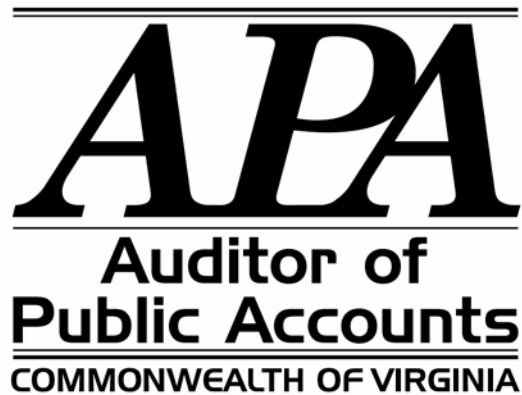


VIRGINIA RETIREMENT SYSTEM

**REPORT ON AUDIT
FOR THE YEAR ENDED
JUNE 30, 2006**



AUDIT SUMMARY

Our audit of the Virginia Retirement System for the year ended June 30, 2006, found:

- the financial statements are presented fairly, in all material respects;
- no instances of noncompliance with material laws and regulations or other matters that are required to be reported;
- one matter we consider a reportable condition; however, we do not consider this matter to a material weakness in internal controls; and
- a reportable condition from the prior year audit that is repeated in this report.

Our audit finding again includes a recommendation to update their business impact analysis and risk assessment. Although we understand that the Virginia Retirement System is in the process of performing this update, it was not complete prior to the date of this report. We discuss this recommendation in the section entitled "Internal Control Finding and Recommendation."

The Virginia Retirement System publishes an annual report that contains their financial statements and required disclosures. The Virginia Retirement System expects to publish their report by the end of November 2006.

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INTERNAL CONTROL FINDING AND RECOMMENDATION

Update Business Impact Analysis and Risk Assessment

As noted in our prior audit report, the Virginia Retirement System (System) last updated their business impact analysis and risk assessment in December 2000. The System's policy requires that they update the assessment every three to five years, or as necessary. Since their last update, the System has added a new computer center, which is not included or analyzed in the documents.

Without a current risk assessment, the System does not have a documented record of their present risks and the measures taken to minimize those risks. Although the System informally assesses risk regularly, the formal risk assessment process creates a record for succession planning. The addition of new systems, changes in location or ownership of systems, and other factors change the risks and also the priority of systems during disaster recovery.

The System's fiscal year 2007 budget includes funding for a comprehensive review and update of their Business Continuity Plan, including a risk and cost-benefit analysis. We understand that the System is actively updating their plans and analyses as of the date of this report. We recommend that the System finish updating their business impact analysis, risk assessment, and business continuity plan during fiscal year 2007 and continue to update it in the future as required by their policy.



Commonwealth of Virginia

Walter J. Kucharski, Auditor

Auditor of Public Accounts
P.O. Box 1295
Richmond, Virginia 23218

October 20, 2006

The Honorable Timothy M. Kaine
Governor of Virginia

The Honorable Thomas K. Norment, Jr.
Chairman, Joint Legislative Audit
and Review Commission

Board of Trustees
Virginia Retirement System

INDEPENDENT AUDITOR'S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS

We have audited the basic financial statements of the **Virginia Retirement System** as of and for the years ended June 30, 2006 and 2005, and have issued our report thereon dated October 20, 2006. Our report on the financial statements is included in the Comprehensive Annual Financial Report issued by the Virginia Retirement System. 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.

Internal Control over Financial Reporting

In planning and performing our audit, we considered the Virginia Retirement System's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide an opinion on the internal control over financial reporting. However, we noted a certain matter involving the internal control over financial reporting and its operation that we consider to be a reportable condition. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over financial reporting that, in our judgment, could adversely affect the Virginia Retirement System's ability to record, process, summarize, and report financial data consistent with the assertions of management in the financial statements. The reportable condition, entitled "Update Business Impact Analysis and Risk Assessment" is described in the section titled "Internal Control Finding and Recommendation."

A material weakness is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by error or fraud in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. However, we believe that the reportable condition described above is not a material weakness.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Virginia Retirement System's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under Government Auditing Standards.

Status of Prior Findings

The Virginia Retirement System has not taken adequate corrective action with respect to the previously reported finding "Update Business Impact Analysis and Risk Assessment." Accordingly, we included this finding in the section entitled "Internal Control Finding and Recommendation."

The "Independent Auditor's Report on Internal Control Over Financial Reporting and on Compliance and Other Matters" is intended solely for the information and use of the Governor and General Assembly of Virginia, Board of Trustees and management, and is not intended to be and should not be used by anyone other than these specified parties. However, this report is a matter of public record and its distribution is not limited.

EXIT CONFERENCE

We discussed this report with management at an exit conference held on October 25, 2006.

AUDITOR OF PUBLIC ACCOUNTS

KKH:sk
sk: 46



November 1, 2006

MEMORANDUM

TO: Walter J. Kucharski
Auditor of Public Accounts

FROM: Robert P. Schultze
Director

SUBJECT: Response to APA's - VRS Report on Audit for the Year Ended June 30, 2006

Please consider this as VRS' response to APA's management point regarding an update to our business impact analysis and risk assessment. The management point as written in the report is restated as follows:

Update Business Impact Analysis and Risk Assessment:

As noted in our prior audit report, the Virginia Retirement System (System) last updated their business impact analysis and risk assessment in December 2000. The System's policy requires that they update the assessment every three to five years, or as necessary. Since their last update, the System has added a new computer center, which is not included or analyzed in the documents.

Without a current risk assessment, the System does not have a documented record of their present risks and the measures taken to minimize those risks. Although the System informally assesses risk regularly, the formal risk assessment process creates a record for succession planning. The addition of new systems, changes in location or ownership of systems, and other factors change the risks and also the priority of systems during disaster recovery.

The System's fiscal year 2007 budget includes funding for a comprehensive review and update of their Business Continuity Plan, including a risk and cost-benefit analysis. We understand that the Virginia Retirement System is actively updating their plans and analyses as of the date of this report. We recommend that the System finish updating their business impact analysis, risk assessment, and business continuity plan during fiscal year 2007 and continue to update it in the future as required by their policy.

VRS Response:

In November 2005, our response to the APA Report on Audit for the Year Ended June 30, 2005 acknowledged that a formal risk assessment update had not been completed since December 2000. VRS further noted that funds for a risk assessment update were included in the FY 2007 budget, and that update process would begin once funds were available on July 1, 2006.

VRS issued a request for services to the vendor community on July 17, 2006, and a contract was issued five weeks later. Our vendor worked closely with VRS staff to complete an update of the risk assessment that included the following:

- mapping all essential VRS functions and supporting business processes
- examining all VRS facilities
- interviewing business process experts and IT/IS staff who manage the technology systems that support key processes
- developing recovery alternatives and recommendations

A draft of the report was delivered on October 24, and the contractor is now incorporating VRS feedback. A final report should be issued in early November.

If you have any questions concerning the above item, please call me at 344-3120.

c: VRS Board of Trustees

VIRGINIA RETIREMENT SYSTEM

BOARD MEMBERS

As of June 30, 2006

Paul W. Timmreck
Chairman

John M. Albertine
Vice Chairman

A. Marshall Acuff, Jr.	Edwin T. Burton, III
J. Douglas Conway, Jr.	Judith Ewell
Palmer P. Garson	Vernard W. Henley

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Robert P. Schultze
Director