

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

Compliance Examination

Year ended June 30, 2014

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



Assurance ■ Tax ■ Consulting

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, 2014, 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. Alise M. White

Chief Fiscal Officer

Willie Genette Bacon-Cordova

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 5, 2015

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

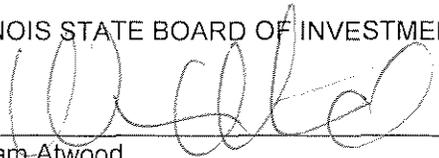
Ladies and Gentlemen:

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, 2014. Based on this evaluation, we assert that during the year ended June 30, 2014, 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 Atwood
 Executive Director



 Alise White
 Deputy
 Executive Director



 Linsey J. Schoemehl
 General Counsel/ Chief
 Compliance Officer



 Genette Bacoff
 Chief Fiscal Officer

ILLINOIS STATE BOARD OF INVESTMENT
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Compliance Report

Summary

Year ended June 30, 2014

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	-	-

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

<u>Item No.</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 December 19, 2014, 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, 2014. 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. 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 of ISBI's compliance with specified requirements.

In our opinion, ISBI complied, in all material respects, with the compliance requirements listed in the first paragraph of this report during the year ended June 30, 2014.

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 to determine the examination procedures that are appropriate in the circumstances 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 ISBI's internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of ISBI's internal control over compliance.

A deficiency in 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 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. *A significant deficiency in internal control over compliance* is a deficiency, or a combination of deficiencies, in internal control over compliance that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

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 material weaknesses or significant deficiencies. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

Supplementary Information for State Compliance Purposes

As Special Assistant Auditors for the Auditor General, we have audited the Statement of Net Position and the related Statement of Changes in Net Position of ISBI as of and for the year ended June 30, 2014, and the Statement of Net Position and the related Statement of Changes in Net Position of its investment trust fund, the Illinois Power Agency Trust Fund as of and for the year ended June 30, 2014, and have issued our report thereon dated December 2, 2014, which contained unmodified 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 2, 2014. The accompanying supplementary information for the year ended June 30, 2014 in Schedules 1 through 6 is presented for the 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, 2014 in Schedules 1 through 6 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, the accompanying supplementary information for the year ended June 30, 2014 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, 2014.

We also previously audited, in accordance with auditing standards generally accepted in the United States of America, the ISBI's basic financial statements as of and for the years ended June 30, 2013, and have issued our report thereon dated December 6, 2013, which contained an unmodified opinion on the financial statements. The accompanying supplementary information for the year ended June 30, 2013 in Schedules 1 through 6, 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, 2013 financial statements. The accompanying supplementary information for the year ended June 30, 2013 in Schedules 1 through 6 has been subjected to the auditing procedures applied in the audit of the June 30, 2013 basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare those basic financial statements or to those basic financial 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, 2013 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 5, 2015



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, in accordance with the 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, the Statements of Net Position and Statements of Changes in Net Position of the Illinois State Board of Investment Member Systems (ISBI Member Systems), as of and for the years ended June 30, 2014 and June 30, 2013, and the Statements of Net Position of its investment trust fund, the Illinois Power Agency Trust Fund (Trust Fund), as of June 30, 2014 and June 30, 2013, and the Statements of Changes in Net Position for the years ended June 30, 2014 and June 30, 2013, which collectively comprise the Illinois State Board of Investment's (ISBI) basic financial statements, and have issued our report thereon dated December 2, 2014.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered ISBI's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of ISBI's internal control. Accordingly, we do not express an opinion on the effectiveness of ISBI's internal control.

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 a 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. *A significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether ISBI's financial statements are free from 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*.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and results of that testing, and not to provide an opinion on the effectiveness of ISBI's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering ISBI's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

McGladrey LLP

Schaumburg, Illinois
December 2, 2014

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

Schedule of Findings

Current Findings

Year ended June 30, 2014

None.

ILLINOIS STATE BOARD OF INVESTMENT
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Schedule of Findings

Prior Finding Not Repeated

Year ended June 30, 2014

None.

ILLINOIS STATE BOARD OF INVESTMENT
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Supplementary Information for State Compliance Purposes

Year ended June 30, 2014

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 Position Allocation as of June 30, 2014 (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, 2014 and 2013

	2014	2013	Increase (decrease)
Investment income:			
Interest	\$ 264,388,234	\$ 216,655,123	\$ 47,733,111
Dividends	154,291,279	150,346,989	3,944,290
Securities lending	3,242,232	4,750,591	(1,508,359)
Realized gain on investments	585,954,938	247,580,743	338,374,195
Unrealized gain on investments	<u>1,326,884,197</u>	<u>1,005,988,055</u>	<u>320,896,142</u>
Total investment income	<u>2,334,760,880</u>	<u>1,625,321,501</u>	<u>709,439,379</u>
Administrative expenses:			
Salaries and benefits	1,897,689	1,972,176	(74,487)
Operating	605,158	539,357	65,801
External support	<u>40,276,981</u>	<u>35,397,479</u>	<u>4,879,502</u>
Total expenses	<u>42,779,828</u>	<u>37,909,012</u>	<u>4,870,816</u>
Excess of investment income over administrative expenses	<u>\$ 2,291,981,052</u>	<u>\$ 1,587,412,489</u>	<u>\$ 704,568,563</u>

ILLINOIS STATE BOARD OF INVESTMENT
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Schedule 2

Fiscal Schedules and Analysis
Schedules of Investment Portfolio
June 30, 2014 and 2013

Fair value	2014		2013	
	Amount	Percentage of portfolio	Amount	Percentage of portfolio
Fixed income securities:				
Government and agency obligations:				
U.S. Treasury	\$ 380,521,606	2.52%	\$ 381,380,855	2.97%
Federal agencies and other governments	403,954,042	2.67	506,019,218	3.94
Foreign government obligations	832,282,402	5.50	415,070,013	3.23
Corporate obligations:				
Finance	208,156,262	1.38	166,390,995	1.29
Industrials	465,408,474	3.08	409,132,090	3.18
Collateralized mortgage obligations	-	0.00	912,944	0.01
Asset backed	650,237	0.01	771,437	0.01
Miscellaneous	125,299,269	0.83	96,946,662	0.75
Total fixed income securities	<u>2,416,272,292</u>	<u>15.99</u>	<u>1,976,624,214</u>	<u>15.38</u>
Equities:				
Common stocks:				
U.S. equities:				
Consumer discretionary	632,337,241	4.18	601,964,559	4.68
Consumer staples	313,760,798	2.08	295,294,021	2.30
Energy	409,957,581	2.71	337,747,551	2.63
Financials	834,468,541	5.52	774,434,969	6.03
Healthcare	541,175,519	3.58	429,385,210	3.34
Industrials	693,569,736	4.59	578,851,632	4.50
Information technology	699,896,152	4.63	551,354,471	4.29
Materials	219,483,392	1.45	183,687,034	1.43
Telecommunication services	82,005,301	0.54	52,336,593	0.41
Utilities	123,738,453	0.82	104,879,942	0.82
Other	2,890,602	0.02	6,542,323	0.05
Commingled funds	733,010,980	4.85	317,408,396	2.47
Non-U.S. equities	2,346,576,036	15.52	2,329,869,123	18.13
Total equities	<u>7,632,870,332</u>	<u>50.49</u>	<u>6,563,755,824</u>	<u>51.08</u>
Hedge funds	1,485,145,060	9.82	1,166,602,482	9.08
Real estate funds	1,483,445,971	9.81	1,294,600,976	10.07
Private equity	667,730,266	4.41	643,775,529	5.01
Money market instruments	217,737,000	1.44	237,649,781	1.85
Real assets	524,284,793	3.47	550,739,042	4.29
Bank loans	689,256,558	4.56	416,649,247	3.23
Foreign currency forward contracts	(637,600)	0.01	(412,825)	0.01
Total investments	<u>\$ 15,116,104,672</u>	<u>100.00%</u>	<u>\$ 12,849,984,270</u>	<u>100.00%</u>

ILLINOIS STATE BOARD OF INVESTMENT
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Schedule 3

Fiscal Schedules and Analysis
 Schedules of Investment Manager Fees
 Years ended June 30, 2014 and 2013

	2014	2013
Amalgamated Bank NY	\$ 315,014	\$ 617,621
Ariel Investments	480,455	21,013
Ashmore	175,544	-
Channing	405,984	306,612
Chicago Equity Partners	492,670	741,289
Credo	100,783	370,173
Crescent Capital	1,158,737	741,570
Decatur	98,202	77,861
Entrust	3,474,279	2,471,611
Fiduciary Management Associates	467,764	377,420
Fort Washington	1,205,052	899,913
Garcia Hamilton	113,432	76,739
Globeflex Capital	241,253	484,571
Grosvenor Capital Management	17,190	673,491
Herndon Capital	386,997	454,005
IronBridge Capital Management	368,755	1,342,097
LM Capital	437,675	411,451
LSV Asset Management	4,005,556	3,130,508
Lombardia	170,751	-
Macquarie	2,975,379	3,547,521
Mesirow	2,155,326	1,887,564
Opus Capital Management	594,072	494,837
Rhumblin	178,667	161,970
Rockcreek	3,410,427	2,500,601
Segall Bryant and Hamill	1,514,155	1,146,497
Standish	592,094	-
State Street Bank	280,000	280,000

(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, 2014 and 2013

	2014	2013
SSgA (Cash Overlay)	\$ 166,659	\$ 137,813
SSgA Emerging Markets	27,350	114,589
SSgA Emerging Markets Commingled Fund	137,492	-
SSgA MSCI ACWI Index	276,207	267,483
SSgA Mid Cap Growth	149,781	119,626
SSgA Small Cap Core	87,149	54,527
SSgA Small Cap Global	1,907,612	1,398,090
THL Credit	860,097	588,626
Templeton	1,990,429	1,819,740
Union Labor Life Investment Co. (ULLICO)	460,171	626,975
Various (allocated equally to all Investment Managers)	38,000	38,000
Vontobel Asset Management	2,416,110	2,424,059
Wellington	992,512	855,638
William Blair	3,233,146	2,210,063
	<u>\$ 38,558,928</u>	<u>\$ 33,872,164</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
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Fiscal Schedules and Analysis

Schedules of Property and Equipment

Year ended June 30, 2014

Changes in property and equipment are as follows:

	Schedule 4						
	Balance at June 30, 2012	Additions	Deletions	Balance at June 30, 2013	Additions	Deletions	Balance at June 30, 2014
Cost	\$ 93,453	\$ 10,873	\$ -	\$ 104,326	\$ 648	\$ (7,720)	\$ 97,254
Less accumulated depreciation	(55,854)	(4,396)	-	(60,250)	(2,210)	7,720	(54,740)
Net property and equipment	<u>\$ 37,599</u>	<u>\$ 6,477</u>	<u>\$ -</u>	<u>\$ 44,076</u>	<u>\$ (1,562)</u>	<u>\$ -</u>	<u>\$ 42,514</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

	2014			2013
	Illinois State Board of Investment	Illinois Power Agency Trust Fund	Total	
Balance per State Treasurer at June 30	\$ 473,059	\$ 1,024	\$ 474,083	\$ 449,417
Vouchers in transit	-	-	-	(153,741)
Balance per ISBI at June 30	<u>\$ 473,059</u>	<u>\$ 1,024</u>	<u>\$ 474,083</u>	<u>\$ 295,676</u>

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 in fiscal year 2012. 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
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Fiscal Schedules and Analysis

Schedules of Property and Equipment

Year ended June 30, 2014

Analysis of Accounts Receivable

Schedule 6

A summary of ISBI's receivables are as follows:

Receivables	<u>2014</u>	<u>2013</u>
Foreign taxes	\$ 2,741,543	\$ 3,827,119
Accounts receivable	1,522,662	-
Investments sold	357,652,133	379,123,089
Interest and dividends	39,381,775	35,978,861
Total receivables	<u>\$ 401,298,113</u>	<u>\$ 418,929,069</u>

ISBI's receivable balance at June 30, 2014 and 2013 amounted to \$401,298,113 and \$418,929,069, respectively. The balance consisted of \$43,645,980 and \$39,805,980 of dividends, interest, foreign taxes, and accounts receivable on investments held as of June 30, 2014 and 2013, respectively, and included receivables of \$357,652,133 and \$379,123,089 for investments sold prior to June 30, 2014 and 2013, 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, 2014

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. In June 2013 the Asset Allocation was again revised after a search for a General Consultant was completed. There were no major changes to the asset allocation, however, certain strategies were refined within allocations.

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Analysis of Operations (Unaudited)

Year ended June 30, 2014

Members of the Board of Trustees as of June 30, 2014 include:

Roderick Bashir	Steven Powell
Devon Bruce	Treasurer Dan Rutherford
Michelle Bush	Justice Mary Seminara Schostok
John Casey	Comptroller Judy Baar Topinka
Senator James 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.

Number of Employees (Unaudited)

ISBI had 11 full-time employees at June 30, 2014 and had 11 full-time employees at June 30, 2013.

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

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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 2014 and 2013, respectively, 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 2014 and 2013. In fiscal year 2014 ISBI received \$16,000,000 in contributions from the Judges Retirement System which was deposited into the Master Trust Account the same day.

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

Series	Return
General Obligation Bonds, Pension Fund Series June 2003	7.8%
General Obligation Bonds, Taxable Bond Series January 2010	11.0%
General Obligation Bonds, Taxable Bond Series February 2011	11.3%

Third-Party Marketing Fees Paid (Unaudited)

ISBI discloses whether investment managers hired marketing groups to assist with promoting their investment product to ISBI. There were no third party marketing fees paid by investment managers as of June 30, 2014 and June 30, 2013, respectively.

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)

	2014	2013	2012	2011	2010
Annual total return	17.9%	14.1%	0.1%	21.7%	9.1%
Compound annual rate of return since July 1, 1982	9.5	9.2	9.1	9.4	9.0

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Analysis of Operations (Unaudited)

Year ended June 30, 2014

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 (7.25% as of June 30, 2014), as SERS' net assets represents approximately 95% of ISBI's net position as of June 30, 2014.
- At least equal to the return of a composite benchmark of market indices in the same proportions as ISBI's asset allocation policy targets.

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Year ended June 30, 2014

ISBI earned a total rate of return of 17.9% for the year ended June 30, 2014.

	(Annualized)							
	2014	2013	2012	2011	2010	3 Yrs.	5 Yrs.	10 Yrs.
	%	%	%	%	%	%	%	%
Total Fund	17.9	14.1	0.1	21.7	9.1	11.6	3.9	6.6
Composite Benchmark*	16.3	11.8	0.9	19.6	10.2	10.5	4.1	7.3
Consumer Price Index	2.1	1.8	1.7	3.6	1.1	2.3	1.3	2.4
U.S. Equities	24.1	23.3	1.3	33.9	17.3	18.7	8.0	8.5
Russell 3000 Index	25.2	21.5	3.8	32.4	15.7	18.6	7.3	7.8
Hedge Funds **	15.0	12.6	(4.3)	12.7	4.4	6.7	2.3	N/A
HFRX Equity Hedge	8.5	8.3	(10.7)	3.4	3.1	0.0	(3.8)	0.2
International Equities	23.8	16.8	(10.7)	32.7	13.1	11.4	2.1	9.4
MSCI-ACWI ex US Index	22.8	14.4	(14.4)	30.9	6.4	8.6	(1.2)	7.6
Fixed Income	6.5	2.4	6.8	5.7	5.5	4.9	3.5	3.9
Barclays Capital U.S. Universal Index	5.2	0.2	7.4	4.8	10.6	4.1	5.5	4.8
Real Estate	14.5	13.0	5.3	17.0	(8.2)	11.7	(2.7)	4.5
NCREIF Real Estate Index	11.7	11.1	11.3	16.7	(1.5)	13.0	2.7	8.6
Private Equity	24.7	16.2	7.6	24.0	14.0	15.7	7.5	12.2

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

Total fund return is presented net of fees. All other return information is presented gross of fees.

* Composite Benchmark:
Effective 06/14:

30% Russell 3000; 20% MSCI-ACWI ex US; 25% Barclays Capital U.S. Universal; 10% NCREIF ODCE; 5% Custom Private Equity Benchmark which is based on preliminary data subject to change; 10% HFR1 Fund of Funds Index. The Custom Private Equity benchmark is based on peer universe return data compiled and published by Cambridge Associates, LLC. The custom benchmark returns are calculated as pooled internal rates of return (IRR).

Effective 01/14:

30% Russell 3000; 20% MSCI-ACWI ex US; 25% Barclays Capital U.S. 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% HFR1 Fund of Funds Index.

Effective 07/11:

30% Russell 3000; 20% MSCI-ACWI ex US; 25% Barclays Capital U.S. 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;

Effective 12/03:

5% Lehman High Yield; 10% Lehman Aggregate; 10% Lehman Int. Govt/Corp; 10% NCREIF; 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 U.S. Universal is the benchmark currently used by ISBI.

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Analysis of Operations (Unaudited)

Year ended June 30, 2014

Net Position Allocation as of June 30, 2014 (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	\$ 4,553,283,316	30	30%
U.S. equity hedge funds	1,485,145,060	10	10
International equity	2,346,576,036	16	20
Commingled funds ⁴	733,010,980	5	-
Fixed income ¹	2,416,272,292	16	16
Bank loans	689,256,558	5	4
Real estate	1,483,445,971	10	10
Private equity ²	667,730,266	4	5
Real assets ²	524,284,793	3	5
Cash ³	210,370,103	1	-
Total	<u>\$ 15,109,375,375</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.

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Analysis of Operations (Unaudited)

Schedules of Soft Dollar Credits (Unaudited)

Years ended June 30, 2014 and 2013

	2014	2013
Soft dollar credits outstanding, at beginning of fiscal year	\$ 5,917	\$ -
Soft dollar credits earned	9,851	5,917
Bank of New York payout amount	(11,139)	-
Soft dollar credits outstanding, at end of fiscal year	<u>\$ 4,629</u>	<u>\$ 5,917</u>

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, 2014 and 2013

	2014	2013
Investment brokerage firms:		
ABG Sundal Collier Inc.	\$ 6,050	\$ -
Auerbach Grayson Co. Inc.	7,488	8,884
Banc of America Securities Inc.	16,544	40,873
Barclays Capital	22,808	39,281
Blaylock	9,629	8,221
Bley Investment Group	-	10,563
Bloomberg Tradebook	-	5,940
BMO Harris	-	7,558
BNY Brokerage	14,429	37,430
BTIG Trading	14,057	22,933
Cabrera Capital Markets LLC	98,807	150,354
Canacord Genuity Inc.	5,665	-
Cantor Fitzgerald & Co.	61,173	92,288
CastleOak Securities	18,673	11,622
Cheevers & Company	188,919	141,336
CIMB Group	10,746	-
Citigroup Smith Barney Inc.	64,237	93,499
CLSA Singapore Pte. Ltd.	5,500	18,698
ConvergEx	7,028	21,331
Craig Hallum	6,720	-
Credit Lyonnais Securities	13,269	11,447
Credit Suisse First Boston Corp.	63,181	81,819
CRT Capital	5,220	-
Deutsche Banc Securities Inc.	31,950	37,147
Direct Access Partners	-	66,622
DNB Markets	6,121	8,113
Fig Partners	28,197	40,050
Friedman Billings and Ramsey & Co. Inc.	21,215	11,718
Global Hunter Securities LLC	6,288	-
Goldman Sachs & Company	39,555	39,837

(Continued)

ILLINOIS STATE BOARD OF INVESTMENT
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Analysis of Operations (Unaudited)
Schedules of Investment Commissions (Unaudited) (Continued)
Years ended June 30, 2014 and 2013

	2014	2013
Investment brokerage firms (Continued):		
Goodbody Stockbrokers	\$ -	\$ 5,308
Greentree Brokerage	9,381	9,245
HSBC Securities	5,053	7,164
Instinet	57,709	85,514
Investment Technology Group	84,731	84,379
Ivy Securities	-	5,093
J.P. Morgan Securities, Inc.	37,383	34,863
Jefferies & Company	34,851	13,412
Joh Berenberg, Glossler & Co.	-	12,655
Jones Trading	11,887	17,410
KCG Corp Access	6,196	-
Keefe Bruynette and Woods Inc.	-	5,014
KeyBank Inc	17,718	-
Knight Equity Markets	-	9,534
Liberum Capital	13,018	7,915
Liquidnet Inc.	37,201	62,198
Loop Capital Markets	406,293	260,028
M. Ramsey King Securities	27,893	31,771
Macquarie Equities Ltd	30,191	33,833
MainFirst Group	10,793	-
Merrill Lynch Pierce Fenner & Smith	37,638	18,580
Mischler Financial Group	6,562	-
Morgan Stanley & Co.	36,323	64,929
MR Beal	6,107	22,471
Needham & Co.	12,465	-
Nomura Securities	-	45,594
North South Capital	47,582	11,524

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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, 2014 and 2013

	2014	2013
Investment brokerage firms (Continued):		
Oppenheimer	\$ 28,253	\$ -
Pacific Crest Securities Inc	8,189	-
Piper, Jaffrey & Hopwood Inc.	-	5,123
Podesta & Co.	-	5,823
Rabo Securities	-	5,114
Ramsey King	16,633	36,672
Raymond James & Assoc	12,428	-
RBC Capital Markets	-	10,271
Redburn Partners LLC	-	9,362
Robert W. Baird & Co.	61,118	28,751
Sanford C. Bernstein	23,546	54,441
Sidoti & Co.	5,406	-
Societe Generale	16,140	39,621
State Street Global	-	9,664
Stephens Inc.	9,896	-
Sterne, Agee & Leach	6,910	-
Stiffel, Nicolaus & Company Inc.	18,599	34,139
Telsey Advisory Group	-	9,447
UBS Securities	49,486	104,274
Weeden & Co.	29,130	10,925
Wells Fargo	5,680	-
William Blair & Co.	5,346	9,399
Williams Capital Group	78,613	107,690
Various (Under \$5,000)	159,604	137,973
	<u>\$ 2,245,421</u>	<u>\$ 2,474,687</u>

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