

FY 2010 Annual Report



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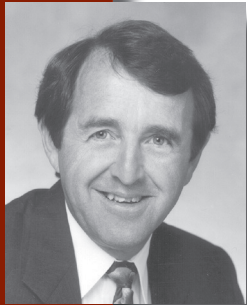
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Introduction

Message from the Chair



Since 2007, we have significantly increased the share of investments managed by SWIB's own professional investment staff and reduced reliance on outside investment firms. Our staff now internally manages nearly 50 percent of our stock and bond holdings, almost double the average for large public pension funds according to recent national surveys.

The net annual savings to the Wisconsin Retirement System (WRS) from active internal management currently exceeds \$26 million and is growing. Active internal management costs in the public markets for the five years ending December 31, 2009, averaged just seven basis points of assets under management, only one-quarter the cost of external management. More importantly, two recent reports from industry experts—one specifically about SWIB and the other regarding a group of large public pension funds—observed that investment results from internal management have been as good as or better than those of external management after costs.

Some public markets, such as economically emerging countries, are less suited to internal management because having staff in country can be an important part of the investment process. In private markets like venture capital and real estate, it is impractical for SWIB and most public pension funds to staff up to the level needed to internally select and manage a large portfolio of start-up companies or individual properties. Even so, SWIB staff has an important role in these markets because they select and monitor the external managers or general partners that make investments on our behalf.

Building a robust and successful internal management program requires the ability to attract and retain experienced staff. The trust funds have benefited financially from the decisions of Wisconsin policymakers and WRS leaders to support adding the staff and offering the compensation necessary for SWIB to sustain and expand low cost internal management. In fact, the cumulative added return from our internal investments in stocks and bonds over the five years ending December 31, 2009, was over \$200 million after costs.

By being directly engaged in the markets, SWIB's internal management program also helps the WRS in other important ways. SWIB is more informed in setting overall long-term strategy and can be more nimble in the volatile financial markets that continue to challenge investors.

A handwritten signature in black ink, reading "James A. Senty". The signature is stylized with a large, sweeping "J" and "S".

James A. Senty, Chair

The Core Fund gained 13.3 percent for fiscal year 2010 and surpassed its one-, five- and ten-year performance benchmarks. The Fund's five-year return at June 30 exceeded 70 percent of the public pension funds tracked by Callan Associates and it took less risk to add return than most peers.

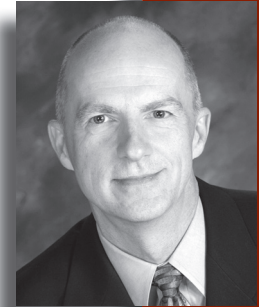
The Core Fund gain came in the first half of the fiscal year as U.S. and international stocks continued to recover from the market collapse of 2008. In the second half of the fiscal year, concerns about the pace of economic recovery and the European debt crisis contributed to a decline in U.S. and international stocks. This was partially offset by gains from the fixed income market.

For several years, SWIB has been exploring strategies to lessen the impact of a volatile stock market on Core Fund returns and fund participants. In 2010, SWIB took a further measured step on that path. The target allocation to equities (stocks) was reduced from 55 percent to 53 percent of the Fund and the multi-asset allocation was increased from four to six percent. When implemented, this change will enable SWIB to gradually consider more new investment opportunities aimed at further reducing Fund volatility.

As SWIB evaluates and implements further risk reduction strategies, an outcome may be that Core Fund gains will be somewhat less when stock markets are rising, but losses will be smaller when markets are in decline. This would provide increased stability in contribution rates and benefits to members.

SWIB is also taking steps to ensure we have the infrastructure to support risk reducing investment strategies that may be more complex to implement. In 2010, we benchmarked our information technology and operations services with those of 35 leading public and private investment organizations. This exercise confirmed that SWIB successfully implemented a significant increase in internally managed assets with fewer internal and external resources than most of its peers. It also provided a valuable road map to ensure we have the appropriate tools and practices for the future.

Because the Core Fund is in sound financial condition, SWIB can focus its attention on ways to keep it that way and reduce risk, rather than having to increase investment risk to try to boost returns. Many other pension funds are not as fortunate to be in our position.



A handwritten signature in black ink, consisting of a stylized 'K' followed by a cursive 'B' and a long horizontal stroke.

Keith Bozarth, Executive Director

Overview

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 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 statutes. The Board's duties as manager of the State's 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.

SWIB is directed by a nine-person, independent Board of Trustees and staffed with professional money managers and support personnel. The Board of Trustees appoints the executive director of the Investment Board. The executive director oversees the staff, develops and recommends agency and investment policies for Board adoption, and ensures adherence to state law and policies.

Assets Under Management - June 30, 2010

Fund	in Millions	% of Total
<i>Core Retirement Investment Trust Fund</i>	\$ 64,618	87%
<i>Variable Retirement Investment Trust Fund</i>	<u>4,532</u>	<u>6</u>
Wisconsin Retirement System	\$ 69,150	93
State Investment Fund*	4,537	6
Various Funds		
Injured Patients and Families Compensation Fund	652	1
State Life Insurance Fund	98	0
Local Govt Property Insurance Fund	47	0
Historical Society Trust Fund	9	0
Tuition Trust Fund	<u>8</u>	<u>0</u>
	<u>\$ 74,501</u>	<u>100 %</u>

*Excludes deposits from Core Retirement Investment Trust Fund, Variable Retirement Investment Trust Fund and Various Funds.

Note: Values and percentages may not add due to rounding.

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.

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.

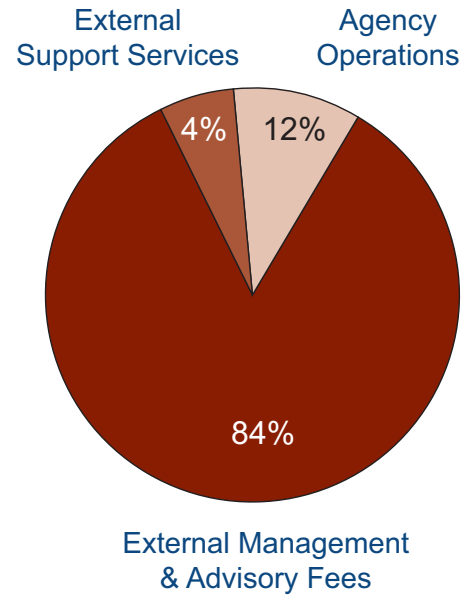
Management costs of the State of Wisconsin Investment Board include external management and advisory fees, external investment support services as well as expenses incurred to manage agency operations. Expenses are paid from investment earnings of the funds SWIB manages. The majority of expenses are fees paid to outside advisors and fund managers, which were \$194.7 million in calendar year 2009 and represented about 84% of total costs. Costs of other external support services include custodial banking services, investment research, and legal services.

Agency operating expenses for staff compensation, overhead and equipment were **\$28.4 million** in calendar year 2009 and represented about **12%** of total costs. SWIB participates in an annual independent review of costs which compares SWIB to other investment managers and public pension fund peers. The 2009 analysis provided by CEM Benchmarking, Inc.¹ concluded that SWIB's total cost to manage the Core Fund was **41¢** per \$100 managed. The CEM report indicated that this amount was **less than the costs** incurred by peers with a similar mix of assets.

The cost to manage the Core Fund was **\$224.2 million** in 2009. This represents **96.6%** of SWIB's total cost of management. In addition to the Core Fund, SWIB manages seven other funds. SWIB's costs to manage all funds were **\$232.2 million**, or **32.5¢** per \$100 managed in 2009.

Management Costs

Calendar Year Ended 12/31/09



- Costs for managing all funds were 32.5¢ per \$100 under management.
- All management costs are funded with earnings from the funds.
- Total costs for managing all funds for the calendar year ending December 31, 2009 were \$232.2 million.
- According to CEM¹, SWIB's costs for the Core Fund in calendar year 2009 were considered low cost compared to its peers based on the mix of assets managed.

Total Management Costs

Calendar Year Ended 12/31/09

External Management & Advisory	\$194,724,500
Agency Operations	28,383,500
Consulting*	4,115,800
Custodial Banking	504,700
Investment Research	<u>4,461,000</u>
Total	<u>\$232,189,500</u>

* Includes legal services

¹ CEM Benchmarking, Inc. is a Toronto-based firm that provides cost measurement and analysis of corporate and public pension funds.

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.
 - 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.



James Senty



Thomas Boldt



Bruce Colburn



David Geertsen



David Kruger



William Levit, Jr.



Wayne McCaffery



Daniel Schooff



David Stella

Public Members*

James Senty, Board Chair, President of Midwest Gas Companies, La Crosse

Thomas Boldt, Board Vice Chair, President of The Boldt Group, Inc./CEO, The Boldt Co., Appleton

Bruce Colburn, Director, Central States Property Services Division, Services Employees International Union

David Geertsen, Local Government, Finance Director, Kenosha County

David Kruger, CEO/Owner, The Fiore Companies, Madison

William Levit, Jr., Attorney, Godfrey & Kahn S.C., Milwaukee

WRS Participant Members*

Wayne McCaffery, Educator, Retired Teacher, Stevens Point

David Stella, Board Secretary, Non-educator, Secretary, Department of Employee Trust Funds

Department of Administration

Daniel Schooff, Department Secretary

*Appointed Board members serve six-year terms.

SWIB has 124.25 authorized positions. The executive director oversees the staff. Portfolio managers, analysts and traders are responsible for daily investment decisions made within the parameters of the investment policy. Investment managers are supported by a well-trained staff with legal, technical, accounting and administrative expertise.

There are three investment groups — public equities (stocks), public fixed income, and private markets. A funds management group is responsible for a wide range of external manage strategies and risk management.

Domestic stocks primarily consist of investments in U.S. companies. International stocks encompass investments in markets for developed and emerging countries.

Fixed income investments include U.S. government bonds and corporate bonds purchased in public markets, corporate securities, U.S. Treasury and agency securities and global bonds.

Private markets investments include real estate, private equity and private debt investments. Real estate investments are commercial real estate with SWIB as a sole direct owner, or in joint ventures and partnerships. The portfolio is diversified by region and by property type. Private equity/debt investments primarily focus on leveraged buyouts (LBOs), venture capital, partnerships and structured investments.

The analytics and fund management group has the principle role in the development of external management strategies and oversees their execution. The group also is responsible for achieving performance targets within acceptable risk characteristics.

Senior Management

Keith S. Bozarth
Executive Director

David C. Villa
Chief Investment Officer

Gail L. Hanson
Deputy Executive Director

Brandon Duck
Internal Audit Director

Chuck Carpenter
Managing Director Private
Markets

Kenneth W. Johnson
Chief Operating Officer/
Chief Financial Officer

L. Jane Hamblen
Chief Legal Counsel

Ronald A. Mensink
Managing Director Analytics
& Fund Management

Ledell Zellers
Human Resources Director

A majority of the investment staff holds or is pursuing the Chartered Financial Analyst (CFA) designation and the Board adheres to CFA standards. Senior investment staff experience ranges between 10 and 34 years.

Wisconsin Retirement System

- WRS includes current and former employees of state agencies, the university system, school districts and most local governments.
- 9th largest public pension fund in the U.S.
- 30th largest pension fund in the world.
- Comprised of the Core Fund, a balanced fund, and the Variable Fund, a stock fund.
- Core Fund gains and losses are spread over five years to smooth the effect on participants' accounts.
- Variable Fund participant accounts fully reflect prior year gains and losses of the investments.
- About 110,000 people participate in the Variable Fund.

The Wisconsin Retirement System (WRS) makes up 93% of the assets managed by SWIB. As a fiduciary for the funds, SWIB is dedicated to earning the best possible rate of return within acceptable risk parameters consistent with "prudent investor" standards. As of June 30, 2010, the total assets of the WRS were \$69.1 billion.

The WRS includes the pension funds available through most public employers in Wisconsin other than the City of Milwaukee and Milwaukee County. Contributions made to the WRS by participating employees and their employers are invested by the Investment Board to finance retirement benefits.

More than 566,000 people participate in the WRS. Over \$3.7 billion in benefits were paid in 2009 to 151,000 annuitants in the WRS. Investment earnings account for the majority of the annuities paid, thus lowering the costs paid by taxpayers.

The WRS is comprised of two trust funds. The larger of the two is the Core Fund, which is a broadly diversified portfolio of stocks, bonds, real estate and other holdings. The second fund is the Variable Fund, which is invested in stocks.

The process for determining the effect of investment returns on employee accounts ("effective rate") and changes in benefits for retirees differs between the Variable and Core Funds.

The Department of Employee Trust Funds (ETF) is responsible for administering the benefits of the WRS. Most employees who retire receive a pension annuity initially determined by a formula (calculated by ETF) using years of service, salary and job type.

ETF computes benefit changes based on the December 31 rate of return for each of the two trust funds to determine the impact on participants.

Annualized Performance Ending 6/30/10

Retirement Funds	1-Year Return	5-Year Return	10-Year Return
Core Fund	13.3%	3.3%	3.7%
Benchmark	12.1%	3.2%	3.5%
Variable Fund	14.6%	0.3%	-0.2%
Benchmark	14.1%	0.3%	-0.4%
S&P 500	14.4%	-0.8%	-1.6%

The State Investment Fund (SIF) is a pool of cash balances of various state and local governmental units. The objectives of this fund are to provide safety of principal, liquidity and a reasonable rate of return. SWIB's Fixed Income Group manages the State Investment Fund.

The State Investment Fund includes retirement trust funds' cash balances pending longer-term investment by SWIB's other investment groups. This fund also functions as the State's cash management fund. By pooling the idle cash balances of all 60 state funds, it provides the State's general fund with the needed liquidity for operating expenses.

Over 1,000 local units of government also deposit revenues in the SIF until they are needed. These funds are commingled in the Local Government Investment Pool (LGIP). The cash balances available for investment vary daily as cash is accumulated or withdrawn from the agency funds. The SIF is invested primarily in obligations of the U.S. government and its agencies, and high quality commercial bank and corporate debt obligations. Net assets of the State Investment Fund as of June 30, 2010, were \$6.5 billion.

State Investment Fund Annualized Time- Weighted Returns

<i>Fiscal Year</i>	<i>Return</i>
2000	5.49%
2001	5.97
2002	2.50
2003	1.49
2004	1.03
2005	2.08
2006	4.23
2007	5.40
2008	4.02
2009	1.33
2010	0.25

SIF Portfolio Characteristics as of June 30, 2010

- 89% of Fund invested in U.S. government securities and U.S. government agency securities.
- Average maturity 78 days versus iMoneyNet* at 36 days.
- Short-term liquidity (0 - 3 months) equal to 188% of LGIP and 76% of SIF.
- 30% of portfolio assets change rates overnight, 62% in three months.

Portfolio Rankings

- SIF provided a superior rate of return, ranking 1st out of 194 government money market funds.
- SIF also ranked 21st out of 1,127 money market funds (top 2%).*

* iMoneyNet All Taxable Money Market Index

Source: The iMoneyNet financial company money fund statistics.

To achieve its objectives, the SIF adheres to rigorous quality standards, pays careful attention to maturity schedules and places emphasis on high marketability. Enhanced return is sought through intensive portfolio management, which considers probable changes in the general structure of interest rates.

Earnings for the SIF are calculated and distributed monthly based on the participant's average daily balance as a percent of the total pool.

Contact Information

Injured Patients and Families Compensation Fund

(608) 266-6830 (Madison)
<http://oci.wi.gov/pcf.htm>

State Life Insurance Fund

(608) 266-0107 (Madison) (800) 562-5558 (toll-free)
<http://oci.wi.gov/slif.htm>

Local Government Property Insurance Fund

(608) 266-3585 (Madison) (800) 236-8517 (toll-free)
<http://oci.wi.gov/lgpif.htm>

State Historical Society

(608) 264-6400
<http://www.wisconsinhistory.org/>

EdVest

(608) 264-7899 (Madison)
(888) 338-3789 (toll-free)
<http://www.wellsfargoadvantagefunds.com/wfweb/wf/ev/index.jsp>

SWIB manages five funds for various state agencies. These funds represent about 1% of the total assets managed. Each is invested to meet specific objectives.

INJURED PATIENTS AND FAMILIES COMPENSATION FUND

The Fund was created by statute in 1975 to provide excess medical malpractice coverage for Wisconsin health care providers. Health care providers obtain primary medical malpractice insurance from private insurance companies in an amount required by law. Coverage in excess of the primary insurance is purchased by the Fund. The program is administered by the Office of the Commissioner of Insurance.

STATE LIFE INSURANCE FUND

The Fund is a state-sponsored life insurance program for the residents of Wisconsin. The applicant must be a state resident at the time of application for coverage through the Fund. The Fund operates on a nonprofit basis and receives no subsidies from the state. The program is administered by the Office of the Commissioner of Insurance.

LOCAL GOVERNMENT PROPERTY INSURANCE FUND

The purpose of the Fund is to make reasonably priced property insurance available for tax-supported local government property such as government buildings, schools, libraries, and motor vehicles. The Fund provides policy and claim service to the policyholders. The program is administered by the Office of the Commissioner of Insurance.

HISTORICAL SOCIETY TRUST FUND

The State Historical Society of Wisconsin is both a state agency and a private membership organization. SWIB is responsible for investing the endowment funds of the Historical Society to help with its goal to promote a wider appreciation of the American heritage, with an emphasis on the collection, advancement, and dissemination of knowledge of the history of Wisconsin and the region.

TUITION TRUST FUND

The Tuition Trust Fund was created to invest the funds for EdVest Wisconsin, a state-sponsored way to save for the cost of college expenses. This Fund is currently closed to new participants. Other options are administered through the Office of the State Treasurer.

SWIB's Corporate Governance Program has two primary goals: (a) to protect and increase SWIB's long-term returns and (b) to meet SWIB's fiduciary obligation to manage shareholder rights as an asset of the trust funds. In 2010, the passage of the Dodd-Frank Wall Street Reform and Consumer Protection Act concluded a significant multi-year effort by SWIB and other institutional investors to improve shareholder rights and advance governance initiatives.

Our primary focus continues to be working with directors and management of a company with a goal of increasing economic value. It is one way SWIB works to fulfill its fiduciary obligation to the WRS beneficiaries. The program incorporates traditional corporate governance practices, corporate citizenship and litigation. Its strategy is developed by SWIB's governance and investment staff working together within parameters approved by Trustees.

Corporate governance — the relationship between the shareholders, directors and management of a company, as defined by the corporate charter, bylaws, formal policy and rule of law — makes up the largest part of our program. Governance issues are considered when voting our proxies and evaluating investments. Each year SWIB identifies key issues based on staff recommendations and national trends.

Then SWIB monitors companies within its portfolios that could benefit from improvements in the identified areas. SWIB determines ways to work

Key Corporate Governance Issues

1. **Improve Integrity of Proxy Voting Process.** Over 85,000 company meetings take place annually with thousands of shareholders vote on various issues. Counting votes is complex due to the volume of votes, manual processing and lack of transparency. SWIB is working to improve the proxy voting process so that investors can ensure each vote is counted.
2. **Unify Global Financial Reporting.** Globalization of world markets is driving the demand for uniform financial reporting standards. Analysts and portfolio managers must evaluate the performance and financial viability of foreign companies in a manner that is consistent with domestic companies. SWIB is participating on an international advisory group to address these issues.
3. **Improve Shareholder Rights.** SWIB participated in meetings in Washington and communicated with federal officials on behalf of shareholder rights. Progress was made in 2010 when financial reform became a reality. The Securities and Exchange Commission (SEC) will be allowed to develop rules relating to proxy access and requiring companies to allow shareholders to vote on compensation at least every three years.
4. **Strengthen Market Oversight and Regulation.** The full impact of the newly enacted reform legislation is yet to be determined. SWIB will continue to work for strong federal oversight to ensure investors' rights are better protected.

with company management, corporate boards and shareholders to make positive changes. Initially, we contact company management and company directors to resolve concerns. If companies are not responsive, SWIB may vote against proposals or choose to withhold its proxy votes from certain director candidates. We may also seek adoption of a shareholder resolution or decide to sell the stock.

Policies for voting corporate citizenship resolutions also reinforce investment goals to enhance returns. SWIB considers sustainability issues when initially investing in a company. Making investments or using proxy votes solely for promoting environmental, social or political causes or goals is contrary to our fiduciary duties. We believe acceptability of products and practices is an economic consideration that should be part of the investment decision.

Financial Section



STATE OF WISCONSIN

Legislative Audit Bureau

22 East Mifflin Street, Suite 500
Madison, Wisconsin 53703
(608) 266-2818
Fax (608) 267-0410
www.legis.wisconsin.gov/lab

Janice Mueller
State Auditor

INDEPENDENT AUDITOR'S REPORT

Senator Kathleen Vinehout and
Representative Peter Barca, Co-chairpersons
Joint Legislative Audit Committee

Members of the Board of Trustees and
Mr. Keith Bozarth, Executive Director
State of Wisconsin Investment Board

We have audited the accompanying Statement of Net Investment Assets for the Retirement Investment Trust Funds (Core Retirement Investment Trust Fund and Variable Retirement Investment Trust Fund) of the State of Wisconsin as of June 30, 2010, and the related Statement of Changes in Net Investment Assets for the year then ended. These financial statements are the responsibility of the State of Wisconsin Investment Board's management. Our responsibility is to express an opinion on these financial statements based on our audit.

The financial statements for the year ended June 30, 2009, are being presented for informational purposes only. These financial statements were audited by us and we expressed an unqualified opinion on them in our report dated November 24, 2009, but we have not performed any auditing procedures since that date.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

As discussed in Note 1, the financial statements referred to in the first paragraph present only the investment activity of the Retirement Investment Trust Funds attributable to the transactions of the Investment Board. The financial statements do not purport to, and do not, present the financial activity of the Retirement Investment Trust Funds attributable to the Department of Employee Trust Funds. Further, they do not purport to, and do not, present fairly the financial position and the changes in financial position of the Investment Board or of the State of Wisconsin in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to in the first paragraph present fairly, in all material respects, the respective net investment assets of each of the Retirement Investment Trust Funds as of June 30, 2010, and the respective changes in net investment assets for the year then ended in conformity with accounting principles generally accepted in the United States of America.

As discussed in Note 2 to the financial statements, for fiscal year 2009-10, the Investment Board implemented Governmental Accounting Standards Board Statement 53, *Accounting and Financial Reporting for Derivative Instruments*.

As also discussed in Note 2, 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, and, 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.

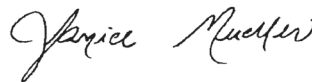
Our audit was conducted for the purpose of forming an opinion on the financial statements of the Retirement Investment Trust Funds. The supplementary information included as Management's Discussion and Analysis, which precedes the financial statements, is presented for purposes of additional analysis and is not a required part of the financial statements. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However, we did not audit the information and express no opinion on it. The introduction section of the annual report has not been subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on it.

In accordance with *Government Auditing Standards*, we have also issued a report dated November 29, 2010, on our consideration of the Investment Board's internal control over financial reporting for the Retirement Investment Trust 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, which is included in a management letter to the Investment Board, is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

LEGISLATIVE AUDIT BUREAU

November 29, 2010

by



Janice Mueller
State Auditor

Retirement Funds

Management Discussion and Analysis

The State of Wisconsin Retirement Funds' narrative discussion and analysis of the financial activities for the fiscal year ended June 30, 2010 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

Following this section are the financial statements and footnotes which reflect only the investment activity of the 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 Receipts (Disbursements)" in the Statement of Changes in Net Investment Assets.

The **Statement of Net Investment Assets** provides information on the financial position of the funds at year-end. It indicates the investment assets available for payment of future benefits and any current liabilities related to the investments.

The **Statement of Changes in Net Investment Assets** 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 assets on the Statement of Net Investment Assets.

The **Notes to the Financial Statements** offer additional discussion that is essential to the full understanding of the data presented in the financial statements. The notes give 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 Trust Funds

Approximately 566,000 people participate in the Wisconsin Retirement System (WRS), including current and former employees of Wisconsin's state agencies and most local governments in Wisconsin. Contributions made to the WRS by these employees and their employers are invested by the State of Wisconsin Investment Board to finance retirement and other benefits. The WRS is comprised of the Core Retirement Investment Trust Fund (Core Fund) and the Variable Retirement Investment Trust Fund (Variable Fund) collectively, whose combined net investment assets total \$69.1 billion as of June 30, 2010.

Core Retirement Investment Trust Fund

The larger of the two trust funds comprising the Wisconsin Retirement System is the Core Fund with \$64.6 billion of net assets. All WRS members have invested at least half — if not all — of their pension account in the Core Fund. It is a fully diversified, balanced fund invested for the long-term needs of the WRS. Diversification helps to stabilize the effects of market changes. The basic investment objective of this trust fund is to achieve an average 7.8% annual return over the long-term, which consists of an annual rate of return of 3.8% above an estimated 4.0% growth in wages. This objective is based on market rate of return and actuarial assumptions needed to meet obligations of the pension system.

The Core Fund Net Investment Income was approximately \$7.7 billion, due to total investment

Core Retirement Investment Trust Fund Condensed Financial Information

Fiscal Year Ended:	2010	2009	% Change
Cash and Cash Equivalents	\$ 2,327,289,323	\$ 2,328,412,776	0.0
Receivables	554,887,566	1,205,791,566	(54.0)
Invested Securities Lending Collateral	4,967,590,150	4,679,615,874	6.2
Other Assets	10,837,217	9,863,837	9.9
Investments	62,306,127,743	56,626,873,893	10.0
Total Investment Assets	<u>\$70,166,731,999</u>	<u>\$ 64,850,557,946</u>	8.2
Payables	\$ 562,641,134	\$ 937,270,303	(40.0)
Securities Lending Collateral Liability	4,967,590,150	4,679,615,874	6.2
Other Liabilities	18,256,397	19,188,983	(4.9)
Total Investment Liabilities	<u>\$ 5,548,487,681</u>	<u>\$ 5,636,075,160</u>	(1.6)
Net Investment Assets	<u><u>\$64,618,244,318</u></u>	<u><u>\$ 59,214,482,786</u></u>	9.1
Investment Income (Loss)	\$ 7,886,388,201	\$(13,321,373,780)	159.2
Investment Expense	(233,560,554)	(219,389,072)	6.5
Net Investment Income (Loss)	<u>\$ 7,652,827,647</u>	<u>\$(13,540,762,852)</u>	156.5
Net Disbursements	<u>(2,249,066,115)</u>	<u>(2,294,483,121)</u>	(2.0)
Net Increase (Decrease) in Net Investment Assets	<u><u>\$ 5,403,761,532</u></u>	<u><u>\$(15,835,245,973)</u></u>	134.1

returns of 13.3%. Core Fund asset class returns for fiscal year 2010 were: public equities 13.8%, fixed income 10.7%, real estate -10.1%, private equity 22.5% and multi-asset strategies 13.5%. Net Investment Assets were reduced by approximately \$2.2 billion, representing net disbursements made by the Department of Employee Trust Funds mainly for net benefit payments.

The statements presented here reflect the investment activity of these funds, as well as net cash flows related to the Department of Employee Trust Funds which include benefit payments, contribution receipts and transfers to/from the Variable Retirement Investment Trust Fund.

Receivables and Payables decreased significantly over the previous fiscal year due to a reduction in pending

investment sales and purchases. The 2009 balances were larger in magnitude as they reflected a transition of equity assets, a portion of which moved investments from external portfolios to internally managed index funds over the 2009 fiscal-year end.

The Invested Securities Lending Collateral and the Securities Lending Collateral Liability increased by 6.2% when compared to the previous year-end. These balances represent the cash collateral held for securities lending transactions in separately managed accounts. The increase in cash collateral was largely due to an increase in lendable assets caused by positive investment returns and a transition from collective trust fund investments to funds held in separate accounts.

Expenses increased by roughly 6.5% when

comparing fiscal year 2010 to 2009. The majority of the change can be attributed to external manager fees, which increased by \$10.4 million over the prior period. The Core Fund saw asset growth (due to positive performance) in more expensive externally managed areas, such as emerging market equities. Additionally, there were situations where passive portfolios were replaced with more expensive active strategies. On the other hand, performance based fees decreased by \$1.8 million when comparing fiscal year 2010 to 2009. This decrease can be attributed to the discontinuation of several externally managed portfolios. In an effort to capitalize on SWIB's cost-effective internal investment management, SWIB continues to reduce the share of the Core Fund's assets managed externally. At the end of fiscal year 2010, 43.2% of the Core Fund assets were managed internally, compared to 38.8% the prior year.

When compared to the prior fiscal year, fees incurred on private market assets increased by \$3.3 million. This asset type generally has higher fees at the beginning of the investment's life because management fees are based on committed assets, rather than assets under management. During the fiscal year, SWIB committed to funding an additional \$1.0 billion, contributing to the increase in fees.

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 20% of WRS members participate in the Fund, which totaled \$4.5 billion at the end of fiscal year 2010. Employees who choose this fund accept a higher degree of market risk for the potential of greater long-run returns. The investment objective of the Variable Fund is to exceed

similar equity-oriented portfolios over a full market cycle.

The Variable Fund Net Investment Income was \$606 million, due to investment returns of 14.6%. Equity portfolios returned 14.8% for the fiscal year ended June 30, 2010. The Variable Fund also contains a multi-asset component, which is comprised of cash equitized with equity futures contracts. This category was initiated for the sole purpose of meeting the liquidity needs of the Variable Fund, assuring minimal disruption to other investment strategies when the fund needs to raise cash to make benefit payments. The multi-asset strategy earned 14.0% for the Variable Fund for the year ended June 30, 2010.

Cash and Cash Equivalents balances increased by 141.4% over the prior fiscal year end. The majority of this increase can be attributed to securitized cash positions within the Variable Fund. In prior years, the Variable Fund met cash needs for benefit payments by selling out of externally managed stock index funds. SWIB management has implemented a more efficient internally managed strategy whereby the Variable Fund holds cash which is securitized with equity futures positions.

As was the case with the Core Fund, Receivables and Payables decreased significantly over the previous fiscal year due to a reduction in pending investment sales and purchases. The 2009 balances were larger in magnitude as they reflected a transition of equity assets, a portion of which moved investments from external portfolios to internally managed index funds over the 2009 fiscal-year end.

The Variable Fund's Invested Securities Lending Collateral and the Securities Lending Collateral Liability increased by 7.2% over the prior fiscal year end. This increase in collateral balance can be attributed to an

Variable Retirement Investment Trust Fund Condensed Financial Information

Fiscal Year Ended:	2010	2009	% Change
Cash and Cash Equivalents	\$ 275,077,418	\$ 113,933,844	141.4
Receivables	49,812,373	216,905,519	(77.0)
Invested Securities Lending Collateral	385,136,468	359,212,985	7.2
Investments	4,251,424,104	4,010,847,205	6.0
Total Investment Assets	\$4,961,450,363	\$ 4,700,899,553	5.5
Payables	\$ 44,445,623	\$ 216,054,590	(79.4)
Securities Lending Collateral Liability	385,136,468	359,212,985	7.2
Other Liabilities	193,541	-	N/A
Total Investment Liabilities	\$ 429,775,632	\$ 575,267,575	(25.3)
Net Investment Assets	<u>\$4,531,674,731</u>	<u>\$ 4,125,631,978</u>	9.8
Investment Income (Loss)	\$ 612,972,121	\$(1,548,312,489)	139.6
Investment Expense	(7,204,509)	(6,298,102)	14.4
Net Investment Income (Loss)	\$ 605,767,612	\$(1,554,610,591)	139.0
Net Disbursements	(199,724,859)	(280,783,565)	(28.9)
Net Increase (Decrease) in Net Investment Assets	<u>\$ 406,042,753</u>	<u>\$(1,835,394,156)</u>	122.1

increase in lendable assets caused by positive investment returns and a transition from collective trust fund investments to funds held in separate accounts.

Expenses for the Variable Fund increased by 14.4% when comparing fiscal year 2010 to the previous fiscal year. The primary cause of this increase was due to higher external manager fees. In general, the increase in fees can be attributed to asset growth due to positive investment returns. While fees paid to external managers increased in 2010, SWIB is focused on reducing the cost of investment management. To further this effort, SWIB continues to reduce the percentage of Variable Fund assets that are managed by more expensive outside firms. At the end of fiscal year 2010, 63.9% of Variable Fund assets were managed internally, compared to 54.2% the

prior year.

Positive investment returns were offset by net disbursements out of the fund. Net Disbursements include employee and employer contributions, annuity payments to retirees, expenses related to administering the benefit programs and transfers between the Core and Variable Funds due to active participants opting into or out of the Variable Fund. When comparing fiscal year 2009 to fiscal year 2010 net disbursements decreased 28.9%. The majority of this decrease is due to significantly lower annuity payments to retirees. Each year annuity payments are increased, decreased or left unchanged based on the prior calendar year investment results.

RETIREMENT FUNDS

Statements of Net Investment Assets

as of June 30, 2010

	<u>Core Retirement Investment Trust Fund</u>	<u>Variable Retirement Investment Trust Fund</u>
Assets		
Cash and Cash Equivalents	\$ 2,327,289,323	\$ 275,077,418
Due from Other Funds	193,541	40
Receivables:		
Interest & Dividends	203,178,915	6,673,155
Securities Lending Income	2,853,566	691,580
Investment Sales	348,661,544	42,447,598
Invested Securities Lending Collateral	4,967,590,150	385,136,468
Other Assets	10,837,217	-
Investments (at fair value):		
Stocks	33,605,683,588	4,257,481,703
Fixed Income	20,771,407,598	60
Limited Partnerships	6,446,075,085	-
Multi Asset	1,073,263,812	-
Real Estate	337,274,292	-
Preferred Securities	88,533,280	6,660,991
Convertible Securities	68,290,865	-
Commercial Mortgages	44,840,896	-
Foreign Currency Contracts	(1,132,901)	469,695
Option Contracts	(3,366,840)	(536,728)
Financial Futures Contracts	(124,741,932)	(12,651,617)
Total Investment Assets	\$ 70,166,731,999	\$ 4,961,450,363
Liabilities		
Payable for Investments Purchased	420,848,415	42,722,332
Obligations Under Reverse Repurchase Agreements	107,529,792	-
Accounts Payable	34,262,927	1,723,291
Due to Other Funds	18,256,397	193,541
Securities Lending Collateral Liability	4,967,590,150	385,136,468
Total Investment Liabilities	\$ 5,548,487,681	\$ 429,775,632
Net Investment Assets Held in Trust	<u>\$ 64,618,244,318</u>	<u>\$ 4,531,674,731</u>

The accompanying notes are an integral part of this statement.

RETIREMENT FUNDS
Statement Changes in Net Investment Assets
For the Fiscal Year Ended June 30, 2010

	<u>Core Retirement Investment Trust Fund</u>	<u>Variable Retirement Investment Trust Fund</u>
Additions:		
Investment Income:		
Net Increase (Decrease) in the Fair Value of Investments	\$ 6,613,943,688	\$ 538,073,075
Interest	569,984,117	443,736
Dividends	604,096,127	72,671,246
Securities Lending Commissions	20,130,065	1,634,801
Other Income	79,454,019	-
Less:		
Investment Expense	(233,560,554)	(7,204,509)
Securities Lending Rebates	357,781	304,342
Securities Lending Fees	(1,577,596)	(155,079)
	<hr/>	<hr/>
Total Investment Income (Loss)	\$ 7,652,827,647	\$ 605,767,612
 Deductions:		
Net Receipts (Disbursements) - Department of Employee Trust Funds	 (2,249,066,115)	 (199,724,859)
	<hr/>	<hr/>
 Net Increase (Decrease)	 \$ 5,403,761,532	 \$ 406,042,753
 Net Investment Assets Held in Trust:		
Beginning of Year	 59,214,482,786	 4,125,631,978
	<hr/>	<hr/>
End of Year	 \$ 64,618,244,318	 \$ 4,531,674,731
	<hr/>	<hr/>

The accompanying notes are an integral part of this statement.

RETIREMENT FUNDS
Statements of Net Investment Assets
Comparative Amounts as of June 30, 2009

	<u>Core Retirement Investment Trust Fund</u>	<u>Variable Retirement Investment Trust Fund</u>
Assets		
Cash and Cash Equivalents	\$ 2,328,412,776	\$ 113,933,844
Due from Other Funds	-	160
Receivables:		
Interest & Dividends	182,402,853	6,114,491
Securities Lending Income	5,535,742	547,535
Investment Sales	1,017,852,971	210,243,333
Invested Securities Lending Collateral	4,679,615,874	359,212,985
Other Assets	9,863,837	-
Investments (at fair value):		
Stocks	31,663,015,752	4,002,457,191
Fixed Income	17,758,300,013	69
Limited Partnerships	5,323,131,440	-
Multi Asset	1,293,141,586	-
Real Estate	390,887,893	-
Preferred Securities	117,819,371	7,950,599
Convertible Securities	27,453,980	-
Commercial Mortgages	51,523,759	-
Foreign Currency Contracts	28,544,995	1,398,785
Financial Futures Contracts	(26,944,896)	(959,439)
Total Investment Assets	\$ 64,850,557,946	\$ 4,700,899,553
Liabilities		
Payable for Investments Purchased	896,838,810	213,902,622
Accounts Payable	40,431,493	2,151,968
Due to Other Funds	19,188,983	-
Securities Lending Collateral Liability	4,679,615,874	359,212,985
Total Investment Liabilities	\$ 5,636,075,160	\$ 575,267,575
Net Investment Assets Held in Trust	<u>\$ 59,214,482,786</u>	<u>\$ 4,125,631,978</u>

The accompanying notes are an integral part of this statement.

RETIREMENT FUNDS

Statements of Changes in Net Investment Assets

Comparative Amounts For the Fiscal Year Ended June 30, 2009

	<u>Core Retirement Investment Trust Fund</u>	<u>Variable Retirement Investment Trust Fund</u>
Additions:		
Investment Income:		
Net Increase (Decrease) in the Fair Value of Investments	\$ (14,515,011,871)	\$ (1,619,955,880)
Interest	525,814,319	857,289
Dividends	550,097,281	67,630,160
Securities Lending Commissions	102,274,907	4,266,359
Other Income	69,511,061	-
Less:		
Investment Expense	(219,389,072)	(6,298,102)
Securities Lending Rebates	(49,970,948)	(837,668)
Securities Lending Fees	(4,088,529)	(272,749)
	<hr/>	<hr/>
Total Investment Income (Loss)	\$ (13,540,762,852)	\$ (1,554,610,591)
Deductions:		
Net Receipts (Disbursements) - Department of Employee Trust Funds	<hr/> (2,294,483,121) <hr/>	<hr/> (280,783,565) <hr/>
Net Increase (Decrease)	\$ (15,835,245,973)	\$ (1,835,394,156)
Net Investment Assets Held in Trust:		
Beginning of Year	<hr/> 75,049,728,759 <hr/>	<hr/> 5,961,026,134 <hr/>
End of Year	<hr/> <u>\$ 59,214,482,786</u> <hr/>	<hr/> <u>\$ 4,125,631,978</u> <hr/>

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) has control of the investment and collection of principal, interest, and dividends of all monies invested by the Core Retirement Investment Trust Fund (Core Fund) and the Variable Retirement Investment Trust Fund (Variable Fund). The Core Fund and Variable Fund collectively represent the Retirement Funds (Retirement Funds). 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 the "Investment Expense" account included in the Statement of Changes in Net Investment Assets. This account 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. 25.14 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 highly diversified portfolio of securities. SWIB is required to make investment management decisions for the

trust funds solely for the benefit of the members of the Wisconsin Retirement System (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 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 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 retirement fund contributions are invested in this trust fund unless participants have elected to have half of their contributions invested in the Variable Fund. In addition to the retirement contributions, the assets of various other benefit programs are invested as part of 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, 2010 (Dollars in Millions)

Program	
Accumulated Sick Leave	\$1,793.1
Duty Disability	334.5
Long Term Disability Insurance	218.9
Active Employee Health Insurance	206.6
Milwaukee Retirement System	100.5
Income Continuation Insurance	78.6
Police and Firefighters Pension Group	35.3
State Retiree Health Insurance	17.8
Total	<u>\$2,785.3</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. 25.14 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).

The Variable Fund also consists primarily of the assets invested for the WRS. In addition, the Milwaukee Retirement Systems had \$15.6 million invested in the Variable Fund as of June 30, 2010.

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 program 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. 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.

SWIB applies all applicable GASB pronouncements and those Financial Accounting Standards Board (FASB) pronouncements issued on or before November 30, 1989 which do not conflict with or contradict GASB pronouncements.

C. Valuation of Securities

The investments of the Core Fund and the Variable Fund are valued at fair value, per Wisconsin Statutes s. 25.17(14). Monthly, the investments are

adjusted to fair value, with unrealized gains and losses reflected in the Statement of Changes in Net Investment Assets as “Net Increase (Decrease) in the Fair Value of Investments”.

Generally, fair value information represents actual bid prices or the quoted yield equivalent for securities of comparable maturity, quality and type as obtained from one or more major investment brokers. If quoted market prices are not available, a variety of third party pricing methods are used, including appraisals, certifications, pricing models and other methods deemed acceptable by industry standards.

Commercial mortgages are priced via a matrix pricing system. The traditional discounted cash flow methodology is employed, where discount rates are developed based on market derived spreads over a base Treasury or London inter-bank offering rate yield. Spreads incorporate such factors as coupon rates, term to maturity, agency ratings, and sector/industry information.

Private placements are 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
2. Prices provided by a contracted third party with expertise in the bond market
3. Modeled prices utilizing CMS BondEdge where spreads are supplied by a contracted third party

In a few instances private placements 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.

Limited partnerships’ fair value is estimated based on periodic reports from the limited partnerships’ management. Annually, the reports are audited by independent auditors.

Real estate valuations are based on generally accepted industry standards and are most typically based on discounted cash flow and comparable sales methodologies. The basis for valuing direct real estate holdings is independent appraisals, which are prepared once every three years. In years when appraisals are not performed, the asset managers are responsible for providing market valuations. Annually, direct real estate holdings, including valuation assumptions, are audited by independent auditors.

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.

Derivative financial instruments are reported at fair value in the Statement of Net Investment Assets. The instruments are marked to fair value at least monthly, with valuation changes recognized in income. Gains and losses are recorded in the Statement of Changes in Net Investment Assets as “Net Increase (Decrease) in Fair Value of Investments” 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.

Notes to the Financial Statements

D. 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.

E. Reclassification of Comparative Information

The financial statements include prior year information provided for comparative purposes. Accordingly, this prior year comparative information should be read in conjunction with the Retirement Funds' financial statements for the year ended June 30, 2009. Certain reclassifications have been made to the comparative amounts as of and for the year ended June 30, 2009 to conform to the presentation as of June 30, 2010.

F. Recently Adopted Accounting Pronouncements

GASB Statement No. 53, *Accounting and Financial Reporting for Derivative Instruments*, was implemented for the fiscal year ended June 30, 2010. This Statement enhances the usefulness and comparability of derivative information reported in the financial statements. There was no significant impact on the Retirement Funds' financial statements with the implementation of this GASB Statement.

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 spell out 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 several nationally recognized statistical rating organizations on debt securities held by the Core Fund and the Variable Fund as of June 30, 2010. Included in this table are fixed income securities including certain short term securities classified as cash equivalents on the Statement of Net Investment Assets. Also included are investments

**Credit Quality Distribution
June 30, 2010**

Ratings	Fair Value	% of Total
P-1 or A-1	\$ 2,469,500,175	9
Aaa or AAA	6,436,717,305	23
Aa3 to Aa1 or AA- to AA+	2,364,612,821	8
A3 to A1 or A- to A+	2,467,772,084	9
Baa3 to Baa1 or BBB- to BBB+	1,507,536,639	5
Ba3 to Ba1 or BB- to BB+	449,225,622	2
B3 to B1 or B- to B+	529,598,104	2
Caa1 to Caa3 or CCC- to CCC+	193,695,116	1
Ca1 to Ca3 or CC- to CC+	21,573,499	0
C	7,758,679	0
D	16,013	0
Collective Trust Funds	10,232,939,279	36
Not Rated	1,367,353,920	5
Total	<u>\$ 28,048,299,256</u>	<u>100%</u>

held in the Retirement Funds securities lending collateral reinvestment pools, which are managed by SWIB's securities custodian. See Note 4 for additional information regarding the securities lending program.

Obligations of the United States and obligations explicitly guaranteed by the U.S. government have been included in the AAA rating although they are considered to be without credit risk. The table also includes investments in externally managed collective trust funds which have not been rated by an independent rating agency. Although the funds themselves do not carry 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.

Reverse Repurchase Agreements — SWIB had \$107.5 million reverse repurchase agreements outstanding at June 30, 2010. Investment guidelines permit certain portfolios to enter into reverse repurchase agreements, that is, a sale of securities with a simultaneous agreement to repurchase the exact 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 dealers default on their obligations to resell these securities or provide cash of equal value, SWIB would suffer an economic loss equal to the difference between the market value plus accrued interest of the underlying securities and the agreement obligation, including accrued interest. This credit exposure at year-end was \$3.1 million.

Since the proceeds from reverse repurchase

agreements are used for short term financings, the maturities of the purchases made with the proceeds of reverse repurchase agreements are not matched to the maturities of the agreements. The repurchase agreement transactions as of June 30, 2010, had underlying collateral with fair values of approximately 103% of the cost of the repurchase agreements. The agreed-upon yields were between 0.24% and 0.28% with maturity dates through August 5, 2010.

The liabilities resulting from reverse repurchase agreements are reported as "Obligations Under Reverse Repurchase Agreements" and the underlying assets used as collateral are reported in the "Investments" section on the Statement of Net Investment Assets. Any interest cost associated with the reverse repurchase agreements is reported as "Investment Expense" on the Statement of Changes in Net Investment Assets.

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, 2010 were \$413.5 million. A portion of the deposits, totaling \$2.9 million, are covered by federal depository insurance. The remaining uninsured and uncollateralized deposits, totaling \$410.6 million, were held in foreign currencies or margin accounts in SWIB's custodian's nominee name. In addition, SWIB held time deposits with foreign financial institutions with a fair value of \$330.7 million,

Interest Rate Sensitivity by Investment Type
June 30, 2010

Investment Type	Fair Value*	Modified Duration (years)
Asset Backed Securities	\$ 50,963,688	3.30
Asset Backed Securities	11,627,535	N/A
Certificates of Deposit	4,500,000	0.08
Commercial Paper	76,879,714	0.18
Corporate Bonds & Private Placements	4,920,564,128	4.90
Corporate Bonds & Private Placements	30,632,034	N/A
Futures Contracts	(544,753,936)	6.73
Futures Contracts	2,524,237	N/A
Government Agency	485,624,446	2.88
Commercial Mortgages	44,840,896	2.24
Municipal Bonds	47,306,824	13.02
Repurchase Agreements	49,667,797	0.00
Sovereign Debt	3,053,659,832	7.09
United States Treasury Securities	4,060,544,437	7.33
	<u>\$ 12,294,581,632</u>	
Intermediate and Long Term Collective Trust Funds		
Emerging Market Fixed Income	\$ 257,452,152	8.03
Global Fixed Income	526,726,362	5.79
Domestic Fixed Income	7,528,645,394	5.34
	<u>\$ 8,312,823,908</u>	
		Weighted Average Maturity (days)
Short Term Collective Trust Funds	<u>\$ 1,920,115,371</u>	<u>77</u>
Securities Lending Collateral Pool		
Asset Backed Securities	\$ 164,664,938	36
Certificates of Deposit	1,070,608,340	40
Commercial Paper	1,352,363,324	34
Corporate Bonds	1,653,604,462	35
Repurchase Agreements	737,307,583	1
	<u>\$ 4,978,548,647</u>	
Total Fair Value	<u><u>\$ 27,506,069,558</u></u>	

N/A = data not available

* Notional amount presented for futures contracts

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, 2010 the Retirement Funds held 18 tri-party repurchase agreements totaling \$787.0 million. These repurchase agreements were held in SWIB's cash management and securities lending cash collateral reinvestment portfolios, which are both managed by SWIB's custodian. The repurchase agreement's underlying securities were held by the counterparty'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 assets.

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 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 interest rate exposure for the Core and Variable Fund assets. Weighted average maturity, where reset dates are assumed to be the effective maturity date for the security, is presented for the securities lending collateral reinvestment pool 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.

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. The Retirement Funds hold foreign currency denominated cash and securities invested directly in designated actively managed portfolios and indirectly through their investment in certain collective trust funds.

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.

As of June 30, 2010 the Core Fund and the Variable Fund assets were denominated in the currencies shown in the table entitled **Currency Exposures by Investment Type**.

4. Securities Lending Transactions

State statutes and Board policies permit SWIB to use investments of the Core and Variable 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 securities 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 percent 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 foreign securities are loaned against collateral denominated in a different currency, the borrower is required to place collateral totaling 105 percent 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.

Cash collateral is reinvested by the lending agent in accordance with contractual investment guidelines which are designed to minimize the risk of principal loss and obtain a moderate rate of return. The investment guidelines include very high credit quality

standards and also require a portion of the collateral investments to be invested in short-term securities. The earnings generated from the collateral investments, less the amount of rebates paid to the dealers and fees paid to agents, results in the gross earnings from lending activities, which are then split on a percentage basis with the lending agent.

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 pool's 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. During fiscal year 2010, the securities lending reinvestment pools' NAVs were below the typical money market fund market floor value of \$.9950. The NAVs improved by the end of the fiscal year. As of June 30, 2010, the U.S. dollar cash collateral reinvestment pool's NAV was \$.9960 while the foreign reinvestment pool had an NAV of \$.9982.

At fiscal year-end, the Retirement Funds had no credit risk exposure to borrowers because the amounts the Retirement Funds owed the borrowers exceeded the amounts the borrowers owed the Retirement Funds. 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 margin 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 can be terminated

on demand by the Retirement Funds or the borrower. The average term of the loans is approximately three days which is shorter than the weighted average maturity/days to reset of 28 days for investments made with the U.S. dollar cash collateral and the weighted average maturity/days to reset of 20 days for investments made with foreign cash collateral at June 30, 2010.

When non-cash collateral is posted by the borrower, pledging or selling these collateral securities cannot be done unless a borrower defaults. The quantity or dollar value of securities lending contracts that the Retirement Funds may enter into is not restricted by statute.

The Retirement Funds also earn securities lending income as part of total net earnings from the investment in several collective trust funds. These earnings are automatically reinvested in the collective trust fund, and as a result the earnings are combined with all other earnings and gains and losses for these funds, and reported in the Statement of Changes in Net Investment Assets as "Net Increase (Decrease) in the Fair Value of Investments".

5. Derivative Financial Instruments

Derivatives may be used to implement investment strategies for the Core and Variable 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

Currency Exposures by Investment Type June 30, 2010

Currency	Cash & Cash Equivalents	Commercial Mortgages	Convertible Securities	Stocks	Options	Fixed Income
Australian Dollar	\$ 943,201	\$ -	\$ -	\$ 434,291,258	\$ -	\$ 36,149,685
Brazil Real	2,352,240	-	-	34,155,644	-	29,182,037
British Pound Sterling	2,705,665	-	-	1,860,468,034	-	200,539,967
Canadian Dollar	3,639,951	-	-	600,844,688	-	89,270,701
Colombian Peso	-	-	-	-	-	8,827,134
Czech Koruna	1,469	-	-	12,108,503	-	-
Danish Krone	423,476	-	-	72,640,143	-	25,615,824
Euro Currency Unit	63,749,605	-	-	2,526,848,011	-	1,075,639,818
Hong Kong Dollar	1,210,450	-	-	371,255,013	-	-
Hungarian Forint	398,277	-	-	1,269,959	-	4,772,105
Indian Rupee	725,272	-	-	163,898,933	-	-
Indonesian Rupiah	12,594	-	-	14,252,396	-	21,395,111
Israeli Shekel	369,297	-	-	5,432,831	-	-
Japanese Yen	19,247,781	-	-	1,764,638,327	-	1,012,719,293
Malaysian Ringgit	670,075	-	-	54,958,565	-	45,694,993
Mexican New Peso	709,846	-	-	43,059,630	-	31,023,414
Moroccan Dirham	5,152	-	-	1,793,019	-	-
New Taiwan Dollar	1,889,573	-	-	178,727,647	-	-
New Turkish Lira	285,956	-	-	47,118,644	-	-
New Zealand Dollar	8,599	-	-	708,646	-	9,719,193
Norwegian Krone	246,196	-	-	34,390,916	-	15,932,601
Peruvian Nuevo Sol	-	-	-	32,452	-	5,177,770
Philippines Peso	296,273	-	-	3,720,385	-	-
Polish Zloty	507,946	-	-	24,678,842	-	30,753,952
Russian Rubel	-	-	-	-	-	966,447
S. African Comm Rand	1,192,358	-	-	36,484,278	-	10,972,635
Singapore Dollar	385,519	-	-	111,095,478	-	-
South Korean Won	288,964	-	-	208,918,570	-	8,843,063
Swedish Krona	369,175	-	-	87,691,448	-	30,612,309
Swiss Franc	536,728	-	-	496,962,625	-	-
Thailand Baht	118,345	-	-	67,459,319	-	-
United States Dollar	2,499,076,758	44,840,896	68,290,865	28,603,261,087	(3,903,568)	18,069,276,036
Uruguayan Peso	-	-	-	-	-	8,323,570
Total	\$2,602,366,741	\$ 44,840,896	\$ 68,290,865	\$37,863,165,291	\$(3,903,568)	\$ 20,771,407,658

Currency Exposures by Investment Type

June 30, 2010

Currency	Financial Futures Contracts	Multi-Asset	Preferred Securities	Limited Partnerships	Real Estate	Total
Australian Dollar	\$ (8,757,774)	\$ -	\$ -	\$ -	\$ -	\$ 462,626,370
Brazil Real	-	-	65,383,107	-	-	131,073,028
British Pound Sterling	(20,688,658)	-	-	86,692,127	-	2,129,717,135
Canadian Dollar	(5,272,938)	-	-	32,936,845	-	721,419,247
Colombian Peso	-	-	-	-	-	8,827,134
Czech Koruna	-	-	-	-	-	12,109,972
Danish Krone	-	-	-	-	-	98,679,443
Euro Currency Unit	(19,302,874)	-	9,296,200	604,216,700	-	4,260,447,460
Hong Kong Dollar	-	-	-	-	-	372,465,463
Hungarian Forint	-	-	-	-	-	6,440,341
Indian Rupee	-	-	-	-	-	164,624,205
Indonesian Rupiah	-	-	-	-	-	35,660,101
Israeli Shekel	-	-	-	-	-	5,802,128
Japanese Yen	(8,168,414)	-	-	-	-	2,788,436,987
Malaysian Ringgit	-	-	-	-	-	101,323,633
Mexican New Peso	-	-	-	-	-	74,792,890
Moroccan Dirham	-	-	-	-	-	1,798,171
New Taiwan Dollar	-	-	-	-	-	180,617,220
New Turkish Lira	-	-	-	-	-	47,404,600
New Zealand Dollar	-	-	-	-	-	10,436,438
Norwegian Krone	-	-	-	-	-	50,569,713
Peruvian Nuevo Sol	-	-	-	-	-	5,210,222
Philippines Peso	-	-	-	-	-	4,016,658
Polish Zloty	-	-	-	-	-	55,940,740
Russian Rubel	-	-	-	-	-	966,447
S. African Comm Rand	-	-	-	-	-	48,649,271
Singapore Dollar	-	-	-	-	-	111,480,997
South Korean Won	-	-	5,198,594	-	-	223,249,191
Swedish Krona	-	-	-	4,048,061	-	122,720,993
Swiss Franc	-	-	-	-	-	497,499,353
Thailand Baht	-	-	-	-	-	67,577,664
United States Dollar	(75,202,891)	1,073,263,812	15,316,370	5,718,181,352	337,274,292	56,349,675,009
Uruguayan Peso	-	-	-	-	-	8,323,570
Total	\$ (137,393,549)	\$ 1,073,263,812	\$ 95,194,271	\$ 6,446,075,085	\$ 337,274,292	\$ 69,160,581,794

the Board. Where derivatives are permitted, guidelines stipulate allowable instruments and the manner in which they are to be used.

Investment guidelines have been established which provide minimum credit ratings for counterparties. Additionally, policies have been established which, where possible, seek to provide master netting arrangements with counterparties to over-the-counter derivative transactions.

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

The following are the types of derivatives that SWIB uses in its dedicated account portfolios. SWIB also invests in derivative instruments indirectly through several collective trust funds. These derivatives have not been included in the following narrative.

A. Foreign Currency Spot and Forward Contracts

Currency exposure management is permitted through the use of exchange traded currency instruments, and through the use of over-the-counter spot and forward contracts in foreign currencies. 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.

No cash is exchanged when a foreign exchange

spot or forward contract is initiated. Collateral postings are not required for foreign currency spot or forward contract counterparties. Net amounts due are paid or received on the contracted settle date. The net receivable or payable for spot and forward contracts is reflected as Foreign Currency Contracts on the Statement of Net Investment Assets. 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. Spot and forward contracts are valued daily with the changes in fair value included in the Net Increase (or Decrease) in Fair Value of Investments on the Statement of Changes in Net Investment Assets.

SWIB may employ discretionary currency overlay strategies at the total fund level when currency market conditions suggest such strategies are warranted. Only the currencies of developed market countries in the MSCI ex US Index may be used to implement the currency overlay. Exchange-traded currency instruments and over-the-counter spot and forward contracts in foreign currencies are used to execute these strategies.

During the fiscal year presented in these financial statements some of SWIB's currency exposure management involved the use of foreign currency spot and forward contracts. 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 Core and Variable Funds as of June 30, 2010.

SWIB's foreign exchange spot and forward positions are over-the-counter contracts, entered into with various counterparties. Guidelines have been established which provide minimum credit ratings for counterparties. Additionally, policies have been established which, where possible, seek to implement

Foreign Currency Spot and Forward Contracts
June 30, 2010

Currency	Notional (local currency)	Fair Value of Foreign Currency Contracts Receivable (\$US)
Foreign Exchange Contracts Sold		
AUSTRALIAN DOLLAR	347,147,753	\$ (6,110,910)
BRAZIL REAL	2,175,706	(7,416)
BRITISH POUND STERLING	308,214,922	1,734,662
CANADIAN DOLLAR	313,183,231	(8,834,938)
DANISH KRONE	85,407,956	(113,430)
EURO CURRENCY UNIT	408,745,654	(7,766,332)
HONG KONG DOLLAR	159,243,219	(5,475,878)
HUNGARIAN FORINT	155,492,000	(5,506)
INDONESIAN RUPIAN	6,779,681,115	586
ISRAELI SHEKEL	9,700,000	85
JAPANESE YEN	49,409,130,784	15,812,942
MALAYSIAN RINGGIT	26,215,059	95,414
MEXICAN NEW PESO	26,889,000	(51,643)
NEW ZEALAND DOLLAR	77,476,000	193,565
NORWEGIAN KRONE	448,967,318	364,849
PHILIPPINES PESO	156,312,000	25,091
POLISH ZLOTY	7,472,000	(35,025)
SINGAPORE DOLLAR	14,171,552	(64,884)
SWEDISH KRONA	808,572,311	(1,053,478)
SWISS FRANC	105,386,176	2,832,639
THAILAND BAHT	24,845,897	(2,223)
		\$ (8,461,830)
Fair Value of Foreign Currency Contracts Payable*		
Foreign Exchange Contracts Purchased	Notional (local currency)	(\$US)
AUSTRALIAN DOLLAR	(67,196,659)	\$ 2,508,590
BRAZIL REAL	(20,988,000)	(270,280)
BRITISH POUND STERLING	(81,231,284)	(318,081)
CANADIAN DOLLAR	(53,249,512)	1,478,018
COLOMBIAN PESO	(4,876,470,798)	18,034
DANISH KRONE	(137,000)	168
EURO CURRENCY UNIT	(562,139,499)	9,999,211
HONG KONG DOLLAR	(163,005,690)	(280,708)
HUNGARIAN FORINT	(736,526,000)	196,595
INDIAN RUPEE	(20,773,617)	(3,303)
INDONESIAN RUPIAN	(12,675,113,000)	(27,939)
ISRAELI SHEKEL	(9,131,143)	(57)
JAPANESE YEN	(42,010,894,167)	(5,462,019)
MALAYSIAN RINGGIT	(2,372,255)	(2,908)
MEXICAN NEW PESO	(32,480,419)	44,158
NEW TAIWAN DOLLAR	(60,491,490)	(7,885)
NEW TURKISH LIRA	(2,079,000)	92
PERUVIAN NUEVO SOL	(23,394,000)	(70,511)
S AFRICAN COMM RAND	(79,487,593)	158,679
SINGAPORE DOLLAR	(6,978,823)	30,591
SOUTH KOREAN WON	(75,568,602)	(939)
SWEDISH KRONA	(71,825,522)	131,919
SWISS FRANC	(17,733,883)	(322,113)
THAILAND BAHT	(7,705,093)	(688)
		\$ 7,798,624
Net Foreign Exchange Currency Spot and Forward Contracts		\$ (663,206)

* Net effect of cross currency contracts is reflected in the "Foreign Exchange Contracts Purchased" section.

Exposures by Counterparty June 30, 2010

Foreign Currency Spot and Forward Contracts

Counterparty	Payable	Receivable	Net	Counterparty Credit Rating
Bank of America Corp	\$ (497,099,955)	\$ 484,878,116	\$(12,221,839)	A
Bank of New York Mellon Corp/The	(546,348,211)	548,860,271	2,512,060	AA-
Barclays Bank PLC	(689,822)	688,560	(1,262)	AA-
BlackRock Inc	(22,148,531)	22,561,942	413,411	A+
BNP Paribas	(9,460,256)	9,519,822	59,566	AA
Brown Brothers Harriman & Co	(420,104)	419,571	(533)	A+
Citigroup Inc	(81,066,231)	80,687,403	(378,828)	A
Credit Suisse Group AG	(298,726)	295,605	(3,121)	A
Deutsche Bank AG	(28,526,094)	28,178,389	(347,705)	A+
Goldman Sachs Group Inc/The	(15,171,844)	15,129,007	(42,837)	AA-
HSBC Holdings PLC	(60,479,201)	62,153,868	1,674,667	A+
JPMorgan Chase & Co	(459,150,640)	464,582,332	5,431,692	A
Morgan Stanley	(12,676,200)	12,838,690	162,490	AA-
Royal Bank of Canada	(729,303,507)	720,193,071	(9,110,436)	A
Standard Chartered PLC	(1,882,300)	1,925,162	42,862	A+
State Street Corp	(134,765,785)	134,696,367	(69,418)	A+
Toronto Dominion Bank	(5,506,984)	5,366,904	(140,080)	AA-
UBS AG	(1,189,393,496)	1,202,499,338	13,105,842	A+
United Kingdom of Great Britain and Northern Ireland	(21,961,471)	22,342,895	381,424	AAA
Westpac Banking Corp	(179,372,888)	177,241,727	(2,131,161)	AA
Total	\$(3,995,722,246)	\$3,995,059,040	\$ (663,206)	

master netting arrangements with counterparties to over-the-counter derivative transactions. The table entitled **Exposures by Counterparty**, details the counterparties with whom SWIB has entered into foreign exchange spot and forward contracts as of June 30, 2010.

B. Futures Contracts

A financial futures contract is an exchange traded agreement to buy or sell a financial instrument at an agreed upon price and time in the future. Upon entering into a futures contract, collateral is deposited with the broker, in SWIB's name, in accordance with

initial margin requirements. 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. The resulting gain/loss is typically received/paid the following day until the contract expires.

The fair value of futures contracts represents the unrealized gain/loss on the contract and is reflected as Financial Futures Contracts on the Statement of Net Investment Assets. Gains and losses as a result of 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 Assets.

Futures contracts involve, to varying degrees,

Futures Contracts
June 30, 2010

Description	Expiration Date	Notional Amount	Unrealized Appreciation (Depreciation)*
INTEREST RATE FUTURES			
3MO EUROYEN TIFF FUTURE (TFX)	12/13/2010 - 9/16/2011	\$ 1,970,717	\$ 283
90DAY STERLING LIBOR FUT (LIF)	12/15/2010 - 9/21/2011	3,329,253	3,422
FIXED INCOME FUTURES			
AUSTRALIAN 10YR BOND FUT (SFE)	9/15/2010	34,595,735	809,872
AUSTRALIAN 3YR BOND FUT (SFE)	9/15/2010	1,141,914	-
CANADA 10YR BOND FUTURE (MSE)	9/21/2010	26,685,240	577,199
EURO BUXL 30 YR BOND FUT (EUX)	9/8/2010	274,623	441
EURO-BOBL FUTURE (EUX)	9/8/2010	6,516,517	9,040
EURO-BUND FUTURE (EUX)	9/8/2010	7,132,042	1,654
EURO-SCHATZ FUTURE (EUX)	9/8/2010	12,208,860	7,135
JAPAN 10YR MINI BD FUTURE(SGX)	9/8/2010	17,284,394	163,770
UK LONG GILT FUTURE (LIF)	9/28/2010	(43,283,594)	(574,891)
US TREAS BD FUTURE (CBT)	9/21/2010	3,315,000	76,937
US ULTRA BOND (CBT)	9/21/2010	4,346,000	137,656
US 10YR NOTE FUTURE (CBT)	9/21/2010	(553,421,687)	(9,838,328)
US 2YR TREAS NTS FUT (CBT)	9/30/2010	128,233,282	396,344
US 5YR TREAS NTS FUT(CBT)	9/30/2010	(192,557,993)	(2,633,377)
EQUITY FUTURES			
DJ EURO STOXX 50 FUTURE (EUX)	9/17/2010	383,158,617	(19,321,144)
DOW JONES MINI FUTURE (CBT)	9/17/2010	825,860	(36,210)
FTSE 100 INDEX FUTURE (LIF)	9/17/2010	310,468,966	(20,117,189)
MSCI EAFE EMINI INDEX FUT (CME)	9/17/2010	2,367,360	(155,990)
RUSSELL 2000 MINI IND FUT(NYF)	9/17/2010	318,426,420	(23,901,905)
S&P 500 EMINI INDEX FUT (CME)	9/17/2010	538,451,700	(36,923,498)
S & P MID 400 EMINI (CME)	9/17/2010	46,576,000	(2,324,520)
S&P/TSE 60 INDEX FUTURES (MSE)	9/16/2010	164,264,960	(5,850,137)
SPI 200 INDEX FUTURE (SFE)	9/16/2010	158,485,523	(9,567,646)
TOPIX INDEX FUTURE (TSE)	9/9/2010	304,073,513	(8,332,467)
Total		\$ 1,684,869,222	\$ (137,393,549)

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

risk of loss in excess of the variation margin disclosed in the Statement of Net Investment Assets. Losses may arise from future changes in the value of the underlying instrument.

Financial futures contracts may be entered into for the following objectives: facilitate asset class rebalancing, protect portfolios against the risk of changing asset values or interest rates, enhance liquidity, aid in cash flow management, manage interest rate

exposure, adjust duration, equitize cash and receivable positions or as a substitute for cash market transactions. Futures contracts are secured by collateral deposited with brokers which can be in the form of cash, U.S. Treasuries and equity securities.

The table entitled **Futures Contracts** presents the Retirement Funds investments in futures contracts as of June 30, 2010.

Notes to the Financial Statements

C. Options

Option contracts give the purchaser of the contract the right 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 options. Options may be used to improve the efficiency or to enhance the expected return of the Core and Variable Funds' strategic rebalancing procedures. Exchange traded options may be purchased or sold in conjunction with managing asset class exposure if the

exercise of the options will move the asset allocation closer to the target established by the Board. The aggregate notional value of the options is limited to 2% of the market value of the trust fund at the date of purchase. The term of options used for this purpose may not exceed one year.

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 Assets. 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 Assets. The table entitled **Option Contracts** presents the fair value of option contracts held by the Core and Variable Funds as of June 30, 2010.

Option Contracts
June 30, 2010

Security Description	Contract Type	Maturity	Number of Contracts	Cost/(Proceeds)	Market Value	Unrealized Gain (Loss)
AMERICAN INTL GROUP INC COM	CALL	JUL 10	1,000	\$ 187,000	\$ 25,000	\$ (162,000)
FIDELITY NATL INFORMATION SVCS	CALL	AUG 10	2,770	10,969	2,770	(8,199)
FIDELITY NATL INFORMATION SVCS	CALL	JUL 10	1,550	7,750	7,750	-
AIRGAS INC	PUT	AUG 10	(212)	(11,720)	(11,660)	60
AIRGAS INC	PUT	JUL 10	(744)	(60,775)	(11,160)	49,615
AMERICAN INTL GROUP INC COM	PUT	JUL 10	(1,000)	(706,000)	(555,000)	151,000
FIDELITY NATL INFORMATION SVCS	PUT	AUG 10	(2,770)	(2,310,762)	(2,354,500)	(43,738)
FIDELITY NATL INFORMATION SVCS	PUT	JUL 10	(736)	(557,152)	(592,480)	(35,328)
MILLIPORE CORP COM	PUT	JUL 10	(600)	(30,000)	(3,000)	27,000
RUSSELL 1000 INDEX	PUT	JUL 10	(120)	(24,600)	(24,000)	600
S&P 500 EOM OPTION SEP 10	PUT	JUL 10	(186)	(283,650)	(372,000)	(88,350)
SYBASE INC	PUT	JUL 10	(275)	(9,625)	(3,438)	6,187
SYBASE INC	PUT	SEP 10	(340)	(25,670)	(11,850)	13,820
Total				<u>\$ (3,814,235)</u>	<u>\$ (3,903,568)</u>	<u>\$ (89,333)</u>

6. Summary of Investments

The tables entitled **Core Retirement Investment Trust Fund** and **Variable Retirement Investment Trust Fund** provides summary information by investment classification for the Core Fund and Variable Fund at June 30, 2010.

7. Milwaukee Retirement System

The Milwaukee Retirement System (MRS), consisting of several funds within the Milwaukee Public School Retirement System, invests in the Core Fund and Variable Fund through the WRS. Since the MRS is a separate legal entity from the WRS, both the Core Fund

Core Retirement Investment Trust Fund
June 30, 2010

<u>Classification</u>	<u>Coupon Rate (%)</u>	<u>Maturity Dates</u>	<u>Cost</u>	<u>Fair Value</u>
Stocks	N/A	N/A	\$33,504,732,449	\$33,605,683,588
Fixed Income	Variable & 0.00 - 21.00	7/2010 - 4/2057	18,525,202,183	20,771,407,598
Limited Partnerships	N/A	N/A	7,802,269,700	6,446,075,085
Multi Asset	N/A	N/A	804,550,985	1,073,263,812
Real Estate	N/A	N/A	284,471,968	337,274,292
Preferred Securities	N/A	N/A	79,382,442	88,533,280
Convertible Securities	Variable & 0.25 - 8.00	10/2011 - 12/2049	62,510,573	68,290,865
Commercial Mortgages	7.13 - 7.36	7/2011 - 12/2014	41,470,591	44,840,896
Foreign Currency Contracts	N/A	7/2010 - 9/2010	-	(1,132,901)
Option Contracts	N/A	7/2010 - 9/2010	(3,277,795)	(3,366,840)
Financial Futures Contracts	N/A	9/2010 - 9/2011	-	(124,741,932)
			<u>\$61,101,313,096</u>	<u>\$62,306,127,743</u>

Variable Retirement Investment Trust Fund
June 30, 2010

<u>Classification</u>	<u>Coupon Rate (%)</u>	<u>Maturity Dates</u>	<u>Cost</u>	<u>Fair Value</u>
Stocks	N/A	N/A	\$ 4,282,706,317	\$ 4,257,481,703
Fixed Income*	Variable	N/A	692,877	60
Preferred Securities	N/A	N/A	6,356,361	6,660,991
Foreign Currency Contracts	N/A	7/2010 - 9/2010	-	469,695
Option Contracts	N/A	7/2010 - 9/2010	(536,440)	(536,728)
Financial Futures Contracts	N/A	9/2010	-	(12,651,617)
			<u>\$ 4,289,219,115</u>	<u>\$ 4,251,424,104</u>

* The Variable fund held one defaulted fixed income investment related to securities lending cash collateral as of 6/30/10

and the Variable Fund qualify as external investment trust funds. Participation by the MRS in the Core Fund and Variable Fund is described in the ETF Administrative Code, Chapter 10.12. MRS provides assets to ETF for investment in the Core Fund and Variable Fund which are managed by SWIB. Each month the ETF distributes to the MRS their pro-rata share of the total Core Fund's earnings less administrative expenses, as well as the Variable Fund's earnings less administrative expenses. The MRS accounts are adjusted to fair value and gains/losses are recorded directly in the accounts per ETF Administrative Code 10.12(2). No State statute, legal provision, or legally binding guarantee exists to support the value of MRS's portion of the Core Fund or the Variable Fund.

8. 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 totaled \$5.2 billion as of June 30, 2010. Unfunded commitments are not included in the financial statements since the amount and timing of the funding is not certain.

9. 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. 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 liability, as a putative transferee of SCC assets, would be limited to \$28.3 million of SCC's tax deficiency, plus interest.

SWIB is aggressively contesting the IRS' assertions of SWIB's tax liability. Furthermore, SWIB believes that the loss, if any, resulting from the claim will not have a material impact on SWIB's net investment assets or net 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 Assets.



STATE OF WISCONSIN

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Janice Mueller
State Auditor

INDEPENDENT AUDITOR'S REPORT

Senator Kathleen Vinehout and
Representative Peter Barca, Co-chairpersons
Joint Legislative Audit Committee

Members of the Board of Trustees and
Mr. Keith Bozarth, Executive Director
State of Wisconsin Investment Board

We have audited the accompanying Statement of Net Assets for the State Investment Fund of the State of Wisconsin as of June 30, 2010, and the related Statement of Operations and Changes in Net Assets for the year then ended. These financial statements are the responsibility of the State of Wisconsin Investment Board's management. Our responsibility is to express an opinion on these financial statements based on our audit.

The financial statements for the year ended June 30, 2009, are being presented for informational purposes only. These financial statements were audited by us and we expressed an unqualified opinion on them in our report dated August 25, 2009, but we have not performed any auditing procedures since that date.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

The financial statements referred to in the first paragraph present only the State Investment Fund and do not purport to, and do not, present fairly the financial position and results of operations of the Investment Board or of the State of Wisconsin in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to in the first paragraph present fairly, in all material respects, the net assets of the State Investment Fund as of June 30, 2010, and the results of its operations and changes in net assets for the year then ended in conformity with accounting principles generally accepted in the United States of America.

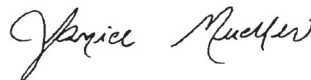
Our audit was conducted for the purpose of forming an opinion on the financial statements of the State Investment Fund. The supplementary information included as Management's Discussion and Analysis, which precedes the financial statements, is presented for purposes of additional analysis and is not a required part of the financial statements. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However, we did not audit the information and, accordingly, we express no opinion on it. The introduction section of the annual report has not been subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on it.

In accordance with *Government Auditing Standards*, we have also issued a report dated August 26, 2010, on our consideration of the Investment Board's internal control over financial reporting for the State Investment Fund; 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, which is included in a management letter to the Investment Board, is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

LEGISLATIVE AUDIT BUREAU

August 26, 2010

by



Janice Mueller
State Auditor

State Investment Fund

Management Discussion and Analysis

Management's 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 its agencies, the Wisconsin Retirement System (WRS), and various local government units (Local Government Investment Pool – LGIP). At June 30, the ownership of the SIF was as follows:

	2010	2009
State of Wisconsin & Agencies	31%	19%
Wisconsin Retirement System	29%	30%
Local Gov't Investment Pool	40%	51%

Following this section are the Financial Statements and Notes to the Financial Statements. The Statement of Net Assets provides information on the types of assets and the liabilities of the SIF. The Statement of Operations and Changes in Net Assets provides information on the net income of the SIF and its net assets 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, 2010 and 2009 (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, 2010, SIF Net Assets had increased by \$56 million from the prior year due to the increase in the Wisconsin agencies (+\$784 million) balance exceeding the combined decrease in both the WRS (-\$30 million) and the LGIP (-\$698 million) balances. The Average Daily Portfolio Balance increased by \$760 million in the current fiscal year compared to the prior year. The monthly average peaked at \$8.651 billion in February 2010.

The Net Income decrease of 81.4% from the previous fiscal year was largely due to the Federal Open Markets Committee maintaining the Federal Funds Rate during fiscal year 2010 at 0.25%. This also caused the Time Weighted Annual Yield to decrease from 1.33% to 0.25%.

SIF Condensed Financial Information

Fiscal Year Ended:	2010	2009	% Change
Total Assets	\$ 6,606,334,844	\$ 6,529,206,269	1.2
Total Liabilities	121,941,844	100,907,269	20.8
Net Assets	<u>\$ 6,484,393,000</u>	<u>\$ 6,428,299,000</u>	0.9
Investment Income	\$ 20,201,005	\$ 87,840,020	(77.0)
Investment Expenses	1,656,651	1,943,880	(14.8)
State Working Bank Charges	3,170,693	3,343,029	(5.2)
Net Income	<u>\$ 15,373,661</u>	<u>\$ 82,553,111</u>	(81.4)
Average Daily Cash Balance	\$ 7,406,327,382	\$ 6,646,201,307	11.4
Time Weighted Annual Yield	0.25%	1.33%	
Weighted Average Maturity (WAM)	78 days	69 days	

STATE INVESTMENT FUND
Statement of Net Assets
As of June 30, 2010 (with Comparative Amounts for June 30, 2009)

	<u>June 30, 2010</u>	<u>June 30, 2009</u>
Assets		
Investments (at fair value):		
Bank NOW Account Deposits	\$ 755,623,512	\$ 867,905,000
Repurchase Agreements	1,249,000,000	901,000,000
Government & Agencies	4,598,987,609	4,557,665,170
Commercial Paper	-	-
Certificates of Deposit	290,000	198,900,000
Asset Backed Securities	-	-
Mortgage Backed Securities	21,222	84,259
Yankee/Euro Issues	-	-
Total Investments	<u>\$ 6,603,922,343</u>	<u>\$ 6,525,554,429</u>
Other Assets:		
Accrued Interest Receivable	<u>2,412,501</u>	<u>3,651,840</u>
Total Assets	<u>\$ 6,606,334,844</u>	<u>\$ 6,529,206,269</u>
Liabilities		
Check Float Invested	\$ 120,752,294	\$ 99,062,276
Earnings Distribution Payable	1,077,394	1,736,961
Accrued Expenses	<u>112,156</u>	<u>108,032</u>
Total Liabilities	<u>\$ 121,941,844</u>	<u>\$ 100,907,269</u>
NET ASSETS	<u>\$ 6,484,393,000</u>	<u>\$ 6,428,299,000</u>
Net Assets consist of:		
Participating Shares	\$ 6,484,393,000	\$ 6,428,299,000
Undistributed Unrealized Gains (Losses)	<u>-</u>	<u>-</u>
NET ASSETS	<u>\$ 6,484,393,000</u>	<u>\$ 6,428,299,000</u>

The accompanying notes are an integral part of this statement.

STATE INVESTMENT FUND

Statement of Operations and Changes in Net Assets

For the Fiscal Year Ended June 30, 2010 (with Comparative Amounts for June 30, 2009)

	2010	2009
Investment Income	\$ 20,201,005	\$ 87,840,020
Investment Expenses		
Management Operating Expenses	\$ 1,305,380	\$ 1,641,013
Custodial Bank Charges	149,800	106,384
Electronic Services	195,071	178,121
Legal and Consulting Fees	6,400	18,362
Total Expenses	\$ 1,656,651	\$ 1,943,880
Net Investment Income	\$ 18,544,354	\$ 85,896,140
State Working Bank Charges	3,170,693	3,343,029
Net Income	\$ 15,373,661	\$ 82,553,111
Distributions Paid and Payable	15,373,661	82,553,111
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	\$ 29,705,226,000	\$ 32,404,364,000
Disbursements by Transfer from Fund	(29,649,132,000)	(31,589,941,000)
Net Change in Participating Shares	\$ 56,094,000	\$ 814,423,000
Beginning of Period Participating Shares	6,428,299,000	5,613,876,000
End of Period Participating Shares	\$ 6,484,393,000	\$ 6,428,299,000
NET ASSETS	\$ 6,484,393,000	\$ 6,428,299,000

The accompanying notes are an integral part of this statement.

Notes to the Financial Statements

1. Description of Fund

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 and 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.

SWIB applies all applicable GASB pronouncements and those Financial Accounting Standards Board (FASB) pronouncements issued on or before November 30, 1989, which do not conflict with or contradict GASB pronouncements.

C. Valuation of Securities

Generally, investments are valued at fair value for financial statement purposes and amortized cost for purposes of calculating income to participants (See Footnote 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.

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 ninety 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.

Repurchase Agreements and Non-Negotiable Certificates of Deposit are valued at cost because they are nonparticipating contracts that do not capture interest rate changes in their value. In addition, a bond issued by a State of Wisconsin agency, having a par value at June 30, 2010 of \$21,222, is valued at par, which management believes approximates fair value. The table entitled **Summary Information by Investment Classification** contains information on SIF holdings.

D. Management Operating Expenses

Management operating expenses are SWIB's investment and administrative costs that are allocated to the SIF participants.

E. 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.

3. Pool Earnings 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

Summary Information by Investment Classification
June 30, 2010

	Interest Rates	Maturity Dates	Book Value (Amort. Cost)	Fair Value
Bank NOW Acct Deposits	0.31 - 0.35	Demand	\$ 755,623,512	\$ 755,623,512
Repurchase Agreements	0.01 - 0.15	07/01/10	1,249,000,000	1,249,000,000
Government and Agencies	0.20 - 0.47	07/15/10 - 06/09/11	4,598,987,609	4,598,987,609
Commercial Paper	--	--	-	-
Certificates of Deposit	5.70	07/15/10	290,000	290,000
Asset Back Securities	--	--	-	-
Mortgage Backed Securities	1.35	05/27/11	21,222	21,222
Yankee/Euro Issues	--	--	-	-
Total Investments			<u>\$ 6,603,922,343</u>	<u>\$ 6,603,922,343</u>
Ratio of Fair Value to Book Value				100%

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 assets as "Undistributed Unrealized Gains (Losses)".

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 Compliance and Investment Committees 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 SIF's investment guidelines establish very specific 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, 2010, 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, 2010, the SIF held a Certificate of Deposit (CD) with an estimated fair value of \$290,000 invested pursuant to the Wisconsin Certificate of Deposit Program (administered by Bankers' Bank) established in July 1987. Investment guidelines provide that banks accepted into this program 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 as a public depository. Approximately \$290,000 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.

Credit Quality Distribution for Securities
June 30, 2010

	Rating	Fair Value	%
Bank NOW Account Deposits	NR	\$ 755,623,512	11.4
Repurchase Agreements (Collateral):			
US Government Debt	AAA	937,000,000	14.2
Govt Sponsored Entity US Agency	AAA - A	312,000,000	4.7
U.S. Treasury	AAA	650,079,664	9.8
FHLB (Federal Home Loan Bank)	A-1+/AAA	1,352,746,112	20.5
FHLMC (Federal Home Loan Mortgage Corp)	A-1+/AAA	1,278,253,519	19.4
FNMA (Federal National Mortgage Association)	A-1+	1,317,908,314	20.0
Certificates of Deposit:			
Non-Negotiable (Wisc Bank)	NR	290,000	0.0
Mortgage Backed Securities	NR	21,222	0.0
Total Investments		<u>\$ 6,603,922,343</u>	<u>100.0</u>

The SIF also had bank Negotiable Order of Withdrawal (NOW) accounts with various Wisconsin banks (\$355.1 million), administered by Bankers' Bank, and with Fifth Third Bank (\$400.5 million). Because these bank NOW accounts had interest rates no higher than 0.50%, these balances are fully guaranteed under the transaction account guarantee component (TAG) of the FDIC's Temporary Liquidity Guarantee Program (TLGP).

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, 2010 the SIF has more than five percent of its investments in a Fifth Third Bank NOW Account Deposit (6.1%), FHLB (20.5%),

FHLMC (19.4%), FNMA (20.0%), and Repurchase Agreement collateral consisting of various securities issued by these same three U.S. Agencies (4.7%). 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 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 summary WAM analysis 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

**Weighted Average Maturities (WAM) for Securities
June 30, 2010**

	<u>Fair Value</u>	<u>WAM (Days)</u>
Bank NOW Acct Deposits	\$ 755,623,512	0
Repurchase Agreements	1,249,000,000	1
Government and Agencies	4,598,987,609	112
Commercial Paper	-	--
Certificates of Deposit	290,000	15
Asset Backed Securities	-	--
Mortgage Backed Securities	21,222	331
Yankee/Euro Issues	-	--
Total Investments	<u>\$ 6,603,922,343</u>	
Portfolio Weighted Average Maturity		<u>78</u>

investment. SIF guidelines allow the investment in U.S. dollar denominated issues only.

5. Related Party Transactions

The SIF held one bond issued by a State of Wisconsin agency, the Department of Veterans Affairs, with a remaining par and carrying value of \$21,222 as of June 30, 2010. SWIB management believes the rate of interest received is comparable to rates for bonds with similar characteristics issued by an unaffiliated third party.

Wisconsin Statutes Chap. 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 2010, Chapter 20.002 (11) (b) 2 provides that General Fund borrowings may not exceed 7% of defined revenues (estimated borrowing cap of \$940 million). 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 \$1.3 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, 2010 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, 2010**

<u>Fund</u>	<u>Loan Amount</u>
Medical Assistance Trust	\$ 257,227,000
Police & Fire Protection	5,021,000
Environmental	<u>10,376,000</u>
Total Loans	<u>\$ 272,624,000</u>



STATE OF WISCONSIN

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Janice Mueller
State Auditor

INDEPENDENT AUDITOR'S REPORT

Senator Kathleen Vinehout and
Representative Peter Barca, Co-chairpersons
Joint Legislative Audit Committee

Members of the Board of Trustees and
Mr. Keith Bozarth, Executive Director
State of Wisconsin Investment Board

We have audited the accompanying Statement of Net Investment Assets for 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 June 30, 2010, and the related Statement of Changes in Net Investment Assets for the year then ended. These financial statements are the responsibility of the State of Wisconsin Investment Board's management. Our responsibility is to express an opinion on these financial statements based on our audit.

The financial statements for the year ended June 30, 2009, are being presented for informational purposes only. These financial statements were audited by us and we expressed an unqualified opinion on them in our report dated November 24, 2009, but we have not performed any auditing procedures since that date.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

As discussed in Note 1, the financial statements referred to in the first paragraph present only the investment activity of the Various Funds attributable to the transactions of the State of Wisconsin Investment Board. The financial statements do not purport to, and do not, present 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 and results of operations of the Investment Board or of the State of Wisconsin in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to in the first paragraph present fairly, in all material respects, the respective net investment assets of each of the Various Funds as of June 30, 2010, and the respective changes in net investment assets for the year then ended in conformity with accounting principles generally accepted in the United States of America.

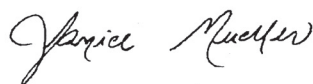
Our audit was conducted for the purpose of forming an opinion on the financial statements of the Various Funds. The supplementary information included as Management's Discussion and Analysis, which precedes the financial statements, is presented for purposes of additional analysis and is not a required part of the financial statements. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However, we did not audit the information and express no opinion on it. The introduction section of the annual report has not been subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on it.

In accordance with *Government Auditing Standards*, we have also issued a report dated November 29, 2010, 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, which is included in a management letter to the Investment Board, is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

LEGISLATIVE AUDIT BUREAU

November 29, 2010

by



Janice Mueller
State Auditor

Various Funds

Management Discussion and Analysis

Management Discussion and Analysis provides general information on the investment financial activities of the Local Government Property Insurance Fund (LGPIF), State Life Insurance Fund (Life Fund), Injured Patients and Families Compensation Fund (IPFCF), EdVest Tuition Trust Fund (EdVest), and Historical Society Trust Fund (HSTF) (collectively known as the “Various Funds”). The State of Wisconsin Investment Board (SWIB) has exclusive control of 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. The **Statement of Net Investment Assets** provides information on the types of investments and the liabilities of the Various Funds. The **Statement of Changes in Net Investment Assets** provides information on the investment income of the

Various Funds and their net assets 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, 2010 (with comparable amounts for 2009) is in the table entitled **Various Funds Condensed Investment Financial Information**.

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

For Fiscal Year 2010, both equity markets and bond prices were generally significantly higher during the year. The Federal Open Markets Committee

Various Funds Condensed Investment Financial Information

Fiscal Year Ended June 30:	2010	2009	% Change	% Annual Return	
				Fund	Benchmark
<u>Net Investment Assets:</u>					
Local Govt Property Ins Fund	\$ 47,403,885	\$ 52,717,233	(10.1)		
State Life Insurance Fund	98,531,216	87,883,468	12.1		
Inj Patients & Families Comp Fd	652,061,055	567,854,617	14.8		
EdVest Tuition Trust Fund	8,325,332	8,894,696	(6.4)		
Historical Society Trust Fund	9,394,970	8,790,182	6.9		
<u>Net Investment Income:</u>					
Local Govt Property Ins Fund	\$ 662,416	\$ 737,289	(10.2)	1.3	0.4
State Life Insurance Fund	13,486,590	5,425,054	148.6	15.6	13.9
Inj Patients & Families Comp Fd	68,037,376	(5,123,893)	1427.8	11.7	10.4
EdVest Tuition Trust Fund	610,847	386,135	58.2	7.5	6.6
Historical Society Trust Fund	1,236,815	(2,000,340)	161.8	14.1	14.3

Management Discussion and Analysis

(FOMC) maintained the federal funds target rate at 0.25%. Since the Local Government Property Insurance Fund was primarily invested in the State Investment Fund (SIF), the lower short-term interest rates resulted in a 10.2% decrease in Net Investment Income.

The Life Fund, IPFCF, and EdVest 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 148.6% increase in Net Investment Income of the Life Fund was due to significantly higher bond prices.

In addition to higher bond prices, the increase in Net Investment Income for the Injured

Patients and Families Compensation Fund was due to four indexed stock funds, representing 15.8% of investments, which experienced a \$12.9 million increase in fair value during the current year as compared to a \$33.1 million decrease in fair value during the prior year.

The 58.2% increase in Net Investment Income for EdVest was due to appreciation in the prices of government sponsored entity bonds it held as compared to depreciation in the prior year.

The increase in Net Investment Income for the Historical Society Trust Fund was largely due to an indexed stock fund, representing 73.6% of Net Investment Assets, which experienced a \$0.9 million increase in fair value during the current year as compared to a \$2.1 million decrease in fair value during the prior year.

VARIOUS FUNDS

Statement of Net Investment Assets

As of June 30, 2010

	Local Govt Property Ins Fund	State Life Insurance Fund	Injured Patients & Families Compensation Fund	EdVest Tuition Trust Fund	Historical Society Trust Fund
Investment Assets					
Cash and Cash Equivalents	\$ 26,305,089	\$ 1,280,305	\$ 53,327,345	\$ 1,523,771	\$ 200,634
Receivables:					
Investment Income	135,115	1,364,427	7,154,971	13,495	9,924
Investment Sales	-	-	-	-	7,465
Investments:					
Fixed Income	20,963,681	95,886,484	489,929,000	6,788,066	2,279,192
Stocks	-	-	101,659,440	-	6,898,406
Total Investment Assets	\$ 47,403,885	\$ 98,531,216	\$ 652,070,756	\$ 8,325,332	\$ 9,395,621
Liabilities					
Investment Purchases Payable	-	-	6,280	-	101
Accounts Payable	-	-	3,421	-	550
Due to State Investment Fund	-	-	-	-	-
Total Liabilities	\$ -	\$ -	\$ 9,701	\$ -	\$ 651
Net Investment Assets	\$ 47,403,885	\$ 98,531,216	\$ 652,061,055	\$ 8,325,332	\$ 9,394,970

VARIOUS FUNDS

Statement of Changes in Net Investment Assets

For the Fiscal Year Ended June 30, 2010

	Local Govt Property Ins Fund	State Life Insurance Fund	Injured Patients & Families Compensation Fund	EdVest Tuition Trust Fund	Historical Society Trust Fund
From Investment Activities:					
Investment Income					
Net Increase (Decrease) in Fair Value of Investments	\$ 287,133	\$ 8,591,829	\$ 41,050,141	\$ 267,612	\$ 1,247,863
Interest	377,808	4,900,547	27,032,930	343,235	503
Investment Expenses	(2,525)	(5,786)	(45,695)	-	(11,551)
Net Investment Income	\$ 662,416	\$ 13,486,590	\$ 68,037,376	\$ 610,847	\$ 1,236,815
From Participant Transactions:					
Net Receipts (Disbursements) - Non-Investment Activity	(5,975,764)	(2,838,842)	16,169,062	(1,180,211)	(632,027)
Net Increase (Decrease) in Net Investment Assets	\$ (5,313,348)	\$ 10,647,748	\$ 84,206,438	\$ (569,364)	\$ 604,788
Net Investment Assets					
Beginning of Year	52,717,233	87,883,468	567,854,617	8,894,696	8,790,182
End of Year	\$ 47,403,885	\$ 98,531,216	\$ 652,061,055	\$ 8,325,332	\$ 9,394,970

The accompanying notes are an integral part of this statement.

VARIOUS FUNDS

Statement of Net Investment Assets

Comparative Amounts for June 30, 2009

	Local Govt Property Ins Fund	State Life Insurance Fund	Injured Patients & Families Compensation Fund	EdVest Tuition Trust Fund	Historical Society Trust Fund
Investment Assets					
Cash and Cash Equivalents	\$ 33,602,685	\$ 1,626,743	\$ 287	\$ 1,612,402	\$ 293,921
Receivables:					
Investment Income	174,658	1,346,308	8,435,276	23,015	29,316
Investment Sales	-	-	750,000	-	7,201
Investments:					
Fixed Income	18,939,890	84,910,417	547,121,817	7,259,279	1,898,830
Stocks	-	-	88,709,713	-	6,561,750
Total Investment Assets	\$ 52,717,233	\$ 87,883,468	\$ 645,017,093	\$ 8,894,696	\$ 8,791,018
Liabilities					
Investment Purchases Payable	-	-	6,656	-	371
Accounts Payable	-	-	4,820	-	465
Due to State Investment Fund	-	-	77,151,000	-	-
Total Liabilities	\$ -	\$ -	\$ 77,162,476	\$ -	\$ 836
Net Investment Assets	\$ 52,717,233	\$ 87,883,468	\$ 567,854,617	\$ 8,894,696	\$ 8,790,182

VARIOUS FUNDS

Statement of Changes in Net Investment Assets

Comparative Amounts for the Fiscal Year Ended June 30, 2009

	Local Govt Property Ins Fund	State Life Insurance Fund	Injured Patients & Families Compensation Fund	EdVest Tuition Trust Fund	Historical Society Trust Fund
From Investment Activities:					
Investment Income					
Net Increase (Decrease) in Fair Value of Investments	\$ (21,181)	\$ 633,758	\$ (35,256,593)	\$ (32,740)	\$ (1,989,485)
Interest	759,304	4,796,784	30,176,790	418,875	3,034
Investment Expenses	(834)	(5,488)	(44,090)	-	(13,889)
Net Investment Income	\$ 737,289	\$ 5,425,054	\$ (5,123,893)	\$ 386,135	\$ (2,000,340)
From Participant Transactions:					
Net Receipts (Disbursements) - Non-Investment Activity	(1,227,310)	(2,738,776)	(162,608,708)	(822,216)	(441,559)
Net Increase (Decrease) in Net Investment Assets	\$ (490,021)	\$ 2,686,278	\$ (167,732,601)	\$ (436,081)	\$ (2,441,899)
Net Investment Assets					
Beginning of Year	53,207,254	85,197,190	735,587,218	9,330,777	11,232,081
End of Year	\$ 52,717,233	\$ 87,883,468	\$ 567,854,617	\$ 8,894,696	\$ 8,790,182

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. Also excluded from the statements are SWIB’s administrative receipts and disbursements related to the investment function.

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 (LGPIF) 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 LGPIF, 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, certificates of deposit issued by banks in the United States, and solvent financial institutions in Wisconsin.

B. State Life Insurance Fund

The State Life Insurance Fund (Life Fund) offers low cost 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 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 (IPFCF) provides medical malpractice insurance protection to health care providers permanently practicing or operating in Wisconsin. Management of the IPFCF 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. Since September 1990, SWIB has been 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 IPFCF. 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 governmental units or of corporations, loans secured by mortgages, preferred or common stock, real property and other investments not specifically prohibited by statute.

D. Historical Society Trust Fund

The State Historical Society of Wisconsin 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 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 (HSTF). 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 Historical Society in accordance with provisions of the gift, grant or bequest. The Historical Society funds available for investment are authorized to be invested in "every kind of property, real, personal or mixed, and every kind of investment, specifically including but not by the way of limitation, bonds, debentures, and other corporate obligations, stocks, preferred or common, and shares of investment companies and investment trusts, which persons of prudence, discretion, and intelligence acquire or retain for their own account."

E. EdVest Tuition Trust Fund

The EdVest Wisconsin program offers families a way to prepare for future higher education costs. When the program 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 Office of State Treasurer is responsible for the administration of the EdVest Wisconsin program. Wisconsin Statute 14.63(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 State Treasurer in his or her quarterly reports. All income derived from such investments shall be credited to the fund. The sale of tuition units was discontinued in 2002. Other investment options are available under the EdVest program, but these are not managed by the Investment Board.

2. Significant Accounting Policies

A. Basis of Presentation

The accompanying financial statements of the investment activity of the Various Funds are prepared in accordance 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. In reporting the investment activity of proprietary funds, SWIB applies all applicable GASB pronouncements and those Financial Accounting Standards Board (FASB) pronouncements issued on or before November 30, 1989, which do not conflict with or contradict GASB pronouncements. The Historical Society Trust Fund is reported by the State as a governmental fund and the EdVest Tuition Trust Fund is reported by the State as a fiduciary fund.

B. 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 Governmental Accounting Standards Board Statement No. 31, the investments of the Various Funds are valued at fair value, with unrealized and realized gains and losses reflected in the **Statement of Changes in Net Investment Assets** as “Net Increase (Decrease) in Fair Value of Investments”.

Generally, fair value is based on quoted market prices. Private placements, when held, are priced via a multi-tiered method. This method prices each holding based on the best available information using a hierarchy of pricing sources.

D. 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.

E. Cash and Cash Equivalents

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

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

Notes to the Financial Statements

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, guideline exceptions, when identified, are reviewed by SWIB's 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' (except for EdVest) 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). IPFCF guidelines provide that, at the time of

purchase, at least 80% of the bond portfolio must be rated "A3/A1-" or better, using the lower of split ratings. EdVest guidelines do not specifically list a minimum credit quality. As of June 30, 2010, these credit ratings and aggregate exposures by investment type can be found in the table entitled **Credit Quality Distribution for Fixed Income Securities**.

B. Custodial Credit Risk

Deposits — Custodial credit risk for 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, 2010, the Various Funds had \$3,144 deposited in a bank

Credit Quality Distribution for Fixed Income Securities

June 30, 2010

	LGPIF		State Life		IPFCF		EdVest		Historical Society	
	<u>Fair Value</u>	<u>%</u>	<u>Fair Value</u>	<u>%</u>	<u>Fair Value</u>	<u>%</u>	<u>Fair Value</u>	<u>%</u>	<u>Fair Value</u>	<u>%</u>
AAA	\$ 20,963,681	44.4	\$ 39,356,810	40.5	\$ 204,662,584	37.7	\$ 6,059,663	72.9	\$ -	0.0
AA	-	0.0	4,563,174	4.7	16,399,815	3.0	115,189	1.4	-	0.0
A	-	0.0	31,577,594	32.5	154,732,476	28.5	402,069	4.9	-	0.0
BBB	-	0.0	18,701,191	19.2	91,428,688	16.8	-	0.0	-	0.0
BB	-	0.0	1,027,715	1.1	19,380,437	3.6	211,145	2.5	-	0.0
B	-	0.0	660,000	0.7	3,300,000	0.6	-	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	25,000	0.0	-	0.0	-	0.0
Bond Fund	-	0.0	-	0.0	-	0.0	-	0.0	2,279,192	92.0
Subtotals	\$ 20,963,681	44.4	\$ 95,886,484	98.7	\$ 489,929,000	90.2	\$ 6,788,066	81.7	\$ 2,279,192	92.0
SIF (unrated)	26,305,000	55.6	1,280,000	1.3	53,327,000	9.8	1,523,000	18.3	199,000	8.0
Totals	\$ 47,268,681	100.0	\$ 97,166,484	100.0	\$ 543,256,000	100.0	\$ 8,311,066	100.0	\$ 2,478,192	100.0

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

account covered by FDIC insurance.

Investments — Custodial credit risk for investments is the risk that, in the event of the 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, 2010, 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. With the exception of EdVest, 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 LGPIF further limits AAA-rated mortgage-backed, AAA-rated asset-backed, and individual corporate issuers to 3% of the market value of the fund investments.

Excluding investments issued or explicitly guaranteed by the U.S. government and pooled investments, as of June 30, 2010 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 LGPIF guidelines require that a bond's maturity must not exceed ten years. The Life Fund guidelines require the Weighted Average Maturity (WAM) of the portfolio, including cash, shall be a minimum of ten years. The IPFCF guidelines require that the average duration of the aggregate bond portfolio shall be less than ten years. Summary duration analysis is found in the table entitled **Duration or WAM 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 Fund investment guidelines do not specifically address foreign currency risk with the exception that the Life Fund only allows investments in U.S. dollar denominated instruments. As of June 30, 2010, 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

Duration or WAM (in years) for Fixed Income Securities

June 30, 2010

	LGPIF		State Life		IPFCF		EdVest		Historical Society	
	<u>Fair Value</u>	<u>Duration</u>	<u>Fair Value</u>	<u>WAM</u>	<u>Fair Value</u>	<u>Duration</u>	<u>Fair Value</u>	<u>Duration</u>	<u>Fair Value</u>	<u>Duration</u>
Govt/Agcy	\$ 10,216,240	0.95	\$ 38,256,997	15.66	\$ 195,718,161	4.72	\$ 6,059,663	4.42	\$ -	0.00
Corporate	10,747,441	1.58	57,629,487	17.48	294,210,839	5.43	728,403	4.90	-	0.00
Bond Fund	-		-		-		-		2,279,192	5.50
Subtotal / Wtd Ave	\$ 20,963,681	1.28	\$ 95,886,484	16.75	\$ 489,929,000	5.15	\$ 6,788,066	4.47	\$ 2,279,192	5.50
SIF (WAM)	26,305,000	0.21	1,280,000	0.21	53,327,000	0.21	1,523,000	0.21	199,000	0.21
Total / Wtd Ave	\$ 47,268,681	0.68	\$ 97,166,484	16.53	\$ 543,256,000	4.66	\$ 8,311,066	3.69	\$ 2,478,192	5.08

for traditional United States Treasury obligations.

As of June 30, 2010, the EdVest Tuition Trust Fund held interest only strips valued at \$6.06 million, representing approximately 72.9% of portfolio investments.

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