

INTRODUCTORY SECTION

THE COMPREHENSIVE ANNUAL FINANCIAL REPORT
FOR FISCAL YEAR ENDED JUNE 30, 2010



Giving You Our Best

Maximizing staff potential through enhanced skills and new knowledge



A COMPONENT UNIT OF THE STATE OF ILLINOIS

Letter of Transmittal



State Universities Retirement System of Illinois

Serving Illinois Community Colleges and Universities

1901 Fox Drive • Champaign, IL 61820
1-800-ASK SURS • (217) 378-8800 (C-U)
(217) 378-9800 (FAX)

December 13, 2010

Board of Trustees and Executive Director
State Universities Retirement System
1901 Fox Drive
Champaign, IL 61820

I am pleased to present the 69th Comprehensive Annual Financial Report for the State Universities Retirement System of Illinois (SURS or the System, a component unit of the State of Illinois). This retirement system was created in 1941 by the State of Illinois for the benefit of the staff members and employees of the state universities, community colleges, and certain affiliated organizations, certain other state educational and scientific agencies, and the survivors, dependents, and other beneficiaries of those employees.

The management of SURS is responsible for the compilation and accuracy of the financial, investment, actuarial, and statistical information contained in this report. To the best of our knowledge and belief, the enclosed information is accurate in all material respects and is reported in a manner designed to present fairly the financial position and results of operations of SURS.

Accounting principles generally accepted in the United States of America require that management provide a narrative introduction, overview, and analysis to accompany the basic financial statements in the form of Management's Discussion and Analysis (MD&A). This letter of transmittal is designed to complement the MD&A and should be read in conjunction with it. The System's MD&A can be found immediately following the report of the independent auditors.

Summary of Financial Information

The following table summarizes the change in System's plan net assets available for benefits between fiscal years 2010 and 2009.

(\$ millions)

	2010	2009	Increase/(Decrease)	
			Amount	%
Additions	\$ 2,788.6	(\$ 2,155.1)	\$ 4,943.7	229.4
Deductions	1,553.7	1,441.0	112.7	7.8
Change	\$ 1,234.9	(\$ 3,596.1)	\$ 4,831.0	134.3

The overall increase of \$1.2 billion in net assets available for benefits is primarily due to an increase in additions of \$4.9 billion, composed of an increase in net investment income of \$4.7 billion and an increase in employer contributions of \$0.25 billion. Deductions in the form of benefit payments showed a relatively small increase of \$0.10 billion over the prior year. More detailed analysis can be found in the Financial Section of this report.

Letter of Transmittal

Funding

The State of Illinois, the largest employer covered by SURS, provides funding from three sources: the General Revenue Fund, the Educational Assistance Fund and the State Pensions Fund which is funded with proceeds from unclaimed property. The determination of the total employer contributions for fiscal year 2010 was based upon Public Act 88-0593, a funding plan which calls for increasing contributions between 1995 and 2010, and then sustaining contributions at a level which would result in a 90% funding ratio by 2045. In fiscal year 2010 state contributions were set at \$702.5 million, an increase of \$250 million from the prior year. In fiscal year 2010, the majority of the appropriations paid to the state pension systems was funded with the proceeds of the January 7, 2010 sale of \$3.466 billion in pension obligation notes, as required by Public Act 96-0043.

The actuarial accrued liability for the defined benefit plan at June 30, 2010 was \$30.1 billion as calculated by the projected unit credit method. The actuarial value of assets available for benefits at June 30, 2010, equaled \$14.0 billion. The amount by which the liability exceeds the assets is called the unfunded accrued actuarial liability, and it equaled \$16.1 billion at the end of fiscal year 2010. The System Board of Trustees authorized a change in the assumed rate of investment return from 8.5% to 7.75%, effective at June 30, 2010. It is expected that the growth in state contributions versus benefit payments will continue to result in a deficit of contributions over expenses, requiring the Board of Trustees to utilize investment assets to cover benefit payments as needed.

Investments

Investments are made under the authority of the prudent expert rule, which states that fiduciaries must discharge their duties with the care, skill, prudence, and diligence that a prudent person acting in a like capacity and familiar with such matters would use under conditions prevailing at the time. This standard has enabled the System to invest in different types of asset classes seeking to increase return while lowering risk through diversification.

Investment policy provides for a goal of 65% of the fund to be invested in equities, 28% of which may be invested in non-U.S. common stock and global equities, and 6% in private equities; 18% in fixed income; 10% in real estate investment trusts and direct real estate; 4% in treasury inflation-protected securities, and 3% in the Opportunity Fund. The System retains professional investment firms who serve as fiduciaries and are afforded full discretion to manage the assets entrusted to them in accordance with written policies and guidelines established by the Board of Trustees.

The majority of SURS investments are insured or collateralized with securities held by its agent except for mutual funds, which are not evidenced by securities that exist in physical or book entry form.

Yield information is detailed in the Investment Section of this report. Taken as a whole, the SURS portfolio of investments produced a return of 15%, net of fees, for the year ended June 30, 2010.

Subsequent to year end, the System has shown a positive return of 12.8% through October 31, 2010, bringing total investments to approximately \$13.3 billion.

Major Initiatives

The mission statement of SURS provides the foundation for the System's initiatives and ongoing programs. The mission of SURS is "To provide for SURS annuitants, participants, and their employers, in accordance with state law, the best and most cost effective benefit administration services in the United States, to manage and invest the fund's assets prudently, and to endeavor to achieve and maintain a financially sound retirement system."

Letter of Transmittal

Work continued during the year on various internet-based system application improvements and general operational refinements. Included in these was the migration to a new, server-based imaging system; the revision of the benefit payment system programming to incorporate the expanded opportunities for lump sum distributions including partial rollovers, Roth IRA rollovers, and rollovers by non-spouse beneficiaries; and the replacement of current direct insurance billing for certain annuitants with a direct debit feature.

Accounting System and Internal Control

SURS uses the accrual basis of accounting to record assets, liabilities, revenues, and expenses. Revenues for SURS are taken into account when earned, without regard to date of collection. Expenses are recorded when the corresponding liabilities are incurred, regardless of when payment is made. Market value has been used to present the assets of the System in accordance with Governmental Accounting Standards Board Statements #25 and #27, implemented effective July 1, 1996.

In developing and evaluating the accounting system, consideration has been given to the adequacy of internal accounting controls. These controls are designed to provide reasonable assurance regarding safekeeping of assets and reliability of financial records. SURS maintains an internal audit program that employs the services of two internal auditors to determine that all controls implemented are as designed.

Independent Audit

The Illinois Pension Code requires an annual audit of the financial statements of the System by independent public accountants, selected by the State Auditor General. This requirement has been complied with, and the independent auditors' unqualified report on the System's 2010 financial statements has been included in this report.

Certificate of Achievement for Excellence in Financial Reporting

The Government Finance Officers Association of the United States and Canada (GFOA) awarded a Certificate of Achievement for Excellence in Financial Reporting to SURS for its component unit financial report for the fiscal year ended June 30, 2009. This is the twenty sixth consecutive year the System has earned this award.

To be awarded the Certificate of Achievement, a governmental unit must publish an easily readable and efficiently organized comprehensive annual financial report whose contents conform to program standards. The report must satisfy both generally accepted accounting principles and applicable legal requirements. A Certificate of Achievement is valid for a period of one year only.

We believe our current report continues to conform to Certificate of Achievement Program requirements, and we are submitting it to GFOA to determine its eligibility for another certificate.

Appointment of Trustees

As of June 30, 2010, the composition of the SURS eleven-member Board of Trustees is as follows. Serving as active member-elected trustees are Mr. Jeffrey Beaulieu and Ms. Dorinda Miller who concluded the first year of their three-year terms, and Dr. J. Fred Giertz and Mr. Antonio Vasquez who concluded the first year of their six-year terms. Serving as annuitant-elected trustees are Dr. John Engstrom who concluded the first year of his three-year term and Mr. Mitchell Vogel who concluded the first year of his six-year term. Serving upon appointment by the Governor are Ms. Patricia Cassidy and Mr. Steven Rogers who concluded the first year of their three-year terms, and Mr. Matthew Berns and Dr. Marva Williams who concluded the first year of their six-year terms. As called for by Public Act 96-0006, the chairperson of the System Board of Trustees will be the appointed Chair of the Illinois Board of Higher Education, Ms. Carrie Hightman.

Letter of Transmittal

Acknowledgements

The preparation of the annual report by the Finance Division reflects the combined efforts of the SURS staff under the leadership of the Board of Trustees. It is intended for use by the Trustees and staff in making management decisions, in judging compliance with legal provisions, and in determining responsible stewardship for the assets contributed by System members and the State of Illinois. The report is made available to all employers covered by the State Universities Retirement System and is also available to members and other interested persons upon request.

On behalf of the Board of Trustees, I would like to express my gratitude to the staff, the consultants, and the many other people who work so effectively to assure the successful operation of this System.

Respectfully submitted,



Shelley M. Porter, CPA
Chief Financial Officer

Board of Trustees



Carrie J. Hightman
Chairwoman
Chicago



J. Fred Giertz
Champaign



Antonio Vasquez
Vice-Chairman
Chicago



Dorinda Miller
Urbana



Patricia Cassidy
Treasurer
Elmhurst



Steven Rogers
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Jeffrey Beaulieu
Carbondale



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Steven L. Hayward
CPA
Internal Auditor



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Associate Executive Director



Angela Lieb
Director of
Member Services



Daniel L. Allen
Chief Investment Officer



M. Christopher Hansen
Director of Operations



Douglas Wesley
Deputy Chief
Investment Officer

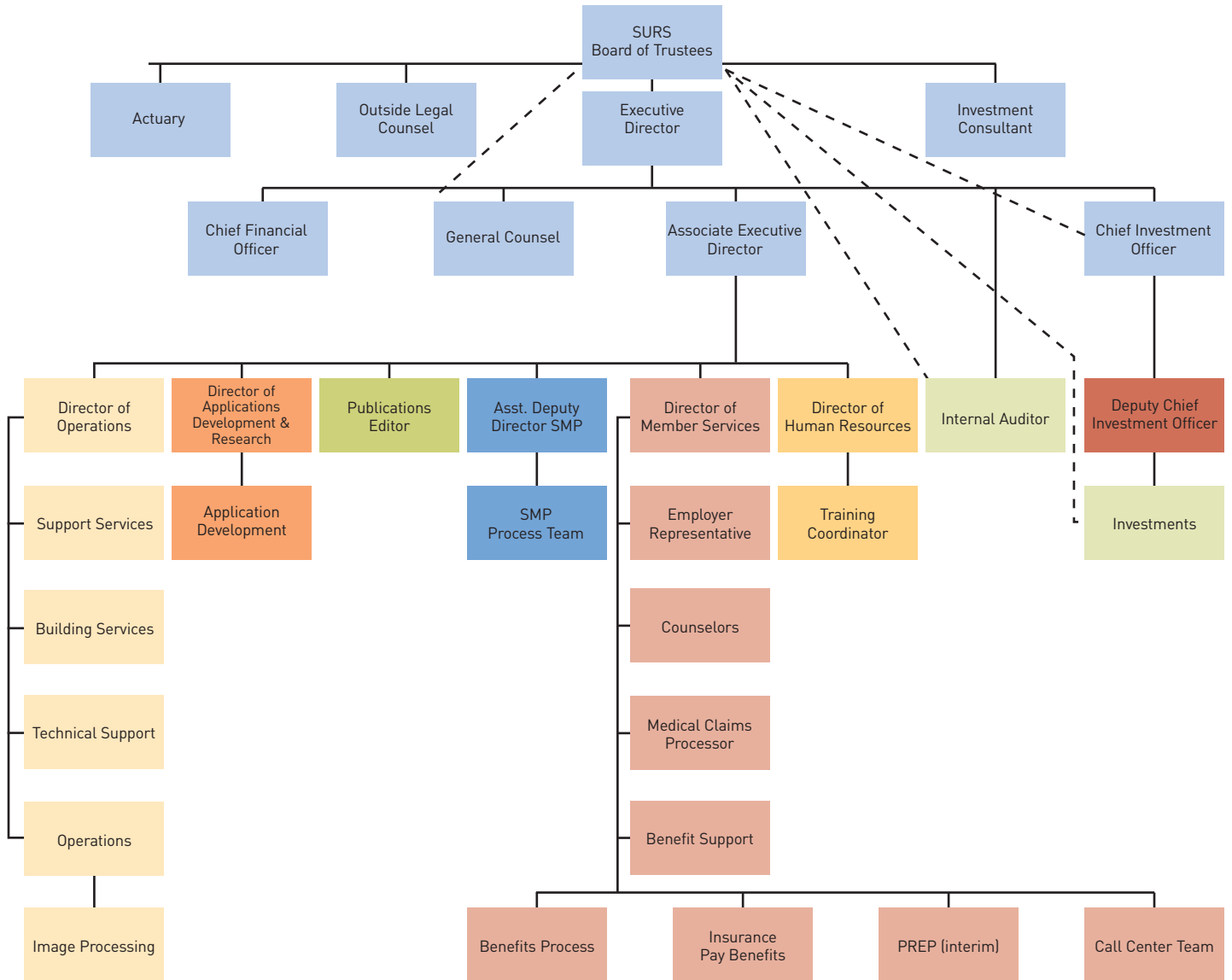


Douglas J. Steele
Director of Application
Development & Research



Shelley Porter
Chief Financial Officer

Organizational Chart



Consulting and Professional Services

Actuary

Gabriel, Roeder, Smith & Co.- Southfield, Michigan

Auditor

McGladrey & Pullen, LLP - Schaumburg, Illinois
(Acting as Special Assistant Auditor for the Illinois Office of the Auditor General)

Legal Counsel

Burke, Burns & Pinelli, Ltd. - Chicago, Illinois
Mayer Brown, LLP - Chicago, Illinois
Thomas, Mamer & Haughey - Champaign, Illinois

Information Systems

Champaign Systems, Inc. - Champaign, Illinois
MRC Information Technology, Inc. - Omaha, Nebraska
MIS Systems Integrators - Omaha, Nebraska

Master Custodian & Performance Measurement

The Northern Trust Company - Chicago, Illinois

Investment Consultant

EnnisKnupp + Associates, Inc. - Chicago, Illinois

Investment Advisors

Aberdeen Asset Management - Edinburgh, Scotland
Adams Street Partners - Chicago, Illinois
Alinda Capital Partners - New York, New York
Angelo Gordon GECC - New York, New York
BlackRock Financial Management - New York, New York
Calamos Advisors - Naperville, Illinois
Dune Capital Management - New York, New York
GlobeFlex Capital, L.P. - San Diego, California
ING Clarion Real Estate Securities - Radnor, Pennsylvania
Jacobs Levy Equity Management - Florham Park,
New Jersey
Macquarie Capital - New York, New York
Martin Currie, Inc. - Edinburgh, Scotland
Metropolitan West Asset Management - Los Angeles,
California
Mondrian Investment Partners - London, England
Muller and Monroe - Chicago, Illinois

Northern Trust Investments - Chicago, Illinois
Oaktree Capital Management - Los Angeles, California
Pacific Investment Management Company - Newport Beach, California
Pantheon Ventures - San Francisco, California
Payden & Rygel - Los Angeles, California
Piedmont Investment Advisors - Durham, North Carolina
Progress Investment Management Company - San Francisco, California
Pyramis Global Advisors Trust Company - Smithfield, Rhode Island
RhumbLine Advisers - Boston, Massachusetts
RLJ Western Asset Management - Bethesda, Maryland
RREEF - Chicago, Illinois
T. Rowe Price - Baltimore, Maryland
Taplin, Canida & Habacht - Miami, Florida
UBS Realty Investors - Hartford, Connecticut
Wellington Management Company - Boston, Massachusetts
Western Asset Management - Pasadena, California

Manager Development Program Investment Advisors

Ativo Capital Management - Chicago, Illinois
Buford, Dickson, Harper & Sparrow - St. Louis, Missouri
Channing Capital Management - Chicago, Illinois
Davis Hamilton Jackson & Associates - Houston, Texas
Herndon Capital Management - Atlanta, Georgia
Holland Capital Management - Chicago, Illinois
Lombardia Capital Partners - Pasadena, California

Longfellow Investment Management - Boston, Massachusetts
NCM Capital Management - Durham, North Carolina
New Century Advisors - Bethesda, Maryland
Profit Investment Management - Silver Spring, Maryland
Pugh Capital Management - Seattle, Washington
Smith Graham & Company - Houston, Texas
Strategic Global Advisors - Newport Beach, California

Progress Investment Management Company

Emerging Manager Investment Advisors

AH Lisanti Capital Growth - New York, New York
Ambassador Capital Management - Detroit, Michigan
Brown Capital Management - Baltimore, Maryland
Cheswold Lane Asset Management - West Conshohocken,
Pennsylvania
Davis Hamilton Jackson & Associates - Houston, Texas
Fortaleza Asset Management - Chicago, Illinois
Graham and Dodd Fund - New York, New York
GW Capital - Bellevue, Washington
Herndon Capital Management - Atlanta, Georgia
High Pointe Capital Management- Chicago, Illinois

Holland Capital Management - Chicago, Illinois
John Hsu Capital Group - New York, New York
LM Capital Group - San Diego, California
Mar Vista Investment Partners - Santa Monica, California
New Century Advisors - Bethesda, Maryland
Palisades Investment Partners - Santa Monica, California
Piedmont Investment Advisors - Durham, North Carolina
Redwood Investments - Newton, Massachusetts
Strategic Global Advisors - Newport Beach, California
Windsor Capital Management - Phoenix, Arizona

Self-Managed Plan Service Providers

Fidelity Investments - Boston, Massachusetts
Teachers Insurance Annuity Association - College
Retirement Equities Fund - New York, New York