

Orange County Employees  
Retirement System

COMPREHENSIVE  
ANNUAL FINANCIAL  
REPORT

For the Year Ended December 31, 2003

# COMPREHENSIVE ANNUAL FINANCIAL REPORT

For the Year Ended December 31, 2003

Orange County Employees Retirement System  
Orange County, California

Keith Bozarth  
Chief Executive Officer



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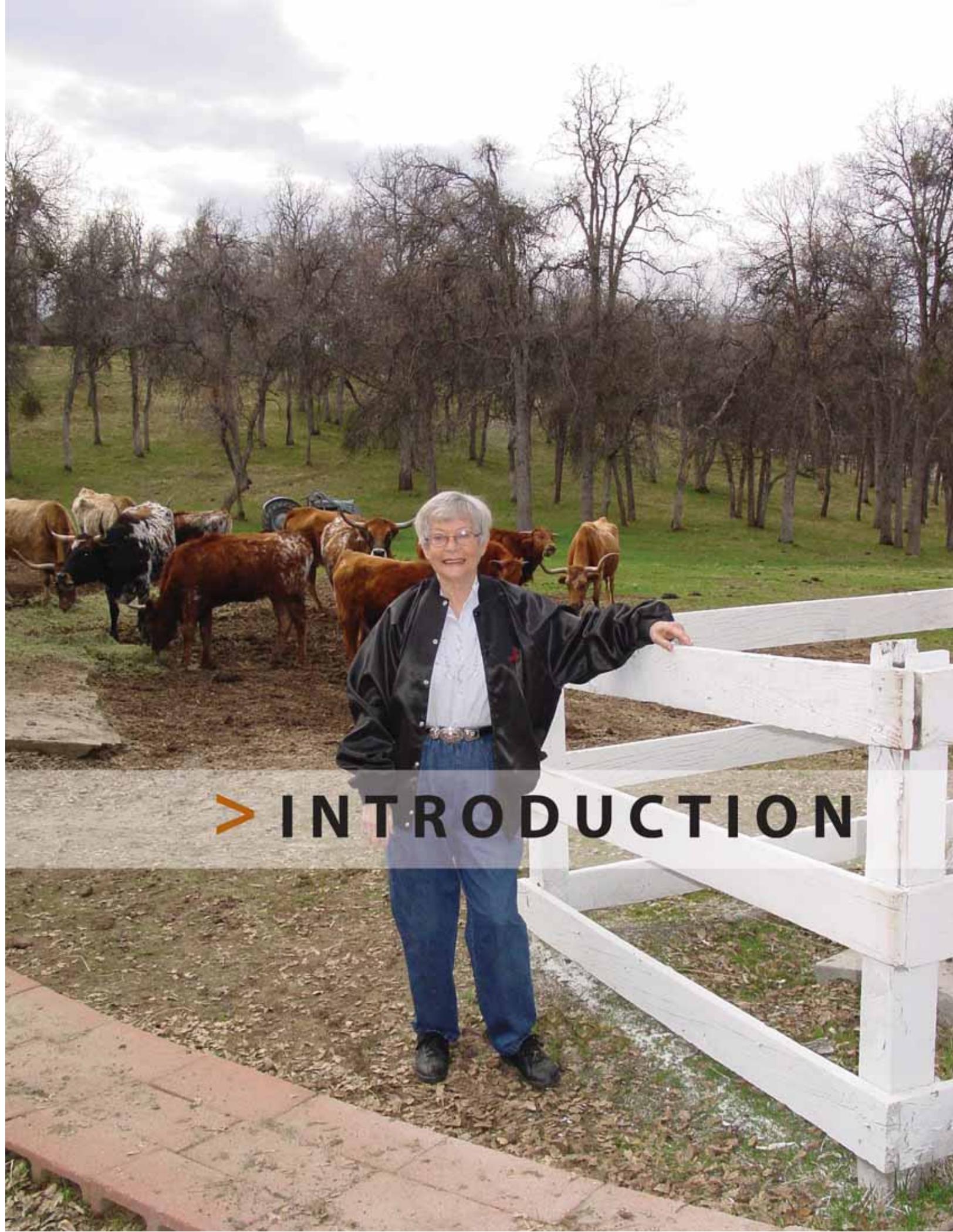
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SECTION

1



> **INTRODUCTION**



*Serving the Active and Retired Members of:*

ORANGE COUNTY  
LAFCO

CITY OF SAN JUAN  
CAPISTRANO

COUNTY OF ORANGE

ORANGE COUNTY  
CHILDREN & FAMILIES  
COMMISSION

FOOTHILL/EASTERN/  
SAN JOAQUIN HILLS  
TRANSPORTATION  
CORRIDOR AGENCY

ORANGE COUNTY  
CEMETERY DISTRICT

ORANGE COUNTY  
EMPLOYEES  
RETIREMENT SYSTEM

ORANGE COUNTY FIRE  
AUTHORITY

ORANGE COUNTY LAW  
LIBRARY

ORANGE COUNTY  
TRANSPORTATION  
AUTHORITY

ORANGE COUNTY VECTOR  
CONTROL DISTRICT

SANITATION DISTRICT OF  
ORANGE COUNTY

ORANGE COUNTY  
DEPARTMENT OF  
EDUCATION  
(closed to new  
members)

UCI MEDICAL CENTER  
(closed to new  
members)

May 14, 2004

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

Dear Board Members:

It is with great pleasure that we submit the Comprehensive Annual Financial Report (CAFR) of the Orange County Employees Retirement System (OCERS) for the calendar year ended December 31, 2003, the System's 59<sup>th</sup> year of operation. Information contained in this report is designed to provide a complete and accurate review of the year's operations and is the responsibility of the OCERS' management. Please review the basic financial statements in conjunction with the Management's Discussion and Analysis pages 16-20.

**Structure of the Report:**

This report is presented in five sections:

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

**Certificate of Achievement:**

The Government Finance Officers Association of the United States and Canada (GFOA) awarded a Certificate of Achievement for Excellence in Financial Reporting to OCERS for its Comprehensive Annual Financial Report for the fiscal year ended December 31, 2002 (page 6).

Board of Retirement  
May 14, 2004

This was the ninth consecutive year that OCERS has achieved this prestigious award. The Certificate of Achievement is a national award recognizing conformance with the highest standards for preparation of state and local government financial reports.

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

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

**Major Initiative:**

OCERS is continuing with the enhancement of the new Membership Accounting Record System (MARS), commonly known as PensionGold, which is a product of Levi, Ray & Shoup, Inc, that became operational in July 2003.

**Additional Retiree Benefit Account (ARBA):**

Due to insufficient realized earnings in year 2003, all of the ARBA balances were used to credit the interest to Reserves. The balance of the ARBA account at December 31, 2003 was zero.

**Retired Members Benefit Reserve (RMBR):**

The Retired Members Benefit Account was created in 2002 to ensure the continued funding of medical grants and similar supplemental benefits for an additional period. All participating agencies transferred a projected three years of benefit payments to the RMBR balance that was created as a sub-account of the Employer Advanced Reserve Account. The RMBR account will be used to pay additional benefits to retirees when the ARBA balance is depleted. The RMBR balance will be funded on a three-year rolling method. As of December 31, 2003, the balance for the RMBR account was \$20,422,000.

**Accounting System and Report:**

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

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

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

Board of Retirement  
May 14, 2004

**Additions to Plan Net Assets:**

Due to improved market conditions during 2003, the total additions to plan net assets, including net appreciation in fair value of investments, were \$994,910,000. This amount includes member and employer contributions of \$205,824,000, net investment gains of \$788,036,000, net security lending income of \$872,000 and net commission recapture income of \$178,000. Net investment gain, excluding net security lending income and net commission recapture income, represented an increase of \$1,058,690,000 over the prior year. This increase was attributable mainly to a \$1,056,874,000 increase in net appreciation in fair value of investments over the prior year, \$19,397,000 in lower interest earnings on fixed income investments and \$114,618,000 increase in contributions. Details of the additions to plan net assets are included in the Statement of Changes in Plan Net Assets on page 22.

**Deductions to Plan Net Assets:**

Deductions for 2003, excluding investment management and security lending fees, were \$225,533,000 which represented an increase of \$31,223,000 over the prior year. This increase was the result of higher retirement benefit payments, an increase in the number of retirees and an increase in refunds/withdrawals to terminated members. The components of the total deductions are payments of retirement benefits of \$210,273,000, refunds of contributions and interest to terminated members of \$6,412,000 and administrative expenses of \$8,848,000.

**Changes in System Membership:**

OCERS' membership increases (decreases) for the calendar year 2003 were as follows:

	2003	2002	Increase (Decrease)	Change
Active Members	22,672	22,723	(51)	(0.22%)
Retired Members	8,950	8,688	262	3.02%
Deferred Members	1,665	1,377	288	20.92%
Pending Status Members	613	800	(187)	(23.38%)

Pending status numbers are members who terminated membership with OCERS but had not selected an option regarding the management of their balances.

**Investment and Economic Summary:**

After three years of negative annual returns 2003 turned out to be a strong year for equities with U.S. and non U.S. markets generating strong returns.

The markets continued to be volatile in the first quarter of 2003. But in the second quarter, the sentiment turned positive. The broad equity benchmark Russell 3000 was up 31.06% for 2003 and the international market benchmark, MSCI Eafe was up 41.41% in 2003.

In the domestic fixed income arena, the Lehman Aggregate, proxy for fixed income, returned 4.10% while the benchmark for non U.S. fixed income markets returned 1.89%. In 2002, investors sought safety, whereas in 2003, low quality and high yield performed strongly with investors reaching for a higher yield in a 50 year low interest rate environment.

Board of Retirement  
May 14, 2004

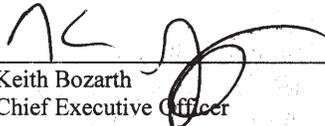
**Funding:**

OCERS' funding objective is to meet long-term benefit obligations through contributions and investment income. As of December 31, 2003, the funding ratio of the System was 78.53%. A six-year history of OCERS' funding progress is presented on page 36. For 2003, OCERS experienced an increase of \$769,377,000 in plan net assets. Details of the components of this increase are included in the Statement of Changes in Plan Net Assets on page 22.

**Conclusion:**

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

Respectfully submitted,

  
\_\_\_\_\_  
Keith Bozarth  
Chief Executive Officer

  
\_\_\_\_\_  
Toi Dang  
Chief Financial Officer

# Certificate of Achievement for Excellence in Financial Reporting

Presented to

## Orange County Employees Retirement System, California

For its Comprehensive Annual  
Financial Report  
for the Fiscal Year Ended  
December 31, 2002

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.



A handwritten signature in cursive script, reading "Edward Haney".

President

A handwritten signature in cursive script, reading "Jeffrey R. Emer".

Executive Director

## MEMBERS OF THE BOARD OF RETIREMENT

As of December 31, 2003

Reed L. Royalty  
*Chairman*



*Appointed by the  
Board of Supervisors*



Sharon Neebe  
*Vice-Chairman*

*Elected by  
General Members*

Frank E. Eley



*Elected by  
General Members*



Lisa Welch Silbar

*Appointed by the  
Board of Supervisors*



George W. Jeffries

*Appointed by the  
Board of Supervisors*

Thomas J. Lightvoet

*Appointed by the  
Board of Supervisors*



Richard A. White Jr.



*Elected by  
Safety Members*



David Thompson

*Alternate  
Elected by  
Safety Members*

John M.W. Moorlach

*Ex-Officio Member  
Treasurer-Tax Collector  
County of Orange*



Keith L. Concannon

*Elected by  
Retired Members*

## Board of Retirement

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

## Executive

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

## Investment Department

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

## Operations Department

This department is comprised of the Member Services, Administrative Services, Information Technology, and Communications divisions. The Member Services Division is responsible for providing all benefit services to the members of the system. This includes benefit calculations, evaluation of claims for disability retirement, preparation of data to support applications for retirement, preparation of the retiree payroll, and membership counseling. The Administrative Services Division is responsible for providing the contract administration, purchasing, and human resources functions of OCERS. The Information Technology Division is responsible

for OCERS' network systems, personal computers and Web site, while providing programming and technical support on our Benefits Administration System. In addition, this division is responsible for the production of retiree payroll and administering all audio/visual functions. The Communications Division is responsible for producing publications such as the Comprehensive Annual Financial Report, a quarterly news magazine and brochures, as well as producing content for the Web site and Board of Retirement Extranet. The Communications Division also coordinates financial and pre-retirement seminars for more than 1,500 members annually.

## Finance Department

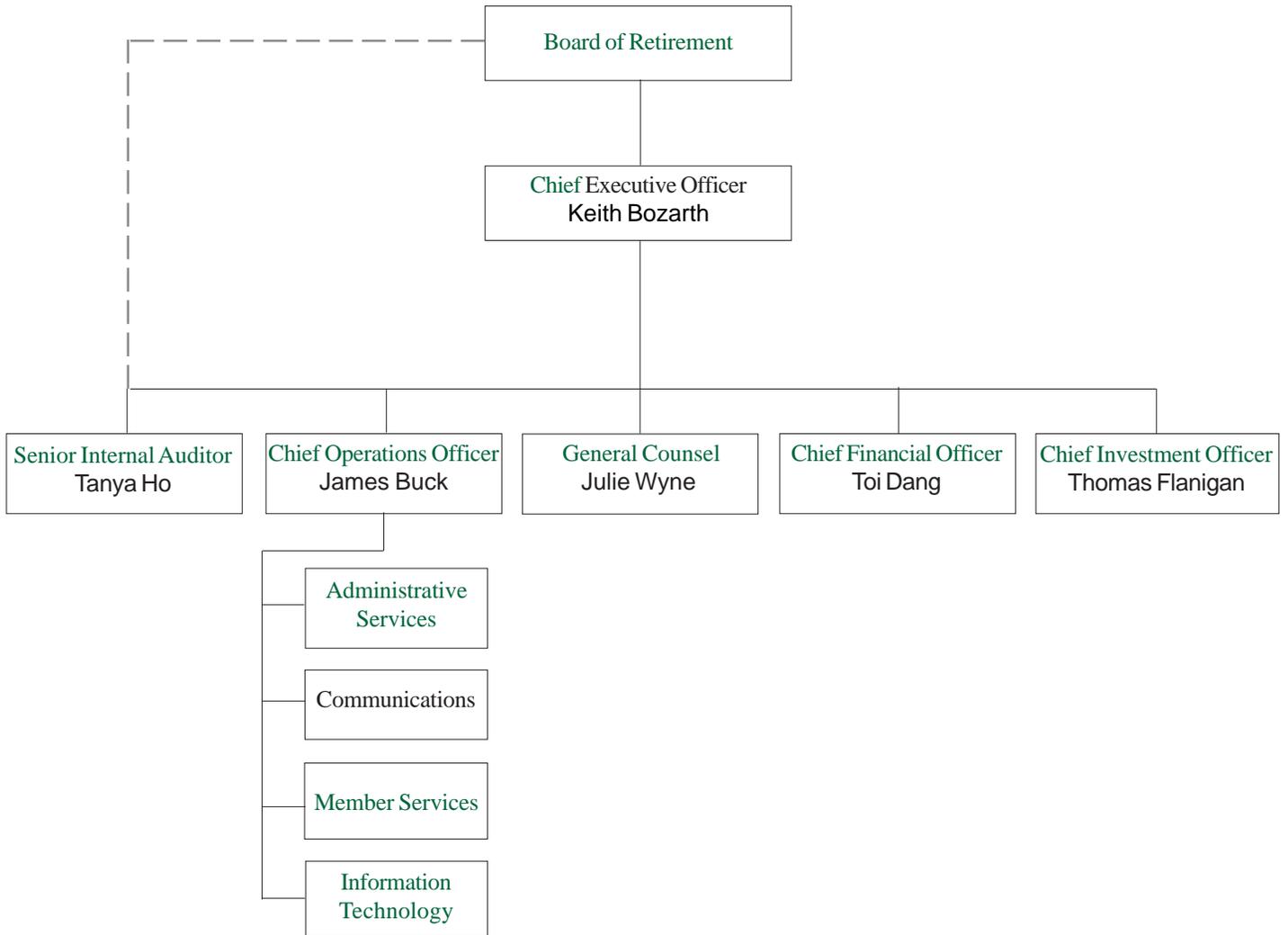
This department is comprised of the Accounting Division. The Accounting Division is responsible for all the financial records and reports of OCERS. This includes the preparation of the Comprehensive Annual Financial Report, monthly and quarterly financial statements and the annual operating budget. The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

## Legal Department

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

## ADMINISTRATIVE ORGANIZATION CHART

as of December 31, 2003



## Consulting Services

As of December 31, 2003

### Actuary

Towers Perrin

### Investment Consultant

Callan Associates, Inc.

### Real Estate Consultant

The Townsend Group

### Independent Auditor

Link, Murrel & Company

### Investment Counsel

Stradling, Yocca, Carlson & Rauth

### Fiduciary Counsel

Steeffel Levitt & Weiss

### Tax Counsel

Foley & Lardner

---

## Investment Managers

As of December 31, 2003

### Domestic Equity

Artisan Partners

Barclays Global Investors

Cadence Capital Management

Capital Guardian Trust Company

Dodge & Cox

Delaware Investment Advisers

Peregrine Capital Management

### Domestic Fixed Income

Barclays Global Investors

Loomis, Sayles & Company

Pacific Investment Management Company (PIMCO)

### International Equity

Capital Guardian Trust Company

Barclays Global Investors

### International Fixed Income

Delaware International Advisers, Ltd.

## Investment Managers

As of December 31, 2003

(Continued)

### Real Estate

#### Domestic

American Realty Advisors

CB Richard Ellis

Sentinel Real Estate Corporation

#### International

PRICOA Property Investment  
Management, Ltd.

### Non-Traditional Investments

#### Managers

Adams Street Partners

HarbourVest Partners, LLC

#### Limited Partnerships

TCW Asset Management Company

Vega Partners

#### Timber

Hancock Timber Resource Group

Prudential Timber Investments, Inc.

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## Custodian

As of December 31, 2003

State Street California



SECTION

2

# JOHN WAYNE AIRPORT



**FINANCIAL**

## Link, Murrel & Company

A PARTNERSHIP INCLUDING PROFESSIONAL CORPORATIONS

### REPORT OF INDEPENDENT AUDITORS

#### **Orange County Employees Retirement System Board of Retirement**

We have audited the accompanying statements of plan net assets of the Orange County Employees Retirement System ("System") as of December 31, 2003 and 2002, and the related statements of changes in plan net assets for the years then ended. These financial statements are the responsibility of the System'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. Those standards require that we plan and perform the audits 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 the Orange County Employees Retirement System at December 31, 2003 and 2002, and the changes in plan net assets for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

The Management's Discussion and Analysis and the required supplementary information listed in the table of contents 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 of the required supplementary information. However, we did not audit the information and express no opinion on it.

**Orange County Employees Retirement System**

Board of Retirement

Page 2

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



April 7, 2004

Irvine, California

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OCERS management is pleased to provide this overview and analysis of the financial activities of the Orange County Employees Retirement System (OCERS) for the calendar year ending December 31, 2003. Please review it in conjunction with the Letter of Transmittal (starting on page 2) and the Basic Financial Statements beginning on page 21.

**Financial Highlights** (Dollars in thousands):

- Net Assets Held in Trust for Pension Plan Benefits, as reported in the Statement of Plan Net Assets, totaled \$4,959,626 an increase of \$769,377 or 18.36% from the prior year, primarily as a result of the increases in fair market values of investments and increase in contributions.
- Total Additions, as reported in the Statement of Changes in Plan Net Assets were \$994,910, the major components of which is the appreciation in the fair value of investments and increase in contributions.
- Total Deductions, as reported in the Statement of Changes in Plan Net Assets, were \$225,533. This represented an increase of \$31,223 over the prior year primarily as a result of increases in benefit payments.
- The firm of Towers, Perrin, Inc. is OCERS' actuary. The latest actuarial valuation completed as of December 31, 2003 indicated that the funding status (the ratio of system assets to system liabilities) was 78.53%.

**Overview of Financial Statements:**

This section serves as an introduction to the Basic Financial Statements that are comprised of these components:

1. Statement of Plan Net Assets (page 21): This is a snapshot of account balances at the end of calendar year. This statement reflects assets available for future payments to members and their beneficiaries and any current liabilities that are owed.
2. Statement of Changes in Plan Net Assets (page 22): This report reflects all of the financial activities that occurred during the calendar year and shows the impact of those activities as Additions to or Deductions from the Plan.
3. Notes to Basic Financial Statements (pages 23-34): The Notes are an integral part of the financial reports; they provide detailed discussion to key policies, programs and activities that occurred during the year.
4. Required Supplementary Information (pages 35-37): This section includes the Schedule of Funding Progress that shows the historical trend for the actuarially funding status of the Plan; and the Schedule of Employer Contributions that shows the annual required contributions and the percentage of contributions made.

The Other Supplementary Information (pages 38-41), the Investment Section (pages 42-57), the Actuarial Section (pages 58-75) and the Statistical Section (pages 76-86) provide additional detailed financial, investment, actuarial, and statistical data supporting information reported in the basic financial statements.

**Plan Net Assets (Dollars in thousands):**

	<u>December 31</u>			<u>Increase/ (Decrease) Amount</u>	<u>Increase/ (Decrease) Amount</u>	<u>Increase/ (Decrease) Amount</u>
	<u>2003</u>	<u>2002</u>	<u>2001</u>	<u>2003-2002</u>	<u>2003-2001</u>	<u>2002-2001</u>
Current Assets	\$ 996,489	\$ 462,249	\$ 431,786	\$ 534,240	\$ 564,703	\$ 30,463
Investments	4,299,544	4,043,188	4,587,870	256,356	(288,326)	(544,682)
Capital Assets	4,231	3,538	3,205	693	1,026	333
<b>Total Assets</b>	<b>5,300,264</b>	<b>4,508,975</b>	<b>5,022,861</b>	<b>791,289</b>	<b>277,403</b>	<b>(513,886)</b>
<b>Total Liabilities</b>	<b>340,638</b>	<b>318,726</b>	<b>460,320</b>	<b>21,912</b>	<b>(119,682)</b>	<b>(141,594)</b>
<b>Total Plan Net Assets</b>	<b>\$ 4,959,626</b>	<b>\$ 4,190,249</b>	<b>\$ 4,562,541</b>	<b>\$ 769,377</b>	<b>\$ 397,085</b>	<b>\$ (372,292)</b>

	<u>Increase/ (Decrease) Amount</u>	<u>Increase/ (Decrease) Amount</u>	<u>Increase/ (Decrease) Amount</u>	<u>Increase/ (Decrease) %</u>	<u>Increase/ (Decrease) %</u>	<u>Increase/ (Decrease) %</u>
	<u>2003-2002</u>	<u>2003-2001</u>	<u>2002-2001</u>	<u>2003-2002</u>	<u>2003-2001</u>	<u>2002-2001</u>
Current Assets	\$ 534,240	\$ 564,703	\$ 30,463	115.57%	130.78%	7.06%
Investments	256,356	(288,326)	(544,682)	6.34%	-6.28%	-11.87%
Capital Assets	693	1,026	333	19.59%	32.01%	10.39%
<b>Total Assets</b>	<b>791,289</b>	<b>277,403</b>	<b>(513,886)</b>	<b>17.55%</b>	<b>15.52%</b>	<b>-10.23%</b>
<b>Total Liabilities</b>	<b>21,912</b>	<b>(119,682)</b>	<b>(141,594)</b>	<b>6.87%</b>	<b>-26.00%</b>	<b>-30.76%</b>
<b>Total Changes</b>	<b>\$ 769,377</b>	<b>\$ 397,085</b>	<b>\$ (372,292)</b>	<b>18.36%</b>	<b>8.70%</b>	<b>-8.16%</b>

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

The reserves needed to finance retirement benefits are accumulated through the collection of employer and employee contributions and through interest credited to the reserves. Earnings (losses) on investments increase (decrease) the Net Assets Held in Trust for Pension Benefits that, in turn, decrease (increase) employers' contribution. Gains, including net appreciation in fair market value of investments, net securities lending income, net commission recapture income and net of investment expenses for the year ended December 31, 2003, totaled \$789,086. (See page 22).

Overall additions to plan net assets were \$994,910 due primarily to investment gains and an increase in overall contributions.

**Additions to Plan Net Assets (Dollars in thousands):**

	<u>Years Ended December 31</u>			<u>Increase/ (Decrease) Amount</u>	<u>Increase/ (Decrease) Amount</u>	<u>Increase/ (Decrease) Amount</u>
	<u>2003</u>	<u>2002</u>	<u>2001</u>	<u>2003-2002</u>	<u>2003-2001</u>	<u>2002-2001</u>
Employer Contributions	\$ 124,243	\$ 13,289	\$ 12,060	\$ 110,954	\$ 112,183	\$ 1,229
Employee Contributions	81,581	77,917	68,635	3,664	12,946	9,282
Investment Gains (Losses)	789,086	(269,188)	(149,858)	1,058,274	938,944	(119,330)
<b>Total Additions</b>	<b>\$ 994,910</b>	<b>\$ (177,982)</b>	<b>\$ (69,163)</b>	<b>\$ 1,172,892</b>	<b>\$ 1,064,073</b>	<b>\$ (108,819)</b>

**Additions to Plan Net Assets (Dollars in thousands):**

	Increase/ (Decrease) Amount <u>2003-2002</u>	Increase/ (Decrease) Amount <u>2003-2001</u>	Increase/ (Decrease) Amount <u>2002-2001</u>	Increase/ (Decrease) % <u>2003-2002</u>	Increase/ (Decrease) % <u>2003-2001</u>	Increase/ (Decrease) % <u>2002-2001</u>
Employer Contributions	\$ 110,954	\$ 112,183	\$ 1,229	834.93%	930.21%	10.19%
Employee Contributions	3,664	12,946	9,282	4.70%	18.86%	13.52%
Investment Gains (Losses)	<u>1,058,274</u>	<u>938,944</u>	<u>(119,330)</u>	<u>393.14%</u>	<u>626.56%</u>	<u>-79.63%</u>
<b>Total Changes</b>	<b><u>\$ 1,172,892</u></b>	<b><u>\$ 1,064,073</u></b>	<b><u>\$ (108,819)</u></b>	<b>658.99%</b>	<b>1538.50%</b>	<b>(157.34%)</b>

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

OCERS was created to provide lifetime retirement annuities, survivor benefits and permanent disability benefits to qualified members and their beneficiaries. The cost of such programs includes recurring benefit payments, as designated by the Plan, refund of contributions to terminated employees and the cost of administering the system. Deductions for the year ended December 31, 2003, totaled \$225,533 (see page 22).

**Deductions from Plan Net Assets (Dollars in thousands):**

	Years Ended December 31			Increase/ (Decrease) Amount	Increase/ (Decrease) Amount	Increase/ (Decrease) Amount
	<u>2003</u>	<u>2002</u>	<u>2001</u>	<u>2003-2002</u>	<u>2003-2001</u>	<u>2002-2001</u>
Benefits Paid	\$ 210,273	\$ 181,549	\$ 163,378	\$ 28,724	\$ 46,895	\$ 18,171
Withdrawals/Refunds	6,412	4,482	5,896	1,930	516	(1,414)
Administrative Expenses	<u>8,848</u>	<u>8,279</u>	<u>7,146</u>	<u>569</u>	<u>1,702</u>	<u>1,133</u>
<b>Total Deductions</b>	<b><u>\$ 225,533</u></b>	<b><u>\$ 194,310</u></b>	<b><u>\$ 176,420</u></b>	<b><u>\$ 31,223</u></b>	<b><u>\$ 49,113</u></b>	<b><u>\$ 17,890</u></b>

	Increase/ (Decrease) Amount <u>2003-2002</u>	Increase/ (Decrease) Amount <u>2003-2001</u>	Increase/ (Decrease) Amount <u>2002-2001</u>	Increase/ (Decrease) % <u>2003-2002</u>	Increase/ (Decrease) % <u>2003-2001</u>	Increase/ (Decrease) % <u>2002-2001</u>
Benefits Paid	\$ 28,724	\$ 46,895	\$ 18,171	15.82%	28.70%	11.12%
Withdrawals/Refunds	1,930	516	(1,414)	43.06%	8.75%	-23.98%
Administrative Expenses	<u>569</u>	<u>1,702</u>	<u>1,133</u>	<u>6.87%</u>	<u>23.82%</u>	<u>15.86%</u>
<b>Total Changes</b>	<b><u>\$ 31,223</u></b>	<b><u>\$ 49,113</u></b>	<b><u>\$ 17,890</u></b>	<b>16.07%</b>	<b>27.84%</b>	<b>10.14%</b>

**Reserves (Dollars in thousands):**

OCERS' reserves are established from contributions and the amount of interest credited to reserve accounts at the actuarially assumed rate of 7.5% on a bi-annual basis. The Active Members Reserve account was credited with an interest rate of 5.5% on a bi-annual basis; the remaining 2.0% was credited to the Employer Advanced Reserve, also on a bi-annual basis. Reserve balances are as follows:

	December 31		
	2003	2002	2001
Active Members Reserve	\$ 927,970	\$ 858,121	\$ 785,920
Retired Members Reserve	2,503,128	2,148,469	1,880,464
Employer Advanced Reserve	1,268,602	1,350,611	1,403,701
Additional Retiree Benefit Account Reserve	-	25,703	-
Retired Members Benefit Account	20,422	56,950	363,077
Death Benefits Reserve	-	1,074	932
	<u>4,720,122</u>	<u>4,440,928</u>	<u>4,434,094</u>
Less: Accounts Receivable for Interest Credited to Reserve	(122,922)	-	-
<b>Net Total Reserve</b>	<b><u>\$ 4,597,200</u></b>	<b><u>\$ 4,440,928</u></b>	<b><u>\$ 4,434,094</u></b>

### Investment and Economic Summary:

After three years of negative annual returns 2003 turned out to be a strong year for equities with U.S. and non U.S. markets generating strong returns.

The markets continued to be volatile in the first quarter of 2003. But in the second quarter, the sentiment turned positive. The broad equity benchmark Russell 3000 was up 31.06% for 2003 and the international market benchmark, MSCI Eafe was up 41.41% in 2003.

In the domestic fixed income arena, the Lehman Aggregate, proxy for fixed income, returned 4.10% while the benchmark for non U.S. fixed income markets returned 1.89%. In 2002, investors sought safety, whereas in 2003, low quality and high yield performed strongly with investors reaching for a higher yield in a 50 year low interest rate environment.

### Capital Assets (Dollars in thousands):

OCERS' investment in capital assets increased from \$3,538 to \$4,231 (net of accumulated depreciation and amortization). This investment in capital assets includes equipment, furniture and computer system-installation. The total increase in OCERS' investment in capital assets for the current year was 19.59% over 2002. The major capital asset investment during 2003 was the development and installation of OCERS' information technology infrastructure, the Membership Accounting Records System (MARS). This project has involved movement of OCERS' Retirement Database from one platform to another (Oracle).

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

Positive market returns and increases in contributions were the primary factors in an increase in net assets by \$769,377, thereby accounting for an increase of 18.36% over the prior year. Key elements of this increase are described in the section that follows:

	<b>Years Ended December 31</b>		
	<b>2003</b>	<b>2002</b>	<b>2001</b>
Contributions Received	\$ 205,824	\$ 91,206	\$ 80,695
Net Investment Gains (Losses)	788,036	(270,654)	(152,076)
Net Securities Lending Income and Other Income	1,050	1,466	2,218
Participant's Benefits	(210,273)	(181,549)	(163,378)
Withdrawals and Refunds	(6,412)	(4,482)	(5,896)
Administrative Expenses	(8,848)	(8,279)	(7,146)
<b>Increases (Decreases) in Plan Net Assets</b>	<b>\$ 769,377</b>	<b>\$ (372,292)</b>	<b>\$ (245,583)</b>

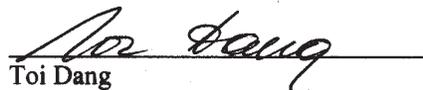
**OCERS' Fiduciary Responsibilities:**

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

**Requests for Information:**

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

OCERS  
 Attention: Toi Dang  
 2223 Wellington Avenue  
 Santa Ana, CA 92701

  
 Toi Dang  
 Chief Financial Officer

**Statement of Plan Net Assets**  
(in thousands)

	2003	December 31	2002
<b>ASSETS</b>			
Cash and Short-Term Investments			
Cash and Cash Equivalents (Note E-3)	\$ 672,569	\$	191,402
Collateral Held for Securities Lent (Note E-6)	290,166		227,024
Total Cash and Short-Term Investments	962,735		418,426
Receivables			
Forward Currency Contracts, Net (Note F-1)	378		285
Investment Income	13,585		22,585
Securities Sales	6,615		10,858
Employer/Employee Contributions	13,176		10,095
Total Receivables	33,754		43,823
Investments, at Fair Value (Notes B-2 and E)			
United States Government Debt			
Securities and Corporate Bonds	1,183,590		1,459,003
Foreign Bonds	237,560		231,359
Domestic Equity Securities	1,727,507		1,309,199
International Equity Securities	748,239		525,473
Real Estate	250,291		351,704
Venture Capital and Limited Partnership Interests	152,357		166,450
Total Investments	4,299,544		4,043,188
Capital Assets, Net (Note B-3)	4,231		3,538
Total Assets	5,300,264		4,508,975
<b>LIABILITIES</b>			
Collateral Held for Securities Lent (Note E-6)	290,166		227,024
Securities Purchased	24,318		69,615
Other	26,154		22,087
Total Liabilities	340,638		318,726
Net Assets Held in Trust for Pension Plan Benefits	\$ 4,959,626	\$	4,190,249

(See accompanying notes to financial statements beginning on page 23.)

**Statement of Changes in Plan Net Assets**  
(in thousands)

	Years Ended December 31	
	2003	2002
<b>ADDITIONS</b>		
Contributions (Note C)*		
Employer	\$ 124,243	\$ 13,289
Employee	81,581	77,917
Total Contributions	205,824	91,206
Investment Income (Loss):		
Net Appreciation (Depreciation) in Fair Value of Investments (Note E-5)	649,697	(407,177)
Interest on:		
Domestic and International Securities	66,368	85,765
Cash with County Treasurer (Note E-3)	105	65
Domestic Dividends	11,092	10,963
Rental Income	49,287	34,939
International Dividends	12,088	12,354
Venture Capital and Limited Partnership	16,168	10,703
Total Investment Income (Loss)	804,805	(252,388)
Less Investment Expenses	(16,769)	(18,266)
Net Investment Income (Loss)	788,036	(270,654)
Securities Lending Revenue (Note E-6)	1,236	1,580
Less Securities Lending Fees (Note E-6)	(364)	(461)
Net Securities Lending Income	872	1,119
Net Income from Commission Recapture	178	347
Total Additions (Decreases)	994,910	(177,982)
<b>DEDUCTIONS</b>		
Participants' Benefits	210,273	181,549
Member Withdrawals	6,412	4,482
Administrative Expenses (Note G)	8,848	8,279
Total Deductions	225,533	194,310
<b>NET INCREASE (DECREASE)</b>	769,377	(372,292)
<b>NET ASSETS HELD IN TRUST FOR PENSION PLAN BENEFITS</b>		
Beginning of Year	4,190,249	4,562,541
End of Year	\$ 4,959,626	\$ 4,190,249

\*Employer contributions reflect cash payments only. Please see Note C on page 27 for amounts transferred from the County Investment Account.

(See accompanying notes to financial statements beginning on page 23.)

**A. Description and History of Plan**

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

**1. General**

OCERS is a cost-sharing multiple-employer, defined benefit pension plan covering substantially all employees of the County of Orange (County) and of the following agencies:

- City of Rancho Santa Margarita
- City of San Juan Capistrano
- Orange County Cemetery District
- Orange County Children and Families Commission
- Orange County Department of Education (closed to new members)
- Orange County Employees Retirement System
- Orange County Fire Authority
- Orange County Local Agency Formation Commission
- Orange County Public Law Library
- Orange County Sanitation District
- Orange County Superior Court
- Orange County Transportation Authority
- Orange County Vector Control District
- Transportation Corridor Agencies
- University of California, Irvine Medical Center and Campus (closed to new members).

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

Following an effort by the employees of Orange County, a proposition was submitted to the people of Orange County. As a result of the General Election, OCERS was established in 1945 under the provisions of the County Employees Retirement Law of 1937 (County Retirement Law). OCERS provides members with retirement, death, disability, and cost-of-living benefits. OCERS is a related organization of the County of Orange, California.

The Retirement Board consists of nine members of which four are appointed by the County’s Board of Supervisors, four are elected by the members of OCERS, the County Treasurer is an ex-officio member and an alternate member is elected by the safety members. The County of Orange is not financially accountable for OCERS.

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

**2. Membership**

All regular full-time employees or part-time employees, scheduled to work 20 hours or more per week for the County or other participating employers become members of the plan upon employment.

**3. Monthly Salary Base for Benefits**

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

**4. Service Retirement**

a. Eligibility: Ten years of service and age 50, or 30 years of service and any age (20 years for safety members), or age 70 with any service.

b. Benefit Formula per Year of Service:

General Tier I – 2%    General Tier II – 1.6667%  
 Firefighters and Law Enforcement – 3%  
 Probation Officers, Rancho Santa Margarita and San Juan Capistrano – 2%

Benefits are reduced or increased for retirement ages according to the following sections of the County Employees Retirement Law of 1937:

Fire/Law Enforcement	31664.1
Probation Officers	31664
San Juan Capistrano	31676.19
Rancho Santa Margarita	31676.18
All other General members:	
• Tier 1	31676.12
• Tier 11	31676.1

**5. Non-Service Connected Disability**

- a. Eligibility: Five years of service.
- b. Benefit Formula per Year of Service:

**Tier I**

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

**Tier II**

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

**6. Service Connected Disability**

- a. Eligibility: No age or service requirement.
- b. Benefit: 50% of final average monthly compensation, or service retirement if the benefits are higher.

**7. Active Member Death**

- a. If not eligible for a service retirement or for a non-service connected disability at the time of death, refund of employee contributions with interest plus one month's salary for each year of service to a maximum of six months' salary.
- b. If eligible to retire for a service or for a non-service connected disability at the time of death, qualified surviving spouse, or child, has the following options:
- Refund of employee contributions with interest plus one month's salary for each year of service to a maximum of six months' salary;

or

- 60% of earned benefit payable to surviving eligible spouse;

or

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

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

- c. Service-Connected Death:

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

**8. Death After Retirement**

- a. Non-Service Connected Disability Retirement:

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

- b. Service-Connected Disability Retirement:

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

- c. \$750 Burial Benefit:

Payable to named beneficiary following death of original retiree.

- d. Service Retirement:

Benefit depends upon option chosen.

**9. Termination of Employment**

Members may elect a refund of accumulated contributions and interest. Contributions left on deposit continue to draw interest regardless of the amount of service the member has earned. If the member does leave his contributions on deposit and has at least five years of service, he will be eligible to a benefit at

the point that he attains retirement age and would have met the service requirements had he not terminated covered employment.

27.37% (27.37%) for the City of Rancho Santa Margarita; 29.15% (29.16%) for the City of San Juan Capistrano.

**10. Post-Retirement Cost-of-Living Benefits**

The annual Cost-of-Living Adjustment (COLA) is intended to increase retirement payments to account for inflation. The COLA applies to all retired members who retired on or before April 1 of that year. Retirees receive an increase equal to the actual U.S. Department of Labor Consumer Price Index (CPI) as it relates to the Orange County area (which includes Orange, Los Angeles and Riverside counties), to a maximum of 3% per year. Percentage in excess of 3% is “banked” for future increases and may be applied to a future year in which the change is less than 3%.

In addition to the annual Cost-of-Living Adjustment (COLA), the Board of Retirement grants a STAR (Supplemental Targeted Adjustment for Retirees) COLA for eligible retirees who have lost more than 20% of their purchasing power to inflation since retirement.

The adjustment allows retirees to keep at least 80% of their purchasing power, regardless of how many years they have been retired.

**11. Employer Contributions**

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

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

Normal based on entry age, 1/200 (1/120) at 60 for General Members; 1/200 (1/100) at 50 for Safety Members.

Cost-of-Living contributions equal to percentage of normal: 51.90% (31.40%) for Non-OCTA General; 50.96% (35.56%) for OCTA General; 108.80% (54.86%) for Firefighters; 113.32% (57.36%) for Law Enforcement; 28.28% (14.10%) for probation officers;

**13. Active and Retired Members**

The following is a summary of OCERS’ membership composition at December 31, 2003 and 2002:

	Active Personnel (unaudited)	
	December 31	
	2003	2002
<u>General Members</u>		
County and Agencies Paid by County Payroll	15,857	15,999
Outside Agencies	3,166	3,003
Subtotal - General Members	19,023	19,002
<u>Safety Members</u>		
County and Agencies Paid by County Payroll	2,854	2,930
Outside Agencies	795	791
Subtotal - Safety Members	3,649	3,721
<b>Total Active Members</b>	<b>22,672</b>	<b>22,723</b>
<u>Deferred (General &amp; Safety) Members</u>		
Regular	1,638	661
Employment with Other Agencies (Reciprocity)	27	716
Subtotal - Deferred Members	1,665	1,377
<u>Pending - Retirement or Withdrawal Members</u>		
General	598	766
Safety	15	34
Subtotal - Pending Members	613	800
<b>Total Active, Deferred, and Pending</b>	<b>24,950</b>	<b>24,900</b>

**Retired Personnel Receiving Benefits**  
(unaudited)

	December 31, 2003			December 31, 2002		
	Gen.	Safety	Total	Gen.	Safety	Total
Service Retirements	5,962	680	6,642	5,892	592	6,484
Continuances	1,065	94	1,159	661	52	713
Subtotal	7,027	774	7,801	6,553	644	7,197
Service Connected						
Disability	564	307	871	546	305	851
Continuances	-	11	11	46	20	66
Subtotal	564	318	882	592	325	917
Nonservice - Connected						
Disability	247	16	263	448	29	477
Continuances	4	-	4	95	2	97
Subtotal	251	16	267	543	31	574
Total Retired Personnel	7,842	1,108	8,950*	7,688	1,000	8,688

#### 14. Employee Purchased Annuities

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

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

#### 15. Federal Income Tax Status

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

is being operated in compliance with the applicable requirements of the Code and, therefore, believes that the Plan is qualified and the related trust is tax exempt.

### B. Summary of Significant Accounting Policies

#### 1. Basis of Accounting

OCERS' financial statements are prepared on the accrual basis of accounting. Contributions from employers and members are recognized when due pursuant to formal commitments, as well as statutory requirements; benefits and refunds are recognized when payable in accordance with the provisions of the plan. Investment income is recognized as revenue when earned. The net appreciation (depreciation) in fair value of assets held by OCERS is recorded as an increase (decrease) to investment income based on the valuation of investments at year end. Expenses are recorded when corresponding liabilities are incurred, regardless of when payment is due. OCERS has elected to apply GASB Statement No. 20, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities That Use Proprietary Fund Accounting*.

#### 2. Valuation of Investments

Quoted market prices are used to value United States Government and agency securities, corporate and foreign bonds and debentures, and domestic and international common stocks. Real estate equity

\*Excludes 129 Qualified Domestic Relations Orders (QDRO) payees.

investments are stated at fair value, determined by independent appraisals performed on the properties held. The values of venture capital funds and limited partnership investments were determined by the investment managers based on the underlying financial statements and performance of the investments and acceptable valuation methodologies.

### 3. Capital Assets

Capital assets are carried at cost less accumulated depreciation. Depreciation is calculated using the straight-line method with a 10 year useful life for computer software, and 5 to 15 years for equipment and furniture. The cost and accumulated depreciation of capital assets at December 31, 2003 and 2002, were as follows:

	2003	2002
Furniture and Equipment	\$ 1,784,000	\$ 1,784,000
Computer Software	4,887,000	3,883,000
Total Capital Assets (at cost)	6,671,000	5,667,000
Less Accumulated Depreciation	(2,440,000)	(2,129,000)
Total Capital Assets Net of Depreciation	\$ 4,231,000	\$ 3,538,000

### 4. Reclassification

Certain figures on the Statement of Changes in Plan Net Assets for year 2002 have been reclassified to conform with year 2003 presentation.

## C. Contributions Required and Contributions Made

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

Present members' accumulated contributions at December 31, 2003 and 2002, were \$927,971,000 and \$858,121,000, respectively, including interest credited. Interest was credited at an interest rate of 5.0% per annum as of June 30, on the balance of the members' accounts as of the prior

December 31 and as of December 31 on the balance of the members' accounts as of the prior June 30. The incremental difference of 2.5% is credited to the Employer Reserves account.

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

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

For accounting purposes, OCERS maintains the proceeds for the POB's in the County Investment Account (Investment Account). OCERS and the County of Orange, a single participating district, entered into an agreement which provided an offsetting credit based upon an amount actuarially determined to deplete the County Investment Account over the then remaining UAAL amortization period. The offsetting credits for years 2003, 2002, 2001, 2000, 1999 and 1998 were \$26,209,000, \$65,180,000, \$41,319,000, \$48,555,000, \$47,129,000 and \$42,020,000, respectively.

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

Subsequently, in 1996, the Board of Retirement and the County of Orange entered into an agreement for the use of the Investment Account over a new funding period of 20 years. The agreement provided that the Investment Account would be used to fund the County's employer contribution and in a decreasing percentage each year. In 1997, the Investment Account funded approximately 90% of the County's employer contribution and the County made cash contributions for the remaining 10%. For each subsequent year the funding by the Investment Account would decrease by 5.0% annually, while the County of Orange employer cash contribution would increase by a corresponding amount.

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

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As of December 31, contributions for 2003 and 2002 were approximately \$205,824,000 (\$124,243,000 employer and \$81,581,000 member) and \$91,206,000 (\$13,289,000 employer and \$77,917,000 member), respectively, consisting of:

	<b>2003</b>	<b>2002</b>
Normal Cost	\$ 172,353,000	\$ 114,482,000
Amortization of Unfunded Actuarial Accrued Liability	33,471,000	(20,276,000)
<b>Total</b>	<b>\$ 205,824,000</b>	<b>\$ 91,206,000</b>

The contributions to OCERS for 2003 and 2002 were made in accordance with the actuarially determined requirements as follows:

**Percent of Members' Payroll**

	<u>07/03–12/03</u>	<u>07/02–06/03</u>	<u>07/01–06/02</u>
<b>Employer Contributions - General - OCTA</b>			
Normal Cost	4.36%	4.20%	4.94%
Amortization of Unfunded Actuarial Accrued Liability	3.37%	0.27%	-3.98%
Subtotal	7.73%	4.47%	0.96%
Additional Contribution	0.50%	0.50%	0.00%
<b>Total</b>	<b>8.23%</b>	<b>4.97%</b>	<b>0.96%</b>
<b>Employer Contributions - General - Non-OCTA</b>			
Normal Cost	5.44%	5.04%	4.94%
Amortization of Unfunded Actuarial Accrued Liability	3.21%	0.12%	-3.98%
Subtotal	8.65%	5.16%	0.96%
Additional Contribution	0.50%	0.50%	0.00%
<b>Total</b>	<b>9.15%</b>	<b>5.66%</b>	<b>0.96%</b>
<b>Employer Contributions - Safety - Law Enforcement</b>			
Normal Cost	16.53%	15.87%	8.57%
Amortization of Unfunded Actuarial Accrued Liability	20.84%	8.65%	0.16%
Subtotal	37.37%	24.52%	8.73%
Additional Contribution	0.50%	0.50%	0.00%
<b>Total</b>	<b>37.87%</b>	<b>25.02%</b>	<b>8.73%</b>
<b>Employer Contributions - Safety - Fire Protection</b>			
Normal Cost	17.85%	10.30%	8.57%
Amortization of Unfunded Actuarial Accrued Liability	16.31%	1.39%	0.16%
Subtotal	34.16%	11.69%	8.73%
Additional Contribution	0.50%	0.50%	0.00%
<b>Total</b>	<b>34.66%</b>	<b>12.19%</b>	<b>8.73%</b>

## Percent of Members' Payroll (Continued)

	07/03–12/03	07/02–06/03	07/01–06/02
<u>Employer Contributions - Safety - Probation</u>			
Normal Cost	4.38%	5.04%	4.94%
Amortization of Unfunded Actuarial Accrued Liability	3.69%	0.12%	-3.98%
Subtotal	8.07%	5.16%	0.96%
Additional Contribution	0.50%	0.50%	0.00%
<b>Total</b>	<b>8.57%</b>	<b>5.66%</b>	<b>0.96%</b>
<u>Employer Contributions - City of San Juan Capistrano 2.7%</u>			
Normal Cost	5.44%	5.04%	4.94%
Amortization of Unfunded Actuarial Accrued Liability	7.65%	0.12%	-3.98%
Subtotal	13.09%	5.16%	0.96%
Additional Contribution	0.50%	0.50%	0.00%
<b>Total</b>	<b>13.59%</b>	<b>5.66%</b>	<b>0.96%</b>
<u>Employer Contributions - City of Rancho Santa Margarita 2.5%</u>			
Normal Cost	1.69%	N/A	N/A
Amortization of Unfunded Actuarial Accrued Liability	3.40%	N/A	N/A
Subtotal	5.09%	N/A	N/A
Additional Contribution	0.00%	N/A	N/A
<b>Total</b>	<b>5.09%</b>	<b>N/A</b>	<b>N/A</b>

The Memorandum of Understanding (MOU) between OCERS and all participating employers requires that Employer Contributions must increase by the lesser of .50% of pay or the amount necessary to increase OCERS' Unallocated Fund Balance (UFB) to 3% of OCERS' adjusted total assets. The balance of the UFB as of December 31, 2003 was zero; therefore, Employer Contributions for the fiscal year beginning July 1, 2003 increased by .50% of pay to restore the UFB to the 3% of OCERS' adjusted total assets. The total payments made during the second and third quarters of calendar year 2003 pursuant to such provision was \$2,141,722.

#### D. Plan Termination

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

#### E. Investments

##### 1. Investments Authorized

Investments in securities are held by the Plan's custodian, State Street Bank and Trust Company.

Government Code Section 31595 authorizes OCERS to invest in any form or type of investment deemed prudent, including security lending transactions, in the informed opinion of the Retirement Board, except as otherwise expressly restricted by California Constitution or by law.

##### 2. Investment Concentration

At December 31, 2003 and 2002, OCERS had investments in Barclays Global Investors (BGI) Russell 1000 that individually represented 15.34% and 13.87%, respectively of OCERS' plan net assets. In addition, OCERS had investments in BGI Fixed Income Index for the same periods that represented 15.32% and 7.18% respectively of OCERS' plan net assets. No other investments exceeded 5.00% of the system's net assets.

##### 3. Cash and Cash Equivalents

OCERS' investment portfolios may not be entirely invested in securities at a given time. Those funds not in the form of securities are invested in short-term

money market funds including the Orange County Investment Pool. In addition OCERS maintains an operating cash balance at a local financial institution, Wells Fargo Bank, to be used for retirement payroll and other operational expenses. At December 31, 2003, OCERS had money market funds of \$634,499,000 invested with OCERS' master trust custodian bank, State Street Bank and Trust Company, \$21,786,000 invested with Wells Fargo Bank and \$16,284,000 invested with the Orange County Investment Pool. All of the cash invested is uninsured and uncollateralized; interests in the money market funds and in the Orange County Investment Pool are computed on an average daily balance. The total amount classified as Cash and Cash Equivalents as of December 31, 2003 was \$672,569,000.

#### 4. Credit Risk

OCERS' investments are categorized below to give an indication of the level of risk assumed by OCERS at year-end. The categories are:

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

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

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

Investments not evidenced by securities are not categorized. The investment values (in thousands) at December 31, 2003 are summarized as follows:

	<b>Cost</b>	<b>Fair Value</b>
<u>Category 1 Classification</u>		
U.S. Government Debt Securities	\$ 16,756	\$ 13,721
Corporate Debt Securities	191,195	206,052
Foreign Bonds	209,658	230,954
Domestic Equity Securities	779,254	907,402
International Equity Securities	365,929	451,750
Subtotal	1,562,792	1,809,879
<u>Amounts Not Subject to Classification</u>		
Investments Held by Broker-Dealers Under Securities Loans with Cash Collateral:		
U.S. Government Bonds	74,616	80,848
Corporate Debt Securities	14,474	16,773
U.S. Government Debt Securities	97,633	104,219
Domestic Equity Securities	46,234	57,371
International Equity Securities	75,305	98,835
Foreign Bonds	5,986	6,606
Orange County Treasurer's Pooled Investment	16,284	16,284
Real Estate Investments	262,057	250,291
Domestic Equity Index Fund	911,544	762,734
International Pooled Equity Funds	158,277	197,654
Domestic Pooled Fixed Income	678,450	761,977
Alternative Investment in Venture Capital and Limited Partnership	193,496	152,357
Subtotal	2,534,356	2,505,949
Less: Orange County Treasurer's Pooled Investment	(16,284)	(16,284)
<b>Total Investments</b>	<b>\$ 4,080,864</b>	<b>\$ 4,299,544</b>

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

## 5. Net Appreciation (Depreciation)

During 2003 and 2002, OCERS' investments (including investments bought and sold, as well as held during each year) appreciated (depreciated) in values by \$649,697,000 and by (\$407,177,000), respectively, as follows:

	Years Ended December 31 (in thousands)	
	2003	2002
Net Appreciation (Depreciation) in Fair Value as Determined by Quoted Market Prices:		
Domestic Equity Securities	\$ 414,694	\$ (318,168)
United States Government Debt Securities, Corporate & Foreign Bonds & Debentures	102,152	74,098
International Equity Securities	194,425	(117,575)
Subtotal	711,271	(361,645)
Net Appreciation (Depreciation) in Fair Value as Determined by Estimated Fair Value:		
Real Estate	(33,636)	(5,545)
Alternative	(27,938)	(39,987)
Total Net Appreciation (Depreciation)	\$ 649,697	\$ (407,177)

## 6. Securities Lending Contracts

Included in the investment accounts for United States Government securities, international securities, corporate bonds and debentures, foreign bonds and debentures, and common stocks at December 31, 2003 and 2002 were securities with fair values of \$283,805,000 and \$220,437,000 respectively, which had been lent by OCERS, through a securities lending agent, to various securities brokers in return for cash collateral equal to 102 percent (105 percent for international investments) of the fair value (priced daily) of the securities lent, and additional collateral has to be provided by the next day if its value falls to less than 100 percent of the fair value of the securities lent. OCERS invests the cash collateral in short-term securities that cannot be pledged or sold by OCERS unless the borrower defaults. Securities on loan at year-end are presented as unclassified in the preceding schedule of custodial credit risk. In lending of both domestic and international securities, the term to maturity of the securities lent is matched with the term to maturity of the investment of collateral. Such matching existed at year-end. There are no restrictions on the amount of securities that can be lent at one time. There were no violations of the security lending provisions that occurred during 2003.

OCERS invested the cash collateral in short-term securities, which included certificates of deposit and commercial paper from certain domestic banks and savings and loans, repurchase agreements through certain brokers, and certain money market funds. Investments purchased with cash collateral are held by State Street Bank and Trust Company in separate collateral accounts. The contract with State Street Bank and Trust Company requires it to indemnify OCERS if the borrowers fail to return the securities (and if the collateral is inadequate to replace the securities lent). The risks involved in a security lending program generally include: borrower bankruptcy, collateral deficiencies, problems with settlements, corporate actions, and dividends and interest. OCERS had no losses on securities lending transactions resulting from the default of a borrower or the lending agents for the years ended December 31, 2003 and 2002.

Gross security lending revenues for 2003 and 2002 were \$1,236,000 and \$1,580,000 respectively. The costs of securities lending transactions are reported as investment expenses in the accompanying financial statements.

OCERS' securities lending agents are responsible for monitoring the fair value of the securities lent to

ensure that the value of the collateral equals or exceeds 100 percent of the fair value of the securities lent as of the valuation date. At December 31, 2003 and 2002, OCERS held broker collateral with fair values totaling \$290,166,000 and \$227,024,000, respectively. At year end, the system has no credit risk exposure to borrowers because the amounts the system owes the borrowers exceed the amounts the borrowers owe the system.

## 7. International Investments

Investments in international securities are managed by three investment managers. Other investments are held in two pooled funds, all of which are invested in equities of companies located in international markets.

## 8. Alternative Investments

OCERS' alternative investments represent investments made in private debt and equity securities through limited partnership and venture capital arrangements. OCERS has employed two investment methods. One method is the use of investment management firms to invest OCERS' assets in limited partnerships as well as direct private placements. The second method of investment is OCERS' participation as a limited partner in limited partnership funds. As of December 31, 2003, OCERS has approximately \$80,656,000 of open commitments in four alternative investments. These investments are diversified between venture capital, corporate finance, buyout, energy, and oil and gas investments.

## 9. Derivative Holdings Held for Trading Purposes

Of the total investments in OCERS' domestic fixed income portfolio of \$1,183,590,000 as of December 31, 2003, approximately \$114,820,000 are classified as derivative securities in accordance with the GASB definition (see note F for other derivative investments). These holdings include asset-backed securities, mortgage-backed securities, zero coupon bonds, variable rate securities, fixed income options, and interest rate caps. The investment objective of these derivative securities is to achieve favorable yields and advantageous risk/reward profiles with the vast majority of the holdings being guaranteed by either the U.S. Government or one of its agencies. Details of these derivative securities are as follows:

Securities	Fair Value	Fair Value
	2003	2002
FHLMC	\$30,066,000	\$20,361,000
FNMA	54,429,000	198,148,000
GNMA	9,169,000	97,763,000
CMO	4,135,000	20,670,000
Others	17,021,000	33,354,000
Total Derivative Securities	\$114,820,000	\$ 370,296,000

## F. Financial Investments with Off Balance Sheet Risk

### 1. Forward Currency Contracts

OCERS' international investment managers invest in forward currency contracts. These are agreements to exchange different currencies at specified rates and settlement dates. Differences between the contract and market exchange rates at settlement result in gains or losses. Risks arise from the possible inability of counterparties to meet the terms of their contracts and from movements in exchange and interest rates. OCERS' balances for the forward currency receivables and payable accounts are based upon the currencies' contract exchange rates in relation to their market exchange rates at December 31, 2003 and 2002. An accounts receivable balance that is greater than the payable balance represents a net gain on the contracts. An accounts receivable balance that is less than the payable balance indicates a net loss. At December 31, 2003 and 2002, OCERS had net forward currency contract receivables of \$378,000 and \$285,000, respectively.

### 2. Financial Futures Contracts Held for Purposes Other than Trading

The net changes in fair value of financial futures contracts held for purposes other than trading comprised (\$631,000) and \$3,337,000 of net appreciation (depreciation) during 2003 and 2002, respectively. As of December 31, 2003 and 2002, OCERS had open contracts of \$82,035,000 and \$46,716,000, respectively, for the purchase of U.S. Treasury notes and Financial Future Euro Dollars with delivery at specified future dates. Risks arise from movements in securities values and interest rates.

OCERS is required to maintain a deposit with the broker as collateral to support open futures contracts. As of December 31, 2003 and 2002, OCERS had collateral deposits of \$3,280,000 and \$2,405,000, respectively, in cash equivalents, U.S. Treasury bills and notes.

### G. Administrative Expenses

Section 31580.2 of the Government Code limits the annual administrative expenses of the retirement system to 18/100 (18 basis points) of the total assets of the retirement system. Total administrative expenses for the year ended December 31, 2003 were \$7,312,000 or approximately 14.74 basis points. As of December 31, 2003, 18 basis points of the assets of the system was approximately \$9,540,000. Additionally, Section 31596.1 of the Government Code allows certain costs to be excluded from administrative expenses that are subject to statutory limitation. The excluded costs are included in the amounts classified as administrative expenses for OCERS' financial statements.

	Years Ended December 31	
	(in thousands)	
	2003	2002
Expenses Subject to Statutory Limitation:		
Personnel Services:		
Board Members' Allowance	\$ 13	\$ 12
Employee Salaries and Benefits	4,167	3,871
Total Personnel Services	4,180	3,883
Office Operating Expenses:		
Operating Expenses	856	865
Professional Services	1,216	1,149
Rent/Leased Real Property	750	861
Depreciation/Amortization	310	193
Total Office Operating Expenses	3,132	3,068
Total Expenses Subject to Statutory Limitation	7,312	6,951
Expenses Not Subject to Statutory Limitation:		
Commingled Interest Cost	11	3
Actuarial Fees	354	254
Fund Evaluation Costs	315	313
Custodian Services	321	309
Investment Department Expenses	474	308
Legal Costs	4	29
Additional Death Benefit Costs	57	112
Total Expenses Not Subject to Statutory Limitation	1,536	1,328
Total Administrative Expenses	\$ 8,848	\$ 8,279

**H. Reserve Accounts**

The plan net assets of \$4,959,626,000 as of December 31, 2003 include reserves of \$4,720,122,000 and unreserved net assets of \$239,504,000. The unreserved net assets include the County Investment Account. The reserve balances as of December 31, 2003 are as follows (in thousands):

	Active Members Reserve	Retired Members Reserve	Employer Advanced Reserve	ARBA Reserve	RMBR Reserve	Total Reserves
General Ledger Balance	\$ 927,970	\$ 2,503,128	\$ 1,268,602	\$ -	\$ 20,422	\$ 4,720,122
Less: Accounts Receivable for						
Interest Credited to Reserves	(15,351)	(60,722)	(46,849)	-	-	(122,922)
Net Reserves	\$ 912,619	\$ 2,442,406	\$ 1,221,753	\$ -	\$ 20,422	\$ 4,597,200

The Additional Retiree Benefit Account (ARBA) results from a Memorandum of Understanding (MOU) with the County of Orange and subsequently with all employers. The amounts maintained in the ARBA are to be applied to health insurance or other supplemental benefits for OCERS' retirees. There were no transfers to the ARBA accounts in years 2002 and 2003 because the UFB was zero.

The Retirement Board adopted the creation of the Retired Members Benefit Reserve (RMBR) for OCERS' retirees in the year 2002 to ensure the continued funding of the retiree supplemental benefits for three years. All participating agencies could transfer a projected three year benefit payment to the RMBR balance that was created as a sub-account of the Employer Advanced Reserve Account. The RMBR account will be used to pay additional benefits to retirees in lieu of payments out of the ARBA balance in circumstances where the ARBA balance is depleted. The RMBR balance will not receive the bi-annual interest credit and it will be funded on a three year rolling method. The balance of the RMBR at year-end was approximately \$20,422,000.

# Required Supplementary Information

**Schedule of Funding Progress for the Years Ended December 31**  
(in thousands)

Actuarial Valuation Date December 31	Actuarial Value (\$) of (a)	Actuarial Accrued Liability (\$) (b)	Total Unfunded Actuarial Accrued Liability (UAAL) (\$) (b-a=c)	Funded Ratio (%) (a/b)	Covered Payroll (\$) (d)	UAAL as a Percentage (%) of Covered Payroll (c/d)
1998	3,504,708	3,682,686	177,978	95.17%	863,199	20.62%
1999	3,931,744	4,017,279	85,535	97.87%	912,490	9.37%
2000	4,497,362	4,335,025	(162,337)	103.74%	994,669	-16.32%
2001	4,586,844	4,843,899	257,055	94.69%	1,122,763	22.89%
2002	4,695,675	5,673,754	978,079	82.76%	1,242,348	78.73%
2003	4,790,099	6,099,433	1,309,334	78.53%	1,243,964	105.25%

**Note:**

1. The 12/31/98, 12/31/99, 12/31/00, 12/31/01, 12/31/02 and 12/31/03 actuarial value of assets exclude \$322,333,000, \$302,909,000, \$286,139,000, \$272,789,000, \$221,643,000, \$143,675,000 and \$143,744,000 of the County Investment Account balances respectively. Effective December 31, 2002, the Retirement Board elected to change the amortization period for the General Member and Probation Officer unfunded actuarial accrued liability (UAAL) to 30 years. The amortization is a level dollar amount.

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

**Schedule of Employer Contributions for the Years Ended December 31**  
(in thousands)

	2003	2002	2001	2000	1999	1998
Annual Required Contribution*	\$124,243	\$13,289	\$12,060	\$15,561	\$17,591	\$17,977
Percentage Contributed	100%	100%	100%	100%	100%	100%

\* Employer contributions reflect cash payments only. Please see Note C on page 27 for amounts transferred from the County Investment Account.

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

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

### Actuarial Assumptions and Method

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

Valuation date	12/31/2003.
Actuarial cost method	Projected Unit Credit.
Amortization method	Level dollar (closed)
Remaining amortization period	20 years (closed) for Fire Authority and Law Enforcement personnel.
Remaining amortization period	29 years (closed) for others.
Asset valuation method	5-year moving average of the ratio of market value to book value multiplied by the current year's book value.
Actuarial assumptions	
Investment rate of return	7.5%
Projected Salary Increases	4.5% per annum
Includes inflation at	4.5% subject to Tier maximum.
Cost-of-living adjustments	3% per annum with excess banked.

### Significant Factors Affecting Trends in Actuarial Information

#### 2003 Changes in Plan Provisions and Actuarial Assumptions Since Prior Year

The City of Rancho Santa Margarita, a new plan sponsor, adopted a 2.5% at 55.  
Retirement formula for the City of San Juan Capistrano changed to 2.7% at 55.

#### 2002 Changes in Plan Provisions and Actuarial Assumptions Since Prior Year

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

#### 2001 Changes in Plan Provisions and Actuarial Assumptions Since Prior Year

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

#### 1998 Changes in Plan Provisions and Actuarial Assumptions Since Prior Year

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

#### 1997 California Supreme Court Decision - Ventura County

Expanded the definition of compensation earnable.

#### 1995 Changes in Plan Provisions and Actuarial Assumptions Since Prior Year

Salary scale changed from 6.0% to 3.5% per annum per individual through the year 2000, and 5.5% thereafter.

#### 1993 Changes in Plan Provisions and Actuarial Assumptions Since Prior Year

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

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

# Other Supplementary Information

**Schedule of Administrative Expenses**  
**Years Ended December 31, 2003 and 2002**  
(in thousands)

	2003	2002
<b>Expenses Subject to Statutory Limitation</b>		
Personnel Services:		
Board Members' Allowance	\$ 13	\$ 12
Employee Salaries and Benefits	4,167	3,871
<b>Total Personnel Services</b>	<b>4,180</b>	<b>3,883</b>
Professional Services:		
Legal Fees	268	478
Financial and Internal Audits	75	99
Mortality Verification	4	5
Information Technology Consultant	380	5
Team Building Consultant	-	40
Governance Workshop	-	55
Hearing Officers/Medical Consultants	305	279
Financial Strategy Seminars	13	11
Miscellaneous	171	177
<b>Total Professional Services</b>	<b>1,216</b>	<b>1,149</b>
Other Operating Expenses:		
Telephone and Communication	74	52
Maintenance	243	249
Printing and Duplicating	140	126
Building and Equipment Leases	750	861
Transportation, Travel and Training	93	149
Postage Expenses	194	151
Office Supplies and Expenses	112	138
Depreciation Expenses	310	193
<b>Total Other Operating Expenses</b>	<b>1,916</b>	<b>1,919</b>
<b>Total Expenses Subject to Statutory Limitation</b>	<b>7,312</b>	<b>6,951</b>
<b>Expenses Not Subject to Statutory Limitation</b>		
Fund Evaluation Cost	315	313
Custodian Services	321	309
Commingled Interest Cost	11	3
Actuarial Cost, net	354	254
Legal Costs	4	29
Additional Death Benefits Cost	57	112
Investment Department Expenses	474	308
<b>Total Expenses Not Subject to Statutory Limitation</b>	<b>1,536</b>	<b>1,328</b>
<b>Total Administrative Expenses</b>	<b>\$ 8,848</b>	<b>\$ 8,279</b>

**Schedule of Payments for Professional Services**  
**Years Ended December 31, 2003 and 2002**  
(in thousands)

Name of Firms	Type of Services	2003	2002
<b>Professional Expenses Subject to Statutory Limitation</b>			
County of Orange	Board Elections	\$ 39	\$ -
County of Orange	AHRS Dial Up & Others	19	26
County of Orange	Cost Allocation (CWCAP)	18	21
Kathleen Wells Webster & Assoc.	Team Building Workshop	-	40
DMG Maximus, Inc.	Recruitment Costs	-	25
Epoch Internet	Internet Access	-	15
Netifice Communication, Inc.	Internet Usage	15	-
Cortex Applied Research	Governance Workshop	-	55
Manpower, Inc.	Temporary Personnel	61	53
E-Partners	System Consulting	1	5
Valarie Desporough	Transcribing Services	21	22
Ice Miller	Legal Services	-	10
Barbara Evans	Legal Services	-	16
Hanson Bridgett	Legal Services	10	7
Foley & Lardner	Legal Services	55	63
Steeffel, Levitt & Weiss	Legal Services	127	351
Schott & Lites Advocates	Legislative Counseling	18	-
Various Firms	Legal Services	11	-
Link, Murrel & Company	Audit Services	75	99
The Berwyn Group	Mortality Verification	4	5
Various Firms	Disability/Medical Hearings	352	310
Financial Management Specialists	Financial Strategy Seminars	13	10
Iron Mountain	Offsite Data Storage	4	-
Linea Solutions	System Consulting	162	-
Levi, Ray, & Shoup, Inc.	System Improvement	202	-
Various Professional Firms	Other Services	9	16
<b>Total Professional Expense Subject to Limitation</b>		<b>\$ 1,216</b>	<b>\$ 1,149</b>
<b>Professional Expenses Not Subject to Statutory Limitation</b>			
Callan Associates, Inc./ The Townsend Group	Performance Evaluation	282	297
EEI Analytical	Performance Evaluation	1	-
G. Shilling	Board and Staff Education	5	-
ISI Group	Performance Evaluation	25	-
Gillespie, Dough	Performance Evaluation	2	-
State Street Bank and Trust Company	Master Trust Custody	321	309
Bankers Trust	Master Trust Custody	-	16
County of Orange	Commingled Interest Cost	11	3
Towers Perrin	Actuarial Services	354	254
Stradling, Yocca, Carlson, & Rauth	Legal Counsel	4	29
Additional Death Benefits Cost	Member Benefits	57	112
Investment Department Expenses	Investment Expenses	474	308
<b>Total Professional Expenses Not Subject to Limitation</b>		<b>1,536</b>	<b>1,328</b>
<b>Total All Professional Expenses</b>		<b>\$ 2,752</b>	<b>\$ 2,477</b>

**Schedule of Fees and Other Investment Expenses**  
**Years Ended December 31, 2003 and 2002**  
(in thousands)

	<b>2003</b>		<b>2002</b>
Domestic Equity	\$ 3,591	\$	3,284
International Equity	2,390		2,937
Global Fixed Income	2,921		3,466
Real Estate	2,784		3,648
Venture Capital	4,402		4,093
Other Alternative Investments	681		838
<b>Total Fees &amp; Other Investment Expenses</b>	<b>\$ 16,769</b>	<b>\$</b>	<b>18,266</b>



SECTION

3

A zookeeper in a khaki uniform and cap stands in an enclosure. In the foreground, a sloth is resting on a rock. To the left, a waterfall flows over a rocky ledge. The background features a large, textured rock wall and a wire mesh fence. The scene is set outdoors with lush green foliage.

**> INVESTMENT**

# CALLAN ASSOCIATES<sup>BMC</sup>



SAN FRANCISCO

NEW YORK

CHICAGO

ATLANTA

DENVER

April 19, 2004

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

Dear Board Members:

This letter reviews the investment performance of the Orange County Employees Retirement System (OCERS) for the calendar year ended December 31, 2003.

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

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

After three poor years, the equity markets rebounded strongly in 2003. The S&P 500 rose 28.68%, the Dow was up 28.20% and the NASDAQ jumped 50.76%. Small stocks and technology especially shined. In fact, many stocks in the S&P 500 and Russell 2000 ended the year higher than they were when the indexes peaked in 2000. The best performers for the year were low priced stocks, stocks of companies with no earnings and small cap stocks. High quality, very large companies enjoyed attractive gains but lagged the rebound in more speculative issues.

The year got off to a wobbly start over concerns of war with Iraq. However, the economy did stage a comeback, fueled by tax cuts, lean inventories and the lowest

interest rates in more than four decades. The economic rebound and a weak dollar provided the stimulus for the final missing piece: corporate profits, which had enjoyed a strong recovery.

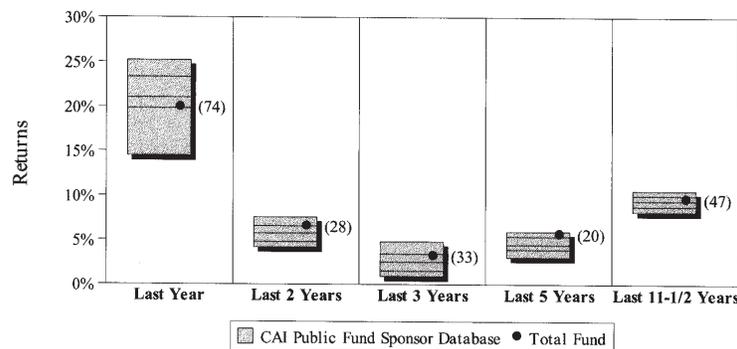
Within the fixed income market, the Lehman Aggregate posted a return of 4.10% for the year. Corporate bonds (7.70%) led all sectors in 2003. Treasuries lagged as investors sought higher yields. Interest rates on Treasury instruments were volatile during the year but ended near the same levels as of the end of 2002.

The resurgence in the overseas stock markets that began in the second quarter continued through the year, outperforming domestic stock indices. MSCI EAFE advanced 38.59% for the year. Nearly every corner of the globe participated. Stocks in Japan and Argentina rebounded in 2003. In dollar terms, some emerging markets saw triple-digit gains, including Brazil, Turkey and Thailand

For the calendar year, OCERS' total fund had a time-weighted total return of 19.84%. The return exceeded the System's strategic policy benchmark target return of 18.76%. The policy benchmark is comprised of the following indices in the percentages as indicated: Russell 3000 (33%); MSCI-All Country World ex-U.S. (14%); Lehman Brothers U.S. Universal Bond Index (34%); NCREIF Total Index (9%); Non-traditional assets (5%); and Salomon Non-\$ Bond Index Hedged (5%). Over the trailing 5-year period, a span that includes the last year of the bull market, three years of bear market and then one year of market recovery, OCERS has achieved an annualized return of 5.55%. While this return is below the System's actuarial earnings target, this result was better than the System's policy index return of 4.71% and ranked in the top quartile relative to other public funds. Over longer-term periods, the System's total return also has been strong particularly when evaluated on a risk adjusted basis. For example, the eleven and one-half year return (the longest for which Callan has performance data) of 9.51% was 6 basis points above the policy benchmark's 9.45% annualized return.

The graph below depicts the Total Fund relative to Callan's Total Public Fund Database for cumulative periods ended December 31, 2003.

**CAI Public Fund Sponsor Database**



The System's well-diversified and comparatively conservative allocation strategy was the primary driver in the achievement of strong relative performance results for all periods that include the difficult bear market of 2000-2002. It also explains the slightly lower than median performance during 2003. OCERS' better than target index performance was attributable to better than market performance in domestic equities, and both domestic and international bonds.

OCERS' domestic bond component strongly outperformed its target index for the year (+11.14% versus +5.82% for the Lehman U.S. Universal Bond Index). The outperformance for the year was primarily attributable to OCERS managers' emphasis on corporate bonds, including their exposure to BAA and lower rated securities. These securities had underperformed in the prior year but rebounded strongly in 2003 and significantly outpaced government securities. Over the long-term, OCERS' aggregate bond composite continues to outperform market indices and peers. For the eleven and one-half years ended 12/31/03, OCERS' bond composite ranks in the seventh percentile of the Public Fund database. The 8.79% annualized return exceeds the target index return of 7.43%.

OCERS' U.S. equity composite rebounded 32.02% in 2003. This result was better than the Russell 3000 Stock Index return of 31.06% and also better than the Callan Public Fund Domestic Equity peer group median. Over all cumulative periods considered, OCERS' domestic equity composite has achieved very strong comparative returns. For example, the trailing five-year return of positive 2.1% ranked in the 34th percentile and exceeded the target benchmark return of 0.55%.

OCERS' international equities achieved a composite return of 37.76%. While this result lagged the target index return of 41.41%, it did exceed the peer group median and importantly aided total fund performance.

In summary, calendar 2003 was an unusually strong year that was a very welcome change from the three preceding challenging years.

Sincerely,



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

## Investment Returns

The table below details the annualized rates of return for the different asset categories over various time periods ended December 31, 2003. The returns for each asset class represent the composite returns of all the manager portfolios within that asset class. All returns are gross of fees except for alternative assets and real estate, where some of the fees are deducted at source. The method of computation of investment return is time-weighted approximation.

	<b>1 Year</b>	<b>3 Year</b>	<b>5 Year</b>
Domestic Equity	32.02%	-0.26%	2.10%
<i>Russell 3000 Index</i>	31.06%	-3.08%	0.37%
International Equity	37.46%	-3.38%	2.90%
<i>MSCIAC World Ex US Index</i>	41.41%	-0.96%	1.55%
<i>MSCI Eafe Index</i>	38.59%	-2.91%	-0.06%
Domestic Fixed	11.14%	9.04%	7.78%
<i>Lehman Bros Universal Index</i>	5.82%	7.90%	6.88%
International Fixed Income	4.11%	8.29%	6.48%
<i>S/B Non-US Hedged Govt. Index</i>	1.89%	4.93%	5.44%
Cash & Equivalents	1.33%	2.94%	4.81%
Real Estate	7.99%	6.96%	8.11%
<i>NCREIF Property Index</i>	7.83%	7.87%	9.47%
Non - Traditional	2.03%	-12.10%	6.62%
Total Fund	19.84%	3.12%	5.55%
<i>Composite Policy Benchmark*</i>	18.76%	2.56%	4.71%

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

## STATEMENT OF INVESTMENT OBJECTIVES AND POLICIES

### General

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

### Strategic Asset Allocation Policy and Maintenance

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

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

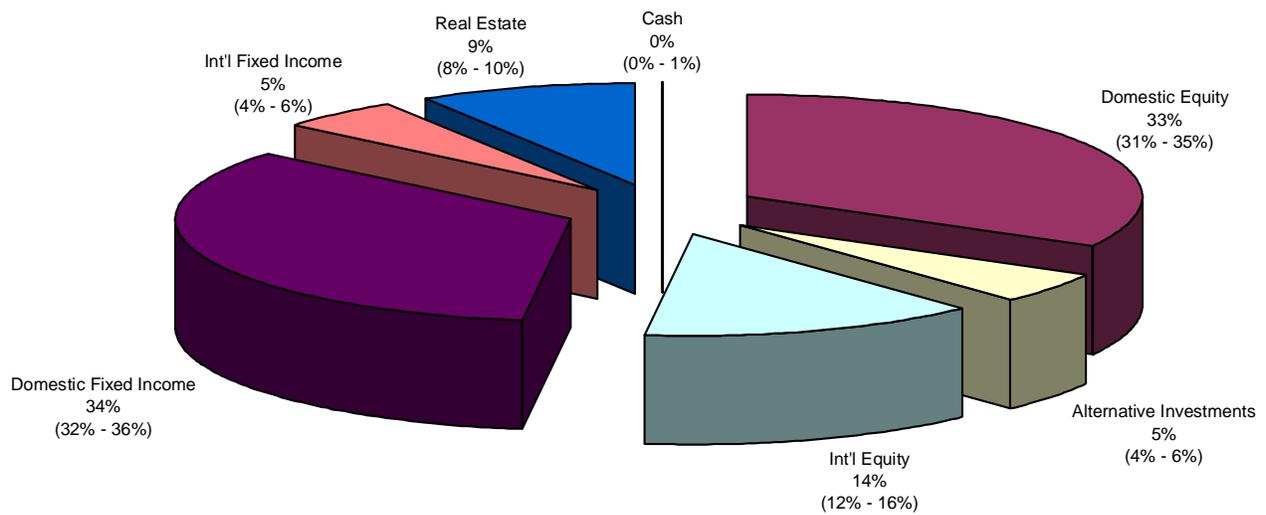
Should expected external flows be judged by staff to be insufficient to bring the plan within permitted ranges within a 12 month period, staff shall inform the Investment Committee. The Investment Committee then will formulate a recommendation to shift assets that will be presented to the full Board.

### Program Administration and Manager Structure

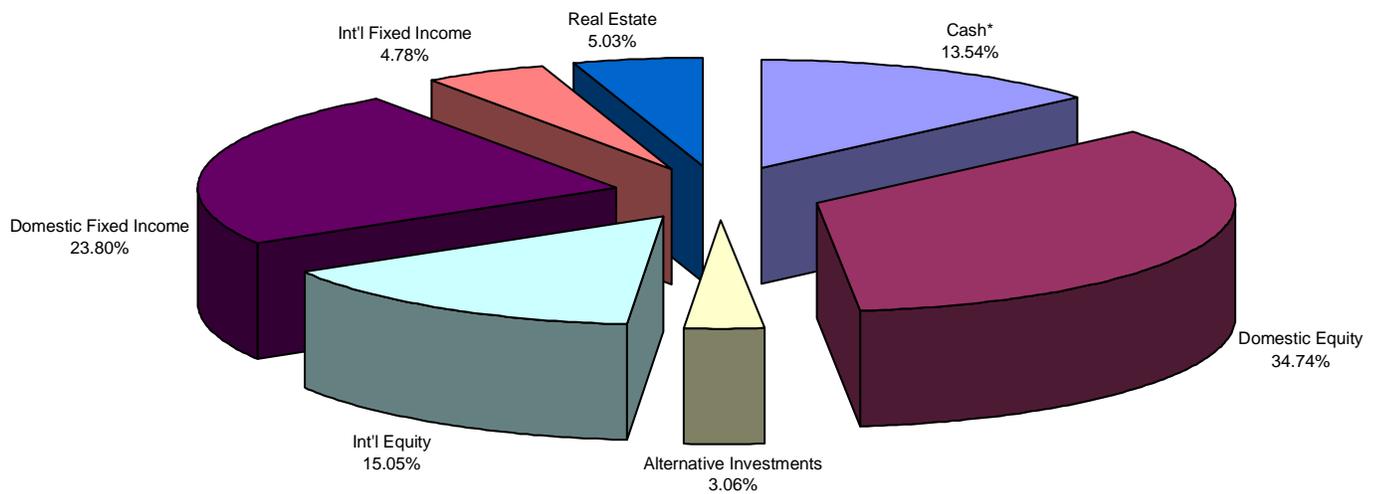
For each major asset class, the System shall diversify assets by employing managers with demonstrated skill in their particular areas of expertise. The System will retain managers who utilize varied investment approaches and allocate assets in a manner that is consistent with the overall strategic plan.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

## Asset Diversification December 31, 2003

### Policy

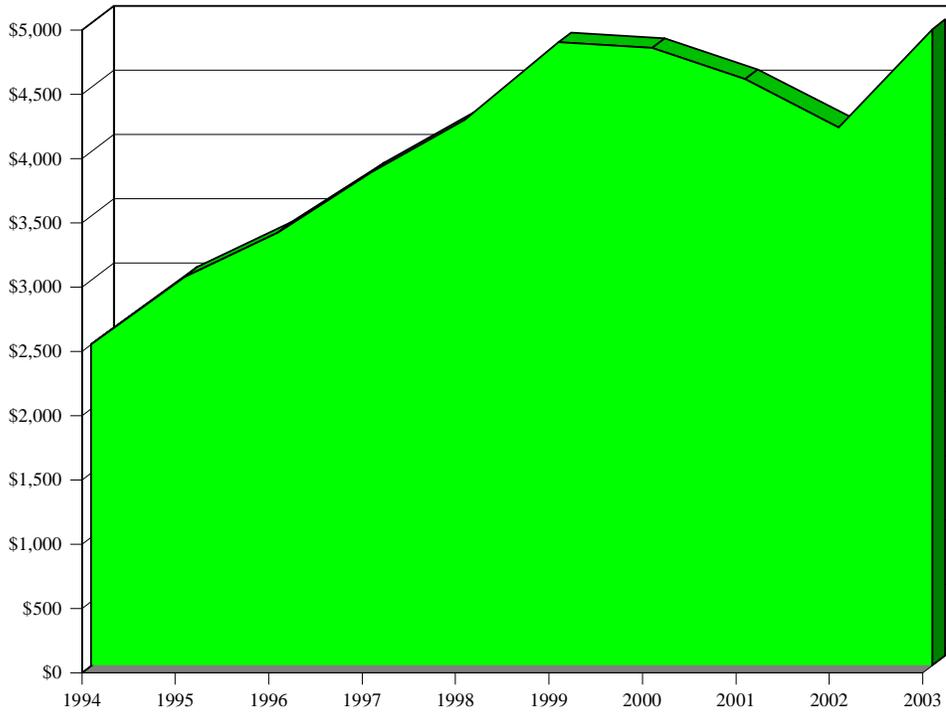


### Actual

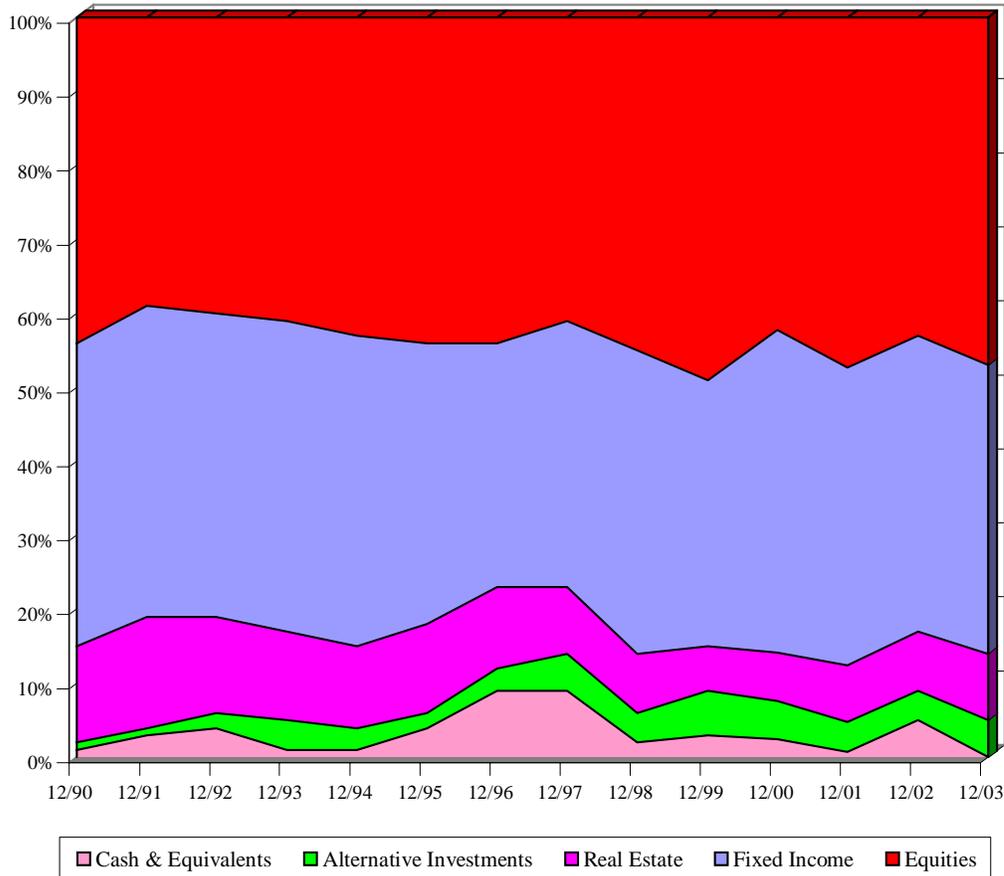


\*Includes cash equivalents held by investment managers.

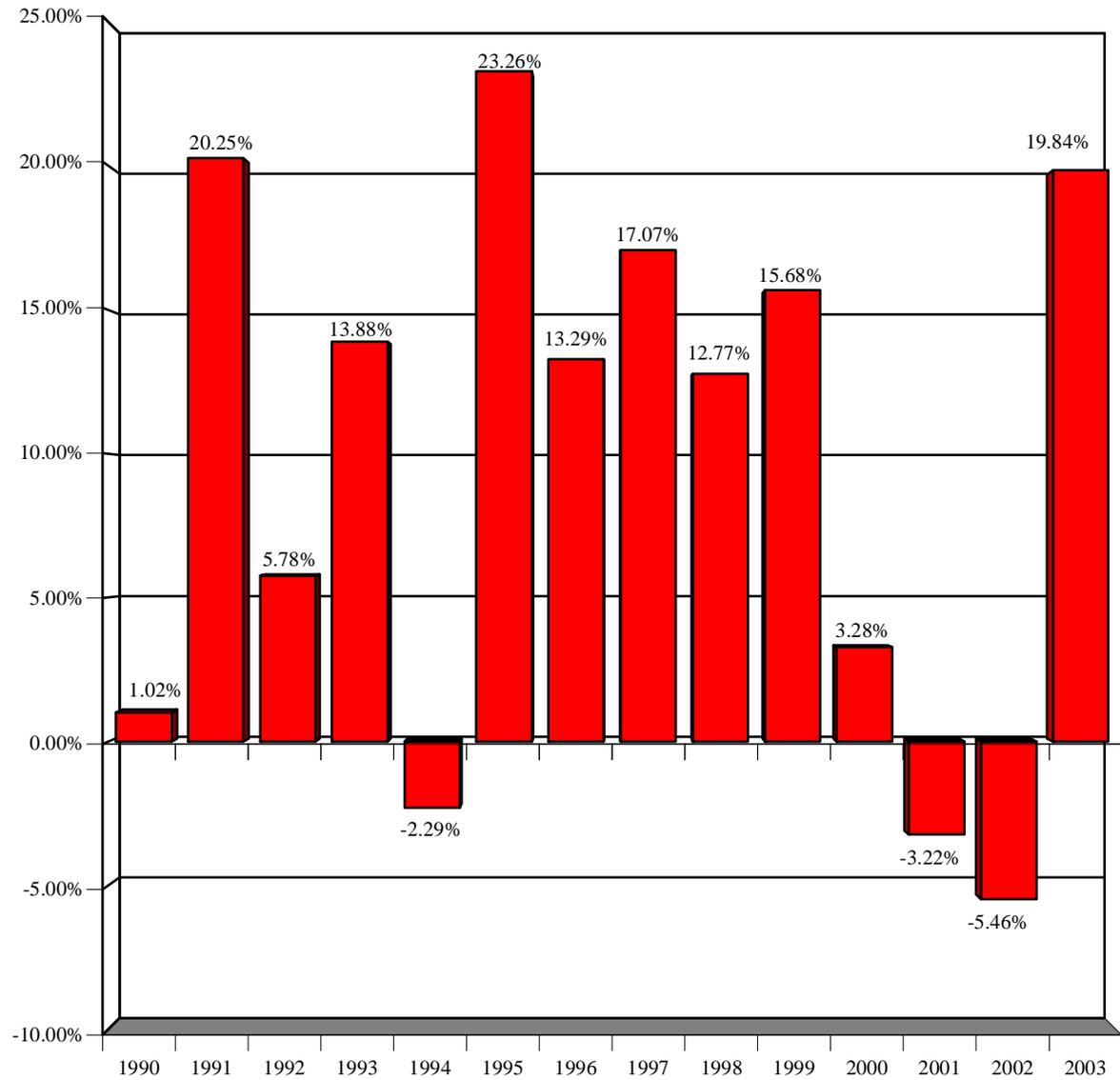
**Growth of System Net Assets at Fair Value  
for Ten Years Ended December 31, 2003**  
(in Millions of Dollars)



**Historical Asset Allocation  
(Actual)**  
**December 1990 – December 2003**



**History of Performance**  
(Based on Fair Value)  
**December 1990 – December 2003**



Schedule of Commissions  
for the Year Ended December 31, 2003

<b>Brokerage Firms</b>	<b>Number of <u>Shares Traded</u></b>	<b>Total <u>Commission</u></b>	<b>Commission <u>Per Share</u></b>
Abel Noser Corporation	918,300	33,650.00	0.03664
ABG Securities AS (Stockholm)	11,300	1,196.12	0.10585
ABN AMRO Auckland NZ.	86,000	643.41	0.00748
ABN AMRO Australia Limited	129,700	803.62	0.00620
ABN AMRO Equities (UK) Ltd. London	324,226	4,617.28	0.01424
ABN AMRO Securities (USA), Inc.	176,000	1,232.30	0.00700
Adams Harkness & Hill, Inc.	117,200	5,860.00	0.05000
Advest, Inc.	34,400	1,720.00	0.05000
America Growth Capital, LLC	65,500	3,275.00	0.05000
American Technology Research, Inc.	14,100	705.00	0.05000
Americas/Deutsche Bank AG London	7,400	370.00	0.05000
Arnold S Bleichroeder, Inc.	25,500	1,564.66	0.06136
Baird, Robert W. & Company Incorporated	299,200	14,947.00	0.04996
Banco Santander Central Hispano	40,200	950.43	0.02364
Bank Julius Baer (Deutschland) AG	12,800	106.66	0.00833
Bank of America Security LLC Montgomery Div.	926,514	35,676.15	0.03851
Bank of New York Clearing Services	17,500	858.00	0.04903
Banque Nationale De Paris, Lion	2,600	256.97	0.09883
Barclay's Global Investors, N.A.	2,457,437	7,584.18	0.00309
Baring Securities (Hong Kong)	109,600	2,122.44	0.01937
Bayerische Hypo Und Vereinsbank AG	9,500	1,605.97	0.16905
Bear Stearns & Co., Inc.	769,350	37,923.50	0.04929
Bear Stearns Securities Corporation	1,277,431	32,955.43	0.02580
BHC Securities, Inc.	194,900	9,003.00	0.04619
BHF Securities Corporation	196,200	2,843.36	0.01449
Blackwatch Broker AGE., Inc.	16,400	820.00	0.05000
BNP Paribas Securities Services	1,150,500	3,701.36	0.00322
Boston Institutional Services	18,500	925.00	0.05000
Brick Securities Div. Of Gerard Klauer	17,200	860.00	0.05000
Bridge Trading	425,234	18,797.83	0.04421
Broadcort Capital (Thru MI)	162,700	6,068.00	0.03730
Brockhouse & Cooper, Inc.	1,021,618	11,429.02	0.01119
Brown Brothers Harriman & Company	80,200	3,935.00	0.04906
B-Trade Services, LLC	574,242	11,548.34	0.02011
Buckingham Research Group	48,600	1,972.00	0.04058
Burnham Securities	2,700	135.00	0.05000
Canadian Imperial Bank Of Commerce	85,200	3,392.11	0.03981
Cantor Fitzgerald & Company	526,447	24,486.32	0.04651
Capital Institutional Services	435,846	7,095.03	0.01628
Carnegie International, Ltd.	10,000	765.65	0.07657
Cazenove Incorporated	51,729	942.16	0.01821
Charles Schwab Co., Inc.	1,899,343	94,912.15	0.04997
Chase Manhattan	64,619	1,223.99	0.01894
CIBC World Markets Corporation	391,050	19,409.62	0.04963
Citation Group	100,600	5,030.00	0.05000
Citigroup Global Markets, Ltd.	15,628,990	205,532.26	0.01315
CJS Securities	17,600	880.00	0.05000

<b>Brokerage Firms</b>	<b>Number of Shares Traded</b>	<b>Total Commission</b>	<b>Commission Per Share</b>
Commerce Capital Markets	3,500	175.00	0.05000
Commerzbank Capital Markets Corporation	56,400	1,639.72	0.02907
Compass Point Research and Trading	410,900	20,545.00	0.05000
Correspondent Services, Inc.	900	45.00	0.05000
Credit Agricole Indosuez Securities	388,100	11,339.45	0.02922
Credit Lyonnais Securities	358,440	9,495.81	0.02649
Credit Suisse First Boston	3,739,120	85,908.04	0.02298
Daiwa Securities America, Inc.	514,326	1,562.66	0.00304
Davidson D.A. & Company, Inc.	15,400	768.00	0.04987
Davis, Mendel And Regenstein	6,700	335.00	0.05000
Davy (J&E)	96,100	2,480.02	0.02581
Deutsche Bank Securities, Inc.	4,237,526	70,144.85	0.01655
Direct Brokerage, Inc.	6,600	132.00	0.02000
Donaldson, Lufkin & Jenrette Securities	13,800	634.00	0.04594
Dowling & Partners Securities, LLC	90,500	4,291.00	0.04741
Dresdner Kleinwort Wasserstein, LLC	4,885	494.26	0.10118
E Trade Securities, Inc.	52,400	2,620.00	0.05000
Edwards AG Sons, Inc.	62,600	3,308.00	0.05284
Enskilda Securities AB	209,100	4,897.30	0.02342
Exane, Inc.	54,500	3,854.63	0.07073
External Swap DVP	1,313,890	31,872.40	0.02426
F P Maglio & Co., Inc.	5,600	168.00	0.03000
Factset Data Systems (Thru Bear Stearns)	96,100	4,592.00	0.04778
Fano Securities, LLC	41,400	2,070.00	0.05000
Fidelity Capital Markets	58,650	2,932.50	0.05000
First Albany Corporation	75,600	3,780.00	0.05000
First Clearing, LLC	4,700	235.00	0.05000
First Tennessee Securities Corporation	13,500	540.00	0.04000
First Union Capital Markets	230,860	11,283.00	0.04887
Fiserv Securities, Inc.	90,400	4,086.00	0.04520
Fox Pitt Kelton, Inc.	205,400	10,270.00	0.05000
Frank Russell	57,200	2,860.00	0.05000
Freimark Blair & Company, Inc.	32,600	1,630.00	0.05000
Friedman Billings & Ramsey	31,400	1,570.00	0.05000
Fuji Securities	400	32.05	0.08013
Fulcrum Global Partners, LLC	144,300	7,215.00	0.05000
G.K. Goh Stockbrokers PTE, Ltd.	38,000	717.31	0.01888
Gerard Klauer Mattison & Company	12,400	620.00	0.05000
Goldman Sachs & Company	8,584,299	151,516.23	0.01765
Goodbody Stockbrokers	44,649	977.94	0.02190
Green Street Advisors Incorporated	59,200	2,613.00	0.04414
Griswold Company	3,000	150.00	0.05000
Harborside Securities	21,900	657.00	0.03000
Harris Nesbitt Corporation	25,200	1,260.00	0.05000
Hibernia Southcoast Capital, Inc.	25,500	1,275.00	0.05000
Hoenig & Company, Inc.	17,000	850.00	0.05000
Howard Weil Division Legg Mason	45,300	2,265.00	0.05000
HSBC	1,277,947	14,785.63	0.01157
Indosuez WI CARR Securities, Ltd.	151,800	3,893.10	0.02565
Inferential Brokerage	4,300	215.00	0.05000
ING Financial Markets, LLC	241,300	2,358.80	0.00978

<b>Brokerage Firms</b>	<b>Number of Shares Traded</b>	<b>Total Commission</b>	<b>Commission Per Share</b>
Instinet Clearing Services, Inc.	195,500	4,464.50	0.02284
Intermonte Securities SPA	17,600	1,396.19	0.07933
Investment Technology Group, Ltd.	4,313,271	60,335.84	0.01399
ISI Group, Inc.	27,800	1,390.00	0.05000
J B Were & Son	3,600	105.06	0.02918
J P Morgan Securities, Inc.	294,700	13,879.00	0.04710
Janco Partners, Inc.	3,800	190.00	0.05000
Janney Montgomery, Scott, Inc.	553,940	27,697.00	0.05000
JB Were and Son (NZ), Ltd.	115,200	871.98	0.00757
Jeffries Company, Inc.	1,591,581	64,826.30	0.04073
JMP Securities	4,500	225.00	0.05000
Johnson Rice & Company	68,700	3,435.00	0.05000
Jones & Associates, Inc.	175,060	8,187.00	0.04677
JP Morgan Securities, Inc.	1,171,873	14,671.20	0.01252
Julius Baer Securities	42,600	1,468.75	0.03448
Keefe Bruyette & Woods, Inc	117,300	5,865.00	0.05000
King, Cl. & Associates, Inc.	67,300	3,365.00	0.05000
Kleinwortbenson Securities, Ltd.	890,299	13,629.84	0.01531
Knight Securities	974,288	46,323.74	0.04755
KV Execution Services, LLC	2,600	78.00	0.03000
La Branche Financial #2	606,400	27,462.00	0.04529
Lazard Capital Markets	116,600	1,139.45	0.00977
Lazard Freres & Company	594,937	29,697.85	0.04992
Leerink Swann & Company	335,700	16,785.00	0.05000
Legg Mason Wood Walker, Inc.	572,856	28,642.80	0.05000
Lehman Brothers, Inc.	3,414,479	61,814.73	0.01810
Liquidnet, Inc.	188,400	3,775.00	0.02004
Lombard, Odier & CIE	23,100	2,674.43	0.11578
LTG Europe, Ltd.	1,300	18.74	0.01442
Lynch Jones and Ryan, Inc.	2,945,360	136,208.00	0.04624
M M Warburg	38,500	1,073.57	0.02788
Macquarie Investment	10,500	80.81	0.00770
Main First Bank DE	5,700	755.38	0.13252
Mc. Donald & Company Securities, Inc.	367,101	18,355.05	0.05000
Merrill Lynch & Co., Inc.	9,944,548	213,873.17	0.02151
Merrion Capital Group	4,400	139.50	0.03170
Midwest Research Securities	193,000	9,329.00	0.04834
Miller Tabak & Company, LLC	524,415	26,068.75	0.04971
Mizuho Securities USA, Inc.	25,868	2,003.99	0.07747
Moors & Cabot, Inc.	71,800	3,590.00	0.05000
Morgan Guaranty Trust Bank Of New York	63,900	934.68	0.01463
Morgan Keegan & Co., Inc.	54,100	2,705.00	0.05000
Morgan Stanley Co. Incorporated	2,673,044	89,070.93	0.03332
National Financial Services Corporation	23,700	1,185.00	0.05000
NBCN Clearing, Inc.	28,000	1,400.00	0.05000
NCB Stockbrokers, Ltd.	41,000	1,056.02	0.02576
Needham & Company	15,900	774.00	0.04868
Nesbitt Burns	82,000	2,276.93	0.02777
Neuberger & Berman	81,900	3,021.00	0.03689
Nomura Securities Co., Ltd.	6,100	373.94	0.06130
Nomura Securities International, Inc.	557,539	4,905.70	0.00880

<b>Brokerage Firms</b>	<b>Number of Shares Traded</b>	<b>Total Commission</b>	<b>Commission Per Share</b>
NY Fix Transaction Services	6,900	275.00	0.03986
Odd Lot Sale	70	17.66	0.25229
Oppenheimer & Co., Inc.	5,300	265.00	0.05000
Pacific Crest Securities	17,800	890.00	0.05000
Pacific Growth Equities	16,200	810.00	0.05000
Panmure Gordon & Co., Ltd.	40,121	1,766.35	0.04403
Paribas Corporation	73,200	3,644.31	0.04979
PCS Securities, Inc.	45,400	1,836.00	0.04044
Pershing, LLC	156,300	7,135.00	0.04565
Petrie Parkman & Company	69,600	3,351.00	0.04815
Polcari/Weicker Div. Of Garban Corp.	2,500	75.00	0.03000
Prudential Securities Incorporated	299,830	14,938.50	0.04982
Pulse Trading, LLC	59,100	2,303.00	0.03897
Quaker Securities, Inc.	2,500	125.00	0.05000
Rabo Securities NV	15,300	532.55	0.03481
Ragen Mackenzie Incorporated	4,600	230.00	0.05000
Raymond James & Associates, Inc.	111,300	5,565.00	0.05000
RBC Dain Rauscher, Inc.	168,800	8,200.00	0.04858
RBC Dominion Securities	59,800	2,296.02	0.03839
Robotti & Company	13,822	672.88	0.04868
Rochdale Securities Corporation	448,300	7,043.00	0.01571
RTX Securities	17,300	865.00	0.05000
Salomon Smith Barney	4,743,978	24,031.68	0.00507
Samsung Securities Co., Ltd.	3,800	863.70	0.22729
Sanders Morris Mundy	39,179	1,856.58	0.04739
Sandler Oneill & Part LP	269,370	13,468.50	0.05000
Sanford C. Bernstein, Ltd.	598,870	28,757.67	0.04802
Santander Central Hispano Bolsa	17,700	426.34	0.02409
Scotia Capital (USA), Inc.	85,600	2,447.23	0.02859
Scott & Stringfellow, Inc.	103,830	5,191.50	0.05000
SG Cowen Securities Corporation	601,901	29,294.25	0.04867
Sidoti & Company	52,100	2,556.00	0.04906
Simmons & Company International	8,600	430.00	0.05000
Societe Generale London Branch	20,000	567.78	0.02839
Southwest Securities	363,700	17,206.00	0.04731
Spear, Leeds & Kellogg	39,400	1,512.00	0.03838
Standard & Poors Securities, Inc.	15,900	621.00	0.03906
State Street Brokerage Services	17,200	257.95	0.01500
Stephens, Inc.	79,900	3,995.00	0.05000
Stifel Nicolaus & Co., Inc.	440,400	16,747.00	0.03803
Suntrust Capital Markets, Inc.	159,800	7,379.00	0.04618
Thomas Weisel Partners	123,300	5,845.00	0.04740
Thomason Institutional Services, Inc.	66,000	3,300.00	0.05000
Toronto Dominion Securities, Inc.	15,200	547.02	0.03599
Tullett Liberty, Ltd.	40,600	755.79	0.01862
U S Bancorp Piper Jaffray, Inc.	158,380	7,915.00	0.04997
U S Clearing Institutional Trading	42,800	2,140.00	0.05000
UBS Warburg, LLC	2,634,672	56,211.82	0.02134
Veritas Securities	370,300	13,228.00	0.03572
Vontobel Securities	5,500	307.76	0.05596
W.J. Bonfanti, Inc.	7,500	112.50	0.01500

<b><u>Brokerage Firms</u></b>	<b><u>Number of Shares Traded</u></b>	<b><u>Total Commission</u></b>	<b><u>Commission Per Share</u></b>
Wachovia Securities, LLC	106,500	5,210.00	0.04892
Warburg Dillon Read Securities, Ltd.	9,912,323	26,222.32	0.00265
Weeden & Company	443,160	21,381.00	0.04825
Wells Fargo Securities, LLC	17,500	875.00	0.05000
Westminster Res. Assoc./ Broadcort Capital	63,900	3,195.00	0.05000
William Blair & Company, LLC	76,100	3,805.00	0.05000
William Smith Securities	74,900	3,745.00	0.05000
Wit Soundview Corporation	51,900	2,461.00	0.04742
WR Hambrecht & Company	3,100	155.00	0.05000

**Investment Summary**  
**December 31, 2003**  
(in thousands)

Investment	Fair Value	Percentage
Domestic Equity	\$ 1,727,507	34.74%
Domestic Fixed Income	1,183,590	23.80%
International Equity	748,239	15.05%
International Fixed Income	237,560	4.78%
Alternative Investments	152,357	3.06%
Real Estate	250,291	5.03%
Cash and Cash Equivalents	672,569	13.54%
<b>Total</b>	<b>\$ 4,972,113</b>	<b>100.00%</b>

**Schedule of Largest Stock Holdings (by Fair Value)\***  
**December 31, 2003**

Stock	Security Description	Fair Value
Intel Corporation	Common Stock	\$ 13,610,940.00
E-Bay, Inc.	Common Stock	12,982,590.00
Goldman Sachs Group, Inc.	Common Stock	12,499,218.00
Medtronic, Inc.	Common Stock	12,074,724.00
Microsoft Corporation	Common Stock	11,759,580.00
First Data Corporation	Common Stock	9,845,164.00
CISCO System, Inc.	Common Stock	9,767,009.00
American International Group, Inc.	Common Stock	8,298,256.00
PFIZER, Inc.	Common Stock	7,981,047.00
Amgen, Inc.	Common Stock	7,434,540.00

**Schedule of Largest Bond Holdings (by Fair Value)\***  
**December 31, 2003**

Bonds	Moody's Quality Rating	Fair Value
United States Treasury Notes 3.875%, 15 Jan. 2009	AAA	\$ 60,221,959.75
Netherlands (Kingdom) 5.85%, 15 February 2007	AAA	20,253,221.49
Bundesrepublik Deutschland 5.00%, 04 July 2011	AAA	16,382,169.38
Spain (Kingdom of) 5.15%, 30 July 2009	AAA	15,710,270.38
United States Treasury Bills .001%, 13 May 2004	AAA	14,971,864.50
Sweden (Kingdom of) 6.75%, 05 May 2014	AAA	14,607,882.65
Poland (Government of) 5.00%, 24 October 2013	A2	12,963,057.16
Germany (Federal Republic of) 4.00%, 04 July 2004	AAA	12,846,828.33
Italy (Republic of) 4.50%, 01 May 2009	NA	12,587,617.99
FHLMC Discount Notes .001%, 04 May 2004	AAA	12,480,588.75

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



SECTION

4



**ACTUARIAL**



May 21, 2004

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

Members of the Board:

The financing objective of the system has been to reduce the unfunded actuarial accrued liability (UAAL) to zero over a 28-year period commencing December 31, 1995, while maintaining contribution rates that remain approximately the same from generation to generation. Emerging gains and losses have been amortized separately over individual 15-year periods. Other changes to the UAAL, created by assumption changes or plan amendments, have been amortized over periods established by the Board. Effective with the December 31, 2002 actuarial valuation, the Board elected to restart the amortization period for General Members, including Probation Officers, to 30 years. Future changes to UAAL will be amortized as described above. The amortization periods for Safety Members will be reviewed in future periods. The progress being made toward the realization of the financing objectives through December 31, 2003 is illustrated in the attached Exhibits I and II.

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

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

Retirement Board  
May 21, 2004  
Page 2.



The actuarial assumptions used in the December 31, 2003 valuation are summarized in the attachments and are identical to the assumptions used in the prior year's valuation. All assumptions were determined by the actuary and were adopted by the Board. The actuarial assumptions and methods used for funding purposes satisfy the disclosure requirements of GASB 25.

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

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

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

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

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

On the basis of the December 31, 2003 valuation, it is our opinion that OCERS continues to be in sound condition in accordance with the actuarial principles of level cost financing.

Respectfully submitted,

A handwritten signature in cursive script that reads "Timothy J. Marnell".

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

Orange County Employees Retirement System  
**HISTORY OF UNFUNDED ACTUARIAL ACCRUED LIABILITY**  
(In Thousands)

Valuation Date	Actuarial Accrued Liability	Actuarial Value of Assets*	Unfunded Actuarial Accrued Liability	Ratio of Assets to Actuarial Accrued Liability	Annual Active Member Compensation	Ratio of Unfunded Actuarial Accrued Liability to Active Compensation
12/31/94	2,550,059	2,177,673	372,386	85.40%	769,175	48.41%
12/31/95	2,633,884	2,434,406	199,478	92.43%	727,768	27.41%
12/31/96	2,851,894	2,675,632	176,262	93.82%	758,897	23.23%
12/31/97	3,332,967	3,128,132	204,835	93.85%	781,890	26.20%
12/31/98	3,682,686	3,504,708	177,978	95.17%	863,199	20.62%
12/31/99	4,017,279	3,931,744	85,535	97.87%	912,490	9.37%
12/31/00	4,335,025	4,497,362	(162,337)	103.74%	994,669	(16.32%)
12/31/01	4,843,899	4,586,844	257,055	94.69%	1,122,763	22.89%
12/31/02	5,673,754	4,695,675	978,079	82.76%	1,242,348	78.73%
12/31/03	6,099,433	4,790,099	1,309,334	78.53%	1,243,964	105.25%

Notes:

- The 12/31/03 valuation included the following benefit changes:
  - The City of San Juan Capistrano adopted a new benefit formula, which produces benefits of 2.7% of final average pay at age 55.
  - The City of Rancho Santa Margarita adopted a new benefit formula, which produces benefits of 2.5% of final average pay at age 55.
- The 12/31/02 valuation included changes to the interest rate and salary increase assumptions. The interest rate changed from 8.0% to 7.5% and the salary increase assumption from 5.5% to 4.5%. These changes increased employer rates and generally decreased member contribution rates slightly. The retirement benefit for Firefighters was changed to a 3% per year of service benefit payable unreduced at age 50. Probation Officers became Safety Members with a portion of service for Tier II members converted to Safety Member service at less than one-for-one.
- The 12/31/01 valuation included changes to the assumed withdrawal rates, the assumed termination rates, the assumed service connected disability rates and the assumed retirement rates. These changes increased both member and employer contribution rates. The retirement benefit for Law Enforcement was changed to a 3% per year of service benefit payable unreduced at age 50.
- The 12/31/98 valuation included changes to the assumed withdrawal rates, the assumed preretirement mortality and the assumed retirement rates. These changes increased both member and employer contribution rates.

- The 12/31/97 valuation included an increase in plan benefits to reflect the impact of the California Supreme Court decision in the Ventura County case regarding compensation earnable.
  - The 12/31/95 valuation included a change in the salary scale from 6.0% to 3.5% per annum through the year 2000, and 5.5% thereafter. The aggregate payroll increase assumption was also changed from 5.0% to 4.5% per annum.
- \* Each year's assets exclude an amount as shown in the following table of the County's unamortized 1994 funding of its portion of the Unfunded Actuarial Accrued Liability, which funding for 1995 was being amortized over a 14-year period beginning July 1, 1994 and for 1996 and later was being amortized over a 28-year period beginning July 1, 1996. Beginning July 1, 2003, the County can utilize this amount at its discretion to fund any portion of the employer contribution.

<b>Valuation Date</b>	<b>Amount Excluded from Assets</b>
12/31/94	\$311,022,000
12/31/95	\$329,064,000
12/31/96	\$313,250,000
12/31/97	\$322,333,000
12/31/98	\$302,909,000
12/31/99	\$286,139,000
12/31/00	\$272,789,000
12/31/01	\$221,643,000
12/31/02	\$143,675,000
12/31/03	\$143,744,000

Orange County Employees Retirement System  
**HISTORY OF EMPLOYER CONTRIBUTION RATES**

**Employer Contribution Rate (% of pay)**

Valuation Date	General				Safety			
	December 31, 1994	Normal	3.68	UAAL	<u>1.71*</u>	Normal	6.58	UAAL
	Total	5.39	Total	28.43				
December 31, 1995	Normal	3.33	UAAL	<u>(0.47)*</u>	Normal	5.59	UAAL	<u>18.84*</u>
	Total	2.86	Total	24.43				
December 31, 1996	Normal	3.38	UAAL	<u>(1.06)</u>	Normal	5.77	UAAL	<u>17.77</u>
	Total	2.32	Total	23.54				
December 31, 1997	Normal	3.77	UAAL	<u>(1.91)</u>	Normal	6.79	UAAL	<u>19.65</u>
	Total	1.86	Total	26.44				
December 31, 1998	Normal	4.35	UAAL	<u>(2.35)</u>	Normal	8.00	UAAL	<u>16.41</u>
	Total	2.00	Total	24.41				
December 31, 1999	Normal	4.56	UAAL	<u>(3.60)</u>	Normal	8.27	UAAL	<u>13.95</u>
	Total	0.96	Total	22.22				
December 31, 2000	Normal	4.94	UAAL	<u>(3.98)</u>	Normal	8.57	UAAL	<u>0.16</u>
	Total	0.96	Total	8.73				
	<i>Non-OCTA</i>	<i>OCTA</i>	<i>Rancho Santa Margarita</i>	<i>San Juan Capistrano</i>	<i>Law Enforcement</i>	<i>Fire Authority</i>	<i>Probation</i>	
December 31, 2001	Normal 5.04 UAAL <u>0.62*</u>	Normal 4.20 UAAL <u>0.77*</u>	N/A	Normal 5.04 UAAL <u>0.62*</u>	Normal 15.87 UAAL <u>9.15*</u>	Normal 10.30 UAAL <u>1.89*</u>	Normal 5.04 UAAL <u>0.62*</u>	
	Total 5.66	Total 4.97		Total 5.66	Total 25.02	Total 12.19	Total 5.66	
December 31, 2002	Normal 5.44 UAAL <u>3.71*</u>	Normal 4.36 UAAL <u>3.87*</u>	N/A	Normal 5.44 UAAL <u>3.71*</u>	Normal 16.53 UAAL <u>21.34*</u>	Normal 17.85 UAAL <u>16.81*</u>	Normal 4.38 UAAL <u>4.19*</u>	
	Total 9.15	Total 8.23		Total 9.15	Total 37.87	Total 34.66	Total 8.57	
December 31, 2003	Normal 5.56 UAAL <u>7.07*</u>	Normal 4.41 UAAL <u>7.05*</u>	Normal 1.77 UAAL <u>3.43*</u>	Normal 7.22 UAAL <u>10.96*</u>	Normal 16.86 UAAL <u>22.53*</u>	Normal 17.98 UAAL <u>15.40*</u>	Normal 4.02 UAAL <u>8.73*</u>	
	Total 12.63	Total 11.46	Total 5.20	Total 18.18	Total 39.39	Total 33.38	Total 12.75	

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

## Exhibit III

Orange County Employees Retirement System  
SUMMARY OF ACTIVE MEMBERSHIP

Valuation Date	Number	Annual Salary	Annual Average Salary	% Increase in Average Salary
12/31/94				
General	17,084	\$645,117,097	\$37,761	2.81%
Safety	2,289	124,058,327	54,198	2.94
Total	19,373	\$769,175,424	\$39,703	2.91
12/31/95				
General	15,658	\$597,800,535	\$38,179	1.11%
Safety	2,351	129,967,110	55,282	2.00
Total	18,009	\$727,767,645	\$40,411	1.78
12/31/96				
General	15,736	\$623,682,535	\$39,634	3.81%
Safety	2,354	135,214,811	57,440	3.90
Total	18,090	\$758,897,346	\$41,951	3.81
12/31/97				
General	16,266	\$643,115,556	\$39,537	(0.24%)
Safety	2,427	138,774,560	57,179	(0.45)
Total	18,693	\$781,890,116	\$41,828	(0.29)
12/31/98				
General	16,976	\$706,507,935	\$41,618	5.26%
Safety	2,456	156,691,236	63,799	11.58
Total	19,432	\$863,199,171	\$44,422	6.20
12/31/99				
General	17,801	\$738,956,477	\$41,512	(0.25%)
Safety	2,556	173,533,473	67,893	6.42
Total	20,357	\$912,489,950	\$44,824	0.90
12/31/00				
General	18,382	\$809,054,612	\$44,016	6.04%
Safety	2,605	185,614,420	71,256	4.95
Total	20,987	\$994,669,032	\$47,400	5.76
12/31/01				
General	19,653	\$921,057,200	\$46,860	6.46%
Safety	2,676	201,705,606	75,372	5.78
Total	22,329	\$1,122,762,806	\$50,280	6.08
12/31/02				
General	19,002	\$976,660,649	\$51,398	9.68%
Safety	3,721	265,638,289	71,389	(5.28)
Total	22,723	\$1,242,348,938	\$54,674	8.74
12/31/03				
General	19,023	\$985,534,535	\$51,808	0.80%
Safety	3,649	258,429,279	70,822	(0.79)
Total	22,672	\$1,243,963,814	\$54,868	0.35

Excludes Deferred and Pending members.

Orange County Employees Retirement System  
SUMMARY OF RETIRED MEMBERSHIP

Year	Number of Members				Annual Allowance	% Increase in Annual Allowance	Average Monthly Allowance
	At Beginning of Year	Added During Year	Removed During Year	At End of Year			
1/94 to 12/94	5,512	504	(200)	5,816	\$77,629,436	12.11	\$1,112
1/95 to 12/95	5,816	690	(147)	6,359	92,332,920	18.94	1,210
1/96 to 12/96	6,359	426	(154)	6,631	99,751,438	8.03	1,254
1/97 to 12/97	6,631	505	(224)	6,912	109,661,326	9.93	1,322
1/98 to 12/98	6,912	547	(215)	7,244	125,439,610	14.39	1,443
1/99 to 12/99	7,244	549	(256)	7,537	137,542,880	9.65	1,521
1/00 to 12/00	7,537	618	(240)	7,915	149,002,518	8.33	1,569
1/01 to 12/01	7,915	606	(305)	8,216	162,552,549	9.09	1,649
1/02 to 12/02	8,216	727	(255)	8,688	186,286,465	14.60	1,787
1/03 to 12/03	8,688	793	(402)	9,079*	210,913,427	13.22	1,936

\* Includes 129 QDRO recipients.

Exhibit V

Orange County Employees Retirement System  
DEVELOPMENT OF ACTUARIAL VALUE OF ASSETS  
As of December 31, 2003

Plan Year Ending	Fair Value	Book Value	Ratio of Fair Value to Book Value
2003	\$4,822,375,669	\$4,589,984,771	1.050630
2002	3,983,071,947	4,377,410,744	0.909915
2001	3,793,056,765	4,071,017,323	0.931722
2000	4,015,261,166	3,826,675,630	1.049282
1999	4,183,305,471	3,277,313,800	1.276443

(1) Average ratio in five years preceding December 31, 2003	1.043598
(2) Book value on December 31, 2003	\$4,589,984,771
(3) Actuarial value of assets: (1) x (2)	\$4,790,098,927

## Exhibit VI

## Orange County Employees Retirement System

**SHORT-TERM SOLVENCY TEST**

(\$ Amounts in Thousands)

Valuation Date	(1) Active Member Contributions	(2) Liability for Inactive Participants	(3) Liability for Active Members (Employer Financed Portion)	Valuation Assets	Portion of Accrued Liability Covered by Valuation Assets		
					(1)	(2)	(3)
12/31/94	\$413,058	\$1,002,300	\$1,134,701	\$2,177,673	100	100	67.18
12/31/95	438,949	1,201,057	993,878	2,434,406	100	100	79.93
12/31/96	484,451	1,295,334	1,072,109	2,675,632	100	100	83.56
12/31/97	523,770	1,554,017	1,255,180	3,128,132	100	100	83.68
12/31/98	567,932	1,632,708	1,482,047	3,504,708	100	100	87.99
12/31/99	618,463	1,782,432	1,616,383	3,931,744	100	100	94.71
12/31/00	671,152	1,911,328	1,752,545	4,497,362	100	100	100
12/31/01	739,084	2,085,697	2,019,118	4,586,844	100	100	87.27
12/31/02	858,121	2,496,133	2,319,500	4,695,675	100	100	57.83
12/31/03	852,016	2,843,236	2,404,180	4,790,099	100	100	45.54

Orange County Employees Retirement System  
**ACTUARIAL METHODS AND ASSUMPTIONS**

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

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

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

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

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

Table I

Orange County Employees Retirement System

**PROBABILITY OF OCCURRENCE**

(Includes Eligibility)

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

*Table II*

Orange County Employees Retirement System  
**EXPECTATION OF LIFE**  
**Age and Service Retirees**  
1983 Group Annuity Mortality

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

*Table III*

Orange County Employees Retirement System  
**EXPECTATION OF LIFE**  
**Disabled Retirees**  
 1981 Disabled Mortality

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

## Orange County Employees Retirement System

**ASSUMPTIONS SPECIFIC TO THE  
VENTURA COUNTY RULING**

The Ventura County Ruling changed the definition of compensation earnable, a key variable in the determination of benefits payable from the Orange County Employees Retirement System. Because many of the elements of compensation and certain information about member contribution account balances were unavailable, assumptions needed to be made to complete the December 31, 2003 actuarial valuation. The following describes the key assumptions that were made and the rationale behind the assumptions. Overall, the assumptions used in the actuarial valuation are conservative, but not overly conservative. As more information becomes available, changes to these assumptions will be considered.

**Compensation Earnable**

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

As a result, the normal cost and actuarial accrued liability for active members were increased by the following percentages:

	General	Safety		
		Fire	Law Enforcement	Probation
Tier 1	4.5%	5.1%	9.3%	4.5%
Tier 2	2.1%	2.4%	6.3%	2.1%

Orange County Employees Retirement System

**SUMMARY OF MAJOR PLAN PROVISIONS**

1. **Membership Requirements**

Date of employment.

2. **Monthly Salary Base for Benefits**

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

3. **Service Retirement**

A. **Eligibility**

10 years of service and age 50, or 30 years of service.

B. **Benefit Formula per Year of Service**

2% for General Tier I; 1.667% for General Tier II; 3% for Firefighters and Law Enforcement; 2% for Probation Officers, Rancho Santa Margarita, and San Juan Capistrano.

Benefits are reduced or increased for retirement ages according to the following sections of the County Employees Retirement Law of 1937:

Law Enforcement/Firefighters	31664.1
Probation Safety	31664
San Juan Capistrano	31676.19
Rancho Santa Margarita	31676.18
All other General Members:	
■ Tier 1	31676.12
■ Tier 2	31676.1

4. **Ordinary Disability**

A. **Eligibility**

Five years of service.

B. **Benefit Formula per Year of Service**

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

5. **Line-of-Duty Disability**

A. **Eligibility**

No age or service requirement.

B. **Benefit**

The greater of 50% of salary or the service retirement benefit, if larger and the member otherwise satisfies the service retirement eligibility.

6. **Ordinary Death before Eligible to Retire**

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

7. **Ordinary Death after Eligible to Retire for Service or Ordinary Disability**  
60% of earned benefit payable to surviving eligible spouse.
8. **Line-of-Duty Death**  
50% of salary payable to spouse.
9. **Death after Retirement**
  - A. **Service or Ordinary Disability Retirement**  
60% of member's unmodified allowance continued to eligible spouse.
  - B. **Line-of-Duty Disability**  
100% of member's allowance continued to spouse.
  - C. **\$750 Lump Sum**
10. **Withdrawal Benefits**
  - A. **Fewer than Five Years of Service**  
Refund of accumulated employee contributions with interest.
  - B. **Five or More Years of Service**  
If contributions left on deposit, entitled to earned benefits commencing at any time after member would have been eligible to retire.
11. **Postretirement Cost-of-Living Benefits**  
Based on changes in Consumer Price Index to maximum of 3% per year; excess "banked."
12. **Member Contributions - Tier I (Tier II in parentheses)**  
Normal based on entry age, 1/200 (1/120) at 60 for General Members; 1/200 (1/100) at 50 for Safety Members. Cost-of-living contributions equal to percentage of normal: 51.90% (31.40%) for non-OCTA General; 50.96% (35.56%) for OCTA General; 108.80% (54.86%) for Firefighters; 113.32% (57.36%) for Law Enforcement; 28.28% (14.10%) for Probation Officers; 27.37% (27.37%) for Rancho Santa Margarita; 29.15% (29.16%) for San Juan Capistrano.

## Orange County Employees Retirement System

**EXPERIENCE ANALYSIS**

(\$000)

<b>Gains &amp; Losses in Accrued Liabilities During Years Ended December 31, Resulting from Differences Between Assumed Experience &amp; Actual Experience</b>					
<b>Type of Activity</b>	<b>Gains (or Losses) Per Year</b>				
	<b>1999</b>	<b>2000</b>	<b>2001</b>	<b>2002</b>	<b>2003</b>
Retirements	\$(60,138)	\$(29,367)	\$(48,490)	\$(82,392)	\$(119,420)
Disabilities	13,197	16,780	17,696	(8,012)	24,833
Withdrawal From Employment	(23,003)	(4,633)	(13,932)	(15,328)	(1,962)
Pay Increases	(1,890)	(24,585)	(40,448)	(91,887)	103,234
Investment Income	163,736	286,267	(221,192)	(220,329)	(287,828)
Mortality	24,804	28,836	(3,021)	(7,422)	7,574
Other	<u>(17,803)</u>	<u>(20,775)</u>	<u>(20,534)</u>	<u>(18,001)</u>	<u>(35,343)</u>
Gain (or Loss) During Year From Experience	<b>\$ 98,903</b>	<b>\$252,523</b>	<b>\$(329,921)</b>	<b>\$(443,371)</b>	<b>\$(308,912)</b>
Non Recurring Items. Adjustment for Plan Amendments, Assumption Changes, etc.	<u>0</u>	<u>0</u>	<u>(85,395)</u>	<u>(238,027)</u>	<u>(2,338)</u>
Composite Gain (or Loss) During Year	<b>\$ 98,903</b>	<b>\$252,523</b>	<b>\$(415,316)</b>	<b>\$(681,398)</b>	<b>\$(311,250)</b>



SECTION

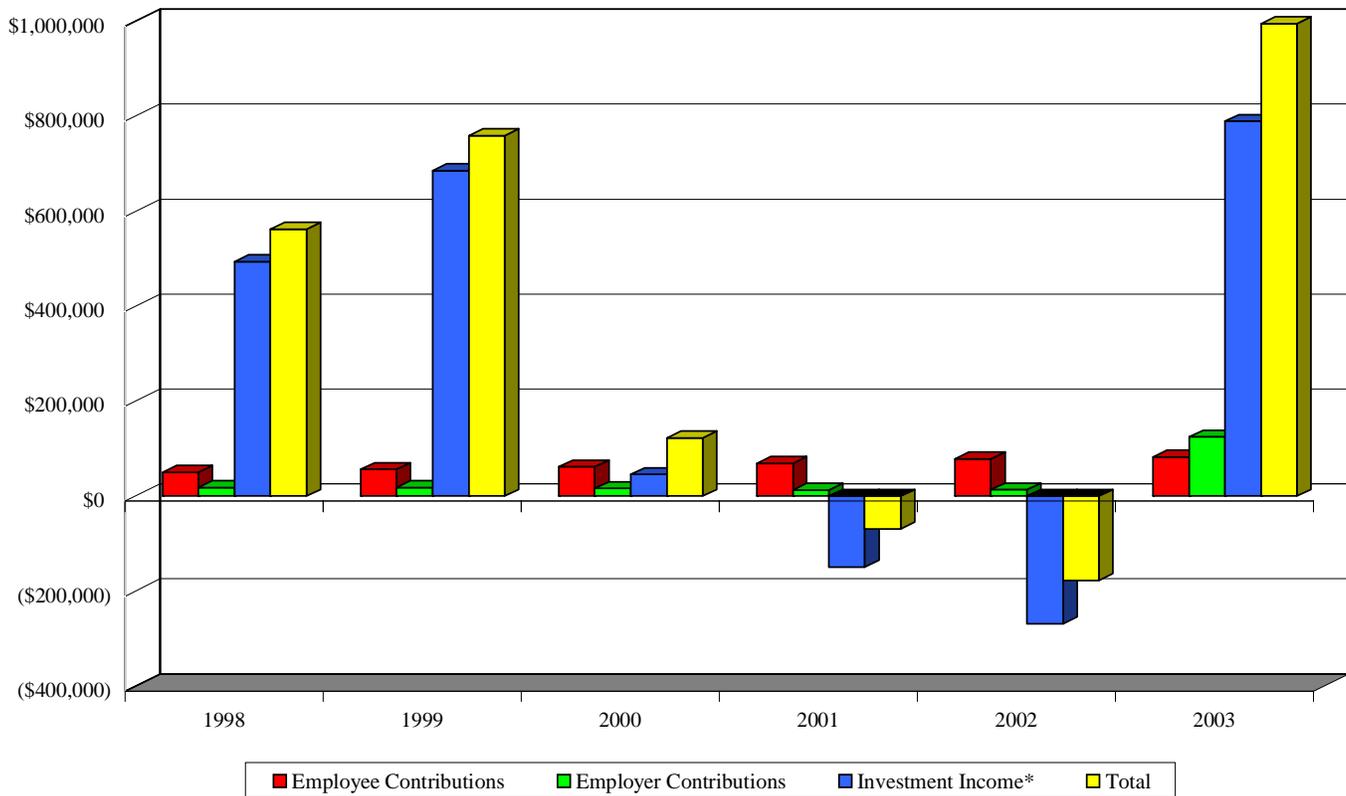
5



> STATISTICAL

**Schedule and Graph of  
Revenues by Source  
(in thousands)  
1998 – 2003**

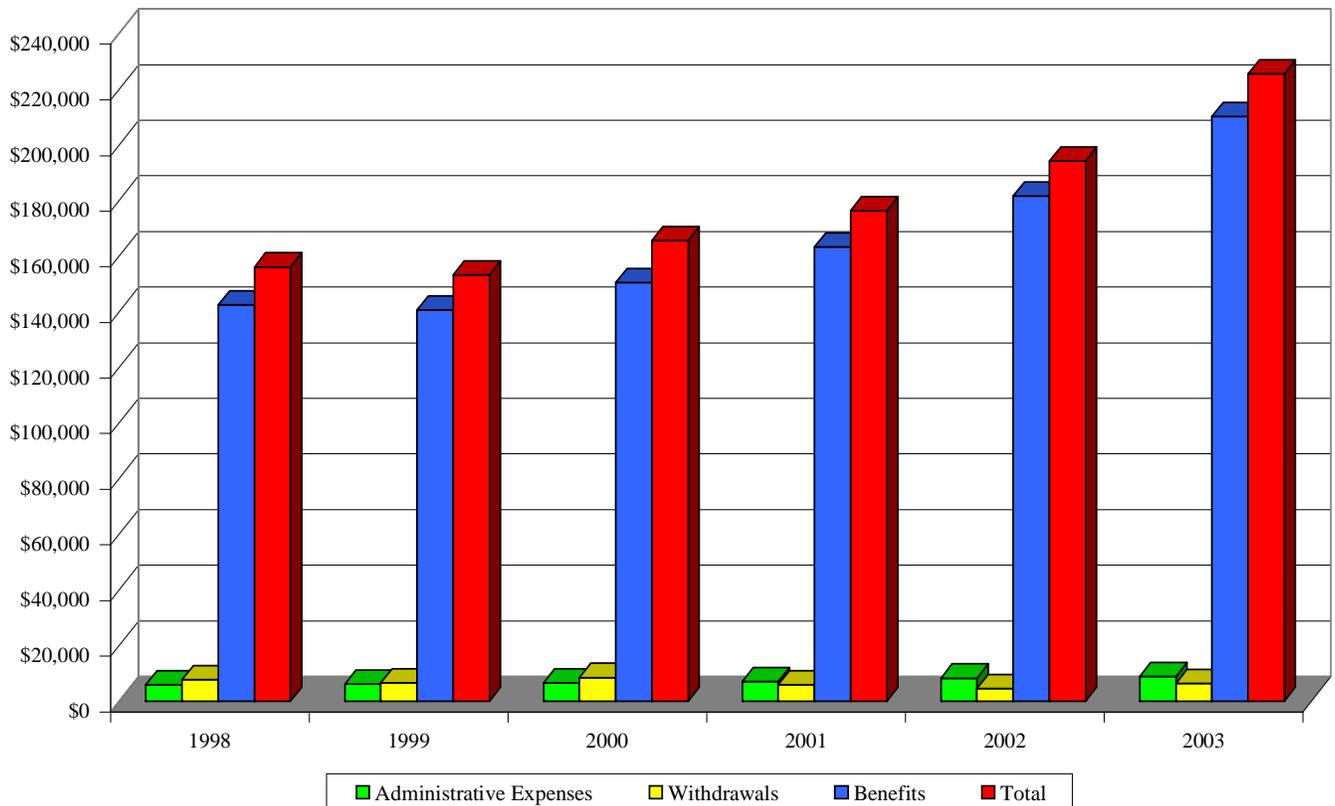
	1998	1999	2000	2001	2002	2003
<b>Employee Contributions</b>	\$50,557	\$55,693	\$61,179	\$68,635	\$77,917	\$81,581
<b>Employer Contributions</b>	\$17,977	\$17,591	\$15,561	\$12,060	\$13,289	\$124,243
<b>Investment Income*</b>	\$493,491	\$685,718	\$45,284	(\$149,858)	(\$269,188)	\$789,086
<b>Total</b>	\$562,025	\$759,002	\$122,024	(\$69,163)	(\$177,982)	\$994,910



\* Net of investment manager fees and security lending fees.

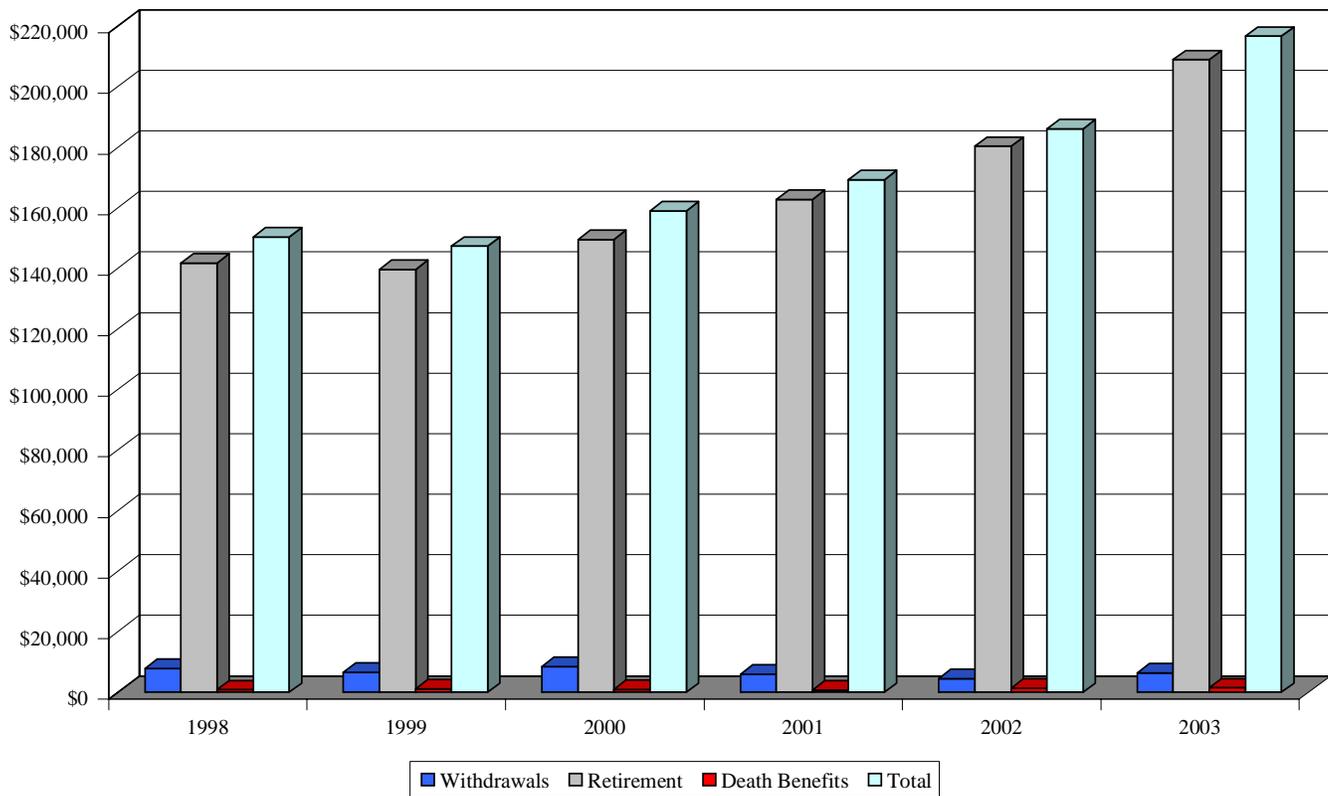
### Schedule and Graph of Expenses by Type (in thousands) 1998 – 2003

	1998	1999	2000	2001	2002	2003
<b>Administrative Expenses</b>	\$5,850	\$6,094	\$6,631	\$7,146	\$8,279	\$8,848
<b>Withdrawals</b>	\$7,848	\$6,513	\$8,515	\$5,896	\$4,482	\$6,412
<b>Benefits</b>	\$142,457	\$140,736	\$150,466	\$163,378	\$181,549	\$210,273
<b>Total</b>	\$156,155	\$153,343	\$165,612	\$176,420	\$194,310	\$225,533



## Schedule and Graph of Benefit Expenses by Type (in thousands) 1998 – 2003

	1998	1999	2000	2001	2002	2003
<b>Withdrawals</b>	\$7,848	\$6,513	\$8,515	\$5,896	\$4,482	\$6,412
<b>Retirement</b>	\$141,629	\$139,611	\$149,555	\$162,732	\$180,263	\$208,861
<b>Death Benefits</b>	\$828	\$1,125	\$911	\$646	\$1,286	\$1,412
<b>Total</b>	\$150,305	\$147,249	\$158,981	\$169,274	\$186,031	\$216,685



### Schedule of Retired Members by Type of Benefit December 31, 2003

Monthly Benefit	Types of Retirement						Total Retirees	QDRO	Total Payees
	1	2	3	4	5	7			
\$0-250	59	79	5	6	1	189	339	25	364
\$251-500	179	186	1	14	1	310	691	26	717
\$501-750	369	241	-	33	1	186	830	25	855
\$751-1000	518	168	8	45	1	124	864	8	872
\$1001-1250	569	118	41	63	-	73	864	9	873
\$1251-1500	448	98	53	41	2	46	688	7	695
\$1501-1750	412	54	122	19	-	36	643	9	652
\$1751-2000	369	46	154	16	-	23	608	7	615
\$2001-2250	307	43	104	7	-	20	481	2	483
\$2251-2500	281	34	75	8	-	8	406	3	409
\$2501-2750	248	21	72	2	-	8	351	2	353
\$2751-3000	188	16	61	3	-	10	278	1	279
\$3001-3250	177	13	64	3	-	9	266	1	267
\$3251-3500	177	10	34	2	-	2	225	1	226
\$3501-3750	138	6	18	1	-	1	164	1	165
\$3751-4000	139	10	17	-	-	1	167	2	169
Over \$4000	1,013	16	50	1	-	5	1,085	-	1,085
<b>Total</b>	<b>5,591</b>	<b>1,159</b>	<b>879</b>	<b>264</b>	<b>6</b>	<b>1,051</b>	<b>8,950</b>	<b>129</b>	<b>9,079</b>

### Schedule of Retired Members by Option Selected December 31, 2003

Monthly Benefit	Option Selected						UNMJS	Total* Payees
	JSURV	SL100	SL60	SLIFE	SLR60			
\$0-250	13	0	0	20	0	331	364	
\$251-500	45	0	1	35	0	636	717	
\$501-750	48	0	4	62	2	739	855	
\$751-1000	26	0	0	37	0	809	872	
\$1001-1250	38	1	1	45	1	787	873	
\$1251-1500	26	0	0	37	0	632	695	
\$1501-1750	29	0	0	29	0	594	652	
\$1751-2000	20	0	1	23	0	571	615	
\$2001-2250	21	0	0	14	0	448	483	
\$2251-2500	20	0	0	17	0	372	409	
\$2501-2750	16	1	0	12	0	324	353	
\$2751-3000	15	0	0	7	0	257	279	
\$3001-3250	16	0	0	5	0	246	267	
\$3251-3500	9	0	0	9	0	208	226	
\$3501-3750	10	0	0	11	0	144	165	
\$3751-4000	16	0	0	3	0	150	169	
Over \$4000	107	0	0	51	0	927	1085	
<b>Total</b>	<b>475</b>	<b>2</b>	<b>7</b>	<b>417</b>	<b>3</b>	<b>8175</b>	<b>9079</b>	

\* Total payees includes 129 Qualified Domestic Relations Orders (QDRO) payees.

## Schedule of Retired Members by Type of Benefit and Option Selected as of December 31, 2003 (continued)

### Definition of Terms

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

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

### Type of Retirement

1. Normal Retirement for age and service
2. Survivor Payment - normal retirement
3. Service Connected Disability Retirement
4. Nonservice Connected Disability Retirement
5. Survivor Payment - Disability retirement
6. Active Death
7. Deferred Retirement
8. QDROs (retirees, alternate payees)

### Option Selected

**JSURV:** Contingent joint survivor.

**SL100:** Single life with 100% joint survivor adjustment.

**SL60:** Single life with 60% adjustment.

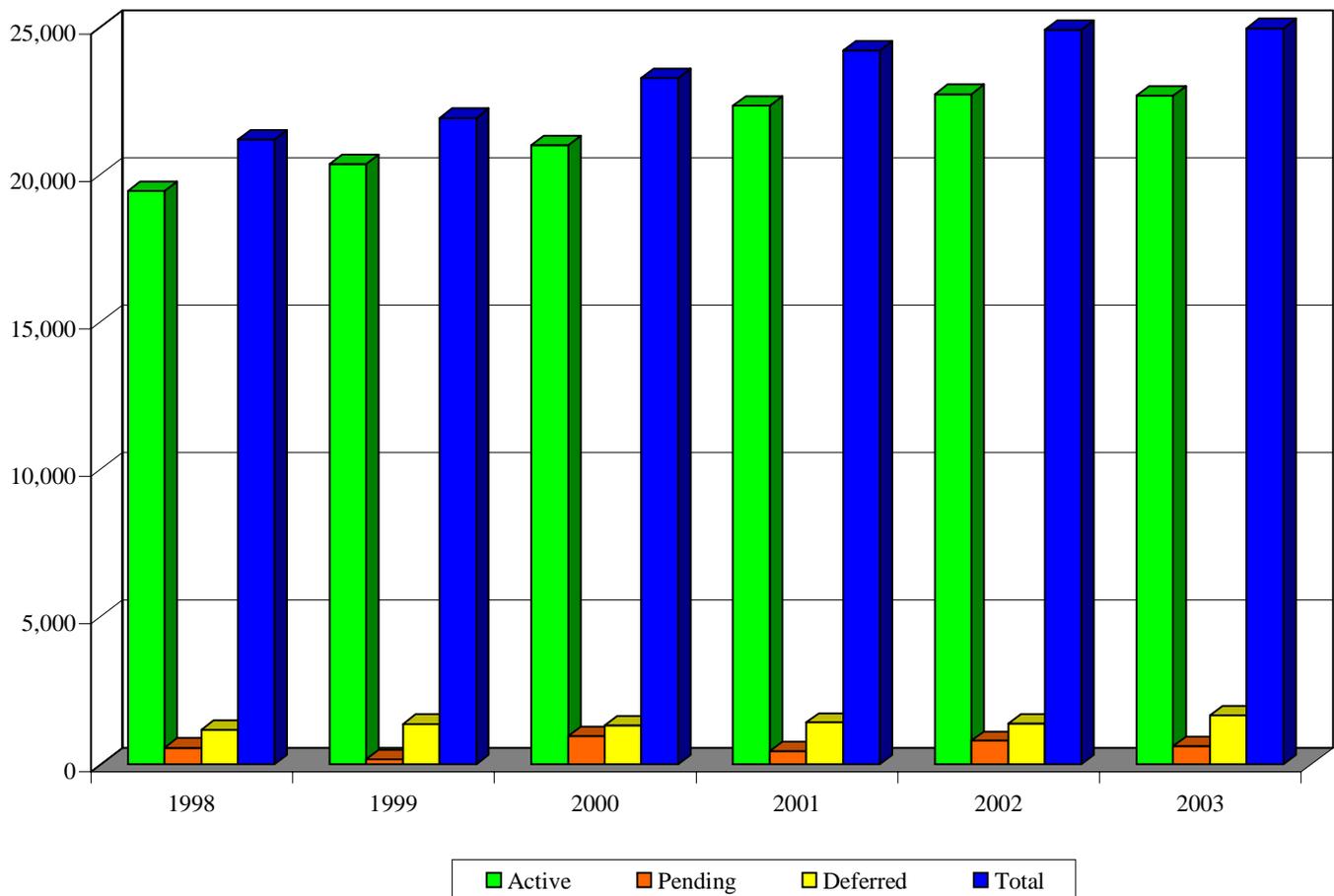
**SLIFE:** Lifetime payment.

**SLR60:** Single life with 60% adjustment with reduction.

**UNMJS:** Unmodified with joint survivor.

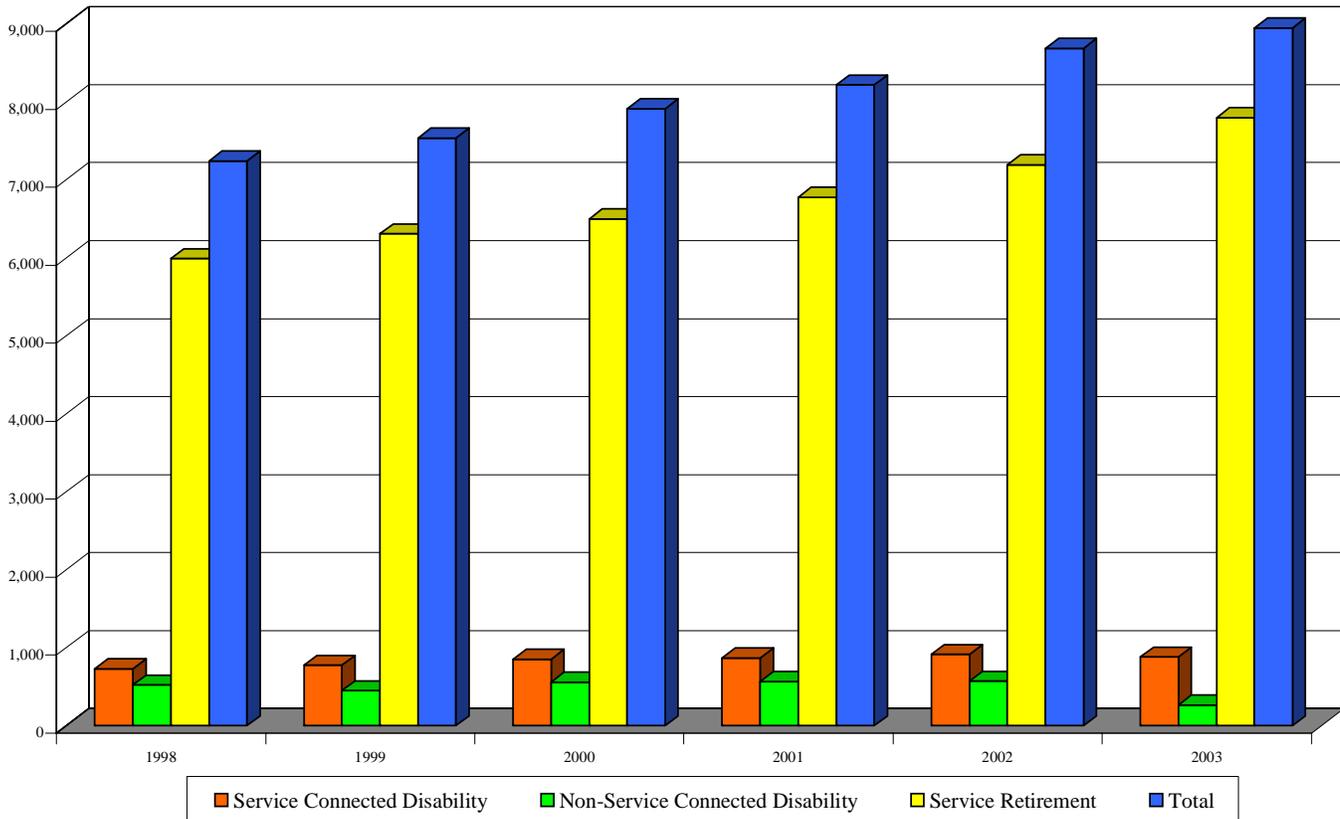
## Schedule and Graph of Active, Pending and Deferred Members 1998 – 2003

	1998	1999	2000	2001	2002	2003
<b>Active</b>	19,432	20,357	20,987	22,329	22,723	22,672
<b>Pending</b>	571	177	960	454	800	613
<b>Deferred</b>	1,179	1,376	1,325	1,418	1,377	1,665
<b>Total</b>	21,182	21,910	23,272	24,201	24,900	24,950



## Schedule and Graph of Retired Members 1998 – 2003

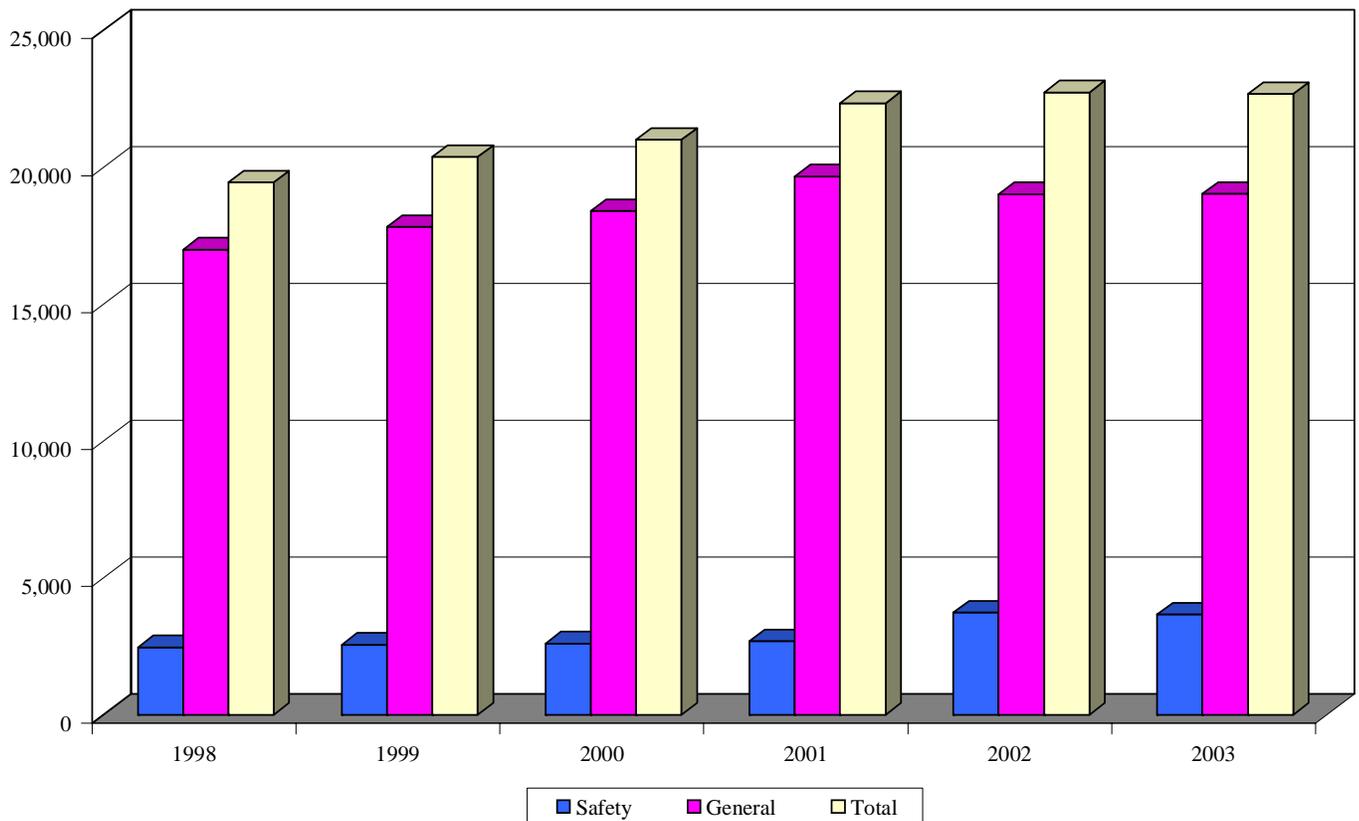
	1998	1999	2000	2001	2002	2003
<b>Service Connected Disability</b>	729	775	853	868	917	882
<b>Non-Service Connected Disability</b>	524	453	561	570	574	267
<b>Service Retirement</b>	5,991	6,309	6,501	6,778	7,197	7,801
<b>Total</b>	7,244	7,537	7,915	8,216	8,688	8,950*



\*Excludes 129 Qualified Domestic Relations Orders (QDRO) payees.

### Schedule and Graph of Active Members by Membership Classification\* 1998 – 2003

	1998	1999	2000	2001	2002	2003
<b>Safety</b>	2,456	2,556	2,605	2,676	3,721	3,649
<b>General</b>	16,976	17,801	18,382	19,653	19,002	19,023
<b>Total</b>	19,432	20,357	20,987	22,329	22,723	22,672



\* Excludes members with Deferred and Pending Status

## History of Actuarial Assumption Rates for the Period January, 1945 – December, 2003

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

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

### History of OCERS Actuarial Assumption Rates

<u>Effective Date</u>	<u>Interest Rate</u>	<u>Salary Assumption Rate</u>
1/1/45	2.50%	0.00%
7/1/62	3.50%	0.00%
12/31/65	4.00%	0.00%
7/1/69	4.50%	0.00%
6/30/70	5.00%	0.00%
8/31/73	5.75%	0.00%
7/1/75	6.00%	0.00%
7/1/81	7.25%	5.00%
7/1/89	7.50%	5.50%
7/1/91	8.00%	6.00%
7/1/96	8.00%	3.50%
7/1/00	8.00%	5.50%
7/1/03	7.50%	4.50%