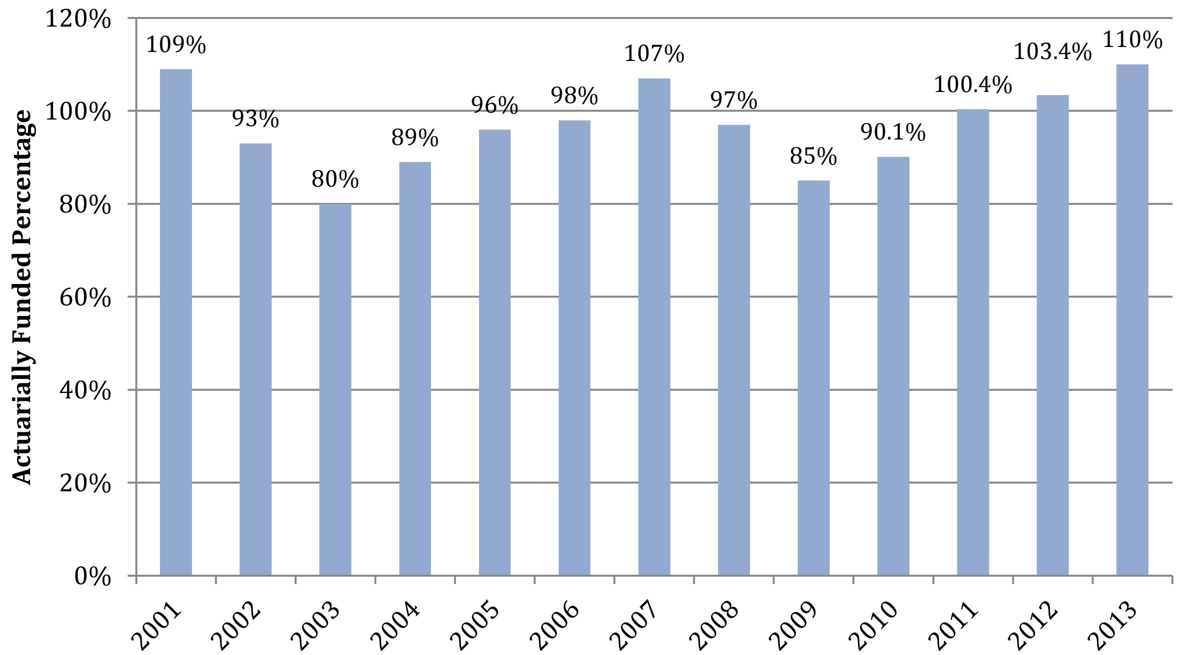



Table 6 represents the condensed Statement of Cash Flows for the Enterprise Fund for the fiscal years ended June 30, 2013 and 2012. VA529's year-end cash balance in the Enterprise Fund increased by $17.7 million primarily as a result of several investment managers increasing their cash positions pending asset transitions or further investment opportunities.

### Table 6 – Enterprise Fund
### Statement of Cash Flows (dollars in millions)

| As of June 30, | 2013 | 2012 |
|---|---|---|
| Cash provided (used) by: | | |
| Operating activities | $ 13.2 | $ 20.9 |
| Noncapital financing activity | (0.3) | (0.4) |
| Capital and related financing activities | (1.0) | (0.8) |
| Investing activities | 5.8 | (51.5) |
| Net increase (decrease) in cash | 17.7 | (31.8) |
| Cash – beginning of year | 57.5 | 89.3 |
| Cash – end of year | $ 75.2 | $ 57.5 |

The change in the amount reflected as investing activities for fiscal year 2013 is primarily attributable to an increase of realized gains booked by VA529's external investment managers during the fiscal year.

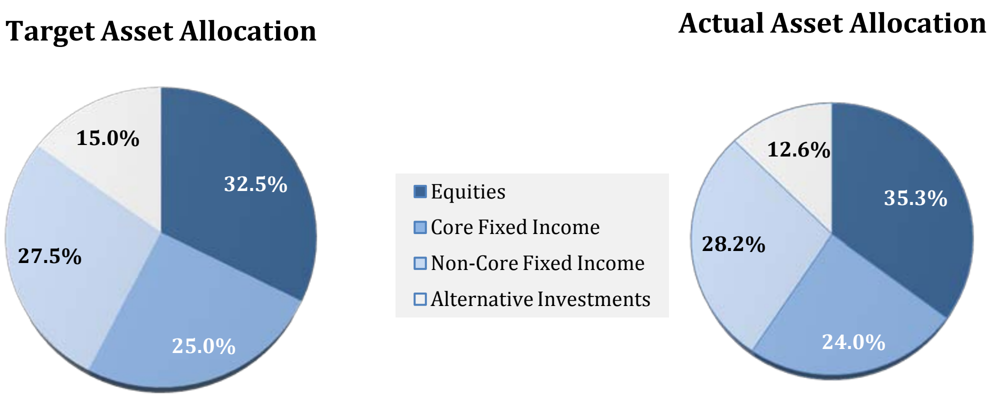
In December 2012, the Board revised its Investment Policies and Guidelines for prePAID and inVEST. The revisions were primarily related to updating applicable benchmarks. The overall asset allocation targets for prePAID, most recently revised in June 2009, did not change.

Since 2009, VA529, working with the Investment Advisory Committee and Board, has continued the transition process to the new target asset allocation in prePAID (see Chart 4). The transition is largely complete with the alternatives category steadily being brought towards target as VA529's private equity managers issue capital calls. Capital committed to private equity managers but not yet called is currently primarily held in the equities category and is largely invested in domestic equities.

In May 2013 the Investment Advisory Committee terminated Lord Abbett & Co., LLC, VA529's prePAID convertible bond manager, replacing them with two convertible bond managers, Advent Capital Management, LLC and Ferox Capital, LLP. As of June 30, 2013 the transition had yet to begin. In addition, the Committee engaged Shenkman Capital Management, Inc. to manage a senior secured bank loans strategy. This mandate was to be funded through a partial liquidation of VA529's investment in the Vanguard Total Bond Market Index Fund and the State Street TIPS Non-Lending Index Common Trust Fund. The transition and funding of these managers occurred in early fiscal 2014.

During fiscal 2013, the Investment Advisory Committee also engaged Commonfund as a private equity fund of funds manager for prePAID. A complete list of prePAID managers as of June 30, 2013 can be found in Appendix B.

**Chart 4**
**prePAID Asset Allocation as of June 30, 2013**




## Analysis of Fiduciary Fund (inVEST) Financial Activities

Contributions from inVEST participants increased from the previous year by approximately $44.5 million and there were more than 19,750 new inVEST accounts opened during the fiscal year. Contributions represent amounts received from new and existing account holders. Net income on inVEST investments increased by $146.0 million over the prior year due to improved market conditions compared to the prior year. As anticipated, overall disbursements to inVEST beneficiaries and institutions increased over the prior year by approximately 21.5 percent as more participants withdrew funds for higher education expenses.

During fiscal 2013, the Investment Advisory Committee closed the inVEST money market portfolio. Participants in the money market portfolio were automatically transferred to the stable value portfolio on December 31, 2012.

**Table 7**
**inVEST**
**Change in Fiduciary Net Position (dollars in millions)**

| Fiscal year ended June 30 | 2013 | 2012 | Change |
|---|---|---|---|
| Additions | $ 486.0 | $ 295.5 | $ 190.5 |
| Deductions | 144.8 | 117.8 | 27.0 |
| Net Increase | 341.2 | 177.7 | 163.5 |
| Net position held in trust, beginning | 1,960.7 | 1,784.8 | 175.9 |
| Net position held in trust, ending | $ 2,301.9 | $ 1,962.5 | $ 339.4 |

The difference in FY13 beginning and FY12 ending net position is due to a restatement of an overstated beginning balance in fiscal 2011 when VA529 converted to the Banner Finance accounting system. See Footnote 2 for additional information.

## CollegeAmerica and CollegeWealth

Assets under management in CollegeAmerica increased during the fiscal year increasing by approximately 18.4 percent from $32.9 billion to $39.0 billion. There were an additional 63,027 unique CollegeAmerica accounts at fiscal year end. A complete list of CollegeAmerica investment options as of June 30, 2013 can be found in Other Information.

Assets under management in CollegeWealth increased by 52.7 percent in fiscal year 2013, to more than $63.4 million at year end. The assets represented amounts held in savings instruments at the two participating banks (BB&T and Union First Market Bank) and were thus not subject to fair market value adjustments at year-end.

CollegeAmerica and CollegeWealth are presented as Other Information to VA529. Additional information on these programs can be found in this section of the report.

## Economic Factors and Outlook

VA529 continues to remain optimistic that its asset allocation and investment strategies will result in the prePAID portfolio meeting or exceeding performance expectations over the long-term. VA529 has assumed a long-term rate of return of 6.75 percent on the prePAID investments. As of June 30, 2013, the total return since inception was about 6.4 percent net of fees and reflected prePAID's 8.4 percent performance during fiscal 2013. Global and domestic equity and fixed income markets experienced gains from June 30, 2013 into fiscal 2014. Portfolio performance through the balance of fiscal 2014 will depend on many factors.

In assessing prePAID's financial condition and in pricing prePAID contracts, VA529 has projected that tuition and fee increases at Virginia's public higher education institutions will increase annually by approximately 7.5 percent for four-year and two-year institutions for fiscal years 2015 and thereafter. Changes in public education funding or changes in tuition models that result in tuition increases above VA529's projections would have an immediate, detrimental impact on VA529's outstanding long-term prePAID obligations. However, with the statutory requirement that institutions provide updated, long-term tuition projections, VA529 remains in a favorable position to prepare for future tuition and fee increases.

The performance of participants' inVEST and CollegeAmerica portfolios will depend on many of the same investment factors as those impacting prePAID. In inVEST, CollegeAmerica, and CollegeWealth, the participants rather than VA529 bear the risk of portfolio declines as a result of the market or other factors. As a result, no further information as to economic factors and outlook is provided.

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# **Financial** Statements

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VIRGINIA529
STATEMENT OF NET POSITION
ENTERPRISE FUND
As of June 30, 2013

| | Administration and Operations | prePAID | Total Enterprise |
|---|---|---|---|
| ASSETS | | | |
| Current assets: | | | |
| Cash and cash equivalents (Note 1E and 3) | $ 2,480,861 | $ 72,724,062 | $ 75,204,923 |
| Interest receivable | | 3,217,724 | 3,217,724 |
| prePAID contract payments receivable (Note 1G and 9) | | 54,289,408 | 54,289,408 |
| Prepaids | 11,543 | | 11,543 |
| Accounts receivable (Note 1H) | 9,745,081 | 856,586 | 10,601,667 |
| Total current assets | 12,237,485 | 131,087,780 | 143,325,265 |
| Noncurrent assets: | | | |
| Investments (Note 1E and 3) | - | 2,089,337,458 | 2,089,337,458 |
| prePAID contract payments receivable (Note 1G and 9) | - | 174,088,934 | 174,088,934 |
| Non-depreciable capital assets | - | - | - |
| Depreciable capital assets, net (Note 1J and 8) | 9,948,148 | - | 9,948,148 |
| Total noncurrent assets | 9,948,148 | 2,263,426,392 | 2,273,374,540 |
| Total assets | 22,185,633 | 2,394,514,172 | 2,416,699,805 |
| LIABILITIES | | | |
| Current liabilities: | | | |
| Accounts payable | 565,873 | | 565,873 |
| Program distributions payable | - | 324,609 | 324,609 |
| Due to program participants (Note 1K) | - | 247,800 | 247,800 |
| Tuition benefits payable (Note 7 and 9) | - | 209,131,385 | 209,131,385 |
| Compensated absences (Note 1L and 7) | 164,234 | - | 164,234 |
| Obligations under capital lease (Note 7) | 380,378 | - | 380,378 |
| Total current liabilities | 1,110,485 | 209,703,794 | 210,814,278 |
| Noncurrent liabilities: | | | |
| Tuition benefits payable (Note 7 and 9) | - | 1,979,946,957 | 1,979,946,957 |
| Compensated absences (Note 1L and 7) | 402,346 | - | 402,346 |
| Obligations under capital lease (Note 7) | 6,072,469 | - | 6,072,469 |
| Total noncurrent liabilities | 6,474,815 | 1,979,946,957 | 1,986,421,772 |
| Total liabilities | 7,585,300 | 2,189,650,751 | 2,197,236,051 |
| NET POSITION | | | |
| Net investment in capital assets | 3,495,301 | | 3,495,301 |
| Unrestricted | 11,105,033 | 204,863,421 | 215,968,454 |
| Total net position | $ 14,600,333 | $ 204,863,421 | $ 219,463,754 |

The accompanying notes are an integral part of this financial statement.

VIRGINIA529
STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN NET POSITION
ENTERPRISE FUND
For the Fiscal Year Ended June 30, 2013

| | Administration and Operations | prePAID | Total Enterprise |
|---|---|---|---|
| Operating revenues: | | | |
| Charges for sales and services | $ 40,999,341 | $ - | $ 40,999,341 |
| Interest, dividends, rents, and other investment income | - | 103,192,615 | 103,192,615 |
| Net increase in fair value of investments | - | 56,025,105 | 56,025,105 |
| prePAID contract payments | - | 116,182,014 | 116,182,014 |
| Actuarial prePAID contract payments (Note 9) | - | (16,417,311) | (16,417,311) |
| Other | 841,069 | 28 | 841,097 |
| Total operating revenues | 41,840,410 | 258,982,451 | 300,822,861 |
| Operating expenses: | | | |
| Personal services | 7,928,558 | - | 7,928,558 |
| Contractual services | 6,117,903 | - | 6,117,903 |
| Supplies and materials | 46,645 | - | 46,645 |
| Depreciation | 497,661 | - | 497,661 |
| Rent, insurance, and other related charges | 122,320 | - | 122,320 |
| Tuition benefits expense | - | 124,208,513 | 124,208,513 |
| Actuarial tuition benefits expense (Note 9) | - | 13,782,689 | 13,782,689 |
| Expendable equipment | 397,178 | - | 397,178 |
| SOAR Virginia (Note 12) | 2,000,000 | - | 2,000,000 |
| Other | 18,964 | - | 18,964 |
| Total operating expenses | 17,129,229 | 137,991,202 | 155,120,431 |
| Operating gain | 24,711,181 | 120,991,249 | 145,702,430 |
| Non-operating interest Expense | (139,627) | - | (139,627) |
| Transfers: | | | |
| Transfers to the General Fund of the Commonwealth | (290,901) | - | (290,901) |
| Operating transfer in (out) (Note 1) | (21,482,021) | 21,482,021 | - |
| Change in net position | 2,798,632 | 142,473,270 | 145,271,901 |
| Net position - July 1, 2012 | 11,801,700 | 62,390,152 | 74,191,852 |
| Net position - June 30, 2013 | $ 14,600,332 | $ 204,863,422 | $ 219,463,754 |

The accompanying notes are an integral part of this financial statement.

VIRGINIA529
STATEMENT OF CASH FLOWS
ENTERPRISE FUND
For the Fiscal Year Ended June 30, 2013

| | | |
|---|---|---|
| Cash flows from operating activities: | | |
| Receipts for sales and services | $ | 38,682,599 |
| Contributions Received | | 105,710,245 |
| Internal Activity - Payments to Other Funds | | (366,890) |
| Payments to Suppliers for Goods & Services | | (1,045,139) |
| Payments to Employees | | (7,948,343) |
| Other Operating Revenue | | 841,000 |
| Payments for Contractual Services | | (6,385,439) |
| Distributions | | (114,209,809) |
| Other Operating Expenses | | (2,022,230) |
| Net cash provided by (used for) operating activities | $ | 13,255,994 |
| Cash flows from noncapital financing activities: | | |
| Transfer to the General Fund of the Commonwealth | | (290,901) |
| Net cash provided by (used for) noncapital financing activities | $ | (290,901) |
| Cash flows from capital and related financing activities: | | |
| Acquisition of fixed assets | $ | (420,900) |
| Payment of Principal and Interest on Capital Leases | | (588,885) |
| Net cash provided by (used for) capital and related financing activities | $ | (1,009,785) |
| Cash flows from investing activities: | | |
| Purchase of investments | $ | (742,710,116) |
| Proceeds from sales or maturities of investments | | 645,289,886 |
| Interest income on cash, cash equivalents, and investments | | 103,192,615 |
| Net cash provided by (used for) investing activities | $ | 5,772,385 |
| Net increase in cash and cash equivalents | | 17,727,692 |
| Cash and cash equivalents - July 1, 2012 | | 57,477,229 |
| Cash and cash equivalents - June 30, 2013 | $ | 75,204,922 |
| Reconciliation of cash and cash equivalents: | | |
| Per the Statement of Net Position: | | |
| Cash and cash equivalents | $ | 75,204,922 |
| Cash and cash equivalents per the Statement of Cash Flows | $ | 75,204,922 |

| | |
|---|---|
| Reconciliation of operating income to net cash provided by operating activities: | |
| Operating gain | $ 145,702,430 |
| | |
| Adjustments to reconcile operating income to net cash provided by (used for) operating activities: | |
| Depreciation | 497,661 |
| Interest, dividends, rents and other investment income | (103,192,615) |
| Net increase in fair value of investments | (56,025,105) |
| Changes in assets and liabilities: | |
| (Increase) decrease in receivables | (2,644,389) |
| (Increase) decrease in tuition contributions receivable | 16,417,311 |
| (Increase) Decrease in Assets | (270) |
| Increase (decrease) in accounts payable | (1,080,885) |
| Increase (decrease) in amounts due to program participants | 218,118 |
| Increase (decrease) in current tuition benefits payable | 16,661,088 |
| Increase (decrease) in current compensated absences | (21,885) |
| Increase (decrease) current obligations under capital lease | (449,256) |
| Increase (decrease) in noncurrent tuition benefits payable | (2,878,399) |
| Increase (decrease) in noncurrent compensated absences | 52,190 |
| Increase (decrease) non current obligations under capital lease | - |
| | |
| Net cash provided by (used for) operating activities | $ 13,255,994 |
| | |
| Noncash investing, capital, and financing activities: | |
| The following transaction occurred prior to the statement of net position date: | |
| Change in fair value of investments | $ 56,025,105 |

The accompanying notes are an integral part of this financial statement.

VIRGINIA529
STATEMENT OF FIDUCIARY NET POSITION
PRIVATE-PURPOSE TRUST FUND
Virginia529 inVEST
As of June 30, 2013

| | |
|---|---|
| Assets: | |
| Cash and cash equivalents (Note 1E and 3) | $ 29,425,682 |
| Receivables: | |
| Interest and dividends | 1,553,898 |
| Accounts Receivable | 979 |
| Investments: | |
| Bonds | 67,942,149 |
| Mutual funds - Non Index | 982,647,208 |
| Mutual funds - Index | 707,786,807 |
| Stable Value | 447,568,423 |
| Equities | 69,724,424 |
| Total investments | 2,275,669,011 |
| Total assets | 2,306,649,571 |
| Liabilities: | |
| Accounts payable | 426,859 |
| Due to program participants (Note 1K) | 2,982,020 |
| Program distributions payable | 1,376,034 |
| Total liabilities | 4,784,913 |
| Assets held in trust for program participants | $ 2,301,864,658 |

The accompanying notes are an integral part of this financial statement.

Virginia529
STATEMENT OF CHANGES IN FIDUCIARY NET POSITION
PRIVATE-PURPOSE TRUST FUND
Virginia529 inVEST
For the Fiscal Year Ended June 30, 2013

| | |
|---|---|
| Additions: | |
| Contributions: | |
| From participants | $ 322,215,896 |
| Total contributions | 322,215,896 |
| Investment income: | |
| Net increase in fair value of investments | 91,922,887 |
| Interest, dividends, and other investment income | 76,979,118 |
| Other | (840,644) |
| Total investment income | 168,061,361 |
| Less: | |
| Investment expenses | (4,262,590) |
| Net investment income | 163,798,771 |
| Total additions | 486,014,667 |
| Deductions: | |
| Educational expense benefits | 130,489,632 |
| Shares redeemed | 13,967,839 |
| Other Expenses | 389,017 |
| Total deductions | 144,846,488 |
| Net increase | 341,168,179 |
| Assets held in trust for program: | |
| July 1, 2012, as restated (Note 2) | 1,960,696,479 |
| June 30, 2013 | $ 2,301,864,658 |

The accompanying notes are an integral part of this financial statement.

# **Notes** to the **Financial Statements**

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## 1. Summary of Significant Accounting Policies

The Virginia College Savings Plan (VA529), an independent agency of the Commonwealth of Virginia, was created in 1994 by the Virginia General Assembly and its enabling legislation is codified at §23-38.75 through §23-38.87:1 of the *Code of Virginia*, as amended. VA529 operates the Commonwealth's Internal Revenue Code (IRC) §529 qualified tuition plan, which offers four programs, Virginia529 prePAID (prePAID), Virginia529 inVEST (inVEST), CollegeAmerica and CollegeWealth.

prePAID is a defined benefit program, which offers contracts, at actuarially determined amounts, that provide for the future payment of undergraduate tuition for the normal full-time course load for students enrolled in a general course of study at any Virginia public higher educational institution and all mandatory fees required as a condition of enrollment of all students. The contract provisions also allow benefits to be used at in-state private or out-of-state institutions with payouts based on earnings and the amounts charged by Virginia's public higher education institutions. Calculations and payouts differ between in-state private and out-of-state institutions. prePAID has a limited enrollment period each year, and is open to children in the ninth grade or younger if the child or participant is a Virginia resident. Since inception, over 111,400 accounts have been opened, with 68,637 contracts remaining active at year-end. The program had total assets invested from contributions, net earnings and other revenue of approximately $2.1 billion as of June 30, 2013. The program invests contract payments to meet future obligations. Operating costs are paid from program earnings and other revenue. VA529 does not receive any general fund appropriations. VA529's enabling legislation provides that all moneys remaining in the enterprise fund at the end of a biennium shall not revert to the general fund. VA529 annually assigns net operating revenue to prePAID to support its funded status. The program's assets and income are exempt from federal, state, and local income taxation, except for taxes on unrelated business income. VA529's enabling legislation also provides that a sum sufficient appropriation be included by the Governor in his budget to cover current obligations of VA529, including prePAID's contractual obligations, in the event of a funding shortfall.

inVEST is a defined contribution savings program, which allows participants of all ages to save for qualified higher education expenses, including tuition and fees, at any qualified higher education institution by making contributions into the investment portfolio(s) of their choice. Participants are allowed to select from among 17 investment portfolios. One additional portfolio remains open in the inVEST program but is closed to new participants. inVEST accounts are subject to investment risks, including the possible loss of principal. The inVEST program is open year round and has no age or residency restrictions. inVEST began operation in December 1999. As of June 30, 2013, 200,326 accounts had been opened, with 157,118 accounts remaining active at year end. These accounts had a net asset value of approximately $2.3 billion as of June 30, 2013. Investment management fees and inVEST operating expenses are paid on a pro-rata basis by each inVEST account owner and vary according to the portfolio selected. inVEST accounts provide investors with the same federal and state tax benefits available to participants in the prePAID program.

CollegeAmerica, a broker-sold IRC §529 college savings option, is a defined contribution savings program and is administered by the American Funds pursuant to a contract using 38 of the American Funds mutual funds. CollegeWealth is also a defined contribution savings program under which participants invest in FDIC-insured savings products offered through participating banks. CollegeAmerica and CollegeWealth are presented as Other Information.

An eleven-member Board administers VA529, consisting of four ex-officio members and seven non-legislative citizens, four to be appointed by the Governor, one to be appointed by the Senate Committee on Rules, and two to be appointed by the Speaker of the House of Delegates. The ex-officio members are the Executive Director of the State Council on Higher Education for Virginia, the Chancellor of the Virginia Community College System, the State Treasurer, and the State Comptroller. The non-legislative citizen members shall have significant experience in finance, accounting, law or investment management. In order to assist the Board in fulfilling its fiduciary duty with the investment of VA529 assets; and in fulfilling its responsibilities relating to VA529's financial reporting processes and internal and financial controls; the Board has appointed an Investment Advisory Committee (IAC) and Audit and Actuarial Committee (A&AC), respectively. The IAC and A&AC are permanent advisory committees of the Board pursuant to §23-38.79:1 of the *Code of Virginia*, as amended. The Board has adopted charters that describe the purpose of the committees as well as their duties and responsibilities, composition and conduct of business.

A separate report is prepared for the Commonwealth of Virginia, which includes all agencies, boards, commissions, and authorities over which the Commonwealth exercises or has the ability to exercise oversight authority. VA529 is an integral part of the reporting entity of the Commonwealth of Virginia and is included in the basic financial statements of the Commonwealth.

The following is a summary of significant accounting policies employed by the VA529.

A. Basis of Presentation

The accompanying financial statements have been prepared in conformance with accounting principles generally accepted in the United States of America as prescribed by the Governmental Accounting Standards Board (GASB).

B. Reporting Entity

The accompanying financial statements report the financial position, changes in financial position and cash flows of VA529 as of and for the fiscal year ended June 30, 2013. For financial reporting purposes, VA529 includes all funds and entities over which VA529 is financially accountable and exercises oversight authority.

C. College Savings Systems (CSS)

College Savings Systems is the software development and technical services division of VA529, which was formed in 2004. VA529 has an agreement with Ellucian (formerly SunGard Higher Education) to maintain the College Savings Program (CSP) module of the Banner software suite. CSS provides record keeping software and technical services to other savings and prepaid qualified tuition plans including Virginia. As of June 30, 2013, CSS also provided services to Colorado, Maryland, Texas, and Washington.

VA529's contracts with the aforementioned states have two components; maintenance fees and fees for additional services. The maintenance fees are annual charges assessed to support the Banner CSP module and continued development thereof, and benefits all users/clients. The programming fees are assessed to the states when providing specific software programming changes, at their request, to enhance or change application, contract, transaction or distribution processing; customer web access; or make other system enhancements. The programming fees vary year-to-year based on user/client needs.

CSS fee revenue is included in the enterprise fund operating revenue. In accordance with the 2013 Appropriation Act, revenue from operations performed for programs outside of Virginia in fiscal 2013, exceeded all direct and indirect costs of providing the services.

D. Measurement Focus, Basis of Accounting, and Financial Statement Presentation

VA529 reports the activity of the prePAID program as an enterprise fund, which is a type of proprietary fund. Enterprise funds typically account for transactions related to resources received and used for financing self-supporting entities that offer products and services on a user-charge basis to external users. All operating expenses and all administrative fee revenue collected to support VA529 operations, including administrative revenue and expenses of inVEST, CollegeAmerica and CollegeWealth, are reflected in the enterprise fund.

VA529 reports the activity of the inVEST program as a private-purpose trust fund, which is a type of fiduciary fund. Private-purpose trust funds account for transactions of trust arrangements in which the principal and income benefit individuals, private organizations, or other governments.

The financial statements of the proprietary and fiduciary funds are reported using the economic resources measurement focus and the accrual basis of accounting. Revenues are recorded when earned and expenses are recognized when a liability is incurred, regardless of the timing of related cash flows.

Proprietary funds distinguish operating revenues and expenses from nonoperating items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with a proprietary fund's principal ongoing operations. Revenues and expenses not meeting this definition are reported as nonoperating. The principal revenues of VA529 are prePAID contract payments for program participants and investment income. Expenses of VA529 include tuition benefits expenses.

VA529's operating component is presented in a separate column, improving transparency in reporting operating funds and expenses. Operating revenues include administrative and other fees received from CSS as well as the prePAID, inVEST, CollegeAmerica, and CollegeWealth programs. Operating expenses include contractual and personal services.

All proprietary funds reported herein apply all applicable GASB principles per the Codification of Governmental Accounting and Financial Reporting Standards.

E. Cash Equivalents and Investments

Money market investments of VA529, which are deemed short-term, highly liquid investments, are reported at amortized cost. Long-term investments of VA529 are reported at fair value based upon quoted market prices, except for stable value investments, which are reported at contract value. Cash equivalents are investments with an original maturity of three months or less.

VA529 also participates in the Commonwealth's General Account pool, which is managed by the State Treasurer. These pooled investments are valued on an amortized cost basis. VA529 receives no additional distribution of unrealized gains or losses in the fair values of the pool's investments.

F. Use of Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

G. prePAID Contract Payments Receivable

prePAID contract payments receivable represent the actuarially determined present value of future payments due from contract holders. prePAID contract purchasers can elect to pay their contract in full via a lump sum payment or can pay over time. Customized financing options are available for purchasers electing to pay over time, allowing for payments to be spread over a period determined by the contract purchaser. Contracts must be paid in full prior to drawing benefits and accordingly the maximum number of years available for those purchasers electing to pay over time is approximately equal to the number of years between the beneficiary's current age and their expected college entrance date.

Approximately 56.44 percent of contract holders of outstanding (active) contracts as of June 30, 2013 had elected to pay over time.

H. Accounts Receivable

Accounts receivable reflected in VA529 operating column of the enterprise fund reflect amounts due to VA529 at June 30th for administrative and other services provided. These fees include second quarter administrative fees collected on behalf of VA529 for the CollegeAmerica and the CollegeWealth programs, as well as CSS service fees.

The American Funds pays VA529 an annual fee equal to ten basis points (.10 percent) of the average daily net asset value of the underlying funds held in CollegeAmerica up to $30 billion. The fee is reduced to nine basis points (.09 percent) for amounts in excess of $30 billion up to $60 billion with further reductions above $60 billion. This fee is calculated and accrued daily and paid to VA529 on a quarterly basis.

CollegeWealth banking partners, Branch Banking & Trust (BB&T) and Union First Market Bank (UFM), pay VA529 an annual fee equal to ten basis points (.10 percent) of the average daily assets held in 529 Bank Products issued by the Bank under the Program. These fees are calculated, accrued and paid to VA529 on a quarterly basis.

I. Administrative Expenses and Budget

VA529 is an independent state agency that does not receive a general fund appropriation from the Commonwealth of Virginia. However, VA529's expenditures, funded with non-general fund revenues, are included in the Commonwealth's Appropriation Acts and accordingly are subject to approval by the General Assembly and the Governor. The Board annually reviews and approves an operating budget. Operating expenses are primarily funded from administrative fee revenue. VA529 prepares and submits a biennial budget to the Commonwealth in compliance with biennial budgetary requirements (cash basis). Also, in accordance with its fiduciary responsibility, the Board reviews a comparison of actual versus budgeted expenses each quarter.

J. Capital Assets

Tangible assets are recorded at cost at the time of acquisition and are reported net of accumulated depreciation. VA529 capitalizes all property, plant, and equipment that have a cost or value greater than $5,000 and an expected useful life greater than two years. Depreciation is computed on a straight-line basis over the estimated useful life of the property, ranging from five to 40 years. Intangible assets with a value of $100,000 or greater are capitalized. These assets are depreciated over its useful life.

Intangible assets are nonfinancial in nature, lack physical substance and have an initial useful life extending beyond a single reporting period. These assets may be acquired by purchase or license, through non-exchange transactions or internally generated. These assets are also capital assets and adhere to the same policies of other property, plant and equipment. VA529 has one type of intangible asset, computer software. These assets were acquired through retail purchases and/or internally generated, and are reported in footnote 8, Capital Assets.

K. Amounts Due To Program Participants

Amounts due to program participants reflects accrued amounts due and payable at June 30, 2013 to participants for distributions to other qualified tuition programs, or for cancelled or overpaid prepaid contracts or savings accounts. In the Fiduciary Statement of Net Position, due to program participants also includes contributions received from participants that have yet to settle. These funds are classified as a liability until the settlement process is complete.

L. Accrued Leave Policy

Employees accrue annual leave at a rate of four to nine hours semi-monthly, depending on their length of service. The maximum accumulation is dependent upon years of service, but in no case may it exceed 54 days. All employees leaving the agency are paid for accrued vacation leave up to a maximum limit, not to exceed 36 days for 15-19 years of service and 42 days for 20 or more years of service, at their current earnings rate.

In conformance with Section C60 of GASB Codification, the monetary value of accumulated annual leave payable upon termination is included in the accompanying financial statements. The liability at June 30, 2013, was computed using salary rates effective at that date and represents vacation and compensatory leave earned up to the allowable ceilings, including the liability for VA529's share of Social Security and Medicare taxes on leave balances for which employees will be compensated.

Employees of VA529 have elected to participate in the Virginia Sickness and Disability Program (VSDP). The Virginia Retirement System (VRS) administers the program to provide income protection for absences due to sickness or disability. For employees hired after July 1, 2009, there is a one year waiting period for VSDP and coverage is not provided from the first day on the job.

After a seven calendar-day waiting period following the first incident of disability, eligible employees receive short-term disability benefits ranging from 60 to 100 percent of compensation up to a maximum of 125 work days, based upon months of State service. After a 180 calendar-day waiting period (125 work days of short-term disability) eligible employees receive long-term disability benefits equal to 60 percent of compensation until they return to work, until age 65, or until death.

Employees enrolled in this program are not eligible for disability retirement benefits under the VRS.

One employee, hired prior to January 1, 1999, opted to remain in the traditional sick leave program in which classified employees accrue five hours of leave for each pay period, regardless of the length of service. The employee is not covered under VSDP and remains eligible for disability retirement. Non-VSDP sick leave is payable upon termination of employment and is limited to 25 percent of the value accumulated or $5,000, whichever is less, under the Commonwealth of Virginia's sick leave pay-out policy for employees with five or more years of service.

All State agencies are required to contribute to the cost of providing disability benefits. Initial contribution requirements to fund the program were determined by the VRS actuary based on an estimate of the amount of the liability for disability benefits that would transfer from VRS to the new program. The contribution requirement was 1.78 percent of payroll for State employees. Further information about this program can be found in the Commonwealth of Virginia's Comprehensive Annual Financial Report.

M. prePAID – Investment in Real Estate

On February 15, 2008, VA529 established Aventura Holdings LLC, a limited liability company, for the purpose of acquiring and owning real estate. VA529 is the sole member of Aventura. On March 20, 2008 VA529's Board approved adding Aventura as an investment vehicle under prePAID and the purchase by Aventura Holdings of a 48,500 square foot office building in Chesterfield County, Virginia. On April 18, 2008, VA529 funded Aventura with $8.8 million for the purpose of acquiring real estate and Aventura acquired the office building on April 22nd.

The investment in Aventura is reflected in prePAID's assets at $6.55 million as of fiscal year end. The value was determined by a professional real estate appraisal in June 2013.

The building was originally leased to VA529 pursuant to a five-year Lease Agreement dated September 10, 2008. The Lease was renewed for another five years beginning July 1, 2013. Although the Lease Agreement does not meet the specific criteria for classification as a capital lease under the Codification of Governmental Accounting and Financial Reporting Standards, Section L20 - Leases, the Lease is shown as a capital lease in enterprise fund financial statements. The Lease is carried as a capital lease as VA529's intent is to renew the lease every five years and occupy the building for a time period greater than 75% of the asset's useful life. Accordingly, the financial statements reflect the lease obligation as a liability and the office building as an asset in enterprise fund's financial statements. See the Long-Term Liabilities Note 7 below for a description of the Lease Agreement.

## 2. Beginning Net Position Restatement (Fiduciary Fund)

The Fiduciary Fund's 2013 beginning net position of $1,960.7 million differs from the previous fiscal year's ending balance of $1,962.5 million. The difference resulted from an overstated beginning balance in fiscal 2011 when VA529 converted to the Banner Finance accounting system. This was primarily the result of Banner's treatment of contributions received by account owners but not yet applied to their respective accounts at year-end. Under the Banner Finance system these assets are matched with a liability (unapplied payments) until applied to the respective customer accounts. The liability account was understated in fiscal 2011. The inclusion of this liability to correct the balance resulted in the approximate $1.8 million adjustment to the beginning net position.

## 3. Cash, Cash Equivalents, and Investments

The Board of VA529 has established Statements of Investment Policy and Guidelines for VA529's investment programs in accordance with §23-38.80 of the *Code of Virginia*, as amended. This section of the *Code* requires the Board to discharge its duties in a manner which will provide the investment return and risk level consistent with the actuarial return requirements and cash flow demands of VA529 and conforming to all statutes governing the investment of VA529 funds. The Board shall exercise the judgment of care under the circumstances then prevailing, which persons of prudence, discretion, and intelligence exercise in the management of their own affairs, not in regard to speculation but to the permanent disposition of funds, considering the probable income as well as the probable safety of their capital when investing funds. In order to meet the return requirements, VA529's portfolio shall be invested in a broadly diversified investment portfolio including, but not limited to, domestic and foreign stocks, bonds, mutual funds and cash equivalent investments, which are defined as investments with an original maturity of three months or less. The Board's allocation target for the prePAID portfolio, at market value, is 32.5 percent equities, 25.0 percent core fixed income, 27.5 percent non-core fixed income, and 15 percent alternatives. The Board's allocation targets for the inVEST program vary according to the investment objective of each portfolio.

To assist the Board in fulfilling its fiduciary duty with the investment of VA529 assets, the Board has appointed an Investment Advisory Committee (IAC). The IAC provides the Board with objective and prudent investment advice on all matters related to the management of investments, within the parameters set by the Board's Statement of Investment Policy and Guidelines. The Board has also selected a group of 23 external managers and/or funds. See complete lists of Investment Managers in Appendices A and B. In addition, prePAID contractual payments and inVEST contributions received from customers are considered Commonwealth revenue and as a result must pass through the State Treasury. Prior to being moved to VA529's custodian, these monies along with other minor balances may be invested with the State Treasurer as part of the Commonwealth's General Account. VA529 receives no interest on balances held at the State Treasury and accordingly minimizes amounts held at Treasury.

The Board has authorized its partner, the American Funds, to offer a subset of their mutual funds to investors in CollegeAmerica. At fiscal year-end, 38 mutual funds were available through the CollegeAmerica program. The Board has oversight and review authority for the investment activity and operations of the CollegeAmerica program. The American Funds is required to seek renewed approval of the use of these mutual funds on an annual basis.

### Private Equity Investment Commitments

In fiscal year 2013, VA529 extended investment commitments under limited partnership agreements for private equity investments in prePAID. At June 30, 2013, VA529's investment commitments amounted to $129,661,056.

### Custodial Credit Risk

*Custodial Credit Risk – Deposits*: Custodial credit risk is the risk that in the event of a bank failure, VA529's deposits may not be returned to it. VA529 does not hold deposits for CollegeAmerica or CollegeWealth. All deposits of the prePAID and inVEST programs are secured in accordance with the provisions of the Virginia Security for Public Deposits Act, Section 2.2-4400, of the *Code of Virginia*.

*Custodial Credit Risk – Investments:* For an investment, custodial credit risk is the risk that, in the event of the failure of the counterparty, VA529 will not be able to recover the value of its investments or collateral securities that are in the possession of an outside party. At June 30, 2013, all investments of the prePAID and inVEST programs, except those investments in open-end mutual funds, private equity or hedge funds, were held in VA529's name by VA529's custodian, BNY Mellon Asset Servicing. Approximately 69 percent of total prePAID investments (reported as enterprise fund assets) and 75 percent of total inVEST investments (reported as a private-purpose trust fund) are invested in these vehicles. All investments of the CollegeAmerica program (also a private-purpose trust fund) are invested in mutual funds. Investments in open-end mutual funds, private equity and hedge funds are not directly exposed to custodial credit risk because their existence is not evidenced by individual securities.

## Interest Rate Risk – Fixed Income Securities

As of June 30, 2013, VA529 had fixed income investment securities held in prePAID and inVEST with the following maturities and effective duration. Effective duration is a measure of interest rate and price sensitivity that takes into account options, such as early call provisions, embedded in the securities. It is widely used in the management of fixed income portfolios as it quantifies the risk of interest rate changes.

| prePAID | | Investment Maturities (in Years) | | | | Duration |
|---|---|---|---|---|---|---|
| **Investment Type** | **Fair Value** | **Less than 1** | **1-5** | **6-10** | **More than 10** | **Effective Duration (years)** |
| Money Market Funds | $73,372,016 | $73,372,016 | - | - | - | - |
| Non-Agency Mortgage-Backed Securities | 6,162,932 | 1,166,940 | - | - | $4,995,992 | 2.19 |
| Asset-Backed Securities | 785,170 | 785,170 | - | - | - | 0.24 |
| Corporate Bonds | 193,936,523 | 2,673,362 | $106,194,774 | $80,924,880 | 4,143,507 | 4.72 |
| Convertible Securities | 154,056,743 | 55,267,896 | 51,381,239 | 10,240,090 | 37,167,518 | - |
| Bond Funds | 637,761,817 | - | 244,537,422 | 393,224,395 | - | 6.70 |
| Treasury and Agency Securities | 268,147 | 268,147 | - | - | - | 13.21 |
| Stable Value[1] | 87,111,539 | - | 87,111,539 | - | - | 3.55 |
| Total | **$1,153,454,887** | **$133,533,531** | **$489,224,974** | **$484,389,365** | **$46,307,017** | |

| inVEST | | Investment Maturities (in Years) | | | | Duration |
|---|---|---|---|---|---|---|
| **Investment Type** | **Fair Value** | **Less than 1** | **1-5** | **6-10** | **More than 10** | **Effective Duration (years)** |
| Money Market Funds | $27,309,125 | $27,309,125 | - | - | - | - |
| Corporate Bonds | 67,942,149 | 854,375 | $35,450,867 | $29,588,945 | $2,047,962 | 4.73 |
| Bond Funds | 377,021,836 | - | 232,348,717 | 144,673,119 | - | 6.11 |
| Stable Value[1] | 447,568,423 | - | 447,568,423 | - | - | 3.13 |
| Total | **$919,841,533** | **$28,163,500** | **$715,368,007** | **$174,262,064** | **$2,047,962** | |

[1]Reported at contract value

VA529's Statements of Investment Policy and Guidelines do not limit investment maturities as a means of managing its exposure to fair value losses arising from increasing interest rates. Although not an explicit requirement, duration of fixed income portfolios, if applicable, is expected to be within +/-20 percent of each portfolio's designated benchmark.

### Credit Risk of Fixed Income Securities

VA529's Statements of Investment Policy and Guidelines require its fixed income securities managers to invest in holdings which, on average, are comprised of high quality securities and may not include securities deemed to be below investment grade. Investment grade is generally defined as a rating of BBB or above by one of the three major rating agencies. This requirement does not apply to VA529's managers who are instructed to manage a specific high-yield fixed income investment strategy, whether in a separate account or as a dedicated allocation within a broader fixed income portfolio. VA529's fixed income investment securities held in prePAID and inVEST as of June 30, 2013 were rated by Standard & Poor's and/or Moody's and the ratings are presented in the charts entitled credit quality by investment type.

### Concentration of Credit Risk

At June 30, 2013, VA529 had no investment securities held in separately managed accounts in prePAID and inVEST in any one issuer that represented 5 percent or more of total investments.

### Mutual Fund Risks

At June 30, 2013, VA529 participated in a number of open-end domestic and foreign equity and fixed income mutual funds in prePAID and inVEST. These funds are subject to various investment risks, including the possibility that the value of the fund's portfolio holdings may fluctuate in response to events specific to the companies in which the fund invests, as well as economic, political or social events in the United States and abroad. Certain of the mutual funds may be subject to additional risks due to investments in a more limited group of sectors and industries than the broad market. Those funds with holdings issued by entities based outside the United States are subject to foreign securities risks, including currency fluctuations.

The value of and the income generated by fixed income securities held by certain of the mutual funds in which VA529 participates, may be affected by changing interest rates and credit risk assessments. Lower quality or longer maturity bonds may be subject to greater price volatility than higher quality or shorter maturity bonds.

Prospectuses for each of the mutual funds in which VA529 participates may be requested from the Virginia529, 9001 Arboretum Parkway, North Chesterfield, VA 23236, or at Virginia529.com. A prospectus may also be requested directly from each of the underlying fund managers. Prospectuses for each CollegeAmerica mutual fund offering may be obtained directly from the American Funds or from a financial adviser. Please see Supplementary and Other Information for a listing of prePAID, inVEST and CollegeAmerica mutual funds.

### Foreign Currency Risk

Foreign currency risk is the risk that changes in currency exchange rates will adversely affect the fair value, in U.S. dollars, of non-U.S. dollar denominated securities. At June 30, 2013 VA529 had indirect exposure to this risk through its investments in certain mutual funds and other pooled vehicles. More information relating to foreign currency risk in VA529's mutual fund investments can be found in each fund's prospectus.

## Counterparty Risk

Counterparty risk is the risk of loss arising from the failure of one party to a transaction to fulfill its contractual obligation to the other. VA529 has exposure to counterparty risk through its investments. Higher levels of this risk are attributable to VA529's investments in hedge funds, as these types of investments are subject to the potential usage of over the counter derivatives transactions. Other potential examples of risk for over the counter transactions may include transaction costs/inefficiencies/errors, fraud or reputation risk. As of June 30, 2013 approximately 8 percent of prePAID investments were invested in these vehicles.

| Rating Agency | inVEST Credit Quality by Investment Type | | | |
|---|---|---|---|---|
| **Standard & Poor's Quality Rating** | Corporate Bonds | Money Market Funds | Bond Funds | Stable Value |
| AAA | - | $27,309,125 | - | - |
| BBB+ | $306,450 | - | - | - |
| BBB | 888,892 | - | - | - |
| BBB- | 2,280,742 | - | - | - |
| BB+ | 10,869,224 | - | - | - |
| BB | 14,701,361 | - | - | - |
| BB- | 9,887,744 | - | - | - |
| B+ | 10,957,372 | - | - | - |
| B | 7,471,041 | - | - | - |
| B- | 3,903,492 | - | - | - |
| Less than B- | 3,575,192 | - | - | - |
| **Moody's Quality Rating** | | | | |
| Baa2 | 323,375 | - | - | - |
| Ba2 | 719,344 | - | - | - |
| Ba3 | 45,012 | - | - | - |
| | | | | |
| **Unrated**[1] | $2,012,908 | - | $377,021,836 | $447,568,423 |

[1]Securities have not been rated by either Moody's or Standard & Poor's

| Rating Agency | prePAID Credit Quality by Investment Type | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| **Standard & Poor's Quality Rating** | Non-Agency Mortgage Backed Securities | Asset-Backed Securities | Corporate Bonds | Convertibles | Money Market Funds | Bond Funds | Treasury and Agency Securities | Stable Value |
| AAA | $10,425 | - | - | - | $73,372,016 | - | - | - |
| AA+ | 2,682 | - | - | - | - | - | $268,147 | - |
| A+ | 194,381 | $442,520 | - | $1,610,000 | - | - | - | - |
| A | - | - | - | 4,304,690 | - | - | - | - |
| A- | - | 24,404 | - | 10,974,738 | - | - | - | - |
| BBB+ | 224,017 | - | $791,663 | 16,046,167 | - | - | - | - |
| BBB | - | - | 2,948,254 | 13,940,673 | - | - | - | - |
| BBB- | - | - | 8,326,477 | 9,811,397 | - | - | - | - |
| BB+ | - | - | 30,080,598 | 16,596,213 | - | - | - | - |
| BB | - | - | 39,301,571 | 1,899,610 | - | - | - | - |
| BB- | 377,642 | - | 27,114,019 | 6,894,947 | - | - | - | - |
| B+ | - | - | 33,391,843 | 9,672,406 | - | - | - | - |
| B | - | 64,543 | 21,623,740 | 3,963,315 | - | - | - | - |
| B- | - | - | 11,005,998 | 6,167,524 | - | - | - | - |
| Less than B- | 4,869,745 | $253,703 | 9,500,282 | 1,026,406 | - | - | - | - |
| **Moody's Quality Rating** | | | | | | | | |
| Baa2 | - | - | 995,000 | - | - | - | - | - |
| Ba2 | - | - | 2,083,276 | - | - | - | - | - |
| Ba3 | - | - | 110,796 | - | - | - | - | - |
| B2 | - | - | 144,797 | - | - | - | - | - |
| Less than B2 | 484,034 | - | - | - | - | - | - | - |
| | | | | | | | | |
| **Unrated**[1] | $6 | - | $6,518,209 | $51,148,657 | - | $637,761,817 | - | $87,111,539 |

[1]Securities have not been rated by either Moody's or Standard & Poor's

## 4. Investment Derivative Instruments

GASB Statement No. 53, *Accounting and Financial Reporting for Derivative Instruments*, requires that VA529 disclose its exposure to investment derivative instruments and certain investments described as synthetic guaranteed investment contracts.

Pursuant to the Statements of Investment Policy and Guidelines established for VA529's investment programs, investments in derivative securities are prohibited except where specifically permitted in the investment manager agreement for a separate account or prospectus for a fund. The Board may permit managers in certain asset classes to use derivatives consistent with the overall investment guidelines and objectives of that asset class. As of June 30, 2013, one separate account manager was permitted to use derivatives as shown in the table below.

| **Program** | **Manager** | **Asset Class** |
|---|---|---|
| prePAID | Prudential Investment Management, Inc. | High Yield Fixed Income |
| inVEST | Prudential Investment Management, Inc. | High Yield Fixed Income |

Pursuant to its investment management agreement, Prudential Investment Management may invest in derivatives for hedging, duration and cash management. The portfolio's exposure to derivatives, as measured on a net market value basis, is limited to 10 percent of the market value of the high yield account. At June 30, 2013, both the inVEST and prePAID Prudential accounts held credit default swaps. The following two tables contain information relating fair value, changes in fair value, notional value and credit risk relating to these derivative instruments. In aggregate, the fair value of these derivatives was $293,334 as of June 30, 2013. Concentration of credit risk relating to these derivatives did not equate to a significant percentage of the inVEST or prePAID program's total assets.

**Investment Derivatives – Credit Default Swaps**

| | **Changes in Fair Value** | | **Fair Value at June 30, 2013** | | |
|---|---|---|---|---|---|
| | **Classification** | **Amount** | **Classification** | **Amount** | **Notional Amount** |
| **Enterprise Fund** | Revenue | $117,611 | Investment | $230,137 | $5,375,000 |
| **Fiduciary Fund** | Revenue | $52,633 | Investment | $63,198 | $2,125,000 |

**Aggregate Credit Risk by Counterparty as of June 30, 2013**

| **Counterparty** | **Fair Value** | **Collateral** | **Credit Rating (S&P)** |
|---|---|---|---|
| Bank of America, N.A. | $263,594 | $351,456 | A |
| Barclays Bank PLC | 29,740 | 0 | A+ |
| Total | $293,334 | $351,456 | |

GASB Statement No. 53 defines stable value investment vehicles as synthetic guaranteed investment contracts. Stable value funds are invested in a high quality, diversified, intermediate term, fixed income portfolio that is protected against interest rate volatility by wrap or investment contracts from banks and insurance companies that guarantee the payment of benefits at book value (cost plus accrued interest) which enables the entire investment to be carried at its book value. VA529 utilizes stable value investments in both the prePAID and inVEST programs. VA529's stable value investments meet the definition of fully benefit-responsive synthetic guaranteed investment contracts and are reported at contract value. At June 30, 2013, VA529 had the following stable value investments outstanding in the respective programs as shown in the table below.

| Program | Wrap Provider | Notional Amount | Effective Date | Maturity Date | Crediting Rate |
|---|---|---|---|---|---|
| prePAID | ING Life & Annuity | $47,116,564 | 12/3/2002 | Open ended | 2.11% |
| | State Street Bank | 22,830,297 | 5/1/2002 | Open ended | 2.52% |
| | Transamerica Life Ins. | 17,164,676 | 3/5/2003 | Open ended | 3.08% |
| inVEST | Aviva Life & Annuity Co. | $158,145,019 | 5/1/2012 | Open ended | 1.15% |
| | ING Life & Annuity | 132,434,013 | 12/3/2002 | Open ended | 2.69% |
| | ING Life & Annuity | 108,524,564 | 10/5/2012 | Open ended | 0.78% |
| | State Street Bank | 48,464,824 | 5/1/2002 | Open ended | 2.80% |

At June 30, 2013, the fair value of the underlying investments for both prePAID and inVEST exceeded the book value (notional amount) of the wrap contracts. The book value of the wrap contracts provides a guaranteed minimum value that program participants would receive upon liquidation, and therefore it would have a separate fair value only in the circumstance that the fair value of the associated underlying investment pool fell below the book value of the wrap contracts. In that case the fair value of the wrap contracts would be the amount required to bring the total value of the stable value investments up to the book value of the wrap contracts. Therefore, there is no separate fair value associated with the wrap contracts as of June 30, 2013.

In the prePAID program, the fair value of the stable value investments at June 30, 2013, was $89,975,201.

| prePAID - Stable Value Components | Fair Value |
|---|---|
| Underlying Investments | $89,975,201 |
| Wrap Contracts | - |
| Total | $89,975,201 |

In the inVEST program, the fair value of the stable value investments at June 30, 2013, was $454,724,878.

| inVEST - Stable Value Components | Fair Value |
|---|---|
| Underlying Investments | $454,724,878 |
| Wrap Contracts | - |
| Total | $454,724,878 |

## 5. Securities Lending Transactions

A portion of the balance sheet line item Cash and Cash Equivalents represents cash held in the General Account of the Commonwealth and thus represents VA529's allocated share of securities received for securities lending transactions conducted therein. Information related to the credit risk of these investments and securities lending transactions held in the General Account is available on a statewide level in the Commonwealth of Virginia's Comprehensive Annual Financial

Report. The Commonwealth's policy is to record unrealized gains and losses in the General Fund in the Commonwealth's basic financial statements. When gains or losses are realized, the actual gains and losses are recorded by the affected agencies. VA529 receives no interest on balances held at the State Treasury. Accordingly, VA529 did not share in any gain or loss on securities lending transactions during fiscal 2013.

## 6. Commitments

VA529 is committed under operating leases for business equipment and building space rental. The equipment lease is for a three-year term. The space rental is for one year, automatically renewing each year. In both cases, VA529 expects that in the normal course of business, these leases will be renewed or replaced by similar leases. Rental expense for the fiscal year ended 2013 was $116,562.

VA529 has, as of June 30, 2013, the following total future minimum rental payments due under the above leases.

| Fiscal Year | Amount |
|---|---|
| 2014 | $ 88,987 |
| 2015 | 49,236 |
| 2016 | 29,360 |
| 2017 | 29,360 |
| 2018 | 29,360 |
| Total future minimum rental payments | $ 226,303 |

## 7. Long-Term Liabilities

Long-term liabilities include tuition benefits payable, capital lease payments, and compensated absences.

### A. Tuition Benefits Payable

This liability represents the actuarially determined present value of future obligations anticipated for payment of benefits and administrative expenses for prePAID.

### B. Capital Lease

On July 01, 2013, VA529 entered into the first 5-year extension of its Lease Agreement with Aventura Holdings, LLC under which it leases a 48,500 square foot office building. The Lease provides for two additional 5-year renewal options. Pursuant to the Lease, VA529 will make base rent payments as reflected below on an annual basis in advance, and will make additional rent payments on a quarterly basis in advance in an amount sufficient to pay building operating costs for the next quarter. Aventura has entered into an agreement with a property management company for the purpose of providing facilities maintenance, grounds keeping, custodial services, etc. The additional rent payments will cover operating costs incurred by Aventura under the property management agreement. At the end of each quarter, VA529 and Aventura reconcile expenses before funding operating expenses for the subsequent quarter.

| Base Rent Periods (1) | Annual Base Rent |
|---|---|
| July 1, 2013 – June 30, 2014 | $533,500 |
| July 1, 2014 – June 30, 2015 | $546,838 |
| July 1, 2015 – June 30, 2016 | $560,508 |
| July 1, 2016 – June 30, 2017 | $574,521 |
| July 1, 2017 – June 30, 2018 | $588,884 |

(1) 2014 rent at $11.00 psf with a 2.5% annual escalator.

Changes in long-term liabilities are shown below:

| Enterprise Fund | Beginning Balance (as restated) | Increases | Decreases | Ending Balance | Due Within One Year |
|---|---|---|---|---|---|
| Compensated absences | $ 536,275 | $ 364,623 | $ 334,318 | $ 566,580 | $ 164,234 |
| Tuition benefits payable | 2,175,295,653 | 111,993,441 | 98,210,752 | 2,189,078,342 | 209,131,385 |
| Capital lease obligation (*) | 6,902,105 | - | 449,257 | 6,452,848 | 380,378 |
| Total | $2,182,734,033 | $112,358,064 | $98,994,327 | $2,196,097,770 | $209,675,997 |

(*) The value of the capital lease extension has been recognized for the remainder of the useful life of the building. The long-term capital lease obligation of $6,452,848 reflects the principal portion of the projected remaining lease payments assuming they were calculated using a 40-year term, a 2.5% escalator, and discounted back using a 7% capitalization rate.

## 8. Capital Assets

The following schedule presents capital asset activity of VA529 for the year ended June 30, 2013.

| Enterprise Fund | Balance July 1, 2012 (as restated) | Increases | Decreases | Balance June 30, 2013 |
|---|---|---|---|---|
| Nondepreciable capital assets: | | | | |
| Software | $ 380,892 | $ - | $ 380,892 | $ - |
| Total non-depreciable capital assets | 380,892 | | 380,892 | - |
| Depreciable capital assets: | | | | |
| Equipment | 1,575,171 | 174,414 | - | 1,749,585 |
| Software | 411,088 | 627,378 | - | 1,038,466 |
| Building * | 8,800,000 | - | - | 8,800,000 |
| Total depreciable capital assets | 10,786,259 | 801,792 | - | 11,588,051 |
| Less accumulated depreciation: | | | | |
| Equipment | 806,560 | 186,590 | - | 993,150 |
| Software | 110,747 | 72,875 | - | 183,621 |
| Building | 224,936 | 238,196 | - | 463,132 |
| Total accumulated depreciation | 1,142,243 | 497,661 | - | 1,639,904 |
| Net depreciable capital assets | 9,644,016 | 304,131 | - | 9,948,147 |
| Total net capital assets | $ 10,024,908 | $ 304,131 | $ 380,892 | $ 9,948,147 |

* Asset purchased under a capital lease. The beginning balance has been adjusted to reflect the fair value of the building as of the original lease inception date.

** Amounts may not sum due to rounding

## 9. Summary of Actuarial Assumptions and Methods

VA529's statute requires that it annually determine the actuarial soundness of prePAID. VA529 has assumed that actuarially sound, when applied to prePAID, means that VA529 has sufficient assets (including the value of future installment payments due under current prePAID contracts) to cover the actuarially estimated value of the tuition obligations under those contracts, including any administrative costs associated with those contracts.

The two most significant assumptions used to prepare prePAID's actuarial valuation report are the rates of investment return and future tuition growth. The following assumptions were used in the actuarial valuation for June 30, 2013:

Investment Rate of Return: 6.75 percent per annum.

Projected Tuition Increase: The assumed tuition increase rates used in the current and prior year's valuations are outlined in the table below.

| | Universities | | Community Colleges | |
|---|---|---|---|---|
| | Current assumption | Prior assumption | Current assumption | Prior assumption |
| Fall 2014 | 7.5% | 7.5% | 7.5% | 7.5% |
| Fall 2015 and thereafter | 7.5% | 7.5% | 7.5% | 7.5% |

Attendance and Bias: It is assumed that 80 percent of beneficiaries will attend a public university in Virginia, 10 percent will attend a private university in Virginia and 10 percent will attend a university in another state. Weighted average tuition for four-year public universities in Virginia was adjusted with a 10 percent load to add a bias for attendance at more expensive schools. The highest tuition for a public university in Virginia was assumed to be 50 percent higher than weighted average tuition. Out-of-state students are assumed to receive a benefit equal to the payments made on the contract plus interest at the composite reasonable rate of return.

Utilization: It is assumed that participants will begin utilizing their contract at actuarially determined rates, and then redeem one year of tuition per year until the contract is depleted.

Expenses: The expenses included in the present value of future obligations are those relating to Annual Maintenance Expense per Contract of $52.39 and Annual Distribution Cost per Contract in Payment Status of $23.19. These expenses are developed by VA529 staff and are assumed to increase annually at the rate of inflation plus 0.5 percent.

The actuarial prePAID contract payments and the actuarial tuition benefits expense line items represent the annual accrual of contract payments receivable and the obligation for distribution expenses determined by the actuarial valuation. At June 30, 2013, the accrual of the actuarially determined prePAID contract payments receivable decreased over the prior year, which resulted in negative actuarial prePAID contract payments reported as a reduction in operating revenue.

**Actuarial Valuation Results**

| | 2013 | 2012 |
|---|---|---|
| prePAID Contract Payments Receivable | $228,378,342 | $ 257,360,763 |
| Present Value of prePAID Obligations Payable | $2,189,078,342 | $2,215,260,763 |

## 10. Retirement and Pension Plan

Employees of VA529 are employees of the Commonwealth of Virginia. The employees participate in a defined benefit pension plan administered by the Virginia Retirement System (VRS). The VRS also administers life insurance for employees and retirees. Information relating to these plans is available at the statewide level only in the Commonwealth of Virginia's Comprehensive Annual Financial Report. The Commonwealth, not VA529, has overall responsibility for determining contributions to these plans.

## 11. Risk Management

VA529 is exposed to various risks of loss related to torts; theft or, damage to, and destruction of assets; errors and omissions; non-performance of duty; injuries to employees; and natural disasters. VA529 participates in insurance plans maintained by the Commonwealth of Virginia. The state employee health care and worker's compensation plans are administered by the Department of Human Resource Management and the risk management insurance plans are administered by the Department of Treasury, Division of Risk Management. Risk management insurance includes property, general liability, faithful performance of duty bond, automobile, and air planes. VA529 pays premiums to each of these Departments for its insurance coverage. Information relating to the Commonwealth's insurance plans is available at the statewide level in the Commonwealth of Virginia's Comprehensive Annual Financial Report.

VA529's information technology disaster recovery site is provided through a co-location agreement. The co-location has a fully equipped network environment as well as multiple direct-access Internet feeds necessary to facilitate recovery of mission critical VA529 systems.

## 12. SOAR Virginia

VA529's Board approved the creation and funding of SOAR Virginia® as a pilot program in fiscal 2010. SOAR Virginia is an early commitment scholarship program created to inspire and assist high school students to reach their post-secondary education goals. To participate, eligible students pledge to meet program requirements. In return, participating students receive a range of assistance and accumulate scholarship support up to $2,000 to apply toward their post-secondary education expenses. SOAR Virginia is a unique program created by VA529 to further its mission to make college more affordable and accessible to all Virginians and is offered in partnership with local Virginia college access providers.

The Board approved initial funding of $2 million per fiscal year beginning in 2011 and continuing through 2014 into a inVEST account in the name of VA529 for the development of the pilot program. As of June 30, 2013, $6 million had been deposited in the SOAR account. Amounts deposited, plus earnings thereon, remain in the account until distributed. Amounts will be allocated to students once awarded pursuant to program rules. VA529 will not commit support in excess of amounts on-hand in the SOAR Virginia account. As of June 30, 2013, the SOAR Virginia account had a balance of $6.24 million. Details as to the number of students enrolled in the pilot program and amounts committed as of June 30, 2013 are shown below.

| Number of Students Enrolled (1) | Award Amounts Allocated to Enrolled Students | Additional Awards Enrolled Students May Receive | Total SOAR Commitment |
|---|---|---|---|
| 613 | $158,000 | $1,154,500 | $1,312,500 |

(1) Number of students that have completed a SOAR application and pledge, and have been admitted to and are currently enrolled in the program

## 13. Scholarship Program And Promotional Accounts

The VA529 scholarship program consists of prePAID and inVEST third party scholarship accounts (excluding SOAR Virginia) established to provide a range of benefits to future beneficiaries. The purpose of the program is to enable individuals, organizations, community groups, corporations, and trusts to make qualified charitable contributions, which are used to purchase prePAID and inVEST accounts for beneficiaries. VA529's scholarship program's mission is to work with community partners to make the dream of college a reality for deserving youth in Virginia.

In addition to scholarship accounts, VA529 awards prePAID or inVEST promotional accounts that do not specifically qualify as scholarships as defined by federal law. Like scholarship accounts, these accounts are funded by VA529, individuals, organizations, school groups, or other entities.

Active scholarship (excluding SOAR) and promotional accounts at June 30, 2013:

| **Program** | **Scholarship** | | **Promotional** | |
|---|---|---|---|---|
| | **Accounts** | **Value** | **Accounts** | **Value** |
| **inVEST** | 284 | $921,485 | 170 | $951,047 |
| **prePAID** | 25 | $463,956 | 24 | $375,080 |

prePAID value represents the cancellation value of accounts at June 30, 2013
inVEST value represents the aggregate market value of the investments in the portfolios at June 30, 2013

## 14. Unrelated Business Income Tax

As a qualified tuition program under IRC §529, VA529 is subject to tax on unrelated business income. VA529 invests in certain agreements and funds that may produce unrelated business income. As such, VA529 may pay taxes on unrelated business income. During fiscal year 2013 VA529 paid no taxes as there was no reportable unrelated business income during the prior fiscal year. VA529 will determine and pay its unrelated business income tax liability, if any, for fiscal 2013 after it receives all Schedule K-1s at the end of calendar 2013.

# **Supplementary** Information

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## APPENDIX A

## Mutual Funds by Program

### Virginia529 prePAID℠

| | |
|---|---|
| Aberdeen Asset Management, Inc. | Emerging Market Equity Fund |
| BlackRock, Inc. | T-Fund (Cash and Equivalents) |
| Capital Research & Management Co. | American Funds EuroPacific Growth Fund |
| Franklin Templeton Investments | Templeton Foreign Equity Series |
| The Vanguard Group, Inc. | Institutional Index Fund |
| The Vanguard Group, Inc. | Total Bond Market Index Fund |

### Virginia529 inVEST℠

| | |
|---|---|
| Aberdeen Asset Management, Inc. | Emerging Market Equity Fund |
| Capital Research & Management Co. | American Funds EuroPacific Growth Fund |
| Franklin Templeton Investments | Templeton Foreign Equity Series |
| Morgan Stanley Institutional Fund, Inc. | Institutional Global Real Estate Fund |
| Parnassus Investments | Equity Income Fund |
| Stone Harbor Investment Partners LP | Emerging Market Debt Fund |
| The Vanguard Group, Inc. | Institutional Index Fund |
| The Vanguard Group, Inc. | Small Cap Index Fund |
| The Vanguard Group, Inc. | LifeStrategy Growth Fund |
| The Vanguard Group, Inc. | LifeStrategy Moderate Growth Fund |
| The Vanguard Group, Inc. | LifeStrategy Income Fund |
| The Vanguard Group, Inc. | Total Stock Market Index Fund |
| The Vanguard Group, Inc. | Total Bond Market Index Fund |
| The Vanguard Group, Inc. | Total International Stock Index Fund |
| The Vanguard Group, Inc. | Inflation-Protected Securities Fund |
| The Vanguard Group, Inc. | REIT Index Fund |

## APPENDIX B

## Separate Account, Commingled Fund & Alternative Managers by Program

### Virginia529 prePAID℠

| Investment Manager | Investment Strategy |
|---|---|
| Adams Street Partners | Private Equity Fund of Funds |
| Aurora Investment Management, LLC | Market Neutral Hedge Fund of Funds |
| Commonfund | Private Equity Fund of Funds |
| Donald Smith & Co. | Small Cap Value Domestic Equity |
| Harmonic Capital Partners | Global Macro Hedge Fund |
| Invesco Advisers, Inc. | Stable Value Fixed Income |
| Lord Abbett & Co., LLC | Convertible Fixed Income |
| Private Advisors, LLC | Private Equity Fund of Funds |
| Prudential Investment Management, Inc. | High Yield Fixed Income |
| State Street Global Advisors | Indexed US Inflation Protected Securities |
| Stone Harbor Investment Partners LP | Emerging Market Debt |
| Thompson, Siegel & Walmsley, LLC | SMID Cap Value Domestic Equity |
| UBS Realty Investors, LLC | Private Real Estate |
| Wellington Management Co., LLP | Emerging Market Debt Blend |
| Westfield Capital Management Co., LP | Mid Cap Growth Domestic Equity |

### Virginia529 inVEST℠

| Investment Manager | Investment Strategy |
|---|---|
| Invesco Advisers, Inc. | Stable Value Fixed Income |
| Prudential Investment Management, Inc. | High Yield Fixed Income |
| Rothschild Asset Management | SMID Cap Value Domestic Equity |

## Appendix C
## Investment Details by Program as of June 30, 2013
### Virginia529 prePAID℠

| Investment Manager | Asset Class | Mutual Fund(s) (if applicable) | Aggregate Fair Value[3] | % of Total Fund[1] |
|---|---|---|---|---|
| **Equities** | | | | |
| Aberdeen Asset Management, Inc. | Emerging Market | Emerging Market Equity | $ 150,068,091 | 7.0% |
| Capital Research & Management Co. | International Core | American Funds EuroPacific Growth | 108,967,325 | 5.1% |
| Donald Smith & Co. | Small Cap Value | N/A | 57,857,730 | 2.7% |
| Franklin Templeton Investments | International Value | Templeton Foreign Equity Series | 109,725,659 | 5.1% |
| The Vanguard Group, Inc. | Large Cap Domestic Blend | Institutional Index | 135,576,160 | 6.3% |
| Thompson, Siegel & Walmsley, LLC | Small/Mid Cap Value | N/A | 70,028,604 | 3.3% |
| Westfield Capital Management Co., LP | Mid Cap Growth | N/A | 125,219,217 | 5.8% |
| *Total Equities* | | | *757,442,786* | *35.4%* |
| **Core Fixed Income** | | | | |
| BlackRock, Inc.[2] | Cash Equivalents | T-Fund | 797,400 | 0.0% |
| Invesco Advisers, Inc.[3] | Stable Value | N/A | 94,240,653 | 4.4% |
| State Street Global Advisors | Inflation Protected Securities | N/A | 203,710,582 | 9.5% |
| The Vanguard Group, Inc. | Intermediate Core Fixed Income | Total Bond Market Index | 211,792,613 | 9.9% |
| Treasurer of Virginia | Cash Equivalents | N/A | 1,832,906 | 0.1% |
| VA529 Transition Account | N/A | N/A | 763,435 | 0.0% |
| *Total Core Fixed Income* | | | *513,137,589* | *24.0%* |
| **Non-Core Fixed Income** | | | | |
| Lord Abbett & Co., LLC | Convertible Bonds | N/A | 167,807,970 | 7.8% |
| Prudential Investment Management, Inc. | High Yield Bonds | N/A | 210,693,276 | 9.8% |
| Stone Harbor Investment Partners LP | Emerging Markets Debt Blend | Emerging Markets Debt & Local Markets | 68,150,497 | 3.2% |
| Wellington Management Co., LLP | Emerging Markets Debt | N/A | 154,108,125 | 7.2% |
| *Total Non-Core Fixed Income* | | | *600,759,868* | *28.1%* |
| **Alternative Investments** | | | | |
| Adams Street Partners | Private Equity Fund of Funds | N/A | 12,203,780 | 0.6% |
| Aurora Investment Management, LLC | Hedge Fund of Funds | N/A | 125,587,487 | 5.9% |
| Aventura Holdings, LLC | Private Real Estate | N/A | 7,390,875 | 0.3% |
| Commonfund | Private Equity Fund of Funds | N/A | 584,561 | 0.0% |
| Harmonic Capital Partners | Hedge Fund | N/A | 47,002,938 | 2.2% |
| Private Advisors, LLC | Private Equity Fund of Funds | N/A | 15,194,150 | 0.7% |
| UBS Realty Investors, LLC | Private Real Estate | N/A | 62,056,613 | 2.9% |
| *Total Alternative Investments* | | | *270,020,404* | *12.6%* |
| **Grand Total** | | | *$2,141,360,647* | *100%* |

[1]May not total 100% due to rounding. [2]BlackRock, Inc. operating cash in the amount of $23,181,733 is not included in the total above. [3]Stable value assets shown at contract value.

## Investment Details by Program as of June 30, 2013

### Virginia529 inVEST℠

| Investment Manager | Asset Class | Mutual Fund (if applicable) | Aggregate Fair Value[1] |
|---|---|---|---|
| **Age-Based Evolving Portfolios** | | | |
| Aberdeen Asset Management, Inc. | Emerging Markets Equity | Emerging Market Equity Fund | $ 97,931,799 |
| Capital Research & Management Co. | International Core Equity | American Funds EuroPacific Growth | 95,377,585 |
| Franklin Templeton Investments | International Value Equity | Templeton Foreign Equity Series | 94,361,565 |
| Invesco Advisers, Inc. | Stable Value | N/A | 468,735,452 |
| Morgan Stanley Institutional Fund, Inc. | Global REITs | Institutional Global Real Estate Fund | 109,371,009 |
| Prudential Investment Management, Inc. | High Yield Bonds | N/A | 71,958,695 |
| Rothschild Asset Management | Small/Mid Cap Domestic Equity | N/A | 71,848,819 |
| Stone Harbor Investment Partners LP | Emerging Markets Debt | Emerging Market Debt Fund | 122,515,270 |
| The Vanguard Group, Inc. | Intermediate Core Fixed Income | Total Bond Market Index Fund | 211,405,834 |
| The Vanguard Group, Inc. | Large-Cap Domestic Equity Blend | Institutional Index Fund | 202,001,698 |
| The Vanguard Group, Inc. | Small Cap Domestic Equity Blend | Small Cap Index Fund | 49,186,969 |
| *Total Age-Based Evolving Portfolios* | | | *1,594,694,695* |
| **Static Portfolios** | | | |
| Parnassus Investments | Socially Responsible Large Cap Core Equity | Equity Income Fund | 8,489,496 |
| The Vanguard Group, Inc. | 80% Equities 20% Fixed Income | LifeStrategy Growth Fund | 281,083,718 |
| The Vanguard Group, Inc. | 60% Equities 40% Fixed Income | LifeStrategy Moderate Growth Fund | 127,371,878 |
| The Vanguard Group, Inc. | 20% Equities 80% Fixed Income | LifeStrategy Income Fund | 46,144,888 |
| The Vanguard Group, Inc. | Inflation Protected Securities | Inflation-Protected Securities Fund | 22,157,849 |
| The Vanguard Group, Inc. | Real Estate Investment Trust | REIT Index Fund | 24,414,477 |
| The Vanguard Group, Inc. | Intermediate Core Fixed Income | Total Bond Market Index Fund | 20,942,883 |
| The Vanguard Group, Inc. | International Equity | Total International Stock Index Fund | 49,175,552 |
| The Vanguard Group, Inc. | Domestic Equity Blend | Total Stock Market Index Fund | 128,501,545 |
| *Total Static Portfolios* | | | *708,282,286* |
| **Grand Total** | | | *$2,302,976,981* |

Cash held with the Treasurer of Virginia as well with BNY Mellon (custodian) in the amount of $2,117,711 is not included in the total above.

[1]Stable value assets shown at contract value

# **Other** Information

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## CollegeAmerica®

CollegeAmerica, a broker-sold IRC §529 college savings option, was launched on February 15, 2002. CollegeAmerica is a defined contribution savings program administered by Capital Research and Management Company, American Funds Distributors, Inc., and American Funds Service Company, Inc. (together, the American Funds) pursuant to a contract. The American Funds acts as program manager and provides all back office and operational services for the program. As a result of this structure, VA529's staff has minimal day-to-day administrative responsibility, other than program oversight and review. VA529 has contracted these services with American Funds through February 15, 2027.

As of June 30, 2013, 38 American Funds mutual funds were approved by VA529 and available through the program. A complete list is shown in the tables on the following pages. In June 2012 the Board approved the American Funds' new College Target Date Series comprised of seven funds. The Target Date funds became available during fiscal 2013 and ended the fiscal year with over $1.05 billion in aggregate assets. CollegeAmerica is available year round and has no age or residency restrictions. Accounts are subject to market risk, including the possible loss of principal. As of June 30, 2013, approximately 2.06 million unique active accounts were open with net assets in excess of $38.9 billion. American Funds defines unique active accounts as unique open account numbers at period end. Fees and expenses of the program are also paid on a pro-rata basis by each account owner and vary according to the fund and share class selected.

A separate audited report for each of the 38 funds offered in the CollegeAmerica program is published annually by the American Funds. Each of the funds has a different year ending date, so these audited reports are published throughout the year. An individual fund audit report includes that fund's results for all share classes offered in the fund, including the IRC §529 share classes created for the CollegeAmerica program. The individual fund reports are available in their entirety from the American Funds. A summary of the 529 Share Class Net Assets as of Fund Fiscal Year End and at June 30, 2013 for each fund are presented in the following charts.

## CollegeAmerica
## 529 Share Class Net Assets as of Fund Fiscal Year End (dollars and shares in thousands)

| Fund | Shares | Net Assets | Fiscal Year End |
|---|---|---|---|
| **Growth funds** | | | |
| AMCAP Fund® | 53,349 | $ 1,209,668 | 02/28/13 |
| EuroPacific Growth Fund® | 35,767 | 1,494,010 | 03/31/13 |
| The Growth Fund of America® | 166,098 | 5,373,371 | 08/31/12 |
| The New Economy Fund® | 10,152 | 287,905 | 11/30/12 |
| New Perspective Fund® | 51,788 | 1,550,991 | 09/30/12 |
| New World Fund® | 17,479 | 905,379 | 10/31/12 |
| SMALLCAP World Fund® | 26,753 | 1,031,434 | 09/30/12 |
| **Growth-and-income funds** | | | |
| American Mutual Fund® | 23,972 | 675,861 | 10/31/12 |
| Capital World Growth and Income Fund® | 86,663 | 3,172,898 | 11/30/12 |
| Fundamental Investors℠ | 40,292 | 1,641,152 | 12/31/12 |
| International Growth and Income Fund℠ | 3,970 | 127,112 | 06/30/13 |
| The Investment Company of America® | 70,212 | 2,113,215 | 12/31/12 |
| Washington Mutual Investors Fund℠ | 59,144 | 2,068,872 | 04/30/13 |
| **Equity-income funds** | | | |
| Capital Income Builder® | 50,033 | 2,638,327 | 10/31/12 |
| The Income Fund of America® | 91,921 | 1,618,704 | 07/31/12 |
| **Balanced funds** | | | |
| American Balanced Fund® | 153,333 | 3,123,917 | 12/31/12 |
| American Funds Global Balanced Fund℠ | 5,839 | 153,853 | 10/31/12 |
| **Bond funds** | | | |
| American High-Income Trust℠ | 46,584 | 520,895 | 09/30/12 |
| The Bond Fund of America℠ | 135,123 | 1,749,731 | 12/31/12 |
| Capital World Bond Fund® | 30,383 | 656,315 | 09/30/12 |
| Intermediate Bond Fund of America® | 44,145 | 608,916 | 08/31/12 |
| Short-Term Bond Fund of America℠ | 39,259 | 396,477 | 08/31/12 |
| U.S. Government Securities Fund℠ | 23,095 | 337,784 | 08/31/12 |
| American Funds Mortgage Fund℠ | 1,758 | 18,107 | 08/31/12 |
| **Money market fund** | | | |
| American Funds Money Market Fund® | 997,469 | 997,507 | 09/30/12 |
| **American Funds College Target Date Series funds** | | | |
| American Funds College 2015 Fund℠ | 2,764 | 27,687 | 10/31/12 |
| American Funds College 2018 Fund℠ | 3,228 | 32,211 | 10/31/12 |
| American Funds College 2021 Fund℠ | 2,888 | 28,686 | 10/31/12 |
| American Funds College 2024 Fund℠ | 2,085 | 20,586 | 10/31/12 |
| American Funds College 2027 Fund℠ | 1,430 | 14,051 | 10/31/12 |
| American Funds College 2030 Fund℠ | 679 | 6,653 | 10/31/12 |
| American Funds College Enrollment Fund℠ | 1,163 | 11,640 | 10/31/12 |
| **American Funds Portfolio Series℠ funds** | | | |
| American Funds Global Growth Portfolio℠ | 1,035 | 11,545 | 10/31/12 |
| American Funds Growth Portfolio℠ | 2,825 | 31,077 | 10/31/12 |
| American Funds Growth and Income Portfolio℠ | 4,924 | 53,525 | 10/31/12 |
| American Funds Balanced Portfolio℠ | 4,726 | 50,998 | 10/31/12 |
| American Funds Income Portfolio℠ | 2,234 | 23,571 | 10/31/12 |
| American Funds Preservation Portfolio℠ | 2,761 | 27,816 | 10/31/12 |

*Data compiled from American Funds audited fund statements*

## CollegeAmerica
## 529 Share Class Net Assets as of June 30, 2013 (dollars and shares in thousands)

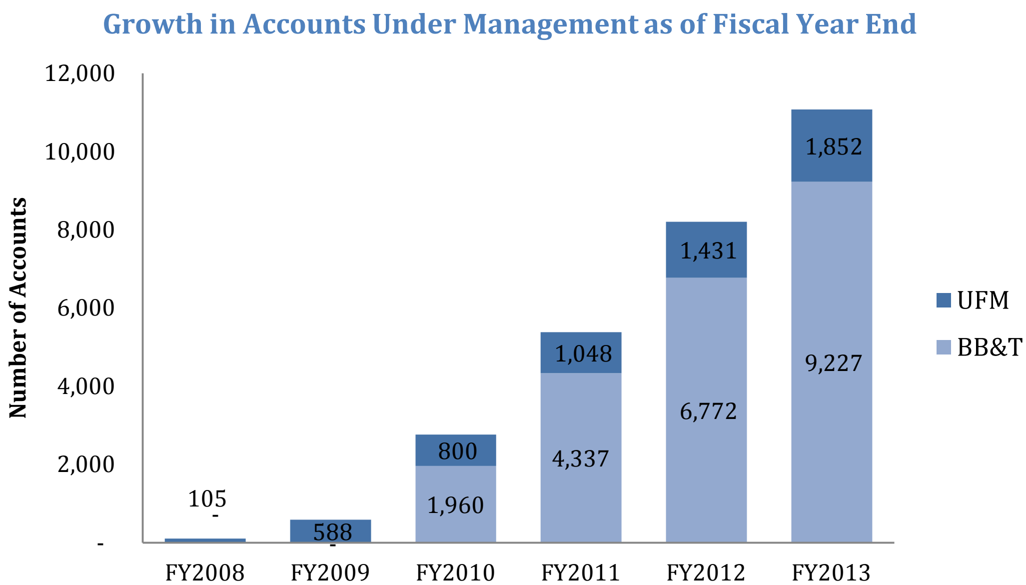
| Fund | Shares | Net Assets |
|---|---|---|
| **Growth funds** | | |
| AMCAP Fund® | 54,836 | $ 1,303,479 |
| EuroPacific Growth Fund® | 35,603 | 1,474,372 |
| The Growth Fund of America® | 164,280 | 6,232,911 |
| The New Economy Fund® | 11,382 | 364,982 |
| New Perspective Fund® | 51,768 | 1,724,361 |
| New World Fund® | 18,014 | 953,742 |
| SMALLCAP World Fund® | 27,168 | 1,174,638 |
| **Growth-and-income funds** | | |
| American Mutual Fund® | 25,002 | 787,176 |
| Capital World Growth and Income Fund® | 87,768 | 3,441,487 |
| Fundamental Investors℠ | 40,778 | 1,858,808 |
| International Growth and Income Fund℠ | 3,970 | 127,066 |
| The Investment Company of America® | 69,773 | 2,343,123 |
| Washington Mutual Investors Fund℠ | 59,186 | 2,092,397 |
| **Equity-income funds** | | |
| Capital Income Builder® | 51,207 | 2,789,000 |
| The Income Fund of America® | 95,777 | 1,820,152 |
| **Balanced funds** | | |
| American Balanced Fund® | 155,536 | 3,429,231 |
| American Funds Global Balanced Fund℠ | 7,211 | 199,627 |
| **Bond funds** | | |
| American High-Income Trust℠ | 49,035 | 545,273 |
| The Bond Fund of America℠ | 131,479 | 1,639,542 |
| Capital World Bond Fund® | 31,532 | 626,792 |
| Intermediate Bond Fund of America® | 45,188 | 607,773 |
| Short-Term Bond Fund of America℠ | 43,206 | 430,610 |
| U.S. Government Securities Fund℠ | 21,525 | 296,976 |
| American Funds Mortgage Fund℠ | 2,684 | 26,578 |
| **Money market fund** | | |
| American Funds Money Market Fund® | 1,115,891 | 1,115,891 |
| **American Funds College Target Date Series funds** | | |
| American Funds College 2015 Fund℠ | 17,387 | 171,513 |
| American Funds College 2018 Fund℠ | 22,555 | 230,245 |
| American Funds College 2021 Fund℠ | 20,554 | 212,928 |
| American Funds College 2024 Fund℠ | 16,062 | 167,983 |
| American Funds College 2027 Fund℠ | 11,180 | 118,522 |
| American Funds College 2030 Fund℠ | 8,554 | 91,972 |
| American Funds College Enrollment Fund℠ | 6,630 | 65,032 |
| **American Funds Portfolio Series℠ funds** | | |
| American Funds Global Growth Portfolio℠ | 3,574 | 43,926 |
| American Funds Growth Portfolio℠ | 7,234 | 89,812 |
| American Funds Growth and Income Portfolio℠ | 12,720 | 147,697 |
| American Funds Balanced Portfolio℠ | 10,015 | 115,685 |
| American Funds Income Portfolio℠ | 5,573 | 60,568 |
| American Funds Preservation Portfolio℠ | 5,794 | 57,105 |
| **Total Assets** | | **$ 38,978,975** |

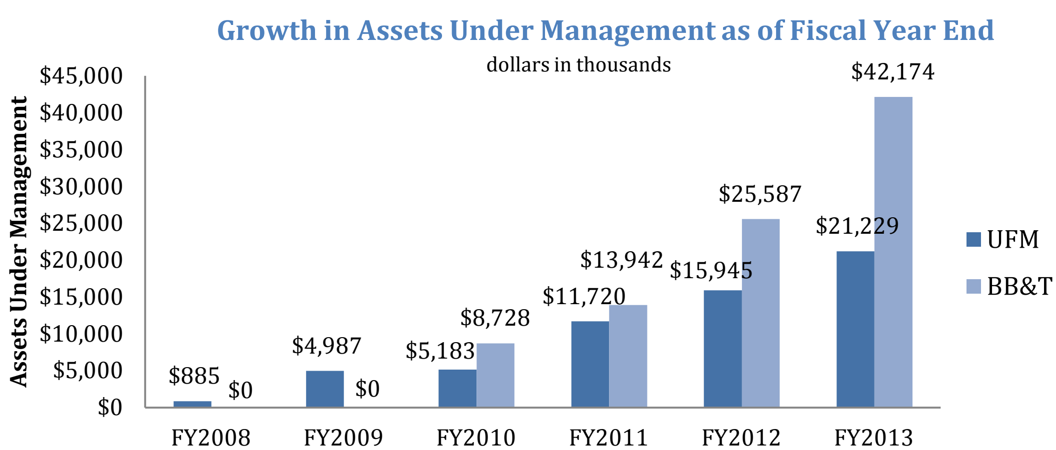
*Data compiled from American Funds reports*

### CollegeWealth®

CollegeWealth is VA529's FDIC-insured defined contribution 529 college savings program, provided in partnership with two participating financial institutions; BB&T and Union First Market Bank. Each CollegeWealth college savings account with a value up to $250,000 (when combined with any other holdings of an individual at any one bank) is insured by the FDIC. CollegeWealth began in the autumn of 2007 with Union First Market Bank (UFM) as VA529's first banking partner. In the autumn of 2009, VA529 added Branch Banking and Trust (BB&T) Corporation as a banking partner in an effort to significantly expand the availability of CollegeWealth within and outside of the Commonwealth. The partnership made CollegeWealth available throughout Virginia and across the country. As of June 30, 2013 there were 11,079 unique active accounts with net assets in excess of $63 million. Unique active accounts represent all active accounts at period end. The net assets represented amounts held in savings instruments at the participating banks and were thus not subject to fair market value adjustments at year end.

Since its inception, the CollegeWealth program has continued to grow. The charts below provide details on the growth in the number of accounts and assets for the program.



**VIRGINIA COLLEGE SAVINGS PLAN**
N. Chesterfield, Virginia