# NOTES TO THE FINANCIAL STATEMENTS

# STATE OF INDIANA

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## (schedule amounts are expressed in thousands)

## I. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

### A. Reporting Entity

As required by generally accepted accounting principles, these financial statements present the government (State of Indiana) and its component units. Blended component units, although legally separate entities, are in substance part of the government's operations; data from these units are combined with data of the primary government. Discretely presented component units are reported in one column in the government-wide financial statements. This column contains the governmental fund types, proprietary fund types and colleges and universities. This is to emphasize that, as well as being legally separate from the government, they also provide services to and benefit local governments and/or the citizens of the State of Indiana. Of the component units, the Indiana Housing and Community Development Authority, Ports of Indiana, Indiana State Fair Commission, Indiana Comprehensive Health Insurance Association, and the Indiana Political Subdivision Risk Management Commission have a December 31, 2011, fiscal year-end.

*Blended Component Units*

The following component units are reported under the blended method as the primary government appoints a voting majority of the board and is able to impose its will. These units, although legally separate from the State, are reported as part of the State because they provide services entirely or almost entirely to the State. These component units are audited by the State Board of Accounts.

The Bureau of Motor Vehicle Commission (BMVC) was established by state law to develop and update Bureau of Motor Vehicles (BMV) policy, establish standards for the operation and maintenance of license branches, and submit budget proposals for the BMVC, BMV, and license branches. The BMVC has significant interrelated operations with the BMV and license branches. The BMV is responsible for the accurate and timely distribution of the fees and taxes (excise and wheel) collected at the license branches for driver licenses, auto and watercraft registrations, and license plates.

The BMVC consists of four individuals appointed by the governor and the chairperson who is the commissioner of the BMV. No more than three of the members may be of the same political party. The BMVC is reported as a non-major governmental fund.

The State Student Assistance Commission of Indiana (SSACI) was established by state law to assist the State in increasing the opportunities of higher education for every person who resides in Indiana and who, though being highly qualified and desiring to receive a higher education, is deterred by financial considerations. They provide data to the General Assembly to allow them to make educated policy decisions about financial aid. In addition, they assist the State in identifying which students qualify for financial aid enabling the State to efficiently distribute funds.

The SSACI consists of ten citizens appointed by the governor. Each of Indiana’s nine congressional districts must be represented by a resident of the district. An at-large student member who is a student at an approved postsecondary educational institution is also an appointed member. The SSACI is reported as a non-major governmental fund.

*Discretely Presented Component Units*

The following are discretely presented component units of the State of Indiana. The primary government appoints a voting majority of their boards and is able to impose its will. All governmental and proprietary component units are audited by outside auditors except for the Indiana Economic Development Corporation and State Fair Commission which are audited by the State Board of Accounts. The State Board of Accounts audits the colleges, universities, and the discrete pension trust funds. College and university foundations are audited by outside auditors.

The Indiana Economic Development Corporation (IEDC) was created to improve the quality of life for the citizens of Indiana by encouraging the diversification of Indiana’s economy, by the orderly economic development and growth of Indiana, the creation of new jobs, the retention of existing jobs, the growth and modernization of existing industry and the promotion of Indiana. The IEDC is composed of 12 members, none of whom may be members of the general assembly. These members consist of the governor and 11 individuals appointed by the governor. At least five members must belong to the same political party as the governor. At least three members must belong to a major political party other than the party of which the governor is a member. The IEDC is reported as a non-major governmental fund. The IEDC does not issue their own separately audited financial statements.

Formed on May 15, 2005, the Indiana Finance Authority (IFA) combined five formerly independent bodies under one entity. The entities combined included the Indiana Development Finance Authority, State Office Building Commission, Indiana Transportation Finance Authority, Recreational Development Commission and the State Revolving Fund. Effective July 1, 2005, all records, money, and other property held by the Auditor of State with respect to the Supplemental Drinking Water and Wastewater Assistance Programs were transferred to the IFA as the successor entity. The IFA is a body both corporate and politic, and though separate from the State of Indiana (State); the exercise by the IFA of its powers constitutes an essential governmental function. Indiana's constitution restricts State incurrence of debt. As a result, the General Assembly created the IFA and authorized it to issue revenue bonds and other obligations to finance projects for lease to the State.

The IFA finances and refinances state hospitals, state office buildings, state garages, correctional facilities, recreational facilities, highways, bridges, airport facilities, and other related facilities for the benefit of the State. The IFA also provides low interest loans to Indiana communities for environmental improvements. It also promotes business and employment opportunities by issuing tax-exempt financing for industrial development projects, rural development projects, childcare financing, and educational facility projects.

The IFA's revenue bonds and notes are special and limited obligations of the IFA, payable from lease rental revenue, bond or note proceeds and investment income. The IFA's revenue bonds are not general obligations of the IFA nor are they State debt within the meaning of any constitutional provision or limitation. The IFA cannot compel the General Assembly to make appropriations to pay lease rentals. The Authority is reported as a proprietary fund.

The Indiana Bond Bank, created in 1984, is controlled by a board composed of the Treasurer of State, Director of Public Finance and five appointees of the Governor. The Bond Bank issues debt obligations and invests the proceeds in various projects of State and local governments. The unit is reported as a proprietary fund.

The Indiana Housing and Community Development Authority was created in 1978 for the purpose of financing residential housing for persons and families of low and moderate incomes. The Authority's board consists of the Public Finance Director of the Indiana Finance Authority, the Lieutenant Governor, the State Treasurer and four persons appointed by the Governor. The Lieutenant Governor chairs the board. The unit is reported as a proprietary fund.

The Indiana Board for Depositories was established to ensure the safekeeping and prompt payment of all public funds deposited in Indiana banks. The Board, consisting of the Governor, Treasurer of State, Auditor of State, Chairman of the Commission for Financial Institutions, State Examiner of the State Board of Accounts and four members appointed by the Governor, provides insurance on public funds in excess of the Federal Deposit Insurance Corporation limit. The unit is reported as a proprietary fund.

The Indiana Secondary Market for Education Loans, Inc. (ISM) was formed at the request of the Governor to purchase education loans in the secondary market. The Governor appointed the original Board of Directors. ISM provides in its articles of incorporation that changes in the composition of its directors or in its bylaws are subject to the approval of the Governor. The unit is reported as a proprietary fund.

The State Lottery Commission of Indiana is composed of five members appointed by the Governor. Net proceeds from the Lottery are distributed to the State to be used to supplement teachers' retirement, public employees' retirement, and the Build Indiana Fund. A portion of the Build Indiana Fund is then used to supplement the Motor Vehicle Excise Tax Replacement Fund. The Commission is reported as a proprietary fund.

Effective May 15, 2005, the Indiana Stadium and Convention Building Authority was established pursuant to House Bill 1120, which has now been codified at Indiana Code 5-1-17, as an entity of the

State to finance, design, construct and own the new Indiana Stadium in Indianapolis and the upcoming expansion of the adjacent Indiana Convention Center. The Building Authority is governed by a seven member board, comprised of four appointments by the Governor, two appointments by the Mayor of the City of Indianapolis and one appointment by the Governor following nomination from one of the counties surrounding Marion County. The Authority is reported as a proprietary fund.

The White River State Park Development Commission has the responsibility to design and implement a plan for the establishment and development of park, exposition, educational, athletic, and recreational projects to be located within one mile from the banks of the Indiana White River in a consolidated first-class city and county. The Commission is reported as a non-major proprietary fund.

The Ports of Indiana is created under Indiana Code 8-10-1-3 to construct, maintain, and operate public ports with terminal facilities and traffic exchange points for all forms of transportation on Lake Michigan and the Ohio and Wabash Rivers. The Commission consists of seven members appointed by the governor. The Commission is reported as a non-major proprietary fund.

The State Fair Commission was established per Indiana Code 15-13-2 as the trustee for and on behalf of the people of the State of Indiana to administer the State Fairgrounds as trust property of the State of Indiana. The Commission is responsible for holding the annual Indiana State Fair in August, as well as providing accessible, cost-effective, secure and modern facilities for the variety of events held at the Fairgrounds and other properties it owns. The Commission consists of eight members appointed by the governor. The Commission is reported as a non-major proprietary fund.

The Indiana Comprehensive Health Insurance Association was created by the State of Indiana to assure that health insurance is made available throughout the year to each eligible Indiana resident applying to the Association for coverage. The board of directors of the Association consists of nine members whose principal residence is in Indiana. Four members are appointed by the insurance commissioner from the members of the Association, one of which must be a representative of a health maintenance organization. Two members are appointed by the commissioner and shall be consumers representing policyholders. Other members are the state budget director or designee and the commissioner of the department of insurance or designee. One member appointed by the commissioner must be a representative of health care providers. The Association is reported as a non-major proprietary fund.

The Indiana Political Subdivision Risk Management Commission was created per Indiana Code 27-1-29 to administer the Political Subdivision Risk Management Fund (Basic fund) and the Political Subdivision Catastrophic Liability Fund (Catastrophic fund). These funds aid political subdivisions in protecting themselves against liabilities. The Commission consists of eleven members appointed by the governor. The Commission is reported as a non-major proprietary fund.

The Indiana State Museum and Historic Sites Corporation was created per Indiana Code 4-37 and is responsible for operating and administering the twelve State Historic Sites including the Indiana State Museum. The twelve Historic Sites include Angel Mounds, Corydon Capitol, Culbertson Mansion, J.F.D. Lanier Mansion, Levi Coffin, Limberlost, New Harmony, T.C. Steele, Gene Stratton-Porter, Vincennes, Whitewater Canal and the Indiana State Museum. The Corporation is governed by a thirty member board of trustees of which twenty-five are voting members and five are non-voting members. Of the twenty-five voting members, thirteen persons are appointed by the governor and twelve are appointed by the board. The five non-voting members include the chief executive officer, the governor or governor’s designee, one member of the House of Representatives, one member of the Senate, and the director of the Department of Natural Resources or the director’s designee. The Corporation is reported as a non-major proprietary fund.

Each of the seven colleges and universities included in this report was established by individual legislation to provide higher education opportunities to the citizens of Indiana. The authority to administer the operations of each institution is granted to a separate board of trustees for each of the seven institutions. The number and makeup of the board of trustees of each college and university is prescribed by legislation specific for that institution. Four universities have nine member boards; two have ten member boards; Ivy Tech Community College has a fourteen-member board of trustees. Appointments to the boards of trustees are made by the Governor and by election of the alumni of the respective universities. Indiana

University and Purdue University are reported as a major discretely presented component unit.

*Fiduciary in Nature Component Unit*

Effective July 1, 2011, the Indiana Public Retirement System (INPRS) was established as an independent body corporate and politic. INPRS is not a department or agency for the State, but is an independent instrumentality exercising essential government functions. The INPRS board is composed of nine trustees appointed by the Governor which includes the director of the budget agency or the director's designee as an ex officio voting member of the board. The board of trustees administers the following plans: Public Employees' Retirement Fund, Teachers' Retirement Fund, Judges' Retirement System, State Excise Police, Gaming Agent, Gaming Control Officer and Conservation Enforcement Officers' Retirement Plan, the 1977 Police Officers' and Firefighters' Pension and Disability Fund, the Legislators' Retirement System Defined Benefit Plan, the Legislators' Retirement System Defined Contribution Plan, the Prosecuting Attorneys' Retirement Fund, the Pension Relief Fund, and two death benefit funds. For more information on the plans see Note V(E) Employee Retirement Systems and Plans. All of these funds have been aggregated for presentation from INPRS' financial statements.

The Indiana Public Retirement System was determined to be significant for note disclosure purposes involving the fiduciary in nature component units.

The primary government's officials are also responsible for appointing the members of the boards of other organizations, but the primary government's accountability for these organizations does not extend beyond making the appointments.

**The financial statements of the individual component units whom issue separately audited financial statements may be obtained from their administrative offices as follows:**

| | | |
|---|---|---|
| Indiana Finance Authority<br>One North Capitol Ave., Suite 900<br>Indianapolis, IN 46204 | Indiana Bond Bank<br>10 West Market St. Suite 2980<br>Indianapolis, IN 46204 | State Lottery Commission of Indiana<br>1302 N. Meridian St.<br>Indianapolis, IN 46202 |
| Indiana Stadium and Convention<br>Building Authority<br>425 W. South Street<br>Indianapolis, IN 46225 | Indiana Housing and Community Development Authority<br>40 South Meridian, Suite 1000<br>Indianapolis, IN 46204 | Secondary Market for Education Loans, Inc.<br>Capital Center, Suite 400<br>251 N. Illinois<br>Indianapolis, IN 46204 |
| Indiana Board for Depositories<br>One North Capitol Ave., Suite 444<br>Indianapolis, IN 46204 | Indiana White River State Park<br>Development Commission<br>801 West Washington Street<br>Indianapolis, IN 46204 | Indiana Comprehensive Health Insurance Association<br>9465 Counselors Row, Suite 200<br>Indianapolis, IN 46240 |
| Ports of Indiana<br>150 West Market Street, Suite 100<br>Indianapolis, IN 46204 | Indiana State Fair Commission<br>1202 E. 38th Street<br>Indianapolis, IN 46205 | Indiana Political Subdivision Risk Management Commission<br>c/o Indiana Department of Insurance<br>311 W. Washington St., Suite 300<br>Indianapolis, IN 46204 |
| Indiana State Museum and Historic Sites Corporation<br>650 W. Washington St.<br>Indianapolis, IN 46204 | Ivy Tech Community College<br>50 West Fall Creek Parkway North Drive<br>Indianapolis, IN 46208 | University of Southern Indiana<br>8600 University Boulevard<br>Evansville, IN 47712 |
| Indiana University<br>Poplar's Room. 500, 107 S. Indiana Ave.<br>Bloomington, IN 47405-1202 | Ball State University<br>Administration Bldg., 301<br>2000 West University Avenue<br>Muncie, IN 47306 | Indiana State University<br>Office of the Controller<br>210 N. 7th Street<br>Terre Haute, IN 47809 |
| Vincennes University<br>1002 North 1st Street<br>Vincennes, IN 47591 | Purdue University<br>Accounting Services<br>401 South Grant Street<br>West Lafayette, IN 47907-2024 | Indiana Public Retirement System<br>One North Capitol Ave., Suite 001<br>Indianapolis, IN 46204 |

## B. Government-Wide and Fund Financial Statements

The government-wide financial statements consist of a statement of net assets and a statement of activities. These statements report information about the overall government. They exclude information about fiduciary activities, including component units, which are fiduciary in nature, such as the public employee retirement systems. They distinguish between the primary government and its discretely presented component units as defined under the reporting entity above. They also distinguish between governmental activities and business-type activities of the State. Governmental activities rely on taxes and intergovernmental revenues for their support. Business-type activities, on the other hand, rely on fees and charges for services provided for their support.

The statement of activities matches the State's direct functional expense with the functional program revenue to identify the relative financial burden of each of the State's functions. This format identifies the extent to which each function of the government draws from the general revenues of the government or is self-financing through fees and intergovernmental aid. Certain indirect costs are included in the program expense reported for individual functions of government. Program revenues derive directly from the program itself or from parties outside the State's taxpayers, as a whole. They reduce the net cost of the function to be financed from the general revenues. Program revenues include charges for services, program-specific operating grants and contributions, and program-specific capital grants and contributions. Revenues that do not meet the criteria of program revenues are general revenues. These include all taxes, even those levied for a specific purpose and are reported by type of tax. Investment income is also a general revenue.

Separate financial statements are presented for the State's governmental, proprietary and fiduciary funds. Governmental fund financial statements are the balance sheet and the statement of revenues, expenditures, and changes in fund balances. Major governmental funds are presented in separate columns and non-major funds are aggregated in a separate column. Proprietary and fiduciary funds are reported using the statement of net assets and the statement of changes in net assets. In addition proprietary funds include a statement of cash flows.

**C. Measurement Focus, Basis of Accounting and Financial Statement Presentation**

**Measurement Focus and Basis of Accounting**

***The government-wide statements and the proprietary and fiduciary fund statements*** use the economic resources measurement focus and the accrual basis of accounting. Revenues, expenses, gains, losses, assets, and liabilities resulting from exchange and exchange-like transactions are recognized when the exchange takes place. Government-mandated nonexchange revenues and voluntary nonexchange revenues, including federal government mandates on the State, certain grants and entitlements, and most donations, are recognized in the period when all applicable eligibility requirements have been met.

For the government-wide financial statements and enterprise and fiduciary fund statements, the State applies all applicable FASB pronouncements issued before December 1, 1989, and those issued after that date which do not contradict any previously issued GASB pronouncements.

***Governmental funds*** are used to account for the government's general government activities. Governmental fund types use the flow of current financial resources measurement focus and the modified accrual basis of accounting. Under the modified accrual basis of accounting revenues are recognized when susceptible to accrual (i.e., when they are "measurable and available"). "Measurable" means the amount of the transaction can be determined and "available" means collectible within the current period or soon enough thereafter to pay liabilities of the current period. For the State of Indiana, "available" means collectible within one month of the fiscal year end. Expenditures are recorded when the related fund liability is incurred, except for unmatured interest on general long-term debt which is recognized when due, and certain compensated absences and related liabilities, and claims and judgments which are recognized when the obligations are expected to be liquidated with expendable available financial resources.

Individual and corporate income tax, sales tax, inheritance tax, cigarette tax, alcoholic beverage tax, motor fuel tax, fines, and penalties are accrued using one month's revenues.

Gaming taxes and fees and vehicle licenses are received daily via electronic funds transfer with a one to three working day delay, so the first several working days in July revenues are reviewed for materiality and accrued accordingly.

**Financial Statement Presentation**

A fund is an independent fiscal and accounting entity with a self-balancing set of accounts. Fund accounting segregates funds according to their intended purpose and is used to aid management in demonstrating compliance with finance-related legal and contractual provisions.

***Governmental funds*** are used to account for the government's general government activities. Governmental funds include the general fund, special revenue funds, capital projects funds, debt service funds and permanent funds.

The *General Fund* is the State's primary operating fund. It is maintained to account for resources obtained and used for those services traditionally provided by State government, which are not required to be accounted for in another fund. The General Fund is a major fund.

The *special revenue* funds account for specific revenue sources that are legally restricted or committed to expenditure for specific purposes except for major capital projects.

The following special revenue funds are presented as major.

- The *Public Welfare-Medicaid Assistance Fund* receives federal grants and State appropriations which are used to administer the Medicaid program. Federal grant revenues, quality assessment fees, Intermediate Care Facility for the Mentally Retarded fees, and other resources disclosed under interfund transfers in Note IV(B) are reported in this fund.

- The *Major Moves Construction Fund* distributes money received from the Toll Road lease. This money is used for new construction and major preservation of highways and bridges throughout Indiana. Interest income and other resources disclosed under interfund transfers in Note IV(B) are reported in this fund.

- The *ARRA of 2009* Fund is used to account for funds received under the American Recovery and Reinvestment Act of 2009 which became law on February 17, 2009. These funds are supplementing existing federal programs in areas such as Medicaid, education, transportation, housing, and employment services. Federal grant revenues and other resources disclosed under interfund transfers in Note IV(B) are reported in this fund.

- The *U.S. Department of Transportation Fund* receives federal grants and State appropriations that are used for State transportation programs. Federal grant revenues and other resources disclosed under interfund transfers in Note IV(B) are reported in this fund.

- The *U.S. Department of Health and Human Services Fund* receives federal grants that are used to carry out health and human services programs. Federal grant revenues, child support annual fees, and other resources disclosed under interfund transfers in Note IV(B) are reported in this fund.

The *capital projects funds* account for financial resources that are restricted, committed, or assigned to expenditures for the acquisition of fixed assets or construction of major capital projects not being financed by proprietary or fiduciary funds. There are no major capital project funds.

The *permanent funds* are used to account for resources that are legally restricted to the extent that only earnings and not principal may be used for the benefit of the government or its citizens. There are no major permanent funds.

**Proprietary funds** focus on the determination of operating income, changes in net assets, financial position and cash flows. Operating revenues and expenses are the revenues and expenses that pertain to the fund's principal operations. Nonoperating revenues and expenses are those revenues resulting from secondary or auxiliary activities of the fund. Nonoperating items include interest/investment revenue and expense. Proprietary funds include both enterprise funds and internal service funds.

*Enterprise funds* are used to account for those operations that are financed and operated in a manner similar to private business or where the board has decided that the determination of revenues earned, costs incurred and/or net income is necessary for management accountability.

The State reports the following major enterprise fund:

- The *Unemployment Compensation Fund* collects employer taxes and the federal share of unemployment compensation. Benefits are paid to eligible individuals.

*Internal service funds* account for operations that provide goods and services to other departments or agencies of the government, or to other governments, on a cost-reimbursement basis. The goods and services provided include fleet management, information technology and communication, aviation, printing, products of correctional industries, self-insurance, and centralized accounting. Major fund reporting requirements do not apply to internal service funds. Combined totals for all internal service funds are reported as a separate column on the face of the proprietary fund financial statements.

***Fiduciary funds*** account for assets held by or on behalf of the government in a trustee capacity or as an agent on behalf of others. They cannot be used to support the State's own programs. Fiduciary funds include pension (and other employee benefit) trust funds, private-purpose trust funds, investment trust funds, and agency funds.

*Pension (and other employee benefit) trust funds* are used to report resources held in trust for the members and beneficiaries of defined benefit pension plans, and defined contribution pension plans. Pension and other employee benefits trust funds include the Indiana Public Retirement System, State Police Pension Fund, State Employee Retiree Health Benefit Trust Fund – DB, and the State Employee Retiree Health Benefit Trust Fund – DC.

*Private-purpose trust funds* are used to account for trust arrangements in which both the principal and interest may be spent for the benefit of individuals, private organizations or other governments. Private Purpose funds include the Abandoned Property Fund and the Private Purpose Trust Fund.

*Investment trust funds* are used to report the external portion of investment pools operated by a sponsoring government. The Treasurer of State, local units of government, and quasi-governmental units in Indiana have the opportunity to invest in a common pool of investments that preserves the principal of the public's funds, remains highly-liquid, and maximizes the return on the investment of public funds. The State's investment trust fund is TrustINdiana operated by the state treasurer. The amounts reported represent the external portion of the pool.

*Agency funds* are custodial in nature and do not present results of operations or have a measurement focus. These funds are used to account for assets that the government holds for others in an agency capacity. Agency Funds include Employee Payroll Withholding and Benefits, Local Distributions, Child Support and Department of Insurance.

**D. Eliminating Internal Activity**

Interfund loans including those from cash overdrafts in funds, interfund services provided or used, and prepaid expenditures of internal service funds are eliminated as internal balances in the government-wide statement of net assets. This is to minimize the "grossing-up" effect on assets and liabilities within the governmental and business-type activities columns of the primary government. As a result, interfund loans and interfund services provided and/or used reported in the governmental funds balance sheet have been eliminated in the government-wide statement of net assets.

Eliminations were made in the statement of activities to remove the "doubling-up" effect of internal service fund activity. The effect of similar internal events that are, in effect, allocations of overhead expenses from one function to another or within the same function have also been eliminated, so that the allocated expenses are reported only by the function to which they were allocated. The effect of interfund services provided and used between functions has not been eliminated in the statement of activities since to do so would misstate both the expenses of the purchasing function and the program revenues of the selling function.

**E. Assets, Liabilities and Equity**

***1. Deposits, Investments and Securities Lending***

For purposes of reporting cash flows, cash and cash equivalents are defined as short-term, highly liquid investments that are both readily convertible to known amounts of cash and near their maturity (generally three months or less from the date of acquisition).

Cash balances of most State funds are commingled in general checking accounts and several special purpose banking accounts. The available cash balance not necessary beyond immediate need is pooled and invested. Interest earned from investments purchased with pooled cash is deposited in the general fund, except as otherwise provided by statute.

Investments and secured lending transactions are stated at fair value. However, money market investments and participating interest-earning investment contracts that mature within one year of acquisition are reported at amortized cost, which approximates fair value. Fair value is determined by quoted market prices which approximate fair value.

Indiana Code 5-13-9 and 5-13-10.5 authorizes the Treasurer to invest in deposit accounts issued or offered by a designated depository; securities backed by the full faith and credit of the United States Treasury; securities issued by any U.S. government agency; AAA money market mutual funds with a portfolio limited to direct obligations of the U.S., obligations of any federal agency, and/or repurchase agreements fully collateralized with U.S. government obligations or U.S. agency obligations; AAA rated commercial paper, and repurchase agreements that are fully collateralized, as determined by the current market value computed on the day the agreement is effective, by interest-bearing obligations that are issued, fully insured or guaranteed by the United States or any U.S. government agency.

The Treasurer of State is authorized by statute to accept as collateral safekeeping receipts for securities from: (1) a duly designated depository or (2) a financial institution located either in or out of Indiana, having physical custody of securities, with a combined capital and surplus of at least $10 million, according to the last statement of condition filed by the financial institution with its governmental supervisory body. The Treasurer may not deposit aggregate funds in deposit accounts in any one designated depository in an amount aggregating at any one time more than 50% of the combined capital, surplus and undivided profits of that depository as determined by the last published statement.

The Indiana Public Retirement System (INRPS) Board of Trustees administers seven retirement systems and three non-retirement funds. Indiana law requires the Board to establish investment guidelines and limits on all types of investments and take other actions necessary to fulfill its duty as fiduciary for all assets under its control. The INPRS Board of Trustees is required to diversify investments in accordance with the prudent investor standards. At June 30, 2012, cash and investments of the funds were held by banks or trust companies under custodial agreements with INPRS. The INPRS Board of Trustees contracts with investment counsel, trust companies or banks to assist INPRS in its investment program. The Investment Policy Statement adopted by the INPRS Board of Trustees and the asset allocation approved by the Board of Trustees contains target allocations and allowable ranges that are expected to meet target rates of return over a long period of time while minimizing risk. The investments of INPRS are subject to the provisions of IC 5-10.3-5-3 and IC 5-10.4-3-10. See Note IV(A)(3) for more information.

Investments which are authorized for the State Police Retirement fund include: U.S. Treasury and Agency obligations, State and municipal obligations, domestic corporate bonds/notes, common stock and equity securities, foreign stocks and bonds, mortgage pool investments, and repurchase agreements. The investments of the State Police Retirement fund are subject to the provisions of IC 10-12-2-2.

### *2. Receivables and Payables*

In the government-wide and proprietary fund financial statements, revenues are recognized on the flow of economic resources measurement focus. Material receivables are recognized as follows. Uncollected taxes due in the following periods are subject to accrual.

> Individual income tax – Individual withholding tax is due from employers by the 20th day after the end of the month collected. Estimated payments are due from individuals by the 15th of the month immediately following each quarter or the calendar year.
>
> Corporate income tax - Due quarterly on the 20th day of April, June, September, and December with the last payment due on April 15th for a calendar year taxpayer.
>
> Sales tax – Due by the 20th day after the end of the month collected.
>
> Fuel tax – Gasoline tax is due the 20th day after the end of the month collected. Special fuel tax, depending on the status of the taxpayer, is due by the 15th day after the end of the month collected or the 15th day after the end of the quarter collected. Motor carrier surtax is due at the end of the month following the end of the quarter.
>
> Financial institutions tax – same laws as corporate income taxes (see above) for making payments.
>
> Alcohol and tobacco taxes – Cigarette distributors must purchase tax stamps within 6 days after they accept delivery of the cigarettes. Cigarette tax is due within 30 days of the issuance of the tax stamp. Alcoholic beverage tax is due by the 20th day after the end of the month collected.
>
> Inheritance tax – except as otherwise provided in IC 6-4.1-6-6(b), the inheritance tax imposed as a result of a decedent's death is due twelve (12) months after the person's date of death.

In the governmental fund financial statements, revenue is recognized on the flow of current financial resources. Material receivables are subject to accrual for receipts collected in the month of July.

The State of Indiana does not collect property tax, which is collected by local units of government.

Deferred revenue is the liability for the full accrual income taxes receivable net of the allowance for doubtful accounts plus cash on hand from federal grant programs.

### *3. Interfund Transactions and Balances*

The State has the following types of interfund transactions in the governmental fund and proprietary financial statements:

> Interfund services provided and used (reciprocal interfund activity) – Charges for goods or services rendered by one fund to another are treated as

revenues of the recipient fund and expenditures/expenses of the disbursing fund.

Interfund Transfers (non-reciprocal interfund activity) – Legally authorized transfers whereby the two parties do not receive equivalent cash, goods or services are reported as transfers.

The types of assets and liabilities resulting from these transactions are:

Interfund loans – These are balances arising from the short-term and long-term portion of interfund transactions.

Interfund services provided/used – These are balances arising in connection with reciprocal interfund activity or reimbursements. Balances relating to discretely presented component units are presented as 'Due from/to component units'.

Interfund services provided and interfund loans are eliminated in the government-wide statements because they are provided by one governmental activity on behalf of another or by one business-type activity on behalf of another.

### *4. Inventories and Prepaid Items*

Inventories for the Inns & Concessions, Institutional Industries and Administrative Services Revolving funds are valued at cost. The costs of governmental fund-type inventories are recorded as expenditures when purchased. The first in/first out (FIFO) method is used for valuation of inventories.

Certain payments to vendors reflect costs applicable to future accounting periods and are recorded as prepaid items.

### *5. Restricted Net Assets*

Certain net assets are classified as restricted net assets because their use is completely restricted by bond indentures, contracts, grantors, contributors, laws or regulations of other governments, or through constitutional provisions or enabling legislation. Net assets restricted by enabling legislation for governmental activities totals $0.9 billion, of which $0.5 billion is permanent funds principal and $0.4 billion is for the Economic Stabilization Fund as discussed in Note V(D).

### *6. Capital Assets*

Capital outlays are reported as expenditures in the governmental funds and as assets in the government-wide statements to the extent the State's $20,000 capitalization threshold for external financial reporting is met. In accordance with GASB Statement No. 34, all infrastructure assets have been capitalized retroactively.

The Indiana Department of Transportation (INDOT) uses the modified approach for reporting its infrastructure. The Department of Natural Resources (DNR) uses the depreciation approach for reporting its infrastructure.

Under the modified approach, the State has determined that the condition level for INDOT infrastructure assets to be maintained is:

- a network average International Roughness Index (IRI) of no more than 95 and no more than 10% of all pavements in the unacceptable range for Interstates, National Highway Safety (NHS) Non-Interstate roads, and Non-NHS roads,
- an average sufficiency rating of 87% for interstate bridges,
- an average sufficiency rating of 85% for NHS Non-Interstate bridges, and
- an average sufficiency rating of 83% for Non-NHS bridges.

The Asset Management, Program Engineering, and Road Inventory Division of INDOT is responsible for determining the appropriate condition level of the infrastructure assets.

No amounts are capitalized in connection with improvements that lengthen the lives of such assets, unless the improvements also increase their service potential.

INDOT projects are capitalized based on capitalization and preservation percentages assigned to three hundred seventy-seven (377) work types. For example, the cost for constructing a new bridge would likely be 100% capitalized; whereas, the cost for adding travel lanes to a road would likely be assigned a work type code resulting in capitalization at 50% and preservation at 50%.

The State maintains an inventory of these infrastructure assets and performs periodic condition assessments to establish that the predetermined condition level is being maintained. Road pavement condition assessments are performed annually on all INDOT state routes, including interstates. Condition assessments of all bridges are determined on a bi-annual basis. Sufficiency ratings of all bridges are determined on an annual basis by the Federal Highway Administration based on annual submittal of bridge condition data.

The State makes annual estimates of the amounts that must be expended to preserve and maintain these infrastructure assets at the predetermined condition levels.

Capital assets are recorded at historical cost or estimated historical cost if purchased or constructed. Donated fixed assets are recorded at their estimated fair value at the date of donation.

Capital assets are depreciated in the proprietary and similar trust funds using the straight-line method on both the fund basis and the government-wide basis. Both the government-wide statements and proprietary and similar trust funds use the following estimated useful lives:

| Assets | Months |
|---|---|
| Buildings and other structures including improvements to buildings and other structures | 240-480 |
| Computer software | 36 |
| Infrastructure (not using modified approach) | 240-720 |
| Furniture, machinery and equipment | 12-168 |
| Motor pool vehicles | 96-168 |

The State of Indiana maintains several collections of works of art, historical treasures, and similar assets that are not capitalized. While the collections are maintained by different agencies, each collection is:

- Held for public exhibition, education, or research in furtherance of public service, rather than financial gain.
- Protected, kept unencumbered, cared for, and preserved.
- Subject to an organizational policy that either prohibits sale or requires the proceeds from sales of collection items to be used to acquire other items for collections.

The State's major collections are:

- The Commission on Public Records, State Archives Collection consists of historical and legal documents, that are generated on: paper or paper substitutes; photographic or chemically based media; magnetic or machine readable media; or any other materials, regardless of form or characteristics.
- The State Library has two collections, the Manuscript Collection and the Indiana History Collection. These collections include historical documents and works of art, most of it of Indiana origin.

Other collections include the Historical Bureau's Indiana Governors' Portrait Collection, the Department of Administration's Statehouse Collection, and the Indiana Arts Commission's Collection. These collections consist primarily of art objects.

### 7. *Compensated Absences*

Full-time employees of the State of Indiana are permitted to accumulate earned but unused vacation and sick pay benefits. Vacation leave accumulates at the rate of one day per month and sick leave at the rate of one day every two months plus an extra day every four months. Bonus vacation days are awarded upon completion of five, ten and twenty years of employment.

Personal leave days are earned at the rate of one day every four months; any personal leave accumulated in excess of three days automatically becomes part of the sick leave balance. Upon separation of service, in good standing, employees will be paid for a maximum of thirty (30) unused vacation leave days. In addition, qualifying retiring employees are paid an additional payment up to a maximum of $5,000, which is made up of unused vacation leave over 30 days, unused personal leave, and unused sick leave.

Employees of the legislative and judicial branches as well as those of the separately elected officials (i.e., Auditor of State) may convert a portion of accrued but unused vacation and sick leave into the deferred compensation plan. An employee must have at least 300 hours of vacation or sick leave accrued in order to participate in this plan. There is a sliding scale which determines how many hours are converted from those hours the employee has accrued. The hours converted are deposited into the deferred compensation program's 401(a) plan at 60% of the employee's hourly rate. Employees of the legislative branch of government have elected to participate in this program for FY 2013.

Vacation and personal leave and salary-related payments that are expected to be liquidated with expendable available financial resources are reported as an expenditure and a fund liability of the governmental fund that will pay it. Amounts not expected to be liquidated with expendable available financial resources are reported as long term liabilities in the government-wide, proprietary, and fiduciary fund financial statements.

### 8. *Long-Term Obligations*

Long-term debt and other obligations are reported in the government-wide statements and the proprietary funds statements as liabilities in the applicable governmental activities, business-type activities, or proprietary fund.

In the governmental fund financial statements, bond issuance costs and bond discounts are treated as period costs in the year of issue. Proceeds of long term debt, issuance premiums or discounts and certain payments to escrow agents for bond refundings are reported as other financing sources and uses.

### *9. Fund Balance*

In the fund financial statements, fund balances are categorized as nonspendable, restricted, committed, assigned, or unassigned. A brief description of each category is as follows:

*Nonspendable* – represents amounts that are either not in spendable form, such as inventories, and activity that is legally or contractually required to be maintained intact, such as a principal balance in a permanent fund.

*Restricted* – represents amounts restricted to specific purposes because of constraints placed on their use that are either externally imposed such as by grantors or imposed by law through constitutional provisions or enabling legislation.

*Committed* – represents amounts that can only be used for a specific purpose pursuant to constraints imposed by the government's highest level of decision making authority. The State of Indiana's highest level of decision making authority is the General Assembly. The formal action necessary would be the enactment of a State law that specifically establishes, modifies, or rescinds a fund balance commitment.

*Assigned* – represents amounts that are constrained by the government's intent to be used for specific purposes as expressed by the governing body itself or the official to which the governing body has delegated the authority to assign amounts to be used for specific purposes. The State Budget Agency has the authority per the biennial budget bill to make assignments of fund balances for specific purposes except for those restricted by law. The State Board of Finance comprised of the Governor, Auditor of State and Treasurer of State is empowered to make assignments of funds except for trust funds per I.C. 4-9.1-1-7.

*Unassigned* – represents fund balance that has not been assigned to other funds and that has not been restricted, committed, or assigned to specific purposes within the general fund. Only the general fund may report a positive unassigned fund balance; whereas, other governmental funds may need to report a negative unassigned fund balance if expenditures incurred for specific purposes exceeded the amounts restricted, committed, or assigned to those purposes.

Funds on the State's accounting system are assigned one of the five fund balance classifications. If a fund has resources that are both restricted and unrestricted, then expenditures are applied first to restricted fund balance and then unrestricted amounts. A fund's unrestricted fund balance would have committed amounts reduced first, assigned amounts second, and unassigned amounts third when expenditures are incurred for purposes for which amounts in any of these unrestricted fund balance classifications could be used.

## II. RECONCILIATION OF GOVERNMENT-WIDE AND FUND FINANCIAL STATEMENTS

As described in Note I, Summary of Significant Accounting Policies, differences exist between the government-wide and the governmental fund financial statements. These differences are summarized in the reconciliations that follow the governmental fund financial statements.

### A. Reconciliation of the Governmental Funds Balance Sheet to the Statement of Net Assets

In the government-wide financial statements, capital assets are considered economic resources and are capitalized at cost or estimated historical cost at time of acquisition. Where applicable these costs are offset by accumulated depreciation.

The government-wide statements use the flow of economic resources and accrue receivables that are not available soon enough in the subsequent period to pay for the current period's expenditures. Also under the flow of economic resources, expenses reported in the statement of activities do not require the use of current financial resources. Both these receivables and payables are accrued in the government-wide statements, but not in the fund financial statements.

Internal service funds are used by management to charge the costs of certain activities to individual funds. In the government-wide financial statements, the assets and liabilities of internal service funds are included in governmental activities in the statement of net assets. In the proprietary fund financial statements internal service fund balances are segregated and reported as their own fund type.

### B. Reconciliation of the Statement of Revenues, Expenditures, and Changes in Fund Balances of Governmental Funds to the Statement of Activities

In the government-wide financial statements, the cost for capital outlays, except for governmental infrastructure, is allocated over the assets' useful lives and is reported as depreciation expense. In the fund financial statements, capital outlays are reported as expenditures in the functional line items.

The government-wide statements use the flow of economic resources and therefore do not report revenues and expenses dependent on the availability of financial resources, as is reported in the fund financial statements. Revenues in the statement of activities that do not provide current financial resources are not reported as revenues in the fund financial statements. Expenses reported in the statement of activities that do not require the use of current financial resources are not reported as expenditures in the fund financial statements. Bond proceeds provide current financial resources to governmental funds, but issuing debt increases long-term liabilities in the statement of net assets. Repayment of bond principal is an expenditure in the governmental fund financial statements, but the repayment reduces long-term liabilities in the statement of net assets.

Internal service funds are used by management to charge the costs of certain activities to individual funds. In the government-wide financial statements, the expenses of internal service funds are included in governmental activities in the statement of activities. In the proprietary fund financial statements internal service fund balances are segregated and reported as their own fund type.

## III. STEWARDSHIP, COMPLIANCE AND ACCOUNTABILITY

### A. Deficit Fund Equity

At June 30, 2012, various funds had a deficit fund balance caused by overdrafts from pooled cash and investments and the posting of accruals to the balance sheet. Temporary cash overdrafts are reported as interfund loans from the general fund.

| Fund | Overdraft from pooled cash | Accrual deficits |
|---|---|---|
| **Governmental Funds** | | |
| US Department of Transportation | $ (18,582) | $ (62,184) |
| US Department of Health & Human Services | (58,560) | (22,038) |
| US Department of Agriculture | - | (88,464) |
| S&S Children Home Construction | (709) | - |

### B. Fund Balance

The State of Indiana reports its fund balances for governmental funds as nonspendable, restricted, committed, assigned, and unassigned. The detail of the fund balance classifications at June 30, 2012 is as follows:

| | General Fund | Major Special Revenue Funds: Public Welfare-Medicaid Assistance Fund | Major Moves Construction Fund | ARRA of 2009 | US Department of Transportation | US Department of Health & Human Services | Non-Major Funds |
|---|---|---|---|---|---|---|---|
| **Fund balances:** | | | | | | | |
| **Nonspendable:** | | | | | | | |
| Permanent fund principal | $ - | $ - | $ - | $ - | $ - | $ - | $ 501,125 |
| **Restricted:** | | | | | | | |
| General Government | 363,212 | - | - | - | - | - | - |
| **Committed:** | | | | | | | |
| General Government | 20,859 | - | - | - | - | - | 580,218 |
| Welfare | - | - | - | - | - | - | 306,793 |
| Conservation, culture and developm | - | - | - | - | - | - | 103 |
| Education | - | - | - | - | - | - | 72 |
| Transportation | - | - | - | - | - | - | 171,733 |
| **Assigned:** | | | | | | | |
| General Government | 96,629 | - | - | - | - | - | 408,602 |
| Public Safety | 14,600 | - | - | - | - | - | 538,959 |
| Health | 985 | - | - | 1,910 | - | - | 20,357 |
| Welfare | 72,317 | 414,034 | - | 8,135 | - | - | 324,787 |
| Conservation, culture and develop. | 18,717 | - | - | 1,600 | - | - | 318,116 |
| Education | 6,304 | - | - | 2,286 | - | - | 65,967 |
| Transportation | 1,068 | - | 1,181,837 | - | - | - | 307,495 |
| Encumbrances | 441,412 | - | - | - | - | - | - |
| **Unassigned:** | 2,338,589 | - | - | - | (80,766) | (80,598) | (97,186) |
| **Total fund balance** | $ 3,374,692 | $ 414,034 | $ 1,181,837 | $ 13,931 | $ (80,766) | $ (80,598) | $ 3,447,141 |

# IV. DETAILED NOTES ON ALL FUNDS

## A. Deposits, Investments and Securities Lending

### *1. Primary Government – Other than Major Moves Construction Fund and Next Generation Trust Fund, Investment Trust Funds, and Pension and Other Employee Benefit Trust Funds.*

*Investment Policy*

Indiana Code, Title 5, Article13, Chapters 9, 10, and 10.5, establishes the investment powers and guidelines regarding the State of Indiana investments. However, the Major Moves Construction Fund and the Next Generation Trust Fund have separate investment authority as established under Indiana Code 8-14-14 and Indiana Code 8-14-15, respectively. The Treasurer of State shall invest these funds in the same manner as the public employees' retirement fund under Indiana Code 5-10.3-5 with the exception that monies may not be invested in equity securities. For more information, please see the PERF policy in note IV(A)3. There are no formal deposit or investment policies for the investment of these funds other than compliance to State statute. State statute does not establish any parameters or guidelines related to the concentration of investment risk, investment credit risk, nor interest rate risk.

Indiana Code 5-13-9 authorizes the Treasurer to invest in deposit accounts issued or offered by a designated depository; securities backed by the full faith and credit of the United States Treasury; and repurchase agreements that are fully collateralized, as determined by the current market value computed on the day the agreement is effective, by interest bearing obligations that are issued, fully insured or guaranteed by the United States or any U.S. government agency.

*Interest Rate Risk*

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. State statute does not establish any parameters or guidelines related to interest rate risk.

The following is a summary of the Interest Rate Risk Disclosure as of June 30, 2012:

| **Primary Government** | | | | |
|---|---|---|---|---|
| | **Fair** | **Investment Maturities (in Years)** | | |
| **Investment Type** | **Value Totals** | **Less than 1** | **1 - 5** | **6- 10** |
| U.S. Treasuries | $ 149,943 | $ 149,943 | $ - | $ - |
| U.S. Agencies | 4,110,068 | 3,864,378 | 245,690 | - |
| Supranationals | 118,502 | 99,993 | 18,509 | - |
| Municipal Bonds | 39,180 | 19,736 | - | 19,444 |
| Local Govt Investment Pool | 200,000 | 200,000 | - | - |
| Non-U.S. Fixed Income | 30,072 | 5,006 | 25,066 | - |
| Certificate of Deposits | 161,722 | 161,722 | - | - |
| Money Market Mutual Funds | 395,400 | 395,400 | - | - |
| Total | $ 5,204,887 | $ 4,896,178 | $ 289,265 | $ 19,444 |

*Custodial Credit Risk*

Deposits – The custodial credit risk for deposits is the risk that, in the event of the failure of a depository financial institution, a government will not be able to recover deposits or will not be able to recover collateral securities that are in the possession of an outside party.

At June 30, 2012, the balance of the State of Indiana's deposits was covered in full by federal depository insurance or by the Public Deposit Insurance Fund, which covers all public funds held in approved depositories.

Investment Custodial Credit Risk – The custodial credit risk for investments is the risk that, in the event of the failure of the counterparty to a transaction, a government will not be able to recover the value of investment or collateral securities that are in the possession of an outside party. Investments are exposed to custodial credit risk if the securities are uninsured and unregistered and are either held by the counterparty's trust department or agent, but not in the name of the State of Indiana. None of the State's investments are exposed to custodial credit risk because they are held in the name of the State of Indiana. Additionally, the Treasurer of State requires all custodians to indemnify the State against all out-of-pocket expenses or losses incurred as a result of (i) the custodian's operational failure, (ii) custodians failure to carry out the credit analysis, (iii) custodian's failure to maintain proper collateral for each loan, or (iv) failure of an approved counterparty to comply with its obligations under the applicable securities lending agreement.

*Credit Risk*

Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. Indiana Code 5-13-9-2 authorizes the State Treasurer to invest or reinvest in securities fully guaranteed and issued by (1) the United States Treasury, (2) a federal agency, (3) a federal instrumentality, or (4) a federal government sponsored enterprise. The State Treasurer also may invest or reinvest in money market mutual funds that are in the form of securities of or interests in an open-end, no-load, management-type investment company or investment trust registered under the provisions of the federal Investment Company Act of 1940. The portfolio of the investment company or investment trust must be limited to direct obligations of the United States, a federal agency, a federal instrumentality, a federal government sponsored enterprise, or repurchase agreements fully collateralized by obligations described in numbers (1) through (4) above. The statute also states the securities of or interests in an investment company or investment trust must be rated as one of the following: (1) AAA, or its equivalent, by Standard & Poor's Corporation or its successor; or (2) Aaa, or its equivalent, by Moody's Investors Service, Inc. or its successor.

The following table provides information on the credit quality ratings for investments in debt securities as well as investments in external investment pools, money market funds, bond mutual funds, and other pooled investments of fixed-income securities as of June 30, 2012. The following table reflects the greatest risk rating (the credit rating reflecting the greatest degree of risk) as set by three nationally recognized rating organizations (S&P, Moody, and Fitch) for each type of investment:

| **Primary Government** | **Greatest Risk** | |
|---|---|---|
| **Investment Type** | **Rating** | **Fair Value** |
| U.S. Treasuries | AA | $ 149,943 |
| U.S. Agencies | AAA | 50,003 |
| | AA | 4,060,065 |
| Supranationals | AAA | 65,008 |
| | NR | 53,494 |
| Certificate of Deposits | NR | 161,722 |
| Municipal Bonds | NR | 39,180 |
| Non-US Fixed Income Bonds | A | 30,072 |
| Local Govt Investment Pool | NR | 200,000 |
| Money Market Mutual Funds | AAA | 395,400 |
| Total | | $ 5,204,887 |

*Concentration of Credit Risk*

Concentration of credit risk is the risk of loss attributed to the magnitude of a government's investment in a single issuer. Indiana Code 5-13-10-3 states that the State Treasurer may not deposit aggregate funds in deposit accounts in any one designated depository in an amount aggregating at any one time more than fifty percent (50%) of the combined capital, surplus, and undivided profits of that depository as determined by its last published statement of condition filed with the State Board for Depositories.

Investments in any one issuer, other than securities issued or guaranteed by the US government, that represent 5% or more of the total investments are:

| | | |
|---|---|---|
| FHLMC | 27.93% | $1,702,364 |
| FHLB | 22.46% | $1,368,786 |
| FNMA | 12.38% | $754,208 |

*Foreign Currency Risk*

Foreign currency risk is the risk that changes in exchange rates will adversely affect the fair value of an investment or a deposit. As of June 30, 2012, there were no deposits or investments denominated in foreign currencies, thus there was no foreign currency risk.

*Securities Lending*

The Treasurer of State is authorized by Indiana Code 5-13-10.5-13 to lend securities. Securities may be lent only if the agreement under which the securities are lent is collateralized by (1) cash or (2) interest bearing obligations that are issued by, fully insured by, or guaranteed by the United States, an agency of the United States, a federal instrumentality, or a federal government sponsored enterprise, in excess of the total market value of the loaned securities. The Treasurer of State is authorized by statute (IC 5-13-10.5) to accept as collateral safekeeping receipts for securities from: (1) a duly designated depository, having physical custody of securities, with a combined capital and surplus of at least $10 million, according to the last statement of condition filed by the financial institution with its governmental supervisory body. The Treasurer may not deposit aggregate funds in deposit accounts in any one designated depository in an amount or (2) a financial institution located either in or out of Indiana aggregating at any one time more than 50% of the combined capital, surplus and undivided profits of that depository as determined by the last published statement.

Indiana Code 5-13-10.5-13 states that securities may be lent only if the agreement under which the securities are lent is collateralized by (1) cash or (2) interest bearing obligations that are issued by, fully insured by, or guaranteed by the United States, an agency of the United States government, a federal instrumentality, or a federal government sponsored enterprise; in excess of the total market value of the loaned securities. State statutes and policies permit the State to lend securities to broker-dealers and other entities (borrowers) for collateral with a simultaneous agreement to return the collateral for the same securities in the future.

The State's custodial banks manage the securities lending programs and receive cash or securities as collateral. The types of securities lent during the year may include U.S. Treasury and agency obligations, corporate bonds/notes, and foreign bonds. Collateral securities and cash are initially pledged at 102% of the market value of the securities lent. Cash received as collateral is reported as an asset and a liability on the balance sheet. Securities received as non-cash collateral are not reported on the balance sheet because the State does not have the ability to pledge or sell them without a borrower default. Generally, there are no restrictions on the amount of assets that can be lent at one time, except for the Indiana Public Retirement System (fiduciary in nature component unit), which allow no more than 40% to be lent at one time.

Cash collateral may be invested. Cash collateral is generally invested in securities of a longer term with the mismatch of maturities generally 0-35 days. The weighted average maturity gap at June 30, 2012 was 12 days. The contracts with the State's custodians requires them to indemnify the funds if the borrowers fail to return the securities (and if the collateral is inadequate to replace the securities lent) or fail to pay the funds for income distributions by the securities' issuers while the securities are on loan.

At year end, the State had no credit risk exposure to any borrowers because the amount the State owes the borrowers exceeds the amounts the borrowers owe the State.

As of June 30, 2012, the fair values of the underlying securities on loan were:

| Security Type | Fair Value |
|---|---|
| U.S. Governments | $ 98,722 |
| U.S. Agencies | 80,707 |
| Total | $ 179,429 |

The fair values of the cash and non-cash collateral received were:

| Security Type | Fair Value |
|---|---|
| U.S. Governments | $ 100,744 |
| U.S. Agencies | 82,386 |
| Total | $ 183,130 |

Collateral percentage: 102.06%

| Collateral Type | Fair Value |
|---|---|
| Non-cash collateral | $ 100,744 |
| Cash collateral | 82,386 |
| Total | $ 183,130 |

***Major Moves Construction Fund/Next Generation Trust Funds***

*Investment Policy*

Indiana Code, Title 5, Article13, Chapters 9, 10, and 10.5, establishes the investment powers and guidelines regarding the State of Indiana investments. However, the Major Moves Construction Fund and the Next Generation Trust Fund have separate investment authority as established under Indiana Code 8-14-14 and Indiana Code 8-14-15, respectively. The Treasurer of State shall invest these funds in the same manner as the public employees' retirement fund under Indiana Code 5-10.3-5, except the funds may not be invested in equity securities. Investment Policy Statements for the investment of these two funds has been adopted by the Treasurer of State. The Investment Policy Statements are written in conformity with the applicable investment statutes and in accordance with prudent investor standards. There is no formal deposit policy other than compliance to State statute. State statute does not establish any parameters or guidelines related to the concentration of investment risk, investment credit risk, nor interest rate risk. The Investment Policy Statements establish asset allocations for both Funds and set limits for the exposure in securities from any one issuer to not more than 5% of a Core Fixed Income Investment Manager's portfolio and not more than 10% of a Core Plus Fixed Income Investment Manager's portfolio.

*Interest Rate Risk*

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of the investments. The Fund's policy for controlling its exposure to interest rate fluctuations should be viewed with the appropriate perspective. A long-term strategy was employed to achieve the Fund's objectives, but there was consideration given to the short-term liquidity needs to meet disbursements required by the Fund. The asset allocation and investment manager structure was designed to tolerate some interim fluctuations in market value while maintaining a long-term return objective of 5.25%.

The following table provides the interest rate risk disclosure for the Major Moves/Next Generation Trust Fund as of June 30, 2012:

| Major Moves/Next Generation Funds | | Investment Maturities (in Years) | | | |
|---|---|---|---|---|---|
| Investment Type | Fair Value | Less than 1 | 1 - 5 | 6- 10 | More than 10 |
| U.S Treasuries | $ 331,213 | $ 113,031 | $ 177,845 | $ 16,741 | $ 23,596 |
| U.S. Agencies | 39,253 | 18,968 | 9,697 | 6,042 | 4,546 |
| Government Asset and Mortgage Backed | 170,350 | - | 276 | 27,322 | 142,752 |
| Collateralized Mortgage Obligations | | | | | |
| Government CMOs | 35,448 | - | 390 | 7,232 | 27,826 |
| Corp CMOs | 25,084 | - | 142 | 5,205 | 19,737 |
| Corporate Bonds | 658,387 | 188,975 | 370,398 | 71,181 | 27,833 |
| Corporate Asset Backed | 151,544 | - | 68,869 | 16,503 | 66,172 |
| Private Placements | 242,672 | 16,141 | 174,219 | 31,276 | 21,036 |
| Municipal Bonds | 27,294 | 8,750 | 12,526 | 1,457 | 4,561 |
| Commercial Paper | 2,661 | 2,661 | - | - | - |
| Non US Government/Corp Bonds | 27,045 | 135 | 13,620 | 6,910 | 6,380 |
| Money Market Mutual Funds | 73,667 | 73,667 | - | - | - |
| | $ 1,784,618 | $ 422,328 | $ 827,982 | $ 189,869 | $ 344,439 |

*Custodial Credit Risk*

Deposits – The custodial credit risk for deposits is the risk that, in the event of the failure of a depository financial institution, a government will not be able to recover deposits or will not be able to recover collateral securities that are in the possession of an outside party.

At June 30, 2012, the balance of the State of Indiana's deposits was covered in full by federal depository insurance or by the Public Deposit Insurance Fund, which covers all public funds held in approved depositories.

Investment Custodial Credit Risk – The custodial credit risk for investments is the risk that, in the event of the failure of the counterparty to a transaction, a government will not be able to recover the value of investment or collateral securities that are in the possession of an outside party. Investments are exposed to custodial credit risk if the securities are uninsured and unregistered and are either held by the counterparty's trust department or agent, but not in the name of the State of Indiana. None of the State's investments are exposed to custodial credit risk because they are held in the name of the State of Indiana. Additionally, the Treasurer of State requires all custodians to indemnify the State against all out-of-pocket expenses or losses incurred as a result of (i) the custodian's operational failure, (ii) custodians failure to carry out the credit analysis, (iii) custodian's failure to maintain proper collateral for each loan, or (iv) failure of an approved counterparty to comply with its obligations under the applicable securities lending agreement.

*Credit Risk*

Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations.

The investment managers must adhere to the following guidelines:

Intermediate and Core Fixed Income Managers

a. The average credit quality of each manager's portfolio shall not be lower than Aa3/AA-
b. All securities at the time of purchase shall have a Moody's, S&P's and/or Fitch's credit quality rating of no less than BBB
c. In the event a holding is downgraded to less than BBB, the manager will have the discretion over when to sell the security, generally, no later than 90 days following the downgrade.

Core Plus Fixed Income Managers

d. At least 60% of the securities held in the portfolio shall have a credit rating of no less than BBB
e. Investments in high-yield and non-US debt are permitted, but combined exposure to those sectors should not exceed 40%
f. The average credit quality of each manager's portfolio shall not be lower than single A

Hybrid Fixed Income Managers

g. High-yield and non-US debt securities are permitted
h. Non US-dollar currency exposure is permitted

The following table provides information on the credit quality ratings for investments in debt securities, short-term money market funds, bond mutual funds and bond commingled funds, municipal securities, asset-backed, and mortgage-backed securities as of June 30, 2012. The following table below reflects the “greatest risk” rating (the credit rating reflecting the greatest degree of risk) as set by three nationally recognized rating organizations (S&P, Moody, and Fitch) for each type of investment.

**Major Moves/Next Generation Funds**

| | Greatest Risk | |
|---|---|---|
| Investment Type | Ratings | Fair Value |
| U.S. Treasuries | AA | $ 331,213 |
| U.S. Agencies | AA | 34,444 |
| | A | 4,302 |
| | NR | 507 |
| Government Asset and Mortgage Backed | AA | 131,953 |
| | NR | 38,397 |
| Collateralized Mortgage Obligations | | |
| Government CMO's | AA | 35,448 |
| Corporate CMO's | AAA | 11,561 |
| | AA | 1,253 |
| | A | 1,145 |
| | BBB | 1,004 |
| | BB | 111 |
| | B | 1,867 |
| | CCC&Below | 6,889 |
| | NR | 1,254 |
| Non US Govt/Corp Bonds | AAA | - |
| | AA | - |
| | A | 4,657 |
| | BBB | 14,888 |
| | BB | 6,480 |
| | B | 278 |
| | CCC&Below | - |
| | NR | 742 |
| Corporate Bonds | AAA | 6,860 |
| | AA | 36,548 |
| | A | 278,659 |
| | BBB | 257,928 |
| | BB | 33,520 |
| | B | 27,964 |
| | CCC&Below | 11,843 |
| | NR | 5,065 |
| Corporate Asset and Mortgage Backed | AAA | 125,369 |
| | AA | 13,280 |
| | A | 6,418 |
| | BBB | 1,968 |
| | BB | 193 |
| | B | 1,467 |
| | CCC&Below | 2,364 |
| | NR | 485 |
| Private Placements | AAA | 40,348 |
| | AA | 24,399 |
| | A | 21,994 |
| | BBB | 32,639 |
| | BB | 8,548 |
| | B | 15,903 |
| | CCC&Below | 13,361 |
| | NR | 85,480 |
| Commercial Paper | A | 2,481 |
| | NR | 180 |
| Municipal Bonds | AAA | - |
| | AA | 14,022 |
| | A | 12,369 |
| | BBB | 866 |
| | BB | 37 |
| | NR | - |
| Money Market Mutual Funds | NR | 73,667 |
| Total | | $ 1,784,618 |

*Concentration of Credit Risk*

Concentration of credit risk is the risk of loss attributed to the magnitude of a government's investment in a single issuer representing 5% or more of the total investments. The only exemptions from disclosures are US Government Debt, US Government Guaranteed Investments, Mutual Funds, or External Investment Pools. For Intermediate and Core Fixed Income Managers, securities in any one issuer should be limited to not more than 5% of the investment manager's portion of the Fund portfolio measured at market value. For Core Plus Fixed Income Managers, the exposure of each manager's portfolio should be limited to not more than 10% of the manager's portion of the Fund portfolio measured at market value.

Investments in any one issuer that represent 5% or more of the total investments are:

FNMA 7.31% $128,410,810

*Foreign Currency Risk*

Foreign currency risk is the risk that changes in exchange rates will adversely affect the fair value of an investment or a deposit. The Major Moves/Next Generation Trust Fund's foreign currency exposure is focused primarily in fixed income securities. The exposure to foreign currency fluctuation is as follows:

| Currency | Combined Total | % of Total Market Value |
|---|---|---|
| Brazil Real | $ 2,709 | 0.16 |
| Chilean Peso | 213 | 0.01 |
| Columbian Peso | 1,544 | 0.09 |
| Euro | (3,370) | -0.19 |
| Hungarian Forint | 316 | 0.02 |
| Indonesian Rupian | 738 | 0.04 |
| Malaysian Ringgit | 1,628 | 0.09 |
| Mexico New Peso | 5,766 | 0.33 |
| New Turkish Lira | 336 | 0.02 |
| Philippines Peso | 723 | 0.04 |
| Russian Rubel | 829 | 0.05 |
| South African Comm | 866 | 0.05 |
| South Korean Won | 1,027 | 0.06 |
| Uruguayan Peso | 2,157 | 0.12 |
| Others | 74 | 0.01 |
| Total | $ 15,556 | 0.90 |

*Securities Lending*

The Treasurer of State is authorized by Indiana Code 5-13-10.5-13 to lend securities. Securities may be lent only if the agreement under which the securities are lent is collateralized by (1) cash or (2) interest bearing obligations that are issued by, fully insured by, or guaranteed by the United States, an agency of the United States, a federal instrumentality, or a federal government sponsored enterprise, in excess of the total market value of the loaned securities.

At year end, the State had no credit risk exposure to any borrowers because the amount the State owes the borrowers exceeds the amounts the borrowers owe the State.

As of June 30, 2012, the fair values (in thousands) of the underlying securities on loan were:

| Security Type | Fair Value |
|---|---|
| U.S. Governments | $ 324,031 |
| U.S. Corporates | 16,439 |
| Total | $ 340,470 |

The fair values of the cash and non-cash collateral received were:

| Security Type | Fair Value |
|---|---|
| U.S. Governments | $ 330,677 |
| U.S. Corporates | 16,885 |
| Total | $ 347,562 |

Collateral percentage: 102.08%

| Collateral Type | Fair Value |
|---|---|
| Non-cash collateral | $ 287,610 |
| Cash collateral | 59,952 |
| Total | $ 347,562 |

***TrustINdiana, Local Government Investment Pool (Investment Trust Funds)***

*Investment Policy*

Indiana Code, Title 5, Article13, Chapter 9, Section 11 established the local government investment pool (TrustINdiana) within the office and custody of the Treasurer of State. The Treasurer of State shall invest the funds in TrustINdiana in the same manner, in the same type of instruments, and subject to the same limitations provided for the deposit and investment of state funds by the Treasurer of State under Indiana Code 5-13-10.5. State statute does not establish any parameters or guidelines related to the concentration of investment risk, investment credit risk, nor interest rate risk. However, pursuant to IC 5-13-9-11(g)(7), no less than fifty percent of funds available for investment shall be deposited in banks qualified to hold deposits of participating local government entities. Investment criteria have been established to create the principles and procedures by which the funds of TrustINdiana shall be invested and to comply with state statute relating to the investment and deposit of public funds.

*Valuation of Investments*

Consistent with the provisions of a 2a-7 like pool as defined by GASB Statement No. 31, TrustINdiana securities are valued at amortized cost, which approximates market value.

*Interest Rate Risk*

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

The following is a summary of the Interest Rate Risk Disclosure as of June 30, 2012:

**TrustINdiana - Local Government Investment Pool**

| Investment Type | Amortized Cost | Investment Maturity (in Years) Less than 1 |
|---|---|---|
| U.S. Agencies | $ 39,079 | $ 39,079 |
| Commercial Paper | 110,667 | 110,667 |
| Total | $ 149,746 | $ 149,746 |

*Custodial Credit Risk*

Deposits – The custodial credit risk for deposits is the risk that, in the event of the failure of a depository financial institution, a government will not be able to recover deposits or will not be able to recover collateral securities that are in the possession of an outside party.

At June 30, 2012, the balance of all bank deposits were covered in full by federal depository insurance or by the Public Deposit Insurance Fund, which covers all public funds held in approved depositories.

Investment Custodial Credit Risk – The custodial credit risk for investments is the risk that, in the event of the failure of the counterparty to a transaction, a government will not be able to recover the value of investment or collateral securities that are in the possession of an outside party. Investments are exposed to custodial credit risk if the securities are uninsured and unregistered and are either held by the counterparty's trust department or agent, but not in the name of the State of Indiana. None of the State's investments are exposed to custodial credit risk because they are held in the name of the State of Indiana. Additionally, the Treasurer of State requires all custodians to indemnify the State against all out-of-pocket expenses or losses incurred as a result of (i) the custodian's operational failure, (ii) custodians failure to carry out the credit analysis, (iii) custodian's failure to maintain proper collateral for each loan, or (iv) failure of an approved counterparty to comply with its obligations under the applicable securities lending agreement.

*Credit Risk*

Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. TrustINdiana limits its investments in any one issuer to the highest rating category issued by one nationally recognized statistical rating organization.

The following table provides information on the credit quality ratings for investments in TrustINdiana:

**TrustINdiana - Local Government Investment Pool**

| Investment Type | Greatest Risk Ratings | Fair Value |
|---|---|---|
| U.S. Agencies | AA+ | $ 39,079 |
| Commercial Paper | A1 | 110,667 |
| Total | | $149,746 |

*Concentration of Credit Risk*

Concentration of credit risk is the risk of loss attributed to the magnitude of a government's investment in a single issuer representing 5% or more of the total investments. As noted above, TrustINdiana is required to be comprised of no less than 50% of deposits in banks from an approved list maintained by the State of Indiana. In addition, TrustINdiana limits its investments in any one issuer to 40% of net assets if the issuer is rated A1+/P1 and 25% of net assets if the issuer is rated A1/P1. The only exemptions from disclosures are US Government Debt, US Government Guaranteed Investments, Mutual Funds, or External Investment Pools.

Investments in any one issuer, not exempt from disclosure, that represents 5% or more of the total investments were (amount in thousands):

| | | |
|---|---|---|
| Federal Farm Credit Bank | 8.71% | $ 32,564 |

*Securities Lending*

The Treasurer of State is authorized by Indiana Code 5-13-10.5-13 to lend securities. Securities may be lent under an agreement which requires the loaned securities to be collateralized in the form of (1) cash or (2) interest bearing obligations that are issued by, fully insured by, or guaranteed by the United States, an agency of the United States, a federal instrumentality, or a federal government sponsored enterprise, in an amount at least equal to 102% of the current market value of the loaned securities. The net income earned through securities lending is recorded as additional income to the Pool. As of June 30, 2012, there were no securities on loan and therefore, no credit risk exposure.

### 2. *Pension and Other Employee Benefit Trust Funds – Primary Government*

*State Police Pension Fund*

*Investment Policy* – The Indiana State Police Pension Trust was established in 1937 to provide pension, death, survivor, and other benefits to present and former employees of the department and their beneficiaries who meet the statutory requirement for such benefits.

Indiana Code 10-1-2-2(c), established the prudent investor standard as the primary statutory provision governing the investment of the Trust's assets. IC 10-1-2-2 (c) reads as follows:

The trust fund may not be commingled with any other funds and shall be invested only in accordance with Indiana laws for the investment of trust funds, together with such other investments as are specifically designated in the pension trust. Subject to the terms of the pension trust, the Trustee, with the approval of the Department and the Pension Advisory Board, may establish investment guidelines and limits on all types of investments (including, but not limited to, stocks and bonds) and take other action necessary to fulfill its duty as a fiduciary for the trust fund. However, the Trustee shall invest the trust fund assets with the same care, skill, prudence, and diligence, that a prudent person acting in a like capacity and familiar with such matters would use in the conduct of an enterprise of a like character with like aims. The Trustee shall also diversify such investments in accordance with prudent investment standards. There is no formal deposit policy other than compliance to State statute.

*Credit Risk* – Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations.

The following table provides information on the credit quality ratings for investments in debt securities, short term money market funds, bond mutual/commingled funds, municipal securities, asset-backed, and mortgage backed securities for the State Police Pension Trust. The table reflects the "greatest risk" rating (the credit rating reflecting the greatest degree of risk) as set by three nationally recognized rating organizations (S&P, Moody, and Fitch) for each investment type.

**State Police Pension**

| Investment Type | Greatest Risk Ratings | Fair Value |
|---|---|---|
| U.S. Treasuries | AA | $ 10,885 |
| U.S. Agencies Assets and Mortgage | AA | 13,318 |
| Backed Securities | NR | 2,540 |
| Collateralized Mortgage Obligations | | |
| Corporate CMO's | AAA | 1,034 |
| | CCC & Below | 209 |
| | NR | 111 |
| U.S. Agencies CMOs | AA | 2,786 |
| | NR | 921 |
| Corporate Bonds | AA | 644 |
| | A | 7,374 |
| | BBB | 13,831 |
| | BB | 2,006 |
| | B | 657 |
| | NR | 136 |
| Corporate Asset Backed | AAA | 7,277 |
| | AA | 869 |
| | A | 1,200 |
| | BBB | 1,126 |
| | BB | 19 |
| | B | 16 |
| | CCC & Below | 285 |
| | NR | 200 |
| Foreign Bonds | A | 380 |
| | BBB | 160 |
| Private Placements | AAA | 585 |
| | AA | 161 |
| | A | 797 |
| | BBB | 2,317 |
| | BB | 213 |
| | CCC & Below | 29 |
| Municipal Bonds | AAA | 236 |
| | AA | 1,779 |
| | A | 553 |
| | BBB | 312 |
| | NR | 170 |
| Mutual/Commingled Funds | NR | 197,356 |
| Total | | $ 272,492 |

*Custodial Credit Risk*

Deposits – The custodial credit risk for deposits is the risk that, in the event of the failure of a depository financial institution, a government will not be able to recover deposits or will not be able to recover collateral securities that are in the possession of an outside party.

At June 30, 2012, the balance of the State Police Pension Trust deposits was covered in full by federal depository insurance or by the Public Deposit Insurance Fund, which covers all public funds held in approved depositories.

Investment Custodial Credit Risk – The custodial credit risk for investments is the risk that, in the event of the failure of the counterparty to a transaction, a government will not be able to recover the value of investment or collateral securities that are in the possession of an outside party. Investments are exposed to custodial credit risk if the securities are uninsured and unregistered and are either held by the counterparty's trust department or agent, but not in the name of the customer. None of the Indiana State Police Pension Trust's investments are exposed to custodial credit risk because they are held in the name of the Indiana State Police Pension Trust. Additionally, the Treasurer of State requires all custodians to indemnify the State against all out-of-pocket expenses or losses incurred as a result of (i) the custodian's operational failure, (ii) custodians failure to carry out the credit analysis, (iii) custodian's failure to maintain proper collateral for each loan, or (iv) failure of an approved counterparty to comply with its obligations under the applicable securities lending agreement.

*Concentration of Credit Risk* – Concentration of credit risk is the risk of loss attributed to the magnitude of a government's investment in a single issuer. The Indiana State Police Trust has thirteen different investments managers. The purchase of securities in any one nongovernmental corporation shall be limited to an initial cost of 5% of the market value of an investment manager's portfolio. Additionally, the following limits are set to further limit credit exposure:

Large/Mid/Small Capitalization Equity Managers: equity holdings in any one company should not exceed 7.5% of the market value of the investment manager's portion of the Fund's portfolio. Equity holdings in any one industry should not exceed 25% of the market value of the investment manager's portion and equity holdings in any one sector should not exceed 35% of the investment manager's portfolio market value.

Non-US Equity Investment Managers: equity holdings in any one international company shall not exceed 7.5% of the total value of all investments in international equity securities and equity holdings in any one country shall not exceed 35% of all investments in international equity securities.

Domestic Core Fixed/ Domestic Core Plus/Hybrid Managers: securities of any one issuer are limited to not more that 5% of the investment manager's portion of the portfolio measured at market value. Securities backed by the full faith and credit of the United States Government or any of its instrumentalities shall not be subject to exposure limitations. Investments in high-yield and non-US debt securities should be limited to 20% high-yield and 20% non-U.S. debt with a combined exposure to those sectors not to exceed 30%.

There were no investments in any one issuer that represents 5% or more of the total investments.

*Interest Rate Risk* – Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of the investments. The Fund's policy for controlling its exposure to interest rate fluctuations should be viewed with the appropriate perspective. A long-term strategy was employed to achieve the Fund's objectives, but there was consideration given to the short-term liquidity needs to meet disbursements required by the Fund. The asset allocation and investment manager structure was designed to tolerate some interim fluctuations in market value while maintaining a long-term return objective to exceed the actuarial assumed interest rate of 6.75%.

The following table provides the interest rate risk disclosure for the Indiana State Police Pension Fund:

**State Police Pension**

| Investment Type | Fair Value | Investment Maturities (in Years) Less than 1 | 1 - 5 | 6- 10 | More than 10 |
|---|---|---|---|---|---|
| U.S. Treasuries | $ 10,885 | $ 110 | $ 4,005 | $ 3,766 | $ 3,004 |
| U.S. Agencies | 19,565 | 2,926 | 273 | 1,337 | 15,029 |
| Collateralized Mortgage Obligations | | | | | |
| Corporate CMO's | 1,354 | - | 22 | 146 | 1,186 |
| Corporate Bonds | 24,648 | 1,852 | 6,585 | 11,465 | 4,746 |
| Corporate Asset Backed | 10,992 | 2,313 | 3,064 | 157 | 5,458 |
| Foreign Bonds | 540 | 261 | 279 | - | - |
| Private Placements | 4,102 | 236 | 1,563 | 1,962 | 341 |
| Municipal Bonds | 3,050 | - | 449 | 192 | 2,409 |
| Mutual/Commingled Funds | 197,356 | 197,356 | - | - | - |
| Total Fixed Income Securities | $ 272,492 | $ 205,054 | $ 16,240 | $ 19,025 | $ 32,173 |

*Foreign Currency Risk* – Foreign currency risk is the risk that changes in exchange rates will adversely affect the fair value of an investment or a deposit. The State Police Pension Trust's foreign currency exposure is focused primarily in international and global equity holdings. The exposure to foreign currency fluctuation is as follows:

| Currency | Market Value | % of Total Market Value |
|---|---|---|
| Australian Dollar | $ 410 | 0.11% |
| Brazil Real | 299 | 0.08 |
| Canadian Dollar | 445 | 0.12 |
| Danish Krone | 176 | 0.05 |
| Euro | 3,629 | 0.94 |
| Hong Kong | 210 | 0.05 |
| Japanese Yen | 968 | 0.25 |
| Norwegian Krone | 380 | 0.10 |
| Pound Sterling | 1,837 | 0.48 |
| S. African Rand | 88 | 0.02 |
| Swiss Franc | 893 | 0.23 |
| Total | $ 9,335 | 2.43% |

*Securities Lending* - The Treasurer of State is authorized by Indiana Code 5-13-10.5-13 to lend securities. Securities may be lent only if the agreement under which the securities are lent is collateralized by (1) cash of (2) interest bearing obligations that are issued by, fully insured by, or guaranteed by the United States, an agency of the United States, a federal instrumentality, or a federal government sponsored enterprise. The market value of the required collateral must be in an amount at least equal to 102% of the current market value of the loaned securities. As of June 30, 2012, the State Police Pension Trust had received cash as collateral in an amount exceeding 102% of the fair value of the underlying securities on loan. The State Police Pension Trust recorded the value of the cash collateral received as an asset in the accompanying financial statements. A corresponding liability has also been recorded because the cash collateral must be returned to the borrower upon expiration of the loan. The lending agent invests the cash collateral received by the borrowers. The weighted average maturity of the cash collateral investments generally matched the term of the securities loans.

At year end, the State Police Pension Trust had no credit risk exposure to any borrowers because the amount the State Police Pension Trust owes the borrowers exceeds the amounts the borrowers owe the State Police Pension Trust.

As of June 30, 2012, all lent securities were collateralized with cash. The fair value of the securities on loan was:

| Security Type | Fair Value |
|---|---|
| U.S. Governments | $ 2,431 |
| U.S. Equities | 2,317 |
| Total | $ 4,748 |

*State Employee Retiree Health Benefit Trust Fund-DB*

*Investment Policy* – The State Retiree Health Benefit Trust Fund – DB fund is comprised of the State Police Retiree Health Benefit Trust Fund, the

SPD OPEB Trust Fund, the DNR OPEB Trust Fund, and the ATC/Excise OPEB Trust Fund.

The State Police Retiree Health Benefit Trust Fund consists of sections 401(h) and 115 established pursuant to the Internal Revenue Service that are separate accounts established within the State Police Pension Fund for the purpose of paying benefits for sickness, accident, hospitalization, and medical expenses. The assets in this account may be commingled for investment purposes only with the other accounts of the Indiana State Police Pension Fund. The investment authority for this Fund, since it is to be invested in the same manner as the State Police Pension Fund, is established under Indiana Code IC 10-12-2-2(c). There is no formal deposit policy other than compliance to State statute.

IC 10-12-2-2(c) reads as follows:

The trust fund shall be invested only in accordance with Indiana laws for the investment of trust funds, together with such other investments as are specifically designated in the pension trust. Subject to the terms of the pension trust, the Trustee, with the approval of the Department and the Pension Advisory Board, may establish investment guidelines and limits on all types of investments (including, but not limited to, stocks and bonds) and take other action necessary to fulfill its duty as a fiduciary for the trust fund. However, the Trustee shall invest the trust fund assets with the same care, skill, prudence, and diligence, that a prudent person acting in a like capacity and familiar with such matters would use in the conduct of an enterprise of a like character with like aims. The Trustee shall also diversify such investments in accordance with prudent investment standards.

The SPD, DNR, and the ATC/Excise OPEB Trust Funds were established pursuant to HEA 1123 of the 2012 Indiana General Assembly. The State Personnel Department administers the SPD OPEB Trust Fund. The Department of Natural Resources administers the DNR OPEB Trust Fund. The ATC/Excise OPEB Trust Fund is administered by the Alcohol and Tobacco Commission. These trust funds were created to provide for the prefunding of annual required contributions and for covering the OPEB liability of covered individuals. The Treasurer of State shall invest monies in these trust funds not currently needed to meet the obligations of the trust funds in the same manner as other public money may be invested. Indiana Code, Title 5, Article13, Chapters 9, 10, and 10.5, establishes the investment powers and guidelines regarding the State of Indiana investments. There are no formal deposit and investment policies for the investment of these funds other than compliance to State statute. State statute does not establish any parameters or guidelines related to the concentration of investment risk, investment credit risk, nor interest rate risk.

*Credit Risk* – Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations.

The following table provides information on the credit quality ratings for investments in the State Retiree Health Benefit Trust Fund-DB:

**State Retiree Health Benefit Trust Fund - DB**

| Investment Type | Greatest Risk Ratings | Fair Value |
|---|---|---|
| U.S. Agencies | AA+ | $ 13,755 |
| Certificate of Deposits | NR | 685 |
| Total | | $ 14,440 |

*Custodial Credit Risk*

Deposits – The custodial credit risk for deposits is the risk that, in the event of the failure of a depository financial institution, a government will not be able to recover deposits or will not be able to recover collateral securities that are in the possession of an outside party.

At June 30, 2012, the balance of any bank deposits was covered in full by federal depository insurance or by the Public Deposit Insurance Fund, which covers all public funds held in approved depositories.

Investment Custodial Credit Risk – The custodial credit risk for investments is the risk that, in the event of the failure of the counterparty to a transaction, a government will not be able to recover the value of investment or collateral securities that are in the possession of an outside party. Investments are exposed to custodial credit risk if the securities are uninsured and unregistered and are either held by the counterparty's trust department or agent, but not in the name of the State of Indiana. None of the State's investments are exposed to custodial credit risk because they are held in the name of the State of Indiana. Additionally, the Treasurer of State requires all custodians to indemnify the State against all out-of-pocket expenses or losses incurred as a result of (i) the custodian's operational failure, (ii) custodians failure to carry out the credit analysis, (iii) custodian's failure to maintain proper collateral for each loan, or (iv) failure of an approved counterparty to comply with its obligations under the applicable securities lending agreement.

*Concentration of Credit Risk* – Concentration of credit risk is the risk of loss attributed to the magnitude of a government's investment in a single issuer representing 5% or more of the total investments. The only exemptions from disclosures are US Government Debt, US Government Guaranteed Investments, Mutual Funds, or External Investment Pools.

Investments in any one issuer, not exempt from disclosure, that represent 5% or more of the total investments were:

| | | |
|---|---|---|
| Federal Home Loan Banks | 48.47% | $ 6,999 |
| Federal National Mortgage Assoc. | 20.13 | 2,906 |
| Federal Agricultural Mortgage Corp. | 26.66 | 3,849 |

*Foreign Currency Risk* – Foreign currency risk is the risk that changes in exchange rates will adversely affect the fair value of an investment or a deposit. There was no foreign currency risk.

*Securities Lending* - The Treasurer of State is authorized by Indiana Code 5-13-10.5-13 to lend securities. Securities may be lent only if the agreement under which the securities are lent is collateralized by (1) cash or (2) interest bearing obligations that are issued by, fully insured by, or guaranteed by the united states, an agency of the United State, an agency of the united States government, a federal instrumentality, or a federal government sponsored enterprise in excess of the total market value of the loaned securities.

At year end, there were no securities on loan and therefore, no credit risk exposure.

*Interest Rate Risk* – Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment.

The following is a summary of the Interest Rate Risk Disclosure as of June 30, 2012:

**State Retiree Health Benefit Trust Fund - DB**

| | | Investment Maturities (in Years) | |
|---|---|---|---|
| Investment Type | Fair Value | Less than 1 | 1 - 5 |
| U.S. Agencies | $ 13,754 | $ 11,848 | $ 1,906 |
| Certificate of Deposits | 685 | 685 | - |
| Total Fixed Income Securities | $ 14,439 | $ 12,533 | $ 1,906 |

*State Employee Retiree Health Benefit Trust Fund-DC*

*Investment Policy* – Indiana Code, Title 5, Article13, Chapters 9, 10, and 10.5, establishes the investment powers and guidelines regarding the State of Indiana investments. However, the Retiree Health Benefit Trust Fund has separate investment authority as established under Indiana Code 5-10-8-8.5 (b). The Treasurer of State shall invest the money in the trust fund not currently needed to meet the obligations of the trust fund in the same manner as other public money may be invested. There are no formal deposit and investment policies for the investment of these funds other than compliance to State statute. State statute does not establish any parameters or guidelines related to the concentration of investment risk, investment credit risk, nor interest rate risk.

*Credit Risk* – Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations.

The following table provides information on the credit quality ratings for investments in State Retiree Health Benefit Trust Fund:

**State Employee Retiree Health Benefit Trust Fund - DC**

| Investment Type | Greatest Risk Rating | Fair Value |
|---|---|---|
| U.S. Agencies | AAA | $ 5,002 |
| | AA+ | 155,839 |
| Total | | $ 160,841 |

*Custodial Credit Risk*

Deposits – The custodial credit risk for deposits is the risk that, in the event of the failure of a depository financial institution, a government will not be able to recover deposits or will not be able to recover collateral securities that are in the possession of an outside party.

At June 30, 2012, the balance of any bank deposits was covered in full by federal depository insurance or by the Public Deposit Insurance Fund, which covers all public funds held in approved depositories.

Investment Custodial Credit Risk – The custodial credit risk for investments is the risk that, in the event of the failure of the counterparty to a transaction, a government will not be able to recover the value of investment or collateral securities that are in the possession of an outside party. Investments are exposed to custodial credit risk if the securities are uninsured and unregistered and are either held by the counterparty's trust department or agent, but not in the name of the State of Indiana. None of the State's investments are exposed to custodial credit risk because they are held in the name of the State of Indiana. Additionally, the Treasurer of State requires all custodians to indemnify the State against all out-of-pocket expenses or losses incurred as a result of (i) the custodian's operational failure, (ii) custodians failure to carry out the credit analysis, (iii) custodian's failure to maintain proper collateral for each loan, or (iv) failure of an approved counterparty to comply with its obligations under the applicable securities lending agreement.

*Concentration of Credit Risk* – Concentration of credit risk is the risk of loss attributed to the magnitude of a government's investment in a single issuer representing 5% or more of the total investments. The only exemptions from disclosures are US Government Debt, US Government Guaranteed Investments, Mutual Funds, or External Investment Pools.

Investments in any one issuer, not exempt from disclosure, that represent 5% or more of the total investments were:

| | | |
|---|---|---|
| Federal Home Loan Banks | 31.11% | $ 50,038 |
| Federal Home Loan Mortgage Corp. | 24.94% | 40,112 |
| Federal National Mortgage Association | 40.84% | 65,689 |

*Foreign Currency Risk* – Foreign currency risk is the risk that changes in exchange rates will adversely affect the fair value of an investment or a deposit. There was no foreign currency risk.

*Securities Lending* - The Treasurer of State is authorized by Indiana Code 5-13-10.5-13 to lend securities. Securities may be lent only if the agreement under which the securities are lent is collateralized by (1) cash or (2) interest bearing obligations that are issued by, fully insured by, or guaranteed by the United States, an agency of the United States, an agency of the United States government, a federal instrumentality, or a federal government sponsored enterprise in excess of the total market value of the loaned securities.

At year end, there were no securities on loan and therefore, no credit risk exposure.

*Interest Rate Risk* – Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment.

The following is a summary of the Interest Rate Risk Disclosure as of June 30, 2012:

**State Employee Retiree Health Benefit Trust Fund - DC**

| | | Investment Maturities (in Years) | |
|---|---|---|---|
| Investment Type | Fair Value | Less than 1 | 1 - 5 |
| U.S. Agencies | $ 160,841 | $ 70,046 | $ 90,795 |
| Total Fixed Income Securities | $ 160,841 | $ 70,046 | $ 90,795 |

### *3. Pension Trust Funds – Fiduciary in Nature Component Unit*

*Indiana Public Retirement System*

*Investment Guidelines and Limitations* – The Indiana General Assembly enacted the prudent investor standard to apply to the INPRS Board of Trustees and govern all its investments. Under statute (IC 5-10.3-5-3(a)) for PERF and (IC 5-10.4-3-10(a)) for TRF, the Board of Trustees must "invest its assets with the care, skill, prudence and diligence that a prudent person acting in a like capacity and familiar with such matters would use in the conduct of an enterprise of a like character with like aims." The Board of Trustees also is required to diversify such investments in accordance with the prudent investor standard.

Within these governing statutes, the INPRS Board of Trustees has broad authority to invest the assets of the plans. The INPRS Board of Trustees utilizes external investment managers, each with specific mandates to achieve the investment objectives of the retirement funds. Depending on the mandate and the contractual agreement with the investment manager, investments may be managed in separate accounts, commingled accounts, mutual funds or other structures acceptable to the INPRS Board of Trustees. An asset allocation review is conducted periodically.

Effective January 1, 2012, the INPRS Board of Trustees adopted a new Investment Policy Statement and the new strategic asset allocation for the Consolidated Defined Benefit Assets is as follows:

| Asset Classes | Target Allocation - % | Allowable Ranges - % |
|---|---|---|
| Public Equity | 22.5 | 20-25 |
| Private Equity | 10 | 7-13 |
| Fixed Income - Ex Inflation - Linked | 22 | 19-25 |
| Fixed Income - Inflation - Linked | 10 | 7-13 |
| Commodities | 8 | 6-10 |
| Real Estate | 7.5 | 4-11 |
| Absolute Return | 10 | 6-14 |
| Risk Parity | 10 | 5-15 |

Contributions and asset reallocation in the PERF and TRF Annuity Savings Accounts and the Legislators' Defined Contribution Plan (LEDC) are directed by the members in each plan and as such, the asset allocation will differ from that of the Consolidated Defined Benefit Assets.

The Pension Relief Fund (PR Fund) is invested 100 percent in a money market fund. The State Employees' Death Benefit Fund and the Public Safety Officers' Special Death Benefit Fund are 100 percent invested in fixed income investments.

The following key factors are used in the analysis of the investment performance of the retirement funds:

- Net of fees, 10-year rolling annual rate of return equal to the target rate of return for the retirement funds.
- Net of fees, 1-year and 3-year rolling investment rate of return of the retirement funds, no less than a weighted average of benchmark indices which best describe the retirement funds' asset allocation.
- Net of fees, 3-year and 5-year Sharpe Ratio of the retirement funds, no less than a weighted average of benchmark indices' Sharpe Ratio which best describe the retirement funds' asset allocation.

*Custodial Credit Risk* – Deposits, investment securities, and collateral securities are exposed to custodial credit risk if they are uninsured and uncollateralized. Custodial credit risk is the risk that, in the event of a failure of the counterparty, that INPRS will not be able to recover the value of its deposits, investments or collateral securities that are in the possession of an outside party. Investment securities are exposed to risk if the securities are uninsured, are not registered in the name of INPRS and are held by either the counterparty or the counterparty trust department's agent, but not in INPRS' name.

Per IC 5-10.3-5-4(a) and IC 5-10.3-5-5 for PERF and IC 5-10-4-3-14(a)) and IC 5-10.4-3-13 for TRF, securities are required to be held for the fund under custodial agreements. INPRS' custody agreement with the custodian requires that the custodian segregate the securities on the custodian's books and records from the custodian's own property. In addition, any investment manager for INPRS is not allowed, under any circumstances, to take possession, custody, title, or ownership of any managed assets.

There was no custodial credit risk for investments including investments related to securities lending collateral as of June 30, 2012.

Deposits are exposed to custodial credit risk if they are not covered by depository insurance and the deposits are uncollateralized or collateralized with securities held by the pledging financial institution. Deposits held in the demand deposit accounts are carried at cost and are insured up to $250 thousand for each institution. Deposits in the demand accounts held in excess of $250 thousand are not collateralized. Deposits with the Indiana Treasurer of State are entirely insured. Deposits held with the investment custodian are insured up to $250 thousand. Deposits held with brokers and counterparties are carried at cost and are not insured or collateralized.

| **Cash Deposits** | **Total** |
|---|---|
| Demand Deposit Account – Bank Balances | $ 12,684 |
| Held with Treasurer of State | 15,451 |
| Held with Counterparties | 10 |
| Held with Brokers | 323,859 |
| Total | $ 352,004 |

*Interest Rate Risk* – Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of the investments. Duration is a measure of interest rate risk. The longer the maturity, the more the value of the fixed-income investment will fluctuate with interest rate changes. The INPRS Investment Policy Statement recognizes interest rate risk as a market risk factor that is monitored on an absolute and relative basis.

As of June 30, 2012 the debt securities had the following duration information:

| Debt Security Type | Fair Value 6/30/2012 | % of All Debt Securities | Portfolio Weighted Average Effective Duration (Years) |
|---|---|---|---|
| **Short Term Investments** | | | |
| Cash at Brokers | $ 323,859 | 2.3% | 0 |
| Money Market Sweep Vehicle | 1,749,484 | 12.3% | 0.01 |
| Commercial Paper | 3,000 | 0.0% | 0.01 |
| U.S. Treasury Obligations | 413,976 | 2.9% | 0 |
| Non-U.S. Government | 3,720 | 0.0% | 0 |
| **Total Short Term Investments** | **2,494,039** | **17.6%** | |
| **Fixed Income Investments** | | | |
| U.S. Governments | 3,497,061 | 24.7% | 1.78 |
| Non-U.S. Government | 723,737 | 5.1% | 0.43 |
| U.S. Agencies | 1,589,888 | 11.2% | 0.42 |
| Corporate Bonds | 3,451,561 | 24.4% | 1.12 |
| Asset-Backed Securities | 1,141,669 | 8.1% | 0.19 |
| Duration Not Available | 1,268,918 | 9.0% | N/A |
| **Total Fixed Income Investments** | **11,672,834** | **82.4%** | |
| **Total Debt Securities** | **$ 14,166,873** | **100.0%** | |

The $1,269 million, for which no duration was available, is primarily made up of commingled debt funds.

*Credit Risk* – The credit risk of investments is the risk that the issuer will default and not meet their obligations. The INPRS Investment Policy Statement recognizes credit (quality) risk as a market and strategic risk factor that is monitored on an absolute and relative basis.

The quality rating of investments in debt securities as described by Moody's at June 30, 2012 is as follows:

| Moody's Rating | Total | Percentage of Debt & Cash Equivalents |
|---|---|---|
| Aaa | $ 6,490,994 | 45.7% |
| US Government Guaranteed | 433,768 | 3.1% |
| Aa | 363,980 | 2.6% |
| A | 1,134,046 | 8.0% |
| Baa | 1,643,343 | 11.6% |
| Ba | 224,041 | 1.6% |
| B | 151,288 | 1.1% |
| Below B | 61,090 | 0.4% |
| Unrated | 3,664,323 | 25.9% |
| Subtotal | 14,166,873 | 100.0% |
| Cash - not applicable | - | |
| Total | $14,166,873 | |

The $3,664 million not rated by Moody's is primarily in the following security types: cash at broker, money market sweep vehicles, asset-backed securities, commercial mortgages, CMO/Remics and commingled debt funds.

*Concentration of Credit (Issuer) Risk* – Concentration of credit risk is the risk of loss that may arise in the event of default by a single issuer. The INPRS Investment Policy Statement recognizes issuer risk as a strategic risk factor that is monitored on an absolute and relative basis.

INPRS Investment Policy Statement has placed an upper limit on the concentration of assets placed with an investment manager.

No investment manager shall manage more than 10 percent of the system's assets in actively managed portfolios at the time of funding. Through capital appreciation and additional purchases, no investment manager shall be allowed to manage in excess of 15 percent of the systems' assets in actively managed portfolios without Board approval.

No investment manager shall manage more than 15 percent of the system's assets in passively managed portfolios at the time of funding. Through capital appreciation and additional purchases, no investment manager shall be allowed to manage in excess of 20 percent of the system's assets in passively managed portfolios without Board approval

No investment manager shall manage more than 25 percent of the system's assets in a combination of actively and passively managed portfolios.

At June 30, 2012, there was no concentration of credit (issuer) risk for the Consolidated Defined Benefit Assets.

*Foreign Currency Risk* – Foreign currency risk is the risk that changes in exchange rates will adversely affect the fair value of an investment or a deposit. INPRS' foreign currency exposure is focused primarily in international equity holdings.

The INPRS Investment Policy Statement recognizes foreign exchange risk and the impact on incremental risk and return is assessed based on overall portfolio exposure. Unless otherwise approved by the Board, management of foreign currency exposure will only be implemented (1) by an Investment Manager on its Portfolio when the Investment Manager possesses recognized foreign exchange experience or (2) by an overlay manager or other third-party expert for a specific Portfolio or Retirement Fund. Any hedging strategy recommendation will be presented to the Board for approval and incorporated into the benchmark. The management and implementation of Board approved hedging activities will be implemented by the CIO, with the advice of the Executive Director and Consultants who are approved by the Board.

INPRS has exposure to foreign currency fluctuation as follows:

| Currency | Short Term Investments | Debt Securities | Equity Securities | Other Investments | Grand Total | % of Total |
|---|---|---|---|---|---|---|
| Australian Dollar | $ 2,206 | $ 16,093 | $ 76,300 | $ - | $ 94,599 | 0.4% |
| Brazilian Dollar | 250 | 12,111 | 36,765 | - | 49,126 | 0.2% |
| British Pound Sterling | 670 | 143,544 | 295,294 | 3,248 | 442,756 | 1.7% |
| Canadian Dollar | 263 | 95,895 | 90,037 | - | 186,195 | 0.7% |
| Chilean Peso | - | 1,332 | - | - | 1,332 | 0.1% |
| Colombian Peso | - | 2,215 | 678 | - | 2,893 | 0.0% |
| Czech Koruna | 27 | - | 3,023 | - | 3,050 | 0.0% |
| Danish Krone | 27 | - | 20,269 | - | 20,296 | 0.1% |
| Egyptian Pound | 13 | - | 551 | - | 564 | 0.0% |
| Euro Currency Unit | 2,010 | 306,522 | 488,023 | 190,809 | 987,364 | 3.7% |
| Hong Kong Dollar | 84 | - | 121,300 | - | 121,384 | 0.5% |
| Hungarian Forint | 10 | - | 483 | - | 493 | 0.0% |
| Indian Rupee | - | - | 14,996 | - | 14,996 | 0.1% |
| Indonesian Rupiah | 79 | - | 5,729 | - | 5,808 | 0.0% |
| Israeli Shekel | 14 | - | 2,489 | - | 2,503 | 0.0% |
| Japanese Yen | 3,370 | 66,528 | 330,794 | - | 400,692 | 1.5% |
| Korean Won | 397 | - | 58,971 | - | 59,368 | 0.2% |
| Malaysian Ringgit | 4 | - | 7,637 | - | 7,641 | 0.0% |
| Mexican Peso | 4,234 | 28,102 | 8,549 | - | 40,885 | 0.2% |
| New Zealand Dollar | 12 | 7,899 | 833 | - | 8,744 | 0.0% |
| Norwegian Krone | 22 | - | 25,827 | 26,845 | 52,694 | 0.2% |
| Philipine Peso | 8 | 10,147 | 1,843 | - | 11,998 | 0.0% |
| Polish Zloty | - | 7,128 | 2,264 | - | 9,392 | 0.0% |
| Singapore Dollar | 211 | - | 37,633 | - | 37,844 | 0.1% |
| South African Rand | 44 | - | 38,869 | - | 38,913 | 0.1% |
| Swedish Krona | 17 | 37,754 | 69,079 | - | 106,850 | 0.4% |
| Swiss Franc | 1,164 | - | 114,578 | - | 115,742 | 0.4% |
| Taiwan Dollar | 646 | - | 34,721 | - | 35,367 | 0.1% |
| Thai Baht | 2 | - | 17,926 | - | 17,928 | 0.1% |
| Turkish Lira | 42 | - | 23,619 | - | 23,661 | 0.1% |
| Held in Foreign Currency | 15,826 | 735,270 | 1,929,080 | 220,902 | 2,901,078 | 10.9% |
| Held in US Dollar | 2,478,213 | 10,937,564 | 4,352,038 | 5,998,341 | 23,766,156 | 89.1% |
| **Total** | **$ 2,494,039** | **$ 11,672,834** | **$ 6,281,118** | **$ 6,219,243** | **$ 26,667,234** | **100.0%** |

*Securities Lending* – Indiana Code 5-10.2-2-13(d) provides that the INPRS Board of Trustees may authorize a custodian bank to enter into a securities lending program agreement under which certain securities held by the custodian on behalf of INPRS may be loaned. The statute requires that collateral initially in excess of the total market value of the loaned securities must be pledged by the borrower and must be maintained at no less than the total market value of the loaned securities.

The purpose of such a program is to provide additional revenue for the Consolidated Defined Benefits Assets. The INPRS Investment Policy Statement requires that collateral securities and cash be initially pledged at 102 percent of the market value of the securities lent for domestic securities and 105 percent for international securities. No more than 40 percent of the Consolidated Defined Benefit Assets may be lent at one time. The custodian bank and/or its securities lending sub-agents provide 100 percent indemnification of the Consolidated Defined Benefit Assets against borrower default, overnight market risk and failure to return loaned securities. Securities received as collateral cannot be pledged or sold unless the borrower defaults. INPRS retains the market value risk with respect to the investment of the cash collateral.

Cash collateral investments are subject to the investment guidelines specified by the INPRS Investment Policy Statement. It states that the maximum weighted average days to maturity may not exceed 60. The securities lending agent matches the maturities of the cash collateral investments with stated securities loans' termination dates. Cash collateral received for open-ended loans that can be terminated on demand are invested with varying maturities.

| Securities Lending as of June 30, 2012 | |
|---|---|
| Market value of securities on loan | $ 1,692,637 |
| Fair value of cash and non-cash collateral by investment type: | |
| U.S. Governments | $ 1,077,653 |
| Domestic Equities | 486,010 |
| Corporate Bonds | 104,316 |
| International Equities | 66,305 |
| Fair value of cash and non-cash collateral | 1,734,284 |
| Fair value of non-cash collateral that is not included in the Statements of Fiduciary Plan Net Position | 836,553 |
| Fair value of cash collateral (liability to borrowers) | 897,731 |
| Fair value of reinvested cash collateral by type: | |
| Commercial Paper | 376,699 |
| Repurchase Agreements | 248,954 |
| Floating Rate Notes | 139,744 |
| Certificate of Deposits | 132,334 |
| Fair value of reinvested cash collateral | $ 897,731 |
| Net unrealized gain | - |

The quality rating of the reinvested cash collateral investments as described by Standard and Poor's at June 30, 2012 is as follows:

| Standard and Poor's Rating | Fair Value of Reinvested Cash Collateral | Percent of Portfolio |
|---|---|---|
| A-1 and A-1+ | 507,045 | 56.5% |
| AA+ | 10,636 | 1.1% |
| AA- | 114,552 | 12.8% |
| A+ | 11,419 | 1.3% |
| A | 3,115 | 0.3% |
| Unrated | 250,964 | 28.0% |
| Total | 897,731 | 100.0% |

The majority of the unrated reinvested cash collateral investments consist of repurchase agreements.

*Repurchase Agreements* – A repurchase agreement is an agreement in which INPRS transfers cash to a broker-dealer or financial institution. The broker dealer or financial institution transfer securities to INPRS and promises to repay the cash plus interest in exchange for the same securities. Repurchase agreements are assets with the security collateral held at INPRS' custodian bank.

A reverse repurchase agreement is the same as a repurchase agreement, but from the perspective of the buyer rather than the seller. Repurchase agreements are secured loans with INPRS' collateral held at the broker dealer or financial institution's custodian bank.

The amounts held at June 30, 2012, exclusive of securities lending reinvested cash collateral, are as follows:

| Repurchase Agreements by Collateral Type | Cash Collateral Received | Market Value |
|---|---|---|
| U.S. Agencies | $ 96,400 | $ 98,731 |
| Corporate Bond | 1,090 | 1,111 |
| **Total Repurchase Agreements** | **$ 97,490** | **$ 99,842** |

| Reverse Repurchase Agreements by Collateral Type | Market Value | Cash Collateral Posted |
|---|---|---|
| US Inflation Linked Bonds | $ 147,680 | $ 148,198 |
| **Total Reverse Repurchase** | **$ 147,680** | **$ 148,198** |

*Derivative Financial Instruments* – Derivative instruments are financial contracts whose values depend on the values of one or more underlying assets, reference rates, or financial indices. The fair value of all derivative financial instruments is reported in the Statement of Fiduciary Net Position as either assets or liabilities, and the change in the fair value is recorded in the Statement of Changes in Fiduciary Net Position as investment income. A derivative instrument could be a contract negotiated on behalf of the Master Trust and a specific counterparty. This would typically be referred to as an "OTC contract" (Over the Counter) such as swaps, forward contracts and TBAs (Mortgage To Be Announced). Alternatively, a derivative instrument, such as futures, could be listed and traded on an exchange and referred to as "exchange traded". Due to the level of risk associated with certain derivative investment securities, it is reasonably possible that changes in the value of investment securities will occur in the near term, and such changes could affect the amounts reported in the financial statements. Investments in limited partnerships may include derivatives that are not shown in the derivative total.

During the year, the Fund's derivative investments included:

**Futures**

A futures contract is an agreement between two parties to buy and sell a financial instrument at a set price on a future date.

INPRS' investment managers use financial futures to replicate an underlying security or index they intend to hold or sell in the portfolio. In certain instances, it may be beneficial to own a futures contract rather than the underlying security. Additionally, INPRS' investment managers use

futures contracts to adjust the portfolio risk exposure. Futures contracts may be used for the purpose of investing cash flows or modifying duration, but in no event may leverage be created by any individual security or combination of securities. No short sales of equity securities or equity index derivatives are permitted.
As the market value of the futures contract varies from the original contract price, a gain or loss is recognized and paid to, or received from, the clearinghouse. The cash or securities to fulfill these obligations are held in the investment portfolio.

**Options**

Options are agreements that give the owner of the option the right, but not obligation, to buy (in the case of a call) or to sell (in the case of a put) a specific amount of an asset for a specific price on or before a specified expiration date.

The purchaser of put options pays a premium at the outset of the agreement and stands to gain from an unfavorable change (i.e., a decrease) in the price of the instrument underlying the option. The writer of a call option receives a premium at the outset of the agreement and bears the risk of an unfavorable change (i.e., an increase) in the price of the instrument underlying the option. An interest rate swaption is the option to enter into an interest rate swap based off a set of predetermined conditions.

Options are generally used to manage interest rate risk, adjust portfolio duration, or rebalance the total portfolio to the target asset allocation. The fair value of exchange traded options is determined based upon quoted market prices.
The fair value of over the counter options is determined by external pricing services, using various proprietary methods, based upon the type of option.

**Rights/Warrants**

Rights provide the holder with the right, but not the obligation, to buy a company's common stock at a predetermined price, the subscription price. The right is good until its expiration date. A right permits the investor to buy at a price that may be below the actual market price for that stock. A warrant is an option to buy an underlying equity security at a predetermined price for a finite period of time.

**Forwards**

Foreign Currency
A forward exchange contract is a commitment to purchase or sell a foreign currency at a future date at a negotiated forward rate. A contract is classified as a forward contract when the settlement date is more than two days after the trade date. Risks associated with such contracts include movement in the value of a foreign currency relative to the U.S. dollar. The contracts are valued at forward exchange rates and include net appreciation / depreciation in the Statement of Fiduciary Net Position. Realized gains or losses on forward currency contracts is the difference between the original contract and the closing value of such contract and is included in the Statement of Changes in Fiduciary Net Position.

The Fund enters into forward currency forwards to manage exposure to fluctuations in foreign currency exchange rates on portfolio holdings and to settle future obligations.

TBA
A TBA (Mortgage To Be Announced) is a contract for the purchase or sale of agency mortgage-backed securities to be delivered at a future agreed upon date. Associated gains are derived from the change in market value of the contract due to a change in price of the underlying security. Future settlement risk is the risk of not receiving the asset or associated gains specified in the contract.

TBA's are used to achieve the desired market exposure of a security or asset class or adjust portfolio duration. The fair value is determined by external pricing services using various proprietary methods.

TBA's are classified as fixed income investments.

**Swaps**

Interest Rate Swaps
Interest rate swaps are derivative instruments in which one party exchanges a stream of fixed interest rate cash flows for floating interest rate cash flows. A notional amount of principal is required to compute the actual cash amounts and is determined at the inception of the contract.

Interest rate swaps are generally used to manage interest rate risk, adjust portfolio duration, or rebalance the total portfolio to the target asset allocation.

The fair value is determined by external pricing services using various proprietary methods.

Inflation Swap
An inflation swap is a derivative used to transfer inflation risk from one party to another through an

exchange of cash flows. In an inflation swap, one party pays a fixed rate on a notional principal amount, while the other party pays a floating rate linked to an inflation index, such as the Consumer Price Index (CPI) or an inflation bond.

Credit Default Swaps

Credit default swap agreements involve one party (referred to as the buyer of protection) making a stream of payments to another party (the seller of protection) in exchange for the right to receive a specified return in the event of a default or other predetermined credit event for the referenced entity, obligation or index.

Credit default swaps are used to achieve the desired credit exposure of a security or basket of securities. One of the main advantages of a credit default swap is it allows for exposure to credit risk while limiting exposure to other risks, such as interest rate and currency risk.

The fair value is determined by external pricing services using various proprietary methods.

The table below summarizes INPRS' derivative information for the year ending June 30, 2012 (dollars in thousands):

| Investment Derivatives | Changes in Fair Value | Fair Value | Notional (USD) |
|---|---|---|---|
| **Futures** | | | |
| **Listed** | | | |
| Commodity | $ (7,505) | $ (7,505) | $ 1,009,250 |
| Equity Index | 13,986 | 13,986 | 498,757 |
| Bond | (256) | (198) | 278,813 |
| Currency | (230) | 275 | 246,611 |
| Interest Rate | 220 | 220 | 50,645 |
| **Total Futures** | **6,215** | **6,778** | **2,084,076** |
| **Options** | | | |
| **Listed** | | | |
| Currency | (98) | 83 | 10,870 |
| Subtotal Listed | (98) | 83 | 10,870 |
| **OTC** | | | |
| Swaptions | 2,493 | (483) | 498,720 |
| Subtotal OTC | 2,493 | (483) | 498,720 |
| **Total Options** | **2,395** | **(400)** | **509,590** |
| **Swaps:** | | | |
| **OTC** | | | |
| Interest Rate Swaps | (1,007) | (2,104) | 1,074,362 |
| Inflation Swaps | 49 | 49 | 13,440 |
| Equity Index | 68 | (8) | 8,100 |
| Credit Default Swaps Single Name | 827 | 1,195 | 263,429 |
| Credit Default Swaps Index | 1,191 | 664 | 301,647 |
| **Total Swaps** | **1,128** | **(204)** | **1,660,978** |
| **TBA** | **73** | **(70,287)** | **65,500** |
| **Total** | **$ 9,811** | **$ (64,113)** | **$ 4,320,144** |

| Swap Type | Swap Maturity Profile at June 30, 2012 < 1 yr | 1 - 5 yrs | 5 -1 0 yrs | 10 - 20 yrs | 20 + yrs | Total |
|---|---|---|---|---|---|---|
| Credit Default - Index | $ - | $ 726 | $ (62) | $ - | $ - | $ 664 |
| Credit Default - Single Name | (28) | 151 | (169) | - | 1,241 | 1,195 |
| Equity Index | - | - | (8) | - | - | (8) |
| Inflation Swaps | - | (98) | 147 | - | - | 49 |
| Interest Rate Swaps | - | (369) | (967) | 553 | (1,321) | (2,104) |
| **Total Swap Fair Value** | **$ (28)** | **$ 410** | **$ (1,059)** | **$ 553** | **$ (80)** | **$ (204)** |

## Credit Risk

Counterparty credit risk exists on all open OTC positions. Counterparty credit risk is the risk that a derivative counterparty may fail to meet its payment obligation under the derivative contract.

INPRS' investment managers use International Swaps and Derivative Association Master Agreements to further reduce counterparty risk by specifying credit protection mechanisms and providing standardization that improves legal certainty, thereby reducing the probability of unforeseen losses. Furthermore, the master agreements can provide additional credit protection through the requirement of collateral exchange and certain event of default and mutual termination provisions. Securities eligible as collateral are typically United States government bills and U.S. dollar cash.

The maximum amount of loss due to credit risk that the Fund would incur if the counterparty to the derivative instrument failed to perform according to the terms of the contract, without respect to any collateral or other security, or netting arrangements, is the total unrealized gain of derivatives at the end of the reporting period. The aggregate fair value of investment derivative instruments in asset positions at June 30, 2012, was $19,072 thousand of which $13,336 thousand was uncollateralized.

The tables below summarize INPRS's swap positions as of June 30, 2012:

| | | Fair Value | | | Collateral | |
|---|---|---|---|---|---|---|
| Swaps Counterparty | S&P Rating | Receivable/ Unrealized Gain | Payable/ (Unrealized Loss) | Total Fair Value | Posted | Received |
| Bank of America Corp | A | $ 1,467 | $ (1,431) | $ (191) | $ - | $ - |
| Barclays Capital London | A | 1,748 | (2,078) | 393 | 473 | (1,380) |
| BNP Paribas Securities Corp | AA- | 15 | (2) | 15 | - | - |
| Citibank | A | 2,515 | (3,126) | (680) | 3,438 | (970) |
| CME Central | AA- | 2,698 | (2,213) | 792 | - | - |
| Credit Suisse | A | 1,836 | (1,965) | (413) | 1,030 | (520) |
| Deutsche Bank | A+ | 3,104 | (2,777) | (40) | 500 | (750) |
| Goldman | A- | 1,084 | (464) | 301 | 9 | (790) |
| HSBC Securities Inc | A+ | 175 | (127) | 189 | - | (330) |
| JPMorgan Chase Bank | A | 2,379 | (2,044) | (1,211) | 940 | - |
| Morgan Stanley Capital Services | A- | 957 | (1,203) | 592 | 60 | (715) |
| Royal Bank of Scotland | A- | 436 | (121) | 302 | 54 | (1,190) |
| Societe Generale Paris | A | 2 | - | - | - | - |
| UBS | A | 656 | (394) | (253) | 151 | - |
| Grand Total | | $ 19,072 | $ (17,945) | $ (204) | $ 6,655 | $ (6,645) |

| Credit Default Swaps | | | | |
|---|---|---|---|---|
| **Investment Type** | | **Reference** | **Fair Value** | **Notional** |
| Index | Bought | CDX IG | $ 270 | $ 264,071 |
| Index | Bought | CDX EM | 637 | 8,800 |
| Index | Bought | CDX HY | (128) | 13,976 |
| Index | Bought | CDX ITRAXX | (115) | 14,800 |
| **Total CDS - Index** | | | **$ 664** | **$ 301,647** |
| | | | | |
| Single Name | Sold | Various | $ (1,002) | $ 202,416 |
| Single Name | Bought | Various | 2,197 | 61,013 |
| **Total CDS - Single Name** | | | **$ 1,195** | **$ 263,429** |

**Interest Rate Risk**

The Fund has exposure to interest rate risk due to investments in interest rate and inflation swaps and TBAs. The required risk disclosures are included in the Interest Rate Risk schedule.

The table below summarizes INPRS's Investments that are highly sensitive to interest rate changes:

| Reference Rate | Fair Value | Notional |
|---|---|---|
| **TBA Securities:** | | |
| 3.50% | $ (7,396) | $ 7,000 |
| 4.00% | (2,660) | 2,500 |
| 4.50% | (38,590) | 36,000 |
| 5.00% | (21,641) | 20,000 |
| | (70,287) | 65,500 |
| **Interest Rate Swap:** | | |
| Pay Variable 3M CDOR / Receive Fixed Various 2.0% to 6.2% | 2,826 | 52,087 |
| Pay Fixed Various 1.8375% to 3.586% / Receive Variable 3M CDOR | (1,041) | 26,191 |
| Pay Fixed Various 1.01% to 3.06% / Receive Variable 6M EURIBOR | (1,912) | 260,891 |
| Pay Variable 6M EURIBOR / Receive Fixed Various 1.40% to 2.82% | 1,829 | 243,137 |
| Pay Variable 6M GBP-LIBOR / Receive Fixed Various 2.25% to 3.76% | 132 | 18,178 |
| Pay Fixed Various 2.25% to 3.94% / Receive Variable 6M GBP-LIBOR | (399) | 40,842 |
| Pay Variable MXN-TIIE / Receive Fixed Various 5.50% to 6.35% | 102 | 9,690 |
| Pay Fixed Various 1.135% to 2.75% / Receive Variable 3M USD-LIBOR | (4,945) | 308,901 |
| Pay Variable 3M USD-LIBOR / Receive Fixed Various 1.50% to 2.50% | 1,106 | 108,500 |
| Pay Variable BZDIOVRA / Receive Fixed Various 10.38% to 10.58% | 198 | 5,945 |
| | (2,104) | 1,074,362 |
| **Inflation Swap:** | | |
| Receive Variable CPURNSA / Pay 2.46% | (6) | 3,100 |
| Pay Variable CPURNSA / Receive 1.84% | (98) | 5,800 |
| Pay Variable CPURNSA / Receive 2.66% | 153 | 4,540 |
| | $ 49 | $ 13,440 |

**Foreign Currency Risk**

The Fund is exposed to foreign currency risk on its foreign currency forward contracts and futures contracts. The required risk disclosures are included in the Foreign Currency Risk schedule in Note 5.

At June 30, 2012, INPRS' investments included the following currency forwards balances:

| | |
|---|---|
| Foreign Currency Contract Receivable | $ 963.7 |
| Foreign Currency Contract Payable | 967.1 |

*Long Term Commitments for Alternative Investments* – INPRS enters into long term commitments for funding other investments in private equity and private real estate. These amounts include Euro-currency denominated, Norwegian Krone denominated and British Pound Sterling denominated commitments to limited liability partnerships. The remaining amount of unfunded commitments, converted to U.S. dollars using the closing exchange rate, as of June 30, 2012 is as follows:.

| Currency | Total Unfunded Commitments |
|---|---|
| Euro Currency Unit | $ 102,907 |
| Norwegian Krone | 19,624 |
| British Pound Sterling | 2,222 |
| U.S. Dollar | 1,763,899 |
| **Total** | **$ 1,888,652** |

## B. Interfund Transactions

### Interfund Loans

As explained in Note III(A) above, temporary cash overdrafts in various funds are reported as interfund loans from the General Fund. As of June 30, 2012, the following funds had temporary cash overdrafts covered by loans from the General Fund: US Department of Transportation Fund, $18.6 million, US DHHS Fund, $58.6 million, US Department of Labor Fund, $.2 million, U.S. Department of Education Fund, $3.8 million, and S&S Children's Home Construction Fund, $0.7 million.

The following is a summary of the Interfund Loans as of June 30, 2012:

Interfund Loans - Current

| | Loans To Governmental Funds | Loans From Governmental Funds |
|---|---|---|
| Governmental Funds | | |
| General Fund | $ 81,915 | $ - |
| US Department of Transportation | - | 18,582 |
| US DHHS | - | 58,560 |
| Nonmajor Governmental Funds | - | 4,773 |
| Total Governmental Funds | 81,915 | 81,915 |
| Total Interfund Loans | $ 81,915 | $ 81,915 |

### Interfund Services Provided/Used

Interfund Services Provided of $7.0 million represents amounts owed by various governmental funds to the Institutional Industries Fund and the Administrative Services Revolving Funds, both internal service funds, for goods and services rendered.

The following is a schedule of Interfund Services Provided/Used as of June 30, 2012:

**Interfund Services Provided/Used**

| | Interfund Services Provided To Governmental Funds | Interfund Services Used By Governmental Funds |
|---|---|---|
| **Governmental Funds** | | |
| General Fund | $ - | $ 2,489 |
| ARRA of 2009 | - | 22 |
| U.S. Department of Transportation | - | 7 |
| U.S. Department of Health & Human Services | - | 1,042 |
| Nonmajor Governmental Funds | - | 3,391 |
| Total Governmental Funds | - | 6,951 |
| **Proprietary Funds** | | |
| Internal Service Funds | 6,951 | - |
| Total Proprietary Funds | 6,951 | - |
| **Total Interfund Services Provided/Used** | $ 6,951 | $ 6,951 |

**Due From/Due Tos**

*Current* – Indiana University owed $1.7 million to the General Fund for the State Department of Toxicology per IC 10-20-2-7(c). The interfund balance of $3.1 million represents the accrued distribution amount from the State Lottery Commission to the Build Indiana Fund.

*Non-current* – The interfund balance of $50.0 million represents funds the General Fund borrowed in June 2004, interest free, from the Indiana Board for Depositories, a discretely presented component unit. This money is due to be repaid, either from the General Fund prior to January 1, 2023, or by a budget request submitted to the 2023 session of the general assembly. This non-current interfund balance appears on the government-wide statements, but not the General Fund statements.

The following are current and non-current schedules of Due From/Due Tos of Component Units, as of June 30, 2012:

**Component Units - Current**

| | Due From Component Units | Due To Primary Government |
|---|---|---|
| **Governmental Funds** | | |
| General Fund | $ 1,693 | $ - |
| Nonmajor Governmental Funds | 3,093 | - |
| Total Governmental Funds | 4,786 | - |
| **Component Units** | | |
| Indiana University | - | 1,693 |
| State Lottery Commission | - | 3,093 |
| Total Component Units | - | 4,786 |
| **Total Due From/To** | **$ 4,786** | **$ 4,786** |

**Component Units - Non-current**

| | Due From Primary Government | Due To Component Units |
|---|---|---|
| **Governmental Funds** | | |
| General Fund | $ - | $ 50,000 |
| Total Governmental Funds | - | 50,000 |
| **Component Units** | | |
| Board for Depositories | 50,000 | - |
| Total Component Units | 50,000 | - |
| **Total Due From/To** | **$ 50,000** | **$ 50,000** |

**Interfund Transfers**

*Major Governmental Funds*

Transfers constitute the movement of money from the fund that receives the resources to the fund that utilizes them. These numerous transfers generally result from legislation passed by the Indiana General Assembly that directs how the transfers are made. In the case of the General Fund, many appropriations are made in the General Fund and then are transferred during the year to the funds where these appropriations are used. Also in the case of the General Fund, various taxes and other revenues are collected in other funds and transferred to the General Fund. Following are the principal purposes of the State's interfund transfers:

**General Fund** – $614.1 million was transferred in from the State Gaming Fund which was wagering taxes from riverboats and slot machines at horse tracks. The Build Indiana Fund transferred in $236.2 million as Motor Vehicle Excise Tax Cut Replacement distributions. $177.7 million was transferred in from the Public Welfare-Medicaid Assistance Fund of which $154.1 million was a return of funds at fiscal year end and $23.6 million was qualifying assessment fees that can only be used for the State's share of Medicaid services under Title XIX of the Social Security Act. $85.6 million was received from the Fund 6000 Programs of which $48.2 million was distribution of financial institutions tax per IC 6-5.5; $14.4 million was transferred in for Indiana Veterans' Home administration from the Comfort-Welfare Fund's receipts of resident fees and Medicaid and Medicare reimbursements; $12.0 million was the recapture of financial institutions tax based on the FIT distribution that would have been based on property tax levies that were assumed by the State in 2009; $5.7 million was transferred to the Office of Medicaid Policy and Planning's State Medicaid General Fund which was appropriation transfers; and $5.3 million was transferred in from permit fees collected from business that sell alcoholic beverages per IC 7.1-4-9-4. $46.5 million was transferred in from the Tobacco Master Settlement Fund for various health and welfare purposes including residential services for the developmentally disabled, Indiana's Children with Special Health Care Needs health insurance coverage, and substance abuse treatment. $46.3 million was transferred in from the Mental Health Center Fund to the Office of Medicaid and Policy and Planning's State Medicaid General Fund to fund the state match of Medicaid expenditures for services to adults who are seriously mentally ill. $40.0 million was a reversion of funds at fiscal year end from the Administrative Services Revolving Fund. $32.8 million was transferred in from the Medicaid Indigent Care Trust Fund for the State's share of supplemental payments and to fund Safety Net payments made in fiscal year 2012. $27.0 million was transferred in from the Motor Vehicle Commission Fund at the request of the Bureau of Motor Vehicles which was unobligated funds. $15.0 million was transferred in from the U.S. Department of Health and Human Services Fund of which $12.7 million was reimbursement of federal indirect costs to the State Budget Agency; $1.6 million was the return of Temporary Assistance for Needy Families program state match; $0.5 million was for the Attorney General's Office's Medicaid and welfare fraud units; and $0.2 million was returned to the Indiana Soldiers' and Sailors' Children's Home at fiscal year end.

The following were transfers out from the General Fund: The Public Welfare Medicaid Assistance Fund received $2.0 billion in transfers for Medicaid current obligations and for Medicaid administration to enable the Office of Medicaid Policy and Planning to carry out all services under IC 12-8-6. These services include, but may not be limited to the provision of care and treatment for individuals with mental illness, developmental disability, long term care needs, and family and child services needs. $314.2 million was transferred to the U.S. Department of Health and Human Services Fund in support of: the State Medicaid program; child care services and the temporary assistance for needy families program both administered through the FSSA's Division of Family Resources; case management services to children by the Department of Child Services (DCS); the Family and Children Fund of the Department of Child Services; DCS administrative costs; Social Security Title IV-D services to needy families with children; county prosecutors' and local judges' salaries; children psychiatric services through FSSA's Division of Mental Health; information systems for the Department of Child Services; Medicare/Medicaid certification program administered by the Indiana State Department of Health; child welfare training administered by DCS; and other health and human services programs and services. $275.2 million was transferred to the State Student Assistance Commission of Indiana mostly for the awarding of the State's grants and scholarships for Hoosier students to attend colleges. The Mental Health Center Fund received appropriation transfers in totaling $93.1 million to fund services to adults who are seriously mentally ill in comprehensive community health centers and for the administration of services by the Department of Mental Health. The Build Indiana Fund received $99.4 million from riverboat wagering and pari-mutuel taxes which went to the Lottery and Gaming Surplus Account. $63.0 million was transferred from the General Fund to the Motor Vehicle Highway Fund primarily for State Police administration and pensions. $57.0 million was transferred to the Hospital Care for the Indigent Fund for the Hospital Care for the Indigent Program. $55.9 million was transferred to the U.S. Department of Agriculture Fund for the Federal Food Stamp Program administered by FSSA's Division of Family Resources. $41.4 million was received by the Indiana Department of Transportation for the Public Mass Transportation Fund, which is used for the promotion and development of public transportation.

**Medicaid Assistance Fund** – The Medicaid Assistance Fund had a transfer in of $2.0 billion from the General Fund to support the state Medicaid program administered through the Office of Medicaid Policy and Planning. $30.0 million was transferred in from the Medicaid Indigent Care Trust Fund, which is part of the U.S. Department of Health and Human Services Fund, for reimbursement of hospital care for the indigent supplement payments made from the Medicaid Assistance Fund.

Transfers out included $177.7 million to the General Fund of which $154.1 million was a return of funds at fiscal year end and $23.6 million was qualifying assessment fees that can only be used for the State's share of Medicaid services under Title XIX of the Social Security Act.

**Major Moves Construction Funds –** The Major Moves Construction Fund had a transfer out of $543.3 million to the State Highway Department for construction and maintenance of the State's highways, roads, and bridges.

**ARRA of 2009 Fund** – The American Recovery and Reinvestment Act of 2009 Fund transferred out $33 thousand to the General Fund for payment of federal indirect costs and $3 thousand to the U.S. Department of Labor Fund for expenditure adjustments made by the Indiana Department of Workforce Development.

**U.S. Department of Transportation Fund** – The U.S. Department of Transportation Fund received $165.9 million of state and local match money from the State Highway Fund for use by the Indiana Department of Transportation for transportation projects.

The U.S. Department of Transportation Fund returned $88.9 million of state and local match money to the State Highway Fund at fiscal year end.

**U.S. Department of Health and Human Services Fund** – The U.S. Department of Health and Human Services (USDHHS) Fund had transfers in totaling $314.2 million from the General Fund. Of this $314.2 million, $111.9 million was for the state's share of the Medicaid administrative payments; $34.4 million was for child care services; $28.0 million was for the state's share of Temporary Assistance for Needy Families payments; $28.1 million is to provide adoption services grants and assistance; $26.7 million for case management services to children by the Department of Child Services (DCS); $25.4 million for family and children services through DCS; $21.1 million for DCS administrative costs; $7.5 million for Social Security Title IV-D services to needy families with children; $7.1 million for county prosecutors' salaries; $5.4 million for children psychiatric services; $4.8 million for the Indiana Support enforcement tracking system established by DCS as the official record for child support payments; $4.8 million for local judges' salaries; $1.6 million for Medicare/Medicaid Certification; $1.4 million for the Child Protection Automation Project of DCS; $1.4 million for child welfare training; and $4.6 million was for various other health and human services programs. $37.0 million was received from the Tobacco Settlement Fund for the Children's Health Insurance Program administered by the Indiana Family and Social Services. $0.9 million was received from the Tobacco Master Settlement Fund for the Indiana Department of Health's U.S. Department of Health and Human Services Fund.

The U.S. Department of Health and Human Services transferred out to the General Fund $15.0 million of which: $12.8 million was reimbursement of federal indirect costs to the State Budget Agency; $1.6 million was the return of state match from the Temporary Assistance for Needy Families program; $0.5 million was for the Attorney General's Office's Medicaid and welfare fraud units; and $0.2 million was returned to the Soldiers' and Sailors' Children's Home at fiscal year end. $30.0 million was transferred to the Medicaid Assistance Fund to reimburse indigent supplement payments for hospital care.

***Proprietary Funds***

**Non-Major Enterprise Funds**

**The Inns and Concessions Fund** – This fund had transfers out of $2.1 million, representing cash contributions to the Department of Natural Resources (DNR) which are to be used for repayments of bonds made by the Indiana Finance Authority.

**Internal Service Funds**

$0.6 million was transferred to the Administrative Services Revolving Fund from the pay phone fund to cover a shortfall of information technology services. $40.0 million was transferred from the Administrative Services Revolving Fund to the General Fund for a reversion of funds at fiscal year end.

A summary of interfund transfers for the year ended June 30, 2012 is as follows:

| | Operating transfers in | Operating transfers (out) | Net transfers |
|---|---|---|---|
| **Governmental Funds** | | | |
| General Fund | $ 1,401,233 | $ (3,116,679) | **$ (1,715,446)** |
| Public Welfare-Medicaid Assistance Fund | 1,984,049 | (177,712) | **1,806,337** |
| Major Moves Construction Fund | - | (543,342) | **(543,342)** |
| ARRA of 2009 | - | (36) | **(36)** |
| U.S. DOT Fund | 168,635 | (92,541) | **76,094** |
| U.S. DHHS Fund | 352,170 | (14,951) | **337,219** |
| Nonmajor Governmental Fund | 2,248,900 | (2,168,175) | **80,725** |
| **Proprietary Funds** | | | |
| Inns and Concessions | - | (2,101) | **(2,101)** |
| Internal Service Funds | 550 | (40,000) | **(39,450)** |
| Total | $ 6,155,537 | $ (6,155,537) | **$ -** |

## C. Taxes Receivable/Tax Refunds Payable

Taxes Receivable/Tax Refunds Payable as of year end, including the applicable allowances for uncollectible accounts, are as follows:

| | Governmental Activities | | | |
|---|---|---|---|---|
| | General Fund | Special Revenue Funds | Capital Projects Funds | Total Primary Government |
| Income taxes | $ 1,164,553 | $ - | $ - | **$ 1,164,553** |
| Sales taxes | 777,162 | 1,169 | - | **778,330** |
| Fuel taxes | - | 96,791 | - | **96,791** |
| Gaming taxes | 954 | 12,637 | - | **13,591** |
| Inheritance taxes | 38,355 | - | - | **38,355** |
| Alcohol and tobacco taxes | 33,081 | 18,525 | 1,856 | **53,462** |
| Insurance taxes | 2,055 | - | - | **2,055** |
| Financial institutions taxes | - | 48,118 | - | **48,118** |
| Other taxes | 23,747 | 1,502 | - | **25,249** |
| Total taxes receivable | 2,039,907 | 178,742 | 1,856 | **2,220,504** |
| Less allowance for uncollectible accounts | (409,882) | (32,090) | (6) | **(441,977)** |
| Net taxes receivable | **$ 1,630,025** | **$ 146,653** | **$ 1,850** | **$ 1,778,527** |
| Tax refunds payable | **$ 27,807** | **$ 13,729** | **$ -** | **$ 41,536** |

## D. Capital Assets

Capital asset activity for governmental activities for the year ended June 30, 2012, was as follows:

### Primary Government – Governmental Activities

| | Balance, July 1, As restated | Increases | Decreases | Balance, June 30 |
|---|---|---|---|---|
| **Governmental Activities:** | | | | |
| Capital assets, not being depreciated/amortized: | | | | |
| Land | $ 1,658,421 | $ 93,155 | $ (41,618) | $ 1,709,958 |
| Infrastructure | 8,385,668 | 555,708 | (17,211) | 8,924,165 |
| Construction in progress | 1,571,645 | 798,875 | (564,497) | 1,806,023 |
| Total capital assets, not being depreciated/amortized | 11,615,734 | 1,447,738 | (623,326) | 12,440,146 |
| Capital assets, being depreciated/amortized: | | | | |
| Buildings and improvements | 1,614,088 | 36,457 | (49,941) | 1,600,604 |
| Furniture, machinery, and equipment | 518,249 | 17,550 | (25,749) | 510,050 |
| Computer software | 38,099 | 3,511 | (1,497) | 40,113 |
| Infrastructure | 22,860 | - | (211) | 22,649 |
| Total capital assets, being depreciated/amortized | 2,193,296 | 57,518 | (77,398) | 2,173,416 |
| Less accumulated depreciation/amortization for: | | | | |
| Buildings and improvements | (835,962) | (34,682) | 32,978 | (837,666) |
| Furniture, machinery, and equipment | (349,691) | (37,192) | 21,460 | (365,423) |
| Computer software | (35,325) | (2,007) | 1,469 | (35,863) |
| Infrastructure | (14,087) | (483) | 69 | (14,501) |
| Total accumulated depreciation/amortization | (1,235,065) | (74,364) | 55,976 | (1,253,453) |
| Total capital assets being depreciated/amortized, net | 958,231 | (16,846) | (21,422) | 919,963 |
| Governmental activities capital assets, net | $ 12,573,965 | $ 1,430,892 | $ (644,748) | $ 13,360,109 |

## Primary Government – Business-Type Activities

| | Balance, July 1 | Increases | Decreases | Balance, June 30 |
|---|---|---|---|---|
| **Business-Type Activities:** | | | | |
| Capital assets, being depreciated: | | | | |
| Land improvements | - | - | - | - |
| Buildings and improvements | $ 149 | $ - | $ - | $ 149 |
| Furniture, machinery, and equipment | 261 | - | - | 261 |
| Infrastructure | - | - | - | - |
| Total capital assets, being depreciated | 410 | - | - | 410 |
| Less accumulated depreciation for: | | | | |
| Buildings and improvements | (100) | (12) | - | (112) |
| Furniture, machinery, and equipment | (226) | (12) | - | (238) |
| Infrastructure | - | - | - | - |
| Total accumulated depreciation | (326) | (24) | - | (350) |
| Total capital assets being depreciated, net | 84 | (24) | - | 60 |
| Business-type activities capital assets, net | $ 84 | $ (24) | $ - | $ 60 |

Depreciation/amortization expense was charged to functions/programs of the primary government as follows:

| | |
|---|---|
| **Governmental activities:** | |
| General government | $ 5,994 |
| Public safety | 30,643 |
| Health | 938 |
| Welfare | 5,172 |
| Conservation, culture and development | 10,440 |
| Education | 1,404 |
| Transportation | 19,773 |
| Total depreciation/amortization expense - governmental activities | $ 74,365 |
| **Business-type activities:** | |
| Inns and Concessions | $ 24 |
| Total depreciation expense - business-type activities | $ 24 |

## E. Leases

The future minimum lease obligations, the net present value of these minimum lease payments as of June 30, 2012 and the assets acquired through capital leases are as follows:

**Future minimum lease payments**

| Year ending June 30, | Operating leases | Capital leases Governmental Activities |
|---|---|---|
| 2013 | $ 33,717 | $ 106,368 |
| 2014 | 27,954 | 107,052 |
| 2015 | 24,155 | 108,142 |
| 2016 | 22,117 | 106,843 |
| 2017 | 20,470 | 105,538 |
| 2018-2022 | 34,817 | 510,672 |
| 2023-2027 | 274 | 510,169 |
| 2028-2032 | - | 209,733 |
| 2033-2037 | - | 2,718 |
| **Total minimum lease payments (excluding executory costs)** | **$ 163,504** | **1,767,235** |
| Less: | | |
| Remaining premium(discount) | | (17,761) |
| Amount representing interest | | (539,497) |
| Present value of future minimum lease payments | | **$ 1,209,977** |

**Assets acquired through capital lease**

| | |
|---|---|
| Building | $ 29,849 |
| Machinery and equipment | 2,077 |
| Infrastructure | 1,184,129 |
| less accumulated depreciation | (9,348) |
| | **$ 1,206,707** |

*Operating Leases*

The State leases building and office facilities and other equipment under non-cancelable operating leases. Total payments for such leases with aggregate payments of $20,000 or more were $37.3 million for the year ended June 30, 2012. A table of future minimum lease payments (excluding executory costs) is presented above.

*Capital Leases Liabilities*

The State has entered into various lease agreements with aggregate payments of $20,000 or more to finance the acquisition of buildings, land and equipment. These lease agreements qualify as capital leases for accounting purposes and, therefore, have been recorded at the present value of the future minimum lease payments as of the inception date in the government-wide statements.

## F. Long-Term Obligations

Changes in long-term obligations for the primary government for the year ended June 30, 2012 were as follows:

| Changes in Long-Term Obligations | Balance, July 1, as Restated | Increases | Decreases | Balance, June 30 | Amounts Due Within One Year | Amounts Due Thereafter |
|---|---|---|---|---|---|---|
| **Governmental activities:** | | | | | | |
| Compensated absences | $ 135,713 | $ 75,568 | $ (70,232) | $ 141,049 | $ 77,295 | $ 63,754 |
| Due to component unit | 66,637 | - | (16,637) | 50,000 | - | 50,000 |
| Net pension obligation | 1,191,515 | 152,782 | - | 1,344,297 | - | 1,344,297 |
| Other postemployment benefits | 118,229 | 8,023 | (6,621) | 119,631 | - | 119,631 |
| Pollution remediation | 41,308 | 4,643 | - | 45,951 | 7,260 | 38,691 |
| Intergovernmental payable | 187,552 | 12,118 | (10,000) | 189,670 | 169,670 | 20,000 |
| Capital leases | 1,229,314 | 31,817 | (51,154) | 1,209,977 | 51,198 | 1,158,779 |
| | $ 2,970,268 | $ 284,951 | $ (154,644) | $ 3,100,575 | $ 305,423 | $ 2,795,152 |
| **Business-type activities:** | | | | | | |
| Compensated absences | $ 472 | $ 187 | $ (203) | $ 456 | $ 205 | $ 251 |
| Claims liability | 33,063 | 1,501 | (4,393) | 30,171 | 3,888 | 26,283 |
| | $ 33,535 | $ 1,688 | $ (4,596) | $ 30,627 | $ 4,093 | $ 26,534 |

Long term obligations of governmental activities include capital lease obligations of governmental funds as presented in Note IV(E), net pension obligations for the State Police Retirement Fund, Public Employees Retirement Fund-State, Prosecuting Attorney's Retirement Fund, and the State Teachers' Retirement Fund (Pre-1996 Account) as presented in Note V(E), other postemployment benefits, pollution remediation, amounts due to component units, and compensated absence obligations. The General Fund typically has been used to liquidate any other long-term liabilities.

Long-term obligations of the business-type activities consist of claims liability of the Indiana Residual Malpractice Insurance Authority and compensated absences of the Inns and Concessions Fund.

Revenue bonds are issued by entities established by statute as corporate and politic units with the separate legal authority to finance certain essential governmental functions. Income from the acquired or constructed assets is used to pay debt service.

## G. Prior Period Adjustments and Reclassifications

For the fiscal year ended June 30, 2012, certain changes have been made to the financial statements to more appropriately reflect financial activity of the State of Indiana. These prior period adjustments and restatements are reflected in the beginning net assets in the government-wide statement of activities.

Prior Period Adjustments

In the fund statements for governmental funds, there is an increase of $29.9 million in net assets of the General Fund and a corresponding decrease in net assets of the Non-major Governmental funds for revenues not properly reported by the Department of Revenue in prior years.

In the fund statements for governmental funds, and the government-wide statements, there is a decrease of $64.9 million in net assets of the General Fund due to incorrect reporting of local income tax receipts held in the local distributions agency fund.

In the fund statements for governmental funds, and the government-wide statements, net assets of the ARRA of 2009 Fund decreased $5.2 million for adjustments for cash overstated in prior years due to errors in recording transfers to component units.

In the fund financial statements for Special Revenue Funds, and the government-wide statements, net assets increased by $12.2 million due to errors in the presentation of cash in the BMV holding fund.

In the fund statements for Special Revenue funds, and the government-wide statements, there is a decrease of $11.3 million in net assets for cash that was incorrectly transferred in the prior year from the Indiana Economic Development Fund, a discrete governmental component unit.

In the fund statements for Special Revenue funds and the government-wide statements, there is a decrease of $276 thousand due to errors relating to current receivable and payable accruals in 2011.

For the government-wide statements, there is a decrease of $70.2 million in net assets for infrastructure assets included in INDOT infrastructure as of June 30, 2011.

For the government-wide statements, there is an increase of $2.5 million in net assets for Department of Administration (DoA) work in process. This was the result of omission in projects that were in progress as of June 30, 2011.

For the government-wide statements, there is an increase of $90.9 million in net assets for capital assets. This was the result of not capitalizing capital assets by June 30, 2011 that were acquired prior to this date and for corrections to acquisition cost by state agencies.

For the government-wide statements, there is an increase of $34.8 million for software that was in development by June 30, 2011 that was omitted from presentation in the prior year.

For the government-wide statements, there is a decrease of $4.0 million in net assets for liabilities for assets acquired through leases that were incorrectly reported in the prior year.

For the government-wide statements, there is a decrease of $198 million in net assets to recognize the 2011 actuarial liability for net pension obligations.

For the Internal Service funds and the government-wide statements, there is an increase of $38 thousand in net assets for the correction of errors.

For the discrete component units, the Indiana Economic Development Corporation's net assets increased by $5.8 million for loans receivable not included in their 2011 financial statements.

There was an increase of $3.5 million in beginning net assets for the inclusion of the Indiana State Museum and Historical Sites Corporation which is a new discrete component unit of the State. The corporation's foundation which was not previously reported had beginning net assets of $3.4 million and $180 thousand was reclassified from a previously reported governmental fund.

The following schedule reconciles June 30, 2011 net assets as previously reported, to beginning net assets, as restated:

| | Governmental Activities | Business-Type Activities | Discretely Presented Component Units (Non Fiduciary) |
|---|---|---|---|
| **June 30, 2011, fund balance/retained earnings/net assets as reported** | $ 19,112,313 | $ (1,690,456) | $ 11,083,658 |
| **Correction of errors** | (214,653) | - | 9,261 |
| **Reclassifications of funds** | (180) | - | 180 |
| **Balance July 1, 2011 as restated** | $ 18,897,480 | $ (1,690,456) | $ 11,093,099 |

# V. OTHER INFORMATION

## A. Risk Management

The State of Indiana is exposed to various risks of loss. This includes damage to property owned by the agencies, personal injury or property damage liabilities incurred by a State officer, agent or employee, errors, omissions and theft by employees, certain employee health benefits, employee death benefits, and unemployment and worker's compensation costs for State employees.

The State records an expenditure for any loss as the liability is incurred or replacement items are purchased. The State purchases commercial insurance coverage for certain DNR Inns properties. The State also purchases immaterial amounts of commercial insurance related to errors, omissions, and theft by employees. Settlements related to commercial insurance have not exceeded coverage in the past three fiscal years.

The State does have risk financing activity for the State employees' disability, certain State employees' health benefits, and certain health, disability and death benefits for State Police officers. These are reported in three individual Internal Service Funds.

The State employees' disability program is financed partially by State employees through payroll withholdings and by the funds from which employees are paid. The employees' health benefits and the State Police traditional health plan are funded by the employees who have selected certain health care benefit packages and the funds from which those employees are paid. (An insurance carrier does provide claims administration services for the health insurance programs.)

Located below is the table of claim liabilities. The liabilities are not maintained in the accounting records of the State. The claim liabilities for the health insurance programs and the State Disability fund were estimated based on the historical experience rate of claims paid that were for service dates incurred during a prior fiscal year. The surplus retained earnings in these funds are reserved for future catastrophic losses.

| | State Police Health Insurance Fund | State Employees' Health Insurance Fund | State Employee Disability Fund | Total |
|---|---|---|---|---|
| **2012** | | | | |
| Unpaid Claims, July 1 | $ 4,144 | $ 33,745 | $ 5,131 | **$ 43,020** |
| Incurred Claims and Changes in Estimate | 30,651 | 301,378 | 20,841 | **352,870** |
| Claims Paid | (30,869) | (294,668) | (21,558) | **(347,095)** |
| Unpaid Claims, June 30 | **$ 3,926** | **$ 40,455** | **$ 4,414** | **$ 48,795** |
| **2011** | | | | |
| Unpaid Claims, July 1 | $ 4,004 | $ 39,641 | $ 4,932 | **$ 48,577** |
| Incurred Claims and Changes in Estimate | 28,644 | 276,553 | 21,405 | **326,602** |
| Claims Paid | (28,504) | (282,449) | (21,206) | **(332,159)** |
| Unpaid Claims, June 30 | **$ 4,144** | **$ 33,745** | **$ 5,131** | **$ 43,020** |

## B. Contingencies and Commitments

*Litigation*

The State does not establish reserves for judgments or other legal or equitable claims against the State. Judgments and other such claims must be paid from the State's unappropriated balances and reserves, if any.

With respect to tort claims only, the State's liability is limited to: (A) $300,000 for a cause of action that accrues before January 2006; (B) $500,000 for a cause of action that accrues between 2006 and 2008; or (C) $700,000 for a cause of action that accrues on or after January 2008, for injury to or death of one person in any one occurrence and $5 million for injury to or death of all persons in that occurrence.

The Indiana Attorney General's office estimates a total payment for liabilities and litigation expenses of $6.5 million to be made from the Tort Claim Fund during the next fiscal year. During the fiscal year ending June 30, 2012, the State paid $8.8 million for settlements, judgments, claims and litigation expenses from the Tort Claim Fund.

In addition, the State paid $4.7 million to settle claims arising from the Indiana State Fair tragedy during the fiscal year ending June 30, 2012. The 2012 General Assembly approved an additional $6 million as a supplemental fund to be paid to Indiana State Fair claimants during the next fiscal year.

The following is a summary of certain significant litigation and claims currently pending against the State involving amounts exceeding $5 million individually or in the aggregate. This summary is not exhaustive, either as to the description of the specific litigation or claims described or as to all of the litigation or claims currently pending or threatened against the State.

The Indiana Attorney General's office is currently handling the following cases that could result in significant liabilities to the State:

In 1968, a lawsuit seeking to desegregate the Indianapolis Public Schools was filed in the United States District Court for the Southern District of Indiana. Since 1978, the State has paid several million dollars per year for inter-district busing that is expected to continue through 2016. The District Court entered its final judgment in 1981 holding the State responsible for most of the costs of its desegregation plan, and those costs have been part of the State's budget since then. In June 1998, the parties negotiated an 18-year phase out of the desegregation plan that was approved by the Court for some school corporations and a 13-year phase out of the desegregation plan for the school corporations that had already began the desegregation plan. State expenditures will be gradually reduced as the plan is phased out.

In 1993, Plaintiffs filed a breach of employment contract lawsuit in a state trial court alleging that the State has failed to pay certain similarly classified state employees at an equal rate of pay from 1973 to 1993. The Court certified Plaintiffs' class and class notification was completed. Plaintiffs seek to recover damages as well as attorney fees and costs. A four-day bench trial was conducted. The Court took the matter under advisement and gave the parties time to submit proposed findings of fact and conclusions of law. In July 2009, the Court entered judgment against the State in the total amount of $43 million ($21 million awarded to merit, overtime eligible employees; $17 million awarded to non-merit, overtime eligible employees; $3 million awarded to merit, overtime exempt employees; $2 million awarded to non-merit, overtime exempt employees). In November 2009, Plaintiffs reduced their settlement demand to $20 million. The State responded with an offer of $8.5 million (inclusive of fees and costs) and later increased the offer to $10 million. The matter is fully briefed in the Court of Appeals. In its October 2010 opinion, the Court of Appeals reversed in part, affirmed in part and remanded to trial court for determination of damages; excused exhaustion of administrative remedies, but limited back pay to 10 days (instead of 20 years) for merit employees; affirmed 20 years of back pay for non-merit employees. Impact of the opinion is a reduction in the trial court's judgment from $43 million to approximately $19 million. In November 2010, both Plaintiffs and the State filed Petitions for Rehearing. Defendants' Petition for Rehearing denied. Plaintiff's Petition for Rehearing granted in part remanding to trial court for determination of if/when individual merit plaintiffs filed administrative complaints. Plaintiffs and the State each filed Petitions for Transfer to the Indiana Supreme Court, which were granted in June 2011. Oral argument was held in the Supreme Court in September 2011. The Indiana Supreme Court ruled in February 2012 that both the "Merit and Non-Merit" employees, overtime-exempt and overtime-eligible, are all owed back pay on their claims for the same period (ten days prior to each class member filing claims or, if no claims filed, ten days prior to filing the lawsuit). This opinion further reduced the amount of damages owed to the plaintiffs. Plaintiffs' and the State's Petitions for Rehearing filed with Supreme Court in March 2012 were denied. The matter is now remanded to the trial court to determine damages in accordance with the ten-day limit on back pay. Parties are involved in informal discovery related to back pay.

In August 2011, due to a sudden wind gust resulting from inclement weather conditions, an outdoor stage collapsed at the Indiana State Fair resulting in multiple injuries and deaths. Tort claim notices against the Indiana State Fair Commission and the State were filed with the Indiana Attorney General. Lawsuits against the State and other parties were filed. The State contends that immunities and limitations on damages under the Indiana Tort Claims Act apply to these claims. Under the Indiana Tort Claims Act, Indiana Code 34-13-3, claims are capped at $5 million per event and $700,000 per person. The State, on behalf of the Commission, settled with many of the claimants, distributing $4.7 million during fiscal year 2012 with one case remaining under litigation. The 2012 General Assembly supplemented this amount with an additional $6 million which will be distributed pursuant to legislative directives during the next fiscal year. $6 million has been accrued as an expense and payable in the government-wide financial statements for this distribution. Tort claims were paid from the State General Fund and not the funds of the Commission. The remaining open litigation concerns the constitutionality of the tort claim caps and indemnification claims as a result of this incident.

*Other Litigation*

The State on behalf of the Indiana Family and Social Services Administration (FSSA) is currently involved in the following case that could result in significant liability to the State:

In May 2010 the State of Indiana, on behalf of the Indiana Family and Social Services Administration (FSSA), and counterclaim Plaintiff sued each other regarding counterclaim Plaintiff's state welfare system contract entered into in 2006. In October 2009 the State announced its intention to terminate the 10-year contract early effective December 2009 due to counterclaim Plaintiff's deficient performance. The court issued rulings in July and August of 2012 awarding the counterclaim Plaintiff $62.7 million. This amount includes $9.5 million for equipment retained by the state, $2.5 million in early termination close-out payments, $40 million in subcontractor assignment fees (previously granted to the counterclaim Plaintiff on summary judgment), and $10.7 million in prejudgment interest. The court also ruled that the counterclaim Plaintiff was not entitled to recover $43 million claimed for deferred fees. The court also ruled that there was no material breach so the State could not recover damages from the counterclaim Plaintiff for breach of contract. The State has appealed. The court granted the State's motion to stay the enforcement of the judgment pending appeal.

*Other Loss Contingencies*

The U.S. Office of Inspector General (USOIG) has issued multiple audit reports on Indiana's Medicaid Assistance Program. Findings in these reports identify several issues including state psychiatric hospitals that were ineligible to receive Medicaid Inpatient payments and unreported Medicaid overpayments. The State has worked with Centers for Medicare and Medicaid Services (CMS) to resolve the findings. As of June 30, 2012 there was $55.5 million in findings that CMS had not recommended for closure, but FSSA believes the possible loss contingency for these findings totals $16.7 million. FSSA management is continuing to work with CMS on a settlement of these findings. It is unknown how much of this loss contingency, if any, will have to be repaid to the federal government.

*Construction Commitments*

As of June 30, 2012, the Indiana Department of Transportation had outstanding construction commitments totaling $1.3 billion for road and bridge projects. It is anticipated that these projects will be financed with approximately 3% State funds, 2% local funds, 54% traditional Federal funds, 1% ARRA of 2009 fund, and 40% from the Major Moves Construction Fund.

The Indiana Department of Administration, Public Works Division, had remaining construction commitments totaling $10.1 million for building and improvement projects of the State's agencies as of June 30, 2012. These projects are to be funded through State appropriations, the State Highway Department Fund, capital projects funds, and federal funds.

The State had $32.2 million in total commitments for software in development as of June 30, 2012. These commitments are to be funded through federal funds and state dedicated funds.

*Encumbrances*

Significant encumbrances by major funds and non-major funds in the aggregate as of June 30, 2012 were as follows:

| Governmental Funds | | Encumbrances |
|---|---|---|
| General Fund | $ | 561,876 |
| ARRA of 2009 | | 28,068 |
| US Department of Transportation | | 1,052,618 |
| US Department of Health & Human Services | | 225,644 |
| Non-Major Governmental Funds | | 1,229,390 |
| **Total** | **$** | **3,097,596** |

## C. Other Revenue

Other revenue represents revenue received which cannot accurately be included with any of the other revenue sources. In most cases, the amount of “other revenue" received by a fund is insignificant in comparison with total revenues received.

## D. Economic Stabilization Fund

In 1982 the Indiana General Assembly adopted Indiana Code 4-10-18, which established the Counter-Cyclical Revenue and Economic Stabilization Fund ("Rainy Day Fund").

This fund was established to assist in stabilizing revenue during periods of economic recession and is accounted for within the State general fund.

Each year the State Budget Director determines calendar year Adjusted Personal Income (API) for the State and its growth rate over the previous year, using a formula determined by the legislature.

In general, monies are deposited automatically into the Rainy Day Fund if the growth rate in API exceeds 2%; monies are removed automatically from the Rainy Day Fund if API declines by more than 2%. If the balance in the fund at the end of the fiscal year exceeds 7% of total general fund revenues for the same period, the excess is transferred from the Rainy Day Fund to the State General Fund.

Loans can be made from the Rainy Day Fund to local units of government for specific purposes. The Rainy Day Fund cash and investment balance at the end of fiscal year 2012 was $351.6 million. Total outstanding loans were $11.6 million, resulting in total assets of $363.2 million. Because the API increased by more than 2%, $291.0 million was transferred from the General Fund to the Rainy Day Fund.

## E. Employee Retirement Systems and Plans

The State of Indiana sponsors eight public employee retirement systems (PERS) that are included in the State's financial statements. They are reported and administered as described in Note I(A).

<u>Summary of Significant Accounting Policies (Primary government and fiduciary in nature component units)</u>

The accrual basis is used for financial statement reporting purposes. Contributions are recognized as revenues when due, pursuant to formal commitments, as well as statutory or contractual requirements. Throughout the year, the investments are maintained on the accounting records at the net asset value per the custodian banks. The custodian banks maintain records of the detailed holdings and accounts that comprise the net asset value. At fiscal year end, the accounting records and financial statements recognize investment assets and liabilities using investment unit trust accounting. Investments of defined benefit plans are reported at fair value. Short-term investments are reported at market value when available, or at cost, which approximates fair value.

Securities traded on a national or international exchange are valued at the official closing price at current exchange rates. Collective trust funds’ fair values are determined by the fair value per share of the pool’s underlying portfolio as provided by the trustee. Mortgages are valued on the basis of future principal and interest payments, and are discounted at prevailing interest rates for similar instruments. Values for limited partnership interests are those estimates most recently provided by the general manager, plus or minus cash flows transacted since the valuation date. Investments that do not have an established market are reported at estimated fair value.

*The State sponsors the following defined benefit single-employer plans:*

<u>State Police Retirement Fund (Presented as a pension fund)</u>

<u>Plan Description</u> The State Police Retirement Fund (SPRF) is a defined benefit, single-employer PERS, and is administered by the Treasurer of the State of Indiana as Trustee under a Pension Trust Agreement with the Indiana Department of State Police. Indiana Code 10-12-2-2 grants authority to the Department to establish and operate an

actuarially sound pension plan governed by a pension trust. It also authorizes the Department to make annual contributions as necessary to prevent any deterioration in the actuarial status of the trust.

The State Police Retirement Fund does not issue a stand-alone financial report. The SPRF's financial statements are included in the State of Indiana's CAFR as part of the statements presented with fiduciary funds.

Funding Policy The pre-1987 plan required employee contributions of five percent of the salary of a sixth-year trooper. The 1987 plan applies to all officers hired after June 30, 1987. In addition, State police officers hired prior to July 1, 1987 could elect to be covered under this plan if the employee filed an election with the trustee before July 1, 1989. Participants under the 1987 plan contribute six percent of their monthly salary.

Periodic employer contributions to the pension plan are determined on an actuarial basis using the entry age normal cost actuarial method. Normal cost is funded on a current basis. Under the terms of the Trust Agreement, in the event the Department fails to make the minimum contribution for five successive years, the Trust shall terminate and the fund shall be liquidated. The unfunded actuarial accrued liability is being funded over a thirty-year closed period which commenced July 1, 2010. Periodic contributions for both normal cost and the amortization of the unfunded actuarial accrued liability are based on the level dollar of payroll method. The funding policy for normal cost and unfunded actuarial accrued liability should provide sufficient resources to pay employee pension benefits on a timely basis.

Funded Status and Funding Progress As of June 30, 2012, the most recent actuarial valuation date, the plan was 74 percent funded. The actuarial accrued liability for benefits was $504.8 million, and the actuarial value of assets was $372.2 million, resulting in an unfunded actuarial accrued liability (UAAL) of $132.6 million. The covered payroll (annual payroll of active employees covered by the plan) was $66.1 million, and the ratio of the UAAL to the covered payroll was 201 percent.

The schedule of funding progress, presented as RSI following the notes to the financial statement, presents multi-year trend information about whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liability for benefits.

State Excise Police, Gaming Agent, Gaming Control Officer and Conservation Enforcement Officers' Retirement Plan (Presented as part of INPRS – a fiduciary in nature component unit)

Plan Description The State Excise Police, Gaming Agent, Gaming Control Officer and Conservation Enforcement Officers' Retirement Plan (EG&C) is a single employer defined benefit plan administered by the Board of Trustees of the Indiana Public Retirement System. The retirement fund is for certain employees of the Indiana Department of Natural Resources, the Indiana Alcohol and Tobacco Commission, and any State excise police officer, Indiana state conservation enforcement officer, gaming agent or any gaming control officer who is engaged exclusively in the performance of law enforcement duties.

The State Excise Police, Gaming Agent, Gaming Control Officer, and Conservation Enforcement Officers' Retirement Plan provides retirement, disability, and survivor benefits. Indiana Code 5-10-5.5 governs the requirements of the Fund. The Indiana Public Retirement System issues a publicly available financial report that includes financial statements and required supplementary information for the plan as a whole. That report may be obtained by writing the Indiana Public Retirement System, One North Capitol, Suite 001, Indianapolis, IN 46204, by calling 888-526-1687, or by visiting INPRS' website, www.in.gov/inprs.

Funding Policy The funding policy for the EG&C Plan is in accordance with IC 5-10-5.5-8.5. Members are required by statute to contribute 4 percent of the member's annual salary to the Plan. The employer contribution rate is actuarially determined. The required contributions are determined by the INPRS Board of Trustees based on actuarial investigation and valuation. During fiscal year 2012, all participating employers were required to contribute 20.75 percent of covered payroll.

Funded Status and Funding Progress As of June 30, 2012, the most recent actuarial valuation date, the plan was 67 percent funded. The actuarial accrued liability for benefits was $113.3 million, and the actuarial value of assets was $76.0 million, resulting in an unfunded actuarial accrued liability (UAAL) of $37.3 million. The covered payroll (annual payroll of active employees covered by the plan) was $25.8 million, and the ratio of the UAAL to the covered payroll was 145 percent.

The schedule of funding progress, presented as RSI following the notes to the financial statement, presents multi-year trend information about whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liability for benefits.

Prosecuting Attorneys' Retirement Fund (Presented as part of INPRS – a fiduciary in nature component unit)

Plan Description The Prosecuting Attorneys' Retirement Fund (PARF) is a defined benefit single-employer plan administered by the Board of Trustees of the Indiana Public Retirement System. The Prosecuting Attorneys' Retirement Fund provides retirement, disability, and survivor benefits for individuals who serve as a prosecuting attorney or chief deputy prosecuting attorney; or serve as the executive director or assistant executive director of the Indiana Prosecuting Attorneys Council or as a state-paid deputy prosecuting attorney.

These individuals' salaries are paid from the General Fund of the State of Indiana. Indiana Code 33-39-7 governs the requirements of the Fund. The Indiana Public Retirement System issues a publicly available financial report that includes financial statements and required supplementary information for the plan as a whole. That report may be obtained by writing the Indiana Public Retirement System, One North Capitol, Suite 001, Indianapolis, IN 46204, by calling 888-526-1687, or by visiting INPRS' website, www.in.gov/inprs.

Funding Policy Contributions made by or on the behalf of members are not actuarially determined but are set by statute at six percent (6%) of wages. The amount required to actuarially fund participants' retirement benefits, as determined by the INPRS Board of Trustees on the recommendations of the actuary, is to be appropriated from the State's General Fund.

Funded Status and Funding Progress As of June 30, 2012, the most recent actuarial valuation date, the plan was 49 percent funded. The actuarial accrued liability for benefits was $56.1 million, and the actuarial value of assets was $27.5 million, resulting in an unfunded actuarial accrued liability (UAAL) of $28.6 million. The covered payroll (annual payroll of active employees covered by the plan) was $21.7 million, and the ratio of the UAAL to the covered payroll was 132 percent.

The schedule of funding progress, presented as RSI following the notes to the financial statement, presents multi-year trend information about whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liability for benefits.

Legislators' Retirement System – Legislators' Defined Benefit Plan (Presented as part of INPRS – a fiduciary in nature component unit)

Plan Description The Legislators' Defined Benefit Plan (IC 2-3.5-4), a single-employer defined benefit plan, applies to each member of the Indiana General Assembly who was serving on April 30, 1989 and filed an election under IC 2-3.5-3-1(b). The Legislators' Defined Benefit Plan provides retirement, disability and survivor benefits. The plan is administered by the Board of Trustees of the Indiana Public Retirement System. The Indiana Public Retirement System issues a publicly available financial report that includes financial statements and required supplementary information for the plan as a whole. That report may be obtained by writing the Indiana Public Retirement System, One North Capitol, Suite 001, Indianapolis, IN 46204, by calling 888-526-1687, or by visiting INPRS' website, www.in.gov/inprs.

Funding Policy The amount required by the funding policy to actuarially fund participants' retirement benefits, as determined by the INPRS Board of Trustees on the recommendation of the actuary, is to be appropriated from the State's General Fund.

Funded Status and Funding Progress As of June 30, 2012, the most recent actuarial valuation date, the plan was 75 percent funded. The actuarial accrued liability for benefits was $4.5 million, and the actuarial value of assets was $3.4 million, resulting in an unfunded actuarial accrued liability (UAAL) of $1.1 million. The benefit formula is determined based on service rather than compensation. The unfunded liability per active participant was $187,726 as of the most recent actuarial valuation.

The schedule of funding progress, presented as RSI following the notes to the financial statement, presents multi-year trend information about whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liability for benefits.

Judges' Retirement System (Presented as part of INPRS – a fiduciary in nature component unit)

Plan Description The Judges' Retirement System (JRS) is a defined benefit single-employer public employee retirement system administered by the Board of Trustees of the Indiana Public Retirement System, and is governed by IC 33-38-6, 33-38-7, and IC 33-38-8. The Judges' Retirement System provides retirement, disability, and survivor benefits. Coverage is for any person who has served, is serving or shall serve as a regular judge or justice of any of the following courts: Supreme Court of the State of Indiana; Court of Appeals; Circuit Court of a Judicial Circuit; Indiana Tax Court; or county courts including Superior, Criminal, Probate, Juvenile, Municipal and County Courts. The system consists of two plans: the 1977 system and the 1985 system. IC 33-38-7 applies to judges who began service before September 1, 1985. IC 33-38-8 applies to judges beginning service after August 31, 1985. The Indiana Public Retirement System issues a publicly available financial report that includes financial statements and required supplementary information for the plan as a whole. That report may be obtained by writing the Indiana Public Retirement System, One North Capitol, Suite 001, Indianapolis, IN 46204, by calling 888-526-1687, or by visiting INPRS' website, www.in.gov/inprs.

Funding Policy  Member contributions are established by statute at six percent of total statutory compensation paid by the state of Indiana, deducted from the member's salary and remitted by the Auditor of State. However, no contribution is required and no such amounts shall be paid by the member for more than 22 years of service.

Employer contributions are actuarially determined and approved by the INPRS Board of Trustees and by the Indiana General Assembly as biennial appropriations from the State's General Fund. Indiana Code 33-38-6-17 provides that this appropriation only include sufficient funds to cover the aggregate liability of the fund for benefits to the end of the biennium, on an actuarially funded basis. The statute also provide for remittance of docket fees and court fees. These are considered employer contributions.

Funded Status and Funding Progress As of June 30, 2012, the most recent actuarial valuation date, the plan was 59 percent funded. The actuarial accrued liability for benefits was $437.9 million, and the actuarial value of assets was $260.1 million, resulting in an unfunded actuarial accrued liability (UAAL) of $177.8 million. The covered payroll (annual payroll of active employees covered by the plan) was $45.1 million, and the ratio of the UAAL to the covered payroll was 394 percent.

The schedule of funding progress, presented as RSI following the notes to the financial statement, presents multi-year trend information about whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liability for benefits.

*The State sponsors the following defined benefit agent multiple-employer plan:*

Public Employees' Retirement Fund (Presented as part of INPRS – a fiduciary in nature component unit)

Plan Description  The Public Employees' Retirement Fund (PERF) is a defined benefit agent multiple-employer plan for units of state and local governments administered by the Indiana Public Retirement System Board of Trustees. PERF provides retirement, disability, and survivor benefits. Indiana Code 5-10.2, 5-10.3, and 5-10.5 governs the requirements of the Fund. The Indiana Public Retirement System issues a publicly available financial report that includes financial statements and required supplementary information for the plan as a whole. That report may be obtained by writing the Indiana Public Retirement System, One North Capitol, Suite 001, Indianapolis, IN 46204, by calling 888-526-1687, or by visiting INPRS' website, www.in.gov/inprs. At June 30, 2012, the number of participating political subdivisions was 1,121, and there were also 17 State-related participating employers.

Funding Policy  The State of Indiana and any political subdivision that elects to participate in the PERF fund is obligated by statute to make contributions to the plan. The required contributions are determined by the INPRS Board of Trustees based on actuarial investigation and valuation. The funding policy provides for periodic employer contributions at actuarially determined rates that, expressed as percentages of annual covered payroll, are sufficient to fund the pension benefits when they become due.

Contributions made by or on the behalf of members are not actuarially determined but are set by statute at three percent (3%) of compensation. These contributions are credited to the member's annuity savings account that is a separate benefit from the defined pension benefit. The State is required to contribute for State employees at an actuarially determined rate; during fiscal year 2012, State-related participating employers were required to contribute 8.6% of covered payroll.

Funded Status and Funding Progress  Funded status and funding progress information is being disclosed for the State of Indiana employee portion of the plan. The funded status and funding progress information presented is for active and retired assets.

State of Indiana Employees: As of June 30, 2012, the most recent actuarial valuation date, the state employees portion of the plan was 75 percent funded. The actuarial accrued liability for benefits was $5.5 billion, and the actuarial value of assets was $4.1 billion, resulting in an unfunded actuarial accrued liability (UAAL) of $1.4 billion. The covered payroll (annual payroll of active employees covered by the plan) was $1.6 billion, and the ratio of the UAAL to the covered payroll was 85 percent.

The schedule of funding progress, presented as RSI following the notes to the financial statements, presents multi-year trend information about whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liability for benefits.

Annual Pension Cost and Net Pension Obligation The annual pension cost and net pension obligations, the significant actuarial assumptions, and three-year historical trend information of the single and agent multiple employer defined benefit plans are as follows:

| | Primary Government | Fiduciary in Nature Component Unit | | | | | |
|---|---|---|---|---|---|---|---|
| | SPRF | PERF -State | ECRF | JRS | PARF | LRS | TRF - Pre-1996 Account |
| **Annual Pension Cost and Net Pension Obligation (Asset)** | | | | | | | |
| Annual required contribution | $ 14,517.0 | $ 183,389.3 | $ 5,532.4 | $ 19,664.4 | $ 2,037.0 | $ 113.1 | $ 866,207.0 |
| Interest on net pension obligation | 1,147.3 | 404.1 | (179.5) | (1,960.8) | 538.9 | (2.7) | 82,463.0 |
| Adjustment to annual required contribution | (1,334.9) | (465.2) | 206.6 | 2,257.3 | (620.3) | 3.1 | (94,935.0) |
| Annual pension cost | 14,329.4 | 183,328.2 | 5,559.5 | 19,961.0 | 1,955.6 | 113.5 | 853,735.0 |
| Contributions made | (12,365.9) | (138,327.5) | (5,053.1) | (18,896.2) | (1,838.9) | (113.1) | (764,423.0) |
| Increase (decrease) in net pension obligation | 1,963.5 | 45,000.7 | 506.4 | 1,064.8 | 116.6 | 0.4 | 89,312.0 |
| Net pension obligation, beginning of year | 16,389.9 | 5,772.7 | (2,564.0) | (28,011.3) | 7,697.9 | (38.1) | 1,178,044.0 |
| Net pension obligation, end of year | $ 18,353.4 | $ 50,773.4 | $ (2,057.6) | $ (26,946.5) | $ 7,814.6 | $ (37.7) | $ 1,267,356.0 |
| **Significant Actuarial Assumptions** | | | | | | | |
| Investment rate of return | 7.00% | 6.75% | 6.75% | 6.75% | 6.75% | 6.75% | 6.75% |
| Projected future salary increases: | | | | | | | |
| Total | 3.50 - 9.00% | 3.25 - 4.50% | 3.25% | 4.00% | 4.00% | 3.00% | 3.00 - 12.50% |
| Attributed to inflation | 3.5% | 3.00% | 3.00% | 3.00% | 3.00% | 3.00% | 3.00% |
| Cost of living adjustments | N/A | 1.00% | 1.00% | 4.00% | N/A | 1.00% | 1.00% |
| Contribution rates: | | | | | | | |
| State | 25.70% | 8.20% | 20.75% | Appropriation 60.10% | Appropriation 11.40% | Flat Dollar Amount | * Pay-As-You-Go |
| Plan members | 5.00% - 6.00% | 3.00% | 4.00% | 6.00% | 6.00% | 0.00% | 3.00% |
| Actuarial valuation date | 7/1/2012 | 6/30/2012 | 6/30/2012 | 6/30/2012 | 6/30/2012 | 6/30/2012 | 6/30/2012 |
| Actuarial cost method | entry age normal cost | entry age normal cost | entry age normal cost | entry age normal cost | entry age normal cost | traditional unit credit | entry age normal cost |
| Amortization method | level dollar | level dollar | level dollar | level dollar | level dollar | level dollar | level dollar |
| Amortization period | 30 years | 30 years | 30 years | 30 years | 30 years | 30 years | 30 years |
| Amortization period (from date) | 7/1/2010 | 7/1/2008 | 7/1/2007 | 7/1/2006 | 7/1/2007 | 7/1/1992 | N/A |
| Amortization period (open or closed) | closed | closed | closed | closed | closed | closed | closed |
| Asset valuation method | smoothed basis | 4-year smoothed market value with 20% corridor | 4-year smoothed market value with 20% corridor | 4-year smoothed market value with 20% corridor | 4-year smoothed market value with 20% corridor | 4-year smoothed market value with 20% corridor | 4-year smoothed market value with 20% corridor |
| **Historical Trend Information** | | | | | | | |
| Year ended June 30, 2012 | | | | | | | |
| Annual pension cost (APC) | $ 14,329.4 | $ 183,328.2 | $ 5,559.5 | $ 19,961.0 | $ 1,955.6 | $ 113.5 | $ 853,735.0 |
| Percentage of APC contributed | 86.3% | 75.5% | 90.9% | 94.7% | 94.0% | 99.6% | 89.5% |
| Net pension obligation (asset) | $ 18,353.4 | $ 50,773.4 | $ (2,057.6) | $ (26,946.5) | $ 7,814.6 | $ (37.7) | $ 1,267,356.0 |
| Year ended June 30, 2011 | | | | | | | |
| Annual pension cost (APC) | $ 12,121.4 | $ 176,881.5 | $ 5,206.5 | $ 19,206.5 | $ 1,896.3 | $ 114.7 | $ 883,459.0 |
| Percentage of APC contributed | 78.0% | 65.1% | 99.8% | 100.0% | 9.0% | 0.0% | 84.8% |
| Net pension obligation (asset) | $ 16,389.9 | $ 5,772.7 | $ (2,564.0) | $ (28,011.3) | $ 7,697.9 | $ (38.1) | $ 1,178,044.0 |
| Year ended June 30, 2010 | | | | | | | |
| Annual pension cost (APC) | $ 14,117.4 | $ 118,839.0 | $ 5,263.1 | $ 16,409.8 | $ 1,608.7 | $ 74.5 | $ 841,500.0 |
| Percentage of APC contributed | 67.1% | 93.9% | 99.9% | 113.5% | 10.6% | 0.0% | 86.5% |
| Net pension obligation (asset) | $ 13,718.2 | $ (55,876.6) | $ (2,573.9) | $ (28,017.9) | $ 5,971.6 | $ (152.8) | $ 1,043,563.0 |

SPRF - State Police Retirement Fund
PERF - Public Employees' Retirement Fund (Administered by the INPRS Board of Trustees)
ECRF - State Excise Police, Gaming Agent, Gaming Control Officer, and Conservation Enforcement Officers' Retirement Plan (Administered by the INPRS Board of Trustees)
JRS - Judges' Retirement System (Administered by the INPRS Board of Trustees)
PARF - Prosecuting Attorneys' Retirement Fund (Administered by the INPRS Board of Trustees)
LRS - Legislators' Retirement System (Administered by the INPRS Board of Trustees)
TRF - Teachers' Retirement Fund (Administered by the INPRS Board of Trustees)
N/A - Not Applicable
* - $138,300 based on June 30, 2012 actuarial valuation

*The State sponsors the following cost-sharing multiple-employer plans:*

State Teachers' Retirement Fund (Presented as part of INPRS – a fiduciary in nature component unit)

Plan Description The State Teachers' Retirement Fund (TRF), is a defined benefit, multiple-employer cost-sharing PERS, administered by the Indiana Public Retirement System Board of Trustees. Indiana Code 5-10.2, IC 5-10.4, and IC 5-10.5 govern the requirements of the Fund. The Indiana Public Retirement System issues a publicly available financial report that includes financial statements and required supplementary information for the plan as a whole. That report may be obtained by writing the Indiana Public Retirement System, One North Capitol, Suite 001, Indianapolis, IN 46204, by calling 888-526-1687, or by visiting INPRS' website, www.in.gov/inprs.

At June 30, 2012, the number of participating employers was 367.

Funding Policy Each member is required to contribute 3% of his/her compensation to the plan. The Indiana State Teachers' Retirement Fund is funded on a "pay as you go" basis for employees hired prior to July 1, 1995, and who have maintained continuous employment with the same school corporation or covered institution since that date (Pre-1996 Account). State appropriations are made for the amount of estimated pension benefit payouts for each fiscal year. If the actual pension benefit payout for the fiscal year exceeds the amount appropriated, the difference is paid from the Pension Stabilization Fund.

For employees hired on or after July 1, 1995; or hired before July 1, 1995, and prior to June 30, 2005, were either hired by another school corporation or institution covered by the Fund or were re-hired by a covered prior employer (1996 Account); the employer contribution rate is actuarially determined. The required contributions are determined by the INPRS Board of Trustees based on actuarial investigation and valuation. The funding policy provides for periodic employer contributions at actuarially determined rates that, expressed as percentages of annual covered payroll, are sufficient to fund the pension benefits when they become due. During fiscal year 2012, all participating employers in the TRF 1996 account were required to contribute 7.5% of covered payroll.

As of June 30, 2012, TRF was 43% funded. Members in the Pre-1996 Account are funded on a "pay as you go" method for the employer portion of the pension and members in the 1996 Account are funded with employer contributions as they work. TRF accounts for these two classes of members as "Pre-1996 Account" and "1996 Account", respectively. The Pre-1996 Account is 30% funded and the 1996 Account is 91% funded.

The funded ratio of the Fund has decreased from 45% at June 30, 2004, to the ratio of 43% at June 30, 2012. The actuarial value of the Fund's assets as of the June 30, 2011 valuation was $8.9 billion and the actuarial accrued liability was $20.8 billion. The difference is the Fund's unfunded actuarial accrued liability of $11.9 billion. The annual covered payroll as of the June 30, 2012, actuarial valuation was $4.2 billion and the ratio of the unfunded actuarial liability to the annual covered payroll was 282%.

1977 Police Officers' and Firefighters' Pension and Disability Fund (Presented as part of INPRS – a fiduciary in nature component unit)

Plan Description The 1977 Police Officers' and Firefighters' Pension and Disability Fund (1977 Fund) is a defined benefit, multiple employer cost sharing public employees retirement system administered by the Indiana Public Retirement System Board of Trustees. Indiana Code 36-8-8 governs the requirements of the Fund that provides retirement, disability, and survivor benefits. The Indiana Public Retirement System issues a publicly available financial report that includes financial statements and required supplementary information for the plan as a whole. That report may be obtained by writing the Indiana Public Retirement System, One North Capitol, Suite 001, Indianapolis, IN 46204, by calling 888-526-1687, or by visiting INPRS' website, www.in.gov/inprs.

At June 30, 2012, the number of participating employer units totaled 162 (which includes 257 police and fire departments).

Funding Policy A participant is required by statute to contribute six percent of a first class officer's or firefighter's salary for the term of their employment up to 32 years. Employer contributions are determined actuarially and during fiscal year 2012, all participating employers were required to contribute 19.5% during the period of July 1 – December 31, 2011 and 19.7% during the period of January 1 – June 30, 2012 of the salary of a first-class officer or firefighter. The funding policy mandated by statute requires quarterly remittances of member and employer contributions based on percentages of locally established estimated salary rates, rather than actual payroll.

The annual required contributions, percentage contributed, and three-year historical trend information, for the cost sharing, multiple-employer plans are as follows:

| | Discretely Presented Component Units | |
|---|---|---|
| **Historical Trend Information** | STRF | PFPF |
| Year ended June 30, 2012 | | |
| Annual required contribution | $ 866,207 | $ 141,988 |
| Percentage contributed | 88% | 96% |
| Employer contribution | $ 764,423 | $ 135,605 |
| Year ended June 30, 2011 | | |
| Annual required contribution | $ 894,507 | $ 133,903 |
| Percentage contributed | 84% | 100% |
| Employer contribution | $ 748,978 | $ 133,726 |
| Year ended June 30, 2010 | | |
| Annual required contribution | $ 850,493 | $ 126,558 |
| Percentage contributed | 86% | 103% |
| Employer contribution | $ 727,766 | $ 130,775 |

STRF - State Teachers' Retirement Fund - Pre-1996 Account
PFPF - 1977 Police Officers and Firefighters' Retirement Fund (Administered by PERF)

*The State sponsors the following defined contribution plan:*

Legislators' Retirement System – Legislators' Defined Contribution Plan (Presented as part of INPRS – a fiduciary in nature component unit)

Plan Description The Legislators' Defined Contribution Plan (IC 2-3.5-5), a single employer defined contribution plan applies to each member of the General Assembly who was serving April 30, 1989 and files an election under IC 2-3.5-3-1(b), and each member of the General Assembly who is elected or appointed after April 30, 1989. The plan is administered by the Board of Trustees' of the Indiana Public Retirement System. The Indiana Public Retirement System issues a publicly available financial report that includes financial statements and required supplementary information for the plan as a whole. That report may be obtained by writing the Indiana Public Retirement System, One North Capitol, Suite 001, Indianapolis, IN 46204, by calling 888-526-1687, or by visiting INPRS' website, www.in.gov/inprs.

Funding Policy For the Legislators' Defined Contribution Plan, each participant is required to contribute 5 percent of annual salary. In addition, the state of Indiana is required to contribute a percentage of the member's annual salary on behalf of the participant as determined by INPRS Board of Trustees and confirmed by the State Budget Agency each year. Effective January 1, 2012 the rate was established at 11.6 percent.

## F. Other Postemployment Benefits

### *Defined Benefit Plans*

Plan Descriptions The State of Indiana sponsors and contributes to four single-employer defined benefit healthcare plans: State Personnel Plan (SPP); Legislature Plan (LP); Indiana State Police Plan (ISPP); and the Conservation and Excise Police Plan (CEPP). The SPP and LP are administered by the State Personnel Department. The Indiana State Police administer the ISPP. The CEPP is administered by the Indiana State Excise Police and Indiana Conservation Officers Health Insurance Committee. All four plans provide medical plan health care benefits to eligible State employee retirees and beneficiaries. The medical benefits provided to retirees are the same benefit options afforded active employees. Benefit provisions for each plan are established and may be amended by Indiana Code 5-10-8 *et seq*. Separate financial reports are not issued for these plans.

Funding Policy and Annual OPEB Cost The contribution funding policy for each of the four plans is on a pay-as-you-go cash basis. However, trust funds as authorized by the Indiana General Assembly were created during the last few years to start pre-funding the SPP, ISPP, and CEPP plans. The State of Indiana's annual other postemployment benefit (OPEB) cost (expense) for each plan is calculated based on the annual required contribution (ARC) of the employer, an amount actuarially determined in accordance with the parameters of GASB Statement 45. The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover normal cost each year and to amortize any unfunded actuarial liabilities (or funding excess) over a period not to exceed thirty years.

The State of Indiana's annual OPEB cost for the current year and the related information for each plan are as follows:

| | State Personnel Healthcare Plan | Legislature's Healthcare Plan | Indiana State Police Healthcare Plan | Conservation and Excise Police Health Care Plan |
|---|---|---|---|---|
| Contribution rates: | | | | |
| State of Indiana | Pay-as-you-go | Pay-as-you-go | Pay-as-you-go | Pay-as-you-go |
| Plan members (monthly premium) | See next chart | See next chart | See next chart | See next chart |
| Annual required contribution | $ 2,964 | $ 815 | $ 27,794 | $ 3,675 |
| Interest on net OPEB obligation | 223 | 36 | 5,309 | 590 |
| Amortization adjustment to ARC | (257) | (50) | (6,767) | (804) |
| Annual OPEB Cost | 2,930 | 801 | 26,336 | 3,461 |
| Contributions made | (33,849) | (487) | (18,627) | (6,891) |
| Change in net OPEB obligation | (30,919) | 314 | 7,709 | (3,430) |
| Net OPEB obligation - beginning of year | 3,191 | 806 | 101,131 | 13,101 |
| Net OPEB obligation - end of year | $ (27,728) | $ 1,120 | $ 108,840 | $ 9,671 |

The plan administrators (see plan descriptions above) establish the contribution requirements of plan members. Plan members (retirees and eligible dependents) who participate in these healthcare plans must pay the full 2012 monthly premiums (except for grandfathered LP current retirees) as shown in the following chart.

| | Monthly Premium |
|---|---|
| State Personnel Healthcare Plan (SP) and Legislature's Healthcare Plan (LP) | |
| Consumer Driven Health Plan #1 | |
| Single (Non-Tobacco) | $ 380.38 |
| Family (Non-Tobacco) | 1,143.48 |
| Consumer Driven Health Plan #2 | |
| Single (Non-Tobacco) | 502.19 |
| Family (Non-Tobacco) | 1,456.39 |
| Traditional PPO | |
| Single (Non-Tobacco) | 808.73 |
| Family (Non-Tobacco) | 2,272.40 |
| Indiana State Police Healthcare Plan (ISPP) | |
| Basic Plan - Medical Only | |
| Retiree Only (Pre-Medicare) | 369.14 |
| Retiree Plus One Dependent (Pre-Medicare) | 474.80 |
| Retiree Only (Post-Medicare) | 136.84 |
| Retiree Plus One Dependent (Post-Medicare) | 164.74 |
| Optional Plan - Medical, Dental, & Vision | |
| Retiree Only (Pre-Medicare) | 386.42 |
| Retiree Plus One Dependent (Pre-Medicare) | 463.15 |
| Retiree Only (Post-Medicare) | 140.46 |
| Retiree Plus One Dependent (Post-Medicare) | 172.23 |
| Conservation and Excise Police Health Care Plan (CEPP) | |
| Single - Under Age 60 (Pre-Medicare) | 320.00 |
| Family - Under Age 60 (Pre-Medicare) | 561.00 |
| Single - Age 60 -64 (Pre-Medicare) | 213.00 |
| Family - Age 60-64 (Pre-Medicare) | 320.00 |
| Single (Post-Medicare) | 128.00 |
| Family (Post-Medicare) | 183.00 |

The State of Indiana's annual OPEB cost, the percentage of annual OPEB cost contributed, and the net OPEB obligation for June 30, 2010 through June 30, 2012 for each of the plans were as follows:

| | Year Ended | Annual OPEB Cost | Percentage of OPEB Cost Contributed | Net OPEB Obligation |
|---|---|---|---|---|
| | 6/30/2012 | $ 2,930 | 1155.1% | $ (27,728) |
| State Personnel Healthcare Plan | 6/30/2011 | 4,499 | 376.1% | 3,191 |
| | 6/30/2010 | 6,105 | 31.3% | 15,615 |
| | 6/30/2012 | $ 802 | 60.9% | $ 1,120 |
| Legislature's Healthcare Plan | 6/30/2011 | 551 | 64.0% | 806 |
| | 6/30/2010 | 512 | 61.1% | 608 |
| | 6/30/2012 | $ 26,336 | 70.7% | $ 108,840 |
| Indiana State Police Healthcare Plan | 6/30/2011 | 28,915 | 47.7% | 101,131 |
| | 6/30/2010 | 41,224 | 21.9% | 86,003 |
| | 6/30/2012 | $ 3,460 | 199.1% | $ 9,671 |
| Conservation and Excise Police | 6/30/2011 | 4,257 | 31.4% | 13,101 |
| Health Care Plan | 6/30/2010 | 5,271 | 24.7% | 10,180 |

Funded Status and Funding Progress The funded status of the plans as of June 30, 2012, was as follows:

| | State Personnel Healthcare Plan | Legislature's Healthcare Plan | Indiana State Police Healthcare Plan | Conservation and Excise Police Health Care Plan |
|---|---|---|---|---|
| Actuarial accrued liability (a) | $ 36,643 | $ 11,956 | $ 291,148 | $ 41,804 |
| Actuarial value of plan assets (b) | 44,008 | - | 17,033 | 5,773 |
| Unfunded actuarial accrued liability (funding excess) (a) - (b) | $ (7,365) | $ 11,956 | $ 274,115 | $ 36,031 |
| Funded ratio (b)/(a) | 120.1% | 0.0% | 5.9% | 13.8% |
| Covered payroll (c) | $ 1,166,823 | $ 1,787 | $ 87,040 | $ 12,600 |
| Unfunded actuarial accrued liability (funding excess) as a percentage of covered payroll ([(a)-(b)]/(c)) | -0.6% | 669.1% | 314.9% | 286.0% |

GASB 45 regulations permit employers to use the most recent available actuarial information up to two years prior to the current period. Accordingly, the State has elected to use the actuarial results for the period ending on June 30, 2011 for the period ending June 30, 2012.

Actuarial valuations involve estimates of the value of reported amounts and assumptions about the probability of events in the future. Amounts determined regarding the funded status of the plan and the annual required contributions of the employer are subject to continual revisions as actual results are compared to past expectations and new estimates are made about the future. The required schedule of funding progress presented as required supplementary information provides multiyear trend information that shows whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liability for benefits.

Actuarial Methods and Assumptions Projections of benefits are based on the substantive plan (the plan as understood by the employer and plan members) and include the types of benefits in force at the valuation date. Actuarial calculations reflect a long-term perspective and employ methods and assumptions that are designed to reduce short-term volatility in actuarial accrued liabilities and the actuarial value of assets.

Significant methods and assumptions were as follows:

| | State Personnel Healthcare Plan | Legislature's Healthcare Plan | Indiana State Police Healthcare Plan | Conservation and Excise Police Health Care Plan |
|---|---|---|---|---|
| Actuarial valuation date | 6/30/2012 | 6/30/2012 | 6/30/2012 | 6/30/2012 |
| Actuarial cost method | Projected unit credit | Projected unit credit | Projected unit credit | Projected unit credit |
| Amortization method | Level dollar amount, open | Level dollar amount, open | Level dollar amount, open | Level dollar amount, open |
| Remaining amortization period | 30 years | 30 years | 30 years | 30 years |
| Asset valuation method | Market Value of Assets | N/A | Market Value of Assets | Market Value of Assets |
| Actuarial assumptions: | | | | |
| Inflation rate | 3.0% | 3.0% | 3.0% | 3.0% |
| Investment rate of return | 7.0% | 4.5% | 5.3% | 4.5% |
| Projected salary increases | 4.0% | 4.0% | 4.0% | 4.0% |
| Healthcare inflation rate | 9.2% | 9.2% pre-65 & 10.0% post-65 | 9.2% pre-65 & 10.0% post-65 | 9.2% pre-65 & 10.0% post-65 |

GASB 45 regulations permit employers to use the most recent available actuarial information up to two years prior to the current period. Accordingly, the State elected to use the actuarial results for the period ending June 30, 2011 for the period ending June 30, 2012. There have been no material changes in the retiree health benefits or contribution requirements from the most recent available actuarial valuation for the period ending June 30, 2010 except for the pre-funding of retiree health benefits for CEPP, ISPP and SPP. However, the healthcare inflation rates and the per capita costs were updated for the current year valuation.

***Defined Contribution Plan***

Plan Description The State of Indiana sponsors one single employer defined contribution OPEB plan established as a trust fund, the Retiree Health Benefit Trust Fund, in IC 5-10-8-8.5. The State established this trust fund to provide funding for the retiree health benefit plan developed under IC 5-10-8.5. The plan is a benefit to employees who retire and are eligible for and have received a normal, unreduced or disability retirement benefit (as determined by statutes and codes governing a State public employee retirement fund). Qualified retirees of the State are eligible to receive retirement medical benefits from this Plan. Retirees' and/or covered dependents' qualifying health insurance and medical costs are eligible for reimbursement from their reimbursement account, subject to Plan conditions and limitations.

Plan Provisions Benefit provisions for this plan are established or may be amended by the State legislature. The State Budget Agency of the State of Indiana is the administrator of the plan pursuant to Indiana Code 5-10-8-8.5. The plan establishes a retirement medical benefits account for elected officers, appointed officers, and most employees of the executive, legislative, and judicial branches of state government to pay for participants' medical insurance after retirement. Legislation passed by the 2012 Indiana General Assembly removed from eligibility in the DC plan all Conservation Officers, all Excise Officers, and employees of the Indiana State Police who did not previously waive coverage under the agency's DB plan. Benefits are entitled to be received from this account for a participant who: a) is eligible for and has applied to receive a normal, unreduced or disability retirement benefit under the Public Employees' Retirement Fund; or b) has completed at least 10 years of service as an elected or appointed officer; or c) has completed at least 15 years of service with the state for an employee. A surviving spouse or IRS dependent of a retired participant is allowed to receive the benefit from this account. Amounts credited to a retired participant are forfeited if the participant dies without a surviving spouse or IRS dependent.

The trust meets the requirements of a qualified OPEB trust. The trust is qualified under section 115 of the Internal Revenue Code.

Contributions The State is required to make annual contributions to the account based on the following schedule:

| Employee's Age | Annual State Contributions |
|---|---|
| Less than 30 | $500 |
| At least 30, but less than 40 | $800 |
| At least 40, but less than 50 | $1,100 |
| At least 50 | $1,400 |

An additional bonus contribution is to be made upon a participant's retirement with normal unreduced benefits if the retirement occurs between July 1, 2007 and July 1, 2017, and the retiree on the last day of service has completed at least 15 years of service or 10 years of service as an elected or appointed officer. The additional bonus contribution amount is one thousand dollars ($1,000) multiplied by the participant's years of service (rounded down to the nearest whole year).

At June 30, 2012, the plan participants consisted of:

| Description | Number |
|---|---|
| Active participants with accounts, not yet retired | $27,816 |
| Retired participants with accounts | 4,344 |
| Total | $32,160 |

At June 30, 2012, plan participants' retirement medical plan account balances totaled $225.3 million which consisted of $133.0 million in unretired active participants' accounts and $92.3 million in retired participants' accounts.

This plan is a defined contribution individual account for GASB 45 purposes. The employer subsidy is defined in terms of an annual contribution to an individual account. Plan assets are maintained in the Retiree Health Benefit Trust Fund created by the State as a dedicated trust fund.

The trust fund consists of cigarette tax revenues deposited in the fund under IC 6-7-1-28.1(7) and other appropriations, revenues, or transfers to the trust fund under IC 4-12-1. Cigarette tax revenues to the fund were suspended effective July 1, 2011 and are to resume on July 1, 2014. The plan benefits satisfy the condition of being a defined contribution OPEB benefit and by definition, there is no unfunded liability.

The annual required contribution for the fiscal year ending June 30, 2012 is $34.4 million with $22.4 million being contributed by state agencies that are funded by federal or dedicated funds for their portion of funding and the remainder coming from the accumulated General Fund balance held by the trust. The retiree contribution includes the bonus contributions of $1,000 per year of service to employees retiring after July 1, 2007 who also met certain minimum age and service requirements.

### G. Pollution Remediation Obligations

Nature and source of pollution remediation obligations: Four state agencies have identified themselves as responsible or potentially responsible parties to remediate fifty-five pollution sites pursuant to the State's implementation of GASB 49, Accounting and Financial Reporting for Pollution Remediation Obligations effective July 1, 2008. Obligating events for the cleanup of these sites include the federal Superfund law, being named by a regulator to remediate hazardous wastes and contamination, violation of the Resource Recovery and Conservation Act, being named in a lawsuit, and voluntarily assuming responsibility because of imminent threats to human health and the environment.

Amount of the estimated liability, methods and assumptions used for the estimate, and the potential for changes: The State's total estimated liability is $46.0 million of which $7.3 million is estimated to be payable within one year and $38.7 million estimated to be payable in more than one year. State agencies calculated their estimated liabilities using various approaches including existing agreements, contractor bids/surveys, records of decisions from regulators, matching requirements under the Superfund law, previous actual costs to cleanup similar sites, investigation activities, well known and recognized estimation methods, and through the sampling and knowing the size and volume of existing contamination at a site. Superfund site estimated liabilities also applied a rolling thirty year liability as this was the number of years determined to be reasonably estimable. The estimated liabilities of state agencies are subject to annual review and adjustment for changes in agreements, laws, regulations, court decisions, price increases or decreases for goods and services used in cleanup, and other relevant changes that come to light.

Estimated recoveries reducing the liability: The estimated recoveries total $18.2 million. Of this total, $0.3 million is unrealizable or has not yet been realized and has been applied to reduce the State's total estimated liability. Estimated recoveries include the proceeds from the sale of stock from a bankruptcy court settlement, coverage of allowable costs by the State's Excess Liability Trust Fund (ELTF), and credits received for work performed on Superfund sites. The ELTF state law states that if insufficient funds exist to pay claims neither the State nor the Fund are liable for unpaid claims. The State recognized $3.8 million of program revenue for four sites whose realized recoveries exceeded the pollution remediation liability.