



State of Wisconsin Investment Board Annual Report

Fiscal Year Ended June 30, 2013



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Introduction

Message from the Executive Director

During my first year as executive director of the State of Wisconsin Investment Board (SWIB), I had the pleasure of meeting people from across the state that are part of the Wisconsin Retirement System (WRS). In talking with active public employees, employers and retirees, I was given the opportunity to discuss the WRS, its unique design and SWIB's performance to ensure the system meets its obligations today and in the future. It was encouraging to hear from participants that they believe in the system and are thankful that the WRS is not facing many of the same problems other public pension funds across the country are facing. However, those same participants I talked with all wanted to know what SWIB is doing to protect the solid foundation of the WRS, given the volatile economic times in which we live.



The financial downturn of 2008 was unprecedented and virtually no type of public or private investment went untouched. WRS participants personally felt the impact through increased contributions for active employees and decreased annuity payments for retirees. The impact felt by participants has been, understandably difficult. However, through that downturn, the WRS remained strong and the system functioned the way it was designed. While other public pension funds are struggling to meet obligations, the WRS has remained one of the top-funded and best managed public pension systems in the country. In addition to favorable returns, the WRS stands on solid ground today because employers and employees have made the required contributions to the system and the Legislature has designed a system that has employees, retirees and employers all sharing in the investment risk and rewards of the plan. Together, we have worked to protect the system and build on the solid foundation of the WRS.

While having a pension system as well respected as the WRS is good, it means we have to work that much harder to ensure its continued stability. The economy, although showing signs of recovery, is still faced with challenges. SWIB remains prudent in its management of the retirement funds of public employees in Wisconsin. Since its creation in 1951, SWIB has made significant changes in the management of the trust funds and the way it invests billions of dollars, all in an effort to help protect the WRS from extreme swings in the market and, most importantly, dramatic declines. That is more true today than at any other time in the history of the system. Those changes have allowed for the hiring of talented and capable investment professionals to manage the trust funds and generate positive returns while managing costs, all of which benefit the WRS, its participants and the state. The results have been impressive. Our investment strategies and the corresponding returns, not employee or employer contributions, have generated on average 80% of the assets that are in the fund today. To ensure the system remains a solid performer, we continue to make changes and implement initiatives that will help meet the goals of the WRS and its participants. Some of those initiatives include developing additional investment strategies; managing more assets with internal staff at lower costs, improving systems and processes; and creating a dynamic strategic plan to help guide the agency as it moves forward.

While there is always a great deal of uncertainty in the investment world, one thing is certain. We will continue to do our best to serve the participants of the Wisconsin Retirement System by providing a critical piece of their retirement savings- the WRS pension benefit.

A handwritten signature in black ink, reading "Michael Williamson". The signature is fluid and cursive, with a long horizontal line extending from the end.

Michael Williamson
Executive Director

Mission

To provide prudent and cost-effective management of funds held in trust by the State. This is achieved with solid investment returns, consistent with the purpose and risk profile of each fund.

Vision

SWIB strives to be a premier public investment organization, a place where professional excellence and public service thrive. Superior investment returns, the highest ethical and professional standards, teamwork and a rewarding work environment will make SWIB the investment management organization of choice.

The State of Wisconsin Investment Board (SWIB) is a state agency responsible for investing the assets of the Wisconsin Retirement System (WRS), the State Investment Fund (SIF) and five smaller trust funds established by the State. Investments are made according to the purpose and risk profile of each trust. The WRS -- the 9th largest U.S. public pension fund and the 30th largest pension fund in the world -- includes the Core Retirement Investment Trust Fund (Core Fund) and the Variable Retirement Investment Trust Fund (Variable Fund).

The Investment Board was created under section 15.76 of the state statutes. The Board's duties as manager of these trust funds are provided in Chapter 25 of the statutes. SWIB staff and Trustees are fiduciaries of the pension funds and are governed by the "prudent investor" standard, which requires them to use the diligence, skill and care that a prudent person acting in a similar capacity and with the same resources would use in managing a large public pension fund.

The law also requires SWIB to make investment decisions and conduct every aspect of its operations in the best financial interest of the trust funds.

Strong Governance

SWIB is directed by a nine-person, independent Board of Trustees. The Board of Trustees appoints the executive director and internal audit director of the Investment Board and sets the overall policy for SWIB. The executive director oversees the staff, develops and recommends agency and investment policies for Board adoption, and ensures adherence to state law and policies. The chief investment officer (CIO) serves as chair of the Investment Committee. The committee provides oversight to the agency's investments, reports to Trustees and makes recommendations to Trustees.

Experienced Staff

SWIB's investments are managed by its own professional staff and by outside money management firms. With support from the Governor and Legislature, SWIB has the flexibility to build a strong internal management program. SWIB employs a staff of approximately 141 people, including portfolio managers, analysts and traders who are responsible for daily investment decisions made within the parameters of the board established investment policy, as well as well-trained professionals with legal, financial, accounting and administrative expertise. SWIB adheres to Chartered Financial Analyst (CFA) ethical standards. About 70% of SWIB staff hold advanced degrees or professional certifications. One-third holds multiple degrees or certifications.

Internal Management

Having a strong internal management program provides a significant financial benefit to the WRS. SWIB's Board of Trustees has committed to this concept, growing the number of internal staff positions over the years and, enabling SWIB to increase the share of WRS assets managed internally from 20.8% in 2007 to 56% in 2013. Further increases in internal management are under consideration. As an added benefit, SWIB's dedication to internal management has also resulted in new investment jobs being created in Wisconsin. SWIB provides top-quartile performance relative to peers and is a low cost manager based on an independent study by CEM Benchmarking, Inc.

Board of Trustees

The Board of Trustees is responsible for setting long-term investment policies, asset allocation, benchmarks, fund level risk, and monitoring investment performance. The Board is comprised of the following:

- Six public members appointed by the Governor and confirmed by the State Senate including four with at least 10 years investment experience, and one with at least 10 years financial experience and who works for a local government in the Local Government Investment Pool.
- Educator participant in the Wisconsin Retirement System (WRS) appointed by the Teachers Retirement Board.
- Non-educator participant in the WRS appointed by the Wisconsin Retirement Board.
- Secretary of the Department of Administration or designee.

Public Members*

1. Lon Roberts, Board Chair, Attorney at Ruder Ware, Wausau
2. Thomas Boldt, Board Vice Chair, President of the Boldt Group, Inc. and CEO of The Boldt Co., Appleton
3. Bruce Colburn, Director, Central States Property Services Division, Services Employees International Union
4. Norm Cummings, Director of Administration, Waukesha County
5. William Levit, Jr., Attorney, Godfrey & Kahn S.C., Milwaukee
6. (Vacant)



Lon Roberts



Thomas Boldt



Bruce Colburn



Norm Cummings



Mike Huebsch



William Levit, Jr.

WRS Participant Members*

1. Wayne McCaffery, Retired Teacher, Stevens Point
2. David Stella, Board Secretary, Non-educator, retired Secretary, Department of Employee Trust Funds



Wayne McCaffery

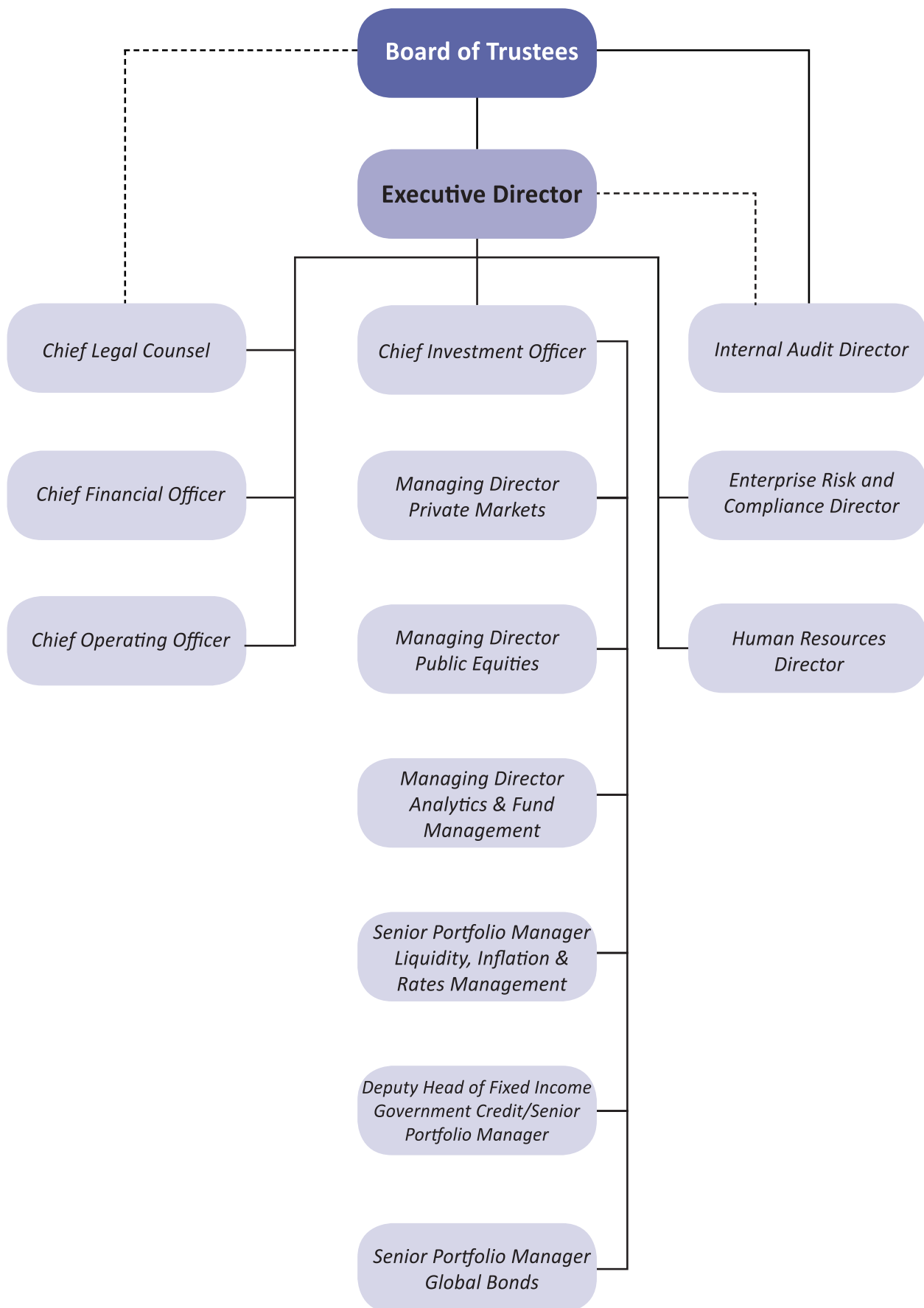


David Stella

Department of Administration

1. Mike Huebsch, Wisconsin Department of Administration Secretary

*Appointed Board members serve six-year terms.



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Financial Section



STATE OF WISCONSIN

Legislative Audit Bureau

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Joe Chrisman
State Auditor

Independent Auditor's Report on the Financial Statements and Other Reporting Required by *Government Auditing Standards*

Senator Robert Cowles and
Representative Samantha Kerkman, Co-chairpersons
Joint Legislative Audit Committee

Mr. Michael Williamson, Executive Director, and
Members of the Board of Trustees
State of Wisconsin Investment Board

Report on the Financial Statements

We have audited the accompanying financial statements and the related notes of the Retirement Funds (Core Retirement Investment Trust Fund and Variable Retirement Investment Trust Fund) of the State of Wisconsin as of and for the year ended June 30, 2013, as listed in the table of contents.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

Our responsibility is to express opinions on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, which is issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor

considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of the accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinions on these financial statements.

Opinions

In our opinion, the financial statements referred to in the first paragraph present fairly, in all material respects, the respective financial position of each of the Retirement Funds as of June 30, 2013, and the respective changes in financial position for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Emphases of Matter

As discussed in Note 1 to the financial statements, the financial statements referred to in the first paragraph present only the investment activity of the Retirement Funds attributable to the Investment Board. The financial statements do not purport to, and do not, present fairly the financial activity of the Retirement Funds attributable to the Department of Employee Trust Funds. Further, they do not purport to, and do not, present fairly the financial position of the Investment Board or of the State of Wisconsin as of June 30, 2013, or the changes in financial position for the year then ended, in accordance with accounting principles generally accepted in the United States of America. Our opinions are not modified with respect to this matter.

As discussed in Note 2c to the financial statements, the Investment Board implemented Governmental Accounting Standards Board Statement Number 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position*, which made presentation changes to the Retirement Funds financial statements. Our opinions are not modified with respect to this matter.

As discussed in Note 2d to the financial statements, the financial statements include investments that do not have readily ascertainable market prices and are valued based on a variety of third-party pricing methods. We have reviewed the procedures used by the Investment Board in arriving at estimates of the values of such investments and have inspected underlying documentation. Given the circumstances, we believe the procedures are reasonable and the documentation appropriate. However, because of the inherent uncertainty of valuation, those estimated values may differ from the values that would have been used had a ready market for the investments existed. Our opinions are not modified with respect to this matter.

Other Matter

Our audit was conducted for the purpose of forming opinions on the financial statements of the Retirement Funds. The supplementary information included as Management's Discussion and Analysis, which precedes the financial statements, is presented for purposes of additional analysis and is not a required part of the financial statements. We have applied certain limited

procedures to the information that included inquiries of management about the methods of preparing the information. We further compared the information for consistency with management's responses to our inquiries, the financial statements, and other knowledge we obtained during our audit of the financial statements. However, we do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to do so. The introduction section of the annual report is presented for purposes of additional analysis and is not a required part of the financial statements. Such information has not been subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we do not express an opinion or provide any assurance on it.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued a report dated November 25, 2013, on our consideration of the Investment Board's internal control over financial reporting for the Retirement Funds; our tests of its compliance with certain provisions of laws, regulations, and contracts; and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Investment Board's internal control over financial reporting and compliance.

LEGISLATIVE AUDIT BUREAU

A handwritten signature in black ink, appearing to read "Joe Chrisman", written in a cursive style.

Joe Chrisman
State Auditor

November 25, 2013

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Retirement Funds

Management Discussion and Analysis

The State of Wisconsin Retirement Funds' discussion and analysis of the financial activities for the fiscal year ended June 30, 2013, is presented by management as an introduction to the financial statements. It is meant to assist the reader in understanding the financial statements by providing an overall review of the financial activities during the year as well as to provide a comparison of the prior year's activity and results.

Overview of Basic Financial Statements

The State of Wisconsin Investment Board (SWIB) is responsible for managing the assets of the Wisconsin Retirement System (WRS). The Core Retirement Investment Trust Fund (Core Fund) and Variable Retirement Investment Trust Fund (Variable Fund), collectively (Retirement Funds), represent the assets of the WRS. Following this section are the financial statements and footnotes which reflect only the investment activity of the Retirement Funds. Retirement reserves, contribution revenue and benefit expense are specifically excluded from presentation in these statements although contribution revenue and benefit expenses are reflected in "Net Disbursements" in the Statement of Changes in Net Investment Position. The Wisconsin Department of Employee Trust Funds (ETF) prepares a Comprehensive Annual Financial Report for the WRS and can be found on their website: www.etf.wi.gov.

The **Statement of Net Investment Position** provides information on the financial position of

the Retirement Funds at year-end. It reflects the investment assets available for payment of future benefits and any current liabilities related to the investments.

The **Statement of Changes in Net Investment Position** presents the results of the investing activities during the year. The changes reflected on this statement support the overall change that has occurred to the prior year's net investment position on the Statement of Net Investment Position.

The **Notes to the Financial Statements** provide additional information that is essential to a full understanding of the data presented in the financial statements. The notes provide more detail about accounting policies, significant account balances and activities, material risks, obligations, contingencies and subsequent events, if any.

The financial statements and related notes are prepared in accordance with Governmental Accounting Standards Board Pronouncements.

Retirement Funds

Approximately 579,000 people participate in the WRS, including current and former employees of Wisconsin's state agencies, most local governments and school districts in Wisconsin. Contributions made to the WRS by these employees, and their employers, are invested by SWIB to finance retirement and other benefits. The WRS had a combined Net Investment Position of \$86.5 billion as of June 30, 2013.

Time Weighted Annualized Returns

June 30, 2013

	1-Year Return %	5-Year Return %	10-Year Return %
Core Fund	11.1	5.2	7.8
Benchmark	10.2	4.6	7.4
Variable Fund	19.9	5.8	7.8
Benchmark	19.2	5.1	7.7

Core Retirement Investment Trust Fund

The larger of the two trust funds comprising the WRS is the Core Fund with a Net Investment Position of \$80.3 billion at the end of fiscal year 2013. All WRS members have at least half, if not all, of their pension contributions invested in the Core Fund. It is a diversified, balanced fund invested for the long-term needs of the WRS. Diversification helps to stabilize the effects of market changes. The investment objective of this trust fund is to meet or exceed an average 7.2% annual return over the long-term, which consists of an annual rate of return of 4.0% above an estimated 3.2% growth in wages. This objective is based on market rate of return and actuarial assumptions needed to meet obligations of the WRS.

The statements presented here reflect the investment activity of the Core Fund as well as changes in cash balances due to net disbursements related to ETF. Net disbursements include, but are not limited to, benefit payments, contribution receipts, transfers to/from the Variable Fund and administrative expenses.

Condensed Core Fund financial information for the fiscal years ended June 30, 2013 and June 30, 2012 is included in the table entitled **Core Fund Condensed Financial Information**.

Cash and Cash Equivalents increased by \$835.6 million when comparing fiscal year-end 2013 to 2012. There are several reasons for the increase in cash balances, including the following:

Core Fund Condensed Financial Information

	2013	2012	% Change
Cash and Cash Equivalents	\$ 3,277,049,696	\$ 2,441,405,647	34
Receivables	962,685,753	455,084,834	112
Invested Securities Lending Collateral	1,288,521,206	1,144,719,006	13
Prepaid Expenses	5,803,750	8,477,409	(32)
Investments	77,872,120,685	72,890,068,963	7
Total Investment Assets	83,406,181,090	76,939,755,859	8
Payables & Other Liabilities	854,067,547	276,698,888	209
Securities Lending Collateral Liability	1,288,521,206	1,144,719,006	13
Obligations Under Reverse Repurchase Agreements	968,176,006	649,424,494	49
Total Investment Liabilities	3,110,764,759	2,070,842,388	50
Net Investment Position Held in Trust	\$ 80,295,416,331	\$ 74,868,913,471	7
Investment Income	\$ 8,226,827,782	\$967,740,336	750
Investment Expense	(322,237,795)	(239,859,017)	34
Net Investment Income	7,904,589,987	727,881,319	986
Net Disbursements - Department of Employee Trust Funds	(2,478,087,127)	(2,585,303,774)	(4)
Net Increase (Decrease) in Net Investment Position Held in Trust	\$ 5,426,502,860	\$ (1,857,422,455)	392

Retirement Funds

Management Discussion and Analysis

- The vast majority of the change relates to securitized cash balances in liquidity portfolios. These portfolios had a combined cash balance of \$1.3 billion at June 30, 2013, as compared to \$552.5 million the prior fiscal year-end. The liquidity portfolios are the primary source of cash for near-term benefit payments and operating cash needs. Cash is securitized with public market instruments through the use of futures contracts. Cash balances in these portfolios are maintained within a predetermined range. The liquidity portfolios' cash balances were closer to the top of this range at June 30, 2013, as compared to the prior fiscal year-end, when the balances were nearer to the bottom of the range.
- Another contributing factor to the increase in Cash and Cash Equivalents relates to a portfolio established in 2013 which maintains an investment in a short-term cash fund for the express purpose of being available to fund new investment ideas. This portfolio's cash and cash equivalents balance totaled \$104.3 million at June 30, 2013.
- The Core Fund also held an additional \$96.7 million in cash at the end of fiscal year 2013, as compared to 2012, in order to meet margin requirements associated with U.S. Treasury futures contracts. Futures positions increased over the 2013 fiscal year due to SWIB's investment strategy to efficiently reduce equity exposure, reduce total fund volatility and better position the fund for varying economic environments.

Receivables increased by 112% when comparing current fiscal year end balances to the prior year end balances. This increase is mainly due to higher investment sales receivable balances resulting from deferrals of proceeds associated with the sale of private equity limited partnership interests, as well as the pending settlement of trades related to rebalancing equity index positions.

The Core Fund's Invested Securities Lending Collateral and Securities Lending Collateral Liability increased by 13% as of June 30, 2013, as compared to June 30, 2012. The collateral balances represent the cash collateral held for securities lending transactions in separately managed accounts. The Core Fund's securities lending activity increased by almost 26% when comparing June 30, 2013 to the prior fiscal year-end. The majority of the increase is due to an increase in lending fixed income securities.

Payables & Other Liabilities increased by 209% when comparing fiscal year-end 2013 to 2012. A few factors contribute to this change:

- The largest contributor to the increase is pending trade activity. About 40% of the increase is attributed to the timing of the reconstitution of indexed equity assets which transpired over the 2013 fiscal year end. Another 38% of the increase was due to pending purchases of bonds that had previously been replicated through the use of futures contracts.
- The remaining contributor to the change in Core Fund Payables & Other Liabilities is an increase of approximately \$88.3 million in Short Sell Obligations. A short sale transaction is created when the investor sells a security it does not own, in anticipation of purchasing the security later at a lower price. SWIB's investment guidelines permit certain portfolios to short securities.

The balance of Obligations Under Reverse Repurchase Agreements increased by \$318.7 million over the course of the 2013 fiscal year. SWIB increased its implementation of risk reducing strategies whereby the Core Fund's overall exposure to stock holdings was reduced and exposure to lower volatility securities was increased through a modest use of leverage. Reverse repurchase agreements involve the sale of assets with the simultaneous agreement to repurchase those assets for a pre-determined price, plus interest, at a future date. The proceeds from these reverse repurchase agreements were invested in U.S. Treasury Inflation Protected Securities.

Core Fund Time Weighted Annualized Asset Class Returns

	2013 Return %	2012 Return %
Public Equities	18.9	(4.5)
Fixed Income	0.0	7.6
Inflation Sensitive Assets	(4.7)	13.0
Real Estate	15.1	14.3
Private Equity	13.2	6.5
Multi Asset	7.9	3.3

Investment Income increased by \$7.3 billion, when comparing fiscal year 2013 to 2012. This change is due to a total fund investment return of 11.1% in fiscal year 2013, compared to a total fund investment return of 1.3% for the previous fiscal year. Core Fund asset class returns for fiscal year 2013 and 2012 are presented in the table entitled **Core Fund Time Weighted Annualized Asset Class Returns**.

Investment Expense increased by 34% when comparing fiscal year 2013 to 2012. This increase is explained in part by an increase of \$52.5 million in base and performance fees paid to external managers. Base management fees are calculated as a percentage of assets under management. Performance fees are accrued when a portfolio exceeds specified performance targets.

Base fees increased by \$6.4 million over the prior fiscal year. As a whole, the percentage of the Core Fund's externally managed assets decreased during fiscal year 2013, dropping from 47.3% at June 30, 2012 to 45.8% at June 30, 2013. However, externally managed assets tend to be invested in higher-cost strategies whereby SWIB seeks to capitalize on external managers' expertise in highly specialized markets or products. The increase in base fees over

the prior fiscal year is primarily the result of market value appreciation and increased investment with these types of managers.

Performance fees accounted for a \$39.1 million increase in fees accrued to external managers. The Core Fund had certain external managers which exceeded their performance targets by a greater extent in fiscal 2013 than the prior fiscal year, thus generating an increase in fees.

Fees incurred on private market assets increased by nearly \$7.0 million, when comparing fiscal year 2013 to 2012. This asset type generally has higher fees at the beginning of the investment's life because management fees are typically based on committed assets, rather than assets under management. During fiscal year 2013, SWIB committed to funding an additional \$1.4 billion, contributing to the increase in fees.

Another contributor to the increase in Investment Expense is attributed to a large portion of the Core Fund's operating expenditures which were charged against an accumulated budget reserve balance in fiscal year 2012. During fiscal years 2000 to 2011, SWIB's budget authority was based on the percentage of assets under management. Under this budget process, any unspent funds were accumulated in a reserve to mitigate the risk of operating budget shortfalls in down markets. In 2011, the Wisconsin Legislature eliminated SWIB's basis point budget process, allowing SWIB's Board to approve the internal operating budget based on operating and staffing needs. With this change, the Board approved eliminating the previously accumulated budget reserve, applying the balance to fiscal year 2012 expenses. Core Fund fiscal year 2012 operating expenditures totaled \$27.1 million, of which \$19.2 million was charged against the reserve balance. In comparison, operating expenditures for fiscal year 2013 totaled \$31.9 million.

Retirement Funds

Management Discussion and Analysis

Variable Retirement Investment Trust Fund

The Variable Fund allows active employees participating in the WRS to put half of their pension fund contributions into this stock fund. Approximately 17% of WRS members participate in the Variable Fund, with a Net Investment Position of \$6.2 billion at the end of fiscal year 2013. Employees who choose this fund accept a higher degree of market risk. The investment objective of the Variable Fund is to meet or exceed broad equity market indices over a full market cycle.

Condensed Variable Fund financial information for the fiscal years ended June 30, 2013 and June 30, 2012 is included in the table entitled **Variable Fund Condensed Financial Information**.

Balances for Receivables, as well as Payables & Other Liabilities, increased significantly over the previous fiscal year largely due to an increase in pending investment sales and purchases. The 2013 balances were larger due to the timing of the reconstitution of indexed equity assets which transpired over the 2013 fiscal year-end.

The Variable Fund's Invested Securities Lending Collateral and Securities Lending Collateral Liability decreased by 24% at June 30, 2013, when compared to June 30, 2012. The collateral balances represent the cash collateral held for securities lending transactions in separately managed accounts. The non-cash collateral balances are not presented within the WRS financial statements because SWIB does not have the ability to pledge or sell the securities without

Variable Fund Condensed Financial Information

	2013	2012	% Change
Cash and Cash Equivalents	\$ 203,658,472	\$ 198,041,451	3
Receivables	213,879,106	45,018,450	375
Invested Securities Lending Collateral	147,499,687	194,144,537	(24)
Investments	5,995,963,801	5,193,072,861	15
Total Investment Assets	6,561,001,066	5,630,277,299	17
Payables & Other Liabilities	186,561,721	33,593,405	455
Securities Lending Collateral Liability	147,499,687	194,144,537	(24)
Total Investment Liabilities	334,061,408	227,737,942	47
Net Investment Position Held in Trust	\$ 6,226,939,658	\$ 5,402,539,357	15
Investment Income	\$ 1,054,641,417	\$ (107,230,449)	1,084
Investment Expense	(8,669,119)	(5,290,972)	64
Net Investment Income	1,045,972,298	(112,521,421)	1,030
Net Disbursements - Department of Employee Trust Funds	(221,571,997)	(244,179,486)	(9)
Increase (Decrease) in Net Investment Position Held in Trust	\$ 824,400,301	\$ (356,700,907)	331

a borrower default. On the whole, the Variable Fund's securities lending collateral holdings (both cash and non-cash) increased 87% when comparing June 30, 2013 to the prior fiscal year-end. Despite the considerable increase in securities lending collateral holdings overall, the reduction in the Invested Securities Lending Collateral and Securities Lending Collateral Liability as reported is explained by a large shift in the type of collateral provided by the borrowers. Securities borrowers are increasingly electing to provide non-cash collateral instead of cash collateral.

Fiscal year 2013 Investment Income increased by \$1.2 billion, when compared with the prior year. The increase in income was the result of a total fund investment return of 19.9% in fiscal year 2013, as compared to -1.6% in fiscal year 2012.

The Variable Fund's Investment Expense increased by 64%, as compared to the previous fiscal year. Several factors contribute to the overall increase:

- Performance fees accounted for approximately one-half of the increase in Investment Expense. The Variable Fund had certain external managers

which exceeded their performance targets by a greater extent in fiscal 2013 than the prior fiscal year, thus generating an increase in fees.

- A majority of the remaining change in Investment Expense is explained by the Variable Fund's operating expenditures which were charged against an accumulated budget reserve balance in fiscal year 2012. During fiscal years 2000 to 2011, SWIB's budget authority was based on the percentage of assets under management. Under this budget process, any unspent funds were accumulated in a reserve to mitigate the risk of operating budget shortfalls in down markets. In 2011, the Wisconsin Legislature eliminated SWIB's basis point budget process, allowing SWIB's Board to approve the internal operating budget based on operating and staffing needs. With this change, the Board approved eliminating the previously accumulated budget reserve, applying the balance to fiscal year 2012 expenses. Variable Fund operating expenditures for fiscal year 2012 totaled \$1.6 million, of which \$1.1 million was charged against the reserve balance. In comparison, fiscal year 2013 operating expenditures totaled \$1.8 million.

Retirement Funds

Financial Statements

Statement of Net Investment Position

as of June 30, 2013

	Core Retirement Investment Trust Fund	Variable Retirement Investment Trust Fund
Investment Assets		
Cash and Cash Equivalents	\$ 3,277,049,696	\$ 203,658,472
Due from Other Funds	63,403	-
Receivables:		
Interest & Dividends	250,340,731	10,974,210
Securities Lending Income	1,973,714	212,120
Investment Sales	710,307,905	202,692,776
Invested Securities Lending Collateral	1,288,521,206	147,499,687
Prepaid Expenses	5,803,750	-
Investments (at fair value):		
Stocks	38,314,831,045	5,993,602,867
Fixed Income	25,350,610,476	-
Limited Partnerships	10,003,179,161	-
Multi Asset	3,300,779,676	-
Real Estate	756,622,013	-
Preferred Securities	143,850,535	10,976,639
Convertible Securities	52,226,082	-
Foreign Currency Contracts	13,531,085	516,015
Option Contracts	(27,344,490)	(7,511,388)
Futures Contracts	(36,164,898)	(1,620,332)
Total Investment Assets	83,406,181,090	6,561,001,066
Investment Liabilities		
Payable for Investments Purchased	723,550,779	174,685,481
Obligations Under Reverse Repurchase Agreements	968,176,006	-
Short Sell Obligations	88,744,819	10,846,626
Collateral Due to Counterparty	3,890,000	-
Accounts Payable	36,700,150	924,996
Other Liabilities	1,181,799	41,215
Due to Other Funds	-	63,403
Securities Lending Collateral Liability	1,288,521,206	147,499,687
Total Investment Liabilities	3,110,764,759	334,061,408
Net Investment Position Held in Trust	\$ 80,295,416,331	\$ 6,226,939,658

The accompanying notes are an integral part of this statement.

Statement of Changes in Net Investment Position

For the Fiscal Year Ended June 30, 2013

	Core Retirement Investment Trust Fund	Variable Retirement Investment Trust Fund
Additions		
Investment Income:		
Net Increase (Decrease) in the Fair Value of Investments	\$ 6,359,952,489	\$ 919,660,346
Interest	654,607,349	282,426
Dividends	1,014,963,820	132,169,263
Securities Lending Income	15,283,576	1,351,432
Securities Lending Rebates	9,900,670	1,416,383
Limited Partnership Income	135,224,972	-
Income from Real Estate	39,121,727	-
Less		
Investment Expense	322,237,795	8,669,119
Securities Lending Fees	2,226,821	238,433
Net Investment Income	7,904,589,987	1,045,972,298
Deductions		
Net Disbursements - Department of		
Employee Trust Funds	(2,478,087,127)	(221,571,997)
Net Increase (Decrease) in Net Investment Position Held in Trust	5,426,502,860	824,400,301
Net Investment Position Held in Trust		
Beginning of Year	74,868,913,471	5,402,539,357
End of Year	\$ 80,295,416,331	\$ 6,226,939,658

The accompanying notes are an integral part of this statement.

Retirement Funds

Notes to the Financial Statements

1. Description of Funds

The State of Wisconsin Investment Board (SWIB) is responsible for managing the assets of the Wisconsin Retirement System (WRS). The Core Retirement Investment Trust Fund (Core Fund) and the Variable Retirement Investment Trust Fund (Variable Fund), collectively (Retirement Funds), represent the assets of the WRS. The statements presented here reflect only the investment activity of these funds. Excluded from presentation in the statements are, for example, retirement reserves, contribution revenue, and benefit expense.

All of the Retirement Funds' administrative expenses are funded through employer and employee contributions and investment earnings. The administrative expenses are reflected in "Investment Expense" in the Statement of Changes in Net Investment Position. This represents SWIB's operating expenses as well as expenses directly related to the investment function such as external management fees, legal fees, custodial bank fees, and investment consulting fees.

A. Core Retirement Investment Trust Fund

The Core Fund is managed by SWIB with oversight by a Board of Trustees as authorized in Wisconsin Statutes ss. 25.15 and 25.17. The Core Fund and SWIB are not registered with the Securities and Exchange Commission as an investment company. The investments of the Core Fund consist of a diversified portfolio of securities. SWIB is required to make investment management decisions for the Retirement Funds solely for the benefit of the members of the WRS. Wisconsin Statutes s. 25.182, authorizes SWIB to manage the Core Fund in accordance with the "prudent investor" standard of responsibility as described in Wisconsin Statutes s. 25.15(2) which requires that SWIB manage the Retirement Funds with the diligence, skill and care that a prudent person acting in a similar capacity and with the same resources would use in managing a large public pension fund.

The Core Fund consists primarily of assets invested for the WRS which is administered by the Department of Employee Trust Funds (ETF) in accordance with Chapter 40 of the Wisconsin Statutes. All WRS contributions are invested in this trust fund unless participants have elected to have one-half of their contributions invested in the Variable Fund. In addition to the retirement contributions, the assets of various other benefit programs are invested in the Core Fund as listed in the table entitled **Other Benefit Programs Within the Core Fund**.

Other Benefit Programs Within the Core Fund

June 30, 2013 (Dollars in Millions)

Program	
Accumulated Sick Leave	\$ 2,174.8
Duty Disability Insurance	539.8
Long Term Disability Insurance	195.6
Active Employee Health Insurance	294.0
Milwaukee Retirement System	152.0
Income Continuation Insurance	89.1
Police and Firefighters Pension Group	23.8
Total	<u>\$ 3,469.1</u>

B. Variable Retirement Investment Trust Fund

The Variable Fund is managed by SWIB with oversight by a Board of Trustees as authorized by Wisconsin Statutes ss. 25.15 and 25.17. The Variable Fund and SWIB are not registered with the Securities and Exchange Commission as an investment company. Wisconsin Statutes s. 25.17(5) states assets of the Variable Fund shall be invested primarily in equity securities which shall include common stocks, real estate or other recognized forms of equities whether or not subject to indebtedness, including securities convertible into common stocks and securities of corporations in the venture capital stage. Subject to

that requirement, SWIB may invest the Variable Fund in any manner consistent with the “prudent investor” standard of responsibility in Wisconsin Statutes s. 25.15(2), which requires that SWIB manage the trust funds with the diligence, skill and care that a prudent person acting in a similar capacity and with the same resources would use in managing a large public pension fund.

The Variable Fund consists primarily of the assets invested for the WRS. In addition, the Milwaukee Retirement System had \$21.1 million invested in the Variable Fund as of June 30, 2013.

Participation in the Variable Fund is at the option of the employee. Participants have elected to invest one-half of their retirement contributions and matching amounts of employer contributions to this fund, and have the remainder invested in the Core Fund. Individual participants in the Variable Fund have a one-time option to terminate their Variable Fund participation and transfer their account to the Core Fund.

2. Significant Accounting Policies

A. Basis of Presentation

The accompanying financial statements were prepared in conformity with generally accepted accounting principles (GAAP) for governments as prescribed by the Governmental Accounting Standards Board (GASB).

B. Measurement Focus and Basis of Accounting

The financial statements are prepared based upon the flow of economic resources measurement focus and the full accrual basis of accounting. Under the accrual basis of accounting, revenues are recognized in the accounting period in which they are earned and become measurable, and expenses are recognized in the period incurred, if measurable. Security transactions and the related gains and losses are recorded on a trade date basis. Dividend income is recorded on the ex-dividend date, and interest income is accrued as earned.

C. New Accounting Pronouncement

In June 2011, GASB issued Statement No. 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position*. The objective of this statement is to provide financial reporting guidance for deferred outflows of resources and deferred inflows of resources as required elements of the financial statements. The implementation of this statement did not impact the financial position of the Retirement Funds. However, the adoption of this statement resulted in presentation changes to replace “Net Investment Assets” with “Net Investment Position” on the financial statements.

D. Valuation of Securities

The investments of the Retirement Funds are reported in the Statement of Net Investment Position at fair value as prescribed by GASB and per Wisconsin Statutes s. 25.17(14). Unrealized gains and losses are reflected in the Statement of Changes in Net Investment Position as “Net Increase (Decrease) in the Fair Value of Investments.”

The fair value of the Retirement Funds’ assets are obtained or estimated in accordance with a pricing hierarchy established with SWIB’s custodian, Bank of New York Mellon (BNY Mellon). As prescribed by the hierarchy, a variety of independent pricing sources are used to price assets based on type, class or issue.

When a portfolio includes securities or instruments for which the custodial bank does not receive fair value information from its vendor pricing sources, a variety of third party pricing methods are used, including appraisals, pricing models and other methods deemed acceptable by industry standards.

Privately held debt, which is included in “Fixed Income” investments on the Statement of Net Investment Position, is priced using a multi-tiered approach that prices each holding based on the best available information using the following hierarchy of pricing sources:

1. Custodian supplied prices for assets that are in the Barclays Capital U.S. Aggregate Bond Index

Retirement Funds

Notes to Financial Statements

2. Prices provided by a third party with expertise in the bond market
3. Modeled prices where interest rate spreads are supplied by a third party

In a few instances, privately held debt cannot be priced by one of the above three sources. In these circumstances, the investment is priced using an alternative bond index price or, if no independent quotation exists, the investment is priced by SWIB management, usually at cost.

For alternative investments where no readily ascertainable market value exists, including limited partnerships and real estate pooled funds, fair value is estimated based on the net asset value as reported by the general partner. The capital account balance as stated in the most recent available quarterly reporting period is adjusted for subsequent cash flows to derive fair value. The financial statements of the limited partnerships and real estate pooled funds are audited by independent auditors annually.

Real estate properties wholly owned by SWIB are valued by independent appraisers every three years. In years when appraisals are not performed, properties are informally appraised by the asset advisor. Each year, audited financial statements are prepared for each property.

Monthly, SWIB values hedge funds based on statements received from each of the hedge fund's administrators. Essentially, a hedge fund administrator serves as an independent third party that protects the interests of investors. The main function of a third-party administrator is to independently calculate the net asset value of the fund. Generally, hedge fund administrators price financial instruments traded in active markets based on quoted market prices or binding dealer quotations. For certain over-the-counter instruments, fair value is determined based on valuation models used by the administrator. Annually, the financial statements prepared by the administrator are audited by independent auditors.

Derivative financial instruments are marked to fair value daily, with valuation changes recognized in income during the period the instruments are held and when the instrument is sold or expires. The nature and use of derivative instruments is discussed in Note 5.

A limited number of securities are carried at cost. Certain non-public or closely held stocks are not reported at fair value, but are carried at cost since no independent quotation is available to estimate fair value for these securities.

E. Use of Estimates

The preparation of financial statements in accordance with GAAP requires management to make estimates that affect amounts reported herein. Due to the inherent uncertainty involved, actual results could differ from those estimates.

3. Deposit and Investment Risk

A. Credit Risk

Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations to SWIB. Fixed income credit risk investment guidelines outline the minimum ratings required at the time of purchase by individual portfolios, or groups of portfolios, based on the portfolios' investment objectives. In addition, some fixed income portfolios are required to carry a minimum weighted average rating at all times. Information regarding SWIB's credit risk related to derivatives is found in Note 5.

The table entitled **Credit Quality Distribution** displays the lowest credit rating assigned by nationally recognized statistical rating organizations on debt securities held by the Retirement Funds as of June 30, 2013. Included in this table are fixed income securities, including certain short term securities, classified as cash equivalents on the Statement of Net Investment Position. Also included are interest rate sensitive investments held in the Retirement Funds' securities lending collateral reinvestment pools, which are managed by SWIB's custodian. See Note 4 for additional information regarding the securities lending

program. The table also includes SWIB's investment in commingled fixed income funds, which are not assigned ratings. Although the funds themselves are not assigned ratings, external management investment guidelines govern minimum credit quality standards for the investments within each portfolio. These standards are determined based on the investment objectives and risk parameters of each fund. The table entitled **Credit Quality Breakdown of Commingled Fixed Income Funds** presents the aggregated credit ratings for the underlying investments held by commingled fixed income funds within the Retirement Funds.

United States Treasury obligations (UST) and obligations explicitly guaranteed by the U.S. government (AGY) historically were not considered to have credit risk. However, following federal legislation which raised the statutory U.S. debt ceiling in August 2011, the three major U.S. rating agencies (Moody's Investors Service "Moody's", Fitch Investors "Fitch", and Standard & Poor's "S&P")

issued divergent perspectives regarding sovereign U.S. debt rating assignments. At June 30, 2013, SWIB's holdings of UST and AGY are included within the "AA" category.

SWIB held \$968.2 million in reverse repurchase agreements at June 30, 2013. Investment guidelines permit certain portfolios to enter into reverse repurchase agreements, which are a sale of securities with a simultaneous agreement to repurchase the securities in the future at the same price plus a stated rate of interest. The market value of the securities underlying reverse repurchase agreements exceeds the cash received, providing the dealers a margin against a decline in market value of the securities. If the counterparty defaults on their obligations to sell these securities back to SWIB or provide cash of equal value, SWIB could suffer an economic loss equal to the difference between the market value of the underlying securities plus accrued interest and the agreement obligation, including accrued interest. The counterparty credit exposure is monitored daily

Credit Quality Distribution

As of June 30, 2013

Rating	Fair Value	% of Total
P-1 or A-1	\$ 302,224,381	1
AAA/Aaa	569,047,470	2
AA/Aa	10,899,361,674	36
A	2,560,964,125	9
BBB/Baa	2,501,650,028	8
BB/Ba	497,365,150	2
B	525,219,437	2
CCC/Caa	156,079,614	1
CC/Ca	7,539,280	-
C	2,375,225	-
D	1,689,965	-
Commingled Fixed Income Funds	9,531,161,837	31
Not Rated	2,550,003,035	8
Total	\$ 30,104,681,221	100 %

Credit Quality Breakdown of Commingled Fixed Income Funds

As of June 30, 2013

Rating*	Fair Value	% of Total
P-1 or A-1	\$ 919,053,030	10
AAA/Aaa	3,378,029,993	36
AA/Aa	1,737,625,419	18
A	1,446,738,940	15
BBB/Baa	1,639,474,986	17
BB/Ba	85,030,299	1
B	237,834,049	3
CCC/Caa	42,731,197	-
CC/Ca	350,595	-
C	1,665,324	-
D	4,776,851	-
Not Rated	37,851,154	-
Total Commingled Fixed Income Funds	\$ 9,531,161,837	100 %

*Reflects aggregated ratings of underlying investments as reported by the commingled fixed income fund managers.

Retirement Funds

Notes to Financial Statements

and managed through the transfer of margin, in the form of cash or securities, between SWIB and the counterparty. The Retirement Funds' counterparty credit exposure for reverse repurchase agreements at June 30, 2013 is summarized in the table entitled **Reverse Repurchase Agreements**.

The cash proceeds from reverse repurchase agreements are reinvested by the Retirement Funds. The maturities of the purchases made with the proceeds of reverse repurchase agreements are not necessarily matched to the maturities of the agreements. The agreed-upon yields earned by the counterparty were between 0.20% and 0.30% for the reverse repurchase agreements held at June 30, 2013. The reverse repurchase agreements had open maturities, whereby a maturity date is not established upon entering into the agreement; however, interest rates on the agreements are negotiated daily. The agreements can be terminated at the will of either SWIB or the counterparty and may remain open for several months.

The cash due to counterparties resulting from reverse repurchase agreements is reported as "Obligations Under Reverse Repurchase Agreements" and the interest due to counterparties is included in "Other Liabilities" on the Statement of Net Investment Position. The underlying assets, as well as the reinvested proceeds, are reported in the "Investments" section on the Statement of Net Investment Position.

B. Custodial Credit Risk

The Retirement Funds do not have a deposit or investment policy specifically related to custodial credit risk.

Deposits — Custodial credit risk related to deposits is the risk that, in the event of the failure of a depository financial institution, SWIB will not be able to recover deposits that are in possession of an outside party. Bank deposits as of June 30, 2013 were \$533.1 million. A portion of the deposits, totaling \$77.6 million, are covered by federal depository insurance. The remaining uninsured and uncollateralized deposits, totaling \$455.5 million, were held in foreign currencies in SWIB's custodian's nominee name or were posted as collateral for derivatives transactions. In addition, SWIB held time deposits with foreign financial institutions with a fair value of \$190.6 million, all of which were uncollateralized and uninsured.

Investments — Custodial credit risk for investments is the risk that, in the event of the failure of the counterparty to a transaction, SWIB will not be able to recover the value of investments that are in the possession of an outside party. As of June 30, 2013 the Retirement Funds held 23 repurchase agreements totaling \$1.9 billion. All of these repurchase agreements were tri-party agreements held in short-term cash management portfolios managed by SWIB's custodian. The underlying securities for these

Reverse Repurchase Agreements

Counterparty Credit Exposure

As of June 30, 2013

Fair Value of Collateral and Margin Held by Counterparty		\$ 979,984,565
Less:		
Cash due to Counterparty	\$ 968,176,006	
Interest due to Counterparty	777,538	
Total due to Counterparty		968,953,544
Net Counterparty Credit Exposure		\$ 11,031,021

repurchase agreements were held by the tri-party's agent, not in SWIB's name.

C. Concentration of Credit Risk

Concentration of credit risk is the risk of loss attributed to the magnitude of an organization's investment in a single issuer. SWIB limits concentrations of credit risk by establishing investment guidelines for individual portfolios or groups of portfolios that generally restrict issuer concentrations in any one company or Rule 144A securities to less than 5% of the portfolio's market value. The Retirement Funds did not hold any investments with a single issuer, exclusive of investments issued or explicitly guaranteed by the U.S. government, representing 5% or more of the Retirement Funds' value at June 30, 2013.

D. Interest Rate Risk

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. SWIB uses a number of different methods to manage interest rate risk.

Generally, SWIB analyzes long or intermediate term portfolios' interest rate risk using various duration calculations. Modified duration, which is stated in years, is the measure of price sensitivity of a fixed income security to an interest rate change of 100 basis points. The calculation is based on the weighted average of the present values for all cash flows. Some pooled investments are analyzed using an option adjusted duration calculation which is similar to the modified duration method. Option adjusted duration

Interest Rate Sensitivity by Investment Type

As of June 30, 2013

Investment Type	Fair Value	Duration (years)	Weighted Average Maturity (days)
Asset Backed Securities	\$ 30,849,406	3.40	
Commercial Paper	292,373,451	0.17	
Corporate Bonds & Private Placements	4,786,714,377	5.26	
Corporate Bonds & Private Placements	3,162,500	Not Available	
Foreign Government/Agency Bonds	3,716,278,368	7.15	
Futures Contracts*	2,221,041,902	5.01	
Municipal Bonds	101,065,043	10.62	
Repurchase Agreements	1,867,584,799		1
U.S. Government Agencies	643,149,168	2.00	
U.S. Treasury Inflation Protected Securities	5,988,317,811	7.81	
U.S. Treasury Securities	3,144,024,460	5.47	
Commingled Funds:			
Short Term Cash Management	2,225,371,244		34
Emerging Market Fixed Income	337,157,047	7.29	
Global Fixed Income	438,243,250	4.85	
Domestic Fixed Income	6,530,390,295	5.53	
Total	<u>\$ 32,325,723,121</u>		

*Notional amount presented for fair value.

Retirement Funds

Notes to Financial Statements

incorporates the duration shortening effect of any embedded call provisions in the securities.

Short-term portfolios use the weighted average maturity (to next reset) to analyze interest rate risk. Weighted average maturity is the maturity of each position in a portfolio weighted by the dollar value of the position to compute an average maturity for the portfolio as a whole. This measure indicates a portfolio's sensitivity to interest rate changes: a longer weighted average maturity implies greater volatility in response to interest rate changes.

SWIB's investment guidelines related to interest rate risk vary by portfolio. Some fixed income portfolios are required to be managed within a range of a targeted duration, while others are required to maintain a weighted average maturity at or below a specified number of days or years.

The table entitled **Interest Rate Sensitivity by Investment Type** presents the aggregated interest rate exposure for the Retirement Funds' assets. Weighted average maturity, where reset dates are assumed to be the effective maturity date for the security, is presented for repurchase agreements and short term pooled investments. Longer term instruments held by the Retirement Funds are presented using modified duration, as this measure more accurately states the interest rate sensitivity of these investments. The duration statistic is calculated utilizing reset dates for some floating rate instruments, such as term loans.

E. Foreign Currency Risk

Foreign currency risk is the risk that changes in exchange rates will adversely impact the fair value of an investment. It includes the risk that currencies in which a portfolio's investments are denominated, or currencies in which a portfolio has taken on an active position, will decline in value relative to the U.S. dollar.

Foreign currency exchange rates may fluctuate significantly for a number of reasons, including the forces of supply and demand in the foreign exchange markets, actual or perceived changes in interest rates, intervention by U.S. or foreign governments or central

banks, currency controls, or political developments in the U.S. or abroad.

SWIB's policies include foreign currency risk management objectives relating to each individual portfolio. These guidelines address the foreign currency management activities permitted for each portfolio based on the portfolios mandates, risk tolerances and objectives. SWIB also employs discretionary currency overlay strategies at the total fund level when currency market conditions suggest such strategies are warranted. Additional information related to the management of foreign currencies through the use of derivatives is discussed in Note 5.

The table entitled **Currency Exposures by Investment Type** presents the Retirement Fund investments which were exposed to foreign currency risk at June 30, 2013.

4. Securities Lending Transactions

State statutes and Board policies permit SWIB to use investments of the Retirement Funds to enter into securities lending transactions. These transactions involve the lending of securities to broker-dealers and other entities in exchange for collateral, in the form of cash or securities, with the simultaneous agreement to return the collateral for identical securities in the future. SWIB's custodian is an agent in lending the Retirement Funds' directly held domestic and international securities. When the Retirement Funds' securities are delivered to a borrower as part of a securities lending agreement, the borrower is required to place collateral equal to 102% of the loaned securities' fair value, including interest accrued, as of the delivery date with the lending agent, so long as the securities and the collateral are denominated in the same currency. In the event that securities are loaned against collateral denominated in a different currency, the borrower is required to place collateral totaling 105% of the loaned securities' fair value, including interest accrued, as of the delivery date with the lending agent. Collateral is marked to market daily and adjusted as needed to maintain the required minimum level. Pledging or selling non-cash collateral securities cannot be done without a borrower default.

Cash collateral is reinvested by the lending agent in two separate pools, a U.S. dollar cash collateral pool and a pool denominated in Euros. These pools are administered in accordance with contractual investment guidelines which are designed to minimize the risk of principal loss and provide a modest rate of return. Investment guidelines limit credit and liquidity risk by restricting new investments to overnight repurchase agreements collateralized with high quality U.S. government, U.S. government agencies, and sovereign debt securities. To further reduce credit risk, SWIB's custodian provides indemnification to SWIB against counterparty default. The earnings generated from the collateral investments, plus or minus the rebates received from or paid to the dealers and less fees paid to agents, results in the net earnings from lending activities, which are then split on a percentage basis with the lending agent. Cash from the U.S. dollar pool may be posted as collateral relating to short sale transactions and earns a comparable overnight repurchase agreement market rate of return for the duration of the posting. See Note 6 for additional information relating to short sales.

In accordance with money market mutual fund industry standards, the cash collateral reinvestment pools are valued at amortized cost. The amortized or book value of a fund's assets and underlying fair market value of the assets may differ based on market conditions. The pools' market value relative to its amortized cost is expressed as net asset value (NAV) and is derived by dividing total market value by amortized cost. As of June 30, 2013, the U.S. dollar cash collateral reinvestment pool's NAV was 0.9995 while the Euro reinvestment pool had a NAV of 1.0000.

At fiscal year-end, the Retirement Funds had minimal credit risk exposure to borrowers because the amounts owed to the borrowers exceeded the amounts the borrowers owed the Retirement Funds. In addition to the cash collateral reinvestment indemnification, the contract with the lending agent requires it to indemnify the Retirement Funds if the borrowers fail to return the loaned securities and

the collateral is inadequate to replace the securities lent. The Retirement Funds are also indemnified against losses resulting from violations of investment guidelines.

The majority of security loans are open-ended and can be terminated on demand by the Retirement Funds or the borrower. Maturities of investments made with cash collateral are not necessarily matched to the maturities of the securities loaned because most loans do not have a fixed maturity date. The risk that SWIB would be unable to return collateral to securities borrowers upon termination of the loan is low because the majority of investments made with cash collateral mature in one to two business days. At June 30, 2013, the average maturities of the loans and the assets of the collateral reinvestment pools did not materially differ.

Securities lending is allowed in certain commingled fund investments. As an investor in such funds, SWIB does not own the underlying securities and does not separately report on securities lending activity. All earnings of these funds are reported in the Statement of Changes in Net Investment Position as "Net Increase (Decrease) in the Fair Value of Investments."

5. Derivatives

A derivative instrument, as defined by GASB Statement No. 53, is a financial instrument or other contract that has all of the following characteristics:

- **Settlement factors.** It has (1) one or more reference rates and (2) one or more notional amounts or payment provisions or both. Those terms determine the amount of the settlement or settlements and, in some cases, whether or not a settlement is required.
- **Leverage.** It requires no initial net investment or an initial net investment that is smaller than would be required for other types of contracts that would be expected to have a similar response to changes in market factors.
- **Net settlement.** Its terms require or permit net settlement, it can readily be settled net by a means

Retirement Funds

Notes to Financial Statements

Currency Exposures by Investment Type

June 30, 2013 (Stated in U.S. Dollars)

Currency	Cash & Cash Equivalents	Stocks	Fixed Income	Limited Partnerships	Multi Asset	Real Estate
Australian Dollar	\$ 2,241,777	\$ 934,251,543	\$ 69,794,931	\$ -	\$ -	\$ -
Brazilian Real	730,379	84,505,070	27,663,710	-	-	-
British Pound Sterling	7,786,395	3,501,851,248	286,079,226	105,207,399	-	-
Canadian Dollar	11,171,679	1,216,924,856	51,234,033	11,096,455	-	-
Chilean Peso	-	-	681,398	-	-	-
Colombian Peso	-	-	2,365,080	-	-	-
Czech Koruna	941,948	2,439,166	-	-	-	-
Danish Krone	(3,407)	132,870,109	25,298,589	-	-	-
Euro Currency Unit	61,011,890	3,969,004,507	1,491,754,083	829,371,682	-	-
Hong Kong Dollar	3,244,302	624,866,760	-	-	-	-
Hungarian Forint	1,133	94,083	7,696,390	-	-	-
Indian Rupee	158,544	56,026,526	-	-	-	-
Indonesian Rupiah	78,239	10,542,434	-	-	-	-
Israeli New Shekel	535,430	37,259,565	-	-	-	-
Japanese Yen	18,845,550	3,304,537,505	1,122,080,063	-	-	-
Malaysian Ringgit	1,401,101	46,712,397	39,908,616	-	-	-
Mexican New Peso	1,490,183	40,873,016	85,771,347	-	-	-
Moroccan Dirham	11,731	126,420	-	-	-	-
New Taiwan Dollar	2,304	190,225,592	-	-	-	-
New Zealand Dollar	105,446	9,716,224	5,701,804	-	-	-
Norwegian Krone	1,729,341	108,872,106	9,038,116	-	-	-
Peruvian Nuevo Sol	107,420	53,484	2,991,143	-	-	-
Philippine Peso	1,872	4,836,137	5,374,183	-	-	-
Polish Zloty	1,302,050	32,752,637	34,162,154	-	-	-
Russian Ruble	125,541	-	6,666,839	-	-	-
Singapore Dollar	632,156	179,069,998	-	-	-	-
South African Rand	910,690	41,600,918	28,717,647	-	-	-
South Korean Won	205,803	278,526,487	8,307,204	-	-	-
Swedish Krona	4,762,597	320,466,367	16,106,770	14,470,869	-	-
Swiss Franc	7,384,934	1,373,506,782	-	-	-	-
Thailand Baht	1,550,539	105,047,684	-	-	-	-
Turkish Lira	203	86,042,474	5,127,291	-	-	-
United States Dollar	3,352,240,398	27,614,831,816	22,011,493,523	9,043,032,756	3,300,779,676	756,622,013
Uruguayan Peso	-	-	6,596,334	-	-	-
Total	\$ 3,480,708,168	\$ 44,308,433,912	\$ 25,350,610,476	\$ 10,003,179,161	\$ 3,300,779,676	\$ 756,622,013

1) Commingled funds (including limited partnerships and other pooled vehicles) represent investments where the Retirement Funds own only a portion of the overall fund. While the overall fund may be denominated in U.S. dollars, the underlying investments may be exposed to foreign currency risk in various currencies. Commingled funds are shown in the denomination used by the fund for financial reporting.

2) Short Sell Obligations are reported as liabilities on the Statement of Net Investment Position. They are included in the above table because they have exposure to foreign currency risk.

3) Values may not add due to rounding.

Currency Exposures by Investment Type

June 30, 2013 (Stated in U.S. Dollars)

Currency	Preferred Securities	Convertible Securities	Options	Futures Contracts	Short Sell Obligations	Total
Australian Dollar	\$ -	\$ -	\$ (61,284)	\$ (84,011)	\$ -	\$ 1,006,142,956
Brazilian Real	63,874,550	-	-	-	-	176,773,710
British Pound Sterling	-	-	-	(2,555,174)	-	3,898,369,093
Canadian Dollar	-	-	-	(581,705)	(4,682,020)	1,285,163,298
Chilean Peso	-	-	-	-	-	681,398
Colombian Peso	-	-	-	-	-	2,365,080
Czech Koruna	-	-	-	-	-	3,381,114
Danish Krone	-	-	-	-	-	158,165,291
Euro Currency Unit	68,211,697	462,006	(44,739)	(682,733)	(3,095,694)	6,415,992,697
Hong Kong Dollar	-	-	-	-	-	628,111,063
Hungarian Forint	-	-	-	-	-	7,791,607
Indian Rupee	-	-	-	-	-	56,185,070
Indonesian Rupiah	-	-	-	-	-	10,620,673
Israeli New Shekel	-	-	-	-	-	37,794,994
Japanese Yen	-	-	-	2,439,744	(20,461,405)	4,427,441,457
Malaysian Ringgit	-	-	-	-	-	88,022,114
Mexican New Peso	-	-	-	-	-	128,134,547
Moroccan Dirham	-	-	-	-	-	138,151
New Taiwan Dollar	-	-	-	-	-	190,227,896
New Zealand Dollar	-	-	-	-	-	15,523,474
Norwegian Krone	-	-	-	-	-	119,639,564
Peruvian Nuevo Sol	-	-	-	-	-	3,152,048
Philippine Peso	-	-	-	-	-	10,212,191
Polish Zloty	-	-	-	-	-	68,216,841
Russian Ruble	-	-	-	-	-	6,792,380
Singapore Dollar	-	-	-	-	(5,698,943)	174,003,211
South African Rand	-	-	-	-	-	71,229,256
South Korean Won	-	-	-	-	-	287,039,494
Swedish Krona	-	-	-	-	-	355,806,604
Swiss Franc	-	-	-	-	(4,872,293)	1,376,019,423
Thailand Baht	-	-	-	-	-	106,598,223
Turkish Lira	-	-	-	-	-	91,169,968
United States Dollar	22,740,927	51,764,076	(34,749,856)	(36,321,351)	(60,781,090)	66,021,652,890
Uruguayan Peso	-	-	-	-	-	6,596,334
Total	\$ 154,827,174	\$ 52,226,082	\$ (34,855,878)	\$ (37,785,230)	\$ (99,591,446)	\$ 87,235,154,109

Retirement Funds

Notes to Financial Statements

outside the contract, or it provides for delivery of an asset that puts the recipient in a position not substantially different from net settlement.

Derivatives may be used to implement investment strategies for the Retirement Funds. All derivative instruments are subjected to risk analysis and monitoring processes at the portfolio, asset class and fund levels. Investment guidelines define allowable derivative activity for each portfolio and are based on the investment objectives which have been approved by the Board. Where derivatives are permitted, guidelines stipulate allowable instruments and the manner and degree to which they are to be used.

A derivative can take the form of a contract negotiated between the Retirement Funds and a specific counterparty. This is referred to as an over-the-counter (OTC) contract, such as a forward contract. Alternatively, standardized derivative instruments, such as futures contracts, may be traded on an organized exchange and are referred to as "exchange-traded."

Inherent in the use of OTC derivatives, the Retirement Funds are exposed to counterparty credit risk on OTC positions. Counterparty credit risk is the risk that a derivative counterparty may fail to meet its payment obligation under the derivative contract. SWIB seeks to mitigate this risk through counterparty credit evaluations and approvals, counterparty credit limits, and exposure monitoring procedures. Additionally, policies have been established which

seek to implement master netting arrangements with counterparties that permit the closeout and netting of transactions with the same counterparty upon the occurrence of certain events, such as payment default, rating downgrade, bankruptcy, illegality or force majeure. Agreements may also require daily collateral postings to further mitigate credit risk. At June 30, 2013, the Retirement Funds posted \$8.6 million in cash collateral to OTC counterparties. No securities were pledged relating to OTC positions. The table entitled **OTC Derivative Investments Subject to Counterparty Credit Risk**, summarizes, by credit rating, the Retirement Funds' exposure to OTC derivative instruments' counterparty credit risk as of June 30, 2013, without respect to any collateral or netting arrangement.

Conversely, counterparty credit risk is mitigated by an intermediary for exchange-traded derivatives. For this type of derivative investment, the clearinghouse interposes itself as counterparty to all trades and extends a guarantee that trades will be settled as originally intended. To ensure performance, the exchange establishes, and the clearinghouse monitors, margin requirements to cover nearly all expected price changes for a given product within a specified time period based on market risk. Margin payments are settled daily based upon the price movements of the contracts, thereby significantly reducing counterparty credit risk. At June 30, 2013, the Retirement Funds posted \$189.2 million in cash and \$65.8 million in equity securities as collateral with exchange clearing brokers.

OTC Derivative Investments Subject to Counterparty Credit Risk

As of June 30, 2013

Counterparty Credit Rating	Payable	Receivable	Fair Value
AA	\$ (611,072,826)	\$ 619,147,884	\$ 8,075,058
A	(2,893,707,693)	2,899,679,735	5,972,042
Total	\$ (3,504,780,519)	\$ 3,518,827,619	\$ 14,047,100

Gains and losses for all derivative instruments are reported in the Statement of Changes in Net Investment Position as “Net Increase (Decrease) in the Fair Value of Investments.”

SWIB invests in derivative investments directly, as well as indirectly through commingled or pooled investments. Information relating to investments held in commingled funds has not been separately disclosed in the financial statements or the accompanying footnotes.

A. Foreign Currency Spot and Forward Contracts

Foreign Currency Spot and Forward contracts are OTC agreements between two counterparties to exchange designated currencies at a specific time in the future. No cash is exchanged when a foreign exchange spot or forward contract is initiated. Amounts due are paid or received on the contracted settle date.

Currency exposure management is permitted through the use of currency derivative instruments. Direct hedging of currency exposure back to the U.S. dollar is permitted when consistent with the strategy of the portfolio. Cross-currency exposure management to transfer out of an exposed currency and into a benchmark currency is permitted. In some portfolios, currencies of non-benchmark countries may be held through the use of forward contracts, provided that the notional value of any single non-benchmark currency does not exceed 5% of the market value of the portfolio. SWIB may employ discretionary currency overlay strategies at the total fund and asset class level when currency market conditions suggest such strategies are warranted.

Losses may arise from future changes in the value of the underlying currency, or if the counterparties do not perform under the terms of the contract. The aggregate fair value of receivables relating to OTC foreign currency spot and forward contracts at June 30, 2013 was \$3.5 billion. This represents the maximum loss that would be recognized at the reporting date if all seventeen counterparties failed to perform as contracted. This maximum exposure

is reduced to \$116.4 million when counterparty collateral and master netting arrangements are taken into account.

Spot and forward contracts are valued daily with the changes in fair value included in “Net Increase (or Decrease) in Fair Value of Investments” on the Statement of Changes in Net Investment Position. The net receivable or payable for spot and forward contracts is reflected as “Foreign Currency Contracts” on the Statement of Net Investment Position. The table entitled **Foreign Currency Spot and Forward Contracts** presents the fair value of foreign currency spot and forward contract assets and liabilities held by the Retirement Funds as of June 30, 2013.

B. Futures Contracts

A futures contract is an exchange-traded agreement to buy or sell a financial instrument, index or commodity at an agreed upon price and time in the future.

The fair value of futures contracts represents the unrealized gain/(loss) on the contracts, since trade inception, and is reflected as “Futures Contracts” on the Statement of Net Investment Position. Futures contracts are marked to market daily, based upon the closing market price of the contract at the board of trade or exchange on which they are traded. Gains and losses resulting from investments in futures contracts are included in the “Net Increase (Decrease) in the Fair Value of Investments” on the Statement of Changes in Net Investment Position.

Futures contracts involve, to varying degrees, risk of loss in excess of the margin deposited with the broker. Losses may arise from future changes in the value of the underlying instrument.

Futures contracts may be entered into to efficiently gain or adjust market exposures for purposes that include trust fund rebalancing, sector, interest rate, or duration types of exposure adjustments; the securitization of cash or as a substitute for cash market transactions.

The table entitled **Futures Contracts** presents the

Retirement Funds

Notes to Financial Statements

Foreign Currency Spot and Forward Contracts

As of June 30, 2013

Currency	Notional (local currency)	Fair Value (\$US)	Unrealized Gain/(Loss) (\$US)
Foreign Currency Contract Receivables			
Australian Dollar	262,527,129	\$ 239,513,908	\$ (6,852,397)
Brazilian Real	55,770,000	24,929,224	(1,676,731)
British Pound Sterling	111,783,850	169,489,580	(404,579)
Canadian Dollar	335,418,334	317,631,572	(3,742,741)
Chilean Peso	6,709,200,000	13,095,631	(487,000)
Colombian Peso	3,782,736,744	1,957,744	(17,407)
Danish Krone	157,758,249	27,500,602	(2,777)
Euro Currency Unit	272,309,460	354,000,272	(652,532)
Hong Kong Dollar	563,066,790	72,601,102	21,547
Indian Rupee	1,649,891,000	27,307,414	(836,881)
Israeli New Shekel	30,779,726	8,450,006	996
Japanese Yen	27,148,318,942	273,338,877	435,319
Mexican New Peso	2,509,556,639	191,975,884	(1,184,060)
New Zealand Dollar	4,034,484	3,108,510	(43,429)
Nigerian Naira	135,533,000	831,372	(14,388)
Norwegian Krone	71,691,107	11,718,658	(411,673)
Peruvian Nuevo Sol	3,703,146	1,323,716	(35,735)
Polish Zloty	44,015,000	13,185,569	(540,119)
Russian Ruble	416,935,000	12,550,360	(359,603)
Singapore Dollar	66,425,584	52,377,947	29,578
South African Rand	161,503,000	16,226,530	(1,324,147)
Swedish Krona	594,831,075	88,065,200	(383,342)
Swiss Franc	67,980,509	71,874,199	(544,341)
United States Dollar	1,525,773,743	1,525,773,743	-
		3,518,827,620	(19,026,442)
Foreign Currency Contract Payables			
Australian Dollar	(55,035,151)	(50,244,829)	4,560,762
Brazilian Real	(59,914,000)	(26,769,822)	1,688,612
British Pound Sterling	(277,799,024)	(421,227,200)	7,830,566
Canadian Dollar	(198,512,571)	(187,999,218)	4,645,786
Chilean Peso	(2,176,400,000)	(4,252,997)	198,629
Colombian Peso	(5,844,572,584)	(3,022,042)	15,336
Danish Krone	(97,174,181)	(16,939,690)	3,031
Euro Currency Unit	(301,964,796)	(392,552,085)	2,665,336
Hong Kong Dollar	(478,936,546)	(61,757,851)	(14,779)
Indian Rupee	(477,355,000)	(7,911,829)	47,958
Israeli New Shekel	(93,979,000)	(25,799,370)	18,682
Japanese Yen	(36,362,589,420)	(366,098,301)	2,110,570
Malaysian Ringgit	(48,000,000)	(15,070,033)	215,131
Mexican New Peso	(204,574,138)	(15,682,622)	538,403
New Zealand Dollar	(7,460,000)	(5,728,862)	104,858
Nigerian Naira	(135,533,000)	(831,372)	12,808
Norwegian Krone	(27,706,423)	(4,533,289)	8,729
Peruvian Nuevo Sol	(12,416,000)	(4,438,185)	158,631
Polish Zloty	(32,525,800)	(9,737,633)	105,181
Russian Ruble	(428,128,000)	(12,876,685)	447,278
Singapore Dollar	(10,884,402)	(8,582,360)	(26,172)
South African Rand	(182,705,000)	(18,345,579)	872,271
South Korean Won	(9,051,000,000)	(7,880,324)	415,355
Swedish Krona	(47,256,391)	(6,997,262)	22,796
Swiss Franc	(98,016,692)	(103,616,289)	1,286,588
Taiwan New Dollar	(1,683,947)	(56,186)	(76)
Thailand Baht	(38,441,012)	(1,239,433)	(7,349)
United States Dollar	(1,724,589,172)	(1,724,589,171)	-
		(3,504,780,519)	27,924,921
Total		\$ 14,047,100	\$ 8,898,479

Retirement Funds investments in futures contracts as of June 30, 2013.

C. Options

An option contract gives the purchaser of the contract the right, but not the obligation, to buy (call) or sell (put) the security or index underlying the contract at an agreed upon price on or before the expiration of the option contract. The seller of the contract is subject to market risk, while the purchaser is subject to credit risk and market risk, to the extent of the premium paid to enter into the contract.

Trust fund rebalancing policies and portfolio investment guidelines permit the use of exchange-traded and OTC options. Investment Guidelines allow options to be used to improve market exposure efficiency, enhance expected returns, or provide market exposure hedges. Exchange rules require that the seller of exchange-traded call option contracts cover these positions either by collateral deposits in the form of cash or securities or by pledging, in escrow, the actual securities that would be transferred to the option purchaser in the event the option contract were exercised.

The fair value of option contracts is based upon the closing market price of the contract and is reflected as "Option Contracts" on the Statement of Net

Investment Position. Gains and losses as a result of investments in option contracts are included in the "Net Increase (Decrease) in the Fair Value of Investments" on the Statement of Changes in Net Investment Position. The table entitled **Option Contracts** presents the fair value of option contracts as of June 30, 2013.

6. Short Sell Obligations

The Retirement Funds may sell a security it does not own in anticipation of purchasing the security later at a lower price. This is known as a short sale transaction. For the duration of the short sale transaction, a liability is recorded under "Short Sell Obligations" on the Statement of Net Investment Position. The liability presented on the Statement of Net Investment Position represents the fair value of the borrowed securities necessary for delivery to the purchaser and is marked-to-market daily. Realized and unrealized gains and losses associated with short sales are recorded on the Statement of Changes in Net Investment Position within the "Net Increase (Decrease) in Fair Value of Investments" category. While the transaction is open, the Retirement Funds incur expenses for securities borrowing costs. In addition, as a security borrower, the Retirement Funds may incur dividend and interest expense as such payments must be remitted to the security

Futures Contracts

June 30, 2013

Description	Expiration	Notional Amount	Unrealized Appreciation (Depreciation)*
Fixed Income Futures	Sept 13	\$ 2,221,041,902	\$ (26,176,174)
Equity Index Futures	Jul 13 - Nov 13	1,140,823,535	(12,665,601)
Commodity Futures	Aug 13 - Oct 13	(13,742,760)	1,056,545
Total		<u>\$ 3,348,122,677</u>	<u>\$ (37,785,230)</u>

*Unrealized appreciation/(depreciation) includes foreign currency gains/(losses).

Retirement Funds

Notes to Financial Statements

lender during the course of the loan. Such expenses are included in "Investment Expense" on the Statement of Changes in Net Investment Position.

Risks arise from short sales due to the possible illiquidity of the securities markets and from potential adverse movements in security values. The cost to acquire the securities sold short may exceed the amount of proceeds initially received, as well as the amount of the liability recorded as "Short Sell Obligations" in the Statement of Net Investment Position. Short sales expose the short seller to potentially unlimited liability because there is no upward limit on the price a shorted security could attain. Certain portfolio guidelines permit short sales and, to mitigate risks, typically limit the total value of short sales in any portfolio to 20% of a portfolio's value. In addition, portfolios which engage in short sales have long only benchmarks established by the

Board. Investment performance and risk associated with each portfolio is measured against benchmarks and monitored by management.

When a short sale occurs, the shorting portfolio must borrow the security and deliver it to the buyer. If the shorted security is owned by another Retirement Fund portfolio, investment policies allow the borrowing of the shorted securities from other Retirement Fund portfolios, including inter-fund borrowings.

Except in the case of borrowings within the same trust fund, the Retirement Funds are required to post collateral to the lender, at the required rate of 102% for in-currency loans and 105% for cross-currency loans. At June 30, 2013, the Retirement Funds posted \$120.3 million in collateral to security lenders. This represented \$5.4 million in excess of the

Options Contracts

June 30, 2013

Security Description	Contract Type	Expiration	Notional	Unrealized Gain (Loss)	Fair Value
Options Sold					
Exchange-Traded					
Equity	Call	Jul 13 - Aug 13	(29,810,470)	(156,899)	(556,028)
Equity	Put	Jul 13 - Jan 14	(550,564,979)	(2,190,441)	(34,267,955)
Fixed Income	Put	Jul 13	(25,305,012)	1,104	(68,990)
Commodity	Put	Jul 13 - Sep 13	(2,276,400)	(20,057)	(65,150)
Over-the-Counter					
Equity	Call	Jul 13	(986,534)	7,958	(1,471)
Equity	Put	Jul 13	(2,280,295)	(50,932)	(85,249)
			(611,223,690)	(2,409,267)	(35,044,843)
Options Purchased					
Exchange-Traded					
Equity	Call	Jul 13 - Sep 13	\$ 138,674,915	\$ (260,265)	\$ 188,965
Total			\$ (472,548,775)	\$ (2,669,532)	\$ (34,855,878)

fair market value of the securities borrowed. If the security lender recalled the security and SWIB was not able to supply the lender with the security, the lender would be permitted to use SWIB's collateral to fund the purchase of the security.

7. Multi Asset

SWIB employs portfolio strategies which involve investment across multiple asset classes. The "Multi Asset" category on the Statement of Net Investment Position consists of risk parity and hedge fund multi asset strategies. Risk parity and hedge fund investments are either in the form of a commingled fund, with ownership through fund shares, or a limited partnership.

The risk parity portfolios seek to equally weight asset allocation risk across multiple assets and geographies. Exposures are expected to deliver improved risk and return tradeoffs versus conventional portfolios comprised primarily of stocks and bonds. The risk parity portfolios also intend to provide more diversified exposure over various economic environments.

The Retirement Funds invest in a diversified set of hedge fund strategies, invested across multiple asset classes. In general, a hedge fund is a private investment fund that seeks to produce absolute returns using a broad range of strategies with low to moderate levels of volatility, typically employing both long and short positions. An allocation to a diversified hedge fund portfolio is intended to have low correlation to traditional publicly traded equities and contribute to overall total fund diversification.

Hedge funds can be illiquid, either by virtue of the illiquidity of underlying assets or due to lock-up terms. However, SWIB has taken steps to minimize this risk by investing in hedge funds with more liquid asset classes and by structuring its investments to stagger lock-up periods. Hedge funds also use leverage to varying degrees, and while it is possible that a hedge fund can lose a significant portion of its capital, SWIB has limited the amount it invests in hedge funds in

total and with any individual hedge fund manager.

At fiscal year-end, the majority of SWIB's risk parity and hedge fund investments are reflected within the "Multi Asset" category on the Statement of Net Investment Position. Hedge fund portfolios with a long only equity strategy are included within the "Stocks" classification on the Statement of Net Investment Position.

8. Long-Term Receivables

Included in the Core Fund's June 30, 2013 Investment Sales Receivable balance on the Statement of Net Investment Position is \$114.9 million in receivables which are due September 2015. These receivables represent the final payments from the sale of private equity limited partnership interests.

9. Summary of Investments

The tables entitled **Summary of Investments – Core Retirement Investment Trust Fund** and **Summary of Investments – Variable Retirement Investment Trust Fund** provide summary information by financial statement classification for the Core Fund and Variable Fund as of June 30, 2013.

10. Unfunded Capital Commitments

The Core Fund has committed to fund various limited partnerships and side-by-side agreements related to its private equity and real estate holdings. Commitments that have not been funded total \$4.9 billion as of June 30, 2013. Unfunded commitments are not included in the financial statements since the amount and timing of the funding is not certain.

11. Loss Contingency

On September 5, 2008, the Internal Revenue Service (IRS) provided SWIB with a "Notice of Transferee Liability." This claim seeks taxes, penalties and interest relating to the sale of Shockley Communications Corporation (SCC) stock in 2001.

SWIB is classified as a tax exempt entity by the IRS.

Retirement Funds

Notes to Financial Statements

Summary of Investments - Core Retirement Investment Trust Fund

June 30, 2013

Financial Statement Classification	Coupon Rate (%)	Maturity Dates	Fair Value
Stocks	N/A	N/A	\$ 38,314,831,045
Fixed Income	Variable & 0.10 - 16.25	7/2013 - 3/2087	25,350,610,476
Limited Partnerships	N/A	N/A	10,003,179,161
Multi Asset	N/A	N/A	3,300,779,676
Real Estate	N/A	N/A	756,622,013
Preferred Securities	N/A	N/A	143,850,535
Convertible Securities	Variable & 0.25 - 7.00	10/2013 - 12/2066	52,226,082
Foreign Currency Contracts	N/A	7/2013 - 11/2013	13,531,085
Option Contracts	N/A	7/2013 - 1/2014	(27,344,490)
Futures Contracts	N/A	7/2013 - 11/2013	(36,164,898)
Total			<u>\$ 77,872,120,685</u>

N/A = Not Applicable

Summary of Investments - Variable Retirement Investment Trust Fund

June 30, 2013

Financial Statement Classification	Maturity Dates	Fair Value
Stocks	N/A	\$ 5,993,602,867
Preferred Securities	N/A	10,976,639
Foreign Currency Contracts	7/2013 - 9/2013	516,015
Option Contracts	7/2013 - 10/2013	(7,511,388)
Futures Contracts	9/2013	(1,620,332)
Total		<u>\$ 5,995,963,801</u>

N/A = Not Applicable

However, the IRS asserts that the shareholders' sale of SCC stock in 2001 should have been characterized as a sale of assets by SCC, on which SCC should have paid income taxes. Based on the theory of transferee liability, the IRS asserts that the former SCC shareholders, including SWIB, would be liable for those taxes, plus penalties and interest. Transferee liability is limited to the amount actually received by the putative transferee, plus interest. As a result, SWIB's potential liability, as a putative transferee of SCC assets, is estimated to be \$46.2 million, including taxes, interest and potential penalties.

SWIB is aggressively contesting the IRS' assertions of SWIB's tax liability. Furthermore, SWIB believes that the loss, if any, resulting from the claim is not probable and will therefore not have a material impact on SWIB's Net Investment Position Held in Trust or Net Investment Income in future years. As such, SWIB has not recognized a loss relating to this matter in the current year, nor does it appear as a contingent liability in the Statement of Net Investment Position.



STATE OF WISCONSIN

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Joe Chrisman
State Auditor

Independent Auditor's Report on the Financial Statements and Other Reporting Required by *Government Auditing Standards*

Senator Robert Cowles and
Representative Samantha Kerkman, Co-chairpersons
Joint Legislative Audit Committee

Members of the Board of Trustees and
Mr. Michael Williamson, Executive Director
State of Wisconsin Investment Board

Report on the Financial Statements

We have audited the Statement of Net Position, Statement of Operations and Changes in Net Position, and the related notes of the State Investment Fund of the State of Wisconsin as of and for the year ended June 30, 2013.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

Our responsibility is to express an opinion on the financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, which is issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the

financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of the accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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

Opinion

In our opinion, the financial statements referred to in the first paragraph present fairly, in all material respects, the financial position of the State Investment Fund as of June 30, 2013, and the respective changes in its financial position for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Emphases of Matter

As discussed in Note 1, the financial statements referred to in the first paragraph present only the State Investment Fund. These statements do not purport to, and do not, present fairly the financial position of the Investment Board or of the State of Wisconsin as of June 30, 2013, or the changes in its financial position for the year then ended, in conformity with accounting principles generally accepted in the United States of America. Our opinion is not modified with respect to this matter.

As discussed in Note 2 to the financial statements, the Investment Board implemented Governmental Accounting Standards Board Statement Number 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position*, which made presentation changes to the State Investment Fund financial statements. Our opinion is not modified with respect to this matter.

Other Matters

Prior-Year Comparative Information—We previously audited the State Investment Fund's financial statements as of and for the year ended June 30, 2012, and we expressed an unqualified opinion in our report dated August 29, 2012. In our opinion, the State Investment Fund's comparative financial information presented herein as of and for the year ended June 30, 2012, is consistent, in all material respects, with the audited financial statements from which it is derived.

Accompanying Information—Our audit was conducted for the purpose of forming an opinion on the financial statements of the State Investment Fund. The supplementary information included as Management Discussion and Analysis is presented for purposes of additional analysis and is not a required part of the financial statements. We applied certain limited procedures to the information that included inquiries of management about the methods of preparing the information. We further compared the information for consistency with management's responses to our inquiries, the financial statements, and other knowledge we obtained during our audit of the financial statements. However, we do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to do so.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued a report dated September 13, 2013, on our consideration of the Investment Board's internal control over financial reporting; our tests of its compliance with certain provisions of laws, regulations, and contracts; and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Investment Board's internal control over financial reporting and compliance.

LEGISLATIVE AUDIT BUREAU

A handwritten signature in black ink, appearing to read "Joe Chrisman".

Joe Chrisman
State Auditor

September 13, 2013

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State Investment Fund

Management Discussion and Analysis

Management Discussion and Analysis provides general information on the financial activities of the State Investment Fund (SIF). The SIF temporarily invests the operating funds of the State of Wisconsin and agencies, the Wisconsin Retirement System (WRS), and various local government units (Local Government Investment Pool – LGIP). The table below provides information about ownership at June 30.

Following this section are the financial statements and notes to the financial statements. The **Statement of Net Position** provides information on the types of assets and the liabilities of the SIF. The **Statement of Operations and Changes in Net Position** provides information on the net income of the SIF and its net position at year end. The **Notes to the Financial Statements** provide additional information that is essential to a full understanding of the data provided in the SIF financial statements. The table entitled **SIF Condensed Financial Information** contains a summary for the fiscal years ended June 30, 2013 and 2012 (for comparison).

Because the SIF is used to temporarily invest participants' operating cash flows, investments are in

highly liquid, short-term fixed income securities. At June 30, 2013, SIF Net Position had increased by \$2.311 billion from the prior year due to the combined increase in the State of Wisconsin and agencies (+\$1.290 billion), the WRS (+\$693 million), and the LGIP (+\$328 million) balances. The SIF Average Daily Balance increased by \$1.226 billion in the current fiscal year compared to the prior year. The monthly average balance peaked at \$10.229 billion in March 2013.

The Net Income increase of 31.4% from the previous fiscal year was largely due to an Average Daily Balance increase of 17.3% to \$ 8.318 billion. The Time Weighted Return remained low at 0.15% due to the ongoing low interest rate environment caused by the Federal Reserve continuing to maintain the federal funds rate "target range" to between zero and 0.25% since December 16, 2008. For fiscal year 2013, the average federal funds effective rate was 0.14%. Investment Expenses increased by 356.2% during fiscal year 2013 because \$1,201,076 of Management Operating Expenses allocated to the SIF in the prior year were charged against a reserve balance which had accumulated over the years. During fiscal year 2013, Management Operating Expenses allocated to the SIF were charged against the remaining reserve balance of \$84,329.

SIF Condensed Financial Information

	2013	2012	% Change
Total Assets	\$ 9,273,688,319	\$ 6,951,887,107	33.4
Total Liabilities	122,614,319	111,505,107	10.0
Net Position	<u>\$ 9,151,074,000</u>	<u>\$ 6,840,382,000</u>	33.8
Investment Income	\$ 13,976,289	\$ 10,504,745	33.0
Investment Expenses	1,580,035	346,315	356.2
State Working Bank Charges	2,843,631	2,889,287	(1.6)
Net Income	<u>\$ 9,552,623</u>	<u>\$ 7,269,143</u>	31.4
Average Daily Balance	\$ 8,317,930,810	\$ 7,091,886,359	17.3
Weighted Avg. Maturity (WAM)	34 DAYS	75 DAYS	
<u>SIF Ownership:</u>			
State of Wisconsin & Agencies	46%	42%	
Wisconsin Retirement System	24%	23%	
Local Govt Investment Pool	30%	35%	
Total	<u>100%</u>	<u>100%</u>	

SIF Annualized Time Weighted Returns

Fiscal Year Ended	% Return
2004	1.03
2005	2.08
2006	4.23
2007	5.40
2008	4.02
2009	1.33
2010	0.25
2011	0.19
2012	0.14
2013	0.15

Statement of Net Position

As of June 30, 2013 (with Comparative Amounts as of June 30, 2012)

	June 30, 2013	June 30, 2012
Assets		
Investments (at fair value):		
Repurchase Agreements	\$ 5,291,000,000	\$ 1,631,000,000
Government & Agencies	3,910,778,873	4,075,664,223
Certificates of Deposit	25,800,000	24,150,000
Banker's Acceptances	45,987,078	19,537,012
Bank Demand Deposits	-	1,200,000,000
	<hr/>	<hr/>
Total Investments	9,273,565,951	6,950,351,235
Other Assets:		
Accrued Interest Receivable	122,368	1,535,872
	<hr/>	<hr/>
Total Assets	9,273,688,319	6,951,887,107
	<hr/>	<hr/>
Liabilities		
Payable for Investments Purchased	3,572,424	-
Check Float Invested	118,483,270	110,675,048
Earnings Distribution Payable	430,105	710,737
Accrued Expenses	128,520	119,322
	<hr/>	<hr/>
Total Liabilities	122,614,319	111,505,107
	<hr/>	<hr/>
Net Position	\$ 9,151,074,000	\$ 6,840,382,000
	<hr/>	<hr/>
Net Position consist of:		
Participating Shares	\$ 9,151,074,000	\$ 6,840,382,000
Undistributed Unrealized Gains (Losses)	-	-
	<hr/>	<hr/>
Net Position	\$ 9,151,074,000	\$ 6,840,382,000
	<hr/>	<hr/>

The accompanying notes are an integral part of this statement.

State Investment Fund

Financial Statements

Statement of Operations and Changes in Net Position

For the Fiscal Year Ended June 30, 2013 (with Comparative Amounts for June 30, 2012)

	2013	2012
Investment Income	\$ 13,976,289	\$ 10,504,745
Investment Expenses		
Management Operating Expenses (Note 2E)	1,229,545	-
Custodial Bank Charges	181,120	121,864
Electronic Services	168,370	222,451
Legal and Consulting Fees	1,000	2,000
Total Expenses	1,580,035	346,315
Net Investment Income	12,396,254	10,158,430
State Working Bank Charges	2,843,631	2,889,287
Net Income	9,552,623	7,269,143
Distributions Paid and Payable	9,552,623	7,269,143
Change in Undistributed Unrealized Gains (Losses)	-	-
Beginning of Period Undistributed Unrealized Gains (Losses)	-	-
End of Period Undistributed Unrealized Gains (Losses)	-	-
Participant Transactions:		
Receipts by Transfer to Fund	32,115,484,000	31,960,280,000
Disbursements by Transfer from Fund	29,804,792,000	31,660,903,000
Net Change in Participating Shares	2,310,692,000	299,377,000
Beginning of Period Participating Shares	6,840,382,000	6,541,005,000
End of Period Participating Shares	9,151,074,000	6,840,382,000
NET POSITION	\$ 9,151,074,000	\$ 6,840,382,000

The accompanying notes are an integral part of this statement.

Notes to the Financial Statements

1. Description of Funds

The State Investment Fund (SIF) pools the cash of the State of Wisconsin and its agencies, the Wisconsin Retirement System (WRS), and various local government units (Local Government Investment Pool – LGIP) into a commingled fund with the investment objective of safety of principal and liquidity while earning a competitive money market rate of return. Only State of Wisconsin agencies are required to invest their operating cash in the SIF. In the State's Comprehensive Annual Financial Report (CAFR), the SIF is not reported as a separate fund; rather, each State fund's share in the "pool" is reported on the balance sheet as "Cash and Cash Equivalents." Shares of the SIF belonging to other participating public institutions are presented in the Local Government Pooled Investment Fund, an investment trust fund. The staff of the State of Wisconsin Investment Board (SWIB) manages the SIF with oversight by the Board of Trustees as authorized in Wisconsin Statutes 25.14 and 25.17. The SWIB is not registered with the SEC as an investment company.

Wisconsin Statutes 25.17(3)(b), (ba), (bd), and (dg) enumerate the various types of securities in which the SIF can be invested, which include direct obligations of the United States or its agencies, corporations wholly owned by the United States or chartered by an act of Congress, securities guaranteed by the United States, the unsecured notes of financial and industrial issuers, direct obligations of or guaranteed by the government of Canada, certificates of deposit issued by banks in the United States including solvent financial institutions in Wisconsin and bankers acceptances. The Board of Trustees may specifically approve other prudent legal investments.

2. Significant Accounting Policies

A. Basis of Presentation

The accompanying financial statements of the investment activity of the SIF are prepared in conformity with accounting principles generally accepted in the United States as prescribed by the Governmental Accounting Standards Board (GASB).

B. Basis of Accounting

The accompanying statements are prepared based upon the flow of economic resources measurement focus and the full accrual basis of accounting. Under the accrual basis of accounting, revenues are recognized in the accounting period in which they are earned and become measurable, and expenses are recognized in the period incurred, if measurable. Security transactions and the related gains and losses are recorded on a trade date basis. Interest income is accrued as earned.

C. Comparative Information

The financial statements include certain prior year comparative information, but not at the level of detail required for a presentation in conformity with accounting principles generally accepted in the United States of America. Accordingly, such information should be read in conjunction with the State Investment Fund's prior year financial statements, from which the comparative information was derived, available at www.swib.state.wi.us.

D. Valuation of Securities

Generally, securities are valued at fair value for financial statement purposes and amortized cost for purposes of calculating income to participants (See Note 3). BNY Mellon, as custodial bank, compiles fair value information for applicable securities by utilizing third party pricing services. The fair value of investments is determined at the end of each month.

State Investment Fund

Notes to Financial Statements

U.S. Government/Agency securities and Commercial Paper are priced using matrix pricing. This method estimates a security's fair value by using quoted market prices for securities with similar interest rates, maturities, and credit ratings. Further, short-term debt investments with remaining maturities of up to 90 days are valued using amortized cost to estimate fair value, provided that the fair value of those investments is not significantly affected by the impairment of the credit standing of the issuer or by other factors.

Bank Demand Deposits, Repurchase Agreements, non-negotiable Certificates of Deposit and Banker's Acceptances are valued at cost because they are nonparticipating contracts that do not capture interest rate changes in their value. The table entitled **Summary of Information by Investment Classification** contains additional information on SIF holdings as of June 30, 2013.

E. Management Operating Expenses

Management Operating Expenses are SWIB's investment and administrative costs that are allocated to the SIF participants. During fiscal years 2000 to 2011, the billed expense was determined by between 2.75 and 3.25 basis points of assets under management. Unspent billed budget authority was allowed to be carried forward in a reserve held in the

General Fund. In 2011, Wisconsin Act 32 eliminated SWIB's basis point budget process and authorized SWIB's Board to approve the internal operating budget based on operating and staffing needs. In September 2011, the Board approved eliminating the reserve. As a result, the fiscal year 2013 and 2012 Management Operating Expenses allocated to the SIF of \$84,329 and \$1,201,076, respectively, were charged against the reserve, eliminating the reserve balance.

F. State Working Bank Charges

State Working Bank Charges represent charges for various state banking services such as lockbox, ePay, and depository services. These expenses are allocated to SIF participants based on their proportionate usage of banking services and, accordingly, reduce the participant's share of the Net Investment Income.

G. New Accounting Standard

In June 2011, GASB issued Statement No. 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position*. The objective of this statement is to provide financial reporting guidance for deferred outflows of resources and deferred inflows of resources as required elements of the financial statements. The implementation of this statement did not impact the

Summary of Information by Investment Classification

June 30, 2013

Investment Type	Interest Rates %	Maturity Dates	Book Value (Amort. Cost)	Fair Value
Repurchase Agreements	0.10 - 0.12	07/01/13	\$ 5,291,000,000	\$ 5,291,000,000
Government & Agencies	0.02 - 0.46	07/01/13 - 05/31/15	3,910,778,873	3,910,778,873
Certificates of Deposit	0.20 - 1.00	07/15/13 - 06/16/14	25,800,000	25,800,000
Banker's Acceptances	0.15 - 0.33	07/05/13 - 12/23/13	45,987,078	45,987,078
Total Investments			<u>\$ 9,273,565,951</u>	<u>\$ 9,273,565,951</u>
Ratio of Fair Value to Book Value				100%

financial position of the SIF. However, the adoption of this statement resulted in presentation changes to replace net assets with net position on the financial statements.

3. SIF Investment Income and Pool Shares

For purposes of calculating earnings to each participant, all investments are valued at amortized cost. Specifically, the SIF distributes income to pool participants monthly, based on their average daily share balance. Distributions include interest income based on stated rates (both paid and accrued), amortization of discounts and premiums on a straight-line basis, realized investment gains and losses calculated on an amortized cost basis, and investment expenses. This method differs from the fair value method used to value investments in these financial statements because the amortized cost method is not designed to distribute to participants unrealized gains and losses generated by the pool's investments. The total difference between the fair values of the investments in the pool and the values distributed to the pool participants using the amortized cost method described above is reported in the equity section of the Statement of Net Position as "Undistributed Unrealized Gains (Losses)".

SIF pool shares are bought and redeemed at \$1.00 based on the amortized cost of the investments in the SIF. The State of Wisconsin does not provide any legally binding guarantees to support the value of pool shares.

4. Deposit and Investment Risk

SWIB recognizes that risk issues permeate the entire investment process from asset allocation to performance evaluation. SWIB monitors risk through multiple forms of analysis and reporting. For the SIF, evaluations of levels of diversification,

nominal risk exposures including sector, maturity, and interest rate exposures, and risk/return plots form the core of the monitoring process. In addition, the portfolio is reviewed daily for compliance with investment guidelines. At least quarterly, comprehensive reporting is presented to SWIB's Investment Committee and the Board of Trustees.

A. Credit Risk

Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations to the SIF. The Board established SIF investment guidelines with maximum exposure limits by security type based on the minimum credit ratings as issued by Nationally Recognized Statistical Rating Organizations (NRSROs). As of June 30, 2013, these credit ratings and aggregate exposures by investment type are found in the table entitled **Credit Quality Distribution for Securities**.

B. Custodial Credit Risk

Deposits — Custodial credit risk related to deposits is the risk that, in the event of the failure of a depository financial institution, SWIB will not be able to recover deposits that are in possession of an outside party. SWIB does not have a deposit policy specifically for custodial credit risk. As of June 30, 2013, the SIF held Certificates of Deposit (CD) with a value of \$25,800,000 invested pursuant to the Wisconsin Certificate of Deposit Program (administered by Bankers' Bank) established in July 1987. Investment guidelines provide that to be accepted into this program, banks must accept deposits in Wisconsin and meet credit-screening criteria designed to assure the safety of the deposits.

The Federal Deposit Insurance Corporation (FDIC) insures the pro rata share of Certificates of Deposit held by the LGIP up to \$250,000, and the State of Wisconsin appropriation for losses on public deposits protects a depositing municipality up to \$400,000 if the local governing body has designated the LGIP

Credit Quality Distribution for Securities

As of June 30, 2013

Investment Type	Rating	Fair Value	%
Repurchase Agreements (Collateral):			
U.S. Government Debt	AA	\$ 4,686,000,000	50.5
Government Sponsored Entity U.S. Agency	AA	605,000,000	6.5
U.S. Treasury:			
Short-Term (Bills)	A-1+	699,785,556	7.6
Long-Term (Notes)	AA+	49,943,965	0.5
Government Sponsored Entity U.S. Agency:			
Federal Home Loan Bank (FHLB)	A-1+	913,428,575	9.9
Federal Home Loan Mortgage Corp (FHLMC)	A-1+	1,121,860,966	12.1
Federal Home Loan Mortgage Corp (FHLMC)	AA+	25,000,000	0.3
Federal National Mortgage Association (FNMA)	A-1+	1,050,759,811	11.3
Federal National Mortgage Association (FNMA)	AA+	50,000,000	0.5
Certificates of Deposit:			
Non-Negotiable (Wisconsin CD Program)	NR	25,800,000	0.3
Banker's Acceptances	A-1+	45,987,078	0.5
Total Investments		<u>\$ 9,273,565,951</u>	<u>100.0</u>

as a public depository. Approximately \$25,800,000 is insured through FDIC insurance and the State of Wisconsin appropriation for losses on public deposits. The actual coverage of these deposits can fluctuate daily based on the allocable share of participants' accounts.

C. Concentration of Credit Risk

Concentration of credit risk is the risk of loss attributed to the magnitude of an organization's investment in a single issuer. The SIF's investment guidelines limit concentrations of credit risk by establishing maximum issuer and/or issue exposure limits based on credit rating. These guidelines do

not place a limit on maximum exposure for any U.S. Treasury or Agency securities. As of June 30, 2013 the SIF has more than five percent of its investments in FHLB (9.9%), FHLMC (12.4%), FNMA (11.8%), and Repurchase Agreement collateral consisting of various securities issued by these same three U.S. Agencies (6.5%). Since the Repurchase Agreements mature each day, new collateral, consisting of a different blend of U.S. Treasury and Agency securities, is assigned each night.

D. Interest Rate Risk

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an

Weighted Average Maturities (WAM) for Securities

June 30, 2013

Investment Type	Fair Value	WAM (Days)
Repurchase Agreements	\$ 5,291,000,000	1
Government & Agencies	3,910,778,873	78
Certificates of Deposit	25,800,000	125
Banker's Acceptances	45,987,078	77
Total Investments	<u>\$ 9,273,565,951</u>	
Portfolio Weighted Average Maturity (Days)		<u>34</u>

investment. The SIF uses the Weighted Average Maturity (WAM) method to analyze interest rate risk and investment guidelines mandate that the WAM for the entire portfolio will not exceed one year. SIF WAM summary by investment type is found in the table entitled **Weighted Average Maturities (WAM) for Securities**.

E. Foreign Currency Risk

Foreign currency risk is the risk that changes in exchange rates will adversely impact the fair value of an investment. SIF guidelines allow the investment in U.S. dollar denominated issues only.

5. Related Party Transactions

Wisconsin Statutes Chapter 20.002 (11) provides for the short-term temporary reallocation of surplus moneys between statutory funds, provided that the borrowing fund anticipates receiving future revenues to pay back the temporary loan. For Fiscal Year 2013, Chapter 20.002 (11) (b) 2 provides that General Fund borrowings may not exceed 9% of defined revenues (estimated borrowing cap of \$1.329 billion). Chapter 20.002 (11) (b) 3 permits an

additional temporary allocation not to exceed 3% of defined revenues for a period of up to 30 days (estimated total borrowing cap of \$1.772 billion). Further, Chapter 20.002 (11) (b) 1 limits the total amount of any temporary reallocations to a fund other than the General Fund to \$400 million. The borrowing fund is charged interest on the inter-fund loan at the SIF monthly interest rate. As of June 30, 2013 the amount of inter-fund borrowings between statutory funds invested in the SIF is listed in the table entitled **Inter-Fund Loans**.

Inter-Fund Loans

June 30, 2013

Fund	Loan Amount
Medical Assistance Trust Fund	\$ 232,817,000
Environmental Fund	7,991,000
Democracy Trust Fund	1,000
Total Loans	<u>\$ 240,809,000</u>



STATE OF WISCONSIN

Legislative Audit Bureau

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Joe Chrisman
State Auditor

Independent Auditor's Report on the Financial Statements and Other Reporting Required by *Government Auditing Standards*

Senator Robert Cowles and
Representative Samantha Kerkman, Co-chairpersons
Joint Legislative Audit Committee

Mr. Michael Williamson, Executive Director, and
Members of the Board of Trustees
State of Wisconsin Investment Board

Report on the Financial Statements

We have audited the accompanying financial statements and the related notes of the Various Funds (Local Government Property Insurance Fund, State Life Insurance Fund, Injured Patients and Families Compensation Fund, EdVest Tuition Trust Fund, and Historical Society Trust Fund) of the State of Wisconsin as of and for the year ended June 30, 2013, as listed in the table of contents.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

Our responsibility is to express opinions on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, which is issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor

considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of the accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinions on these financial statements.

Opinions

In our opinion, the financial statements referred to in the first paragraph present fairly, in all material respects, the respective financial position of each of the Various Funds as of June 30, 2013, and the respective changes in financial position for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Emphases of Matter

As discussed in Note 1 to the financial statements, the financial statements referred to in the first paragraph present only the investment activity of the Various Funds attributable to the Investment Board. The financial statements do not purport to, and do not, present fairly the financial activity of the Various Funds attributable to other state agencies. Further, they do not purport to, and do not, present fairly the financial position of the Investment Board or of the State of Wisconsin as of June 30, 2013, or the changes in financial position for the year then ended, in accordance with accounting principles generally accepted in the United States of America. Our opinions are not modified with respect to this matter.

As discussed in Note 2 to the financial statements, the Investment Board implemented Governmental Accounting Standards Board Statement Number 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position*, which made presentation changes to the Various Funds financial statements. Our opinions are not modified with respect to this matter.

Other Matter

Our audit was conducted for the purpose of forming opinions on the financial statements of the Various Funds. The supplementary information included as Management's Discussion and Analysis, which precedes the financial statements, is presented for purposes of additional analysis and is not a required part of the financial statements. We have applied certain limited procedures to the information that included inquiries of management about the methods of preparing the information. We further compared the information for consistency with management's responses to our inquiries, the financial statements, and other knowledge we obtained during our audit of the financial statements. However, we do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to do so. The introduction section of the annual report is presented for purposes of additional analysis and is not a required part of the financial statements. Such information has not been subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we do not express an opinion or provide any assurance on it.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued a report dated November 25, 2013, on our consideration of the Investment Board's internal control over financial reporting for the Various Funds; our tests of its compliance with certain provisions of laws, regulations, and contracts; and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Investment Board's internal control over financial reporting and compliance.

LEGISLATIVE AUDIT BUREAU

A handwritten signature in black ink, appearing to read "Joe Chrisman", written in a cursive style.

Joe Chrisman
State Auditor

November 25, 2013

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Various Funds

Management Discussion and Analysis

Management Discussion and Analysis provides an overview of the investment financial activities of the state trust funds collectively known as the “Various Funds”:

- Local Government Property Insurance Fund (LGP)
- State Life Insurance Fund (State Life)
- Injured Patients & Families Compensation Fund (Patients Comp)
- EdVest Tuition Trust Fund (EdVest)
- Historical Society Trust Fund (Historical Society)

The State of Wisconsin Investment Board (SWIB) has exclusive control over the investment and collection of principal, interest, and dividends of all monies invested of the Various Funds.

Following this section are the financial statements and notes which reflect only the investment activity of the Various Funds. The **Statement of Net Investment Position** provides information on the

types of investment assets and the liabilities of the Various Funds. The **Statement of Changes in Net Investment Position** provides information on the investment income of the Various Funds and their net investment position at year-end. The **Notes to the Financial Statements** provide additional information that is essential to a full understanding of the data provided in the financial statements. Condensed Various Funds financial information for the fiscal year ended June 30, 2013 (with comparable amounts for 2012) is in the table entitled **Various Funds Condensed Investment Financial Information**.

Percentage changes in the Net Investment Position of the Various Funds were due to Net Investment Income, as discussed below, and due to program activities within each fund that were not investment related.

During the fiscal year 2013, bond prices closed the fiscal year slightly lower from the beginning of the fiscal year. During the prior fiscal year 2012, bond prices closed the fiscal year significantly higher from the beginning of the fiscal year. Domestic equity markets in the current fiscal year closed significantly higher from the beginning of the fiscal year, as compared to slightly higher during

Various Funds Condensed Investment Financial Information

	2013	2012	% Change		
Net Investment Position					
LGP Fund	\$ 27,027,192	\$ 30,228,364	(10.6)		
State Life Fund	109,665,279	115,646,900	(5.2)		
Patients Comp Fund	1,076,621,533	1,027,638,200	4.8		
EdVest Fund	6,679,402	7,389,508	(9.6)		
Historical Society Fund	12,638,725	11,435,232	10.5		
				One Year Return %	
Net Investment Income				Fund	Benchmark
LGP Fund	\$ 44,069	\$ 68,719	(35.9)	0.1	0.1
State Life Fund	(2,818,033)	18,159,662	(115.5)	(2.6)	(2.6)
Patients Comp Fund	30,772,994	67,477,089	(54.4)	3.0	2.4
EdVest Fund	62,937	382,595	(83.5)	0.9	(0.1)
Historical Society Fund	1,764,232	550,349	220.6	15.8	15.6

the prior fiscal year. The Federal Reserve maintained the federal funds rate “target range” between zero and 0.25% during both fiscal years.

The 35.9% decrease in the Net Investment Income for the LGP Fund was due to a total reduction in allocation of bonds and low short-term interest rates on the increased investment in the State Investment Fund (SIF) as compared to the prior fiscal year.

The State Life, Patients Comp, and EdVest Funds are primarily “buy and hold” portfolios. Highly rated bonds (at time of purchase) are acquired for each portfolio and held to maturity. Net Investment Income is subject to swings caused by the effect of interest rate changes on bond prices.

The 115.5% decrease in Net Investment Income for the State Life Fund was due to slightly lower bond prices during the current fiscal year, compared to significantly higher prices during the prior fiscal year.

The Patients Comp Fund also experienced a decrease in Net Investment Income due to slightly lower bond prices. However, the decrease was more than offset by four indexed stock funds, representing 20.2% of Investments, which experienced a \$34.5 million increase in fair value during the current fiscal year as compared to a \$7.1 million increase in fair value during the prior fiscal year.

The 83.5% decrease in Net Investment Income for the EdVest Fund was due to depreciation in the prices of government sponsored entity bonds it held as compared to appreciation in the prior fiscal year.

The 220.6% increase in Net Investment Income for the Historical Society Fund was largely due to an indexed stock fund, representing 76.3% of Investments, which experienced a \$1.8 million increase in fair value during the current fiscal year as compared to a \$0.3 million increase in fair value during the prior fiscal year.

Various Funds

Financial Statements

Statement of Net Investment Position

As of June 30, 2013

	Local Gov't Property Insurance Fund	State Life Insurance Fund	Injured Patients & Families Compensation Fund	EdVest Tuition Trust Fund	Historical Society Trust Fund
Investment Assets					
Cash and Cash Equivalents:					
Unrestricted	\$ 26,962,591	\$ 2,175,081	\$ 41,419,282	\$ 1,378,032	\$ 244,190
Restricted	-	-	39,304,363	-	-
Receivables:					
Income	64,601	1,354,849	9,324,324	11,430	59,358
Sales	-	-	-	-	5,062
Investments (at fair value):					
Fixed Income	-	106,507,716	786,887,680	5,289,940	2,921,435
Equity	-	-	199,697,194	-	9,409,198
Total Investment Assets	27,027,192	110,037,646	1,076,632,843	6,679,402	12,639,243
Investment Liabilities					
Purchases Payable	-	-	5,545	-	158
Accounts Payable	-	372,367	5,765	-	360
Total Investment Liabilities	-	372,367	11,310	-	518
Net Investment Position	\$ 27,027,192	\$ 109,665,279	\$ 1,076,621,533	\$ 6,679,402	\$ 12,638,725

Statement of Changes in Net Investment Position

For the Fiscal Year Ended June 30, 2013

	Local Gov't Property Insurance Fund	State Life Insurance Fund	Injured Patients & Families Compensation Fund	EdVest Tuition Trust Fund	Historical Society Trust Fund
Investment Activities					
Income					
Net Increase (Decrease) in					
Fair Value of Investments	\$ (27,891)	\$ (8,054,407)	\$ (745,743)	\$ (179,402)	\$ 1,776,726
Interest & Dividends	74,979	5,242,419	31,582,966	242,339	255
Expenses	(3,019)	(6,045)	(64,229)	-	(12,749)
Net Investment Income (Loss)	44,069	(2,818,033)	30,772,994	62,937	1,764,232
Participant Transactions					
Net Receipts (Disbursements) -					
Non-Investment Activity	(3,245,241)	(3,163,588)	18,210,339	(773,043)	(560,739)
Change in Net Investment Position	(3,201,172)	(5,981,621)	48,983,333	(710,106)	1,203,493
Net Investment Position - Beginning of Year	30,228,364	115,646,900	1,027,638,200	7,389,508	11,435,232
Net Investment Position - End of Year	\$ 27,027,192	\$ 109,665,279	\$ 1,076,621,533	\$ 6,679,402	\$ 12,638,725

The accompanying notes are an integral part of this statement.

Notes to the Financial Statements

1. Description of Funds

The State of Wisconsin Investment Board (SWIB or the Investment Board) has control of the investment and collection of principal, interest, and dividends of all monies invested of the Local Government Property Insurance Fund, State Life Insurance Fund, Injured Patients and Families Compensation Fund, EdVest Tuition Trust Fund, and Historical Society Trust Fund (collectively known as the “Various Funds”).

The statements presented herein reflect only the investment activity of the Various Funds. Excluded from the presentation in the statements are, for example, claim reserves, reserves for life policies and contracts, contribution revenue, premiums earned, benefit expense, and expenditures from endowment income.

The State of Wisconsin’s Comprehensive Annual Financial Report contains all of the activity of the Various Funds.

The State Investment Fund (SIF) is used to temporarily invest the operating cash flows of the Various Funds. SWIB manages the SIF with oversight by a Board of Trustees, as authorized in Wisconsin Statutes 25.14 and 25.17. SWIB is not registered with the Securities and Exchange Commission (SEC) as an investment company.

A. Local Government Property Insurance Fund

The Local Government Property Insurance Fund (LGP) provides property insurance protection to local government units on an optional basis. The Office of the Commissioner of Insurance (OCI) is responsible for administering the operations of the LGP Fund, while SWIB performs the investment activities for the fund. SWIB’s investment objective is to ensure safety of principal and maximization of return within liquidity needs established by the OCI. Wisconsin Statute 25.17(3)(b) allows investments in direct obligations of the United States and Canada, securities guaranteed

by the United States, unsecured notes of financial and industrial issuers, Yankee/Euro dollar issues, and certificates of deposit issued by banks in the United States, including solvent financial institutions in Wisconsin.

B. State Life Insurance Fund

The State Life Insurance Fund (State Life) offers life insurance protection to Wisconsin residents in amounts up to \$10,000 per person. The Office of the Commissioner of Insurance is responsible for administering the operations of the State Life Fund. SWIB’s investment objective is to maintain a diversified portfolio of high quality publicly issued fixed income obligations that will preserve principal, maximize income while minimizing costs to policyholders, and approximate the expected life of the fund’s insurance contracts. Wisconsin Statute 25.17(3)(a) allows investments in loans, securities and any other investments as authorized by s. 620.22, Wis. Stats. Permitted classes of investments include bonds of government units or of corporations, loans secured by mortgages, preferred or common stocks, real property and other investments not specifically prohibited by statute.

C. Injured Patients and Families Compensation Fund

The Injured Patients and Families Compensation Fund (Patients Comp) provides medical malpractice insurance protection to health care providers permanently practicing or operating in Wisconsin. Management of the Patients Comp Fund is vested with a Board of Governors and administration of the operations of the fund is the responsibility of the Office of the Commissioner of Insurance. SWIB is responsible for investing the securities held by this fund. SWIB’s investment objective is to maintain a diversified portfolio of investments to provide a balance between capital appreciation, preservation of capital, and current income consistent with the needs of the Patients Comp Fund. Wisconsin Statute 25.17(3)(a) allows investments in loans, securities

Various Funds

Notes to Financial Statements

and any other investments as authorized by s. 620.22, Wis. Stats. Permitted classes of investments include bonds of governmental units or of corporations, loans secured by mortgages, preferred or common stock, real property and other investments not specifically prohibited by statute.

D. EdVest Tuition Trust Fund

The EdVest Tuition Trust Fund offered families a way to prepare for future higher education costs. When the plan was established in 1997, it offered a bond-based tuition unit investment option. These units, plus investment earnings, are expected to equal one percent of the projected average annual cost of tuition at University of Wisconsin campuses in the year of their use. The Department of Administration is responsible for the administration of EdVest. Wisconsin Statute 16.64(10)(b) directs SWIB to invest moneys held in the Tuition Trust Fund in investments with maturities and liquidity that are appropriate for the needs of the fund as reported by the Department of Administration in its quarterly reports. All income derived from such investments shall be credited to the fund. The sale of EdVest tuition units was discontinued in 2002. Other investment options are available under the Wisconsin 529 college savings plans, but these are not managed by the Investment Board.

E. Historical Society Trust Fund

The Wisconsin Historical Society collects and preserves historical and cultural resources relating to the history of Wisconsin and the western United States, conducts historical research, facilitates and encourages education in Wisconsin history, and serves as the Trustee of the State for the preservation and care of government records. In addition to state and federal funds, the Wisconsin Historical Society receives gifts, grants, and bequests to assist it in carrying out its mission. The gifts, grants and bequests are deposited into the Historical Society Trust Fund (Historical Society). SWIB is responsible for managing and supervising the fund's investments with an investment objective of maintaining a diversified portfolio of

high quality publicly issued equities and fixed income obligations providing long-term growth in capital and income generation. Any income earned, except where reinvestment is required by the terms of the gift or bequest, may be expended by the fund in accordance with provisions of the gift, grant or bequest.

2. Significant Accounting Policies

A. Basis of Presentation

The accompanying financial statements of the investment activity of the Various Funds are prepared in conformity with accounting principles generally accepted in the United States of America for governments as prescribed by the Governmental Accounting Standards Board (GASB).

The Local Government Property Insurance Fund, the State Life Insurance Fund, and the Injured Patients and Families Compensation Fund operate similar to insurance enterprises and are reported by the State as proprietary funds. The EdVest Tuition Trust Fund is reported by the State as a fiduciary fund and the Historical Society Trust Fund is reported by the State as a governmental fund.

B. Measurement Focus and Basis of Accounting

The accompanying statements are prepared based upon the flow of economic resources measurement focus and the accrual basis of accounting. Under the accrual basis of accounting, revenues are recognized in the accounting period in which they are earned and become measurable, and expenses are recognized in the period incurred, if measurable. Security transactions and the related gains and losses are recorded on a trade date basis. Interest income is accrued as earned and dividend income, if any, is recorded on the ex-dividend date.

C. Valuation of Securities

As required by GASB Statement No. 31, the investments of the Various Funds are reported at fair value, with unrealized and realized gains and

losses reflected in the **Statement of Changes in Net Investment Position** as “Net Increase (Decrease) in Fair Value of Investments.” Generally, fair value is based on quoted market prices.

D. Use of Estimates

The preparation of financial statements in accordance with generally accepted accounting principles (GAAP) requires management to make estimates that affect amounts reported herein. Due to the inherent uncertainty involved, actual results could differ from those estimates.

E. Cash and Cash Equivalents

“Cash and Cash Equivalents” reported on the **Statement of Net Investment Position** include bank deposits and the individual funds’ shares in the State Investment Fund.

Beginning in January 2011, the Patients Comp Fund segregated as restricted certain cash balances which represent amounts awarded by court judgments to pay for the future medical expenses of injured plaintiffs.

F. New Accounting Pronouncement

In June 2011, GASB issued Statement No. 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position*. The objective of this statement is to provide financial reporting guidance for deferred outflows of resources and deferred inflows of resources as required elements of the financial statements. The implementation of this statement did not impact the financial position of the Various Funds. However, the adoption of this statement resulted in presentation changes to replace net assets with net position on the financial statements.

3. Deposits and Investments

SWIB recognizes that risk issues permeate the entire investment process from asset allocation to performance evaluation. SWIB monitors risk through

multiple forms of analysis and reporting. Inspection of levels of diversification, nominal risk exposures, risk/return plots, and matching liabilities with assets form the core of the monitoring process. In addition, portfolios and asset classes are reviewed monthly for compliance with investment guidelines and exceptions, if any, are remedied in a prudent manner. On a quarterly basis, identified guideline exceptions are reviewed by SWIB’s Enterprise Risk and Compliance Committee.

A. Credit Risk

Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations to the Various Funds. The Various Funds’ investment guidelines generally require that issues be rated “A-” or better at the time of purchase based on the minimum credit ratings as issued by Nationally Recognized Statistical Rating Organizations (NRSROs). Patients Comp Fund guidelines provide that, at the time of purchase, at least 80% of the bond portfolio must be rated “A3/A-” or better, using the lower of split ratings. As of June 30, 2013, these credit ratings and aggregate exposures by investment type can be found in the table entitled **Credit Quality Distribution for Fixed Income Securities**. While the Historical Society’s bond fund investment is not assigned a rating by S&P, the underlying holdings have an average S&P rating of AA-.

B. Custodial Credit Risk

Deposits — Custodial credit risk related to deposits is the risk that, in the event of the failure of a depository financial institution, the Various Funds will not be able to recover deposits that are in possession of an outside party. The Various Funds do not have a deposit policy specifically for custodial credit risk. As of June 30, 2013, the Various Funds had a total of \$3,539 deposited in a bank account, all of which was covered by FDIC insurance.

Investments — Custodial credit risk related to investments is the risk that, in the event of the

Various Funds

Notes to Financial Statements

Credit Quality Distribution for Fixed Income Securities

June 30, 2013

Rating	LGP		State Life		Patients Comp		EdVest		Historical Society	
	Fair Value	%	Fair Value	%	Fair Value	%	Fair Value	%	Fair Value	%
AAA	\$ -	0.0	\$ 1,116,010	1.0	\$ 15,775,969	1.8	\$ -	0.0	\$ -	0.0
AA	-	0.0	43,761,135	40.3	345,272,276	39.8	4,648,418	69.7	-	0.0
A	-	0.0	38,796,642	35.7	277,858,137	32.0	292,996	4.4	-	0.0
BBB	-	0.0	21,860,188	20.1	132,446,114	15.3	348,526	5.2	-	0.0
BB	-	0.0	973,741	0.9	15,535,134	1.8	-	0.0	-	0.0
B	-	0.0	-	0.0	-	0.0	-	0.0	-	0.0
CCC	-	0.0	-	0.0	-	0.0	-	0.0	-	0.0
D	-	0.0	-	0.0	-	0.0	-	0.0	-	0.0
Not Rated	-	0.0	-	0.0	50	0.0	-	0.0	-	0.0
Bond Fund	-	0.0	-	0.0	-	0.0	-	0.0	2,921,435	92.4
Subtotals	-	0.0	106,507,716	98.0	786,887,680	90.7	5,289,940	79.3	2,921,435	92.4
SIF (unrated)	26,962,000	100.0	2,175,000	2.0	80,723,000	9.3	1,378,000	20.7	242,000	7.6
Totals	\$ 26,962,000	100.0	\$ 108,682,716	100.0	\$ 867,610,680	100.0	\$ 6,667,940	100.0	\$3,163,435	100.0

Note: SIF shares are reported on the Statement of Net Investment Position as Cash and Cash Equivalents.

failure of the counterparty to a transaction, the Various Funds will not be able to recover the value of investments that are in the possession of an outside party. The Various Funds do not have an investment policy specifically for custodial credit risk. As of June 30, 2013, the Various Funds did not have any direct investment securities exposed to custodial credit risk.

C. Concentration of Credit Risk

Concentration of credit risk is the risk of loss attributed to the magnitude of an organization's investment in a single issuer. The Various Funds' investment guidelines limit concentrations of credit risk by establishing maximum issuer and/or sector exposure limits. Generally, the guidelines require that no single issuer may exceed 5% of the fund investments, with the exception of the U.S. Government and its Agencies, whose exposure is unlimited. The LGP Fund further limits AAA-rated U.S. mortgage-backed, AAA-rated asset-backed, and individual corporate issuers to 3% of the market value

of the fund investments. None of these issuers were owned at fiscal year end.

Excluding investments issued or explicitly guaranteed by the U.S. government and pooled investments, as of June 30, 2013, none of the Various Funds had more than 5% of their total investments (including the SIF) in a single issuer.

D. Interest Rate Risk

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. The Various Funds use the duration method to identify and manage interest rate risk. Three of the Various Funds have investment guidelines relating to interest rate risk. The LGP Fund guidelines require that a bond's maturity must not exceed ten years. The State Life Fund guidelines require the Weighted Average Maturity (WAM) of the portfolio, including cash, to be a minimum of ten years. The Patients Comp Fund guidelines require the average

Duration or WAM (in years) for Fixed Income Securities

June 30, 2013

Investment	LGP		State Life		Patients Comp		EdVest		Historical Society	
Type	Fair Value	Duration	Fair Value	WAM	Fair Value	Duration	Fair Value	Duration	Fair Value	Duration
Govt/Agcy	\$ -		\$ 41,308,946	13.98	\$ 316,201,313	5.35	\$ 4,648,418	3.03	\$ -	
Corporate	-		65,198,770	16.69	470,686,367	6.21	641,522	3.43	-	
Bond Fund	-		-		-		-		2,921,435	5.37
Subtotal / Wtd Avg	-		106,507,716	15.64	786,887,680	5.86	5,289,940	3.08	2,921,435	5.37
SIF (WAM)	26,962,000	0.09	2,175,000	0.09	80,723,000	0.09	1,378,000	0.09	242,000	0.09
Total / Wtd Avg	\$ 26,962,000	0.09	\$ 108,682,716	15.33	\$ 867,610,680	5.33	\$ 6,667,940	2.46	\$ 3,163,435	4.97

duration of the aggregate bond portfolio to be less than ten years. Summary duration or WAM analysis is found in the table entitled **Duration or WAM (in Years) for Fixed Income Securities**.

E. Foreign Currency Risk

Foreign currency risk is the risk that changes in exchange rates will adversely impact the fair value of an investment. The Various Funds' investment guidelines do not specifically address foreign currency risk with the exception that the State Life Fund only allows investments in U.S. dollar denominated instruments. As of June 30, 2013, the Various Funds did not directly own any issues denominated in a foreign currency.

4. Derivative Financial Instruments

Interest Only Strips — Interest only strips are securities that derive cash flow from the payment of interest on underlying debt securities. EdVest held several interest only strips for yield enhancement purposes. Because the underlying securities are United States Treasury obligations, the credit risk is low. On the other hand, interest only strips may be more sensitive to interest rate fluctuations, which results in greater price volatility, and thus the market risk is higher than for traditional United States Treasury obligations.

As of June 30, 2013, EdVest held interest only strips valued at \$4.6 million, representing approximately 69.7% of portfolio investments.

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