

**State of Illinois
Office of the State Treasurer
The Illinois Funds**

Financial Audit
Years Ended June 30, 2013 and 2012
Performed as Special Assistant Auditors
for the Auditor General, State of Illinois



Assurance ■ Tax ■ Consulting

**State of Illinois
Office of the Treasurer
The Illinois Funds**

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**State of Illinois
Office of the Treasurer
The Illinois Funds**

Treasurer's Office Officials

Treasurer	Honorable Dan Rutherford
Chief of Staff	Mr. Kyle Ham
Executive Director of Finance	Ms. Bridget Byron (March 21, 2012 – present)
Deputy Treasurer/CFO	Mr. Edward Buckles (through December 31, 2011)
General Counsel	Ms. Maureen Lydon (through September 15, 2013) Mr. Neil P. Olson (September 16, 2013 - Present)
Director of The Illinois Funds Acting Director of The Illinois Funds	Mr. Randy Coffey (through November 30, 2011) Mr. Ashvin Lad (December 1, 2011 - September 30, 2012)
Director of Invest in IL / IL Funds Sales	Mr. Ashvin Lad (October 1, 2012 – Present)
Director of Operations, The Illinois Funds	Mr. Jose Gonzalez (October 1, 2012 – Present)
Portfolio Manager	Mr. Mark Polistina
Inspector General	Mr. David Wells
Chief Internal Auditor	Ms. Barbara Ringler

The Office of the Treasurer maintains the following four office locations:

Executive Office
State Capitol
219 State House
Springfield, Illinois 62706

Operational Divisions
Illinois Business Center
400 West Monroe
Springfield, Illinois 62704

Unclaimed Property & Other Divisions
Myers Building
1 W. Old State Capitol Plaza
Springfield, Illinois 62701

Chicago Office Legal / Programmatic
James R. Thompson Center
100 West Randolph Street
Suite 15-600
Chicago, Illinois 60601

FINANCIAL STATEMENT REPORT

**State of Illinois
Office of the Treasurer
The Illinois Funds**

Financial Statement Report

Summary

The audits of the accompanying financial statements of The Illinois Funds of the State of Illinois, Office of the Treasurer, were performed by McGladrey LLP as of and for the years ended June 30, 2013 and 2012.

Based on their audits, the auditors expressed unmodified opinions on The Illinois Funds' financial statements.

Independent Auditor's Report



Independent Auditor's Report

The Honorable William G. Holland
Auditor General
State of Illinois

Report on the Financial Statements

As Special Assistant Auditors for the Auditor General, we have audited the accompanying financial statements of The Illinois Funds, a fiduciary (investment trust) fund of the State of Illinois, Office of the Treasurer, as of and for the years ended June 30, 2013 and 2012, and the related notes to the financial statements, as listed in the table of contents.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits 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 from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of The Illinois Funds, of the State of Illinois, Office of the Treasurer as of June 30, 2013 and 2012, and the changes in financial position thereof for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis of Matter

As discussed in Note 1, the financial statements present only The Illinois Funds, and do not purport to, and do not, present fairly the financial position of the State of Illinois or the State of Illinois, Office of the Treasurer, as of June 30, 2013 and 2012, and the changes in its financial position, for the years then ended in accordance with accounting principles generally accepted in the United States of America. Our opinion is not modified with respect to this matter.

Other Matters

Required Supplementary Information

Management has omitted management's discussion and analysis that accounting principles generally accepted in the United States of America require to be presented to supplement the financial statements. Such missing information, although not a part of the financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the financial statements in an appropriate operational, economic, or historical context. Our opinion on the financial statements is not affected by this missing information.

Other Information

Our audit was conducted for the purpose of forming an opinion on the financial statements of The Illinois Funds of the State of Illinois, Office of the Treasurer. The Supplementary Information (pages 16 – 22), and the other Information (pages 23 – 28) are presented for purposes of additional analysis and are not a required part of the financial statements.

The Supplementary Information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. Such information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the Supplementary Information is fairly stated, in all material respects, in relation to the financial statements as a whole.

The Other Information, consisting of the Money Market Fund Investment Policy has not been subjected to the auditing procedures applied in the audit of the financial statements, and accordingly, we do not express an opinion or provide any assurance on it.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our reports dated December 10, 2013, and November 30, 2012 on our consideration of the State of Illinois, Office of the Treasurer's internal control over financial reporting of The Illinois Funds and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of these reports 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 internal control over financial reporting or on compliance. These reports are an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the State of Illinois, Office of the Treasurer's internal control over financial reporting of The Illinois Funds and its compliance.

McGladrey LLP

Schaumburg, Illinois
December 10, 2013

**State of Illinois
Office of the Treasurer**

**The Illinois Funds
Statements of Fiduciary Net Position
June 30, 2013 and 2012**

	2013	2012
Assets		
Cash equivalents		
Repurchase agreements, including accrued interest of \$19,667 and \$26,292 in 2013 and 2012, respectively	\$ 2,350,019,667	\$ 3,150,026,292
Commercial paper, net of unamortized discount of \$73,292 and \$60,916 in 2013 and 2012, respectively	891,926,708	1,509,939,084
Money market mutual funds	498,404,345	243,950,787
U.S. Treasury Bills, net of unamortized discount of \$461 and \$0 in 2013 and 2012, respectively	149,999,539	-
U.S. agency obligations		
Federal Home Loan Mortgage Corporation Discount Notes, net of unamortized discount of \$123 and \$0 in 2013 and 2012, respectively	13,999,878	-
Federal National Mortgage Association Discount Notes, net of unamortized discount of \$250 and \$0 in 2013 and 2012, respectively	24,999,750	-
Federal Farm Credit Banks Discount Notes, net of unamortized discount of \$2,708 and \$0 in 2013 and 2012, respectively	49,997,292	-
Federal Home Loan Bank Discount Notes, net of unamortized discount of \$10,663 and \$556 in 2013 and 2012, respectively	289,241,337	24,999,444
Federal Agricultural Mortgage Corporation Discount Notes, net of unamortized discount of \$0 and \$402 in 2013 and 2012, respectively	-	67,659,598
Total cash equivalents	4,268,588,516	4,996,575,205
Deposits and investments		
Commercial paper, net of unamortized discount of \$165,084 and \$153,472 in 2013 and 2012, respectively	499,834,916	249,846,528
U.S. Treasury Bills net of unamortized discount of \$16,839 and \$20,581 in 2013 and 2012, respectively	149,983,161	124,979,420
U.S. Treasury Notes, net of unamortized premium of \$1,937,966 and \$791,490 and unamortized discount of \$6,897 and \$0 in 2013 and 2012, respectively	751,931,069	225,791,490

(Continued)

**State of Illinois
Office of the Treasurer**

**The Illinois Funds
Statements of Fiduciary Net Position (Continued)
June 30, 2013 and 2012**

	2013	2012
Assets (Continued)		
U.S. agency obligations		
Federal Home Loan Bank Debentures	\$ -	\$ 150,000,000
Federal Home Loan Mortgage Corporation Discount Notes, net of unamortized discount of \$22,236 and \$18,278 in 2013 and 2012, respectively	74,977,764	49,981,722
Federal National Mortgage Association Discount Notes, net of unamortized discount of \$16,976 and \$0 in 2013 and 2012, respectively	74,983,024	-
Federal Home Loan Bank Discount Notes, net of unamortized discount of \$27,903 and \$5,531 in 2013 and 2012, respectively	<u>24,972,097</u>	<u>24,994,469</u>
Total deposits and investments	1,576,682,031	825,593,629
Accrued interest receivable	<u>1,402,609</u>	<u>714,930</u>
Total assets	<u>\$ 5,846,673,156</u>	<u>\$ 5,822,883,764</u>
Liabilities and Net Position		
Accrued liabilities		
Bank custodial fees	\$ 150,985	\$ 149,882
State management fees	<u>180,492</u>	<u>231,700</u>
Total liabilities	<u>331,477</u>	<u>381,582</u>
Net position held in trust for pool participants	<u>\$ 5,846,341,679</u>	<u>\$ 5,822,502,182</u>
The pricing of shares		
Participant shares outstanding (\$1.00 par, unlimited shares authorized)	<u>\$ 5,846,341,679</u>	<u>\$ 5,822,502,182</u>
Participant net position value, offering and redemption price per share	<u>\$ 1.00</u>	<u>\$ 1.00</u>

The accompanying notes are an integral part of these statements.

**State of Illinois
Office of the Treasurer**

**The Illinois Funds
Statements of Changes in Fiduciary Net Position
For the Years Ended June 30, 2013 and 2012**

	2013	2012
Operations		
Investment income		
Investment earnings	\$ 9,109,827	\$ 8,828,652
Investment expenses		
Bank custodial fees	1,861,841	1,854,023
State management fees	2,818,133	2,882,591
Total investment expenses	<u>4,679,974</u>	<u>4,736,614</u>
Net investment income	<u>4,429,853</u>	<u>4,092,038</u>
Dividends to participants from net investment income	(4,429,853)	(4,092,038)
Share transactions (dollar amounts and number of shares are the same)		
Subscriptions	18,562,005,902	18,922,359,929
Reinvestments	4,409,554	4,091,739
Redemptions	<u>(18,542,575,959)</u>	<u>(18,678,042,549)</u>
Change in net position and shares resulting from share transactions	23,839,497	248,409,119
Net position, beginning of year	<u>5,822,502,182</u>	<u>5,574,093,063</u>
Net position, end of year	<u>\$ 5,846,341,679</u>	<u>\$ 5,822,502,182</u>

The accompanying notes are an integral part of these statements.

**State of Illinois
Office of the Treasurer
The Illinois Funds**

Notes to the Financial Statements

Background

The Illinois Funds was established in 1976 (through 15 ILCS 505/17) to supplement and enhance the investment opportunities available to custodians of public agency funds throughout the State of Illinois. The management, custodianship, and operation of The Illinois Funds are under the supervision of the State of Illinois, Office of the Treasurer (“Treasurer”).

Note 1. Summary of Significant Accounting Policies

Financial Reporting Entity: As described in the Illinois Comprehensive Annual Financial Report, the State of Illinois is the primary government, which includes all funds, elected offices, departments, and agencies of the State, as well as boards, commissions, authorities, universities and colleges over which the State’s executive or legislative branches exercise legal control.

The Illinois Funds is not legally separate from the State of Illinois and is, therefore, determined to be part of the primary government. The Illinois Funds is included in the Illinois Comprehensive Annual Financial Report as an investment trust fund. The Illinois Funds consists of an internal and external portion. The internal portion is the portion that belongs to the State and its component units. The external portion is the portion belonging to the noncomponent-unit participants. The scope of The Illinois Funds’ financial statements presented herein is limited to the financial position of The Illinois Funds, including net position available to all participants, both internal and external, and the changes in net position. The internal portion of The Illinois Funds is included in the various funds in the Illinois Comprehensive Annual Financial Report as an investment.

As a governmental sponsored investment pool, The Illinois Funds is not eligible to register with the Securities and Exchange Commission (“SEC”) and thus is not a registrant with the SEC; however The Illinois Funds has adopted operating procedures consistent with those required of a SEC 2a-7 Fund (2a-7-like Fund). The Illinois Funds has a policy that it will, and does, operate in a manner consistent with SEC Rule 2a-7, which governs the operation of SEC regulated money market funds.

Fiduciary Fund: The Illinois Funds is classified as an investment trust fund. This investment trust fund is used to account for assets held by The Illinois Funds in a trustee capacity or as an agent for public treasurers and other custodians of public monies throughout the State of Illinois. This investment trust fund is not held in the State Treasury and is a non-appropriated fund.

Basis of Accounting and Measurement Focus: The accounts of The Illinois Funds are maintained and reported using the accrual basis of accounting. Revenues are recorded when earned and expenses are recorded at the time liabilities are incurred, regardless of when the related cash flow takes place.

Cash Equivalents, Deposits, and Investments: Cash equivalents are defined as short-term, highly liquid investments readily convertible to cash with maturities of 90 days or less at time of purchase.

Repurchase agreements (securities purchased under agreements to resell) are reported at cost plus accrued interest.

Commercial paper is stated at amortized cost, which excludes accrued interest and includes accretion of discounts and amortization of premiums. Commercial paper utilizes the straight-line method of amortization or accretion. It is the intent of management to hold commercial paper to maturity.

**State of Illinois
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The Illinois Funds**

Notes to the Financial Statements

Note 1. Summary of Significant Accounting Policies (Continued)

Money market mutual funds are carried at cost and are purchased from various brokerage firms. The funds are comprised of U.S. Treasury and U.S. agency obligations. Mutual fund yields are subject to market rate fluctuations.

U.S. agency obligations are stated at amortized cost, which excludes accrued interest and includes accretion of discounts and amortization of premiums. U.S. agency coupon notes utilize the constant yield method and, when applicable, all others use straight-line amortization. It is the intent of management to hold U.S. agency securities to maturity unless market conditions provide for realization of a gain and management determines a sale would be in the best interest of The Illinois Funds.

U.S. Treasury obligations are stated at amortized cost, which excludes accrued interest and includes accretion of discounts and amortization of premiums. Treasury notes utilize the constant yield method and strips and bills use straight-line amortization. It is the intent of management to hold U.S. Treasury obligations to maturity unless market conditions provide for realization of a gain and management determines a sale would be in the best interest of The Illinois Funds.

Investment expenses consist of bank custodial fees and State management fees. Both custodial fees and State management fees are accrued daily based on the net asset value of The Illinois Funds. For more information, see Note 4.

Management Estimates: To prepare financial statements in conformity with accounting principles generally accepted in the United States of America, management is required to make certain estimates that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reported period. These estimates may differ from actual results.

Net Position Available to Participants: The net position available to participants represent the total value of all participant deposits including late deposits held in an overnight investment account as of June 30, 2013 and 2012.

The Illinois Funds operates in a manner similar to an open-end mutual fund. Participants' deposits and withdrawals were accounted for as purchases and sales of The Illinois Funds' capital shares. The amount of net proceeds from the sale of shares represents the gross withdrawals, which were redeemed from The Illinois Funds' shares during the year. The cost of shares purchased represents the gross deposits, which were invested in The Illinois Funds' shares during the year. These amounts did not include deposits or earnings, which were remitted directly to participants versus invested (or reinvested) in The Illinois Funds' shares.

**State of Illinois
Office of the Treasurer
The Illinois Funds**

Notes to the Financial Statements

Note 2. Deposits and Investments

Governmental Accounting Standards Board Statement No. 31, *Accounting and Financial Reporting for Certain Investments and External Investment Pools*, established standards for accounting for investments held by governmental entities. The Illinois Funds operates as a 2a7-like pool and, thus, reports all investments at amortized cost rather than fair value.

Permitted Deposits and Investments: The Treasurer's investment activities are governed by the Treasurer's published investment policies, which were developed in accordance with State statute and the desire to maintain The Illinois Funds' AAAM rating from Standard & Poor's. In addition, the Treasurer's Office has adopted its own investment practices, which supplement the statutory requirements.

For The Illinois Funds, the Treasurer may invest in time deposits and other interest-bearing accounts in banks and savings and loan associations located in Illinois that are insured by the Federal Deposit Insurance Corporation ("FDIC"), credit unions whose principal office is located in Illinois, obligations of the United States and its agencies, short-term obligations of corporations whose obligations are rated among the two highest classifications established by at least two standard rating services, repurchase agreements, or other investments approved by State law.

The Illinois Funds is rated AAAM by Standard & Poor's Ratings.

The Illinois Funds determines the fair value of investments annually in connection with year-end financial reporting. A summary of investments held at June 30, 2013 and 2012 is as follows:

Summary of Investments at June 30, 2013:

Type	Carrying Amount	Fair Value	Face / Par Principal Amount	Range of Interest Yields	Range of Maturity Dates
Repurchase Agreements	\$ 2,350,019,667	\$ 2,350,019,667	\$ 2,350,000,000	0.080 - 0.120%	07/01/2013
Commercial Paper	1,391,761,624	1,391,709,460	1,392,000,000	0.071 - 0.213%	7/2/13 - 10/4/13
Money Market Mutual Funds	498,404,345	498,404,345	498,404,345	NA	NA
United States Treasury Bills	299,982,700	299,994,750	300,000,000	0.009 - 0.105%	7/5/13 - 9/26/13
United States Treasury Notes	751,931,069	751,928,250	750,000,000	0.115 - 0.200%	7/15/13 - 7/15/14
Federal Home Loan Mtg Corp Discount Notes	88,977,642	88,981,500	89,000,000	0.045 - 0.100%	7/8/13 - 1/22/14
Federal National Mtg Assoc Discount Notes	99,982,774	99,987,000	100,000,000	0.040 - 0.100%	7/2/13 - 11/13/13
Federal Home Loan Bank Discount Notes	314,213,434	314,221,750	314,252,000	0.040 - 0.140%	7/3/13 - 4/14/14
Federal Farm Credit Banks Discount Notes	49,997,292	49,998,750	50,000,000	0.050 - 0.070%	7/16/13 - 8/15/13
	<u>\$ 5,845,270,547</u>	<u>\$ 5,845,245,472</u>	<u>\$ 5,843,656,345</u>		

**State of Illinois
Office of the Treasurer
The Illinois Funds**

Notes to the Financial Statements

Note 2. Deposits and Investments (Continued)

Summary of Investments at June 30, 2012:

Type	Carrying Amount	Fair Value	Face / Par Principal Amount	Range of Interest Yields	Range of Maturity Dates
Repurchase Agreements	\$ 3,150,026,292	\$ 3,150,026,292	\$ 3,150,000,000	0.110 - 0.170%	7/2/12 - 7/5/12
Commercial Paper	1,759,785,612	1,759,703,800	1,760,000,000	0.101 - 0.345%	7/2/12 - 9/4/12
Money Market Mutual Funds	243,950,787	243,950,787	243,950,787	NA	NA
United States Treasury Bills	124,979,420	124,990,500	125,000,000	0.105 - 0.136%	8/2/12 - 9/6/12
United States Treasury Notes	225,791,490	225,798,500	225,000,000	0.095 - 0.270%	7/31/12 - 5/31/13
Federal Home Loan Mtg Corp Discount Notes	49,981,722	49,988,500	50,000,000	0.140%	10/3/2012
Federal Home Loan Bank Debentures	150,000,000	149,981,250	150,000,000	0.250 - 0.300%	2/8/13 - 6/21/13
Federal Home Loan Bank Discount Notes	49,993,913	49,997,750	50,000,000	0.080 - 0.135%	7/11/12 - 8/29/12
Federal Agricultural Mortgage Corporation Discount Notes	67,659,598	67,660,000	67,660,000	0.070 - 0.100%	7/2/12 - 7/6/12
	<u>\$ 5,822,168,834</u>	<u>\$ 5,822,097,379</u>	<u>\$ 5,821,610,787</u>		

Custodial Credit Risk: Custodial credit risk for deposits and investments is the risk that, in the event of a financial institution failure, The Illinois Funds would not be able to recover the value of the deposits and investments in the possession of an outside party. The Office of the Treasurer has a formal policy to address custodial risk.

Repurchase agreements are purchased from various brokerage firms and financial institutions. Securities pledged as collateral to secure these agreements are required to have a fair value of at least 102% of the agreement. The agreements require both parties to maintain an acceptable margin (yield) on underlying securities to ensure that the agreements are adequately collateralized. The Treasurer accepts only U.S. agency obligations and U.S. Treasury obligations as collateral for repurchase agreements. All securities pledged to secure repurchase agreements are required to be delivered to the appointed Custodian of The Illinois Funds.

Other instruments, such as U.S. Treasury obligations, may be purchased from various brokerage firms and are held in safekeeping by the appointed Custodian of The Illinois Funds.

**State of Illinois
Office of the Treasurer
The Illinois Funds**

Notes to the Financial Statements

Note 2. Deposits and Investments (Continued)

Investments: The Illinois Funds had the following investments, stated at carrying value, and maturities as of June 30, 2013 and 2012. (Amounts are in thousands.)

	2013					2012				
	Thirty Days or Less	Thirty One to Ninety Days	Ninety One Days to One Year	One to Two Years	Total	Thirty Days or Less	Thirty One to Ninety Days	Ninety One Days to One Year	Total	
Repurchase agreements	\$ 2,350,020	\$ -	\$ -	\$ -	\$ 2,350,020	\$ 3,150,026	\$ -	\$ -	\$ 3,150,026	
Commercial paper	741,987	499,846	149,929	-	1,391,762	1,259,970	499,816	-	1,759,786	
U.S. Treasury obligations	275,014	225,044	501,622	50,234	1,051,914	-	225,023	125,748	350,771	
U.S. agency obligations	303,248	124,989	124,934	-	553,171	92,659	-	224,976	317,635	
Subtotal	<u>\$ 3,670,269</u>	<u>\$ 849,879</u>	<u>\$ 776,485</u>	<u>\$ 50,234</u>	<u>5,346,867</u>	<u>\$ 4,502,655</u>	<u>\$ 724,839</u>	<u>\$ 350,724</u>	<u>5,578,218</u>	
Treasury-only money market mutual funds					498,404				243,951	
Investments					<u>\$ 5,845,271</u>				<u>\$ 5,822,169</u>	

The master repurchase agreements utilized by The Illinois Funds require the broker or financial institution to maintain the fair value of collateral securities at 102% of the agreement. The carrying amount of the repurchase agreements (excluding accrued interest) was \$2,350,000,000 and \$3,150,000,000 as of June 30, 2013 and 2012, respectively. The fair value, including accrued interest, of the underlying securities to be resold based on commitments under the repurchase agreements was \$2,409,564,255 and \$3,213,008,186 as of June 30, 2013 and 2012, respectively.

Interest Rate Risk: Interest Rate risk is the risk that changes in the interest rates will adversely affect the fair value of an investment. As a means of limiting its exposure to fair value losses arising from rising interest rates, the investment policies limit the investment portfolio maturities. The Illinois Funds investment policy limits its investment portfolio to maturities not to exceed two years with a minimum of 75% required to be in authorized investments with less than one-year maturity. The investment policy specifically requires that no more than 50% of total assets can be invested in securities with maturities greater than 30 days issued by any single permissible United States government agency or instrumentality. The Treasurer's Office uses the segmented time distribution method to identify and manage interest rate risk.

**State of Illinois
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Notes to the Financial Statements

Note 2. Deposits and Investments (Continued)

Credit Risk: Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. As of June 30, 2012, The Illinois Funds' investments in U.S. Agencies, including collateral for repurchase agreements were rated AA+ by Standard & Poor's Ratings or Aaa by Moody's Investors Service with the exception of Federal Agricultural Mortgage Corporation obligations which were not rated. The Illinois Funds' investments in commercial paper were rated P-1 by Moody's Investors Services and A-1 by Standard & Poor's Ratings, except for those issued by General Electric Capital which were rated A-1+ by Standard & Poor's Ratings, and those issued by RBS securities which were rated P-2 by Moody's Investors Service. The Illinois Funds' investments in money market mutual funds were rated Aaa by Moody's Investors Service and AAAM by Standard & Poor's Ratings.

As of June 30, 2013, The Illinois Funds' investments in U.S. Agencies, including collateral for repurchase agreements were rated AA+ by Standard & Poor's Ratings or Aaa by Moody's Investors Service. The Illinois Funds' investments in commercial paper were rated P-1 by Moody's Investors Service and A-1 by Standard and Poor's Ratings, except for those issued by Prudential Funding which were rated A-1+ by Standard and Poor's Ratings and P-2 by Moody's Investors Service. The Illinois Funds' investments in money market mutual funds were rated Aaa by Moody's Investors Service or AAAM by Standard & Poor's Ratings.

Concentration of Credit Risk: Concentration of credit risk is the risk of loss attributed to the magnitude of The Illinois Funds' investment in a single issuer. The following investments exceeded 5% of The Illinois Funds' total investments at June 30, 2013 and 2012. (Amounts are in thousands.)

	2013		2012	
	Carrying Value	% of Total Investments	Carrying Value	% of Total Investments
Repurchase agreements				
Bank of Montreal	\$ 300,002	5.13 %	\$ 1,150,011	19.75 %
HSBC*	1,500,013	25.66	1,200,009	20.61
Barclay's*	-	-	250,002	4.29
Merrill Lynch	-	-	400,003	6.87
RBS	300,003	5.13	-	-
U.S. Agency				
Federal Home Loan Bank	314,213	5.38	-	-
Commercial Paper				
Barclay's*	-	-	249,999	4.29
HSBC*	99,969	1.71	249,995	4.29

*Issuer total exceeds 5%

No more than 5% of total assets can be invested in securities issued by any single commercial paper issuer (calculated at the time of purchase); and, a maximum of 33.3% of the portfolio may be invested in direct commercial paper obligations that do not exceed 180 days to maturity. Additionally, a maximum of 25% of the total assets may be invested in any approved AAAM Money Market Fund.

**State of Illinois
Office of the Treasurer
The Illinois Funds**

Notes to the Financial Statements

Note 3. Investment Income

The Illinois Funds follows the accounting practice known as equalization. Accordingly, distributable investment income is allocated daily and paid monthly to participants on a pro rata (per share) basis and accumulated investment income payable is credited to The Illinois Funds' net asset base. A portion of the proceeds from sales and costs of repurchases of The Illinois Funds' capital shares (equivalent, on a per share basis, to the amount of distributable investment income on the date of the transaction) are credited or charged to undistributed income. As a result, undistributed investment income per share is unaffected by sales or redemptions of The Illinois Funds capital shares.

Periodically, throughout the fiscal year, market conditions may enable The Illinois Funds to realize capital gains by selling securities, which have appreciated in value. These gains are placed in a separate account within The Illinois Funds' portfolio. These gains may be distributed to participants during the fiscal year based on average daily account balances. During fiscal years 2013 and 2012, there were none of these sales.

Note 4. Administrative Fees

To administer The Illinois Funds, the Treasurer has established a division entitled "The Illinois Funds' Administrative Office." This division had 21 and 23 average full time equivalent employees for the years ended June 30, 2013 and 2012, respectively. The revenues and expenditures of the division are recorded in an enterprise fund maintained by the Treasurer entitled The Illinois Funds' Administrative Trust Fund No. 195.

US Bank (USB) performs the custodial responsibilities for the administration of The Illinois Funds. USB calculates the administrative and custodial fees paid to the State Treasurer and USB, respectively.

Fees are calculated on a tiered structure. Both fees are paid from a charge based on the net asset value of The Illinois Funds. The fee is accrued daily and withdrawn monthly from the fund. The custodian's fee is calculated at 0.0395% for the first \$3,000,000,000; 0.0245% for the next \$2,000,000,000; 0.0235% for the next \$1,000,000,000; 0.0185% for the next \$4,000,000,000; and 0.0135% for the amount over \$10,000,000,000 per annum of the market value of the total amount of The Illinois Funds.

The State Treasurer received 0.05% per annum of the net asset value of The Illinois Funds. This fee is used to defray administrative costs associated with investing The Illinois Funds' assets, to increase marketing efforts needed to expand participation in The Illinois Funds, and to improve the level of service to participants.

The Treasurer's Office has the ability to rebate to The Illinois Funds' participants any excess administrative fees collected during the fiscal year. There were no excess administrative fees rebated to The Illinois Funds' participants during fiscal years 2013 and 2012.

**State of Illinois
Office of the Treasurer
The Illinois Funds**

Notes to the Financial Statements

Note 4. Administrative Fees (Continued)

The Treasurer received fees and paid expenditures from the Administrative Trust Fund No. 195 as follows:

	<u>2013</u>	<u>2012</u>
Fees received	\$ 2,818,000	\$ 2,883,000
Expenditures	3,092,000	2,878,000

Note 5. Related Parties

The Illinois Funds' Administrative Office, a division of the State Treasurer's Office, is responsible for the administration of The Illinois Funds, including management of investments and marketing services. The Illinois Funds' Administrative Office received fees as stated in Note 4 during fiscal years 2013 and 2012, respectively. The Illinois Funds' Administrative Trust Fund No. 195 was maintained by the Treasurer in a separate investment account of The Illinois Funds. The cash balance at June 30, 2013 and 2012, was approximately \$2,952,000 and \$3,153,000, respectively.

The State of Illinois, its agencies, and its universities invest in The Illinois Funds. The detail follows:

	<u>2013</u>	<u>2012</u>
Total number of participants	2,268	2,285
Number of State of Illinois participants	31	31
Balance of State of Illinois investments	\$ 1,794,407,765	\$ 1,722,887,260

SUPPLEMENTARY INFORMATION

**State of Illinois
Office of the Treasurer**

**The Illinois Funds
Portfolio of Investments
June 30, 2013**

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	Execution Date	Interest Rate	Maturity Date	Face Amount	Current Value*
Repurchase Agreements					
BANK OF MONTREAL	06/28/2013	0.080%	07/01/2013	\$ 300,000,000	\$ 300,002,000
HSBC SECURITIES	06/28/2013	0.110%	07/01/2013	1,200,000,000	1,200,011,000
HSBC SECURITIES	06/28/2013	0.080%	07/01/2013	300,000,000	300,002,000
MERRILL LYNCH	06/28/2013	0.080%	07/01/2013	250,000,000	250,001,667
RBS SECURITIES	06/28/2013	0.120%	07/01/2013	300,000,000	300,003,000
Total Repurchase Agreements				<u>\$ 2,350,000,000</u>	<u>\$ 2,350,019,667</u>

**State of Illinois
Office of the Treasurer**

**The Illinois Funds
Portfolio of Investments (Continued)
June 30, 2013**

	Execution Date	Effective Yield	Maturity Date	Fair Value**	Amortized Cost
Commercial Paper					
ABN AMRO FUNDING	05/28/13	0.162%	07/08/13	\$ 249,992,500	\$ 249,992,222
HSBC USA INC	05/30/13	0.193%	08/28/13	99,968,000	99,969,389
JP MORGAN CHASE	03/22/13	0.183%	07/02/13	100,000,000	99,999,500
JP MORGAN CHASE	06/06/13	0.183%	10/04/13	149,901,000	149,928,750
MIZUHO FUNDING	06/03/13	0.213%	09/03/13	249,902,500	249,906,666
PEPSICO INC	06/28/13	0.071%	07/26/13	41,994,960	41,997,958
PRUDENTIAL FUNDING	06/07/13	0.132%	07/08/13	99,997,000	99,997,472
UBS FINANCE DELAWARE	06/26/13	0.132%	08/26/13	149,953,500	149,969,667
US BANCORP	06/05/13	0.120%	07/03/13	250,000,000	250,000,000
				<u>\$ 1,391,709,460</u>	<u>\$ 1,391,761,624</u>
Total Commercial Paper					

**State of Illinois
Office of the Treasurer**

**The Illinois Funds
Portfolio of Investments (Continued)
June 30, 2013**

	<u>Cost</u>
Money Market Mutual Funds	
Milestone Money Market Fund	\$ 11,081,485
First American Government Sweep	14,075,021
Goldman Government Fund #465	96,398,225
Western Asset Instl Gov't	155,000,000
Morgan Stanley Gov't Inst	151,235,675
AIM Government & Agency Portfolio	70,613,939
	<hr/>
Total Money Market Mutual Funds	<u><u>\$ 498,404,345</u></u>

**State of Illinois
Office of the Treasurer**

**The Illinois Funds
Portfolio of Investments (Continued)
June 30, 2013**

	Execution Date	Effective Yield	Maturity Date	Fair Value**	Amortized Cost
United States Treasury Obligations					
U.S. Treasury Bills					
Treasury Bills	03/20/13	0.075%	07/05/13	\$ 50,000,000	\$ 49,999,583
Treasury Bills	06/10/13	0.037%	07/05/13	50,000,000	49,999,795
Treasury Bills	06/10/13	0.037%	07/05/13	50,000,000	49,999,797
Treasury Bills	06/28/13	0.009%	07/05/13	50,000,000	49,999,947
Treasury Bills	02/07/13	0.098%	07/25/13	24,999,750	24,998,375
Treasury Bills	02/07/13	0.098%	08/01/13	24,999,500	24,997,890
Treasury Bills	03/28/13	0.105%	09/26/13	49,995,500	49,987,313
Total U.S. Treasury Bills				<u>\$ 299,994,750</u>	<u>\$ 299,982,700</u>
U.S. Treasury Notes					
Treasury Notes	12/28/12	0.123%	07/15/13	\$ 50,017,500	\$ 50,016,937
Treasury Notes	12/17/12	0.136%	07/31/13	100,023,000	100,019,810
Treasury Notes	01/24/13	0.121%	08/15/13	50,041,000	50,039,072
Treasury Notes	12/10/12	0.183%	09/30/13	25,002,000	24,996,400
Treasury Notes	12/10/12	0.178%	09/30/13	25,002,000	24,996,702
Treasury Notes	12/07/12	0.188%	10/15/13	25,028,250	25,022,543
Treasury Notes	12/10/12	0.190%	10/15/13	25,028,250	25,022,428
Treasury Notes	12/07/12	0.189%	10/31/13	25,012,750	25,005,077
Treasury Notes	12/11/12	0.192%	10/31/13	25,012,750	25,004,775
Treasury Notes	12/07/12	0.200%	11/15/13	50,072,000	50,055,824
Treasury Notes	01/24/13	0.155%	11/15/13	25,036,000	25,032,047
Treasury Notes	01/24/13	0.169%	01/15/14	50,236,500	50,223,507
Treasury Notes	05/21/13	0.119%	02/28/14	25,018,500	25,021,824
Treasury Notes	05/29/13	0.115%	02/28/14	25,018,500	25,022,452
Treasury Notes	05/21/13	0.135%	04/15/14	25,212,000	25,219,879

(Continued)

State of Illinois
Office of the Treasurer

The Illinois Funds
Portfolio of Investments (Continued)
June 30, 2013

	Execution Date	Effective Yield	Maturity Date	Fair Value**	Amortized Cost
U.S. Treasury Notes (Continued)					
Treasury Notes	05/31/13	0.136%	04/15/14	\$ 25,212,000	\$ 25,219,692
Treasury Notes	05/31/13	0.137%	04/30/14	25,016,500	25,360,988
Treasury Notes	06/10/13	0.144%	04/30/14	25,351,500	25,022,011
Treasury Notes	05/21/13	0.133%	05/15/14	25,176,750	25,188,860
Treasury Notes	05/29/13	0.138%	05/15/14	25,176,750	25,187,814
Treasury Notes	06/26/13	0.170%	05/31/14	25,014,750	25,018,364
Treasury Notes	06/19/13	0.158%	07/15/14	25,109,500	25,121,220
Treasury Notes	06/26/13	0.190%	07/15/14	25,109,500	25,112,843
Total U.S. Treasury Notes				<u>\$ 751,928,250</u>	<u>\$ 751,931,069</u>
United States Agency Obligations***					
Federal Home Loan Mtg Corp Discount Notes					
Federal Home Loan Mtg Corp Discount Notes	06/12/13	0.045%	07/08/13	\$ 14,000,000	\$ 13,999,878
Federal Home Loan Mtg Corp Discount Notes	03/20/13	0.090%	07/16/13	24,999,750	24,999,062
Federal Home Loan Mtg Corp Discount Notes	05/30/13	0.090%	10/22/13	24,996,000	24,992,938
Federal Home Loan Mtg Corp Discount Notes	05/30/13	0.100%	01/22/14	24,985,750	24,985,764
Total Federal Home Loan Mtg Corp Discount Notes				<u>\$ 88,981,500</u>	<u>\$ 88,977,642</u>
Federal Home Loan Bank Discount Notes					
Federal Home Loan Bank Discount Notes	06/13/13	0.055%	07/03/13	\$ 25,000,000	\$ 24,999,924
Federal Home Loan Bank Discount Notes	06/19/13	0.040%	07/03/13	25,000,000	24,999,944
Federal Home Loan Bank Discount Notes	06/11/13	0.045%	07/08/13	50,000,000	49,999,563
Federal Home Loan Bank Discount Notes	06/12/13	0.045%	07/08/13	14,252,000	14,251,875
Federal Home Loan Bank Discount Notes	06/14/13	0.055%	07/12/13	24,999,750	24,999,580
Federal Home Loan Bank Discount Notes	05/17/13	0.050%	07/17/13	24,999,750	24,999,444
Federal Home Loan Bank Discount Notes	05/17/13	0.050%	07/19/13	24,999,750	24,999,375
Federal Home Loan Bank Discount Notes	06/24/13	0.060%	08/01/13	49,998,500	49,997,417
Federal Home Loan Bank Discount Notes	06/20/13	0.075%	08/21/13	24,999,000	24,997,344
Federal Home Loan Bank Discount Notes	06/24/13	0.085%	08/23/13	24,999,000	24,996,871
Federal Home Loan Bank Discount Notes	05/30/13	0.140%	04/14/14	24,974,000	24,972,097
Total Federal Home Loan Bank Discount Notes				<u>\$ 314,221,750</u>	<u>\$ 314,213,434</u>

(Continued)

**State of Illinois
Office of the Treasurer**

**The Illinois Funds
Portfolio of Investments (Continued)
June 30, 2013**

	Execution Date	Effective Yield	Maturity Date	Fair Value**	Amortized Cost
Federal Farm Credit Bank Discount Notes					
Federal Farm Credit Bank Discount Notes	06/24/13	0.050%	07/16/13	\$ 24,999,750	\$ 24,999,479
Federal Farm Credit Bank Discount Notes	06/20/13	0.070%	08/15/13	24,999,000	24,997,813
Total Federal Farm Credit Bank Discount Notes				<u>\$ 49,998,750</u>	<u>\$ 49,997,292</u>
Federal National Mortgage Association Discount Notes					
Federal National Mortgage Association Discount Notes	01/25/13	0.100%	07/02/13	\$ 25,000,000	\$ 24,999,930
Federal National Mortgage Association Discount Notes	06/10/13	0.040%	07/10/13	24,999,750	24,999,750
Federal National Mortgage Association Discount Notes	05/23/13	0.090%	11/06/13	24,993,750	24,992,000
Federal National Mortgage Association Discount Notes	05/23/13	0.095%	11/13/13	24,993,500	24,991,094
Total Federal National Mortgage Association Discount Notes				<u>\$ 99,987,000</u>	<u>\$ 99,982,774</u>

* Current value represents the face amount plus accrued interest, which approximates fair value.

** Fair value represents the closing bid price on June 30, 2013.

*** It is the intent of management to hold direct U.S. Agency Securities to maturity unless market conditions provide for realization of a gain and management determines a sale would be in the best interest of The Illinois Funds.

**State of Illinois
Office of the Treasurer**

**The Illinois Funds
Condensed Statement of Fiduciary Net Position by Investor Type and
Condensed Statement of Changes in Fiduciary Net Position by Investor Type
June 30, 2013
(Dollars in thousands)**

CONDENSED STATEMENT OF FIDUCIARY NET POSITION BY INVESTOR TYPE
June 30, 2013

	Total	Internal	External
Assets			
Cash equivalents	\$ 4,268,588	\$ 1,310,151	\$ 2,958,437
Deposits and investments	1,576,682	483,928	1,092,754
Interest receivable	1,403	430	973
	5,846,673	1,794,509	4,052,164
Liabilities			
Bank fees	151	46	105
Management fees	180	55	125
Net position	<u>\$ 5,846,342</u>	<u>\$ 1,794,408</u>	<u>\$ 4,051,934</u>

CONDENSED STATEMENT OF CHANGES IN FIDUCIARY
NET POSITION BY INVESTOR TYPE
Year Ended June 30, 2013

	Total	Internal	External
Participant deposits	\$ 18,566,416	\$ 11,637,254	\$ 6,929,162
Interest and other investment income	9,110	2,823	6,287
Investment expense	(4,680)	(1,436)	(3,244)
Redemptions	(18,542,576)	(11,565,964)	(6,976,612)
Dividends to shareholders	(4,430)	(1,157)	(3,273)
Change in net position and shares	23,840	71,520	(47,680)
Beginning net position	5,822,502	1,722,888	4,099,614
Ending net position	<u>\$ 5,846,342</u>	<u>\$ 1,794,408</u>	<u>\$ 4,051,934</u>

**State of Illinois
Office of the Treasurer**

**The Illinois Funds
Money Market Fund Investment Policy
For the Year Ended June 30, 2013
(Unaudited)**

1.0 Policy: The State Treasurer of Illinois (“Treasurer”) has authority under Section 17 of the State Treasurer’s Act (15 ILCS 505/17) to establish and administer an investment pool to supplement and enhance investment opportunities otherwise available to managers of public funds or public agencies in the state. It is the policy of the Treasurer to invest funds pooled by local governments in the Money Market Fund within The Illinois Funds (previously referred to as the Illinois Public Treasurers' Investment Pool or IPTIP) in a manner which will provide the highest investment return using authorized instruments, while meeting the daily cash flow demands of participants and conforming to all state statutes governing the investment of public funds. It is the policy of The Illinois Funds to operate in a manner consistent with SEC Rule 2a7.

2.0 Objective: The primary objective in the investment of funds within the Money Market Fund is the safety of principal, while providing all participants a competitive rate of return and daily access to invested funds.

2.1 Safety: The safety of principal is the foremost objective of the investment program. Money Market Fund investments shall be undertaken in a manner, which seeks to ensure the preservation of principal in the portfolio. To obtain this objective, diversification among permissible investments is required to ensure that the Money Market Fund properly manages market, interest rate and credit risk.

2.2 Liquidity: The investment portfolio shall remain sufficiently liquid to enable the Money Market Fund to meet all Participant redemption demands that might be reasonably anticipated.

2.3 Return on Investment: The investment portfolio shall be designed to obtain the highest available return, taking into account the Money Market Fund's investment risk constraints and cash flow needs. The Treasurer will select accepted industry benchmarks which best reflects the Money Market Fund's portfolio and measure performance against certain benchmarks over time. The Treasurer will periodically review benchmarks for suitability.

3.0 Ethics and Conflicts of Interest: Authorized investment staff and employees in policy making positions for the Money Market Fund shall refrain from personal business activity that conflicts with proper execution of the investment program, or which impairs their ability to make impartial investment decisions. Such individuals shall disclose to the Treasurer any material financial interests in financial institutions or broker/dealers that conduct business within the State. They shall further disclose any personal investments that are related to the performance of the Money Market Fund's portfolio. In addition, such individuals shall subordinate their personal investment transactions to those of the Money Market Fund, particularly with regard to the time of purchase and sales.

4.0 Authorized Broker/Dealers and Financial Institutions: Authorized investment staff shall utilize the Treasurer's approved list of broker/dealers and financial institutions when selecting institutions to provide investment services. No monies may be deposited in any financial institution until investment officers have conducted a safety and soundness review of the financial institution by consulting various bank rating services, unless the financial institution has not yet been rated by the bank rating services, in which case the institution may be eligible for a deposit that at maturity will not exceed \$100,000. The amount and duration of deposits shall be based on the safety and soundness review in accordance with guidelines established by the Investment Policy Committee and the diversification limits set forth in Section 9.0. No public deposit may be made except in a qualified public depository as defined by the Deposit of State Moneys Act (15 ILCS 520). In addition, a list shall also be maintained of approved security broker/dealers selected according to their credit worthiness, and their financial significance in the

**State of Illinois
Office of the Treasurer**

**The Illinois Funds
Money Market Fund Investment Policy
For the Year Ended June 30, 2013
(Unaudited)**

State, which shall be measured in terms of the location of the broker/dealer's corporate office and the extent to which the broker/dealer has a large labor or economic impact on the State. They may include "primary" dealers or regional dealers that qualify under Securities and Exchange Commission Rule 15C3-1 (uniform net capital rule).

All brokers/dealers interested in becoming qualified parties for investment transactions must supply the Treasurer's authorized investment staff with the following or equivalent acceptable to the Treasurer, where applicable:

- Audited financial statements or a published Statement of Condition;
- Proof of minority/female/disabled broker status;
- A signed copy of the Treasurer's trading authorization;
- Proof of National and State of Illinois registration;
- Completed Broker/Dealer Questionnaire;
- Certification of notice and knowledge of this Policy;
- Any other documentation determined necessary by the Treasurer.

An annual review of the financial condition and registration of qualified parties and investments will be conducted by the Treasurer's authorized investment staff. More frequent reviews may be conducted.

5.0 Authorized and Suitable Investments: The following investments are permitted investments of state funds according to the Deposit of State Moneys Act (15 ILCS 520/22.5) and the Public Funds Investment Act (30 ILCS 235/2) and are authorized to the extent they are approved by Standard & Poor's for AAAM rated funds:

- In bonds, notes, certificates of indebtedness, treasury bills or other securities now or hereafter issued, which are guaranteed by the full faith and credit of the United States of America as to principal and interest; Public Funds Investment Act (30 ILCS 235/2) & Deposit of State Moneys Act (15 ILCS 520/22.5).
- In bonds, notes, debentures, or similar obligations of the United States of America or its agencies; Public Funds Investment Act (30 ILCS 235/2) & Deposit of State Moneys Act (15 ILCS 520/22.5).
- Repurchase agreements of government securities having the meaning set out in the Government Securities Act of 1986 subject to the provisions of that Act and the regulations issues thereunder; Public Funds Investment Act (30 ILCS 235/2) & Deposit of State Moneys Act (15 ILCS 520/22.5).
- In short term obligations of corporations organized in the United States with assets exceeding \$500,000,000 if (i) such obligations are rated at the time of purchase at one of the 2 highest classifications established by at least 2 standard rating services and which mature not later than 180 days from the date of purchase, (ii) such purchases do not exceed 10% of the corporations outstanding obligations, and (iii) no more than one-third of the public agency's funds may be invested in short term obligations of corporations and (iv) the corporation is not a forbidden entity as defined in Section 22.6 of the Deposit of State Moneys Act (effective Jan 27, 2006); Public Funds Investment Act (30 ILCS 235/2) and Deposit of State Moneys Act (15 ILCS 520/22.5).

**State of Illinois
Office of the Treasurer**

**The Illinois Funds
Money Market Fund Investment Policy
For the Year Ended June 30, 2013
(Unaudited)**

- In money market mutual funds registered under the Investment Company Act of 1940, provided the portfolio of any such money market mutual fund is limited to United States Treasury and United States Agency Securities and agreements to repurchase such obligations provided the funds are rated AAA; Public Funds Investment Act (30 ILCS 235/2) & Deposit of State Moneys Act (15 ILCS 520/22.5).
- Bonds, notes, debentures, or similar obligations of a foreign government, other than the Republic of Sudan (effective Jan 27, 2006), that are guaranteed by the full faith and credit of that government as to principal and interest, but only if the foreign government has not defaulted and has met its payment obligations for a period of at least 25 years immediately before the time of acquiring those obligations; Deposit of State Moneys Act (15 ILCS 520/22.5).
- Bonds issued by counties or municipal corporations of the State of Illinois; Deposit of State Moneys Act (15 ILCS 520/22.5).
- Interest bearing savings accounts, interest-bearing certificates of deposits or interest-bearing time deposits or any other investments constituting direct obligations of any bank as defined by the Illinois Banking Act (205 ILCS 5/1 et seq.); Public Funds Investment Act (30 ILCS 235/2) & Deposit of State Moneys Act (15 ILCS 520/22.5)

Suitable securities in the Money Market Funds portfolio may be lent in accordance with the Federal Financial Institution Examination Council Guidelines.

6.0 Investment Restrictions: The following restrictions will apply to all Money Market Fund investment transactions:

- Investments in derivative products and leveraging of assets through reverse repurchase agreements are prohibited.
- Repurchase agreements may only be executed with financial institutions or broker/dealers meeting the Treasurer's standards, which will include mutual execution of a Master Repurchase Agreement adopted by the Treasurer.
- There will be no investments in mortgage-backed securities of any kind.
- There will be no investments in asset-backed securities of any kind.
- Certificates of deposit may not be purchased from the Money Market Fund's custodial institution or any of its subcontractors.
- Investments in Bankers' Acceptances of any kind.
- There will be no investments prohibited by Section 22.6 of the Deposit of State Moneys Act (effective Jan. 27, 2006).

**State of Illinois
Office of the Treasurer**

**The Illinois Funds
Money Market Fund Investment Policy
For the Year Ended June 30, 2013
(Unaudited)**

7.0 Collateralization: All Money Market Fund deposits and repurchase agreements shall be secured by direct U.S. Treasury and/or U.S. Agency obligations as required by the Treasurer and provided for by the Deposit of State Moneys Act (15 ILCS 520) and the Treasurer's Acceptable Collateral Listing, which may change from time to time.

8.0 Safekeeping and Custody: All direct treasury, agency and instrumentality security transactions entered into by the Money Market Fund shall be conducted on a delivery-versus-payment ("DVP") or receipt-versus-payment ("RVP") basis. Securities shall be held by a safekeeping agent designated by the Treasurer, and evidenced by safekeeping receipts. Commercial Paper will settle daily with the Depository Trust Company.

9.0 Diversification: The primary purpose of diversification in general is to control credit and market risk. The Money Market Fund portfolio will be diversified to eliminate the risk of loss resulting from concentration of assets in a specific maturity, a specific issuer or a specific class of securities. The majority of Money Market Fund investments will be in direct obligations of the United States Treasury and United States Government Agencies and Instrumentalities and Cash Equivalents as listed in section 5.0. In order to properly manage any risk that may be attendant to the investment of Money Market Fund assets, The Money Market Fund portfolio will observe the following diversification limits, at the time of purchase:

- The Money Market Fund will invest no more than 50 percent of its total assets in securities with maturities greater than 30 days issued by any single permissible United States Government Agency or Instrumentality.
- The Money Market Fund will invest no more than 5 percent of its total assets in securities issued by any single Commercial Paper Issuer (calculated at the time of purchase).
- A maximum of 33.3 percent of the portfolio may be invested in direct Commercial Paper Obligations not to exceed 180 days to maturity.
- A maximum of 25 percent of total assets may be invested in any approved AAAm Money Market Fund.
- The Money Market Fund will seek to achieve diversification in the portfolio by reasonably distributing investments within authorized investment categories, issuers and broker/dealers.
- The Money Market Fund shall at no time hold certificates of deposit constituting more than 10 percent of any single financial institution's total deposits.
- The Money Market Fund shall invest a minimum of 75% of its assets in authorized investments of less than one-year maturity. No investment shall exceed two years maturity.

10.0 Internal Controls: The Treasurer shall establish a system of internal controls, which shall be documented in writing and filed with the Treasurer's Chief Internal Auditor for review. The controls shall be designed to prevent losses of public funds arising from fraud, employee error, and misrepresentation by third parties, unanticipated changes in financial markets or imprudent actions by authorized investment staff of the Money Market Fund. The Treasurer shall publish the current investment policy on the Illinois Funds website and in accordance with the statutes.

**State of Illinois
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**The Illinois Funds
Money Market Fund Investment Policy
For the Year Ended June 30, 2013
(Unaudited)**

11.0 Asset Allocation: The Treasurer shall approve asset allocation among investment categories authorized under Section 5.0 of this Investment Policy.

12.0 Competitive Bidding: Authorized investment staff shall obtain competitive bids from at least three broker/dealers prior to executing repurchase agreements, purchasing United States Treasury securities, United States Government Agency or Instrumentality securities or Commercial Paper from a broker/dealer. Reverse inquiry investments and investments in a new issue are exempt from this provision. Certificates of deposit shall be purchased by authorized investment staff on the basis of a financial institution's ability to pay the Treasurer's required interest rate.

13.0 Liability: Authorized investment staff, acting in accordance with written procedures and this investment policy and exercising due diligence, shall be relieved of personal responsibility for an individual security's credit risk or market price changes, provided deviations from expectations are reported in a timely fashion and appropriate action is taken to control adverse developments. The Treasurer is bonded to a level of \$150,000 for the faithful performance of duties in relations to the Illinois Public Treasurers' Investment Pool.

14.0 Reporting: Reports shall be made available quarterly by the Director of The Illinois Funds to the Treasurer and The Illinois Funds' participants. The quarterly report shall contain the following:

- performance as compared to the established benchmark
- asset allocation
- any deviation from the standards established in Section 9.0 above
- any change in investment policy adopted during the quarter
- the average days to maturity

A listing of all investments in the portfolio marked to market shall be made available to the Treasurer and The Illinois Funds participants annually.

15.0 Emergency Powers: In the event of an emergency, the Treasurer may, at his or her discretion, invoke emergency powers and suspend any or all of the provisions of this policy provided that:

- a)** The Treasurer shall, even in the event that emergency powers are invoked, comply with all state statutes governing the use and investment of monies;
- b)** The Treasurer reasonably believes that deviating from the Investment Policy is in the best interest of the Participants;
- c)** Within 30 days of invoking emergency powers the Treasurer shall provide an explanation in writing to the Chief Internal Auditor and the Investment Policy Committee, a notice of which shall be posted on the Treasurer's website that includes:

**State of Illinois
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**The Illinois Funds
Money Market Fund Investment Policy
For the Year Ended June 30, 2013
(Unaudited)**

- i) The date and time that the emergency powers were invoked;
- ii) The date and time that the emergency powers were repealed, if occurred;
- iii) The section or sections of the Investment Policy that were affected by the emergency or use of emergency powers; and
- iv) The reason for deviating from the written Investment Policy.

16.0 All statutory references in this policy shall include any amendments to or repeals of those statutes.



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

The Honorable William G. Holland
Auditor General
State of Illinois

As Special Assistant Auditors for the Auditor General, we have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of The Illinois Funds, a fiduciary (investment trust) fund of the State of Illinois, Office of the Treasurer, as of and for the year ended June 30, 2013, and the related notes to the financial statements, and have issued our report thereon dated December 10, 2013.

Internal Control Over Financial Reporting

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

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

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

Compliance and Other Matters

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

Purpose of this Report

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

McGladrey LLP

Schaumburg, Illinois
December 10, 2013