The Popular Annual Financial Report looks at IMRF’s 2002 investment and overall financial performance for the year. We also outline who the members of IMRF are—by age and gender—and include an overview of 2002 events.

Continued investment declines over the past two years have raised concerns among IMRF members. They worry if “the money will be there” when they retire. Rest assured: your IMRF pension is safe.

**Defined Benefit security**
When it comes to retirement plans, two basic types exist—defined benefit (DB) plans and defined contribution (DC) plans.

In a DB plan like IMRF, your contributions and your employer’s contributions are invested to provide a defined retirement benefit based upon a specific formula using your final rate of earnings, total service credit, and age at retirement. All three factors determine the amount payable to you. In a DB plan, you are guaranteed payment of this amount for as long as you live.

**Defined Contribution risk**
The other type of retirement plan is a DC plan, such as a 401(k), 457, or 403(b) plan. DC plans do not promise a specific benefit amount, and if you participate in a DC plan, you assume responsibility—and risk—for all of your investments.

Under these plans, the amount of money available during retirement varies—depending upon how well (or how poorly) your investments perform. With many DC accounts, you select the number of payments to receive upon retirement. If too small a number is selected, you could actually outlive your monthly payments. If you participate in a DC plan, you’ve probably seen the value of your account decrease over the past two years.

**Designed to meet the challenge**
Defined benefit plans—like IMRF—are designed to meet the challenges of difficult markets.

*First,* outside actuaries use various financial and demographic assumptions to calculate how much your employer needs to set aside each year to accumulate sufficient assets to pay for your future retirement.

*Second,* IMRF follows an investment philosophy of diversification. Simply said: don’t put all your eggs in one basket. We invest in a variety of investments and, within each investment type, use a variety of investment styles. History has shown that diversification provides better long-term results with less overall risk.

*Third,* an individual investor may look at a 10, 15, or 20-year timeline. As an institutional investor, IMRF is investing for the lifetimes of our 300,000+ members. We view our investment return over a much longer timeline.

**Your future is secure**
The past several years have proven difficult for all investors, both individual and institutional. However, you can look at IMRF’s net assets of $13.5 billion and know that these assets are irrevocably committed to the payment of your future IMRF pension.

For more detailed information, you can request a copy of IMRF’s 2002 Comprehensive Annual Financial Report by calling 1-800-ASK-IMRF (1-800-275-4673) or by visiting the IMRF website, www.imrf.org.
As a defined benefit pension system, IMRF accumulates assets to provide benefits to members today and in the future.

**Additions to plan net assets**
IMRF accumulates money needed to fund benefits through member and employer contributions as well as returns on invested funds.

Member and employer contributions for 2002 totaled $529 million, which was the same amount as in 2001. For the first time in its history, IMRF incurred investment losses for two consecutive years. The $1,325 million investment loss in 2002 represents a $314 million increase from 2001.

- **Member contributions**
The increase in member contributions is due to an increase in total member earnings from $4,505 million in 2001 to $4,796 million in 2002.

- **Employer contributions**
The decrease in employer contributions resulted from several factors. Although member earnings increased overall by 6.4 percent—which caused employer contributions to increase—that increase was more than offset by lower average employer rates.

**Net investment loss**
In 2002, IMRF experienced a loss in the value of our investments of $1,625 million, more than $280 million greater than the $1,345 million depreciation recorded in 2001.

Although IMRF earned interest, dividends and equity fund income of $338 million, that amount was $32 million less than what was earned in 2001. Net security lending income was $4.6 million, a decrease of $2.6 million from 2001. Direct investment expenses decreased to $42.5 million in 2002 from $42.9 million the previous year.

The total rate of return for the portfolio in 2002 was –8.72 percent compared to –6.08 percent in 2001.

**Deductions to plan assets**

The increase in benefit payments to members and beneficiaries resulted primarily from growth in the number of retirees, increasing to 74,668 in 2002 from 72,832 in 2001 as well as an increase in the amount of the average benefit.

### Condensed Statements of Changes in Plan Net Assets

<table>
<thead>
<tr>
<th></th>
<th>2002</th>
<th>2001</th>
<th>Change</th>
<th>% Change</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Additions</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Member contributions</td>
<td>$234</td>
<td>$216</td>
<td>$18</td>
<td>8%</td>
</tr>
<tr>
<td>Employer contributions</td>
<td>295</td>
<td>313</td>
<td>(18)</td>
<td>(6)</td>
</tr>
<tr>
<td>Net investment loss</td>
<td>(1,325)</td>
<td>(1,011)</td>
<td>(314)</td>
<td>(31)</td>
</tr>
<tr>
<td>Total additions (loss)</td>
<td>(796)</td>
<td>(482)</td>
<td>(314)</td>
<td>(65)</td>
</tr>
<tr>
<td><strong>Deductions</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Benefits</td>
<td>613</td>
<td>571</td>
<td>42</td>
<td>7</td>
</tr>
<tr>
<td>Refunds</td>
<td>37</td>
<td>27</td>
<td>10</td>
<td>37</td>
</tr>
<tr>
<td>Administrative expenses</td>
<td>19</td>
<td>18</td>
<td>1</td>
<td>6</td>
</tr>
<tr>
<td>Total deductions</td>
<td>669</td>
<td>616</td>
<td>53</td>
<td>9</td>
</tr>
<tr>
<td>Net decrease</td>
<td>(1,465)</td>
<td>(1,098)</td>
<td>(367)</td>
<td>(33)</td>
</tr>
</tbody>
</table>

**Net Assets Held in Trust for Pension Benefits**

<p>| | | | | |</p>
<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Beginning of year</td>
<td>$14,966</td>
<td>$16,064</td>
<td>(1,098)</td>
<td>(7)</td>
</tr>
<tr>
<td>End of year</td>
<td>$13,501</td>
<td>$14,966</td>
<td>(1,465)</td>
<td>(10%)</td>
</tr>
</tbody>
</table>

**IMRF Revenues by Source**

<table>
<thead>
<tr>
<th></th>
<th>Members</th>
<th>Employers</th>
<th>Investment</th>
</tr>
</thead>
<tbody>
<tr>
<td>2002</td>
<td>$600</td>
<td>$0</td>
<td>$0</td>
</tr>
<tr>
<td>2001</td>
<td>$300</td>
<td>$0</td>
<td>$0</td>
</tr>
<tr>
<td>2000</td>
<td>$0</td>
<td>$0</td>
<td>$0</td>
</tr>
</tbody>
</table>

**IMRF 2002 Expenses by Type**

- Disability 1.5%
- Administrative 2.8%
- Death 3.2%
- Refunds 5.5%
- Annuities 87.0%
While the Statement of Changes in Plan Net Assets measures the value of IMRF’s net assets, another important factor needs to be considered to determine IMRF’s financial health. That factor is IMRF’s funded status—the difference between its actuarial liability and the value of its net assets.

**Checking the pulse**

You can think of IMRF’s actuarial liability as the dollar value of “benefit promises” to our members.

If you are vested, you have a promise from IMRF that we will pay you a certain amount at a certain age (your pension). The more service you earn and the larger your salary, the greater the dollar value of the promise.

If you are retired, you have a promise from IMRF that we will pay you a certain amount every month for the rest of your life. If your spouse is eligible for a surviving spouse pension, he or she also has a promise from IMRF. IMRF benefit promises also include refunds and death benefits.

When you add up all of the “benefit promises” IMRF has with all of our members—including members who left IMRF but still have contributions on deposit—you have the value of IMRF’s actuarial liability.

In 2002, IMRF collected member and employer contributions of $529 million; spent $669 million for benefit payments, refunds and administrative costs; and lost $1,325 million on our investments. These net results brought IMRF’s net asset base down to $13.5 billion. By law, those net assets are permanently committed to the payment of all of our benefit promises, including current retirees’ pensions and your future IMRF pension.

**Valuing IMRF assets**

When looking at the value of IMRF assets, you can look at them in one of two ways.

The first method is the simplest and most familiar: the market value. What is the value of all IMRF’s assets and liabilities today? Or for the purposes of this Popular Annual Report, what was the value on December 31, 2002?

The other method is less familiar—and not as simple. That method is called the “actuarial value” of assets. IMRF’s outside actuaries determine the actuarial value of IMRF’s assets by using a “five-year smoothing” technique.

With five-year smoothing, investment gains (or losses) are spread over five years; they are not “recognized” each year. The smoothing prevents employer contribution rates from changing drastically year-to-year because of short-term fluctuations in the investment markets.

**A healthy system**

A healthy pension fund—like IMRF—ensures that the “actuarial value” of its assets (the assets needed to pay benefit promises) closely matches its “actuarial liability” (benefit promises themselves).
Investment earnings are a major contributor to IMRF. Years 2002 and 2001 were unusual because IMRF suffered its first two consecutive years of investment losses. The total rate of return for IMRF’s portfolio in 2002 was –8.72 percent compared to –6.08 percent in 2001. As of December 31, 2002, IMRF’s investments totaled $13.9 billion, down from $15.2 billion at the end of 2001.

Long-term results
When looking at IMRF’s investment returns, it is important to remember that as a pension fund, the long-term timeline of IMRF’s investment program is designed to weather the ups and downs of the market. If you look at longer-term investment returns for IMRF, the results improve:

Three years (2002 through 2000) ............-4.4% per year
Five years (2002 through 1998) ............. 3.5% per year
Ten years (2002 through 1993) .......... 8.1% per year

IMRF’s income (“additions” to net assets, see table on page 2) comes from three sources: member contributions, employer contributions, and investment income. In the five years prior to 2002 and 2001, investment income represented the following percentage of additions to plan net assets:

<table>
<thead>
<tr>
<th>Year of Plan Additions</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>2000</td>
<td>33.7%</td>
</tr>
<tr>
<td>1999</td>
<td>82.5%</td>
</tr>
<tr>
<td>1998</td>
<td>71.9%</td>
</tr>
<tr>
<td>1997</td>
<td>75.4%</td>
</tr>
<tr>
<td>1996</td>
<td>73.4%</td>
</tr>
</tbody>
</table>

For the four months ended April 30, 2003, the overall return on IMRF’s investments has been approximately 3 percent, 9 percent on an annualized basis. As of April 30, 2003, IMRF’s total investments were approximately $14.4 billion, an increase of $500 million since December 31, 2002.

Professional management
Currently 39 professional investment management firms, handling 50 separate accounts, manage IMRF’s investment portfolio. These firms make investment decisions under the “prudent man” rule authorized by the Illinois Pension Code and by IMRF investment policy guidelines.

The IMRF Board of Trustees employs an investment consultant who monitors and evaluates the investment management firms’ performance, aids in the selection of investment management firms, and assists in the development of investment policy. A second consultant provides a real estate investment performance report.

The IMRF Board, its consultant and IMRF staff review IMRF’s asset allocation annually. Through diversification of investment type (stocks, bonds, real estate, etc.), region (domestic, international, global, etc.) and management style (growth, value, small, medium, or large capitalization, etc.), we enhance our goal of improving expected long-term returns while maintaining an acceptable level of risk.
The IMRF Plan

IMRF administers what is known as an “agent multiple-employer” public employee retirement system. The Illinois State Legislature established IMRF in 1939 to provide employees of local governments and school districts a sound and efficient retirement system.

**IMRF is NOT part of state government**

You may have read about Governor Rod Blagojevich’s plan to issue $10 billion in pension bonds to help balance the Illinois state budget. This proposal does not, in any way, affect IMRF. IMRF is not a state pension fund and is not funded by any state dollars.

IMRF is entirely funded by member contributions, investment returns, and contributions from IMRF employers. These employers include cities, villages, counties, school districts, townships and various special districts, such as parks, forest preserves and sanitary districts. IMRF employers are not state agencies.

**Participation**

Although more than 167,000 public employees across Illinois participate in IMRF, IMRF is a local program. Your employer builds up an account to provide future benefits for its own employees. As of December 31, 2002, 2,853 local units of government participated in IMRF, an increase of 27 employers over 2001.

IMRF employers must enroll an employee in IMRF if the employee’s position meets the qualifications for IMRF membership. However, some exceptions exist for city hospital employees and elected officials.

**Funding**

IMRF member contribution rates—4.5 percent for Regular members, 6.5 percent for SLEP members, and 7.5 percent for the Elected County Officials Plan (ECO)—are determined by Illinois statute.

Illinois statutes also require each IMRF employer to contribute the amount needed, in addition to contributions from members, to finance the retirement coverage of its own employees.

Employer contributions for disability benefits, death benefits, and the “13th check” are pooled. IMRF administrative costs are financed by investment income.
How closely do you match the “average” member?

An outside actuary uses specific membership demographics to determine how much money IMRF requires to pay its pension obligations. For detailed actuarial information, refer to the Actuarial Section of IMRF’s 2002 Comprehensive Annual Financial Report.

Are you an “average” member?
How closely do you match the “average member”? Of our 167,776 active members, here is the picture of the “average” IMRF member as of December 31, 2002:
- Female
- Slightly older than 45
- Participates in the Regular IMRF plan
- Most likely works for a school district
- Earns approximately $28,600 a year
- Received a 4.0% salary increase in 2002
- Has 8.5 years of service credit

Are you an “average” retiree?
If you are one of the 3,101 members who retired in 2002 under IMRF’s Regular plan, you are most likely:
- Female
- Had a final rate of earnings of approximately $2,558 a month
- Retired with approximately 20 years of service credit
- Receiving a pension of approximately $965 a month

Where the money for your benefits comes from
Both you and your employer contribute toward your future retirement benefits. You contribute a percentage of your salary as established by the Illinois Pension Code.

The percentage depends on which IMRF plan you participate in: Regular members contribute 4.5 percent, SLEP members contribute 6.5 percent, and ECO members contribute 7.5 percent.

IMRF employers each have a unique contribution rate based upon their own situation—their members’ salaries, ages, years of service credit, etc. Employers pay most of the cost for member and survivor pensions and all of the cost for death and disability benefits.

Employers in total will contribute more to IMRF in 2003 than they did in 2002. The increased contributions are due to generally higher employer contribution rates caused by investment losses during the 2000-2002 period and an anticipated 6.4 percent increase in total payroll reported to IMRF.
Looking Back at 2002

Board of Trustees
R. Steven Sonnemaker, County Auditor of Peoria County, was re-elected as an executive trustee. His five-year term began January 1, 2003.
Rita J. Miotti, Contract Management Services Coordinator for the Village of Matteson, was appointed on January 24, 2003, as an employee trustee to fill a vacancy created when former Trustee Julie A. Newell left the Board. Ms. Miotti’s term ends on December 31, 2003.

Mainframe Computer System Development
Changes were implemented in the disability processing system to eliminate the pre-existing conditions provisions for temporary disability benefits eligibility.
A separate enhancement to the disability system automated more than 98% of initially calculated claims as well as those claims recalculated when new data is received.
The development of a comprehensive purchase of service system reached the system testing phase.
The member enrollment and member data maintenance system development project is in the coding phase.
Significant progress was made on our project to enhance the death claim processing system.

Investment Activities
In 2002, at the direction of the Board of Trustees, the IMRF staff, assisted by its investment consultant and IMRF’s outside actuaries, performed an Asset Liability Study. The purpose of the study was to harmonize various investment policies with contribution and benefit policies to achieve IMRF’s mission.
The main recommendation arising from this study was to decrease the asset allocation to equities by 5 percent and to increase the allocation to fixed income by 5 percent.

IMRF Website, www.imrf.org
Significant progress was made in 2002 towards developing a secure area on our website for members to view personal information and to develop benefit estimates using their most current earnings and service data. This interactive website went live on April 1, 2003.

Please turn to page 8

Member Contributions Paid vs. Retirement Benefits Received

When you apply for your IMRF pension, we calculate the total cost of your pension. We then subtract the member contributions you paid from the cost of your pension. Whatever cost remains is deducted from your former IMRF employer’s account. Typically, the employer pays approximately 80% of the cost for an IMRF pension. Employers pay for all of the costs for disability benefits, death benefits, and the “13th check.”

To better illustrate the value of an IMRF pension, the chart at left compares what an average member paid in contributions to what an average retiree received in retirement benefits.
Springfield Regional Counseling Center
Year 2002 was the first full year of operations for IMRF’s Springfield office. The three-person office handled 396 individual counseling sessions, 32,828 telephone calls and generated 3,447 pension estimates. Average hold times for the 1-800-ASK-IMRF telephone line decreased significantly. Other workshops, presentations and legislative meetings were held in the office.

Business Continuity Planning
IMRF has a Disaster Recovery Plan in place that would allow staff to quickly reestablish our computer and telecommunications systems at a backup location if our main office was unavailable due to some disaster event. We are working to expand that Plan into a comprehensive Business Continuity Management program that would help us restore order as quickly as possible in the event of a disruption of our operations.