POLICEMEN'S ANNUITY AND BENEFIT FUND OF CHICAGO

(Component Unit of the City of Chicago)
Financial Statements
For the Years Ended December 31, 2010 and 2009

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December 31, 2010 and 2009

TABLE OF CONTENTS

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REPORT OF INDEPENDENT AUDITORS

Board of Trustees
Policemen's Annuity and Benefit Fund of Chicago

We have audited the accompanying statements of plan net assets of the Policemen's Annuity and Benefit Fund of Chicago (the Fund) as of December 31, 2010 and 2009, and the related statements of changes in plan net assets for the years then ended. These financial statements are the responsibility of the Fund'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. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Fund's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, 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 Policemen's Annuity and Benefit Fund of Chicago as of December 31, 2010 and 2009, and the changes in plan net assets for the years then ended in conformity with accounting principles generally accepted in the United States.

The accompanying management's discussion and analysis and the required supplementary information as listed in the table of contents are not a required part of the basic financial statements but are supplementary information required by the Governmental Accounting Standards Board (GASB). We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However, we did not audit the information and we express no opinion on it.

Our audit was conducted for the purpose of forming an opinion on the basic financial statements taken as a whole. The other supplementary schedules of administrative expenses, consulting costs, and investment fees are presented for the purpose of additional analysis and are not a required part of the basic financial statements. These other supplementary schedules have been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, are fairly stated in all material respects in relation to the basic financial statements taken as a whole.

Mitchell & Titus, LLP

June 22, 2011

The Management's Discussion and Analysis section of this report is intended to serve as an introduction to the financial statements of the Policemen's Annuity and Benefit Fund of Chicago (the Fund) and to supplement the information contained therein.

Overview of Financial Statements and Accompanying Information

The basic financial statements are prepared in accordance with generally accepted accounting principles as established by the Governmental Accounting Standards Board (GASB) and are described below:

- **The Statements of Plan Net Assets** report the Fund's assets, liabilities, and the resultant net assets where assets minus liabilities equal net assets available at the end of the year.

- **The Statements of Changes in Plan Net Assets** show the sources and uses of funds during the calendar year, where additions minus deductions equal the net increase (or decrease) in net assets available for the year.

- **The Notes to the Financial Statements** are an integral part of the financial statements and include important information and schedules to provide a more comprehensive understanding of the data provided in the financial statements. Information contained in the note disclosures includes the Fund's accounting policies, descriptions of pension and health benefits and related liabilities, detail of investments and related risks, fund reserves, and various other relevant topics.

- **Required Supplementary Information** presents detailed required historical information and is presented after the Notes to the Financial Statements. This supplementary information includes data on funding progress and employer contributions, along with other information useful in evaluating the financial condition of the Fund.

Financial Highlights

- The net assets of the Fund increased by $114 million, or 3.3% to $3,440 million during 2010; increasing from $3,326 million at December 31, 2009; and from $3,001 million at December 31, 2008.

- Fund investment income earned, net of investment-related expenses, approximately $378 million during 2010 compared to a gain of approximately $576 million during 2009. The positive return reflects additional improvement in global capital markets, which delivered positive returns, as economic indicators hinted further stabilization following the 2008 credit crisis. All asset classes experienced positive earnings in 2010, and the main contributors to absolute performance were again U.S. and International Equity, as well as Fixed Income. On a relative basis, Private Capital (comprised of Private Equity, Real Estate and Infrastructure), Fixed Income and Non-U.S. Equity compared favorably to their respective benchmarks. While the overall Equity allocation showed a strong year, U.S. Equity slightly trailed its benchmark on a relative basis. In the Alternatives Investment space, the Fund of Hedge Fund allocation also trailed its benchmark by a small margin in 2010.

Financial Highlights *(continued)*

- The Fund received contributions of $108.4 million from members and $183.8 million from the City of Chicago in 2010, compared to contributions of $95.6 million from members and $180.5 million from the City of Chicago in 2009. The number of active members declined by 3.2% from 2009 to 2010; however, the increase in contributions is primarily due to a retroactive wage increase provided to active members in August 2010, which was reflective of a new employment contract between the City of Chicago and collective bargaining groups for various ranks within the Chicago Police Department, with salary increases effective July 1, 2007. The retroactive increases resulted in $12.3 million of additional member contributions in 2010. Also contributing to the increase is approximately $2.0 million of incremental purchases of service credit from prior law enforcement positions, including military service. Employer contributions from the City of Chicago decreased by 1.8%. Employer contributions are mandated by a statutorily set multiplier of 2.0 times member contributions collected two years prior. The decrease in contributions is reflective of member contributions from 2009. Active membership declined by 1.6% from 2008 to 2009.

- Benefit payments, excluding death benefits and refunds, increased by approximately $27.6 million in 2010, from $506.9 million in 2009 to $534.5 million in 2010. The number of retirees and beneficiaries increased in 2010 by 226 members or 1.6%, thus contributing to the increase. Another reason for the increase is the annual cost of living adjustments provided to retirees born prior to January 1, 1955, and retroactive retirement and disability benefits provided to members in 2010, reflective of the new salary contract between the City of Chicago and collective bargaining groups for various ranks within the Chicago Police Department, with revised salary increases dating to July 1, 2007. Death benefits and refunds of employee deductions increased slightly from 2009 to 2010 by approximately $1.5 million, from $7.9 million to $9.4 million, respectively.

- Administrative expenses declined by approximately $.38 million, or 8.8%, from $4.304 million in 2009 to $3.925 million in 2010. The decreased administrative expense is primarily due to reduced consulting fees related to actuarial, medical, and software development service fees.

- The funding objective of the Fund is to meet its long-term defined pension benefit obligations. The funding ratio of the Fund on a fair value basis experienced an insignificant decrease, from 37.4% at December 31, 2009 to 36.7% at December 31, 2010.

- Under Government Accounting Standard Board (GASB) numbers 25 and 43, the Fund uses a five-year actuarial smoothing method in valuing its assets to determine its funded status and the contributions required to fund the plan going forward. This actuarial valuation method reduces the effect of short-term market volatility and provides a more stable trend valuation for the Fund's long-term planning needs. The funding ratio of the Fund using an actuarial value of assets experienced a decrease, from 43.7% at December 31, 2009 to 39.7% at December 31, 2010.

Financial Highlights *(continued)*

- In compliance with GASB No. 45, the Fund recognizes a liability for other post-employment benefits (OPEB), which represent health insurance coverage for active and retired employees of the Fund. This obligation was first accrued as an expense in the 2008 financial statements in the amount of $.345 million at December 31, 2008; expense of $.174 million and $.440 million was recognized in 2009 and 2010, respectively, resulting in a total accrued liability of $.831 million as of December 31, 2010.

Plan Net Assets

A summary of plan net assets is presented below:

Plan Net Assets
(In millions)
As of December 31, 2010, 2009 and 2008

				2010–2009 Change	
	2010	**2009**	**2008**	**$**	**%**
Receivables	$ 212.9	$ 204.9	$ 197.9	$ 8.0	3.9
Brokers – unsettled trades	276.4	121.3	359.4	155.1	127.9
Investments, at fair value	3,301.1	3,150.0	2,847.3	151.1	4.8
Invested securities lending collateral	295.7	375.1	287.6	(79.4)	(21.2)
Total assets	4,086.1	3,851.3	3,692.2	234.8	
Brokers – unsettled trades	344.2	144.1	393.2	200.1	138.9
Securities lending payable	295.7	376.1	292.6	(80.4)	(21.4)
OPEB obligation	0.8	0.5	0.3	0.3	60.0
Accounts payable and accrued expenses	5.7	4.5	5.1	1.2	26.7
Total liabilities	646.4	525.2	691.2	121.2	
Net assets	$ 3,439.7	$ 3,326.1	$ 3,001.0	$ 113.6	

The increase in net assets of $113.6 million in 2010 was primarily driven by investment income. The assets available for investment earned 12.72% in 2010, compared to an investment gain of 21.5% in 2009. The combination of continuous government programs and extremely accommodative monetary policy around the world helped sustain the recovery. This has enabled the Fund to continue to recover part of the severe losses experienced in 2008.

Changes in Plan Net Assets

The following table reflects a comparative summary of various changes in plan net assets.

Changes in Plan Net Assets
(In millions)
Years Ended December 31, 2010, 2009 and 2008

				2010–2009 Change	
	2010	**2009**	**2008**	**$**	**%**
Additions:					
Member contributions	$ 108.4	$ 95.6	$ 93.2	$ 12.8	13.4
Employer contributions	183.8	180.5	181.5	3.3	1.8
Net investment gains (losses) and investment income	368.7	566.0	(1,104.4)	(197.3)	(34.9)
Securities lending income (loss)	0.9	1.3	(0.5)	(0.4)	(30.8)
Miscellaneous income	0.0	0.8	0.2	(0.8)	(100.0)
Total additions	661.8	844.2	(830.0)	(182.4)	(21.6)
Deductions:					
Annuity, disability, and death benefits	$ 536.3	$ 508.5	$ 491.6	$ 27.8	5.5
Refunds of contributions	7.6	6.2	6.1	1.4	22.5
OPEB expense	0.4	0.2	0.3	0.2	100.0
Administrative expenses	3.9	4.3	4.2	(0.4)	8.8
Total deductions	548.2	519.2	502.2	29.0	5.6
Net increase	$ 113.6	$ 325.0	$ (1,332.2)	$ (211.4)	

The Fund continues to experience a net increase in net assets, with net increases in both 2010 and 2009. The increases are primarily due to positive investment returns, with net assets available for investment earning 12.72% and 21.5% in 2010 and 2009, respectively. The net investment gains in 2010 were slightly offset by an increase in deductions of approximately $29 million, primarily due to increased member benefits as the number of retirees increased in 2010 and retirements were significantly above levels in 2009 and 2008. This increased retirement levels are partially attributed to some early retirement health care benefits offered to members by the City of Chicago in 2010.

Investment Activities

The Fund continues to move cautiously toward alternative investments and the Board of Trustees approved a revised strategic allocation in late 2010. Overall, rebalancing activity was marginal during 2010, other than continuous selling of U.S. Equity investments to bring the current allocation closer to policy targets. Proceeds from such sales were used immediately for benefit funding requirements.

By year-end 2010, the Board of Trustees, working closely with its investment consultant, had established target allocations of: U.S. equities, 21%; international equities, 20%; fixed income, 22%; tactical and opportunistic, 19%; real assets, 4%; private equity, 7%; real estate, 5%; and infrastructure, 2%. The previously established target asset allocation was: U.S. equities, 30%; international equities, 18%; fixed income, 25%; real estate, 7%; private equity, 7%; opportunistic strategies, 9%, and infrastructure, 4%.

Investment Returns
Years Ended December 31, 2010, 2009 and 2008

	2010	2009	2008
Total Fund	12.72%	21.50%	(27.83)%
Equities	15.60	34.78	(40.16)
Fixed Income	7.91	11.62	(4.08)
Alternatives	5.29	10.96	-
Private Capital	11.40	(16.49)	(8.06)
Cash and Cash Equivalents	.19	.48	2.55

Private Capital consists of investments in private equity, real estate and infrastructure. Alternative investments consists of fund of hedge fund investments.

Plan Membership

The following table reflects the plan membership as of December 31, 2010, 2009 and 2008.

Changes in Plan Membership
As of December 31, 2010, 2009 and 2008

	2010	2009	2008	2010-2009 Change	2010-2009 %
Retirees and beneficiaries receiving benefits	12,380	12,154	12,183	226	1.9
Active employees	12,737	13,154	13,373	(417)	(3.1)
Terminated (inactive members) employees entitled to benefits or refunds of contributions	620	634	636	(14)	(2.2)
Total	25,737	25,942	26,192	(205)	

Funding Status

The actuarial value of assets, using the GASB 25 and 43 methods, for the December 31, 2010 valuation was $3,719 million and the actuarial liability was $9,375 million. The actuarial liability increased by approximately $474 million in 2009, from $8,901 million in 2009 to $9,375 million in 2010. The assets currently fund 39.7% of this liability, a decrease from the 43.7% funded ratio in 2009. The decrease in the funded ratio resulted largely from the collapse in U.S. and global financial markets in 2008. As the Fund uses a five-year actuarial smoothing method in valuing its assets to determine its funded status, investment losses experienced in 2008 will be reflected in the actuarial value of assets over a five-year period, concluding in 2012.

The Board of Trustees is very concerned with the funded level of actuarial liabilities. The unfunded accrued actuarial liability for pension benefits and for the health insurance supplement increased from 2009 to 2010. Additionally, the annual required contribution for these benefits, as computed under GASB 25 and 43, was not reached in 2010 or 2009. However, the Board has taken steps to ensure a sufficient level of liquidity within the portfolio to fund monthly benefits, while pursuing its long-term goal of maximum investment performance.

On December 30, 2010, Governor Pat Quinn signed into law, SB 3538, as part of Public Act 096-1495. This new legislation included provisions which will significantly change the method by which contributions to the Fund by the Employer are determined, as well as the level of benefits afforded police officers hired by the City of Chicago after January 1, 2011.

Police officers hired after January 1, 2011, will be subject to different provisions in their defined benefit pension plan provisions. The changes are similar to other revisions made to various state and local pension systems in Illinois, including a change in the minimum retirement age for a non-reduced benefit, changes in the method of determining final average salary, changes in the calculation of the annual cost of living increase for retirees, changes in survivor benefits, and a salary cap on compensation included in the calculation of pension benefits.

The formula by which the Employer, the City of Chicago, will fund members' pension benefits was significantly changed, effective with the City of Chicago tax levy beginning in 2015. Previously, the City of Chicago met its fiduciary obligation for funding through a tax multiplier calculation which was based upon active member contributions. Public Act 096-1495 changes that funding obligation such that annually actuarially-determined employer contributions will be calculated and required. Such actuarially-determined contributions will be established with a funding goal of 90% by the end of 2040, based upon the market value of Fund assets and application of certain required actuarial assumptions and methodologies. The Public Act also provides an enhancement mechanism such that failure by the City of Chicago to remit the required contributions can result in withholding of certain grants owed by the State of Illinois Comptroller to the City of Chicago, and direct deposit of such monies to the Fund.

Contact Information

This financial report is designed to provide the employer, plan participants, and others with a general overview of the Fund's finances and to show accountability for the monies received. Questions concerning any data provided in this report can be submitted to:

Mr. John J. Gallagher, Jr.
Executive Director
Policemen's Annuity and Benefit
Fund of Chicago
221 N. LaSalle
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POLICEMEN'S ANNUITY AND BENEFIT FUND OF CHICAGO
(A Component Unit of the City of Chicago)
Statements of Plan Net Assets
As of December 31, 2010 and 2009

	2010	2009
ASSETS		
Cash	$ 250	$ 250
Receivables		
Employer tax levies, net of allowance for loss of $18,417,241 in 2010 and $17,476,339 in 2009	199,875,680	191,450,555
Member contributions	4,624,607	4,511,386
Interest and dividends	8,381,341	8,933,655
Accounts receivable—due from brokers	276,373,195	121,339,956
	489,254,823	326,235,552
Investments at fair value		
U.S. common stock and other equity	1,041,332,798	1,134,330,611
Collective investment funds, stock	285,809,608	243,475,859
Collective investment funds, fixed income	260,847,982	219,399,032
International equity	667,432,501	547,973,699
Bonds and notes	557,575,568	472,823,948
Short-term instruments	91,970,139	112,012,093
Infrastructure	38,165,359	31,501,982
Forward contracts and swaps	4,728,596	8,105,495
Hedge fund-of-funds	81,704,551	104,425,380
Real estate	94,421,845	90,428,931
Venture capital and private equity	177,116,975	185,516,853
	3,301,105,922	3,149,993,883
Invested securities lending cash collateral	295,714,545	375,111,985
Total Assets	4,086,075,540	3,851,341,670
LIABILITIES		
Refunds and accounts payable	5,676,240	4,550,594
Trade accounts payable—due to brokers	344,185,437	144,123,721
Securities lending cash collateral	295,714,545	376,098,401
OPEB obligation	830,621	518,200
Total Liabilities	646,406,843	525,290,916
Net assets held in trust for pension benefits	$ 3,439,668,697	$ 3,326,050,754

The accompanying notes are an integral part of these financial statements.

POLICEMEN'S ANNUITY AND BENEFIT FUND OF CHICAGO
(A Component Unit of the City of Chicago)
Statements of Changes in Plan Net Assets
For the Years Ended December 31, 2010 with and 2009

	2010	2009
ADDITIONS		
Contributions		
Employer	$ 183,834,639	$ 180,510,851
Plan member salary deductions	108,402,353	95,614,390
Total contributions	292,236,992	276,125,241
Investment income		
Net appreciation in fair value of investments	316,282,278	512,929,419
Interest	27,113,326	30,186,909
Dividends	29,784,972	30,177,953
Real estate income	5,300,838	2,561,835
	378,481,414	575,856,116
Investment activity expenses		
Investment management fees	(9,109,616)	(8,987,507)
Custodial fees	(183,525)	(197,804)
Investment consulting fees	(542,554)	(616,179)
Total investment activity expenses	(9,835,695)	(9,801,490)
Net income from investing activities	368,645,719	566,054,626
From securities lending activities		
Net depreciation in fair value of investments	-	(986,416)
Securities lending income	1,132,624	1,513,641
Borrower rebates	10,242	1,145,050
Bank fees	(230,530)	(412,078)
Net income from securities lending activities	912,336	1,260,197
Total net investment income	369,558,055	567,314,823
Miscellaneous income	20,031	799,364
Total additions	661,815,078	844,239,428
DEDUCTIONS		
Pension and disability benefits	534,462,320	506,853,184
Death benefits	1,782,400	1,662,800
Refunds of employee deductions	7,587,436	6,193,872
	543,832,156	514,709,856
Administrative expenses	3,924,928	4,303,599
OPEB expense	440,051	173,600
Total deductions	548,197,135	519,187,055
Net increase	113,617,943	325,052,373
Net assets held in trust for pension benefits:		
Beginning of year	3,326,050,754	3,000,998,381
End of year	$ 3,439,668,697	$ 3,326,050,754

The accompanying notes are an integral part of these financial statements.

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Reporting Entity

Accounting principles generally accepted in the United States as established by the Governmental Accounting Standards Board (GASB) define a financial reporting entity as consisting of the primary government and its component units, for which the primary government is financially accountable. Financial accountability includes appointing a voting majority of a component unit's governing board, the ability of the primary government to impose its will on the component unit, or a potential for the component unit to provide specific financial benefits to or impose specific financial burdens on the primary government. A primary government may also be financially accountable for its component units.

Based on the above criteria, the Policemen's Annuity and Benefit Fund of Chicago (the Fund, or PABF) is considered to be a component unit of the City of Chicago (the City). The Fund is part of the City's financial reporting entity and is included in the City's fiduciary statement of net assets as pension trust funds.

Basis of Accounting

The Fund's financial statements are prepared on the accrual basis of accounting. Employee and employer contributions are recognized as additions in the period in which employee services are performed. Benefits and refunds are recognized as deductions when payable. Expenses are recorded when the corresponding liabilities are incurred, regardless of when payment is made.

Use of Estimates

The preparation of financial statements in accordance with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Accordingly, actual results may differ from those estimates.

Investments

The Fund is authorized to invest in bonds, notes, and other direct obligations of the U.S. Government and U.S. Government agencies; corporate bonds, debentures, and notes; certain notes secured by mortgages, including pass-through securities; common and preferred stocks; certain pooled funds; limited partnerships and other types of investment vehicles as set forth in the Illinois Compiled Statutes.

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(continued)*

Method Used to Value Investments

Investments are reported at fair value. Short-term investments are reported at cost, which approximates fair value. Securities traded on a national or international exchange are valued at the last reported sales price at current exchange rates. Fixed-income securities are valued principally using quoted market prices provided by independent pricing services. For collective investments, net asset value is determined and certified by the investment managers as of the reporting date. Real estate investments are valued at estimated fair value as determined by the general partner, based upon appraisals provided by the investment manager. Hedge fund, venture capital, infrastructure, and certain opportunistic investments are reported at estimated fair value as determined by the general partner of the investment vehicle.

Furniture and Office Equipment

Furniture and office equipment are not capitalized as they are immaterial and are charged to expenses in the year of purchase.

Administrative Expenses

Administrative expenses are recorded as incurred and are budgeted and approved by the Fund's Board of Trustees. Administrative expenses are funded by the employer contributions.

Income Taxes

Income earned by the Fund is not subject to federal income tax.

Securities Lending Transactions

Cash received as collateral on securities lending transactions and investments made with that cash are reported as assets in the statements of plan net assets at fair value. Securities received as collateral are reported as assets only if the Fund has the ability to pledge or sell them without a borrower default. Liabilities resulting from these transactions are reported in the statements of plan net assets.

NOTE 2 PENSION PLAN

Plan Description and Contribution Information

The Policemen's Annuity and Benefit Fund of Chicago is the administrator of a defined benefit, single-employer pension plan with a defined contribution minimum for the purpose of providing benefits to the police officers of the City of Chicago, their widows, and their children. Any employee of the City employed under the provisions of the municipal personnel ordinance as police service is covered by the Fund. The defined benefits as well as the employer and employee contribution levels are mandated in Illinois Compiled Statutes (40 ILCS Act 5, Article 5) and may be amended only by the Illinois State Legislature. The Fund is governed by an eight-member Board of Trustees (four appointed by the City, three elected by the policemen, and one elected by the annuitants), whose duties are to administer the Fund under the Illinois Pension Code.

The City of Chicago payrolls for employees covered by the Fund for the years ended December 31, 2010 and 2009 were $1,048,084,301 and $1,011,205,359, respectively. At December 31, 2010 and 2009, the Fund membership consisted of the following:

	2010	**2009**
Active employees	12,737	13,154
Retirees and beneficiaries currently receiving benefits	12,380	12,154
Terminated employees entitled to benefits or a refund of contributions but not yet receiving them	620	634
	25,737	25,942

The Fund provides retirement benefits as well as death and disability benefits. Employees age 50 or older with at least 10 years of service are entitled to receive a money purchase annuity and partial City contributions if less than 20 years of service have been completed. Effective 2003, the mandatory retirement age for a participant is 63. Employees age 50 or older with at least 20 years of service are entitled to receive a minimum formula annuity of 2.5% per year for the first 20 years of service, plus 2.5% per year for each following year or fraction thereof times the final average salary (highest average annual salary for any four consecutive years within the last ten years of service immediately preceding the date of retirement). The annuity shall not exceed 75% of the highest average annual salary.

NOTE 2 PENSION PLAN *(continued)*

The monthly annuity increases by 3% of the original annuity at the first of the month following the later of the attainment of age 55 or the first anniversary of retirement, and by 3% on each January 1 thereafter, if the recipient was born before January 1, 1955.

If the recipient was born after January 1, 1955, the monthly annuity increases by 1.5% of the original annuity at the first of the month following the later of the attainment of age 60 or the first anniversary of retirement, and 1.5% on each January 1 thereafter, but will not exceed a total of 30%.

Covered employees are required to contribute 9.0% of their salary to the Fund. If an employee leaves covered employment without qualifying for an annuity, accumulated contributions are refunded with interest. The City is required by state statutes to contribute the remaining amounts necessary to finance the requirements of the Fund. It is required to levy a tax at a rate not more than an amount equal to the total amount of contributions by the employees to the Fund made in the calendar year two years prior to the year for which the annual applicable tax is levied, multiplied by 2.00 annually.

The total annual actuarial required contribution to the Fund (financed by the employees and the City) is equal to the normal cost plus interest only on the unfunded actuarial accrued liabilities determined using the entry age normal method. This actuarial cost method amortizes the costs of the participants' benefits over the entire career of each member as a level of percentage of compensation. The employer contribution required for interest only on the unfunded actuarial accrued liabilities results in a decreasing annual employer cost expressed as a percentage of payroll as future payrolls increase. Since the tax levy is expressed as a multiple of the total salary deductions made two years prior, the City is effectively contributing a level annual percentage of payrolls.

Funded Status and Funding Progress

The funded status of the Fund as of December 31, 2010 and 2009, the most recent actuarial valuation dates, is as follows:

NOTE 2 PENSION PLAN *(continued)*

Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) Entry Age (b)	Unfunded AAL (UAAL) (b-a)	Funded Ratio (a/b)	Covered Payroll (c)	UAAL as a Percentage of Covered Payroll ((b-a)/c)
12/31/10	$ 3,718,954,539	$ 9,210,056,428	$ 5,491,101,889	40.38%	$ 1,048,084,301	523.92%
12/31/09	3,884,978,241	8,736,101,666	4,851,123,425	44.47	1,011,205,359	479.74

The schedule of funding progress, presented as required supplementary information (RSI) following the notes to the financial statements, present multiyear trend information regarding the actuarial values of Fund assets and the ratio to the AAL for benefits.

Additional information as of the latest actuarial valuation follows:

Valuation date	12/31/2010 and 2009
Actuarial cost method	Entry age
Amortization method	Level percent open
Remaining amortization period	30 years
Asset valuation method	5-year smoothed market
Actuarial assumptions:	
Investment rate of return	8.0%
Projected salary increases	4.0% per year, plus additional percentage related to service
Cost of living allowance	3.0% (1.50% for retirees born after January 1, 1955)
General inflation rate	3.0%

NOTE 3 HEALTH INSURANCE SUPPLEMENT

Plan Description and Contribution Information

The City offers group health benefits to annuitants and their eligible dependents through the City's health care plans.

NOTE 3 HEALTH INSURANCE SUPPLEMENT *(continued)*

Premiums are established by the City, with the City paying 50% of the claims or premiums, whichever are applicable, with the remaining amount to be paid by all annuitants participating in the City's health care plans. Currently, the Fund pays to the City on behalf of each of the annuitants who chooses to participate in any of the City's health care plans, up to a maximum of $85 per month from July 1, 2003 through June 30, 2008, and $95 per month from July 1, 2009 through June 30, 2013 for each annuitant who is not qualified to receive Medicare benefits; and up to a maximum of $55 per month from July 1, 2003 through June 30, 2008, and $65 per month from July 1, 2009 through June 30, 2013 for each annuitant who is qualified to receive Medicare benefits. Health care benefits provided through this supplement are not dependent upon inflation, as the benefits paid are a fixed dollar amount.

The health insurance supplement is financed with current contributions on a pay-as-you-go basis. There is no separate healthcare account or assets to pay the health insurance supplement.

At December 31, 2010 and 2009, the number of annuitants or surviving spouses who had subsidized health insurance totaled 10,118 and 10,048, respectively. Of the 2,261 remaining annuitants or surviving spouses, substantially all were eligible for subsidized health insurance, subject to their election of such benefits at a future date, and successful completion of the City's enrollment procedures, which includes certificate of insurability or an annual exam. Additionally, of the 620 terminated employees entitled to benefits or a refund, approximately 178 of these terminated employees would be eligible for subsidized health insurance, subject to their election of such benefits at a future date and successful completion of the City's enrollment procedures. The annual required contribution represents a level of funding that, if paid on an ongoing basis, is projected to cover normal costs each year and amortize any unfunded actuarial liabilities over a period not to exceed 30 years. The estimated City contribution represents the expected benefit payments for the health insurance supplement. In 2010 and 2009, the Fund received contributions of $9,354,163 and $9,266,431 from the City, and remitted contributions of insurance premiums to the City of $9,354,163 and $9,266,431, respectively. Contributions to the health insurance supplement are equal to insurance premium payments to the City. There were no net assets to report for the health insurance supplement at December 31, 2010 or 2009.

NOTE 3 HEALTH INSURANCE SUPPLEMENT *(continued)*

Funded Status and Funding Progress

The funded status of Fund's health care plans as offered by the City as of December 31, 2010 and 2009, the most recent actuarial valuation dates, is as follows:

Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) Entry Age (b)	Unfunded AAL (UAAL) (b-a)	Funded Ratio (a/b)	Covered Payroll (c)	UAAL as a Percentage of Covered Payroll ((b-a)/c)
12/31/10	$ -	$ 164,796,449	$ 164,796,449	0.00%	$ 1,048,084,301	15.72%
12/31/09	-	164,799,819	164,799,819	0.00	1,011,205,359	16.30

The schedule of funding progress, presented as required supplementary information (RSI) following the notes to the financial statements, present multiyear trend information regarding the actuarial values of Fund assets and the ratios to the AALs for benefits.

Additional information as of the latest actuarial valuation follows:

Valuation dates	12/31/2010 and 12/31/2009
Actuarial cost method	Entry age normal
Amortization method	Level percent open
Remaining amortization period	30 years
Asset valuation method	No assets (Pay-as-you-go)
Actuarial assumptions:	
OPEB investment rate of return	4.5%
Projected salary increases	4.0% per year, plus additional percentage related to service
Health cost trend rate	0.0% (fixed dollar subsidy)

NOTE 4 CASH AND INVESTMENT RISK

Cash

The bank balance and carrying amount of the Fund's deposits at December 31, 2010 were $680,800 and ($3,663), respectively; and $804,310 and ($917,989) at December 31, 2009, respectively. These balances exclude $250 of petty cash. The bank balance at December 31, 2010 and 2009 is on deposit with the City Treasurer and is insured or collateralized by securities held by the City Treasurer in the Fund's name.

Investment Policy

The Fund's overall investment policy is based on the following principles established by the Trustees:

- Maintain a long-term investment horizon for the Fund
- Emphasize equity investments to enhance long-term return
- Diversify investments across several asset classes

The Board has indicated interest in developing a risk policy statement in parallel to the Fund's investment policy. The policy would highlight those risks managed at the Fund level and those managed by external managers. The risk policy would also state the types of risks that are monitored and how they are measured. Until such policy is developed by PABF staff and adopted by the Board, there is no formal policy relating to specific investment-related risk.

In order to minimize the impact of large losses and reduce annual variability of returns, the Fund's assets are allocated across several different asset classes and diversified broadly within each asset class.

NOTE 4 CASH AND INVESTMENT RISK *(continued)*

Investment Summary

The following table presents a summary of the Fund's investments by type at December 31, 2010 and 2009.

	2010	2009
U.S. Government and agency fixed income	$ 280,131,869	$ 214,424,267
U.S. corporate fixed income	277,443,699	258,399,681
U.S. common collective fixed income funds	260,847,982	219,399,032
U.S. equities	1,041,332,798	1,134,330,611
U.S. common collective stock funds	285,809,608	243,475,859
Foreign equities	667,432,501	547,973,699
Pooled short-term investment funds	39,528,450	50,909,140
Infrastructure	38,165,359	31,501,982
Real estate	94,421,845	90,428,931
Venture capital	177,116,975	185,516,853
Forward contracts and swaps	4,728,596	8,105,495
Hedge fund-of-funds	81,704,551	104,425,380
Cash and cash equivalents	52,441,689	61,102,953
Total investments at fair value	$ 3,301,105,922	$ 3,149,993,883

There are no individual investments held by the Fund that represent 5% or more of net assets held in trust for pension benefits, except for the Fund's investment in the Northern Trust Collective Daily U.S. Market Cap Equity Index Fund, which amounted to $285,809,608 and $243,475,859 at December 31, 2010 and 2009, respectively.

Investment Risks

The Fund's investments are subject to certain types of risks, including interest rate risk, credit risk, custodial credit risk, and foreign currency risk. Due to the level of risk associated with certain investment securities, it is at least reasonably possible that changes in the value of investment securities will occur in the near term and that such changes could materially affect the amounts reported in the statements of plan net assets.

NOTE 4 CASH AND INVESTMENT RISK *(continued)*

Interest Rate Risk—Interest rate risk is the risk that the fair value of debt securities decreases due to increases in the prevailing market interest rate. Generally, the longer the maturity of an investment, the greater the sensitivity of its fair value to changes in market interest rates. The Fund manages its exposure to fair value loss arising from increasing interest rates in several ways. All fixed-income investments are managed by external investment managers. The Fund employed six such managers in 2010 and 2009. Each investment manager is required to determine the maturities of all fixed-income securities in their portfolio. Additionally, guidelines are provided to the external investment managers, given the level of risk within the investment manager's portfolio. These guidelines include a target duration range that is consistent with each investment manager's respective strategy.

The following tables show the segmented time distribution of the Fund's investments into time periods of maturities based on the investments' cash flows.

At December 31, 2010, the Fund had the following investments and maturities related to certain fixed-income securities (bonds and notes):

		Investment Maturities			
Investment Type	**Fair Value**	**Less than 1 Year**	**1 to 6 Years**	**7 to 10 Years**	**More than 10 Years**
Asset backed securities	$ 32,578,424	$ 65,804	$ 19,264,484	$ 5,111,930	$ 8,136,206
Commercial mortgage backed securities	37,206,916	774,204	-	221,211	36,211,501
Corporate bonds	191,479,418	6,572,238	72,928,834	64,234,070	47,744,276
Government agency securities	7,891,724	352,300	6,610,419	929,005	-
Government bonds	85,696,817	1,507,597	49,840,074	9,199,568	25,149,578
Government mortgage backed securities	178,085,262	-	1,236,546	11,050,140	165,798,576
Government issued commercial mortgage backed securities	1,736,490	-	-	1,736,490	-
Guaranteed fixed income	795,621	-	795,621	-	-
Index linked government funds	6,721,576	-	1,812,517	4,909,059	-
Municipal principal bonds	5,211,889	-	-	720,789	4,491,100
Non-government backed collateralized mortgage obligations	10,171,431	-	223,823	2,805,996	7,141,612
	$ 557,575,568	$ 9,272,143	$ 152,712,318	$ 100,918,258	$ 294,672,849

NOTE 4 CASH AND INVESTMENT RISK *(continued)*

At December 31, 2009, the Fund had the following investments and maturities related to certain fixed-income securities (bonds and notes):

		Investment Maturities			
Investment Type	**Fair Value**	**Less than 1 Year**	**1 to 6 Years**	**7 to 10 Years**	**More than 10 Years**
Asset backed securities	$ 22,602,827	$ -	$ 12,213,394	$ 3,942,795	$ 6,446,638
Commercial mortgage backed securities	44,894,255	-	661,503	622,956	43,609,796
Corporate bonds	181,709,894	4,013,217	62,205,179	68,199,262	47,292,236
Government agency securities	7,872,709	422,000	6,826,078	624,631	-
Government bonds	57,082,993	764,531	10,745,531	20,486,218	25,086,713
Government mortgage backed securities	135,226,796	-	-	15,176,107	120,050,689
Government issued commercial mortgage backed securities	2,122,677	-	-	2,122,677	-
Guaranteed fixed income	777,053	-	777,053	-	-
Index linked government funds	6,739,265	-	3,073,584	3,665,681	-
Municipal principal bonds	5,379,827	-	2,471,827	487,558	2,420,442
Non-government backed collateralized mortgage obligations	8,415,652	-	259,444	2,277,706	5,878,502
	$ 472,823,948	$ 5,199,748	$ 99,233,593	$ 117,605,591	$ 250,785,016

Credit Risk—Credit risk is the risk that the issuer or other counterparty to an investment will not fulfill its obligations. One measure of credit risk is the quality ratings issued by national ratings agencies such as Moody's Investors Services and Standard & Poor's Financial Services (S&P). The Fund's investment policy establishes guidelines for diversification and credit quality of investment portfolios for each investment manager. Suggested levels of credit quality ratings less than investment grade are provided to the external investment managers.

NOTE 4 CASH AND INVESTMENT RISK *(continued)*

The following table provides information on the credit ratings associated with the Fund's investments in debt securities. Rates were obtained from S&P:

	Fair Value	
	2010	**2009**
Quality Rating:		
AAA	$ 56,463,793	$ 55,095,266
AA	14,360,688	16,198,738
A	69,473,070	67,074,877
BBB	96,777,172	87,518,343
BB	8,903,126	6,381,400
B	2,417,108	2,534,624
Not rated	23,956,102	19,863,946
CCC through D	5,092,640	3,732,487
Total credit risk of U.S. corporate fixed income	277,443,699	258,399,681
U.S. Government and agency fixed income securities	280,131,869	214,424,267
	$ 557,575,568	$ 472,823,948

Custodial Credit Rate Risk: Custodial credit risk applies to investments, cash and certificates of deposit. For an investment, custodial credit risk is the risk that, in the event of the failure of the counterparty, the Fund will not be able to recover the value of its investments or collateral securities that are in the possession of an outside party. For cash and certificates of deposit, custodial credit risk is the risk that in the event of a bank failure, the Fund's deposits may not be returned. As of December 31, 2010 and 2009 deposits of $4,244,367 and $1,236,478, respectively, were exposed to custodial credit risk as uninsured and uncollateralized. The Fund does not have a formal policy regarding custodial credit risk.

Foreign Currency Risk: Foreign currency risk is the risk that changes in exchange rates will adversely affect the fair value of an investment.

NOTE 4 CASH AND INVESTMENT RISK *(continued)*

The Fund does not have a formal investment policy governing foreign currency risk, but does manage its exposure to loss in the fair value of investments by requiring managers of foreign investments to maintain diversified portfolios. The Fund's equity and fixed-income portfolios include investments that are subject to foreign currency risk. Such investments include non-U.S. equities, government bonds, corporate bonds, and derivative instruments. The fund's exposure to foreign currency risk is as follows:

	Fair Value	
	2010	**2009**
Currency		
Australian Dollar	$ 9,385,547	$ 14,334,054
Brazilian Real	8,985,936	9,363,148
British Pound Sterling	96,477,892	84,107,739
Canadian Dollar	22,440,604	15,818,307
Czech Koruna	324	243,455
Danish Krone	7,511,992	4,130,053
Egyptian Pound	-	274,658
Euro Currency Unit	117,606,602	133,425,125
Hong Kong Dollar	51,072,671	36,604,250
Hungarian Forint	201	221
Indian Rupee	5,614,096	8,485,379
Indonesian Rupiah	4,201,582	3,096,460
Japanese Yen	85,348,057	60,586,454
Malaysian Ringgit	4,387,940	1,187,530
Mexican Peso	2,173,325	5,072,079
New Israeli Shekel	2,470,998	1,900,758
New Taiwan Dollar	-	10,502,828
Norwegian Krone	3,036,361	4,337,136
Polish Zloty	2,768,388	380,222
Singapore Dollar	10,042,919	11,717,775
South African Rand	4,818,026	5,121,557
South Korean Won	15,422,037	6,566,762
Swedish Krona	13,187,507	7,873,577
Swiss Franc	42,507,285	43,671,940
Taiwan Dollar	9,908,375	-
Thai Baht	2,653,278	664,631
Turkish Lira	1,898,448	1,061,630
Total investments in foreign currency	$ 523,920,391	$ 470,527,728

NOTE 4 CASH AND INVESTMENT RISK *(continued)*

Derivatives

The Fund's investment managers may enter into derivative transactions as permitted by their guidelines. A derivative financial instrument is an investment whose payoff depends on the value of an underlying instrument such as bond or stock prices, a market index, or commodity prices. Derivative financial instruments involve, to varying degrees, credit risk and market risk. Credit risk is the possibility that a loss may occur because a party to a transaction fails to perform according to terms. Market risk is the possibility that a change in the underlying element of the derivative will cause the value of a financial instrument to decrease or become more costly to settle. Most of the derivative transactions executed by the Fund's investment managers are related to currency through foreign exchange contracts, the vast majority of which is for hedging purposes, and interest rates through interest rate futures and forward contracts, the purpose of which is mostly duration management. In addition to derivative transactions executed directly by the Fund's investment managers, the Fund holds interests in collective funds, hedge funds, and private equity funds, which may engage in derivative transactions. The Fund does not directly purchase derivatives with borrowed funds.

Futures Contracts: The Fund's external investment managers enter into futures contracts in the normal course of investing activities to manage market risk associated with the Fund's fixed-income investments and to achieve overall investment portfolio objectives. These contracts involve elements of market risk in excess of amounts recognized in the statements of plan net assets. The credit risk associated with these contracts is minimal, as they are traded on organized exchanges and settled daily.

At December 31, 2010, the Fund had interest rate futures contracts to purchase United Kingdom Treasury bonds, LIBOR/Euro dollars, and U.S. Treasury securities with notional amounts of $6,360,703, $20,915,475 and $26,700,094, respectively. The Fund also had interest rate futures contracts to (sell) German Treasury bonds, LIBOR/Euro dollars, and U.S. Treasury securities with notional amounts of ($9,862,244), ($44,304,938) and ($60,466,462), respectively. At December 31, 2009, the Fund had interest rates futures contracts to purchase (sell) Australian Treasury bonds, LIBOR/Euro dollars and United Kingdom Treasury bonds with notional amounts of $9,859,187, ($45,425,321), and (9,144,441), respectively. Additionally, the Fund had interest rate futures contracts to purchase (sell) U.S. Treasury securities with notional amounts of $5,408,862 and ($5,307,200), respectively. Notional amounts do not quantify risk or represent assets or liabilities of the Fund, but are used in the calculation of cash settlements under the contracts.

NOTE 4 CASH AND INVESTMENT RISK *(continued)*

The fair value of futures contracts in the statements of plan net assets was zero at December 31, 2010 and 2009, as settlements are by cash daily. The Fund realized (losses) of ($979,018) on futures contracts in 2010. These losses are accounted for as net appreciation (depreciation) in fair value of investments.

Interest Rate and Credit Default Swaps: The Fund's external investment managers utilize interest rate and credit default swaps in the management of the Fund's fixed-income portfolio. Swap agreements are contractual agreements between two or more parties in which each party agrees to exchange sets of cash flows based on certain agreed-upon parameters. The holder is exposed to credit risk for nonperformance and to market risk for changes in interest rates. Gains and losses on swaps are determined based on fair values and are recorded in the statements of changes in plan net assets. The fair value of swaps outstanding at December 31, 2010 and 2009 was a net unrealized loss of ($40,300) and ($2,534,915), respectively.

Foreign Exchange Contracts: The Fund's external investment managers utilize foreign currency forward contracts, primarily for hedging purposes. Foreign currency forward contracts are contractual agreements to buy or sell a specific amount of a foreign currency at a certain date for an agreed price. As the fair value of the underlying foreign currency varies from the contractual agreed price, the Fund records an unrealized gain or loss. The holder is exposed to credit risk for nonperformance and to market risk for changes in interest rates. The Fund had pending foreign currency purchases and sales of Australian dollars, Brazilian real, British pound sterling, Canadian dollars, Euros, Hong Kong dollars, Japanese yen, Mexican pesos, New Israeli shekel, Norwegian krone, Polish zloty, South African rand, Swedish krona, Swiss francs, Thai baht and U.S. dollars at December 31, 2010. Total pending foreign purchases and (sales) were $112,794,150 and ($113,138,764), respectively, at December 31, 2010. Thus the Fund had a net unrealized (loss) on pending foreign currency forward contracts of ($344,615) at December 31, 2010. At December 31, 2009, total pending foreign purchases and (sales) were $88,139,635 and ($87,629,245), respectively. The Fund had a net unrealized (loss) on pending foreign currency forward contracts of ($510,390) at December 31, 2009.

Forward Interest Rate Contracts: The Fund's external investment managers entered into forward contracts to purchase U.S. Treasury strips during 2010 and 2009. Forward contracts are contracts for delayed delivery of securities in which the seller agrees to make delivery at a specified future date of a specified instrument, at a specified price or yield. The holder is exposed to credit risk for nonperformance and to market risk for changes in interest rates.

NOTE 4 CASH AND INVESTMENT RISK *(continued)*

These instruments involve, to varying degrees, elements of credit risk in excess of the amount recognized in the statements of plan net assets. The Fund's external investment managers attempt to mitigate this credit risk through structured trading with reputable parties.

The fair value of the forward contracts was $4,132,105 and $7,098,810 as of December 31, 2010 and 2009, respectively. The unrealized (loss) on the contracts was ($205,932) and ($516,467) at December 31, 2010 and 2009, respectively. Sales of the forward contracts generated realized gains of $1,329,440 during 2010. These earnings are included in net appreciation in the fair value of investments in the statements of changes in net assets.

NOTE 5 SECURITIES LENDING PROGRAM

State statutes and Board of Trustees policies permit the Fund to lend its securities to broker-dealers and other entities with a simultaneous agreement to return the collateral for the same securities in the future. The Fund's master custodian, Northern Trust Bank, lends securities of the type on loan at year-end for collateral in the form of cash, irrevocable letters of credit, or other securities to a minimum of 102% for U.S. securities and 105% for non-U.S. securities. The contract with the Fund's master custodian requires it to indemnify the Fund if the borrowers fail to return the securities (and if the collateral is inadequate to replace the securities lent) or fail to pay the Fund for income distributions by the securities' issuers while the securities are on loan.

All securities loans can be terminated on demand by either the Fund or the borrower, although the average term of the loans is 101 days and 81 days, as of December 31, 2010 and 2009, respectively. Cash collateral is invested in the lending agent's Core USA Collateral Pool, which at December 31, 2010 and 2009, had a weighted-average life, as measured by interest sensitivity, of 25 days and 41 days, respectively. The relationship between the maturities of the investment pool and the Fund's loans is affected by the maturities of the securities loans made by other entities that use the agent's pool, which the Fund cannot determine. The Fund cannot pledge or sell collateral securities received unless the borrower defaults.

NOTE 5 SECURITIES LENDING PROGRAM *(continued)*

Loans outstanding as of December 31, 2010 and 2009 were as follows:

	2010	2009
Market value of securities loaned	$ 289,657,158	$ 363,732,687
Market value of cash collateral from Borrowers	295,714,545	375,111,985
Market value of non-cash collateral from borrowers	1,581,537	731,857

As of December 31, 2010 and 2009, the Fund had limited credit risk exposure to borrowers because the amounts owed to the borrowers exceeded the amounts owed to the Fund.

There was an unrealized loss of $986,416 recorded in the financial statements as of December 31, 2009, calculated based on the difference between book value of cash collateral due to borrowers under the securities lending program and the fair value of invested cash collateral under the securities lending program.

NOTE 6 UNFUNDED INVESTMENT COMMITMENTS

The Fund had unfunded commitments of approximately $169 million and $223 million at December 31, 2010 and 2009, respectively, in connection with real estate, infrastructure, and private equity investments.

NOTE 7 POST-RETIREMENT BENEFITS OF THE FUND—STAFF RETIREE HEALTH PLAN

(a) Plan Description

The Policemen's Annuity and Benefit Fund of Chicago (PABF), as an employer, administers a single-employer defined benefit post-retirement healthcare plan (Staff Retiree Health Plan). The Staff Retiree Health Plan provides lifetime health and dental insurance for eligible retirees and their spouses through PABF's group health insurance plan, which covers both active and retired members. As of December 31, 2010 and 2009, seven retirees were in the Staff Retiree Health Plan and 21 and 20 active employees, respectively, could be eligible at retirement. Benefit subsidy provisions have been established by PABF's Board of Trustees. The amount of the subsidy varies according to a retiree's years of service with PABF and the coverages elected. These benefit subsidy provisions can be modified or terminated at the sole discretion of the PABF Board.

NOTE 7 POST-RETIREMENT BENEFITS OF THE FUND—STAFF RETIREE HEALTH PLAN *(continued)*

Funding Policy

The required contribution is based on projected pay-as-you-go financing requirements. For 2010 and 2009, PABF contributed approximately $120,990 and $101,400, respectively, to the Staff Retiree Health Plan for current premiums, with an implicit subsidy of $6,640 and $19,600, for 2010 and 2009, respectively. Members receiving benefits contributed approximately $23,000, or 19% of the total premiums, for 2010, and approximately $25,000, or 20% of the total premiums, for 2009.

Annual OPEB Cost and Net OPEB Obligation

PABF's annual other post-employment benefit (OPEB) expense is calculated based on the annual required contribution of the employer (ARC), an amount actuarially determined in accordance with the parameters of GASB Statement 45. The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover normal costs each year and amortize any unfunded actuarial liabilities over a period not to exceed 30 years. The amortization period is open. The following table shows the components of PABF's annual OPEB cost for 2010 and 2009, the amount actually contributed to the Staff Retiree Health Plan, and changes in PABF's net OPEB obligation to the Staff Retiree Health Plan:

	2010	2009
Annual required contribution	$ 434,005	$ 290,600
Interest on net OPEB obligation	23,319	15,500
Adjustment to annual required contribution	(17,273)	(11,500)
Annual OPEB expense	440,051	294,600
Employer contributions made	127,630	121,000
Increase in net OPEB obligation	312,421	173,600
Net OPEB obligation at beginning of year	518,200	344,600
Net OPEB obligation at end of year	$ 830,621	$ 518,200

NOTE 7 POST-RETIREMENT BENEFITS OF THE FUND—STAFF RETIREE HEALTH PLAN *(continued)*

The annual OPEB cost, the percentage of annual OPEB cost contributed to the Staff Retiree Health Plan, and the net OPEB obligation for 2010 and 2009 is as follows:

Year Ended	Annual OPEB Cost	Percentage of Annual OPEB Cost Contributed	Net OPEB Obligation
12/31/2010	$ 440,051	29.0%	$ 830,621
12/31/2009	294,600	41.1	518,200

Funded Status and Funding Progress

The funded status of PABF's Staff Retiree Health Plan as of December 31, 2010, and 2009, is as follows:

Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) Entry Age (b)	Unfunded AAL (UAAL) (b-a)	Funded Ratio (a/b)	Covered Payroll (c)	UAAL as a Percentage of Covered Payroll ((b-a)/c)
12/31/10	$ -	$ 5,588,688	$ 5,588,688	0.00%	$ 1,486,848	375.9%
12/31/09	-	3,474,800	3,474,800	0.00	1,256,800	276.5

Actuarial valuations of an ongoing plan involve estimates of the value of reported amounts and assumptions about the probability of occurrence of events far into the future. Examples include assumptions about future employment, mortality, and the healthcare cost trend. Amounts determined regarding the funded status of the Staff Retiree Health Plan and the annual required contributions of the employer are subject to continual revision as actual results are compared with past expectations and new estimates are made about the future. The schedule of funding progress, presented as required supplementary information (RSI) following the notes to the financial statements, present multiyear trend information on the actuarial values of assets of the Staff Retiree Health Plan and its ratio to the AAL for benefits.

Actuarial Methods and Assumptions

Projections of benefits for financial reporting purposes are based on the substantive plan (the plan as understood by the employer and the plan members) and include the types of benefits provided at the time of each valuation and the historical pattern of sharing of benefit costs between the employer and members to that point. The actuarial methods and assumptions used include techniques that are designed to reduce the effects of short-term volatility in actuarial accrued liabilities consistent with the long-term perspective of the calculations.

NOTE 7 POST-RETIREMENT BENEFITS OF THE FUND—STAFF RETIREE HEALTH PLAN *(continued)*

For the December 31, 2010 and 2009 actuarial valuations the entry age actuarial cost method was used. The actuarial assumptions included a 4.5% investment rate of return based on the employer's assumed return on its assets and at December 31, 2010, an annual healthcare cost trend rate of 8.5% initially, reduced by increments of 0.5 percentage point per year to an ultimate rate of 5.0% after eight years. At December 31, 2009, the annual healthcare cost trend rate is assumed at 9.0% initially, reduced by increments of 1.0 percentage point per year to an ultimate trend rate of 5.0% after four years. At December 31, 2010 and 2009, the wage inflation assumption was 4.5%. The unfunded actuarial accrued liability is being amortized as a level percentage of projected payroll over a period of 30 years.

NOTE 8 RESERVES

The Fund maintains several reserves, as required by the Illinois Pension Code and Board policy. The following are brief descriptions of the reserves:

City Contribution Reserve

	2010	2009
Balances at December 31	$ 1,908,133,221	$ 1,729,155,112

The City Contribution Reserve is maintained for the payment of the City's portion of future retirement benefits for active and inactive participants. Interest at 3% is credited to this reserve annually. When the amount of annuity for a policeman or widow is fixed, the City Contribution Reserve is charged with the amount of the present value of retirement benefit and the Annuity Payment Reserve is credited with such amount.

The City Contribution Reserve does not equal the present value of expected retirement benefits. The reserve is maintained on a cost basis, in accordance with the Illinois Pension Code.

Salary Deduction Reserve

	2010	2009
Balances at December 31	$ 1,251,989,944	$ 1,190,282,943

NOTE 8 RESERVES *(continued)*

The Illinois Pension Code requires the Fund to maintain separate accounts for each policeman for the amounts of salary deductions with interest at 3% per year. When a policeman retires, the amount of his annuity is charged to the Salary Deduction Reserve and credited to the Annuity Payment Reserve. If a policeman takes a separation refund, his salary deductions are refunded to him and charged to the Salary Deduction Reserve. This reserve is fully funded.

Annuity Payment Reserve

	2010	2009
Balances at December 31	$ 2,161,395,092	$ 1,669,671,740

When the amount of annuity has been fixed, the present value of expected benefit is transferred from the City Contribution Reserve and the Salary Deduction Reserve to the Annuity Payment Reserve for the payment of annuity. All age and service annuities, widow's annuities, and refunds are charged to this reserve.

Annually, the actuary calculates the present value of all annuities. The Investment and Interest Reserve will transfer amounts to the Annuity Payment Reserve to ensure that the balance in the Annuity Payment Reserve equals the present value of annuities. This reserve is fully funded.

Prior Service Annuity Reserve

	2010	2009
Balances at December 31	$ (1,142,243,383)	$ (622,643,823)

The Prior Service Annuity Reserve is increased by the City's contributions for policemen and widows' prior service annuities and all prior service annuities payable to policemen and widows are charged to this reserve. This reserve included an unfunded liability of $6,215,148,607 and $5,683,524,900 as of December 31, 2010 and 2009, respectively.

NOTE 8 RESERVES *(continued)*

Gift Reserve

	2010	2009
Balances at December 31	$ 13,541,513	$ 13,911,648

The Gift Reserve is maintained for gifts, grants, bequests, or other amounts received by the Fund. The Board of Trustees determines the use of these funds. Interest is credited to the Gift Reserve annually.

(f) Investment and Interest Reserve

All gains and losses from investments and investment earnings are recorded in the Investment and Interest Reserve. Interest due to the City Contribution Reserve, Salary Deduction Reserve, Prior Service Annuity Reserve, Gift Reserve, and Supplementary Payment Reserve is transferred from the Investment and Interest Reserve to those reserves.

(g) Ordinary Death Benefit Reserve

	2010	2009
Balances at December 31	$ (18,155,098)	$ (16,017,798)

Amounts contributed by policemen and the City for death benefits are credited to the Ordinary Death Benefit Reserve. Death benefit payments are charged to this reserve. The Ordinary Death Benefit Reserve had a deficit.

Automatic Increase Reserve

	2010	2009
Balances at December 31	$ (735,439,994)	$ (638,756,470)

The Automatic Increase Reserve is credited with amounts deducted from the salaries of policemen and matching contributions by the City for automatic increase in annuity with interest thereon. Payments of increased annuities and salary deduction refunds for increase in annuity are charged to this reserve. At December 31, 2010 and 2009, the Automatic Increase Reserve had a deficit.

NOTE 8 RESERVES *(continued)*

Supplementary Payment Reserve

	2010	2009
Balances at December 31	$ 447,402	$ 447,402

The Supplementary Payment Reserve receives amounts transferred from the Investment and Interest Reserve for supplemental increases in annuity for certain eligible retirees. This reserve is fully funded.

Child's Annuity Reserve

Amounts contributed by the City for child's annuity are credited to the Child's Annuity Reserve, and payments of child's annuity are charged to this reserve.

Duty Disability Reserve

The Duty Disability Reserve is increased by the City's contributions for duty disability benefits, child's disability benefits, and compensation annuities and is decreased by the payments of these benefits.

Ordinary Disability Reserve

Amounts contributed by the City for ordinary disability benefits are credited to the Ordinary Disability Reserve. Payments of ordinary disability benefits are charged to this reserve.

Hospitalization Fund Reserve

The health care premiums are paid from the tax levies and are credited to the reserve for Group Hospitalization Fund. Premium payments to the City are charged against this reserve.

Expense Reserve

Amounts contributed toward the cost of administration are credited to the Expense Reserve, while expenses of administration are charged to this reserve.

NOTE 9 DEFERRED COMPENSATION PLAN

The Fund offers its employees a deferred compensation plan created in accordance with Internal Revenue Code Section 457. The plan, available to all employees of the Fund, permits them to defer a portion of their salary until future years. Participation in the plan is optional. The deferred compensation is not available to employees until termination, retirement, death, or unforeseeable emergency. The plan is managed by a third-party administrator.

The assets of the plan were placed in trust accounts with the plan administrator for the exclusive benefit of participants and their beneficiaries and are not considered assets of the Fund.

NOTE 10 LEASE AGREEMENT

The Fund leases its office facilities under a noncancellable agreement that expires June 30, 2016. There is a renewal option for a ten year extension on the lease, however, such option has not yet been exercised. Office rental expense amounted to $233,234 and $229,294 for the years ended December 31, 2010 and 2009, respectively.

Future minimum rental payments under the office lease at December 31, 2010 are as follows:

Year	Amount
2011	$ 239,258
2012	244,687
2013	248,626
2014	252,562
2015	256,502
Thereafter	129,073
	$ 1,370,708

NOTE 11 RISK MANAGEMENT

The Fund is exposed to various risks of loss related to tort, theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. The Fund carries commercial insurance to reduce its exposure to risk of loss. There is no significant change in insurance coverage from year to year. Settled claims resulting from these risks have not exceeded commercial insurance coverage in any of the past three fiscal years.

NOTE 12 SUBSEQUENT EVENTS

On December 30, 2010, Public Act 096-1495 was signed into law and became effective January 1, 2011. The legislation included two matters that will impact the Fund in future years.

Members hired after January 1, 2011, will be subject to different provisions within their defined benefit pension plan. The new provisions include a minimum retirement age of 55, a final average salary calculation based upon 96 consecutive months within the last 120 months of employment, an annual salary cap for purposes of calculating a pension benefit, and cost of living increases for a pension benefit that include considerations related to the consumer price index for urban consumers. Additionally, surviving spouse benefits will be calculated at 66-2/3 percent of a policemen's earned annuity at the date of death, and a surviving spouse benefit will be subject to cost of living increases commencing when the survivor reaches age 60.

The financing for the Fund will be changed effective with the City of Chicago tax levy beginning in 2015. Such changes mandate that the Fund will be 90% funded by 2040. The funded level of 90% considers the (a) fair value of the Fund's assets and (b) application of certain required actuarial assumptions and methodologies. If the City of Chicago fails to remit the statutorily required contributions as calculated given criteria (a) and (b), then the State of Illinois could withhold certain grants owed to the City of Chicago and directly deposit the withheld funds with PABF.

REQUIRED SUPPLEMENTARY INFORMATION

POLICEMEN'S ANNUITY AND BENEFIT FUND OF CHICAGO
(A Component Unit of the City of Chicago)
Required Supplementary Information
Schedule of Funding Progress—Pension
For the Years Ended December 31, 2010 and 2009
(Unaudited)

Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) Entry Age (b)	Unfunded AAL (UAAL) (b-a)	Funded Ratio (a/b)	Covered Payroll (c)	UAAL as a Percentage of Covered Payroll ((b-a)/c)
12/31/04	$ 3,933,031,342	$ 7,034,271,474	$ 3,101,240,132	55.91%	$ 874,301,958	354.71%
12/31/05	3,914,431,654	7,722,737,147	3,808,305,493	50.69	948,973,732	401.31
12/31/06	3,997,990,919	7,939,561,277	3,941,570,358	50.36	1,012,983,634	389.11
12/31/07	4,231,681,817	8,220,352,638	3,988,670,821	51.48	1,038,957,026	383.91
12/31/08	4,093,719,894	8,482,574,033	4,388,854,139	48.26	1,023,580,667	428.77
12/31/09	3,884,978,241	8,736,101,666	4,851,123,425	44.47	1,011,205,359	479.74
12/31/10	3,718,954,539	9,210,056,428	5,491,101,889	40.38	1,048,084,301	523.92

The accompanying notes are an integral part of this schedule.

POLICEMEN'S ANNUITY AND BENEFIT FUND OF CHICAGO
(A Component Unit of the City of Chicago)
Required Supplementary Information
Schedule of Employer Contributions—Pension
For the Years Ended December 31, 2010 and 2009

(Unaudited)

Year Ended December 31	**Contributions**			**Percentage Contributed**
	Annual Required	**Actual Employee**	**Actual Employer**	
2004	$ 203,757,534	$ 78,800,816	$ 135,744,173	66.62%
2005	238,423,459	89,109,811	178,278,371	74.77
2006	262,657,025	91,965,685	150,717,705	57.38
2007	312,726,608	93,299,996	170,598,268	54.55
2008	318,234,870	93,207,408	172,835,805	54.31
2009	339,488,187	95,614,390	172,043,785	50.68
2010	363,624,570	108,402,353	174,500,507	47.99

The accompanying notes are an integral part of this schedule.

(Unaudited)

Valuation date	December 31, 2010 and 2009, respectively
Actuarial cost method	Entry age normal
Amortization method	Level percent open
Remaining amortization period	30 years
Actuarial value of assets	5-year smoothed market
Actuarial assumptions:	
Pension investment rate of return	8.0%
Projected salary increases	4.0% per year, plus additional percentage related to service
Cost of living allowance	3.0% (1.5% for retirees born after January 1, 1955)
General Inflation rate	3.0%

POLICEMEN'S ANNUITY AND BENEFIT FUND OF CHICAGO

(A Component Unit of the City of Chicago)

Required Supplementary Information

Schedule of Funding Progress—Health Insurance Supplement

For the Years Ended December 31, 2010 and 2009

(Unaudited)

Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) Entry Age (b)	Unfunded AAL (UAAL) (b-a)	Funded Ratio (a/b)	Covered Payroll (c)	UAAL as a Percentage of Covered Payroll ((b-a)/c)
12/31/05	$ -	$ 176,117,539	$ 176,117,539	0.00%	$ 948,973,732	18.56%
12/31/06	-	176,981,897	176,981,897	0.00	1,012,983,634	17.47
12/31/07	-	179,039,841	179,039,841	0.00	1,038,957,026	17.23
12/31/08	-	169,972,156	169,972,156	0.00	1,023,580,667	16.61
12/31/09	-	164,799,819	164,799,819	0.00	1,011,205,359	16.30
12/31/10	-	164,796,449	164,796,449	0.00	1,048,084,301	15.72

The accompanying notes are an integral part of this schedule.

POLICEMEN'S ANNUITY AND BENEFIT FUND OF CHICAGO
(A Component Unit of the City of Chicago)
Required Supplementary Information
Schedule of Employer Contributions—Health Insurance Supplement
For the Years Ended December 31, 2010 and 2009
(Unaudited)

Year Ended December 31	Contributions: Annual Required	Actual Employee	Actual Employer	Percentage Contributed
2006	$ 11,076,022	$ -	$ 8,041,573	72.60%
2007	11,220,081	-	8,107,708	72.26
2008	11,348,959	-	8,850,186	77.98
2009	11,810,766	-	9,266,431	78.46
2010	10,659,006	-	9,354,163	87.76

The accompanying notes are an integral part of this schedule.

Valuation date	December 31, 2010 and 2009, respectively
Actuarial cost method	Entry age normal
Actuarial value of assets	No assets (pay-as-you-go)
Amortization method	Level percent open
Remaining amortization period	30 years
Actuarial assumptions:	
OPEB investment rate of return	4.5%
Projected salary increases	4.0% per year, plus additional percentage related to service
Healthcare Cost Trend Rate	0.00% (fixed dollar subsidy)

POLICEMEN'S ANNUITY AND BENEFIT FUND OF CHICAGO
(A Component Unit of the City of Chicago)
Required Supplementary Information
Schedule of Funding Progress—Staff Retiree Health Plan
For the Years ended December 31, 2010 and 2009
(Unaudited)

Actuarial Valuation Date	GASB Value of Assets (a)	Actuarial Accrued Liability (AAL) Entry Age (b)	Unfunded AAL (UAAL) (b-a)	Funded Ratio (a/b)	Covered Payroll (c)	UAAL as a Percentage of Covered Payroll ((b-a)/c)
12/31/07	$ -	$ 3,021,300	$ 3,021,300	0.00%	$ 1,150,900	262.5%
12/31/08	-	3,239,700	3,239,700	0.00	1,202,700	269.4
12/31/09	-	3,474,800	3,474,800	0.00	1,256,800	276.5
12/31/10	-	5,588,688	5,588,688	0.00	1,486,848	375.9

The accompanying notes are an integral part of this schedule.

POLICEMEN'S ANNUITY AND BENEFIT FUND OF CHICAGO
(A Component Unit of the City of Chicago)
Required Supplementary Information
Schedule of Employer Contributions—Staff Retiree Health Plan
For the Years Ended December 31, 2010 and 2009
(Unaudited)

Year Ended December 31	Contributions Annual Required	Contributions Actual Employee	Contributions Actual Employer	Percentage Contributed
2007	$ 261,500	$ -	$ 88,800	34%
2008	274,600	-	104,700	38
2009	290,600	-	121,000	42
2010	434,005	-	127,630	29

The accompanying notes are an integral part of this schedule.

Valuation date	December 31, 2010 and 2009, respectively
Actuarial cost method	Entry age normal
Actuarial value of assets	No assets (pay-as-you-go)
Amortization method	Level percent open
Remaining amortization period	30 years
Actuarial assumptions:	
OPEB investment rate of return	4.5% per year
Wage inflation	4.5% per year
Healthcare trend	December 31, 2010 8.5% per year, graded down to 5.0% per year, ultimate trend in 0.5% increments
	December 31, 2009 9.0% per year, graded down to 5.0% per year ultimate trend in 1.0% increments

OTHER SUPPLEMENTARY INFORMATION

POLICEMEN'S ANNUITY AND BENEFIT FUND OF CHICAGO
(A Component Unit of the City of Chicago)
Other Supplementary Information
Schedule of Administrative Expenses
For the Years Ended December 31, 2010 and 2009

	2010	2009
Administrative expenses		
Actuary services	$ 147,539	$ 265,200
Benefits disbursement	193,951	189,755
Equipment service and rent	67,030	53,016
External auditors	54,520	58,805
Fiduciary insurance	104,564	110,343
Legal services	315,263	291,210
Medical consultant	187,073	240,341
Miscellaneous	589,491	855,623
Occupancy and utilities	240,075	240,843
Personnel salaries and benefits	2,004,179	1,978,905
Postage	7,500	6,000
Supplies	13,743	13,558
	$ 3,924,928	$ 4,303,599

POLICEMEN'S ANNUITY AND BENEFIT FUND OF CHICAGO
(A Component Unit of the City of Chicago)
Other Supplementary Information
Schedule of Consulting Costs
For the Years Ended December 31, 2010 and 2009

	2010	2009
Payment to consultants		
External auditors	$ 54,520	$ 58,805
Medical consultant	187,073	240,341
Legal services	315,263	291,210
Actuary service	147,539	265,200
Investment manager fees	9,109,616	8,987,507
Master trustee fees	183,525	197,804
Consulting fees	542,554	616,179
	$ 10,540,090	$ 10,657,046

POLICEMEN'S ANNUITY AND BENEFIT FUND OF CHICAGO
(A Component Unit of the City of Chicago)
Other Supplementary Information
Schedule of Investment Fees
For the Years Ended December 31, 2010 and 2009

	2010	2009
Investment managers		
Ariel Capital Management	$ 320,177	$ 227,946
Artisan Partners	495,093	433,358
Attucks Asset Management	42,651	35,077
Capital Guardian Trust Co.	467,486	482,652
Channing Capital	164,141	132,732
Chicago Equity Partners	313,561	393,057
Cordillera Asset Management	-	64,442
Dearborn Partners LLC	181,294	169,346
Denali Advisors	103,359	86,315
European Investors	42,733	122,723
Great Lakes Advisors	516,238	465,186
Holland Capital Management	229,200	187,463
ING Clarion	56,596	82,136
Invesco Capital Management	379,564	385,546
JP Morgan Fleming Asset Management	605,289	501,214
LM Capital Group	80,810	74,242
McKinley Capital	367,077	318,397
Montag & Caldwell	732,840	633,410
Northern Trust Global Investments - Index Funds	106,849	88,679
Piedmont Investment Advisors	214,599	138,925
Taplin, Canida, & Habacht	117,495	112,567
UBS Global Asset Management	1,588,191	1,509,302
Wellington Management	330,776	407,513
Wells Capital Management	410,825	377,781
William Blair & Co.	1,242,772	1,557,498
Total investment managers fees	9,109,616	8,987,507
Investment consultants		
Elkins McSherry Inc	20,000	25,000
Ennis Knupp & Associates	175,100	350,810
Courtland Partners	54,325	107,824
NEPC LLC	187,093	-
Kolhberg & Associates	106,036	132,545
Total investment consultants fees	542,554	616,179
Master custodian		
The Northern Trust Company	183,525	197,804
Total investment fees	$ 9,835,695	$ 9,801,490