

# Comprehensive Annual Financial Report



*For the year ended December 31, 2002*



**Ohio  
Police  
& Fire** Pension  
Fund



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# *Comprehensive Annual Financial Report*

*For the Year Ended December 31, 2002*



William J. Estabrook, Executive Director  
Arleen Rhodes, Acting Chief Financial Officer

Prepared through the combined efforts of the OP&F staff  
140 E. Town Street, Columbus, Ohio 43215

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# Comprehensive Annual Financial Report

For the Year Ended December 31, 2002

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## Board of Trustees

### Elected Members



**Thomas Bennett**  
*Chairman*  
Dayton Police Department  
Term expires June 1, 2003



**Ken Gehring**  
Toledo Fire Department  
Term expires June 4, 2006



**William Gallagher**  
*Vice Chairman*  
Cleveland Police Department  
(Retired)  
Term expires June 1, 2003



**David Harker**  
Dayton Fire Department  
Term expires June 6, 2004



**Robert Beck**  
Cleveland Police Department  
Term expires June 7, 2005



**Kevin Watts**  
Lancaster Fire Department  
(Retired)  
Term expires June 1, 2003

### Statutory Members



**Richard T. Balazs**  
Director of Finance  
City of Euclid  
As appointed by the  
governor  
Term expires June 30, 2004



**Jim Petro**  
*Auditor of State*



**Betty Montgomery**  
*Attorney General*

## Administrative Staff



**William J. Estabrook**  
*Executive Director*



**Diane M. Lease**  
*General Counsel*



**Theodore G. Hall**  
*Chief Investment Officer*



**Kay Penn**  
*Director of Member Services*



**Robert Hartsook**  
*Director of Health Services*



**Scott Miller**  
*Internal Auditor*



**George Kaitso**  
*Chief Operating Officer*



**Arleen Rhodes**  
*Acting Chief Financial Officer*

## Professional Consultants

### *Actuaries*

Segal Company

### *Independent Accountants*

KPMG LLP

### *Legal Counsel*

Attorney General Betty Montgomery

### *Investment Consultants & Managers*

See page 39



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# Certificate of Achievement for Excellence in Financial Reporting

Presented to

Ohio Police & Fire  
Pension Fund, Ohio

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.



*William Patrick Wozniak*

President

*Jeffrey R. Emen*

Executive Director

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# Letter of Transmittal



140 E. Town Street, Columbus, Ohio 43215

May 15, 2003

Dear Chairman and Members of the Board of Trustees:

We are pleased to submit to you the Comprehensive Annual Financial Report (CAFR) of the Ohio Police and Fire Pension Fund (OP&F) for the year ended December 31, 2002. This CAFR was prepared to aid interested parties in assessing OP&F's status at December 31, 2002, and its results for the year then ended.

The report is divided into five sections:

- (1) The Introductory Section contains this Letter of Transmittal, along with the identification of the administrative organization of OP&F and the Certificate of Achievement for Excellence in Financial Reporting;
- (2) The Financial Section includes the Management's Discussion and Analysis, Independent Auditors' Report and the financial statements of the Fund;
- (3) The Investment Section contains the investment report, portfolio summary, and the investment policy and guidelines;
- (4) The Actuarial Section includes significant actuarial data pertaining to OP&F and the certification letter of The Segal Company and results of their annual actuarial valuation; and
- (5) The Statistical Section includes historical data reporting progress of OP&F.

## Accounting System and Internal Controls

The financial statements were prepared in accordance with accounting principles generally accepted in the United States of America applicable to governmental units, including the pronouncements of the Governmental Accounting Standards Board (GASB). Additional information on OP&F's significant accounting policies are contained in Note 1 of the Notes to Combining Financial Statements in the Financial Section.

Management is responsible for establishing and maintaining an internal control structure designed to ensure that the assets of OP&F are protected from loss, theft or misuse and to ensure that adequate accounting data is compiled to allow for the preparation of combining financial statements in conformity with accounting principles generally accepted in the United States of America. The internal control structure is designed to provide reasonable, but not absolute, assurance that these objectives are met. The concept of reasonable assurance recognizes that: (1) the cost of a control should not exceed the benefits likely to be derived; and (2) the valuation of costs and benefits requires estimates and judgments by management. Management believes its internal control structure meets these objectives.

## Plan History and Overview

OP&F is a cost sharing multiple-employer public employee retirement system and was created by the Ohio General Assembly in 1965, replacing 454 separate local police and firemen's relief and pension funds in Ohio. The statewide Fund began operating January 1, 1967. On that date, the local pension funds transferred their assets and liabilities to OP&F. Assets transferred to OP&F totaled approximately \$75 million, while OP&F's actuary computed the liabilities accrued up to 1966 at approximately \$490 million. The remaining unfunded accrued liability is being paid by employers over a 67-

year period, which began in 1969 and totaled nearly \$38.2 million as of December 31, 2002.

OP&F provides pension, disability and health care benefits to qualified participants, survivor and death benefits and health care benefits to qualified spouses, children and dependent parents. Please refer to the Plan Summary in the Actuarial Section for further information on plan benefits.

Membership in OP&F is mandatory under Ohio law for all full-time police officers employed by Ohio municipalities. Full-time fire fighters employed by townships, municipalities, township joint fire districts or other political subdivisions must become members of OP&F if satisfactory completion of a firefighter training course approved under former Section 3303.07, Section 4765.55 or conducted under Section 3737.33 of the Ohio Revised Code is required for employment. The table below is a tabulation of current participating employers at December 31, 2002:

#### Participating Employers

	<u>Police</u>	<u>Fire</u>
Municipalities	252	219
Townships	-	106
Villages	<u>307</u>	<u>29</u>
<b>Total</b>	<b><u>559</u></b>	<b><u>354</u></b>

#### Major Initiatives and Accomplishments

OP&F continued its project to redesign our member information system and clean up member data. As part of our initiative to implement a new integrated pension administration system, we went through a vigorous competitive bidding process to obtain a vendor who would provide a fully functional system including system implementation and related data conversion services. That system was selected and implementation began in January 2003. It is expected that the implementation will take a minimum of thirty months.

Many months were spent studying our health care costs, which have risen beyond predictions. Our analysis involved reviewing medical trends, forecast studies, the benefit recipient health care contribution schedule, and health care plan designs. The goal is to ensure that the Post-Employment Healthcare Fund remains solvent for 10 years, as required by the Board's Benefit Funding Policy. In order to keep the Post-Employment Healthcare Fund solvent, we anticipate changing the overall plan design, changing eligibility, and increasing premiums paid by the members.

Senate Bill 134, which would allow OP&F to offer a Deferred Retirement Option Plan (DROP) to members, was passed into law at the beginning of 2002. OP&F staff spent most of 2002 planning and programming for DROP so that we would be ready for the first member to enroll in January of 2003. We were successful in meeting our deadlines, and we now have over 1,000 members enrolled.

#### Financial Overview

OP&F receives virtually all of its funds from the following sources: member contributions, employer contributions, retiree medical benefit contributions, state subsidies and reimbursements, and investment earnings. Additions to net assets totaled (\$350,522,341) in 2002. The employee and employer contribution rates during 2002 remained unchanged from the prior year at 10% for employees, 19.5% for police employers and 24% for fire employers.

<b>Additions to Plan Net Assets</b> (in thousands)	<b>2002</b> <u>Amount</u>	<b>2001</b> <u>Amount</u>
Net Investment Income (loss)	\$ (870,448)	\$ (443,461)
Contributions	504,214	472,423
Interest on Local Funds Receivable	1,633	1,873
Other	14,079	5,098
<b>Total</b>	<b><u>\$ (350,522)</u></b>	<b><u>\$ 35,933</u></b>

Investment loss increased due to the continued decline in global equity markets in 2002.

<b>Deductions to Plan Net Assets</b> (in thousands)	<b>2002</b>		<b>2001</b>	
	<u>Amount</u>	<u>Percent</u>	<u>Amount</u>	<u>Percent</u>
Benefits	\$ 677,586	95%	\$ 621,572	92%
Administrative Expenses	14,887	2	13,122	2
Discount on Early Payoff of Receivables	0	0	3,721	4
Refund of Employee Contributions	16,838	3	10,438	2
Other	<u>1,015</u>	<u>0</u>	<u>1,051</u>	<u>0</u>
<b>Total</b>	<b>\$ 710,326</b>	<b>100%</b>	<b>\$ 649,904</b>	<b>100%</b>

The early payoff program of employer pre-1967 liabilities expired in early 2001. Included in benefits expense are health care costs which increased 18.8%, largely due to the rising costs of prescription drugs.

### Funding Practices and Actuarial Overview

Funds are derived from the excess of additions over deductions, and are accumulated by OP&F in order to meet current and future benefit obligations to retirees and beneficiaries. Due to unrealized losses in the investment portfolio, OP&F experienced a net decrease plan net assets in 2002, reducing net assets by approximately \$1.061 billion. Health care currently operates on a pay-as-you-go basis with a minimal amount of reserves being held to operate the program.

### Investment Policy

OP&F invests all available funds in order to maximize both current income yield and long-term appreciation.

The primary objective of OP&F's investment policy is to assure that OP&F meets its responsibilities for providing retirement and other benefits. The portfolio is diversified to provide adequate cash flow and to provide the highest possible total return on OP&F's assets with the least exposure to risk. OP&F's total rate of return on its investment portfolio decreased significantly due to the declining stock market, with a return of (9.9)% in 2002, (3.88%) in 2001, and (1.1%) in 2000.

Details of portfolio composition, rates of return, analysis of significant economic conditions, and additional information concerning OP&F's investment policy are provided in the Investment Section.

### Material Plan Amendments

There were no material plan amendments in 2002, though some assumptions were changed based on the most recent experience study. See the "Actuarial Section" for the assumption changes.

### Independent Audit

KPMG LLP, independent certified public accountants, audited the financial statements of OP&F for the year ended December 31, 2002, and their opinion thereon is included in the "Financial Section."

### Notes to Combining Financial Statements

The notes to combining financial statements, which follow the combining financial statements, contain additional information and are an integral part of such statements.

### 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 OP&F for its Comprehensive Annual Financial Report for the fiscal year ended December 31, 2001. The Certificate of Achievement is the highest form of recognition for excellence in state and local government financial reporting.

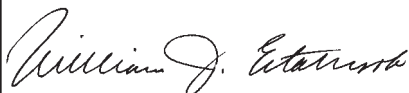
In order to be awarded a Certificate of Achievement, a government unit must publish an easily readable and efficiently organized Comprehensive Annual Financial Report, whose contents conform to program standards. Such reports must satisfy both accounting principles generally accepted in the United States 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 the GFOA to determine its eligibility for another certificate.

### **Acknowledgments**

The preparation of this report reflects the combined efforts of OP&F's staff under the direction of the Board of Trustees. It is intended to provide complete and reliable information as a basis for making management decisions, to disclose compliance with legal provisions, and as a means of determining responsible stewardship for the assets contributed by the members and their employers.

The cooperation of OP&F's employers is also very important to our success and is greatly appreciated.

Respectfully submitted,



William J. Estabrook  
Executive Director



Arleen Rhodes  
Acting Chief Financial Officer



## *Financial Section*

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### **Independent Auditors' Report**

### **Management's Discussion and Analysis**

### **Basic Financial Statements**

Statements of Plan Net Assets

Statements of Changes in Plan Net Assets

Notes to Financial Statements

### **Required Supplementary Information**

1. Schedule of Funding Progress
2. Schedule of Contributions from Employers and Other Contributing Entities
3. Notes to the Required Supplementary Schedules

### **Additional Information**

Schedule of Administrative Expenses

Schedule of Investment Expenses

## Independent Auditors' Report



191 West Nationwide Boulevard  
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Columbus, OH 43215-2568

Telephone 614 249 2300  
Fax 614 249 2348

### Independent Auditors' Report

To the Board of Trustees of Ohio  
Police and Fire Pension Fund:

We have audited the accompanying statements of plan net assets of Ohio Police and Fire Pension Fund (OP&F) as of December 31, 2002 and 2001, and the related statements of changes in plan net assets for the years then ended. These financial statements are the responsibility of OP&F's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the plan net assets of OP&F as of 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.

As described in Note 1, OP&F has implemented GASB Statement No. 34, *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments*; GASB Statement No. 37, *Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments: Omnibus*; and GASB Statement No. 38, *Certain Financial Statement Note Disclosures* effective January 1, 2001.

In accordance with *Government Auditing Standards*, we have also issued a report dated May 9, 2003, on our consideration of OP&F's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts and grants. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audit.

The management's discussion and analysis on pages 14 through 16 and the schedules of funding progress and contributions from employers and other contributing entities on page 28 are not a required part of the basic financial statements, but are supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation, over the supplementary information. However, we did not audit the information and express no opinion on it.

Our audit was conducted for the purpose of forming an opinion on the financial statements of OP&F. The information in the introductory, investment, actuarial, and statistical sections, as listed in the table of contents, are presented for the purpose of additional analysis and are not a required part of the basic financial statements. The schedule of administrative expenses and schedule of investment expenses have been subjected to the auditing procedures applied in our audit of the basic financial statements and, in our opinion, are fairly stated in all material respects in relation to the basic financial statements taken as a whole. The introductory, investment, actuarial, and statistical sections have not been subjected to the auditing procedures applied in the audit of the basic financial statements and, accordingly, we express no opinion on them.

**KPMG LLP**

May 9, 2003



KPMG LLP, KPMG LLP, a U.S. limited liability partnership, is  
a member of KPMG International, a Swiss association.



## Management's Discussion and Analysis

This management's discussion and analysis (MD&A) of the Ohio Police & Fire Pension Fund's (OP&F) financial performance provides a narrative overview of financial activities for the fiscal year ended December 31, 2002 and 2001. The MD&A is designed to focus on the years' activities, resulting changes and currently known facts expected to have a financial impact on OP&F. We encourage you to read it in conjunction with OP&F's financial statements, notes to the financial statements, and the letter of transmittal included in the Introductory section of OP&F's Comprehensive Annual Financial Report.

### Financial Highlights

#### 2002

Contributions and investment loss for fiscal year 2002 netted (\$350,522,341). This amount includes realized and unrealized investment gains and losses. The employee and employer contribution rates during 2002 remained unchanged from the prior year. Employee contributions are 10% for all members, while employer contributions are 19.5% and 24% for police and fire employers, respectively. Most of the net loss for the year is due to the continued poor performance of the equity markets. The fair value of our investment portfolio decreased by over a billion dollars in 2002. OP&F has a long-term outlook, so we are continuing with our current asset mix.

Expenses are incurred primarily for the purpose for which OP&F was created, the payment of benefits. Included in the deductions from plan net assets for 2002 were retirement, disability, healthcare, and survivor benefits. Also included were contribution refunds and administrative expenses. Pension benefits are funded through a combination of employee and employer contributions and investment income. Healthcare expenses are funded on a pay-as-you-go basis through a portion of employer contributions, member premiums, and investment income. Deductions totaled \$710,325,881 in 2002, which is a 9% increase from the prior year.

#### 2001

Contributions and investment loss netted a gain of \$35,932,755 in 2001. Our steady income stream from contributions were reduced by the investment loss of (\$443,461,307). 2001 was another year of poor equity performance.

2001 expenses consisted of the same type of items as described in 2002. Total 2001 expenses increased by 4.6%. This net increase is the result of rising healthcare costs offset by the completion of our discount on the early payoff of the local fund receivable program.

### Overview of Financial Statements

Following the MD&A are the Statements of Plan Net Assets and the Statements of Changes in Plan Net Assets. OP&F's financial statements are prepared using the accrual basis of accounting and applicable Governmental Accounting Standards Board Statements.

The two basic financial statements of OP&F are the Statement of Plan Net Assets and the Statement of Changes in Plan Net Assets. Statements are shown for the most recent and previous fiscal years for comparison and analysis of changes in individual line items. The statements are prepared in the conformity with accounting principles generally accepted in the United States of America.

The Statement of Plan Net Assets is a measure of OP&F's assets and liabilities at the close of the fiscal year. Total assets less liabilities equal net assets held in trust for future benefits.

The Statement of Changes in Plan Net Assets shows revenues (additions) and expenses (deductions) for the years. The net increase (or decrease) is the change in net assets available for benefits since the end of the previous fiscal year.

A Schedule of Funding Progress and a Schedule of Employer Contributions are included as a required supplementary information. These schedules emphasize the long-term nature of pension plans and show progress of OP&F in accumulating sufficient assets to pay benefits when due.



The Schedule of Funding Progress shows actuarial trend information for the past six years. It includes the ratio of valuation assets to actuarial accrued liability (funded ratio). The funded ratio increases or decreases over time dependent upon the relationships between contributions, investment performance, benefit changes and actuarial assumption change based upon participant information and characteristics. The Schedule of Funding Progress also shows the unfunded actuarial accrued liability as a percentage of member payroll. This schedule shows the relationship between the funding status of the plan and the growth of payroll.

The Schedule of Employer Contributions shows the amount of required employer contributions determined in accordance with parameters established by Governmental Accounting Standards Board Statement No. 25 and the percentage actually contributed.

### CONDENSED PLAN NET ASSET INFORMATION

(in thousands)	2002	2001	2000	2002 Change		2001 Change	
				Amount	Percent	Amount	Percent
Cash and Short-Term Invest.	\$ 419,159	\$ 331,903	355,121	\$ 87,256	26.2%	(\$ 23,218)	(6.5%)
Receivables	193,810	208,340	231,047	(14,530)	(6.9)	(22,707)	(9.8)
Investments	7,196,112	8,210,810	8,708,528	(1,014,698)	(12.3)	(497,718)	(5.7)
Capital Assets, net	24,641	22,077	20,054	2,564	11.6	2,023	10.1
Other Assets	<u>415</u>	<u>803</u>	<u>1,129</u>	<u>(388)</u>	<u>(48.3)</u>	<u>(326)</u>	<u>(28.9)</u>
Total Assets	7,834,137	8,773,933	9,315,879	(939,796)	(10.7)	(541,946)	(5.8)
Benefits and Accounts Payable	48,819	40,209	37,300	8,610	21.4	2,909	7.8
Investments Payable	<u>344,246</u>	<u>231,804</u>	<u>162,687</u>	<u>112,442</u>	<u>48.5</u>	<u>69,117</u>	<u>42.5</u>
Total Liabilities	393,065	272,013	199,987	121,052	44.5	72,026	36.0
<b>Net Assets Available</b>	<b><u>7,441,072</u></b>	<b><u>8,501,920</u></b>	<b><u>9,115,892</u></b>	<b><u>(1,060,848)</u></b>	<b><u>(12.4)</u></b>	<b><u>(613,972)</u></b>	<b><u>(6.7)</u></b>

### CONDENSED CHANGES IN PLAN NET ASSET INFORMATION

(in thousands)	2002	2001	2000	2002 Change		2001 Change	
				Amount	Percent	Amount	Percent
Contributions	\$ 504,214	\$ 472,423	458,627	\$ 31,791	6.7%	\$ 13,796	3.0%
Net Investment Loss	(870,448)	(443,461)	(165,141)	(426,987)	(96.2)	(278,320)	(169.5)
Other	<u>15,712</u>	<u>6,971</u>	<u>7,735</u>	<u>8,741</u>	<u>125.3</u>	<u>(764)</u>	<u>(9.9)</u>
Total Additions	(350,522)	35,933	301,221	(386,455)	(1075.4)	(265,288)	(88.1)
Benefits	677,586	621,572	573,783	56,014	9.0	47,789	8.3
Refunds	16,838	10,439	11,070	6,399	61.3	(631)	(5.7)
Discount on Early Payoff	0	3,721	22,322	(3,721)	-	(18,601)	(83.3)
Administration and other	<u>15,902</u>	<u>14,173</u>	<u>13,938</u>	<u>1,729</u>	<u>12.1</u>	<u>235</u>	<u>1.7</u>
Total Deductions	710,326	649,905	621,113	60,421	9.2	28,792	4.6
<b>Net Decrease</b>	<b><u>(1,060,848)</u></b>	<b><u>(613,972)</u></b>	<b><u>(319,892)</u></b>	<b><u>(446,876)</u></b>	<b><u>(72.7)</u></b>	<b><u>(294,080)</u></b>	<b><u>(91.9)</u></b>
<b>Net Assets, beginning of year</b>	<b><u>8,501,920</u></b>	<b><u>9,115,892</u></b>	<b><u>9,435,784</u></b>				
<b>Net Assets, end of year</b>	<b><u>7,441,072</u></b>	<b><u>8,501,920</u></b>	<b><u>9,115,892</u></b>				

## Financial Analysis

### 2002

Additions - Contributions from employees and employers increased \$26.1 million or 5.3% in 2002 because of growth in the number of active members and average annual salary. The active member population increased by 392 to 28,328.

Contributions paid by members and beneficiaries for their share of the health care costs increased \$5.7 million or 83.6% in 2002. Because of the rising costs of health care, including prescription drugs, OP&F increased the rates charged to its members for health care. In 2002, members contributed premiums which covered 12% of their health care costs. In 2001, the members paid 6% of the costs.

Net investment loss increased significantly as the U.S. stock market continued its downward trend. Included in the net investment loss is \$145.6 million in bond interest and \$529.4 million in foreign securities income.

Deductions - Health care expenses took another double-digit increase in 2002. \$24.4 million of the increase in benefits related to health care benefits, which represents an 18.8% increase over 2001. This trend mirrors that of health care costs nationally.

Benefit payments for retirement, disability and survivors increased \$31.5 million or 6% in 2002. This increase is attributed to the increase in retirees and beneficiaries by 543 or 2.3% plus a 3% cost of living adjustment.

Refunds to members increased \$6.4 million in 2002. Though actual refunds paid only increased slightly in 2002, the number of non-vested members leaving employment resulting in them becoming inactive has increased significantly during the last 2-3 years. OP&F accrues a liability for the accumulated contributions on deposit for these members, as these contributions will not be refunded until a request for refund is made.

The discount on early payoff on our local funds receivable program ended in 2001. Employers could pay off their liability to OP&F at a discount if payment was made in full by certain deadlines. The last date to take advantage of this program was in May 2001.

Net assets decreased by \$1.06 billion in 2002, mainly due to the poor performing U.S. Equity Markets.

Included in the 2002 investment commitments payable are \$135.8 million in mortgage notes payable associated with our real-estate holdings. This is comparable to the mortgage note payable in 2001.

### 2001

Additions - Contributions from employees and employers increased \$12.7 million or about 3% in 2001 because the growth in the number of active members and average annual salary.

Net investment loss increased in 2001 due to the U.S. equity market's poor performance. Included in the net loss is \$143.8 million in bond interest.

Deductions - Health care expenses increased double-digits in 2001 as well. \$17.3 million of the increase in benefits related to health care benefits, which represents a 15.3% increase over 2000.

Benefit payments for retirement, disability, and survivors increased \$30,432,425 or about 7% in 2001. The increase is due to 430 more retirees and beneficiaries in 2001 plus a 3% cost of living adjustment.

The discount on early payoff of the local Fund receivables decreased by \$18.6 million due to the program ending early in 2001. Most of the early payoff discounts were taken in 2000.

Net assets decreased by approximately \$614 million in 2001. This decrease was also due to the poor performing U.S. Equity Markets.

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## Combining Statements of Plan Net Assets as of December 31, 2002 and 2001

### 2002

	Pensions	Postemployment Healthcare	Death Benefit Fund	2002 Total
<i>Assets:</i>				
Cash and Short-term Investments	\$ 394,014,091	\$ 10,619,850	\$ 14,524,899	\$ 419,158,840
<i>Receivables:</i>				
Employers' Contributions	54,899,392	30,086,258		84,985,650
Employees' Contributions	13,218,708			13,218,708
Accrued Investment Income	31,550,538	850,381		32,400,919
Investment Sales Proceeds	24,311,538	655,268		24,966,806
Local Funds Receivable	38,237,439			38,237,439
<b>TOTAL RECEIVABLES</b>	<b>162,217,615</b>	<b>31,591,907</b>		<b>193,809,522</b>
<i>Investments, at fair value:</i>				
Bonds	1,035,130,100	27,899,830		1,063,029,930
Mortgage & Asset Backed Securities	778,750,771	20,989,646		799,740,417
Stocks	3,141,082,280	84,661,495		3,225,743,775
Real Estate	595,142,720	16,040,864		611,183,584
Commercial Mortgage Funds	117,338,544	3,162,622		120,501,166
Private Equity	91,737,796	2,472,606		94,210,402
International Securities	1,248,064,009	33,639,031		1,281,703,040
<b>TOTAL INVESTMENTS</b>	<b>7,007,246,220</b>	<b>188,866,094</b>		<b>7,196,112,314</b>
Collateral on Loaned Securities	1,149,670,663	30,987,039		1,180,657,702
<i>Capital Assets:</i>				
Building, Furniture and Equipment	29,737,531	801,515		30,539,046
Accumulated Depreciation	(5,742,896)	(154,788)		(5,897,684)
Total Capital Assets	23,994,635	646,727		24,641,362
<i>Prepaid Expenses and Other:</i>				
	404,117	10,892		415,009
<b>TOTAL ASSETS</b>	<b>8,737,547,341</b>	<b>262,722,509</b>	<b>14,524,899</b>	<b>9,014,794,749</b>
<i>Liabilities:</i>				
Medical Benefits Payable		16,754,185		16,754,185
Investment Commitments Payable	335,210,696	9,034,924		344,245,620
Accrued Administrative Expenses	6,345,484	171,030		6,516,514
Liabilities for Death Benefit Fund Benefits			14,524,899	14,524,899
Other Liabilities	10,734,198	289,318		11,023,516
Obligations Under Securities Lending	1,149,670,663	30,987,039		1,180,657,702
<b>TOTAL LIABILITIES</b>	<b>1,501,961,041</b>	<b>57,236,496</b>	<b>14,524,899</b>	<b>1,573,722,436</b>
<b>Net assets held in trust for pension and postemployment healthcare benefits</b>	<b>\$7,235,586,300</b>	<b>\$205,486,013</b>	<b>-</b>	<b>\$7,441,072,313</b>

(An unaudited schedule of funding progress is presented on page 28.)

See Notes to Financial Statements

## 2001

Pensions	Postemployment Healthcare	Death Benefit Fund	2001 Total
\$ 309,416,673	\$ 8,845,921	\$ 13,640,695	\$ 331,903,289
57,064,635	30,628,683		87,693,318
12,792,191			12,792,191
34,913,551	998,144		35,911,695
32,209,906	920,850		33,130,756
38,811,522			38,811,522
<b>175,791,805</b>	<b>32,547,677</b>		<b>208,339,482</b>
1,201,503,557	34,349,816		1,235,853,373
782,103,508	22,359,577		804,463,085
3,837,667,827	109,715,185		3,947,383,012
563,152,428	16,099,978		579,252,406
123,995,545	3,544,912		127,540,457
73,515,448	2,101,735		75,617,183
1,400,657,196	40,043,426		1,440,700,622
<b>7,982,595,509</b>	<b>288,214,629</b>		<b>8,210,810,138</b>
1,062,448,486	30,374,367		1,092,822,853
26,146,521	747,504		26,894,025
(4,683,184)	(133,888)		(4,817,072)
21,463,337	613,616		22,076,953
781,108	22,331		803,439
<b>9,552,496,918</b>	<b>300,618,541</b>	<b>13,640,695</b>	<b>9,866,756,154</b>
	12,834,603		12,834,603
225,361,186	6,442,857		231,804,043
7,030,776	201,004		7,231,780
		13,640,695	13,640,695
6,320,936	180,709		6,501,645
1,062,448,486	30,374,367		1,092,822,853
<b>1,301,161,384</b>	<b>50,033,540</b>	<b>13,640,695</b>	<b>1,364,835,619</b>
<b>\$ 8,251,335,534</b>	<b>\$ 250,585,001</b>	<b>-</b>	<b>\$ 8,501,920,535</b>

# Statements of Changes in Plan Net Assets

For the years ended December 31, 2002 and 2001

## 2002

	Pensions	Postemployment Healthcare	2002 Total
<i>Additions:</i>			
Contributions:			
Members'	\$ 167,137,216		\$ 167,137,216
Employers'	203,212,482	\$ 118,459,642	321,672,124
State of Ohio - Subsidies	2,780,378		2,780,378
Medical Benefits		<u>12,623,875</u>	<u>12,623,875</u>
Total Contributions	373,130,076	131,083,517	504,213,593
<i>Investment Income:</i>			
Net Depreciation			
of Fair Value of Investments	(1,567,167,396)	(42,621,006)	(1,609,788,402)
Bond Interest	141,784,564	3,856,002	145,640,566
Dividends	28,801,907	783,303	29,585,210
Real Estate Operating Income, net	43,783,624	1,190,748	44,974,372
Foreign Securities	515,413,639	14,017,295	529,430,934
Other	6,410,299	174,336	6,584,635
Less Investment Expenses	<u>(18,939,352)</u>	<u>(515,078)</u>	<u>(19,454,430)</u>
Net Investment Loss	(849,912,715)	(23,114,400)	(873,027,115)
From Securities Lending Activities:			
Securities Lending Income	22,315,727	606,903	22,922,630
Securities Lending Expense:			
Borrower Rebates	(18,729,088)	(509,360)	(19,238,448)
Management Fees	<u>(1,075,615)</u>	<u>(29,253)</u>	<u>(1,104,868)</u>
Total Securities Lending Expense	<u>(19,804,703)</u>	<u>(538,613)</u>	<u>(20,343,316)</u>
Net Income from Securities Lending	2,511,024	68,290	2,579,314
Interest on Local Funds Receivable	1,633,254		1,633,254
Other Income	<u>11,316,623</u>	<u>2,761,990</u>	<u>14,078,613</u>
<b>TOTAL ADDITIONS</b>	<b>(461,321,738)</b>	<b>110,799,397</b>	<b>(350,522,341)</b>
<i>Deductions:</i>			
Benefits:			
Retirement	335,997,524		335,997,524
Disability	137,566,788		137,566,788
Health Care		153,651,881	153,651,881
Survivor	50,369,762		50,369,762
Contribution Refunds	16,838,054		16,838,054
Discount on Early Payoff of Receivable			
Administrative Expenses	12,640,585	2,246,504	14,887,089
Other Expenses	<u>1,014,783</u>		<u>1,014,783</u>
<b>TOTAL DEDUCTIONS</b>	<b>554,427,496</b>	<b>155,898,385</b>	<b>710,325,881</b>
Net Decrease	(1,015,749,234)	(45,098,988)	(1,060,848,222)
Net assets held in trust for pension and postemployment healthcare benefits:			
Balance, Beginning of year	8,251,335,534	250,585,001	8,501,920,535
Balance, End of year	<u>\$ 7,235,586,300</u>	<u>\$ 205,486,013</u>	<u>\$ 7,441,072,313</u>

See Notes to Financial Statements

## 2001

Pensions	Postemployment Healthcare	2001 Total
\$ 150,531,967		\$ 150,531,967
203,048,580	\$ 109,036,669	312,085,249
2,931,250		2,931,250
<u>356,511,797</u>	<u>6,874,699</u>	<u>6,874,699</u>
	115,911,368	472,423,165
(652,898,420)	(15,704,826)	(668,603,246)
140,382,647	3,376,766	143,759,413
31,037,797	746,583	31,784,380
41,135,814	989,481	42,125,295
10,300,463	247,767	10,548,230
12,008,969	288,864	12,297,833
<u>(17,509,910)</u>	<u>(421,183)</u>	<u>(17,931,093)</u>
(435,542,640)	(10,476,548)	(446,019,188)
43,397,534	1,043,885	44,441,419
(40,042,773)	(963,189)	(41,005,962)
(856,963)	(20,613)	(877,576)
<u>(40,899,736)</u>	<u>(983,802)</u>	<u>(41,883,538)</u>
2,497,798	60,083	2,557,881
1,872,544		1,872,544
4,452,820	645,533	5,098,353
<b>(70,207,681)</b>	<b>106,140,436</b>	<b>35,932,755</b>
319,641,712		319,641,712
125,003,758		125,003,758
	129,173,470	129,173,470
47,753,173		47,753,173
10,438,362		10,438,362
3,721,025		3,721,025
10,007,576	3,114,771	13,122,347
1,050,563		1,050,563
<u>517,616,169</u>	<u>132,288,241</u>	<u>649,904,410</u>
(587,823,850)	(26,147,805)	(613,971,655)
8,839,159,384	276,732,806	9,115,892,190
<b><u>\$ 8,251,335,534</u></b>	<b><u>\$ 250,585,001</u></b>	<b><u>\$ 8,501,920,535</u></b>

## Notes to Financial Statements

December 31, 2002 and 2001

### 1. Summary of Significant Accounting Policies

The following are the significant accounting policies followed by the Ohio Police & Fire Pension Fund (OP&F), formerly known as the Police & Firemen's Disability and Pension Fund of Ohio.

**Basis of Accounting**—OP&F's financial statements have been prepared using the accrual basis of accounting. Revenues are recognized when earned and expenses are recorded when a liability is incurred.

During the year ended December 31, 2002, OP&F adopted the provisions of Governmental Accounting Standards Board Statement No. 34, Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments and Statement No. 37, Basic Financial Statements and Management's Discussion and Analysis for State and Local Governments: Omnibus, effective January 1, 2001. These Statements required the presentation of management's discussion and analysis which is presented on pages 14 through 16.

During the year ended December 31, 2002, OP&F adopted the provisions of Governmental Accounting Standards Board Statement No. 38, Certain Financial Statement Note Disclosure, effective January 1, 2001. This Statement modifies, establishes and rescinds certain financial statement note disclosures. The financial statements have been prepared in accordance with this Statement.

**Investments**—Investment purchases and sales are recorded on a trade date basis. Dividend income is recognized on the ex-dividend date, while interest and rental income is recognized when earned.

Investments are reported at fair value. Short-term investments are valued at cost, which approximates fair value. Securities traded on a national or international exchange are valued at the last reported sales price at current exchange rates. Mortgages are valued on the basis of future principal payments discounted at prevailing interest rates for similar instruments. The fair value of real estate is based on independent appraisals and internal valuations. Investments that do not have an established market are reported at estimated fair value. Private equity limited partnership interest is based on values established by valuation committees.

Net appreciation is determined by calculating the change in the

fair value of investments between the end of the year and the beginning of the year, less the cost of investments purchased, plus sales of investments at fair value. Investment expense consists of administrative expenses directly related to the OP&F's investment operations and a proportional amount of all other administrative expenses allocated based on the ratio of OP&F's investment staff to total OP&F staff.

OP&F has no individual investment that exceeds 5% of net assets available for benefits.

**Federal Income Tax Status**—OP&F was determined to be exempt from Federal income taxes under Section 501(a) of the Internal Revenue Code.

**Property and Equipment**—Property and equipment are recorded at cost. Depreciation is computed using the straight-line method over the estimated useful lives of the related assets. The range of estimated useful lives is as follows:

Buildings	40 years
Furniture, fixtures, equipment and software	3 to 10 years

**Contributions and Benefits**—Member and employer contributions are recorded in the period the related member salaries are earned. Benefits and refunds are recognized when due and payable in accordance with the terms of the plan.



## 2. Description of the System

**Organization**—The Ohio Police & Fire Pension Fund (OP&F) is a cost-sharing multiple-employer public employee retirement system established by Chapter 742 of the Ohio Revised Code (ORC) in 1967 to consolidate the various individual local police and firemen's relief and pension funds into one statewide plan. OP&F is administered by a nine member Board of Trustees, consisting of four active members, two retired members, two ex-officio members (the State Auditor and Attorney General) and a municipal finance officer appointed by the Governor. OP&F administers pension, disability and health care benefits to qualified participants, and survivor, death and health care benefits to qualified spouses, children and dependent parents. OP&F is a separate financial reporting

entity in accordance with criteria established by Governmental Accounting Standards Board Statement No. 14 because it is legally separate, a voting majority of the governing board is not appointed by the State, and it is fiscally independent of other state and local governments.

**Plan Membership**—The Ohio Police & Fire Pension Fund is a statewide retirement plan established by Chapter 742 of the Ohio Revised code (ORC). Employee and employer membership data as of January 1, 2002 and 2001, based on the most recent actuarial valuation, is as follows:

Employee Members	2002			2001		
	Police	Fire	Total	Police	Fire	Total
Retirees and beneficiaries currently receiving benefits	13,174	10,239	23,413	12,833	10,037	22,870
Terminated employees entitled to benefits but not yet receiving them	93	40	133	99	44	143
Current employees:						
Vested	5,092	4,219	9,311	5,059	4,205	9,264
Nonvested	10,785	8,232	19,017	10,719	7,953	18,672
	15,877	12,451	28,328	15,778	12,158	27,936
<b>Total Members</b>	<b>29,144</b>	<b>22,730</b>	<b>51,874</b>	<b>28,710</b>	<b>22,239</b>	<b>50,949</b>
<b>Employer Members</b>						
Municipalities	252	219		251	215	
Townships	-	106		0	105	
Villages	307	29		322	32	
	559	354		573	352	

**Benefits**—Plan benefits are established under Chapter 742 of the ORC. Members are eligible for normal retirement benefits at age 48 with 25 years of service credit or at age 62 with 15 years of service credit. The normal retirement benefit is equal to 2.5% of annual earnings for each of the first 20 years of service, 2.0% for each of the next 5 years of service, and 1.5% for each year of service thereafter. However, this normal retirement benefit is not to exceed 72% of the member's "average annual salary" for the three consecutive years during which the total "salary" was greatest or the member's "recalculated average annual salary" for any three years during which such salary was the greatest. Retirement with reduced benefits is available upon reaching age 48 with 15 years of service credit and 25 years from the date the member became a qualified employee.

In addition to retirement benefits, OP&F also provides disability, survivor and death benefits. Disability benefits are available to all members and vary by length of service and type of

disability. Survivor benefits are specified dollar amounts paid to eligible survivors upon the death of an active member or retiree if in the line of duty. A death benefit of \$1,000 is payable to the surviving spouse or estate of each deceased retired member.

An eligible spouse or dependent of a member whose death resulted from injury or disease sustained while on active duty as a police officer or firefighter is entitled to receive the member's full monthly salary, which will be reduced at the member's retirement eligibility date. The dependent's benefit will be terminated at the dependent's attainment of age 18 (or 22 if attending school). The spouse's benefit is a lifetime benefit. These death benefit payments are in addition to any optional payment plan benefits elected by the member. Funding for death benefits is received from the State of Ohio, as the ORC requires the State to finance 100% of death benefit payments.

**Healthcare Benefits**—OP&F provides comprehensive health care benefits to eligible benefit recipients and their eligible dependents. These medical benefits are not guaranteed and are subject to change at any time upon action of the Board of Trustees. Coverage includes hospitalization, physician’s fees, prescription drugs and reimbursement of Medicare Part B premiums. Benefit recipients pay a portion of the health care cost through a monthly contribution.

Under Ohio law, medical costs paid from the funds of the plan are included in the employer contribution rates, which are currently 19.5% and 24% of salaries for police and fire employers, respectively. The Board of Trustees allocates employer contributions equal to 7.75% and 7.50% of salaries to the Health Care Stabilization Fund within the Pension Reserve Fund in 2002 and 2001, respectively.

**Refunds**—Upon termination of employment, members may withdraw accumulated contributions to OP&F. Acceptance of a refund cancels the member’s rights and benefits in OP&F. Employer contributions to OP&F are not refundable.

### 3. Contributions and Reserves

**Contributions**—The ORC requires contributions by active members and their employers. The contribution requirement was not actuarially determined but rather established by law under the ORC. Contribution rates are, however, subject to annual review by the Ohio Retirement Study Commission. Additionally, an actuary is used to determine the actuarial implications of the requirement. The adequacy of contribution rates is determined annually using the entry age normal with frozen initial liability actuarial cost method. Contribution rates as required by the ORC are as follows:

Rates established by the ORC at December 31, 2002 and 2001:

	<b>Police</b>	<b>Fire</b>
	(% of active member payroll)	
Employer	19.50	24.00
Member	<u>10.00</u>	<u>10.00</u>
<b>Total statutory rate</b>	<b>29.50</b>	<b>34.00</b>

7.75% and 7.50% of the 19.5% and 24% employer rates were allocated to the Health Care Stabilization Fund in 2002 and 2001, respectively.

House Bill No. 721 required the January 1, 1997 and future actuarial valuations be based on the entry age normal actuarial cost method. Senate Bill 82 established the length of the amortization period for unfunded pension liability as the primary measure of OP&F’s financial status, with a period of 30 years or less being considered satisfactory. This 30-year target is to be attained by the year 2007, and maintained thereafter. As of January 1, 2002, the amortization period under the

current statutory rates is 28 years.

Contributions as a percentage of active member payroll required and made for 2002 and 2001 represented 29.50% for police and 34.00% for firefighters. Employer and member contributions were \$162,402,893 and \$94,114,866 respectively, for police and \$159,269,231 and \$73,022,350, respectively, for firefighters for the year ended December 31, 2002. Employer and member contributions were approximately \$159,432,053 and \$84,743,346, respectively, for police and \$152,653,196 and \$65,788,621, respectively, for firefighters for the year ended December 31, 2001.

In accordance with the ORC, the State of Ohio is required to contribute additional amounts to finance the cost of certain State-legislated benefit improvements. The total amount contributed by the State was \$2,780,378 and \$2,931,250 for the years ended December 31, 2002 and 2001, respectively.

**Local Funds Receivable**—Local governments are required by state statute to pay the unfunded portion of the actuarially determined liability of the local police and firemen’s relief and pension funds that were merged to form OP&F in 1967. The ORC names this obligation of local governments the “Employers’ Accrued Liability.” Interest on the outstanding balance is being accrued at a rate of 4.25%, compounded semi-annually. Local governments began repayment in 1969 and payments are required to be made until 2035. Between 1969 and 1973, payments of principal and interest were received at incremental semiannual rates ranging from 1% to 2% of the original receivable balance. Between 1973 and 2035, semiannual payments of principal and interest are required to be made by the local governments at a rate of 2.5% of the original receivable balance. The balance due at December 31, 2002 and 2001, respectively, includes \$280,360 and \$283,481 due from local governments which had previously underpaid their semi-annual payment and from local governments that joined OP&F subsequent to 1967 according to a 20-year payment plan.

The following is a summary of the amounts due on the local funds receivable:

Year ending December 31,	
2003	2,207,882
2004	2,207,882
2005	2,207,882
2006	2,207,882
2007	2,207,882
Thereafter	<u>59,077,250</u>
Total projected payments	70,116,660
Less interest portion	<u>31,879,221</u>
<b>Balance at December 31, 2002</b>	<b>\$38,237,439</b>

**Reserves**—As required by the ORC, the following accounts have been established for the reserves held for current and future benefits:

**The Police Officers' and Firefighters' Contribution**

**Accounts** accumulates the contributions deducted from the salaries of members. Upon retirement, a member's accumulated contributions are transferred to the Policemen's or Firemen's Pension Reserve Accounts.

**The Police Officers and Firefighters Employers'**

**Contribution Accounts** is the depository for employer contributions. Based on actuarial valuations, amounts are transferred from this account to the Policemen's and Firemen's Pension Reserve Account.

**The Police Officers' and Firefighters' Pension Reserve**

**Accounts** is the accounts from which all retirement, disability, health care and survivor benefits are paid. Included in these Accounts is the Health Care Stabilization Fund from which payments for health care benefits are made. Amounts are transferred into the Pension Reserve Accounts from the Contribution Accounts and the Guarantee Account.

**The Guarantee Account** records all investment earnings of OP&F. In addition, contributions from the State of Ohio, exclusive of death benefit contributions, are recorded in this account. Annually, investment earnings are transferred to the Pension Reserve Funds and the Expense Account.

**The Expense Account** is used to record all expenses for the administration and management of OP&F. Annually, funds are transferred from the Guarantee Account to cover expenses incurred.

Net assets available for benefits for the various accounts were as follows:

	<u>2002</u>	<u>2001</u>
Members' Contribution	\$ 1,339,747,923	\$ 1,250,373,374
Employers' Contribution	725,729,390	2,323,181,161
Pension Reserve	5,375,595,000	4,928,366,000
	<u>\$ 7,441,072,313</u>	<u>\$ 8,501,920,535</u>

## 4. Cash and Investments

**Cash Deposits**—The carrying amount of OP&F's cash deposits at December 31, 2002 was \$58,183,973 and the depository balance was \$34,719,435. Of the depository balance, \$1,533,415 was insured by the Federal Depository Insurance Corporation and \$16,501,461 was covered by collateral held in the name of OP&F's pledging financial institutions, as required by the state statute (category 1 as defined by the Governmental Accounting Standards Board). The remaining depository balance of \$16,684,559 was uninsured and uncollateralized and was held in the name of OP&F's pledging financial institution, as required by the Ohio Revised Code (Category 3).

The carrying amount of OP&F's cash deposits at December

31, 2001 was \$63,641,039 and the depository balance was \$55,669,378. Of the depository balance, \$1,991,020 was covered by federal depository insurance and \$27,706,278 was covered by collateral held in the name of OP&F's legally-designated custodian, the Treasurer of the State of Ohio (Category 1 as defined by the Governmental Accounting Standards Board). The remaining depository balance of \$25,972,080 was uninsured and uncollateralized and was held in the name of OP&F's pledging financial institution, as required by the Ohio Revised Code (Category 3).

**Investments**—Section 742.11 of the Ohio Revised Code grants the Board of Trustees full power to invest the assets of OP&F. This statute requires that investments be made with care, skill, prudence and diligence under the circumstances then prevailing that a prudent and informed person would use.

Statement No. 3 of the Governmental Accounting Standards Board requires OP&F to categorize its investments to give an indication of the level of collateral risk assumed by OP&F. Category 1 includes investments that are insured or registered or for which the securities are held by OP&F or its agent in OP&F's name. Category 2 includes uninsured and unregistered investments for which the securities are held by the counterparty's trust department or agent in OP&F's name. Category 3 includes uninsured and unregistered investments for which the securities are held by the counterparty, or its trust department or agent, but not in OP&F's name.

All investments subject to categorization met the criteria of Category 1 at December 31, 2002 and 2001 and are held in the name of OP&F or its nominee by the Treasurer of State of Ohio as custodian. Investments in domestic pooled common stocks, real estate, commercial mortgage funds and private equity, by their nature, are not required to be categorized.

A summary of short-term securities and investments at fair value is as follows:

<u>Category</u>	<u>2002</u>	<u>2001</u>
Commercial paper	\$ 360,974,867	\$ 268,262,250
U.S. government bonds	265,858,290	445,742,801
Corporate bonds and obligations	797,171,640	780,964,012
Mortgage & asset backed obligations	799,740,417	804,463,085
Foreign & Canadian bonds	0	9,146,560
Domestic stocks	1,943,517,574	2,401,667,977
Domestic pooled stocks	1,282,226,201	1,545,715,035
International securities	1,281,703,040	1,440,700,621
Real estate	611,183,584	579,252,406
Commercial mortgage funds	120,501,166	127,540,457
Private equity	94,210,402	75,617,183
	<u>\$ 7,557,087,181</u>	<u>\$ 8,479,072,387</u>

Commercial Paper is included in cash and short-term investments on the Statements of Plan Net Assets.

**Securities Lending**—OP&F participates in a domestic securities lending program, as authorized by the board of trustees, administered by a custodial agent. These securities are loaned for collateral with a simultaneous agreement to return the collateral for the same securities in the future. The equity securities are loaned to independent broker/dealers (borrowers) in exchange for collateral of 102% of the market value of the loaned securities. OP&F has minimized its exposure to credit risk due to borrower default by having the custodial agent bank determine daily that required collateral meets 102% of the market value of securities on loan. There are no restrictions on the amount of securities that can be lent at one time or to one borrower. Contracts with the lending agents require them to indemnify OP&F if the borrowers fail to return the securities or fail to pay OP&F for income distributions by the securities' issuers while the securities are on loan. All securities loans can be terminated on demand, and the maturities of the investments made with cash collateral generally match the maturities of securities loans.

OP&F has not experienced any losses due to credit or market risk on securities lending activity since implementation of the program. OP&F does have the ability to pledge or sell collateral securities absent a borrower default.

Securities loaned to brokers/dealers totaled \$1,155,472,570 and \$1,066,942,916 at December 31, 2002 and 2001, respectively, and the associated collateral at that date was \$1,180,657,702 and \$1,092,822,853. Securities lending net income totaled \$2,579,314 and \$2,557,881 for the years ended December 31, 2002 and 2001, respectively.

**Derivatives**—OP&F invested in Planned Amortization Class and Sequential Pay Real Estate Mortgage Investment Conduit bonds issued by GNMA, FHLMC and FNMA. Planned Amortization Class bonds are retired according to a payment schedule so as to have a stable average life and yield even if expected prepayment rates change within a specified broad range of prepayment possibilities. Sequential Pay bonds begin to pay principal when classes with an earlier priority have paid to a zero balance. Such bonds enjoy uninterrupted payment of principal until paid to a zero balance. In terms of credit risk, the United States government explicitly backs GNMA mortgage securities programs and implicitly backs FHLMC and FNMA mortgage securities programs. OP&F has not violated any legal, regulatory or contractual provisions by such participation and there is no undue credit, market or legal risk. These securities were purchased in order to enhance OP&F's overall total rate of return.

OP&F also has invested in one commingled EAFE (Europe, Australia, Far East) and one commingled S&P 500 index fund. Those funds to a minor extent utilized futures contracts to maintain a fully invested posture, and also utilized certain derivative money market instruments in their short-term invest-

ment funds. OP&F's exposure represented less than 1% of the total portfolio market value at year-end. OP&F has not violated any legal, regulatory, or contractual provisions by such participation and there is no undue credit, market or legal risk.

## 5. Mortgage Notes Payable

Mortgage notes payable are included in investment commitments payable on the statement of plan net assets.

In 1998, OP&F entered into a \$5,000,000 mortgage loan payable, secured by a deed of trust, in connection with the purchase of St. Andrews Apartments. The loan bears interest at 6.5%. Also in 1998, a \$16,500,000 mortgage loan payable, secured by a deed of trust, was assumed with the purchase of the St. Andrews Apartments. The loan bears interest at 7.91%.

In 2000, OP&F assumed mortgage notes payable of \$25,625,000. These loans are secured by real properties and bear per annum interest of 7.16%. A mortgage loan in the amount of \$15,840,000 was assumed in 1995 and secured by a deed of trust for the Vista Ridge building, which bears interest of 7.8% per annum.

In 2002 OP&F assumed a \$27,250,000 mortgage loan payable with the purchase of The Loop, bearing interest at 6.41%.

Aggregate and annual payments of principal on the mortgage loans are as follows:

Year ending December 31,	
2003	1,675,406
2004	24,145,123
2005	14,821,241
2006	29,528,444
2007	31,343,405
Thereafter	<u>34,315,522</u>
<b>Total payments</b>	<b>\$ 135,829,141</b>

A roll-forward of mortgage notes payable is as follows:

Balance at December 31, 2001	\$128,909,316
Additional debt assumed	27,250,000
Principal payments made	<u>(20,330,175)</u>
<b>Balance at December 31, 2002</b>	<b>\$ 135,829,141</b>



## 6. Defined Benefit Pension Plan

OP&F contributes to the Public Employees Retirement System of Ohio, (PERS), a cost-sharing multiple-employer defined benefit pension plan. PERS provides retirement and disability benefits, annual cost-of-living adjustments, and death benefits to plan members and beneficiaries. Benefit provisions and contribution requirements are established by the Ohio State Legislature and are codified in Chapter 145 of the Ohio Revised Code. PERS issues a publicly available financial report that includes financial information and required supplementary information for the plan. That report may be obtained by writing to PERS, 277 East Town Street, Columbus, Ohio 43215-4642 or by calling (614) 466-2085 or 1-800-222-7377.

Plan members are required to contribute 8.5% of their annual covered salary, while employers are required to contribute 13.31%. OP&F's contributions to PERS for the years ending December 31, 2002, 2001 and 2000 were \$ 1,074,938, \$925,516 and \$694,552, respectively, equal to the required contributions for each year.

## 7. Other Postemployment Benefits

In addition to the pension benefits described in note 6, PERS provides postretirement health care coverage to age and service retirants with 10 or more years of qualifying Ohio service credit. Health care coverage for disability recipients and primary survivor recipients is available. The health care coverage provided by PERS is considered an Other Postemployment Benefit (OPEB) as described in GASB Statement No. 12. At December 31, 2002, the plan had 402,041 active participants.

A portion of each employer's contribution to PERS is set aside for the funding of post retirement health care. The 2002 employer rate was 13.55% of covered payroll, of which 5.0% was the portion used to fund health care for the year. For the year ended December 31, 2002, approximately \$397,000 of employer contributions OP&F made to PERS was the portion used to fund health care.

The Ohio Revised Code provides statutory authority requiring public employers to fund postretirement health care through their contributions to PERS.

The actuarial value of PERS' net assets available for OPEB at December 31, 2001 were \$11.6 billion. The actuarially accrued liability and the unfunded actuarial accrued liability, based on the actuarial cost method used, were \$16.4 billion and \$4.8 billion respectively.

The actuarial present value of accrued postemployment benefits was determined based on the entry age normal method of funding. Significant actuarial assumptions based on PERS's

latest Actuarial Review performed as of December 31, 2001 and are as follows: an investment rate of return of 8.0%, investments valued at market value, adjusted annually to reflect 25% of unrealized market appreciation or depreciation on investment assets, no change in the number of active employees, base pay rate increases of 4.0% and annual pay increases over and above the 4.05% base increase ranging from .50% to 6.30%, and health care costs assume an increase of 4.0% annually.

## 8. Commitments and Contingencies

OP&F is a defendant in a number of lawsuits pertaining to matters that are incidental to performing routine business functions. OP&F management is of the opinion that ultimate settlement of such claims will not result in a material, adverse effect on OP&F's financial position as of December 31, 2002.

OP&F is committed to make additional capital contributions of \$256,135,873 towards our private equity program. Our private equity program has \$94,210,402 and \$75,617,183 invested at December 31, 2002 and 2001, respectively.

## 9. State of Ohio Death Benefit Fund

Pursuant to Section 742.63 of the Ohio Revised Code, the Board of Trustee of the Ohio Police and Fire Pension Fund administers the State of Ohio Public Safety Officers Death Benefit Fund. This program was established by the State of Ohio to provide monthly benefit payments to surviving family members of Ohio firefighters and law enforcement officers who have been killed in the line of duty or die of a duty-related accident or illness. Funds are disbursed to OP&F each State fiscal year (July 1-June 30) and are paid monthly by OP&F to eligible recipients. The unused balance at June 30 is returned to the State. The Death Benefit Fund is considered to be an agency fund administered by the Ohio Police and Fire Pension Fund and, accordingly, its assets of \$14,524,899 and \$13,640,695 and the related liability for unpaid benefits are included in the accompanying Combining Statement of Plan Net Assets as of December 31, 2002 and 2001, respectively.

## Required Supplementary Information

### 1. Schedule of Funding Progress

As of January 1 (Data for earlier periods is not available because a different funding method was used.)

Valuation Year	Valuation Assets	Actuarial Accrued Liabilities (AAL)	Unfunded Actuarial Accrued Liabilities (UAAL)	Ratio of Assets to AAL	Active Member Payroll	UAAL as % of Active Member Payroll
1998	6,231,419,000	7,697,677,000	1,466,258,000	81.0%	1,190,878,000	123.1%
1999	7,306,814,000	8,452,622,000	1,145,808,000	86.44%	1,249,114,000	91.73%
2000	7,988,578,000	8,995,564,000	1,006,986,000	88.81%	1,338,514,000	75.23%
2001	8,498,069,000	9,506,283,000	1,008,214,000	89.39%	1,407,542,000	71.63%
2002	9,076,469,000	9,785,766,000	709,297,000	92.75%	1,534,336,000	46.23%

The amounts reported in this schedule do not include assets or liabilities for postemployment healthcare benefits.

### 2. Schedule of Contributions from Employers and Other Contributing Entities

Year Ended December 31	Annual Required Contributions	Percentage Contributed
1997	176,567,663	100%
1998	185,548,447	100%
1999	191,646,415	100%
2000	206,796,608	100%
2001	205,979,830	100%
2002	205,992,860	100%

Contributions include funding from the State of Ohio to finance the cost of certain benefit improvements. Amounts do not include contributions for postemployment healthcare benefits

### 3. Notes to the Required Supplementary Schedules

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

Valuation date	January 1, 2002
Actuarial cost method	Entry Age Normal
Amortization method	Level percent of payroll, open
Remaining amortization period	28 years
Asset valuation method	5-year adjusted market value*
Actuarial assumptions:	
Investment rate of return	8.25%
Projected salary increases	5.0-11.0%
Cost-of-living adjustments	3.0%

\*with a corridor of 10% of the market value for 2002 and a corridor of 20% thereafter.

## Schedule of Administrative Expenses\*

For The Years Ended December 31, 2002 and 2001

	2002	2001
<b>Personnel Services:</b>		
Salaries and Wages	\$ 7,667,914	\$ 7,907,879
Retirement Contributions	1,074,938	932,516
Employee Benefits	1,716,488	1,288,613
<b>Total Personnel Services</b>	<b>\$ 10,459,340</b>	<b>\$ 10,129,008</b>
<b>Professional Services:</b>		
Auditing	109,599	76,775
Actuarial	296,452	216,000
Medical	723,978	683,946
Legal	108,648	119,014
Investment	16,096,293	14,818,363
Treasurer of State Charges	8,332	8,214
Employee Training	323,209	441,005
Temporary Employees	254,807	94,032
Other Professional Services	1,970,331	1,733,423
<b>Total Professional Services</b>	<b>\$ 19,891,649</b>	<b>\$ 18,190,772</b>
<b>Building Rent</b>	<b>\$ 1,085,245</b>	<b>-</b>
<b>Communications:</b>		
Telephone	122,959	109,832
Postage	300,043	302,689
Transportation and Travel	123,380	110,000
<b>Total Communications Services</b>	<b>\$ 546,382</b>	<b>\$ 522,521</b>
<b>Miscellaneous:</b>		
Office Supplies	179,401	155,049
Printing and Publications	203,332	252,535
Dues and Subscriptions	66,027	68,792
Equipment and Maintenance	626,525	479,564
Retirement Study Council	42,746	47,055
Insurance—Administrative	156,872	182,423
Depreciation Expenses	1,084,000	1,025,721
<b>Total Miscellaneous</b>	<b>\$ 2,358,903</b>	<b>\$ 2,211,139</b>
<b>TOTAL ADMINISTRATIVE EXPENSES</b>	<b>\$ 34,341,519</b>	<b>\$ 31,053,440</b>

\* Includes investment related administrative expenses

### Schedule of Investment Expenses\*

For The Years Ended December 31, 2002 and 2001

	2002	2001
Investment Manager Fees	\$ 15,046,390	\$ 13,950,653
Custodial Fees	1,049,903	867,710
Other Professional Services	665,334	646,250
Other Direct Investment Department Expenses	1,368,696	1,390,287
Allocation of Other Administrative Expenses	1,324,107	1,076,193
	<b>\$ 19,454,430</b>	<b>\$ 17,931,093</b>

*\*A portion of the non-Investment Department administrative expenses of OP&F is allocated to Investment Expense based on the ratio of OP&F's investment staff to total Fund staff. All of the investment expenses are included in the Schedule of Administrative Expenses displayed on the previous page.*





## *Investment Section*

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- 1. Investment Report**
- 2. Investment Portfolio Summary**
- 3. Schedule of Investment Results**
- 4. Investment Consultants and Money Managers**
- 5. Schedule of Brokers' Fees**
- 6. Investment Policy and Guidelines**

# 1. Investment Report *Prepared through a combined effort of the Investment Department*

## Introduction

The investment authority of the Fund is specified in Section 742 of the Ohio Revised Code. Importantly, the Code requires that the Board and other fiduciaries discharge their duties solely in the interest of the participants and beneficiaries, for the exclusive purpose of providing benefits to participants and their beneficiaries and defraying reasonable expenses of administering the Fund. Within the guidelines of the Code, the Fund has developed an internal Investment Policy that provides for appropriate diversification of assets, and an acceptable expected return on investments after consideration of investment risks. Performance returns are prepared by Wilshire Associates in accordance with the Association for Investment Management and Research (AIMR) standards.

## Significant Developments in 2002

Most of our efforts last year were aimed at implementing and then maintaining the recommendations of an asset/liability study completed in 2000. The study focused on finding a way for the Fund to meet its statutory funding targets and to help defray growing health care costs, both growing problems throughout the pension world. The major recommendation of the study was for the Fund to move to a more aggressive, equity oriented asset mix in order to target a higher expected return of 8.75%. More specifically, the study suggested that we shift a significant amount of assets out of core fixed income and reinvest them in public and private equity and to make our first ever investments in high yield bonds. Obviously, higher equity exposures have been punished over the past few years. While this has been painful in the short-run, pension funds have a very long-term outlook, and we are confident that our philosophy and patience will ultimately be rewarded. On the plus side, our active management has added value, especially our bias toward value style equities. This bias, of course, will not pay off forever, and last year we began taking steps to move to a neutral style posture. Following are these and other noteworthy investment issues with which the Fund dealt last year:

- While we struggled through another year of difficult absolute performance, the Fund's total portfolio did outperform its benchmark by 0.91%.
- Our team of external US equity managers outperformed the Fund's US equity benchmark by slightly more than 1% thanks largely to our value managers, especially small cap value.
- We completed development of a more streamlined real estate acquisition process that gives more discretion to our external advisors. This required us to work in concert with our advisors to develop a more clearly defined investment plan for the Fund and more specific acquisition guidelines for each advisor.

- We completed our search for an emerging markets manager with the hiring of Montgomery Asset Management (subsequently merged into Wells Capital Management).
- After terminating a large cap growth manager, we completed a search for a replacement, which resulted in the hiring of Waddell & Reed and Enhanced Investment Technologies (INTECH).
- In order to reach and maintain our asset allocation targets, we continued to shift assets out of fixed income and real estate and into US equity, international equity, and private equity.
- We continued to work steadily toward our 3% long-term private equity target allocation and made our first dedicated private equity secondary fund investments.
- Staff and Board completed evaluations of all managers in all asset classes according to policy.

## Economic Environment

The Federal Open Market Committee came into 2002 with an expectation of continued economic weakness after aggressively pursuing a series of eleven interest rate cuts throughout the prior year. The Fed's economic outlook, or bias, alternated between weakness and a balanced risk assessment for the rest of the year, but they acted only once, cutting rates by 50 basis points in early November. The Fed was concerned about weak labor market conditions, softness in manufacturing, declining consumer confidence and weakening retail sales. Given the slack in labor and production markets, inflationary pressures were minimal, thus giving the Fed a green light to make its November move.

The low interest rate environment engendered by the Fed gave some support to the weak economy, but did little to bolster consumer confidence. Consumer confidence had in fact continued its decline from a high water mark in 2000. This important psychological measure improved early in 2002, but tumbled through the rest of the year. Confidence suffered in concert with significant stock market declines, continued job losses and early rhetoric about a possible conflict with Iraq. Meanwhile, overall economic growth, as measured by GDP, swung back into positive territory in late 2001 and continued a choppy, but positive pattern last year. Following strong 5.0% growth in the first quarter and a modest 1.3% growth in the second quarter, real GDP rose 4.0% in the third quarter before falling off to a 1.4% growth rate in the fourth quarter. For all of last year, real GDP grew just 2.4% after gaining only 0.3% in 2001 and 3.8% in 2000.

Consumers continued to support the economy aided largely by the very favorable low interest rate environment. Discounted auto financing kept car buyers coming to the showrooms, and

low mortgage rates made the “American Dream” a possibility for huge numbers of homebuyers. Existing homeowners also took advantage of low rates and refinanced their mortgages to improve their personal balance sheets or to free up funds for other purchases. After a significant drop in 2001, business activity as measured by industrial production showed a minor, but still positive bounce. Businesses were once again working to replenish inventory levels that had been drawn down the prior year. Nevertheless, companies, looking to regain or boost profitability, continued to cut costs through payroll reductions. As a result, the unemployment rate of 5.8% at December 2001, after dipping early in the year, moved sideways to slightly higher to end the year at 6.0%. Although US payrolls did increase for several months around the middle of the year, overall, the economy continued to lose jobs in 2002. Coupled with the payroll decline in 2001, this represented the first back-to-back years of job losses since the 1950s. If there is a positive aspect to this story, it is the fact that productivity continued to surge. With productivity growing faster than GDP, job growth has been restrained. In fact, US productivity posted its biggest gain since 1950 helping keep prices down and support company profits even in this slow growth economy. The still slow economy and minimal wage pressures were offset slightly by rising energy costs. This resulted in a CPI increase last year of 2.4% compared with 1.6% in 2001 and 3.4% in 2000.

Early in 2003, the economy has been faced with severe winter storms, geopolitical concerns of impending war with Iraq and strained relations with North Korea, rapidly rising energy costs and continued declines in consumer confidence. While the Fed is still guarding against weakness, they have taken no additional action since their November meeting. Looking forward, a quick resolution to the brewing crisis with Iraq would remove one of the major uncertainties holding back the economy. A favorable outcome should also bring energy prices down and boost confidence levels. Combined with the Fed’s accommodative monetary policy, the economy should improve over the course of the year.

### Total Fund

Due to our high equity exposure, our performance reflects that of the global equity markets. As a result, 2002 was another difficult year for our portfolio. As the year began, our portfolio was worth over \$8.3 billion, and, given that the equity markets had recovered from the terrorist attacks by the end of 2001, we looked forward to a year of better performance. However, events did not transpire that way. Domestic equity markets were essentially in a relatively narrow trading range for the first five months of the year, and then began a steep decline, reaching new lows in October before staging a rebound by year-end. International equity markets fared even worse. The net result of rather large negative returns from equities, significantly positive returns from fixed income, modestly positive returns from high yield and real estate was that our portfolio

ended the year above \$7.4 billion, net of mortgage loans. On a positive note, our total portfolio outperformed both its interim and long-term policy benchmarks for the year. Specifically, the total portfolio exceeded our Interim Policy Benchmark by 91 basis points and our Long-Term Policy Benchmark by 69 basis points. This past year’s returns resulted in our 3- and 5-year annualized returns exceeding their corresponding policy benchmarks. Although the portfolio has performed well on a relative basis, we, like most investors, have been very disappointed in the absolute returns. That being said, we take comfort in our maintenance of a long-term perspective and a belief that a well-diversified portfolio should serve the Fund well over the long-term. We continue our efforts to rebalance the portfolio as dictated by policy allocation ranges and not attempt to time the markets in order to remove human emotion from the decision making process.

### Equities

Not since the periods from 1939-41, in the midst of World War II, and the Great Depression era of 1929-32 has the S&P 500 declined for at least three consecutive years. Unfortunately, with the decline in calendar year 2002, the three-year period from 2000-2002 joined that infamous group. Specifically, the S&P 500 declined -22.1% last year despite a strong rebound in the fourth quarter. On a cumulative basis, the index has fallen -37.6% in the last three years, compared to a -20.6% cumulative loss for the years of 1939-41 and -64.2% for 1929-32. Any number of factors weighed heavily on the market during the past year: an uneven economic recovery, terrorism, the prospect of war with Iraq, continued accounting scandals and governmental probes into conflicts of interest in Wall Street research. On the economic front, rising unemployment, a cautious outlook for corporate profits and declining consumer sentiment were three of the most influential factors affecting the market. In addition, low capacity utilization and below average business capital expenditures muted the economic recovery in 2002. On the geopolitical front, the uncertainty of conflict with Iraq as well as the threat of terrorism made investors seek “safe haven” investments such as U.S. Treasury bonds and gold and avoid riskier assets such as stocks. On a related note, these tensions and problems in Venezuela pushed the price of oil up approximately 60% over the past year, resulting in an effective tax on consumer incomes. Taken together, all of this uncertainty made the market, as measured by the S&P 500, the most volatile in its recorded history. Of all trading days last year, 20% of them witnessed an average daily gain/loss of 2% or more. On a more positive note, the Fed has remained accommodative by keeping short-term interest rates at historical lows. This, of course, led to lower mortgage rates and auto financing rates, which helped buoy consumer spending. In addition, lower interest rates helped to keep price earning ratios higher than they otherwise might have been and helped make equity returns more competitive. Like the S&P 500, all other major market indexes posted double-digit losses in 2002. The Nasdaq Index, which is heavily

weighted in Technology, posted a loss of -30.2% for the year. On a cumulative basis, the Nasdaq Composite has lost -73.5% since its peak in March of 2000. Unlike 2001, when small- and mid-cap value indices posted positive returns, all size/style segments of the markets were negative in 2002. Mid-cap value was the strongest performer of the six size/style categories by posting a -9.7% return for 2002, followed by small-cap value which delivered a -11.4% return. Taking all these factors into consideration, our domestic equity composite return of -19.81% outperformed our benchmark, the Wilshire 5000, by 1.05%. This 105 basis points outperformance was mainly attributable to the performance of our value managers relative to their respective benchmarks and peer groups. As we look to 2003, odds seem to favor a positive year. Since 1926, the S&P 500 has only once declined more than three consecutive calendar years: the Great Depression years of 1929-1932. Although we are currently experiencing the longest bear market since World War II, we are mindful of the fact that it follows on the heels of the longest bull market ever recorded. Until the excesses of the bull market have been purged, one should not expect the stock market to return to its high-octane growth rate anytime soon.

During 2002, OP&F terminated one large-cap growth manager due to organizational issues. In that replacement, OP&F hired two large-cap growth managers, Waddell & Reed and INTECH. Other developments within our domestic equity structure included several contributions throughout the year to our S&P 500 Index fund in order to rebalance to our target weighting. Due to the decline in market values, we had breached the lower end of our domestic equity allocation range.

In terms of the international equity markets, 2002 was a decidedly negative year. For the year, the MSCI EAFE Index, representing non-US developed markets, declined -15.94%, while the MSCI Emerging Markets Free Index fell -6.00%. The negative returns for the non-US developed markets were actually muted by a weak dollar, which benefited US investors' holdings in foreign currencies. In fact, the MSCI EAFE Index was down over -26% in local currencies. Non-US markets were affected by the same factors as US markets, war concerns, terrorism threats and weak economies. As a group, our active and passive non-US developed markets managers posted a return of -17.7% compared to the benchmark return of -15.94%. Our emerging markets managers posted a -8.69% return, 269 basis points below the MSCI Emerging Markets Free Index.

As with our domestic equity allocation, our allocation to international developed markets fell below the lower end of our target allocation range and required us to make contributions to our managers to bring them closer to our target weight of 17%. In emerging markets, we hired one new manager to replace a manager terminated in late 2001 for performance and organizational issues. In addition, we withdrew some funds from this asset class because we were above our new target weighting.

## Fixed Income

Last year was another excellent year for the fixed income market. The Lehman Aggregate Index posted a return of 10.26%, and it outperformed equities for the third consecutive year. While our internal fixed income team suffered through an uncharacteristically poor year, our external manager, Western Asset Management, turned in a very strong performance. Interest rates on Treasuries dropped approximately one and one-quarter percentage points as investors continued to worry about the strength of the economy. Reacting to these concerns, the Federal Reserve Board lowered short-term interest rates an additional one-half percent. A flight to quality provided additional demand for Treasuries and government sponsored mortgages as investors fled the scandal-ridden corporate bond market. Corporate fraud at companies such as WorldCom, Qwest and Tyco along with low profits led to a record number of corporate bond defaults and credit downgrades. As a result, corporate bonds underperformed similar maturity Treasuries by nearly two percentage points. At the end of the year, the economy remained sluggish despite very stimulative monetary and fiscal policies. However, many investors were hopeful that a successful resolution of the Iraq crisis would lead to improved consumer and business confidence and lower oil prices. This, in turn, would hopefully increase spending and economic growth.

Unfortunately, the Iraq crisis is not the only impediment to economic growth in 2003. A victory over Iraq does not guarantee significantly lower oil prices because Iraqi oil wells may be destroyed, and Venezuelan oil production is likely to remain below normal due to political unrest. Significantly higher oil prices tend to act as a tax on consumers, which may limit their spending on other goods. In addition, consumer spending has been strong for several years leaving the likelihood of little pent-up demand to generate higher spending. Low capacity utilization, poor profitability, and a desire to strengthen balance sheets will keep capital spending weak in early 2003. However, by late 2003 or early 2004, capital spending will probably increase because it has been very low in recent years. In 2002, depreciation of capital equipment was greater than capital spending, so the value of business equipment actually dropped. This cannot continue for long without a material effect on production. Businesses will eventually have to replace worn-out and obsolete equipment. This process will hopefully begin in late 2003 or early 2004. Low inventory levels will ensure that an increase in demand will quickly lead to additional production. Therefore, we expect bonds to do well in early 2003, but weaken in late 2003 as the economy recovers or the market anticipates an early 2004 recovery. Bond returns should be relatively low in 2003, providing a total return less than 5%.



## High Yield

During 2002, the high yield market performed as well as could be expected in the face of the market conditions discussed earlier. In addition to these factors, the fixed income market in general had to deal with a large number of defaults and a record number of credit downgrades. The high yield market as measured by the CSFB Developed Countries High Yield Index returned 3.06% for the year. Our three active high yield managers combined to beat the index with a return of 4.12%. On an historical basis, the high yield market continued to look relatively cheap due to the fact that yields were still about 1,000 basis points higher than 10-year Treasuries. The high yield market benefited from relatively strong inflows into mutual funds as investors sought higher income securities. The high yield market also drew support from a sparse new issue calendar. However, the general decline in interest rates witnessed during the year was not fully reflected in the high yield market as a still soft economy kept credit risk fears at a heightened level. If the economy cooperates in 2003, we believe the prospects for the high yield market look very promising.

## Real Estate

Real estate fundamentals weakened in 2002 as the nation faced a weak job market and an uncertain geopolitical environment. Weak tenant demand, new supply, competitive leasing markets and economic uncertainty caused vacancy levels to rise across all property types. Meanwhile, rental rates declined in a year that was considered one of the most challenging for asset managers in over a decade.

With a weak job market, household formation slowed, adversely affecting apartment properties. The weak economy was not the only force that exerted downward pressure on this property type as it competed with extremely low mortgage rates that led many would-be renters into single-family homes. Industrial vacancy rates also continued to climb as low levels of trade and industrial production along with stagnant inventory levels caused a contraction in demand. The national vacancy rate for industrial properties at year-end was 11%. Although this compares favorably to a 16.5% office vacancy, it is actually quite high by historical standards. Since the crash of the high tech industry, office vacancy continued to climb although at a reduced rate. A weak job market, exacerbated by large corporate bankruptcies, efficiencies in productivity and tenant defaults, caused an uncertain outlook for the office sector. Returns on retail property were strong as consumers continued their robust spending patterns. As long as consumers continue to spend, demand for retail space will be strong.

In spite of the weakened real estate fundamentals, the NCREIF return for 2002 was 6.8%, consisting of 8.4% income and a negative -1.6% appreciation. For the same period, the OP&F real estate portfolio return was 10.4% consisting of 9.1% income and 1.2% appreciation. This return exceeded NCREIF by 360 basis points.

The NCREIF return of 6.8% in 2002 is down from 7.4% in 2001. However, this is still relatively attractive compared to the 10.26% return for the Lehman Aggregate Bond index and the loss of -22.1% for S&P 500 index. As a result, investment capital looking for safe haven feverishly chased real estate, driving property prices up and possibly creating a new paradigm. In a future with diminished return expectations, low inflation and low interest rates, some investors think cap rates may have made a long-term secular shift downward.

In 2002, OP&F acquired only one property, The Loop, a retail center located in Methuen, Massachusetts, a distant suburb of Boston. As capital chased real estate and prices trended higher, we sold an apartment portfolio in Houston, Texas generating over an 18% return. As of this writing, we are under contract to sell an office building in New Jersey and an office building in suburban Denver. Both sales are expected to generate healthy returns for the Fund.

The Fund is posturing for an acquisition mode in 2003. It is uncertain how long sluggish economic growth will last, making it difficult to predict the full impact on the real estate market. Therefore, our investment strategy for 2003 will be that of extreme caution and selectivity in the acquisition process. We will continue to seek well leased, stable and superior quality assets in major metropolitan markets that will provide stability to our portfolio regardless of the economic climate.

## Private Equity

For the year ending September 2002 (private equity returns are lagged by one quarter), our small allocation to private equity provided a return of -21.61% versus its benchmark (Wilshire 5000 + 5%) return of -12.52%. The year 2002, in many respects, was a carbon copy of 2001 with regard to the private equity asset class. Negative returns, continued portfolio write-downs, slow exit markets and poor economic conditions all had a profoundly negative effect on the private equity marketplace in 2002. Despite this unfavorable environment, there have been several positive developments that are likely to increase the odds of positive private equity returns in the years ahead. For example, valuation multiples have decreased significantly, which allows investors to put their money to work at a lower cost. Fundraising has tailed off considerably, ensuring that a more appropriate supply of capital will not outstrip demand and lead to lower returns. Finally, the focus of the industry has returned to its origins, to nurture and build viable businesses.

We continued to work toward our 3% target allocation by committing capital to various Ohio and non-Ohio based venture capital, buyout and fund of funds vehicles. In addition, we made our first commitments to secondary funds, whose focus is to purchase an existing interest in private equity partnerships and portfolio companies, usually at a discount, from an original investor seeking an early exit from a partnership investment. OP&F made four new commitments to the following firms in

2002: \$10 million to Kirtland Capital Partners IV (Ohio based buyout fund), \$20 million to Landmark Equity Partners XI (secondary fund), \$20 million to Lexington Capital Partners V (secondary fund), \$17 million to Wilshire Private Markets Fund V (fund-of-funds) and \$3 million to Wilshire European Private Markets Fund V (fund-of-funds). This brought our total capital committed since the inception of our private equity program to \$428 million, of which \$260.3 still has yet to be called. Distributions since the inception of the program have totaled \$87.5 million.

In the future, we will continue to work toward our 3% target by reviewing and monitoring our existing relationships for further investment and by looking at a limited number of new managers. In addition, we will continue to look for ways to diversify our private equity program in order to achieve the highest risk adjusted return.

### 2003 Developments and Challenges Ahead

As mentioned earlier, the Board and staff were fairly active in 2002. While it is still very early in the year, we are off to a good start in our efforts to evaluate and implement ways to provide prudent and competitive returns for our membership.

- We undertook a review of our domestic equity structure. As a result, one of our large cap managers was terminated, and another large cap portfolio was assigned to a different management team within the same organization. In addition, it was determined that we should increase our weighting to large cap growth managers to achieve a manager structure that better reflects our composite benchmark, the Wilshire 5000 Index.
- We terminated one of our international core EAFE equity managers, and will initiate a search for a replacement manager.
- As mandated by the Treasurer of the State of Ohio, we are working toward an April 1 transition to a new domestic custodian, Huntington National Bank.

We have always stated our intention to earn at least an 8.25%

## 2. Investment Portfolio Summary December 31, 2002

Type	% of Fair Value	Market Value
Commercial paper	3.16%	\$ 360,974,867
U.S. government bonds	5.25%	265,858,290
Corporate bonds and obligations	9.20%	797,171,640
Mortgage & asset back obligations	9.48%	799,740,417
Domestic stocks	28.29%	1,943,517,574
Domestic pooled stocks	18.21%	1,282,226,201
International securities	16.97%	1,281,703,040
Real estate	6.73%	611,183,584
Commercial mortgage funds	1.5%	120,501,166
Private equity	1.10%	94,210,402
	<b>100.00%</b>	<b>\$ 7,557,087,181</b>

return over time, which is our actuarial assumption rate. As mentioned earlier, we are targeting an 8.75% return to meet statutory funding requirements and to lessen the impact of rising health care costs. Like many other plan sponsors, we will review our return assumptions to determine if we need to modify our asset allocation plan. We will continue to explore new investment ideas and hope to improve the efficiency of and reduce the costs of our operations. As we look ahead, we intend to tackle a number of issues related to these goals.

- Review the reasonableness of our current asset allocation assumptions.
- Explore ways to add return, e.g., derivative use for asset allocation rebalancing, cash equitization and manager transitions, enhanced index products, hedge fund strategies.
- Review investment products that do not fit neatly into our traditional categories.
- Implement the managed discretion process for real estate acquisitions.
- Implement our transition to a new domestic custodian.
- Implement the new domestic equity structure mentioned above. This will involve shifting assets from existing and terminated managers to our two new growth managers and to a new management team and product within an existing manager organization.
- Review our fixed income structure, including a strategic allocation to TIPS.
- Establish an overall risk management program, independent of OP&F managers, which will facilitate timely identification of potential risks and ensure appropriate investment strategies are in place.
- Implement the compliance and performance functions of our investment accounting software and acquire a compatible attribution function.
- Evaluate incentive compensation for personnel retention.
- Review our proxy policy in light of recent corporate scandals and legislation.

### Ten Largest Common Stocks (by Market Value)

	Shares	Market Value
Citigroup Inc	1,204,517	\$ 42,386,953
Microsoft Corp.	789,300	40,806,810
American International	532,976	30,832,661
Merck & Co., Inc.	419,600	23,753,556
Federal Home Loan Mtg. Corp	399,200	23,572,760
Berkshire Hathaway "B"	9,000	21,807,000
Pfizer Inc.	694,797	21,239,944
UST Inc.	601,820	20,118,842
Exxon Mobil Corporation	572,400	19,999,656
Wyeth	505,000	18,887,000

### Ten Largest Bonds and Obligations (by Market Value)

	Par Value	Market Value
GNMA I 30YR JAN FWD 7% 01/01/33	\$ 60,000,000	\$ 63,562,200
FNMA 30YR JAN FWD 6% 01/01/33	54,550,000	56,373,606
Treasury Inflation Protected Security 3 7/8 % 04/15/29	24,680,000	33,333,656
US Treasury Bond 11 1/4% 02/15/15	18,755,000	31,232,889
US Treasury Bond 5 3/8% 02/15/31	27,130,000	29,575,769
Socgen Real Estate Co LLC Stp% 12/29/49	25,850,000	28,430,088
US Treasury Bond 7 1/2% 11/15/16	20,620,000	26,967,042
US Treasury Bond 6 7/8% 8/15/25	21,271,000	26,901,220
FNMA 30YR JAN FWD 7% 01/01/33	25,350,000	26,654,468
Continental Mortgage Home Equity Loan Trust 7.68% 12/25/29	22,810,000	24,488,816

### Ten Largest Real Estate Holdings (by Market Value)

	Market Value
Pointe at Park Center	\$ 60,700,000
The Loop	54,500,000
200 Tower Place	48,600,000
St. Andrew's Apartments	47,500,000
Vista Ridge	47,400,000
Bernards 78	42,075,000
Tempe Commerce	39,900,000
Inland Empire	26,300,000
Great Southwest	24,900,000
49 Stevenson	23,000,000

A complete listing of the portfolio's holdings can be obtained by contacting the Ohio Police & Fire Pension Fund at 614-228-2975.

### 3. Schedule of Investment Results

For Year Ended December 31, 2002

	Annualized Rates of Return		
	1-Year	3-Year	5-Year
<b>U.S. Equity</b>			
OP&F	-19.81%	-10.37%	-0.12%
Wilshire 5000	-20.86%	-14.37%	-0.86%
<b>Int'l Equity</b>			
OP&F	-17.70%	-19.95%	-2.69%
MSCI EAFE	-15.94%	-17.24%	-2.89%
<b>Emerging Markets</b>			
OP&F	-8.69%	-14.82%	NA
MSCI EMF Index	-6.00%	-13.96%	NA
<b>Fixed Income</b>			
OP&F - Core	8.60%	10.70%	7.95%
Lehman Aggregate	10.26%	10.10%	7.54%
OP&F - High Yield	4.12%	NA	NA
CSFB Developed Countries HY	3.06%	NA	NA
<b>Real Estate (one quarter in arrears)</b>			
OP&F	5.70%	8.92%	11.64%
Wilshire Real Estate Fund	3.44%	4.56%	7.99%
NCREIF	5.60%	9.10%	11.40%
<b>Private Equity (one quarter in arrears)</b>			
OP&F	-21.61%	-2.17%	5.45%
Wilshire 5000 + 5%	-12.52%	-7.75%	3.48%
<b>Total Portfolio</b>			
OP&F	-9.90%	-5.03%	2.09%
* Interim Policy Index	-10.81%	-6.99%	1.58%

\* Interim Policy Benchmark - 48% of Wilshire 5000, 18% of Lehman Aggregate, 17% of MSCI EAFE Index, 8% of Wilshire Real Estate Fund, 3% MSCI Emerging Markets Free, 5% CSFB Dev. Countries HY, 1% Wilshire 5000 + 5%



## 4. Investment Consultants and Money Managers

### *Investment Consultants*

Wilshire Associates  
The Townsend Group

### *Investment Managers—Private Equity*

Abbott Capital Management, LLC  
Alpha Capital Partners Ltd.  
Athenian Venture Partners  
Blue Chip Venture Partners, LP  
Blue Point Capital Partners, LP  
Brantley Venture Partners  
Chemicals & Materials Enterprise Associates  
Harbourvest Partners, LLC  
Horseley Bridge Partners, LLC  
Landmark Equity Partners  
Lexington Capitol Partners  
Linsalata Capital Partners  
MV Economic Development, Ltd.  
Morgenthaler Venture Partners  
Northcoast Fund, L.P.  
Northwest Ohio Venture Fund General  
Park Street Capitol  
Peppertree Partners, LLC  
Primus Venture Partners  
Wilshire Private Markets, LLC

### *Investment Managers—International Equity*

Capital Guardian Trust Company  
Capital International Inc.  
Lombard Odier International Portfolio Mngt, Ltd.  
Montgomery Asset Management  
Zurich Scudder Investments  
SSB Citi Asset Management Group  
State Street Global Advisors

### *Investment Managers—US Equity*

Alliance Capital Management, LP  
American Express Asset Management Group, Inc.  
Boston Partners Asset Management, L.P.  
Columbis Asset Management  
Fidelity Management Trust Co.  
Harris Investment Management, Inc.  
Oak Associates Ltd  
State Street Global Advisors

### *Investment Managers—Real Estate*

AEW Capital Management  
Conning Asset Management  
DLJ Real Estate Capital Partners, Inc.  
GMAC Institutional Advisors  
Lend Lease Real Estate Investments, Inc.  
Lowe Enterprises  
Lubert-Adler Management Co., LLC  
Paine Webber Real Estate  
The RREEF Funds  
Walton Street Capital, LLC  
Westbrook Partners, LLC

### *Investment Managers—Fixed Income*

Mackay Shields, LLC  
Shenkman Capital Management, Inc.  
Western Asset Management  
W.R. Huff Asset Management Co., LLC

## 5. Schedule of Brokers' Fees Total 2002 Trading

For Year Ended December 31, 2002

<b>Broker Name</b>	<b>Fees Paid</b>	<b>Units Traded</b>	<b>Average Cost Per Unit</b>
Warburg Securities	\$794,612	61,244,000	\$0.013
Merrill Lynch	\$780,267	128,071,000	\$0.006
UBS Securities	\$452,469	20,284,000	\$0.022
Salomon Smith Barney	\$415,892	63,536,000	\$0.007
Capital Institutional Ser	\$400,328	8,083,000	\$0.050
Boston Institutional Serv	\$385,272	7,836,000	\$0.049
Lehman Brothers	\$360,275	12,072,000	\$0.030
Goldman Sachs	\$333,348	18,200,000	\$0.018
Credit Suisse First Boston	\$274,545	249,463,000	\$0.001
Morgan Stanley	\$251,265	40,142,000	\$0.006
Instinet	\$248,716	10,890,000	\$0.023
Bear Stearns	\$186,050	5,298,000	\$0.035
Investment Technology Group	\$174,930	9,307,000	\$0.019
JP Morgan	\$167,801	5,816,000	\$0.029
Bridge Co. - Clearing	\$116,194	2,423,000	\$0.048
Cazenove	\$87,593	3,970,000	\$0.022
Fox Pitt Kelton Inc.	\$87,116	2,718,000	\$0.032
HSBC	\$86,944	75,054,000	\$0.001
Deutsche Bank Securities	\$75,039	2,039,000	\$0.037
BancAmerica	\$74,163	1,511,000	\$0.049
Standard & Poors	\$69,306	1,490,000	\$0.047
Jefferies & Co., Inc.	\$67,248	1,432,000	\$0.047
Prudential Securities	\$65,698	1,255,000	\$0.052
Sanford C. Bernstein	\$63,336	1,325,000	\$0.048
Donaldson Lufkin & Jenrette	\$62,654	1,368,000	\$0.046
Lynch Jones	\$59,962	1,249,000	\$0.048
Cantor Fitzgerald & Co.	\$56,468	1,363,000	\$0.041
Morgan Grenfell and Co.	\$55,411	2,654,000	\$0.021
Factset Data Systems	\$53,062	1,309,000	\$0.041
SG Cowen Securities Corp	\$51,031	1,650,000	\$0.031
CIBC	\$46,082	928,000	\$0.050
Nomura Securities	\$46,023	2,424,000	\$0.019
Piper Jaffray	\$45,037	924,000	\$0.049
Edwards (A.G.) & Sons	\$44,410	844,000	\$0.053
First Tennessee Securitie	\$43,861	853,000	\$0.051
Legg Mason	\$41,180	814,000	\$0.051
Robert Baird	\$40,053	767,000	\$0.052
ABN Amro	\$39,702	1,512,000	\$0.026
Broadcort Capital Corp.	\$39,698	938,000	\$0.042
BT Alex Brown	\$36,672	733,000	\$0.050
Francis Maglio	\$36,419	1,561,000	\$0.023
Keefe Bruyette And Woods	\$32,440	626,000	\$0.052
Credit Agricole Indosuez	\$31,706	932,000	\$0.034
First Union Capital	\$30,382	579,000	\$0.052
Mid West Research	\$30,250	620,000	\$0.049
Weeden	\$29,270	578,000	\$0.051
Citation Group	\$25,436	552,000	\$0.046
C. L. King	\$23,127	395,000	\$0.059
Needham	\$23,116	462,000	\$0.050
First Analysis Securities	\$22,910	442,000	\$0.052
Broker's Fees Less Than \$20,000 each	\$757,574	398,513,000	\$0.002
<b>Total</b>	<b>\$7,822,343</b>	<b>1,159,049,000</b>	<b>\$0.007</b>

## 6. Investment Policy and Guidelines

### I. Introduction

The purpose of this Statement of Investment Policy and Guidelines is to define the framework for investing the assets of the Ohio Police & Fire Pension Fund (OP&F). This Statement is intended to provide general principles for establishing the goals of OP&F, the allocation of assets and the employment of outside asset management. The statutory authority of the Board is set forth in Sections 742.11 to 742.112 of the Ohio Revised Code and these policies are established and adopted as required under that authority.

The objectives of OP&F have been established in conjunction with a comprehensive review of the current and projected financial requirements. These objectives are:

- To have the ability to pay all benefit and expense obligations when due.
- To maintain the purchasing power of the current assets and all future contributions by maximizing the rate of return on Fund assets.
- To achieve and maintain a fully funded status with regard to the accumulated benefit obligation.
- To control costs of administering OP&F and managing the investments.

In order to achieve these objectives, the Board of Trustees will conduct itself in accordance with Sec. 742.11 of the Ohio Revised Code: “The Board and other Fiduciaries shall discharge their duties with respect to OP&F solely in the interest of the participants and beneficiaries.” These duties shall be carried out “with care, skill, prudence, and diligence under the circumstances then prevailing that a prudent person acting in a like capacity and familiar with such matters would use in the conduct of an enterprise of a like character and like aims.” All aspects of this statement should be interpreted in a manner consistent with OP&F’s objectives. The Board shall adopt in regular meetings, policies, objectives or criteria for the operation of the investment program at least annually.

### II. Definition of Responsibilities

#### A. BOARD of TRUSTEES’ RESPONSIBILITIES

- Establish the strategic investment policy for OP&F (asset allocation) and periodically review policy in light of any changes in actuarial variables and market conditions.
- Select qualified consultants and investment managers to advise on and manage OP&F’s assets.
- Monitor and review the performance of selected managers to determine achievement of goals and compliance with policy guidelines.
- Monitor the costs of the investment operations on a semi-annual basis.

#### B. INVESTMENT COMMITTEE RESPONSIBILITIES

- Review, on a continuing basis, the current Investment Policies of OP&F and make changes as appropriate.
- Review the annual investment plan prepared by the staff. As conditions warrant, revise the annual investment plan as the year progresses.
- Monitor the monthly investment activity for compliance with Board policies and adherence by investment managers to strategy and direction.
- Review the overall performance to determine whether it meets the benchmarks established by the Board and report its findings to the whole Board.
- Review suggested changes or additions to the functions and operations regarding the Investment operations of similar institutional investors and report to the whole Board.
- Report its activities and recommendations to the full Board following each committee meeting.

#### C. STAFF RESPONSIBILITIES

- Manage OP&F assets under its care, custody and/or control in accordance with the Investment Policy Statement objectives and guidelines set forth herein.
- Monitor both internally & externally managed assets to ensure compliance with guidelines set forth in this policy statement.
- Promptly vote all proxies and related actions in a manner consistent with the long-term interests and objectives of the Plan set forth herein. Maintain detailed records of said voting of proxies and related actions and comply with all regulatory objectives related thereto.
- Report to the Board quarterly regarding the status of the portfolio and its performance for various time periods. Meet with the Board at least annually to report on their performance and compliance with goals and objectives.
- Acknowledge and agree in writing to their fiduciary responsibility to fully comply with the entire Investment Policy Statement set forth herein, and as modified in the future.

#### D. INVESTMENT CONSULTANTS’ RESPONSIBILITIES

- Provide independent and unbiased information.
- Assist in the development of Investment Policy Statement.
- Monitor compliance with Investment Policy Statement.
- Assist in the development of strategic asset allocation targets.
- Assist in development of performance measurement standards.
- Monitor and evaluate manager performance on an ongoing basis.

- Conduct due diligence when a manager fails to meet a standard.
- Establish a procedural due diligence search process.
- Conduct manager searches when needed for policy implementation.

#### E. INVESTMENT MANAGERS' RESPONSIBILITIES

- Manage OP&F assets under its care, custody and/or control in accordance with the Investment Policy Statement objectives and guidelines set forth herein.
- Exercise full investment discretion over the assets in their care within the guidelines set forth in this policy statement and the specific guidelines established for the manager.
- Promptly inform the Board and staff in writing regarding all changes of a material nature pertaining to the firm's organization and professional staff.
- If directed, promptly vote all proxies and related actions in a manner consistent with the long-term interests and objectives of OP&F set forth herein. Each manager designated to vote shall keep detailed records of said voting of proxies and related actions and will comply with all regulatory obligations related thereto.
- Report to the Board quarterly regarding the status of the portfolio and its performance for various time periods.
- Meet with the Board at least annually to report on their performance and compliance with goals and objectives.
- Acknowledge and agree in writing to their fiduciary responsibility to fully comply with the entire Investment Policy Statement set forth herein, and as modified in the future.

### III. Asset Allocation

It is the responsibility of the Board to determine the allocation of assets among distinct capital and private markets. The allocation will be completed in a manner consistent with commonly recognized financial principles. Application of these principles is expected to lead to a portfolio with the highest level of return consistent with the risk tolerance of OP&F.

The procedure for determining the allocation will consider the relevant characteristics of the liabilities and potential assets of OP&F. The liability considerations shall include, but not be limited to, current and expected future values of the benefits, contributions and total assets. These factors are important for identifying the investment horizon of OP&F and its cash flow requirements. The asset characteristics considered shall include, but not be limited to, the potential return relative to the potential risk.

The asset allocation must be consistent with the investment standards specified in Section 742.11 of the Ohio Revised Code.

Based on an asset allocation and liability study, which analyzed the expected returns of various asset classes, projected liabilities and the risks associated with alternative asset mix strategies, the Board has established the following asset allocation:

Asset Class	Target Allocation (%)	Range (%)
Domestic Equity	46	± 5
International Equity	17	± 2
Domestic Fixed Income	18	± 2
High Yield	5	± 2
Real Estate	8	± 2
Emerging Markets	3	± 2
Private Equity	3	± 2
Cash Equivalents	0	+ 0.5
<b>Total</b>	<b>100%</b>	

The study has shown that this is a favorable asset mix for meeting longer-term goals under both good and bad market conditions.

The asset allocation represents a long-term strategy. Short-term market shifts may cause the asset mix to drift from the allocation targets. Should the target percentage fall out of the indicated range for a particular asset class, the Board will cause the staff and investment manager(s) to rebalance from the over-allocated class to the under-allocated class.

### IV. Performance Expectations

The most important expectation is the achievement of results consistent with this Policy Statement and the analysis set forth in the asset allocation study of April 2000. A long-term 4% annualized real rate of return (net of inflation as measured by the Consumer Price Index) is a reasonable expectation in light of this policy. Long-term is defined as a market cycle (generally 3-5 years).

OP&F shall also strive to achieve a long-term rate of return, which is equal to or greater than the actuarial rate assumption. The Board expects the total fund to rank in the top half of a comparable public fund universe.

OP&F shall attempt to achieve these return goals without unnecessary risk to principal. The risk/return characteristics of OP&F shall be reviewed on a periodic basis (no less than every five years) through a comprehensive asset allocation and liability study. The goal of the study shall be to formulate a portfolio which maximizes return while minimizing overall risk through the most efficient combination of legal asset classes.

## V. Investment Implementation

The implementation of an investment portfolio designed to achieve the above objectives must be consistent with governing statutes as specified in Sections 742.11 to 742.112.

An Investment Committee composed of three or more Board members shall be responsible for working closely with the Investment Staff in conjunction with the advisors, and shall make recommendations to the Board on investment matters.

Where appropriate, OP&F will invest assets through the use of qualified investment managers. The allocations to these managers will be made in accordance with the results of the Asset Allocation process and established procedures.

The Board, in conjunction with the Consultant, will establish specific search procedures, including the specification of minimum criteria for the selection of new qualified investment managers, to implement the strategic asset allocation plan. Among the criteria to be used for screening purposes will be assets managed, manager style, track record, staff, communication, fees, risk/reward statistics, etc. All managers, with the exception of emerging management firms that may warrant specialized criteria, must meet the criteria established by the Investment Committee. The Investment Manager Search Policy is included later in this Policy as Section XI.

The Board shall give equal consideration to minority owned and controlled firms and firms owned and controlled by women which otherwise meet the criteria established by the Board. Ohio based firms shall also be given consideration, providing that specified criteria are met.

## VI. Specific Guidelines

### A. DOMESTIC EQUITY

#### *Investment Objectives*

- Total return of the managed equity portfolio should exceed the return of the Wilshire 5000 Index over a three-year period on an annualized basis.
- Total return of each manager's portfolio should rank above median when compared to their peer groups (growth, value) over a three-year period on an annualized basis and should exceed their benchmark return as specified in each manager's guidelines.

#### 1. Large Capitalization Specialist Managers

The Board of Trustees has determined that diversification of the equity asset base into large capitalization companies will offer the opportunity for enhanced returns, while lessening overall risk through increased diversification. Assets eligible to be managed in this class of investments will be found in the Ohio Revised Code Sec. 742.11.

The following objectives and guidelines shall apply:

- Eligible equity purchases include all US stocks with exceptions when approved by the Board of Trustees and as delineated in the managers' guidelines.
- The main focus of investing will be on companies with market capitalizations included in commonly accepted large capitalization indices.
- No single holding shall account for more than 6% of the entire portfolio at market, or 5% of the outstanding common stock of any one corporation, unless otherwise approved by the Board of Trustees.
- Specialist managers shall be subject to all other investment provisions listed under Sec. 742.11 that are not specifically mentioned above.
- Trading shall be left to the discretion of the investment manager with the exception that OP&F may direct a reasonable amount of commissions to help defray expenses.
- Cash equivalent positions shall be limited to a maximum of 5% unless otherwise approved by the Board of Trustees.
- Derivatives whose underlying asset is allowed by statute may be used in the management of the portfolio.

#### 2. Small/Mid Capitalization Specialist Managers

The Board of Trustees has determined that diversification of the equity asset base into small capitalization and mid-range capitalization companies will offer the opportunity for enhanced returns, while lessening overall risk through increased diversification. The structure of this asset class shall consist of several complementary style managers with a demonstrated 'growth' and 'value' style of investing.

The following objectives and guidelines shall apply to the asset class:

- The guidelines, which apply to the large cap specialist managers, shall also apply to the small/mid cap managers except that;
- The main focus of investing will be on companies with market capitalizations included in commonly accepted small to mid capitalization indices.

### B. INTERNATIONAL

OP&F will allocate a portion of the investment portfolio to international securities in accordance with allowable limits. This is intended to enhance the overall return of the portfolio while lowering risk through increased diversification. The structure of the international equity allocation will be diversified among three approaches: passive and active developed markets and active emerging markets. Trading shall be left to the discretion of the investment manager.

#### *Passive International Equity Investments*

The passive component has a target allocation of one-third of the International developed markets allocation. This is an index fund portfolio intended to provide diversification to OP&F's U.S. investments through holdings in non-U.S. equities and is to be constructed so as to match the return of



the Morgan Stanley Capital International Europe, Australia, Far East Index. Non-U.S. equity securities in EAFE countries are authorized. The manager will have the MSCI-EAFE Index as a benchmark.

#### *Active International Equity Investment*

The active component has a target allocation of two-thirds of the International developed markets allocation and will be divided among at least three managers. These will be discretionary portfolios intended to provide diversification to OP&F's U.S. investments as well as OP&F's passive EAFE Index manager.

For each active manager, the use of American Depository Receipts (ADRSs) and Global Depository Receipts (GDRs) will be limited to 20% of the portfolio.

While the geographic and economic sector diversification will be left to the manager's discretion, the portfolio shall be appropriately diversified as consistent with the manager's stated investment approach.

The investment managers may enter into forward exchange or futures contracts on currency provided that use of such contracts is designed for defensive purposes.

#### *Investment Objectives*

- Total return of the active equity portfolios should exceed the return of the MSCI EAFE Index over a three-year period on an annualized basis.
- Total return of each manager's portfolio should rank above median when compared to their peer groups over a three-year period on an annualized basis and should exceed their benchmark return as specified in each manager's guidelines.

#### *Emerging Markets*

The emerging markets allocation will be implemented as a distinct mandate with a separate allocation. The allocation will be divided between at least two active managers. In order to minimize the administrative and transaction costs of emerging market investing, commingled investment vehicles will be utilized. Sector and security selection, portfolio structure, and timing of purchases and sales are delegated to the Manager subject to policies established by the commingled funds.

#### *Investment Objectives*

- Total return of the active equity portfolios should exceed the return of the MSCI Emerging Markets Free Index over a three-year period on an annualized basis.
- Total return of each manager's portfolio should rank above median when compared to their peer groups over a three-year period on an annualized basis and should exceed their benchmark return as specified in each manager's guidelines.

### **C. Fixed Income**

It shall be the responsibility of the Investment Staff to give careful consideration to the needs of the system in its recommendation for bond investments, emphasizing relative value, quality and, to a lesser extent, liquidity. The Board may also retain external investment managers for this purpose.

The portfolio shall be actively managed in an effort to outperform the Lehman Aggregate Index over a market cycle. The effective duration of the portfolio shall not deviate beyond + or - 20% from that of the benchmark, unless otherwise approved by the Board of Trustees.

In order to qualify for inclusion in the fixed income portfolio, securities shall be rated "BBB-" or better by two standard rating services at the time of purchase.

No more than 10 percent of the fixed income portfolio may be invested in the securities of any one issuer, and no more than 5 percent in any one issue on a dollar duration basis, with the exception of United States Government or Agency securities.

Investments in high risk derivatives are prohibited. Low risk mortgage derivatives are permitted.

Cash equivalents positions shall be included in the calculation of the portfolio's effective duration.

#### *Investment Objectives*

- Total return of the active fixed income portfolios should exceed the return of the Lehman Aggregate Index over a three-year period on an annualized basis.
- Total return of each manager's portfolio should rank above median when compared to their peer groups over a three-year period on an annualized basis and should exceed their benchmark return as specified in each manager's guidelines.

### **D. HIGH YIELD BONDS**

The Board of Trustees has determined that the inclusion of high yield bonds into the portfolio will enhance the overall return of the portfolio while lowering risk through increased diversification. The Board will utilize active management in this asset class to minimize the probability of exposure to securities in default.

The following objectives and guidelines shall apply:

- The primary investment in the portfolio will be fixed income securities issued by US corporations with a minimum credit rating of CCC or equivalent. Investments are not allowed in emerging market debt or non-US dollar denominated bonds.
- No more than 10% of the entire portfolio at market shall be invested in securities of a single issue or issuer, unless otherwise approved by the Board of Trustees.

- The portfolio will be diversified by economic sector; however, the diversification restrictions will be tailored for each investment manager consistent with the manager's stated investment approach.
- Investments in Rule 144A securities are allowed while investments in non-Rule 144A private placements are limited to 5% of the entire portfolio at market.

#### *Investment Objectives*

- Total return of the high yield portfolio should exceed the return of the CS First Boston Domestic Plus High Yield Index over a three-year period on an annualized basis.
- Total return of each manager's portfolio should rank above median when compared to their peer groups over a three year period on an annualized basis and should exceed their benchmark return as specified in each manager's guidelines.

### **E. REAL ESTATE**

OP&F has adopted Strategic and Investment Plans that provide for the completion of OP&F's allocation to real estate.

The role of real estate in OP&F's portfolio is to provide an inflation hedge and a return that negatively correlates with stock and bond returns, thereby reducing the volatility and risk of the total portfolio. Also, real estate must provide a total return that is competitive on a risk-adjusted basis with stocks and bonds. OP&F is primarily interested in investing in core properties (i.e., operating, substantially leased, well located, institutional quality in the traditional property types which include office, apartment, retail and industrial). They generally offer relatively high and more predictable current income returns. OP&F will, however, consider investments in non-core properties to capture superior risk-adjusted returns caused by imbalances in the real estate and capital markets. To access these opportunities, OP&F will make investments in institutional properties, which may present a higher level of risk including leasing, renovation, development, re-positioning, distressed assets, international and a degree of business or operating risk (e.g., hotels, senior housing, etc.). The investment strategy typically is to cure the identified deficiency, increase cash flow and capture the premium through a short term hold. OP&F's preferred investment vehicle is a separate account because it affords OP&F the highest degree of control over its investments. OP&F also prefers to own 100% of each core property investment. Commingled fund investments will be made to allow OP&F to invest in higher return, higher risk assets and in extraordinarily large properties. OP&F employs a number of risk management strategies to minimize portfolio return volatility. These strategies include diversification by property type, by geographic location, by size of individual investments and by advisors. Leverage will be utilized only if acceptable debt service coverage, loan to value ratios and other protection can be provided. The maximum debt to equity ratio is 1:1 and 2:1 for and individual asset.

#### *Investment Objectives*

The performance objective for real estate is to produce a total return, prior to investment advisor fees equal to the NCREIF Property Index plus 100 basis points measured over rolling three-year periods.

### **F. COMMERCIAL MORTGAGES**

The Board of Trustees has determined that inclusion of Commercial Mortgage Investments secured by real estate may, depending on market circumstances, enhance the risk/return characteristics of OP&F. Therefore, the allocation to this asset class shall be targeted at 0% of OP&F's total investable assets, but will allow for up to a 2% allocation, which shall be included within the Fixed Income allocation.

Commercial Mortgage investments provide for fixed income payments derived from underlying property cash flows. Flexibility in investing in commercial mortgage backed securities or whole loans shall be provided. Risk shall be controlled through diversification strategies and the retention of qualified managers with acceptable loan underwriting and/or commercial mortgage acquisition experience.

#### *Investment Objectives*

The benchmark return for the commercial mortgage portfolio, consistent with investment risk, is a real rate of return of four percent, net of investment management fees, over rolling ten-year periods.

The policies and guidelines set forth in OP&F's "Commercial Mortgage Strategic and Investment Plan" are incorporated herein by reference.

### **G. PRIVATE EQUITY INVESTMENTS**

The private equity class of investments is designed to provide an attractive risk adjusted rate of return to benefit OP&F. By its very nature, it possesses a long-term investment horizon, liquidity and a high degree of risk.

To assist in diversifying the risks of this asset class, OP&F shall invest only in eligible private equity partnerships or funds and shall avoid individual direct company investments.

For these reasons, this asset class is limited to 3% of the overall Fund and expected returns should exceed those of other asset classes.

#### *Investment Objectives*

OP&F seeks a long-term target return of 5% greater than the Wilshire 5000 Index net of fees.

### **H. CASH EQUIVALENTS**

To provide effective cash management when investing cash balances, emphasis shall be placed on the protection of principal through the purchase of higher quality money market instru-



ments, while at the same time attempting to achieve the highest available return.

Short-term investments may be made in commercial paper, which shall at the time of purchase be rated within the two highest classifications established by two standard rating services. Treasury obligations, certificates of deposits, banker's acceptances, or repurchase agreements may be purchased with the responsibility resting on the Investment Staff regarding the selection of the specific type of investment at any given point in time. These obligations shall mature within 270 days of the date of purchase.

## VII. Proxy Voting

OP&F's Board of Trustees believes that common stock proxies are valuable and should be voted in the long-term interests and objectives of the Plan set forth herein. Each manager, staff or individual that exercises a proxy vote shall keep detailed records of said voting of proxies and related actions and will comply with all regulatory obligations related thereto and the policies set forth in the Board's "Proxy Voting Policy Statement."

Common stock proxies may be executed by the Sr. Investment Officer and the Chief Investment Officer, or their designees, and by designated outside money managers.

The internal staff shall provide a semi-annual summary report of proxy voting actions to the Investment Committee.

## VIII. Securities Lending

The investment objective for the securities lending program is to generate incremental income within a high quality investment program that safeguards the return of principal, maintains adequate daily liquidity, ensures diversification and tightly controls exposure to fluctuating interest rates.

The program may be operated by a bank trustee or a third party lending agent. Marking to market shall be performed daily and a minimum of 102% collateral shall be diligently maintained.

Securities lending reports shall be provided quarterly by the agent to the Investment Committee detailing investment instruments utilized and the appropriate breakdown of revenues.

## IX. Investment Monitoring and Evaluation Policy

The purpose of the OP&F Investment Manager Monitoring and Evaluation Policy is to establish the process and discipline for managing the investment manager relationship. The policy states the process, responsibilities and important factors for

consideration in the monitoring and evaluation process.

The successful monitoring and evaluation of managers depends on synthesizing a multi-faceted array of investment factors, including historical data and forward looking characteristics that are often linked. The process must also examine the investment manager's business capabilities and ability to attract and retain investment and support professionals. The Policy seeks to examine all material information about OP&F's investment managers that may materially impact the relationship and investment objectives of the Board.

OP&F will consider, but not be limited, to the following factors in monitoring and evaluating its investment managers:

- A. Stability and experience of firm in the investment product;
  1. Stability of the firm, as measured by the quality of the organizational structure of the firm; the existence of, or potential for, significant developments in the firm; and the expected financial stability of the firm.
  2. Experience of the firm in providing investment management services to similar institutional investors, as measured by the firm's history of providing such services.
  3. Ownership of the firm, as measured by the depth and structure of the incentive programs and the ownership type for key investment professionals in the subject product.
  4. Firm commitment to improvement as measured by whether or not there is a clear business plan/strategy, reinvestment in the firm with an overall commitment for enhancements/improvements.
  5. Adverse organizational issues, as measured by the existence of litigation or other investigations; and the existence of financial problems.
- B. Quality, stability, depth and experience of investment professionals;
  1. Experience of portfolio manager(s) in providing similar services to similar institutional investors, as measured by the length of time the portfolio manager(s) has served as a portfolio manager to such investors; demonstrated expertise in providing such services to other such investors.
  2. Stability of the firm's professional base, as measured by personnel turnover.
  3. Depth of personnel, as measured by the firm's account/portfolio manager and account/investment management personnel ratios; and back-up procedures for providing services to OP&F in the absence of the portfolio manager(s).
- C. Client service and relationships;
  1. Assets under management, as measured by the amount in the subject product as well as the experi-

ence of managing other similar asset class products.

2. The similarity of a firm's clients to OP&F, as measured by the amount of institutional tax-exempt assets under management and the size of the individual accounts currently under management.
3. Stability of the firm's client base, as measured by the number of accounts gained or lost.
4. Procedures for client contact, timely reporting, compliance monitoring, reconciliation process with OP&F's custodian and responsiveness to reporting data and formatting requirements.

D. Investment philosophy and process;

1. Defined philosophy and process implementation, as measured by whether the philosophy is effectively communicated and what the process is and why it works. It should be identified as to whether the process is based on sound research and whether or not they are focusing on temporary or permanent inefficiencies in the market.
2. Portfolio construction process, as measured by whether or not the manager is benchmark oriented such that there are distinct portfolio objectives and on-going monitoring relative to these objectives. It should be identified as to whether the process contains risk controls, and if so, are they part of a disciplined process and who is performing the monitoring.
3. Research, as measured by whether there are appropriate resources given the product style, whether the research performed is qualitative or quantitative, and whether or not there are separate research departments by product type or one fully integrated research staff.
4. Sources of information, as measured by whether the data used in the process is collected and/or assimilated by outside organizations or generated internally and how the information is processed and interpreted.

E. Investment performance and risk control;

1. The investment manager's alpha for active managers and tracking error for passive managers relative to the target benchmark. Active managers will also be expected to rank in the top half of managers with similar objectives over a 3 to 5 year period, if available. Additional focus will be placed on return/risk ratios and information ratios which incorporate both absolute and manager specific risk.

F. Investment fees;

1. Investment management fees shall be competitive and of an appropriate structure for the product type and assets under management.

## MONITORING RESPONSIBILITIES

It is important for the roles of the participants in the implementation of this Policy be clear and delineated. The following is intended as a guide to reflect the overall framework for the participants in the process. Participant responsibilities may vary from time to time.

**Board**—Responsible for the overall management of OP&F and investment manager relationship. Staff and consultant will provide the Board with periodic updates on the investment structure, overall investment manager performance and compliance with guidelines.

**Investment Committee**—Responsible for the overall management of OP&F's investment program. This shall include ongoing review of the asset allocation plan, investment structure, investment performance and other related issues. The Committee shall be responsible for recommending investment policies and procedures and shall assign investment managers to a monitoring category (except that only the Board may assign categories 4 and P4, termination).

**Staff**—Responsible for the day-to-day management of this Policy and the investment manager relationship, including investment reporting and investment guideline compliance. Staff will report all material manager issues to the consultant for review and to the Board for its consideration.

**Investment Consultant**—Responsible for assisting the staff and Board in establishing strategic investment policy and strategy. The consultant will monitor the consistency of investment manager mandates with the investment objectives, investment manager guidelines and will prepare quarterly performance measurement reports. The consultant will report all material investment manager issues to the staff and Board.

**Investment Manager**—Responsible for managing the investment portfolio within the objectives and guidelines established by the Board. The investment manager is responsible for self-monitoring of the portfolio and notifying the staff when there are any deviations from the guidelines and when modifications to the guidelines may be appropriate. The investment manager is responsible for the quality and timeliness of its reporting, including the reconciliation of its portfolio with OP&F's custodian.

## FREQUENCY OF MONITORING

The investment manager's performance, risk and portfolio characteristics will be monitored on a monthly/quarterly basis, or more frequently, and will be evaluated relative to the Board approved investment manager guidelines and objectives.

## MANAGER MONITORING CONCLUSIONS

The Board seeks long-term and successful relationships with its investment managers. The monitoring process is intended to ensure the success of the relationship. All investment

managers will be assigned, as noted above, to one of the following categories, which will be reviewed by the Investment Committee at least annually:

1. Retain the investment manager with no material changes in the relationship;
2. Retain the investment manager with issues of a non-material nature to be noted and monitored on a regular basis;
3. Retain the investment manager and place on probation with specific material issues identified and a plan and time period developed to resolve issue; and
4. Terminate the investment manager relationship and redeploy the assets.

Where potentially material and adverse issues arise in OP&F's current investment manager relationships, the Investment Committee will review the issues and may re-assign the manager to another category in the case of 1-3 rating. The assignment of a 4 rating must be approved by the Board.

Once a manager has been downgraded, they may not be upgraded for at least 6 months. During this time period the reasons for the rating downgrade will be evaluated thoroughly by the staff and the manager's progress on their corrective action plans will be followed. Although managers will be prohibited from obtaining a rating upgrade within 6 months of a rating downgrade, a manager may be further downgraded or recommended for termination at any time.

In conjunction with the annual manager evaluation conducted by the staff and the Investment Committee, the following review schedule will be followed for managers rated either a '2' or '3':

'2' —The staff and the Investment Committee will review manager performance and the issues which resulted in the rating downgrade at least every 6 months until the rating has been upgraded to a '1'. Further downgrading to a '3' will result in the review schedule noted below:

'3' —Due to the severity of this rating, quarterly reviews will be conducted of managers rated a '3'.

When deemed necessary by the staff or Investment Committee, managers will be requested to attend these reviews.

In the case of investment managers or general partners who act as managers of private, essentially non-marketable, investment vehicles such as private equity and commingled real estate investment funds, all investment managers will be assigned, as noted above, to one of the following categories which will be reviewed by the Investment Committee at least annually:

- P1. The investment manager may be considered for future assignments.

P2. The investment manager has specific material issues which need to be resolved before the manager may be considered for future assignments.

P3. The investment manager may not be considered for future assignments.

P4. Removal of the investment manager or sale of our interest should be actively pursued and acted upon if in the best interest of OP&F.

Where potentially material and adverse issues arise in OP&F's current investment manager relationships, the Investment Committee will review the issues and may re-assign the manager to another category in the case of a P1-P3 rating. The assignment of a P4 rating must be approved by the Board.

#### **TERMINATION OF AN INVESTMENT MANAGER**

The Board will review the adverse material issues and circumstances prior to terminating an investment manager. The major issues to consider will include:

- Longer term prospects of the investment manager in correcting the issue;
- Potential changes in the relationship;
- The cost of termination;
- Replacement alternatives; and
- How the investment manager's assets will be redeployed.

#### **MANAGER DUE DILIGENCE VISITS**

The staff will meet with those investment managers whose performance falls below the 70th percentile relative to their peers for all of the following: current quarter; year-to-date; and trailing one year time periods. The staff will also meet with investment managers for non-performance issues that are material to the relationship, including but not limited to: firm or investment product stability, key professional turnover, client service and investment reporting.

### *X. Communications*

Each manager will provide hard copy reports at least quarterly, including performance measurement, asset inventories, transaction summaries, market commentary or anything else deemed significant at the time of reporting. Each manager is expected to meet with OP&F's Board at least annually, unless notified otherwise.

### *XI. Investment Manager Search Policy*

The selection of investment managers will be conducted only under a Request for Proposal (RFP) process that will consider the following issues:

- A. The investment strategy for the manager search will be considered within the strategic asset allocation plan, investment structure and other applicable investment policies and procedures approved by the Board.
- B. The RFP minimum criteria will be consistent with the search investment strategy and will be established by the Investment Committee, with the assistance of staff and the investment consultant. The selection criteria may include such items as:
1. Stability and experience of firm in the investment product;
    - a. Stability of the firm, as measured by the quality of the organizational structure of the firm; the existence of, or potential for, significant developments in the firm; and the expected financial stability of the firm.
    - b. Experience of the firm in providing investment management services to similar institutional investors, as measured by the firm's history of providing such services.
    - c. Ownership of the firm, as measured by the depth and structure of the incentive programs and the ownership type for key investment professionals in the subject product.
    - d. Firm commitment to improvement as measured by whether or not there is a clear business plan/strategy, reinvestment in the firm with an overall commitment for enhancements/improvements.
    - e. Adverse organizational issues, as measured by the existence of litigation or other investigations; and the existence of financial problems.
  2. Quality, stability, depth and experience of investment professionals;
    - a. Experience of portfolio manager(s) in providing similar services to similar institutional investors, as measured by the length of time the portfolio manager(s) has served as a portfolio manager to such investors; demonstrated expertise in providing such services to other such investors.
    - b. Stability of the firm's professional base, as measured by personnel turnover.
    - c. Depth of personnel, as measured by the firm's account/portfolio manager and account/investment management personnel ratios; and back up procedures for providing services to OP&F in the absence of the portfolio manager(s).
  3. Client service and relationships;
    - a. Assets under management, as measured by the amount in the subject product as well as the experience of managing other similar asset class products.
    - b. The similarity of a firm's clients to OP&F, as measured by the amount of institutional tax exempt assets under management and the size of the individual accounts currently under management.
  - c. Stability of the firm's client base, as measured by the number of accounts gained or lost.
  - d. Procedures for client contact, timely reporting, compliance monitoring, reconciliation process with OP&F's custodian and responsiveness to reporting data and formatting requirements.
  4. Investment philosophy and process;
    - a. Defined philosophy and process implementation, as measured by whether the philosophy is effectively communicated and what the process is and why it works. It should be identified as to whether the process is based on sound research and whether or not they are focusing on temporary or permanent inefficiencies in the market.
    - b. Portfolio construction process, as measured by whether or not the manager is benchmark oriented such that there are distinct portfolio objectives and on-going monitoring relative to these objectives. It should be identified as to whether the process contains risk controls, and if so, are they part of a disciplined process and who is performing the monitoring.
    - c. Research, as measured by whether there are appropriate resources given the product style, whether the research performed is qualitative or quantitative, and whether or not there are separate research departments by product type or one fully integrated research staff.
    - d. Sources of information, as measured by whether the data used in the process is collected and/or assimilated by outside organizations or generated internally and how the information is processed and interpreted.
  5. Investment performance and risk control;
    - a. The investment manager's alpha for active managers and tracking error for passive managers relative to the target benchmark. Active managers will also be expected to rank in the top half of managers with similar objectives over a 3 to 5 year period, if available. Additional focus will be placed on return/risk ratios and information ratios which incorporate both absolute and manager specific risk.
  6. Investment fees;
    - a. The total cost of performing investment advisory services as measured by the Fee Proposal based on a total account size. The managers in the search will be evaluated relative to each other as well as to a representative peer universe.
- C. The search may be on a closed or open manager universe basis. Closed universe searches shall be used only in circumstances where an expedited process is required to avoid material harm to OP&F or where there is approval

by a super majority of the Board (7 or more) to reconsider the finalists of a prior search concluded within the preceding two years. The retention of a manager in a closed universe search shall be subject to a due diligence review by the Investment Committee, staff and consultant. When reopening a prior search, due diligence shall be performed on those managers constituting the finalists of the original search.

- D. RFPs will be sent to managers identified as likely to meet the stated qualifications and to those requesting the RFP in an open universe search. An advertisement will be placed in an investment industry or national business publication in open universe searches. In closed universe searches, the Investment Committee shall approve all potential candidates with the assistance of the staff and consultant.
- E. Staff, with the assistance of the Board's investment consultant, will review all timely submitted RFPs to ensure that all search criteria have been met.
- F. Staff, with the assistance of the Board's investment consultant, will evaluate all RFPs having met established criteria and produce a written report summarizing the findings and manager rankings to the Investment Committee. The staff and consultant may produce separate reports to the Investment Committee where there may be material differences in findings or manager rankings.
- G. The Investment Committee will consider the staff and consultant report as well as other material information when determining the list of managers for finalist interviews.
- H. The staff and/or investment consultant may conduct a due diligence visit with the finalists prior to the finalist interviews.
- I. The Investment Committee will interview and evaluate the finalists with the assistance of staff and the investment consultant.
- J. Only the Investment Committee has authority to recommend managers to the Board for final consideration. The recommendations may also include information on the amount and timing of funding, investment guidelines and fees.
- K. The Board will approve or fail to approve the manager recommendations of the Investment Committee. The Board may approve, fail to approve or modify the amount and/or timing of funding, investment guidelines and fees of the approved managers.

## XII. Review Procedures

In addition to the regular performance reviews, the Board in conjunction with its consultant will review this policy statement at least once a year to determine if revisions are warranted.

It is not expected that investment policy will change frequently, in particular short-term changes in the financial markets should generally not require an adjustment in the investment policy.





## *Actuarial Section*

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- 1. Report of Actuary**
- 2. Summary of Actuarial Assumptions and Methods**
- 3. Active Member Valuation Data**
- 4. Retirants and Beneficiaries Added to and Removed from Rolls**
- 5. Short-Term Solvency Test**
- 6. Plan Summary**

# 1. Report of Actuary


**THE SEGAL COMPANY**

6300 S. Syracuse Way Suite 750 Englewood, CO 80111-7302  
 T 303.714.9900 F 303.714.9990 www.segalco.com

June 5, 2003

Board of Trustees  
 Ohio Police and Fire Pension Fund  
 140 East Town Street  
 Columbus, OH 43215

DIRECT DIAL NUMBER  
**303-714-9936**  
 WRITER'S E-MAIL ADDRESS  
**lthompson@segalco.com**

**Members of the Board:**

This letter is to certify that The Segal Company's preparation of the January 1, 2002 actuarial valuation report for the Ohio Police and Fire Pension Fund ("Fund") presents the actual position of the Fund. Actuarial valuations are prepared annually for the Fund for the purpose of measuring the Fund's actuarial liabilities and determining the progress made toward the funding objectives of the Board. The 2002 actuarial valuation is the first valuation performed by Segal for the Fund.

**Funding Objectives and Progress**

The actuary uses an actuarial cost method to determine the portion of the Fund's liabilities accrued by the members as of the valuation date and the portion that is attributable to future years of service. A rate of contribution necessary to systematically fund the future service liabilities, the normal cost rate, is calculated under the cost method to be a level percentage of active member payroll. The portion of the liabilities determined as accrued by the members is compared to a market-related value of the Fund's assets. The amount of liabilities in excess of the assets is called the unfunded actuarial accrued liability. The actuary determines how many years is required by the Fund to completely amortize the unfunded actuarial accrued liability, using the member and employer contributions reduced by the amount of normal cost for the year.

Section 742.16 of the Revised Code, as amended by Senate Bill No. 82, sets forth an objective that the number of years required to amortize the unfunded actuarial accrued liability (the amortization period) be not more than 30 years. If the amortization period exceeds 30 years, a plan shall be developed and presented by the Board of Trustees to reduce the period to not more than 30 years by the 2007 plan year.

The 2002 actuarial valuation results in an amortization period of 28 years, which compares to the 30-year amortization period developed in the 2001 actuarial valuation. The slight decrease is primarily attributable to the changes in assumptions and methods adopted by the Board as a result of the latest actuarial experience study.

**Actuarial Assumptions and Methods**

The actuarial assumptions and methods used in the January 1, 2002 actuarial valuation were recommended by The Segal Company and adopted by the Board. These assumptions and methods were based on the results of the 2002 experience study, using the experience data for the 5-year period ending December 31, 2001. These assumptions and methods were developed in accordance with the applicable Actuarial Standards of Practice, and meet the parameters proscribed in Government Accounting Standards Board Statement No. 25 for determining the annual required contribution.

**Benefits, Compensation and HR Consulting** ATLANTA BOSTON CHICAGO CLEVELAND DENVER HARTFORD HOUSTON LOS ANGELES MINNEAPOLIS  
 NEW ORLEANS NEW YORK PHILADELPHIA PHOENIX SAN FRANCISCO SEATTLE TORONTO WASHINGTON, DC



Multinational Group of Actuaries and Consultants AMSTERDAM BARCELONA GENEVA HAMBURG LONDON MELBOURNE MEXICO CITY OSLO PARIS



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June 5, 2003  
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#### Actuarial Valuation Data

The actuarial valuations are based upon census data and audited financial information submitted by the Fund. The Segal Company reviews the data for reasonableness. Information suspected of being in error is submitted to the Fund for correction. The benefit provisions valued in the valuation report reflect the status of the Ohio Revised Code as of the valuation date.

#### Supporting Schedules

The required supplementary information and actuarial schedules listed below were prepared by the Fund for the 2002 Comprehensive Annual Financial Report and include information from the 2002 actuarial valuation report prepared by The Segal Company. The prior year information included in trend data schedules are from prior valuation reports prepared by Wyatt.

- Schedule of Funding Progress
- Schedule of Contributions from Employers and Other Contributing Entities
- Notes to the Required Supplementary Information
- Schedule 2: Summary of Actuarial Assumptions and Methods; provided in Section 4, Exhibit V of the 2002 actuarial report.
- Schedule 3: Active Member Valuation Data; provided in Segal's 2002 actuarial report and prior actuarial reports prepared by Wyatt.
- Schedule 4: Retirants and Beneficiaries Added to and Removed from Rolls; provided in Segal's 2002 actuarial report and prior actuarial reports prepared by Wyatt.

Respectfully Submitted,

The Segal Company



Leslie L. Thompson, FSA, MAAA, EA  
Senior Vice President and Consulting Actuary



John J. Garrett, ASA, MAAA  
Vice President and Consulting Actuary

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## 2. Summary of Actuarial Assumptions and Methods

### A. INTEREST

A rate of 8¼% per annum, compounded annually. Adopted by the Board of Trustees in 1989.

### B. RATES AND OTHER ASSUMPTIONS

#### a) Mortality:

Mortality is based on the 1994 Group Annuity Mortality (sex distinct) Tables. Police include a five year set back for males and three year set forward for females. Fire include a seven year set back for males and a three year set back for females. The following rates at selected ages are illustrative:

Age	Rate of Mortality			
	Police		Fire	
	Male	Female	Male	Female
25	0.046	0.031	0.051	0.031
30	0.059	0.042	0.066	0.042
35	0.075	0.060	0.080	0.060
40	0.085	0.088	0.085	0.088
45	0.094	0.121	0.107	0.121
50	0.135	0.191	0.158	0.191
55	0.210	0.336	0.258	0.336

#### b) Termination:

The rates of termination are based upon the age and service tables. The following rates at selected ages are illustrative:

#### Withdrawal Rate (Police):

Age	Years of Service										
	0	1	2	3	4	5	6	7	8	9	10+
25	0.02440	0.02440	0.02475	0.02031	0.01745	0.01511	0.01420	0.01384	0.01218	0.01311	0.01311
30	0.02056	0.02056	0.02113	0.02012	0.01824	0.01608	0.01452	0.01355	0.01211	0.01168	0.01168
35	0.02309	0.02309	0.02400	0.02376	0.02158	0.01863	0.01601	0.01405	0.01230	0.01059	0.00959
40	0.03017	0.03017	0.03130	0.03043	0.02715	0.02279	0.01866	0.01532	0.01271	0.00969	0.00590
45	0.04104	0.04104	0.04204	0.03944	0.03458	0.02846	0.02247	0.01742	0.01337	0.00919	0.00311
50	0.02201	0.05500	0.05546	0.05012	0.04339	0.03543	0.02737	0.02041	0.01449	0.00957	0.00299
55	0.07155	0.07155	0.07112	0.06199	0.05322	0.04350	0.03327	0.02436	0.01621	0.01124	0.00737

#### Withdrawal Rate (Fire):

Age	Years of Service										
	0	1	2	3	4	5	6	7	8	9	10+
25	0.00530	0.00749	0.00864	0.00903	0.00858	0.00749	0.00607	0.00510	0.00453	0.00434	0.00434
30	0.00912	0.00882	0.00824	0.00749	0.00684	0.00632	0.00588	0.00549	0.00515	0.00483	0.00483
35	0.01145	0.00989	0.00866	0.00767	0.00714	0.00699	0.00699	0.00679	0.00631	0.00547	0.00417
40	0.01277	0.01082	0.00978	0.00931	0.00916	0.00923	0.00925	0.00893	0.00799	0.00628	0.00359
45	0.01308	0.01159	0.01161	0.01242	0.01293	0.01307	0.01269	0.01193	0.01022	0.00729	0.00312
50	0.01242	0.01218	0.01412	0.01700	0.01846	0.01851	0.01731	0.01581	0.01302	0.00850	0.00282
55	0.01082	0.01257	0.01728	0.02306	0.02575	0.02557	0.02310	0.02057	0.01640	0.00993	0.00272

#### c) Disability:

The rates of disability are based upon the 1994 Group Annuity Mortality Table (male only), Police include a six year set forward and Fire include a five year set forward. The following rates at selected ages are illustrative:

Age	Rate of Disability			
	Police		Fire	
	Male	Female	Male	Female
25	0.002	0.002	0.015	0.015
30	0.124	0.124	0.068	0.068
35	0.344	0.344	0.143	0.143
40	0.708	0.708	0.380	0.380
45	1.304	1.304	1.166	1.166
50	2.533	2.533	2.939	2.939
55	4.270	4.270	5.270	5.270

Note: The present values of future benefits for active members resulting from the use of these disability rates reflect the fact that the occurrence of disability by type approximates the following

	Police	Fire
On duty permanent and total	35%	35%
On duty partial	61	61
Off duty ordinary	4	4

**d) Salary Increase Rate:**

Salary increases included an inflation rate of 3% plus a productivity increase of 1% and service-graded promotional increases. Annual total salary increase shown below:

<b>Years of Service</b>	<b>Annual Total Salary Increase</b>
1 and less	11%
2	9.5
3	8.5
4	6.5
5 and more	5

**e) Retirement:**

The rates of retirement are based upon the 1994 Group Annuity Mortality Table (male only), set forward one year for all employees. These rates are applicable after the member has satisfied the conditions for retirement.

<b>Police</b>		<b>Fire</b>	
<b>Age(s)</b>	<b>Rate</b>	<b>Age(s)</b>	<b>Rate</b>
48	0.30	48	0.30
49 - 58	0.20	49 - 58	0.20
59 - 64	0.25	59 - 64	0.25
65	1.00	65	1.00

**C. PROBABILITIES AMONG SURVIVORS****1. Percent Married:**

85%

**2. Age of Spouse:**

Female (or male) spouses three years younger (or older) than their spouses.

**3. Dependent Children:**

No specific allowance has been made, in the calculation of this benefit, for the probability of mortality prior to age 18, or the probability of disability at age 18 and thereafter. In valuing the benefit beyond age 18, it is assumed that all the dependent children will be students and eligible for payments to age 22.

**4. Dependent Parents:**

Costs based upon allowance for mortality (same rate as for beneficiaries) but no specific allowance for change in dependency status.

**5. Number of Dependent Children:**

Each member is assumed to have two children, born when the

member was age 26. Dependency is assumed to cease when the child is 22.

**D. COLA ANNUITIES**

It has been assumed that where an election is possible, all members will elect the COLA annuity. It has also been assumed that the Consumer Price Index will increase each year at a rate equal to or greater than 3%.

**E. Administrative Expenses:**

The Normal Cost is increased by all pension administrative expenses budgeted, net of the State subsidy received.

**F. Actuarial Value of Assets:**

The difference between actual market value and expected market value is recognized over five years (20% per year). The actuarial value is the market value adjusted by the total unrecognized gains or losses incurred during the five year period, further adjusted if necessary to be within 10% of the market value for 2002 and 20% of the market value thereafter.

**G. Subsidy State Credit:**

The subsidy received from the State of Ohio during the valuation year is an offset to the Administrative Expenses.

**H. Actuarial Cost Method:**

Entry Age Normal Actuarial Cost Method. Entry Age is the age at the time the participant would have commenced participation if the plan had always been in existence. Normal Cost and Actuarial Accrued Liability are calculated on an individual basis and are allocated by service, with Normal Cost determined as if the current benefit accrual rate had always been in effect. For 2002 and future valuations, the Actuarial Accrued Liability is net of the present value of employer accrued liability, instead of being included in the valuation assets.

**I. Changes in Assumptions and Actuarial Cost Method :**

Based on the most recent experience study, the following changes in actuarial assumptions have been made since the last valuation. Details of these assumptions are shown in the experience study report.

*Mortality Rates:*

The 1994 Group Annuity Mortality Table was used for all rates. The assumption changes made were to the age adjustment and use of the female table.

*Withdrawal Rates:*

The change in assumption of an age related table in the prior year to an age and service related table for the current year.

*Retirement Rates:*

The rates decreased for some ages and increased for ages 59 and 60 under Police.

*Disability Rates:*

The rates decreased from the prior valuation.

*Occurrence of Disability:*

The assumptions (which are the same for Police and Firefighters), changed from the prior valuation as follows:

	<b>Prior Year</b>	<b>Current Year</b>
On duty permanent and total	20%	35%
On duty partial	76	61
Off duty Ordinary	4	4

*Salary Increases:*

The assumptions changed from an age related table for the prior year to a service related table for the current year.

*Dependent Children:*

Change in assumption from one-third of dependent children continue as students beyond age 18 to age 22, to all dependent children continue as students to age 22.

*Administrative Expense Loading:*

Change in assumption of the expense load to Normal Cost from the amount of pension administrative expense budgeted in excess of .05% of market value assets and net of the State Subsidy received, to loading the Normal Cost by all pension administrative expense budgeted, net of the State Subsidy received.

*Actuarial Cost Method:*

Change from the Fund to Decrement version of the Entry Age Normal Cost Method to the Fund to Maximum Retirement Age version of the Entry Age Normal Cost Method.

*Annual Valuation Payroll:*

Change from assuming that the member pay reported for the prior year increased by one-half a year of salary increase to assuming a full year of salary increase.

*Actuarial Value of Assets Methodology:*

The prior year method developed an actuarial value of assets under a four-year market Adjustment Method. The current year method calculates the assets under the five-year expected market value technique with a 10.0% corridor of the market value.

*Present Value of Employer Accrued Liability:*

For 2001, the present value of employer accrued liability was added to the Actuarial of Assets. For 2002, the present value of employer accrued liability was deducted from the Actuarial Accrued Liability.

### 3. Active Member Valuation Data

Actuarial Valuation as of Jan. 1	Number of Employers		Number of Active Members		Average Annual Salary		Percentage of Average Annual Salary Increases		Annual Payroll (Millions)
	Police	Fire	Police	Fire	Police	Fire	Police	Fire	
	1997	582	316	14,851	10,972	\$ 42,049	\$ 42,509	2.5%	
1998	616	354	15,247	11,316	43,561	44,077	3.6%	3.7%	1,190.9
1999	621	353	15,533	11,600	44,892	45,052	3.1%	2.2%	1,249.1
2000	590	350	15,775	11,867	47,241	47,416	5.2%	5.2%	1,338.5
2001	573	352	15,778	12,158	49,113	49,459	4.0%	4.3%	1,407.6
2002	559	354	15,877	12,451	54,335	54,402	7.8%	7.2%	1,534.3

### 4. Retirants and Beneficiaries Added to and Removed from Rolls

Year at Jan. 1	Police		Fire		Total Members at Year End	
	Additions	Removals	Additions	Removals	Police	Fire
	1997	760	400	666	358	11,537
1998	610	418	431	444	11,729	9,284
1999	878	445	636	348	12,162	9,572
2000	783	400	599	327	12,545	9,844
2001	842	455	614	377	12,932	10,081
2002	669	427	505	347	13,174	10,239

## 5. Short-Term Solvency Test

A short-term solvency test is one means of checking a system's progress under its funding program. In a short-term solvency test, the plan's valuation assets are compared with: 1) Active member contributions on deposit; 2) The liabilities for future benefits to present retired lives; 3) The liabilities for service already rendered by active members. In a system that has been following the discipline of level percent of payroll financing, the liabilities for active member contributions on deposit (liability 1) and the liabilities for future benefits to present retired lives (liability 2) will be fully covered by present assets

(except in rare circumstances). In addition, the liabilities for service already rendered by active members (liability 3) will be partially covered by the remainder of present assets.

Generally, if the system has been using level cost financing, the funded portion of liability 3 will increase over time.

Liability 3 being fully funded is very rare. Because OP&F changed its actuarial cost method from the aggregate method to the entry age normal method effective January 1, 1997, comparable solvency test data is not available for years prior to that date.

### Accrued Liabilities (\$ Amounts in Thousands)

	Valuation Year	(1) Active Member Contributions	(2) Retirants and Beneficiaries	(3) Active Members (Employer Financed Portion)	Valuation Assets	Portion of Accrued Liabilities Covered by Reported Assets		
						(1)	(2)	(3)
Police	1997	\$ 498,283	\$ 1,964,911	\$ 1,520,487	\$ 3,065,410	100%	100%	40%
Fire	1997	\$ 380,192	\$ 1,537,474	\$ 1,123,208	\$ 2,488,704	100%	100%	51%
Police	1998	\$ 524,911	\$ 2,214,921	\$ 1,634,939	\$ 3,431,556	100%	100%	42%
Fire	1998	\$ 405,865	\$ 1,683,441	\$ 1,233,600	\$ 2,799,863	100%	100%	58%
Police	1999	\$ 548,372	\$ 2,509,175	\$ 1,751,789	\$ 3,957,516	100%	100%	51%
Fire	1999	\$ 423,342	\$ 1,885,760	\$ 1,334,184	\$ 3,236,100	100%	100%	69%
Police	2000	\$ 603,980	\$ 2,674,691	\$ 1,840,992	\$ 4,330,425	100%	100%	57%
Fire	2000	\$ 467,926	\$ 1,987,723	\$ 1,420,252	\$ 3,574,761	100%	100%	79%
Police	2001	\$ 644,164	\$ 2,839,294	\$ 1,914,232	\$ 4,632,337	100%	100%	60%
Fire	2001	\$ 508,155	\$ 2,089,072	\$ 1,511,366	\$ 3,865,732	100%	100%	84%
Police	2002	\$ 699,146	\$ 3,099,628	\$ 1,711,626	\$ 5,110,025	100%	100%	77%
Fire	2002	\$ 551,227	\$ 2,275,967	\$ 1,448,172	\$ 3,996,417	100%	100%	79%

## 6. Plan Summary

### Purpose

The Ohio Police & Fire Pension Fund (OP&F) was established by the Ohio General Assembly to provide disability and pension benefits to members of OP&F and their surviving spouses, children, and dependent parents.

### Administration

The administration, control, and management of OP&F are vested in the Ohio Police & Fire Pension Board of Ohio which is comprised of nine members as follows:

- Three representatives of police departments
- Three representatives of fire departments
- One municipal fiscal officer, as appointed by the Governor
- The Auditor of State
- The Attorney General

The representatives of police and fire departments are elected for four-year terms by the members with one police and one fire position being a retired member or surviving spouse. The municipal fiscal officer is appointed by the Governor.

The Auditor of State and Attorney General serve by virtue of their office and are also members of other state retirement boards.

The Board appoints an executive director as the chief administrative officer of OP&F. The executive director oversees the daily activity of the staff.

### Membership

Membership in OP&F is mandatory under Ohio law for all full-time police officers employed by Ohio municipalities. Full-time firefighters employed by townships, municipalities, joint fire districts or other political subdivisions must become members of OP&F if satisfactory completion of a firefighter training course approved under former Section 3303.07, Section 4765.55 or conducted under Section 3737.33 of the Ohio Revised Code is required for employment.

### Contributions

Contributions are established by statute. Employers of police officers pay 19.5% of salary; employers of firefighters pay 24% of salary. Members contribute 10% of salary.

<sup>1</sup> *Average annual salary* means one-third of the total salary during the three years of highest earnings.

### Benefits

#### A. SERVICE RETIREMENT

Upon attaining a qualifying age with sufficient service credit, a member of OP&F may retire and receive a lifetime monthly cash pension.

##### 1. Normal Pension

- (a) Eligibility: Age 48 and 25 years of service.
- (b) Benefit: An annual pension equal to a percentage of the “average annual salary.” The percentage equals 2.5% for each of the first 20 years of service, 2% for each of the next five years of service, and 1.5% for each year of service in excess of 25 years, to a maximum of 72% of the “average annual salary.”

##### 2. Service Commuted

- (a) Eligibility: 15 years of service.
- (b) Benefit: Commencing at age 48 plus 25 years from full-time hire date, whichever is later; an annual pension equal to 1.5% of the average annual salary multiplied by the number of complete years of service.

##### 3. Age/Service Commuted

- (a) Eligibility: Age 62 and 15 years of service
- (b) Benefit: The same formula applies as for the normal service pension.

#### B. DISABILITY RETIREMENT

Members who become unable to perform their official duties and whose earning capacities are impaired may qualify for disability retirement benefits.

Disability retirement benefits are classified as either service-incurred (on-duty) or non-service-incurred (off-duty), and differ in eligibility requirements and benefit formulas. Annual medical evaluations are required for disability benefit recipients who would not have met the age and service requirements for normal service retirement unless an OP&F physician certifies the disability is ongoing and further evaluation would not be cost effective.

##### 1. Permanent and Total Disability (On-Duty)

- (a) Eligibility: No age or service requirement.
- (b) Benefit: An annual benefit equal to 72% of the average annual salary<sup>1</sup>.

##### 2. Partial Disability (On-Duty)

- (a) Eligibility: No age or service requirement.
- (b) Benefit: An annual benefit fixed by the Board of Trustees to be a certain percent of the average annual salary up to 60%. If the member has 25 or more years of service the annual disability benefit is equal to the accrued normal service pension.



**3. Non-service Incurred Disability (Off-Duty)**

- (a) Eligibility: Any age and five years of service.  
 (b) Benefit: An annual benefit is the percent awarded by the Board and may not exceed 60% of the average annual salary<sup>1</sup>. Service credit over 25 years cannot be used in calculating an off duty disability award.

**C. RIGHTS UPON SEPARATION FROM SERVICE****1. Deferred Pension**

If a member meets the service credit requirement for any service retirement pension but leaves service before attaining the required age, a pension becomes payable upon attainment of the qualifying age.

**2. Refund of contributions**

Upon separation from service, a member can receive the contributions made to the plan by himself or, on his behalf, by his employer. Employer contributions are not refundable.

**D. FLAT SURVIVOR BENEFITS****1. Eligibility:**

Upon death of any member of OP&F, active or retired.

**2. Benefit:**

- (a) Surviving Spouse's Benefit-An annual amount equal to \$6,600, plus an annual cost of living allowance of 3% of the original base, paid each July 1.  
 (b) Surviving Child-An annual amount equal to \$1,800, payable until such child attains age 18 or marries, whichever occurs first. The payment can continue to an unmarried full-time student until age 22. A dependent disabled child is entitled to a benefit regardless of age at time of member's death until marriage, death, or recovery. A cost-of-living allowance of 3% of the original base is payable each July 1.  
 (c) Dependent Parents-If there is no surviving spouse or children, an annual amount of \$2,400 is payable to one dependent parent or \$1,200 each to two dependent parents for life or until dependency ceases or remarriage. A cost-of-living allowance of 3% of the original base is payable each July 1.

**E. LUMP SUM DEATH BENEFIT**

On the death of a retired member of OP&F, a lump sum payment of one thousand dollars (\$1,000) is paid to the member's surviving spouse, or the estate if there is no surviving spouse.

**F. ANNUITIES**

Effective February 28, 1980, for those retiring on either service pensions or disability benefits, optional annuity plans can be chosen. Members can elect actuarially reduced benefits under a joint and survivor annuity or life annuity certain and continuous plans.

Effective April 25, 1984, Pre-retirement Survivor Annuity was added to the plan.

**Annuity Types****1. Pre-retirement Survivor Annuity**

- (a) Eligibility: Upon death before retirement but after having satisfied the requirements for normal service retirement.  
 (b) Benefit: The surviving spouse or contingent dependent beneficiary will receive the equivalent of a 50% joint and survivor annuity, calculated under the assumption that the decedent had retired effective the day following his death.

**2. Single Life Annuity**

For unmarried members, this is the normal annuity plan. Married members may elect this plan only if the spouse consents to the selection.

**3. Joint and Survivor Annuity**

For married members, this is the normal annuity plan at the 50% continuation level. Any percent between 1% and 100% of the members reduced pension may be continued to the surviving nominated beneficiary. This plan automatically terminates upon death of the beneficiary or it may be cancelled upon divorce with the consent of the member's spouse.

**4. Life Annuity Certain and Continuous**

The minimum guarantee is 5 years and the maximum is 20 years. 100% of the members reduced pension continues to the beneficiary for the guarantee period selected.

**G. GROUP HEALTH INSURANCE AND MEDICARE**

Commencing January 1, 1974, the Board may contract for group health insurance on the basis of part or all of the cost of the premium for the coverage to be paid by OP&F. Medical expense benefits are not a vested right and are subject to change at any time upon action of the Board of Trustees.

Effective January 1, 1977, OP&F will pay the premium for supplemental Medicare (Part B), upon obtaining the proper documentation from members of their enrollment in the medicare program.

**H. TIERED RETIREMENT PLAN: COLA or Terminal Pay**

Members retiring after July 24, 1986, who had 15 or more years of service as of January 1, 1989, are allowed to select between two different pension calculation plans. Under the terminal pay method, a pension is calculated using terminal payments such as accrued sick leave and vacation compensation to increase the average annual salary. Under the COLA method, no terminal payments are added, but the pension is subject to annual increases equal to a 3% increase of the original base per year. The COLA method is the automatic cal-

ulation method for an active member with fewer than 15 years of service as of January 1, 1989.

**I. POST-RETIREMENT COST-OF-LIVING ALLOWANCE (COLA)**

Members who retired prior to July 24, 1986 or their surviving beneficiaries under optional plans are entitled to cost-of-living increases. The annual increase is paid on July 1st of each year. The annual COLA increase is \$360 under a Single Life Annuity Plan with proportional reductions for optional payment plans.

**J. RE-EMPLOYED RETIRANTS' DEFINED CONTRIBUTION PLAN BENEFIT**

Effective June 30, 1991, every person who is retired under an Ohio public pension plan and who is employed in a Fund-covered position must contribute to OP&F at the same rate as other police officers or firefighters. The employer pays the normal rate as well. When the re-employed retiree terminates employment, he or she has the option of receiving either a lump sum payment or a lifetime annuity paid monthly.

The lump sum payment is an amount equal to twice his/her contributions plus interest. The lifetime monthly cash payment is based on the value of the lump sum option. If the monthly annuity would be less than \$25, then only the lump sum option is available.

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## *Statistical Section*

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- 1. Revenues by Source**
- 2. Expenses by Type**
- 3. Benefit Expenses by Type**
- 4. Retired Membership by Type of Benefits**
- 5. Average Monthly Benefit Payments**
- 6. Number of Employer Units**
- 7. Death Benefit Fund**

## 1. Revenues by Source

Year	Member Contributions and Purchases	Employer Contributions	Employer Contributions as a percentage of Covered Payroll	Investment and Securities Lending Income	Other Revenues	Total
1997	\$ 121,104,430	\$ 248,145,383	20.5%	\$ 1,118,944,933	\$ 19,408,804	\$ 1,507,603,550
1998	128,673,433	261,618,507	20.3%	913,733,524	19,282,940	1,323,308,404
1999	135,814,320	279,474,521	20.6%	1,101,763,658	18,829,767	1,535,882,266
2000	144,967,340	304,889,375	21.0%	(165,140,849)	16,504,642	301,220,508
2001	150,531,967	312,085,249	20.6%	(443,461,307)	16,776,846	35,932,755
2002	167,137,216	321,672,124	21.0%	(870,447,801)	31,116,120	(350,522,341)

## 2. Expenses by Type

Year	Benefit Payments	Administrative Expenses	Refund of Employee Contributions	Discount on on Early Payoff	Other Expenses	Total
1997	\$ 449,956,880	\$ 8,245,224	\$ 5,655,445		\$ 381,672	\$ 464,239,222
1998	482,070,798	10,899,807	5,685,196	\$ 8,864,703	591,938	508,112,442
1999	542,653,929	11,548,719	11,389,439	12,470,563	887,352	578,950,002
2000	573,783,703	13,224,510	11,069,721	22,321,629	713,134	621,112,697
2001	621,572,113	13,122,347	10,438,362	3,721,025	1,050,563	649,904,410
2002	677,585,955	14,887,089	16,838,054	-	1,014,783	710,325,881

## 3. Benefit Expenses by Type

Year	Retirement	Disability	Health Care	Survivor	Total Benefits
1997	\$ 244,008,942	\$ 97,064,363	\$ 76,459,832	\$ 32,423,743	\$ 449,956,880
1998	263,238,748	101,409,248	83,928,305	33,494,497	482,070,798
1999	282,847,246	107,409,570	100,522,731	51,874,382	542,653,929
2000	301,252,668	115,063,199	111,817,485	45,650,351	573,783,703
2001	319,641,712	125,003,758	129,173,470	47,753,173	621,572,113
2002	335,997,524	137,566,788	153,651,881	50,369,762	677,585,955

## 4. Retired Membership by Type of Benefits\*

Year	Service		Disability		Survivors		Total Beneficiaries
	Police	Fire	Police	Fire	Police	Fire	
1997	5,602	4,858	2,739	1,861	2,898	2,306	20,264
1998	5,571	4,926	2,749	1,869	3,104	2,391	20,610
1999	5,968	5,004	2,841	1,945	3,162	2,472	21,392
2000	6,204	5,125	2,947	2,021	3,211	2,451	21,959
2001	6,312	5,155	3,046	2,082	3,244	2,550	22,389
2002	6,321	5,155	3,055	2,088	3,798	2,996	23,413

\* Source: Actuarial valuation

## 5. Average Monthly Benefit Payments\*\*

for Members Placed on Retirement Rolls

### Service Retirement

Year	Normal	Service Commuted	Age Commuted	Age/Service
1997	2,624	564	0	1,311
1998	2,780	835	0	2,091
1999	2,828	653	0	1,300
2000	2,783	732	0	1,232
2001	2,987	830	0	1,500
2002	3,130	742	0	1,840

### Disability Retirement

Year	Permanent and Total	P&T Presumptive	Partial	Partial Presumptive	Off Duty
1997	2,454	2,633	1,853	2,129	1,220
1998	2,321	2,968	1,953	2,134	1,330
1999	2,388	2,559	2,194	2,361	1,629
2000	2,380	2,061	2,380	2,258	1,760
2001	2,373	2,858	2,332	2,278	1,649
2002	2,970	3,029	2,672	2,965	1,993

\*\* Source: Numbers calculated by taking an average of new retirees as listed in OP&F Board of Trustees monthly reports.

## 6. Number of Employer Units\*\*\*

Calendar Year	Municipalities		Townships		Villages	
	Police	Fire	Police	Fire	Police	Fire
1997	242	195	0	88	340	33
1998	269	214	0	107	347	33
1999	270	213	0	107	351	33
2000	258	213	0	105	332	32
2001	251	215	0	105	322	32
2002	252	219	0	106	307	29

\*\*\* Source: Numbers obtained by adding the number of employers by type as stored in our employer master file database.



## 7. Death Benefit Fund

Pursuant to Section 742.63 of the Ohio Revised Code, the Board of Trustees of the Ohio Police & Fire Pension Fund administers the State of Ohio Public Safety Officers Death Benefit Fund (DBF). This program was established by the State of Ohio to provide monthly benefit payments to surviving family members of Ohio firefighters and law enforcement officers who have been killed in the line of duty or die of a

duty-related accident or illness. Funds are disbursed to OP&F each State fiscal year (July 1-June 30) and are paid monthly by OP&F to eligible recipients. The unused balance at June 30 is returned to the State. The assets and liabilities of the DBF are included in OP&F's combining statement of plan net assets as of December 31, 2002 as an agency fund. The following is a schedule of DBF financial activity:

Balance January 1, 2002	\$13,640,695
Less: Survivor Benefits Paid January 1 to June 30, 2002	(10,033,776)
Balance returned to State of Ohio	(3,606,919)
State Funding Received July 2002	\$24,000,000
Less: Survivor Benefits Paid July 1 - December 31, 2002	(9,473,551)
<b>Balance December 31, 2002</b>	<b><u>\$14,524,899</u></b>

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Prepared through the combined efforts of the OP&F staff.

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