

ILLINOIS STATE BOARD OF INVESTMENT
(An Internal Investment Pool of the State of Illinois)

Compliance Examination

Year ended June 30, 2012

Performed as Special Assistant
Auditors for the Auditor General,
State of Illinois

ILLINOIS STATE BOARD OF INVESTMENT
 (An Internal Investment Pool of the State of Illinois)

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Financial Statement Report: The Agency's financial statement report for the year ended June 30, 2012, which includes the independent auditors' report, management discussion and analysis, basic financial statements and notes and the independent auditors' report on internal control over financial reporting and on compliance and other matters based on an audit of basic financial statements performed in accordance with <i>Government Auditing Standards</i> has been issued separately.	
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ILLINOIS STATE BOARD OF INVESTMENT
(An Internal Investment Pool of the State of Illinois)

Agency Officials

Executive Director	Mr. William R. Atwood
Deputy Executive Director	Ms. Katherine A. Spinato
Chief Fiscal Officer	Ms. Adanna Ene
Chief Financial Officer/Investment Portfolio Accounting Officer	Ms. Alise White
General Counsel/Chief Compliance Officer	Ms. Linsey J. Schoemehl

Illinois State Board of Investment Office is located at:

180 N. LaSalle Street
Suite 2015
Chicago, Illinois 60601



ILLINOIS STATE BOARD OF INVESTMENT

180 North LaSalle Street, Suite 2015
Chicago, Illinois 60601
(312)793-5718

January 28, 2013

McGladrey LLP
20 N. Martingale Road, Suite 500
Schaumburg, IL 60173

Ladies and Gentlemen:

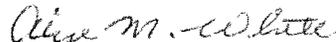
We are responsible for the identification of, and compliance with, all aspects of laws, regulations, contracts, or grant agreements that could have a material effect on the operations of the Illinois State Board of Investment (ISBI). We are responsible for and we have established and maintained an effective system of internal controls over compliance requirements. We have performed an evaluation of ISBI's compliance with the following assertions during the year ended June 30, 2012. Based on this evaluation, we assert that during the year ended June 30, 2012, ISBI has materially complied with the assertions below.

- A. ISBI has obligated, expended, received, and used public funds of the State in accordance with the purpose for which such funds have been appropriated or otherwise authorized by law.
- B. ISBI has obligated, expended, received, and used public funds of the State in accordance with any limitations, restrictions, conditions, or mandatory directions imposed by law upon such obligation, expenditure, receipt or use.
- C. ISBI has complied, in all material respects, with applicable laws and regulations, including the State uniform accounting system, in its financial and fiscal operations.
- D. The State revenues and receipts collected by ISBI are in accordance with applicable laws and regulations and the accounting and recordkeeping of such revenues and receipts is fair, accurate, and in accordance with law.
- E. The money or negotiable securities or similar assets handled by ISBI on behalf of the State or held in trust by ISBI have been properly and legally administered, and the accounting and recordkeeping relating thereto is proper, accurate, and in accordance with law.

Very truly yours,

ILLINOIS STATE BOARD OF INVESTMENT


William A. Wood
Executive Director


Alise White
Acting Deputy
Executive Director


Linsey J. Schoemehl
General Counsel/ Chief
Compliance Officer

ILLINOIS STATE BOARD OF INVESTMENT
 (An Internal Investment Pool of the State of Illinois)

Compliance Report

Summary

Year ended June 30, 2012

The compliance testing performed during this examination was conducted in accordance with *Government Auditing Standards* and in accordance with the Illinois State Auditing Act.

Accountants' Reports

The Independent Accountants' Report on State Compliance, on Internal Control over Compliance, and on Supplementary Information for State Compliance Purposes does not contain scope limitations, disclaimers, or other significant nonstandard language.

Summary of Findings

	<u>Current Report</u>	<u>Prior Report</u>
Number of:		
Findings	-	-
Repeated findings	-	-
Prior recommendations implemented or not repeated	-	1

Details of findings are presented in a separate section of the report.

<u>Item No.</u>	<u>Page</u>	<u>Description</u>	<u>Finding Type</u>
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FINDINGS (GOVERNMENT AUDITING STANDARDS)

None

FINDINGS (STATE COMPLIANCE)

The following findings which are reported as current findings relating to *Government Auditing Standards* also meet the reporting requirements for State Compliance.

None

PRIOR FINDING NOT REPEATED

None

Exit Conference

In correspondence received from the Illinois State Board of Investment on January 15, 2013, ISBI elected to waive a formal exit conference.



**Independent Accountants' Report on State Compliance,
on Internal Control over Compliance, and on
Supplementary Information for State Compliance Purposes**

Honorable William G. Holland
Auditor General
State of Illinois

Board of Trustees
Illinois State Board of Investment

Compliance

As Special Assistant Auditors for the Auditor General, we have examined the Illinois State Board of Investment's (Board) and its investment trust fund, the Illinois Power Agency Trust Fund, (collectively referred to as "ISBI") compliance with the requirements listed below, as more fully described in the Audit Guide for Financial Audits and Compliance Attestation Engagements of Illinois State Agencies (Audit Guide) as adopted by the Auditor General, during the year ended June 30, 2012. The management of ISBI is responsible for compliance with these requirements. Our responsibility is to express an opinion on ISBI's compliance based on our examination.

- A. ISBI has obligated, expended, received, and used public funds of the State in accordance with the purpose for which such funds have been appropriated or otherwise authorized by law.
- B. ISBI has obligated, expended, received, and used public funds of the State in accordance with any limitations, restrictions, conditions, or mandatory directions imposed by law upon such obligation, expenditure, receipt, or use.
- C. ISBI has complied, in all material respects, with applicable laws and regulations, including the State uniform accounting system, in its financial and fiscal operations.
- D. The State revenues and receipts collected by ISBI are in accordance with applicable laws and regulations and the accounting and recordkeeping of such revenues and receipts is fair, accurate, and in accordance with law.
- E. Money or negotiable securities or similar assets handled by ISBI on behalf of the State or held in trust by ISBI have been properly and legally administered and the accounting and recordkeeping relating thereto is proper, accurate, and in accordance with law.

Our examination was conducted in accordance with attestation standards established by the American Institute of Certified Public Accountants; the standards applicable to attestation engagements contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; the Illinois State Auditing Act (Act); and the Audit Guide as adopted by the Auditor General pursuant to the Act; and, accordingly, included examining, on a test basis, evidence about ISBI's compliance with those requirements listed in the first paragraph of this report and performing such other procedures as we considered necessary in the circumstances. We believe that our examination provides a reasonable basis for our opinion. Our examination does not provide a legal determination on ISBI's compliance with specified requirements.

In our opinion, ISBI complied, in all material respects, with the requirements listed in the first paragraph of this report during the year ended June 30, 2012.

Internal Control

Management of ISBI is responsible for establishing and maintaining effective internal control over compliance with the requirements listed in the first paragraph of this report. In planning and performing our examination, we considered ISBI's internal control over compliance with the requirements listed in the first paragraph of this report as a basis for designing our examination procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with the Audit Guide, issued by the Illinois Office of the Auditor General, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of ISBI's internal control over compliance.

A deficiency in an entity's internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with the requirements listed in the first paragraph of this report on a timely basis. *A material weakness in an entity's internal control over compliance* is a deficiency, or combination of deficiencies, in internal control over compliance such that there is a reasonable possibility that material noncompliance with a requirement listed in the first paragraph of this report will not be prevented, or detected and corrected, on a timely basis.

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over compliance that might be deficiencies, significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses, as defined above.

As required by the Audit Guide, immaterial findings excluded from this report have been reported in a separate letter to your office.

Supplementary Information for State Compliance Purposes

As Special Assistant Auditors for the Auditor General, we have audited the Statements of Net Assets of the Board as of June 30, 2012 and the related Statements of Changes in Net Assets for the year then ended, and the Statement of Net Assets of its investment trust fund, the Illinois Power Agency Trust Fund as of June 30, 2012 and have issued our report thereon dated December 13, 2012, which contained unqualified opinions on those financial statements. Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise ISBI's basic financial statements. We have not performed any procedures with respect to the audited financial statements subsequent to December 13, 2012. The accompanying supplementary information for the year ended June 30, 2012, in Schedules 1 through 6, is presented for purposes of additional analysis and is not a required part of the basic financial statements of ISBI. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the basic financial statements. The accompanying supplementary information for the year ended June 30, 2012, in Schedules 1 through 6 and the Analysis of Operations Section, 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 statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the accompanying supplementary information for the year ended June 30, 2012, in Schedules 1 through 6, is fairly stated in all material respects in relation to the basic financial statements as a whole for the year ended June 30, 2012.

We have also previously audited, in accordance with auditing standards generally accepted in the United States of America, the Board's basic financial statements for the years ended June 30, 2011 and June 30, 2010 (not presented herein), and have issued our reports thereon dated December 14, 2011 and January 12, 2011, which contained unqualified opinions on the respective basic financial statements. The accompanying supplementary information for the year ended June 30, 2011 and June 30, 2010, in Schedules 1 through 6, is presented for purposes of additional analysis and is not a required part of the basic financial statements of ISBI. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the June 30, 2011 and June 30, 2010 basic financial statements. The accompanying supplementary information for the year ended June 30, 2011 and June 30, 2010, in Schedules 1 through 6, has been subjected to the auditing procedures applied in the audits of the June 30, 2011 and June 30, 2010 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 statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the accompanying supplementary information for the year ended June 30, 2011 and June 30, 2010, in Schedules 1 through 6, is fairly stated in all material respects in relation to the basic financial statements as a whole from which it has been derived.

The accompanying supplementary information in the Analysis of Operations Section is presented for the purposes of additional analysis and is not a required part of the basic financial statements. Such information has not been subjected to the auditing procedures applied in the audit of the basic financial statements, and accordingly, we do not express an opinion or provide any assurance on it.

This report is intended solely for the information and use of the Auditor General, the General Assembly, the Legislative Audit Commission, the Governor, the Illinois State Board of Investment Board of Trustees, and ISBI's management and is not intended to be and should not be used by anyone other than these specified parties.

McGladrey LLP

Schaumburg, Illinois
January 28, 2013



**Independent Auditors' Report on Internal Control Over
Financial Reporting and on Compliance and Other Matters Based on an Audit of
Financial Statements Performed in Accordance with *Government Auditing Standards***

Honorable William G. Holland
Auditor General
State of Illinois

Board of Trustees
Illinois State Board of Investment

As Special Assistant Auditors for the Auditor General, we have audited the Statements of Net Assets and Statements of Changes in Net Assets of the Illinois State Board of Investment (ISBI), as of and for the years ended June 30, 2012 and June 30, 2011, and the Statement of Net Assets of its investment trust fund, the Illinois Power Agency Trust Fund, as of June 30, 2012, and have issued our report thereon dated December 13, 2012. 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

Management of the Illinois State Board of Investment is responsible for establishing and maintaining effective internal control over financial reporting. In planning and performing our audit, we considered the ISBI's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the ISBI's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the ISBI's internal control over financial reporting.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A *material weakness* is a deficiency, or combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in the internal control over financial reporting that might be deficiencies, significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the ISBI'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*.

This report is intended solely for the information and use of the Auditor General, the General Assembly, the Legislative Audit Commission, the Governor, ISBI's Board of Trustees and the ISBI's management, and is not intended to be and should not be used by anyone other than these specified parties.

McGladrey LLP

Schaumburg, Illinois
December 13, 2012

ILLINOIS STATE BOARD OF INVESTMENT
(An Internal Investment Pool of the State of Illinois)

Schedule of Findings

Current Findings

Year ended June 30, 2012

None.

ILLINOIS STATE BOARD OF INVESTMENT
(An Internal Investment Pool of the State of Illinois)

Schedule of Findings

Prior Finding Not Repeated

Year ended June 30, 2012

None.

ILLINOIS STATE BOARD OF INVESTMENT

(An Internal Investment Pool of the State of Illinois)

Supplementary Information for State Compliance Purposes

Year ended June 30, 2012

Summary

Supplementary Information for State Compliance Purposes presented in this section of the report includes the following:

- Fiscal Schedules and Analysis:

- Comparative Schedules of Operations
- Schedules of Investment Portfolio
- Schedules of Investment Manager Fees
- Schedules of Property and Equipment
- Reconciliation of the State Treasurer's Cash Balance with that of ISBI
- Analysis of Accounts Receivable

- Analysis of Operations (Unaudited):

- Board Functions and Planning Program (Unaudited)
- Number of Employees (Unaudited)
- Proceeds from General Obligation Bonds (Unaudited)
- Third-Party Marketing Fees Paid (Unaudited)
- Service Efforts and Accomplishments (Unaudited)
- Overall Rates of Return (Unaudited)
- Investment Returns – Benchmark and Actual (Unaudited)
- Net Asset Allocation as of June 30, 2012 (Unaudited)
- Schedules of Soft Dollar Credits (Unaudited)
- Schedules of Investment Commissions (Unaudited)

The accountants' report that covers the Supplementary Information for State Compliance Purposes presented in the Compliance Report Section states that it has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in the auditors' opinion, it is fairly stated in all material respects in relation to the basic financial statements as a whole from which it has been derived. The accountants' report also states the Analysis of Operations Section has not been subjected to the auditing procedures applied in the audit of the basic financial statements, and accordingly, they do not express an opinion or provide any assurance on it.

ILLINOIS STATE BOARD OF INVESTMENT
 (An Internal Investment Pool of the State of Illinois)

Schedule 1

Fiscal Schedules and Analysis
 Comparative Schedules of Operations
 Years ended June 30, 2012 and 2011

	2012	2011	Increase (decrease)
Investment income (loss):			
Interest	\$ 163,451,935	\$ 136,079,683	\$ 27,372,252
Dividends	138,635,610	132,335,702	6,299,908
Securities lending	2,856,652	3,494,441	(637,789)
Realized gain on investments	336,892,624	328,255,478	8,637,146
Unrealized gain (loss) on investments	<u>(600,396,365)</u>	<u>1,482,232,941</u>	<u>(2,082,629,306)</u>
Total investment income	<u>41,440,456</u>	<u>2,082,398,245</u>	<u>(2,040,957,789)</u>
Administrative expenses:			
Salaries and benefits	1,854,896	1,777,998	76,898
Operating	535,140	515,534	19,606
External support	<u>34,013,759</u>	<u>34,929,987</u>	<u>(916,228)</u>
Total expenses	<u>36,403,795</u>	<u>37,223,519</u>	<u>(819,724)</u>
Excess of investment income over administrative over expenses	<u>\$ 5,036,661</u>	<u>\$ 2,045,174,726</u>	<u>\$ (2,040,138,065)</u>

ILLINOIS STATE BOARD OF INVESTMENT
(An Internal Investment Pool of the State of Illinois)

Schedule 2

Fiscal Schedules and Analysis
Schedules of Investment Portfolio
June 30, 2012 and 2011

Fair value	2012		2011	
	Amount	Percentage of portfolio	Amount	Percentage of portfolio
Fixed income securities:				
Government and agency obligations:				
U.S. Treasury	\$ 383,122,214	3.40%	\$ 479,422,631	4.17%
Federal agencies and other governments	575,009,065	5.11	887,676,120	7.72
Foreign government obligations	385,628,617	3.43	37,951,769	0.33
Corporate obligations:				
Finance	149,245,144	1.33	204,608,577	1.78
Industrials	412,232,689	3.66	425,847,041	3.70
Collateralized mortgage obligations	1,076,456	0.01	13,492,526	0.12
Asset backed	832,141	0.01	-	0.00
Miscellaneous	93,591,233	0.83	118,885,238	1.03
Total fixed income securities	<u>2,000,737,559</u>	<u>17.78</u>	<u>2,167,883,902</u>	<u>18.85</u>
Equities:				
Common stocks:				
U.S. equities:				
Consumer discretionary	443,462,667	3.94	399,406,954	3.47
Consumer staples	263,054,840	2.34	292,352,546	2.54
Energy	282,792,717	2.51	340,835,612	2.96
Financials	590,584,161	5.25	541,615,534	4.71
Healthcare	368,770,331	3.28	388,948,328	3.38
Industrials	445,858,426	3.96	454,644,071	3.97
Information Technology	513,532,688	4.56	575,451,158	5.00
Materials	176,154,551	1.56	162,314,769	1.41
Telecommunication Services	65,435,689	0.58	77,405,727	0.67
Utilities	97,938,487	0.87	103,955,890	0.91
Other	5,519,009	0.05	43,268,269	0.38
Commingled funds	225,608,712	2.00	256,817,374	2.23
Non-U.S. equities	2,013,366,729	17.88	2,195,241,217	19.09
Total equities	<u>5,492,079,007</u>	<u>48.78</u>	<u>5,832,257,449</u>	<u>50.72</u>
Hedge funds	1,026,725,785	9.12	1,075,584,754	9.36
Real estate funds	967,346,450	8.59	780,336,465	6.79
Private equity	679,423,383	6.04	629,256,286	5.47
Money market instruments	255,922,180	2.27	303,501,465	2.64
Real Assets	507,019,665	4.50	455,984,316	3.96
Bank loans	328,593,596	2.91	253,447,070	2.20
Foreign currency forward contracts	(43,859)	0.01	(353)	0.01
Total investments	<u>\$ 11,257,803,766</u>	<u>100.00%</u>	<u>\$ 11,498,251,354</u>	<u>100.00%</u>

ILLINOIS STATE BOARD OF INVESTMENT
 (An Internal Investment Pool of the State of Illinois)

Schedule 3

Fiscal Schedules and Analysis
 Schedules of Investment Manager Fees
 Years ended June 30, 2012 and 2011

	2012	2011
Amalgamated Bank NY	\$ 663,310	\$ 752,037
Buford, Dixon	-	77,241
Channing	251,523	256,018
Chicago Equity Partners	977,144	1,044,487
Credo	350,129	197,337
Crescent Capital	664,014	655,782
Decatur	66,942	76,328
Entrust	2,104,723	2,041,554
Fiduciary Management Associates	333,571	330,767
Fort Washington	750,472	790,437
Garcia Hamilton	71,056	48,007
Globeflex Capital	467,434	482,053
Grosvenor Capital Management	1,560,559	1,758,416
Herndon Capital	393,731	364,070
IronBridge Capital Management	1,196,074	1,169,319
LM Capital	425,271	434,679
LSV Asset Management	2,997,809	3,473,063
Macquarie	3,606,411	3,669,149
Mesirow	2,001,389	1,939,851

(Continued)

ILLINOIS STATE BOARD OF INVESTMENT
(An Internal Investment Pool of the State of Illinois)

Schedule 3

Fiscal Schedules and Analysis
Schedules of Investment Manager Fees (Continued)
Years ended June 30, 2012 and 2011

	2012	2011
Opus Capital Management	\$ 432,237	\$ 424,333
Profit	-	716,437
Rhumblin	175,941	191,503
Rockcreek	2,193,579	2,064,475
Segall Bryant and Hamill	1,023,254	982,410
State Street Bank	280,000	140,000
SSgA (Cash Overlay)	125,000	125,000
SSgA Emerging Markets	62,632	-
SSgA MSCI ACWI Index	266,612	338,454
SSgA Mid Cap Growth	48,122	-
SSgA Small Cap Core	28,303	-
SSgA Small Cap Global	1,210,345	1,317,286
THL Credit	604,880	592,949
Templeton	1,650,646	1,747,843
Union Labor Life Investment Co. (ULLICO)	664,832	889,152
Various (allocated equally to all Investment Managers)	38,000	36,900
Vontobel Asset Management	2,246,391	2,180,479
Wellington	259,300	-
William Blair	2,056,892	2,011,546
	<u>\$ 32,248,528</u>	<u>\$ 33,319,362</u>

Investment manager fees are related to fees paid to various investment managers. Fees are negotiated primarily on market values. A graduated rate is used for most managers based upon various increments per million dollars of market value.

ILLINOIS STATE BOARD OF INVESTMENT
 (An Internal Investment Pool of the State of Illinois)

Fiscal Schedules and Analysis

Year ended June 30, 2012

Schedules of Property and Equipment

Changes in property and equipment are as follows:

							Schedule 4
	Balance at June 30, 2010	Additions	Deletions	Balance at June 30, 2011	Additions	Deletions	Balance at June 30, 2012
Cost	\$ 116,900	\$ 9,394	\$ (18,943)	\$ 107,351	\$ 11,244	\$ (25,142)	\$ 93,453
Less accumulated depreciation	(66,509)	(4,494)	-	(71,003)	(3,104)	18,253	(55,854)
Net property and equipment	<u>\$ 50,391</u>	<u>\$ 4,900</u>	<u>\$ (18,943)</u>	<u>\$ 36,348</u>	<u>\$ 8,140</u>	<u>\$ (6,889)</u>	<u>\$ 37,599</u>

Note: Amounts reported in the Schedule of Property and Equipment have been reconciled to property reports submitted to the Office of the Comptroller.

Reconciliation of the State Treasurer's Cash Balance with that of ISBI

	2012*			Schedule 5
	Illinois State Board of Investment	Illinois Power Agency Trust Fund	Total	2011
Balance per State Treasurer at June 30	\$ 242,090	\$ 24,854,573	\$ 25,096,663	\$ 119,804
Vouchers in transit	(103,639)	-	(103,639)	(9,354)
Balance per ISBI at June 30	<u>\$ 138,451</u>	<u>\$ 24,854,573</u>	<u>\$ 24,993,024</u>	<u>\$ 110,450</u>

* The assets of the Illinois Power Agency Trust Fund came under management of the Illinois State Board of Investment in fiscal year 2012.

In August 2007, by enactment of 30 ILCS 105/6z-75 of the Illinois Compiled Statutes, ISBI was given responsibility for the management of the Illinois Power Agency Trust Fund. This resulted in the transfer of the Illinois Power Agency Trust Fund's cash amounting to \$24,854,573, to ISBI. This cash was held by the State Treasurer pending transfer to State Street Bank and Trust Company for investment. The transfer of these funds to State Street Bank and Trust Company occurred on July 19, 2012.

ILLINOIS STATE BOARD OF INVESTMENT
(An Internal Investment Pool of the State of Illinois)

Fiscal Schedules and Analysis

Year ended June 30, 2012

Analysis of Accounts Receivable

Schedule 6

A summary of ISBI's receivables are as follows:

Receivables	<u>2012</u>	<u>2011</u>
Foreign taxes	\$ 2,515,736	\$ 2,732,489
Accounts receivable	3,105,150	3,165,120
Investments sold	50,215,916	25,152,183
Interest and dividends	32,854,218	35,369,308
Total receivables	<u>\$ 88,691,020</u>	<u>\$ 66,419,100</u>

ISBI's receivable balance at June 30, 2012 and 2011 amounted to \$88,691,020 and \$66,419,100, respectively. The balance consisted of \$38,475,104 and \$41,266,917 of dividends, interest, foreign taxes, and accounts receivable on investments held as of June 30, 2012 and 2011, respectively, and included receivables of \$50,215,916 and \$25,152,183 for investments sold prior to June 30, 2012 and 2011, respectively, but settled after year-end. Because the collection of this interest is relatively assured and the sale of investments is merely an issue of timing, ISBI does not maintain a reserve for uncollectible receivables or age the receivable detail.

ILLINOIS STATE BOARD OF INVESTMENT
(An Internal Investment Pool of the State of Illinois)

Analysis of Operations (Unaudited)

Year ended June 30, 2012

Board Functions and Planning Program (Unaudited)

The Illinois State Board of Investment (ISBI) was created on October 10, 1969, by Article 22A of the Illinois Pension Code to manage and invest the assets and reserves of any pension fund or retirement system that transfers this responsibility to ISBI. In accordance with Article 22A, the Trustees of the State Employees' Retirement System, the General Assembly Retirement System, and the Judges' Retirement System transferred all of their investment assets to ISBI as of June 30, 1970. Since that date, all additional funds available for investment for those three systems have been transferred to ISBI.

In 1978, in accordance with Article 24, ISBI shall be responsible for developing and establishing the State Employees' Deferred Compensation Plan (the Plan). Initial enrollment began in 1979, at which time the Department of Personnel (now Department of Central Management Services) was named as the Administrator of the Plan. With respect to developing and establishing the Plan, ISBI reviews investment offering options for the Plan and supervises the Department of Central Management Services' administration of the Plan.

Beginning July 1, 1978, ISBI merged the Illinois Board Fund, Illinois Equity Fund, and Illinois Segregated Fund into the Illinois State Board of Investment Commingled Fund (the Commingled Fund). The purpose of this consolidation was to enhance control over investment policy through increased flexibility in the allocation of cash reserves between fixed income and equity investments. ISBI's investment policy and strategy can be more uniformly applied to each member system irrespective of cash flow. In addition, it simplified ISBI's accounting and reporting systems. The result is that the Commingled Fund now represents all of the assets under ISBI's supervision.

Beginning in 1982, ISBI expanded the asset base of the Commingled Fund to include both real estate and venture capital.

In 1992, ISBI completed its investment strategy to have all equity security investments managed externally.

During fiscal year 2004, ISBI engaged Marquette Associates as its investment consultant. ISBI conducted an asset allocation study and, in December 2003, adopted a written Asset Allocation Study. The Asset Allocation Study summarizes ISBI's investment policies and measures of performance, formally documents objectives of ISBI, and details a strategic plan for ISBI. Criteria for the review and evaluation of investment managers are included in the Asset Allocation Study. Additionally, a methodology and format is outlined to highlight the results of the objectives and goals established within the Asset Allocation Study. The Asset Allocation Study reaffirms the broadly diversified investment strategy that has been pursued by ISBI with the belief that, over a period of time, this approach will maximize investment return within a prudent level of risk. In March 2008, the Asset Allocation Study was updated to incorporate asset classes and revise asset allocation percentages. In June 2011, the Asset Allocation Study was again updated to incorporate asset classes and revise allocation percentages effective for fiscal year 2012.

Members of the Board of Trustees as of June 30, 2012 include:

Roderick Bashir	Justice Thomas Hoffman
Devon Bruce	Steven Powell
Michelle Bush	Treasurer Dan Rutherford
John Casey	Comptroller Judy Barr Topinka
Senator John Clayborne	

ISBI has established both long-term and short-term goals with the intention of maximizing earnings for Member Retirement Systems' investments. These goals are reviewed in accordance with the Strategic Investment Policy.

ILLINOIS STATE BOARD OF INVESTMENT
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Analysis of Operations (Unaudited)

Year ended June 30, 2012

Number of Employees (Unaudited)

ISBI had 11 full-time employees at June 30, 2012 and had 10 full-time employees at June 30, 2011.

Proceeds from General Obligation Bonds (Unaudited)

Public Act 93-0002 (the Act) became effective on April 7, 2003 and authorized the State of Illinois to issue \$10 billion of General Obligation Bonds for the purpose of making contributions to designated retirement systems. The State Employees' Retirement System, General Assembly Retirement System, and Judges' Retirement System are "designated retirement systems" for the purpose of this law.

On June 12, 2003, the State of Illinois issued \$10 billion of General Obligation Bonds, Pension Funding Series June 2003. The net bond proceeds were allocated among the five state-funded retirement systems to reduce their actuarial reserve deficiencies as provided in the Act.

The State Employees' Retirement System, General Assembly Retirement System, and Judges' Retirement System (member systems) received an allocation of bond proceeds equal to \$1,544,924,744 on July 1, 2003. The monies were deposited into the Master Trust Account with the Illinois State Board of Investment on July 2, 2003. ISBI initially approved investing the pension bond proceeds in separate index funds. These index funds were subsequently liquidated and combined with ISBI's other investments and invested in accordance with the asset allocation policy of ISBI during the year ended June 30, 2004.

Public Act 96-0043 (the Act) became effective on July 15, 2009 and authorized the State of Illinois to issue \$3.466 billion of General Obligation Bonds for the purpose of making contributions to designated retirement systems. The State Employees' Retirement System, General Assembly Retirement System, and Judges' Retirement System are "designated retirement systems" for the purpose of this law.

On January 7, 2010, the State of Illinois issued \$3.466 billion of General Obligation Bonds, Taxable Bond Series January 2010. The net bond proceeds were allocated among the five state-funded retirement systems to reduce their actuarial reserve deficiencies as provided in the Act. The State Employees' Retirement System, General Assembly Retirement System, and Judges' Retirement System received an allocation of bond proceeds equal to \$809,401,372 on January 20, 2010. The monies were deposited into the Master Trust Account with the Illinois State Board of Investment the same day. The monies were combined with ISBI's other investments and invested in accordance with the asset allocation policy of ISBI during the year ended June 30, 2010.

Public Act 96-1497 (the Act) became effective on January 14, 2011 and authorized the State of Illinois to issue up to \$4.1 billion of General Obligation Bonds for the purpose of making contributions to designated retirement systems. On March 10, 2011, the State of Illinois issued \$3.7 billion of General Obligation Bonds, Taxable Bond Series February 2011. The net bond proceeds were allocated among the five state-funded retirement systems to reduce their actuarial reserve deficiencies as provided in the Act.

The State Employees' Retirement System, General Assembly Retirement System, and Judges' Retirement System received an allocation of bond proceeds equal to \$745,546,496 on March 14, 2011. The monies were deposited into the Master Trust Account with the Illinois State Board of Investment the same day. The monies were combined with ISBI's other investments and invested in accordance with the asset allocation policy of ISBI during the year ended June 30, 2011.

During fiscal year 2012, employer and employee funding transfers were sent directly by the State of Illinois to Member systems, rather than to ISBI. As a result, ISBI reports no Contributions from the State of Illinois in fiscal year 2012.

ILLINOIS STATE BOARD OF INVESTMENT
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Analysis of Operations (Unaudited)

Year ended June 30, 2012

ISBI estimates the annualized return of each pension bond series as follows:

Series	Return
General Obligation Bonds, Pension Fund Series June 2003	5.7%
General Obligation Bonds, Taxable Bond Series January 2010	6.4%
General Obligation Bonds, Taxable Bond Series February 2011	3.6%

Third-Party Marketing Fees Paid (Unaudited)

ISBI disclosed that investment managers hired marketing groups to assist with promoting their investment product to ISBI. Marketing fees paid by investment managers were as follows:

Investment Manager	Third Party Marketer	Type of Fund	Year Ended June 30,	
			2012	2011
Alinda Infrastructure Fund	C.P. Eaton & Associates	Infrastructure	\$ -	\$ 154,267

Service Efforts and Accomplishments (Unaudited)

For purposes of evaluating service efforts and accomplishments, three different measures have been included. One measure presents a historical perspective of overall annual and compound rates of return; another compares benchmark rates of return with actual rates of return by fund; and the last presents asset allocations by fund type.

Overall Rates of Return (Unaudited)

	2012	2011	2010	2009	2008
Annual total return	0.1%	21.7%	9.1%	(20.1)%	(6.2)%
Compound annual rate of return since July 1, 1982	9.1	9.4	9.0	8.9	10.3

Investment Returns – Benchmark and Actual (Unaudited)

ISBI operates under a long-range investment plan with the objective to maximize the total rate of return. The objectives set forth are as follows:

- At least equal to 7.75%, the actuarially assumed interest rate of return for one of ISBI's member systems, the State Employees' Retirement System (SERS). Historically, SERS had adopted 8.5% as the actuarially assumed rate of return, while the other two member systems - General Assembly Retirement System (GARS) and the Judges' Retirement System (JRS) have assumed 8.0%. In September 2010, SERS reduced its return assumption from 8.5% to 7.75%. Similarly, the GARS and JRS reduced their return assumptions from 8.0% to 7.0%. ISBI has assumed the same rate of return as SERS (7.75% as of June 30, 2012), as SERS' net assets represents approximately 95% of ISBI's net assets as of June 30, 2012.
- At least equal to the return of a composite benchmark of market indices in the same proportions as ISBI's asset allocation policy targets.

ILLINOIS STATE BOARD OF INVESTMENT
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Analysis of Operations (Unaudited)

Year ended June 30, 2012

ISBI earned a total rate of return of .1% for the year ended June 30, 2012.

	(Annualized)							
	2012	2011	2010	2009	2008	3 Yrs.	5 Yrs.	10 Yrs.
	%	%	%	%	%	%	%	%
Total Fund	0.1	21.7	9.1	(20.1)	(6.2)	10.0	(0.1)	5.2
Composite Benchmark*	0.9	19.6	10.2	(17.0)	(4.6)	10.0	1.1	6.2
Consumer Price Index	1.7	3.6	1.1	(1.4)	5.0	2.1	2.0	2.5
U.S. Equities	1.3	33.9	17.3	(25.1)	(12.7)	16.8	0.8	6.2
Russell 3000 Index	3.8	32.4	15.7	(26.6)	(12.5)	16.7	0.4	5.8
Hedge Funds **	(4.3)	12.7	4.4	(11.6)	(2.6)	4.1	(0.6)	N/A
HFRX Equity Hedge	(10.7)	3.4	3.1	(20.0)	(4.9)	(1.6)	(6.3)	0.4
International Equities	(10.7)	32.7	13.1	(29.1)	(10.3)	10.3	(3.1)	6.9
MSCI-ACWI Index	(14.4)	30.9	6.4	(31.0)	(10.2)	7.8	(4.0)	7.6
Fixed Income	6.8	5.7	5.5	(2.4)	5.3	6.0	4.2	4.5
Barclays Capital Universal Index	7.4	4.8	10.6	4.9	6.2	7.6	6.8	6.0
Real Estate	5.3	17.0	(8.2)	(31.7)	2.6	4.2	(4.6)	3.4
NCREIF Real Estate Index	11.3	16.7	(1.5)	(19.6)	9.2	7.4	(1.8)	5.6
Private Equity	7.6	24.0	14.0	(18.8)	(4.9)	15.0	3.3	10.0

Note: Calculations are based on a time series of linked monthly returns (IRR), producing a time weighted effect.

* Composite Benchmark:

Effective 07/11:

30% Russell 3000; 20% MSCI-ACWI; 25% Barclays Capital Universal; 10% NCREIF ODCE; 5% Venture Economics Pooled Average Periodic IRR which is based on preliminary data subject to revision on a quarterly basis; 10% HFRX Equity Hedged Index.

Effective 07/07:

30% Russell 3000; 20% MSCI-EAFE; 25% Lehman Universal; 10% NCREIF; 5% Venture Economics Pooled Average Periodic IRR which is based on preliminary data subject to revision on a quarterly basis; 10% HFRX Equity Hedged Index.

Effective 03/06:

8% Russell Midcap Growth; 7% Russell 2000 Value; 5% Russell 1000 Growth; 15% Russell 1000 Value; 10% S&P 500; 3% S&P Dev. Ex-U.S. <\$2B; 7% MSCI-EAFE; 10% NCREIF; 5% Lehman High Yield; 10% Lehman Aggregate; 10% Lehman Int. Govt/Corp; 10% NCREIF

Effective 12/03:

45% Wilshire 5000; 10% MSCI-EAFE; 25% Lehman Universal; 10% NCREIF; 5% Venture Economic All Private Equity Index which is based on preliminary data subject to revision on a quarterly basis; 5% HFRX Equity Hedged Index.

**Hedge Funds:

ISBI began investing in Hedge Funds in Fiscal 2007, therefore actual return information is not available prior to that period.

Note: Effective 11/08, the Lehman Universal benchmark ceased to exist. Barclays Capital Universal is the benchmark currently used by ISBI.

ILLINOIS STATE BOARD OF INVESTMENT
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Analysis of Operations (Unaudited)

Year ended June 30, 2012

Net Asset Allocation as of June 30, 2012 (Unaudited)

The investment policy of ISBI establishes asset allocation targets and ranges for each asset class, selected to accomplish the long-range investment plan. The actual asset mix is roughly in line with the policy target, with modest over-allocations to U.S. equity and unallocated cash with offsetting under-allocations to international equity, alternative investments, and real estate.

	<u>Fair Value</u>	<u>Actual Asset Mix</u>	<u>Policy Target</u>
U.S. equity	\$ 3,253,103,566	29%	30%
U.S. equity hedge funds	1,026,725,785	9	10
International equity	2,013,366,729	18	20
Commingled funds ⁴	225,608,712	2	-
Fixed income ¹	2,000,737,559	18	17
Bank Loans	328,593,596	3	3
Real estate	967,346,450	9	10
Private Equity ²	679,423,383	6	5
Real Assets ²	507,019,665	4	5
Cash ³	282,011,240	2	-
Total	<u>\$ 11,283,936,685</u>	<u>100%</u>	<u>100%</u>

¹ Maturities of one year or longer, including convertible bonds.

² Interests in limited partnerships and other entities which have limited liquidity.

³ Includes money market instruments and other assets, less liabilities.

⁴ Holdings include fixed income and equity investments.

ILLINOIS STATE BOARD OF INVESTMENT
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Analysis of Operations (Unaudited)
 Schedules of Soft Dollar Credits (Unaudited)
 Years ended June 30, 2012 and 2011

	2012	2011
Soft dollar credits outstanding, at beginning of fiscal year	\$ 14,853	\$ 325,187
Soft dollar credits earned	16,176	26,429
Bank of New York payout amount	(16,176)	(357,361)
Citibank payout amount	(14,853)	-
Adjustment***	-	20,598
Soft dollar credits outstanding, at end of fiscal year	<u>\$ -</u>	<u>\$ 14,853</u>

*** This reflects an adjustment to record prior year soft dollar credits earned but not recorded for soft dollars held at Bank of New York and a balance outstanding in soft dollars held at Citibank.

Soft dollar credits are issued to ISBI by certain brokers based on the level of activity of investment managers using that particular broker. ISBI can use these credits to pay for various investment expenses.

ILLINOIS STATE BOARD OF INVESTMENT

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Analysis of Operations (Unaudited)

Schedules of Investment Commissions (Unaudited)

Years ended June 30, 2012 and 2011

	2012	2011
Investment brokerage firms:		
Banc of America Securities Inc.	\$ 59,139	\$ 39,997
Barclays Capital	26,471	-
Bloomberg Tradebook	27,176	-
BNP Paribas Securities	6,893	-
BNY Brokerage	34,255	25,676
Cabrera Asset Management	114,155	277,702
Cantor Fitzgerald & Co.	68,170	64,896
CF Global Trading LLC	18,457	44,751
Cheevers & Company	143,785	183,168
Cheurex de Virieu Paris	7,359	19,932
Chicago Analytic Trading Co.	25,025	82,428
Citigroup Smith Barney Inc.	92,212	85,966
ConvergEx	5,704	-
Credit Agricole Indosuez	8,549	-
Credit Lyonnais Securities	14,782	-
Credit Suisse First Boston Corp.	104,495	128,149
Daiwa Securities	25,907	5,340
Deutsche Banc Securities Inc.	55,326	37,396
Direct Access Partners	45,603	-
Enskilda Securities	-	5,861
Friedman Billings and Ramsey & Co. Inc.	-	8,721
Gardner Rich & Co.	15,241	96,993
Goldman Sachs & Company	47,746	14,930

(Continued)

ILLINOIS STATE BOARD OF INVESTMENT
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Analysis of Operations (Unaudited)
Schedules of Investment Commissions (Unaudited) (Continued)
Years ended June 30, 2012 and 2011

	2012	2011
Investment brokerage firms (Continued):		
Goodbody	\$ 11,370	\$ -
Helvea Inc.	10,970	-
Instinet	63,817	29,301
Investment Technology Group	29,110	47,489
ISI Trading Group	16,338	-
Itau Securities	-	5,321
J.P. Morgan Securities, Inc.	58,581	46,766
Jefferies & Company	24,712	49,112
Joh Berenberg, Glossler & Co.	13,973	-
Keefe Bruynette and Woods Inc.	20,759	-
Kepler Securities	22,514	6,068
Knight Securities	-	7,064
Liquidnet Inc.	62,230	100,772
Loop Capital Markets	381,910	328,847
M. Ramsey King Securities	11,640	59,186
Macquarie Equities Ltd	26,659	25,190
Melvin Securities Corp	-	48,476
Merrill Lynch Pierce Fenner & Smith	-	10,768
Mischler Financial Group	7,572	-
Morgan Stanley & Co.	63,655	54,817
MR Beal	107,278	77,276
Natixis Group	17,250	-
Nomura Securities	84,824	59,373

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ILLINOIS STATE BOARD OF INVESTMENT
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Analysis of Operations (Unaudited)
 Schedules of Investment Commissions (Unaudited) (Continued)
 Years ended June 30, 2012 and 2011

	2012	2011
Investment brokerage firms (Continued):		
Numis Securities	\$ 13,176	\$ -
Piper, Jaffrey & Hopwood Inc.	-	9,592
Pulse Trading	13,138	61,243
Ramsey King	42,147	6,909
RBC Capital Markets	6,014	8,324
Redburn Partners LLC	13,427	-
Robert W. Baird & Co.	41,272	40,912
Sanford C. Bernstein	65,031	6,398
Scotia Capital Markets Toronto	10,983	-
SG Americas Securities	-	13,715
Simmons & Co. International	5,366	-
Societe Generale	10,290	-
Stiffel, Nicolaus & Company Inc.	32,157	16,510
UBS Securities	106,052	124,749
Weeden & Co.	39,235	-
William Blair & Co.	-	12,730
Williams Capital Group	64,752	48,140
Various (Under \$5,000)	412,281	356,136
	<u>\$ 2,856,933</u>	<u>\$ 2,783,090</u>

Commissions relate to fees paid to investment brokerage firms for the purchase and sale of investments.