

Insight

Fourth Quarter 2014



Bruce Rauner, Governor

Exciting changes coming to the State of Illinois Deferred Compensation Plan

Plan enhancements

As part of its commitment to helping you prepare for a more secure retirement, the Illinois State Board of Investment (ISBI) is making several investment enhancements to the State of Illinois Deferred Compensation Plan (DCP) in the coming months. Detailed information about these changes and how they may affect you will be sent to you in the coming weeks. Some highlights are included below.

Investment lineup changes slated for Spring 2015

Currently, ISBI is conducting a search among small cap providers to find a small cap investment that is in line with ISBI's commitment to offering investments with a proven track record of consistent investment management, performance history, and appropriateness for long-term retirement investors. A decision on a small cap fund company will be announced in Spring 2015.

During Spring 2015, the current target-date investments offered in the DCP will be replaced by institutionally priced target-date trusts, which will significantly reduce fees for participants invested in these options.

Choose among two paths for a DCP reenrollment

After the investment lineup changes are complete, you will be given an opportunity to choose from one of two paths to determine how to invest your current DCP assets and your future contributions. You can choose among the DCPs core investment options to create your own diversified portfolio. Or, you may select one of the preassembled, institutionally priced target-date trusts available in the DCP for a diversified portfolio that you can carry to and through retirement. ISBI is pursuing these and other opportunities to help improve your asset allocation and your retirement readiness.

Employee meetings

T. Rowe Price will host onsite meetings in some locations, as well as webinars open to all employees, explaining the changes and what they mean to you.

Don't miss out on key communications!

Log in to the T. Rowe Price website at rps.troweprice.com and update/provide your preferred email address right from the home page.

Understanding plan fees and expenses

The State of Illinois Deferred Compensation Plan (DCP) provides a great way to save for your retirement. It lets you defer part of your salary before taxes and invest the money in a variety of investment options. Of course, there are costs associated with participating in any 457 plan, like the DCP, for services like plan administration and investment management.

So whether you are currently participating in the DCP or you plan to participate in the future, take a few moments to understand these fees and their impact on your retirement savings.

Fees associated with 457 retirement plans

Generally, there are four types of fees associated with 457 plans like the DCP.

Administrative fees

Administrative fees generally cover the costs of operating the plan and may pay for expenses such as recordkeeping, accounting, trustee services, auditing services, legal services, account statements and educational materials. The administrative fee you pay each quarter covers these expenses and appears on your individual quarterly statements.

Fees from investments

All fees paid from investments are included in the investment's expense ratio or trust fee for trust accounts. These fees cover the costs associated with managing plan investments, as well as distribution and marketing fees. These fees are deducted directly from the investment, thereby reducing the investment returns by the amount noted in the expense ratio or trust fee.

Individual fees

There are individual fees associated with things like loans, hardship withdrawals, and the processing of Qualified Domestic Relations Orders. The DCP offers these services to all participants in the DCP, but you only pay for these if you use them. For example, if you were to initiate a loan, you would be assessed a one-time loan initiation fee of \$75, which covers the cost of processing the loan.

Redemption fees

Although the DCP does not currently offer any investments that charge a redemption fee, some 457 plans do carry them. Redemption fees are designed to mitigate the effect of short-term trading and protect the fund and its long-term investors, as well as to help offset the transaction costs that may be generated by frequent trading. Redemption fees are charged only to those participants who sell shares of a mutual fund on or before a designated holding period specified by the fund.

Would you like more information?

If you have questions or would like additional information, you can call **1-888-457-5770** or log in to the website at **rps.troweprice.com** to request a prospectus, trust report, or other information.

Administrative Rules Amendment

Following a recent review, the State of Illinois Deferred Compensation Plan's Administrative Rules are undergoing an amendment to clarify that the alternative Normal Retirement Age for Special Catch-up purposes may not be later than the date the participant attains the age of 70½. This clarification is in compliance with the Internal Revenue Code. The Department of Central Management Services will continue to notify participants of their maximum deferral levels when they are released by the Department of Labor.

Call 1-888-457-5770 to request a prospectus, which includes investment objectives, risks, fees, expenses, and other information that you should read and consider carefully before investing.

To reduce your risk, spread out your assets

When investing, most people want to reduce their risk. One strategy for reducing your risk is called asset allocation. It's how you divide your portfolio between different types of investments.

The State of Illinois Deferred Compensation Plan (DCP) offers a range of investment choices so you can build a well-allocated portfolio.

Don't put all your eggs in one basket

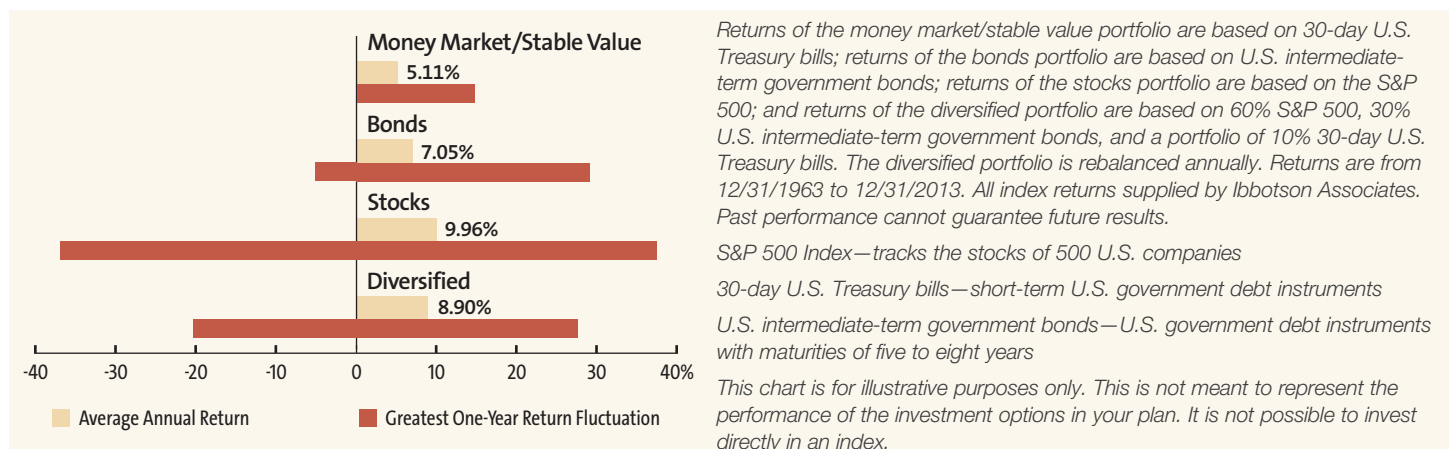
Remember the old saying, "Don't put all your eggs in one basket"? Basically, asset allocation is putting your eggs (or dollars) in several baskets (or types of investments). You can practice asset allocation when you choose several types of investments (stock, bond, or money market/stable value investments). Asset allocation can help reduce the overall market risk of your portfolio. The reason: No single type of investment performs well all the time. When one type of investment is in a slump, another is often performing well. If your money is in many types of investments, you won't lose all of it if one investment is doing poorly. However, asset allocation cannot assure a profit or protect against loss in declining markets.

Generally, your investment choices fall into three broad types. You may invest in all three:

- **Money Market/Stable Value**—lower-risk investments like money market instruments and guaranteed investment contracts (GICs).
- **Bonds**—medium-risk investments.
- **Stocks**—higher-risk investments.

How asset allocation can get results

The graph below shows how an investment would have grown between 1963 and 2013 invested four different ways: money market/stable value investments, bonds, stocks, and a mix of all three. Notice how the allocated mix (diversified)—the combination of all three—outperformed money market/stable value investments and bonds alone, with less fluctuation than stocks.



Putting allocation into practice

The next question to consider is: What mix of investments (stocks, bonds, money market/stable value) may be appropriate for you? The answer depends on your time horizon. The further away you are from retirement, or the longer your time horizon, the more aggressive you can afford to be with your asset allocation. That's because you have more time to ride out short-term market fluctuations.

For example, if you are:

- More than 15 years from retiring, you might invest 100% in stocks.
- Within 10 to 14 years from retiring, you might decrease your stock investments and add fixed income (bonds) investments.
- Less than 10 years from retirement, you might further decrease your allocation to stocks, increase fixed income, and add stable value/money market investments.
- In retirement, which could last up to 30 years, you may want to keep a small percentage of your portfolio invested in stocks for growth potential.

It's also a good idea to rebalance your portfolio on a regular basis, to keep (or adjust as necessary) your asset allocation strategy on track.

Would you like more information?

If you like more information on investing or about the specific investments available through the DCP, visit the website at rps.troweprice.com. Or call 1-888-457-5770. T. Rowe Price representatives are available during business days between 7 a.m. and 10 p.m. eastern time.

What does being on the “Watch List” mean?

It is important that you understand what it means to be on the Watch List and, perhaps more importantly, what it does not mean. Being on the Watch List, as the name would imply, simply means we believe there is good reason to watch this fund more closely. Being on the Watch List does not mean you should immediately sell your fund shares. It is not unusual for a fund to appear on the list from time to time. It does not mean the fund is necessarily a bad investment. If we believe the fund no longer represents a suitable investment option, we will remove the fund from the 457 Plan.

Why are funds placed on the Watch List?

Funds can be placed on the Watch List for several reasons. Why a fund is on the Watch List is more important than the mere fact that it is on the Watch List. The most typical reasons are as follows:

1. **Performance**—The most common reason a fund is placed on the Watch List is poor performance relative to its appropriate market benchmark and/or peer group. When signs of relative underperformance appear, we place a fund on the Watch List.
2. **Risk**—Less obvious to many participants is the risk that a fund manager incurs. If a fund becomes too volatile, we will place it on the Watch List.
3. **Risk-Adjusted Returns**—What returns has the fund manager been able to deliver relative to the risk the fund has incurred? If the manager is unable to deliver adequate returns for the risk taken, we will place the fund on the Watch List.
4. **Portfolio Construction/Style Drift**—Is the fund manager investing the money in the way he or she said? If you invest part of your assets in an aggressive fund that is supposed to be investing in the stocks of small, growth-oriented companies, then you want the manager to do just that. We monitor the manager’s portfolio, and if the security holdings do not reflect what has been communicated, we place the fund on the Watch List.
5. **Operations**—There are many operational reasons for placing a fund on the Watch List. For example, the manager of the fund could leave. Remember, when you purchase shares of a mutual fund, what you are really doing is hiring a professional portfolio manager to invest your money. If that manager leaves, you should watch the fund closely. There could also be firm-level issues. These can include issues such as regulatory violations, turnover in senior management, or a merger or acquisition. Any of these operational issues will automatically place a fund on the Watch List.

Current Watch List as of 12/31/2014

Columbia Acorn Fund, Z (“Acorn Fund”)—The Acorn Fund was placed on “On Notice” status due to performance concerns. Over the past three and five years, the Fund has lagged its benchmark and peer group, ranking in the bottom quartile of returns in the small growth peer group universe. The Fund’s allocation to international stocks detracted from performance. The Fund has less than 6% allocated to small-cap international names. A significantly underweight exposure to healthcare names also detracted from performance. While the majority of the Fund’s assets are invested in small company stocks, an allocation to mid-cap stocks added to returns in this year as the Fund outperformed its benchmark. Participants seeking a similar investment strategy have access to the Northern Trust Small Cap Separate Acct which also invests in domestic small-cap stocks.

-Watch List prepared by Marquette Associates, Inc.

TELEPHONE NUMBERS

DEFERRED COMPENSATION

Plan Rules/Options Information
800-442-1300/217-782-7006

TDD/TTY: 800-526-0844

Internet: <http://www.state.il.us/cms/employee/defcom>

RECORDKEEPER

T. Rowe Price Retirement Plan Services, Inc.
Account Value Information and Investment Changes:
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