

The background of the cover features a large, faint seal of the Orange County Employees Retirement System. The seal is circular and contains a central pyramid with an eye at its apex. The Latin motto "ANNO DOMINI MDCCLXXIII" is inscribed in an arc above the pyramid, and "NOVUS ORDO SECTORUM" is inscribed in an arc below it. The entire seal is surrounded by intricate, decorative scrollwork and patterns.

COMPREHENSIVE ANNUAL FINANCIAL REPORT

FOR THE YEAR ENDED DECEMBER 31, 2002

ORANGE COUNTY EMPLOYEES RETIREMENT SYSTEM
ORANGE COUNTY, CALIFORNIA

COMPREHENSIVE ANNUAL FINANCIAL REPORT

For the Year Ended December 31, 2002

**Orange County Employees Retirement System
Orange County, California**

**Keith Bozarth
Chief Executive Officer**

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I. Introductory Section



Executive Staff

Top row from left, Diane Schumacher, Keith Bozarth, Toi Dang, and Julie Wyne. Bottom row, Tanya Ho, Tracy Ayres, Thomas Flanigan, and James Buck.



Serving the Active and Retired Members of:

- ORANGE COUNTY LAFCD
- CITY OF SAN JUAN CAPISTRANO
- COUNTY OF ORANGE
- ORANGE COUNTY CHILDREN & FAMILIES SERVICES
- FOOTHILL/EASTERN/SAN JOAQUIN HILLS TRANSPORTATION CORRIDOR AGENCY
- ORANGE COUNTY CLUSTER DISTRICT
- ORANGE COUNTY EMPLOYEES RETIREMENT SYSTEM
- ORANGE COUNTY FIRE AUTHORITY
- ORANGE COUNTY LAW LIBRARY
- ORANGE COUNTY TRANSPORTATION AUTHORITY
- ORANGE COUNTY VECTOR CONTROL DISTRICT
- SANITARIUM DISTRICT OF ORANGE COUNTY
- ORANGE COUNTY DEPARTMENT OF EDUCATION (closed to new members)
- UCI MEDICAL CENTER (closed to new members)

May 24, 2003

Board of Retirement
Orange County Employees Retirement System
2223 Wellington Avenue
Santa Ana, CA 92701

Dear Board Members:

It is with great pleasure that we submit the Comprehensive Annual Financial Report (CAFR) of the Orange County Employees Retirement System (OCERS) for the calendar year ended December 31, 2002, the System's 58th year of operation. Information contained in this report is designed to provide a complete and accurate review of the year's operations and is the responsibility of the OCERS' management.

Structure of the Report:

This report is presented in five sections:

- The Introductory Section describes the System's management and organizational structure, a summary of the plan provisions and a listing of the professional services used.
- The Financial Section contains the opinion of the independent auditors, Link, Murrel & Co., Management's Discussion and Analysis, and the general purpose financial statements of the System.
- The Investment Section contains the Investment Consultant's statement produced by Callan Associates, OCERS' investment consulting firm, along with graphs and schedules regarding asset allocation, asset diversification, and history of performance.
- The Actuarial Section includes the certification letter produced by the independent actuary, Towers Perrin, along with supporting schedules and information.
- The Statistical Section contains graphs and schedules with comparative data related to active and deferred membership, retired membership, average monthly retirement benefits, revenues and expenses, and participating employers.

Certificate of Achievement:

The Government Finance Officers Association of the United States and Canada (GFOA) awarded a Certificate of Achievement for Excellence in Financial Reporting to OCERS for its Comprehensive Annual Financial Report for the fiscal year ended December 31, 2001 (page 6). This was the eighth consecutive year that OCERS has achieved this prestigious award. The Certificate of Achievement is a national award recognizing conformance with the highest standards for preparation of state and local government financial reports.

ORANGE COUNTY EMPLOYEES RETIREMENT SYSTEM • 2223 Wellington Avenue, Santa Ana, CA 92701
Telephone (714) 558-6200 Fax (714) 558-6236

In order to be awarded a Certificate of Achievement, a governmental unit must publish an easily readable and efficiently organized Comprehensive Annual Financial Report, whose contents conform to program standards. Such comprehensive annual financial report must satisfy both accounting principles generally accepted in the United States of America and applicable legal requirements.

A Certificate of Achievement is valid for a period of one year only. We believe our current report continues to conform to the Certificate of Achievement program requirements, and we are submitting it to GFOA for evaluation.

Major Initiative:

OCERS is continuing with the installation of the new Membership Accounting Record System (MARS), commonly known as PensionGold, which is a product of Levi, Ray & Shoup, Inc.

Additional Retiree Benefit Account (ARBA):

Due to large realized losses occurring in year 2002, the ARBA account was not credited with interest earnings. In order to have sufficient funds to credit interest to the statutory reserve accounts, approximately \$271,446,000 was transferred from the ARBA account to the Unallocated Fund Balance. The balance of the ARBA account at December 31, 2002, was approximately \$56,950,000.

Retired Members Benefit Reserve (RMBR):

The Retired Members Benefit Account was created in 2002 to ensure the continued funding of medical grants and similar supplemental benefits for an additional period. All participating agencies may transfer a projected three years benefit payments to the RMBR balance that was created as a sub-account of the Employer Advanced Reserve Account. The RMBR account will be used to pay additional benefits to retirees when the ARBA balance is depleted. The RMBR balance will be funded on a three-year rolling method. As of December 31, 2002, the balance for the RMBR account was \$25,703,000.

Accounting System and Reports:

This CAFR was prepared in conformity with accounting principles generally accepted in the United States of America and reporting guidelines set forth by the Governmental Accounting Standards Board (GASB) Statements No. 3, 25, 28, 34, and the County Employees Retirement Law of 1937.

The accompanying financial statements are prepared using the accrual basis of accounting. Contributions from employers and members are recognized in the period in which members provide services; benefits and refunds are recognized when payable in accordance with the provisions of the plan. Investment income is recognized as revenue when earned. Expenses are recorded when corresponding liabilities are incurred, regardless of when payment is due.

Link, Murrel & Co., independent auditors, have audited the general purpose financial statements. Management believes that internal control is adequate and that the accompanying statements, schedules and tables are fairly presented.

Additions and Decreases to Plan Net Assets:

Due to poor market conditions during 2002, the total additions to plan net assets, including net depreciation in fair value of investments and investment management fees, were a negative \$177,982,000. This amount includes member and employer contributions of \$90,908,000, net investment loss of \$270,356,000, net security lending income of \$1,119,000 and net commission recapture income of \$347,000. Net investment loss, excluding net security lending income and net commission recapture income, represented a decrease of \$118,280,000 over the prior year. This decrease was attributable mainly to a \$102,882,000 increase in net depreciation in fair value of investments over the prior year and \$19,955,000 in lower interest earnings on fixed income investments. Details of the components of the additions to plan net assets are included in the Statements of Changes in Plan Net Assets on page 25.

Deductions to Plan Net Assets:

Deductions for 2002, excluding investment management and security lending fees, were \$194,310,000 which represented an increase of \$17,890,000 over the prior year. This increase was the result of higher retirement benefit payments and an increase in the number of retirees. The components of the total deductions are payments of retirement benefits of \$181,549,000, refunds of contributions and interest to terminated members of \$4,482,000 and administrative expenses of \$8,279,000.

Changes in System Membership:

OCERS' membership increases (decreases) for the calendar year 2002 were as follows:

	2002	2001	Increase (Decrease)	Change
Active Members	22,723	22,329	394	1.76%
Retired Members	8,688	8,216	472	5.74%
Deferred Members	1,377	1,418	(41)	(2.89%)
Pending Status Members	800	454	346	76.21%

As of December 31, 2002, there were 800 members who terminated membership with OCERS but had not selected an option regarding the management of their balances. Subsequently, all of the Pending Status Members either withdrew their funds or left them on deposit with OCERS, thus becoming Deferred Members.

Investment and Economic Summary:

The year 2002 continued to be a very challenging investment environment following the pattern of the last two years. The global equity markets continued to be plagued by concerns resulting from the Middle East conflict, terrorism and macroeconomic conditions. These concerns resulted in a tremendous amount of market uncertainty.

Equity markets continued to decline in the US and abroad in 2002. The broad equity benchmark Russell 3000 Index was down 21.54%, while the international markets benchmark MSCI EAFE Index was down 15.94% for the year. This was the third consecutive year in which both domestic and international equity markets had negative returns.

Within the domestic fixed income markets, there was a flight to quality sectors among investors. High quality sectors generated strong returns as investors sought safety amid unprecedented market turmoil.

The Lehman Brothers Universal Index for domestic fixed income markets was up 9.83%. The continued weakening of the US Dollar provided some healthy returns for the non-US fixed income markets as well.

For the 2002 year, OCERS' portfolio earned a negative return of 5.46%, which is 12.96% below the actuarial earnings assumption. Over longer term periods, the portfolio has earned total annualized negative returns of 1.87% over the past three years, a positive 4.27% over the past five years, and positive 8.41% over the past ten years. On a fair value basis, the total plan net assets decreased from \$4,562,541,000 to \$4,190,249,000.

Funding:

OCERS' funding objective is to meet long-term benefit obligations through contributions and investment income. As of December 31, 2002, the funding ratio of the System was 82.76%. A six-year history of OCERS' funding progress is presented on page 40. For 2002, OCERS experienced a decrease of \$372,292,000 in plan net assets. Details of the components of this decrease are included in the Statements of Changes in Plan Net Assets on page 25.

Conclusion:

We would like to take this opportunity to thank the members of the System for their confidence in OCERS during the past year. We also want to express our thanks to the Board of Retirement for its dedicated effort in supporting the System through this past year. Likewise, we thank the consultants and staff for their commitment to OCERS and for their diligent work to assure the System's continued successful operation.

Respectfully submitted,


Keith Bozarth
Chief Executive Officer


Toi Dang
Chief Financial Officer

Certificate of Achievement for Excellence in Financial Reporting

Presented to

Orange County Employees
Retirement System,
California

For its Comprehensive Annual
Financial Report
for the Fiscal Year Ended
December 31, 2001

A Certificate of Achievement for Excellence in Financial Reporting is presented by the Government Finance Officers Association of the United States and Canada to government units and public employee retirement systems whose comprehensive annual financial reports (CAFRs) achieve the highest standards in government accounting and financial reporting.



President

Executive Director

**Members of the Board of Retirement
December 31, 2002**

Regular Members:



Keith L. Concannon
Elected Member - Retired Employees
Term expires December 31, 2004



John M.W. Moorlach
Ex-Officio Member
County Treasurer-Tax Collector
Term expires December 31, 2006



Frank E. Eley, Chairman
Elected Member - General
Public Facilities &
Resources Department
Term expires December 31, 2004



Sharon Neebe
Elected Member - General
County Treasurer-Tax Collector
Term expires December 31, 2003



Thomas N. Fox*
Elected Member - Safety
Sheriff-Coroner Department
Term expires June 30, 2003



Reed L. Royalty, Vice-Chairman
Appointed Member
Appointed by Board of Supervisors
Term expires April 15, 2005



George W. Jeffries
Appointed Member
Appointed by Board of Supervisors
Term expires April 15, 2005



Lisa Welch-Silbar
Appointed Member
Appointed by Board of Supervisors
Term expires September 13, 2005



Thomas J. Lightvoet
Appointed Member
Appointed by Board of Supervisors
Term expires April 15, 2005



Alternate Member:

David Thompson
Elected Member – Safety
(Alternate for Safety Members)
Alternate for all Elected Members
Orange County Fire Authority
Term expires June 30, 2003

*Retired from the Board of Retirement in March 2003

**Summary of Plan Provisions
December 31, 2002**

1. Plan Description and History:

Following an effort by the employees of Orange County, a proposition was submitted to the people of Orange County. As a result of the General Election, OCERS was established in 1945 under the provisions of the County Employees Retirement Law of 1937. OCERS provides members with retirement, death, disability, and cost-of-living benefits. It is a cost-sharing, multiple-employer defined benefit pension plan governed by a nine-member Board of Retirement.

Members employed prior to September 21, 1979, are designated as Tier I members. The Board of Supervisors amended the plan by adopting certain sections of the Government Code for members entering the plan after September 20, 1979, who are designated as Tier II members. All regular full-time employees or part-time employees, scheduled to work 20 hours or more per week for the County or other participating employers become members of the plan upon employment.

2. Monthly Salary Base for Benefits:

Highest one-year average for Tier I members; three-year average for Tier II members.

3. Service Retirement:

A. Eligibility:

10 years of service and age 50, or 30 years of service and any age (20 years for safety members), or age 70 with any service.

B. Benefit Formula per Year of Service:

Please refer to OCERS' Summary Plan Description (SPD) and/or OCERS Website at www.ocers.org for the complete age factor tables.

Tier I: $1/50 \times \text{Final One Year Average Monthly Compensation} \times \text{Years of Service Credit} \times \text{Factor Based on Age at Retirement} = \text{Monthly Allowance}$.

Tier II: $1/60 \times \text{Final Three Year Average Monthly Compensation} \times \text{Years of Service Credit} \times \text{Factor Based on Age at Retirement} = \text{Monthly Allowance}$.

C. Retirement and related benefits for Law Enforcement members classified as Safety Members changed July 2002 to the "3% at 50" benefits under Government Code Section 31664.1. This change was reflected in both member and employer contribution rates and obligations effective with the December 31, 2001 actuarial valuation.

Retirement and related benefits for Fire Authority members classified as Safety Members changed July 2002 to the "3% at 50" benefits under Government Code Section 31664.1. Because this change was not agreed to and effective until after December 31, 2001, it will not be reflected in employer contribution rates and obligations until July 1, 2003, based on results of the December 31, 2002 actuarial valuation. Member contribution rates, however, changed effective July 1, 2002, to reflect the new benefit levels.

All Probation Officers were reclassified to Safety Members status effective June 28, 2002. Tier 1 members had all of their existing credited service converted to Safety Member service. Tier II members could elect to have their existing General Member credited service converted to a lesser amount of Safety Member credited service. These changes will be reflected in employer contribution rates beginning July 1, 2003, based on the December 31, 2002 actuarial valuation.

4. Non-Service Connected Disability:

A. Eligibility:

Five years of service.

B. Benefit Formula per Year of Service:

Tier I: $1.8\% \times \text{Years of Service Credit} \times \text{Final One Year Average Monthly Compensation}$. (If benefit is less than 1/3 of final average monthly compensation, years of service credit to age 62 can be added in order to pay up to a maximum of one-third of final average monthly compensation.)

Tier II: $1.5\% \times \text{Years of Service Credit} \times \text{Final Three Year Average Monthly Compensation}$. (If benefit is less than 1/3 of final average monthly compensation, years of service credit to age 65 can be added in order to pay up to a maximum of one-third of final average monthly compensation.)

5. Service Connected Disability:

A. Eligibility:

No age or service requirement.

B. Benefit:

50% of final average monthly compensation or service retirement if the benefits are higher.

6. Active Member Death:

If not eligible for a service retirement or for a non-service connected disability at the time of death, refund of employee contributions with interest plus one month's salary for each year of service to a maximum of six months' salary.

7. If Eligible to Retire for a Service or for a Non-Service Connected Disability at the Time of Death:

Qualified Surviving Spouse, or child, has the following options:

A. Refund of employee contributions with interest plus one month's salary for each year of service to a maximum of six months' salary; or

B. 60% of earned benefit payable to surviving eligible spouse; or

C. Combined benefit equal to a lump-sum payment plus a reduced monthly allowance.

If no eligible spouse or child exists, the named beneficiary receives refund of employee contributions with interest plus one month's salary for each year of service to a maximum of six months' salary.

8. Service-Connected Death:

50% of final average monthly compensation payable to qualified spouse, or eligible child (if no qualified spouse).

9. Death After Retirement:

A. Non-Service Connected Disability Retirement:

60% of member's unmodified allowance continued to eligible spouse. (Member may elect a modified allowance at time of retirement.)

B. Service-Connected Disability Retirement:

100% of member's allowance continued to eligible spouse or eligible child.

C. \$1,000 Burial Benefit:

Payable to named beneficiary following death of original retiree.

D. Service Retirement:

Benefit depends upon option chosen.

10. Termination of Employment:

Refund of accumulated employee contributions with interest. The five year vesting requirement is eliminated effective January 1, 2003. If contributions are left on deposit, the member is entitled to the earned benefits commencing at any time after the member reaches retirement eligibility age.

11. Post-Retirement Cost-of-Living Benefits:

Based on changes in Consumer Price Index to a maximum of 3% per year; percentage in excess of 3% is "banked" for future increases.

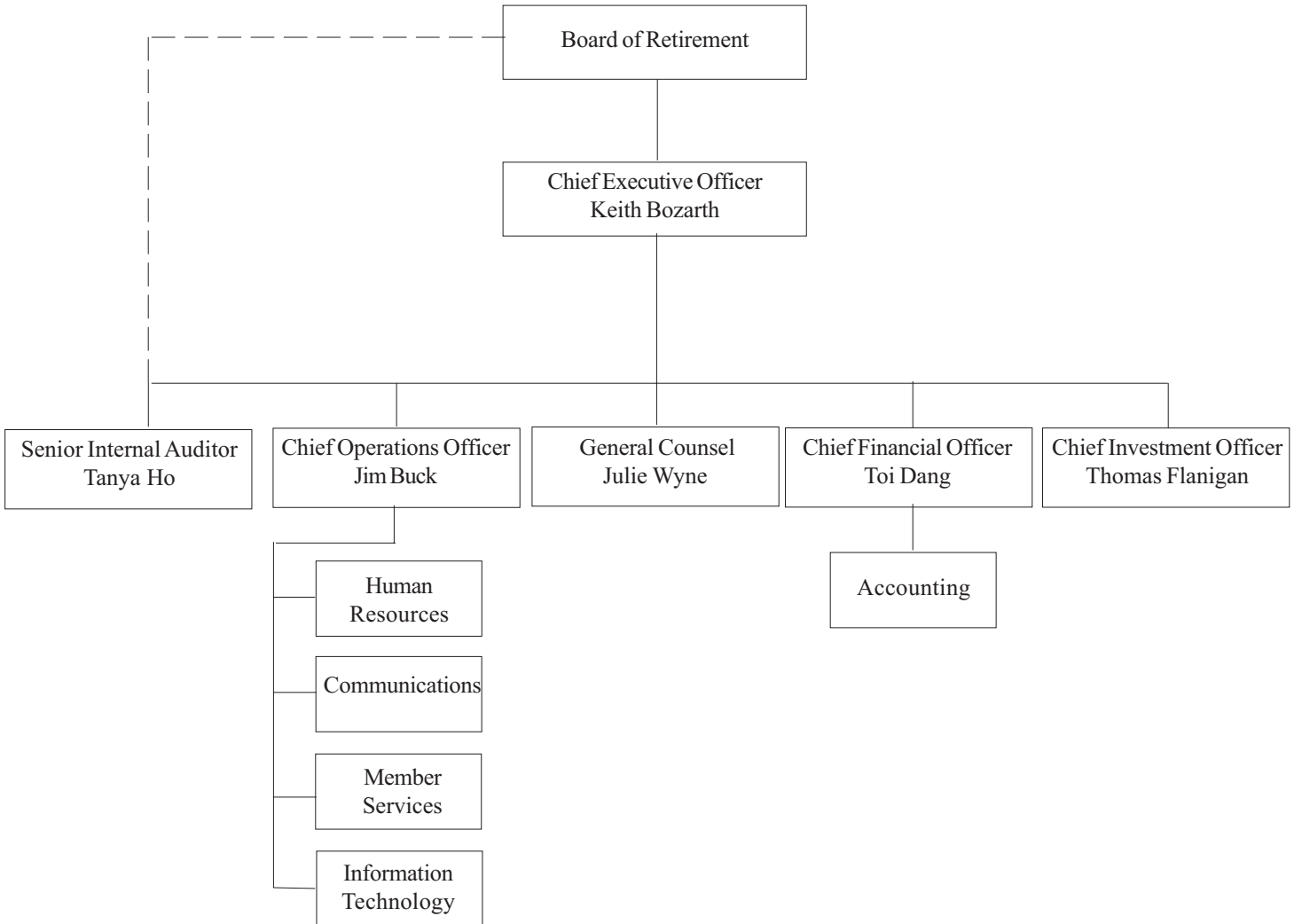
12. Employer Contributions:

Determined by Projected Unit Credit funding method with a 30-year declining period amortization of Unfunded Actuarial Accrued Liability.

13. Member Contributions - Tier I (Tier II in parentheses):

Normal based on entry age, 1/200 (1/120) at 60 for General Members; 1/200 (1/100) at 50 for Safety Members. Cost-of-Living contributions equal to percentage of normal: 51.90% (31.40%) for Non-OCTA General; 50.96% (35.56%) for OCTA General; 108.80% (54.86%) for Firefighters; 113.32% (57.36%) for Law Enforcement; 28.28% (14.10%) for Probation Officers.

**Orange County Employees Retirement System
Organization Chart
December 31, 2002**



Orange County Employees Retirement System Organization

Board of Retirement: The Board of Retirement is responsible for establishing policies governing the administration of the retirement plan, making benefit determinations, establishing investment policy for the system and monitoring execution of its policies. The Board of Retirement consists of nine members and one alternate. Four members of the Board of Retirement are appointed by the Board of Supervisors of the County; three members and one alternate member are elected by active members of the system; one member is elected by the retirees; and the Treasurer of the County is an ex-officio member.

Executive: This department consists of the Chief Executive Officer (CEO) who implements and executes policies promulgated by the Board of Retirement. The Chief Operations Officer (COO), Chief Financial Officer (CFO), Senior Internal Auditor, General Counsel, and the Chief Investment Officer (CIO) assist the CEO in the daily operations of the system.

Investment Department: This department is responsible for the administration and management of the investment program, in accordance with policies, regulations, and guidelines set forth by the Board of Retirement. It is responsible for the interface with investment managers, including monitoring investment performance objectives, adherence to investment guidelines, conducting due diligence visits to investment managers' sites, and interviewing prospective investment managers. This department is also responsible for the interface with outside investment consultants in reviewing and evaluating all investment managers' performance and quarterly investment manager fees.

Operations Department: This department is comprised of the Member Services, Administrative/Human Resources, Information Technology, and Communications divisions. The Member Services Division is responsible for providing all benefit services to the members of the system. This includes benefit calculations, evaluation of claims for disability retirement, preparation of data to support applications for retirement, preparation of the retiree payroll, and membership counseling. The Administrative/Human Resources Division is responsible for providing the contract administration, purchasing, and personnel functions of OCERS. The Information Technology Division is responsible for OCERS' network systems, personal computers and Web site, while providing programming and technical support on our Benefits Administration System. In addition, this division is responsible for the production of retiree payroll and administering all audio/visual functions. The Communications Division is responsible for communications to all active, retired, and deferred members through publications, newsletters and OCER'S Web site.

Finance Department: This department is comprised of the Accounting Division. The Accounting Division is responsible for all the financial records and reports of OCERS. This includes the preparation of the Comprehensive Annual Financial Report, monthly and quarterly financial statements and the annual operating budget. The Accounting Division also maintains OCERS' system of internal control; balances retirement payroll, refunds of contribution and interest to members; balances members' contributions, reconciles investment portfolios and processes all invoices for goods received and services rendered.

Legal Department: This department provides legal advice and representation to the Board of Retirement and the Orange County Employees Retirement System on a wide variety of issues affecting OCERS. Among other things, this includes issues involving disability retirements, investments, legislation, vendor contracts, and family law.

Professional Services
December 31, 2002

Consulting Services

Actuary

Towers Perrin
Chicago, IL

Investment Consultant

Callan Associates, Inc.
Denver, CO

Real Estate Consultant

The Townsend Group
San Francisco, CA

Independent Auditor

Link, Murrel & Company
Irvine, CA

Investment Counsel

Stradling, Yocca, Carlson & Rauth
Newport Beach, CA

Fiduciary Counsel

Steeffel Levitt & Weiss
San Francisco, CA

Tax Counsel

Foley & Lardner
San Diego, CA

Investment Managers

Domestic Equity

Artisan Partners
Atlanta, GA

Barclays Global Investors
San Francisco, CA

Cadence Capital Management
Boston, MA

Capital Guardian Trust Company
Los Angeles, CA

Dodge & Cox
San Francisco, CA

Delaware Investment Advisers
Philadelphia, PA

Geewax, Terker & Company
Chadds Ford, PA

Peregrine Capital Management
Minneapolis, MN

Domestic Fixed Income

Barclays Global Investors
San Francisco, CA

**Boston Partners Asset Management
Company, LP**
Boston, MA

Loomis, Sayles & Company
Boston, MA

**Pacific Investment Management Company
(PIMCO)**
Newport Beach, CA

International Equity

Capital Guardian Trust Company
Los Angeles, CA

Marvin & Palmer International
Wilmington, DE

Schroder Capital Management International
London, England

Sit/Kim International
Minneapolis, MN

International Fixed Income

Delaware International Advisers, Ltd.
London, England

Real Estate

Domestic

American Realty Advisors
Glendale, CA

CB Richard Ellis
Los Angeles, CA

SSR Realty Advisors
San Francisco, CA

PMRealty Advisors
Newport Beach, CA

Sentinel Real Estate Corporation
New York, NY

International

**PRICOA Property Investment
Management, Ltd.**
London, England

Non-Traditional Investments

Managers

Adams Street Partners
Chicago, IL

HarbourVest Partners, LLC
Boston, MA

Limited Partnerships

TCW Asset Management Company
Los Angeles, CA

Whippoorwill Associates, Inc.
White Plains, NY

Timber

Hancock Timber Resource Group
Boston, MA

Prudential Timber Investments, Inc.
Boston, MA

Custodian

State Street Bank and Trust Company
Alameda, CA

II. Financial Section



Finance Department

From left, Isaac Arhin, Teresa Panameno, Nicole Sao, Cora Andaya, Christine Dollar, Diane Dillard, Darlene Huynh, and John Wrye.

Link, Murrel & Company

A PROFESSIONAL CORPORATION

REPORT OF INDEPENDENT AUDITORS

Orange County Employees Retirement System Board of Retirement

We have audited the accompanying general purpose financial statements of the Orange County Employees Retirement System ("System") as of and for the years ended December 31, 2002 and 2001, as listed in the table of contents. These general purpose financial statements are the responsibility of the System's management. Our responsibility is to express an opinion on these general purpose financial statements based on our audits.

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

In our opinion, the general purpose financial statements referred to above present fairly, in all material respects, the plan net assets of the Orange County Employees Retirement System at December 31, 2002 and 2001, and the changes in plan net assets for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

The Management's Discussion and Analysis and the required supplementary information on pages 18 through 22 and 40 through 42 are not a required part of the general purpose financial statements but are supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Our audits were conducted for the purpose of forming an opinion on the general purpose financial statements taken as a whole. The other supplementary information and the investment, actuarial and statistical sections, as listed in the table of contents, are presented for purposes of additional analysis and are not a required part of the general purpose financial statements. The other supplementary information has been subjected to the auditing procedures applied in the audits of the general purpose financial statements and, in our opinion, is fairly stated in all material respects in relation to the general purpose financial statements taken as a whole. The investment, actuarial and statistical sections have not been subjected to the auditing procedures applied in the audit of the general purpose financial statements and, accordingly, we express no opinion on them.

Link, Murrell & Co.

April 29, 2003
Irvine, California

We are pleased to provide this overview and analysis of the financial activities of the Orange County Employees Retirement System (OCERS) for the calendar year ending December 31, 2002. Please review it in conjunction with the Letter of Transmittal (starting on page 2) and the Financial Statements beginning on page 24.

Financial Highlights (Dollars in thousands):

- Net Assets Held in Trust for Pension Plan Benefits, as reported in the Statements of Plan Net Assets, totaled \$4,190,249, a decrease of \$372,292 or 8.16% from the prior year primarily as a result of the declines in fair market values of investments.
- Total Additions, as reported in the Statements of Changes in Plan Net Assets, were negative \$177,982 primarily as a result of the depreciation in the fair value of investments and reduced investment returns due to declines in financial markets. This represented a loss from the prior year of \$108,819.
- Total Deductions, as reported in the Statements of Changes in Plan Net Assets, were \$194,310. This represented an increase of \$17,890 over the prior year primarily as a result of increases in benefit payments.
- The firm of Towers, Perrin, Inc. is OCERS' actuary. The latest actuarial valuation completed as of December 31, 2002 indicated that the funding status (the ratio of system assets to system liabilities) was 82.76%.

Overview of Financial Statements:

This section serves as an introduction to the basic financial statements that are comprised of these components:

1. Statements of Plan Net Assets (page 24): This is a snapshot of account balances at the end of calendar years. This statement reflects assets available for future payments to members and their beneficiaries and any current liabilities that are owed.
2. Statements of Changes in Plan Net Assets (page 25): This report reflects all of the financial activities that occurred during the calendar year and shows the impact of those activities as Additions to or Deductions from the Plan.
3. Notes to Financial Statements (pages 26-38): The Notes are an integral part of the financial reports; they provide detailed discussion to key policies, programs and activities that occurred during the year.
4. Required Supplementary Information (pages 39-42): This section includes the Schedule of Funding Progress that shows the historical trend for the actuarially

funded status of the Plan; and the Schedule of Employer Contributions that shows the annual required contributions and the percentage of contributions made.

The Other Supplementary Information (pages 43-46), the Investment Section (pages 47-62), the Actuarial Section (pages 63-79) and the Statistical Section (pages 81-92) provide additional detailed financial, investment, actuarial, and statistical data supporting information reported in the financial statements.

Plan Net Assets (Dollars in thousands):

	December 31		Increase/ (Decrease) Amount	Increase/ (Decrease) Percentages
	<u>2002</u>	<u>2001</u>		
Current Assets	\$ 462,249	\$ 431,786	\$ 30,463	7.06%
Investments	4,043,188	4,587,870	(544,682)	(11.87%)
Fixed Assets	<u>3,538</u>	<u>3,205</u>	<u>333</u>	<u>10.39%</u>
Total Assets	4,508,975	5,022,861	(513,886)	(10.23%)
Total Liabilities	<u>318,726</u>	<u>460,320</u>	<u>(141,594)</u>	<u>(30.76%)</u>
Total Plan Net Assets	<u>\$ 4,190,249</u>	<u>\$ 4,562,541</u>	<u>\$ (372,292)</u>	<u>(8.16%)</u>

Revenues - Additions to Plan Net Assets (Dollars in thousands):

The reserves needed to finance retirement benefits are accumulated through the collection of employer and employee contributions and through interest credited to the reserves. Earnings (losses) on investments increase (decrease) the Net Assets Held in Trust for Pension Benefits that, in turn, decrease (increase) employers' contribution. Losses, including net depreciation in fair market value of investments, net securities lending income, net commission recapture income and net of investment expenses for the year ended December 31, 2002, totaled \$268,890. (See page 25).

Overall additions to plan net assets were (\$177,982) due primarily to investment losses offset by an increase in overall contributions.

Additions to Plan Net Assets (Dollars in thousands):

	Years Ended December 31		Increase/ (Decrease) Amount	Increase/ (Decrease) Percentages
	<u>2002</u>	<u>2001</u>		
Employer Contributions	\$ 12,991	\$ 12,060	\$ 931	7.72%
Employee Contributions	77,917	68,635	9,282	13.52%
Investment (Loss)	<u>(268,890)</u>	<u>(149,858)</u>	<u>(119,032)</u>	<u>(79.43%)</u>
Total Additions	<u>\$ (177,982)</u>	<u>\$ (69,163)</u>	<u>\$ (108,819)</u>	<u>(157.34%)</u>

Expenses - Deductions from Plan Net Assets (Dollars in thousands):

OCERS was created to provide lifetime retirement annuities, survivor benefits and permanent disability benefits to qualified members and their beneficiaries. The cost of such programs includes recurring benefit payments, as designated by the Plan, refund of contributions to terminated employees and the cost of administering the system. Deductions for the year ending December 31, 2002, totaled \$194,310 (see page 25).

Deductions from Plan Net Assets (Dollars in thousands):

	Years Ended December 31		Increase/ (Decrease) Amount	Increase/ (Decrease) Percentages
	2002	2001		
Benefits Paid	\$ 181,549	\$ 163,378	\$ 18,171	11.12%
Withdrawals/Refunds	4,482	5,896	(1,414)	(23.98%)
Administrative Expenses	8,279	7,146	1,133	15.86%
Total Deductions	\$ 194,310	\$ 176,420	\$ 17,890	10.14%

Reserves (Dollars in thousands):

OCERS' reserves are established from contributions and the amount of interest credited to reserve accounts at the actuarially assumed rate on a bi-annual basis. The Active Members Reserve account was credited with an interest rate of 5.5% on a bi-annual basis; the remainder 2.5% was credited to the Employer Advanced Reserve, also on a bi-annual basis. Reserve balances are as follows:

	December 31	
	2002	2001
Active Members Reserve	\$ 858,121	\$ 785,920
Retired Members Reserve	2,148,469	1,880,464
Employer Advanced Reserve	1,350,611	1,403,701
Retired Members Benefit Reserve	25,703	0
Additional Retiree Benefit Account Reserve	56,950	363,077
Death Benefits Reserve	1,074	932
Total Reserves	\$ 4,440,928	\$ 4,434,094

Investment and Economic Summary:

The year 2002 continued to be a very challenging investment environment following a pattern of the previous two years. The global equity markets continued to be plagued by concerns resulting from the Middle East conflict, terrorism and macroeconomic conditions. These concerns resulted in a tremendous amount of market uncertainty.

Equity markets continued to decline in the US and abroad in 2002. The broad equity benchmark Russell 3000 Index was down 21.54% while the international markets benchmark MSCI EAFE Index was down 15.94% for the year. This was the third consecutive year in which both domestic and international equity markets had negative returns.

Within the domestic fixed income markets, there was a flight to quality sectors among investors. High quality sectors generated strong returns as investors sought safety amid unprecedented market turmoil. The Lehman Brothers Universal Index for domestic fixed income markets was up 9.83%. The continued weakening of the US Dollar provided some healthy returns for the non-US fixed income markets as well.

The downturn in the public markets affected the private markets – slowing down the activity in the private equity and venture capital industries. Real estate provided positive returns and provided some diversification to investors.

Capital Assets (Dollars in thousands):

OCERS' investment in capital assets increased from \$3,205 to \$3,538 (net of accumulated depreciation and amortization). This investment in capital assets includes equipment, furniture and computer system-installation. The total increase in OCERS' investment in capital assets for the current year was 10.39% over 2001. The major capital asset investment during 2002 was the development and installation of OCERS' information technology infrastructure, the Membership Accounting Records System (MARS). This project will migrate OCERS' Retirement Database from one platform to another (Oracle). These costs are capitalized and recorded in the Deferred Capital Assets and will be amortized over the useful life of the system after it becomes operational.

Changes in OCERS' Plan Net Assets (Dollars in thousands):

Negative market returns and increases in benefit payments were the primary factors in a decrease in net assets by \$372,292, thereby accounting for an 8.16% decrease over the prior year. Key elements of this decrease are described in the sections that follow.

Contributions received	\$ 90,908
Net investment losses	(270,356)
Net Securities lending income and other income	1,466
Participant's benefits	(181,549)
Withdrawals and refunds	(4,482)
Administrative expenses	<u>(8,279)</u>
Decreases in Plan Net Assets	<u>\$ (372,292)</u>

OCERS' Fiduciary Responsibilities:

OCERS' Board and management staff members are fiduciaries of the pension trust fund. Under the California Constitution, the assets can be used only for the benefit of plan participants and their beneficiaries and reasonable expenses of operation.

Requests for Information:

This financial report is designed to provide the Board of Retirement, members, beneficiaries, taxpayers, investment managers, and participating employers with a general overview of OCERS' financial condition. Questions concerning any of the information provided in this report or requests for additional financial information should be addressed to:

OCERS
Attention: Finance/Accounting
2223 Wellington Avenue
Santa Ana, CA 92701



Toi Dang
Chief Financial Officer

General Purpose Financial Statements



From left, Isaac Arhin, John Wrye and Toi Dang.

Orange County Employees Retirement System
Statements of Plan Net Assets
(in thousands)

	December 31	
	2002	2001
Assets		
Cash and Short-Term Investments		
Cash and Cash Equivalents (Note E-3)	\$ 191,402	\$ 173,454
Collateral Held for Securities Lent (Note E-6)	227,024	207,503
Total Cash and Short-Term Investments	418,426	380,957
Receivables		
Forward Currency Contracts, Net (Note F-1)	285	872
Investment Income	22,585	21,587
Securities Sales	10,858	22,421
Employer/Employee Contributions	10,095	5,949
Total Receivables	43,823	50,829
Investments, at Fair Value (Notes B-2 and E)		
United States Government Debt		
Securities and Corporate Bonds	1,459,003	1,757,273
Foreign Bonds	231,359	196,692
Domestic Equity Securities	1,309,199	1,547,636
International Equity Securities	525,473	561,195
Real Estate	351,704	343,252
Venture Capital and Limited Partnership Interests	166,450	181,822
Total Investments	4,043,188	4,587,870
Fixed Assets, Net (Note B-3)	3,538	3,205
Total Assets	4,508,975	5,022,861
Liabilities		
Collateral Held for Securities Lent (Note E-6)	227,024	207,503
Securities Purchased	69,615	232,028
Other	22,087	20,789
Total Liabilities	318,726	460,320
Net Assets Held in Trust for Pension Plan Benefits (A schedule of funding progress is presented on page 40)	\$ 4,190,249	\$ 4,562,541

See accompanying notes to financial statements.

Orange County Employees Retirement System
Statements of Changes in Plan Net Assets
(in thousands)

	Years Ended December 31	
	2002	2001
Additions		
Contributions (Note C)		
Employer	\$ 12,991	\$ 12,060
Employee	77,917	68,635
Total Contributions	90,908	80,695
Investment Income (Loss):		
Net Depreciation in		
Fair Value of Investments (Note E-5)	(391,903)	(289,021)
Interest on:		
Domestic and International Securities	85,765	105,720
Cash with County Treasurer (Note E-3)	65	74
Domestic Dividends	10,963	12,876
Rental Income	34,939	28,493
International Dividends	12,354	11,621
Venture Capital and Limited Partnership	(4,273)	(2,910)
Total Investment Income (Loss)	(252,090)	(133,147)
Less Investment Expenses	(18,266)	(18,929)
Net Investment Income (Loss)	(270,356)	(152,076)
Securities Lending Revenue (Note E-6)	1,580	2,271
Less Securities Lending Fees (Note E-6)	(461)	(691)
Net Securities Lending Income	1,119	1,580
Net Income from Commission Recapture	347	638
Total Additions (Decreases)	(177,982)	(69,163)
Deductions		
Participants' Benefits	181,549	163,378
Member Withdrawals	4,482	5,896
Administrative Expenses (Note G)	8,279	7,146
Total Deductions	194,310	176,420
Net Decrease	(372,292)	(245,583)
Net Assets Held in Trust for Pension Plan Benefits		
Beginning of Year	4,562,541	4,808,124
End of Year	\$ 4,190,249	\$ 4,562,541

See accompanying notes to financial statements.

Orange County Employees Retirement System

December 31, 2002

Notes to Financial Statements

A. Description of Plan:

The following is a brief description of the Orange County Employees Retirement System (OCERS). Participants should refer to their Summary Plan Description for more complete information.

- 1. General:** OCERS is a cost-sharing multiple-employer, defined benefit pension plan covering substantially all employees of the County of Orange (County) and of the following agencies: City of Rancho Santa Margarita, City of San Juan Capistrano, Orange County Cemetery District, Orange County Children and Families Commission, Orange County Department of Education (closed to new members), Orange County Employees Retirement System, Orange County Fire Authority, Orange County Local Agency Formation Commission, Orange County Public Law Library, Orange County Sanitation District, Orange County Superior Court, Orange County Transportation Authority, Orange County Vector Control District, Transportation Corridor Agencies, and University of California, Irvine Medical Center and Campus (closed to new members).

The participating entities share proportionally in all risks and costs, including benefit costs. One actuarial valuation is performed for OCERS as a whole, and contribution rates vary among participating entities.

Following an effort by the employees of Orange County, a proposition was submitted to the people of Orange County. As a result of the General Election, OCERS was established in 1945 under the provisions of the County Employees Retirement Law of 1937 (County Retirement Law). OCERS provides members with retirement, death, disability, and cost-of-living benefits. OCERS is a related organization of the County of Orange, California. The Board of Retirement consists of nine members of which four are appointed by the County's Board of Supervisors, four are elected by the members of OCERS, the County Treasurer is an ex-officio member and an alternate member is elected by the safety members. The County of Orange is not financially accountable for OCERS.

The Board of Supervisors adopted certain sections of the Government Code for members employed after September 20, 1979, designated as Tier II members. The establishment of Tier II resulted in reduced allowances to those members. Members employed prior to September 21, 1979, are designated as Tier I members. The differences between Tier I and Tier II benefits are discussed below.

- 2. Retirement Allowances:** An employee with ten or more years of service is entitled to an annual retirement allowance beginning at age 50. The amount of the retirement allowance is based upon the member's age at retirement, the member's "final compensation" as defined in Section 31462 of the Retirement Law of 1937, and the total years of service under OCERS.

Retirement Allowances for Tier I members are calculated using a fixed formula which will provide an allowance equal to 2 percent of the member's "final compensation" for each full year of service credit at age 57. Retirement allowances for Tier II members are calculated using a fixed formula which will provide the same allowance at approximately age 61 ¹/₂.

Notes to Financial Statements (Continued)

Retirement and related benefits for Law Enforcement members classified as Safety Members changed July 2002 to the “3% at 50” benefits under Government Code Section 31664.1. This change was reflected in both member and employer contribution rates and obligations effective with the December 31, 2001 actuarial valuation.

Retirement and related benefits for Fire Authority members classified as Safety Members changed after December 31, 2001, to the “3% at 50” benefits under Government Code Section 31664.1. Because this change was not agreed to and effective until after December 31, 2001, it will not be reflected in employer contribution rates and obligations until July 1, 2003, based on results of the December 31, 2002 actuarial valuation. Member contribution rates, however, changed effective July 1, 2002 to reflect the new benefit levels.

All probation officers were reclassified to Safety Member status effective June 28, 2002. Tier 1 members had all of their existing credited service converted to Safety Member service. Tier II members could elect to have their existing General Member credited service converted to a lesser amount of Safety Member credited service. These changes will be reflected in employer contribution rates beginning July 1, 2003, based on the December 31, 2002 actuarial valuation.

Effective January 1, 2003, any employee who terminates membership with OCERS may elect to leave the accumulated deposits in the retirement fund and be granted a deferred retirement allowance at the time the member would have been entitled to the allowance if service had been continued. This change reflects the elimination of the five-year vesting service requirement.

- 3. Death and Disability Benefits:** Upon the death of an active employee, a death benefit, equal to the deceased member’s accumulated contributions, plus 1/12 of the annual compensation earnable by the deceased member during the 12 months immediately preceding death, multiplied by the number of completed years of service under OCERS, but not exceeding six months' compensation, is paid to the employee’s beneficiary. Upon the death of any member of OCERS who would have been entitled to retirement, the surviving spouse, as an option, may receive an annual allowance equal to 60 percent of the retirement allowance to which the deceased member would have been entitled as of the date of death. The death of a member due to service-connected injury or disease entitles the decedent’s surviving spouse or child under 18 years of age to receive an annual allowance equal to one-half the member’s “final compensation.” In addition, the beneficiary of any member who dies before retirement with at least ten years of service under OCERS, or after retirement while receiving a retirement allowance from OCERS, is paid a death benefit of \$1,000.

An active employee who becomes totally disabled as a result of a service-connected injury or disease is paid an annual disability allowance equal to the larger of 50 percent of the employee’s “final compensation,” or the normal retirement benefits accumulated by the member as of the date the member became disabled. An active employee, with five or more years of service, who becomes totally disabled as a result of nonservice-connected disease or injury is paid an annual allowance up to one-third of the employee’s “final compensation,” or the normal retirement benefits accumulated by the member as of the date of disability, whichever is the larger amount.

Notes to Financial Statements (Continued)

Active Personnel

(unaudited)

4. Active and Retired Members: The following is a summary of OCERS' membership composition at December 31, 2002 and 2001:

	<u>December 31</u>	
	<u>2002</u>	<u>2001</u>
<u>General Members</u>		
County and Agencies Paid by County Payroll	15,999	16,854
Outside Agencies	<u>3,003</u>	<u>2,799</u>
Subtotal - General Members	19,002	19,653
<u>Safety Members</u>		
County and Agencies Paid by County Payroll	2,930	1,897
Outside Agencies	<u>791</u>	<u>779</u>
Subtotal - Safety Members	<u>3,721</u>	<u>2,676</u>
Total Active Members	22,723	22,329
<u>Deferred (General & Safety) Members</u>		
Regular	661	698
Employment with Other Agencies (Reciprocity)	<u>716</u>	<u>720</u>
Subtotal - Deferred Members	1,377	1,418
<u>Pending - Retirement or Withdrawal Members</u>		
General	766	447
Safety	<u>34</u>	<u>7</u>
Subtotal - Pending Members	<u>800</u>	<u>454</u>
Total Active, Deferred and Pending	<u><u>24,900</u></u>	<u><u>24,201</u></u>

Retired Personnel Receiving Benefits

(unaudited)

	<u>December 31, 2002</u>			<u>December 31, 2001</u>		
	<u>Gen.</u>	<u>Safety</u>	<u>Total</u>	<u>Gen.</u>	<u>Safety</u>	<u>Total</u>
Service Retirements	5,892	592	6,484	5,628	464	6,092
Continuances	<u>661</u>	<u>52</u>	<u>713</u>	<u>634</u>	<u>52</u>	<u>686</u>
Subtotal-Service Retirements	<u>6,553</u>	<u>644</u>	<u>7,197</u>	<u>6,262</u>	<u>516</u>	<u>6,778</u>
Service Connected						
Disability	546	305	851	519	285	804
Continuances	<u>46</u>	<u>20</u>	<u>66</u>	<u>46</u>	<u>18</u>	<u>64</u>
Subtotal-Service Disability	<u>592</u>	<u>325</u>	<u>917</u>	<u>565</u>	<u>303</u>	<u>868</u>

Notes to Financial Statements (Continued)
Retired Personnel Receiving Benefits

(unaudited)

	December 31, 2002			December 31, 2001		
	Gen.	Safety	Total	Gen.	Safety	Total
Nonservice Connected						
Disability	448	29	477	453	15	468
Continuances	95	2	97	86	16	102
Subtotal-Nonservice Disability	543	31	574	539	31	570
Total Retired Personnel	7,688	1,000	8,688	7,366	850	8,216

5. Employee Purchased Annuities: OCERS formerly provided accounts for additional member contributions as allowed under Government Code Section 31627. Contributions plus accumulated interest at the actuarial interest rate less 50 basis points are held in individual member accounts.

On December 16, 2002 the Board of Retirement adopted resolution 02-005 to terminate the Employee Purchased Annuities program with an effective date of December 31, 2002. For the members that are currently receiving a monthly distribution, they are given the choice of continuing to receive that distribution or receiving a lump sum payout of their balance as of December 31, 2002. For the members that are not currently receiving a monthly distribution, they are given the choice of receiving a lump sum payout of their balance as of December 31, 2002 or have their balances rolled over to a qualified plan or IRA.

6. Federal Income Tax Status: The Plan has received a determination letter from the Internal Revenue Service dated August 14, 1985, stating that the Plan is qualified, in form, under Section 401 (a) of the Internal Revenue Code (the "Code") and, therefore, the related trust is exempt from taxation. Once qualified, the Plan is required to operate in conformity with the Code to maintain its qualification. The Board of Retirement believes the Plan is being operated in compliance with the applicable requirements of the Code and, therefore, believes that the Plan is qualified and the related trust is tax exempt.

B. Summary of Significant Accounting Policies:

1. Basis of Accounting: OCERS' financial statements are prepared on the accrual basis of accounting. Contributions from employers and members are recognized as revenue in the period in which members provide services; benefits and refunds are recognized when payable in accordance with the provisions of the plan. Investment income is recognized as revenue when earned. The net appreciation (depreciation) in fair value of assets held by OCERS is recorded as an increase (decrease) to investment income based on the valuation of investments at year end. Expenses are recorded when corresponding liabilities are incurred, regardless of when payment is due. Under GASB Statement No. 20, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities That Use Proprietary Fund Accounting*, OCERS has elected not to apply Financial Accounting Standards Board pronouncements issued after November 30, 1989.

2. Valuation of Investments: Quoted market prices are used to value United States Government and agency securities, corporate and foreign bonds and debentures, and domestic and international common stocks. Real estate equity investments are stated at fair value, determined by independent appraisals performed on the properties held. The values of venture capital funds and limited partnership investments were determined by the investment managers based on the underlying financial statements and performance of the investments and acceptable valuation methodologies.

Notes to Financial Statements (Continued)

3. Fixed Assets: Fixed assets are carried at cost less accumulated depreciation. Depreciation is calculated using the straight-line method with a 5 year useful life for computer software, and 5 to 15 years for equipment and furniture. The cost and accumulated depreciation of fixed assets at December 31, 2002 and 2001, were as follows:

	<u>2002</u>	<u>2001</u>
Furniture and Equipment	\$ 1,784,000	\$ 1,783,000
Computer Software	3,883,000	3,358,000
Total Fixed Assets (at cost)	<u>5,667,000</u>	<u>5,141,000</u>
Less Accumulated Depreciation	<u>(2,129,000)</u>	<u>(1,936,000)</u>
Total Fixed Assets - Net of Depreciation	<u>\$ 3,538,000</u>	<u>\$ 3,205,000</u>

C. Contributions Required and Contributions Made:

As a condition of participation under the provisions of the County Employees Retirement Law of 1937, members are required to contribute a percentage of their annual compensation to OCERS. For Tier I members, the normal rate of contribution is based on the member's age of entry into OCERS, and is calculated to provide an annual annuity equal to 1/200 of the member's "final compensation" for each year of service rendered at age 60 for General Members, and at the age of 50 for Safety Members. For Tier II General Members, the rate of contribution is calculated to provide an annual annuity equal to 1/120 of the member's "final compensation" for each year of service rendered at age 60. For Tier II Safety Members, the rate of contribution is calculated to provide an annual annuity equal to 1/100 of the member's "final compensation" for each year of service rendered at age 50.

Present members' accumulated contributions at December 31, 2002 and 2001, were \$858,121,000 and \$785,920,000, respectively, including interest credited. Interest was credited at an interest rate of 5.5% per annum as of June 30 on the balance of the members' accounts as of the prior December 31 and as of December 31 on the balance of the members' accounts as of the prior June 30. The incremental difference of 2.5% is credited to the Employer Reserves account.

The County and participating agencies' funding policy is to make periodic contributions to OCERS in amounts such that, when combined with members' contributions and with investment income, will fully provide for all members' benefits by the time they retire.

In September 1994, the County of Orange issued \$320 million in Pension Obligation Bonds (POB) of which \$318.3 million in proceeds were paid to OCERS to fund the County's portion of the Unfunded Actuarial Accrued Liability (UAAL). The proceeds received were recorded as employer contributions in calendar year 1994.

For accounting purposes, OCERS maintains the proceeds for the POB's in the County Investment Account (Investment Account). OCERS and the County of Orange, a single participating district, entered into an agreement which provides an offsetting credit based upon an amount actuarially determined to deplete the County Investment Account over the then remaining UAAL amortization period. The offsetting credits for years 2002, 2001, 2000, 1999, 1998, and 1997 were \$65,180,000, \$41,319,000, \$48,555,000, \$47,129,000, \$42,020,000, and \$40,807,000, respectively.

Notes to Financial Statements (Continued)

In 1995, the Board of Retirement of OCERS and the County of Orange, modified the previous agreement for the use of the Investment Account. The modification provided, that for the year 1995, the employer contributions for the County of Orange would be paid entirely from the Investment Account.

Subsequently, in 1996, the Board of Retirement and the County of Orange entered into an agreement for the use of the Investment Account over a new funding period of 20 years. The agreement provides that the Investment Account will be used to fund the County's employer contribution and in a decreasing percentage each year. In 1997, the Investment Account funded approximately 90% of the County's employer contribution and the County made cash contributions for the remaining 10%. For each subsequent year the funding by the Investment Account will decrease by 5% annually, while the County of Orange employer cash contribution will increase by a corresponding amount. In November 2002, the Board of Retirement and the County amended the agreement to provide for greater County flexibility by eliminating the draw down schedule to allow the County to determine annually how the account will be used. As of December 31, contributions for 2002 and 2001 were approximately \$90,908,000 (\$12,991,000 employer and \$77,917,000 member) and \$80,695,000 (\$12,060,000 employer and \$68,635,000 member), respectively, consisting of:

	<u>2002</u>	<u>2001</u>
Normal Cost	\$ 111,184,000	\$ 111,228,000
Amortization of Unfunded Actuarial Accrued Liability	<u>(20,276,000)</u>	<u>(30,533,000)</u>
Total	<u>\$ 90,908,000</u>	<u>\$ 80,695,000</u>

The contributions to OCERS for 2002 and 2001 were made in accordance with the actuarially determined requirements as follows:

	Percent of Members' Payroll			
	<u>07/02 – 12/02</u>	<u>07/01 – 06/02</u>	<u>07/00 – 06/01</u>	<u>09/99 – 06/00</u>
<u>Employer Contributions - General - OCTA</u>				
Normal Cost	4.20%	4.94%	4.56%	4.35%
Amortization of Unfunded Actuarial Accrued Liability	<u>0.27%</u>	<u>-3.98%</u>	<u>-3.60%</u>	<u>-2.35%</u>
Subtotal	4.47%	0.96%	0.96%	2.00%
Additional Contribution	<u>0.50%</u>	<u>0.00%</u>	<u>0.00%</u>	<u>0.00%</u>
Total	<u>4.97%</u>	<u>0.96%</u>	<u>0.96%</u>	<u>2.00%</u>
<u>Employer Contributions - General - Non-OCTA</u>				
Normal Cost	5.04%	4.94%	4.56%	4.35%
Amortization of Unfunded Actuarial Accrued Liability	<u>0.12%</u>	<u>-3.98%</u>	<u>-3.60%</u>	<u>-2.35%</u>
Subtotal	5.16%	0.96%	0.96%	2.00%
Additional Contribution	<u>0.50%</u>	<u>0.00%</u>	<u>0.00%</u>	<u>0.00%</u>
Total	<u>5.66%</u>	<u>0.96%</u>	<u>0.96%</u>	<u>2.00%</u>

Notes to Financial Statements (Continued)

	Percent of Members' Payroll			
	<u>07/02 – 12/02</u>	<u>07/01 – 06/02</u>	<u>07/00 – 06/01</u>	<u>09/99 - 06/00</u>
<u>Employer Contributions - Safety - Law Enforcement</u>				
Normal Cost	15.87%	8.57%	8.27%	8.00%
Amortization of Unfunded				
Actuarial Accrued Liability	<u>8.65%</u>	<u>0.16%</u>	<u>13.95%</u>	<u>16.41%</u>
Subtotal	24.52%	8.73%	22.22%	24.41%
Additional Contribution	<u>0.50%</u>	<u>0.00%</u>	<u>0.00%</u>	<u>0.00%</u>
Total	<u>25.02%</u>	<u>8.73%</u>	<u>22.22%</u>	<u>24.41%</u>
 <u>Employer Contributions - Safety - Fire Protection</u>				
Normal Cost	10.30%	8.57%	8.27%	8.00%
Amortization of Unfunded				
Actuarial Accrued Liability	<u>1.39%</u>	<u>0.16%</u>	<u>13.95%</u>	<u>16.41%</u>
Subtotal	11.69%	8.73%	22.22%	24.41%
Additional Contribution	<u>0.50%</u>	<u>0.00%</u>	<u>0.00%</u>	<u>0.00%</u>
Total	<u>12.19%</u>	<u>8.73%</u>	<u>22.22%</u>	<u>24.41%</u>
 <u>Employer Contributions - Safety - Probation*</u>				
Normal Cost	5.04%	4.94%	4.56%	4.35%
Amortization of Unfunded				
Actuarial Accrued Liability	<u>0.12%</u>	<u>-3.98%</u>	<u>-3.60%</u>	<u>-2.35%</u>
Subtotal	5.16%	0.96%	0.96%	2.00%
Additional Contribution	<u>0.50%</u>	<u>0.00%</u>	<u>0.00%</u>	<u>0.00%</u>
Total	<u>5.66%</u>	<u>0.96%</u>	<u>0.96%</u>	<u>2.00%</u>

The Memorandum of Understanding (MOU) between OCERS and the County of Orange requires that Employer Contributions must increase by the lesser of .50% of pay or the amount necessary to increase OCERS' Unallocated Fund Balance (UFB) to 3% of OCERS' adjusted total assets. The balance of the UFB as of December 31, 2002 was zero; therefore, Employer Contributions for the fiscal year of July 1, 2003 will increase by .50% of pay to restore the UFB to the 3% of OCERS' adjusted total assets. The total payment made during the second and third quarter of calendar year 2002 was \$2,231,000.

*Employer contributions for probation officers will remain at the General Employer rate until July 2003.

D. Plan Termination:

There are no plan termination provisions under the County Employees Retirement Law of 1937 which govern the operation of OCERS.

E. Investments:

- Investments Authorized:** Investments in securities are held by the Plan's custodian, State Street Bank and Trust Company. Government Code Section 31595 authorizes OCERS to invest in any form or type of investment deemed prudent, including security lending transactions, in the informed opinion of the Retirement Board, except as otherwise expressly restricted by California Constitution or by law.

Notes to Financial Statements (Continued)

- 2. Investment Concentration:** At December 31, 2002 and 2001, OCERS had investments in Barclays Global Investors Russell 1000 Index and S&P 500 Index Fund which individually represented 14.01% and 14.18%, respectively of OCERS' plan net assets. In addition, OCERS had investments in Barclays Global Investors Fixed Income Index that represented 7.26% and 7.70% respectively, of OCERS' plan net assets. No other investments exceeded 5% of the system's net assets.
- 3. Cash and Cash Equivalents:** OCERS' investment portfolios may not be entirely invested in securities at a given time. Those funds not in the form of securities are invested in short-term money market funds including the Orange County Investment Pool. In addition OCERS maintains an operating cash balance at a local financial institution, Wells Fargo Bank, to be used for retirement payroll and other operational expenses. At December 31, 2002, OCERS had money market funds of \$173,785,000 invested with OCERS' master trust custodian bank, State Street Bank and Trust Company; \$17,499,000 invested with Wells Fargo Bank and \$118,000 invested with the Orange County Investment Pool. All of the cash invested is uninsured and uncollateralized; interests in the money market funds and in the Orange County Investment Pool are computed on an average daily balance. The total amount classified as Cash and Cash Equivalents as of December 31, 2002 was \$191,402,000.
- 4. Credit Risk:** OCERS' investments are categorized below to give an indication of the level of risk assumed by OCERS at year-end. The categories are:

Category 1 includes investments that are insured or registered or for which the securities are held by OCERS or by its agent in its name.

Category 2, of which OCERS has none, includes uninsured and unregistered investments for which the securities are held by the counterparty's trust department or agent in OCERS' name.

Category 3, of which OCERS has none, includes uninsured and unregistered investments for which the securities are held by broker-dealers or by other counterparties, but not in OCERS' name.

Investments not evidenced by securities are not categorized. The investment values (in thousands) at December 31, 2002 are summarized as follows:

<u>Category 1 Classification</u>	<u>Cost</u>	<u>Fair Value</u>
U.S. Government Debt Securities	\$ 287,007	\$ 301,549
Corporate Debt Securities	716,544	702,679
U.S. Government Bonds	56,640	55,697
Foreign Bonds	178,637	189,133
Domestic Equity Securities	757,320	683,603
International Equity Securities	483,873	430,331
Subtotal	2,480,021	2,362,992

Amounts Not Subject to Classification

Investments Held by Broker-Dealers Under
Securities Loans with Cash Collateral:
Corporate Debt Securities

	23,055	21,454
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Notes to Financial Statements (Continued)

	<u>Cost</u>	<u>Fair Value</u>
U.S. Government Debt Securities	44,971	46,722
U.S. Government Bonds	23,924	26,758
Domestic Equity Securities	43,791	38,417
International Equity Securities	60,303	44,859
Foreign Bonds	39,807	42,226
Orange County Treasurer's Pooled Investment	118	118
Real Estate Investments	323,518	351,704
Domestic Equity Index Fund	911,540	587,179
International Pooled Equity Funds	57,747	50,283
Domestic Pooled Fixed Income	232,358	304,144
Alternative Investment in Venture Capital and Limited Partnership	<u>196,492</u>	<u>166,450</u>
Subtotal	1,957,624	1,680,314
Less: Orange County Treasurer's Pooled Investment	<u>(118)</u>	<u>(118)</u>
Total Investments	\$ <u>4,437,527</u>	\$ <u>4,043,188</u>

A detailed report of the investment holdings is available for review at the OCERS location.

- 5. Net Depreciation:** During 2002 and 2001, OCERS' investments (including investments bought and sold, as well as held during each year) depreciated in values by \$391,903,000 and by \$289,021,000, respectively, as follows:

	<u>Years Ended December 31</u>	
	<u>2002</u>	<u>2001</u>
	(in thousands)	
Net Depreciation in Fair Value as Determined by Quoted Market Prices:		
Domestic Equity Securities	\$ (318,168)	\$ (116,235)
United States Government Debt Securities, Corporate & Foreign Bonds & Debentures	74,098	30,970
International Equity Securities	<u>(117,575)</u>	<u>(145,366)</u>
Subtotal	(361,645)	(230,631)
Net Depreciation in Fair Value as Determined by Estimated Fair Value:		
Real Estate	(5,545)	(7,912)
Alternative	<u>(24,713)</u>	<u>(50,478)</u>
Total Net Depreciation	\$ <u>(391,903)</u>	\$ <u>(289,021)</u>

Notes to Financial Statements (Continued)

- 6. Securities Lending Contracts:** Included in the investment accounts for United States Government securities, international securities, corporate bonds and debentures, foreign bonds and debentures, and common stocks at December 31, 2002 and 2001 were securities with fair values of \$220,437,000 and \$201,039,000, respectively, which had been lent by OCERS, through a securities lending agent, to various securities brokers in return for cash collateral equal to 102 percent (105 percent for international investments) of the fair value (priced daily) of the securities lent, and additional collateral has to be provided by the next day if its value falls to less than 100 percent of the fair value of the securities lent. OCERS invests the cash collateral in short-term securities that cannot be pledged or sold by OCERS unless the borrower defaults. Securities on loan at year-end are presented as unclassified in the preceding schedule of custodial credit risk. In lending of both domestic and international securities, the term to maturity of the securities lent is matched with the term to maturity of the investment of collateral. Such matching existed at year-end. There are no restrictions on the amount of securities that can be lent at one time. There were no violations of the security lending provisions that occurred during 2002.

OCERS invested the cash collateral in short-term securities, which included certificates of deposit and commercial paper from certain domestic banks and savings and loans, repurchase agreements through certain brokers, and certain money market funds. Investments purchased with cash collateral are held by State Street Bank and Trust Company in separate collateral accounts. The contract with State Street Bank and Trust Company requires it to indemnify OCERS if the borrowers fail to return the securities (and if the collateral is inadequate to replace the securities lent). The risks involved in a security lending program generally include: borrower bankruptcy, collateral deficiencies, problems with settlements, corporate actions, and dividends and interest. OCERS had no losses on securities lending transactions resulting from the default of a borrower or the lending agents for the years ended December 31, 2002 and 2001.

Gross security lending revenues for 2002 and 2001 were \$1,580,000 and \$2,271,000, respectively. The costs of securities lending transactions are reported as investment expenses in the accompanying financial statements.

OCERS' securities lending agents are responsible for monitoring the fair value of the securities lent to ensure that the value of the collateral equals or exceeds 100 percent of the fair value of the securities lent as of the valuation date. At December 31, 2002 and 2001, OCERS held broker collateral with fair values totaling \$227,024,000 and \$207,503,000, respectively. At year end, the system has no credit risk exposure to borrowers because the amounts the system owes the borrowers exceed the amounts the borrowers owe the system.

- 7. International Investments:** Investments in international securities are managed by three investment managers. Other investments are held in four pooled funds, all of which are invested in equities of companies located in international emerging markets.
- 8. Alternative Investments:** OCERS' alternative investments represent investments made in private debt and equity securities through limited partnership and venture capital arrangements. OCERS has employed two investment

Notes to Financial Statements (Continued)

methods. One method is the use of investment management firms to invest OCERS' assets in limited partnerships as well as direct private placements. The second method of investment is OCERS' participation as a limited partner in limited partnership funds. As of December 31, 2002, OCERS has approximately \$91,433,000 of open commitments in twelve alternative investments. These investments are diversified between venture capital, corporate finance, buyout, energy, and oil and gas investments.

- 9. Derivative Holdings Held for Trading Purposes:** Of the total investments in OCERS' domestic fixed income portfolio of \$1,459,003,000 as of December 31, 2002, approximately \$370,296,000 are classified as derivative securities in accordance with the GASB definition (see note F for other derivative investments). These holdings include asset-backed securities, mortgage-backed securities, zero coupon bonds, variable rate securities, fixed income options, and interest rate caps. The investment objective of these derivative securities is to achieve favorable yields and advantageous risk/reward profiles with the vast majority of the holdings being guaranteed by either the U.S. Government or one of its agencies. Details of these derivative securities are as follows:

Securities	Fair Value 2002	Fair Value 2001
FHA	\$ -	\$ 19,958,000
FHLMC	20,361,000	29,314,000
FNMA	198,148,000	136,649,000
GNMA	97,763,000	379,555,000
CMO	20,670,000	55,369,000
Others	33,354,000	44,126,000
Total Derivative Securities	\$ 370,296,000	\$ 664,971,000

- 10. Reclassifications:** Certain amounts in the 2001 financial statements have been reclassified to conform with the 2002 financial statement presentation.

F. Financial Investments with Off-Balance Sheet Risk:

- 1. Forward Currency Contracts:** OCERS' international investment managers invest in forward currency contracts. These are agreements to exchange different currencies at specified rates and settlement dates. Differences between the contract and market exchange rates at settlement result in gains or losses. Risks arise from the possible inability of counterparties to meet the terms of their contracts and from movements in exchange and interest rates. OCERS' balances for the forward currency receivables and payable accounts are based upon the currencies' contract exchange rates in relation to their market exchange rates at December 31, 2002 and 2001. An accounts receivable balance that is greater than the payable balance represents a net gain on the contracts. An accounts receivable balance that is less than the payable balance indicates a net loss. At December 31, 2002 and 2001, OCERS had net forward currency contract receivables of \$285,000 and \$872,000, respectively.
- 2. Financial Futures Contracts Held for Purposes Other than Trading:** The net changes in fair value of financial futures contracts held for purposes other than trading comprised \$3,337,000 and (\$2,933,000) of net appreciation (depreciation) during 2002 and 2001, respectively. As of December 31, 2002 and 2001, OCERS had open contracts of \$46,716,000 and \$195,871,000, respectively, for the purchase of U.S. Treasury notes and Financial Future Euro Dollars with delivery at specified future dates. Risks arise from movements in securities values and interest rates.

Notes to Financial Statements (Continued)

OCERS is required to maintain a deposit with the broker as collateral to support open futures contracts. As of December 31, 2002 and 2001, OCERS had collateral deposits of \$2,405,000 and \$2,895,000, respectively, in cash equivalents, U.S. Treasury bills and notes.

G. Administrative Expenses:

Section 31580.2 of the Government Code limits the annual administrative expenses of the retirement system to eighteen-hundredths of 1 percent (18 basis points) of the total assets of the retirement system. Total administrative expenses for the year ended December 31, 2002 were \$6,951,000 or approximately 15.4 basis points. As of December 31, 2002, 18 basis points of the assets of the system was approximately \$8,116,000. Additionally, Section 31596.1 of the Government Code allows certain costs to be excluded from administrative expenses that are subject to statutory limitation. The excluded costs are included in the amounts classified as administrative expenses for OCERS' financial statements.

	<u>Years Ended December 31</u>	
	<u>2002</u>	<u>2001</u>
	(in thousands)	
Expenses Subject to Statutory Limitation:		
Personnel Services:		
Board Members' Allowance	\$ 12	\$ 14
Employee Salaries and Benefits	<u>3,871</u>	<u>3,269</u>
Total Personnel Services	3,883	3,283
Office Operating Expenses:		
Operating Expenses	865	673
Professional Services	1,149	952
Rent/Leased Real Property	861	764
Depreciation/Amortization	<u>193</u>	<u>193</u>
Total Office Operating Expenses	<u>3,068</u>	<u>2,582</u>
Total Expenses Subject to Statutory Limitation	6,951	5,865
Expenses Not Subject to Statutory Limitation:		
Commingled Interest Cost	3	2
Actuarial/Fund Evaluation Costs	567	488
Custodian Services	309	309
Investment Department Expenses	308	344
Legal Costs	29	36
Additional Death Benefit Costs	112	102
Total Expenses Not Subject to Statutory Limitation	<u>1,328</u>	<u>1,281</u>
Total Administrative Expenses	\$ <u><u>8,279</u></u>	\$ <u><u>7,146</u></u>

H. Reserve Accounts:

The plan net assets of \$4,190,249,000 as of December 31, 2002 include reserves of \$4,440,928,000 and unreserved net assets of (\$250,679,000). The unreserved net assets include the Investment Account.

Notes to Financial Statements (Continued)

The reserve balances as of December 31, 2002 are as follows (in thousands):

Active Members Reserves	Retired Members Reserves	Employer Advanced Reserves	ARBA Reserves	RMBR Reserves	Death Benefits Reserves	Total Reserves
\$ 858,121	\$ 2,148,469	\$ 1,350,611	\$ 56,950	\$ 25,703	\$ 1,074	\$ 4,440,928

The Additional Retiree Benefit Account (ARBA) results from a Memorandum of Understanding (MOU) with the County of Orange in which \$176,232,000 was used in 1993 to reduce the UFB. By the terms of the MOU, \$125,844,000 was transferred to the County Advance Reserve, which is included in Employer Advanced Reserves. The remaining \$50,388,000 was transferred to the ARBA. The amounts maintained in the ARBA are to be applied to health insurance or other supplemental benefits for OCERS’ retirees. There are no transfers to the ARBA account made in years 2001 and 2002 because the UFB was zero.

The Board of Retirement adopted the creation of the Retired Members Benefit Reserve (RMBR) for OCERS' retirees in the year 2002 to ensure the continued funding of the retiree supplemental benefits for three years. All participating agencies could transfer a projected three year benefit payment to the RMBR balance that was created as a sub-account of the Employer Advanced Reserve Account. The RMBR account will be used to pay additional benefits to retirees in lieu of payments out of the ARBA balance in circumstances where the ARBA balance is depleted. The RMBR balance will not receive the bi-annual interest credit and it will be funded on a three year rolling method.

I. California Supreme Court Decision – Ventura County:

On August 14, 1997, the Supreme Court of the state of California issued a decision in a case entitled Ventura County Deputy Sheriffs Association vs. Board of Retirement of Ventura County Employees’ Retirement Association, Case No. S055682. On October 1, 1997, the decision of the California Supreme Court became final. The Supreme Court held that a County Retirement System operating under the provisions of the County Employees Retirement Law of 1937 must include certain types of cash incentive payments and additional pay elements, received by an employee, within the employee’s “compensation earnable” and “final compensation” when calculating the employee’s retirement benefits.

On February 6, 1998 the Board of Retirement of Orange County Employees Retirement System adopted Resolution No. 98-001 to include certain cash incentive payments and additional pay elements in the definition of compensation earnable to comply with the Supreme Court decision. The Board’s resolution is applicable retroactively to October 1, 1994. On May 4, 1998 the Board of Retirement adopted Resolution No. 98-009 to transfer approximately \$209,205,000 from Unallocated Fund Balance, the balance of excess earnings over the actuarially assumed rates, to Employer Advanced Reserve accounts to defray the retroactive cost of implementing the Supreme Court decision as of December 31, 1997.

After the Board of Retirement implemented the Supreme Court decision, litigation arose in Orange County and in most other counties with retirement systems governed by the County Employees Retirement Law of 1937, challenging the various retirement boards’ actions to implement the decision. In December 1998, the cases were coordinated into a single proceeding in the San Francisco County Superior Court, to resolve the many disputes that arose. In November 2002, the Court approved a final settlement of all claims involving OCERS, resulting in no financial impact to OCERS. All claims against OCERS were dismissed with prejudice and the litigation has been terminated successfully.

Required Supplementary Information



Legal Division

From left, Elaine Reagan and Fred Messerer.

Orange County Employees Retirement System
Required Supplementary Information - Trend Information
Schedule of Funding Progress for the Years Ended December 31
(in thousands)

	Valuation Year					
	2002	2001	2000	1999	1998	1997
Actuarial Value of Assets ¹ (a)	\$4,695,675	\$4,586,844	\$4,497,362	\$3,931,744	\$3,504,708	\$3,128,132
Actuarial Accrued Liability (b)	\$5,673,754	\$4,843,899	\$4,335,025	\$4,017,279	\$3,682,686	\$3,332,967
Total Unfunded Actuarial Accrued Liability (UAAL) (b-a=c)	\$978,079	\$257,055	(\$162,337)	\$85,535	\$177,978	\$204,835
Funded Ratio (a/b)	82.76%	94.69%	103.74%	97.87%	95.17%	93.85%
Covered Payroll (d)	\$1,242,348	\$1,122,763	\$994,669	\$912,490	\$863,199	\$781,890
UAAL as a Percentage of Covered Payroll (c/d)	78.73%	22.89%	(16.32%)	9.37%	20.62%	26.20%

Notes:

- The 12/31/97, 12/31/98, 12/31/99, 12/31/00, 12/31/01, and 12/31/02 actuarial value of assets exclude \$322,333,000, \$302,909,000, \$286,139,000, \$272,789,000, \$221,643,000 and \$143,675,000 respectively. Effective December 31, 2002, the Retirement Board elected to change the amortization period for the General Member and Probation Officer unfunded actuarial accrued liability (UAAL) to 30 years. The amortization is a level dollar amount.

The amortization of the Safety Member UAAL has not changed. That UAAL is amortized in pieces as follows. The UAAL as of December 31, 1995, is amortized as a level dollar amount over 28 years. Actuarial gains and losses for each year are amortized over separate 15-year periods on a level dollar basis. Changes in the UAAL arising from assumption changes and plan amendments are amortized over periods determined by the Board. All amortization periods are considered closed (i.e., level dollar amortization with a fixed end date).

The accompanying notes are an integral part of the Required Supplementary Information.

Orange County Employees Retirement System
Required Supplementary Information - Trend Information
Schedule of Employer Contributions for the Years Ended December 31
(in thousands)

	<u>2002</u>	<u>2001</u>	<u>2000</u>	<u>1999</u>	<u>1998</u>	<u>1997</u>
Annual Required Contribution	\$ 12,991	\$ 12,060	\$ 15,561	\$ 17,591	\$ 17,977	\$ 16,463
Percentage Contributed	100%	100%	100%	100%	100%	100%

Notes:

1. In September 1994 the County of Orange issued \$320 million in Pension Obligation Bonds (POB) of which \$318.3 million in proceeds were paid to OCERS, which was recorded as employer contribution in 1994. For accounting purposes, the proceeds were put into the County Investment Account (the Investment Account). Subsequent agreements between the Board of Retirement and the County provide that the Investment Account will be used to fund the County's employer contribution in decreasing percentage each year. In 1996, and 1997, the Investment Account funded approximately 90% of the County's employer contribution. In 1998 and 1999 the Investment Account funded approximately 85% and 80% of the County's employer contribution, respectively. In years 2001 and 2002 the amortization of the UAAL was negative and, on a percentage basis, exceeded the required normal cost funding requirement. Therefore, the County contribution is absorbed 100% by the County Investment Account.

In November 2002 the Board of Retirement and the County approved an amended agreement to provide for greater County flexibility by eliminating the draw down schedule to allow the County to determine annually how the account will be used.

2. Employer contributions for 2002, 2001, 2000, 1999, 1998 and 1997 excluded \$65,180,000, \$41,319,000, \$48,555,000, \$47,129,000, \$42,020,000 and \$40,807,000 respectively, of funds transferred from the Investment Account to pay for the County's employer contribution.

The amounts excluded from total employer contribution for those years represent the County's portion of its annual employer contributions that were amortized annually against the Pension Obligation Bond proceeds of \$318,000,000 that the County paid to the system in 1994. The \$318,000,000 was reported as Employer Contribution in OCERS' 1994 CAFR.

The accompanying notes are an integral part of the Required Supplementary Information.

Orange County Employees Retirement System
Required Supplementary Information - Trend Information
Notes to Required Supplementary Information

Note 1 - Description

The historical trend information about the Orange County Employees Retirement System is presented as required supplementary information. The information is intended to help users assess the funding status of the fund on a going-concern basis and to assess progress made in accumulating assets for paying benefits when due.

Note 2 - Actuarial Assumptions and Method

The information presented in the required supplementary schedules was determined as part of the actuarial valuation at the dates indicated. Additional information as of the latest actuarial valuation follows:

Valuation date	12/31/2002.
Actuarial cost method	Projected Unit Credit.
Amortization method	Level dollar (closed)
Remaining amortization period	21 years (closed) for Fire Authority and Law Enforcement personnel.
Remaining amortization period	30 years (closed) for others.
Asset valuation method	5-year moving average of the ratio of market value to book value multiplied by the current year's book value.
Actuarial assumptions	
Investment rate of return	7.5%
Projected Salary Increases	5.5% per annum at 12/31/2001, 4.5% at 12/31/2002.
Includes inflation at	4.5% subject to Tier maximum.
Cost-of-living adjustments	3% per annum with excess banked.

Note 3 - Significant Factors Affecting Trends in Actuarial Information

2002 Changes in Plan Provisions and Actuarial Assumptions Since Prior Year

Retirement formula for Fire Authority personnel changed to 3% at 50.
All probation officers' status changed from General to Safety.
Interest rate assumption changed from 8.0% to 7.5%.
Salary scale changed from 5.5% to 4.5%.
Reset amortization period to 30 years except for actuarial gains and losses related to Fire Authority and Law Enforcement personnel.

2001 Changes in Plan Provisions and Actuarial Assumptions Since Prior Year

Retirement formula for Law Enforcement personnel changed to 3% at 50.

1998 Changes in Plan Provisions and Actuarial Assumptions Since Prior Year

Reduced termination rates.
Moved retirement age slightly older.
Changed Pre-retirement Mortality Table from 1971 GAM to 1983 GAM.

1996 Changes in Plan Provisions and Actuarial Assumptions Since Prior Year

Salary scale changed from 2.5% to 3.5% per annum per individual through the year 2000, and 5.5% thereafter.

1995 Changes in Plan Provisions and Actuarial Assumptions Since Prior Year

Salary scale changed from 6.0% to 2.5% per annum per individual.

1993 Changes in Plan Provisions and Actuarial Assumptions Since Prior Year

Changed Mortality Table from 1971 GAM (for regular retirement) to 1983 Group Annuity. Changed Expectations of Life After Disability from 80% of Mortality Table to 60%.

Other Supplementary Information



Communications Division

From left, Robert Kinsler and Jayne Ritchey.

Orange County Employees Retirement System
Schedule of Administrative Expenses
for the Years Ended December 31, 2002 and 2001
(in thousands)

	2002	2001
Expenses Subject to Statutory Limitation		
Personnel Services:		
Board Members' Allowance	\$ 12	\$ 14
Employee Salaries and Benefits	3,871	3,269
Total Personnel Services	3,883	3,283
 Professional Services:		
Legal Fees	478	356
Financial and Internal Audits	99	131
Mortality Verification	5	5
Information Technology Consultant	5	11
Team Building Consultant	40	0
Governance Workshop	55	67
Hearing Officers/Medical Consultants	279	245
Pre-retirement Seminars	11	16
Miscellaneous	177	121
Total Professional Services	1,149	952
 Other Operating Expenses:		
Telephone and Communication	52	48
Maintenance	249	103
Printing and Duplicating	126	113
Building and Equipment Leases	861	764
Transportation, Travel and Training	149	187
Postage Expense	151	119
Office Supplies and Expenses	138	103
Depreciation Expenses	193	193
Total Other Operating Expenses	1,919	1,630
 Total Expenses Subject to Statutory Limitation	6,951	5,865
 Expenses Not Subject to Statutory Limitation		
Fund Evaluation Cost	313	277
Custodian Services	309	309
Commingled Interest Cost	3	2
Actuarial Cost	254	223
Legal Costs	29	36
Additional Death Benefits Cost	112	102
Investment Department Expenses	308	332
Total Expenses Not Subject to Statutory Limitation	1,328	1,281
 Total Administrative Expenses	\$ 8,279	\$ 7,146

Orange County Employees Retirement System
Schedule of Payments to Consultants
for the Years Ended December 31, 2002 and 2001
(in thousands)

<u>Name of Firms</u>	<u>Type of Services</u>	<u>2002</u>	<u>2001</u>
Professional Expenses Subject to Statutory Limitation			
County of Orange	Board Election	\$ -	\$ 12
County of Orange	GHRIS Dial Up & Others	26	-
County of Orange	Cost Allocation (CWCAP)	21	-
Kathleen Wells Webster & Assoc.	Team Building Workshop	40	-
DMG Maximus, Inc.	Recruitment Costs	25	12
Keith Bozarth	Relocation Cost	-	45
Epoch Internet	Internet Access	15	18
Cortex Applied Research	Governance Workshop	55	67
Manpower, Inc.	Temporary Personnel	53	37
E-Partners	System Consulting	5	14
Valarie Desporough	Court Reporter	22	-
Carolyn Ford and Associates	System Implementation	-	11
Ice Miller	Legal Services	10	-
Barbara Evans	Legal Services	16	6
Hanson Bridgett	Legal Services	7	-
Scott, P.H. Inc.	Legal Services	31	-
Foley & Lardner	Legal Services	63	20
Phillip Eaton & Associates	Legal Services	-	1
Steeffel, Levitt & Weiss	Legal Services	351	314
William B. Gibson, esq.	Legal Services	-	15
Link, Murrel & Company	Financial and Internal Audits	99	124
The Berwyn Group	Mortality Verification	5	5
Various Firms	Disability/Medical Hearings	279	228
Financial Management Group	Pre-retirement Seminars	10	16
Various Professional Firms	Other Services	16	7
Total Professional Expense Subject to Limitation		\$ 1,149	\$ 952
Professional Expenses Not Subject to Statutory Limitation			
Callan Associates, Inc./ The Townsend Group	Performance Evaluation	297	277
State Street Bank and Trust Company	Master Trust Custody	309	309
Bankers Trust	Master Trust Custody	16	-
County of Orange	Commingled Interest Cost	3	2
Towers Perrin	Actuarial Services	254	223
Stradling, Yocca, Carlson, & Rauth	Legal Counsel	29	36
Additional Death Benefits Cost	Member Benefits	112	102
Investment Department Expenses	Investment Expenses	308	332
Total Professional Expenses Not Subject to Limitation		1,328	1,281
Total All Professional Fees		\$ 2,477	\$ 2,233

Orange County Employees Retirement System
Schedule of Fees and Other Investment Expenses
for the Years Ended December 31, 2002 and 2001
(in thousands)

	<u>2002</u>	<u>2001</u>
Domestic Equity	\$ 3,284	\$ 3,583
International Equity	2,937	2,964
Global Fixed Income	3,466	3,479
Real Estate	3,648	2,489
Venture Capital	4,093	5,265
Other Alternative Investments	<u>838</u>	<u>1,149</u>
Total Fees & Other Investment Expenses	<u>\$ 18,266</u>	<u>\$ 18,929</u>

III. Investment Section



Investment Department
From left, Trish Moran and Shanta Chary.

CALLAN ASSOCIATES

April 18, 2003

MICHAEL J. O'LEARY, JR., CFA
EXECUTIVE VICE PRESIDENT



SAN FRANCISCO

NEW YORK

CHICAGO

ATLANTA

DENVER

Board of Retirement
Orange County Employees Retirement System
2223 Wellington Avenue
Santa Ana, California 92701-3101

Dear Board Members:

This letter reviews the investment performance of the Orange County Employees Retirement System (OCERS) for the calendar year ended December 31, 2002.

The System's custodian during the calendar year, State Street Bank and Trust Company, independently prepared the underlying performance data. The performance calculations were made in compliance with AIMR Performance Presentation Standards. Callan Associates Inc. serves as OCERS' independent investment consultant and evaluates the System's performance in relation to market benchmarks, appropriate manager peer groups and other public pension funds.

OCERS' primary investment objective is to prudently and expertly invest the System's assets, in accordance with governing law and industry practices, in a manner that will ensure the System's ability to pay promised benefits to participants and their beneficiaries. In pursuit of this objective, OCERS' Board periodically evaluates the System's liabilities, expected contributions and potential earnings. This analysis is used to evaluate alternative investment policies. The Board selects a strategic investment policy that balances growth potential and acceptable risk. A policy benchmark index is constructed that mirrors the System's strategic asset allocation policy. This policy benchmark is a custom market index comprised of stock, bond and real estate indices weighted in the same proportions as the System's investment policy.

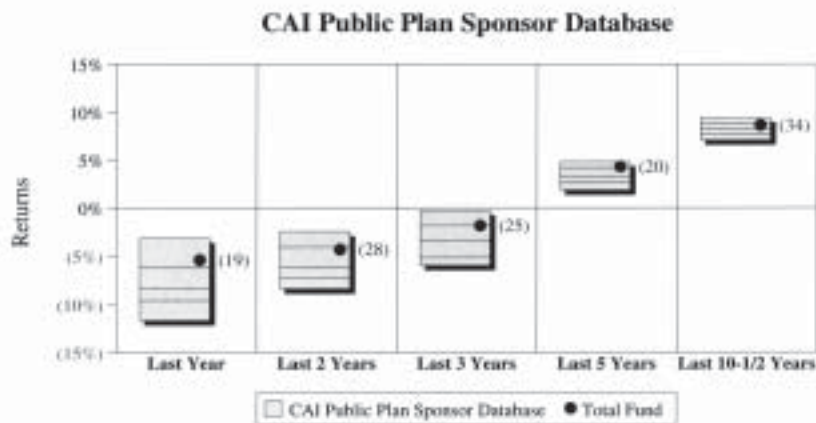
The stock market, as measured by the Russell 3000 Stock Index, registered a substantial decline of 21.54% in calendar 2002. In combination with the losses registered in the prior two years, the stock market decline is now actually more protracted and at least as severe as the 1973-74 bear market. There has literally been no safe place to hide in this market environment. Unlike 2000 and 2001, when small cap stocks and value oriented strategies managed to hold up, the decline in 2002 affected stocks across the board. Fortunately, markets and the economy showed signs of sluggish recovery in the fourth quarter of the year. For the year, international stocks, on balance, mirrored domestic stocks. Weakening of the dollar, however, helped international stock indices post smaller declines in U.S. dollar terms than those experienced in domestic equities. It is interesting to note that emerging markets experienced much smaller declines than either U.S. or developed international markets. Interest rates declined substantially during the year. By year-end, interest rates across the entire maturity spectrum had fallen to levels not experienced in decades. The decline in rates naturally helped bond market values to

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increase substantially. Within the bond market, high quality instruments significantly outperformed comparably dated lower quality instruments.

For the calendar year, OCERS' total fund had a time-weighted total return of negative 5.46%. When compared to Callan's Public Fund Database, OCERS ranked in the 19th percentile; this very strong ranking is largely attributable to the System having a more conservative than average asset policy. The return essentially matched the System's strategic policy benchmark target return of negative 5.45%. The policy benchmark is comprised of the following indices in the percentages as indicated: Russell 3000 (33%); MSCI-All Countries World ex-U.S. (14%); Lehman Brothers U.S. Universal Bond Index (34%); NCREIF Total Index (9%); Non-traditional assets (5%); and Salomon Non-\$ Bond Index Hedged (5%). During the three-year bear market, OCERS has achieved a negative annualized return of 1.87%. While any negative return is clearly disappointing, this result was better than the System's policy index return of negative 2.20% and ranked in the top quartile relative to other public funds. Over longer-term periods, the System's total return also modestly exceeds the policy index. For example, the ten and one-half year return of 8.58% was 4 basis points above the policy benchmark's 8.54% annualized return.

The graph below depicts the Total Fund relative to Callan's Total Public Fund Database for cumulative periods ended December 31, 2002.



As noted earlier, the System's asset allocation strategy was the primary driver in the achievement of strong relative performance results for calendar 2002. For example, OCERS has a 14% target allocation to international equities. The System's target index

for international equity is the MSCI-All Countries World ex-U.S. Index. This index declined 14.67% for the year; OCERS' international equities declined 17.78%. Thus, while OCERS international managers declined slightly more than their market benchmark for the full year, the System still benefited from international diversification as domestic equities declined by a larger percent (the Russell 3000 was down 21.54%). Over longer-term periods, OCERS' international equity composite has achieved better than index returns.

A similar pattern was evident in the bond area. OCERS' domestic bond component underperformed its target index for the year (+7.85% versus +9.83% for the Lehman U.S. Universal Bond Index). The underperformance for the year was primarily attributable to OCERS managers' emphasis on corporate bonds, including their exposure to BAA and lower rated securities. While these securities experienced positive absolute returns, they did not fare as well as government securities. Over the long-term, OCERS' aggregate bond composite continues to outpace market indices and peers. For the ten and one-half years ended 12/31/02, OCERS' bond composite ranks in the second percentile of the Public Fund database. The 8.57% annualized return exceeds the target index return of 7.58%. Another excellent illustration of the importance and benefit of broad diversification is the System's international bond component. This sector of the portfolio benefited from dollar weakness. The decline in the value of the dollar helped this segment of the portfolio achieve a positive return of 20.42% for the year.

OCERS' U.S. equity composite declined 19.29% in 2002. While poor in absolute terms, this result was better than the equity market target return of negative 21.54%. It also ranked exceedingly well in the Callan Public Fund Sponsor database (it placed in the 7th percentile). Over all cumulative periods considered, OCERS' domestic equity composite has achieved very strong comparative returns. For example, the trailing five-year return of positive 1.0% ranked in the 21st percentile and exceeded the target benchmark return of 0.17%.

In summary, calendar 2002 was another difficult and challenging year for investors. Fortunately, OCERS' conservative asset allocation strategy and broad diversification helped the System weather the market declines in a comparatively strong manner.

Sincerely,



Michael J. O'Leary, Jr., CFA
Executive Vice President

**Orange County Employees Retirement System
Investment Returns**

The table below details the annualized rates of return for the different asset categories over various time periods ended December 31, 2002. The returns for each asset class represents the composite returns of all the manager portfolios within that asset class. All returns are gross of fees except for alternative assets and real estate, where some of the fees are deducted at source.

	1 Year	3 Year	5 Year
Domestic Equity	-19.29%	-9.87%	1.00%
<i>Russell 3000 Index</i>	-21.54%	-13.69%	-0.71%
International Equity	-17.78%	-18.65%	-1.30%
<i>MSCI AC World Ex US Index</i>	-14.67%	-16.44%	-2.66%
<i>MSCI Eafe Index</i>	-15.94%	-17.24%	-2.89%
Domestic Fixed	7.85%	8.69%	6.86%
<i>Lehman Bros Universal Index</i>	9.83%	9.58%	7.18%
International Fixed Income	20.42%	8.81%	7.50%
<i>S/B Non-US Hedged Govt. Index</i>	6.85%	7.52%	7.37%
Cash & Equivalents	2.54%	5.28%	6.72%
Real Estate	7.02%	7.14%	8.85%
<i>NCREIF Property Index</i>	5.57%	9.13%	11.35%
Non - Traditional	-8.93%	1.88%	6.74%
Total Fund	-5.46%	-1.87%	4.27%
<i>Composite Policy Benchmark*</i>	-5.45%	-2.20%	4.57%

* Policy Benchmark = 33% Russell 3000 + 34% LB US Universal Index + 9% CAI Real Estate Funds + 5% OCERS Non-Traditional + 14% MSCI All Country World Ex USA + 5% Salomon Non-US Hedged Government Index.

**Orange County Employees Retirement System
Statement of Investment Objectives and Policies**

General:

This statement is intended to set forth the factors involved in the management of investment assets for the Orange County Employees Retirement System (the System). The responsibility of the Board (with the participation of its Investment Committee, Staff and Advisors) is to establish broad investment policy, guidelines and objectives for the total fund and its component parts, to select independent investment managers and to monitor the activities of the investment managers. The responsibility of each investment manager is to develop and implement management strategies in accordance with the stated investment policies, guidelines and objectives, in a manner consistent with the “prudent man” rule for similar funds, i.e., with care, skill, prudence and diligence, with full discretion subject to the guidelines and applicable statutes. The investment manager is responsible for administration of the investment program within parameters established.

Strategic Asset Allocation Policy and Maintenance:

The Board periodically undertakes strategic asset allocation studies. Such studies define the targeted level of diversification among the various major asset classes and the range in which they are permitted to fluctuate. When significant changes are made to the plan, a transition plan is adopted.

In normal circumstances, asset levels are permitted to fluctuate around targeted levels, and cash inflows are administered by staff in a manner that is consistent with maintenance of the desired level of diversification. When asset fluctuations and/or external cash flows take actual allocation outside the accepted range, cash inflows shall be directed toward the underallocated asset categories and cash outflows shall be directed from the overallocated asset classes.

Should expected external flows be judged by staff to be insufficient to bring the plan within permitted ranges within a 12 month period, staff shall inform the Investment Committee. The Investment Committee then will formulate a recommendation to shift assets that will be presented to the full Board.

Program Administration and Manager Structure:

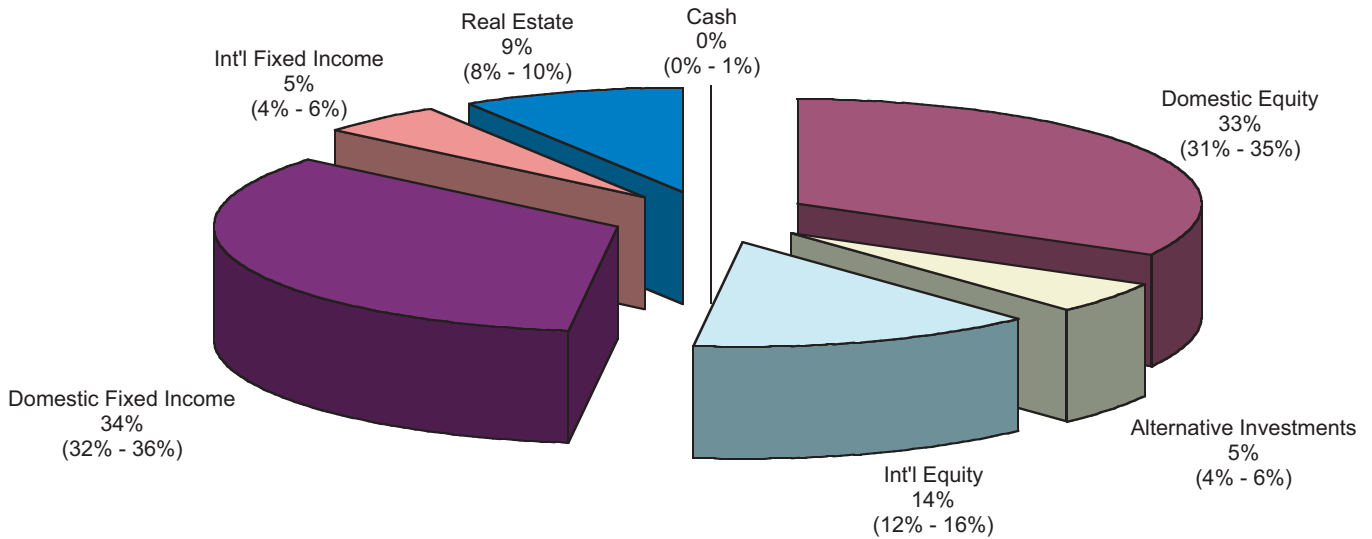
For each major asset class, the System shall diversify assets by employing managers with demonstrated skill in their particular areas of expertise. The System will retain managers who utilize varied investment approaches and allocate assets in a manner that is consistent with the overall strategic plan. So, for example, the sum of all domestic equity managers should exhibit characteristics that are similar, but not necessarily identical, to the overall equity market. When asset fluctuation causes the asset class to exhibit characteristics that are dissimilar from the plan, staff shall direct cash flows to or from the various managers so that actual characteristics are consistent with the plan. Should unusual circumstances create a significant imbalance that cannot be corrected through the routine allocation of external cash flows, the Investment Committee shall formulate a recommendation for Board consideration.

Orange County Employees Retirement System

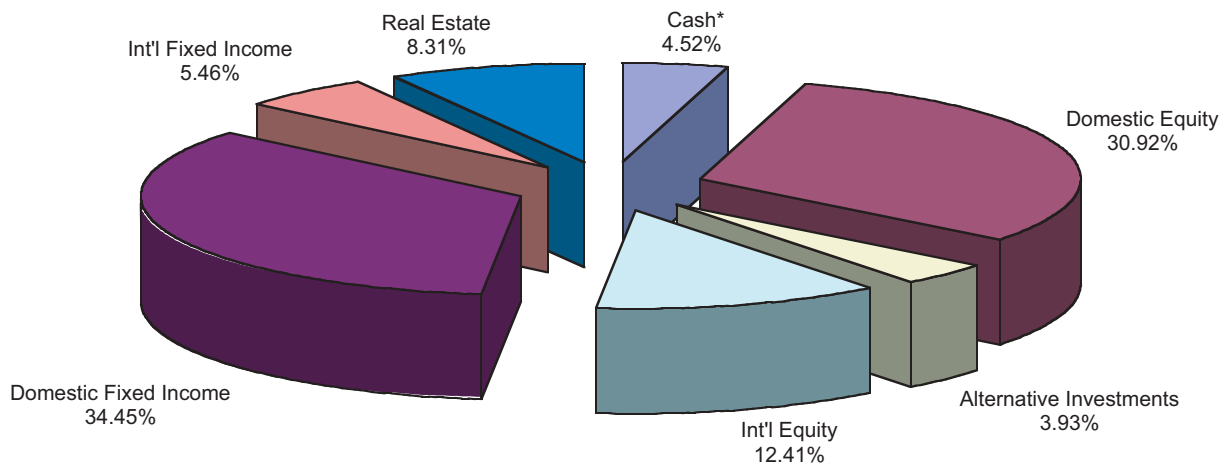
Asset Diversification

December 31, 2002

Policy

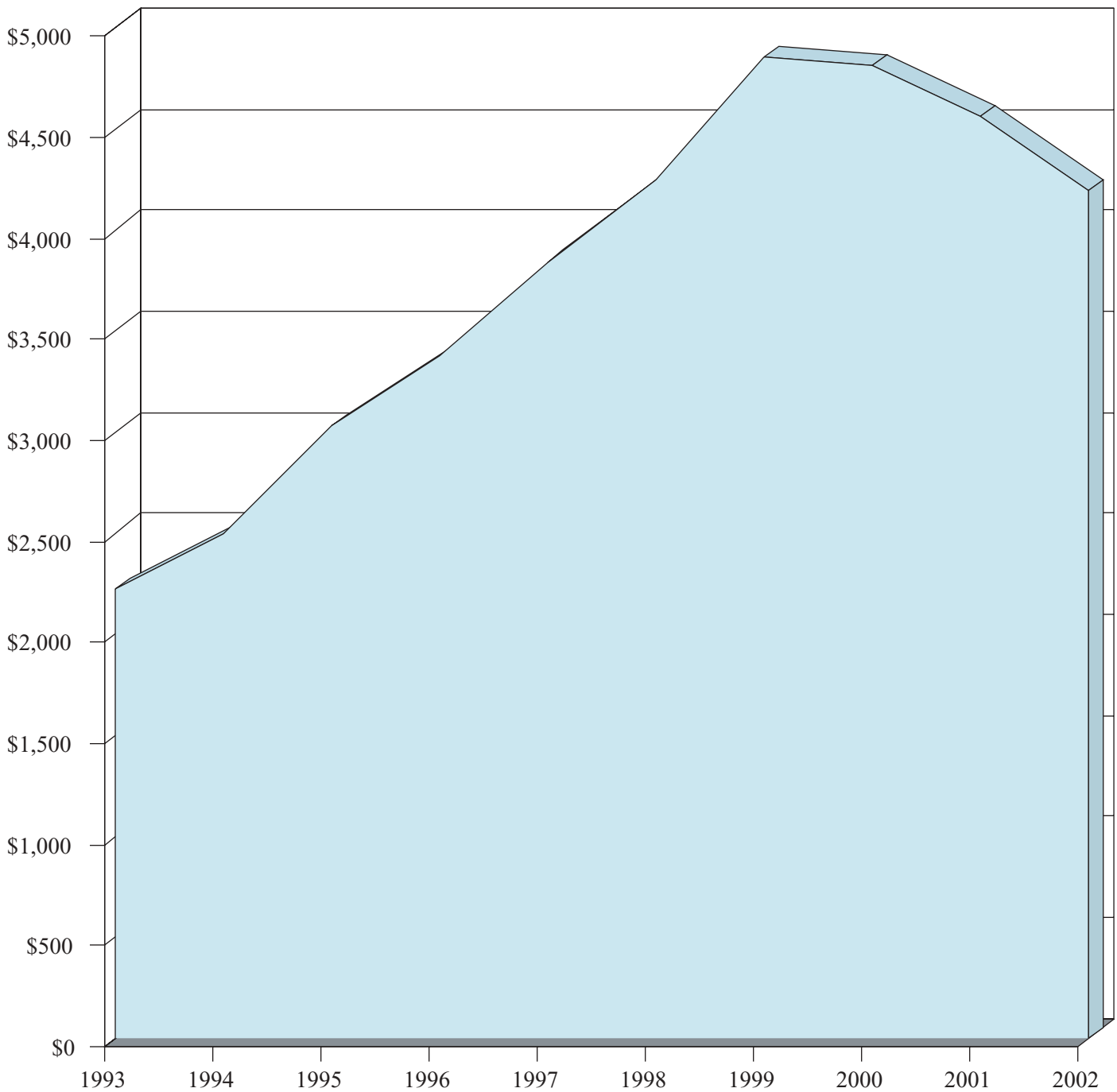


Actual

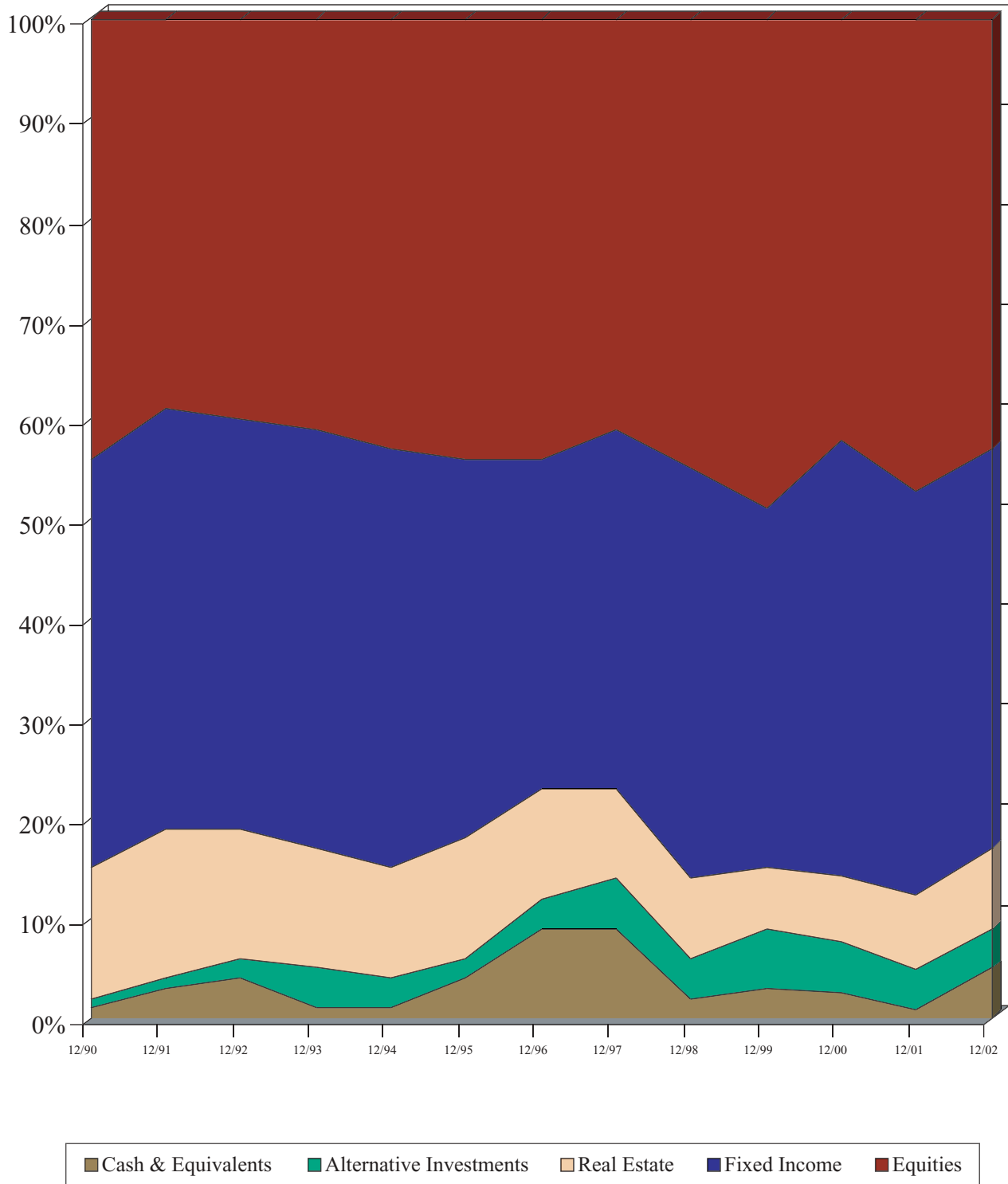


* Includes cash equivalents held by investment managers.

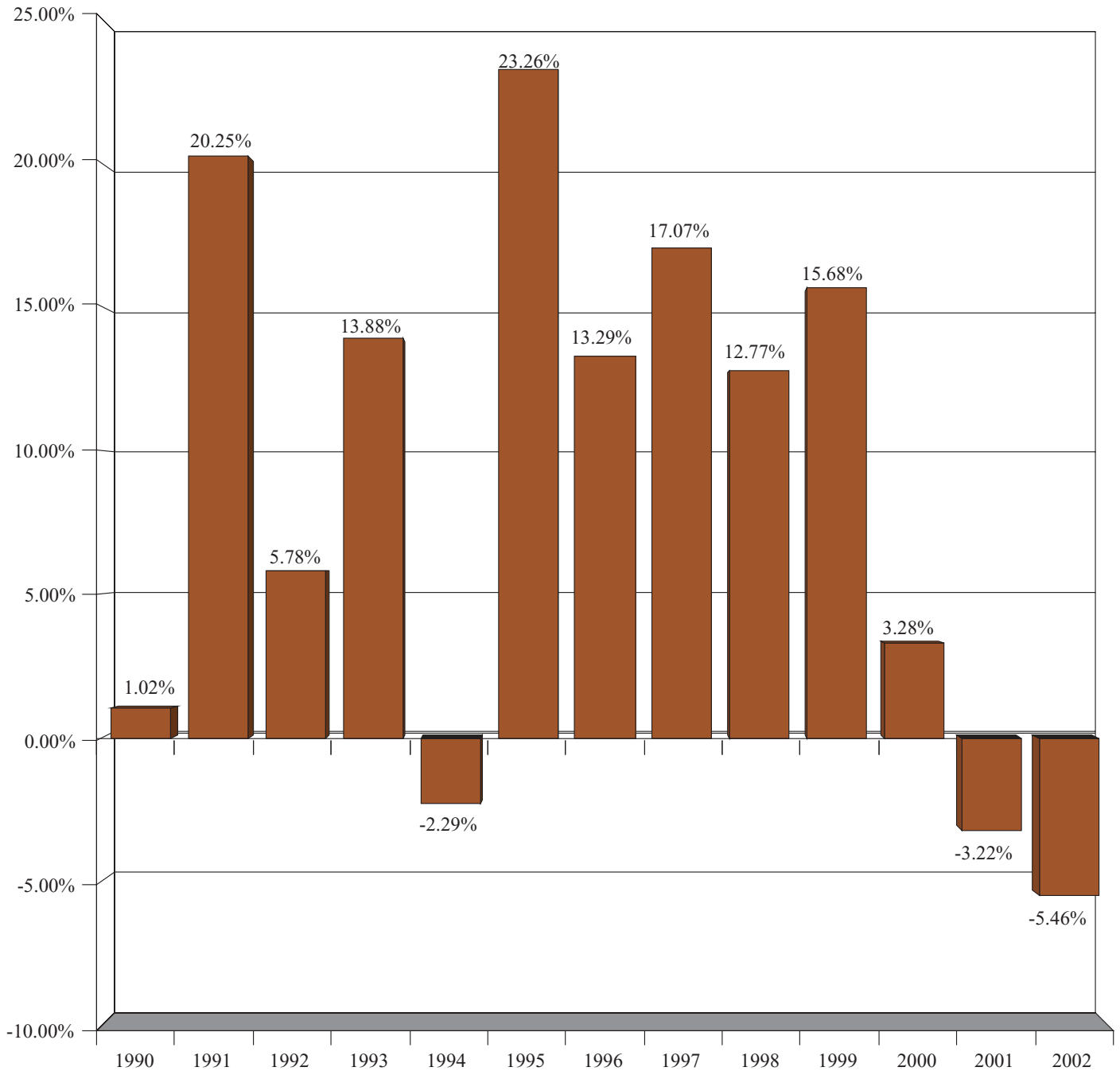
**Orange County Employees Retirement System
Growth of System Net Assets at Fair Value
for Ten Years Ended December 31, 2002
(in Millions of Dollars)**



Orange County Employees Retirement System Historical Asset Allocation (Actual) December 1990 - December 2002



Orange County Employees Retirement System History of Performance (Based on Fair Value)



Orange County Employees Retirement System
Schedule of Commissions
for the Year Ended December 31, 2002

Brokerage Firms	Number of Shares Traded	Total Commission	Commission Per Share
Abel Noser Corporation	1,778,337	65,632	0.03691
ABG Securities (Stockholm)	12,800	17	0.00133
ABN AMRO Securities	991,518	12,823	0.01293
Acciones Y Valores De Mexico	175,500	1,418	0.00808
Adams Harkness & Hill, Inc.	69,320	3,476	0.05015
Advest, Inc.	57,000	2,850	0.05001
Americas/Deutsche Bank AG London	12,200	610	0.05000
Arnold S. Bleichroeder, Inc.	414,300	1,555	0.00375
Auerbach Grayson	13,900	695	0.05000
Baird, Robert W & Co.	589,696	26,456	0.04486
Bank of America Intl. Ltd.	1,897,803	66,767	0.03518
Baring Securities (Hong Kong)	86,500	771	0.00892
Bear, Stearns Securities Corp.	2,127,691	66,869	0.03143
BHC Securities, Inc.	25,700	1,266	0.04927
BHF Securities Corp.	2,800	281	0.10035
BNP Paribas	4,700	172	0.03653
BNY ESI Transition Management	1,144,000	36,792	0.03216
Brick Securities Div. of Gerard Klauer	5,600	285	0.05096
Bridge Trading	538,438	21,265	0.03949
Broadcort Capital (Thru ML)	85,300	4,304	0.05046
Brockhouse & Cooper, Inc., Montreal	702,000	14,720	0.02097
Brown Brothers Harriman & Co.	44,700	2,257	0.05049
B-Trade Services LLC	323,500	6,127	0.01894
Buckingham Research Group	39,400	2,125	0.05394
C.L. Glazer & Company, Inc.	1,600	80	0.05000
C.E. Unterberg, Tobin	2,800	140	0.05000
Canadian Imperial Bank of Commerce	12,000	300	0.02502
Cantor Fitzgerald & Co., Inc.	520,203	22,871	0.04397
Capel, James HSBC Securities Inc.	22,000	1,100	0.05000
Capital Institutional Services	616,200	12,773	0.02073
Cazenove & Co.	290,974	3,138	0.01079
Charles Schwab & Co., Inc.	703,982	33,214	0.04718
CI Nordics Securities AB	1,400	32	0.02313
CIBC World Markets Corp.	437,400	22,032	0.05037
Citation Group	86,000	5,076	0.05902
Commerzbank Capital Market Corp.	124,100	7,597	0.06121
Correspondent Services, Inc.	87,300	4,096	0.04692
Credit Agricole Indoduez Cheuvreux	342,526	12,913	0.03770
Credit Lyonnais Securities	387,900	6,932	0.01787
CSFB Australia Equities Ltd.	4,311,596	114,844	0.02664
Daiwa SBCM Europe	293,400	2,380	0.00811
Davenport & Co. of Virginia, Inc.	6,800	341	0.05012
Davidson D.A. & Company, Inc.	24,300	1,216	0.05002

Orange County Employees Retirement System
Schedule of Commissions
for the Year Ended December 31, 2002

<u>Brokerage Firms</u>	<u>Number of Shares Traded</u>	<u>Total Commission</u>	<u>Commission Per Share</u>
Davy (J &E)	153,375	4,086	0.02664
DB Clearing Services	4,600,000	920	0.00020
Deutsche Securities Asia Ltd.	3,385,316	97,428	0.02878
Donaldson, Lufkin & Jenrette Securities	29,202	424	0.01452
Dowling & Partners Securities, LLC.	27,800	1,400	0.05034
Dresdner Kleinwort Besnon	184,100	2,536	0.01378
E Trade Securities, Inc.	470,018	10,853	0.02309
Edwards AG & Sons Inc.	101,500	5,149	0.05073
Enskilda Securities	42,800	1,487	0.03475
E Trade Securities Ltd., Hong Kong	6,000	247	0.04117
Exane S.A.	77,616	4,669	0.06015
Execution Services, Inc.	22,00	2,682	0.12193
Executive Investment Co.	27,800	666	0.02396
F P Maglio & Co., Inc.	68,900	3,493	0.05069
Factset Data Systems	52,500	2,625	0.05000
Fidelity Capital Markets	168,914	8,569	0.05073
Financial West Group, Inc.	1,600	81	0.05070
First Albany Corp.	53,100	2,663	0.05015
First Clearing Corp.	6,760	7	0.00105
First Energy Capital	800	31	0.03820
First Tennessee Securities Corp.	62,800	3,174	0.05054
First Union Capital Markets	326,900	16,493	0.05045
Fiserv Correspondent Services Inc.	14,100	713	0.05056
Fleet Boston Robertson Stephens	99,885	2,296	0.02299
Fox Pitt Kelton Inc.	117,000	6,130	0.05239
Frank Russell	16,200	828	0.05108
Friendman Billings & Ramsey	50,900	2,578	0.05065
Friend, L.H., Weinress & Frankson	19,200	973	0.05069
Fulcrum Global Partners, LLC	41,200	2,093	0.05081
Girard Securities , Inc.	67,400	3,487	0.05174
Goldman Sachs Secs. Japan	6,055,228	154,592	0.02553
Goodbody Stockbrokers	20,600	481	0.02333
Green Street Advisors, Inc.	19,30	965	0.05000
Griswold Company	9,500	570	0.06000
Guarente & Co.	167,000	526	0.00315
Harborside Securitates	5,400	161	0.03010
Henderson Crosthwaite Ltd.	12,400	96	0.00778
Herzog Heinz Geduld (Equity)	20,320	1,016	0.05001
Hibernia Southcoast Capital Inc.	87,500	4,375	0.05000
Hoeffler & Arnett	16,343	654	0.04003
Hoening & Co.	9,000	450	0.05000

Orange County Employees Retirement System
Schedule of Commissions
for the Year Ended December 31, 2002

Brokerage Firms	Number of Shares Traded	Total Commission	Commission Per Share
Howard Weil Division Legg Mason	19,600	980	0.05000
HSBC Securities, Inc.	203,000	2,604	0.01283
HSBC Securities (Asia) Ltd.	1,023,953	19,140	0.01869
Indosuez Capital Securities	63,900	809	0.01265
ING Barings Securities Ltd.	1,320,875	4,506	0.00341
Instinet U.K. Ltd.	309,804	6,388	0.02062
Investec Ernst & Company	131,800	6,315	0.04792
Invesment Technology Group, Inc.	2,827,710	57,343	0.02028
ISI Group, Inc.	43,200	2,174	0.05033
J. B. Were and Son	609,500	6,110	0.01002
J. Michael Patrick, LLC	7,000	350	0.05000
JP Morgan Securities, Inc.	589,828	26,032	0.04414
Janey Montgomery, Scott	444,730	22,324	0.05020
Jefferies & Co.	1,671,803	64,523	0.03859
Johnson Rice & Co.	32,100	1,610	0.05017
Jones & Associates	96,700	4,411	0.04562
JP Morgan Securities Limited	769,193	25,667	0.03337
Julius Baer Securities	292,702	4,932	0.05105
Keefe Bruyette & Woods, Inc.	59,500	3,037	0.05105
Kleinwort Benson Securities Limited	1,225,028	18,712	0.01528
King CL & Associates, Inc.	64,000	3,213	0.05020
Knight Securities L.P.	326,230	15,742	0.04825
KV Execution Services, LLC	900	27	0.03000
LA Branche Financial Services, Inc.	531,800	26,590	0.05000
Lazard Freres & Co.	608,600	30,711	0.05046
Leerink Swann and Co.	189,300	9,550	0.05045
Legg Mason Wood Walkers Inc.	516,740	26,053	0.05042
Lehman Brothers Securities (Asia)	4,499,209	100,054	0.02224
Levesque Beaubien Geoffrion	48,500	1,258	0.02595
Liquidnet, Inc.	48,600	994	0.02045
Lombard, Odier and CIE	30,630	3,999	0.13056
Lynch Jones and Ryan, Inc.	3,362,162	130,197	0.03872
M.M. Warburg	19,774	1,765	0.08926
M.J. Whitman, Inc.	18,600	933	0.05018
MacQuarie Equity Ltd. (Sydney)	42,877	1,197	0.02792
Main First Bank DE	14,700	1,128	0.07672
McDonald Company Securities, Inc.	223,880	9,816	0.04385
Merrill Lynch Professional Clearing Corp.	9,709,432	273,063	0.02812
Merrion Capital Group	40,500	1,664	0.04109
Midwest Reasearch Securities	16,500	825	0.05000
Miller Tabak Hirsch	755,807	37,985	0.05026
Mizuho Securities	55,500	1,479	0.02665

Orange County Employees Retirement System
Schedule of Commissions
for the Year Ended December 31, 2002

Brokerage Firms	Number of Shares Traded	Total Commission	Commission Per Share
Morgan Grefell and Co., Limited	1,800,906	28,546	0.01585
Morgan Keegan & Co., Inc.	75,651	3,829	0.05061
Morgan Stanley & Co., Inc.	5,853,133	186,462	0.03186
National Investore Services Corp.	6,600	330	0.05000
NBCN Clearing, Inc.	2,800	143	0.05091
NCB Stockbrokers, Ltd.	166,500	5,708	0.03428
Needham & Company	6,500	325	0.05000
Nesbitt Burns	132,300	4,402	0.03327
Net Fondkommission	11,400	131	0.01149
Neuberger & Berman	138,400	6,627	0.04788
NIKKO Salomon Smith Barney, Ltd.	3,900	261	0.06685
Nomura Securites Co., Ltd.	469,744	6,926	0.01474
Pacific Growth Securities	23,500	1,085	0.04618
Panmure Gordon & Co., Ltd.	38,400	2,922	0.07610
Paribas Corp.	185,920	10,196	0.05484
PSC Securities, Inc.	39,600	1,987	0.05017
Pershing Securities, Ltd.	2,400	232	0.09658
Polcari/Weicker Div. of Garban Corp.	3,000	91	0.03021
Prudential Securities, Inc.	481,995	24,139	0.05008
Pulse Trading LLC	53,900	2,151	0.03991
Putnam Lovell Securities, Inc.	29,900	1,495	0.05000
Quaker Securities, Inc.	59,300	2,989	0.05040
Raymond James and Associates, Inc.	117,800	5,881	0.04992
RBC Dominion Securities, Inc.	39,998	1,778	0.04444
Robertson Stephens, Inc.	36,651	1,856	0.05064
Robotti & Company	159,400	7,591	0.04762
Rockhouse Securities LLC	852,200	13,838	0.01624
Russell Frank Securities, Inc.	8,000	400	0.05000
Ryan Beck & Co.	25,800	1,309	0.05075
Safian Investment Research, Inc.	2,300	92	0.04000
Salomon Smith Barney Secs. (Sydney), Inc.	6,138,609	180,026	0.02933
Sanders Morris Mundy	108,600	5,456	0.05024
Sandler O'Neil & Part, L.P.	330,100	16,637	0.05040
Sandford Berstein Co., LLC	579,642	27,839	0.04803
Santaderin Investment Securities, Inc.	4,700	282	0.06000
SBC Warburg London	581,444	13,390	0.02303
Scotia Capital Markets	237,300	7,616	0.03209
Scott & Stringfellow, Inc.	37,600	1,903	0.05060
S G Securities (London) Ltd.	604,766	28,216	0.04666
Sidoti & Co.	56,000	2,818	0.05032
Simmons & Company International	28,800	1,459	0.05064
Skandinaviska Enskilda Banken London	37,200	2,372	0.06376

**Orange County Employees Retirement System
Schedule of Commissions
for the Year Ended December 31, 2002**

<u>Brokerage Firms</u>	<u>Number of Shares Traded</u>	<u>Total Commission</u>	<u>Commission Per Share</u>
Societe General Securities Corporation	300	16	0.05233
Southwest Securities	112,400	5,643	0.05021
Spear, Leeds & Kellogg	35,100	875	0.02492
Standard & Poors Services	38,100	2,230	0.05853
State Street Brokerage Services	2,000	101	0.05024
Stephens, Inc.	13,200	675	0.05116
Stifel Nicolaus & Co., Inc.	792,700	23,982	0.03025
Sunbelt Securities	6,100	305	0.05000
Suntrust Capital Markets, Inc	142,650	7,187	0.05038
Svenska Handelsbanken (London)	400.00	24	0.05975
Thomas Weisel Partners	295,657	13,353	0.04516
Thomson Institutional Service	111,400	5,606	0.05033
U.S. Bancorp Piper Jaffray, Inc.	197,503	9,946	0.05036
U.S. Clearing Institutional Trading	34,500	1,728	0.05009
UBS Warburg LLC	5,187,196	120,325	0.02320
USCC/Santander	5,400	324	0.06000
Veritas Securities	445,433	15,267	0.03427
Vontobel Securities	51,400	4,342	0.08447
Wachovia Securites	24,500	1,470	0.06000
Warburg Dillon Read LLC	552,316	18,576	0.03363
Weeden & Co.	405,452	19,884	0.04904
Wells Fargo Van Kasper LLC	43,100	2,158	0.05008
Westminster Research Associates	77,900	3,902	0.05009
William Blair & Company LLC	76,840	3,878	0.05047
Wit Soundview Corp.	179,900	9,045	0.05028

Orange County Employees Retirement System

Investment Summary

December 31, 2002

(in thousands)

<u>Investment</u>	<u>Fair Value</u>	<u>Percentage</u>
Domestic Equity	\$ 1,309,199	30.92%
Domestic Fixed Income	1,459,003	34.45%
International Equity	525,473	12.41%
International Fixed Income	231,359	5.46%
Alternative Investments	166,450	3.93%
Real Estate	351,704	8.31%
Cash and Cash Equivalents	191,402	4.52%
Total	\$ 4,234,590	100.00%

Schedule of Largest Stock Holdings (by Fair Value)*

December 31, 2002

<u>Stock</u>	<u>Security Description</u>	<u>Fair Value</u>
Vodafone Group	Common Stock	\$ 15,184,187.96
Medtronic, Inc.	Common Stock	11,441,040.00
Microsoft Corp.	Common Stock	11,146,520.00
Sanofi Synthelaboratory	Common Stock	10,910,666.35
Goldman Sachs Grou, Inc.	Common Stock	8,709,990.00
First Data Corporation	Common Stock	8,569,220.00
Royal Dutch Petroleum	Common Stock	8,495,841.46
Aatrazeneca	Common Stock	7,946,527.25
American International Group, Inc.	Common Stock	7,312,240.00
Pfizer, Inc.	Common Stock	6,973,017.00

Schedule of Largest Bond Holdings (by Fair Value)*

December 31, 2002

<u>Bonds</u>	<u>Moody's Quality Rating</u>	<u>Fair Value</u>
FNMA TBA January 15, Single Family 5.500%, 12/31/2099	AAA	\$ 21,741,562.50
Ford Motor Credit Company 1.000% due 02/13/2003	A3	21,628,350.00
Tele Communications, Inc. 8.250% due 01/15/2003	BAA3	20,020,112.00
Federal Republic of Germany 4.000%, 06/04/2009	AAA	18,580,177.09
United States Treasury Bonds, 7.500%, 11/15/2016	AAA	17,801,079.44
Kingdom of Spain, 5.150%. 07/10/2009	AAA	16,924,640.44
FNMA TBA January 15, Single Family, 6.000%, 12/01/2099	AAA	16,712,499.20
United States Treasury Bonds, 7.125%, 02/15/2003	AAA	15,649,412.53
United States Treasury Bonds, 3.875%, 04/15/2029	AAA	15,007,108.23
Republic of France, 5.500%, 04/25/2010	AAA	14,896,202.22

* A complete listing of portfolio holdings is available for review at the OCERS' office.

IV. Actuarial Section



Member Services Division

Top row, from left, Dewey Wiles, Andre Kujawski, Debra Velick, Elena Rosales, Ann Golden, Linda Ealy, Helen Nemeth, Ricki Parker, Stephen Cadena, and Mike Kulzer. Bottom row, from left, Susan Spietz, Irene Rojas, Eunice Lopez, Isabel Linares, Carmen Garcia, Sandy Guevara, Kim Otto, Diana Kahler, Kim Scaife, Debbie Villa, Susan Parrino, and Suzanne Jenike.

Timothy J. Marnell, ASA
Principal
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312 609-9461
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Towers Perrin

May 15, 2003

Retirement Board
Orange County Employees Retirement System
2223 Wellington Avenue
Santa Ana, CA 92701-3101

Members of the Board:

The financing objective of the system has been to reduce the unfunded actuarial accrued liability (UAAL) to zero over a 28-year period commencing December 31, 1995, while maintaining contribution rates that remain approximately the same from generation to generation. Emerging gains and losses have been amortized separately over individual 15-year periods. Other changes to the UAAL, created by assumption changes or plan amendments, have been amortized over periods established by the Board. Effective with the December 31, 2002 actuarial valuation, the Board elected to restart the amortization period for General Members, including Probation Officers, to 30 years. Future changes to UAAL will be amortized as described above. The amortization periods for Safety Members will be reviewed in future periods. The progress being made toward the realization of the financing objectives through December 31, 2002 is illustrated in the attached Exhibits I and II.

An actuarial investigation is performed every three years, during which an analysis is made of the appropriateness of all economic and noneconomic assumptions. Recommendations for changes are presented to the Board for consideration. A regularly scheduled investigation was performed as of December 31, 2001, at which time changes to certain demographic assumptions were recommended to, and adopted by, the Board. Decisions concerning changes to economic assumptions were delayed until the December 31, 2002 actuarial valuation. Effective with that valuation, the interest rate and salary increase assumption were both decreased. Regular valuations are performed every year to comply with GASB requirements, to adjust contribution rates, and to monitor the plan's funded status.

The asset value used in determining employer contribution rates (the actuarial value of assets) is a five-year moving average of book and market values (Exhibit V). We have enclosed a summary of the employee data used in performing actuarial valuations over the past several years (Exhibits III and IV). Exhibit VII provides a summary of plan provisions.

Retirement Board
May 15, 2003
Page 2.

Towers Perrin

The actuarial assumptions used in the December 31, 2002 valuation are summarized in the attachments. All assumptions were determined by the actuary and were adopted by the Board. The actuarial assumptions and methods used for funding purposes satisfy the disclosure requirements of GASB 25.

Beginning with the December 31, 2001 valuation, actuarial experience was analyzed by employer. Using the results of this analysis, separate employer and member contribution rates were developed for certain groups of employees.

The employee census data and asset information were provided by the Retirement Office. The census data was reviewed, compared against the prior year, and appeared to be reasonable. The asset information was accepted without further audit.

All of the schedules in the Actuarial Section were prepared under my direction, including:

- History of Unfunded Actuarial Accrued Liability
- History of Employer Contribution Rates
- Summary of Active Membership
- Summary of Retired Membership
- Development of Actuarial Value of Assets
- Short-Term Solvency Test
- Actuarial Methods and Assumptions, including the attached Tables
- Summary of Major Plan Provisions
- Analysis of Financial Experience

We did not prepare any of the schedules presented in the Financial Section. It is our understanding, however, that OCERS staff used information contained in our actuarial valuation reports to prepare the trend schedules presented in that section.

On the basis of the December 31, 2002 valuation, it is our opinion that OCERS continues to be in sound condition in accordance with the actuarial principles of level cost financing.

Respectfully submitted,



Timothy J. Marnell, A.S.A., M.A.A.A.

Orange County Employees Retirement System
History of Unfunded Actuarial Accrued Liability
(in thousands)

Valuation Date	Actuarial Accrued Liability	Actuarial Value of Assets	Unfunded Actuarial Accrued Liability	Ratio of Assets to Actuarial Accrued Liability	Annual Active Member Compensation	Ratio of Unfunded Actuarial Accrued Liability to Active Compensation
12/31/93	\$2,305,019	\$2,024,447	\$280,572	87.83%	\$725,193	38.69%
12/31/94	2,550,059	2,177,673*	372,386	85.40%	769,175	48.41%
12/31/95	2,633,884	2,434,406*	199,478	92.43%	727,768	27.41%
12/31/96	2,851,894	2,675,632*	176,262	93.82%	758,897	23.23%
12/31/97	3,332,967	3,128,132*	204,835	93.85%	781,890	26.20%
12/31/98	3,682,686	3,504,708*	177,978	95.17%	863,199	20.62%
12/31/99	4,017,279	3,931,744*	85,535	97.87%	912,490	9.37%
12/31/00	4,335,025	4,497,362*	(162,337)	103.74%	994,669	(16.32%)
12/31/01	4,843,899	4,586,844*	257,055	94.69%	1,122,763	22.89%
12/31/02	5,673,754	4,695,675*	978,079	82.76%	1,242,348	78.73%

Notes:

- The 12/31/02 valuation included changes to the interest rate and salary increase assumptions. The interest rate changed from 8.0% to 7.5% and the salary increase assumption from 5.5% to 4.5%. These changes increased employer rates and generally decreased member contribution rates slightly. The retirement benefit for Firefighters was changed to a 3% per year of service benefit payable unreduced at age 50. Probation Officers became Safety Members with a portion of service for Tier II members converted to Safety Member service at less than one-for-one.
- The 12/31/01 valuation included changes to the assumed withdrawal rates, the assumed termination rates, the assumed service connected disability rates and the assumed retirement rates. These changes increased both member and employer contribution rates. The retirement benefit for Law Enforcement was changed to a 3% per year of service benefit payable at age 50.
- The 12/31/98 valuation included changes to the assumed withdrawal rates, the assumed preretirement mortality and the assumed retirement rates. These changes increased both member and employer contribution rates.
- The 12/31/97 valuation included an increase in plan benefits to reflect the impact of the California Supreme Court decision in the Ventura County case regarding compensation earnable.
- The 12/31/95 valuation included a change in the salary scale from 6.0% to 3.5% per annum through the year 2000, and 5.5% thereafter. The aggregate payroll increase assumption was also changed from 5.0% to 4.5% per annum.

* The 12/31/94, 12/31/95, 12/31/96, 12/31/97, 12/31/98, 12/31/99, 12/31/00, 12/31/01 and 12/31/02 assets exclude \$311,022,000, \$329,064,000, \$313,250,000, \$322,333,000, \$302,909,000, \$286,139,000, \$272,789,000, \$221,643,000, and \$143,675,000, respectively, of the County's unamortized 1994 funding of its portion of the Unfunded Actuarial Accrued Liability, which funding for 1995 was being amortized over a 14-year period beginning July 1, 1994 and for 1996 and later was being amortized over a 28-year period beginning July 1, 1996. Beginning July 1, 2003, the County can utilize this amount at its discretion to fund any portion of the employer contribution.

**Orange County Employees Retirement System
History of Employer Contribution Rates
Employer Contribution Rate (% of pay)**

Valuation Date	General		Safety							
December 31, 1993	Normal	3.38	Normal	6.20						
	UAAL	<u>0.53</u>	UAAL	<u>18.56</u>						
	Total	3.91	Total	24.76						
December 31, 1994	Normal	3.68	Normal	6.58						
	UAAL	<u>1.71*</u>	UAAL	<u>21.85*</u>						
	Total	5.39	Total	28.43						
December 31, 1995	Normal	3.33	Normal	5.59						
	UAAL	<u>(0.47)*</u>	UAAL	<u>18.84*</u>						
	Total	2.86	Total	24.43						
December 31, 1996	Normal	3.38	Normal	5.77						
	UAAL	<u>(1.06)</u>	UAAL	<u>17.77</u>						
	Total	2.32	Total	23.54						
December 31, 1997	Normal	3.77	Normal	6.79						
	UAAL	<u>(1.91)</u>	UAAL	<u>19.65</u>						
	Total	1.86	Total	26.44						
December 31, 1998	Normal	4.35	Normal	8.00						
	UAAL	<u>(2.35)</u>	UAAL	<u>16.41</u>						
	Total	2.00	Total	24.41						
December 31, 1999	Normal	4.56	Normal	8.27						
	UAAL	<u>(3.60)</u>	UAAL	<u>13.95</u>						
	Total	0.96	Total	22.22						
December 31, 2000	Normal	4.94	Normal	8.57						
	UAAL	<u>(3.98)</u>	UAAL	<u>0.16</u>						
	Total	0.96	Total	8.73						
	<i>Non-OCTA</i>		<i>OCTA</i>		<i>Law Enforcement</i>		<i>Fire Authority</i>		<i>Probation</i>	
December 31, 2001	Normal	5.04	Normal	4.20	Normal	15.87	Normal	10.30		
	UAAL	<u>0.62*</u>	UAAL	<u>0.77*</u>	UAAL	<u>9.15*</u>	UAAL	<u>1.89*</u>		
	Total	5.66	Total	4.97	Total	25.02	Total	12.19		
December 31, 2002	Normal	5.44	Normal	4.36	Normal	16.53	Normal	17.85	Normal	4.38
	UAAL	<u>3.71*</u>	UAAL	<u>3.87*</u>	UAAL	<u>21.34*</u>	UAAL	<u>16.81*</u>	UAAL	<u>4.19*</u>
	Total	9.15	Total	8.23	Total	37.87	Total	34.66	Total	8.57

* Includes an additional 0.50% of pay as required under an agreement between OCERS and the County.

**Orange County Employees Retirement System
Summary of Active Membership**

Valuation Date	Number	Annual Salary	Annual Average Salary	% Increase in Average Salary
12/31/93				
General	16,611	\$610,095,632	\$36,728	2.21%
Safety	2,186	115,097,702	52,652	1.57
Total	18,797	\$725,193,334	\$38,580	2.15
12/31/94				
General	17,084	\$645,117,097	\$37,761	2.81%
Safety	2,289	124,058,327	54,198	2.94
Total	19,373	\$769,175,424	\$39,703	2.91
12/31/95				
General	15,658	\$597,800,535	\$38,179	1.11%
Safety	2,351	129,967,110	55,282	2.00
Total	18,009	\$727,767,645	\$40,411	1.78
12/31/96				
General	15,736	\$623,682,535	\$39,634	3.81%
Safety	2,354	135,214,811	57,440	3.90
Total	18,090	\$758,897,346	\$41,951	3.81
12/31/97				
General	16,266	\$643,115,556	\$39,537	(0.24%)
Safety	2,427	138,774,560	57,179	(0.45)
Total	18,693	\$781,890,116	\$41,828	(0.29)
12/31/98				
General	16,976	\$706,507,935	\$41,618	5.26%
Safety	2,456	156,691,236	63,799	11.58
Total	19,432	\$863,199,171	\$44,422	6.20
12/31/99				
General	17,801	\$738,956,477	\$41,512	(0.25%)
Safety	2,556	173,533,473	67,893	6.42
Total	20,357	\$912,489,950	\$44,824	0.90
12/31/00				
General	18,382	\$809,054,612	\$44,016	6.04%
Safety	2,605	185,614,420	71,256	4.95
Total	20,987	\$994,669,032	\$47,400	5.76
12/31/01				
General	19,653	\$921,057,200	\$46,860	6.46%
Safety	2,676	201,705,606	75,372	5.78
Total	22,329	\$1,122,762,806	\$50,280	6.08
12/31/02				
General	19,002	\$976,660,649	\$51,398	9.68%
Safety	3,721	265,638,289	71,389	(5.28)
Total	22,723	\$1,242,348,938	\$54,674	8.74

Excludes Deferred and Pending members.

**Orange County Employees Retirement System
Summary of Retired Membership**

Year	Number of Members				Annual Allowance	% Increase in Annual Allowance	Average Monthly Allowance
	At Beginning of Year	Added During Year	Removed During Year	At End of Year			
1/93 to 12/93	5,304	267	(59)	5,512	\$69,241,800	12.03%	\$1,047
1/94 to 12/94	5,512	504	(200)	5,816	77,629,436	12.11	1,112
1/95 to 12/95	5,816	690	(147)	6,359	92,332,920	18.94	1,210
1/96 to 12/96	6,359	426	(154)	6,631	99,751,438	8.03	1,254
1/97 to 12/97	6,631	505	(224)	6,912	109,661,326	9.93	1,322
1/98 to 12/98	6,912	547	(215)	7,244	125,439,610	14.39	1,443
1/99 to 12/99	7,244	549	(256)	7,537	137,542,880	9.65	1,521
1/00 to 12/00	7,537	618	(240)	7,915	149,002,518	8.33	1,569
1/01 to 12/01	7,915	606	(305)	8,216	162,552,549	9.09	1,649
1/02 to 12/02	8,216	727	(255)	8,688	186,286,465	14.60	1,787

**Orange County Employees Retirement System
Development of Actuarial Value of Assets
December 31, 2002**

Plan Year Ending	Fair Value	Book Value	Ratio of Fair Value to Book Value
2002	\$3,983,071,947	\$4,377,410,744	0.909915
2001	3,793,056,765	4,071,017,323	0.931722
2000	4,015,261,166	3,826,675,630	1.049282
1999	4,183,305,471	3,277,313,800	1.276443
1998	3,643,078,679	3,045,622,732	1.196169

(1) Average ratio in five years preceding December 31, 2002	1.072706
(2) Book value on December 31, 2002	\$4,377,410,744
(3) Actuarial value of assets: (1) x (2)	\$4,695,674,770

Orange County Employees Retirement System
Short-term Solvency Test
(in thousands)

Valuation Date	(1) Active Member Contributions	(2) Liability for Inactive Participants	(3) Liability for Active Members (Employer Financed Portion)	Valuation Assets	Portion of Accrued Liability Covered by Valuation Assets		
					(1)	(2)	(3)
12/31/93	\$369,199	\$899,240	\$1,036,580	\$2,024,447	100%	100%	72.93%
12/31/94	413,058	1,002,300	1,134,701	2,177,673	100	100	67.18
12/31/95	438,949	1,201,057	993,878	2,434,406	100	100	79.93
12/31/96	484,451	1,295,334	1,072,109	2,675,632	100	100	83.56
12/31/97	523,770	1,554,017	1,255,180	3,128,132	100	100	83.68
12/31/98	567,932	1,632,708	1,482,047	3,504,708	100	100	87.99
12/31/99	618,463	1,782,432	1,616,383	3,931,744	100	100	94.71
12/31/00	671,152	1,911,328	1,752,545	4,497,362	100	100	100
12/31/01	739,084	2,085,697	2,019,118	4,586,844	100	100	87.27
12/31/02	858,121	2,496,133	3,177,621	4,695,675	100	100	42.21

Orange County Employees Retirement System Actuarial Methods and Assumptions

The Projected Unit Credit method was used with gains and losses being amortized over a 15-year period from the date first identified. The following actuarial assumptions were also used:

1. *Interest:* 7.5% per annum.
2. *Salary scale:* 4.5% per annum; the aggregate salary increase assumed for the entire system is 4.0% per annum. The number of active employees is assumed not to increase.
3. *Consumer Price Index:* Increase of 3.5% per annum subject to tier maximums.
4. *Spouses and dependents:* 80% of male employees and 50% of female employees assumed married at retirement, with wives assumed four years younger than husbands.
5. *Rehire of former employees:* Assumed not to be rehired.
6. *Asset valuation:* Asset values taken directly from statements furnished by OCERS. See Exhibit V for a description of the development of the actuarial value of assets.
7. *Rates of termination of employment:* As shown in Table I, which follows.
8. *Expectation of life after retirement:* As shown in Table II.
9. *Expectation of life after disability:* As shown in Table III.

Effective December 31, 2002, the Retirement Board elected to change the amortization period for the General Member and Probation Officer unfunded actuarial accrued liability (UAAL) to 30 years. The amortization is a level dollar amount.

The amortization of the Safety Member UAAL has not changed. That UAAL is amortized in pieces as follows. The UAAL as of December 31, 1995, is amortized as a level dollar amount over 28 years. Actuarial gains and losses for each year are amortized over separate 15-year periods on a level dollar basis. Changes in the UAAL arising from assumption changes and plan amendments are amortized over periods determined by the Board. All amortization periods are considered closed (i.e., level dollar amortization with a fixed end date).

Certain rates of termination of employment were changed effective December 31, 2001. The interest rate was changed effective December 31, 2002 from 8.0% to 7.5%. The interest rate was last changed on December 31, 1990. The salary increase assumption was changed effective December 31, 2002 from 5.5% to 4.5%. The salary increase rate was last changed December 31, 1995.

Orange County Employees Retirement System
Probability of Occurrence
(includes eligibility)

Age Nearest	Ordinary Withdrawal	Vested Withdrawal	Pre-retirement Death	Ordinary Disability	Service Retirement	Service Disability
Non-OCTA General Members — Male						
20	0.1700	0.0000	0.0004	0.0000	0.0000	0.0000
30	0.0890	0.0090	0.0006	0.0001	0.0000	0.0004
40	0.0430	0.0110	0.0012	0.0004	0.0000	0.0010
50	0.0260	0.0040	0.0039	0.0011	0.0200	0.0016
60	0.0000	0.0000	0.0092	0.0052	0.0632	0.0019
70	0.0000	0.0000	0.0000	0.0000	1.0000	0.0000
Non-OCTA General Members — Female						
20	0.1250	0.0000	0.0002	0.0000	0.0000	0.0000
30	0.0720	0.0080	0.0003	0.0001	0.0000	0.0004
40	0.0440	0.0100	0.0007	0.0006	0.0000	0.0006
50	0.0250	0.0060	0.0016	0.0015	0.0293	0.0016
60	0.0000	0.0000	0.0042	0.0026	0.0721	0.0019
70	0.0000	0.0000	0.0000	0.0000	1.0000	0.0000
OCTA General Members— Male						
20	0.2200	0.0000	0.0004	0.0000	0.0000	0.0000
30	0.1070	0.0090	0.0006	0.0001	0.0000	0.0002
40	0.0520	0.0110	0.0012	0.0004	0.0000	0.0005
50	0.0320	0.0040	0.0039	0.0011	0.0200	0.0022
60	0.0000	0.0000	0.0092	0.0052	0.0632	0.0063
70	0.0000	0.0000	0.0000	0.0000	1.0000	0.0000
OCTA General Members— Female						
20	0.2200	0.0000	0.0002	0.0000	0.0000	0.0000
30	0.1510	0.0080	0.0003	0.0001	0.0000	0.0004
40	0.0750	0.0100	0.0007	0.0006	0.0000	0.0010
50	0.0340	0.0060	0.0016	0.0015	0.0293	0.0100
60	0.0000	0.0000	0.0042	0.0026	0.0721	0.0000
70	0.0000	0.0000	0.0000	0.0000	1.0000	0.0000
Safety Members — Fire Authority						
20	0.0360	0.0000	0.0004	0.0000	0.0000	0.0003
30	0.0120	0.0029	0.0006	0.0001	0.0000	0.0004
40	0.0030	0.0026	0.0012	0.0004	0.0000	0.0009
50	0.0000	0.0015	0.0039	0.0023	0.0300	0.0120
60	0.0000	0.0000	0.0092	0.0000	0.4000	0.0000
70	0.0000	0.0000	0.0000	0.0000	1.0000	0.0000
Safety Members — Law Enforcement						
20	0.0360	0.0000	0.0004	0.0000	0.0000	0.0011
30	0.0120	0.0029	0.0006	0.0001	0.0000	0.0013
40	0.0030	0.0026	0.0012	0.0004	0.0000	0.0066
50	0.0000	0.0015	0.0039	0.0023	0.2660	0.0066
60	0.0000	0.0000	0.0092	0.0000	1.0000	0.0000
70	0.0000	0.0000	0.0000	0.0000	1.0000	0.0000

**Orange County Employees Retirement System
 Expectation of Life
 Age and Service Retirees
 1983 Group Annuity Mortality**

Age	Male	Female
20	57.86	64.15
30	48.11	54.29
40	38.46	44.52
50	29.19	34.92
60	20.64	25.67
70	13.18	17.13
80	7.64	10.20
90	4.28	5.41
100	2.28	2.36

Orange County Employees Retirement System
Expectation of Life
Disabled Retirees
1981 Disabled Mortality

Age	General	Safety
20	38.73	49.29
30	31.98	40.36
40	26.21	31.77
50	21.08	23.59
60	16.37	16.64
70	11.70	11.70
80	7.00	7.00
90	4.09	4.09
100	2.20	2.20

Orange County Employees Retirement System Assumptions Specific to the Ventura County Ruling

The Ventura County Ruling changed the definition of compensation earnable, a key variable in the determination of benefits payable from the Orange County Employees Retirement System. Because many of the elements of compensation and certain information about member contribution account balances were unavailable, assumptions needed to be made to complete the December 31, 2002 actuarial valuation. The following describes the key assumptions that were made and the rationale behind the assumptions. Overall, the assumptions used in the actuarial valuation are conservative but not overly conservative. As more information becomes available, changes to these assumptions will be considered.

Compensation Earnable:

Compensation earnable includes vacation, sick time and compensatory time that is earned and can be cashed out in the measurement period. The amount of these items that are included in final compensation will change over time as members learn the impact that these items can have on their retirement benefits. For the purpose of this valuation, it was assumed that members would cash out the maximum amount available.

**Orange County Employees Retirement System
Summary of Major Plan Provisions**

1. Membership Requirements:

Date of employment.

2. Monthly Salary Base for Benefits:

Highest one-year average (three-year average for Tier II members).

3. Service Retirement:

A. Eligibility:

10 years of service and age 50, or 30 years of service and any age (20 years for safety members), or age 70 with any service.

B. Benefit Formula per Year of Service:

2% for General Tier I; 1.667% for General Tier II; 3% for Firefighters and Law Enforcement; 2% for Probation Officers.

Reduced for retirement before age 57 (50 for Safety Members) and increased for retirement after age 57 (50 for Safety Members). Tier II General Plan Factors are found in Section 31676.1.

4. Ordinary Disability:

A. Eligibility:

Five years of service.

B. Benefit Formula per Year of Service:

For Tier I members, 1.8% per year of service (in most cases a minimum of one-third salary). Tier II members receive 1.5% per year of service. Members eligible for service retirement receive the greater of this benefit or their service retirement benefit.

5. Line-of-Duty Disability:

A. Eligibility:

No age or service requirement.

B. Benefit:

The greater of 50% of salary or the service retirement benefit, if larger and the member otherwise satis-

fies the service retirement eligibility.

6. Ordinary Death Before Eligible to Retire:

Refund of employee contributions with interest plus one month's salary for each year of service to a maximum of six months' salary.

7. Ordinary Death After Eligible to Retire for Service or Ordinary Disability:

60% of earned benefit payable to surviving eligible spouse.

8. Line-of-Duty Death:

50% of salary payable to spouse.

9. Death After Retirement:

A. Service or Ordinary Disability Retirement:

60% of member's unmodified allowance continued to eligible spouse.

B. Line-of-Duty Disability:

100% of member's allowance continued to spouse.

C. \$1,000 Lump Sum.

10. Termination of Employment:

A. Refund of accumulated employee contributions with interest.

B. If contributions left on deposit, entitled to earned benefits commencing at any time after member would have been eligible to retire.

11. Postretirement Cost-of-Living Benefits:

Based on changes in Consumer Price Index to maximum of 3% per year; excess "banked."

12. Member Contributions - Tier I (Tier II in parentheses):

Normal based on entry age, 1/200 (1/120) at 60 for General Members; 1/200 (1/100) at 50 for Safety Members. Cost-of-living contributions equal to percentage of normal: 51.90% (31.40%) for Non-OCTA General; 50.96% (35.56%) for OCTA General; 108.80% (54.86%) for Firefighters; 113.32% (57.36%) for Law Enforcement; 28.28% (14.10%) for Probation Officers.

Orange County Employees Retirement System
Analysis of Financial Experience
(in thousands)

Gains & Losses in Accrued Liabilities During Years Ended December 31 Resulting from Differences Between Assumed Experience & Actual Experience					
Type of Activity	Gains (or Losses) Per Year				
	1998	1999	2000	2001	2002
Retirements	\$(34,552)	\$(60,138)	\$(29,367)	\$(48,490)	\$(82,392)
Disabilities	18,431	13,197	16,780	17,696	(8,012)
Withdrawal From Employment	(7,697)	(23,003)	(4,633)	(13,932)	(15,328)
Pay Increases	(21,705)	(1,890)	(24,585)	(40,448)	(91,887)
Investment Income	141,642	163,736	286,267	(221,192)	(220,329)
Mortality	23,996	24,804	28,836	(3,021)	(7,422)
Other	<u>(15,635)</u>	<u>(17,803)</u>	<u>(20,775)</u>	<u>(20,534)</u>	<u>(18,001)</u>
Gain (or Loss) During Year From Experience	\$104,480	\$98,903	\$252,523	\$(329,921)	\$(443,371)
Non Recurring Items. Adjustment for Plan Amendments, Assumption Changes, etc.	<u>(71,574)</u>	<u>0</u>	<u>0</u>	<u>(85,395)</u>	<u>(238,027)</u>
Composite Gain (or Loss) During Year	\$32,906	\$98,903	\$252,523	\$(415,316)	\$(681,398)



Information Technology Division

From left, Stephen Cadena, Lan Mai, Joseph Bui, Sunny Donn, Cuong Nguyen, Brian Hoang, Javier Lara, and Anthony Beltran.



PensionGold Group

From left, Teresa Panameno, Diane Dillard, Lan Mai, and Debra Velick.

V. Statistical Section

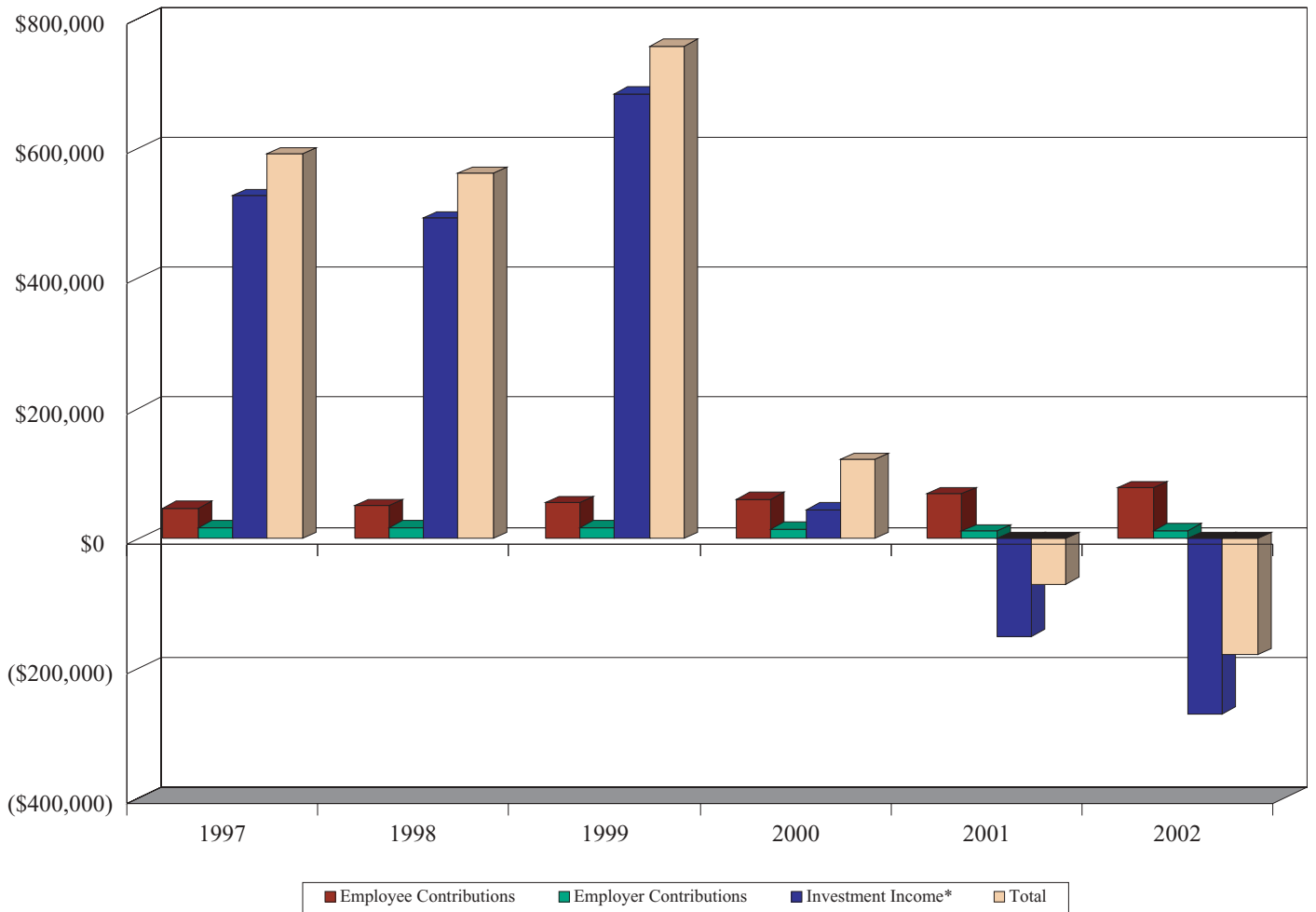


Administration/Human Resources Division

Top row, from left, Tiberina Ugarcovici, Alicia Cavazos, Clara Martiniuc and Michele Guidi. Bottom row, from left, Barbara Hull, Eric Danielsen, and Lisa D’Aiello.

Schedule and Graph of Revenues by Source (in thousands) 1997 - 2002

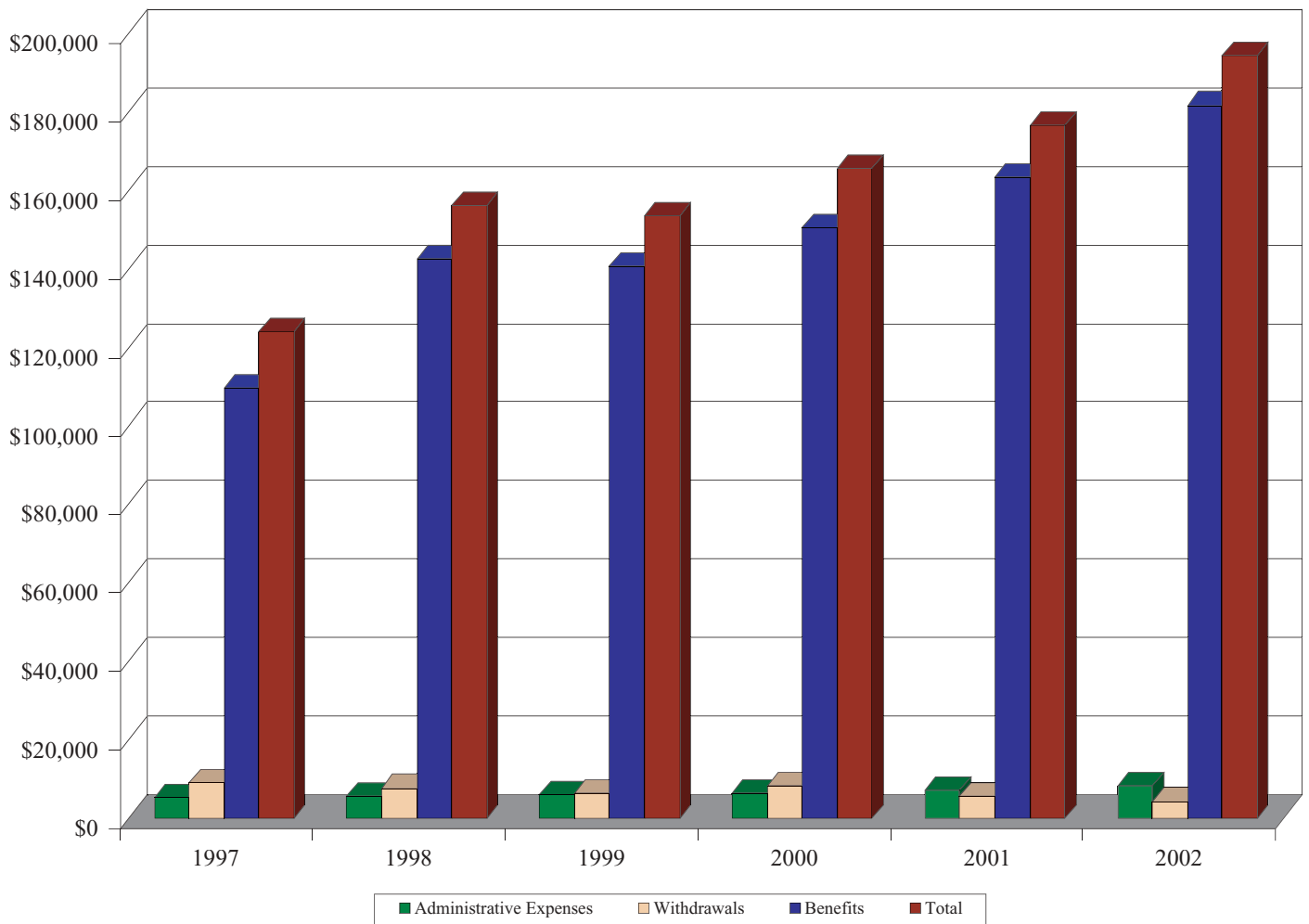
	1997	1998	1999	2000	2001	2002
Employee Contributions	\$47,011	\$50,557	\$55,693	\$61,179	\$68,635	\$77,917
Employer Contributions	\$17,570	\$17,977	\$17,591	\$15,561	\$12,060	\$12,991
Investment Income*	\$527,609	\$493,491	\$685,718	\$45,284	(\$149,858)	(\$268,890)
Total	\$592,190	\$562,025	\$759,002	\$122,024	(\$69,163)	(\$177,982)



* Net of investment manager fees and security lending fees.

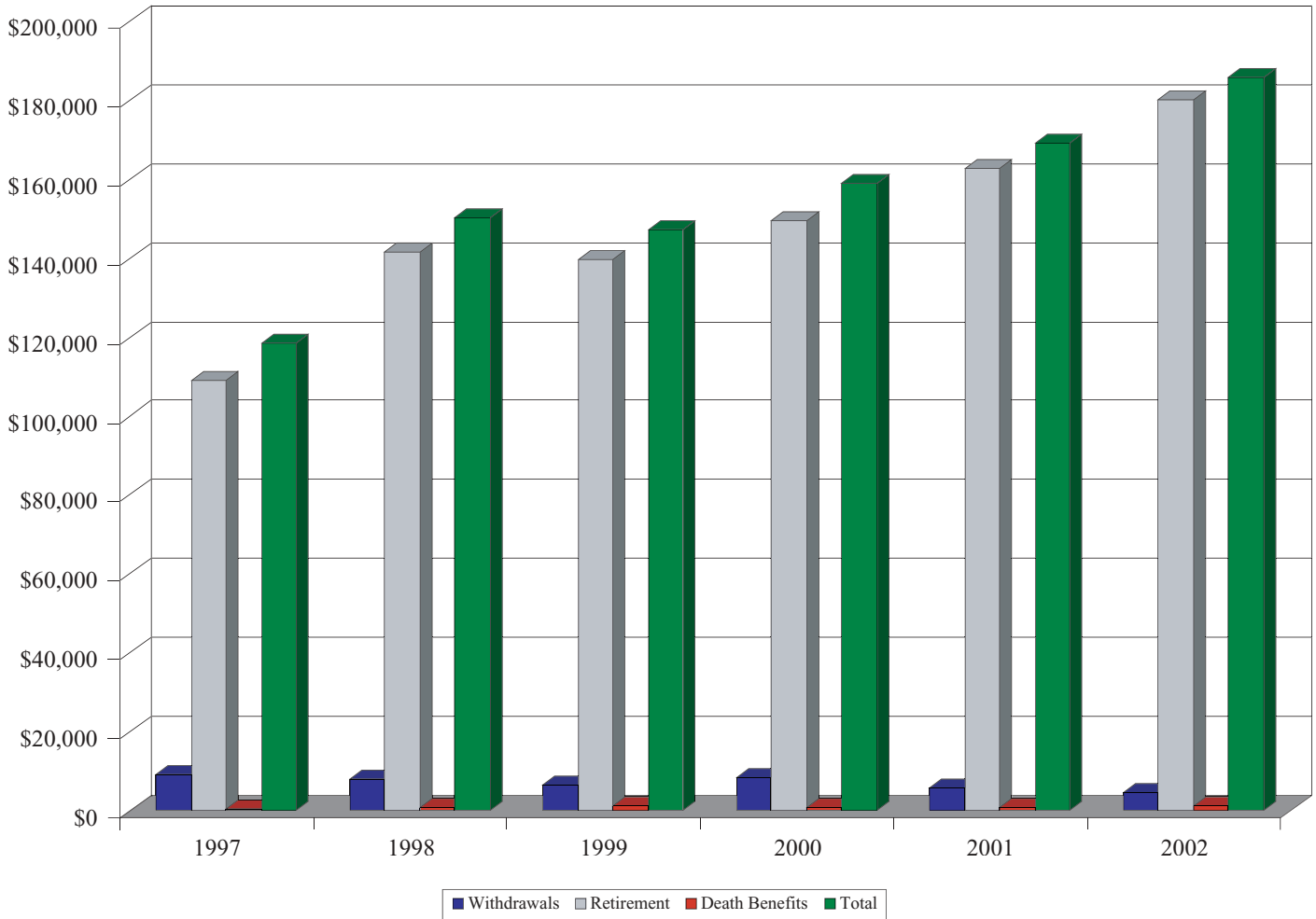
Schedule and Graph of Expenses by Type (in thousands) 1997 - 2002

	1997	1998	1999	2000	2001	2002
Administrative Expenses	\$5,392	\$5,850	\$6,094	\$6,631	\$7,146	\$8,279
Withdrawals	\$9,048	\$7,848	\$6,513	\$8,515	\$5,896	\$4,482
Benefits	\$109,660	\$142,457	\$140,736	\$150,466	\$163,378	\$181,549
Total	\$124,100	\$156,155	\$153,343	\$165,612	\$176,420	\$194,310



Schedule and Graph of Benefit Expenses by Type (in thousands) 1997- 2002

	1997	1998	1999	2000	2001	2002
Withdrawals	\$9,048	\$7,848	\$6,513	\$8,515	\$5,896	\$4,482
Retirement	\$109,206	\$141,629	\$139,611	\$149,555	\$162,732	\$180,263
Death Benefits	\$454	\$828	\$1,125	\$911	\$646	\$1,286
Total	\$118,708	\$150,305	\$147,249	\$158,981	\$169,274	\$186,031



**Orange County Employees Retirement System
Schedule of Participating Employers**

City of San Juan Capistrano (includes Capistrano Valley Water District)

County of Orange

Transportation Corridor Agencies

Orange County Cemetery District

Orange County Employees Retirement System

Orange County Fire Authority

Orange County Law Library

Orange County Transportation Authority

Orange County Vector Control District

Sanitation District of Orange County

Orange County Department of Education (closed to new members)

UCI Medical Center (closed to new members)

Orange County Children and Families Commission

Local Agency Formation Commission

Orange County Superior Court

City of Rancho Santa Margarita (Became member 1/1/2003)

**Orange County Employees Retirement System
Schedule of Retired Members by Type of Benefit
December 31, 2002**

Amount of Monthly Benefit	No. of Retirants	Type of Retirement									Option Selected					Total
		1	2	3	4	5	6	7	8	9	Unmodified	Option 1	Option 2	Option 3	Option 4	
\$1-250	974	280	213	-	5	23	45	36	212	160	943	6	15	5	5	974
\$251-500	1,277	588	219	1	24	49	39	57	239	61	1,239	4	30	4	-	1,277
\$501-750	1,244	750	137	-	53	53	21	51	143	36	1,220	3	20	1	-	1,244
\$751-990	968	624	73	2	88	58	19	22	61	21	948	3	14	3	-	968
\$991-1,250	817	531	33	-	125	42	11	21	40	14	795	4	17	1	-	817
\$1,251-1,500	624	390	31	-	137	10	14	6	22	14	606	6	12	-	-	624
\$1,501-1,750	533	339	23	2	114	14	12	9	11	9	518	1	12	2	-	533
\$1,751-2,000	352	253	12	1	58	5	-	4	8	11	342	2	4	3	1	352
Over \$2,000	1,899	1,562	43	3	236	11	10	9	9	16	1,840	8	40	7	4	1,899
Total	8,688	5,317	784	9	840	265	171	215	745	342	8,451	37	164	26	10	8,688

Definition of Terms:

Eligible Spouse: A member's spouse is considered eligible if the member has been married for at least one year at the time of retirement and remains married throughout the member's retirement.

Eligible Child: An eligible child is an unmarried child under the age of 18, or under the age of 22 if a full-time student.

Type of Retirement:

1. Normal Retirement for age and service.
2. Survivor Payment - normal retirement.
3. Survivor Payment - death in the line of duty.
4. Service Connected Disability Retirement.
5. Non-service Connected Disability Retirement.
6. Survivor Payment - disability retirement.
7. Survivor Payment - active member who died and was eligible to retire.
8. Deferred Regular Retirement
9. Deferred Other Retirement

**Orange County Employees Retirement System
Schedule of Retired Members by Type of Benefit (continued)**

Option Selected

Unmodified Option:

This option provides the member with the maximum allowance available to the member. It also provides a continuation of 60 percent of the member's allowance to the member's eligible spouse or eligible children upon the member's death. If the member retired under the Service Connected Disability status, the continuance percentage is 100 percent instead of the normal 60 percent. If the member does not have an eligible spouse or any eligible child at the time of death, the member's designated beneficiary will receive a refund of the member contributions with interest, less the sum of the monthly allowances paid to the member during the member's lifetime.

Option 1 - Cash Refund Annuity:

This option provides the member with a reduced monthly allowance for the member's lifetime. At the member's death, the member's designated beneficiary will receive the member's remaining contributions, if any.

Option 2 - 100 Percent Joint and Survivor Annuity:

This option provides the member with a reduced monthly allowance for the member's lifetime. At the member's death, the member's designated beneficiary will receive the same monthly allowance for the rest of his or her lifetime.

Option 3 - 50 Percent Joint and Survivor Annuity:

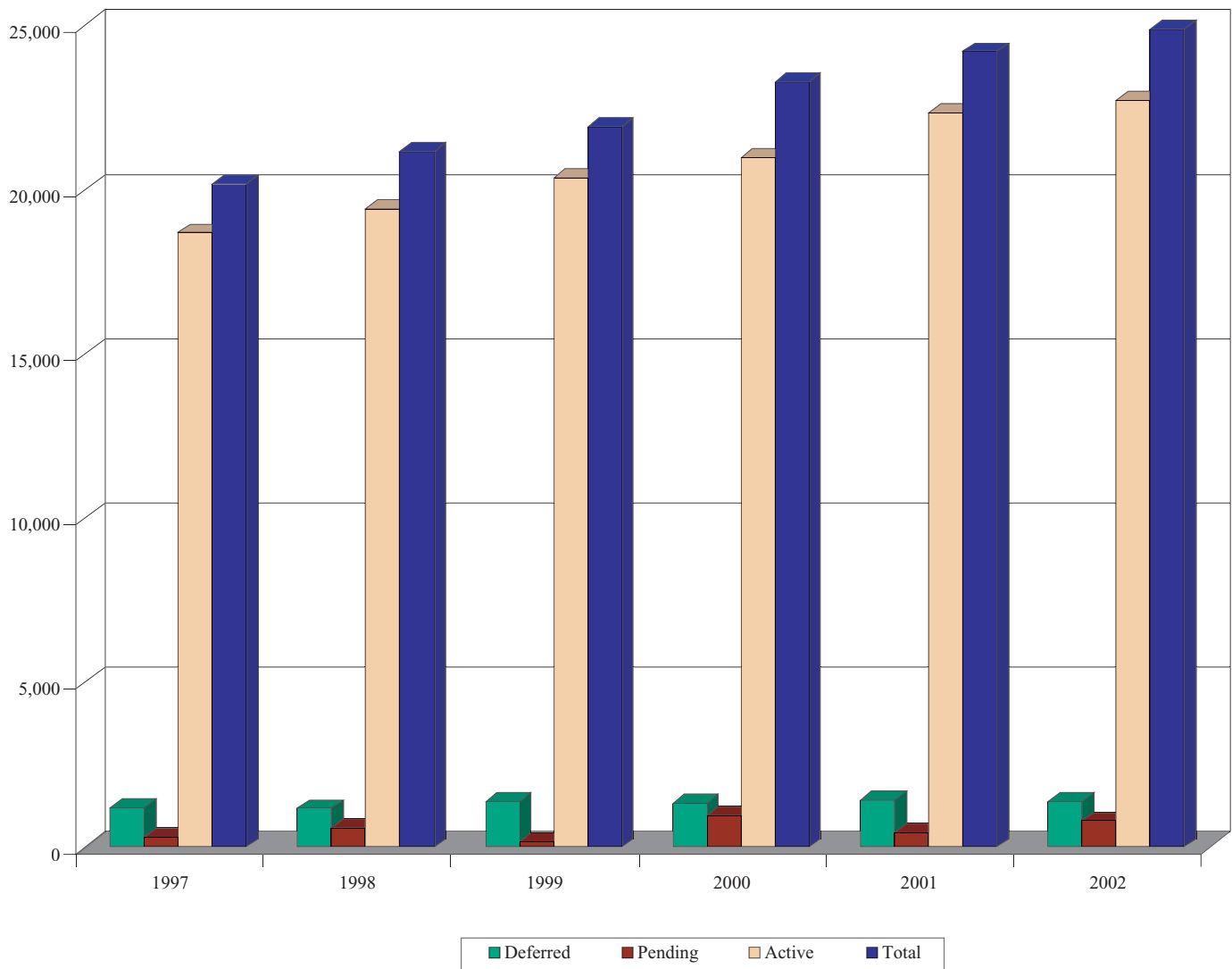
This option provides the member with a reduced monthly allowance for the member's lifetime. At the member's death, the member's designated beneficiary will receive half of the member's monthly allowance for the rest of his or her lifetime.

Option 4 - Other Options:

Other options allow members to designate multiple beneficiaries and other survivor percentages. The member must obtain approval from the Retirement Board.

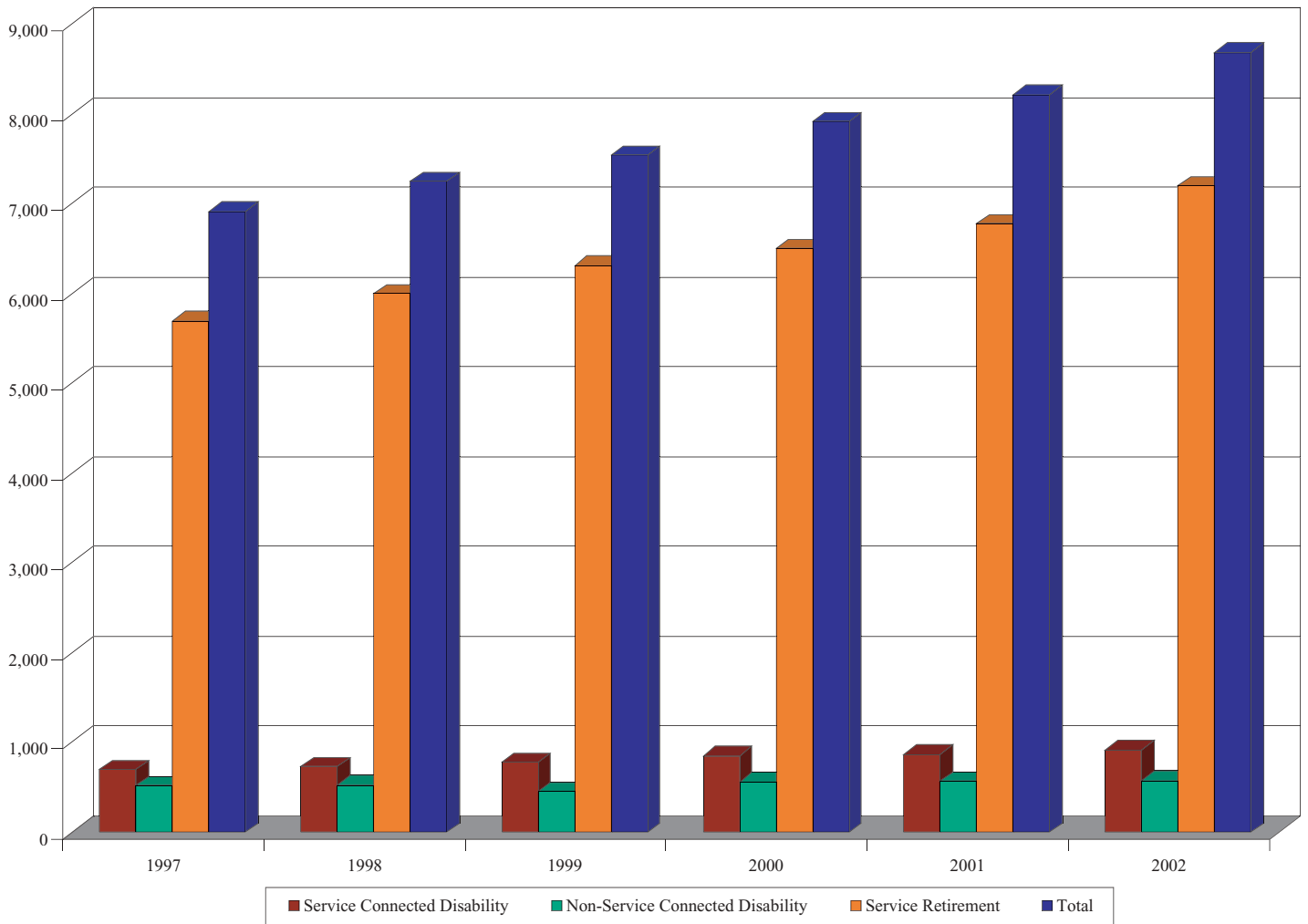
Schedule and Graph of Active, Pending, and Deferred Members 1997 - 2002

	1997	1998	1999	2000	2001	2002
Deferred	1,184	1,179	1,376	1,325	1,418	1,377
Pending	312	571	177	960	454	800
Active	18,693	19,432	20,357	20,987	22,329	22,723
Total	20,189	21,182	21,910	23,272	24,201	24,900



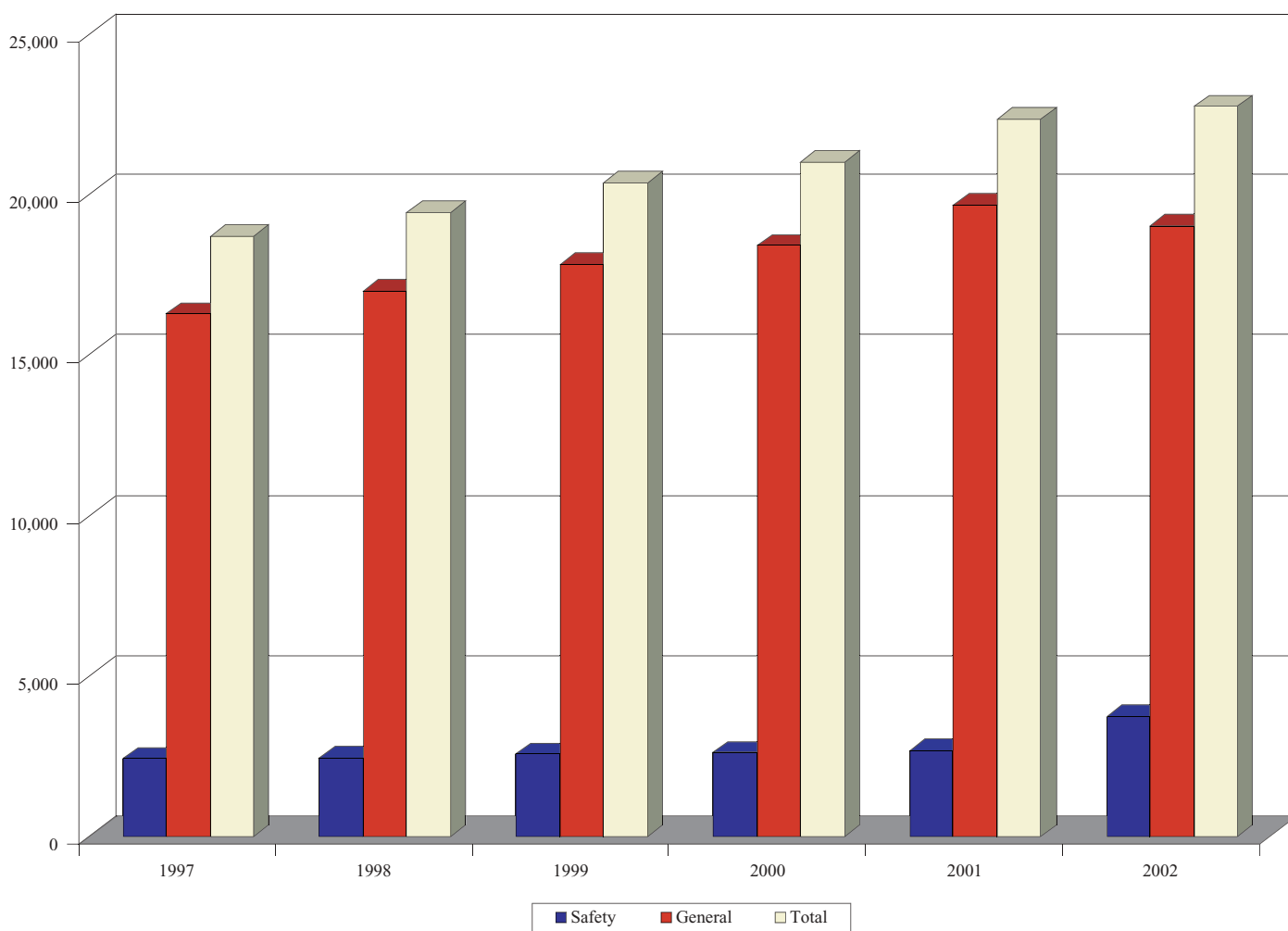
Schedule and Graph of Retired Members 1997 - 2002

	1997	1998	1999	2000	2001	2002
Service Connected Disability	696	729	775	853	868	917
Non-Service Connected Disability	518	524	453	561	570	574
Service Retirement	5,698	5,991	6,309	6,501	6,778	7,197
Total	6,912	7,244	7,537	7,915	8,216	8,688



Schedule and Graph of Active Members by Membership Classification* 1997- 2002

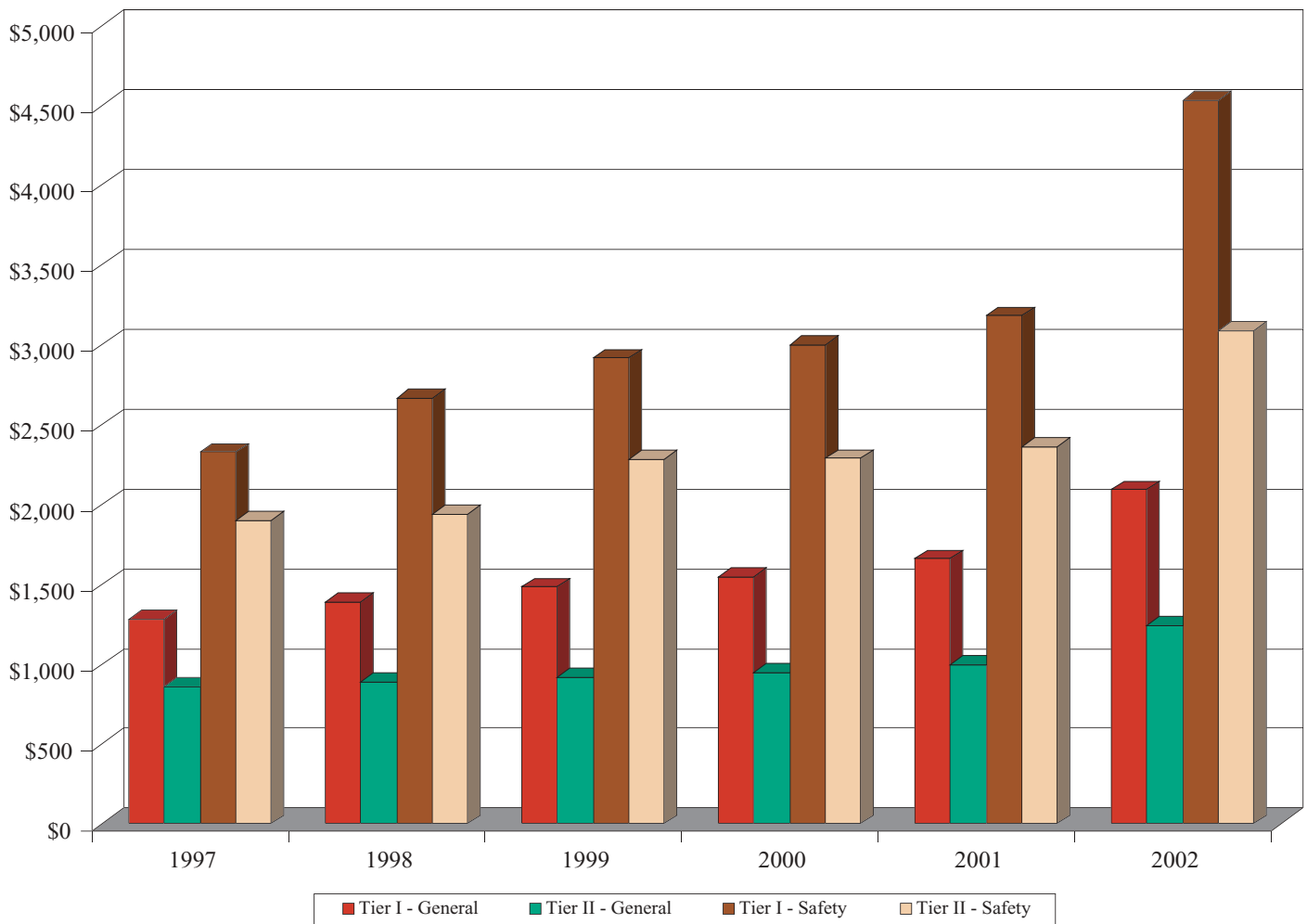
	1997	1998	1999	2000	2001	2002
Safety	2,427	2,456	2,556	2,605	2,676	3,721
General	16,266	16,976	17,801	18,382	19,653	19,002
Total	18,693	19,432	20,357	20,987	22,329	22,723



* Excludes members with Deferred and Pending Status.

Schedule and Graph of Average Monthly Retirement Benefits (by Tier and Membership Classification) 1997- 2002

	1997	1998	1999	2000	2001	2002
Tier I - General	\$1,281	\$1,388	\$1,484	\$1,549	\$1,661	\$2,093
Tier II - General	\$859	\$891	\$919	\$951	\$1,001	\$1,244
Tier I - Safety	\$2,328	\$2,666	\$2,917	\$3,000	\$3,182	\$4,530
Tier II - Safety	\$1,901	\$1,937	\$2,287	\$2,289	\$2,366	\$3,086



**Orange County Employees Retirement System
History of Actuarial Assumption Rates
for the Period January 1945 - December 2002**

The table shown below is a comprehensive history of the interest rate assumption and the salary assumption rates corresponding to the Orange County Employees Retirement System since the inception of the System. These rates are adopted by the Board of Retirement and used by the consulting actuary in the creation of the actuarial valuation of the System.

Specifically, the interest rate assumption estimates the rate at which the funds of the System's investment portfolio will realize earnings over many years into the future. The salary assumption rate estimates the relative increases in the salary of a member from the date of the valuation to the estimated date of separation of the member from active service.

History of OCERS Actuarial Assumption Rates

<u>Effective Date</u>	<u>Interest Rate</u>	<u>Salary Assumption Rate</u>
1/1/45	2.50%	0.00%
7/1/62	3.50%	0.00%
12/31/65	4.00%	0.00%
7/1/69	4.50%	0.00%
6/30/70	5.00%	0.00%
8/31/73	5.75%	0.00%
7/1/75	6.00%	0.00%
7/1/81	7.25%	5.00%
7/1/89	7.50%	5.50%
7/1/91	8.00%	6.00%
7/1/96	8.00%	3.50%
7/1/00	8.00%	5.50%
12/31/02	7.50%	4.50%



RETIREMENT
SYSTEM

ORANGE COUNTY EMPLOYEES RETIREMENT SYSTEM

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