WASHINGTON STATE INVESTMENT BOARD

2012 THIRTY-FIRST ANNUAL REPORT

INTRODUCTION

LETTER OF TRANSMITTAL

June 30, 2012

Trying to predict when the financial markets will get back on track is a little like trying to predict when summer will arrive in the Pacific Northwest. One day it's sunny and warm and you think, "Finally, summer is here." Then the next day it's cool and overcast.

In the past two years we've seen brief periods of economic optimism, quickly followed by market instability and economic uncertainty. Desperate for signs of economic recovery, investors jump at a positive jobs report or consumer spending report. But all too often it is followed by a market downturn after the latest news of Greece's or Spain's financial woes.

In last year's Annual Report, I talked about the benefits of a more global portfolio and how the developing world economies were offsetting the sluggish U.S. economy's drag on the WSIB's returns. This year, however, the strength of the dollar helped the U.S. markets perform better than international markets as the ongoing European debt crisis and fears about the stability of the euro zone continues its grip on the global economy. With more than half of the WSIB's assets invested globally, the economic slowdown in Europe has a direct impact on our investments.

Not all bad news.

Despite the brutal market conditions, the WSIB's returns for fiscal year (FY) 2012 remained positive. Although a 1.4 percent annual return is not something we can brag about, we performed as well or better than most of our peers. Whatever credit the WSIB can take for achieving a positive return during these difficult times goes to its exceptionally talented staff and a strong and capable Board.

This report describes in detail all of our portfolios, performance, operations and finance. I am proud to note that even in these difficult times, the WSIB continues to not only meet but exceed the high standards our beneficiaries expect and deserve.

Sincerely,

Theresa Whitmarsh, Executive Director

MESSAGE FROM THE CHAIR

I am pleased to introduce the Washington State Investment Board's Annual Report for fiscal year ended June 30, 2012. Throughout the WSIB's 31 year history, the organization's excellent investment performance has dramatically contributed to the state's bottom line. We have helped keep taxpayer costs low by earning investment returns that fund 84 cents of every dollar paid to pension beneficiaries. Much to the WSIB's credit, Washington is recognized as having one of the best-funded pension programs in the nation.

In a time of persistent market uncertainty, geopolitical turmoil, and wide-reaching economic difficulties it is important to focus on the WSIB's overall success. Investment performance for the state's Commingled Trust Fund (CTF) for defined benefit pension systems ended FY 2012 with a small but positive 1.4 percent rate of return and a market value of $61.8 billion.

It was not our best year, nor was it our worst. But the average 8.4 percent rate of return for the CTF since its inception in 1992 illustrates that even with market downturns and instability, the WSIB's disciplined long-term investment horizon and highly diversified investment strategy has met and exceeded return expectations overall.

In an effort to further that success, the Board created an *ad hoc* Governance Committee during the past year to improve the WSIB's investment decision-making process, accountability, efficiency, transparency, and effectiveness as a fiduciary body. The goal is to implement "best practices" for monitoring and oversight of investment and organizational risks, and to improve the Board's ability to respond wisely and appropriately in the short and long term.

This year, the WSIB is beginning a year-long Board education and study project that could lead to different asset allocation targets for the CTF. The success of this important endeavor will ultimately be judged by the returns we deliver to our beneficiaries and stakeholders.

As a global investor with a long-term horizon, the WSIB makes investment decisions that have an enormous impact. Thousands of individuals depend upon strong returns from our investments for their retirements, education, and quality of life. I want to thank my fellow Board members and WSIB's excellent staff for their commitment to live up to the highest standards of integrity and professionalism. We are all proud to be part of an organization that, with total confidence and certainty, I believe will deliver the best long-term results for the members and beneficiaries of all the funds for which we manage and invest.

Treasurer James L. McIntire, Chair

BOARD MEMBERS AND COMMITTEES

The WSIB is an independent board of trustees whose fiduciary responsibility is to manage retirement and public fund investments with the highest standard of professional conduct. The Board's primary investment objective is to maximize returns at a prudent level of risk for the exclusive benefit of fund participants and beneficiaries. Individual Board members are appointed by the Chair to serve on any of the Board's four different committees to more efficiently analyze investment and governance issues. Committee recommendations are brought to the Board for consideration and a vote.

Administrative Committee

The Administrative Committee oversees organizational, personnel, budget, legal, and legislative issues, as well as strategic asset allocation.

Audit Committee

The Audit Committee assists the Board in financial oversight of the WSIB including risk management, compliance monitoring, internal and external audits, corporate governance, and proxy voting.

Private Markets Committee

The Private Markets Committee develops policy and structure for private market and real estate opportunities and reviews those investments for recommendations to the Board.

Public Markets Committee

The Public Markets Committee develops policy and structure for public market investments (fixed income, domestic equity, international equity) and reviews individual equity managers to recommend to the Board.

EXECUTIVE MANAGEMENT AND CONSULTANTS

Theresa J. Whitmarsh - Executive Director

Appointed in 2009

The WSIB's executive director is appointed by the Board to oversee the staff, develop and recommend agency and investment policies for Board adoption, and ensure adherence to state policies and laws.

Gary Bruebaker, CFA, CPA - Chief Investment Officer

Appointed in 2001

The Investment Division is comprised of investment professionals who manage investments in major asset classes including public equity, private equity, real estate, and fixed income. The division is also served by a senior investment officer who develops asset allocation and risk budgeting strategies. The division deploys both internal and external investment management strategies.

Victor Moore - Chief Operating Officer/Chief Financial Officer

Appointed in 2010

The Operations Division provides a number of services in support of the investment function, including investment accounting, trade settlement, cash management, private market funding, cash and stock distributions, foreign and domestic tax matters, and investment compliance monitoring. It provides agency-wide risk management, information systems management, human resources, and administrative services.

Liz Mendizabal - Institutional Relations Director

Appointed in 2003

Institutional Relations manages duties typically found in a public affairs and client services division of an investment management agency. These services include performance reporting, annual report preparation, corporate governance, legislative issues, media inquiries, and constituent communications.

Investment Accounting Data System

Financial Control Systems

Master Custodian Bank

JPMorgan Chase

Insurance Portfolio Consultant

Conning Asset Management

General & Specialty Consultants

Callan Associates
Cutter Associates, Inc.
Hewitt EnnisKnupp, Inc.
InvestTech Systems Consulting, Inc.
Jeffrey A. Parker & Associates, Inc.
Mercer Investment Consultants
Pension Consulting Alliance
Peterson Sullivan LLP
ORG Portfolio Management LLC
R.V. Kuhns & Associates Inc.

Legal Services

Allen Matkins Leck Gamble Mallory and Natsis
Barrack Rodos and Bacine
Barroway Topaz Kessler Meltzer and Check
Bernstein Litowitz Berger and Grossman
Cox, Castle, & Nicholson
Goodwin Procter
Kaplan, Fox, and Kilsheimer
K & L Gates
Keller Rohrback
Orrick Herrington and Sutcliffe
Paul Hastings
Proskauer Rose
Robbins Geller Rudman and Dowd
Song Mondress
Washington State Attorney General

Private Equity, Real Estate, and Tangibles Consultant

Hamilton Lane Advisors, LLC

COMMINGLED TRUST FUND PARTNERS AND FUND MANAGERS

Private Equity Partners

Accel Partners
Actis
Advent International
Affinity Equity Partners
Alta Communications
Ampersand Ventures
Apax Partners
Apex Investment Partners
Austin Ventures
Avenue Capital Group
Banc Funds
Battery Ventures
BC Partners
Blackstone Group
Boston Ventures
Bridgepoint Capital
Butler Capital Partners
Canaan Partners
Capital Resource Partners
CDH Investments
Charterhouse Capital Partners
Cinven Ltd.
Clayton Dubilier & Rice
Code, Hennessy & Simmons
Collison, Howe and Lennox
Cypress Group
Denham Capital
Doughty Hanson & Co.
Edgewater Funds
El Dorado Ventures
Elevation Partners
Endeavour Capital
Essex Woodlands
Evercore Capital Partners
Evergreen Pacific Partners
First Reserve Corp.
Fisher Lynch Capital
Flagship Ventures
Fortress Investment Group
FountainVest Partners
Francisco Partners
Frazier & Co.
Geocapital Partners
GGV Capital
Gilbert Global Equity Partners
Great Hill Partners
Green Mountain Partners
Gryphon Investors
GTCR
H.I.G. Ventures
HarbourVest Partners
Healthcare Ventures
Hellman & Friedman
Indigo Capital Partners
Insight Venture Partners
Intersouth Partners
InterWest Partners
JLL Partners
JMI Equity
Kohlberg Kravis Roberts & Co.
KSL Capital Partners
Leonard Green & Partners
M/C Venture Partners
Madison Dearborn Partners
MatlinPatterson Global Advisors
Menlo Ventures
Mobius Venture Capital
Morgan Stanley Venture Partners
New Enterprise Associates
Nordic Capital
Oak Investment Partners
Oaktree Capital Management
Olympus Partners
OVP Venture Partners
Palamon Capital Partners
Permira
Polaris Venture Partners
Prism Venture Partners
Providence Equity Partners
Richland Venture Partners
Silver Lake Partners
Southern Cross Group
Spark Management Partners
Spectrum Equity Investors
Sprout Group
Swander Pace Capital
TA Associates
Tailwind Capital Partners
Technology Crossover Ventures
Three Arch Partners
TPG Partners
Trident Capital Partners
Triton Partners
U.S. Venture Partners
Union Square Ventures
Unitas Capital
VantagePoint Venture Partners
Värde Partners
Vestar Capital Partners
Vision Capital
Vivo Ventures
Warburg Pincus
Welsh Carson Anderson & Stowe
Worldview Technology Partners

Real Estate Partners

Cherokee
Corporate Properties of the Americas
Emerging Markets Fund of Funds
Evergreen Investment Advisors
Fillmore Capital Partners
Global Co-Investment
Hometown America
Hudson Advisors
Morgan Stanley
Pacific Realty
PBSC Holdings
Principal Enterprise Capital
Hemisferio Sul
Terramar Retail Centers
Warburg Pincus
Washington Holdings

Tangibles Partners

Alinda
Campbell Group
Highstar
Sheridan

Public Equity Fund Managers

Aberdeen Asset Management PLC
Arrowstreet Capital, L.P.
BlackRock Institutional Trust Company
Capital Guardian Trust Co.
DE Shaw Investment Management
Grantham, Mayo, Van Otterloo & Co. LLC
JPMorgan Asset Management, Inc.
Lazard Asset Management LLC
Longview
Mondrian Investment Partners Ltd.
State Street Global Advisors
Wentworth, Hauser & Violich
William Blair & Co.

Overlay Manager

State Street Global Advisors

ENTERPRISE RISK MANAGEMENT

Framework

A cornerstone of a successful investment strategy is effective risk management. Enterprise Risk Management (ERM) is intended to cover risk management in the broadest possible terms, encompassing all forms of risk management activity across the entire agency. The WSIB's enterprise-wide approach to risk management includes involvement of the Board, executive management, audit, operational, legal, and investment staff. Risks are seen as opportunities for success as well as failure. The risks the WSIB face arise from both managing the assets and managing the organization. While the WSIB tries to anticipate every risk that it faces, unknown and unprecedented events will occur. The ERM program provides a framework to evaluate and manage uncertainty and rare events.

Managing the Assets

Risks arise from the deployment of the assets under our management in a fiercely competitive environment. Investments need to comply with the standards that a prudent investor would use to manage the assets of others, as well as with the laws of the state of Washington and Board investment policies. The WSIB has identified two primary risks for managing assets, fiduciary and investment risk.

- Fiduciary Risk – This is the risk of acting and making decisions for reasons other than the benefit of our constituents. The WSIB is a fiduciary whose mission is to manage investments for retirement and public trust funds "with the highest standard of professional conduct for the exclusive benefit of fund beneficiaries." To manage this risk, the WSIB has an independent Board, retains the services of legal fiduciary counsel, and complies with state ethics laws. Our code of conduct and conflict of interest policies, established for both the Board and staff, ensures that our values and expectations are understood and integrated throughout the Board and agency at all times. The Board has established investment policies and procedures designed exclusively to maximize return at a prudent level of risk.
- Investment Risk – Investment risks encompass all potential risks resulting from deployment of our assets into various investment strategies. Investment risks include volatility risk, interest rate risk, security pricing risk, liquidity risk, and currency risk, and may stem from changes in political, economic, demographic and technological factors. The WSIB seeks to manage the overall level of investment risk and uncertainty by broadly diversifying across asset classes, investment managers, sectors, strategies, and geographies. The WSIB seeks to evaluate these risks both in normal and worst case scenario environments. Investment risk can also result from not responding as markets change or failing to recognize the emergence of new markets. It can also result from deviating from long term investment strategy during short term market downturns. By managing the agency's strategic and operational risks, and also by fostering a strong ERM program that enables proactive decision making, the WSIB aims to make informed choices about the investment risk it faces

Managing the Organization

These risks stem from building and maintaining an organization that is best suited to managing this investment effort. Our organization must operate within a governmental framework while implementing investment management strategies that are more closely aligned with private investment entities. WSIB has identified three risks under this theme, strategic risk, governmental environment risk, and operational risk.

- Strategic Risk – This is the risk of not being prepared to make the decisions necessary for meeting the needs of our constituents. To manage this risk, we strive to have effective Board governance, the appropriate organizational structure for our mission, capable leadership, and an established strategic planning process. Our organizational structure includes an internal audit department, an enterprise-wide risk management team, and a business coordination group.
- Governmental Environment Risk – This is the risk of not continuously understanding, anticipating, and responding to changes in our environment. The WSIB is a state agency operating under a government framework within a political environment that is not always aligned with the practices and priorities of investment entities. To help manage this, the executive director and our legislative liaison work to monitor actual or proposed legislative changes that may affect our ability to accomplish our mission.
- Operational Risk – Operational risk refers to losses that could arise from shortcomings or failures in internal processes, people or systems, or from failures of external processes, people or systems that the WSIB depends on. We manage this risk through continuous improvements of our control structure; training, supervision and development of our staff; and the commitment of executive management to mitigate key operational risks identified by the ERM team. To foster organizational growth and change, management has committed to creating an environment where staff continues to learn and to institute state of the art practices.

Safeguarding Our Reputation

Reputation Risk – The WSIB must maintain its reputation in order to be a sought after partner in the market place, a trusted fiduciary by stakeholders and the Legislature, and a valued resource for the citizens of Washington state. Failure in any of these prior five risk categories will damage the WSIB's reputation and its credibility, and make it difficult, if not impossible, to achieve the goals of its constituents. The agency has dedicated resources focused on coordinating and monitoring communication for the agency. The Board has also adopted rigorous codes of conduct and conflict of interest policies to ensure that its actions meet the most stringent standards and review. Ongoing education and information assist the Board members make informed decisions. This enables the WSIB to promote and protect our reputation.

CORPORATE GOVERNANCE

The WSIB believes a strong, focused corporate governance program is an important part of managing and protecting pension fund assets. Through active support of corporate governance reforms and prudent voting of company proxies, the WSIB works to enhance shareowner value and support our long-term investment objectives. Good corporate governance is a system of checks and balances that fosters transparency, responsibility, accountability, and market integrity. A growing body of research provides empirical support for good governance practices. A number of studies demonstrate that companies with strong corporate governance tend to have lower risk of fraud and higher returns.

Advocates for good governance have seen substantial progress in the past two years, led largely by reforms mandated by the landmark Dodd-Frank Wall Street Reform and Consumer Protection Act. Among other things, the law requires companies to ask for shareholder approval of their executive compensation plans, referred to as say-on-pay. This year a number of corporate boards made changes to their compensation plans when threatened with an unfavorable vote. Of the 2,546 say-on-pay proposals, the WSIB said "no" to 456 plans.

Of those votes against, there were a few high-profile votes this proxy season in which companies' pay proposals were soundly rejected by shareholders. The first to make headlines was Citigroup, where investors denied the CEO a proposed $15 million pay package. The next shareholder victory was at Nabor Industries, an oil and gas drilling and exploration company, which managed to draw only 25 percent support for its executive pay package, despite the Board chairman's agreement to forgo a $100 million termination payment that he was slated to receive after being replaced as CEO of the company a few months earlier. And finally, at Chesapeake Energy, the country's second largest producer of natural gas, even last-minute attempts by the board to placate shareholders failed to garner more than a 20 percent favorable vote for management's say-on-pay proposal. The company is currently under investigation by the Internal Revenue Service and the Securities and Exchange Commission for a controversial investment program that gave the CEO a minority stake in Chesapeake's natural gas wells.

The 2012 proxy voting season also saw social and environmental shareholder proposals receiving strong support votes, particularly proposals to require companies to be more forthcoming about their political contributions.

The WSIB believes that in order to maximize investment returns we must maintain vigilant oversight of the way companies in which we invest are managed. As a long-term investor, the WSIB doesn't have the option of selling its shares if it doesn't like the way a company is performing. Therefore, active participation is a necessity.

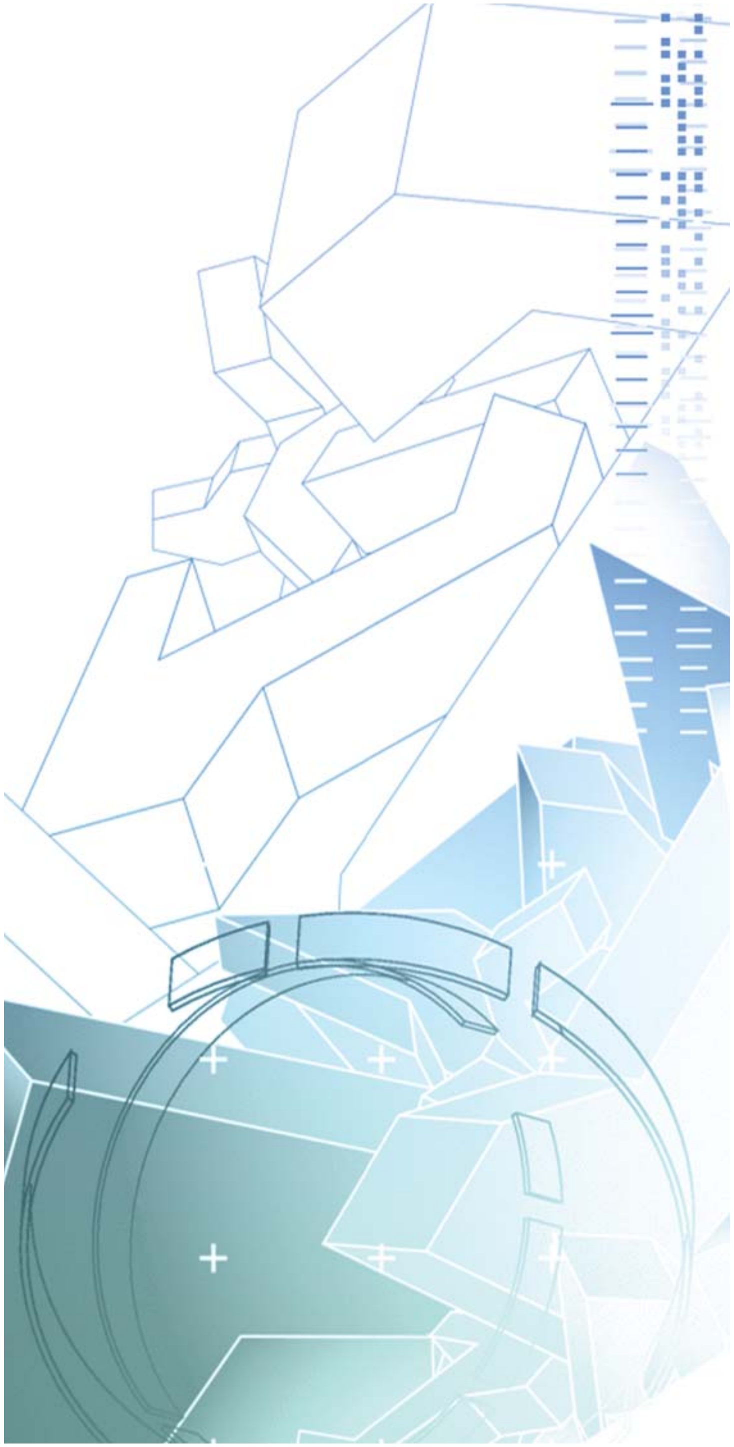
Between July 1, 2011, and June 30, 2012, the WSIB voted 3,562 proxy ballots. Proxy votes were cast on 31,367 individual proposals dealing primarily with election of directors, ratification of auditor, compensation plans, and shareowner proposals. Of the total director votes during that time period, the WSIB withheld – or voted against – 3,072 incumbent directors, largely because of lack of board independence or unreasonably generous compensation practices. The WSIB's policy states that "Executive compensation should be linked directly with performance of the business the executive is charged with managing."

In line with that commitment, the WSIB:

- Voted against 28 percent of the compensation plans proposed; and
- Voted against 326 compensation committee members for paying excessive compensation.

This past year the Corporate Governance program also assumed oversight for how the WSIB's non-U.S. proxies are being voted by our global equity fund managers. With 52 percent of the public equity portfolio invested in non-U.S. companies, the Board adopted new international proxy voting guidelines and directed staff to work more closely with the fund managers responsible for casting the WSIB's vote.

As one of the country's largest institutional investors, the WSIB proxy voting ballot is one of the most effective ways to influence greater board accountability and transparency.



WSIB ANNUAL BUDGET

June 30, 2012

OBJECTS OF EXPENDITURE

APPROPRIATED	Budget	Expenditures	Budget Variance
Salaries	$ 8,102,721	$ 7,776,791	$ 325,930
Benefits	1,985,525	1,906,209	79,316
Personal Service Contracts	206,300	351,804	(145,504)
Goods & Services	2,754,152	2,759,049	(4,897)
Travel	858,800	527,511	331,289
Equipment	183,000	189,562	(6,562)
Treasury Note	89,332	-	89,332
Subtotal Appropriated	$ 14,179,830	$ 13,510,926	$ 668,904 *

NON-APPROPRIATED	Budget	Expenditures	Budget Variance
Public Equity	$ 53,875,000	$ 44,009,090	$ 9,865,910
Private Equity	192,326,000	185,507,649	6,818,351
Real Estate	43,758,000	35,776,145	7,981,855
Tangible Assets	13,195,000	9,950,670	3,244,330
Innovation Portfolio	6,100,000	4,809,642	1,290,358
General Consultants	1,849,149	856,956	992,193
Advisory Services Consultants	3,000,000	-	3,000,000
Legal Fees	1,334,053	349,358	984,695
Custodian Bank Fees	798,153	-	798,153
Securities Lending	15,707,512	10,939,414	4,768,098
Cash Management	2,271,638	4,213,987	(1,942,349)
Cash Overlay	600,000	279,057	320,943
Directed Brokerage	43,621	28,708	14,913
Investment Accounting Data System	1,351,500	1,338,500	13,000
Memberships	75,025	105,439	(30,414)
Research Services	2,549,029	2,331,386	217,643
Subtotal Non Appropriated	338,833,680	300,496,001	38,337,679
TOTAL	$ 353,013,510	$ 314,006,927	$ 39,006,583

* The Balance will be carried forward to fiscal year 2013 since we are granted a biennial appropriation

INVESTMENTS

PLANS UNDER MANAGEMENT

Strategic Asset Allocation

Strategic asset allocation is the process of selecting a mix of asset classes, such as stocks and bonds, and determining their proportions within an investment portfolio. Asset allocation decisions account for nearly 92 percent of the variation between returns on different portfolios and are often considered to be the most important driver of investment performance. Portfolio assets are diversified to help offset declines in any one class, smooth out marketplace ups and downs, and reduce overall investment risk.

The WSIB invests in seven broad based asset classes: public equity, fixed income, private equity, real estate, tangible assets, treasury inflation notes, and cash. A strategic allocation is established for each fund managed by the Board which includes the assets classes used by that fund, long-term policy targets for those asset classes, and the acceptable ranges within which those targets can vary. The WSIB formally reviews the strategic asset allocations at least every four years.

Highlights

- The Board reviewed and made changes to the allocation for the permanent fund portfolios. The changes included an introduction of a U.S. equity allocation with a focus on dividend-paying companies. Staff performed a formal search for the procurement of overlay investment services, which resulted in a change to State Street Global Advisors.

Retirement Funds

To more efficiently manage investments, reduce administrative costs, and minimize investment fees, the defined benefit retirement fund assets are pooled into the Commingled Trust Fund (CTF). Over the past 10 years, the fund has grown from $38.9 billion to $61.8 billion including employer and employee contributions, plus net investment returns, less benefit payments and fund transfers (this does not include Plan 3 self-directed defined contribution funds.

The WSIB measures fund performance by comparing the performance of investment returns of each asset class in the CTF to appropriate benchmarks. Although quarterly and yearly returns change, our long-term realizations should meet or exceed the 8.0 percent actuarially assumed rate of return.

It is important to remember that individual asset classes differ in their behavior and volatility from 1 year to the next. The fair market value of most public market investments can be determined and priced instantly. However, real estate and private equity investments are very illiquid and not easily priced, so it may take years before expected returns are apparent and realized.

Fixed Income

The fixed income program for the CTF is actively managed by WSIB staff against a performance benchmark of the Barclays Universal Index.

The main sectors in the portfolio are U.S. treasury securities, credit bonds, mortgage backed securities (MBS), collateralized mortgage obligations (CMO), asset backed securities (ABS), and commercial mortgage backed securities (CMBS).

During FY 2012, $150 million in cash was moved out of the portfolio. In that same time period, the yield on the 10-year treasury went from 3.16 percent to 1.65 percent, hitting a high of 3.18 percent in July 2011 and a low of 1.45 percent in June 2012.

Highlights

- The portfolio underperformed the Barclays Universal Index for the year, returning 5.51 percent vs. 7.36 percent for the Universal Index.
- Treasuries, agencies and mortgages were underweighted for the portfolio, while credits and CMO were overweighted; ABS and CMBS weighting were neutral.
- Transactions totaled $1.8 billion in sales and $3.6 billion in purchases.

Tangible Assets

The tangible asset portfolio primarily targets investments in infrastructure, natural resource rights (such as oil and natural gas), and timber. Each of these sectors has different return attributes and thus provides diversification benefits to the overall CTF portfolio.

Similar to the real estate program, much of the WSIB's tangible asset program is focused on creating current income for the CTF. These externally-managed partnerships are expected to generate returns that fall between performance expectations for fixed income and equities through the combination of income generation and the potential upside from appreciation. In general, appreciation for this asset class is targeted to be approximately commensurate with inflation.

Tangible assets were established as a separate asset class in 2008. Over time, we expect to create a well-diversified, global tangible asset portfolio with a variety of partners spread among the target sectors noted above, each with their own investment style and geographic diversification.

Highlights

- This asset class is still relatively new, although investment performance over the past four years is largely encouraging.
- Returns for FY 2012 were 2.11 percent.

Real Estate

The WSIB's real estate program focuses primarily on creating high-quality, long-term, stable income streams for the CTF. Our partnership investments target risk-adjusted returns consistent with our long-term expectations for the asset class. The majority of these externally-managed partnerships invest in properties leased to third-parties. The steady income from lease payments, combined with potential appreciation, generate returns that are expected to fall between performance for fixed income and equities over the long-term.

Many of the WSIB's real estate partnerships do not involve co-investment with other financial investors. This provides us with superior governance provisions related to acquisition, disposition, and annual business planning processes. The majority of our partners own real estate assets as private market investments, and as a result, better reflect the actual attributes of real estate investing rather than the potential volatility of public markets. Capital is widely diversified among a variety of partners, each with their own investment style, and real estate assets are geographically diversified, including outside the U.S. Investments are made in a variety of property types to provide further diversification. Finally, diversification is enhanced by our partners investing at different points in the real estate capital structure and at different times in the property life cycle. These varying kinds of diversification provide a degree of stability within a cyclical investment class.

The portfolio continues to produce attractive income yields—the primary goal of the program. The importance of having a long-term investment horizon is evident in the attractive returns for the real estate portfolio over a 10 year period.

Highlights

- For the 1 year period ending June 30, 2012, the portfolio returned 8.57 percent. Over the past year, some of the best returns were from more mainstream sectors, especially warehouse and apartment properties in North America.

- The 10 year return for the WSIB's real estate portfolio was 9.01 percent versus 8.17 percent for the NCREIF index (lagged a quarter). This return also exceeded the WSIB's return benchmark for real estate, which is 8.00 percent over a rolling 10 year period.
- The strongest drivers of the good long-term returns were the WSIB's investments in real estate operating companies (REOCs), geographic diversification, and an emphasis on quality properties and locations.

Public Equity

The public equity program uses a global benchmark, the Morgan Stanley All Country World with USA Gross Investable Market Index, reflecting the globalization of capital markets. In a world in which American companies like Coca-Cola get most of its revenue from overseas and many so-called foreign companies serve mainly the U.S., distinctions between "U.S. stocks" and "international stocks" have become increasingly blurred. The WSIB believes that the future success of the program depends on investment managers finding the most attractive opportunities wherever they are in the world.

Because U.S. equity markets are generally efficient and international equity markets are increasingly efficient, most of the WSIB's public equity investments are in low-cost, broad-based passive index funds. We employ both passive U.S. equity and passive international equity in order to maintain policy weights in both areas. All the global equity mandates, in which investment firms can pick the most attractive stocks wherever they are in the world (U.S. or international), and all the emerging markets equity mandates are actively managed.

Macro-economic and political volatility continued around the globe in FY 2012. During the year, markets witnessed increasing doubts about the strength and durability of the economic recovery, political instability and uncertainty continuing in Middle Eastern countries, the debt crisis worsening in Europe, and increasing concerns about growth in emerging markets like China and Brazil. In this environment, global equity markets suffered a negative return of -6.64 percent.

One of the most important things that an equity program can do is to minimize losses during negative markets. Smaller losses mean more money in the fund to pay benefits. The CTF's program did that, with each segment performing better than its benchmark return. Overall, the program mitigated almost a full percent of the broad market declines, returning -5.78 percent during a year in which broad global equity markets declined -6.64 percent.

Highlights

- The U.S. equity program outperformed its benchmark by 53 basis points (bps) with a return of 4.10 percent versus the benchmark's 3.57 percent return.
- The developed international equity program returned 82 bps more than its benchmark although markets were negative with the portfolio returning -13.50 percent while the benchmark fell -14.32 percent.
- Similarly, the global equity program performed 166 bps better than the benchmark, returning -4.98 percent versus the benchmark return of -6.64 percent.
- The emerging markets equity program provided strong downside protection mitigated over 300 bps of market decline, returning -13.28 percent verus the benchmark return of -16.29 percent.
- The public equity portfolio within the CTF is conservatively structured. The aim is to adopt strategies that protect capital when markets decline, but remain close to market returns when there is a strong market upswing. The program's performance this year delivered on those goals.

Private Equity

As of June 30, 2012, the private equity portfolio was valued at $16.1 billion, or 26.02 percent of the CTF, compared with $15.6 billion and 25.09 percent at the previous fiscal year-end. The growth of the portfolio reflects valuation increases in underlying portfolio companies, as new capital drawn for investment was more than offset by distributions received during the year.

Private equity capital-raising activity picked up during the fiscal year, and new fund commitments in the WSIB portfolio increased accordingly. In addition to 12 "re-up" commitments with existing partners, the program added two new general partner relationships during the year to address portfolio needs. Capital drawn for investment continued at a steady pace, virtually the same as each of the prior two fiscal years. Distribution activity from portfolio company liquidations has been more volatile. Distributions received in FY 2012 were down 26 percent from FY 2011, but up 67 percent over FY 2010.

The goal of the private equity program continues to generate a significant premium above the returns of the public equity markets over the longterm, by investing in a well-diversified portfolio of funds managed by a stable of high-quality general partners.

Highlights

- $4.4 billion in new commitments to funds were closed during FY 2012 compared to $1.2 billion in FY 2011.
- $2.1 billion of committed capital was drawn for investment during the fiscal year compared to $2.2 billion in the prior year.
- $2.5 billion in distributions were returned to the WSIB compared with $3.4 billion in FY 2011.

Innovation Portfolio

The primary investment strategy of the innovation portfolio gives staff the ability to make investments that fall outside the established asset class programs currently used by the Board. Secondly, this portfolio provides the Board with comfort and demonstrated success before committing large dollar amounts to different investment strategies.

Highlights

- No new investment strategies were added to or removed from the innovation portfolio during the fiscal year.

OTHER PLANS UNDER MANAGEMENT

Defined Contribution Retirement Plans

The WSIB oversees the investment options in Plan 3, the Deferred Compensation Program (DCP), and the Judicial Retirement Account (JRA). However, these programs are accounted for and reported on by the Department of Retirements Systems (DRS). Therefore, performance information and the financial statements are provided by DRS.

PERS 3
$1.7 Billion

SERS 3
$1.3 Billion

TRS 3
$5.1 Billion

Deferred Compensation Program
$2.9 Billion

Judicial Retirement Account
$12.3 Million

Daily-Valued Funds for Self-Directed Investment Programs

Bond Market Fund
$1.4 Billion

The goal of this daily-valued fund is to provide participants of the self-directed defined contribution retirement plans (TRS/SERS/PERS Plan 3s, DCP, and JRA) attractive returns while controlling risk by investing in high-quality corporate bonds. The fund is internally managed by the WSIB and is intended for those who want an intermediate-term investment designed to match or moderately exceed the returns of the Lehman Intermediate Credit Index.

Savings Pool
$1.1 Billion

The savings pool is intended as a conservative, short-term investment opportunity where the primary objective is to protect current income and preserve principal. The savings pool is a diversified portfolio of guaranteed investment contracts (GICs) and short-term cash funds.

Labor and Industries' Funds
$13.4 Billion

The WSIB manages Industrial Insurance funds on behalf of the Department of Labor and Industries (L&I). The L&I portfolio consists of four separate funds.

- The Accident Fund primarily pays disability benefits.
- The Medical Aid Fund pays for services required by injured workers and L&I administrative costs.
- The Pension Reserve Fund is maintained by transfers of money from the Accident Fund at the time that a new pensioner is setup.
- The Supplemental Pension Fund supplements time loss and compensates for cost-of-living increases.

Permanent Funds
$903.8 Million

The permanent funds are non-expendable trusts. The principal for each fund remains intact and investment earnings, less expenses, are reinvested or distributed to a beneficiary fund. Five of these funds were established through federal government land grants to help Washington’s schools and colleges with bond repayment, capital development, and facilities maintenance. The Department of Natural Resources transfers proceeds from the sale of land and timber to the WSIB for investment purposes. Fund proceeds are invested in fixed income and short-term holdings, with the exception of the Common School Fund, which is also invested in the U.S. Equity Market Index Fund.

Guaranteed Education Tuition Fund
$2.0 Billion

The Guaranteed Education Tuition (GET) program allows individuals or groups to purchase state college and university tuition units for future use at current prices. Program administration is under the authority of the Committee on Advanced Tuition Payment. The WSIB serves as trustee for the funds and invests them in a mix of short-term holdings, TIPS, U.S. Equity, and International Equity.

Developmental Disabilities Endowment Trust Fund
$33.4 Million

The Developmental Disabilities Endowment Trust Fund (DDEF) supports individuals with developmental disabilities through private contributions and public appropriations. The WSIB invests the fund in a mix of short-term holdings, TIPS, fixed income, and U.S. Equity.

FINANCIALS

OVERVIEW OF FINANCIAL STATEMENTS

This discussion and analysis serves as an introduction to the basic financial statements and notes to the financial statements. The financial statements included are for the Retirement Funds, L&I Funds, Permanent Trust Funds, Other Funds, GET, and DDEF. The financial statements are reported separately due to the unique goals and objectives for each set of funds and each set of funds undergoes a separate financial statement audit.

Basic Financial Statements

The basic financial statements presented include the Statement of Net Assets, which reports the assets by general asset category and the related liabilities as of June 30, 2012, and the Statement of Changes in Net Assets, which reports the contributions to, withdrawals from, and investment earnings for the fiscal year ending June 30, 2012.

The financial statements and notes were prepared by the investment accounting unit of the WSIB.

Notes to the Financial Statements

The notes to the financial statements presented are an integral part of the financial statements and include additional information not readily evident in the financial statements themselves.

Contacting WSIB's Financial Management

This financial report is designed to provide a general overview of WSIB’s investment activities.

If you have any questions about this report or need additional information, contact:
The Washington State Investment Board
2100 Evergreen Park Drive SW
PO Box 40916, Olympia, WA 98504-0916

Phone: 360-956-4600
Website: http://www.sib.wa.gov

PETERSON SULLIVAN LLP
CERTIFIED PUBLIC ACCOUNTANTS
601 UNION STREET, SUITE 2300
SEATTLE, WASHINGTON 98101

TEL 206.382.7777 • FAX 206.382.7777
http://www.pscpa.com

Independent Auditor's Report

To the Members of the Washington State Investment Board

Olympia, Washington

We have audited the accompanying statement of net assets for the Retirement Funds (Commingled Trust Fund and Plan-Specific Investments) of the State of Washington as managed by the Washington State Investment Board ("the Retirement Funds") as of June 30, 2012, and the related statement of changes in net assets for the year then ended. These financial statements are the responsibility of the Washington State Investment Board's management. Our responsibility is to express an opinion on these financial statements based on our audit.

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

The financial statements referred to in the first paragraph present only the investment activity of the Retirement Funds as managed by the Washington State Investment Board. The financial statements do not purport to, and do not, present the financial activity of the Washington State Investment Board or of the State of Washington.

In our opinion, the financial statements referred to in the first paragraph present fairly, in all material respects, the net assets of the Retirement Funds as of June 30, 2012, and the changes in net assets for the year then ended in conformity with accounting principles generally accepted in the United States.

As explained in Note 1, the financial statements include investments valued at $25.5 billion (41% of net assets), whose fair values have been estimated by management in the absence of readily determinable fair values. Management's estimates are based on information provided by the fund managers or, in the case of investments in partnerships, the general partners.

Accounting principles generally accepted in the United States require that the management's discussion and analysis preceding the financial statements be presented to supplement the financial statements. Such information, although not a part of the financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the financial statements in an appropriate operational, economic, or historical context. 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 financial statements, and other knowledge we obtained during our audit of the 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. The introduction section of the annual report has not been subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we do not express an opinion or provide any assurance on it.

/S/ PETERSON SULLIVAN LLP

October 25, 2012

MANAGEMENT DISCUSSION AND ANALYSIS

Management's Discussion and Analysis for the Retirement Funds of the state of Washington, managed by the Washington State Investment Board (WSIB), is presented as an introduction to the financial statements. It is meant to assist the reader in understanding the financial statements by providing an overall review of the financial activities during the year as well as to provide a comparison to the prior year's activities and results. In addition to the Retirement Funds, the WSIB also manages funds for other state of Washington departments. This section of this report represents only the Retirement Funds portion. The Retirement Funds are the largest investor in funds managed by the WSIB.

The financial statements and footnotes follow this section of the report. The Statement of Net Assets provides information on the types of investments and the liabilities of the Retirement Funds. This information is summarized in Table 1. Table 1 also compares the asset, liability, and net asset balances at June 30, 2012, with those at June 30, 2011. The Statement of Changes in Net Assets provides information on investment performance and other increases and decreases in the net assets of the Retirement Funds for the year ended June 30, 2012. This information is summarized in Table 2. Table 2 also compares the financial activities of the Retirement Funds for the year ended June 30, 2012, with those of the year ended June 30, 2011. The Notes to the Financial Statements provide additional information that is essential to a full understanding of the data provided in the financial statements of the Retirement Funds.

As shown in Table 1, the net assets of the Retirement Funds decreased by $(.5) billion during the fiscal year ended June 30, 2012, almost entirely due to current year market movements. Net realized and unrealized gains and losses within the portfolio decreased net assets by $(.4) billion. All asset classes experienced positive investment returns for the fiscal year except publicly traded equity securities with a total fund return of 1.4 percent. Distributions to the retirement system decreased net assets by $(1.3) billion. Other investment income reinvested in the portfolio increased net assets by $1.2 billion.

The following summarizes changes within each grouping listed in Table 1:

- Liquid assets decreased by $(.4) billion. This cash balance represents less than 3 percent of total invested balances. Initially, net investment income received from all asset classes is reinvested in money market funds. Net withdrawals to the Retirement Funds are also funded from cash balances. These balances fluctuate within policy targets as asset allocation decisions are made with accumulated cash to longer term investments. Transfers from other asset classes and reinvested in money market funds totaled $.9 million. Withdrawals by Retirement Funds to cover operating needs reduced liquid assets by $(1.3) billion.
- Fixed income increased by $.8 billion during the current fiscal year. Income of $.5 billion was reinvested in fixed income securities. Transfers from other asset classes totaled $ .2 billion. The remaining increase of $.1 billion was from realized and unrealized gains in the portfolio. The fixed income return for the current fiscal year was 5.5 percent.
- Equities decreased by $(1.5) billion, almost entirely due to negative returns in the equity markets. Net realized and unrealized gains and losses decreased equities by $(1.9) billion. Overall, the equity portfolio returned (5.8) percent for the current fiscal year. An external equity manager was terminated during the current fiscal year and assets totaling $.9 billion were either sold or transferred in kind to other managers. Existing passive equity managers received $.8 billion of this restructuring with the remaining $.1 billion transferred to other asset classes reducing equity balances. Income received and reinvested in this asset class was $.5 billion.
- Alternative investments increased by $.6 billion. Distributions received from general partners totaled $4.3 billion. The cash flow was used to fund capital calls of $3.3 billion. The remaining $1.0 billion of excess distributions received was transferred to other asset classes. Net realized and unrealized gains for the current fiscal year increased alternative investments by $1.3 billion. The remaining increase was due to reinvestment of income within the fund. Investment returns in private equity, real estate, and tangible assets were 5.3 percent, 8.6 percent and 2.1 percent, respectively.
- Collateral held and obligations under securities lending agreements decreased by $(2.7) billion. All securities on loan were recalled as of June 30, 2012, in anticipation of a custodian bank transition on July 1, 2012. Accordingly, the Retirement Funds held no collateral in the securities lending program at year end.
- Open foreign exchange contracts receivable and payable decreased by $(.3) billion. International managers had less open trades at June 30, 2012,

TABLE 1 - SUMMARIZED NET ASSETS	2012	2011	DOLLAR CHANGE	PERCENT CHANGE
Liquid Assets	$1,500,573,033	$1,949,469,436	$(448,896,403)	(23.0%)
Fixed Income Securites	12,570,898,610	11,765,036,513	805,862,097	6.8%
Equities	22,389,165,060	23,872,510,551	(1,483,345,491)	(6.2%)
Alternative Investments	25,514,273,415	24,930,203,442	584,069,973	2.3%
Total Investments	**61,974,910,118**	**62,517,219,942**	**(542,309,824)**	**(0.9%)**
Collateral Held Under Securities Lending Agreements	-	2,718,937,457	(2,718,937,457)	(100.0%)
Open Foreign Exchange Contracts Receivable	1,032,957,451	1,304,357,996	(271,400,545)	(20.8%)
Other Receivables	216,343,312	446,656,492	(230,313,180)	(51.6%)
Total Assets	**63,224,210,881**	**66,987,171,887**	**(3,762,961,006)**	**(5.6%)**
Obligations Under Securities Lending Agreements	-	2,718,937,457	(2,718,937,457)	(100.0%)
Open Foreign Exchange Contracts Payable	1,035,362,703	1,305,228,322	(269,865,619)	(20.7%)
Other Payables	344,136,269	612,866,030	(268,729,761)	(43.8%)
Total Liabilities	**1,379,498,972**	**4,637,031,809**	**(3,257,532,837)**	**(70.3%)**
Net Assets	**$61,844,711,909**	**$62,350,140,078**	**$(505,428,169)**	**(0.8%)**

compared to the prior year, resulting in less open exchange contracts to cover the settlement currency of those trades.

- Other receivables and other payables decreased by $(.2) billion each due to a decrease in open and unsettled security trades. Trading volumes can vary substantially based on the timing of additional cash flows, market movements, and rebalancing of asset classes within a portfolio. Accordingly, there is generally minimal correlation to invested balances.

As shown in Table 2, net investment income for the year decreased by $(10.2) billion almost entirely due to decreases in net realized and unrealized gains and losses from the previous year. The annual return for the year ended June 30, 2012 was 1.4 percent compared to the prior fiscal year return of 21.1 percent. Investment income and expenses remained relatively stable compared to the prior year with a slight decline correlated to decreases in invested balances. Distributions to the Retirement System remained at consistent levels for the year ended June 30, 2012. Large increases in withdrawals, as seen in prior years due to reduced workforces and increasing pension payouts, stabilized during the current fiscal year.

The fair value of the Retirement Funds' assets is directly impacted by the returns of the various capital markets within which the WSIB invests. However, one of the benefits of the diversification gained by investing across various investment types as well as broadly within an asset class is the reduction in aggregate volatility of the total investment portfolio. The WSIB makes the asset allocation decisions for the Retirement Funds based on recommendations from its staff and other investment experts. Retirement Fund assets are rebalanced by WSIB across asset classes, as appropriate, when fair values of assets fall outside policy ranges.

TABLE 2 - SUMMARIZED CHANGES IN NET ASSETS	2012	2011	DOLLAR CHANGE
Net Investment Income			
Investment Income	$1,508,018,825	$1,574,922,015	$(66,903,190)
Net Realized Capital Gain	3,228,420,780	2,780,114,557	448,306,223
Unrealized Gain (Loss)	(3,656,592,676)	6,846,016,594	(10,502,609,270)
Investment Expenses	(259,862,602)	(209,240,226)	50,622,376
Net Investment Income (Loss)	**819,984,327**	**10,991,812,940**	**(10,171,828,613)**
Net Withdrawal by Retirement Plans	(1,325,412,496)	(1,369,578,476)	(44,165,980)
Net Assets - Beginning	**$62,350,140,078**	**$52,727,905,614**	**$9,622,234,464**
Net Assets - Ending	**$61,844,711,909**	**$62,350,140,078**	**$(505,428,169)**

Retirement Funds Statement of Net Assets - June 30, 2012

See notes to financial statements

	Commingled Trust Fund	Plan-Specific Investments	Total	Percent of Plan Assets
ASSETS				
Investments:				
LIQUIDITY				
Cash and Money Market Funds	$ 1,317,165,119	$ 91,893,880	$ 1,409,058,999	
Foreign Currency	91,514,034	-	91,514,034	
Total Liquidity	1,408,679,153	91,893,880	1,500,573,033	2.4%
FIXED INCOME SECURITIES (U.S. DOLLAR DENOMINATED)				
Asset Backed Securities	20,132,797	-	20,132,797	
Residential Mortgage Backed Securities	1,828,200,237	-	1,828,200,237	
Commercial Mortgage Backed Securities	233,568,624	-	233,568,624	
Corporate Bonds - Domestic	980,533,946	-	980,533,946	
Corporate Bonds - Foreign	3,881,367,338	-	3,881,367,338	
U.S. Government Treasury Securities	3,282,516,441	-	3,282,516,441	
Foreign Government and Agency Securities	1,122,852,963	-	1,122,852,963	
Total Fixed Income Securities (U.S. Dollar Denominated)	11,349,172,346	-	11,349,172,346	18.3%
FIXED INCOME SECURITIES (NON U.S. DOLLAR DENOMINATED)				
Corporate Bonds Domestic	62,170,874	-	62,170,874	
Corporate Bonds Foreign	160,521,171	-	160,521,171	
Foreign Government and Agency Securities	619,042,677	-	619,042,677	
Supranational Securities	379,991,542	-	379,991,542	
Total Fixed Income Securities (Non U.S. Dollar Denominated)	1,221,726,264	-	1,221,726,264	2.0%
CORPORATE STOCK (U.S. DOLLAR DENOMINATED)				
Corporate Stock - Domestic	2,090,460,280	-	2,090,460,280	
Corporate Stock - Foreign	826,985,815	-	826,985,815	
Total Corporate Stock (U.S. Dollar Denominated)	2,917,446,095	-	2,917,446,095	4.7%
CORPORATE STOCK (NON U.S. DOLLAR DENOMINATED)				
Corporate Stock - Domestic	2,965	-	2,965	
Corporate Stock - Foreign	9,557,036,627	-	9,557,036,627	
Total Corporate Stock (Non U.S. Dollar Denominated)	9,557,039,592	-	9,557,039,592	15.4%
COMMINGLED EQUITY INDEX FUNDS				
Commingled Index Funds - Domestic	8,281,176,268	-	8,281,176,268	
Commingled Index Funds - Foreign	1,633,503,105	-	1,633,503,105	
Total Commingled Equity Index Funds	9,914,679,373	-	9,914,679,373	16.0%
ALTERNATIVE INVESTMENTS				
Private Equity	16,086,974,092	-	16,086,974,092	
Real Estate	8,594,518,713	-	8,594,518,713	
Tangible Assets (Infrastructure, Natural Resources)	832,780,610	-	832,780,610	
Total Alternative Investments	25,514,273,415	-	25,514,273,415	41.2%
Total Investments	61,883,016,238	91,893,880	61,974,910,118	100.0%
Investment Earnings Receivable	180,706,593	70,010	180,776,603	
Receivables for Investments Sold	35,566,709	-	35,566,709	
Open Foreign Exchange Contracts Receivable	1,032,957,451	-	1,032,957,451	
Total Assets	63,132,246,991	91,963,890	63,224,210,881	
LIABILITIES				
Investment Management Fees Payable	9,332,916	37,003	9,369,919	
Payable for Investments Purchased	334,766,350	-	334,766,350	
Open Foreign Exchange Contracts Payable	1,035,362,703	-	1,035,362,703	
Total Liabilities	1,379,461,969	37,003	1,379,498,972	
NET ASSETS	$ 61,752,785,022	$ 91,926,887	$ 61,844,711,909	

Retirement Funds Statement of Changes in Net Assets - Year Ended June 30, 2012

See notes to financial statements

	Commingled Trust Fund	Plan-Specific Investments	Total
Net Investment Income			
Investment Income:			
Interest, Dividends, and Other Investment Income	$ 1,493,756,864	$ 818,007	$ 1,494,574,871
Securities Lending Income	13,443,954	-	13,443,954
Realized Capital Gains	4,388,731,931	-	4,388,731,931
Realized Capital Losses	(1,160,311,151)	-	(1,160,311,151)
Unrealized Losses	(3,656,592,676)	-	(3,656,592,676)
Less:			
Investment Expenses	(252,141,492)	(471,124)	(252,612,616)
Securities Lending Broker Rebates Paid and Bank Fees	2,952,319	-	2,952,319
WSIB Operating Expenses	(10,202,305)	-	(10,202,305)
Net Investment Income	819,637,444	346,883	819,984,327
Net Withdrawal by Retirement Plans	-	(1,325,412,496)	(1,325,412,496)
Investments in Commingled Funds	740,332,842	(740,332,842)	-
Withdrawals from Commingled Funds	(2,062,946,013)	2,062,946,013	-
Decrease in Net Assets	(502,975,727)	(2,452,442)	(505,428,169)
NET ASSETS, JUNE 30, 2011	62,255,760,749	94,379,329	62,350,140,078
NET ASSETS, JUNE 30, 2012	$ 61,752,785,022	$ 91,926,887	$ 61,844,711,909

NOTES TO FINANCIAL STATEMENTS

Note 1. Description of Funds and Significant Accounting Policies

Description of Funds

The Retirement Funds consist of retirement contributions from employer and employee participants and related earnings on those contributions, in the Washington state Retirement System. The Retirement System is administered by the Department of Retirement Systems (DRS). The financial statements present only the activity of the Retirement Funds as managed by the WSIB. The WSIB has exclusive control of the investment of all money invested in the Retirement Funds. The financial statements do not present the financial position or the results of operations of the WSIB or DRS.

Basis of Accounting

The accompanying financial statements have been prepared in conformity with accounting principles generally accepted in the United States for governments prescribed by the Governmental Accounting Standards Board (GASB) on the accrual basis of accounting.

Valuation of Investments

Investments are reported at fair value. Unrealized gains and losses are included as investment income in the Statement of Changes in Net Assets.

The net assets of the Retirement Funds are valued on a monthly basis using the following sources:

Publicly Traded Securities (Corporate stock, Commingled Funds, Investment Derivatives, and Fixed Income): Fair values are based on published market prices, quotations from national security exchanges, and security pricing services as of each month end closing of the New York Stock Exchange.

Limited Partnerships: The fair value of investments that are organized as limited partnerships and have no readily ascertainable fair value (such as private equity, real estate, and tangible assets) has been determined by management based on the individual investment's capital account balance, reported at fair value by the general partner, at the closest available reporting period, adjusted for subsequent contributions, distributions, management fees, and changes in values of foreign currency and published market prices for certain securities.

The limited partnerships' annual financial statements are audited by independent auditors. These investments are valued at $25.5 billion (41.2 percent of total net assets) as of June 30, 2012. Because of the inherent uncertainties in estimating fair values, it is at least reasonably possible that the estimates will change in the near-term.

Private Equity Limited Partnerships: The fair value of individual capital account balances is based on the valuations reported by private equity partnerships using the following methodologies to value the underlying portfolio companies:

- Valuations of publicly traded portfolio companies are based on active exchanges using quoted market prices as of the close of trading for each month-end.
- When a portfolio company investment does not have a readily available market price, but has a return that is determined by reference to an asset for which a market price is readily available, valuations are based on the closing market price of the reference asset on the valuation date, adjusted for factors that affect the fair value of the investment held.
- When the portfolio company investments are private holdings and are not traded on active security exchanges, valuation methodologies used consist primarily of income and market approaches. The income approach involves a discounted cash flow analysis based on portfolio companies' projections. The market approach involves valuing a company at a multiple of a specified financial measure (generally EBITDA) based on multiples at which comparable companies trade.

Real Estate Limited Partnerships: Real estate partnerships provide quarterly valuations based on the most recent capital account balance to WSIB management. Individual properties are valued by the partnerships at least annually, and are adjusted as frequently as quarterly if material market or operational changes have occurred. Properties are generally externally valued every one to five years, depending upon the partnership. Structured finance investments receive quarterly value adjustments by the partners, generally applying the assumption that all such positions will be held to maturity. Annual audits of most partnerships include a review of compliance with the partnership's valuation policies.

Revenue Recognition

Interest and dividend income is recognized when earned. Capital gains and losses are recognized on a trade-date basis. Purchases and sales of investments are also recorded on a trade-date basis.

Securities Lending

The Retirement Funds record collateral received under securities lending agreements where the Retirement Funds have the ability to spend, pledge, or sell the collateral without borrower default. Liabilities resulting from these transactions are also reported. Additionally, costs associated with securities transactions, broker commissions paid, and lending agent management fees are reported as investment expenses in the accompanying financial statements. The Statement of Net Assets does not include detailed holdings of securities lending collateral by investment classification.

Investments and Withdrawals

Investments and withdrawals are recorded when received or paid.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Actual results could differ from the estimated amounts.

Note 2. The Commingled Trust Fund (CTF) and Plan Specific Investments

The Commingled Trust Fund (CTF) is a diversified pool of investments which is used as an investment vehicle for 14 separate retirement plans and a supplemental insurance fund. These plans hold shares in the CTF, which represent a percentage ownership in the pool of investments. Plans are allowed to purchase or sell shares in the CTF, based on the fair value of the underlying assets, on the first business day of each month.

In addition to share ownership in the CTF, each retirement plan holds short-term investments. These short-term investments are referred to as "plan-specific investments" in the accompanying financial statements and are used to manage the cash needs of each retirement plan.

The CTF consists of the PERS Plans 1 and 2/3; TRS Plans 1 and 2/3; SERS Plans 2/3; LEOFF Plans 1 and 2; WSP Retirement Systems Plans 1 and 2; VFF, PSERS Plan 2, and the Higher Education Supplemental Insurance Fund. The CTF includes both the defined benefit and defined contribution portion of PERS Plan 3, SERS Plan 3 and TRS Plan 3, which are hybrid defined benefit/defined contribution plans. The participants also have the option to invest their defined contributions in other external options. These additional options are not reflected in the accompanying financial statements as the accounting responsibility lies with the Department of Retirement Systems for these invested balances.

Note 3. Breakdown of Plan Assets

The Schedule of Participation presents the net assets broken down by ownership by the various pension plans. "DC" means "defined contribution" and "DB" means "defined benefit," two different types of retirement plans.

Schedule of Participation

RETIREMENT PLANS:	Commingled Trust Fund	Plan-Specific Investments	Total Plan Net Assets	Percent of Plan Assets
HIGHER ED. SUPPLEMENTAL INSURANCE FUND	$ 1,961,958	$ 484,202	$ 2,446,160	trace
LEOFF 1	4,900,311,144	3,008,572	4,903,319,716	7.9%
LEOFF 2	6,608,665,518	14,403,707	6,623,069,225	10.7%
PERS 1	7,373,135,900	5,120,679	7,378,256,579	11.9%
PERS 2/3 (DC and DB Plans)	21,600,476,465	27,468,237	21,627,944,702	35.0%
PUBLIC SAFETY EMPLOYEES 2	169,783,403	2,500,846	172,284,249	0.3%
SCHOOL EMPLOYEES 2/3 (DC and DB Plans)	3,745,654,441	6,947,900	3,752,602,341	6.1%
STATE PATROL 1	862,940,223	301,361	863,241,584	1.5%
STATE PATROL 2	14,657,158	300,524	14,957,682	trace
TEACHERS 1	6,189,794,123	4,216,795	6,194,010,918	10.0%
TEACHERS 2/3 (DC and DB Plans)	10,135,060,758	27,173,969	10,162,234,727	16.4%
VOLUNTEER FIREFIGHTERS	150,343,931	95	150,344,026	0.2%
Total Net Assets at June 30, 2012	**$ 61,752,785,022**	**$ 91,926,887**	**$ 61,844,711,909**	**100.0%**

Note 4. Fees and Expenses

Investment fees and expenses are accounted for as a reduction of investment income or are netted directly from the asset value of Retirement Fund investments. These fees include investment management fees and commissions, investment consultant fees, legal fees, and other investment management related expenses and are summarized in the Schedule of Investment Fees and Expenses. The WSIB operating expenses are charged to the funds based upon actual costs incurred to manage the investments. WSIB operating expenses are allocated to the funds under management based on relative market values, in accordance with state statutes.

Schedule of Investment Fees and Expenses

	Fees Paid	Netted Fees *	Total Fees	Assets Under Management
EQUITY SECURITIES:				
Public Equity - Emerging Markets	$ 10,880,789	$ 7,393,419	$ 18,274,208	$ 2,434,783,177
Active Equtiy - Global	24,954,811	28,708	24,983,519	5,985,534,732
Passive Equity - Global	851,418	-	851,418	13,968,847,150
ALTERNATIVE INVESTMENTS:				
Private Equity	167,017,728	16,318,112	183,335,840	16,086,974,092
Real Estate	34,103,753	4,983,724	39,087,477	8,594,518,713
Tangible Assets	7,899,102	1,991,881	9,890,983	832,780,610
CASH MANAGEMENT	3,120,449	-	3,120,449	1,409,058,999
OTHER FEES:				
Consultants and Accounting	1,120,415	-	1,120,415	NA
Legal Fees	349,358	-	349,358	NA
Research Services	1,935,849	-	1,935,849	NA
Miscellaneous Fees	378,944	-	378,944	NA
Total Investment Expenses	$ 252,612,616	$ 30,715,844	$ 283,328,460	$ 49,312,497,473

*Netted fees are included in unrealized gains (losses) in the accompanying financial statements

Note 5. Unfunded Commitments

The Retirement Funds have entered into a number of agreements that commit the Retirement Funds, upon request, to make additional investment purchases up to predetermined amounts. As of June 30, 2012, the Retirement Funds had a total of $16.8 billion in unfunded commitments in the following asset classes:

Private Equity	$9,066,129,382
Real Estate	$7,176,530,148
Innovation Portfolio	$194,787,894
Tangible Assets	$408,403,197

Note 6. Public Employees' Retirement System Plan 3, Teachers' Retirement System Plan 3, and the School Employees' Retirement System Plan 3

The financial statements only include the portion of the PERS Plan 3, TRS Plan 3, and SERS Plan 3, which are invested in the CTF. The CTF does not include PERS Plan 3, TRS Plan 3, or SERS Plan 3 self-directed investments, which are accounted for and reported on by the DRS.

Note 7. Deposit and Investment Risk Disclosures

Custodial Credit Risk – Deposits

Custodial credit risk for deposits is the risk that, in the event of a bank failure, the Retirement Funds' deposits may not be returned to it. The Retirement Funds do not have a deposit policy for custodial credit risk. As of June 30, 2012, there were no deposits with the custodial bank.

Custodial Credit Risk – Investments

Custodial credit risk for investments is the risk that, in the event of a failure of the counterparty to a transaction, the Retirement Funds will not be able to recover the value of investments that are in the possession of an outside party.

The Retirement Funds mitigates custodial credit risk by having its investment securities held by its custodian. Also, investment securities are registered in the name of the Washington State Investment Board for the benefit of the Retirement Funds, excluding cash and cash equivalents and repurchase agreements held as securities lending collateral.

The WSIB has been authorized by statute as having the investment management responsibility for Retirement Funds. The WSIB is authorized to invest as provided by statute (Chapter 43.33A RCW) and WSIB policy. The WSIB is authorized and invests in the following: U.S. Treasury Bills; discount notes; repurchase agreements; reverse repurchase agreements; banker's acceptances; commercial paper; guaranteed investment contracts; U.S. Government and Agency (government sponsored corporations eligible for collateral purposes at the Federal Reserve) securities; non-U.S. dollar bonds; investment grade corporate bonds; non-investment grade corporate bonds; publicly traded mortgage backed securities; privately placed mortgages; private placements of corporate debt; U.S. and foreign common stock; U.S. preferred stock; convertible securities; private equity including but not limited to investment corporations, partnerships, and limited liability companies for venture capital, leveraged buy-outs, real estate and other tangible assets, or other forms of private equity; asset backed securities; and derivative securities including futures, options, options on futures, forward contracts, and swap transactions. There have been no violations of these investment restrictions during fiscal year 2012.

Interest Rate Risk

Interest rate risk is the risk that changes in interest rates over time will adversely affect the fair value of an investment. Effective duration is the measure of a debt investment's exposure to fair value changes arising from changes in interest rates. Effective duration uses the present value of future cash flows, weighted for those flows as a percentage of the investment's full price. Increases in prevailing interest rates generally translate into decreases in fair values of those investments, and decreases in interest rates result in increases in valuations. The Retirement Funds' fixed income investments are to be actively managed to meet or exceed the return of the Barclays Capital Universal Index, with a duration not higher or lower than 20 percent of the duration of the index. As of June 30, 2012, the Retirement Funds' duration was within the duration target of this index.

Schedule 1 provides information about the interest rate risks associated with the CTF investments as of June 30, 2012. The schedule displays various asset classes held by maturity in years, effective durations, and credit ratings. Residential mortgage backed, commercial mortgage backed, and asset backed securities are reported using the average life within the portfolio. The average life is a calculated estimate of the average time (in years) until maturity for these securities taking into account possible prepayments of principal. All other securities on this schedule are reported using the stated maturity date.

Credit Risk

Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. The Retirement Funds' rated debt investments as of June 30, 2012, were rated by Moody's and/or an equivalent national rating organization. Investment types with multiple ratings are presented in Schedule 2 using the Moody's rating scale.

Concentration of Credit Risk

Concentration of credit risk is the risk of loss attributed to the magnitude of an investment in a single issuer. The Retirement Funds' policy states no corporate fixed income issue shall exceed 3 percent of cost at the time of purchase or 6 percent of fair value thereafter of the fund, and no high yield issues shall exceed 1 percent of cost or 2 percent of fair value of the fund. There was no concentration of credit risk exceeding these policy guidelines as of June 30, 2012.

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 Retirement Funds do not have a formal policy to limit foreign currency risk. The Retirement Funds manage their exposure to fair value loss by requiring their international securities investment managers to maintain diversified portfolios by sector and by issuer to limit foreign currency and security risk. The Retirement Funds exposure to foreign currency risk is presented in Schedule 3 which provides information on deposits and investments held in various foreign currencies. Private equity and real estate are presented according to the financial reporting currency of the individual funds and is not a presentation of currency exposure relating to the underlying holdings. The schedule is stated in U.S. dollars.

Note 8. Securities Lending

State law and WSIB policy permit the Retirement Funds to participate in securities lending programs to augment investment income. The WSIB has entered into an agreement with JPMorgan to act as agent for the WSIB in securities lending transactions. As JPMorgan is the custodian bank for the WSIB, it is counterparty to securities lending transactions.

The Retirement Funds report securities lent (the underlying securities) as assets in the Statement of Net Assets. Cash received as collateral on securities lending transactions and investments made with that cash are reported as assets. Securities received as collateral are reported as assets if the Retirement Funds have the ability to pledge or sell them without a borrower default. Liabilities resulting from these transactions are also reported in the Statement of Net Assets. Securities lending transactions collateralized by securities where the Retirement Fund does not have the ability to pledge or sell unless the borrower defaults are not reported as assets and liabilities.

In anticipation of the custodian bank conversion on July 1, 2012, the Retirement Funds recalled all securities on loan.

There were no assets on loan at June 30, 2012, and no collateral held related to securities lending transactions.

Fixed income and equity securities were loaned during the current fiscal year and collateralized by the Retirement Funds' agent with cash and U.S. Government Securities (exclusive of mortgage backed securities and letters of credit), and irrevocable letters of credit. When the loaned securities had collateral denominated in the same currency, the collateral requirement was 102 percent of the fair value, including accrued interest, of the securities loaned. All other securities were required to be collateralized at 105 percent of the fair value, including accrued interest, of the loaned securities.

During fiscal year 2012, securities lending transactions could be terminated on demand by either the Retirement Funds or the borrower. The weighted average maturity of loans for 2012 was 1.5 days. Cash collateral was invested by the Retirement Funds in the WSIB's short-term investment pool. Because the securities lending agreements were terminable at will, their duration did not generally match the duration of the investments made with the cash collateral. Non-cash collateral could not be pledged or sold absent borrower default. There are no restrictions on the amount of securities that can be lent.

Securities were lent with the agreement that they would be returned in the future for exchange of the collateral. JPMorgan indemnified the WSIB by agreeing to purchase replacement securities or return the cash collateral in the event a borrower failed to return the loaned securities or pay distributions thereon. JPMorgan's responsibilities included performing appropriate borrower and collateral investment credit analyses, demanding adequate types and levels of collateral, and complying with applicable federal regulations concerning securities lending.

During fiscal year 2012, there were no significant violations of legal or contractual provisions, no failures by any borrowers to return loaned securities or to pay distributions thereon. Further, the Retirement Funds incurred no losses during fiscal year 2012 resulting from a default by either the borrowers or the securities lending agents.

Note 9. Derivatives

Retirement Funds are authorized to utilize various derivative financial instruments, including mortgage backed securities, financial futures, forward contracts, interest rate swaps, credit default swaps, equity swaps, and options. Derivative transactions involve, to varying degrees, market and credit risk. In connection with the cash overlay program, at June 30, 2012, the Retirement Funds held investments in financial futures, forward currency contracts and other derivative securities that are recorded at fair value with changes in value recognized in investment income in the Statement of Changes in Net Assets in the period of change.

Derivatives are generally used to achieve the desired market exposure of a security, index or currency, adjust portfolio duration, or rebalance the total portfolio to the target asset allocation. Derivative contracts are instruments that derive their value from underlying assets, indices, reference interest rates, or a combination of these factors. A derivative instrument could be a contract negotiated on behalf of the Retirement Funds and a specific counterparty. This would typically be referred to as an over the counter (OTC) contract such as forward contracts and to be announced (TBA) securities. Alternatively, a derivative instrument, such as futures, could be listed and traded on an exchange and referred to as "exchange traded".

Inherent in the use of OTC derivatives, the Retirement Funds are exposed to counterparty credit risk 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. As of June 30, 2012, the Retirement Funds counterparty risk was not deemed to be significant, whether evaluating counterparty exposure outright or netting collateral against net asset positions on contracts with each counterparty.

Mortgage TBA's are used to achieve the desired market exposure of a security or asset class or adjust portfolio duration. A TBA is a contract for the purchase or sale of agency mortgage backed securities to be delivered at a future agreed-upon date. TBA's carry future settlement risk due to the possibility of not receiving the asset or associated gains specified in the contract and such loss upon failure by counterparties to deliver under the contracts would not be material at June 30, 2012. The fair value of TBA derivatives is included in Residential Mortgage Backed Securities in the Statement of Net Assets.

Futures contracts are standardized, exchange-traded contracts to purchase or sell a specific financial instrument at a predetermined price. Gains and losses on futures contracts are settled daily based on a notional (underlying) principal value and do not involve an actual transfer of the specific instrument. The exchange assumes the risk that the counterparty will not pay and generally requires margin payments to minimize such risk. Futures are generally used to achieve the desired market exposure of a security or index or rebalance the total portfolio.

Forward currency contracts are agreements to exchange the currency of one country for the currency of another country at an agreed-upon price and settlement date. These forward commitments are not standardized and carry credit risk due to the possible nonperformance by one of the counterparties. The maximum potential loss is the aggregate face value in U.S. dollars at the time the contract was opened; however, the likelihood of such loss is remote. At June 30, 2012, the Retirement Funds had outstanding forward currency contracts to purchase foreign currencies with a fair value of $1,028,686,608, and outstanding contracts to sell foreign currencies with a fair value of $1,030,859,754 reported as a component of open foreign currency contracts payable and receivable in the accompanying Statement of Net Assets. The net unrealized gain of $2,173,146 is included in the accompanying Statement of Changes in Net Assets. The contracts have varying maturity dates ranging from July 2, 2012, to September 19, 2012.

At June 30, 2012, the Retirement Funds fixed income portfolio held derivative securities consisting of collateralized mortgage obligations with a fair value of $682,011,205. Domestic and foreign passive equity index fund managers may also utilize various derivative securities to manage exposure to risk and increase portfolio returns. Information on the extent of use and holdings of derivative securities by passive equity index fund managers is unavailable.

Derivatives which are exchange traded are not subject to credit risk. The maximum loss that would be recognized at June 30, 2012, if all counterparties fail to perform as contracted was de minimis.

At June 30, 2012, the counterparties' credit ratings for forwards currency contracts that are subject to credit risk had a credit rating of no less than A1 using the Moody's rating scale.

		Changes in Fair Value - Included in Investment Income	Fair Value at June 30, 2012 - Investment Derivative	
	Classification	Amount	Amount	Notional
FUTURES CONTRACTS:				
Bond Index Futures	Investment	$ 54,597,776	$ 1,839,781	4,520
Equity Index Futures	Investment	(3,769,850)	3,724,752	1,049
		$ 50,827,926	$ 5,564,533	5,569
TO BE ANNOUNCED SECURITES:				
FHLMC TBA	Investment	$ 1,208,239	$ 47,713,528	43,906,000
FNMA TBA	Investment	9,939,838	182,608,754	171,016,000
GNMA TBA	Investment	2,415,083	61,269,598	56,042,000
	Investment	$ 13,563,160	$ 291,591,880	270,964,000
FORWARD CURRENCY CONTRACTS:				
Australian Dollar	Investment	$ (9,146,651)	$ 39,898	240,943,252
Brazilian Real	Investment	(282,471)	-	-
Canadian Dollar	Investment	(6,869,360)	553,846	127,605,659
Danish Krone	Investment	(572,417)	(13,827)	25,932,588
Euro	Investment	(34,124,075)	(2,411,719)	246,524,792
Hong Kong Dollar	Investment	851	(291)	222,301,380
Israeli Shekel	Investment	(1,219)	(1,219)	922,000
Japanese Yen	Investment	(1,821,919)	(9,808)	8,198,145,566
Mexican Peso	Investment	(6,740)	(6,740)	6,500,000
New Zealand Dollar	Investment	(466,631)	(168,676)	6,140,796
Norwegian Krone	Investment	(2,956,908)	(11,421)	142,530,738
Pound Sterling	Investment	(8,655,017)	(114,896)	74,864,693
Singapore Dollar	Investment	(712,967)	(2,795)	1,547,447
South African Rand	Investment	175,170	176,628	56,458,630
Swedish Krona	Investment	(3,565,333)	(187,720)	282,251,023
Swiss Franc	Investment	(8,395,960)	(1,404)	19,690,089
U.S. Dollar	Investment	74,798,237	-	1,023,077,275
		$ (2,603,410)	**$ (2,160,144)**	**10,675,435,928**

Note 10. Summary of Investment Policies

Under RCW 43.33A.030, Trusteeship of the Retirement Funds is vested within the voting members of the WSIB. The Legislature has established a standard of care for investment of these funds in RCW 43.33A.140. Additionally, the WSIB and its staff must comply with other state laws, such as the Ethics in Public Service Act, RCW 42.52, as it makes its investment decisions and seeks to meet the following investment objectives.

Strategic and Performance Objectives

In accordance with RCW 43.33A.110, the portfolio is managed to achieve a maximum return at a prudent level of risk.

The Retirement Funds return objective is to exceed the return of the following measures:

- Passive Benchmark: a custom benchmark consisting of public market indices weighted according to asset allocation targets. Currently, the passive benchmark is comprised of 69 percent MSCI All Country World IMI Index Net with U.S. Gross and 31 percent Barclays Capital Universal; and
- Implementation Value Added: a custom benchmark consisting of the public market indices, as defined in each asset class's policy, weighted according to asset allocation targets. This differs from the passive benchmark as it is not an investable benchmark due to the uninvestable premium added to the real estate and private equity passive benchmarks.

The Retirement Fund Asset Allocation

The WSIB establishes asset allocation targets that must be considered at all times when making investment decisions. The asset mix may deviate from the target. Deviations greater than predetermined acceptable levels require rebalancing back to the target. When an asset class exceeds its range, the goal of rebalancing will be to meet the target allocation within consideration of the other remaining asset classes.

Asset Class	Target	Policy Range	Asset Class Range
Fixed Income	20%	16 - 24%	+ or - 4%
Tangible Assets	5%	3 - 7%	+ or - 2%
Real Estate	13%	10 - 16%	+ or - 3%
Global Equity	37%	32 - 42%	+ or - 5%
Private Equity	25%	21 - 29%	+ or - 4%
Innovation Portfolio	0%	0 - 5%	+ 5%
Cash	0%	0 - 3%	+ 3%

While the Retirement Funds goal is to reach the target (optimal portfolio) as quickly as possible, because of the illiquidity and time lagging nature of the Real Estate, Tangible Assets, and Private Equity investments, it is assumed that it will take time to achieve the target. It is anticipated the optimal target will be reached sometime in 2015. The asset allocation for the CTF is formally reviewed at least every 4 years. The allocation policy is reviewed more frequently if there has been a fundamental change in the structure of the capital markets or in the underlying cash flow or liability structure of the retirement systems.

Assets will be rebalanced across asset classes, as appropriate, when market values fall outside policy ranges. Rebalancing is accomplished by first using normal cash flows and second through reallocations of assets across asset classes. In cases of a major rebalancing, the Retirement Funds can utilize futures, forward contracts, and options in order to maintain exposure within each asset class and reduce transaction costs. Major rebalancing can occur to bring asset classes within their target ranges or when the Retirement Funds are transitioning managers.

Public Markets Equity

To achieve the performance and diversification objectives of the Retirement Funds, the Public Markets equity program seeks to:

- Achieve the highest return possible from active management consistent with prudent risk management and the desire for downside protection with passive management as the default;
- Provide diversification to the Retirement Funds overall investment program;
- Maintain liquidity in public equity; and
- Maintain transparency into all public equity strategies, to the extent possible.

General Strategies

- The public markets equity portion of the Retirement Funds invests in publicly traded equities globally, including equity securities in the U.S., developed non-U.S., and emerging markets. The program has a global benchmark, currently the MSCI All Country World Investable Market Index (MSCI ACWI IMI).
- A mix of external managers approved by the WSIB Board will be used to implement the program.
- Passive management delivers broad diversified equity market exposure at low cost and is used when active managers cannot be identified and monitored with existing resources. Passive management is also used when it is considered an appropriate alternative to active management, typically in more efficient markets.
- Active management is used when the Retirement Funds can identify, access, and monitor successful managers in markets that are less efficient. Active management seeks to enhance the risk/return profile of the program.

Asset Allocation

The U.S. and non-U.S. allocations for the public equity program are managed within the ranges presented below:

United States benchmark weight +/- 5 percent

Non-U.S. Markets (developed and emerging) benchmark weight +/- 5 percent

Emerging Markets benchmark weight -5 percent to +10 percent

Fixed Income

The fixed income segment is to be managed to achieve the highest return possible consistent with the desire to control asset volatility; and emphasize high yield to maturity opportunities to add value through active management, provide diversification to the overall investment program and to meet or exceed the return of the Barclays Capital Universal Bond Index, with volatility similar to or less than the index.

Permissible fixed income market segments include:

- U.S. Treasuries and Government Agencies.
- Credit Bonds.

- Investment Grade Mortgage-Backed Securities as defined by Barclays Capital Global Family of Fixed Income Indices.
- Investment Grade Asset-Backed Securities as defined by Barclays Capital Global Family of Fixed Income Indices.
- Investment Grade Commercial Mortgage-Backed Securities as defined by Barclays Capital Global Family of Fixed Income Indices.
- Convertible Securities.
- Non-Dollar Bonds.
- Washington State Housing Finance Commission (HFC) taxable municipal bonds up to a total of $50 million with a maximum of $10 million purchased per year.

Other fixed income segments and instruments may be added from time to time as they are developed or deemed appropriate.

Fixed Income Portfolio Constraints

- RCW 43.33A.140 prohibits a corporate fixed income issue's cost from exceeding 3 percent of the Retirement CTF's market value at the time of purchase, and its market value from exceeding 6 percent of the Retirement CTF's market value at any time. The Retirement Funds are managed with a more restrictive concentration constraint than required by the cited RCW. Exposure to any corporate issuer will not exceed 3 percent of the Retirement CTF Fixed Income Portfolio's market value.
- The par value of bonds from any one issuer with a below investment grade rating (as defined by Barclays Capital Global Family of Fixed Income Indices) shall not exceed 1 percent of the total portfolio's par value.
- Total market value of below investment grade credit bonds (as defined by Barclays Capital Global Family of Fixed Income Indices) shall not exceed 15 percent of the market value of the fixed income portfolio.
- Although below investment grade mortgage-backed, asset-backed or commercial mortgage-backed securities may not be purchased, portfolio holdings that are downgraded to those levels or are no longer rated may continue to be held.
- The total market value of below investment grade mortgage-backed, asset-backed and commercial mortgage-backed securities shall not exceed 5 percent of the market value of the fixed income portfolio.
- The fixed income portfolio's duration is to be targeted within plus or minus 20 percent of the duration of the portfolio's performance benchmark, the Barclays Capital Universal Index.

Target Allocations for the Fixed Income Sectors:

Range	
U.S. Treasuries and Government Agencies	10% – 45%
Credit Bonds	10% – 60%
Asset Backed Securities	0% – 10%
Commercial Mortgage Backed Securities	0% – 10%
Mortgage Backed Securities	5% – 45%

Private Equity Investing

The Retirement Funds can invest in any appropriate private equity investment opportunity which has the potential for returns superior to traditional investment opportunities and which is not prohibited by the WSIB's policies or by law. These investment types are generally divided into venture capital, corporate finance, growth equity, special situations, distressed, mezzanine, and other investments. Private equity investments are made either through limited partnership or direct investment vehicles.

The objective of the portfolio is to achieve superior total returns compared to traditional asset classes and is diversified away from traditional capital market risks. The portfolio is managed to meet or exceed the returns of the Russell 3000 (lagged by one quarter) plus 300 basis points. To meet the return and plan objectives, the private equity portfolio has diversified investments in companies in a variety of growth stages. The portfolio also includes a broad cross-section of opportunities in different industries and geographic regions.

Real Estate Program

The WSIB's real estate program is an externally managed pool of selected partnership investments, intended to provide alternative portfolio characteristics when compared to traditional stock and bond investments. The majority of the WSIB's partnerships invest in institutional-quality real estate assets that are leased to third parties. The combination of income generated from bond-like lease payments, coupled with the hard asset qualities of commercial real estate, combine to generate returns that are expected to fall between the return expectations for fixed income and equities over the long term. The real estate portfolio is managed to deliver risk-adjusted returns that are consistent with the WSIB's long-term return expectations for the asset class. The Retirement Fund's real estate partnerships typically invest in private real estate assets that are held for long-term income and appreciation. Many of the Retirement Fund's investment partnerships do not involve co-investment with other financial entities, thereby providing the WSIB with control provisions, related transactions, and ongoing operational decisions for annual capital expenditures.

Volatility including the real estate portfolio is minimized through a combination of factors. First, the majority of the Retirement Fund's partners own real estate assets in a private investment form which are not subject to public market volatility. Secondly, real estate capital is diversified among a host of partners with varying investment styles. Thirdly, partnership assets are invested in numerous economic regions, including foreign markets, and in various property types. Finally, Retirement Fund's partners invest at different points within the properties' capital structure and life cycle.

The WSIB's current benchmark for real estate seeks to earn an 8 percent annual investment return over a rolling 10-year period.

Innovation Portfolio

The innovation portfolio investment strategy is to provide WSIB with the ability to invest in assets that fall outside of traditional asset classes and to provide the WSIB with comfort and demonstrated success before committing large dollar amounts to the strategy. The overall benchmark for the innovation portfolio is the weighted average of the underlying benchmark for each asset in the portfolio.

Currently, there are three investment strategies in the innovation portfolio, two involving private partnerships and one investing in public equities. Their individual holdings have been presented according to asset class on the Statement of Net Assets.

Tangible Assets

The primary goal of the tangible asset portfolio is to generate a long-term, high quality, stable income stream. The secondary goal is to generate appreciation approximately commensurate with inflation. The structure of the investments are primarily targeted to those funds, separate accounts, or tangible asset operating companies providing the WSIB with the most robust governance provisions related to acquisition, dispositions, debt levels, and ongoing operational decisions for annual capital expenditures. The tangible asset portfolio invests in a number of sectors, but the primary focus is infrastructure, timber, and natural resource rights (oil and natural gas).

The WSIB's current return objective for tangible assets calls for a target benchmark of 4 percent above the U.S. Consumer Price Index over a long-term investment horizon defined as at least five years.

Schedule 1: Schedule of Maturities and Credit Quality

		Maturity					
Investment Type	Total Fair Value	Less than 1 year	1-5 years	6-10 years	More than 10 years	Effective Duration	Credit Rating
Asset Backed Securities	$ 20,132,797	$ -	$ 20,113,108	$ -	$ 19,689	0.05	Sched 2
Residential Mortgage Backed Securities	1,828,200,237	407,760,269	1,420,378,781	61,187	-	1.68	Sched 2
Commercial Mortgage Backed Securities	233,568,624	-	233,568,624	-	-	3.25	Sched 2
Corporate Bonds Domestic (USD)	980,533,946	-	195,683,148	615,398,216	169,452,582	5.89	Sched 2
Corporate Bonds Domestic (Non USD)	62,170,874	-	62,170,874	-	-	1.86	Sched 2
Corporate Bonds Foreign (USD)	3,881,367,338	15,936,500	659,953,966	2,576,568,812	628,908,060	6.68	Sched 2
Corporate Bonds Foreign (Non USD)	160,521,171	-	73,554,559	55,812,350	31,154,262	5.21	Sched 2
US Government Treasuries	3,282,516,441	300,743,015	2,175,806,946	805,966,480	-	3.79	Aaa
Foreign Government and Agencies (USD)	1,122,852,963	-	135,001,338	829,061,496	158,790,129	6.39	Sched 2
Foreign Government and Agencies (Non USD)	619,042,677	-	154,595,937	285,694,286	178,752,454	6.05	Sched 2
Supranational Securities (Non USD)	379,991,542	7,563,204	271,936,735	100,491,603	-	3.32	Aaa
Total Retirement Funds Investment Categorized	12,570,898,610	$ 732,002,988	$ 5,402,764,016	$ 5,269,054,430	$ 1,167,077,176		
Investments Not Required to be Categorized							
Corporate Stock - U.S. Dollar Denominated	2,917,446,095						
Corporate Stock - Non U.S. Dollar Denominated	9,557,039,592						
Commingled Equity Index Funds	9,914,679,373						
Alternative Investments	25,514,273,415						
Liquidity	1,500,573,033						
Total Investments Not Categorized	49,404,011,508						
Total Investments	$ 61,974,910,118						

Schedule 2: Additional Credit Rating Disclosures

Investment Type	Total Fair Value	Moody's Equivalent Credit Rating										
		Aaa	Aa1	Aa2	Aa3	A1	A2	A3	Baa1	Baa2	Baa3	Ba1 or Lower
Asset Backed Securities	$ 20,132,797	$ 20,113,108	$ 19,689	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -
Commercial Mortgage Backed Securities	233,568,624	189,359,114	-	-	44,209,510	-	-	-	-	-	-	-
Residential Mortgage Backed Securities	1,828,200,237	1,810,712,966	-	2,205,671	-	-	15,281,600	-	-	-	-	-
Corporate Bonds Domestic (USD)	980,533,946	-	-	-	57,490,148	22,032,825	189,905,785	49,639,785	207,127,612	205,089,633	66,946,468	182,301,690
Corporate Bonds Domestic (Non USD)	62,170,874	-	-	-	-	-	21,902,351	-	-	40,268,523	-	-
Corporate Bonds Foreign (USD)	3,881,367,338	-	-	28,541,000	16,479,450	62,278,480	65,031,300	334,750,385	513,424,935	949,835,339	1,072,689,230	838,337,219
Corporate Bonds Foreign (Non USD)	160,521,171	-	-	-	-	10,272,837	31,154,261	32,401,100	21,219,744	20,758,503	44,714,726	-
Foreign Government and Agencies (USD)	1,122,852,963	-	18,408,322	28,825,000	63,094,208	285,193,146	24,132,150	25,617,500	49,459,150	281,266,447	285,937,040	60,920,000
Foreign Government and Agencies (Non USD)	619,042,677	169,111,715	22,018,893	-	-	24,509,596	42,494,425	68,517,270	25,857,857	105,861,973	105,145,688	55,525,260
Total	$ 8,908,390,627	$ 2,189,296,903	$ 40,446,904	$ 59,571,671	$ 181,273,316	$ 404,286,884	$ 389,901,872	$ 510,926,040	$ 817,089,298	$ 1,603,080,418	$ 1,575,433,152	$ 1,137,084,169

Schedule 3: Foreign Currency Exposure by Country

Foreign Currency Denomination	Investment Type In U.S. Dollar Equivalent							
	Currency	Fixed Income	Corporate Stock	Commingled Index Funds	Private Equity	Real Estate	Total	Percent of Total Retirement Funds Investments
Australia-Dollar	$ 1,663,441	$ 387,973,188	$ 556,210,238	$ -	$ -	$ 24,673,974	$ 970,520,841	1.6%
Brazil-Real	323,455	295,386,753	119,276,563	-	-	-	414,986,771	0.7%
Canada-Dollar	4,241,232	-	742,339,744	-	-	-	746,580,976	1.2%
Denmark-Krone	1,808,181	-	105,051,404	-	-	-	106,859,585	0.2%
E.M.U.-Euro	21,940,552	-	2,314,191,440	-	2,112,224,517	168,631,717	4,616,988,226	7.4%
Hong Kong-Dollar	2,602,006	-	388,007,391	-	-		390,609,397	0.6%
India - Rupee	-	123,751,904	83,881,369	-	-	-	207,633,273	0.3%
Indonesia-Rupiah	679,301	71,416,790	61,284,389	-	-	-	133,380,480	0.2%
Japan-Yen	21,097,598	-	1,576,982,179	-	-	-	1,598,079,777	2.6%
Malaysia-Ringgit	2,379,308	68,517,270	25,812,639	-	-	-	96,709,217	0.2%
Mexico-Peso	218,002	57,012,118	41,567,077	-	-	-	98,797,197	0.2%
Singapore-Dollar	1,576,343	-	141,507,565	-	-	-	143,083,908	0.2%
South Korea-Won	500	-	151,774,154	-	-	-	151,774,654	0.2%
Sweden-Krona	2,126,331	-	240,710,209	-	1,654,326	-	244,490,866	0.4%
Switzerland-Franc	2,281,658	-	682,056,710	-	-	-	684,338,368	1.1%
Turkey-Lira	-	62,981,976	40,291,174	-	-	-	103,273,150	0.2%
United Kingdom - Pound	25,144,153	-	1,956,768,877	-	4,173,799	-	1,986,086,829	3.2%
Other - Miscellaneous	3,431,973	154,686,265	329,326,470	-	-	-	487,444,708	0.8%
	91,514,034	1,221,726,264	9,557,039,592	-	2,118,052,642	193,305,691	13,181,638,223	21.3%
Foreign Investments Denominated in U.S. Dollars	-	5,004,220,301	826,985,815	1,633,503,105	3,459,896,184	2,309,795,259	13,234,400,664	21.4%
	$ 91,514,034	$ 6,225,946,565	$ 10,384,025,407	$ 1,633,503,105	$ 5,577,948,826	$ 2,503,100,950	$ 26,416,038,887	42.7%

PETERSON SULLIVAN LLP
CERTIFIED PUBLIC ACCOUNTANTS
601 UNION STREET, SUITE 2300
SEATTLE, WASHINGTON 98101
TEL 206.382.7777 • FAX 206.382.7777
http://www.pscpa.com

INDEPENDENT AUDITORS' REPORT

To the Members of the Washington State Investment Board

Olympia, Washington

We have audited the accompanying statement of net assets for the Labor & Industries' Funds of the State of Washington as managed by the Washington State Investment Board ("the Labor & Industries' Funds") as of June 30, 2012, and the related statement of changes in net assets for the year then ended. These financial statements are the responsibility of the Washington State Investment Board's management. Our responsibility is to express an opinion on these financial statements based on our audit.

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

The financial statements referred to in the first paragraph present only the investment activity of the Labor & Industries' Funds as managed by the Washington State Investment Board. The financial statements do not purport to, and do not, present the financial activity of the Department of Labor & Industries of the State of Washington. Further, they do not purport to, and do not, present the financial activity of the Washington State Investment Board or of the State of Washington.

In our opinion, the financial statements referred to in the first paragraph present fairly, in all material respects, the net assets of the Labor & Industries' Funds as of June 30, 2012, and the changes in net assets for the year then ended in conformity with accounting principles generally accepted in the United States.

Accounting principles generally accepted in the United States require that the management's discussion and analysis preceding the financial statements be presented to supplement the financial statements. Such information, although not a part of the financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the financial statements in an appropriate operational, economic, or historical context. 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 financial statements, and other knowledge we obtained during our audit of the 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. The introduction section of the annual report has not been subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we do not express an opinion or provide any assurance on it.

/S/ PETERSON SULLIVAN LLP

October 25, 2012

MANAGEMENT DISCUSSION AND ANALYSIS

Management's Discussion and Analysis for the Labor & Industries' Funds of Washington state (L&I Funds), managed by the Washington State Investment Board (WSIB), is presented as an introduction to the financial statements. It is meant to assist the reader in understanding the financial statements by providing an overall review of the financial activities during the year as well as to provide a comparison to the prior year's activities and results. The WSIB manages funds for other Washington state departments. This section represents only the L&I Funds portion. The L&I Funds are the second largest pool of investments managed by the WSIB.

The financial statements and footnotes follow this section of the report. The Statement of Net Assets provides information on the types of investments and the liabilities of the L&I Funds. This information is summarized in Table 1. Table 1 also compares the asset, liability, and net asset balances at June 30, 2012, with those at June 30, 2011. The Statement of Changes in Net Assets provides information on investment performance and other increases and decreases in the net assets of the L&I Funds for the year ended June 30, 2012. This information is summarized in Table 2. Table 2 also compares the financial activities of the L&I Funds for the year ended June 30, 2012, with those of the year ended June 30, 2011. The Notes to the Financial Statements provide additional information that is essential to a full understanding of the data provided in the financial statements of the L&I Funds.

As shown in Table 1, the net assets of the L&I Funds increased by $834.8 million during the fiscal year ended June 30, 2012. Interest and other net investment income reinvested in the fund totaled $482.1 million. Net realized and unrealized gains for the year increased net assets by $527.5 million. Distributions to L&I reduced net assets by $(174.8) million.

The following summarizes the changes within each grouping listed within Table 1:

- Money market funds decreased by $(22.2) million. This cash balance represents less than 1 percent of total invested balances and is within policy targets. Cash can fluctuate within policy targets from year to year depending on trading volumes and the cash needs of the L&I Funds. Net investment income received from all asset classes is reinvested into money market funds and used within each asset class to reinvest in longer term securities as the cash becomes available. In addition, the net withdrawals by L&I were funded entirely from earnings deposited to money market funds.
- Fixed income securities increased by $890.3 million. Realized and unrealized gains due to favorable market conditions increased this asset class by $594.6 million. The return for the current fiscal year for TIPS was 12.0 percent. Other fixed income securities returned 9.4 percent. Total fixed income return for the fiscal year end was 8.1 percent. The remaining increase was due to net investment income retained within the fixed income portfolio and reinvested long term. During the current fiscal year, the fixed income portfolio was rebalanced and approximately $30 million was transferred out of the TIPS portfolio and reinvested in other fixed income securities.
- Equity investments decreased by $(59.0) million. Net realized and unrealized losses decreased equities by $(67.1) million due to negative investment returns in the equity markets. The equity portfolio returned (3.6) percent for the current fiscal year. The remaining increase in equity balances was due to net investment income retained within the equity portfolio and reinvested long term. During the current fiscal year, the equity portfolio was rebalanced and approximately $62 million was transferred from the US equity mandate to a global equity strategy.
- Collateral held and obligations under securities lending agreements decreased by $(2.2) billion. The L&I funds recalled all outstanding loans as of June 30, 2012, in anticipation of the asset transfer to the new custodian bank effective July 1, 2012.
- Investment receivables remained consistent from the prior year. The average fixed income coupon payment remained stable during the current fiscal year resulting in marginal change in balances.
- Investments payable decreased by $(24.9) million due to an decrease in pending trades payable, which is a function of open trades as of a specific point in time. This balance can fluctuate a great deal from period to period based on trading strategies, asset allocation, and market movements.

TABLE 1 - SUMMARIZED NET ASSETS	2012	2011	DOLLAR CHANGE	PERCENT CHANGE
Money Market Funds	$119,899,904	$142,101,181	$(22,201,277)	-15.6%
Fixed Income Investments	11,621,705,988	10,731,372,589	890,333,399	8.3%
Equity Investments	1,580,216,024	1,639,241,643	(59,025,619)	-3.6%
Total Investments	**13,321,821,916**	**12,512,715,413**	**809,106,503**	**6.5%**
Collateral Held Under Securities Lending Agreements	-	2,217,078,142	(2,217,078,142)	-100.0%
Investment Receivables - Other	109,788,984	109,028,392	760,592	0.7%
Total Assets	**13,431,610,900**	**14,838,821,947**	**(1,407,211,047)**	**-9.5%**
Obligations Under Securities Lending Agreements	-	2,217,078,142	(2,217,078,142)	-100.0%
Investment Payables - Other	144,820	25,067,513	(24,922,693)	-99.4%
Total Liabilities	**144,820**	**2,242,145,655**	**(2,242,000,835)**	**-100.0%**
Net Assets	**$13,431,466,080**	**$12,596,676,292**	**$834,789,788**	**6.6%**

As shown in Table 2, the net amount withdrawn by L&I decreased by $(175.9) million. Net premiums collected by L&I increased due to an increase in the hours reported by employers and calendar year 2011 rate changes. In addition, benefit payments to insured individuals decreased during the current fiscal year requiring less cash to cover benefit payments.

Net investment income increased from the prior fiscal year by $27.8 million due almost entirely from the increase in the net realized and unrealized gains and loss balances from the prior year. The increases in these balances were a result of positive returns within each of the individual L&I Funds as follows: Accident Fund 8.5 percent, Medical Aid Fund 7.3 percent, Pension Reserve Fund 8.6 percent, and the Supplemental Pension Fund .6 percent. The fixed income portfolio experienced significant appreciation due to the market environment during the current fiscal year. Bond yields decreased causing the bond markets to rally. Securities lending broker commissions decreased by $(2.8) million due to a tightening of the spreads paid to brokers in the current lending environment for the securities L&I has available to lend.

The fair value of L&I assets is directly impacted by the returns of the various capital markets within which the WSIB invests. The returns are expected to have a significant effect on financial position and results of operations in the future. However, one of the benefits of the diversification gained by investing across various investment types as well as broadly within an asset class is the reduction in aggregate volatility of the total investment portfolio. The WSIB, upon receiving recommendations from L&I staff, WSIB staff, and other investment experts, makes the asset allocation decisions for the L&I assets. Staff rebalances the L&I Funds' assets between asset classes as markets move pursuant to WSIB policy.

TABLE 2 - SUMMARIZED CHANGES IN NET ASSETS	2012	2011	DOLLAR CHANGE
Net Investment Income			
Interest, Dividends and Other Investment Income	$488,915,503	$501,470,619	$(12,555,116)
Net Realized Capital Gains	547,773,298	68,767,391	479,005,907
Unrealized Gains (Losses)	(20,280,790)	421,234,255	(441,515,045)
Less:			
Securities Lending Broker Rebates and Management Fees	(2,773,072)	(5,528,523)	(2,755,451)
Investment Expenses	(1,804,151)	(1,690,588)	113,563
WSIB Operating Expenses	(2,194,602)	(2,379,598)	(184,996)
Net Investment Income	**1,009,636,186**	**981,873,556**	**27,762,630**
Net Amount Withdrawn	(174,846,398)	(350,734,014)	(175,887,616)
Net Assets - Beginning	**12,596,676,292**	**11,965,536,750**	**631,139,542**
Net Assets - Ending	**$13,431,466,080**	**$12,596,676,292**	**$834,789,788**

L&I Funds Statement of Net Assets - June 30, 2012

See notes to financial statements

	Accident Fund	Medical Aid Fund	Pension Reserves Fund	Supplemental Pension Fund	Total	Percent of Total
ASSETS						
Investments:						
LIQUIDITY:						
Money Market Funds	$ 31,202,357	$ 6,728,118	$ 44,280,725	$ 37,688,704	$ 119,899,904	0.9%
FIXED INCOME INVESTMENTS:						
Residential Mortgage Backed Securities	766,370,194	518,705,997	458,710,178	22,701	1,743,809,070	
Commercial Mortgage Backed Securities	166,013,949	144,535,971	118,678,292	-	429,228,212	
Corporate Bonds - Domestic	1,155,448,538	940,028,621	1,076,487,629	19,291,562	3,191,256,350	
Corporate Bonds - Foreign (USD)	960,085,561	719,096,151	777,313,895	7,069,574	2,463,565,181	
Foreign Government and Agencies (USD)	388,594,490	233,189,390	316,008,364	4,057,640	941,849,884	
Supranational Securities (USD)	69,117,781	79,318,954	36,344,035	-	184,780,770	
U.S. Government Treasuries	296,361,899	210,248,110	241,085,303	29,989,400	777,684,712	
U.S. Treasury Inflation Protected Securities	538,933,502	989,292,342	361,305,965	-	1,889,531,809	
Total Fixed Income Investments	4,340,925,914	3,834,415,536	3,385,933,661	60,430,877	11,621,705,988	87.2%
EQUITY INVESTMENTS:						
Commingled Index Funds - Domestic	283,787,165	442,505,632	225,103,407	-	951,396,204	
Commingled Index Funds - Foreign	187,007,478	292,419,305	149,393,037	-	628,819,820	
Total Equity Investments	470,794,643	734,924,937	374,496,444	-	1,580,216,024	11.9%
Total Investments	4,842,922,914	4,576,068,591	3,804,710,830	98,119,581	13,321,821,916	100.0%
Investment Earnings Receivable	41,341,210	34,426,795	33,849,295	165,509	109,782,809	
Receivable for Investments Sold	2,524	2,516	1,135	-	6,175	
Total Assets	4,884,266,648	4,610,497,902	3,838,561,260	98,285,090	13,431,610,900	
LIABILITIES						
Accounts Payable	46,054	58,484	31,822	8,460	144,820	
Payable for Investments Purchased	-	-	-	-	-	
Total Liabilities	46,054	58,484	31,822	8,460	144,820	
NET ASSETS	$ 4,884,220,594	$ 4,610,439,418	$ 3,838,529,438	$ 98,276,630	$ 13,431,466,080	

L&I Funds Statement of Changes in Net Assets - Year ended June 30, 2012

See notes to financial statements

	Accident Fund	Medical Aid Fund	Pension Reserves Fund	Supplemental Pension Fund	Total
Net Investment Income					
Investment Income:					
Interest, Dividends and Other Investment Income	$ 183,696,415	$ 149,026,309	$ 147,879,930	$ 406,990	$ 481,009,644
Securities Lending Income	2,585,092	3,502,568	1,798,846	19,353	7,905,859
Realized Capital Gains	164,209,066	316,283,600	69,562,537	2,105	550,057,308
Realized Capital Losses	(777,889)	(975,144)	(530,818)	(159)	(2,284,010)
Unrealized Gains and Losses	36,204,888	(148,285,772)	91,648,704	151,390	(20,280,790)
Less:					
Securities Lending Broker Rebates and Management Fees	(908,648)	(1,237,139)	(621,027)	(6,258)	(2,773,072)
Investment Expenses	(683,988)	(581,409)	(418,196)	(120,558)	(1,804,151)
WSIB Operating Expenses	(794,395)	(759,675)	(627,989)	(12,543)	(2,194,602)
Net Investment Income	383,530,541	316,973,338	308,691,987	440,320	1,009,636,186
Residual Equity Transfer	40,000,000	-	(40,000,000)	-	-
Net Amount Contributed (Withdrawn)	(28,537,605)	(114,015,325)	(99,396,011)	67,102,543	(174,846,398)
Increase in Net Assets	394,992,936	202,958,013	169,295,976	67,542,863	834,789,788
Net Assets - June 30, 2011	4,489,227,658	4,407,481,405	3,669,233,462	30,733,767	12,596,676,292
Net Assets - June 30, 2012	$ 4,884,220,594	$ 4,610,439,418	$ 3,838,529,438	$ 98,276,630	$ 13,431,466,080

NOTES TO FINANCIAL STATEMENTS

Note 1. Description of Funds and Significant Accounting Policies

Description of Funds

The L&I Funds consist mainly of the investment of insurance premiums collected from employers in the state of Washington. The financial statements present only the activity of the L&I Funds as managed by the WSIB. The WSIB has exclusive control of the investments held by the L&I Funds. The financial statements do not present the financial position and results of operations of the WSIB or L&I.

Basis of Accounting

The accompanying financial statements have been prepared in conformity with accounting principles generally accepted in the United States for governments prescribed by the Governmental Accounting Standards Board (GASB) on the accrual basis of accounting.

Valuation of Investments

Investments are reported at fair value. Fair values are based on published market prices, quotations from national security exchanges, and security pricing services. Investments are adjusted to fair values monthly. Unrealized gains and losses are included as investment income in the Statement of Changes in Net Assets.

Revenue Recognition

Interest and dividend income are recognized when earned. Capital gains and losses are recognized on a trade date basis. Purchases and sales of investments are also recorded on a trade-date basis.

Securities Lending

The L&I Funds record collateral received under securities lending agreements where the L&I Funds have the ability to spend, pledge, or sell the collateral without borrower default. Liabilities resulting from these transactions are also recorded. Additionally, costs associated with securities lending transactions, including broker commissions paid and lending fees paid to the custodian bank, are reported as investment expenses in the accompanying financial statements. The Statement of Net Assets does not include detailed holdings of securities lending collateral by investment classification.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Actual results could differ from the estimated amounts.

Contributions and Withdrawals

Contributions and withdrawals are recorded when received or paid.

Note 2. Fees and Expenses

Investment fees and expenses are accounted for as a reduction of investment income or are netted directly from the asset value of the L&I Fund's investments. These fees include investment management fees and commissions, investment consultant fees, legal fees, and other investment management related expenses. The WSIB operating expenses are charged to the funds based upon actual costs incurred to manage the investments. WSIB operating expenses are allocated to the funds under management based on relative market values, in accordance with state statutes.

Note 3. Deposit and Investment Risk Disclosures

Custodial Credit Risk – Deposits

Custodial credit risk for deposits is the risk that in the event of a bank failure the L&I Fund's deposits may not be returned to it. The L&I Funds do not have a deposit policy for custodial credit risk. As of June 30, 2012, there were no deposits with the custodial bank.

Custodial Credit Risk – Investments

Custodial credit risk for investments is the risk that, in the event of a failure of the counterparty to a transaction, the L&I Funds will not be able to recover the value of investments that are in the possession of an outside party. The L&I Funds mitigate custodial credit risk by having its investment securities held by its custodian. Also, investment securities are registered in the name of the Washington State Investment Board for the benefit of the L&I Funds, excluding cash and cash equivalents and repurchase agreements held as securities lending collateral.

Interest Rate Risk

Interest rate risk is the risk that changes in interest rates over time will adversely affect the fair value of an investment. Effective duration is the measure of a debt investment's exposure to fair value changes arising from changes in interest rates. Effective duration uses the present value of cash flows, weighted for those flows as a percentage of the investment's full price. Increases in prevailing interest rates generally translate into decreases in fair values of those investments. As of June 30, 2012, the L&I Funds' portfolio durations were within the duration targets documented in Note 6.

Schedule 1 provides information about the interest rate risks associated with the L&I Funds' investments as of June 30, 2012. The schedule displays various asset classes held by maturity in years, effective durations, and credit ratings. Residential mortgage backed, commercial mortgage backed, and asset backed securities are reported using the average life within the portfolio. The average life is a calculated estimate of the average time (in years) until maturity for these securities taking into account possible prepayments of principal. All other securities on this schedule are reported using the stated maturity date.

Credit Risk

Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. The L&I Funds' rated debt investments as of June 30, 2012, were rated by Moody's and/or an equivalent national rating organization. Investment types with multiple ratings are presented in Schedule 2 using the Moody's rating scale.

Concentration of Credit Risk

Concentration of credit risk is the risk of loss attributed to the magnitude of an investment in a single issuer. The L&I Funds' policy states that corporate fixed income issue's cost shall not exceed 3 percent of the fund's fair value at the time of purchase, nor shall its fair value exceed 6 percent of the fund's fair value at any time. There was no concentration of credit risk as of June 30, 2012.

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 L&I Funds do not have a formal policy to limit foreign currency risk. The only security held by the L&I Funds with foreign currency risk at June 30, 2012, consists of $628,819,820 invested in an international commingled equity index fund.

Note 4. Securities Lending

State law and WSIB policy permit the L&I Funds to participate in securities lending programs to augment investment income. The WSIB has entered into an agreement with JPMorgan to act as agent for the WSIB in securities lending transactions. As JPMorgan is the custodian bank for the WSIB, it is counterparty to securities lending transactions.

The L&I Funds report securities lent (the underlying securities) as assets in the Statement of Net Assets. Cash received as collateral on securities lending transactions and investments made with that cash are reported as assets. Securities received as collateral are reported as assets if the L&I Funds have the ability to pledge or sell them without a borrower default. Liabilities resulting from these transactions are also reported in the Statement of Net Assets. Securities lending transactions collateralized by securities that the L&I Funds do not have the ability to pledge or sell unless the borrower defaults are not reported as assets and liabilities.

In anticipation of the custodian bank conversion on July 1, 2012, the L&I funds recalled all securities on loan. There were no assets on loan at June 30, 2012, and no collateral held related to securities lending transactions.

Fixed income securities were loaned and collateralized by the L&I Funds' agent with cash and U.S. Government Securities (exclusive of mortgage backed securities and letters of credit), and irrevocable letters of credit. When the loaned securities had collateral denominated in the same currency, the collateral requirement was 102 percent of the fair value, including accrued interest, of the securities loaned. All other securities were required to be collateralized at 105 percent of the fair value, including accrued interest, of the loaned securities.

During fiscal year 2012, securities lending transactions could be terminated on demand by either the L&I Funds or the borrower. The weighted average maturity of loans for 2012 was 1.5 days. Cash collateral was invested by the L&I Funds' in the WSIB's short-term investment pool. Because the securities lending agreements were terminable at will, their duration did not generally match the duration of the investments made with the cash collateral. Non-cash collateral could not be pledged or sold absent borrower default. There are no restrictions on the amount of securities that can be lent.

Securities were lent with the agreement that they would be returned in the future for exchange of the collateral. JPMorgan indemnified the WSIB by agreeing to purchase replacement securities or return the cash collateral in the event a borrower failed to return the loaned securities or pay distributions thereon. JPMorgan's responsibilities included performing appropriate borrower and collateral investment credit analyses, demanding adequate types and levels of collateral, and complying with applicable federal regulations concerning securities lending.

During fiscal year 2012, there were no significant violations of legal or contractual provisions, no failures by any borrowers to return loaned securities or to pay distributions thereon. Further, the L&I Funds incurred no losses during fiscal year 2012 resulting from a default by either the borrowers or the securities lending agents.

Note 5. Derivatives

L&I Funds are authorized to utilize various derivative financial instruments, including mortgage backed securities, financial futures, forward contracts, interest rate and equity swaps, and options to manage its exposure to fluctuations in interest and currency rates while increasing portfolio returns. Derivative transactions involve, to varying degrees, market and credit risk. L&I Funds mitigate market risks arising from derivative transactions by requiring collateral in cash and investments to be maintained equal to the securities positions outstanding, and thereby prohibiting the use of leverage or speculation. Credit risks arising from derivative transactions are mitigated by selecting and monitoring creditworthy counterparties and collateral issuers.

Consistent with the L&I Funds' authority to invest in derivatives, international active equity managers may make limited investments in financial futures, forward contracts or other derivative securities to manage exposure to currency rate risk and equitize excess cash holdings. No such derivative securities were held as of June 30, 2012. Domestic and foreign passive equity index fund managers may also utilize various derivative securities to manage exposure to risk and increase portfolio returns. Information on the extent of use and holdings of derivative securities by passive equity index fund managers is unavailable. At June 30, 2012, the only derivative securities held directly by L&I Funds were collateralized mortgage obligations of $1,743,172,909.

Note 6. Summary of Investment Policy

Under RCW 43.33A.030, Trusteeship of the L&I Funds is vested in the voting members of the WSIB. The Legislature has established a standard of care for investment of these funds in RCW 43.33A.140. Additionally, the WSIB and its staff must comply with other state laws, such as the Ethics in Public Service Act, RCW 42.52, as it makes its investment decisions and seeks to meet the following investment objectives.

Strategic Objectives

In accordance with RCW 43.33A.110, these portfolios are to be managed to limit fluctuations in the industrial insurance premiums, and subject to this purpose, achieve a maximum return at a prudent level of risk. Based on this requirement, the order of the objectives shall be:

- Maintain the solvency of the funds;
- Maintain premium rate stability;
- Ensure sufficient assets are available to fund the expected liability payments; and
- Subject to those above, achieve a maximum return at a prudent level of risk.

Performance Objectives

The performance objectives are intended to provide the L&I Funds with a way to measure the success of this investment policy, the overall asset allocation strategy, and the implementation of that strategy over time. First and foremost, the performance of the investment portfolios shall be judged relative to the strategic objectives. With the first three criteria met, the actual rates of return of the portfolios will be compared to the Comparable Market Index (CMI) for each fund. The CMI's are developed and calculated with the goal to construct a hypothetical passive portfolio with the duration, asset allocation, and appropriate mix of fixed income sectors based on the individual targets for each L&I fund. The return for each fund's portfolio should not be significantly different from that of its CMI over the long term.

Portfolio Constraints

- All assets under the management of the WSIB are to be invested to maximize return at a prudent level of risk in accordance with RCW 43.33A.110 and RCW 43.33A.140, which state, in part, that the WSIB is to "...establish investment policies and procedures designed to attempt to limit fluctuations in industrial insurance premiums, and subject to this purpose, to maximize return at a prudent level of risk."
- No corporate fixed income issue's cost shall exceed 3 percent of the fund's fair value at the time of purchase, nor shall its fair value exceed 6 percent of the funds' fair value at any time (RCW 43.33A.140).

Asset Allocation

Fixed Income	TIPS	Equity
Accident Fund		
80%±4	10%±2	10%±2
Pension Reserve Fund		
80%±4	10%±2	10%±2
Medical Aid Fund		
65%±5	20%±3	15%±3
Supplemental Pension Fund		
100%	NA	NA

Asset allocation will be reviewed every 3-4 years, or sooner, if there are significant changes in funding levels or the liability durations.

Market conditions, funding status, and liability assumptions are dynamic, not static; therefore, WSIB staff meet quarterly with L&I staff to review the investment portfolio, the status of the funding levels, the liability durations and to evaluate the percentage of the supplemental pension fund that is to be considered non-cash.

Assets will be rebalanced across asset classes when the fair value of the assets falls outside the policy ranges. The timing of any rebalancing will be based on market opportunities, cash flows, and the consideration of transaction costs; therefore, they need not occur immediately.

Asset Class Structure

Asset class structure is established by the WSIB with guidelines for staff to move assets in order to achieve the Fund's overall objectives.

Equity

Equity Allocation	Target	Range
U.S. Equity	60%	55%-65%
International Equity	40%	35%-45%

The benchmark and structure for U.S. equities will be the broad U.S. stock market as defined by the MSCI US IMI passive mandate. The benchmark and structure for international equities will be the Morgan Stanley Capital International All Country World Ex U.S. Investable Market Index (MSCI ACW Ex U.S. IMI). Both portfolios will be 100 percent passively managed in commingled index funds. The commingled funds may use futures for hedging or establishing a long position.

Treasury Inflation Protection Securities

The treasury inflation protection securities (TIPS) will be managed to plus or minus 20 percent of the duration of the Barclays Capital U.S. TIPS Index.

Fixed Income

The fixed income portfolios' structure will vary widely among funds depending upon the required duration target.

Accident Fund (608): within plus or minus 20 percent of a duration target of 7.
Pension Reserve Fund (610): within plus or minus 20 percent of a duration target of 7.
Medical Aid Fund (609): within plus or minus 20 percent of a duration target of 6.
Supplemental Pension Fund (881): a duration of less than 2.

The duration targets will be reviewed every 3 years, or sooner, if there are significant changes in the funding levels or the liability durations.

It is the goal of the fixed income portfolios to match the target durations. Although there may be differences from the targets due to market conditions, over any extended period of time those differences should not be material.

Permissible Fixed Income Investments

- U.S. Treasuries and Government Agencies
- Credit Bonds
- Mortgage Backed Securities rated investment grade, as defined by Barclays Capital Global Family of Fixed Income Indices
- Asset Backed Securities rated investment grade, as defined by Barclays Capital Global Family of Fixed Income Indices
- Commercial Mortgage Backed Securities rated investment grade, as defined by Barclays Capital Global Family of Fixed Income Indices
- Investment Grade Non-U.S. Dollar Bonds

Sector Allocations

Sector Allocations are to be managed within the ranges presented below. These targets are long-term in nature. Deviations may occur in the short-term as a result of interim market conditions. However, if a range is exceeded, the portfolios must be rebalanced as soon as it is practical to the target allocations.

Target allocations for the Fixed Income Sectors:	
U.S. Treasuries and Government Agencies	5% - 25%
Credit Bonds	20% - 70%
Asset Backed Securities	0% - 10%
Commercial Mortgage Backed Securities	0% - 10%
Mortgage Backed Securities	0% - 25%

Total market value of below investment grade credit bonds (as defined by Barclays Capital Global Family of Fixed Income Indices) shall not exceed 5 percent of the total market value of the funds. Although below investment grade mortgage backed, asset backed and commercial mortgage backed securities may not be purchased, portfolio holdings that are downgraded to those levels or are no longer rated may continue to be held.

Total holdings of below investment grade credit bonds (as defined by Barclays Capital Global Family of Fixed Income Indices) should not exceed 5 percent of total fixed income holdings.

Schedule 1: Schedule of Maturities and Credit Ratings

Investment Type	Total Fair Value	Maturity: Less than 1 year	Maturity: 1-5 years	Maturity: 6-10 years	Maturity: More than 10 years	Effective Duration	Credit Rating
Residental Mortgage Backed Securities	$ 1,743,809,070	$ 25,142,535	$ 1,004,023,290	$ 667,980,334	$ 46,662,911	4.89	Aaa
Commercial Mortgage Backed Securities	429,228,212	30,322,500	377,785,768	21,119,944	-	3.29	Schedule 2
Corporate Bonds - Domestic	3,191,256,350	203,993,783	534,684,640	1,021,459,933	1,431,117,994	8.71	Schedule 2
Corporate Bonds - Foreign (USD)	2,463,565,181	267,206,251	439,805,709	814,804,425	941,748,796	7.65	Schedule 2
Foreign Government and Agencies(USD)	941,849,884	44,791,237	396,712,724	303,047,952	197,297,971	6.34	Schedule 2
Supranational Securities (USD)	184,780,770	45,792,050	138,988,720	-	-	2.85	Aaa
U.S. Government Treasuries	777,684,712	145,357,003	599,355,309	32,972,400	-	2.71	Aaa
U.S. Treasury Inflation Protected Securities	1,889,531,809	-	597,279,585	618,101,376	674,150,848	4.71	Aaa
	11,621,705,988	$ 762,605,359	$ 4,088,635,745	$ 3,479,486,364	$ 3,290,978,520		
Investments Not Required to be Categorized							
Commingled Index Funds-Domestic	951,396,204						
Commingled Index Funds-Foreign	628,819,820						
Money Market Funds	119,899,904						
Total Investments Not Categorized	1,700,115,928						
Total L&I Funds Investments	$ 13,321,821,916						

Schedule 2: Additional Credit Ratings Disclosures

Investment Type	Total Fair Value	Moody's Equivalent Credit Rating: Aaa	Aa1	Aa2	Aa3	A1	A2	A3	Baa1	Baa2	Baa3	Ba1 or Lower
Commercial Mortgage Backed Securities	$ 429,228,212	$ 332,934,517	$ -	$ -	$ 96,293,695	$ -	$ -	$ -	$ -	$ -	$ -	$ -
Corporate Bonds - Domestic	3,191,256,350	6,100,977	-	-	226,939,832	178,665,488	762,671,775	481,086,866	558,673,816	770,300,758	123,108,338	83,708,500
Corporate Bonds - Foreign (USD)	2,463,565,181	-	-	-	224,345,616	225,956,873	35,016,865	313,892,474	425,598,928	636,283,761	443,673,164	158,797,500
Foreign Government and Agencies (USD)	941,849,884	166,302,703	-	53,236,657	139,207,858	248,946,366	-	-	27,297,710	146,050,540	83,252,850	77,555,200
Total	$ 7,025,899,627	$ 505,338,197	$ -	$ 53,236,657	$ 686,787,001	$ 653,568,727	$ 797,688,640	$ 794,979,340	$ 1,011,570,454	$ 1,552,635,059	$ 650,034,352	$ 320,061,200

PETERSON SULLIVAN LLP

CERTIFIED PUBLIC ACCOUNTANTS
601 UNION STREET, SUITE 2300
SEATTLE, WASHINGTON 98101

TEL 206.382.7777 • FAX 206.382.7777
http://www.pscpa.com

INDEPENDENT AUDITORS' REPORT

To the Members of the Washington State Investment Board

Olympia, Washington

We have audited the accompanying statement of net assets for the Permanent Funds (Millersylvania Park, American Indian Scholarship Endowment, Agricultural School, Normal School, Common School, Scientific School, and State University) of the State of Washington as managed by the Washington State Investment Board ("the Permanent Funds") as of June 30, 2012, and the related statement of changes in net assets for the year then ended. These financial statements are the responsibility of the Washington State Investment Board's management. Our responsibility is to express an opinion on these financial statements based on our audit.

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

The financial statements referred to in the first paragraph present only the investment activity of the Permanent Funds as managed by the Washington State Investment Board. The financial statements do not purport to, and do not, present the financial activity of the Permanent Funds of other state agencies. Further, they do not purport to, and do not, present the financial activity of the Washington State Investment Board or of the State of Washington.

In our opinion, the financial statements referred to in the first paragraph present fairly, in all material respects, the net assets of the Permanent Funds as of June 30, 2012, and the changes in net assets for the year then ended in conformity with accounting principles generally accepted in the United States.

Accounting principles generally accepted in the United States require that the management's discussion and analysis preceding the financial statements be presented to supplement the financial statements. Such information, although not a part of the financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the financial statements in an appropriate operational, economic, or historical context. 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 financial statements, and other knowledge we obtained during our audit of the 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. The introduction section of the annual report has not been subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we do not express an opinion or provide any assurance on it.

/S/ PETERSON SULLIVAN LLP

October 25, 2012

MANAGEMENT DISCUSSION AND ANALYSIS

Management's Discussion and Analysis for the Permanent Funds of the state of Washington, managed by the Washington State Investment Board (WSIB), is presented as an introduction to the financial statements. It is meant to assist the reader in understanding the financial statements by providing an overall review of the financial activities during the year as well as to provide a comparison to the prior year's activities and results. The WSIB manages funds for other state of Washington agencies. This section of the report represents only the Permanent Funds portion.

The financial statements and footnotes follow this section of the report. The Statement of Net Assets provides information on the types of investments and the liabilities of the Permanent Funds. This information is summarized in Table 1. Table 1 also compares the asset, liability, and net asset balances at June 30, 2012, with those at June 30, 2011. The Statement of Changes in Net Assets provides information on investment performance and other increases and decreases in the net assets of the Permanent Funds for the year ended June 30, 2012. This information is summarized in Table 2. Table 2 also compares the financial activities of the Permanent Funds for the year ended June 30, 2012, with those of the year ended June 30, 2011. The Notes to the Financial Statements provide additional information that is essential to a full understanding of the data provided in the financial statements of the Permanent Funds.

As shown in Table 1, the net assets of the Permanent Funds increased by $39.2 million during the fiscal year ended June 30, 2012. Contributions from the Department of Natural Resources (DNR) and Higher Education Coordinating Board increased net assets by $10.1 million, which were invested in fixed income and equity securities. Unrealized gains in the fixed income portfolio totaled $23.6 million and the equity portfolio amounted to $5.9 million for a total net asset value increase of $29.5 million. Distributions to beneficiary funds reduced net assets by $(31.5) million. The remaining increase represents other net investment income within the portfolios.

The following summarizes the changes within each grouping listed within Table 1:

- Money market funds increased by $1.6 million. This cash balance represents less than 1 percent of total invested balances and is within policy targets. Cash is held to cover potential cash needs of DNR and to cover distributions to beneficiary funds and can fluctuate within policy targets. In addition, the permanent funds are in the process of rebalancing to a 30 percent equity target and is accumulating cash to invest in equities.
- Fixed income investments decreased by $(64.7) million. Unrealized gains for the year totaled $23.6 million, increasing fixed income net asset values. This gain is attributable to a decrease in fixed income yields of 71 basis points over the prior fiscal year which caused the bond markets to rally and valuations to increase. Transfers to equities decreased fixed income securities by $(96.2) million. The remaining decrease is comprised of distributions from the fund in excess of contributions and current earnings.
- Equity investments increased $102.4 million. A new commingled equity fund was started during the current fiscal year and balances transferred from fixed income totaled $96.2 million. The equity target allocation is 30 percent of total assets and will be funded over the next three years from bond maturities and contributions from the DNR. Unrealized gains increased net assets by $5.7 million. The remaining increase was due to income retained within the commingled equity fund. Distributions from the fund are on a quarterly basis.
- The prior year earnings receivable and distributions payable included large year-end capital gain distribution from the commingled bond fund which resulted in a decrease of $2.1 million in each of these balances from the prior fiscal year. In addition, the WSIB distributes income on a cash basis and fluctuations in balances from period to period would be normal depending on the timing of payments.

TABLE 1 - SUMMARIZED NET ASSETS	2012	2011	DOLLAR CHANGE	PERCENT CHANGE
Money Market Funds	$3,133,013	$1,514,519	$1,618,494	106.9%
Fixed Income Investments	786,533,877	851,254,240	(64,720,363)	(7.6%)
Equity Investments	114,124,758	11,759,131	102,365,627	870.5%
Total Investments	**903,791,648**	**864,527,890**	**39,263,758**	**4.5%**
Earnings Receivable	2,243,305	4,423,126	(2,179,821)	(49.3%)
Total Assets	**906,034,953**	**868,951,016**	**37,083,937**	**4.3%**
Distributions Payable	(2,243,781)	(4,408,370)	(2,164,589)	49.1%
Net Assets	**$903,791,172**	**$864,542,646**	**$39,248,526**	**4.5%**

As shown in Table 2, net investment income increased by $25.8 million, almost entirely due to the increase in unrealized gains. Current year fixed income investments, which comprise 87 percent of the net asset value of the funds, returned 6.6 percent during fiscal year ended June 30, 2012. This is a significant increase from the prior year return of 2.6 percent. The increase in fixed income returns is attributable to a decrease in fixed income yields which caused the bond market to rally and valuations to increase. In addition, the new commingled equity fund returned 5.6 percent from the inception date of June 1, 2012.

Contributions received from DNR decreased by $(2.7) million due to decreased prices and volume of timber sales during the current fiscal year.

Distributions to beneficiaries decreased by $12.6 million due to a decrease in current year distributable income and a one-time distribution of net capital gains which occurred in 2011. The average coupon rate during the current fiscal year remained steady, however current year interest earnings decreased due to the rebalancing from fixed income to equities and high cash balances maintained during the initial restructuring period. This resulted in $(2.5) million decrease in current year interest and distributable income.

The fair value of the Permanent Fund assets is directly impacted by the returns of the various capital markets within which the WSIB invests and the returns are expected to have a significant effect on financial position and results of operations in the future. However, one of the benefits of diversification gained by investing across various investment types as well as broadly within an asset class is the reduction in aggregate volatility of the total investment portfolio.

TABLE 2 - SUMMARIZED CHANGES IN NET ASSETS	2012	2011	DOLLAR CHANGE	PERCENT CHANGE
Net Investment Income				
Interest, Dividends and Other Investment Income	$31,306,472	$33,841,021	$(2,534,549)	(7.5%)
Realized Capital Gains (Losses)	(34,805)	622,003	(656,808)	(105.6%)
Unrealized Gains	29,521,408	559,190	28,962,218	5179.3%
Less:				
Investment Fees	(183,353)	(168,946)	14,407	8.5%
Net Investment Income	**60,609,722**	**34,853,268**	**25,756,454**	**73.9%**
Net Amount Contributed	10,089,582	12,744,842	(2,655,260)	(20.8%)
Distributions to Beneficiaries	(31,450,778)	(44,093,677)	(12,642,899)	(28.7%)
Net Assets - Beginning	**864,542,646**	**861,038,213**	**3,504,433**	**0.4%**
Net Assets - Ending	**$903,791,172**	**$864,542,646**	**$39,248,526**	**4.5%**

Permanent Funds Statement of Net Assets - June 30, 2012

See notes to financial statements

	Millersylvania Park	American Indian Scholarship Endowment	Agricultural School	Normal School	Common School	Scientific School	State University	Total	Percent of Total
ASSETS									
Investments:									
Money Market Funds	$ -	$ 6,190	$ 691,422	$ 883,004	$ 665,825	$ 773,134	$ 113,438	$ 3,133,013	0.4%
Commingled Monthly Bond Fund	-	363,790	174,373,852	222,760,258	165,486,768	194,979,041	28,570,168	786,533,877	87.0%
Commingled Monthly Equity Fund	-	-	23,552,837	29,287,468	31,793,269	25,834,868	3,656,316	114,124,758	12.6%
Total Investments	-	369,980	198,618,111	252,930,730	197,945,862	221,587,043	32,339,922	903,791,648	100.0%
Investment Earnings Receivable	-	992	495,796	632,667	478,854	553,941	81,055	2,243,305	
Total Assets	-	370,972	199,113,907	253,563,397	198,424,716	222,140,984	32,420,977	906,034,953	
LIABILITIES									
Distributions and Other Payables	-	-	496,215	633,134	478,981	554,342	81,109	2,243,781	
NET ASSETS	$ -	$ 370,972	$ 198,617,692	$ 252,930,263	$ 197,945,735	$ 221,586,642	$ 32,339,868	$ 903,791,172	

Permanent Funds Statement of Changes in Net Assets - Year Ended June 30, 2012

See notes to financial statements

	Millersylvania Park	American Indian Scholarship Endowment	Agricultural School	Normal School	Common School	Scientific School	State University	Total
Net Investment Income								
Investment Income:								
Interest, Dividends and Other Investment Income	$ 16	$ 13,905	$ 6,959,066	$ 8,876,720	$ 6,566,885	$ 7,752,631	$ 1,137,249	$ 31,306,472
Net Realized Capital Gains (Losses)	-	(494)	(1,235,764)	(275,238)	2,063,240	(516,610)	(69,939)	(34,805)
Unrealized Gains (Losses)	-	10,438	7,669,631	8,462,221	4,608,315	7,658,287	1,112,516	29,521,408
Less:								
Investment Expenses	(9)	(545)	(7,659)	(9,565)	(7,176)	(8,392)	(1,212)	(34,558)
WSIB Operating Expenses	-	-	(32,639)	(41,743)	(32,643)	(36,423)	(5,347)	(148,795)
Net Investment Income	7	23,304	13,352,635	17,012,395	13,198,621	14,849,493	2,173,267	60,609,722
Other Changes in Net Assets								
Net Amount Contributed	-	5,500	2,899,926	2,438,743	421,643	4,002,423	321,347	10,089,582
Withdrawals and Distributions	(5,152)	(315,766)	(6,938,338)	(8,825,789)	(6,526,882)	(7,708,113)	(1,130,738)	(31,450,778)
Increase (Decrease) in Net Assets	(5,145)	(286,962)	9,314,223	10,625,349	7,093,382	11,143,803	1,363,876	39,248,526
Net Assets - June 30, 2011	5,145	657,934	189,303,469	242,304,914	190,852,353	210,442,839	30,975,992	864,542,646
Net Assets - June 30, 2012	$ -	$ 370,972	$ 198,617,692	$ 252,930,263	$ 197,945,735	$ 221,586,642	$ 32,339,868	$ 903,791,172

NOTES TO FINANCIAL STATEMENTS

Note 1. Description of Funds and Significant Accounting Policies

Description of Funds

The Permanent Funds of the state of Washington include funds established by the State Enabling Act and funds created by private donation. Funds established by the State Enabling Act consist of the Agricultural School Permanent Fund, the Normal School Permanent Fund, the Common School Permanent Fund, the Scientific School Permanent Fund, and the State University Permanent Fund. Originally, land was granted to the state by the federal government at statehood to establish these permanent funds. The Permanent Funds consist of proceeds from sales of these lands and related natural resources. The proceeds from these sales are deposited by the Department of Natural Resources (DNR) in each respective Permanent Fund account for investment by the WSIB. The Permanent Fund known as the Millersylvania Park Permanent Fund was established in 1931 from a gift of cash and securities for the establishment, maintenance, and upkeep of the Millersylvania State Park. The balances in the Millersylvania Park Permanent Fund were transferred to the Office of the State Treasurer as the new investment manager pursuant to legislative changes during the current fiscal year. The American Indian Scholarship Endowment Fund was created in 1990 to help American Indian students obtain a higher education and currently contains only private donations. The matching funds appropriated by the state for this fund were also transferred to the Office of the State Treasurer pursuant to legislative changes during the current fiscal year.

The fixed income investments held by the Permanent Funds are commingled into one fund called the Commingled Monthly Bond Fund (CMBF). The equity investments held by the Permanent funds are commingled into one fund called the Commingled Monthly Equity Fund (CMEF). The Permanent Funds hold shares of the CMBF and the CMEF. The CMBF and CMEF comply with the Permissible Investments and Portfolio Constraints of the WSIB Permanent Funds investment policy. The asset classes held in the CMBF and CMEF are presented in Schedule 1 and Schedule 3 respectively.

The financial statements present only the activity of the Permanent Funds as managed by the WSIB. The WSIB has exclusive control of the investments held by the Permanent Funds. The financial statements do not present the financial position and results of operations of the WSIB.

Basis of Accounting

The accompanying financial statements have been prepared in conformity with accounting principles generally accepted in the United States for governments prescribed by the Governmental Accounting Standards Board (GASB) on the accrual basis of accounting.

Valuation of Investments

Investments are reported at fair value. Fair values are based on published market prices, quotations from national security exchanges, and security pricing services. Investments are adjusted to fair value monthly. Unrealized gains and losses are included as investment income in the Statement of Changes in Net Assets.

Revenue Recognition

Interest and dividend income is recognized when earned. Capital gains and losses are recognized on a trade-date basis. Purchases and sales of investments are also recorded on a trade date basis.

Contributions and Withdrawal Policy

Cash basis investment income is distributed to the beneficiary funds on a monthly or quarterly basis, depending on the policies of the underlying funds. Income distributed includes interest, dividends, capital gains, and capital losses received during the distribution period. Unrealized gains and losses are not distributed pursuant to state accounting policies and procedures. This is necessary to meet legal requirements regarding the preservation of capital.

Contributions are recorded when received.

Securities Lending

The Permanent Funds invest in the CMBF and the CMEF which holds the underlying securities and participates in lending activities. Each Permanent Fund owns shares in the CMBF and CMEF and does not directly participate in securities lending activities. Accordingly, the lending activity is not presented within each individual fund in the accompanying financial statements.

The collateral received under securities lending agreements, where the funds have the ability to spend, pledge, or sell the collateral without borrower default, is included in the CMBF and CMEF net assets. Liabilities resulting from these transactions are also included in each fund's net assets. Additionally, costs associated with securities lending transactions, including broker rebates and investment management fees paid, are part of the CMBF and CMEF and are not reported directly by the Permanent Funds. Securities lending income received by the CMBF and CMEF during fiscal year 2012 was $553,599. Securities lending expenses during the fiscal year totaled $197,686.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Actual results could differ from the estimated amounts.

Note 2. Fees and Expenses

Investment fees and expenses are accounted for as a reduction of investment income or are netted directly from the asset value of Permanent Funds, CMEF, and CMBF investments. These fees include investment management fees and commissions, investment consultant fees, legal fees, and other investment management related expenses. The WSIB operating expenses are charged to the funds based upon actual costs incurred to manage the investments. WSIB operating expenses are allocated to the funds under management based on relative market values, in accordance with state statutes.

Note 3. Deposit and Investment Risk Disclosures

Custodial Credit Risk – Deposits

Custodial credit risk for deposits is the risk that in the event of a bank failure the Permanent Funds deposits may not be returned to it. The Permanent Funds do not have a deposit policy for custodial credit risk. As of June 30, 2012, there were no deposits with the custodial bank.

Custodial Credit Risk – Investments

Custodial credit risk for investments is the risk that, in the event of a failure of the counterparty to a transaction, the Permanent Funds will not be able to recover the value of investments that are in the possession of an outside party. The Permanent Funds mitigates custodial credit risk by having its investment securities held by its custodian. Also, investment securities are registered in the name of the Washington State Investment Board for the benefit of the Permanent Funds, excluding cash and cash equivalents and repurchase agreements held as securities lending collateral.

Interest Rate Risk

Interest rate risk is the risk that changes in interest rates over time will adversely affect the fair value of an investment. Effective duration is the measure of a debt investment's exposure to fair value changes arising from changes in interest rates. Effective duration uses the present value of cash flows, weighted for those flows as a percentage of the investment's full price. Increases in prevailing interest rates generally translate into decreases in fair values of those investments.

Schedule 1 provides information about the interest rate risks associated with the CMBF investments as of June 30, 2012. The schedule displays various asset classes held by maturity in years, effective durations, and credit ratings. Residential mortgage backed, commercial mortgage backed, and asset backed securities are reported using the average life within the portfolio. The average life is a calculated estimate of the average time (in years) until maturity for these securities taking into account possible prepayments of principal. All other securities on this schedule are reported using the stated maturity date.

Credit Risk

Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. The Permanent Funds' CMBF rated debt investments as of June 30, 2012, were rated by Moody's and/or an equivalent national rating organization. Investment types with multiple ratings are presented in Schedule 2 using the Moody's rating scale.

Concentration of Credit Risk

Concentration of credit risk is the risk of loss attributed to the magnitude of an investment in a single issuer. The Permanent Funds' policy states that corporate fixed income issue's cost shall not exceed 3 percent of the fund's fair value at the time of purchase, nor shall its fair value exceed 6 percent of the fund's fair value at any time. There was no concentration of credit risk in the CMBF that exceeded these limits as of June 30, 2012.

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 Permanent Funds have no formal policy to limit foreign currency risk. Currently, the only foreign securities held by the CMBF are traded and denominated in U.S. dollars. The Permanent Funds had no investments with foreign currency risk exposure.

Note 4. Securities Lending

Washington state law and WSIB policy permit the Permanent Funds to participate in securities lending programs to augment investment income. The WSIB has entered into an agreement with JPMorgan to act as agent for the WSIB in securities lending transactions. As JPMorgan is the custodian bank for the WSIB, it is counterparty to securities lending transactions.

The CMBF rand CMEF report securities lent (the underlying securities) as assets. Securities lending activity is part of the commingled funds and, accordingly, is not reported directly by the Permanent Funds in the accompanying financial statements. The Permanent Funds own units in each fund, similar to a mutual fund. The commingled funds engage in all lending activity and report the net lending income activity within the fund as increases in the share price of each fund until distributed to the beneficiary funds. Cash received as collateral on securities lending transactions and investments made with the cash are reported as assets with an offsetting liability. Securities lending transactions collateralized by securities within each fund that do not have the ability to pledge or sell unless the borrower defaults are not reported as assets and liabilities.

Fixed income securities were loaned throughout the year and collateralized by the WSIB's agent with cash and U.S. Government Securities (exclusive of mortgage backed securities and letters of credit), and irrevocable letters of credit. When the loaned securities had collateral denominated in the same currency the collateral requirement was 102 percent of the fair value, including accrued interest, of the securities loaned. All other securities were required to be collateralized at 105 percent of the fair value, including accrued interest, of the loaned securities.

In anticipation of a change of custodian bank effective July 1, 2012, all securities on loan were recalled and there were no loans outstanding as of June 30, 2012.

Cash collateral was invested by the WSIB's agents in the WSIB's short-term investment pool or term loans. Because the securities lending agreements were terminable at will, their duration did not generally match the duration of the investments made with the cash collateral. Non-cash collateral could not be pledged or sold absent borrower default. There are no restrictions on the amount of securities that can be lent.

Securities were lent with the agreement that they would be returned in the future for exchange of the collateral. JPMorgan indemnified the WSIB by agreeing to purchase replacement securities or return the cash collateral in the event a borrower failed to return the loaned securities or pay distributions thereon. JPMorgan's responsibilities included performing appropriate borrower and collateral investment credit analyses, demanding adequate types and levels of collateral, and complying with applicable federal regulations concerning securities lending.

During fiscal year 2012, there were no significant violations of legal or contractual provisions, no failures by any borrowers to return loaned securities or to pay distributions thereon. Further, the commingled funds incurred no losses during fiscal year 2012 resulting from a default by either the borrowers or the securities lending agents.

Note 5. Derivatives

Permanent Funds are authorized to utilize various derivative financial instruments, including mortgage backed securities, financial futures, forward contracts, interest rate and equity swaps, and options to manage its exposure to fluctuations in interest and currency rates while increasing portfolio returns. Derivative transactions involve, to varying degrees, market and credit risk. Permanent Funds mitigate market risks arising from derivative transactions by requiring collateral in cash and investments to be maintained equal to the securities positions outstanding, and thereby prohibiting the use of leverage or speculation. Credit risks arising from derivative transactions are mitigated by selecting and monitoring creditworthy counterparties and collateral issuers.

Consistent with the Permanent Funds' authority to invest in derivatives, international active equity managers may make limited investments in financial futures, forward contracts or other derivative securities to manage exposure to currency rate risk and equitize excess cash holdings. No such derivative securities were held as of June 30, 2012. Domestic and foreign passive equity index fund managers may also utilize various derivative securities to manage exposure to risk and increase portfolio returns. Information on the extent of use and holdings of derivative securities by passive equity index fund managers is unavailable.

At June 30, 2012, the only derivative securities held directly by the Permanent Funds CMBF were collateralized mortgage obligations of $145,893,527.

Note 6. Summary of Investment Policy

Under RCW 43.33A.030, Trusteeship of the Permanent Funds is vested in the voting members of the WSIB. The Legislature has established a standard of care for investment of this fund in RCW 43.33A.140. Additionally, the WSIB and its staff must comply with other state laws, such as the Ethics in Public Service Act, 42.52 RCW, as it makes its investment decisions and seeks to meet the following investment objectives.

Strategic Objectives

The strategic objective for the permanent fund portfolios are to be managed to achieve the highest return possible, at a prudent level of risk, and consistent with the desire to emphasize high current yield to maturity opportunities and to add value through active management.

The strategic objectives include:

- Safety of principal;
- Current income;
- Long-term stability of purchasing power; and
- Preservation of the public's trust.

Taken together, these objectives imply portfolios for which growth keeps pace with inflation over time and that are able to provide a stable level of income sufficient to meet each fund's constituent needs while maintaining the corpus (or principal balances) of the funds.

Performance Objectives

In most cases, the permanent funds' investments are to emphasize stability and maximize income to support the operations of each permanent trust.

Within the required accounting guidelines, the permanent funds' portfolios are to be managed so that their individual performance meets or exceeds the return of each fund's specific benchmark with a volatility of returns that, over time, is similar to or less than the benchmark's for a similar level of returns.

Risk Tolerance

Risk will be managed in a prudent manner. Since the stakeholder only receives the current income adjusted for realized capital gains and losses, the funds have a below average ability to tolerate volatility in current income.

Portfolio Constraints

- All assets under management by the WSIB are to be invested to maximize return at a prudent level of risk in accordance with the requirements of statutes Chapter 43.33A.110 and 43.33A.140 RCW, which state, in part, that the WSIB is to "...establish investment policies and procedures designed to attempt to limit fluctuations in industrial insurance premiums, and, subject to this purpose, to maximize return at a prudent level of risk."
- No corporate fixed income issue's cost shall exceed 3 percent of the fund's market value at the time of purchase, nor shall its market value exceed 6 percent of the fund's market value at any time (Chapter 43.33A.140 RCW).

Permissible Investments

The eight permanent funds managed by the WSIB have differing legal investment restrictions. The following list is comprehensive and any restrictions to an individual fund will be listed separately.

- Any WSIB managed fund that meets a fund's investment objectives and its permissible investments constraints.
- U.S. and non-U.S. public equity.
- Investment Grade Fixed Income. Investment grade is defined using the method employed by the Barclays Capital Global Family of Fixed Income Indices. Although fixed income securities that are rated below investment grade may not be purchased, portfolio holdings that are downgraded to those levels or are no longer rated may continue to be held.

Permissible Fixed Income Market Segments:

- Government Securities
- Credit Bonds
- Mortgage Backed Securities
- Asset Backed Securities
- Commercial Backed Mortgage Securities
- Convertible Securities
- Eurodollar Bonds
- Non-Dollar Bonds

Other fixed income segments and instruments may be added from time to time as they are developed or deemed appropriate.

Fixed Income Sector Allocations

Portfolio allocations are to be managed within the ranges presented below. These targets are long term in nature. Deviations may occur in the short-term as a result of interim market conditions; however, if a range is exceeded, the portfolio must be rebalanced to the target allocations, as soon as it is practical.

Government Securities	10% – 50%
Credit Bonds	10% – 50%
Asset Backed Securities	0% – 10%
Commercial Mortgage Backed Securities	0% – 10%
Mortgage Backed Securities	5% – 40%
Total	100%

Duration Target

The fixed income portfolio's duration is to be targeted within plus or minus 20 percent of the duration of the portfolio's benchmark.

Asset Allocation and Benchmarking:

The Agricultural Permanent Fund, Normal School Permanent Fund, Permanent Common School Fund, Scientific University Permanent Fund, and the State University Permanent Fund have the following asset allocation policies and benchmarks:

Asset Class	Target	Range
Unrestricted Fixed Income	70%	66%-100%
Equities (MSCI U.S. IMI Index)	30%	0%-34%

The benchmark for the above funds is a weighted blend of the Barclays Capital Aggregate and the MSCI U.S. Investable Market Index (MSCI U.S. IMI) that matches the average equity/debt mix of the fund over the measurement time period.

The American Indian Scholarship Endowment Fund has an asset allocation of 100 percent unrestricted fixed income securities. The benchmark for the fund is the Barclays Capital Aggregate.

Schedule 1: Commingled Monthly Bond Fund (CMBF) Schedule of Net Asset Value

Investment Type	Total Fair Value	Maturity: Less than 1 year	Maturity: 1-5 years	Maturity: 6-10 years	Maturity: More than 10 years	Effective Duration	Credit Rating
Residential Mortgage Backed	$ 150,325,150	$ 7,117,761	$ 124,305,479	$ 16,509,500	$ 2,392,410	2.26	Aaa
Commercial Mortgage Backed Securities	16,926,925	-	16,926,925	-	-	3.32	Aaa
Corporate Bonds - Domestic (USD)	189,722,673	20,402,570	58,488,304	67,859,134	42,972,665	6.07	Schedule 2
Corporate Bonds - Foreign (USD)	84,081,857	10,078,510	27,318,560	40,121,668	6,563,119	4.75	Schedule 2
U.S. Government Treasuries	258,159,466	30,118,499	133,978,216	94,062,751	-	4.29	Aaa
Foreign Government and Agencies (USD)	51,254,047	12,189,025	21,706,558	17,358,464	-	3.69	Schedule 2
Supranational Corporate Bonds (USD)	21,655,507	-	21,655,507	-	-	3.59	Aaa
	772,125,625	$ 79,906,365	$ 404,379,549	$ 235,911,517	$ 51,928,194		
Money Market Funds	10,177,102						
Investment Earnings Receivable	6,374,489						
Total Commingled Bond Fund Investments	788,677,216						
Distributions and other payables	(2,143,339)						
CMBF Net Asset Value - June 30, 2012	$ 786,533,877						

Schedule 2: Commingled Monthly Bond Fund (CMBF) Credit Rating (Moody's)

Rating	Corporate Bonds Domestic	Corporate Bonds Foreign (USD)	Foreign Government and Agencies (USD)
AAA	$ -	$ -	$ 15,897,873
Aa1	-	-	-
Aa2	-	-	7,011,200
Aa3	6,086,114	21,605,517	5,514,600
A1	5,109,300	11,722,630	10,986,510
A2	80,094,097	-	-
A3	34,731,062	12,740,789	-
Baa1	24,404,121	13,136,751	-
Baa2	39,297,979	15,847,790	11,843,864
Baa3	-	9,028,380	-
	$ 189,722,673	$ 84,081,857	$ 51,254,047

Schedule 3: Commingled Monthly Equity Fund (CMEF) Schedule of Net Asset Value

Classification	
Cash and Equivalents	$ 226,963
Corporate Stock Domestic	110,207,178
Corporate Stock Foreign	3,407,333
Receivables	386,594
Payables	(103,310)
Net Asset Value June 30, 2012	$ 114,124,758

PETERSON SULLIVAN LLP
CERTIFIED PUBLIC ACCOUNTANTS
601 UNION STREET, SUITE 2300
SEATTLE, WASHINGTON 98101

TEL 206.382.7777 • FAX 206.382.7777
http://www.pscpa.com

INDEPENDENT AUDITORS' REPORT

To the Members of the Washington State Investment Board

Olympia, Washington

We have audited the accompanying statement of changes in net assets for the Other Funds (Budget Stabilization, Reclamation Revolving, Game & Special Wildlife, Health Insurance, and Radiation Perpetual) of the State of Washington as managed by the Washington State Investment Board ("the Other Funds") for the year then ended June 30, 2012. This financial statement is the responsibility of the Washington State Investment Board's management. Our responsibility is to express an opinion on this financial statement based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the statement of changes in net assets is free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the statement of changes in net assets. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall statement of changes in net assets presentation. We believe that our audit provides a reasonable basis for our opinion.

The financial statement referred to in the first paragraph presents only the investment activity of the Other Funds as managed by the Washington State Investment Board. The financial statement does not purport to, and does not, present the financial activity of the Trust Funds of other state agencies. Further, it does not purport to, and does not, present the financial activity of the Washington State Investment Board or of the State of Washington.

In our opinion, the statement of changes in net assets referred to in the first paragraph presents fairly, in all material respects, the change in net assets of the Other Funds for the year then ended June 30, 2012 in conformity with accounting principles generally accepted in the United States.

Accounting principles generally accepted in the United States require that the management's discussion and analysis preceding the statement of changes in net assets be presented to supplement the financial statement. Such information, although not a part of the financial statement, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the financial statement 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 statement of changes in net assets, and other knowledge we obtained during our audit of the financial statement. 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. The introduction section of the annual report has not been subjected to the auditing procedures applied in the audit of the statement of changes in net assets and, accordingly, we do not express an opinion or provide any assurance on it.

/S/ PETERSON SULLIVAN LLP

October 25, 2012

MANAGEMENT DISCUSSION AND ANALYSIS

Management's Discussion and Analysis for the Other Funds of Washington state, managed by the Washington State Investment Board (WSIB), is presented as an introduction to the financial statements. It is meant to assist the reader in understanding the financial statement by providing an overall review of the financial activities during the year as well as to provide a comparison to the prior year's activities and results. The WSIB manages funds for other Washington state departments. This section of the report represents only the Other Funds portion.

The financial statement and footnotes follow this section of the report. Table 1 compares the asset, liability, and net asset balances at June 30, 2012, with those at June 30, 2011. A Statement of Net Assets has not been presented as of June 30, 2012 because the WSIB held no assets on behalf of the Other Funds as of June 30, 2012. The Statement of Changes in Net Assets provides information on investment performance and other increases and decreases in the net assets of the Other Funds for the year ended June 30, 2012. This information is summarized in Table 2. Table 2 also compares the financial activities of the Other Funds for the year ended June 30, 2012, with those of the year ended June 30, 2011. The Notes to the Financial Statements provide additional information that is essential to a full understanding of the data provided in the financial statement of the Other Funds.

As shown in Table 1, all assets held in the Other Funds transferred to the Office of the State Treasurer on May 31, 2012, pursuant to legislative changes.

As shown in Table 2, net investment income decreased due to the reduction of invested balances and reductions in rates earned on short term investment funds during the current fiscal year. The net amount withdrawn represents the transfer of investment balances to the Office of the State Treasurer.

TABLE 1 - SUMMARIZED NET ASSETS	2012	2011	DOLLAR CHANGE	PERCENT CHANGE
Money Market Funds	**$-**	**$94,144,566**	**$(94,144,566)**	**-100.0%**
Fixed Income Investments	-	23,058	(23,058)	-100.0%
Total Investments	**-**	**94,167,624**	**(94,167,624)**	**-100.0%**
Net Receivables	-	1,354	(1,354)	-100.0%
Net Assets	**$-**	**$94,168,978**	**$(94,168,978)**	**-100.0%**

TABLE 2 - SUMMARIZED CHANGES IN NET ASSETS	2012	2011	DOLLAR CHANGE
Net Investment Income	$(7,839)	$59,423	$(67,262)
Net Amount Withdrawn	(94,161,139)	(22,454,997)	71,706,142
Net Assets - Beginning	**$94,168,978**	**$116,564,552**	**$(22,395,574)**
Net Assets - Ending	**$-**	**$94,168,978**	**$(94,168,978)**

Other Funds Statement of Changes in Net Assets - Year ended June 30, 2012

See notes to financial statement

	Budget Stabilization	Reclamation Revolving	Game & Special Wildlife	Health Insurance	Radiation Perpetual	Total
Net Investment Income						
Investment Income	$ 147	$ 527	$ 10,093	$ 171,040	$ 641	$ 182,448
Less:						
Investment Expenses	(142)	(12)	(9,690)	(164,099)	(615)	(174,558)
WSIB Operating Expenses	(12)	(2)	(888)	(14,771)	(56)	(15,729)
Net Investment Income	(7)	513	(485)	(7,830)	(30)	(7,839)
Withdrawals	(76,039)	(24,148)	(5,552,064)	(88,178,311)	(330,577)	(94,161,139)
Decrease in Net Assets	(76,046)	(23,635)	(5,552,549)	(88,186,141)	(330,607)	(94,168,978)
Net Assets - June 30, 2011	76,046	23,635	5,552,549	88,186,141	330,607	94,168,978
Net Assets - June 30, 2012	$ -	$ -	$ -	$ -	$ -	$ -

Note 1. Description of Funds and Significant Accounting Policies

Description of Funds

The Other Funds of Washington state consist of: the Budget Stabilization, Reclamation Revolving, Game and Special Wildlife, Health Insurance, and the Radiation Perpetual funds. These funds were created over the years by Washington state legislation to fund various mandates and can be liquidated as needed to fund those mandates. These funds are invested by the WSIB until they are completely liquidated or legislation closes the funds. The financial statement presents only the activity of the Other Funds as managed by the WSIB. The WSIB has exclusive control of the investments held by the Other Funds. The financial statement does not present the results of operations of the WSIB.

Basis of Accounting

The accompanying financial statement has been prepared in conformity with accounting principles generally accepted in the United States for governments prescribed by the Governmental Accounting Standards Board (GASB) on the accrual basis of accounting.

Valuation of Investments

Investments are reported at fair value. Fair values are based on published market prices, quotations from national security exchanges and security pricing services. Investments are adjusted to fair values monthly. Unrealized gains and losses are included as investment income in the Statement of Changes in Net Assets.

Revenue Recognition

Interest and dividend income is recognized when earned. Capital gains and losses are recognized on a trade date basis. Purchases and sales of investments are also recorded on a trade date basis.

Contributions and Withdrawals

Contributions and withdrawals are recorded when received or paid.

Use of Estimates

The preparation of the financial statement in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Actual results could differ from the estimated amounts.

Note 2. Fees and Expenses

Investment fees and expenses are accounted for as a reduction of investment income or are netted directly from the asset value of Other Fund investments. These fees include investment management fees and commissions, investment consultant fees, legal fees, and other investment management related expenses. The WSIB operating expenses are charged to the funds based upon actual costs incurred to manage the investments. WSIB operating expenses are allocated to the funds under management based on relative market values, in accordance with state statutes.

Note 3. Deposit and Investment Risk Disclosures

Custodial Credit Risk – Deposits

Custodial credit risk for deposits is the risk that, in the event of a bank failure, the Other Funds' deposits may not be returned to it. The Other Funds do not have a deposit policy for custodial credit risk. As of June 30, 2012, there were no deposits with the custodial bank.

Custodial Credit Risk – Investments

Custodial credit risk for investments is the risk that, in the event of a failure of the counterparty to a transaction, the Other Funds will not be able to recover the value of investments that are in the possession of an outside party.

Interest Rate Risk

Interest rate risk is the risk that changes in interest rates over time will adversely affect the fair value of an investment. Effective duration is the measure of a debt investment's exposure to fair value changes arising from changes in interest rates. Effective duration uses the present value of cash flows, weighted for those flows as a percentage of the investment's full price. Increases in prevailing interest rates generally translate into decreases in fair values of those investments.

Credit Risk

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

Concentration of Credit Risk

Concentration of credit risk is the risk of loss attributed to the magnitude of an investment in a single issuer.

As of June 30, 2012, there were no investments held by the Other Funds and no exposure to credit risk, interest rate risk, or foreign currency risk.

Note 4. Investment Policy

Under RCW 43.33A.030, Trusteeship of the Other Funds is vested in the voting members of the WSIB. The Legislature has established a standard of care for investment of these funds in RCW 43.33A.140. Additionally, the WSIB and its staff must comply with other state laws, such as the Ethics in Public Service Act, RCW 42.52, as it makes its investment decisions and seeks to meet the following investment objectives.

Strategic Objectives

These Funds' investments were to be managed to achieve the highest return possible consistent with the desire to emphasize current income. The objectives include:

- Safety of Principal;
- Current Income; and
- Preservation of the Public's Trust.

Performance Objectives

These funds' investments were to emphasize stability and maximize income to support the operations of each program.

Risk Tolerance

Risk will be managed in a prudent manner. The funds had a below average ability to tolerate volatility.

Permissible Investments

- Government agencies and U.S. Treasuries
- Short-term Investment Funds (STIF) that invest strictly in U.S. Government or Government Agency instruments, including Repurchase Agreements for U.S. Government and Agency instruments. The Pension Stabilization Fund was invested in the Blackrock TempCash short-term investment funds which hold various top rated money market instruments, including repurchase agreements.
- Cash collateral for security lending and collateral for repurchase agreements is restricted to U.S. Government and Government Agency securities.

Portfolio Constraints

- All assets under the management of the WSIB are to be invested to maximize return at a prudent level of risk in accordance with RCW 43.33A.110 and RCW 43.33A.140, which state, in part, that the WSIB is to "invest and manage the assets entrusted to it with reasonable care, skill, prudence and diligence under circumstances then prevailing which a prudent person acting in a like capacity and familiar with such matters would use in the conduct of an activity of like character and purpose."

PETERSON SULLIVAN LLP

CERTIFIED PUBLIC ACCOUNTANTS
601 UNION STREET, SUITE 2300
SEATTLE, WASHINGTON 98101

TEL 206.382.7777 • **FAX** 206.382.7777
http://www.pscpa.com

INDEPENDENT AUDITORS' REPORT

To the Members of the Washington State Investment Board

Olympia, Washington

We have audited the accompanying statement of net assets for the Guaranteed Education Tuition Fund of the State of Washington as managed by the Washington State Investment Board ("the Guaranteed Education Tuition Fund") as of June 30, 2012, and the related statement of changes in net assets for the year then ended. These financial statements are the responsibility of the Washington State Investment Board's management. Our responsibility is to express an opinion on these financial statements based on our audit.

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

The financial statements referred to in the first paragraph present only the investment activity of the Guaranteed Education Tuition Fund as managed by the Washington State Investment Board. The financial statements do not purport to, and do not, present the financial activity of the Washington State Investment Board or of the State of Washington.

In our opinion, the financial statements referred to in the first paragraph present fairly, in all material respects, the net assets of the Guaranteed Education Tuition Fund as of June 30, 2012, and the changes in net assets for the year then ended in conformity with accounting principles generally accepted in the United States.

Accounting principles generally accepted in the United States require that the management's discussion and analysis preceding the financial statements be presented to supplement the financial statements. Such information, although not a part of the financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the financial statements in an appropriate operational, economic, or historical context. 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 financial statements, and other knowledge we obtained during our audit of the 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. The introduction section of the annual report has not been subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we do not express an opinion or provide any assurance on it.

/S/ PETERSON SULLIVAN LLP

October 25, 2012

MANAGEMENT DISCUSSION AND ANALYSIS

Management's Discussion and Analysis for the Guaranteed Education Tuition Fund (GET), managed by the Washington State Investment Board (WSIB), is presented as an introduction to the financial statements. It is meant to assist the reader in understanding the financial statements by providing an overall review of the financial activities during the year as well as to provide a comparison to the prior year's activities and results. The WSIB manages funds for other Washington state departments. This section of the report represents only the GET Fund portion.

The financial statements and footnotes follow this section of the report. The Statement of Net Assets provides information on the types of investments and the liabilities of GET. This information is summarized in Table 1. Table 1 also compares the asset, liability, and net asset balances at June 30, 2012, with those at June 30, 2011. The Statement of Changes in Net Assets provides information on investment performance and other increases and decreases in the net assets of GET for the year ended June 30, 2012. This information is summarized in Table 2. Table 2 also compares the financial activities of GET for the year ended June 30, 2012, with those of the year ended June 30, 2011. The Notes to the Financial Statements provide additional information that is essential to a full understanding of the data provided in the financial statements of GET.

As shown in Table 1, the net assets of the GET Program increased by $125.1 million during the fiscal year ended June 30, 2012. Contributions to the GET Program during the year increased net assets by $123.1 million. Realized and unrealized losses increased net assets in the fixed income portfolio by $62.6 million and decreased the equity portfolio by $(94.9) million. The remaining increase was a result of net investment income reinvested within the funds.

The following summarizes the changes within each grouping listed within Table 1:

- Liquid assets increased by $51.3 million. This cash balance represents less than 5 percent of total invested balances. Initially, net investment income received from all asset classes and net contributions are reinvested in money market funds. Investments in longer term securities are made as the cash becomes available and market opportunities exist. These balances fluctuate within policy targets as asset allocation decisions are made with accumulated cash to longer term investments.
- Fixed income investments increased by $9.5 million. Net realized and unrealized gains increased this asset class by $62.6 million. During the current fiscal year the TIPS portfolio returned 12.5 percent and other fixed income securities returned 6.8 percent which contributed to this increase. Fixed income yields decreased during the current fiscal year causing bond values to increase. In addition, the value of TIPS is directly impacted by changes in the Consumer Price Index (CPI). The CPI rose during the year which contributed to the increase in the value of the TIPS holdings. The GET program rebalanced during the year ended June 30, 2012, and $(61.3) million was transferred from fixed income to equity securities. The remaining increase was due to reinvestment of net investment income within the fixed income portfolio.
- Equity investments increased by $62.8 million. During the current fiscal year the portfolio was rebalanced and $142.2 million was transferred from other asset classes and reinvested in equity securities. Net realized and unrealized gains and losses decreased equity balances by $(95.0) million. The equity portfolio in the GET program returned (6.6) percent during the current fiscal year which resulted in the decline in value. The remaining increase was the result of net investment income reinvested in equity securities.
- Net receivables and payables decreased substantially due to securities lending activities. All securities on loan were recalled as of June 30, 2012, in anticipation of a custodian bank transition on July 1, 2012. Accordingly, the GET funds held no collateral in the securities lending program at year end.

As shown in Table 2, net investment income decreased by $(281.8) million during the fiscal year ended June 30, 2012. The current year return for the GET program was .1 percent compared to the prior year return of 20.5 percent. While fixed income returns increased over the prior year, equity returns decreased from 31.7 percent for the year ended June 30, 2011, to (6.6) percent for the current fiscal year end. The decrease in returns over the prior year contributed to the decrease in realized and unrealized gains and losses of $(294.7) million. Interest, dividend, and other investment income increased by $ 11.9 million due to the restructuring of the equity portfolio during the current fiscal year. Additional funding was provided to the equity portfolio. In addition, equity securities were transferred from a commingled fund to a passively managed separate account which holds individual securities. Accordingly, income is now recorded as dividends when received, rather than when declared by the commingled fund manager. Securities lending broker rebates decreased during the current fiscal year due to the narrowing of spreads paid to brokers in the current lending environment contributing to the decrease of $(.9) million in fees and expenses.

Contributions from GET participants decreased by $(119.7) million. During the prior fiscal year, participants continued to take advantage of lower tuition unit purchase prices in anticipation of rate increases.

TABLE 1: SUMMARIZED NET ASSETS	2012	2011	DOLLAR CHANGE	PERCENT CHANGE
Liquid Assets	$67,016,931	$15,721,381	$51,295,550	326.3%
Fixed Income Investments	760,008,938	750,502,410	9,506,528	1.3%
Equity Investments	1,194,246,317	1,131,453,136	62,793,181	5.5%
Total Investments	**2,021,272,186**	**1,897,676,927**	**123,595,259**	**6.5%**
Collateral Held Under Securities Lending Agreements	-	362,718,782	(362,718,782)	-100.0%
Investment Earnings Receivable	5,590,099	3,986,946	1,603,153	40.2%
Total Assets	**2,026,862,285**	**2,264,382,655**	**(237,520,370)**	**-10.5%**
Investment Liabilities	164,845	362,783,965	(362,619,120)	-100.0%
Net Assets	**$2,026,697,440**	**$1,901,598,690**	**$125,098,750**	**6.6%**

WSIB staff rebalances the GET Funds' investments between asset classes as markets move pursuant to WSIB policy. The fair value of the GET Fund assets is directly impacted by the returns of the various capital markets within which the WSIB invests. The returns are expected to have a significant effect on financial position and results of operations in the future. However, one of the benefits of diversification gained by investing across various investment types as well as broadly within an asset class is the reduction in aggregate volatility of the total investment portfolio. The WSIB, after discussions with the GET Committee, makes the asset allocation decisions for GET investments.

TABLE 2: SUMMARIZED CHANGES IN NET ASSETS	2012	2011	DOLLAR CHANGE	PERCENT CHANGE
Net Investment Income				
Interest, Dividends and Other Investment Income	$34,976,036	$23,041,779	$11,934,257	51.8%
Net Capital Gains	168,331,169	7,816,517	160,514,652	2053.5%
Unrealized Gains (Losses)	(200,678,254)	254,536,254	(455,214,508)	(178.8%)
Less: Fees and Expenses	**(591,622)**	**(1,524,370)**	**(932,748)**	**(61.2%)**
Net Investment Income	2,037,329	283,870,180	(281,832,851)	(99.3%)
Net Amount Contributed	123,061,421	242,718,132	(119,656,711)	(49.3%)
Net Assets - Beginning	**1,901,598,690**	**1,375,010,378**	**526,588,312**	**38.3%**
Net Assets - Ending	**$2,026,697,440**	**$1,901,598,690**	**$125,098,750**	**6.6%**

GET Fund Statement of Net Assets - June 30, 2012

See notes to financial statements

			Percent
ASSETS			
Investments:			
Liquid Assets	$	67,016,931	3.3%
Fixed Income			
Treasury Inflation Protected Securities		377,076,298	18.7%
Commingled Intermediate Credit		382,932,640	18.9%
Total Fixed Income		760,008,938	37.6%
Equity			
Corporate Stock - Domestic		555,977,360	27.5%
Corporate Stock - Foreign (Non USD Denominated)		615,159,457	30.4%
Corporate Stock - Foreign (USD Denominated)		23,109,500	1.2%
Total Equity		1,194,246,317	59.1%
Total Investments		2,021,272,186	100.0%
Investment Earnings and Other Receivables		5,590,099	
Total Assets		2,026,862,285	
LIABILITIES			
Accounts Payable		164,845	
Total Liabilities		164,845	
NET ASSETS	$	2,026,697,440	

GET Fund Statement of Changes in Net Assets - Year ended June 30, 2012

See notes to financial statements

Net Investment Income		
Investment Income		
Interest, Dividends and Other Investment Income	$	33,922,591
Securities Lending Income		1,053,445
Realized Capital Gains		177,037,610
Realized Capital Losses		(8,706,441)
Unrealized Losses		(200,678,254)
Less:		
Securities Lending Rebates and Fees		136,297
Investment Expenses		(414,816)
WSIB Operating Expenses		(313,103)
Net Investment Income		2,037,329
Net Amount Contributed		123,061,421
Increase in Net Assets		125,098,750
Net Assets - June 30, 2011		1,901,598,690
Net Assets - June 30, 2012	$	2,026,697,440

Note 1: Description of Fund and Significant Accounting Policies

Description of Fund

Guaranteed Education Tuition Fund (GET) consists of contributions from participants planning on attending advanced education programs in Washington state. This fund is invested by the WSIB until participants begin to withdraw funds as needed to pay for educational expenses. The financial statements present only the activity of GET as managed by the WSIB. The WSIB has exclusive control of the investments held for the GET Program. The financial statements do not present the financial position and results of operations of the WSIB or the GET Program.

Basis of Accounting

The accompanying financial statements have been prepared in conformity with accounting principles generally accepted in the United States for governments prescribed by the Governmental Accounting Standards Board (GASB) on the accrual basis of accounting.

Valuation of Investments

Investments are reported at fair value. Fair values are based on published market prices, quotations from national security exchanges, and security pricing services. Investments are adjusted to fair values monthly. Unrealized gains and losses are included as investment income in the Statement of Changes in Net Assets.

Revenue Recognition

Interest and dividend income is recognized when earned. Capital gains and losses are recognized on a trade date basis. Purchases and sales of investments are also recorded on a trade date basis.

Securities Lending

GET records collateral received under securities lending agreements where GET has the ability to spend, pledge, or sell the collateral without borrower default. Liabilities resulting from these transactions are also recorded. Additionally, costs associated with securities lending transactions, including broker commissions paid and lending fees paid to the custodian bank, are reported in the accompanying financial statements. The Statement of Net Assets does not include detailed holdings of securities lending collateral by investment classification.

Contributions

Contributions are recorded when received.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Actual results could differ from the estimated amounts.

Note 2: Fees and Expenses

Investment fees and expenses are accounted for as a reduction of investment income or are netted directly from the asset value of GET's investments. These fees include investment management fees and commissions, investment consultant fees, legal fees, and other investment management related expenses. The WSIB operating expenses are charged to the funds based upon actual costs incurred to manage the investments. WSIB operating expenses are allocated to the funds under management based on relative market values, in accordance with state statutes.

Note 3: Deposit and Investment Risk Disclosures

Custodial Credit Risk – Deposits

Custodial credit risk for deposits is the risk that, in the event of a bank failure, GET deposits may not be returned to it. GET does not have a deposit policy for custodial credit risk. As of June 30, 2012, there were no deposits with the custodial bank.

Custodial Credit Risk – Investments

Custodial credit risk for investments is the risk that, in the event of a failure of the counterparty to a transaction, the GET Funds will not be able to recover the value of investments that are in the possession of an outside party. The GET Funds mitigates custodial credit risk by having its investment securities held by its custodian. Also, investment securities are registered in the name of the Washington State Investment Board for the benefit of the GET Funds, excluding cash and cash equivalents and repurchase agreements held as securities lending collateral.

Interest Rate Risk

Interest rate risk is the risk that changes in interest rates over time will adversely affect the fair value of an investment. Effective duration is the measure of a debt investment's exposure to fair value changes arising from changes in interest rates. Effective duration uses the present value of cash flows, weighted for those flows as a percentage of the investment's full price. Increases in prevailing interest rates generally translate into decreases in fair values of those investments. The long-term goals of the fixed income portfolio are to return more than inflation, and to limit volatility for the total portfolio. The goals are met through the purchase of inflation indexed bonds to help offset unexpected inflation and nominal bonds for additional coupon return above treasuries which also add diversification. Schedule 1 provides information about the interest rate risks associated with GET investments as of June 30, 2012. The schedule displays various asset classes held by maturity in years, effective durations and credit ratings.

Credit Risk

Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. See Note 5 for credit risk associated with the GET investment program.

Concentration of Credit Risk

Concentration of credit risk is the risk of loss attributed to the magnitude of an investment in a single issuer. GET policy states no corporate fixed income issue's cost shall exceed 3 percent of the fair value at the time of purchase, nor shall its fair value exceed 6 percent of the fair value at any time. There was no concentration of credit risk that exceeded these limits as of June 30, 2012.

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 GET Funds do not have a formal policy to limit foreign currency risk. The GET Funds manage their exposure to fair value loss by requiring their investment managers to maintain diversified portfolios by sector and by issuer to limit foreign currency and security risk. The GET Funds exposure to foreign currency risk is presented in Schedule 3 which provides information on deposits and investments held in various foreign currencies.

Note 4: Securities Lending

State law and WSIB policy permit the GET to participate in securities lending programs to augment investment income. The WSIB has entered into an agreement with JPMorgan to act as agent for the WSIB in securities lending transactions. As JPMorgan is the custodian bank for the WSIB, it is counterparty to securities lending transactions.

GET reports securities lent (the underlying securities) as assets in the Statement of Net Assets. Cash received as collateral on securities lending transactions and investments made with that cash are reported as assets. Securities received as collateral are reported as assets if GET has the ability to pledge or sell them without a borrower default. Liabilities resulting from these transactions are also reported in the Statement of Net Assets. Securities lending transactions collateralized by securities where GET does not have the ability to pledge or sell unless the borrower defaults are not reported as assets and liabilities.

In anticipation of the custodian bank conversion on July 1, 2012, the GET recalled all securities on loan. There were no assets on loan at June 30, 2012, and no collateral held related to securities lending transactions.

Fixed income and equity securities were loaned during the current fiscal year and collateralized by GET's agent with cash and U.S. Government Securities (exclusive of mortgage backed securities and letters of credit), and irrevocable letters of credit. When the loaned securities had collateral denominated in the same currency, the collateral requirement was 102 percent of the fair value, including accrued interest, of the securities loaned. All other securities were required to be collateralized at 105 percent of the fair value, including accrued interest, of the loaned securities.

During fiscal year 2012, securities lending transactions could be terminated on demand by either the GET or the borrower. The weighted average maturity of loans for 2012 was 1.5 days. Cash collateral was invested by GET in the WSIB's short-term investment pool. Because the securities lending agreements were terminable at will, their duration did not generally match the duration of the investments made with the cash collateral. Non-cash collateral could not be pledged or sold absent borrower default. There are no restrictions on the amount of securities that can be lent.

Securities were lent with the agreement that they would be returned in the future for exchange of the collateral. JPMorgan indemnified the WSIB by agreeing to purchase replacement securities or return the cash collateral in the event a borrower failed to return the loaned securities or pay distributions thereon. JPMorgan's responsibilities included performing appropriate borrower and collateral investment credit analyses, demanding adequate types and levels of collateral, and complying with applicable federal regulations concerning securities lending.

During fiscal year 2012, there were no significant violations of legal or contractual provisions, no failures by any borrowers to return loaned securities or to pay distributions thereon. Further, GET incurred no losses during fiscal year 2012 resulting from a default by either the borrowers or the securities lending agents.

Note 5: Derivatives

GET is authorized to utilize various derivative financial instruments, including financial futures and forward contracts. Derivative transactions involve, to varying degrees, market and credit risk. In connection with the global equity strategy within the portfolio, GET held investments in financial futures and forward currency contracts at various times throughout the fiscal year that are recorded at fair value with realized and unrealized gains and losses recognized in investment income in the Statement of Changes in Net Assets.

Derivatives are generally used to achieve the desired market exposure of a security, index or currency. Derivative contracts are instruments that derive their value from underlying assets, indices, reference interest rates, or a combination of these factors. A derivative instrument could be a contract negotiated on behalf of GET and a specific counterparty. This would typically be referred to as an over the counter (OTC) contract such as forward contracts. Alternatively, a derivative instrument, such as futures, could be listed and traded on an exchange and referred to as "exchange traded."

Futures contracts are standardized, exchange-traded contracts to purchase or sell a specific financial instrument at a predetermined price. Gains and losses on futures contracts are settled daily based on a notional (underlying) principal value and do not involve an actual transfer of the specific instrument. The exchange assumes the risk that the counterparty will not pay and generally requires margin payments to minimize such risk. Futures are generally used to achieve the desired market exposure of a security or index or rebalance the total portfolio.

Forward currency contracts are agreements to exchange the currency of one country for the currency of another country at an agreed-upon price and settlement date. These forward commitments are not standardized and carry credit risk due to the possible nonperformance by one of the counterparties. The maximum potential loss is the aggregate face value in U.S. dollars at the time the contract was opened; however, the likelihood of such loss is remote. At June 30, 2012, the GET Funds had no outstanding forward currency contracts.

Inherent in the use of OTC derivatives, GET is exposed to counterparty credit risk 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. As of June 30, 2012, GET had no open OTC derivatives and, accordingly no

		Changes in Fair Value - Included in Investment Income	Fair Value at June 30, 2012 - Investment Derivative	
	Classification	**Amount**	**Amount**	**Notional**
FUTURES CONTRACTS:				
Equity Index Futures	Investment	$ (435,883)	$ 305,648	128
FORWARD CURRENCY CONTRACTS:				
Australian Dollar	Investment	$ (270,074)	$ -	-
Canadian Dollar	Investment	(149,949)	-	-
Danish Krone	Investment	(7,932)	-	-
Euro	Investment	(264,371)	-	-
Hong Kong Dollar	Investment	(4,386)	-	-
Israeli Shekel	Investment	(12,747)	-	-
Japanese Yen	Investment	93,951	-	-
Mexican Peso	Investment	(20,396)	-	-
New Turkish Lira	Investment	(2,862)	-	-
Pound Sterling	Investment	(71,731)	-	-
Polish Zloty	Investment	(35,579)	-	-
Singapore Dollar	Investment	(6,603)	-	-
South African Rand	Investment	(21,368)	-	-
Swedish Krona	Investment	(54,331)	-	-
Swiss Franc	Investment	276,020	-	-
		$ (552,358)	**$ -**	**-**

counterparty credit risk. Derivatives which are exchange traded are not subject to credit risk. The maximum loss that would be recognized at June 30, 2012, if all counterparties fail to perform as contracted, was de minimis.

Note 6: Summary of Investment Policy

Under RCW 43.33A.030, Trusteeship of GET is vested in the voting members of the WSIB. The Legislature has established a standard of care for investment of these funds in RCW 43.33A.140. Additionally, the WSIB and its staff must comply with other state laws, such as the Ethics in Public Service Act, 42.52 RCW, as it makes its investment decisions and seeks to meet the following investment objectives.

In accordance with RCW 43.33A.110, the portfolio is managed to achieve a maximum return at a prudent level of risk. The key determinate is identifying the prudent level of risk for the program considering the program's need to meet or exceed the growth rate of tuition costs. Based on this requirement the order of the objectives shall be:

- Maintain the solvency of the fund and the financial stability of the program as measured by the external actuary;
- Ensure sufficient assets are available to fund the expected college tuition payments;
- Subject to the above requirements, achieve a maximum return that will meet or exceed the rate of growth in college tuition cost over a 10-year period, at a prudent level risk; and
- Invest in a manner that will not compromise public confidence in the program.

Performance Objectives

Performance of the investment portfolio shall be judged relative to the investment objectives, the risk constraint standards, and the investment approach.

The fund has both a long-term absolute goal and several relative performance objectives:

- Achieve or exceed a 4.5 percent real rate of return relative to inflation, as measured by the Consumer Price Index (CPI), over a 10-year period.
- Relative to asset allocation targets, generate a return equal to, or in excess of, the passive benchmark portfolio. Currently, the global equity portfolio benchmark is the Dow Jones Global Stock Market Index.

Risk Constraint Standards

- All assets under management by the WSIB are to be invested to maximize return at a prudent level of risk in accordance with the requirements of RCW 43.33A.110 and RCW 43.33A.140.
- No corporate fixed income issue's cost shall exceed 3 percent of the fund's fair value at the time of purchase, nor shall its fair value exceed 6 percent of the fund's fair value at any time (RCW 43.33A.140).
- Diversify the assets at a prudent level to moderate fluctuations in the fair value of the program.

Permissible Investments

- Global Equity
- Inflation Indexed Bonds
- U.S. Treasuries and Government Obligations
- Credit Bonds
- WSIB Bond Market Fund
- Cash equivalent funds
- Derivatives

Asset Allocation

The asset allocation strategy for the GET program is as follows:

Asset Class	Target	Range
Global Equities	60%	55%-65%
Fixed Income	20%	16%-24%
Inflation Indexed Bonds	20%	16%-24%
Cash	0%	0%-5%

Schedule 1: Schedule of Maturities and Credit Ratings

Investment Type	Total Fair Value	Maturity: Less than 1 year	Maturity: 1-5 years	Maturity: 6-10 years	Maturity: More than 10 years	Effective Duration	Credit Rating
Treasury Inflation Protected Securities	$ 377,076,298	$ -	$ 143,373,987	$ 27,252,058	$ 206,450,253	5.67	AAA
Commingled Intermediate Credit	382,932,640	39,569,527	152,055,974	191,307,139	-	4.61	Schedule 2
	760,008,938	$ 39,569,527	$ 295,429,961	$ 218,559,197	$ 206,450,253		
Investments Not Required to be Categorized							
Corporate Stock - Domestic	555,977,360						
Corporate Stock - Foreign (Non USD Denominated)	615,159,457						
Corporate Stock - Foreign (USD Denominated)	23,109,500						
Liquid Assets	67,016,931						
Total Investments Not Categorized	1,261,263,248						
Total Investments	$ 2,021,272,186						

Schedule 2: Additional Credit Rating Disclosures

Moody's Equivalent Credit Rating	Total Fair Value
Aaa	$ 46,496,379
Aa1	1,309,471
Aa2	6,390,316
Aa3	48,024,278
A1	25,310,884
A2	46,001,376
A3	31,835,762
Baa1	56,602,801
Baa2	79,716,922
Baa3	41,244,451
Total Fair Value	$ 382,932,640

Schedule 3: Foreign Currency Exposure by Country

	Investment Type In U.S. Dollar Equivalent			
Foreign Currency Denomination	Currency	Corporate Stock	Total	Percent of Total GET Funds Investments
Australia-Dollar	$ 51,567	$ 37,431,755	$ 37,483,322	1.9%
Brazil-Real	389,333	17,393,411	17,782,744	0.9%
Canada-Dollar	407,146	54,658,976	55,066,122	2.7%
Chili-Official rate	42,349	2,662,369	2,704,718	0.1%
Denmark-Krone	17,471	4,876,134	4,893,605	0.2%
E.M.U.-Euro	124,839	110,114,969	110,239,808	5.5%
Hong Kong-Dollar	378,992	38,408,457	38,787,449	1.9%
India - Rupee	107,733	9,806,776	9,914,509	0.5%
Indonesia-Rupiah	69,401	3,432,832	3,502,233	0.2%
Israel-Shekel	45,069	2,465,047	2,510,116	0.1%
Japan-Yen	1,523,775	98,620,533	100,144,308	5.0%
Malaysia-Ringgit	51,090	4,646,105	4,697,195	0.2%
Mexico-Peso	65,063	6,741,132	6,806,195	0.3%
Norway-Krone	114,648	4,283,406	4,398,054	0.2%
Singapore-Dollar	86,684	8,290,166	8,376,850	0.4%
South Africa-Rand	93,349	11,961,213	12,054,562	0.6%
South Korea-Won	145,271	22,599,959	22,745,230	1.1%
Sweden-Krona	146,226	13,007,636	13,153,862	0.7%
Switzerland-Franc	102,310	34,362,957	34,465,267	1.7%
Taiwan-Dollar	119,971	18,569,197	18,689,168	0.9%
United Kingdom - Pound	905,843	100,067,244	100,973,087	5.0%
Other - Miscellaneous	328,682	10,759,183	11,087,865	0.6%
	5,316,812	615,159,457	620,476,269	30.7%
Foreign Investments Denominated in U.S. Dollars	-	23,109,500	23,109,500	1.1%
	$ 5,316,812	$638,268,957	$ 643,585,769	31.8%

PETERSON SULLIVAN LLP
CERTIFIED PUBLIC ACCOUNTANTS
601 UNION STREET, SUITE 2300
SEATTLE, WASHINGTON 98101

TEL 206.382.7777 • **FAX** 206.382.7777
http://www.pscpa.com

INDEPENDENT AUDITORS' REPORT

To the Members of the Washington State Investment Board

Olympia, Washington

We have audited the accompanying statement of net assets for the Developmental Disabilities Endowment Trust Fund of the State of Washington as managed by the Washington State Investment Board ("the Developmental Disabilities Endowment Trust Fund") as of June 30, 2012, and the related statement of changes in net assets for the year then ended. These financial statements are the responsibility of the Washington State Investment Board's management. Our responsibility is to express an opinion on these financial statements based on our audit.

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

The financial statements referred to in the first paragraph present only the investment activity of the Developmental Disabilities Endowment Trust Fund as managed by the Washington State Investment Board. The financial statements do not purport to, and do not, present the financial activity of the Trust Funds of other state agencies. Further, they do not purport to, and do not, present the financial activity of the Washington State Investment Board or of the State of Washington.

In our opinion, the financial statements referred to in the first paragraph present fairly, in all material respects, the net assets of the Developmental Disabilities Endowment Trust Fund as of June 30, 2012, and the changes in net assets for the year then ended in conformity with accounting principles generally accepted in the United States.

Accounting principles generally accepted in the United States require that the management's discussion and analysis preceding the financial statements be presented to supplement the financial statements. Such information, although not a part of the financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the financial statements in an appropriate operational, economic, or historical context. 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 financial statements, and other knowledge we obtained during our audit of the 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. The introduction section of the annual report has not been subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we do not express an opinion or provide any assurance on it.

/S/ PETERSON SULLIVAN LLP

October 25, 2012

MANAGEMENT DISCUSSION AND ANALYSIS

Management's Discussion and Analysis for the Developmental Disabilities Endowment Trust Fund (DDEF) of Washington state, managed by the Washington State Investment Board (WSIB), is presented as an introduction to the financial statements. It is meant to assist the reader in understanding the financial statements by providing an overall review of the financial activities during the year as well as to provide a comparison to the prior year's activities and results. The WSIB manages funds for other Washington state departments. This section of the report covers the DDEF funds only.

The financial statements and footnotes follow this section of the report. The Statement of Net Assets provides information on the types of investments, assets, and liabilities of the DDEF as of June 30, 2012. This information is summarized in Table 1. Table 1 also compares the asset, liability, and net asset balances at June 30, 2012, with those at June 30, 2011. The Statement of Changes in Net Assets provides information on investment performance and other increases and decreases in the net assets of the DDEF for the year ended June 30, 2012. This information is summarized in Table 2. Table 2 also compares the financial activities of DDEF for the year ended June 30, 2012, with those of the year ended June 30, 2011. The Notes to the Financial Statements provide additional information that is essential to a full understanding of the data provided in the financial statements of the DDEF.

As shown in Table 1, net assets under management within DDEF increased by $4.8 million during the fiscal year ended June 30, 2012. The increase in net assets was primarily due to the contributions to the private trust fund of $2.9 million and realized and unrealized gains of $1.3 million. The DDEF state trust fund returned 6.5 percent during the current fiscal year and the DDEF private trust fund returned 5.9 percent during the same time period. The remaining net asset value increase was a result of net investment earnings reinvested within the DDEF funds.

The following summarizes the changes within each grouping listed within Table 1:

- Money market funds decreased by $(0.1) million. This cash balance represents less than 1 percent of total invested balances and is within policy targets. Net investment income received from all asset classes and contributions are reinvested into money market funds and used within each asset class to reinvest in longer term securities as the cash becomes available. Money market balance fluctuations are a result of the timing of cash received and the reinvestment to other asset classes.
- Fixed income investments increased by $0.6 million almost entirely due to realized and unrealized gains within the portfolio. Approximately half the fixed income portfolio is comprised of TIPS which returned 11.3 percent during the current fiscal year. Other fixed income securities returned 6.8 percent during the same time period. Bond yields decreased during the year causing the bond markets to rally.
- Balanced mutual funds received the private trust fund contributions of $2.9 million to invest. Realized and unrealized gains increased the portfolio by $.8 million. Balanced mutual funds had a return of 6.0 percent during the current fiscal year with significant positive fixed income returns contributing to the majority of the gain. The remaining increase was due to reinvestment of income within the fund.
- Equity investments had a small increase during the current fiscal year. The equity return within the DDEF portfolio was (6.8) percent which resulted in a value decrease of approximately $(.1) million. The remaining increase was the result of income reinvested in equity securities.
- Cash collateral held under securities lending contracts and the related obligation decreased by $(0.1) million. The DDEF recalled all outstanding loans as of June 30, 2012, in anticipation of the asset transfer to the new custodian bank effective July 1, 2012.

TABLE 1: SUMMARIZED NET ASSETS	2012	2011	DOLLAR CHANGE	PERCENT CHANGE
Money Market Funds	$17,606	$122,350	$(104,744)	-85.6%
Fixed Income Investments	8,567,949	7,934,048	633,901	8.0%
Balanced Funds	22,940,580	18,743,344	4,197,236	22.4%
Equity Investments	1,832,241	1,765,941	66,300	3.8%
Total Investments	**33,358,376**	**28,565,683**	**4,792,693**	**16.8%**
Collateral Held Under Securities Lending Agreements	-	118,990	(118,990)	-100.0%
Earnings Receivable	23,549	24,996	(1,447)	-5.8%
Total Assets	**33,381,925**	**28,709,669**	**4,672,256**	**16.3%**
Investment Liabilities	138	119,055	(118,917)	-99.9%
Net Assets	**$33,381,787**	**$28,590,614**	**$4,791,173**	**16.8%**

As shown in Table 2, net investment income decreased by $(2.1) million from the prior year almost entirely due to decreases in the market value of the underlying investments (realized and unrealized gains and losses). The total DDEF return for fiscal year 2012 was 6.1 percent which was a substantial decrease from the prior year return of 17.2 percent. All asset classes experienced a significant reduction of returns over the prior year except the fixed income portfolio. Contributions increased over the prior year as the private trust fund received additional funds from participants during the current fiscal year.

The fair value of DDEF net assets is directly impacted by the returns of the various capital markets within which the WSIB invests and the returns are expected to have a significant effect on financial position and results of operations in the future. However, one of the benefits of diversification gained by investing across various investment types as well as broadly within an asset class is the reduction in aggregate volatility of the total investment portfolio. The WSIB, with concurrence from the Developmental Disabilities Life Opportunities Trust Governing Board, makes the asset allocation decisions for DDEF assets. WSIB staff rebalances the DDEF's assets between asset classes as markets move, pursuant to WSIB policy.

TABLE 2: SUMMARIZED CHANGES IN NET ASSETS	2012	2011	DOLLAR CHANGE
Net Investment Income			
Investment Income	$525,714	$491,691	$34,023
Net Capital Gains	174,245	444	173,801
Unrealized Gains	1,159,330	3,438,726	(2,279,396)
Less:			
Investment Expenses	(4,123)	(3,874)	249
Net Investment Income	**1,855,166**	**3,926,987**	**(2,071,821)**
Net Amount Contributed	2,936,007	1,971,268	964,739
Net Assets - Beginning	**28,590,614**	**22,692,359**	**5,898,255**
Net Assets - Ending	**$33,381,787**	**$28,590,614**	**$4,791,173**

DDEF Statement of Net Assets - June 30, 2012

See notes to financial statements

	Developmental Disabilities Endowment Trust Fund State	Developmental Disabilities Endowment Trust Fund Private	Total	Percent of Total
ASSETS				
Investments:				
LIQUIDITY:				
Money Market Funds	$ 7,606	$ 10,000	$ 17,606	0.1%
FIXED INCOME INVESTMENTS:				
Treasury Inflation Protected Securities	4,301,514	-	4,301,514	12.9%
Commingled Intermediate Credit	4,266,435	-	4,266,435	12.8%
BALANCED FUNDS:				
Balanced Mutual Funds - Domestic	-	22,940,580	22,940,580	68.7%
EQUITY INVESTMENTS:				
Commingled Equity Index Funds - Domestic	985,606	-	985,606	3.0%
Commingled Equity Index Funds - Foreign	846,635	-	846,635	2.5%
Total Investments	10,407,796	22,950,580	33,358,376	100.0%
Investment Earnings Receivable	23,549	-	23,549	
Total Assets	10,431,345	22,950,580	33,381,925	
LIABILITIES				
Accrued Payables	138	-	138	
NET ASSETS	**$ 10,431,207**	**$ 22,950,580**	**$ 33,381,787**	

DDEF Statement of Changes in Net Assets - Year Ended June 30, 2012

See notes to financial statement

	Developmental Disabilities Endowment Trust Fund State	Developmental Disabilities Endowment Trust Fund Private	Total
Net Investment Income			
Investment Income:			
Interest, Dividends and Other Investment Income	$ 66,285	$ 459,429	$ 525,714
Realized Capital Gains	176,395	-	176,395
Realized Capital Losses	(2,150)	-	(2,150)
Unrealized Gains	403,577	755,753	1,159,330
Less:			
Investment Expenses	(1,805)	(638)	(2,443)
WSIB Operating Expenses	(1,680)		(1,680)
Net Investment Income	640,622	1,214,544	1,855,166
Net Amount Contributed	1,680	2,934,327	2,936,007
Increase in Net Assets	642,302	4,148,871	4,791,173
Net Assets, June 30, 2011	9,788,905	18,801,709	28,590,614
Net Assets, June 30, 2012	$ 10,431,207	$ 22,950,580	$ 33,381,787

Note 1. Description of Funds and Significant Accounting Policies

Description of Funds

The Developmental Disabilities Endowment Fund (DDEF) of Washington state consists of two funds. The State Trust Fund was originally created from a grant by Washington state. The Private Trust Fund consists of contributions by private individual participants of the program. These funds are invested by the WSIB until participants withdraw these funds as needed. The financial statements present only the activity of the DDEF as managed by the WSIB. The WSIB has exclusive control of the investments of all money held by the DDEF. The financial statements do not present the financial position and results of operations of the WSIB or the activity of the DDEF program.

Basis of Accounting

The accompanying financial statements have been prepared in conformity with accounting principles generally accepted in the United States for governments prescribed by the Governmental Accounting Standards Board (GASB) on the accrual basis of accounting.

Valuation of Investments

Investments are reported at fair value. Fair values are based on published market prices, quotations from national security exchanges, and security pricing services. Investments are adjusted to fair values monthly. Unrealized gains and losses are included as investment income in the Statement of Changes in Net Assets.

Revenue Recognition

Interest and dividend income is recognized when earned. Capital gains and losses are recognized on a trade date basis. Purchases and sales of investments are also recorded on a trade date basis.

Securities Lending

DDEF reports collateral received under securities lending agreements where DDEF has the ability to spend, pledge, or sell the collateral without borrower default. Liabilities resulting from these transactions are also recorded. Additionally, costs associated with securities lending transactions, including broker commissions paid and lending fees paid to the custodian bank, are reported as investment expenses in the accompanying financial statements. The Statement of Net Assets does not include detailed holdings of securities lending collateral by investment classification.

Contributions

Contributions are recorded when received.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Actual results could differ from the estimated amounts.

Note 2. Fees and Expenses

Investment fees and expenses are accounted for as a reduction of investment income or are netted directly from the asset value of DDEF's investments. These fees include investment management fees and commissions, investment consultant fees, legal fees, and other investment management related expenses. The WSIB operating expenses are charged to the funds based upon actual costs incurred to manage the investments. WSIB operating expenses are allocated to the funds under management based on relative market values, in accordance with state statutes.

Note 3. Deposit and Investment Risk Disclosures

Custodial Credit Risk – Deposits

Custodial credit risk for deposits is the risk that in the event of a bank failure, DDEF deposits may not be returned to it. DDEF does not have a deposit policy for custodial credit risk. As of June 30, 2012, there were no deposits with the custodial bank.

Custodial Credit Risk – Investments

Custodial credit risk for investments is the risk that in the event of a failure of the counterparty to a transaction, the DDEF Funds will not be able to recover the value of investments that are in the possession of an outside party. The DDEF Funds mitigates custodial credit risk by having its investment securities held by its custodian. Also, investment securities are registered in the name of the WSIB for the benefit of the DDEF Funds, excluding cash and cash equivalents and repurchase agreements held as securities lending collateral.

Interest Rate Risk

Interest rate risk is the risk that changes in interest rates over time will adversely affect the fair value of an investment. Effective duration is the measure of a debt investment's exposure to fair value changes arising from changes in interest rates. Effective duration uses the present value of cash flows, weighted for those flows as a percentage of the investment's full price. Increases in prevailing interest rates generally translate into decreases in fair values of those investments.

Schedule 1 provides information about the interest rate risks associated with DDEF investments as of June 30, 2012. The schedule displays various asset classes held by maturity in years, effective durations, and credit ratings.

Credit Risk

Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. The DDEF's rated debt investments as of June 30, 2012, were rated by Moody's or equivalent rating methodology.

Concentration of Credit Risk

Concentration of credit risk is the risk of loss attributed to the magnitude of an investment in a single issuer. DDEF policy states that corporate fixed income issue's cost shall not exceed 3 percent of DDEF's fair value at the time of purchase, nor shall its fair value exceed 6 percent of DDEF's fair value at any time. There was no concentration of credit risk that exceeded these limits as of June 30, 2012.

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. DDEF has no formal policy to limit foreign currency risk. The only security held by the DDEF with foreign currency risk at June 30, 2012, consists of $846,635 invested in an international commingled equity index fund.

Note 4. Securities Lending

Washington state law and WSIB policy permit DDEF to participate in securities lending programs to augment investment income. The WSIB has entered into an agreement with JPMorgan to act as agent for the WSIB in securities lending transactions. As JPMorgan is the custodian bank for the WSIB, it is counterparty to securities lending transactions.

DDEF reports securities lent (the underlying securities) as assets in the Statement of Net Assets. Cash received as collateral on securities lending transactions and investments made with that cash are reported as assets.

Securities received as collateral are reported as assets if DDEF has the ability to pledge or sell them without a borrower default. Liabilities resulting from these transactions are also reported in the Statement of Net Assets. Securities lending transactions collateralized by securities that DDEF does not have the ability to pledge or sell unless the borrower defaults are not reported as assets and liabilities.

In anticipation of the custodian bank conversion on July 1, 2012, the DDEF funds recalled all securities on loan. There were no assets on loan at June 30, 2012, and no collateral held related to securities lending transactions.

Fixed income securities were loaned and collateralized by the DDEF's agent with cash and U.S. Government Securities (exclusive of mortgage backed securities and letters of credit), and irrevocable letters of credit. When the loaned securities had collateral denominated in the same currency, the collateral requirement was 102 percent of the fair value, including accrued interest, of the securities loaned. All other securities were required to be collateralized at 105 percent of the fair value, including accrued interest, of the loaned securities.

During fiscal year 2012, securities lending transactions could be terminated on demand by either the DDEF Funds or the borrower. The weighted average maturity of loans for 2012 was 1.5 days. Cash collateral was invested by the DDEF Funds' in the WSIB's short-term investment pool. Because the securities lending agreements were terminable at will, their duration did not generally match the duration of the investments made with the cash collateral. Non-cash collateral could not be pledged or sold absent borrower default. There are no restrictions on the amount of securities that can be lent.

Securities were lent with the agreement that they would be returned in the future for exchange of the collateral. JPMorgan indemnified the WSIB by agreeing to purchase replacement securities or return the cash collateral in the event a borrower failed to return the loaned securities or pay distributions thereon. JPMorgan's responsibilities included performing appropriate borrower and collateral investment credit analyses, demanding adequate types and levels of collateral, and complying with applicable federal regulations concerning securities lending.

During fiscal year 2012, there were no significant violations of legal or contractual provisions, no failures by any borrowers to return loaned securities or to pay distributions thereon. Further, the DDEF Funds incurred no losses during fiscal year 2012 resulting from a default by either the borrowers or the securities lending agents.

Note 5. Summary of Investment Policy

Under RCW 43.33A.030, trusteeship of DDEF is vested within the voting members of the WSIB. The Legislature has established a standard of care for investment of these funds in RCW 43.33A.140. Additionally, the WSIB and its staff must comply with other state laws, such as the Ethics in Public Service Act, 42.52 RCW, as it makes its investment decisions and seeks to meet the following investment objectives.

In accordance with RCW 43.33A.110, the portfolio is managed to achieve a maximum return at a prudent level of risk. The key determinate is identifying the prudent level of risk for a program relative to the needs of the Developmental Disabilities Life Opportunities Trust Governing Board and the participants. Based on this requirement, the order of the objectives shall be:

- Maximize return at a prudent level of risk based on identified investment time horizons;
- Ensure sufficient assets are available to fund the expected needs; and
- Invest in a manner that will not comprise public confidence in the program.

Risk Constraint Standards

- All assets under management by the WSIB are to be invested to maximize return at a prudent level of risk in accordance with the requirements of RCW 43.33A.110 and RCW 43.33A.140; and
- Diversify the assets at a prudent level to moderate fluctuations in the fair value of the program.

Permissible Investments

Fixed Income: The fixed income portfolio will be limited to the Bond Market Fund (WSIB Policy 2.14.200). The Treasury Inflation Protection Securities portfolio will be invested in U.S. Inflation Indexed Bonds.
U.S. Equity: The U.S. equity portfolio will be invested in a passive commingled fund managed to track a U.S. broad market index, currently the MSCI U.S. Investable Market Index (MSCI U.S. IMI)
Balanced Mutual Funds: DDEF – Private will invest in the Vanguard Balanced Index – Institutional Share's mutual fund.
Non-US Equity: The international equity portfolio will be invested in a passive commingled fund managed to track a broad non-U.S. market index, currently the MSCI All Country ex U.S. Investable Market Index (MSCI ACWI ex U.S. IMI)
Cash: The cash portfolio will be invested in Short-term Investment Funds and Money Market Funds.

Asset Allocation

The asset allocation policy has been developed with the performance objectives of:

- Short-term: Earn a rate of return that exceeds inflation, with a bias toward preservation of corpus; and
- Long-term: Earn a rate of return that exceeds inflation plus a set spending rate.

Assets are rebalanced across asset classes when market values fall outside respective policy ranges as follows:

State Funds	Target	Range
Cash	0%	0-5%
Fixed Income	41%	38-44%
U.S. Equity	9%	6-12%
International Equity	8%	5-11%
TIPS	42%	39-45%

Private Funds	Target
Cash	$10,000
Fixed Income	40%
Equity	60%

Schedule 1: Schedule of Maturities and Credit Ratings

Investment Type	Total Fair Value	Maturity: Less than 1 year	Maturity: 1-5 years	Maturity: 6-10 years	Maturity: More than 10 years	Effective Duration	Credit Rating
Treasury Inflation Protected Securities	$ 4,301,514	$ -	$ -	$ 4,301,514	$ -	4.40	AAA
Commingled Intermediate Credit	4,266,435	440,863	1,694,128	2,131,444	-	4.61	Schedule 2
	8,567,949	$ 440,863	$ 1,694,128	$ 6,432,958	$ -		
Investments Not Required to be Categorized							
Commingled Equity Index Funds - Domestic	985,606						
Commingled Equity Index Funds - Foreign	846,635						
Commingled Balanced Trust	22,940,580						
Money Market Funds	17,606						
Total Investments Not Categorized	24,790,427						
Total Investments	$ 33,358,376						

Schedule 2: Additional Credit Rating Disclosures

Moody's Equivalent Credit Rating	Market Value
Aaa	$ 518,038
Aa1	14,590
Aa2	71,198
Aa3	535,061
A1	282,001
A2	512,523
A3	354,697
Baa1	630,639
Baa2	888,164
Baa3	459,524
Total Fair Value	$ 4,266,435

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2100 EVERGREEN PARK DRIVE SW, P.O. BOX 40916, OLYMPIA, WA 98504