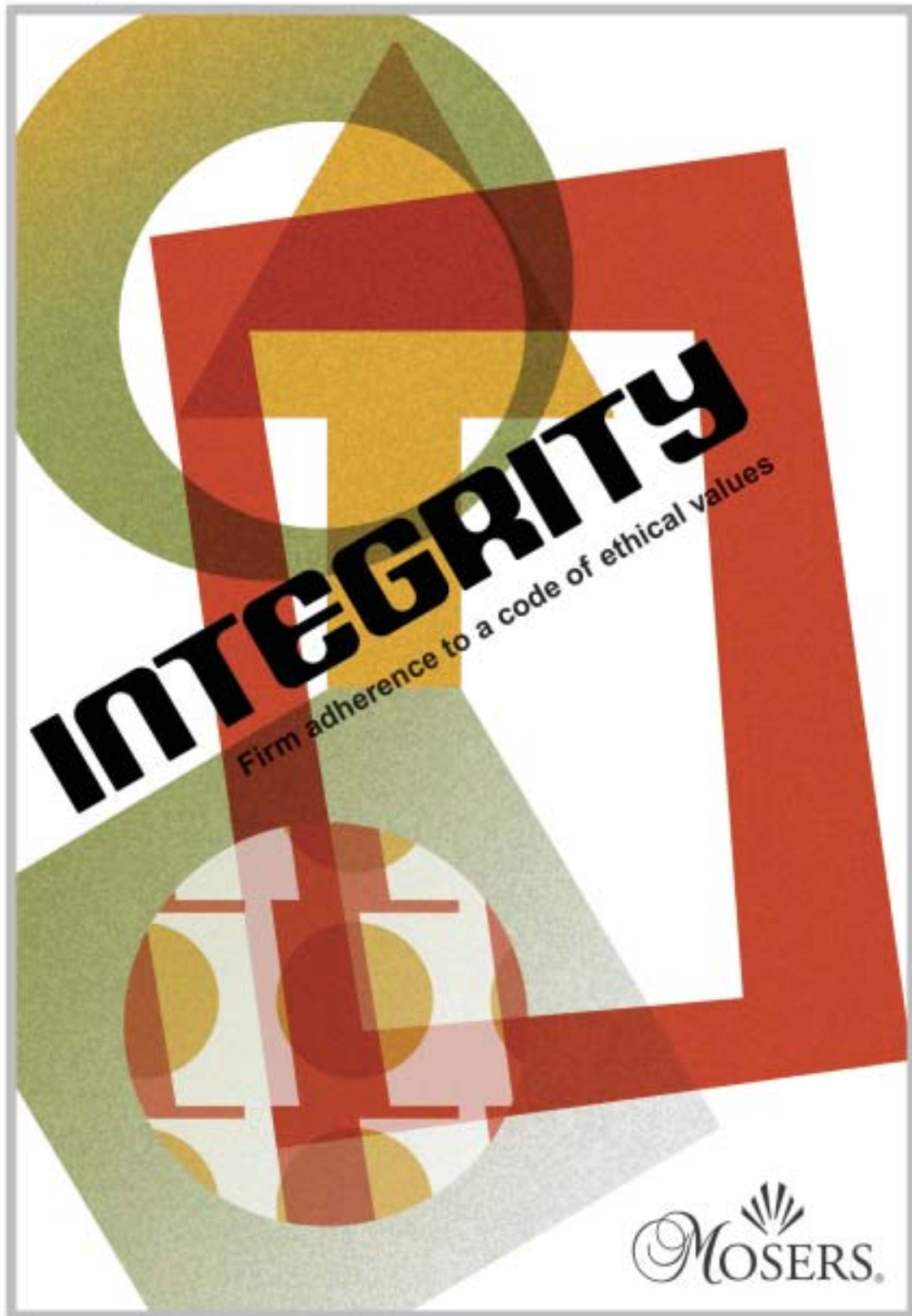
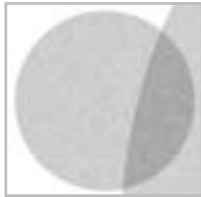


Missouri State Employees' Retirement System
A Component Unit of the State of Missouri



Comprehensive Annual Financial Report
Fiscal Year Ended June 30, 2002



“Integrity, balance, security, trust, strength, and stability – these are the core values that shape MOSERS’ guiding principles. These principles characterize the highest ethical standards and promote a work culture that enables us to act in the exclusive interest of the members of our system.”

Gary Findlay
Executive Director

Missouri State Employees' Retirement System
A Component Unit of the State of Missouri

Gary Findlay
Executive Director

Gary Irwin
Chief Finance Officer



Comprehensive Annual Financial Report
Fiscal Year Ended June 30, 2002

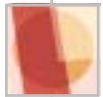


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* Missouri State Employees’ Plan

** Administrative Law Judges and Legal Advisors’ Plan



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Certificate of Achievement



Letter of Transmittal



September 26, 2002

The Board of Trustees
Missouri State Employees' Retirement System
907 Wildwood Drive
Jefferson City, MO 65109

Dear Board Members:

It is again with great pleasure that I submit this year's annual report of the Missouri State Employees' Retirement System (MOSERS).

Fiscal Year 2002 Highlights

Last fiscal year, MOSERS staff began work on the implementation of legislation that provided for a Deferred Retirement Option Provision (BackDROP) for general state employees, which became effective January 1, 2002. As of June 30, 2002, 308 members elected to retire utilizing the BackDROP feature and received \$19,162,726 in BackDROP payments.

Included in these totals were 198 members who chose to directly rollover \$12,739,639 of their payments into another qualified plan or IRA and eleven members who opted to receive their BackDROP payment in three annual installments with \$291,981 being paid in the current fiscal year and \$583,963 to be paid in the future. Additional information regarding the BackDROP option is included in this annual report and on our web site.

New federal legislation also went into effect January 1, 2002, that enabled members to directly rollover funds from their deferred compensation plan to purchase service credit in MOSERS. This resulted in a significant

increase in service purchases processed by MOSERS staff. For the six months ending June 30, 2002, MOSERS received \$3,243,763 for the purchase of service credit, and of that total, \$2,459,427 came from direct rollovers. For the same time period ending June 30, 2001, MOSERS only received \$901,369 for the purchase of service credit.

With the passage of Senate Bill 371 last year, a mandatory defined contribution plan for new "education employees" hired at the regional colleges and universities became effective July 1, 2002. Staff worked in conjunction with our external asset consultant, Summit Strategies, to conduct a formal search and hire a third-party administrator for the new plan. After a thorough search and complete review of investment offerings, educational programs, administrative capabilities, and costs, the Teachers Insurance & Annuity Association – College Retirement Equities Fund (TIAA-CREF) was selected from a competitive pool of candidates as the third-party administrator. Staff worked with TIAA-CREF and the regional colleges and universities throughout Missouri to implement this new plan and will continue to make refinements to the administration of the plan.

Report Contents and Structure

MOSERS is considered a component unit of the state of Missouri for financial reporting purposes and, as such, the financial statements contained in this report are also included in the *State of Missouri Comprehensive Annual Financial Report*. The financial information presented in this report is the responsibility of the management of MOSERS, and sufficient internal accounting controls exist to provide reasonable assurance regarding the safekeeping of assets and fair presentation of the financial statements, supporting schedules, and statistical tables. The report is also designed to comply with the reporting requirements of Sections 104.480, 104.1006, and 105.661 of the Revised Statutes of Missouri (RSMo) as amended. The report is divided into the following five sections:

- the **Introductory Section**, which contains general information regarding the operations of MOSERS.
- the **Financial Section**, which contains the financial statements, schedules, and supplementary financial information regarding the funds administered by MOSERS.
- the **Investment Section**, which contains information pertaining to the management of the investments of the Pension Trust Funds.
- the **Actuarial Section**, which contains information regarding the financial condition and financial position of the retirement plans administered by the system.
- the **Statistical Section**, which contains general statistical information regarding system participants and finances.

Summary of Financial Information

The following schedule is a summary of the Pension Trust Funds' additions and deductions for the years ended June 30, 2002, and June 30, 2001.

	<u>June 30, 2002</u>	<u>June 30, 2001</u>
Additions	\$ (113,571,787)	\$ 128,977,714
Deductions	(291,085,249)	(239,464,885)
Net Change	<u>\$ (404,657,036)</u>	<u>\$ (110,487,171)</u>

Additions decreased by \$242,549,501 primarily due to a decrease in net investment income of \$237,832,244. Deductions increased by \$51,620,364 primarily due to an increase of \$51,611,866 in benefit payouts for the year.

The following schedule is a summary of the revenues and expenses of the Internal Service Fund (insurance activity) for the years ended June 30, 2002, and June 30, 2001.

	<u>June 30, 2002</u>	<u>June 30, 2001</u>
Operating revenues	\$ 25,190,197	\$ 23,649,880
Operating expenses	(25,192,940)	(23,596,435)
Nonoperating revenues	47,767	81,717
Net Change	<u>\$ 45,024</u>	<u>\$ 135,162</u>

Operating revenues increased by \$1,540,317 primarily as a result of an increase in basic life premiums due to the increase in coverage, effective January 1, 2001. The basic life coverage afforded active employees increased from \$15,000 per employee to one times annual salary subject to a floor of \$15,000 of coverage. Likewise, operating expenses increased by \$1,596,505 primarily as a result of transmitting increased premiums to the insurance company, offset by a reduction of \$626,637 in the amount of premium refunds issued. In the fiscal year ended June 30, 2001, there was an unusually high volume of refunds issued as a result of the conversion from premiums paid in advance to premiums paid in arrears and the state of Missouri's conversion to a lag payroll system. The decrease in nonoperating revenues resulted primarily from a continuing decline in interest rates during the fiscal year.

Plan Financial Condition

The funding objective of MOSERS' Pension Trust Funds is to meet long-term benefit promises through contributions, which remain approximately level as a percent of member payroll over decades of time. Historical information relating to progress in meeting this objective is presented on pages 36-41. During the year ended June 30, 2002, the funded ratio of the Missouri State Employees' Plan, which covers 92,375 participants, decreased from 97% to 95.9%, primarily as the result of plan investment experience. The funded ratio of the Administrative Law Judges and Legal Advisors' Plan, which covers 102 participants, decreased from 85.7% to 83.5%, primarily as the result of plan investment experience. Funding of the Judicial Plan, which covers 838 participants, began on July 1, 1998. During the year ended June 30, 2002, the funded ratio of the Judicial Plan increased from 9.1% to 11.6%, primarily as the result of favorable experience in the aggregate. Additional information regarding the financial condition of the Pension Trust Funds can be found in the Actuarial Section of this report.

Investment Activity

MOSERS' investment portfolio produced a total return, net of expenses, of -6.2% for the year ended June 30, 2002. Even though the return was negative again this year, we are pleased that the MOSERS' investment policies in place have worked as intended. The policy benchmark return for the year was off by -8.8%, which indicates MOSERS' practices resulted in a +2.6% value added versus the markets for the year. The fund has achieved its goal of adding value over its policy benchmark and, for the longer term, has continued to exceed the actuarial target rate of a 5% real return. Additional information regarding the investment results for the year is included in the Investment Section of this report.

Legislation Enacted During the 2002

Legislative Session

On July 11, 2002, Governor Bob Holden signed into law HB 1455 – legislation that involved minor modifications to and clarifications of the Missouri State Employees' Plan, the Administrative Law Judges and Legal Advisors' Plan, and the Judicial Plan. These changes were designed to enable MOSERS to more effectively administer these plans as well as ease some of the administrative burden associated with members and their beneficiaries applying for and receiving benefits. There were no benefit increases enacted in the fiscal year ended June 30, 2002.

Certificate of Achievement for Excellence in Financial Reporting

The Government Finance Officers Association of the United States and Canada (GFOA) awarded a *Certificate of Achievement for Excellence in Financial Reporting* to MOSERS for its Comprehensive Annual Financial Report (CAFR) for the fiscal year ended June 30, 2001. The Certificate of Achievement is a prestigious 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 CAFR conforming to program standards. The CAFR must satisfy both generally accepted accounting principles and applicable legal requirements. A Certificate of Achievement is valid for a period of one year only. MOSERS has received a Certificate of Achievement for the last thirteen consecutive years (fiscal years ended 1989-2001). We believe our current report continues to conform to the Certificate of Achievement program requirements, and we are submitting it to GFOA for evaluation.

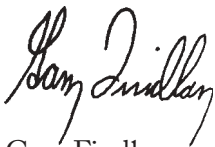
Conclusion

This report is a product of the combined efforts of the MOSERS' staff and advisors functioning under your leadership. It is intended to provide complete and reliable information, that will facilitate the management decision process; serve as a means for determining compliance with legal requirements; and allow for the evaluation of responsible stewardship of the funds of the system. As in the past, MOSERS received an unqualified opinion from our independent auditors on the financial statements included in this report. The opinion of the independent auditor can be found on page 18.

Copies of this report are provided to the Governor, State Auditor, Joint Committee on Public Employee Retirement of the General Assembly, and all state agencies. These agencies form the link between MOSERS and its members, and their cooperation contributes significantly to the success of MOSERS. We hope all recipients of this report find it informative and useful.

I would like to take this opportunity to express my gratitude to you, the staff, the advisors, and other people who have worked so diligently to assure the continued successful operation of the system.

Respectfully submitted,

A handwritten signature in black ink, appearing to read "Gary Findlay". The signature is written in a cursive, flowing style.

Gary Findlay
Executive Director

Letter From The Chairman



September 26, 2002

Dear Members:

On behalf of the board of trustees, I am pleased to present the *MOSERS' Comprehensive Annual Financial Report* for the fiscal year ended June 30, 2002. This report provides information on the financial status of your retirement system while also highlighting significant changes that occurred during the year.

Your retirement system remains well funded and your promised benefits are secure despite the difficult investment environment and sluggish economy. Although the fund generated a loss of -6.2% net of expenses this fiscal year, it outperformed the policy benchmark by 2.6% – a small but welcomed feat in a very volatile investment market. The board policy of preserving system assets and maximizing the long-term growth of those assets through diversification will continue to be our primary focus as we move into the next fiscal year.

The board experienced some turnover this past year due to the retirements of Senator John Scott, and Steve Price, Director of House Appropriations. Mike Hartmann also resigned from the board after leaving his position as Commissioner of Administration to become

the Governor's Chief of Staff. On behalf of the board, staff and membership, I would like to express our collective thanks to these dedicated and experienced individuals for their many contributions to the system and for serving our membership so well. The board also welcomed Senator Ed Quick and Lori Strong-Goeke this year, and we look forward to serving and working with them.

In closing, I would like to thank the staff at MOSERS for continuing to maintain a high level of commitment and service to our plan participants. If you have any questions regarding this report, please contact us at MOSERS, PO Box 209, Jefferson City, MO 65102 or by calling 1-800-827-1063.

Sincerely,

A handwritten signature in cursive script, appearing to read "Bill Skaggs".

Representative Bill Skaggs, Chairman
Board of Trustees



Board of Trustees



Seated left to right

Senator Ed Quick
Member of the Senate

Representative Bill Skaggs
Board Chairman
Member of the House of Representatives

Bryan Ornburn
Elected Retired Member

Tom Hodges
Field Services Coordinator
Board of Probation and Parole
Department of Corrections
Elected Active Member

Jacquelyn White
Commissioner
Office of Administration
Ex-Officio Member

Standing left to right

Lori Strong-Goeke
Assistant Director
Office of Administration
Division of Budget and Planning
Governor Appointed Member

Representative Richard Franklin
Member of the
House of Representatives

Carol Gilstrap
Vice Chairman
Vice President and Team Leader
US Bank - Government Banking Division
Governor Appointed Member

Nancy Farmer
State Treasurer
Ex-Officio Member

Not Pictured

Senator John Russell
Member of the Senate

Vacant
Elected Active Member



Administrative Organization



Pictured left to right

Rick Dahl

Deputy Executive Director
Chief Investment Officer

Karen Stohlgren

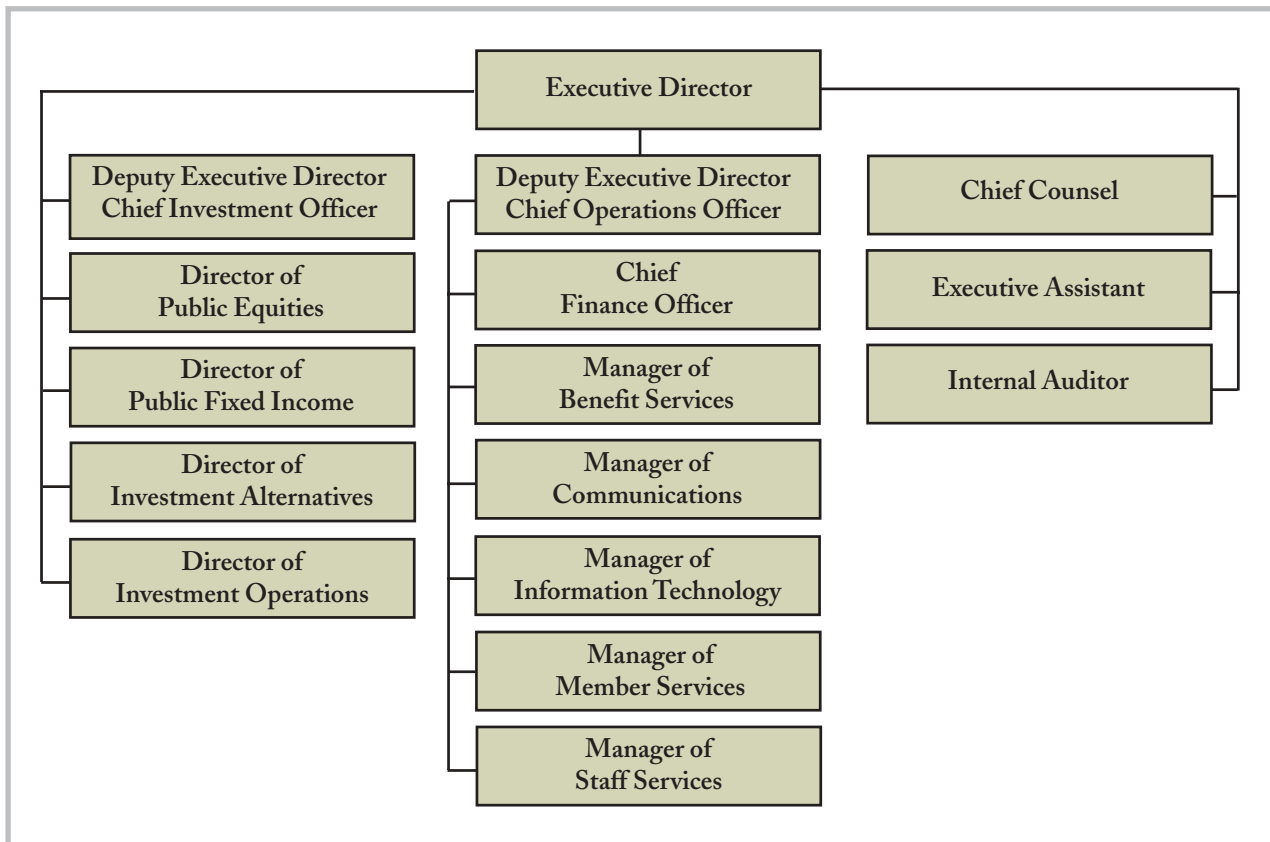
Deputy Executive Director
Chief Operations Officer

Gary Findlay

Executive Director



Administrative Organization





About MOSERS

MOSERS was established September 1, 1957, and is governed by laws of the state of Missouri.

Purpose

MOSERS provides retirement, survivor and disability benefits, and life insurance to its members.

MOSERS administers retirement benefits for most state employees, including members of the Missouri General Assembly, elected state officials, administrative law judges and legal advisors, and judges. MOSERS is responsible for administering the law in accordance with the expressed intent of the Missouri General Assembly and bears a fiduciary obligation to the state employees who are its members and beneficiaries.

MOSERS Mission

To play an integral role in the future financial security of plan participants by promptly and courteously delivering quality benefits and information which members value and trust through professional plan administration and prudent management of system assets.

Administration

State law provides that responsibility for the administration of MOSERS is vested in an eleven member board of trustees. The board is comprised of:

- Two members of the Senate appointed by the President Pro Tem of the Senate.
- Two members of the House of Representatives appointed by the Speaker of the House.
- Two members appointed by the Governor.
- The State Treasurer.
- The Commissioner of Administration.
- Three other members of the system: two active members elected by the active and terminated-vested members, and one retiree elected by the retired members.

The day-to-day management of MOSERS is delegated to the executive director who is appointed by the board and serves at its pleasure. The executive director acts as advisor to the board on all matters pertaining to the system and, contracts for professional services and employs the remaining staff needed to operate the system.

Organization

The executive director, deputy executive director - chief operations officer, and the deputy executive director - chief investment officer are responsible for planning, organizing, and administering the operations of the system under the broad policy guidance and direction of the board.

MOSERS' office is divided into eight administrative sections that perform specific functions for the system.

Executive Services

The executive services team provides administrative support by assisting the executive director and chief operations officer in the major legal, operational, and oversight functions of the retirement, benefit, and communication programs.

Accounting

This section is responsible for all financial records of the programs administered by MOSERS, including the preparation of financial and statistical reports. Accounting performs the purchasing functions for MOSERS and interfaces with the investment custodian, investment managers, Office of Administration accounting, various payroll/personnel departments, life insurance companies, actuaries, banks, and the IRS.



About MOSERS

Benefit Services

Benefit services is responsible for all contact with the membership regarding the benefit programs administered by MOSERS, which include retirement, life insurance, and long-term disability.

Communications

Communications is responsible for providing clearly written and attractively designed publications and educational seminars needed to inform all members about benefit programs administered by MOSERS. Communications and the information technology section are jointly responsible for MOSERS' web site.

Information Technology

Utilizing an IBM AS400 minicomputer and high-end work stations, information technology provides all computer and technical design support for MOSERS' data processing activities. This group is responsible for establishing and updating computer programs to implement plan changes and also maintains members' folder information on FileNet - an optical disk image system that allows information to be stored and processed using computer displayed images of original documents. Information technology is also responsible for administration of the personal computer network and the telephone system. Information technology and the communications section are jointly responsible for MOSERS' web site.

Investments

The primary functions of the investment staff are to provide internal investment management and consulting services to the board and the executive director. Other functions include hiring and terminating external investment managers, analyzing and rebalancing the overall asset allocation and portfolio, serving as a liaison to the investment community, and informing and advising the board and executive director on financial, economic, and political developments which may affect the system. The investments staff also works with the asset consultant and the executive director in selecting and monitoring external money managers. Information regarding the investment professionals who provide services to MOSERS can be found on pages 59-71 of the Investment Section.

Member Services

Member services is responsible for establishing and maintaining all membership records - including maintenance of the data on the electronic imaging system, balancing payroll deductions for insurance, and entering the payroll, service, and leave data into the system's computerized database.

Staff Services

Staff services provides clerical support, mail services, and general building maintenance for MOSERS' personnel. Human resources is also represented in this section.



Outside Professional Services

Actuary

Gabriel, Roeder, Smith & Co.
Actuaries and Consultants
Norman L. Jones, Brad Armstrong
Southfield, Michigan

Auditors

KPMG LLP
Certified Public Accountants
Andrew J. Blossom, Melissa Benton
Kansas City, Missouri

Legal Counsel

Thompson Coburn
Attorneys at Law
Allen Allred, Tom Litz
St. Louis, Missouri

Master Custodian

Mellon Trust
John Vanderpool, Irene Speridakos
Boston, Massachusetts

Investment

Management Consultant
Summit Strategies, Inc.
Steve Holmes, Tom Pollihan
St. Louis, Missouri

Equity Investment Advisors

Advanced Investment Management, Inc.
William Belko, Tom Allen
Pittsburgh, Pennsylvania

AmeriCap Advisers, LLC

Michael Gayed, Steve Shobin
New York, New York

Capital Guardian Trust

Mike Nyeholt, Andy Barth
Los Angeles, California

Dimensional Fund Advisors, Inc.

Rex Sinquefeld, Carol Wardlaw
Santa Monica, California

Legg Mason

Capital Management, Inc.

James P. Daly, Jr.,
Kyle Prechtl Legg
Baltimore, Maryland

Mastholm

Asset Management, LLC
Thomas Garr, Theodore Tyson
Bellevue, Washington

Merrill Lynch

Asset Management Group
Rick Vella, Lisa Torrington
New York, New York

Oak Associates, Ltd.

Sandra Noll, Jim Oelschlager
Akron, Ohio

OakBrook Investments

Michael J. Lorenzen,
Janna L. Sampson
Lisle, Illinois

Silchester International Investors

Christopher B. Cowie,
Stephen C. Butt
London, England

Diversification Pool

Investment Advisors
BlackRock Financial Management
Rob Capaldi, Andy Phillips,
Dennis Schaney
New York, New York

Hoisington Investment

Management Co.
Van Hoisington, Lacy Hunt
Austin, Texas

NISA Investment Advisors, LLC

Robert Krebs, Bill Marshall
St. Louis, Missouri

Risk Management Consultant

Charlesworth & Associates, LLC
Art Charlesworth,
Bob Charlesworth
Overland Park, Kansas

Securities Lending Advisors

Credit Suisse
First Boston Corporation
Dwight Skerrit
New York, New York

Lehman Brothers

Ann Erni
New York, New York

Third-Party Administrators

The Standard Insurance
Tom Trussell
Overland Park, Kansas

TIAA-CREF

Paul Kissel, Lisa Dunkel
Chicago, Illinois