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 If we believe the fund no longer represents a suitable investment option, we will remove the fund from the Plan.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.

WATCH LIST—THE STATE OF ILLINOIS DEFERRED COMPENSATION PLAN

Current Watch List Summary

The following funds are on the watch list as of 06/30/2008:

Ariel Fund has underperformed year-to-date and continues to lag for the longer-term periods. The fund ranks in the 99th percentile for Small-Mid-Cap Value funds year-to-date through May 31, 2008. The fund is down 8.47% vs. its benchmark, which is up 1.07%. The fund has moved up in market cap and therefore we have reclassified it as a Small-Mid Value fund benchmarked to the Russell 2500 Value Index. For those participants who bought this fund for Small Value exposure, the Plan has added a new Small Value option, the Northern Small Cap Value Fund. We are keeping the fund on the watch list due to the poor performance.

Legg Mason Value Trust continues to be hurt by exposure to financial firms. The fund is in the 99th percentile year-to-date through May 31, 2008. The fund is positioned for the rebound from the credit crunch and housing crisis and should do very well when that happens, but it will continue to underperform as long as the crisis continues and it appears that the crisis is continuing much longer than anticipated. This fund is highly concentrated and therefore very volatile. For those wishing for a more stable large-cap blend option, there is the Vanguard index fund in the Plan.

Fidelity Puritan was placed on the watch list due to a manager change. The fund has outperformed slightly for the three-month period, although it has struggled year-to-date through May 31, 2008. The year-to-date issues are primarily due to an overweight of corporate bonds and an underweight to Treasury securities within the fixed-income portion of the portfolio. We are not overly concerned about the short-term performance, but anytime there is a change in the portfolio management we automatically place the fund on the watch list. We will continue to monitor the new managers closely.

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SECOND QUARTER | JULY 2008 | ROD R. BLAGOJEVICH, GOVERNOR

Insight

A QUARTERLY PERIODICAL DEDICATED TO HELPING YOU PREPARE FOR TOMORROW

REMINDER OF YOUR DEFERRED COMPENSATION PLAN FEATURES

As a participant in the State of Illinois Deferred Compensation Plan, you already know the many benefits associated with saving for retirement through the Plan. To ensure that you are up to date on how the Plan works, below is a list of Plan features:

Pretax contributions: Your contributions to the Plan are made pretax, potentially reducing your current taxable income and postponing income tax on your contributions and earnings until you take a withdrawal, usually when you retire.

Contribution amounts: You may contribute as little as $10 per pay period or $20 per month to the Plan, whichever is greater. The maximum amount you can contribute is 100%* of your pay, subject to IRS limits ($15,500 in 2008).

Catch-up contributions: If you will turn 50 or older this year and are already contributing the maximum amount allowed by your Plan, you may contribute an additional amount of "catch-up contributions" up to the IRS limit of $5,000 in 2008.

Rollover contributions: You may consolidate your retirement savings by "rolling over" vested balances from other employers' eligible plans, including 401(k), 403(b), or other 457 plans. These amounts will be credited to your rollover contribution source within your Plan account.

Free tools to help you manage your account: Your Plan also offers easy access to free online calculators and tools that can help you manage your retirement account.

Investment guidance from Morningstar: For help in managing your retirement account, use the Morningstar® Retirement Manager℠ guidance service, which will help you answer the following questions:

- How do I set a retirement goal?
- How much should I save?
- How should I allocate my account?

SAVE THE DATE!

Columbia Acorn Funds Annual Shareholder Information Meeting

When:
Tuesday, September 23, 2008
12 p.m. to 1 p.m. Central time

Where:
Chase Bank Auditorium, Plaza Level
38 South Dearborn Street
Chicago, IL 60602

A buffet lunch will be served at 11:30 a.m.

We will also be offering a Webcast of the meeting. Additional details will be available in July at www.columbiafunds.com and in our semiannual report to shareholders.

Please RSVP by September 18 if you plan to attend. Call (800) 922-6769.

T. Rowe Price Automatic Rebalancing: Rebalancing your account regularly is good investment practice. When you sign up for auto-rebalancing, your account is rebalanced for you quarterly, semiannually, or annually — restoring your chosen allocation of stocks, bonds, and money market/stable value investments.

The Morningstar name and trademarks are used under license from Morningstar Associates, LLC. Investment advisory products and services are provided solely by Morningstar Associates, LLC, a registered investment advisor and a wholly owned subsidiary of Morningstar, Inc. Morningstar Associates, LLC, is not affiliated with, nor is it an employee or agent of, T. Rowe Price. Plan sponsors must elect to make the Morningstar services available.

**Mandatory FICA and FUTA deductions will be taken before salary deductions.*

WHAT EVERY INVESTOR SHOULD KNOW…

When you understand the economic forces that drive the stock market, you'll be less likely to overreact to daily market fluctuation.

Economic indicators

The next time you hear a television or radio report about the economy, stop to consider how the information may affect the market and your investments. By collecting information about demand, production, employment, and income, economists provide insight into the health of our country's economy. Each of these economic indicators is linked to the others. Demand for goods and services requires that they be produced. Production requires employment of workers. Income paid to workers fuels spending, which in turn supports subsequent rounds of production, employment, and income. Strength in one area tends to generate strength in another, and weakness tends to generate weakness. The following is a quick overview of these basic indicators.

Demand

Gross domestic product (GDP) measures the output of goods and services produced in the U.S. based on market demand. It includes information about consumer spending, housing construction and sales, business capital spending, government spending, and foreign trade. If GDP is increasing fast enough to provide jobs for those who want them, the economy is thought to be doing well, and stock markets normally respond in a positive way. Sluggish growth or outright declines in GDP may indicate the economy is not doing well. This may cause stocks to fall and bonds to rise. You can access additional information about GDP by visiting www.doc.gov.

Production

Reviewing the manufacturing sector, which makes up 15% to 20% of the GDP, can help identify strengthening or weakening trends in the economy. The manufacturing sector is cyclical—it tends to shrink when the economy is weak and grow when the economy is strong. The performance of the manufacturing sector allows economists to make inferences about the overall health of the economy. The Institute for Supply Management (ISM) produces a monthly index of manufacturing activity. You can learn more by visiting www.ism.ws.

Employment

One of the most common statistics considered when measuring employment is jobless claims, which are initial claims for unemployment insurance. Jobless claims also provide information about the strength of the economy. Lower levels of unemployment claims are associated with job gains and a strong economy, while higher levels of unemployment claims are indicative of a weak economy. The Bureau of Labor Statistics publishes comprehensive information on employment and unemployment in a monthly report that you can read at www.bls.gov.

Income

The Department of Labor publishes a monthly report on the employment situation in the United States. It includes data about average weekly hours worked, average hourly earnings, and the number of people employed, which can be used to estimate total income from wages. Income is the main driver behind spending, so income-related information helps forecast future spending. At the end of each month, the Commerce Department releases a comprehensive report on personal income during the previous month. You can learn more at www.doc.gov.

What can you do?

Economic indicators may move markets, but try not to overreact to them. You choose an asset allocation strategy to fit your specific goals, time frames, and risk tolerances. Unless these factors have changed, you shouldn't have any reason to move your money around. If you haven't developed a strategy for your retirement savings, please visit ***my***RetirementPlan at **rps.troweprice.com**. The tools and resources available on the Web site can help you make informed decisions about investing your savings. Or call 1-888-457-5770 to speak to a representative.

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:
888-457-5770 or TDD/TTY: 800-521-0325
Internet Access: 800-541-3022
Internet: http://rps.troweprice.com

INCREASE YOUR CONTRIBUTION AND SAVE MORE FOR RETIREMENT

Retiring in comfort means providing yourself with enough income to maintain your lifestyle once you've stopped working. The trick is making sure your contributions increase as your income does.

Here's the good news: More than 50% of American workers are saving for retirement. You're one of them, so take a moment to congratulate yourself. Now for the bad news: Many have saved less than $25,000.[1]

If you're in your 20s...

If you're in your 20s, and just starting out, $25,000 in savings may seem like a lot. So how do you prevent a good start from turning into not enough savings? It's easy. You get in the habit of paying yourself first. Whenever you get a raise or a bonus, you increase the amount of your contributions to your retirement plan account. For many people, that means increasing their contributions once each year.

If you're older...

There is a reason you're not saving more, right? You may be making house payments, car payments, or tuition payments. Or perhaps you're working hard to keep your family clothed and fed. Unfortunately, your expenses during retirement are unlikely to be significantly lower than they are today. That's why it is essential for you to pay yourself first by increasing your contribution amount each year. Remember, your main source of income during retirement may be the money you've put away.

Save while you can

Most people plan to work during retirement; however, the average retiree today left the workforce at age 62 because of health problems, disabilities, or layoffs.[1] The future is unpredictable. Save while you can.

More than 50% of retirees say their income needs in retirement are the same or higher than their preretirement income.[1] You may need more than you think to live comfortably in retirement.

While you may start receiving Social Security benefits as early as age 62, for most, full benefits are not available until age 65 or older. The table below shows you at what age you may start receiving full benefits based on your year of birth.

Boost your deferral amount

While having a state-funded pension helps, boosting your deferred compensation contribution amount each year improves the chance that your retirement nest egg will keep pace with your income. That's important because it can help you maintain your lifestyle in retirement.

To make a change to your deferral amount, visit the ***my***RetirementPlan Web site at **rps.troweprice.com** to download the deferral change form. On the ***my***RetirementPlan Web site, choose Plan Info, click on the Forms & Literature tab, then click on the Change Form link. Once you complete the change form, please return it to Central Management Services (CMS).

RETIREMENT AGE TO RECEIVE FULL SOCIAL SECURITY BENEFITS IS INCREASING

Year of Birth	1938	1939	1940	1941	1942	1943-1954	1955	1956	1957	1958	1959	1960 and later
Full Benefits Retirement Age	65 and 2 mos.	65 and 4 mos.	65 and 6 mos.	65 and 8 mos.	65 and 10 mos.	66	66 and 2 mos.	66 and 4 mos.	66 and 6 mos.	66 and 8 mos.	66 and 10 mos.	67

Source: Social Security online, 2006.

[1]*Source: Employee Benefits Research Institute 2006 Retirement Confidence Survey.*