



FINANCIAL STATEMENTS, MANAGEMENT'S  
DISCUSSION AND ANALYSIS, AND  
OTHER REPORT

State Board of Administration of Florida  
Florida Retirement System (FRS) Investment Plan Trust Fund  
June 30, 2012 and 2011  
With Report of Independent Certified Public Accountants

Ernst & Young LLP

 **ERNST & YOUNG**

State Board of Administration  
FRS Investment Plan Trust Fund

Financial Statements, Management’s Discussion and Analysis  
and Other Reports

June 30, 2012 and 2011

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## Report of Independent Certified Public Accountants

The Board of Trustees  
State Board of Administration of Florida

We have audited the accompanying statements of net assets of the Florida Retirement System Investment Plan Trust Fund (the Trust), administered by the State Board of Administration of Florida (SBA) as trustee as of and for the year ended June 30, 2012 and 2011, and the related statements of changes in net assets for the years then ended. These financial statements are the responsibility of the SBA's management. Our responsibility is to express an opinion on these financial statements based on our audits.

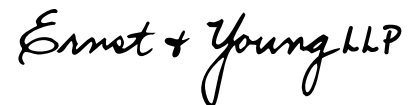
We conducted our audits in accordance with auditing standards generally accepted in the United States and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. We were not engaged to perform an audit of the Trust's internal control over financial reporting. Our audit included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Trust's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

As discussed in Note 1, the financial statements present only the Trust and do not purport to, and do not, present fairly the financial position of the State of Florida, the Florida Retirement System Investment Plan or the SBA as of June 30, 2012 and 2011, and the changes in its financial position for the years then ended, in conformity with accounting principles generally accepted in the United States.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the Trust administered by the State Board of Administration of Florida as of June 30, 2012 and 2011 and the changes in its financial position for the years then ended, in conformity with US generally accepted accounting principles.

In accordance with *Government Auditing Standards*, we have also issued our report dated November 5, 2012, on our consideration of the Trust's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

Accounting principles generally accepted in the United States require that the Management's Discussion and Analysis, on pages 3 through 12, be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

A handwritten signature in black ink that reads 'Ernst & Young LLP'.

November 5, 2012

State Board of Administration  
FRS Investment Plan Trust Fund

Management's Discussion and Analysis  
June 30, 2012 and 2011

**Introduction**

This section of the financial statements of the Florida Retirement System (FRS) Investment Plan Trust Fund (the Trust) presents management's discussion and analysis of the Trust's financial position for the fiscal years ended June 30, 2012 and 2011. Please read it in conjunction with the basic financial statements and the accompanying notes, which follow this section.

As further described in Note 1 to the financial statements, the FRS Investment Plan (the Plan) is a defined contribution plan for eligible members of the Florida Retirement System who elect to participate in the Plan in lieu of participation in the FRS Pension Plan, a defined benefit plan.

The Plan is administered by the State Board of Administration of Florida (the SBA), and the SBA has defined the roles and responsibilities of affected employers, the Division of Retirement within the Department of Management Services (DMS) and other service providers. The Florida Legislature is responsible for setting contribution rates and providing statutory authority to the SBA for the administration of the Plan.

Contributions to the Plan are collected by DMS and transmitted to the SBA, which deposits them in the Trust. Aon Hewitt, the Plan Administrator contracted by the SBA, is responsible for the placement of member-directed trades among investment options offered by the Plan and maintaining records of individual member accounts. Members choose from a diverse offering of low-cost institutional and mutual fund investment options selected by the SBA. Aon Hewitt records in each member's account balance all relevant contributions, withdrawals, fees, and the investment performance of the funds selected by the member. Benefits members receive from the Plan vary based on the members' individual account balances.

**Financial Statements**

The financial reporting entity represented in the basic financial statements and accompanying notes is the Trust, which consists of the assets held in trust by the SBA for the payment of retirement benefits and reasonable administrative expenses of the Plan.

The Trust's basic financial statements include two-year comparative statements of net assets and statements of changes in net assets. The statements of net assets provide information on the financial position of the Trust at the end of each fiscal year. The statements of changes in net assets present the results of investing activities during the fiscal years. The notes to the financial

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Management's Discussion and Analysis (continued)  
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statements offer additional discussion that is essential to the full understanding of the data presented in the financial statements. The notes provide more detail about accounting policies, significant account balances and activities, material risks, obligations, contingencies and subsequent events, if any.

**Statements of Net Assets**

The statements of net assets present the assets, liabilities and net assets (assets minus liabilities) of the Trust as of the end of the fiscal year and are point-in-time financial statements.

The statements of net assets were comprised of the following major components as of the end of each of the last three fiscal years. The primary assets in the Trust are the members' investment accounts.

**Trust Net Assets (*in millions*)**

	<b>June 30</b>		
	<b>2012</b>	<b>2011</b>	<b>2010</b>
Assets:			
Investments	\$ 7,137	\$ 6,737	\$ 5,050
Receivables	54	53	42
Total assets	\$ 7,191	\$ 6,790	\$ 5,092
Liabilities:			
Accounts payable and accrued liabilities	1	3	1
Net assets	\$ 7,190	\$ 6,787	\$ 5,091

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**Statements of Changes in Net Assets**

Changes in net assets from year to year are presented in the statements of changes in net assets. The purpose of these statements is to present the net investment income earned by the Trust as well as the employee and employer contributions and withdrawals for members and/or beneficiaries. A summary of the changes in net assets during the past three fiscal years follows.

**Changes in Trust Net Assets (*in millions*)**

	<b>June 30</b>		
	<b>2012</b>	<b>2011</b>	<b>2010</b>
Additions			
Net investment income	\$ 70	\$ 932	\$ 447
Contributions:			
Transfers from DMS-Employer and Employee Contributions <sup>1</sup>	467	456	425
Member-directed transfers from FRS Pension Plan	967	1,183	675
Member-directed rollover deposits	46	42	34
Subtotal Contributions	<u>1,480</u>	<u>1,681</u>	<u>1,134</u>
Total additions	\$ 1,550	\$ 2,613	\$ 1,581
Deductions			
Benefit payments	\$ 1,104	\$ 874	\$ 576
Member-directed transfers to FRS Pension Plan	34	34	21
Administrative expenses	10	9	9
Total deductions	<u>1,148</u>	<u>917</u>	<u>606</u>
Net increase in net assets	<u>\$ 402</u>	<u>\$ 1,696</u>	<u>\$ 975</u>

<sup>1</sup> Employee Contributions to the Plan were mandated July 1, 2011.

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Management's Discussion and Analysis (continued)  
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**Analysis**

The Trust's net assets increased by \$402 million (6%) and \$1.7 billion (33%) during fiscal years 2012 and 2011, respectively. The lower growth rate in 2012 was due primarily to lower investment income, a 26% reduction in employer contributions to the Plan and a 26% increase in benefit payments. By the end of fiscal year 2012, the equity market returns were well below the 2011 levels, thereby reducing net investment income. The Florida Legislature reduced employer contribution rates for all Plan members beginning in fiscal year 2012 (see the employer contribution rate table further down in this analysis). Finally, with a growing number of retirees and recent economic conditions, the total benefit payments have continued to climb.

Member-directed transfers into the Trust from the FRS Pension Plan spiked in fiscal year 2011, in part, due to members' reaction to the 2011 proposed and actual legislative changes to the FRS Pension Plan and the Deferred Retirement Option Program (DROP). Fiscal year 2011 saw an increase of \$508 million (75%) in these transfers from the previous fiscal year. By the end of fiscal year 2012, member-directed transfers from the FRS Pension Plan decreased by \$216 million (18%) from the fiscal year 2011 level.

Additional Plan highlights and trends follow.



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The following table reflects employer and employee participation in the Plan as of the end of each of the past three fiscal years.

**Plan Participation**

	As of June 30		
	2012	2011	2010
Participating employers	<b>992</b>	980	976
New employees making initial plan choice	<b>37,977</b>	40,051	38,730
Number of new employees joining FRS Investment Plan	<b>10,935</b>	9,959	9,071
% Electing FRS Investment Plan	<b>29%</b>	25%	23%
Employees' second elections <sup>1</sup>	<b>6,443</b>	8,312	4,414
Investment Plan retirees	<b>58,700</b>	47,737	38,542

<sup>1</sup> State of Florida Employees are granted a one-time option to transfer from one retirement plan (Pension or Investment) to the other during their tenure.

While the overall number of new employees eligible to make an initial retirement plan choice has varied over the last three fiscal years, the percentage of employees choosing the Plan has steadily increased. In fiscal year 2012, approximately 29% of the newly hired employees elected to enroll in the Investment Plan compared with 25% in fiscal year 2011 and 23% in fiscal year 2010.

The number of Plan retirees has increased steadily from fiscal year 2010 to 2012. The number of Plan retirees grew by 23% in fiscal year 2012 and 24% in fiscal year 2011.

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Management's Discussion and Analysis (continued)  
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The table below breaks out the active Plan membership by class at the end of each of the past three fiscal years. Active Plan members are those employees currently receiving contributions into their retirement account.

**Active Plan Membership by Class**

	<b>Regular</b>	<b>Senior Management</b>	<b>Special Risk Admin</b>	<b>Elected Officers</b>	<b>Special Risk</b>	<b>Other</b>	<b>Total</b>
2010	84,846	1,996	18	431	10,739	3,478	101,508
2011	90,353	2,131	21	466	12,279	932	106,182
<b>2012</b>	<b>92,529</b>	<b>2,183</b>	<b>16</b>	<b>484</b>	<b>12,500</b>	<b>1,293</b>	<b>109,005</b>

Over the last three fiscal years, active Plan membership has continued to increase in almost every membership class.

The following table shows the breakdown of the number of Plan members' accounts and any related benefit payments at the end of each of the past three fiscal years.

**Plan Accounts and Benefit Payments**

	<b>As of June 30</b>		
	<b>2012</b>	<b>2011</b>	<b>2010</b>
Number of member accounts:			
Active	<b>109,005</b>	106,182	101,508
Inactive <sup>1</sup>	<b>35,294</b>	30,479	26,432
Total	<b>144,299</b>	136,661	127,940
Member requests for benefit payment	<b>38,015</b>	29,054	21,793
Benefit payments ( <i>in millions</i> )			
Rollovers	<b>\$ 656</b>	\$ 528	\$ 324
All other	<b>448</b>	346	252
Total	<b>\$ 1,104</b>	\$ 874	\$ 576

<sup>1</sup> Inactive accounts are held on behalf of members that are not receiving contributions at this time. This often occurs when a member leaves State employment but retains a Plan balance pending payment of benefits.

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As the number of employees electing to participate in the Plan continues to increase, so does the number of member accounts. The number of accounts has increased by 6% to 7% each fiscal year from 2010 through 2012.

Benefit payments reflect withdrawals from the Trust in the form of lump sum distributions, partial distributions, rollovers to other qualified retirement plans, and periodic payments to members. The total number of members requesting benefit payments has increased by 31% and 33% for fiscal years 2012 and 2011, respectively. The total amount of benefits disbursed to plan members has increased significantly over the last couple of fiscal years. Total benefits disbursed increased by \$230 million (26%) in fiscal year 2012 and \$298 million (52%) in 2011.

Employer contribution rates, which are established by the Legislature and reflected in Section 121.72(4), Florida Statutes, vary by membership class. In 2011, legislation was passed that mandated employee contributions to the Plan, equal to 3% of gross compensation, and employer contribution rates were reduced effective July 1, 2011.

The contribution rates presented in the following table were in effect for fiscal years 2010, 2011 and 2012.

**FRS Investment Plan Contribution Rates**

<b>Membership Class</b>	<b>FY 2011-12</b>		<b>FY 2010-11</b>	<b>FY2009-10</b>
	<b>Employee Rate</b>	<b>Employer Rate</b>	<b>Employer Rate</b>	<b>Employer Rate</b>
Regular	3.00%	6.00%	9.00%	9.00%
Special risk	3.00	17.00	20.00	20.00
Special risk administrative support	3.00	8.35	11.35	11.35
Legislators	3.00	10.40	13.40	13.40
Governor, Lt. Governor, cabinet officers	3.00	10.40	13.40	13.40
State Attorney, public defenders	3.00	10.40	13.40	13.40
Justices, judges	3.00	15.90	18.90	18.90
County elected officers	3.00	13.20	16.20	16.20
Senior management service	3.00	7.95	10.95	10.95

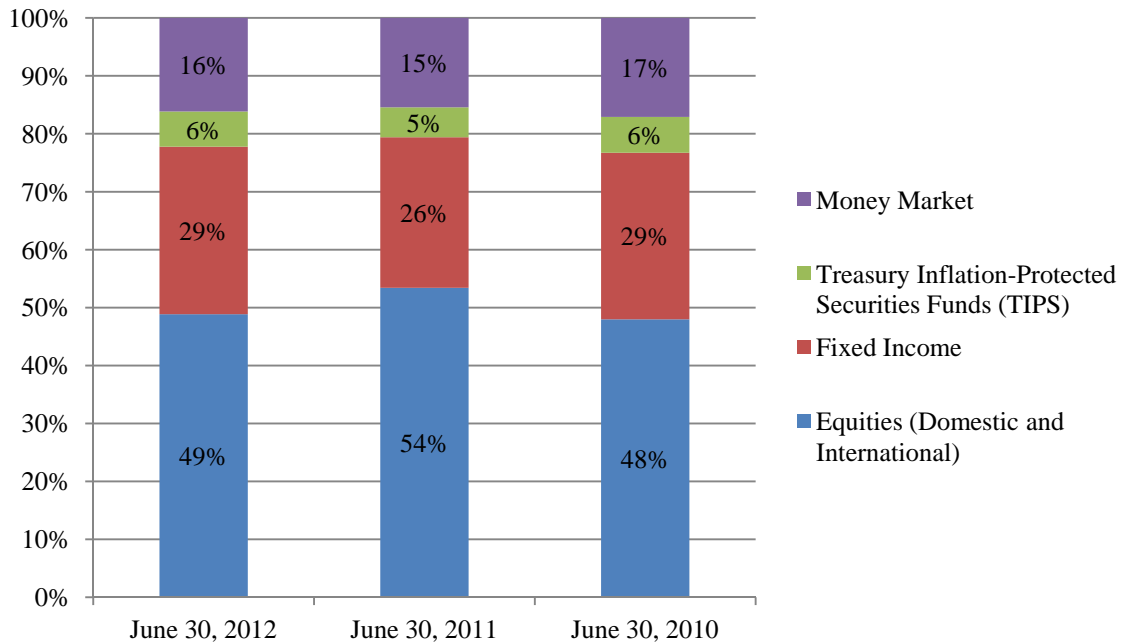
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**Asset Allocation**

The following chart indicates the Trust's asset allocation at the end of each of the past three fiscal years. The asset allocation of the Trust is a function of the members' investment decisions across the various investment options offered. Reflecting the FY 2011 growth and FY 2012 sell-off in international equity markets, the overall allocation as of June 2012 was similar to the June 2010 composition. Note 3 to the financial statements describes the Plan's Investment Policy Statement and oversight of the Trust's investments.

**Asset Allocation**  
*(By Percentage of Invested Assets)*



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Management's Discussion and Analysis (continued)  
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**Investment Performance**

The Trust's performance is a function of the members' investment decisions across the various investment options offered by the Plan. The SBA does not influence these decisions; however, investment performance affects the Trust's net assets and is included below for analysis purposes.

For the fiscal year 2012, improved fixed income markets helped to overcome sluggish equity markets to keep the Trust's overall total return in 2012 a positive 1.1%. The total return for fiscal year 2011 was 18.1%, a record high since the Trust's inception in fiscal year 2002-03. Investment income was driven by the positive performance of fixed income and TIPS funds offsetting the losses in international equity funds.

The table below reflects the investment returns by broad asset class types. The Balanced Funds invest in various FRS investment funds in different proportions within the other asset classes shown in the table.

**Investment Returns by Asset Class Type<sup>1</sup>**

	<u>2012</u>	<u>2011</u>	<u>2010</u>
Balanced Funds	<b>1.5%</b>	15.6%	10.5%
Money Market	<b>0.3</b>	0.3	0.2
TIPS	<b>11.8</b>	7.8	9.6
Fixed Income	<b>7.1</b>	5.0	12.3
Domestic Equity	<b>1.8</b>	36.1	18.6
Foreign Equity	<b>(11.8)</b>	31.2	8.4
Total Plan Return	<b>1.1%</b>	18.1%	11.1%
Total Plan Aggregate Benchmark	<b>1.2%</b>	17.2%	10.3%
Over/(Under) Benchmark	<b>(.1%)</b>	0.9%	0.8%

<sup>1</sup> The above investment performance information as of June 30, 2012 is the official investment return data as of that date supplied by the SBA's master custodian and performance measurement service provider, BNY Mellon Performance Reporting and Analytics Services.

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The Trust has lagged behind its aggregate benchmark over the trailing one-year period, but outperformed over the trailing three- and five-year periods. The Trust's overall performance compared with its benchmark reflects the relative performance for the underlying fund options in which members are investing. More detailed information and analysis of the Trust's performance can be obtained from the SBA's Annual Investment Report, which can be found at [www.sbafla.com](http://www.sbafla.com).

**Contacting the Trust's Financial Management**

This financial report is designed to provide citizens, taxpayers, Plan members, and other interested parties with an overview of the Trust's finances and the prudent exercise of the SBA's oversight. If you have any questions regarding this report or need additional information, please contact the Senior DC Program Officer, State Board of Administration of Florida, P.O. Box 13300, Tallahassee, FL 32317-3300.

State Board of Administration  
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Statements of Net Assets

	<b>June 30</b>	
	<b>2012</b>	<b>2011</b>
	<i>(in thousands)</i>	
<b>Assets</b>		
Investments:		
Money market funds	\$ <b>1,153,469</b>	\$ 1,041,048
Commingled funds, at fair value:		
Treasury inflation-protected securities funds	<b>432,888</b>	348,750
Domestic fixed income	<b>2,063,986</b>	1,754,489
Domestic equity	<b>2,469,281</b>	2,379,757
International equity	<b>1,017,835</b>	1,212,870
Total investments, at fair value	<b>7,137,459</b>	6,736,914
Receivables:		
Accounts receivable	<b>361</b>	378
Transfers due from DMS	<b>52,031</b>	51,851
Interest and dividends	<b>1,085</b>	904
Total receivables	<b>53,477</b>	53,133
Total assets	<b>7,190,936</b>	6,790,047
<b>Liabilities</b>		
Accounts payable and accrued liabilities	<b>1,359</b>	2,549
Net assets held in trust	<b>\$ 7,189,577</b>	\$ 6,787,498

*See accompanying notes.*

State Board of Administration  
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Statements of Changes in Net Assets

	<b>2012</b>	<b>2011</b>
	<i>(in thousands)</i>	
<b>Additions</b>		
Investment income:		
Dividend income	\$ 51,657	\$ 27,719
Interest and other investment income	17	87
Net increase in fair value of investments	<b>20,563</b>	906,142
	<b>72,237</b>	933,948
Investment expenses:		
Bank fees	(621)	(628)
Investment management fees	(1,366)	(1,654)
Total investment expense	<b>(1,987)</b>	(2,282)
Net investment income	<b>70,250</b>	931,666
Contributions:		
Transfers from DMS-employer and employee contributions	<b>466,735</b>	456,393
Member-directed transfers from FRS Pension Plan	<b>967,164</b>	1,183,161
Member-directed rollover deposits	<b>45,869</b>	42,102
Total contributions	<b>1,479,768</b>	1,681,656
Total additions	<b>1,550,018</b>	2,613,322
<b>Deductions</b>		
Benefit payments to members	<b>1,104,216</b>	873,862
Member-directed transfers to FRS Pension Plan	<b>33,681</b>	33,494
Administrative expenses	<b>10,042</b>	9,487
Total deductions	<b>1,147,939</b>	916,843
Net increase in net assets	<b>402,079</b>	1,696,479
Net assets held in trust:		
Beginning of year	<b>6,787,498</b>	5,091,019
End of year	<b>\$ 7,189,577</b>	\$ 6,787,498

*See accompanying notes.*



State Board of Administration  
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Notes to Financial Statements  
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**1. Financial Reporting Entity**

The FRS Investment Plan (the Plan), a defined contribution pension plan, was established pursuant to Section 121.4501, Florida Statutes, to provide for retirement benefits for eligible employees of the State and all participating county, district school board, community college and university employees who elect to participate in the Plan as an alternative to the FRS Pension Plan or other optional retirement plans. Under the Plan, employers and employees make contributions to an account set up in the member's name and the member directs the investments in the account, choosing from twenty diverse investment options selected and monitored by the State Board of Administration of Florida (SBA). The Plan was first offered to public sector employees in fiscal year 2003 and was modeled after private sector 401(k) plans. The Plan's and SBA's financial activities are reported in the Comprehensive Annual Financial Report (CAFR) of the State of Florida. The SBA is governed by a Board of Trustees, comprised of the Governor, the Attorney General, and the Chief Financial Officer of the State of Florida.

The FRS Investment Plan Trust Fund (the Trust) was established pursuant to Section 121.4502, Florida Statutes, to hold the assets of the Plan in trust for the exclusive benefit of the Plan's members and beneficiaries and for the payment of reasonable administrative expenses of the Plan.

The Trust is not a separate legal entity within the State of Florida. These financial statements and notes thereto include only the net assets and changes in net assets of the Trust and do not purport to, and do not, present fairly the financial position of the State of Florida, the SBA or the Plan as of June 30, 2012 and 2011, and the changes in its financial position for the years then ended, in conformity with accounting principles generally accepted in the United States (GAAP).

**2. Summary of Significant Accounting Policies**

***Basis of Presentation*** – The financial statements of the Trust have been prepared in accordance with accounting principles generally accepted in the United States (GAAP) as applicable to governmental units. The Governmental Accounting Standards Board (GASB) is the accepted standard-setting body for establishing governmental accounting and reporting principles. The Trust is accounted for as an investment trust fund pursuant to Governmental Accounting Standards Board Statement No. 31, *Accounting and Financial Reporting for Certain Investments and for External Investment Pools* (GASB 31), and GASB Statement No. 34, *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments* (GASB 34). As such, the Trust's financial statements present Statements of Net Assets and Statements of Changes in Net Assets.

State Board of Administration  
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Notes to Financial Statements (continued)  
June 30, 2012 and 2011

**2. Summary of Significant Accounting Policies (continued)**

***Measurement Focus and Basis of Accounting*** – The financial statements are prepared using the flow of economic resources measurement focus and the accrual basis of accounting. Under the accrual basis of accounting, revenues (additions) are recognized when earned and expenses (deductions) are recognized when incurred, regardless of when the related cash flow takes place.

***Investment Valuation*** – Investments are reported at fair value in accordance with GASB 31, as follows:

- Money market funds – cost, which approximates fair value.
- Other investments – the most recent market prices at the close of the markets on June 30, or the most recent market close of each fiscal year.

***Income Recognition*** – Investment transactions are accounted for on a trade – or investment-date basis. Gains and losses from investment transactions are determined by the average-cost method. Interest and dividend income is recorded on the accrual basis, with dividends accruing on the ex-dividend date.

***Administrative Expenses*** – Pursuant to Section 121.4502, Florida Statutes, reasonable administrative expenses are paid from the Trust’s assets.

***Use of Estimates*** – The preparation of financial statements in accordance with GAAP requires management to make estimates and assumptions that affect reported amounts of assets and liabilities at the date of the financial statements and reported amounts of revenues (additions) and expenses (deductions) during the reporting period. Actual results could differ from those estimates.

***Reclassifications*** – Certain prior year amounts have been reclassified to conform to the current year presentation.

***New Accounting Standards Adopted*** – No new GASB pronouncements enacted during the fiscal year were determined to have a material effective on financial reporting.

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Notes to Financial Statements (continued)  
June 30, 2012 and 2011

**3. Deposits and Investments**

*Deposits* – At June 30, 2012 and 2011, the Trust did not have any deposits on hand. All contributions and transfers are invested immediately according to member directions.

*Investments* – The Plan has an Investment Policy Statement (IPS) that includes, among other items, the investment objectives of the Plan, manager selection and monitoring guidelines, and performance measurement criteria. The IPS is revisited periodically to ensure the structure and guidelines are appropriate, taking into consideration the Plan’s goals and objectives.

The primary investment objectives of the Plan are to: (1) offer a diversified mix of low-cost investment options that span the risk-return spectrum and give members the opportunity to accumulate retirement benefits; (2) offer investment options that avoid excessive risk, have a prudent degree of diversification relative to broad market indices and provide a long-term rate of return, net of all expenses and fees that seek to achieve or exceed the returns on comparable market benchmark indices; and (3) offer members meaningful, independent control over the assets in their account.

The SBA’s Executive Director & Chief Investment Officer is responsible for selecting, evaluating, and monitoring performance of the investment options, with a focus on maximizing return within appropriate risk constraints outlined in the Plan’s IPS. The Trust currently offers twenty low-cost institutional comingled trusts and mutual fund investment options investing in cash, bonds, and stocks. Three risk-targeted balanced funds are available, consisting of mixtures of various assets classes. At fiscal 2012 year-end, more than 78% of the Plan’s members had allocated at least some of their assets to one or more of the three available balanced funds. Approximately 43% of total Trust assets were in the balanced funds. For financial statement purposes, all assets are presented in five asset classes.

The SBA follows the Florida Statutes’ fiduciary standards of care in managing the Plan’s investment options. The SBA Trustees appoint nine members to serve on the Investment Advisory Council (IAC), which provides independent oversight of the Trust’s general objectives, policies, and strategies.

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Notes to Financial Statements (continued)  
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**3. Deposits and Investments (continued)**

The SBA staff, consultants and Trustees review the Trust's performance quarterly. During fiscal year 2011, the IAC reviewed performance every six months; beginning in fiscal year 2012, it reviewed performance quarterly. The long-term performance of each actively managed investment option is expected to exceed the returns on its performance benchmark, net of all fees and charges, while avoiding large year-to-year deviations from the returns of the performance benchmark. The long-term performance of each passively managed investment option is expected to closely approximate returns of the performance benchmark, net of all fees and charges. At the total Trust level, performance is evaluated by asset class and is measured on an absolute basis and relative to appropriate market benchmarks for each investment option. Performance data is aggregated for the total Trust and for each product type or asset class, using member allocations as the weighting factors.

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Notes to Financial Statements (continued)  
June 30, 2012 and 2011

**3. Deposits and Investments (continued)**

The Trust's investments consist of the following as of June 30, 2012 and 2011:

**Investment Portfolio Characteristics\***

	2012		2011	
	Fair Value	% of Portfolio	Fair Value	% of Portfolio
	<i>(in thousands)</i>			
Money Market Funds:				
EB Temporary Investment FD II	\$ 1,992	0.0%	\$ 1,725	0.0%
FRS Select Yield Plus MM Active Fund	1,151,477	16.1%	1,039,323	15.5%
Total Money Market Funds	1,153,469	16.1%	1,041,048	15.5%
Treasury Inflation-Protected Securities (TIPS) Funds:				
FRS Select US TIPS Index Fund	432,888	6.1%	348,750	5.2%
Total Treasury Inflation-Protected Securities Funds	432,888	6.1%	348,750	5.2%
Domestic Fixed Income Funds:				
PIMCO Total Return Fund	310,775	4.4%	284,685	4.2%
Pyramis Intermediate Duration Pool Fund	488,727	6.8%	354,385	5.3%
FRS Select US Bond Enhanced Index Fund	1,119,200	15.7%	980,173	14.5%
FRS Select High Yield Fund	145,284	2.0%	135,246	2.0%
Total Fixed Income Funds	2,063,986	28.9%	1,754,489	26.0%
Domestic Equity Funds:				
American Beacon Small-Cap Value Fund	121,082	1.8%	137,920	2.0%
Fidelity Growth Company Fund	317,388	4.4%	310,485	4.6%
Fidelity Low Priced Stock Fund**	23,080	0.3%	27,072	0.4%
Pioneer Fund	130,356	1.8%	146,285	2.2%
T Rowe Price Small-Cap Stock Fund	235,164	3.3%	251,098	3.7%
Prudential Mid-Cap Quantitative Core Equity Fund	270,197	3.8%	291,537	4.3%
FRS Select US Large Growth Stock Active Fund	95,009	1.3%	78,884	1.2%
FRS Select US Stock Market Index Fund	1,035,920	14.5%	901,484	13.4%
FRS Select US Large Value Stock Active Fund	241,085	3.4%	234,992	3.5%
Total Domestic Equity Funds	2,469,281	34.6%	2,379,757	35.3%
International Equity Funds:				
American Funds Euro-Pacific Growth Fund	154,766	2.2%	195,219	2.9%
American Funds New Perspective Fund	180,167	2.5%	201,572	3.0%
FRS Select Foreign Stock Index Fund	682,902	9.6%	816,079	12.1%
Total International Equity Funds	1,017,835	14.3%	1,212,870	18.0%
Total Investments	\$ 7,137,459	100.0%	\$ 6,736,914	100.0%

\* The FRS Balanced Funds invest in various FRS investment funds in different proportions and are accounted for in the individual investment options in this table.

\*\* Fund closed to new money effective August 1, 2004.

State Board of Administration  
FRS Investment Plan Trust Fund

Notes to Financial Statements (continued)  
June 30, 2012 and 2011

**3. Deposits and Investments (continued)**

**Risks** – The Trust invests in a broad range of financial investments. Financial investments, in general, are exposed to various risks, such as interest rate, credit, and overall market volatility. Due to the level of risk associated with certain financial investments, it is reasonably possible that changes in the values of financial investments will occur in the near term and that such changes could materially affect the amounts reported in the financial statements.

The Plan's Investment Policy Statement provides a statement of objectives for the Trust, general guidelines for each asset class and the balanced funds, and educational services to help members manage the level of risk associated with the choices they make with their individual investment accounts.

As required by GASB Statement 40, *Deposit and Investment Risk Disclosures* (GASB 40), the Trust's exposure to the specific risks of credit risk, custodial credit risk, concentration of credit risk, interest rate risk and foreign currency risk follows. Each of these risks is managed by the investment advisors to the mutual funds and trusts subject to guidelines set forth in prospectuses, Statements of Additional Information and other governing documents of each fund's investment manager.

**Credit Risk and Concentration of Credit Risk of Debt Securities** – Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. Concentration of credit risk is the risk of loss attributed to the magnitude of an investment in a single issuer.

The mutual funds and commingled trust funds in the Trust are institutional funds and, as such, are not rated by the nationally recognized statistical rating agencies such as Standard & Poor's Corporation, Moody's Investors Service, Inc., or Fitch Ratings.

**Custodial Credit Risk** – Custodial credit risk for investments is the risk that, in the event of the failure of the counterparty, the Trust will not be able to recover the value of its investments or collateral securities that are in possession of an outside party other than units or shares of the commingled trusts or mutual funds that are held at the SBA's custodian bank, BNY Mellon. The SBA's negotiated custody contract requires that deposits and investments be held in accounts in the SBA's name, separate and apart from the assets of the custodian bank. As of June 30, 2012 and 2011, the Trust had no securities in the possession of an outside party.

**Interest Rate Risk** – Interest rate risk is the risk that changes in interest rate will adversely affect the fair value of the Trust's investments.

State Board of Administration  
FRS Investment Plan Trust Fund

Notes to Financial Statements (continued)  
June 30, 2012 and 2011

**3. Deposits and Investments (continued)**

The Plan's Investment Policy Statement provides that the money market funds will offer high-quality, liquid, short-term instruments to control interest rate sensitivity. The fixed income funds may be passively or actively managed and will primarily invest in securities in the benchmark. In both cases, the funds' sensitivity to interest rate changes generally will closely approximate that of the performance benchmark.

Presented in the following tables is the effective weighted duration of the money market and fixed income investments as a measure of interest rate risk for the Trust as of June 30, 2012 and 2011.

<b>Investment Type</b>	<b>Fair Value</b> <i>(in thousands)</i>	<b>Effective weighted duration</b> <i>(in years)</i>
As of June 30, 2012		
Money Market Funds	\$ 1,153,469	0.110
Fixed Income and TIPS	2,496,874	4.934
Total Fixed Income Investments	<u>\$ 3,650,343</u>	
As of June 30, 2011		
Money Market Funds	\$ 1,041,048	0.050
Fixed Income and TIPS	2,103,239	4.867
Total Fixed Income Investments	<u>\$ 3,144,287</u>	

**Foreign Currency Risk** – Foreign currency risk is the risk that changes in exchange rates between the U.S. dollar and foreign currencies could adversely affect an investment's fair value. The Trust's investments in international equity funds (which are commingled with other investors) are reported in U.S. dollars by the investment fund managers. The underlying investments in these (commingled) funds may be exposed to foreign currency risk in various currencies. The fair value of the international equity funds as of June 30, 2012 and 2011 was \$1.02 billion and \$1.21 billion, respectively.

State Board of Administration  
FRS Investment Plan Trust Fund

Notes to Financial Statements (continued)  
June 30, 2012 and 2011

**4. Related-Party Transactions**

The Trust considers the State of Florida and its Department of Management Services (DMS), Division of Retirement, and the Florida Retirement System Trust Fund (FRS Trust Fund) to be related parties for the purpose of the financial statements.

The DMS is responsible for the receipt of member demographic data and for collecting employer and employee contributions and remitting those contributions to the SBA for deposit into the Trust for the benefit of the Plan members. The FRS Trust Fund is the source of funding for transfers of a member's accumulated benefit obligation (ABO) when a member in the FRS Pension Plan elects to join the FRS Investment Plan. The FRS Trust Fund also is a recipient of certain transfers.

Significant transactions between the Trust and the DMS and the FRS Trust Fund in fiscal years 2012 and 2011 were as follows:

	<u>2012</u>	<u>2011</u>
	<i>(in thousands)</i>	
Transfers from DMS for:		
Employer and employee contributions*	\$ 466,735	\$ 456,393
Transfers from FRS Trust Fund (ABO) related to member-directed transfers	\$ 967,164	\$ 1,183,161
Transfers to FRS Trust Fund	\$ 33,681	\$ 33,494
Receivables from DMS	\$ 52,030	\$ 51,851

\*Employee contributions to the Plan were mandated effective July 1, 2011.

**5. Contingencies and Litigation**

During the ordinary course of its operations, the SBA on behalf of the Trust may be party to various claims, legal actions, and class action lawsuits. The SBA's General Counsel Office handles these matters either directly or with assistance of outside legal counsel. In the opinion of the SBA's management and legal counsel, these matters are not anticipated to have a material financial impact on the Trust.



State Board of Administration  
FRS Investment Plan Trust Fund

Notes to Financial Statements (continued)  
June 30, 2012 and 2011

**5. Contingencies and Litigation (continued)**

The Trustees of the SBA and the Secretary of the Department of Management Services have been served complaints challenging the constitutionality of Senate Bill 2100 (SB2100), codified as Chapter 2011-68, Laws of Florida, [the legislation mandating the deduction of 3% of employees' salaries for contribution into the Florida Retirement System (FRS)], which became effective July 1, 2011. On March 6, 2012, the trial court ruled the law unconstitutional as to its application to employees who were members of the FRS prior to July 1, 2011 and ordered return of the funds to employees (with interest). The Appellants appealed, and the case was certified to the Florida Supreme Court, which accepted the case. The Court heard oral argument on September 7, 2012. The SBA cannot speculate regarding whether the Florida Supreme Court will affirm the order of the trial court and whether such a conclusion will have a material financial impact on the Trust.

# Other Report

Report of Independent Certified Public Accountants on Internal Control  
Over Financial Reporting and on Compliance and Other Matters  
Based on an Audit of the Financial Statements Performed  
in Accordance With *Government Auditing Standards*

The Board of Trustees  
State Board of Administration of Florida

We have audited the financial statements of the Florida Retirement System Investment Trust Fund (the Trust) as of and for the year ended June 30, 2012, and have issued our report thereon dated November 5, 2012. We conducted our audit in accordance with auditing standards generally accepted in the United States and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

**Internal Control Over Financial Reporting**

Management of the Trust is responsible for establishing and maintaining effective internal control over financial reporting. In planning and performing our audit, we considered the Trust's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Trust's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Trust's internal control over financial reporting.

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

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be deficiencies, significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above.

## Compliance and Other Matters

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

This report is intended solely for the information and use of management, the Board of Trustees of the State Board of Administration of Florida, the State of Florida and others within the entity, and is not intended to be, and should not be used by anyone other than these specified parties.

*Ernst + Young LLP*

November 5, 2012

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