

Taxes are an important consideration for mutual fund investing. There are three ways in which a mutual fund can generate income taxes for you if you hold fund shares in a non-tax-qualified account:

- **Income Distributions**
- **Capital Gains Distributions**
- **Sales or Exchanges of Shares**

State Farm Mutual Funds® generally do not pay federal income tax on the income or capital gains they earn on their investments when those earnings are passed on to you and other shareholders who, in turn, pay taxes on the distributions.

Income is generated by a mutual fund from the dividends and interest it receives on its investments. Operating expenses are then subtracted from these earnings, and the remaining profit is distributed to you and other shareholders in the form of dividends.

Capital gains are generated by a mutual fund through the selling of investments within the portfolio. After netting capital gains and losses of all the sales of investments within the portfolio of the fund, if net long-term capital gain exceeds net short-term capital loss, the fund has a net capital gain. This net capital gain will be distributed to you and other shareholders in the form of a capital gains distribution. A capital gains distribution you receive from a mutual fund will be taxed at the long-term capital gains tax rates even if you held the fund shares for one year or less. If the fund has a net short-term capital gain, this gain is distributed to you and other shareholders as an ordinary dividend rather than a capital gains distribution. Net capital losses are not distributed to you; rather, the fund carries the losses forward to future years to offset future capital gains of the fund.

Sales or exchanges of shares of a mutual fund by you may also generate taxes in a non-tax-qualified account. When you redeem shares of a mutual fund, you realize a capital gain or loss if the sales price differs from your cost basis in the shares you sold.

Your capital gains and losses are categorized into short-term and long-term for federal income tax purposes. If you held your shares of the mutual fund for 12 months or less, your capital gain or loss from fund share sales or exchanges will be categorized as short-term capital gain or loss; if your shares were held longer than 12 months, you will realize a long-term capital gain or loss. The amount of federal income tax you pay depends on your holding period and your particular tax bracket. See the "Dividends, Capital Gains, and Foreign Taxes Information" link for further information.

You may generate capital gains (losses) on any sale of fund shares, including sales of shares in a tax-exempt fund (such as the State Farm Tax Advantaged Bond Fund or the State Farm Municipal Bond Fund) held outside a tax-qualified account. Exchanges between funds held in a non-tax-qualified account may also generate taxes for you because an exchange from one fund into another fund is considered a sale and purchase for tax purposes. Therefore, if the sales proceeds out of the fund differ from your cost basis of the sold shares, the exchange will result in a capital gain or loss. Even if the exchange does not result in a capital gain or loss, your holding period in the new fund will begin as of the date of the exchange, not the date of purchase of the old fund.

This information should assist an individual who is a citizen or resident of the United States with filing their 2008 federal and state income tax returns, but it is not intended to serve as legal or tax advice. For any specific tax questions, you should contact the Internal Revenue Service (IRS) at 1-800-829-1040, or consult your tax advisor.

Tax forms will be mailed to shareowners at the end of January 2009. Your individual tax information can be viewed prior to the actual tax form being mailed when you access your account under the Mutual Funds tab on statefarm.com®. Planning ahead is important during tax season. Allocate enough time to provide a cushion for unexpected situations that may arise (e.g., mail delays). It is a good idea to keep all of your year-end records for each year that your account is open. This will allow you to access your information without any delay. To request a duplicate year-end 2008 record or tax form to be mailed to your address of record, please call us at 1-800-447-4930. It will take a minimum of five days to receive your duplicate record.

At State Farm Mutual Funds, representatives in our Securities Response Center are ready to assist you. However, due to the tax season, we anticipate heavy call volumes during the majority of our regular business hours: 8:00 a.m. to 6:00 p.m. CT Monday through Friday. Your call is important to us, and we look forward to providing you with the best service possible.

Securities Response Center: 1-800-447-4930

Securities through registered representatives of State Farm VP Management Corp., One State Farm Plaza, Bloomington, IL 61710-0001 (1-800-447-4930). Investment return and principal value will fluctuate and your investment, when redeemed, may be worth more or less than its original cost.

Securities, insurance and annuity products are not FDIC insured, are not guaranteed by State Farm Bank® and are subject to investment risk, including possible loss of principal.

In order to comply with Treasury Department regulations, we advise you that this document was prepared to promote and support the marketing of State Farm Mutual Funds. It is not intended to constitute tax advice, was not written or intended to be used by any taxpayer for the purpose of avoiding tax penalties that may be imposed on the taxpayer, and cannot be used by any taxpayer for that purpose. Advice regarding the tax treatment of State Farm Mutual Funds should be sought from an independent tax advisor in light of your particular circumstances.



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