OREGON PUBLIC EMPLOYEES RETIREMENT SYSTEM
BOARD MEETING

Friday, July 23, 2010 1:00 P.M.	PERS 11410 SW 68th Parkway Tigard, OR

	ITEM	PRESENTER
A. Administration – 1:00 P.M.		
1. 2.	May 21, 2010 Board Meeting Minutes Director's Report a. Forward-Looking Calendar b. Budget Report c. OIC Investment Report d. Employer Reporting Update e. Quarterly Report of Member Transactions f. 2011 Legislative Concepts Update	CLEARY
B. Consent Items		
1. 2.	Notice of Senate Bill 897 Data Verification Rule Notice of Retire From One, Retire From All Rule	RODEMAN
C. Final Rule Adoption		
1. 2. 3.	Adoption of Disability Rules Adoption of Employer Remitting of Employee Contributions Rule Adoption of Equal To or Better Than Rule	RODEMAN
D. Action and Discussion Items		
1. 2. 3.	Appointment of Oregon Savings Growth Plan Advisory Board Members 2011-13 Final Agency Request Budget Approval 2009 Valuation System-wide Results	BATH KNOLL / DUFRENE MERCER
E. Executive Session Pursuant to ORS 192.660(2)(f), (h), and/or ORS 40.225		
1.	Litigation Update	LEGAL COUNSEL

*****Audit Committee meeting immediately following *****

Note: *If you have a disability that requires any special materials, services or assistance, call (503) 603-7575 at least 48 hours before the meeting.*

James Dalton, Chair * Thomas Grimsley, Vice-Chair * Eva Kripalani * Mike Pittman * Laurie Warner
Paul R. Cleary, Executive Director

Level 1 - Public

PERS Oregon Public Employees Retirement System

OREGON PUBLIC EMPLOYEES RETIREMENT SYSTEM

Item A.1.

PERS Board Meeting
May 21, 2010
Tigard, Oregon
MINUTES

Board Members:

James Dalton, Chair
Tom Grimsley, Vice-Chair
Eva Kripalani
Laurie Warner

Staff:

Donna Allen
Linda Barnett
Helen Bamford
Gay Lynn Bath
Paul Cleary
David Crosley
Jon DuFrene
Joe DeLillo
Yvette Elledge
Brian Harrington
Kyle Knoll
Jeff Marecic
Zue Matchett
Dale Orr
Brenda Pearson
Susan Riswick
Steve Rodeman
Susan Sjordal
Jason Stanley
Stephanie Vaughn

Others:

Steven Biehn
Eric Blumenthal
Molly Butler
Lance Colley
Kris Day
Mike Eliason
Linda Ely
Marc Feldesman
Robert Graves
Blake Johnson
Rick Harrington
Greg Hartman
Trish Isaak
Keith Kutler
Matt Larrabee
Peter McGarry
C. J. McLeod
P. Peg
Bob Palmer
Jean Polney
Scott Preppernau
Bill Robertson
Lori Sattenspiel
Ron Schmitz
Diane Skutack
John Thoma
Deborah Tremblay
Patrick Weizgerber
Brenda Wilson
Peggy Woolsey
Lori Woova
John Witherell
Pat Witherell

Chair James Dalton called the meeting to order at 1:04 P.M. Board member Mike Pittman was excused with a scheduling conflict.

ADMINISTRATION

A.1. BOARD MEETING MINUTES OF MARCH 29, 2010

The Board unanimously approved the minutes from the March 29, 2010 Board meeting.

A.2. DIRECTOR'S REPORT

Director Paul Cleary reported on the upcoming joint PERS Board and Oregon Investment Council (OIC) meeting Wednesday, May 26, 2010 for a presentation from Strategic Investment Solutions on the asset/liability study results.

Director Cleary presented the Board's 2010 forward-looking calendar noting the next Board meeting will be held on July 23, 2010. Agenda items for the July Board meeting will include the 2011-13 agency request budget and 2009 system-wide valuation results.

Cleary reported the 2011-13 employer rate adoption is scheduled for September Board meeting along with the ongoing actuarial audit results.

Legislative concepts approval will occur at the November Board meeting.

Cleary presented the 2009-11 operating budget report noting a positive variance of approximately $3 million. Of this, $181,000 is dedicated for the RIMS Conversion Project (RCP) budget. Cleary noted the decline in the positive variance is a result of administrators "truing up" their projected spending at the Division level.

Cleary presented a quarterly member transaction report developed to provide the Board with production volume information for retirements, withdrawals, and estimate requests. Cleary noted the IAP retirements pending number should be revised to read approximately 700. Cleary described the estimate request prioritization process and noted recent IT system deployment issues had delayed the processing of estimate requests. Cleary noted there are 60,000 members eligible to retire.

Cleary reported PERS should receive notification from DAS by the end of the month regarding the 2011 Legislative concepts. The Board will make a final decision at the November Board meeting whether to submit any or all concepts to the Governor's office.

Cleary reported the distribution of approximately 255,000 member annual statements for 2009 is going well based on the low call volume and the number of annual statements mailed to date.

Cleary reported on a Washington, D.C. conference he attended regarding the current status of public pension system reforms. He noted Oregon was recognized as being on the leading edge of system reforms. Cleary described a recently produced and posted history of PERS benefit enhancements, caps, and reductions. Cleary noted that PERS By The Numbers has been updated with the 2009 investment earnings and 2009 retirement information. The Board also received a copy of the asset/liability report that will be presented at the joint meeting on Wednesday. All of these documents will also be posted on the PERS website.

Ron Schmitz, Chief Investment Officer for the Oregon State Treasury, presented the preliminary April 2010 OIC report detailing the Fund's asset allocation and related investment returns. Schmitz discussed the outcomes from the January 2010 joint OIC and PERS Board meeting. Schmitz noted the next joint meeting is scheduled for May 26 where the asset/ liability study results will be presented.

CONSENT ITEMS

B.1. NOTICE OF DISABILITY RULES

Deputy Director Steve Rodeman provided notice of rulemaking on the proposed disability payments and benefits rules. No Board action was required.

B.2. NOTICE OF EMPLOYER REMITTANCE OF EMPLOYEE CONTRIBUTION RULE

Rodeman provided notice of rulemaking on the proposed employer remittance of employee contribution rule. No Board action was required.

B.3. NOTICE OF FIRST READING OF OPSRP HEALTH INSURANCE RULES

Rodeman provided the first reading on OPSRP health insurance rules affected by Senate Bill 897. Rodeman described the status of the Board's previous temporary adoption of the OPSRP health insurance rules, noting modifications of these rules could allow PERS to extend this coverage to domestic partnerships pending a decision by the IRS. Rodeman noted that permanent rulemaking will be delayed until September to see if the IRS acts on the PERS plan determination request.

FINAL RULE ADOPTION

C.1. ADOPTION OF DOMESTIC RELATIONS ORDERS RULES

Rodeman presented new rules and modifications to existing rules for adoption dealing with domestic relations orders.

Rodeman presented the walk-in packet which included proposed modifications received from two attorneys during the week of May 17, 2010. In response, PERS extended the public comment period until May 21, 2010.

Staff recommended making two modifications to the rules as originally published in the May 21, 2010 Board packet. Rodeman described those modifications and staff recommendations.

Rodeman recommended the Board pass a motion to adopt the rules as proposed including the further modifications presented in the walk-in packet.

It was moved by Tom Grimsley and seconded by Eva Kripalani to adopt the new and modified PERS Domestic Relations orders rules as recommended. The motion passed unanimously.

C.2. ADOPTION OF HOUSEKEEPING UPDATES TO VARIOUS RULES

Rodeman described and recommended the Board adopt the proposed housekeeping modifications to various rules and repeal of obsolete rules.

It was moved by Laurie Warner and seconded by Kripalani to adopt the housekeeping modifications to various rules and repeal of obsolete rules as recommended. The motion passed unanimously.

C.3. ADOPTION OF RULES TO IMPLEMENT NON-VERIFICATION PORTION OF SB 897

Rodeman recommended the Board adopt permanent modifications to rules affected by Senate Bill 897 regarding retirement credit for retroactive salary payments.

It was moved by Grimsley and seconded by Kripalani to adopt rules to implement the non-verification portions of Senate Bill 897 as recommended. The motion passed unanimously.

ACTION AND DISCUSSION ITEMS

D.1. 2011 RETIREE HEALTH INSURANCE PLAN RENEWALS

Zue Matchett, Retiree Health Insurance Program Manager, presented the Retiree Health Insurance 2011 Plan renewals and rate increases. Matchett described the program history, unique membership characteristics, and plan renewal process. Matchett noted the renewal process is a collaborate effort among plan partners which resulted in the best possible outcomes. Matchett stated there is uncertainty on how ongoing national health care reforms will impact the plans. Insurance providers have Medicare experts on staff tracking and providing updates on reform-related opportunities and impacts.

Molly Butler, PERS Health Insurance consultant, provided her observations on the PERS renewal rates verses other private and public plan renewals, noting that the PERS rate changes were competitive and moderate compared to many others.

Cleary noted a correction to item D.1 page 4. The ODS managed Prescription Drug Plan subsidy of approximately $100 “per month” should read $100 “per year”. The Board expressed appreciation to plan partners for their cooperation and dedication in providing the best possible retiree health insurance plans and premium rates.

It was moved by Grimsley and seconded by Kripalani to approve the proposed PERS Retiree Health Insurance Plan contracts, conditions, and rate changes for 2011 as presented. The motion passed unanimously.

D.2. 2011 PRELIMINARY AGENCY REQUEST BUDGET

Jon DuFrene, Chief Financial Officer and Kyle Knoll, Business Operations Manager presented the 2011-13 Preliminary Agency Request Budget Overview.

Knoll noted PERS is tentatively requesting a total of 47 “new” positions, with 46 permanent and one limited-duration. Of these, 30 positions are carryovers from the previous biennium and 13 are new positions to support additional workload as a result of Senate Bills 399 and 897. Knoll reported the total position request is a conservative approach reflecting a flat-lined workforce except for the 13 Senate Bill related positions. Knoll said the budgeting goal is to stabilize total agency position count while handling increased workload associated with the growing number of members eligible for retirement.

Knoll noted the three policy options packages are a significant decrease from the previous biennium. Knoll reported the policy option packages and related business cases will be discussed in detail at the June 16 budget review work session. Kyle noted attendees will include executive sponsors, a DAS budget analyst, and a LFO analyst. Knoll welcomed Board members to participate if their schedules allowed. Knoll noted the final agency request budget report will be submitted for approval at the July 23 Board meeting. The Board approved agency request budget must be submitted to the Govenor by August 2.

D.3. ETOB TESTING RESULTS

Matt Larrabee and Scott Preppernau, Mercer, presented an update on the Equal to or Better Than (ETOB) testing process. Larrabee noted Morrow County and City of Portland were employers who will satisfy the ETOB based on the preliminary evaluation.

Larrabee reported that the tests must be able to cover two different pension plan types: defined benefit (DB) and defined contributions (DC). Larrabee noted one of the key factors used in the initial round of ETOB testing was the use of a "risk free rate" and that testing results can vary widely based on how it is applied to the different types of plans.

Larrabee presented a comparison of a DB and DC plan using the "risk free rate" methodology. Larrabee noted all DB programs tend to re-price by similar percentages using the risk-free methodology, so the methodology does not significantly affect test results for DB programs. Larrabee noted this statement does not hold true for DC programs, which do not substantially re-price with the "risk free rate" methodology, causing the value of a DC benefit to diminish in comparison to a DB benefit, when discounted to present value.

Larrabee noted a reasonable alternative methodology could be to use the PERS actuarial investment return assumption of 8% to both project the account balance accumulation over an employee's career and discount that projected account balance back to the testing date.

Larrabee described testing results for both the DB and DC plans using an alternative methodology. Larrabee noted if the Board finds that the "risk free rate" methodology in the current OAR does not appropriately reflect the comparative values of DB and DC programs for ETOB testing, appropriate next steps are to modify the OAR based on additional stakeholder input and then complete the testing based on any changes to the methodology specified by modifications to the OAR.

Greg Hartman, PERS Coalition, recommended further discussion among interested stakeholders and reviewing alternatives for employers who need to respond to the final testing results.

Board members discussed the difference between the "risk free rate" and the PERS assumed rate and directed staff to prepare modifications to the OAR and share the proposed changes with stakeholders for further review and input.

Chair Dalton then temporally adjourned the meeting to Executive session for a discussion of ongoing litigation. Chair Dalton reconvened the meeting, thanked the audience, and adjourned the meeting at 3:20 PM.

Respectfully submitted,

Paul R. Cleary
Executive Director

PERS Oregon Public Employees Retirement System

PERS Board Meeting
Forward-Looking Calendar

September 24, 2010

Adoption of Health Insurance Program Rules
Adoption of Recovery of Administrative Costs Rule
Adoption of Retire from One, Retire from All Rule
Adoption of SB 897 Data Verification Rule
Notice of Confidentiality of Member's Records Rule
Notice of Employer Contributions on Retiree Salaries Rules
2011-13 Employer Rate Adoption
Actuarial Audit Results
ETOB Testing Results

November 19, 2010

Adoption of Confidentiality of Member's Records Rule
Adoption of Employer Contributions on Retiree Salaries Rules
Notice of Employer Adjustments to IAP Accounts Rule
2011 Session Legislative Concept Approval
Audit Committee

PERS Oregon Public Employees Retirement System

Oregon

Theodore R. Kulongoski, Governor

Public Employees Retirement System
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www.oregon.gov/pers

July 23, 2010

TO: Members of the PERS Board

FROM: Kyle J. Knoll, Business Operations Manager

SUBJECT: Budget Report

2009-11 BUDGET UPDATE

Operating expenditures for the month of May 2010 were $3,855,969, and preliminary June 2010 expenditures are $2,896,325. Final June expenditures close in the Statewide Financial Management System (SFMS) June 18, 2010, and will be included in the September 24, 2010 Board Report.

- The Agency's 2009-11 Legislatively Approved Budget (LAB) of $83,261,952 reflects an increase of $2,601,324, approved by the May 2010 Emergency Board for six additional positions (two permanent; four limited duration) and IT – Professional Services contracting to support implementation of SB 897 and SB 399.

- To-date, through the first twelve months (50%) of the 2009-11 biennium, the Agency has expended a total of $34,614,448 or 41.57% of PERS' 2009-11 operating budget. And the current projected positive variance is $3,635,863.

PERS Oregon Public Employees Retirement System

2009-11 Agency-wide Operations - Budget Execution

A.2.b.

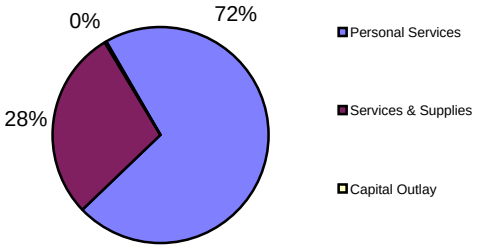
Summary Budget Analysis

For the Month of: June 2010 (prelim)

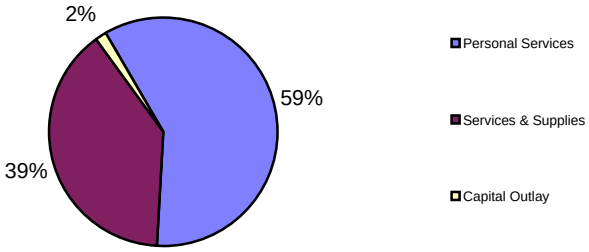
Biennial Summary

Category	Actual Exp. To Date	Projected Expenditures	Total Est. Expend.	2009-11 LAB	Variance
Personal Services	24,638,228	26,694,038	51,332,266	52,751,494	**1,419,228**
Services & Supplies	9,864,406	17,612,704	27,477,110	29,916,870	**2,439,760**
Capital Outlay	111,813	704,900	816,713	593,588	**(223,125)**
Special Payments					
Total	**34,614,448**	**45,011,641**	**79,626,089**	**83,261,952**	**3,635,863**

Actual Expenditures

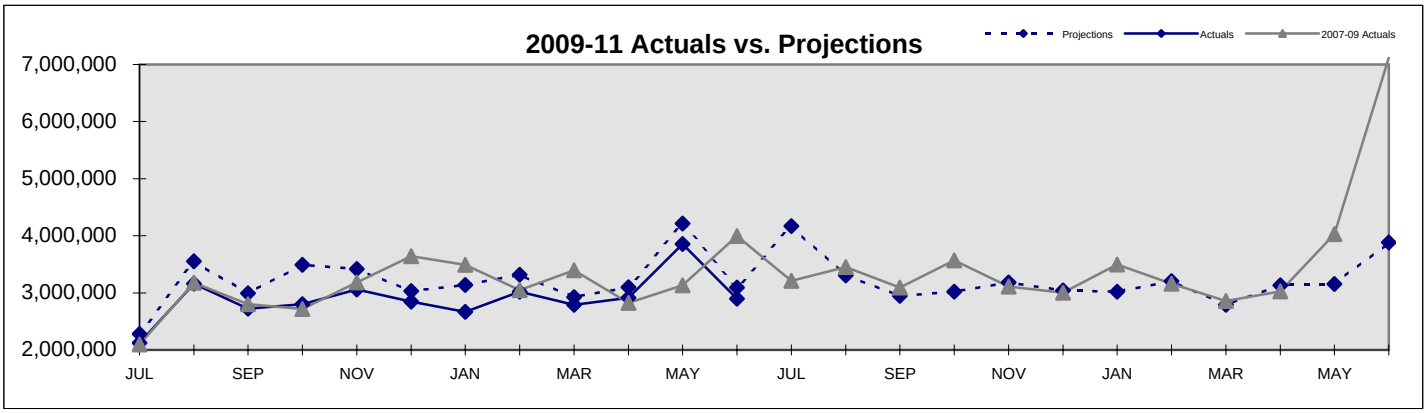


Projected Expenditures



Monthly Summary

Category	Actual Exp.	Projections	Variance	Avg. Monthly Actual Exp.	Avg. Projected Expenditures
Personal Services	2,044,376	2,155,423	111,046	2,053,186	2,224,503
Services & Supplies	851,949	906,015	54,066	822,034	1,467,725
Capital Outlay		30,000	30,000	9,318	58,742
Special Payments					
Total	**2,896,325**	**3,091,438**	**195,112**	**2,884,537**	**3,750,970**



2007-09 Biennium Summary

Category	Actual Exp. To Date	Projected Expenditures	Total Est. Expend.	2007-09 LAB	Variance
Personal Services	49,613,038		49,613,038	53,288,261	**3,675,223**
Services & Supplies	27,421,160		27,421,160	26,553,000	**(868,160)**
Capital Outlay	350,966		350,966	947,701	**596,735**
Special Payments					
Total	**77,385,163**		**77,385,163**	**80,788,962**	**3,403,799**

2009-11 Agency-wide Operations - Budget Execution

Spending Plan - Actual and Estimated Expenditures

2009-11 Summary as of April 30, 2010 (preliminary)

	1st QTR	2nd QTR	3rd QTR	4th QTR	5th QTR	6th QTR	7th QTR	8th QTR	ACTUAL EXPEND. TO DATE	EST. EXPEND.	ENC. & PRE-ENC.	TOTAL ESTIMATED EXPEND.	09-11 LAB BUDGET	VARIANCE
Personal Services														
3110 Salaries & Wages	4,031,030	3,938,000	3,945,280	3,980,299	4,190,870	4,389,448	4,330,402	4,440,327	**15,894,609**	17,351,047		**33,245,656**	36,482,139	**3,236,483**
3160 Temporary Appointments	45,066	28,460	28,773	39,055	45,474	9,000	19,500	19,500	**141,354**	93,474		**234,828**	166,319	**(68,509)**
3170 Overtime	76,447	70,919	71,628	72,522	94,470	70,629	73,788	73,297	**291,517**	312,184		**603,701**	572,860	**(30,841)**
3180 Shift Differential	2,567	4,212	3,006	2,622	3,190	2,490	2,490	2,490	**12,407**	10,660		**23,067**	2,096	**(20,971)**
3190 All Other Differential	58,805	62,584	66,683	70,597	56,019	56,019	56,019	56,019	**258,669**	224,076		**482,745**	221,885	**(260,860)**
3210 ERB Assessment	1,717	1,715	1,755	1,768	1,922	1,922	1,922	1,922	**6,955**	7,686		**14,641**	15,191	**551**
3215 Wokers' Comp. Insurance (SA														
3220 PERS	355,897	334,475	329,723	332,594	357,122	371,428	366,834	375,829	**1,352,689**	1,471,213		**2,823,902**	3,064,330	**240,428**
3221 Pension Bond Contribution	243,260	237,316	233,793	235,611	249,357	261,172	257,659	264,199	**949,980**	1,032,387		**1,982,367**	1,652,716	**(329,651)**
3230 Social Security Taxes	319,033	310,907	314,048	317,803	335,837	346,360	342,888	351,260	**1,261,791**	1,376,345		**2,638,136**	2,856,779	**218,643**
3240 Unemployment Comp.													39,629	**39,629**
3250 Workers' Comp. Assess.	2,162	2,029	2,133	2,170	2,855	2,855	2,855	2,855	**8,493**	11,419		**19,912**	22,423	**2,511**
3260 Mass Transit Tax	25,233	24,687	24,702	25,016	25,145	26,337	25,982	26,642	**99,638**	104,106		**203,744**	225,200	**21,456**
3270 Flexible Benefits	1,035,204	1,061,850	1,122,238	1,140,836	1,174,860	1,174,860	1,174,860	1,174,860	**4,360,127**	4,699,440		**9,059,567**	9,286,530	**226,963**
3455 Vacancy Savings													(165,147)	**(165,147)**
3465 Reconciliation Adj.													(1,691,456)	**(1,691,456)**
Unscheduled P.S.														
Total Personal Services	**6,196,421**	**6,077,152**	**6,143,762**	**6,220,893**	**6,537,120**	**6,712,519**	**6,655,199**	**6,789,200**	**24,638,228**	**26,694,038**		**51,332,266**	**52,751,494**	**1,419,228**
			actual				*estimated*							
Services & Supplies														
4100 Instate Travel	11,279	29,654	22,069	35,279	28,530	28,530	28,830	37,590	**98,281**	123,480		**221,761**	214,341	**(7,420)**
4125 Out-of-state Travel	15	1,782	21	416		1,550			**2,234**	1,550		**3,784**	11,793	**8,009**
4150 Employee Training	19,458	76,008	15,791	66,626	45,935	45,325	44,275	57,150	**177,883**	192,685	40,000	**410,568**	705,298	**294,730**
4175 Office Expenses	147,057	297,703	306,856	251,372	210,985	290,985	280,985	339,330	**1,002,987**	1,122,285		**2,125,272**	2,212,549	**87,277**
4200 Telecommunications	23,389	49,926	64,909	60,928	60,000	60,000	60,000	80,000	**199,152**	260,000		**459,152**	533,647	**74,495**
4225 St. Gov. Svc. Chg.	821,363	181,114	118,474	92,420	714,000	114,000	114,000	144,000	**1,213,370**	1,086,000		**2,299,370**	2,198,294	**(101,076)**
4250 Data Processing	7,126	400,093	204,249	494,151	716,134	452,703	359,289	650,325	**1,101,748**	2,182,322	252,000	**3,536,070**	3,748,524	**212,454**
4275 Publicity/Publications	13,065	9,867	4,638	7,808	18,300	19,400	18,300	24,400	**35,378**	80,400		**115,778**	257,067	**141,289**
4300 Professional Services	162,686	224,422	311,363	230,108	499,147	313,607	294,507	392,316	**928,579**	1,499,577	215,000	**2,643,156**	3,433,877	**790,721**
4315 IT Professional Services	292,694	871,511	935,722	1,668,720	915,130	602,581	627,581	670,181	**3,530,862**	3,053,259	4,968,131	**11,552,252**	12,381,307	**829,055**
4325 Attorney General	25,621	112,538	54,537	79,934	213,500	163,500	163,500	221,600	**272,630**	762,100		**1,034,730**	1,048,583	**13,853**
4350 Dispute Res. Svc.		15,676	5,914	19,846	15,000	15,000	15,000	20,000	**41,436**	65,000	24,000	**130,436**	85,655	**(44,781)**
4375 Empl. Recruit./Devel.	633	3,011	3,348	3,801	5,925	5,925	5,925	7,900	**10,792**	25,675		**36,467**	61,509	**25,042**
4400 Dues & Subscriptions	3,303	4,467	737	4,275	3,720	4,890	1,490	490	**12,782**	10,590		**23,372**	53,737	**30,365**
4425 Facility Rental	114,140	90,741	124,708	158,152	122,400	122,400	122,400	163,200	**487,741**	530,400		**1,018,141**	982,592	**(35,549)**
4450 Fuels/Utilities	24,837	39,891	21,931	26,993	32,250	32,250	32,250	43,000	**113,652**	139,750		**253,402**	170,706	**(82,696)**
4475 Facility Maint.	83,696	152,340	51,064	139,769	106,500	106,500	106,500	116,000	**426,869**	435,500	100,350	**962,719**	959,685	**(3,034)**
4575 Agency/Program S & S														
4625 Other COP Costs		195	30	390		550		300	**615**	850		**1,465**	6,682	**5,217**
4650 Other S & S	14,466	(7,735)	16,979	(4,288)	3,000	3,000	3,000	3,000	**19,423**	12,000		**31,423**	2,861	**(28,562)**
4700 Expendable Property	4,343	7,020	647	7,098					**19,107**			**19,107**	93,562	**74,455**
4715 IT Expendable Property	12,994	8,312	68,500	79,079	50,000	45,000	45,000	260,000	**168,885**	400,000	29,800	**598,685**	754,601	**155,916**
Unscheduled S & S														
Total Services & Supplies	**1,782,166**	**2,568,535**	**2,332,487**	**3,422,876**	**3,760,456**	**2,427,696**	**2,322,832**	**3,230,782**	**9,864,406**	**11,983,423**	**5,629,281**	**27,477,110**	**29,916,870**	**2,439,760**
Capital Outlay														
5100 Office Furn./Fixture													32,716	**32,716**
5150 Telecomm. Equip.					60,000	55,000				115,000		**115,000**	66,506	**(48,494)**
5200 Technical Equipment		63,200							**63,200**			**63,200**		**(63,200)**
5550 Data Proc.-Software													110,226	**110,226**
5600 Data Proc.-Hardware	24,956			23,657	65,000	48,000	33,500	148,400	**48,613**	294,900	150,000	**493,513**	384,140	**(109,373)**
5700 Building & Structure											145,000	**145,000**		**(145,000)**
Total Capital Outlay	**24,956**	**63,200**		**23,657**	**125,000**	**103,000**	**33,500**	**148,400**	**111,813**	**409,900**	**295,000**	**816,713**	**593,588**	**(223,125)**
Special Payments														
Total Special Payments														
Total Expenditures	**8,003,542**	**8,708,887**	**8,476,249**	**9,667,426**	**10,422,576**	**9,243,215**	**9,011,531**	**10,168,382**	**34,614,448**	**39,087,360**	**5,924,281**	**79,626,089**	**83,261,952**	**3,635,863**

Percent of 2009-11 LAB Expended:	**41.57%**
Percent of Biennium Expired:	**50.00%**

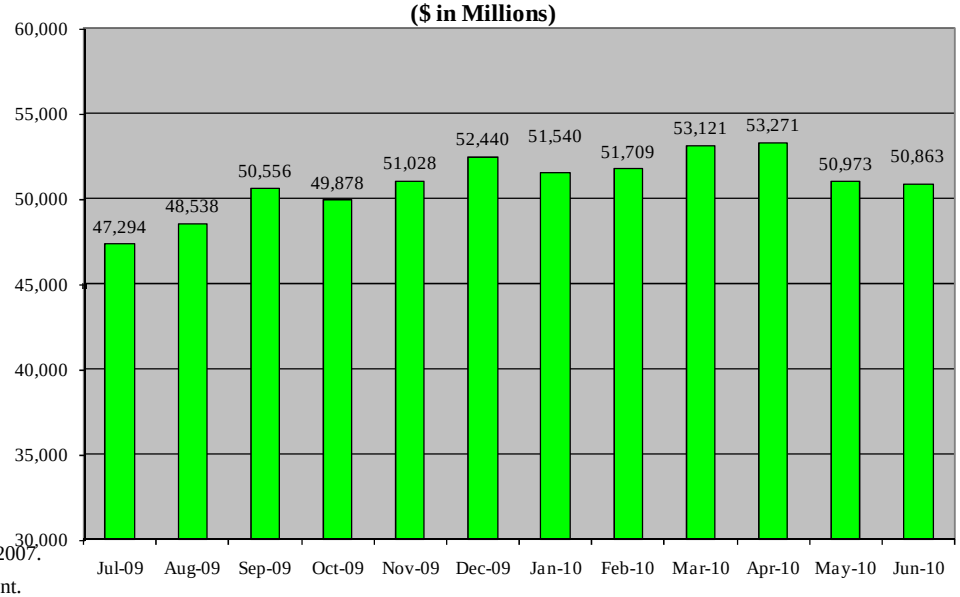
Returns for periods ending 6/30/2010 **Oregon Public Employees Retirement Fund**

OPERF	Policy[1]	Target[1]	$ Thousands[2]	Actual	Year-To-Date[3]	1 YEAR	2 YEARS	3 YEARS	4 YEARS	5 YEARS
	Regular Account				Historical Performance (Annual Percentage)					
Public Equity	41-51%	46%	$ 19,667,733	39.3%	(8.10)	13.94	(10.44)	(10.37)	(2.96)	0.90
Private Equity	12-20%	16%	11,066,890	22.1%	9.30	28.34	(2.39)	0.82	6.59	10.06
Total Equity	**57-67%**	**62%**	**30,734,623**	**61.4%**						
Opportunity Portfolio			1,023,078	2.0%	2.06	28.52	2.89	0.26		
Total Fixed	**22-32%**	**27%**	**13,518,999**	**27.0%**	5.78	18.50	10.00	7.51	7.38	6.06
Real Estate	**8-14%**	**11%**	**4,765,053**	**9.5%**	(8.97)	(0.70)	(15.28)	(10.34)	(3.52)	2.67
Cash	**0-3%**	**0%**	**3,216**	**0.0%**	0.42	1.19	1.15	2.25	3.05	3.25
TOTAL OPERF Regular Account		**100%**	**$ 50,044,969**	**100.0%**	(0.96)	17.03	(4.56)	(4.21)	1.05	3.59
OPERF Policy Benchmark					(1.00)	15.54	(3.16)	(3.11)	1.65	3.66
Value Added					0.04	1.49	(1.40)	(1.10)	(0.60)	(0.07)
TOTAL OPERF Variable Account			**$ 817,834**		(8.41)	13.23	(10.23)	(11.56)	(4.95)	(1.96)

Asset Class Benchmarks:

Russell 3000 Index	(6.05)	15.72	(7.82)	(9.47)	(2.85)	(0.48)
MSCI ACWI Ex US IMI Net	(10.42)	11.49	(11.97)	(10.11)	(1.39)	3.95
MSCI ACWI IMI Net	(8.65)	13.07	(10.34)	(10.17)	(2.37)	1.47
Russell 3000 Index + 300 bps--Quarter Lagged	13.88	56.06	1.73	0.18	3.55	6.18
BC Universal--Custom FI Benchmark	5.78	18.50	10.00	7.51	7.38	6.06
NCREIF Property Index--Quarter Lagged	(1.37)	(9.60)	(12.18)	(4.32)	0.53	4.19
91 Day T-Bill	0.05	0.16	0.55	1.57	2.47	2.77

TOTAL OPERF NAV
(includes variable fund assets)
One year ending June 2010
($ in Millions)



[1]OIC Policy 4.01.18, as revised September 2007.

[2]Includes impact of cash overlay management.

[3]For mandates beginning after January 1 (or with lagged performance), YTD numbers are "N/A". Performance is reflected in Total OPERF.

Returns for periods ending 5/31/2010 **Oregon Public Employees Retirement Fund**

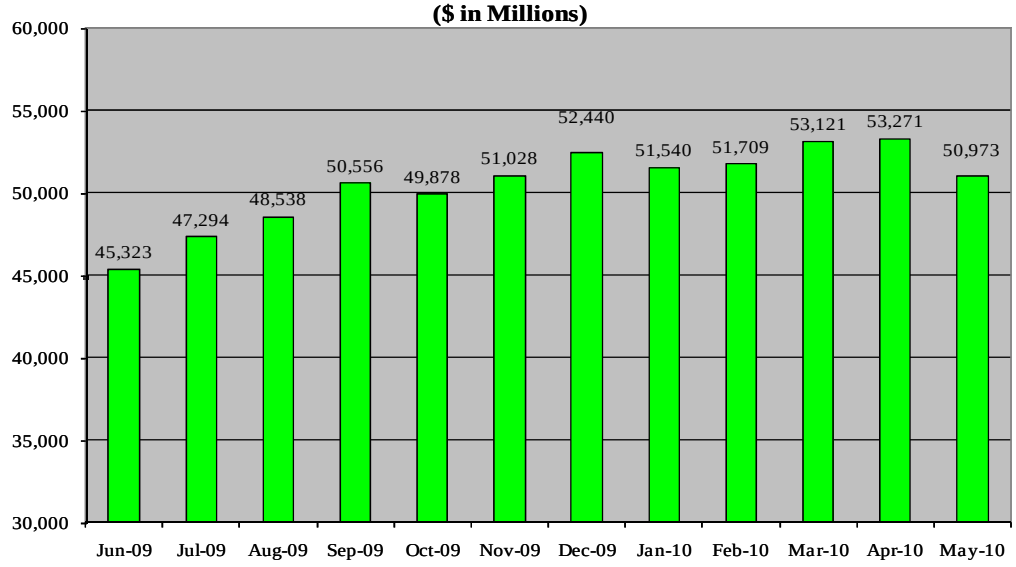
A.2.c.
May 2010

OPERF	Policy[1]	Target[1]	$ Thousands[2]	Actual	Year-To-Date[3]	1 YEAR	2 YEARS	3 YEARS	4 YEARS	5 YEARS
	Regular Account				Historical Performance (Annual Percentage)					
Public Equity	41-51%	46%	$ 19,986,418	39.9%	(5.03)	17.45	(12.61)	(9.60)	(2.20)	1.83
Private Equity	12-20%	16%	10,427,253	20.8%	5.42	19.63	(4.71)	1.60	6.96	10.68
Total Equity	**57-67%**	**62%**	**30,413,671**	**60.7%**						
Opportunity Portfolio			1,013,159	2.0%	3.39	29.66	3.77	1.81		
Total Fixed	**22-32%**	**27%**	**13,958,959**	**27.9%**	4.61	19.55	8.89	6.91	7.14	5.99
Real Estate	**8-14%**	**11%**	**4,735,806**	**9.4%**	(10.31)	(3.85)	(17.41)	(11.06)	(2.96)	3.79
Cash	**0-3%**	**0%**	**-**	**0.0%**	0.40	1.45	1.30	2.39	3.14	3.29
TOTAL OPERF Regular Account		**100%**	**$ 50,121,595**	**100.0%**	(0.83)	16.59	(6.64)	(4.16)	1.28	4.03
OPERF Policy Benchmark					(1.14)	12.67	(5.70)	(3.19)	1.86	3.83
Value Added					0.31	3.92	(0.94)	(0.97)	(0.58)	0.20
TOTAL OPERF Variable Account			**$ 851,227**		(5.49)	16.50	(12.59)	(11.22)	(4.19)	(1.20)

Asset Class Benchmarks:

Russell 3000 Index	(0.32)	23.20	(9.05)	(8.24)	(1.35)	0.84
MSCI ACWI Ex US IMI Net	(9.35)	11.82	(15.18)	(9.50)	(1.13)	4.59
MSCI ACWI IMI Net	(5.64)	16.36	(12.71)	(9.30)	(1.62)	2.40
Russell 3000 Index + 300 bps--Quarter Lagged	6.58	32.47	(5.86)	(1.35)	3.34	4.54
BC Universal--Custom FI Benchmark	3.51	9.32	6.72	6.45	6.58	5.31
NCREIF Property Index--Quarter Lagged	(2.11)	(16.86)	(11.81)	(3.42)	1.24	4.75
91 Day T-Bill	0.04	0.16	0.64	1.70	2.56	2.81

TOTAL OPERF NAV
(includes variable fund assets)
One year ending May 2010
($ in Millions)



[1]OIC Policy 4.01.18, as revised September 2007.

[2]Includes impact of cash overlay management.

[3]For mandates beginning after January 1 (or with lagged performance), YTD numbers are "N/A". Performance is reflected in Total OPERF.

Returns for periods ending 4/30/2010 **Oregon Public Employees Retirement Fund**

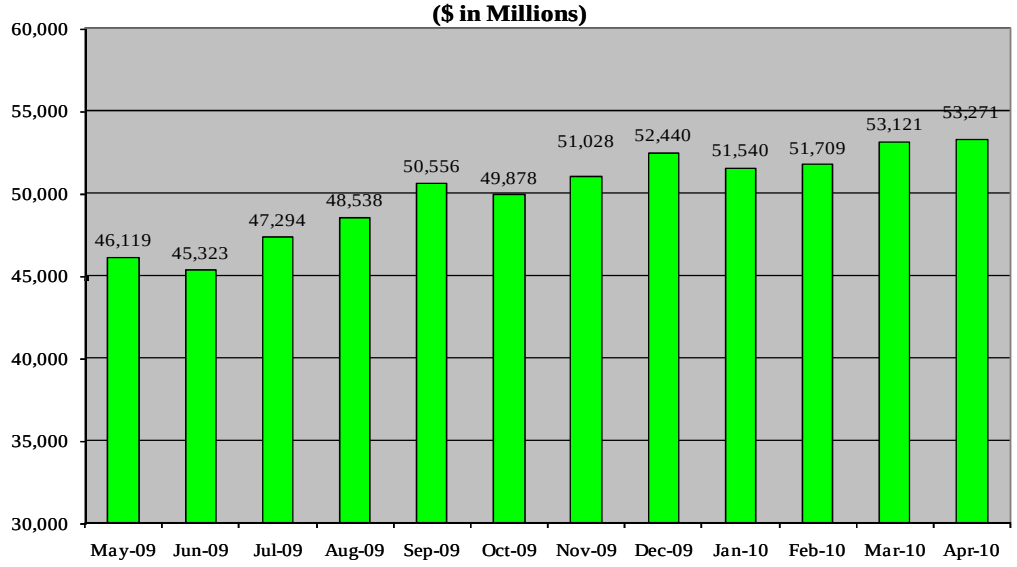
A.2.c.
April 2010

OPERF	Policy[1]	Target[1]	$ Thousands[2]	Actual	Year-To-Date[3]	1 YEAR	2 YEARS	3 YEARS	4 YEARS	5 YEARS
	Regular Account				Historical Performance (Annual Percentage)					
Public Equity	41-51%	46%	$ 22,136,488	42.3%	**4.70**	**42.23**	**(7.24)**	**(5.57)**	**(0.87)**	**4.48**
Private Equity	12-20%	16%	10,295,295	19.7%	**5.42**	**19.63**	**(4.71)**	**1.60**	**6.96**	**10.68**
Total Equity	**57-67%**	**62%**	**32,431,783**	**62.0%**						
Opportunity Portfolio			1,118,982	2.1%	**2.53**	**41.48**	**3.51**	**1.53**		
Total Fixed	**22-32%**	**27%**	**13,769,164**	**26.3%**	**5.56**	**24.43**	**9.08**	**7.03**	**7.34**	**6.44**
Real Estate	**8-14%**	**11%**	**5,006,027**	**9.6%**	**(8.92)**	**(1.15)**	**(16.79)**	**(10.63)**	**(2.77)**	**4.30**
Cash	**0-3%**	**0%**	**4,710**	**0.0%**	**0.40**	**1.87**	**1.37**	**2.53**	**3.24**	**3.35**
TOTAL OPERF Regular Account		**100%**	**$ 52,330,666**	**100.0%**	**3.61**	**28.18**	**(4.16)**	**(2.21)**	**1.73**	**5.40**
OPERF Policy Benchmark					**3.22**	**23.32**	**(3.38)**	**(1.25)**	**2.43**	**5.10**
Value Added					**0.39**	**4.86**	**(0.78)**	**(0.96)**	**(0.70)**	**0.30**
TOTAL OPERF Variable Account			**$ 939,966**		**4.28**	**41.13**	**(7.29)**	**(7.27)**	**(2.68)**	**1.56**

Asset Class Benchmarks:

Russell 3000 Index	8.23	40.90	(4.26)	(4.56)	(0.12)	3.28
MSCI ACWI Ex US IMI Net	1.46	42.51	(9.49)	(5.18)	0.50	7.10
MSCI ACWI IMI Net	4.28	41.45	(7.41)	(5.27)	(0.16)	4.91
Russell 3000 Index + 300 bps--Quarter Lagged	6.58	32.47	(5.86)	(1.35)	3.34	4.54
BC Universal--Custom FI Benchmark	2.98	9.76	6.09	6.04	6.42	5.44
NCREIF Property Index--Quarter Lagged	(2.11)	(16.86)	(11.81)	(3.42)	1.24	4.75
91 Day T-Bill	0.02	0.15	0.64	1.84	2.66	2.86

TOTAL OPERF NAV
(includes variable fund assets)
One year ending April 2010
($ in Millions)



[1]OIC Policy 4.01.18, as revised September 2007.

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PERS Oregon Public Employees Retirement System

Oregon

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July 23, 2010

TO: Members of the PERS Board

FROM: Paul R. Cleary, Director

SUBJECT: Employer Reporting Update

PERS is currently working with 897 employer-reporting units to process all outstanding employer reports and suspended records. In addition, PERS continues to monitor all employer accounts receivables and conduct its Employer Outreach Program.

EMPLOYER REPORTING

The table below shows the status as of June 30, 2010 of employer reports and member records for calendar years 2008, 2009, and 2010.

	CY 2008	CY 2009	CY 2010
Reports due:			
▪ Number expected	13,113	13,256	5,876
▪ Number received	13,093	13.238	5,793
▪ Percent received	99.85%	99.75%	98.59%
▪ Goal	99.0%	99.0%	
Reports fully posted at 100%:			
▪ Number	12,870	12,459	4,951
▪ Percent fully posted at 100%	98.15%	93.99%	84.26%
▪ Goal	95.0%	95.0%	
Records due (estimated)	3,697,968	3,528,993	1,599,611
Records not posted:			
▪ Number	2,627	13,478	35,008
▪ Percent not posted	≤ .1%	0.38%	2.19%
▪ Goal	≤ .2%	≤ .2%	
Contributions posted	$ 483,439,547	$ 504,372,921	$ 238,981,115
Contributions not posted	$ 21,861	$ 617,668	$ 1,454,343

As of June 30, 2010 employers have submitted approximately 98.59% of the reports due for 2010. Of the total reports expected, approximately 84.26% are 100% posted.

There are 83 missing reports distributed across 33 employers so far in 2010. For previous full calendar years, there are 33 missing reports across 6 employers in 2009 and 20 missing reports across 6 employers in 2008.

Since April 2010 the Employer Service Center has implemented an escalation process to identify and contact chronic late reporters. The testing of the escalation process included 4 employers and resulted in a 100% percent success rate in collecting data from the employers missing reports. 75% percent of the employers were in full compliance within 45 days of the first communicated request. One employer in the test group required a physical audit to capture the missing data. All data captured from this physical audit will be entered to the system and invoiced by August 19, 2010.

PERS is in the process of negotiating a contract with the Employment Department to provide wage records and hours for employers with missing data. The Employment Department maintains a data base load of 48 months data in a cycle. A data transfer from their system will allow PERS to provide estimated invoices to employers who are missing reports. This process will automate the audit process resulting in cost savings as well as a decreased turn around time for collecting missing data and revenues.

EMPLOYER OUTREACH PROGRAM

The Spring 2010 Employer Outreach presentation series concluded May 27, 2010. The Spring 2010 series consisted of 31 presentations including a special presentation for Southern Oregon ESD, and two specialized presentations done for charter school groups on the steps to become PERS-participating employers. All but two of the 31 presentations were given between March 26, 2010 and May 27, 2010. Attendance for the entire series totaled 312 individuals representing 239 employers.

The primary focus of the 2010 presentation cycle was review of eligibility rules introduced in 2007, and reporting retirees who return to work. This was the first formal review of eligibility rules since 2008, and questions received by the Employer Service Center staff indicated the growing necessity of eligibility rules review. Reporting retirees who return to work part-time provide consistent challenges for employers, and a review of this topic has been included in each outreach presentation series.

EDX employer training at the PERS headquarters continues, with 47 attendees representing 29 employers having attended to date. EDX employer training through the internet has also been provided to 6 attendees representing 6 employers to date whose location precluded attending training at the PERS headquarters. We hope to integrate EDX employer training through the internet into the EDX training regularly offered at the PERS headquarters, presenting remotely located employers frequent opportunity for EDX employer training. Employer EDX training is designed to equip employer staff responsible for PERS reporting with the basic skills necessary to report wages, hours, contributions and demographic information for their employees. The training comprises a review of EDX basic concepts, and "hands-on" exercise in which those concepts are put into action by creating EDX reports for an imaginary employee, and a review of reporting topics such as the most common EDX errors, eligibility rules and reporting retirees returning to work part-time.

ACCOUNTS RECEIVABLE PLAN

Besides assisting employers with overdue reports and electronic payments, PERS' accounts receivable department proactively collects receivable balances that are more than 30 days overdue. As of June 30, 2010 we had 154 outstanding invoices (36 total employers, 16 of which are charter schools) with an aggregate balance of $527,141.74. Our goal is to collect all outstanding invoices that exceed 30 days by following up with these employers by phone and letters each month.

The current total of invoices that are over 90 days delinquent is $527,141.74**.**
The majority of these past due invoices is the balance of charter schools invoiced for $371,406.69. PERS and Rick Slater, a representative of a group of the charter schools formerly reported by TPA EdChoices, will meet 7/20/10 to review the outstanding balances and discuss payment collection strategies for this particular group of nine charter schools.

Canby Fire District #62 is our next largest group of outstanding invoices. The employer is working diligently with PERS on repayments of invoices totaling $103,155.68.

The improvements over the March 2010 report include:

- Young Case outstanding invoice total reduced to $14,595.82 from $130,784.02.
- Tillamook Soil and Water Conservation District is paid in full.
- Services to Children and Families outstanding invoice total reduced to $4,491 from $113,507.80.

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July 23, 2010

TO: Members of the PERS Board

FROM: Dale S. Orr, Actuarial Services Manager

SUBJECT: Quarterly Report of Member Transactions

Attached is the PERS Quarterly Report of member transactions with the results from second calendar quarter of 2010.

This report reflects incoming, completed and pending workload for five key agency activities. This information is being provided to assist the Board in monitoring the general workload demands and performance of PERS' operations. The report provides a breakout of activity on both a quarterly and a cumulative, calendar year-to-date basis.

In addition, the 'Retirements', 'Withdrawals', and 'Estimates' activities reflect the combined statistics of Tier One, Tier Two and OPSRP pension. Pending counts do not necessarily reflect a backlog of work, but rather the normal end-of-quarter carry-over of items in the processing pipeline.

Supplemental information to assist in understanding the report are as follows:

1. **Pending Retirement Increase.** The number of pending 'Retirements', (Tier One, Two and OPSRP), and 'IAP Retirements', increased significantly in the second quarter due to the usual seasonal spike in July 1, retirements. Typically, 25% to 30% of all annual retirements occur as of July 1 of each year. If historical patterns hold, a significant decline in the pending numbers for these activities will occur in the third quarter as the large volume of July 1 retirements are calculated and paid.

2. **'Estimates' Backlog.** As of the end of the second quarter, Tier One and Tier Two estimates were in backlog status. A backlog occurs when the number of pending estimates exceeds twice the normal amount of work-in-process. This backlog was the result of a series of events. The RCP conversion of pre-retirement functions from RIMS to jClarety caused a halt in estimate production for three weeks in 2009. The learning curve to effectively use the new estimate systems resulted in further erosion in production. Backlog growth has now been halted and some progress in its reduction is being achieved. Staff has prioritized resources to providing estimates to those members with the nearest anticipated retirement dates. Currently, members requesting an estimate with a retirement date within 90 days or less have received an estimate. This time horizon will be expanded as the backlog continues to be reduced.

3. **Derived Pending Numbers.** A few of the pending totals, such as those for the 'Estimate' activity, are derived by adjusting the previous quarter's pending amount by the current quarter's incoming and completed. To gain a precise number of pending estimates, for instance, requires staff to conduct a manual count. Due to the time involved, a manual verification is done only once per year. As a result, some pending numbers will be periodically adjusted to reflect the fine-tuning of the pending totals to reflect the actual count. These adjustments are not expected to be significant and the Board will be notified when the adjustments occur.

The next Quarterly Board Report, reflecting the results from the third calendar quarter of 2010, is scheduled to be presented at the November Board meeting.

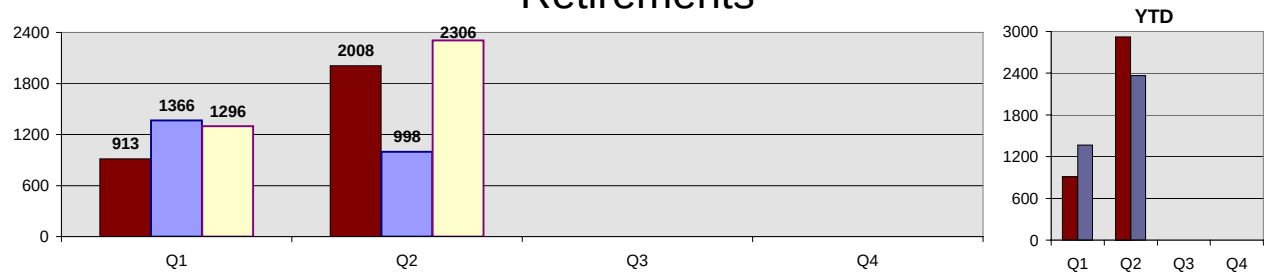
Attachment:

PERS Quarterly Board Report (Through Second Quarter, 2010)

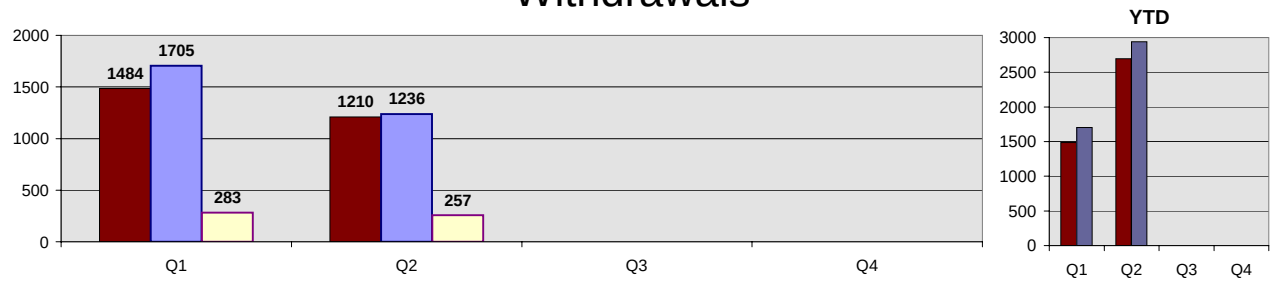
PERS Quarterly Board Report

Through Second Quarter - 2010 Run Date: 7/20/2010

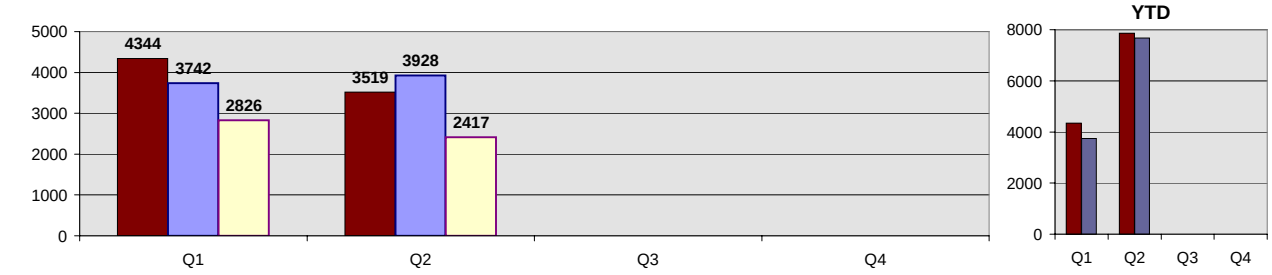
Retirements



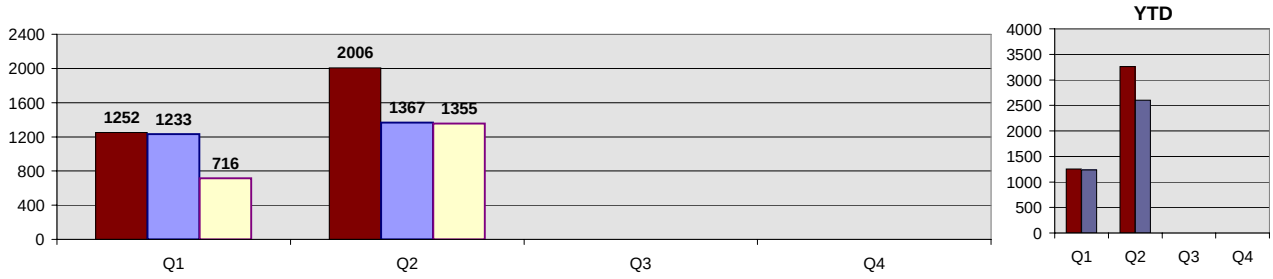
Withdrawals



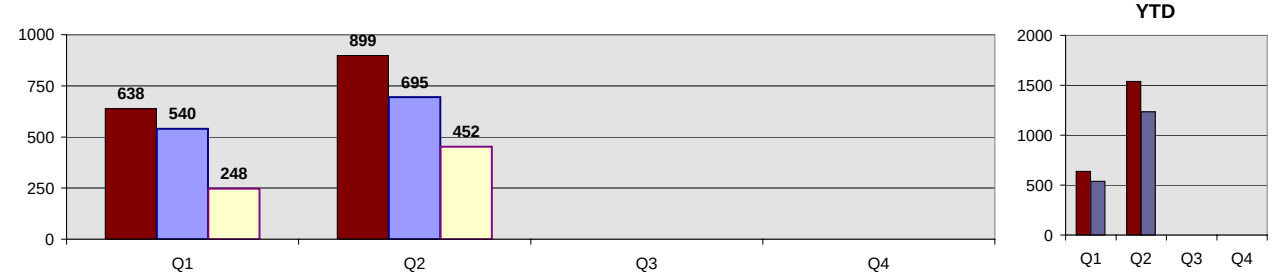
Estimates



IAP Retirements



IAP Withdrawals



Incoming Completed Pending

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July 23, 2010

TO: Members of the PERS Board

FROM: Steven Patrick Rodeman, Deputy Director

SUBJECT: 2011 Legislative Concepts Update

PERS staff submitted Legislative Concept 45900-002 as a placeholder. This concept addresses the issue of OPSRP Pension Program withdrawals. Since this was a placeholder concept, staff was required to follow up by July 14, 2010, with draft language and further supporting materials.

This concept was discussed during the April 29, 2010 meeting of the Legislative Advisory Committee and staff was asked to further develop the options and present them to the Committee. On June 16, 2010, Susan Riswick distributed the attached memo to the Committee with further discussion and a staff recommendation of the concept to be drafted. We requested that any comments be made by June 25, 2010; no members of the Committee submitted comments.

As a result, staff submitted the necessary materials to designate Option #1 (eliminate IAP waiting time on reemployment) as described in the attached memo as the substantive choice for Legislative Counsel to draft under this concept. That concept, as well as the other two concepts staff submitted, will be returned to the PERS Board for their review and consideration at the November 19, 2010 meeting. Those concepts which the PERS Board approves at that meeting will then be submitted to the Governor to consider introducing in the 2011 legislative session.

A.2.f. Attachment 1 – June 16, 2010 Memo on PERS Legislative Concept 45900-002

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June 16, 2010

TO: Members of the PERS Legislative Advisory Committee

FROM: Susan Riswick, Administrator, PPLAD

SUBJECT: 2011 PERS Legislative Concept #LC 45900-002
OPSRP Program Pension Withdrawal Restrictions

BACKGROUND

An OPSRP Pension Program member who leaves PERS-covered employment may withdraw only if the member is vested and the present value of the member's pension is $5,000 or less. That member may, however, withdraw from the Individual Account Program (IAP) without restriction. When a member withdraws from the IAP but is unable to withdraw from OPSRP Pension, they are no longer a member of the IAP but retain their OPSRP Pension membership. If the member subsequently returns to PERS-covered employment, the employee is required to serve another waiting time to establish membership in the IAP but remains as an OPSRP Pension member from the date of re-employment. This "dual status" (member of the OPSRP Pension program but not the IAP) creates irresolvable administrative issues, e.g., employee IAP contributions should not begin until the employee reestablishes active membership in the IAP, but OSPRP Pension employer contributions should start immediately upon reemployment. This "dual status" problem only exists with the OPSRP Pension Program; there are no similar restrictions on withdrawal from the Tier One/Tier Two program. PERS staff has requested that a legislative concept be developed resolving the "dual status" issue caused by these inconsistent withdrawal restrictions.

ALTERNATIVE LEGISLATIVE CONCEPT APPROACHES

1) ELIMINATE IAP WAITING TIME ON REEMPLOYMENT

Amend current statute to specify that, if an OPSRP Pension member who withdrew from the IAP but could not withdraw from the pension program because of the restrictions returns to PERS-covered employment, that member does not need to serve another IAP waiting time. The reemployed member becomes active in both the OPSRP Pension Program and the IAP on the date of reemployment. This option adds six (6) months of employee contributions to the IAP during what is currently the IAP waiting period and, if the employer makes optional employer contributions, this option would result in additional contributions being made. This option does not require any changes to the agency's current system programming.

2) ADDITIONAL OPSRP PENSION PROGRAM WAITING TIME ON REEMPLOYMENT

Amend the current statute to require a “dual status” member to serve another OPSRP Pension Program waiting time to parallel the IAP waiting time upon returning to PERS-covered employment. Employee and employer contributions would not begin until the second pension waiting time is completed. Presumably, the statute would also specify that retirement credit will be granted for the second waiting time in the same manner as for the original pension waiting time under ORS 238A.140. Also, the hours served during the "second waiting time" are hours of service, so there is no loss of hours of service for vesting purposes. However, the salary attributable to the second waiting time will not count toward Final Average Salary. This option would require programming changes to the agency’s current system.

3) REMOVE THE VESTING AND PRESENT VALUE CONDITIONS FOR OPSRP PENSION WITHDRAWALS

This option would amend statute to remove the restrictions on OPSRP Pension Program withdrawals. A member would then be required to withdraw from the OPSRP Pension Program when they withdraw their IAP account. The effect is that a vested member is eligible to withdraw the present value of the pension, regardless of its value, and a non-vested member forfeits their OPSRP Pension Program membership when they withdraw their IAP. This option requires programming changes to the agency’s current system.

4) FORFEITURE OF OPSRP PENSION MEMBERSHIP UPON IAP WITHDRAWAL

One option discussed with the Legislative Advisory Committee was to parallel the administration of withdrawals from the Tier One/Tier Two Program and have the OPSRP Pension benefit be forfeited when the member withdraws from the IAP regardless of the present value. Further research has concluded that this option is not legally administrable by PERS. An OPSRP Pension Program member who withdraws their IAP account would forfeit all OPSRP retirement credit and terminate membership in OPSRP. This option would be inconsistent with federal tax law which specifies that a vested interest is a non-forfeitable right and cannot be taken away. Furthermore, this option would create the dichotomy where an OPSRP Pension member is paid the present value of their benefit upon withdrawal if that value is less than $5000 but if more than that amount, it’s forfeited.

STAFF RECOMMENDATION

Staff is recommending Option #1.

- Reason: This option requires no additional programming and resolves the administrative challenge of “dual status” in the system. This option also creates a consistent standard for waiting time requirements upon re-employment of an OPSRP member who retained their OPSRP Pension program membership when they withdrew their IAP.

NEXT STEPS

PERS staff would appreciate the comments and feedback from LAC members on the alternate approaches and proposed staff recommendation by **June 25, 2010**. The concept was filed as a placeholder and must be submitted in final form to Legislative Counsel before July 14, 2010, so this deadline would allow staff to complete their analysis before that final submission for drafting.

PERS Oregon Public Employees Retirement System

Oregon

Theodore R. Kulongoski, Governor

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July 23, 2010

TO: Members of the PERS Board

FROM: Steven Patrick Rodeman, Deputy Director

SUBJECT: Notice of Senate Bill 897 Data Verification Rules

OAR 459-005-0040, *Verification of Retirement Data*

OVERVIEW

- Action: None. This is notice that staff has begun rulemaking.
- Reason: Clarification and implementation of the data verification provisions of Senate Bill 897.
- Policy Issues:
  1. What constitutes a reasonable time for employers to confirm or modify employee records?
  2. Should all data in the verification be as of the same date or should different dates be used for different data elements?
  3. When should PERS allocate non-recoverable erroneous payments and overpayments attributable to its errors?

BACKGROUND

Senate Bill 897 requires PERS to verify certain retirement data upon an eligible member's request. Under the bill, PERS must notify the member's employers of the request and give those employers a reasonable time to confirm or modify the data previously reported to PERS. After this verification process, the member's employer may not later modify that data. PERS will then produce a verification based on the reported data. With some exceptions, PERS is restricted from using anything less than the verified amounts to calculate the member's service retirement benefit. The proposed rule clarifies standards for implementation and administration of verifications and incorporates several policy decisions necessary for completing implementation.

POLICY ISSUES

1. *What constitutes a reasonable time for employers to confirm or modify employee records?*

PERS cannot derive the data to be verified until the employer's opportunity to modify that data has closed; otherwise, the work would have to be re-done if the employer changes the records. To permit PERS adequate time to reconcile the account and provide the member a verification in a timely manner, the proposed rule at section (2) establishes a period of 60 days. An employer may confirm or modify records at any time during the 60 day period. This standard has been discussed at an Employer Advisory Council meeting and a Legislative Advisory Committee meeting. Though formal consensus has not been reached by either body, the general feeling from

employer representatives was "the longer the better." However, there was no broad opposition to a 60 day standard.

2. *Should all data in the verification be as of the same date or should different dates be used for different data elements?*

Historically, PERS employers have reconciled their employer reports after the close of a calendar year. The "annuals" process allows employers to clean up any records from the prior calendar year during the first few months of the subsequent year. Once annuals closes, the member's records are ready for annual earnings crediting and deriving other data elements, such as creditable service, vesting, etc., and financial records are closed for that calendar year. Typically, the last step in this process is applying the annual earnings crediting rate to member accounts so that their prior year's closing balance can be determined and annual statements generated.

Data that would be included in a verification is therefore subject to change during the course of a calendar year, but is routinely brought to closure as of the end of a calendar year. During this processing time, certain information, such as annual earnings crediting rates, are not available as they have not yet been determined. Providing data elements as of different dates would make a verification less meaningful for members and more difficult to adapt to the online benefit estimator. The proposed rule, at section (3)(a), provides that all verified data will be as of a date certain, December 31 of the last year for which earnings crediting has been adopted, to enhance the accuracy and utility of the verification.

3. *When should PERS allocate non-recoverable erroneous payments and overpayments attributable to its errors?*

Senate Bill 897 provides that erroneous payments and overpayments that would result if verified data were corrected may only be charged to administrative expenses or to the contingency reserve. The proposed rule, at section (5), notes that the Board will allocate these payments annually; staff will present a recommendation during the annual earnings crediting process as to where such payments, if any, should be allocated depending on the nature of the payment(s) in question and the fund's status at that time.

ADDITIONAL OPERATIONAL PROVISIONS

In addition to these policy questions, the proposed rule clarifies some operational aspects of the verifications. For example, the last clause in section (2) explains that an employer may be directed by PERS staff to modify records after they have been confirmed. Account reconciliation regularly requires staff to communicate with employers to clarify employee records and employers frequently adjust reported data at PERS' request to permit accurate reconciliation.

Section (3)(b) specifies that, if a member requests an additional verification, the verification will be based on information from the date of the last verification. The first verification will have closed the data used to develop it and foreclosed the employer's opportunity to change the records and the member's opportunity to challenge them. Reopening completed verifications is inconsistent with the finality sought by the verification process. For these reasons, the proposed rule provides that subsequent verifications will only cover data based on periods after the date specified in the previous verification.

Section (4) of the proposed rule also explains some situations where verified data may change because of subsequent actions. Senate Bill 897 provides that amounts in a verification may be adjusted for service credit accruals, earnings and losses, and salary and sick leave attributable to periods after the date specified in the verification. This statutory provision recognizes that transactions occurring after a verification may affect the data in the verification and must be acknowledged to produce an accurate retirement benefit.

This portion of the proposed rule explains that adjustment of the amounts in a verification may also occur for other transactions initiated by a member or of which the member would be aware. A Tier Two member may restore Tier One membership by voluntary redeposit or purchase at retirement, affecting earnings crediting, account balances, service credit, and final average salary. Under USERRA, in certain circumstances a member who withdraws during military service must be permitted to repay the distribution, which also may affect membership status and other data elements. A member's data may be retroactively affected by a judgment, administrative order, arbitration award, conciliation agreement, or settlement agreement. A member's account balance may be adjusted to reflect the division of the account pursuant to a divorce decree. These adjustments occur because of transactions that are either under the control of the member or within the member's expectations, but their effect on a verification may not be clear, so they're added to the rule to make sure members understand that they might change the outcome of a verification by these specific actions.

PUBLIC COMMENT AND HEARING TESTIMONY

A rulemaking hearing will be held on August 24, 2010 at 1:00 p.m. at PERS headquarters in Tigard. The public comment period ends on September 3, 2010 at 5:00 p.m.

LEGAL REVIEW

The attached draft rule was submitted to the Department of Justice for legal review and any comments or changes will be incorporated before the rule is presented for adoption.

IMPACT

Mandatory: Yes, the statute provides for implementation of employer confirmation of employment data "In a manner specified by the rules of the board…." Other aspects of the rule are not mandatory but necessary to implement the statute and clarify its administration.

Impact: Members, employers, and staff will benefit from clarification of the administration of verifications.

Cost: There are no discrete costs attributable to the rule.

RULEMAKING TIMELINE

June 15, 2010	Staff began the rulemaking process by filing Notice of Rulemaking with the Secretary of State.
July 1, 2010	*Oregon Bulletin* published the Notice. Notice was mailed to employers, legislators, and interested parties. Public comment period began.

July 23, 2010	PERS Board notified that staff began the rulemaking process.
August 24, 2010	Rulemaking hearing to be held at 1:00 p.m. in Tigard.
September 3, 2010	Public comment period ends at 5:00 p.m.
September 24, 2010	Staff will propose adopting the permanent rule modifications, including any changes resulting from public comment or reviews by staff or legal counsel.

NEXT STEPS

A hearing will be held on August 24, 2010 at PERS Headquarters in Tigard. The rule is scheduled to be brought before the PERS Board for adoption at the September 24, 2010 Board meeting.

B.1. Attachment 1 – 459-005-0040, *Verification of Retirement Data*

OREGON ADMINISTRATIVE RULE
PUBLIC EMPLOYEES RETIREMENT BOARD
CHAPTER 459
DIVISION 5 – ADMINISTRATION

459-005-0040

Verification of Retirement Data

(1) For purposes of this rule:

(a) "Eligible member" means an active or inactive member of the system who is within two years of earliest service retirement age. "Eligible member" does not include a member retired for service or disability, an alternate payee, or a beneficiary.

(b) "Verification" means a document provided to an eligible member by PERS pursuant to section 3, chapter 1, Oregon Laws 2010.

(2) Upon receipt of a request for a verification from an eligible member, PERS will notify the member's employer(s) of the request. PERS will base the verification on the employer's reporting of the eligible member's creditable service, retirement credit, final average salary, member contributions, and accumulated unused sick leave as reflected in PERS' records on the 61st day after the notice is issued, or an earlier date if the employer confirms the records before the 61st day in a manner specified by PERS. An employer may not modify an eligible member's records after the earlier of the 61st day or the date the records are confirmed except as directed by PERS to reconcile the member's records for the verification.

(3) For any verification provided by PERS:

(a) All data in a verification will be as of December 31 of the last calendar year before the date PERS received the member's request for which the Board has adopted annual earnings crediting.

(b) If an eligible member requests an additional verification, the verification will provide data based only upon periods after the date specified in the most recent verification.

(4) When a member who has received a verification retires for service, PERS may not use amounts less than the amounts verified to calculate the member's retirement allowance or pension, except as permitted in section 3(3), chapter 1, Oregon Laws 2010, and this section.

(a) If a Tier Two member restores forfeited creditable service and establishes Tier One membership in the manner described in ORS 238.430(2)(b), the amounts in any verification provided before the restoration will be adjusted and the verification reissued by PERS as of the date specified in the original verification.

(b) Amounts in a verification may be adjusted to comply with USERRA.

(c) Amounts in a verification may be adjusted to implement a judgment, administrative order, arbitration award, conciliation agreement, or settlement agreement.

(d) If subsequent to the date specified in a verification a member's account is divided pursuant to ORS 238.465, the member and alternate payee accounts will be used to determine compliance with section 3(3), chapter 1, Oregon Laws 2010 and this section.

(5) Erroneous payments or overpayments not recoverable under section 3(6), chapter 1, Oregon Laws 2010 will be allocated annually by the Board.

Stat. Auth.: ORS 238.650, 238A.450

Stats. Impl.: Sections 2-4, chapter 1, Oregon Laws 2010 (Enrolled Senate Bill 897)

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July 23, 2010

TO: Members of the PERS Board

FROM: Steven Patrick Rodeman, Deputy Director

SUBJECT: Notice of Retire From One, Retire From All Rule

OAR 459-080-0260, *Distribution of IAP Accounts at Retirement*

OVERVIEW

- Action: None. This is notice that staff has begun rulemaking.
- Reason: A new rule is needed to clarify the provisions of ORS 238A.400, "Payment of accounts at retirement."
- Policy Issue: Whether PERS should adopt a standard that requires retirement from the IAP at the time a member retires from their other retirement program?

BACKGROUND

The 2003 PERS Reform legislation created the Individual Account Program (IAP) and directed that all members participate, creating a dynamic where every PERS member is in at least two programs. Subsequent amendments, such as the repeal of "Break-in-Service," and agency actions, like IAP remediation, have addressed some of the complications arising from this dual membership. The proposed new rule attempts to address another complication: retiring from one program but not the other.

IAP retirement eligibility is set forth in ORS 238A.400. This eligibility is not independent, but instead is predicated on the IAP member's eligibility to retire under their other retirement program. A member of the OPSRP Pension Program may begin distribution of IAP benefits "Upon retirement…" from the pension program. (ORS 238A.400(1)). Similarly, a member of the PERS Chapter 238 Program may begin distribution of IAP benefits at the time the member "…retires for service under the provisions of ORS chapter 238." (ORS 238A.400(4)).

Historically, PERS has allowed members to retire from their two programs separately, e.g., commence their OPSRP Pension retirement and leave their IAP account until they make the separate decision to retire from that account. This policy has resulted in complications because members are not in the same status in both programs: they could be retired members for the OPSRP Pension program but inactive members in the IAP. If such a member were to return to part-time employment, for example, their OPSRP retired status would mean one set of reporting standards, but their IAP status could compel another.

POLICY ISSUE

Whether PERS should adopt a standard that requires retirement from the IAP at the time a member retires from their other retirement program?

Another action that addressed the administrative complications arising from dual membership was the 2007 Oregon Legislature's passage of HB 2281, a PERS Board legislative concept that requires a member who withdraws from one program to withdraw from them all. That bill became effective January 1, 2008. This proposed new rule applies that same principle to the time of the member's retirement.

Because the IAP retirement statute is predicated on retirement from the member's other program, the proposed new rule embodies the policy decision made by the legislature as it relates to a member's withdrawal by extending that same policy to the time of retirement. The rule would clarify that retirement from the IAP can begin only at the time the member retires from their other retirement program. Staff recommends adoption of a "retire from one, retire from all" standard to resolve the administrative complications arising from dual memberships and to more closely follow the statutory directives on when IAP retirement should commence.

Also, the proposed new rule establishes that a member retired for disability under the PERS Chapter 238 Program may begin distribution of their IAP account(s) upon reaching earliest service retirement age. Obviously, a Chapter 238 disability retirement can occur at any age and is not an elective decision by the member, so a "retire from one, retire from all" standard has to accommodate for a later distribution since that member may never retire for service. Disability benefits under the OPSRP Pension Program, however, are not retirement benefits and a recipient is not a retired member. Those disability benefits cease when the member reaches normal retirement age. That member may then retire for service and this rule would compel that they begin IAP benefits at that time.

Judge members are excluded from the rule because they do not participate in the IAP for their judge member service. Legislators are excluded because they are one group that could still have concurrent membership in OPSRP and PERS Chapter 238 (unless and until the proposed 2011 legislative concept is adopted).

The effective date of the rule is delayed until January 1, 2011 to permit PERS to inform members and to generate the forms and procedures necessary. Members who retire or have retired from only one program before the effective date of the rule will be contacted and given the opportunity to begin IAP distribution.

PUBLIC COMMENT AND HEARING TESTIMONY

A rulemaking hearing will be held on August 24, 2010 at 1:00 p.m. at PERS headquarters in Tigard. The public comment period ends on September 3, 2010 at 5:00 p.m.

LEGAL REVIEW

The attached draft rule was submitted to the Department of Justice for legal review and any comments or changes will be incorporated before the rule is presented for adoption.

IMPACT

Mandatory: No, the Board need not adopt the rule, but the statutory provisions must be implemented and the rule clarifies that implementation.

Impact: The rule clarifies and simplifies retirement administration.

Cost: There are no discrete costs attributable to the rule.

RULEMAKING TIMELINE

June 15, 2010	Staff began the rulemaking process by filing Notice of Rulemaking with the Secretary of State.
July 1, 2010	*Oregon Bulletin* published the Notice. Notice was mailed to employers, legislators, and interested parties. Public comment period began.
July 23, 2010	PERS Board notified that staff began the rulemaking process.
August 24, 2010	Rulemaking hearing to be held at 1:00 p.m. in Tigard.
September 3, 2010	Public comment period ends at 5:00 p.m.
September 24, 2010	Staff will propose adopting the permanent rule, including any changes resulting from public comment or reviews by staff or legal counsel.

NEXT STEPS

A hearing will be held on August 24, 2010 at PERS Headquarters in Tigard. The rule is scheduled to be brought before the PERS Board for adoption at the September 24, 2010 Board meeting.

B.2. Attachment 1 – 459-080-0260, *Distribution of IAP Accounts at Retirement*

PERS Oregon Public Employees Retirement System

OREGON ADMINISTRATIVE RULE
PUBLIC EMPLOYEES RETIREMENT BOARD
CHAPTER 459
DIVISION 080 – OPSRP INDIVIDUAL ACCOUNT PROGRAM

459-080-0260

Distribution of IAP Accounts at Retirement

(1) Except as provided in this rule, distribution under ORS 238A.400 of a member's Individual Account Program (IAP) account(s) at retirement shall begin only at the time the member retires for service under the PERS Chapter 238 Program or OPSRP Pension Program.

(2) A member of the IAP who is retired for disability under the PERS Chapter 238 Program may begin distribution of the member's IAP accounts upon reaching earliest service retirement age.

(3) This rule does not apply to a member who retires for service as a judge member or legislator.

(4) This rule is effective January 1, 2011.

Stat. Auth.: ORS 238A.450

Stats. Impl.: ORS 238A.400

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July 23, 2010

TO: Members of the PERS Board

FROM: Steven Patrick Rodeman, Deputy Director

SUBJECT: Adoption of Disability Rules

OAR 459-015-0030, *Hearings on Denial or Discontinuance of Disability Retirement Allowances*
OAR 459-015-0055, *Selection of Benefit Option and Commencement of Allowance*

OVERVIEW

- Action: Adopt modifications to disability hearings and benefits rules.
- Reason: Align the standards set forth in the administrative rule for disability proposed orders and non-disability proposed orders, and clarify the payment of a disability retirement allowance and selection of a disability benefit option.
- Policy Issue: No policy issues have been identified.

BACKGROUND

OAR 459-015-0030, *Hearings on Denial or Discontinuance of Disability Retirement Allowances*

In 2008, PERS adopted changes to OAR 459-001-0035, Contested Case Hearing. The rule modifications were made to conform to DOJ model rules and to eliminate overlap and duplicative authorities. When those changes were made, similar changes should have been made to OAR 459-015-0030. In section (4), language is deleted as it is covered by the Office of Administrative Hearing (OAH) procedural rules. The new language in section (4) reflects section (10) of OAR 459-001-0035. Minor edits were made to sections (5) and (6).

OAR 459-015-0055, *Selection of Benefit Option and Commencement of Allowance*

The proposed rule modifications clarify when a disability payment is due, and that the time period of when payment a disability retirement allowance shall commence refers to business days, not calendar days. Other changes to the rule include eliminating redundant language and clarifying that, if a member's disability retirement allowance is canceled before the first benefit payment or is discontinued, the benefit option selected for that disability retirement allowance is canceled and a different option may be selected upon a subsequent retirement.

SUMMARY OF MODIFICATIONS TO RULES SINCE NOTICE

Staff has made no further changes to the proposed rule modifications since these rules were previously distributed.

PUBLIC COMMENT AND HEARING TESTIMONY

A rulemaking hearing was held on May 25, 2010 at 1:00 p.m. at PERS headquarters in Tigard. No members of the public attended. The public comment period ended on June 4, 2010 at 5:00 p.m. No public comment was received.

LEGAL REVIEW

The attached draft rules were submitted to the Department of Justice for legal review and any comments or changes are incorporated in the rules as presented for adoption.

IMPACT

Mandatory: Yes, in part. Changes to OAR 459-015-0030 are needed to eliminate overlap and duplicative authorities.

Impact: Clarification of the hearings process.

Cost: There are no discrete costs attributable to the rules.

RULEMAKING TIMELINE

April 15, 2010	Staff began the rulemaking process by filing Notice of Rulemaking with the Secretary of State.
May 1, 2010	*Oregon Bulletin* published the Notice. Notice was mailed to employers, legislators, and interested parties. Public comment period began.
May 21, 2010	PERS Board notified that staff began the rulemaking process.
May 25, 2010	Rulemaking hearing held at 1:00 p.m. in Tigard.
June 4, 2010	Public comment period ended at 5:00 p.m.
July 23, 2010	Board may adopt the permanent rule modifications.

BOARD OPTIONS

The Board may:

1. Pass a motion to adopt modifications to these rules as presented.
2. Direct staff to make other changes to the rules or explore other options.

STAFF RECOMMENDATION

Staff recommends the Board choose Option #1.

- Reason: Align the standards set forth in the administrative rule for disability proposed orders and non-disability proposed orders, and clarify the payment of a disability retirement allowance and selection of a disability benefit option.

If the Board does not adopt: Staff would return with rule modifications that more closely fit the Board's policy direction if the Board determines that a change is warranted.

C.1. Attachment 1 – 459-015-0030, *Hearings on Denial or Discontinuance of Disability Retirement Allowances*
C.1. Attachment 2 – 459-015-0055, *Selection of Benefit Option and Commencement of Allowance*

PERS Oregon Public Employees Retirement System

OREGON ADMINISTRATIVE RULE
PUBLIC EMPLOYEES RETIREMENT BOARD
CHAPTER 459
DIVISION 015 – DISABILITY RETIREMENT ALLOWANCES

459-015-0030

Hearings on Denial or Discontinuance of Disability Retirement Allowances

(1) A final denial of an application for disability benefits, or any decision discontinuing a previously granted disability retirement allowance may be reviewed in a contested case hearing.

(2) A contested case hearing may be requested by a member by filing with the Board a written request as provided for in OAR 459-001-0035.

(3) The contested case hearing shall be heard before an administrative law judge designated by the Office of Administrative Hearings and conducted in accordance with the Attorney General's Model Rules of Procedure as adopted by OAR 459-001-0005. The member may represent himself**/herself** or be represented by legal counsel. An Assistant Attorney General will appear at the hearing to assist the staff in presenting its position, and to assist in the development of a complete hearing record.

(4) The Board generally deliberates and decides on final orders during regularly scheduled board meetings. The Board may instead deliberate and decide at any other time and place allowed by law, as determined on a case-by-case basis, such as electronically or via a telephone conference.

(4) Following the hearing, the hearings officer shall prepare or direct one of the parties to prepare a Proposed Findings of Fact, Conclusions of Law and Order and serve it on the parties. The administrative law judge's proposed order will become final 90 days following service upon the petitioner, the Director and the Board through the Director, unless objections are filed as provided in this rule. Objections may be filed by the Director or the petitioner within 45 days of service. If the Board determines additional time is necessary to review a proposed order and

issue an amended order, the Board may extend the time after which the proposed order will become final in accordance with ORS 183.464(3).]

(5) In accordance with OAR 459-001-0040, *[prior to]* **before** initiating any judicial review of a final order, an applicant may file with the Board a petition for reconsideration.

(6) Any disputed claim concerning a disability retirement allowance or discontinuance of such allowance may be voluntarily settled on a lump-sum basis subject to recommendation of the assigned Assistant Attorney General and final approval of the Board. Settlements approved by the Board shall be paid upon receipt of a "Release and Covenant Not to Sue" signed by the applicant and *[his or her]* **the applicant's** attorney, if any.

Stat. Auth.: ORS 183.310 - 183.550, 183.600 - 183.690 & 238.650

Stats. Implemented: ORS 238.320 - 238.345

OREGON ADMINISTRATIVE RULE
PUBLIC EMPLOYEES RETIREMENT BOARD
CHAPTER 459
DIVISION 015 – DISABILITY RETIREMENT ALLOWANCES

459-015-0055

Selection of Benefit Option and Commencement of Allowance

(1) Upon filing an application for a disability retirement allowance, the member may make a preliminary designation of beneficiary and a preliminary selection of benefit option.

(a) A member may choose from retirement Options 1, 2, 2A, 3, 3A, 15 year certain or refund annuity as set forth in ORS 238.300 and 238.305, or an optional disability retirement allowance under ORS 238.325.

(b) A member may not choose a lump-sum option.

(2) Within 90 days following the Director's, or the Director's designee's, approval of the application for disability retirement allowance, the member must complete a final designation of beneficiary and selection of benefit option on forms provided by PERS. Receipt of the final forms will super*[c]***s**ede any preliminary beneficiary designation or benefit option.

(a) The final option selected applies only to the corresponding time period the member is receiving a disability retirement allowance.

(b) The beneficiary designation or benefit option may be changed up to 60 days after the date of the first **actual (not estimated)** benefit payment as provided in ORS 238.325(2). **The beneficiary or benefit option change will be retroactive to the effective disability retirement date.**

(c) If a member's disability retirement allowance is canceled **before the first benefit payment or is discontinued**, the option selected for the purposes of that disability retirement allowance is canceled and a new option may be selected upon a subsequent disability or *[a]* service retirement.

(3) If the member does not complete a final selection of benefit option within 90 days following the Director's, or the Director's designee's, approval of the application for disability retirement allowance:

(a) The benefit will be the benefit as set forth under ORS 238.320(1); and

(b) The latest beneficiary designation on file for the PERS Chapter 238 Program will be used to determine the default beneficiary. If no designation exists, the beneficiary will be as provided for under ORS 238.390(2).

(4) Purchases. If a member is eligible to purchase additional creditable service or retirement credit under ORS Chapter 238, the member must submit payment for the purchase(s) at the time the member submits the final selection of benefit option form required under section (2) of this rule.

(5) The payment of a disability retirement allowance shall commence within *[ten]* **10 business** days following receipt by PERS of all of the following items, or the date the first payment is due, as set forth in Section (6) of this rule, whichever is later:

(a) From the member:

(A) Final designation of beneficiary and selection of benefit option form;

(B) Proof of member's age;

(C) Proof of age for the designated beneficiary if a joint survivor option is elected; and

(D) Spousal consent form.

(b) From the employer:

(A) Financial; and

(B) Demographic information indicating the member has separated from PERS-covered employment.

(6) A disability payment is first due on the later of:

(a) The first of the calendar month in which the member files a complete application for disability benefits with PERS; or

(b) The first of the month following the first full calendar month after final payment by the employer of any wages or paid leave benefits to the member, excluding any cash payoff of accrued vacation or compensatory time; or

(c) The first of the calendar month following the date that the disability application is approved by the Director.

[(d)] **(7)** Notwithstanding *[sub]* section*[s (a) , (b) and (c)]* **(6)** of this *[section]* **rule**, no payment shall be made *[prior to]* **before** the end of the period of 90 consecutive days beginning with the date of disability *[as defined in OAR 459-015-0001(4);]* and **shall be retroactive to the effective date of disability.**

[(e) A disability retirement allowance shall be retroactive to the effective date of disability.]

[(7)] **(8)** If PERS cannot calculate the actual disability benefit payment, an estimated payment will be made until PERS receives all the necessary information needed to calculate the actual benefit payment. The payment will be made retroactive to the effective date of disability if the benefits become due before the 90 consecutive day period of incapacitation has elapsed.

(a) If the estimated payment results in an underpayment of $10 or more a month, the member will receive interest based on the provisions set forth in OAR 459-007-0015.

(b) If the estimated payment results in an overpayment of any amount, the overpayments may be recovered by decreasing the monthly benefit amount until the difference between the amount the member received and the amount the member should have received is recovered.

[(8) Within the 60 day period following the issue date of the first actual (not estimated) benefit payment, the member may change their benefit option. The Option change will be retroactive to the effective disability retirement date.]

(9) Minimum disability benefit. A disability benefit will not be less than $100 per month under the non-refund Option 1 benefit or the amount the member would have received for service retirement, if eligible, whichever is higher.

(10) In the event a member applying for a disability retirement allowance dies *[prior to]* **before** the Director's approval of the application:

(a)(A) If the member has made a preliminary benefit option election, the preliminary election shall be effective upon the Director's approval of the application for disability retirement.

(B) If the deceased member was eligible to purchase additional creditable service or retirement credit under ORS Chapter 238, the beneficiary, if any, designated in the preliminary election may make the purchase(s) by submitting the required forms and payment within 90 days from the date the disability application is approved.

(b) If the member has not made a preliminary benefit option election, the member will be considered as having died before retirement.

(A) If the beneficiary designated under ORS 238.390(1) is the surviving spouse, the surviving spouse may, within 90 days from the date the disability application is approved,

elect to have either Option 2 or 3 disability benefits or pre-retirement death benefits, as provided in ORS 238.390 or 238.395, if eligible.

(i) Regardless of the election made by the surviving spouse under paragraph (b)(A) of this section, all benefits will cease upon the surviving spouse's death.

(ii) If the deceased member was eligible to purchase additional creditable service or retirement credit under ORS Chapter 238, a surviving spouse who elects disability benefits under paragraph (b)(A) of this section, may make the purchase(s) by submitting the required forms and payment at the time of the election.

(B) If the beneficiary designated under ORS 238.390(1) is not the surviving spouse, the beneficiary will receive pre-retirement death benefits as provided in ORS 238.390 or 238.395, if eligible.

Stat. Auth.: ORS 238.650

Stats. Implemented: ORS 238.320, 238.325 & 238.330

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July 23, 2010

TO: Members of the PERS Board

FROM: Steven Patrick Rodeman, Deputy Director

SUBJECT: Adoption of Employer Remittance of Employee Contributions Rule 459-009-0200, *Employer Remitting of Employee Contributions*

OVERVIEW

- Action: Adopt modifications to the Employer Remitting of Employee Contributions rule.
- Reason: The rule currently addresses employee contributions made under Chapter 238 and needs to be updated to address employee contributions under 238A and judge member contributions.
- Policy Issue: No policy issues have been identified.

BACKGROUND

OAR 459-009-0200 covers employer remittance of employee contributions under ORS Chapter 238, which have not existed since January 1, 2004. Employee contributions and employer payment of employee contributions are now governed by ORS Chapter 238A for contributions to the Individual Account Program. The proposed rule modifications address employee contributions under ORS Chapter 238A, remitting of judge member employer contributions, and correct both federal Internal Revenue Code citations and the reference to the remittance rule, OAR 459-070-0010.

SUMMARY OF MODIFICATIONS TO RULE SINCE NOTICE

No modifications have been made since notice.

PUBLIC COMMENT AND HEARING TESTIMONY

A rulemaking hearing was held on May 25, 2010 at 1:00 p.m. at PERS headquarters in Tigard. No members of the public attended. The public comment period ended on June 4, 2010 at 5:00 p.m. No public comment was received.

LEGAL REVIEW

The attached draft rule was submitted to the Department of Justice for legal review and any comments or changes are incorporated in the rule as presented for adoption.

IMPACT

Mandatory: Yes; with the statutory re-direction of contributions, the rule should be updated.

Impact: Clarifies employee contributions and employer payment of employee contributions under PERS Chapter 238A and judge member contributions.

Cost: There are no discrete costs attributable to the rule.

RULEMAKING TIMELINE

February 12, 2010	Staff began the rulemaking process by filing Notice of Rulemaking with the Secretary of State.
March 1, 2010	*Oregon Bulletin* published the Notice. Notice was mailed to employers, legislators, and interested parties. Public comment period began.
May 21, 2010	PERS Board notified that staff began the rulemaking process.
May 25, 2010	Rulemaking hearing held at 2:00 p.m. in Tigard.
June 4, 2010	Public comment period ended at 5:00 p.m.
July 23, 2010	Board may adopt the rule modifications.

BOARD OPTIONS

The Board may:

1. Pass a motion to "adopt modifications to the Employer Remitting of Employee Contributions rule, as presented."
2. Direct staff to make other changes to the rule or explore other options.

STAFF RECOMMENDATION

Staff recommends the Board choose Option #1.

- Reason: The rule currently addresses employee contributions made under Chapter 238 and needs to be updated to address employee contributions under 238A and judge member contributions.

If the Board does not adopt: Staff would return with rule modifications that more closely fit the Board's policy direction if the Board determines that a change is warranted.

C.2. Attachment 1 – 459-009-0200, *Employer Remitting of Employee Contributions*

OREGON ADMINISTRATIVE RULE
PUBLIC EMPLOYEES RETIREMENT BOARD
CHAPTER 459
DIVISION 009 – PUBLIC EMPLOYER

459-009-0200

Employer Remitting of Employee Contributions

(1) *[Except as provided in ORS 238.200(1)(b), a]* **A** participating employer shall remit to PERS in accordance with OAR **459-070-0110** *[459-009-0100 six percent (6%) of gross salary and wages for each active member employed as]* **the contributions** required *[in]* **by** ORS *[238.200(1)(a)]* **238A.330**. Unless otherwise agreed to as provided for in sections (2) or (3) of this rule, the employer shall withhold and remit the required contributions on an after-tax basis as defined in OAR 459-005-0001*[(36)]***(2)**, *[and]* **which** shall be known as "member paid after-tax contributions (MPAT)".

(2) In accordance with Internal Revenue Code (IRC) Section 414(h), and under provision of ORS *[238.205(2)]* **238A.335(2)(b)**, participating employers may voluntarily agree to assume and pay the *[six percent]* employee contribution on behalf of its employees, *[and]* **which** shall be known as "employer paid pre-tax contributions (EPPT)". The employer assumption and payment of the *[uniform six percent]* employee contributions shall be subject to the following terms and conditions:

(a) The employer's employment agreement(s) to assume and pay the contributions must be evidenced by a certified copy of the employer's policy established by statute, charter, ordinance, administrative rule, executive order, collective bargaining agreement, or other written employment policy or agreement. The employer's employment policy(s) or agreement(s) shall specify **that**:

(A) *[That t]***T**he required PERS employee contribution *[of six percent of salary]* is deemed to be *["]*picked up*["]* for purposes of IRC Section 414(h)(2) and is assumed and paid for purposes of ORS *[238.205(5)(b)]* **238A.335(2)(b)**;

(B) *[That t]***T**he employees do not have the option of receiving the assumed amount directly;

(C) *[That e]***E**mployee compensation *[shall]* **may** not be reduced and *[that]* the employer shall provide the additional amounts necessary to make the employee contributions; and

(D) *[That t]***T**he employer's employment policy(s) or agreement(s) is not retroactive in its application.

(b) The employer's employment policy(s) or agreement(s) to assume and pay employee contributions *[shall]* **may** not be construed to require an employer to open or renegotiate a pre-existing collective bargaining agreement or change an employment policy before its normal expiration date.

(c) The employer's employment policy(s) or agreement(s) must be to assume and pay the full amount, and not a portion thereof, of the affected employees' *[six percent]* contributions required by ORS *[238.200]* **238A.330**.

(d) The employer's policy(s) or agreement(s) may apply to all its employees or some of its employees. If it applies only to some employees, it shall apply uniformly to all employees of the public employer who are employed in similarly situated positions, such as, but not limited to:

(A) The chief executive officer or administrative head of a public employer.

(B) Management personnel, as defined by the public employer, not otherwise covered by a collective bargaining agreement.

(C) Confidential personnel, as defined by the public employer, not otherwise covered by a collective bargaining agreement.

(D) Administrative personnel, as defined by the public employer, not otherwise covered by a collective bargaining agreement.

(E) Personnel covered by a collective bargaining agreement.

(F) Other personnel, whether full time, part time, temporary, or as a substitute, who are not covered by a collective bargaining agreement.

(3) *[In accordance with IRC Section 414(h) and u]***U**nder provision of ORS *[238.205(3)]* **238A.335(2)(a)**, participating employers may voluntarily agree to "pick-up" the employee contributions withheld, and such picked-up contributions shall be known as "member paid pre-tax contributions (MPPT)". The employer "pick-up" of the *[uniform six percent]* employee contribution**s** shall be subject to the following terms and conditions:

(a) The employer's agreement(s) to "pick-up" the contributions must be evidenced by a certified copy of the employer's policy established by statute, charter, ordinance, administrative rule, executive order, collective bargaining agreement, or other written employment policy or agreement*[,]***.** The employer's policy(s) or agreement(s) shall specify **that**:

[(A) That the required PERS employee contribution of six percent of salary is deemed to be "picked up" for purposes of IRC, Section 414(h)(2) and ORS 238.205(5)(a);]

[(B)] **(A)** *[That t]***T**he employees do not have the option of receiving the picked-up amount directly;

[(C)] **(B)** *[That]* **The** employee compensation shall be reduced by the amount necessary to make the employee contributions; and

[(D)] **(C)** *[That t]***T**he employer's policy(s) or agreement(s) is not retroactive in its application.

(b) The employer's employment policy(s) or agreement(s) to "pick-up" employee contributions withheld *[shall]* **may** not be construed to require an employer to open or re-negotiate a pre-existing collective bargaining agreement or change an employment policy before its normal expiration date.

(c) The employer's policy(s) or agreement(s) must be to "pick-up" the full amount, and not a portion thereof, of the affected employees' *[six percent]* contributions required by ORS *[238.200]* **238A.330**.

(d) The employer's employment policy(s) or agreement(s) may apply to all its employees, or some of its employees. If it applies to only some of its employees, it shall apply uniformly to all employees of the public employer who are employed in similarly situated positions, such as, but not limited to:

(A) The chief executive officer or administrative head of a public employer.

(B) Management personnel, as defined by the public employer, not otherwise covered by a collective bargaining agreement.

(C) Confidential personnel, as defined by the public employer, not otherwise covered by a collective bargaining agreement.

(D) Administrative personnel, as defined by the public employer, not otherwise covered by a collective bargaining agreement.

(E) Personnel covered by a collective bargaining agreement.

(F) Other personnel, whether full time, part time, temporary, or as a substitute, who are not covered by a collective bargaining agreement.

(4) The notification of the employer's written employment policy(s) or agreement(s) to enter into or to revoke (1) the "pick-up", or (2) to assume and pay contributions on behalf of employees, shall be submitted to PERS for review and approval, and shall become effective on the date the notification is received by PERS**.** Additional information related to the employer's policy or agreement shall be provided at the request of staff and in the manner required by staff. If approved by PERS, such policy and agreement *[shall]* **may** not be revoked by the employer except with prior written notice to PERS. All costs to correct any errors caused by failure to give required notice shall be borne by the employer.

(5) Notwithstanding sections (1) to (4) of this rule, judge member contributions shall be made in accordance with ORS 238.515.

Stat. Auth.: ORS 238.650 **& 238A.450**

Stats. Implemented: ORS *[238.205]* **238.515, 238A.330 & 238A.335**

PERS Oregon Public Employees Retirement System

Oregon

Theodore R. Kulongoski, Governor

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July 23, 2010

TO: Members of the PERS Board

FROM: Steven Patrick Rodeman, Deputy Director

SUBJECT: Adoption of "Equal To Or Better Than" Rule:
459-030-0025, *Standards for Review of Police Officers and Firefighters Retirement Plans*

OVERVIEW

- Action: Adopt modifications to the "Equal To Or Better Than" Rule.
- Reason: Preliminary application of the ETOB testing standards in the current administrative rule, particularly when used to compare employer defined contribution plans to the PERS defined benefit plan, did not fully incorporate the fundamental structural differences between those plan types.
- Policy Issue: Whether these rule revisions establish standards that more appropriately compare defined contribution and defined benefit plans?

BACKGROUND

All public employers with non-PERS police and fire retirement plans must ensure their plans are equal to or better than (ETOB) the benefits provided under the PERS plan. ORS 237.620(3) requires the PERS Board to make the ETOB determination by conducting a plan-to-plan comparison.

In developing the testing standards in this rule, staff followed the following principles:

1. ***Comparability*** - the test should strive for an "apples-to-apples" comparison.

2. ***Durability*** - test results should be consistent so long as plan provisions do not change.

3. ***Cost effectiveness*** - an appropriate low-cost method that does not compromise the validity of results should be used.

The ETOB testing standards in the current administrative rule, when used to compare employer's defined contribution plans to the PERS defined benefit plan, did not adequately meet the first principle. With additional input from stakeholders and the PERS Board's actuaries, proposed rule modifications are being presented to better align the test standards with that principle.

SUMMARY OF MODIFICATIONS TO RULE

The attached draft rule contains three substantial changes, as well as a few organizational modifications. The three changes are:

1. Point of Determination. The proposed modifications direct that the ETOB comparison be based on a specific point in time and on how benefits are typically paid out under each of type of plan being tested. By specifying that the measure of a defined benefit plan is the present value of the projected stream of benefit payments, that value can be compared directly to a defined contribution plan based on the present value of the lump sum accumulated under that plan at the time of retirement. The current rule requires the conversion of all benefits to a life annuity, which is not typical for defined contribution plans. The proposed approach applies common assumptions to existing plan structures to improve the comparison basis for the two types of plans.
2. Accumulation and Discount Rates. The proposed draft replaces the 'risk free' rate with the PERS assumed earnings rate, to use in calculating the accumulation and discounting of defined contribution balances. The use of the same interest rate when valuing plans in the ETOB test will improve the comparability between plans, particularly when comparing defined contribution plans to PERS' defined benefit plan.
3. Employer Funding of Member Paid Benefits. The proposed rule directs that, if a plan document requires the employer to pay for benefits that would otherwise be funded by the member, those benefits will be included when valuing the employer's plan. Under the current rule, these benefits were excluded from the ETOB test. The addition of non-elective employer funded benefits to the testing criteria provides clearer direction to the actuary regarding how to value the benefits to be included or excluded in the ETOB test.

The Board's actuary who will conduct the ETOB testing recommends that the proposed rule changes be adopted by the Board as presented and attached to this memo. A copy of a letter from Matt Larrabee, Mercer, is Attachment 2 to this memo.

PUBLIC COMMENT AND HEARING TESTIMONY

On June 23, 2010, a stakeholder group met at PERS headquarters to discuss changes to the existing ETOB testing rule. A rulemaking hearing was held on July 6, 2010 at 1:00 p.m. at PERS headquarters in Tigard. Bob Palmer, representing Mid-Columbia Fire and Rescue, attended and staff answered Mr. Palmer's questions. The public comment period ends on July 23, 2010, at the PERS Board Meeting.

On July 6, 2010, Everett Moreland, who represents four employers undergoing the current ETOB test, submitted comment on the proposed rule modifications. A copy of his letter is Attachment 3 to this memo.

Mr. Moreland objects to the added language that defined 'employer funded benefits'. He believes that the current rule's definition of employer funded benefits was unambiguous and that the proposed rule change will cause some employer funded benefits to be excluded from the test. Mr. Moreland maintains that long-term employer funded benefits should be included as part of

the ETOB test, even if the payment of those benefits are discretionary. A copy of his letter is Attachment 3 to this memo.

Staff recommends that the proposed wording, particularly the 'non-elective' requirement, be retained. Under the current rule, the actuary excluded all employee benefits even if those benefits were being funded by the employer. This rule change will expand the definition of employer paid benefits to include those employee benefits in which funding by the employer is mandated by the plan document.

Additionally, one of the triggers for an ETOB test would be a change in the employer's plan. This standard adds consistency and clarity for determining when an ETOB test should be conducted. With the employer's responsibility imbedded in the plan document, an ETOB test will be required if the plan is changed to eliminate the employer's funding of the employee benefit. Basing the testing trigger, as recommended by Mr. Moreland, on when an employer elects to fund or not fund member benefits can diminish the durability of the test and fog the definition of when a test would be required.

On July 13, 2010, Greg Hartman, who represents the PERS Coalition, provided additional information on this point by stating that in the 1986 Oregon Supreme Court Case, *Salem Fire Fighters Local 314 v. Public Employees Retirement Board*, the court ruled that only employer provided benefits can be used in the ETOB comparison. In addition, Mr. Hartman stated that the PERS Coalition cannot support the proposed change in definition without additional information from PERS staff. Staff believes that the 'nonelective' requirement contained in the proposed rule elevates the status of those employee funded benefits that are required by the plan to be funded by the employer, therefore meeting the requirement that only employer funded benefits be used in the ETOB comparison. Staff will provide additional information to Mr. Hartman confirming this intent. A copy of Mr. Hartman's July 13, 2010 letter is Attachment 4 to this memo.

Mr. Moreland's July 10, 2010 letter also raises the concern that the exclusion of employer electively funded employee benefits could cause employers to fail an ETOB test, compelling the employer to provide a higher level of benefits to meet the ETOB standard and creating an unfunded state mandate subject to Oregon Constitution Article XI, section 15. Staff disagrees. The constitution contains an exemption from the "unfunded mandate" constraint if the legislation in question was passed by three-fifths of each chamber of the Legislative Assembly. The 2007 legislative changes to the ETOB test passed with a margin that exceeded that threshold.

In a letter dated July 6, 2010, Greg Hartman submitted comment on three areas of the proposed rule. A copy of his letter is Attachment 5 to this memo.

First, Mr. Hartman questions the use of the PERS assumed earnings rate for the accumulation of value for the contributions to an ETOB employer's defined contribution plan. While Mr. Hartman does not recommend the retention of the risk-free rate contained in the current rule, he does recommend that a rate lower than the PERS assumed earnings rate be used in the ETOB test. He states that this is supported by a study conducted by the Center For Retirement Research at Boston College (attached to Mr. Hartman's letter), which shows that defined contribution plans have accumulated earnings at a lower rate than defined benefit plans (but still at median rates in the 8% range). Mr. Hartman recommends that PERS further study the accumulation rate of defined contribution plans rather than use the PERS assumed earnings rate.

Staff maintains that the PERS assumed earnings rate should be used for all plans being tested unless an employer's plan guarantees a higher rate. The reasoning for this is that defined contribution plan investments can be directed by either the employer or by the individual employee. This can lead to a wide variation of investment strategies ranging from conservative to aggressive. The current assumed rate of 8% reflects a diversified portfolio with both conservative and aggressive investments and is also the most common rate used by public pension plans in valuing their system's liabilities. To provide better comparability for the ETOB test, staff considers the PERS assumed earnings rate to be both appropriate and supportable.

Second, Mr. Hartman objects to comparing the value of a lump sum from a defined contribution plan, at the time of retirement, to the value of the PERS plan's annuity payments. Mr. Hartman states that the defined contribution's lump sum should first be annuitized for the test comparison. He also believes that the value of the defined contribution annuity should be based on a rate that is tied to an officially developed private sector index. He argues that these rates, which are lower than the PERS assumed rate, recognize that the PERS plan provides investment expertise and coverage of investment risk not available to a defined contribution plan retiree. Staff disagree with this approach.

Initially, note that the comparison is between two present values: that of the defined benefit plan's stream of payments to the lump sum accumulated value of the defined contribution plan, discounted back to the valuation date. This comparison is not based on an annuitization of the defined contribution lump sum. Rather, the present value is derived from a discount rate and the same rate needs to be used for both types of plans to be comparable.

Third, Mr. Hartman states that hypothetical data used in the ETOB test may deviate significantly from the demographics of the ETOB employer's plan. Mr. Hartman recommends that these deviations be considered in the remedy phase of the test should an employer fail the ETOB test. Staff has no comment on this at this time. The use of hypothetical data for cost-effectiveness and durability was decided earlier by the Board and is part of both the current and proposed rule. Staff does not recommend a change to this testing standard. Should an employer fail the ETOB test, that employer will need to discuss the remedy with their employees in satisfying the statutory standards.

LEGAL REVIEW

The attached draft rule was submitted to the Department of Justice for legal review and any comments or changes are incorporated in the rule as presented for adoption.

IMPACT

Mandatory: Yes; the ETOB testing standards must be revised to allow the PERS Board to fulfill its statutory responsibilities.

Impact: Revising the testing standards will allow PERS to make a reasonable ETOB determination.

Cost: The proposed rule change has not changed the original estimated budget.

RULEMAKING TIMELINE

June 10, 2010	Notice of Rulemaking Hearing was mailed to employers, legislators, and interested parties. Public comment period began.
June 15, 2010	Staff filed Notice of Rulemaking Hearing with the Secretary of State.
July 1, 2010	*Oregon Bulletin* published the Notice.
July 6, 2010	Rulemaking hearing held at 2:00 p.m. in Tigard.
July 23, 2010	Public comment period ends at Board meeting. Board may adopt the rule modifications.

BOARD OPTIONS

The Board may:

1. Pass a motion to adopt modifications to the "Equal To Or Better Than" rule, as presented.
2. Direct staff to make other changes to the rule or explore other options.

STAFF RECOMMENDATION

Staff recommends the Board choose Option #1.

- Reason: The ETOB testing standards in the current administrative rule, when used to compare employer defined contribution plans to the PERS' defined benefit plan, did not support the principles used to develop the standards as the results were not comparable.

If the Board does not adopt: Staff would return with rule modifications that more closely fit the Board's policy direction if the Board determines that a change is warranted.

C.3. Attachment 1 – 459-030-0025, *Standards for Review of Police Officers and Firefighters Retirement Plans*
C.3. Attachment 2 – Letter from Matt Larrabee, MERCER, dated July 14, 2010
C.3. Attachment 3 – Letter from Everett Moreland dated July 6, 2010
C.3. Attachment 4 – Letter from Greg Hartman dated July 13, 2010
C.3. Attachment 5 – Letter from Greg Hartman dated July 6, 2010 (with attachments)

PERS Oregon Public Employees Retirement System

OREGON ADMINISTRATIVE RULE
PUBLIC EMPLOYEES RETIREMENT BOARD
CHAPTER 459
DIVISION 030 – LOCAL PUBLIC EMPLOYER RETIREMENT PLANS FOR POLICE OFFICERS AND FIRE FIGHTERS

459-030-0025

Standards for Review of Police Officers and Firefighters Retirement Plans

(1) For purposes of this rule:

(a) "Assumed rate" has the same meaning as provided in OAR 459-007-0001.

(b) "Valuation date" means the date set by the Board as of which the retirement benefits under the public employer's retirement plan and the retirement benefits under the PERS Plan shall be compared.

[(1)] **(2)** A determination whether a public employer provides retirement benefits to its police officers and firefighters that are equal to or better than the benefits that would be provided to them by PERS will be made as of the valuation date. *[The "valuation date" is the date set by the Board as of which the retirement benefits under the public employer's retirement plan and the retirement benefits under the PERS Plan shall be compared.]*

[(2)] **(3)** The Board will consider the aggregate total actuarial present value**, as of the valuation date,** of all retirement benefits accrued up to the valuation date and projected to be accrued thereafter **to the date of projected retirement** by the group of police officers and firefighters employed on the valuation date by the public employer. The Board will compare the retirement benefits provided under the public employer's retirement plan for each of the following classes of employees to the retirement benefits provided to the equivalent class of employees participating in the PERS Plan:

(a) Police officers or firefighters who would have established membership in the system before January 1, 1996, as described in ORS 238.430(2), and would have been entitled to receive benefits under the PERS Plan;

(b) Police officers or firefighters who would have established membership in the system on or after January 1, 1996, as described in ORS 238.430, and before August 29, 2003, as described in ORS 238A.025, and would have been entitled to receive benefits under the PERS Plan; and

(c) Police officers or firefighters who would have established membership in the system on or after August 29, 2003, and would have been entitled to benefits under the PERS Plan.

[(d)] **(4)** *[f]***F**or each class of employees **described in section (3) of this rule***[,]***:**

(a) *[t]***T**he aggregate total **actuarial present value as of the valuation date of the projected full-career** retirement benefits provided by the public employer must be equal to or better than those provided by PERS to the equivalent class of employees.

[(e)] **(b)** The **actuarial present value of projected** retirement benefit**s** for each individual employee need not be equal to or better than the *[particular benefit]* **present value** that employee would have received as a member of that employee's equivalent class in PERS.

[(f)] **(c)** The public employer's retirement plan or plans must provide at least eighty percent (80%) of the actuarial present value of projected retirement benefits in each of the major categories of retirement benefits available under PERS, namely: a service retirement benefit, including post retirement health care and a disability retirement benefit, also including post retirement health care.

[(3)] **(5)** In adopting the following methods and assumptions, to be used in conducting an actuarial review of a public employer's retirement plan, preference has been given to the simplest, least expensive methodology consistent with ORS 237.610 to 237.620 and applicable actuarial standards:

(a) Only employer funded benefits shall be used as the basis for the test comparison. **Any contribution deemed as an employee contribution will be treated as an employee contribution for testing purposes, even if paid for by the employer unless the employer's**

plan specifies that the employer is responsible to make the contribution on the employee's behalf and that responsibility is nonelective.

(b) The Full Formula, Money Match, Formula Plus Annuity, and OPSRP Pension benefit formulas shall be used as the basis for valuing PERS benefits.

(c) Prior service benefits that depend on earnings shall be valued using *[a risk-free earnings]* **the assumed** rate, taking into consideration guaranteed plan returns.

(d) Future service benefits that depend on earnings shall be valued using *[a risk-free earnings]* **the assumed** rate, taking into consideration guaranteed plan returns.

(e) Benefits will be assumed to be paid in the typical and customary distribution form given the structure of the underlying plan. For example, PERS benefits will be paid using the most recent distribution assumption as of the valuation date, and benefits from a defined contribution program will be assumed to be paid as a lump sum at the date of projected retirement.

[(e)] **(f)** Lump sum/annuity conversions**, if needed,** shall be *[valued]* **calculated** using *[a risk-free earnings]* **the assumed** rate.

(g) The assumed rate will be used to discount projected future benefits back to the valuation date.

[(f)] **(h)** Benefit comparisons shall use a hypothetical PERS member data standard for each demographic group.

[(4)] **(6)** In conducting an actuarial review of the public employer's retirement plan, the actuary retained by the Board will use its current actuarial assumptions for police officers and firefighters of public employers participating in PERS for those employees**, subject to any exceptions noted above**.

[(5)] **(7)** The Board will consider the **estimated** cost of the benefits to be provided**, the estimated value of projected benefits to the employee,** and the proportion of the cost being paid by the public employer and the participating police officers and firefighters. Whether the benefits are provided by contract, trust, insurance, or a combination thereof shall have no effect on the Board's determination.

[(6)] **(8)** In considering a public employer's retirement plan provisions, the Board may not value portability of pension credits, tax advantages, Social Security benefits or participation, any worker's compensation component of a public employer's retirement plan as determined by the employer or any portion of a benefit funded by the member.

[(7)] **(9)** The Board may not consider benefits provided by the PERS Plan under ORS 238.375–238.387 or benefits provided by the employer's retirement plan under 237.635–237.637. The employer must identify benefits paid to comply with 237.635–237.637.

[(8)] **(10)** Additional actuarial assumptions needed to evaluate the public employer's retirement plan may be considered by the Board's actuary to be consistent with assumptions specified in these rules. Any disputes as to the appropriateness of additional actuarial assumptions may be resolved by the Board in its sole discretion.

Stat. Auth: ORS 238.650

Stats. Implemented: ORS 237.620

Matthew R. Larrabee, FSA, EA, MAAA
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MERCER

MARSH MERCER KROLL
GUY CARPENTER OLIVER WYMAN

July 15, 2010

Mr. Dale Orr
Manager, Actuarial Analysis Section
Oregon PERS

Via E-Mail

Subject: Comments on Proposed Modifications to ETOB Administrative Rule

Dear Dale:

Per your request, this letter summarizes Mercer's comments in our role as the PERS actuary on the proposed modifications to the Oregon Administrative Rule ("OAR") 459-030-0025 governing mandated Equal to or Better ("ETOB") testing. Our comments in this letter are limited to the proposed revisions to the rule highlighted in the version of the OAR distributed to stakeholders on June 30, 2010. Our comments are organized into two major categories below. In all of our comments, we remain cognizant of the guiding principles framework for ETOB testing developed by PERS staff. Those guiding principles are:

- Comparability
- Durability
- Cost Effectiveness

Use of the "Assumed Rate" of Investment Return

A key proposed modification to the OAR is to replace the "risk-free rate" with an "assumed rate" for ETOB calculations, with the assumed rate specified as the valuation rate used in the PERS actuarial valuation. Mercer believes this proposed modification is consistent with the guiding principles noted above. It is important to note that Mercer feels the pre-modification version of the OAR, which utilized a "risk-free" rate, was also consistent with the guiding principles.

That said, at the May 2010 public meeting of the Public Employees Retirement Board ("Board"), the Board concluded that the OAR should be modified. The guidance from the Board indicated that the modifications should have the ETOB testing comparison focus on the expected value to the employee of retirement benefits instead of the risk-free value to the employee of retirement benefits. We believe that the proposed modifications incorporate that additional guidance from the Board.

Proposed Technical Clarifications

Given the guidance from the Board to modify the OAR to address the issue noted above, it allowed PERS the opportunity to also modify the OAR to provide additional technical clarifications. The proposed modifications in this area provide clarification of how the following two issues should be handled for ETOB testing purposes:

- Anticipated form and timing of benefit payment
- Treatment of what constitutes an employer-funded (vs. an employee-funded) benefit

With respect to precisely how either of the above two issues should be handled technically in the test, Mercer has neither an advisory opinion nor an advocacy position (e.g., we have no advisory opinion as to what the "bright line test" should be that separates employer from employee-funded benefits). That said, as the actuary for the ETOB test we recognize that how each of the above issues is handled technically can materially affect testing results and the magnitude of necessary remedies. As such, we think it serves the best interests of all ETOB stakeholders that the OAR provide as much clear and specific information as possible on how the test will be conducted. In that context, we are comfortable with the proposed modifications because we believe that they provide improved clarity and specificity when compared to the pre-modification version of the OAR. Finally, Mercer feels that the proposed modifications in this area remain consistent with the guiding principles.

Please feel free to contact us with any questions you have on this letter.

Sincerely,

Matthew R. Larrabee, FSA, EA, MAAA
Principal

MRL/sdp/me:gjw

Copy:
Scott Preppernau

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The information contained in this document (including any attachments) is not intended by Mercer to be used, and it cannot be used, for the purpose of avoiding penalties under the Internal Revenue Code that may be imposed on the taxpayer.

HERSHNER HUNTER LLP

EVERETT MORELAND
Direct (541) 302-5248
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July 6, 2010

BY FIRST-CLASS MAIL AND EMAIL (to Daniel.Rivas@state.or.us)

Members of the PERS Board
P.O. Box 23700
Tigard, Oregon 97281-3700

RE: ETOB--Request not to make a proposed addition to OAR 459-030-0025

Dear Board Members:

I represent four public employers whose retirement plans are undergoing the current ETOB test. Michael Pittman asked me at the June 23, 2010, ETOB Stakeholder Discussion to submit this letter to explain why I ask the Board not to adopt a proposed addition to the ETOB rules.

Summary

Request

This letter asks the Board not adopt the following proposed addition to OAR 459-030-0025 (the proposed addition is the following **bold and underlined** sentence):

> "Only employer funded benefits shall be used as the basis for the test comparison. **Any contribution deemed as an employee/member contribution will be treated as an employee/member contribution for testing purposes, even if paid for by the employer unless the employer's plan specifies that the employer must make the contribution on the member's behalf and that responsibility is nonelective.**" (Proposed OAR 459-030-0025(5)(a))

Reasons for request

I believe the proposed addition would:

- Substantively change the ETOB rules by increasing the benefits some employers must provide; and

- Be an unfunded mandate subject to Oregon Constitution Article XI, section 15.

Explanation

What the present ETOB rules require

The present ETOB rules require that employer funded benefits in a local plan be at least equal to employer funded benefits in PERS. See the following OAR 459-030-0025(3)(a) (proposed to be renumbered as OAR 459-030-0025(5)(a)):

> "Only employer funded benefits shall be used as the basis for the test comparison."

A reasonable rationale for the Board's decision not to count employee funded benefits is employees' ability to save for retirement through a deferred compensation plan or IRA or by investing in a commercial (tax-deferred) annuity or in a largely tax-deferred index mutual fund.

What the present ETOB rules do not allow

The present ETOB rules do not allow:

- The Board to require that employer funded benefits in a local plan be better than employer funded benefits in PERS.
- The Board to count only part of the employer funded benefits in a local plan.
- PERS employers to electively expand the mandate of the ETOB statute. Thus elections by PERS employers to fund contributions to PERS member and IAP accounts, or to fund additional contributions, up to 6% of salary, to IAP accounts under ORS 238A.340, do not increase the required amount of employer funded benefits in a local plan.

What the proposed addition to the ETOB rules would require

Of the Board or the PERS Executive Director. The proposed addition would require the Board or the PERS Executive Director to:

- Identify contributions to a local plan that are "deemed as an employee/member contribution."
- Not count those "deemed" employee/member contributions, even if funded by the employer, unless the local plan specifies that the employer has a nonelective responsibility to make the contributions.

Of the employer. A PERS employer is not required to fund contributions to PERS member and IAP accounts. But--merely because many PERS employers have elected to fund those contributions--the proposed addition would require an employer that has funded "deemed"

employee/member contributions to its local plan on an "elective" basis to provide employer funded benefits that are better than the employer funded benefits the employer would have been required to provide through PERS. This is because the proposed addition would require the employer to fund both those "deemed" employee/member contributions plus benefits equal to the employer funded benefits the employer would have been required to provide through PERS.

Why I ask the Board not to adopt the proposed addition

For the following reasons, I ask the Board not to adopt the proposed addition:

- The proposed addition would "clarify" an unambiguous term. I believe the term "employer funded benefits" in OAR 459-030-0025 is unambiguous as applied to member accounts--member accounts are employer funded benefits when the accounts are funded from employer funds rather than from members' salaries.[1] I have found nothing in the history of the present ETOB rules that suggests any ambiguity about the meaning of "employer funded benefits."[2]

---

[1]At the June 23, 2010, ETOB Stakeholder Discussion someone explained the proposed addition by stating that whether accounts are funded from employer funds or members' salaries cannot be determined; for example, an employer could start funding accounts in lieu of increasing salaries. This explanation negates the assumption in the ETOB rules that there is a difference between employer funded benefits and employee funded benefits.

[2]The term "employer funded benefits" was not in the immediately prior ETOB rules, which stated:

> "The Board will consider the cost of the benefits to be provided and the proportion of the cost being paid by the public employer and the participating police officers and firefighters." (From former OAR 459-030-0025(5) as adopted in 2005)

The above language from the immediately prior ETOB rules was in the proposed ETOB rules as last presented to the Board (on September 19, 2008) before the Board adopted the present ETOB rules on February 6, 2009.

The packet for the Board's February 6, 2009, meeting was the first Board meeting packet to include the language of present OAR 458-030-0025(3)(a) ("Only employer funded benefits shall be used as the basis for the test comparison") and to clearly inform the Board that only employer funded benefits would be considered. See Steven Rodeman's February 6, 2009, memo to the Board ("Only those benefits funded by the employer will be compared") and the accompanying decision matrix (the "Benefits to be Included" are "Employer funded only"), both of which are in the packet for the Board's February 6, 2009, meeting. I also reviewed the ETOB materials in the packets for the Board's meetings on September 21 and November 16, 2007, and February 15, March 28, July 25, September 19, and November 21, 2008, and found nothing to suggest any ambiguity.

- The proposed addition would increase the benefits some employers must provide. As illustrated in the paragraph starting at the bottom of page 2, the proposed addition would increase the benefits an employer must provide under the ETOB rules if the employer has funded "deemed" employee/member contributions to its local plan on an "elective" basis.

- The proposed addition appears to be an unfunded mandate. If the proposed addition increases the benefits an employer must provide, I believe it would be an unfunded mandate subject to Oregon Constitution Article XI, section 15, which states in part:

  > "[W]hen the Legislative Assembly or any state agency requires any local government to establish a new program or provide an increased level of service for an existing program, the State of Oregon shall appropriate and allocate to the local government moneys sufficient to pay the ongoing, usual and reasonable costs of performing the mandated service or activity."

  See Oregon Attorney General Opinion OP-8263 (January 22, 1999) ("we conclude that the provision of PERS benefits to retirees constitutes 'financial * * * services to persons' for purposes of Article XI, section 15"); Oregon Attorney General Opinion OP-8277 (February 13, 2001) ("we have previously concluded that 'financial * * * services to persons' includes the provision of retirement benefits to local government retirees," citing Opinion OP-8263).

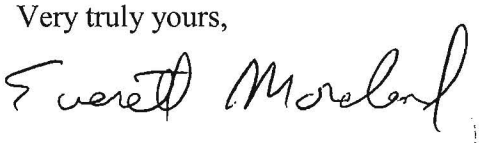
Conclusion and request

I believe the proposed addition would substantively change the unambiguous term "employer funded benefits."

I believe the proposed addition attempts to solve a problem that does not exist--the perceived unfairness of not counting PERS employers' contributions to PERS member and IAP accounts while counting all employer funded benefits in local plans. This difference follows from the Board's decision when it adopted the present ETOB rules to count only employer funded benefits in PERS and local plans and the Board's implicit decision when it adopted the present ETOB rules not to allow PERS employers to electively expand the mandate of the ETOB statute when they elect to fund contributions to PERS member and IAP accounts or additional contributions to IAP accounts under ORS 238A.340. The Board's decision to count only employer funded benefits is justified by employees' ability to save for retirement through a deferred compensation plan or IRA or by investing in a commercial (tax-deferred) annuity or in a largely tax-deferred index mutual fund. The Board's implicit decision not to allow PERS employers to electively expand the mandate of the ETOB statute follows from a reasonable reading of the ETOB statute.

I ask the Board not to adopt the proposed addition.

Very truly yours,



EVERETT R. MORELAND

ERM:em

cc: Mr. Gregory A. Hartman (to hartmang@bennetthartman.com)

PERS Oregon Public Employees Retirement System

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July 13, 2010

Steve Rodeman
Public Employee Retirement System
PO Box 23700
Tigard, OR 97281-3700

Re: PERS Coalition ETOB Material; Proposed Additions to OAR 459-030-0025
Our File No.: 5415-237

Dear Steve:

The purpose of this letter is to comment on behalf of the PERS Coalition on some of the issues raised in Everett Moreland's July 6, 2010 correspondence. In essence Mr. Moreland objects to language which purports to clarify the process of determining whether a benefit is an employer-funded benefit. The purpose of this letter is to bring some additional information to that discussion.

The requirement that the ETOB comparison be of employer-funded benefits derives from a 1986 Oregon Supreme Court Case, *Salem Fire Fighters Local 314 v. Public Employees Retirement Board,* 300 Or 663 (1986). In that case the court determined that the language of the ETOB statute required comparison only of employer-provided benefits. The court invalidated the then-existing ETOB rules which failed to exclude the proportion of an exempt employer's plan which was funded by employee contributions. Though there have been multiple changes to the ETOB statute the language analyzed by the court remains unchanged and continues to require a comparison of employer-funded benefits. It has been my understanding that all subsequent ETOB comparisons were made on the basis of employer-funded benefits in order to fulfill the mandate of the *Salem Fire Fighters* case. PERS has since its inception required an employee contribution and it has been my understanding that in making the ETOB comparison the actuary excluded the value of the benefit attributable to the employee contribution. It is also my understanding that fact that any one employer or that many employers may pick-up, pay, or assume that employee contribution has no bearing on the analysis.

Just as the actuary excludes the value of any employee contribution on the PERS side, the value of any employee contribution on the exempt employer's side must also be excluded. As Mr. Moreland points out, there may be significant challenges in differentiating in exempt plans between employer- and employee-funded benefits. While those challenges may exist, the mandate of the *Salem Fire Fighters* case requires that the analysis be undertaken. Whether the proposed changes to the PERS rule aid in that analysis is not altogether clear. It should be clear that the administrative rule should not be modified unless the modification serves the purpose of carrying out the statutory mandate. To date

there has been no information provided to the stakeholders explaining why this proposed language should be included in the amended rules. The PERS Coalition cannot support this proposed amendment absent such a showing.

Yours very truly,

Gregory A. Hartman

GAH:kaj
cc: Clients
Everett Moreland

Exec

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July 6, 2010

Daniel Rivas
Public Employee Retirement System
PO Box 23700
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Re: ETOB Rules (Proposed OAR 459-030-0025)
Our File No.: 5415-237

Dear Daniel:

The purpose of this letter is to provide written comments on the proposed amendments to OAR 459-030-0025 which were presented by PERS staff at the June 23 stakeholders meeting. All of these comments are being made on behalf of the PERS Coalition. As you will see, to a large extent they echo and expand on some of the comments I made at the stakeholders meeting.

Over the extended period of time that we've been developing this rule we have discussed at some length the difficulties inherent in comparing the value of defined benefit and defined contribution plans. The current rule has as its key assumption the use of what is referred to as a risk-free rate in making that comparison. The development of the concept of a risk-free rate and the analysis which led to the development of a risk-free rate by the PERS actuary took place over an extended period of time. When the preliminary results of the use of that rate were presented to the board at the last meeting, the board indicated quite emphatically that they did not feel that the results being produced by this methodology were making a realistic real-world comparison.

In response to this rejection the proposed rule simply incorporates the PERS actuarial earnings assumption (8%) to be used in comparing the ETOB defined contribution plans with PERS. While the PERS Coalition neither proposed nor advocated the uniform application of a risk-free earnings rate in making this evaluation, the Coalition does not believe that the use of the PERS earnings assumption is appropriate in making this comparison for the reasons discussed below.

Every participant in a pension plan goes through two distinct phases in their relationship with their retirement plan. During their period of active employment they are accumulating benefits in the plan and during their retirement years they are receiving benefits from the plan. In any discussion about comparing pension plans these two phases should be analyzed separately.

The Accumulation Phase

During the active accumulation phase of an employee's career, an ETOB-defined contribution participant receives a series of employer contributions to his or her pension plan. Those contributions

are invested with the goal of providing a lump sum retirement benefit. Investments may be made by the individual or organization designated by the employer or may be self-directed by the employee. The proposed rule uses the PERS earnings assumption to approximate the accumulation of assets during the employee's active career both before and after the evaluation testing date.

It should be noted that the PERS earnings assumption is generated on a biannual basis, based on a meticulous analysis by both the PERS actuary as well as the advisors to the OIC, projecting future earnings based primarily on the asset allocation of the PERS investments. No such analysis has been performed on any of the exempt defined contribution plans. More troubling, to the best of my knowledge not even a minimal examination has been done to determine whether investments in the plan are being and have been made in a manner which is consistent with the investment philosophy of PERS. When this issue was raised at the stakeholder meeting the PERS staff's response was that the 8% assumption currently used by PERS was a common assumption used for pension investments. While that is no doubt true for large, sophisticated public sector defined benefit pension plans, I know of no universal analysis which applies this same assumption to small defined contribution pension plans. In fact during the course of discussion on these issues, the PERS actuary referred to a study which indicated that in general, defined contribution plans have somewhat lesser investment return, more consistent with a 7% assumption. I have attached a copy of that study to these remarks. If the board is to adopt a new earnings assumption to be applied during the accumulation phase for ETOB defined contribution pension participants, it should be based on either an analysis of the returns typically enjoyed by plans of this sort, or alternatively, if the PERS earnings assumption is to be used, there should be at least some minimal investigation to assure that the investment philosophy of these plans are, and have been, comparable to that of PERS.

Payout Phase

The payout for a PERS participant is a monthly benefit guaranteed for life. In contrast the payout for a defined contribution participant is a single lump-sum payment. The new rule proposes to use the PERS 8% earnings assumption to calculate the present value of that flow of monthly payments and compare it to the lump sum payment to be received by an ETOB defined contribution participant. Use of the PERS earnings assumption is entirely inappropriate in making this comparison. Not only does the individual not have access to the level of investment expertise which is available to support the PERS earnings assumption, but that individual cannot bear the risk in his or her individual portfolio to achieve an 8% level of earnings. In evaluating the value of the payout phase of the equation it is more appropriate to use the risk-free earnings assumption or some other comparable assumptions in making this comparison. There are very significant and ample precedents for using such an assumption.

In the private sector ERISA regulates pension plans which permit the conversion of a monthly payment stream into a single lump sum payment. ERISA has provided over the years that such lump sum payments are permissible but only if they use a set of actuarial assumptions at least as favorable to members as that prescribed in ERISA regulations. Over the years the methodology for selecting that rate has changed, going from the PBGC rate to the GAAT rate to the current methodology. Regardless of the methodology used, that rate has typically remained between 4% and 6%. In other words, in the private sector it has long been recognized that when establishing equivalency between a stream of monthly payments and a lump sum, that a rate akin to the risk-free rate is appropriate.

Oregon courts have also recognized the need to use a comparable rate when dividing property in domestic relations cases. I have attached a letter from actuary Brad Creveling reflecting on his experience as an expert witness testifying in innumerable domestic relations cases. In those cases the court is often faced with the task of balancing out the assets to be awarded to each spouse. If one spouse is to retain his or her defined benefit pension (PERS) benefit, then it is necessary to calculate an off-setting cash amount to be awarded to the other spouse. As Mr. Creveling indicates, in making those calculations he has consistently used the PBCG rate and the courts have accepted that rate as an appropriate discount rate to be used in making that comparison. Use of the PERS earnings assumption is simply unsuitable in this portion of the test.

Hypothetical Data

During the course of these proceedings I have expressed reservations on behalf of the Coalition about the use of hypothetical data in making this comparison. While I understand the advantages to the use of hypothetical data, it remains true that the demographics of these small employers are almost invariably not going to match the demographics of any large-number comparison group. I believe that there are substantial concerns in this area, but upon further reflection and additional discussion with the PERS actuary I am hopeful that those concerns can be addressed in the remedy phase of this process for those employers who do not pass the ETOB test. I am also hopeful that at some point in this process we will have a reality check akin to that which took place at the last meeting of the board. At that last meeting the board rejected the use of the risk-free earnings assumption because of the feeling that it did not make a realistic comparison between these pension plans. I trust that at some point perhaps in the remedial phase of this discussion there will be a comparable reality check to make certain that whatever methodology is adopted does realistically protect the interests of ETOB participants.

Finally, as was noted at the recent stakeholders meeting, we have already gone through a laborious and seemingly interminable process of study and review on the ETOB question. The result of that process was the development of the risk-free analysis which was rejected by the board. The current proposal, the use of the PERS earnings assumption, has not been subjected to the same level of review that the prior proposal enjoyed. Indeed we have not had even so much as a formal public presentation by the PERS actuary analyzing whether the use of the PERS earnings assumption is appropriate in this circumstance. I would hope that the board would not take action until they've had the opportunity for both significant participation by stakeholders and input from the system's actuary.

Yours very truly,

Gregory A. Hartman

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Enclosures
cc: Clients (w/enc)
Steve Rodeman (w/enc)

PERS Oregon Public Employees Retirement System

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SEPTEMBER 2006, NUMBER 52

INVESTMENT RETURNS: DEFINED BENEFIT VS. 401(k) PLANS

BY ALICIA H. MUNNELL, MAURICIO SOTO, JERILYN LIBBY, AND JOHN PRINZIVALLI*

Introduction

Pension coverage in the private sector has shifted from defined benefit plans where professionals manage the money to 401(k) plans where participants invest their own accounts. The supposition is that individuals are not very good at investing their own money. The question is whether the supposition is borne out by the facts. That is, are returns on 401(k) plans markedly lower than those on traditional defined benefit plans?

This *brief* first reports rates of return on defined benefit and 401(k) plans over the period 1988-2004. The second section then looks at the holdings of the two types of plans to see whether the differences in returns can be explained by a more risky portfolio. The third section speculates about the role fees play in the results. The fourth section explores the implications of the findings for 401(k) participants. The final section reports on Individual Retirement Accounts (IRAs), because the assets in these accounts now exceed holdings in either defined benefit or defined contribution plans, and most of the money is rolled over from employer-sponsored plans.

The bottom line is that over the period 1988-2004 defined benefit plans outperformed 401(k) plans by one percentage point. This outcome occurred despite the fact that 401(k) plans held a higher portion of their assets in equities during the bull market of the 1990s. Part of the explanation may rest with higher fees, which are deducted before returns are reported to participants. But the one percentage point shortfall understates the investment problem in 401(k) plans, since an aggregate number does not reflect the fact that more than half of participants in 401(k) plans do not follow the prudent investment strategy of diversifying their holdings. Finally, the available data suggest that IRAs produce even lower returns than 401(k) plans, which, if true, implies trouble ahead given the massive amount of money that is being rolled over into these accounts.

* Alicia H. Munnell is the Director of the Center for Retirement Research at Boston College (CRR) and the Peter F. Drucker Professor in Management Sciences at Boston College's Carroll School of Management. Mauricio Soto is a senior research associate, Jerilyn Libby is a research associate, and John Prinzivalli is a student research assistant at the CRR. The authors would like to thank Sylvester Schieber and Brendan McFarland for providing access to Watson Wyatt's previous research and Peter Diamond and Francis Vitagliano for helpful comments.

Rates of Return in Defined Benefit and 401(k) Plans

Financial assets in private sector defined benefit and defined contribution plans (including IRAs) totaled $8.5 trillion at the end of 2005 (see Table 1). At that time, defined benefit assets accounted for only 23 percent of the total, while self-directed defined contribution plans and IRAs made up the rest. Thus, the question of how individuals fare when investing their own retirement funds is an important one.

Table 1. Private Sector Retirement Assets, Year-end 2005

Type of plan	Billions of dollars	Percent of total
Defined benefit	$1,916.5	22.7%
Defined contribution	2,868.7	33.9
IRAs	3,667.0	43.4
Total	8,452.2	100.0

Source: U.S. Board of Governors of the Federal Reserve System (2006).

The first step in assessing the performance is to compare median annual rates of return for defined benefit and 401(k) plans. The analysis focuses on companies that sponsor both types of plans to minimize the effect of company or participant characteristics on the results.[1] The formula for calculating rate of return is one commonly used by actuaries.[2] It relates the change in assets ($A_t - A_{t-1}$), netting out the impact of benefit payments from the plan (B) and contributions to the plan (C), to initial assets (A_{t-1}) plus half of net inflows (C – B):

$$\text{Rate of return} = \frac{(A_t - A_{t-1}) + B - C}{(A_{t-1}) + \frac{1}{2}(C - B)}$$

The Department of Labor's Form 5500 filings provide data on assets, contributions, and benefits for each plan over the period 1988-2004.[3]

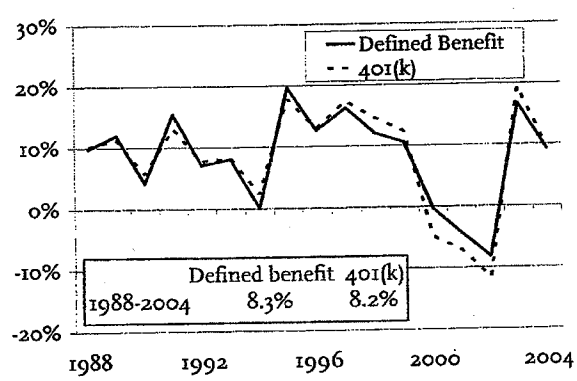
Returns, even median returns, can be calculated in a number of ways. The analysis presented below starts with the simplest approach, and one used in earlier studies, that arrays the plans and reports the return for the plan at the 50th percentile. In terms of the example shown below, the median rate of return would be 5 percent. One obvious question is whether comparing median rates of return is the right exercise, since three-quarters of the total assets in the example are in Plan A earning 10 percent. An alternative measure would be one that weighted returns by plan assets, and then identified the median. Such an approach would yield a return of 10 percent in this example. In our view, this is the preferred approach, although both results are reported below.

Example: Unweighted versus Weighted Medians

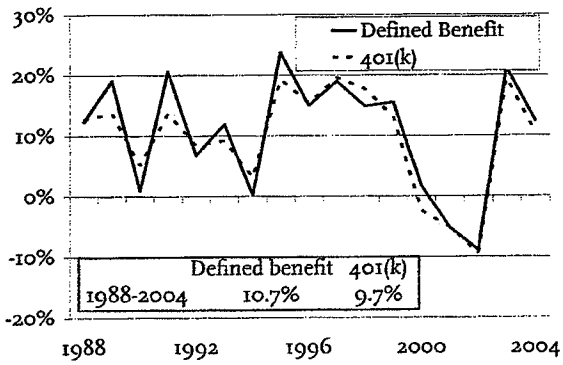
Plan	Assets	Rate of return
Plan A	$75	10%
Plan B	20	5
Plan C	5	2

Figure 1 shows the simple medians over the period 1988-2004.[4] During the period, the average of this measure suggests that the performance of defined benefit and 401(k) plans is virtually identical — 8.3 percent versus 8.2 percent.[5]

Figure 1. Annual Median Rate of Return for Plans Sponsored by Companies Offering Both



Source: Authors' calculations from U.S. Department of Labor (1990-2006).



Source: Authors' calculations from U.S. Department of Labor (1990-2006).

Figure 2 recalculates rates of return weighting returns by assets in the plan. Two factors change. First, the returns are higher. Second, defined benefit plans appear to have outperformed 401(k) plans by one percentage point (10.7 percent versus 9.7 percent).

The higher return reflects the fact that larger plans have historically performed better than smaller ones (see Table 2). The usual explanation is that large plans can hire better managers and spread fees over a larger base. Size matters much less for 401(k) plans, because the outcome reflects a myriad of individual investment decisions.

Table 2. Median Rate of Return in Asset Quintiles for Defined Benefit and 401(k) Plans, 1988-2004

Asset quintile	Defined benefit	401(k)
Largest 20 percent	10.1%	8.8%
Second	8.9	8.1
Third	8.2	7.8
Fourth	7.4	7.6
Smallest 20 percent	5.6	6.6

Source: Authors' calculations from U.S. Department of Labor (1990-2006).

The Impact of Portfolio Allocation

One question is the extent to which portfolio differences can explain differences in rates of return. Based on historical performance, stocks have a high yield and big fluctuations in annual rates of return; corporate bonds have a lower yield and much less variation; Treasury bills are the most predictable investment but provide the lowest return (see Table 3).

Table 3. Annual Total Rates of Return on Various Financial Instruments, 1926-2005

Financial instrument	Rate of return	Standard deviation
Stocks	10.4%	20.2%
Long-term corporate bonds	5.9	8.5
Intermediate government bonds	5.3	5.7
U.S. Treasury bills	3.7	3.1
Inflation	3.0	4.3

Source: Ibbotson Associates (2006). Based on copyrighted works by Ibbotson and Sinquefield. All rights reserved. Used with permission.

Table 4 shows a breakdown by type of investment for both defined benefit and defined contribution plans.[6] Defined benefit plans appear to hold about 59 percent of assets in equities, compared to 35 percent for defined contribution plans.[7] But that is not the end of the story because mutual funds also reflect equity holdings, and mutual funds are a very important component of the assets of defined contribution plans. In 2005, roughly 78 percent of the mutual fund assets in 401(k) plans were equities.[8] Applying that percentage to both the defined benefit and defined contribution mutual fund numbers yields total equity holdings of 67 percent in defined benefit plans and 65 percent in defined contribution plans.

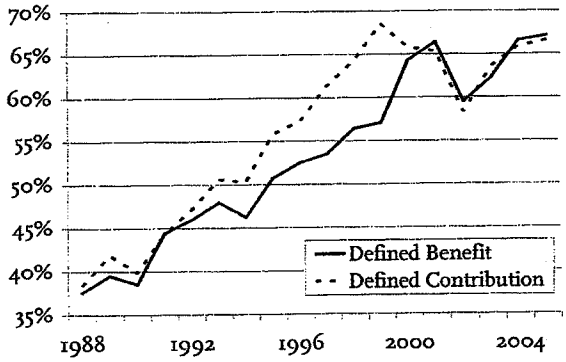
Table 4. Percentage Distribution of Assets in Private Sector Defined Benefit and Defined Contribution Plans, Year End 2005

Financial instrument	Defined benefit	Defined contribution
Equities	58.8%	35.2%
Mutual funds	10.6	38.5
Bonds	21.9	6.7
Cash	3.1	4.5
GICs	3.6	8.7
Other	2.0	6.4
Total	100.0	100.0

Source: U.S. Board of Governors of the Federal Reserve System (2006).

Figure 3 shows the percentage of the portfolios in equities for defined benefit and defined contribution plans over the period 1988-2005, where a portion of mutual funds are included in equities as described above. The higher share in equities for defined contribution plans in the late 1990s allowed 401(k) plans to outperform defined benefit plans. The reliance on equities also meant that 401(k) participants were hurt more when the stock market collapsed in 2000, and then did better when the stock market recovered.

Figure 3. Equities as a Percentage of Total Portfolio for Private Defined Benefit and Defined Contribution Plans, 1988-2005



Sources: Authors' calculations from U.S. Board of Governors of the Federal Reserve System (2006); Investment Company Institute (2005); and Investment Company Institute (2006b).

One interesting aspect of Figure 3 is not the difference between the defined benefit and defined contribution portfolios, but the fact that both professional managers and individual 401(k) participants dramatically increased their holdings of equities over the period. If defined benefit portfolios were optimally balanced in the early 1990s with about 40 percent in equities, what would make 65 percent optimal by the end of the period? In the case of defined benefit plans, an aging beneficiary population would argue, if anything, for less equity investment. Some potential explanations include: 1) professional managers, like individual investors, forgot to re-balance; 2) professional managers, like individual investors, got swept up in the euphoria of the boom and purposely increased their holdings of stocks; 3) sponsors of fully funded defined benefit plans felt like they could gamble with their "surplus" funds; or 4) defined benefit managers wanted to hold the market portfolio and the boom caused equities to increase as a share of the total market. Regardless of the explanation, defined benefit and defined contribution plans both held 40 percent of their portfolios in equities in 1990 and increased their holdings to 65 percent by 2000. The difference is that during most of that period, individual 401(k) investors had higher equity holdings.

The Role of Fees

Another possible explanation for the lower return in defined contribution plans is investment fees, which typically account for 75 to 90 percent of total expenses associated with managing 401(k) plans.[9] These fees compensate providers of, say, mutual funds for selecting the stocks and undertaking the research that leads to buy and sell decisions. These fees are usually assessed as a percentage of invested assets, and are paid by the employee in that they are deducted directly from investment returns.[10]

Mutual funds are the major investment vehicle for 401(k) participants, and Table 5 reports the fees for alternative investments. The fees vary substantially depending on whether the investments are actively managed or follow an index. For example, an actively managed Global Fund costs 1.72 percent of assets annually compared to 0.59 percent for an S&P Index Fund. Given these charges, it is probably reasonable to assume that fees reduce the gross return on 401(k) plans by about one percentage point.

Of course, defined benefit plans also involve some expenses but these are small compared to those associated with 401(k) plans.[11]

Table 5. Annual Fund Fees as a Percent of Assets, [illegible]

Category	Fee
Global Fund	1.72%
Equity Income Fund	1.33
Balanced Fund	1.22
Intermediate Bond Fund	0.92
S&P Index Fund	0.59
Institutional Money Market Fund	0.45

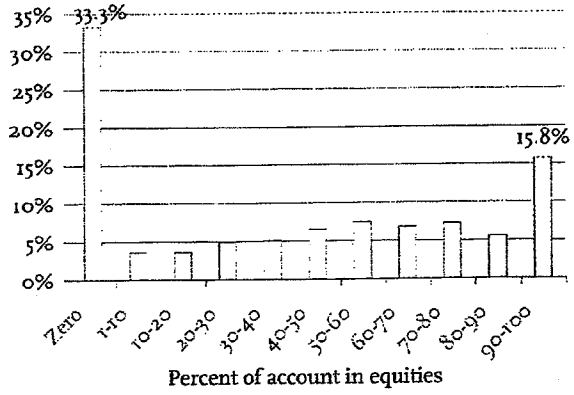
Source: Lipper (2006).

The Implications for Individual 401(k) Participants

So far the discussion has focused only on totals and averages, which tell us little about how individuals might invest. After all, if a plan has 100 participants and half invest all their assets in stocks and the other half all their assets in bonds, the aggregate data suggest that participants are well diversified when in fact they are not. Therefore, it is useful to look at investment data from particular 401(k) plans to see whether the individual participants have balanced portfolios or whether the balance simply reflects offsetting behavior.

As shown in Figure 4, detailed data on the asset allocation of individual participants show that nearly half of all participants have either none of their account in equities or virtually all of their account in equities. So even though the aggregate data suggest that participants make sensible investment choices on average, the individual data reveal that a majority of participants are not diversified at all. Given their choices, most participants face the risk of ending up with inadequate retirement income or exposing themselves to large swings in the value of their assets.[12] Thus, the one percentage point difference in returns between defined benefit and 401(k) plans understates the poor investment decisions made by individuals.

Figure 4. Distribution of Participants in 401(k) Plans by Percentage Allocation to Equities, [illegible]



Source: Holden and VanDerhei (2006).

Table 6. Asset Holdings and IRAs by Institution, [illegible]

Institution	Percent of total
Mutual funds	39.0 %
Life insurance companies	11.1
Money market mutual funds	4.4
Commercial banking	4.6
Saving institutions	1.5
Credit unions	1.3
Other self-directed accounts	38.0
Total	100.0
Memorandum: total assets (billions)	$3,667.0

Source: U.S. Board of Governors of the Federal Reserve System (2006).

The Inclusion of IRAs

It has become impossible to ignore the role of IRAs. As shown earlier in Table 1, IRAs now hold more money than either defined benefit or defined contribution plans. And even though most IRAs are not sponsored by employers, the Investment Company Institute (2006b), the national association for mutual fund companies, reported that 94 percent of the money flowing into traditional IRAs was rolled over from employer-sponsored plans in the period 1997-2003.[13] Although detailed information is not available, it is probably reasonable to assume that most of the rollovers come from defined contribution plans — although lump-sum payments are becoming increasingly common in defined benefit plans.

Only limited information is available on the asset allocation in IRAs. The Flow of Funds data show only the type of institution holding the account, as opposed to the type of asset in the account (see Table 6). About 73 percent of the mutual fund assets — the

largest component — are in stock.[14] But no information is available on the composition of IRA assets held by other institutions, which hold the majority of the assets.

The Investment Company Institute (2006a) provides data on beginning-year assets, year-end assets, contributions, rollovers, and withdrawals for traditional IRAs that make it possible to calculate the aggregate average return for the period 1998-2003. Table 7 summarizes these results and compares them to returns earned on defined benefit and 401(k) plans over the same period. If estimates of the flows into and out of IRAs are correct, the rate of return numbers suggest that IRA investments produced significantly lower returns than either defined benefit or 401(k) plans during the six-year period.[15] More important than the precise numbers, however, is the message that the performance of IRAs will have a significant impact on the retirement security of people in the future.

[illegible]

Year	IRA	Defined benefit	401(k)
1998	13.6 %	14.9 %	17.8 %
1999	15.7	15.5	13.1
2000	-6.0	1.8	-2.4
2001	-4.6	-5.1	-5.1
2002	-8.1	-8.9	-9.5
2003	12.1	21.2	19.4
1998-2003	3.8	6.6	5.6

Source: Authors' estimates based on Investment Company Institute (2006a).

Conclusion

Three main conclusions emerge from this review. First, defined benefit plans outperformed 401(k) plans over the period 1988-2004. This conclusion is most evident using the weighted median. A higher equity allocation most likely led to higher 401(k) returns during the 1990s, while fees inevitably reduced returns. These two effects may well have balanced each other out, leaving a one percentage point shortfall due to poor timing and other investment mistakes.

Second, lower returns are only one component of the investment problems facing 401(k) investors. The other is that despite a reasonable mix for 401(k) assets in the aggregate, nearly half of 401(k) participants are either nearly fully invested in stocks or hold no stocks at all. That is, nearly 50 percent of participants are not diversified in their retirement accounts. The combination of the lack of diversification and the lower returns suggests that introducing balanced portfolios as a default, which would remove the individual from the decision making, would significantly improve the performance of 401(k) plans.

Finally, IRAs are now bigger than either defined benefit or defined contribution plans, and their performance is going to have a major impact on retirement security in the future. Preliminary data suggest that IRAs underperform employer-sponsored plans. IRAs are too big and important a form of retirement saving to not know what is going on with these accounts. Some mechanism is needed to identify the asset allocations in these accounts as well as document the inflows and outflows. Only by including IRAs will it be possible to understand fully how well people are investing for retirement.

Endnotes

1 This formulation follows Watson Wyatt (2002 and 2003). Calculations for the entire universe of plans showed very similar results.

2 Including one half of contributions less benefits assumes that net inflows occur at an even rate over the year so that on average half the annual net inflows are available for investment. This assumption is necessary because the Form 5500 lacks detailed information on the timing of benefits and contributions over the year.

3 See Buessing and Soto (2006) for a detailed description of the Form 5500 data.

4 The median refers to the across-firm rates of return per year for defined benefit and defined contribution plans. The average returns shown are the arithmetic means of the median rates of return over the period 1988-2004. The geometric means do not differ widely from the arithmetic means calculated for the unweighted and weighted median rates of return. Appendix Table A1 shows the unweighted and weighted median rates of return as well as the arithmetic and geometric means.

5 For the 1990-2002 period, the results are similar to results from Watson Wyatt (2004) with defined benefit plans outperforming 401(k) plans. The difference in defined benefit and 401(k) returns is 0.35 percent while Watson Wyatt showed a difference of 0.56 percent for this period. The improved performance of 401(k)s over the 1988-2004 period comes simply from adding four more years of data to what was a very close outcome.

6 Separate data on 401(k) plans are not available on a comparable basis. But in 2004, 401(k) assets accounted for 88 percent of total private sector defined contribution assets for plans sponsored by employers with 100 or more employees. See Munnell and Perun (2006).

7 Since most 401(k) participants invest through mutual funds, the high number for "Equities" for defined contribution plans (that is, direct equity holdings as opposed to equities held through mutual funds) in Table 4 is surprising. The explanation is that "Equities" include pools of stocks that companies set up themselves for their 401(k) plans; only mutual funds bought off the shelf are included in the mutual fund line. The other large category of direct equity holdings is employer stock. The final category of direct equity investment arises from a relatively small percentage of 401(k) participants who invest directly through brokerage accounts.

8 Investment Company Institute (2006a).

9 Munnell and Sundén (2004).

10 Fees are generally not explicitly reported in the Form 5500. See U.S. Department of Labor (2004).

11 Council of Institutional Investors (2005).

12 Of course, critics contend that assessing individuals' 401(k) holdings without knowing their entire asset holdings is of limited value. They argue that most people who save through a 401(k) plan also have Social Security, human capital, defined benefit pension wealth, housing, and taxable savings. But for most people taxable savings are miniscule, and their 401(k) plan is their major financial asset. Thus the investment allocation within their 401(k) plan is important.

13 In 2005, assets in traditional IRAs accounted for 90 percent of total IRA assets. This share was down slightly from 95 percent in 1997.

14 Investment Company Institute (2006a).

15 One likely explanation for the lower returns in IRAs is that IRAs are often held by older workers who have rolled over their 401(k) assets. Older workers tend to invest in assets with lower returns to avoid the potentially large fluctuations that are associated with riskier investments.

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APPENDIX

Appendix A

Table A1. Unweighted and Weighted Median Rates of Return for Defined Benefit and 401(k) Plans, 1988-2004

Year	Unweighted		Weighted	
	Defined benefit	401(k)	Defined benefit	401(k)
1988	9.8	10.1	12.4	12.7
1989	12.0	11.3	19.1	13.7
1990	4.2	5.7	1.0	5.2
1991	15.4	13.1	20.6	13.7
1992	7.1	7.7	6.8	8.5
1993	8.0	8.2	11.9	9.2
1994	0.0	2.3	0.3	3.2
1995	19.6	17.8	23.7	19.3
1996	12.6	12.9	15.0	15.4
1997	16.3	17.4	19.0	19.6
1998	12.1	14.6	14.9	17.8
1999	10.6	12.4	15.5	13.1
2000	-0.3	-4.9	1.8	-2.4
2001	-4.4	-7.1	-5.1	-5.1
2002	-8.2	-11.7	-8.9	-9.5
2003	16.7	19.4	21.2	19.4
2004	9.3	9.7	12.5	10.5
Arithmetic Mean	8.3	8.2	10.7	9.7
Geometric Mean	8.0	7.8	10.2	9.3

Source: Authors' calculations from U.S. Department of Labor (1990-2006).

AN ISSUE IN BRIEF
CENTER FOR
RETIREMENT
RESEARCH
AT BOSTON COLLEGE

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PERS Oregon Public Employees Retirement System

BENNETT, HARTMAN, MORRIS & KAPLAN, LLP
JUL 8 - 2010
5415-237
PORTLAND, OREGON

THE CREVELING COMPANY

July 6, 2010

Gregory A. Hartman
Bennett, Hartman, Morris & Kaplan
111 SW Fifth Avenue, Suite 1650
Portland, OR 97204-1376

Re: Defined Contribution / Defined Benefit equivalence testing

Dear Greg:

You have asked for my opinion as to a reasonable approach in testing whether an individual's benefit from a defined contribution plan is equivalent to a benefit from a defined benefit plan. You have asked your question in the context of an individual at retirement in a defined contribution plan and where the defined benefit plan is PERS Tier 1, PERS Tier 2 or OPSRP.

My opinion is that the account balance in the defined contribution plan should be annuitized over the Member's lifetime and compared with the corresponding benefit the individual would have received from the respective defined benefit plan.

With regard to the interest and mortality assumptions to be used in calculating the annuity factor to convert the account balance to monthly income I would be inclined to use those which reflect current pricing in the annuity marketplace available to plan sponsors. For this I would suggest using the interest and mortality assumptions in the immediate and deferred annuity rates of the Pension Benefit Guaranty Corporation (PBGC).

In 29 CFR Part 4044 under General valuation approach the regulation states in part "The assumptions prescribed by this rule for valuing benefits in terminating plans match the private-sector annuity market to the extent possible".

For your information, the current mortality assumption is the GAM-94 Basic Table (male or female) projected for mortality improvements with Scale AA. The July 2010 interest rates are 4.93% per year for the first 20 years following the valuation date and 4.66% thereafter. Over the 17 year period spanning the period of the current and previous mortality tables the interest rates have varied from a low of approximately 3.5% to a high of approximately 8% (economic fright of December 2008). In the majority of months the rates were in the 4% to 6% range.

It is important to note that in calculating the annuity factor to convert the account balance to monthly income that the ORS Chapter 238 2% annual cost of living adjustment should be included as well.

1180 S.W. Chestnut Drive • Portland, OR 97219-2167 • (503) 246-1654

Re: Defined Contribution / Defined Benefit equivalence testing

In support of this opinion you have asked for qualifications and experience. A record of my employment history and qualifications is attached.

Over the last 26 years my practice has changed from a traditional pension practice of dealing directly with retirement plans to valuing a Member's monthly benefit from a defined benefit plan in the context of a divorce. The purpose of the valuation in generally to compare the value of the defined benefit plan with defined contribution plans or other assets. In round numbers I have completed approximately 10,000 PERS Tier 1, PERS Tier 2 or OPSRP valuations. In doing this work I use the interest and mortality assumptions of the Pension Benefit Guaranty Corporation along with the Chapter 238 2% cost of living adjustment.

To my knowledge all Oregon and Southwest Washington courts routinely accept PERS / OPSRP valuations calculated with the assumptions indicated above. In addition, the market pricing approach receives acceptance in Section 5 of *Richardson and Richardson* (307 Or 370 (1989)).

Note: Acknowledgement of Qualification under Section V of the *Qualification Standards for Prescribed Statements of Actuarial Opinion* of the American Academy of Actuaries.

> I am an Enrolled Actuary and a Member of the American Academy of Actuaries and meet the Qualification Standards of the American Academy of Actuaries to render the actuarial opinion contained herein.

Please give me a call if you have any questions.

Sincerely,

Bradford A. Creveling, EA, MAAA
President

Oregon

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July 23, 2010

TO: Members of the PERS Board

FROM: Gay Lynn Bath, Deferred Compensation Manager

SUBJECT: Appoint Advisory Committee Members for Oregon Savings Growth Plan

OVERVIEW

- Subject: The PERS Board needs to appoint two new members and renew the appointment of two current members to the Oregon Savings Growth Plan ("OSGP") Advisory Committee.
- Action: Appoint two new members; one to fill the unexpired term for a state employee vacancy and one to fill the retiree vacancy. Renew the appointment of two current members.
- Reasons: The Advisory Committee consists of seven members appointed by the PERS Board for fixed terms, but each member serves at the pleasure of the PERS Board.

BACKGROUND:

ORS 243.505 provides for an Advisory Committee for the Oregon Savings Growth Plan that consists of seven members with knowledge of deferred compensation plans. According to that statute and OAR 459-050-0025 (attached hereto), the Committee shall study and advise the Public Employees Retirement Board, upon request, on all aspects of the deferred compensation program, including but not limited to:

(a) The deferred compensation program fee structure and program procedures;

(b) State and federal legislative issues relative to the administration of deferred compensation;

(c) Administration of the catch-up and financial hardship provisions in Section 457 of the Internal Revenue Code;

(d) Ways and means to inform and educate eligible employees about the deferred compensation program;

(e) The expressed desires of eligible employees as to the Deferred Compensation Program.

Advisory Committee members must be OSGP participants and have knowledge of the current program. One member shall be retired from state service. Two members shall be participants with separate local government plan sponsors who offer the OSGP. Four members shall be employees of separate state agencies. No member shall be an employee of PERS during the term of appointment. No two members shall be employed by the same state agency or local government plan sponsor.

Appointment is for three years except in the case of a vacancy during an unexpired term, in which case the Board's appointment will become immediately effective for the remainder of the unexpired term. A member is eligible for reappointment, but no person shall serve more than two consecutive full terms.

Currently, the Advisory Committee is made up of the following members:

Name	**Employer/City**	**Term**	**Term Ends**
Peter Farrelly, Interim Chair	DHS, Portland	First	6/30/2010
Keith Baldwin	Department of Forestry, Molalla	First	6/30/2011
Brian Burleigh	ODOT, Bend	First	6/30/2010
John Lattimer	Marion County, Salem	First	6/30/2012
Robert Swank	LCOG, Eugene	First	6/30/2012
Open	Retiree Position		
Open	State Position		6/30/2011

The criteria staff uses in selecting Advisory Committee members includes:

1. Current participation in OSGP.
2. Meeting the qualifications for the slot to be filled.
3. Possessing a mixture of expertise, knowledge and experience useful to Advisory Committee
4. Sincere interest in deferred compensation program.
5. Willing and able to work in a group setting to review and recommend policies governing the program.

RECOMMENDED APPOINTMENTS

The first 3-year terms of Brian Burleigh and Peter Farrelly will expire on June 30, 2010. OSGP staff recommends reappointing them for additional 3-year terms.

Staff also recommends Sharlyn Rayment, from Salem, to fill the vacant retiree position and Priyanka Shukla, from the Department of Revenue in Salem, to fill the unexpired term of the vacant state employee position.

Board Options:

The Board may:

1. Accept the recommendation to appoint Sharlyn Rayment as the new retiree member on the Advisory Committee, effective immediately.
2. Accept the recommendation to appoint Priyanka Shukla to fill the vacancy of the unexpired term for a state employee, effective immediately.
3. Accept the recommendation to appoint Brian Burleigh and Peter Farrelly to second 3-year terms.
4. Direct staff to solicit new nominations for any or all of the positions.

Staff Recommendation:

Staff recommends the Board adopt Options 1, 2 and 3 above.

Reason: Staff believes Sharlyn Rayment and Priyanka Shukla meet the criteria and service needs of the Advisory Committee, and Brian Burleigh and Peter Farrelly have served well during their first term and are assets to the committee.

PERS Oregon Public Employees Retirement System

Adopted: 1/12/07
Filed and Effective: 1/23/07

OREGON ADMINISTRATIVE RULE
PUBLIC EMPLOYEES RETIREMENT BOARD
CHAPTER 459
DIVISION 050 – DEFERRED COMPENSATION

459-050-0025
Deferred Compensation Advisory Committee

(1) The seven members of the Deferred Compensation Advisory Committee provided for under ORS 243.505, shall be subject to the following qualifications and limitations:
(a) Each member shall be a participant in a deferred compensation plan established under ORS 243.401 to 243.507, and shall have knowledge of the Program.
(b) Four members shall be participants in the state deferred compensation plan.
(c) Two members shall be participants in a local government deferred compensation plan.
(d) One member shall be a retired deferred compensation plan participant.
(e) No two members may be employed by the same state agency or local government except that a member who transfers employment to the employer of another member may continue to serve on the Advisory Committee, but only for the balance of the term of appointment of the transferring member.
(f) No member may serve more than two consecutive full terms.
(g) No member may be an employee of PERS during the term of appointment.
(2) The Advisory Committee shall study and advise the Board on all aspects of the Program, including but not limited to:
(a) The Program fee structure and procedures;
(b) State and federal legislative issues relative to the administration of deferred compensation plans;
(c) The administration of the catch-up and the financial hardship provisions in Section 457 of the Internal Revenue Code;
(d) Ways and means to inform and educate eligible employees about the Program;
(e) The expressed desires of eligible employees as to the Program; and
(f) The actuarial characteristics of eligible employees.
(3) Upon the request of the OIC, the Advisory Committee shall study and advise the Board on the following:
(a) Investment programs, including options and providers; and
(b) Information furnished by the OIC or the State Treasurer concerning the types of available investments, the respective balance of risk and return of each investment, and the administrative costs associated with each investment.
(4) The Advisory Committee shall meet at least four times during a calendar year.
(5) A majority of the Advisory Committee shall constitute a quorum for transacting business. However, the Advisory Committee may establish such other procedures for conducting business that it deems necessary.
(6) Pursuant to the Public Meetings Law, ORS 192.610 to 192.690, the Deferred Compensation Manager shall distribute to the Advisory Committee, and other interested parties, an agenda for a regular meeting a reasonable time prior to the meeting.
(7) Nominations of candidates for the Advisory Committee shall be made as follows:
(a) Notice of a position on the Advisory Committee expected to become vacant upon the expiration of a term of appointment shall be published not later than April 15 of each calendar year.

(b) Persons interested in serving on the Advisory Committee must apply in writing to the Manager not later than May 15 following the publication of a vacancy.
(c) The Manager shall review the written applications of interested persons for completeness, accuracy, and satisfaction of the minimum requirements of the vacant position on the Advisory Committee.
(d) A committee consisting of the Manager and four members of PERS executive or managerial staff designated by the PERS Executive Director shall review the acceptable applications and recommend to the Board candidates for appointment to the Advisory Committee that:
(A) Reflect a cross section of state agencies, participating local governments, and classification levels;
(B) Reflect a mixture of expertise, knowledge, and experience useful to the Advisory Committee;
(C) Appear to have a sincere interest in the Program; and
(D) Appear to be willing and able to work in a group setting to review and recommend policies governing the Program.
(e) In the event of a vacancy for an unexpired term, the Manager may select applications from the most recent list of interested persons established under subsection (c) of this section and the applications of other persons as deemed appropriate for consideration. A committee consisting of the Manager and four members of PERS executive or managerial staff designated by the PERS Executive Director shall review the selected applications and recommend to the Board candidates for appointment to the Advisory Committee. The appointment shall be immediately effective for the remainder of the unexpired term. If no candidate is recommended or appointed, the vacancy must be filled under the provisions of subsections (a) through (d) of this section.

Stat. Auth: ORS 243.470
Stats. Implemented: ORS 243.505

Oregon

Theodore R. Kulongoski, Governor

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July 23, 2010

TO: Members of the PERS Board

FROM: Kyle Knoll, Business Operations Manager

SUBJECT: 2011-13 Agency Request Budget

OVERVIEW

- Action: Request Board approval of PERS' 2011-13 Agency Request Budget (ARB) for submission to the Department of Administrative Services (DAS).
- Reason: To complete and submit the 2011-13 Agency Request Budget to the DAS Budget and Management Office by early August 2010.

BACKGROUND – 2009-11 BUDGET

PERS' original Legislatively Adopted Budget for the current biennium was $80.1 million, with 364 positions. This included a base budget of $59.4 million with 298 positions, supplemented by Policy Option Packages (POPs) that totaled $20.7 million with 66 positions, of which 35 were limited duration and 31 were permanent. Those Policy Option Packages (POPs) were:

1. Business Process Owners. Five limited duration positions to continue serving as Business Process Owners (BPO) Team, coordinating the execution and completion of the RIMS Conversion Project (RCP); refining core business operations; and implementing and monitoring process improvements across the agency.
2. Maintenance & Enhancement of Current Service Levels. Twenty-one permanent positions and twenty-three limited duration positions to continue to support current service level needs across the agency, including program services for the Individual Account Program (IAP), centralized intake for retirement documents, ongoing and increasing workload in retirement benefit calculations, and improved timeliness for eligibility determinations.
3. Infrastructure Maintenance & Enhancement. Three limited duration positions to continue addressing document imaging, and mailroom and supplies workloads. This Policy Option Package (POP) also included limitation for leased office facilities, and maintenance and service charges for leased software and periodic hardware replacement.
4. Enterprise Applications. Four limited duration positions to support data quality/integrity workload needs, and enterprise test and tools development. This Policy Option Package (POP) also included limitation for the RIMS Conversion Project (RCP) and contractor support to screen and prepare data for conversion to the new retirement administration system.

5. Standards, Training, & Certification. Funding limitation to contract for auditing and fiscal reporting services and software.
6. Data Transition & Standard Tool Development. Ten permanent positions to address the agency's challenges in bridging data from the current legacy system to other off-line applications developed to support the new retirement administration system; and develop operational reports to assist in managing data and accounts to incept, calculate and process benefits and payments.
7. Legal Services. Increased funding limitation for legal services related to PERS Board fiduciary counsel, and agency's ongoing need for outside litigation and federal tax counsel.
8. Budget Reconciliation Adjustments (HB 5054). Other Funds reductions of $2,113,017 to the expenditure of appropriated funds. These reductions included removing salary step increases built into the Governor's Recommended Budget (GRB), a decrease in the Department of Justice's hourly rate, and reductions in the Department of Administrative Services (DAS) assessments and charges.

The originally approved 2009-11 Legislatively Approved Budget was increased from $80.1 million to $83.2 million with 368 positions authorized by two subsequent budget actions:

1. February 2010 Special Session. The legislature's over-ride of the Governor's veto of SB 897 also included the budget authority in that bill, which increased PERS' budget limitation by $500.000.

2. May 2010 Emergency Board. The legislature's Emergency Board approved an increase in PERS' budget limitation of $2.6 million, and added six positions (2 Permanent, and 4 Limited Duration) for implementing SB 399 and SB 897.

2011-13 AGENCY REQUEST BUDGET (ARB)

The 2011-13 Agency Request Budget (ARB) and supporting Policy Options Packages (POPs) have been developed with the strategic goals of:

- Continuing to stabilize the agency's core business operations by requesting that limited duration positions approved in 2009-11 and identified as essential for maintaining current service levels be approved as permanent positions in 2011-13.
- Maintaining and continuing process improvements implemented during 2009-11.
- Holding the line, by maintaining a 2011-13 operating budget limitation in line with the agency's 2009-11 budget limitation of $83.2 million, despite significant increases in State Government Service Charges ($690,000), Legislative Concept fiscal impacts ($1,075,000), and the costs associated with funding salary adjustments ($1.2 million).
- Maintain no net increase in agency staffing levels above the previous biennium staffing as supplemented by the Emergency Board's approval of six additional positions to begin implementation of SB 897.

A high-level summary of the agency's six 2011-13 Policy Option Packages is provided below.

Policy Option Package (POP) 131 Business Enterprise – Core Business Functions. Requests about $5.1 million in funding for resources needed to continue progress on process improvements PERS initiated during 2009-11, and to maintain service levels achieved as a result of those process improvements. Improved service levels include:

- Retirement benefits paid within 45 days of the member's effective retirement date increased from 10% in 2008 to 23% in 2009. Performance on this metric has greatly improved in 2010, with almost 60% of retirement benefits paid with 45 days of effective retirement date through June of this year.
- Accounts requiring eligibility investigations have decreased from 21% to 16% by improving the eligibility review process.
- The time allowed for employers to correct member accounts has increased from 30 to 60 days by improving the transaction notification and employer coordination process.
- A pro-active model of eligibility review has been implemented, with 25% of estimate requests being reviewed for increased estimate accuracy.
- A new accuracy-related Key Performance Measure has been developed for consideration by the 2011 legislature. It will be supported by both agency-wide and section-specific accuracy initiatives and a formal corrective action process. The objective is for monthly retirement benefits to be calculated with no more than a $5.00 error.

Policy Option Package (POP) 132 Infrastructure Maintenance & Enhancement. Requests about $2.9 million in funding for basic services and tools that enable agency staff to perform their duties effectively and efficiently. Those basic services and tools include office space and utilities infrastructure, maintenance and enhancement of enterprise systems, disaster recovery infrastructure improvements, production control, and ORION system development and support.

Policy Option Package (POP) 133 Position Reclass. Requests $186,666 in funding for the reclassification of twenty positions within the Information Services Division (ISD), to align those positions with increasingly complex work duties required to maximize in-house agency support of Information Technology (IT) needs. Those duties include higher level technical infrastructure analysis, planning, and design; operational procedures and monitoring to improve system performance and availability; expanded skill sets in enterprise architecture analysis, planning, and design; and improved processes for digitally processing agency data, information, forms, and reports.

Policy Option Package (POP) 134 Legislative Concept: PERS Housekeeping Bill. Requests $475,600 in funding for system programming upgrades supporting proposed changes to OPSRP Pension program and IAP Employer account vesting provisions.

Policy Option Package (POP) 135 Legislative Concept: Repeal Guarantee of Inaccurate Benefits. Requests $599,300 in funding for system programming upgrades to remove restrictions on

benefit changes based on corrected information received by PERS that results in an adjustment to future benefits.

Policy Option Package (POP) 136 Legislative Concept: OPSRP Pension Withdrawal Restrictions. This is a "placeholder" policy option package for system programming upgrades relating to changes on the withdrawal options available to OPSRP Pension program members. As submitted, this Legislative Concept would not have a fiscal impact.

2011 - 13 Agency Request Budget (ARB) At-a-Glance - Operating Budget		
2009-11 Operating Budget (Actual)	368 Positions	$83,261,952
2011-13 Operating Budget (Request)	Positions	Limitation
Current Service Level (CSL)	325 Perms	$54,394,574 (PS) 19,460,861 (S&S) 607,833 (CO)
	325 Perms	$74,463,268
POP 081: May 2010 E-Board (SB 897)	2 Perms (C)	$288,775 (PS) 13,000 (S&S)
	2 Perms	$301,775
POP 131: Business Enterprise - Core Business Functions	29 Perms (C) 4 Perms (C/E) 4 Perms (N)	$4,869,827 (PS) 247,850 (S&S)
	37 Perms	$5,117,677
POP 132: Infrastructure Maintenance & Enhancement	3 Perms (C) 1 Perm (N)	$626,065 (PS) 1,914,140 (S&S) 334,000 (CO)
	4 Perms	$2,874,205
POP 133: Position Reclass / Realignment	20 Re-classes	$186,666 (PS)
POP 134: Legislative Concept / PERS Housekeeping Bill		$475,600 (S&S)
POP 135:Legislative Concept - Repeal Guarantee of Inaccurate Benefits		$599,300 (S&S)
POP 136:Legislative Concept - OPSRP Pension Withdrawal Restrictions	Placeholder	$1 (S&S)
2011-13 Operating Budget (Request)	368 Positions	$84,018,492

Legend:

(C) - Converting 2009-11 LD to Perm
(E) - May 2010 E-Board / SB 897 Positions
(N) - New Positions in 2011-13
(PS) - Personal Services
(S&S) - Service and Supplies
(CO) - Capital Outlay

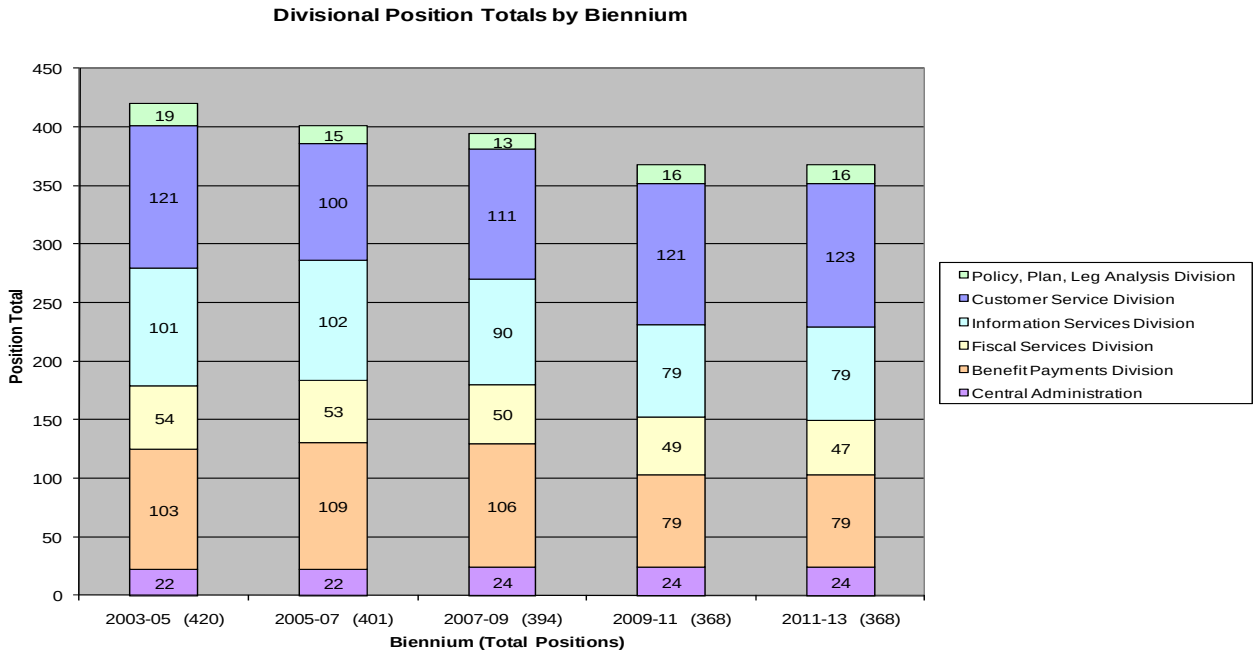
BUDGET COMPARISONS

The following table shows the agency's operating budget in absolute dollars and on a basis point comparison to the PERS Fund over the ten-year time period shown:

PERS Budget / PERF Comparison – 2003 to 2013

Biennium	Legislatively Approved Operations Limited Budget	Fiscal Year Ended June 30th	Limited Budget	PERF Balance	Percent
2003-2005	$ 85,863,923	2004	$ 42,931,962	$ 46,031,766,920	0.0933%
		2005	$ 42,931,961	$ 50,613,623,493	0.0848%
2005-2007	$ 78,371,793	2006	$ 39,185,897	$ 56,554,878,450	0.0693%
		2007	$ 39,185,896	$ 66,009,334,073	0.0594%
2007-2009	$ 81,251,146	2008	$ 40,625,573	$ 61,409,698,133	0.0662%
		2009	$ 40,625,573	$ 46,020,175,297	0.0883%
2009-2011	$ 83,261,952	2010	$ 41,630,976	$ 53,809,195,492	0.0774%
		2011	$ 41,630,976	$ 48,904,338,621	0.0851%
	ARB				
2011-2013	$ 84,018,492	2012	$ 42,009,246	$ 50,247,942,984	0.0836%
		2013	$ 42,009,246	$ 51,591,547,347	0.0814%

Although the agency's 2011-13 budget request is a small increase in absolute dollars over the previous biennium, it still represents a stable percentage of the PERS Fund. Similarly, the following graph shows the agency's staffing levels by division over the previous biennia. As detailed, total staffing peaked in the 2003-05 biennium at 420 positions and has been declining since then. The ARB for 2011-13 will hold the line at the 368 positions already approved through the agency's current 2009-11 Legislatively Approved Budget.



NEXT STEPS/BOARD OPTIONS

PERS is required to submit its Agency Request Budget (ARB) to DAS early in August 2010. To allow staff adequate time to prepare this submission, staff requests that the PERS Board approve the 2011-13 Agency Request Budget (ARB) at this meeting.

The Board may:

1. Approve the 2011-13 Agency Request Budget (ARB) as presented in this report for submission to DAS.
2. Direct the staff to further refine the budget request in specific areas.

STAFF RECOMMENDATION

Staff recommend the Board approve the 2011-13 Agency Request Budget (ARB) as presented for submission to DAS.

Oregon

Theodore R. Kulongoski, Governor

Public Employees Retirement System
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Mailing Address:
P.O. Box 23700
Tigard, OR 97281-3700
(503) 598-7377
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July 23, 2010

TO: Members of the PERS Board

FROM: Dale S. Orr, Manager, Actuarial Analysis Section

SUBJECT: 2009 Valuation System-wide Results

On July 23, 2010, PERS actuaries Matthew Larrabee and Scott Preppernau will present system-wide results from the 2009 Valuation. This presentation, in part, will reflect the impact of the 2008 market downturn and the 2009 investment recovery on system funded status and employer rates at the pooled level.

While the 2009 Valuation will be the basis for setting employer contribution rates for the period beginning July 1, 2011 through June 30, 2013, individual employer rates will not be ready for Board adoption until the September Board meeting.

PERS Oregon Public Employees Retirement System

MERCER

Consulting. Outsourcing. Investments.

MARSH MERCER KROLL
GUY CARPENTER OLIVER WYMAN

July 23, 2010

December 31, 2009 Actuarial Valuation

Oregon Public Employees Retirement System

Matt Larrabee, FSA
Scott Preppernau, FSA

Contents

- Key Findings
- December 31, 2009 Tier 1/Tier 2 and OPSRP Valuation
  - Demographics
  - Assets
  - Liabilities
  - Funded Status
  - Contribution Rates
- December 31, 2009 Retiree Healthcare (RHIA, RHIPA) Valuation
- Next Steps

Key Findings
Overview of System-Wide December 31, 2009 Valuation Results

- Funded status improved during 2009, but is still well below 2007 levels

Tier 1/Tier 2/OPSRP Combined Funded Status as of December 31			
	2007	2008	**2009**
Excluding side accounts	98%	71%	**76%**
Including side accounts	112%	80%	**86%**

- Side accounts represent the market value of deposited but not-yet-utilized prepaid contributions for employers that voluntarily elected to establish side accounts
- Year-to-date 2010 (regular account) investment return through May 31 was -0.8%
  - If overall 2010 return turned out to be -0.8%, we would project December 31, 2010 funded status to decrease to 70% excluding side accounts and 78% including side accounts
  - Contribution rates will not be affected by 2010 investment returns until July 2013, based on results of the December 31, 2011 valuation
- Rates are set biennially based on results of "odd year" actuarial valuations
  - 2009 funded status excluding side accounts is used to set 2011-2013 employer rates
  - 2011-2013 employer contribution rates will increase sharply from their historic lows

Key Findings
Overview of System-Wide December 31, 2009 Valuation Results

- Current policy sets rates to pay off Tier 1/Tier 2 shortfalls over 20 years as a level percent of employer payroll if assumptions are met
- Policy includes a rate collar, which spreads large rate changes across more than one biennium

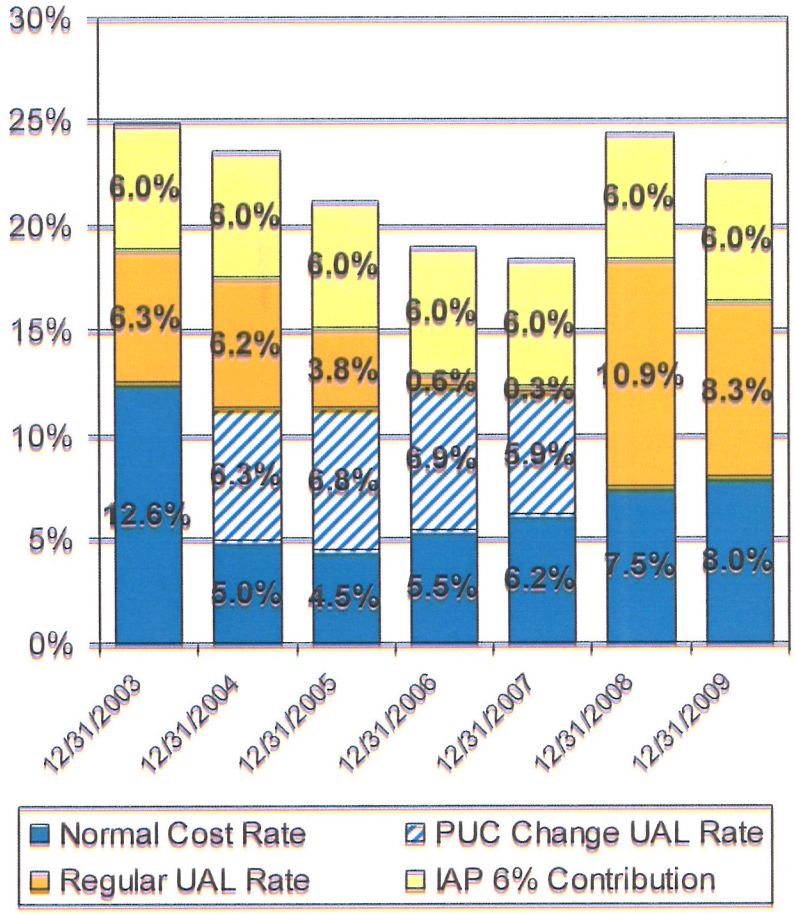
System-Wide Tier 1/Tier 2/OPSRP Plus Retiree Healthcare Contribution Rates			
	2009-2011	**Collared 2011-2013**	Uncollared 2011-2013
Base rates (before effect of side account offsets)	12.4%	**16.3%**	20.3%
Net rates (reflect side account rate offsets)	5.2%	**10.8%**	14.8%

- Unlike base rates, net rates are affected by side account rate offset levels, which will be lower in 2011-2013 due to the 2008 market downturn
- Individual employers with large side accounts will have individual net rate increases greater than the system-wide net rate increase
- Rates shown above do not include contributions to the Individual Account Program (IAP) or debt service payments on pension obligation bonds

Key Findings

Average Base Contribution Rates Including Retiree Healthcare and IAP

- Since active Members projected to retire under the Money Match formula do not generate normal cost, normal cost rates are expected to increase over time as the system continues to migrate from Money Match to Full Formula and OPSRP
  - That migration temporarily accelerated due to the 2008 market downturn
- The regular unfunded actuarial liability (UAL) rate is significantly higher than the rate currently in effect, which was set at 12/31/2007, due to investment losses
  - Absent the rate collar, the regular UAL rate would be 12.3%
- The UAL established at the adoption of the projected unit credit (PUC) cost allocation method will be fully amortized by July 2011
- Rates shown here do not reflect the impact of side accounts or pre-SLGRP liabilities or surpluses



Key Findings

Average Base Contribution Rates Including Retiree Healthcare (Excluding IAP)

- While system-wide base rates increased by 3.9% of payroll, the increase varied from rate pool to rate pool
  - For example, since the State and Local Government Rate Pool (SLGRP) is more well funded (77% funded status excluding side accounts) than the School District rate pool (74%), SLGRP has a narrower rate collar

Average Base Employer Rates	SLGRP	School Districts	Indepen-dents[1]	OPSRP General	OPSRP P&F	System-Wide
2009-2011 Base Rates	11.4%	14.3%	10.7%	12.0%	14.7%	12.4%
2011-2013 Base Rates	**15.8%**	**19.5%**	**14.6%**	**14.5%**	**17.2%**	**16.3%**
Base Rate Increase	4.4%	5.2%	3.9%	2.5%	2.5%	3.9%

- Changes in base rates vary significantly by individual employer and to a lesser extent by rate pool
  - 2011-2013 Tier 1/Tier 2/OPSRP base contribution rates exceed 40% of payroll for some small employers with very poor unpooled demographic experience

[1] *Independent employers, including Judiciary, are treated as a single pool for purposes of this exhibit.*

Key Findings

Average Net Contribution Rates Including Retiree Healthcare (Excluding IAP)

- Net rate increases are greater than base rate increases due to the combination of two effects:
  - An increase in collared base rates, as detailed on the previous slide
  - A decrease in side account rate offset levels effective for 2011-2013 as an outcome of the 2008 market downturn

Average Net Employer Rates	SLGRP	School Districts	Indepen-dents	OPSRP General	OPSRP P&F	System-Wide
2009-2011 Net Rates[1]	4.4%	5.2%	9.6%	4.9%	7.5%	5.2%
2011-2013 Net Rates[2]	**10.8%**	**11.7%**	**13.7%**	**9.0%**	**11.7%**	**10.8%**
Net Rate Increase	6.4%	6.5%	4.1%	4.1%	4.2%	5.6%

- Changes in net rates vary significantly by individual employer and to a lesser extent by rate pool, with larger changes for individual employers with side accounts

1 *In this exhibit, 2009-2011 base rates are adjusted by two factors to calculate estimated system-wide net rates. Adjustments are for side accounts and pre-SLGRP liabilities/(surpluses). The 2009-2011 rates in this exhibit were accumulated on an employer by employer basis for SLGRP and School Districts, and adjustments were limited when an individual employer reaches a 0% contribution rate. Independent employers, including Judiciary, are treated as a single pool for purposes of this exhibit.*

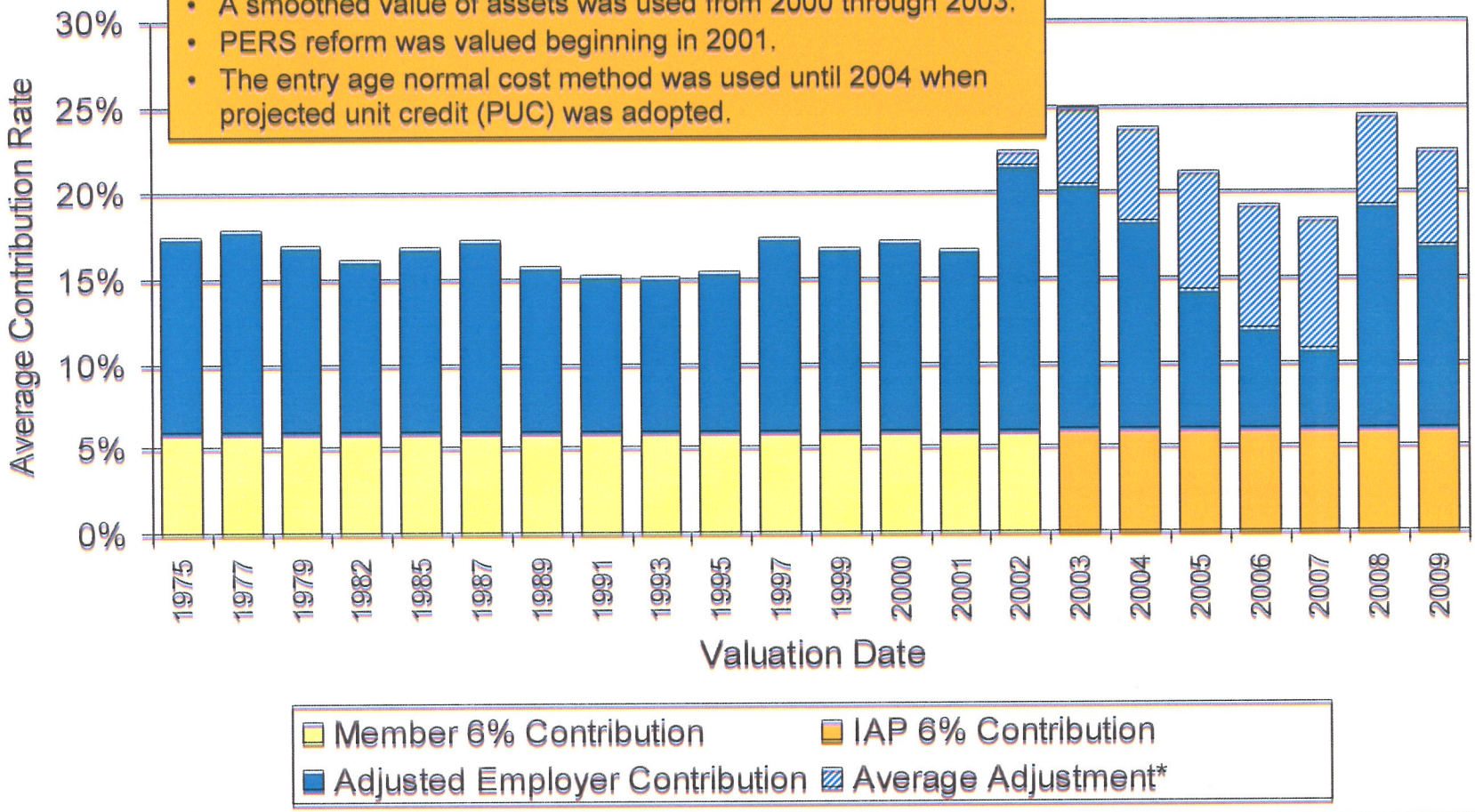
2 *In this exhibit, 2011-2013 base rates are adjusted by two factors to calculate estimated system-wide net rates. Adjustments are for side accounts and pre-SLGRP liabilities/(surpluses) and are assumed not to be limited when an individual employer reaches a 0% contribution rate. Independent employers, including Judiciary, are treated as a single pool for purposes of this exhibit.*

Key Findings

Historical Perspective on Valuation Rates (Including IAP)

When comparing historical valuation rates, please note that there have been a number of changes including:

- Money Match benefits were not valued until 1997.
- A smoothed value of assets was used from 2000 through 2003.
- PERS reform was valued beginning in 2001.
- The entry age normal cost method was used until 2004 when projected unit credit (PUC) was adopted.



* Adjustments to individual employer contribution rates are made for side accounts and pre-SLGRP liabilities or surpluses

Key Findings

Historical Perspective on Valuation Rates (Excluding IAP)

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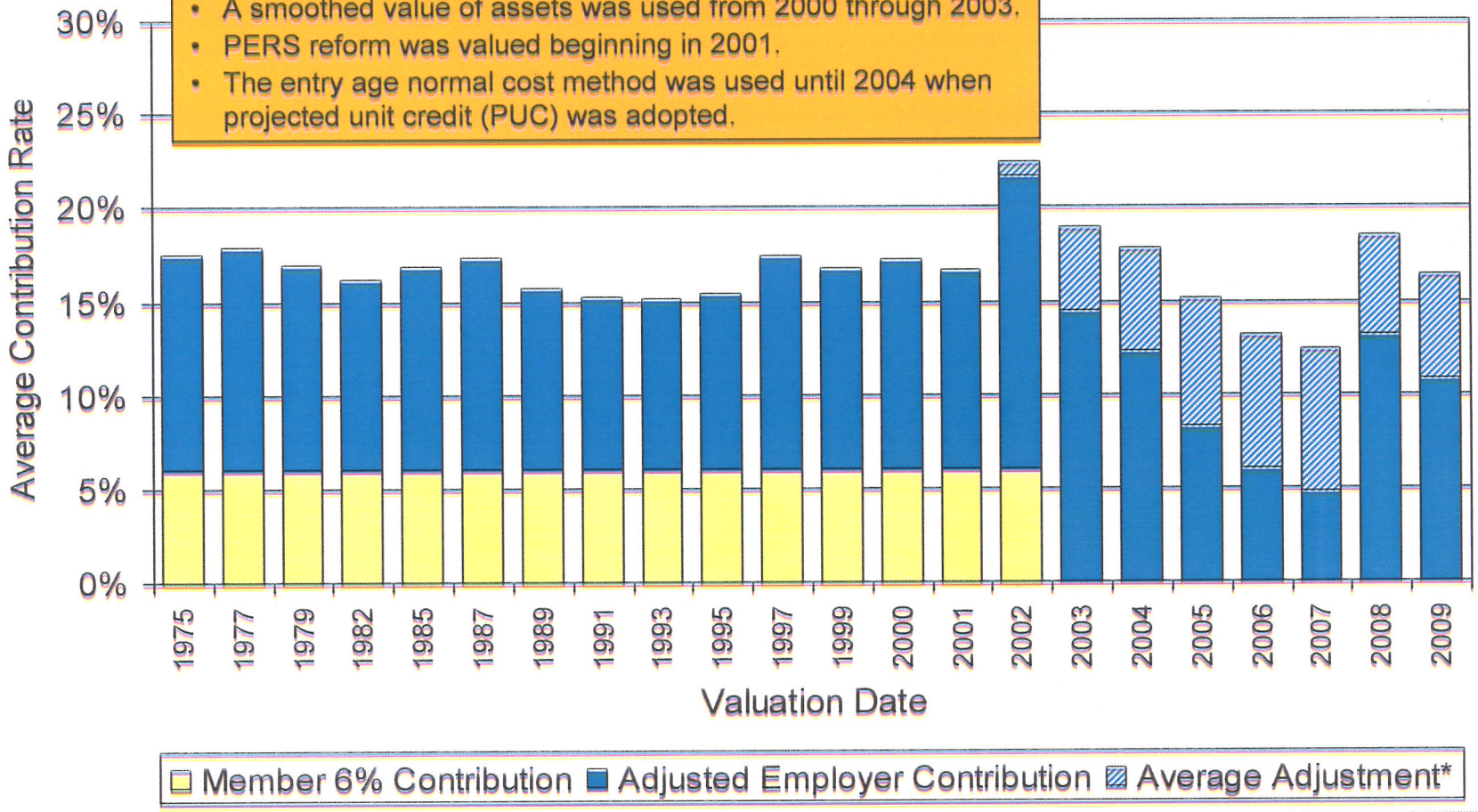
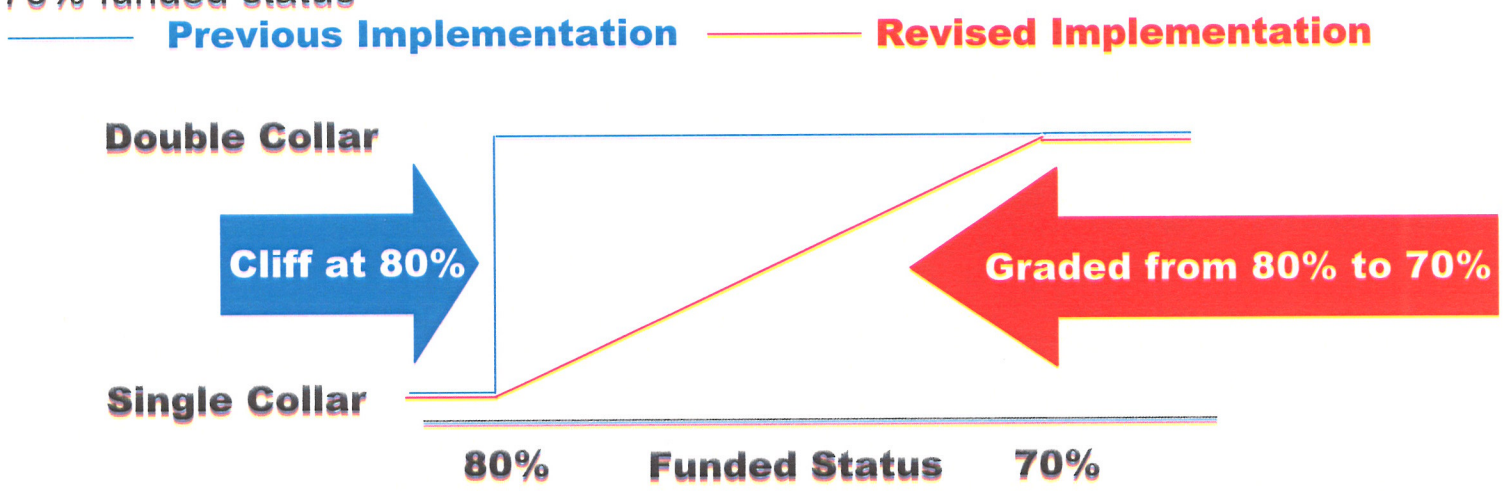


* Adjustments to individual employer contribution rates are made for side accounts and pre-SLGRP liabilities or surpluses

Key Findings
Revised Implementation of the Double Rate Collar

- The rate collar limits changes in the base contribution rate from biennium to biennium
  - Under normal conditions, the collar width is the greater of:
    - 3% of payroll, or
    - 20% of the current base rate
  - If the funded status is low, the width of the collar doubles
- In January, the Board adopted a revised implementation of the double rate collar
  - The prior "cliff" approach doubled the size of the collar immediately when an employer's funded status dropped below 80%
  - The revised implementation provides a graded schedule widening the collar from 80% to 70% funded status



Key Findings
Revised Implementation of the Double Rate Collar

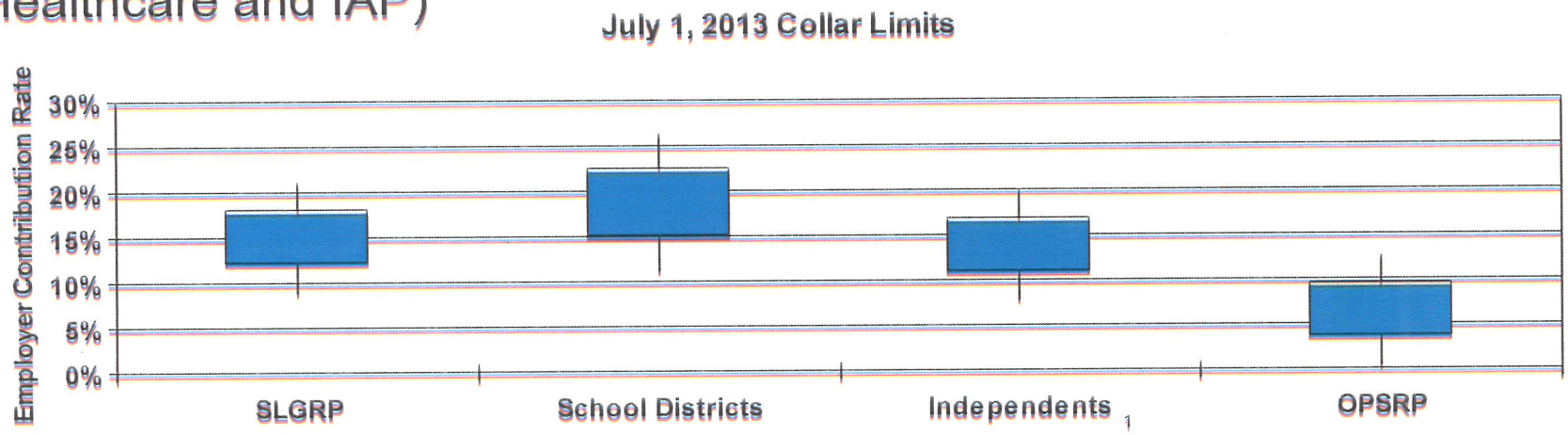
- The collar is applied separately for each rate pool or independent employer
- On an estimated system-wide basis, using the graded approach rather than the cliff approach lowered collared employer rates by 1.8% percent of payroll
- This chart shows the impact of the revised implementation on the Tier 1/Tier 2 rate pools
- Since Tier 1/Tier 2 unfunded accrued liability (UAL) is amortized across combined Tier 1/Tier 2/OPSRP payroll, collar limits on Tier 1/Tier 2 rate pools also affect rates charged on OPSRP payroll

	SLGRP	School Districts	Indepen-dents[1]	System-Wide
Width of Single Collar	3.0%	3.0%	3.0%	3.0%
Funded Status Excluding Side Accounts	77%	74%	82%	76%
12/31/2009 Collar Width – Previous "Cliff" Implementation Approach	6.0%	6.0%	3.0%	6.0%
12/31/2009 Collar Width – Revised "Graded" Implementation Approach	3.9%	4.8%	3.0%	4.2%
Change in Collar Width Due to Revised Implementation	**(2.1)%**	**(1.2)%**	**0.0%**	**(1.8)%**

[1] *Independent employers, including Judiciary, are treated as a single pool for purposes of this exhibit.*

Key Findings

Collar Limits for Base Rates Effective 2013-2015 (Excluding Retiree Healthcare and IAP)



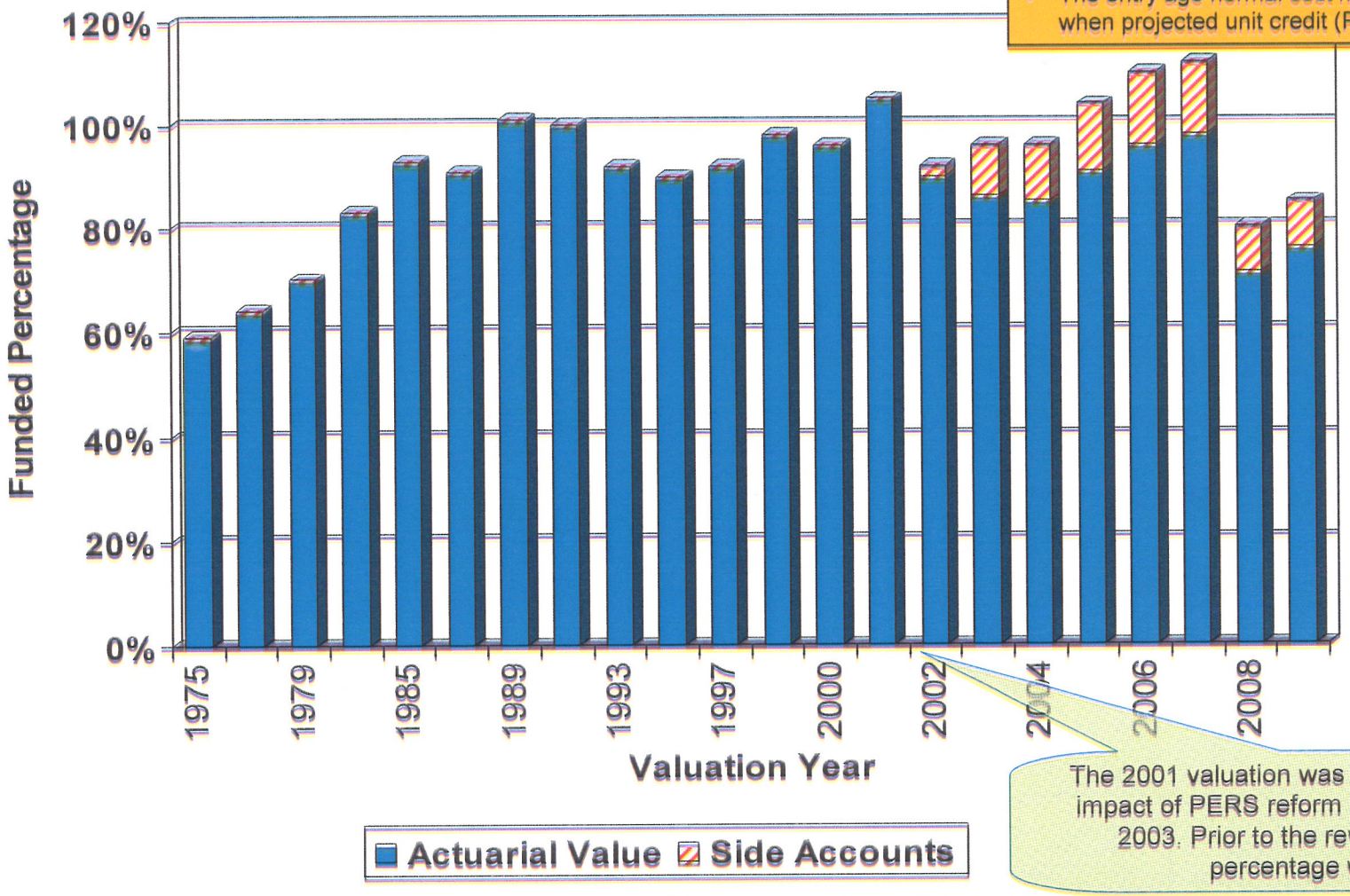
- The rate collar limits the change in employer contribution rates from one period to the next. This valuation determines the actual rates for the period for 2011-2013 and the collar limits for rates that will be effective for 2013-2015.
- The blue boxes above show the collar limits for 2013-2015 assuming the funded status is between 80% and 120%. The lines above and below the boxes represent the potential range if the funded status is below 70% or above 130%. For funded status from 70-80% or 120-130%, the collar would be between these ranges.
- Ranges shown above are rates attributable to each rate pool (for example, the OPSRP range represents OPSRP Normal Cost plus the OPSRP UAL rate)
  - UAL rates are charged on all payroll (for example, Tier 1/Tier 2 UAL is charged on both Tier 1/Tier 2 payroll and OPSRP payroll)

[1] *Independent employers, including Judiciary, are treated as a single pool for purposes of this exhibit.*

Key Findings
Tier 1/Tier 2/OPSRP Historical Funded Status

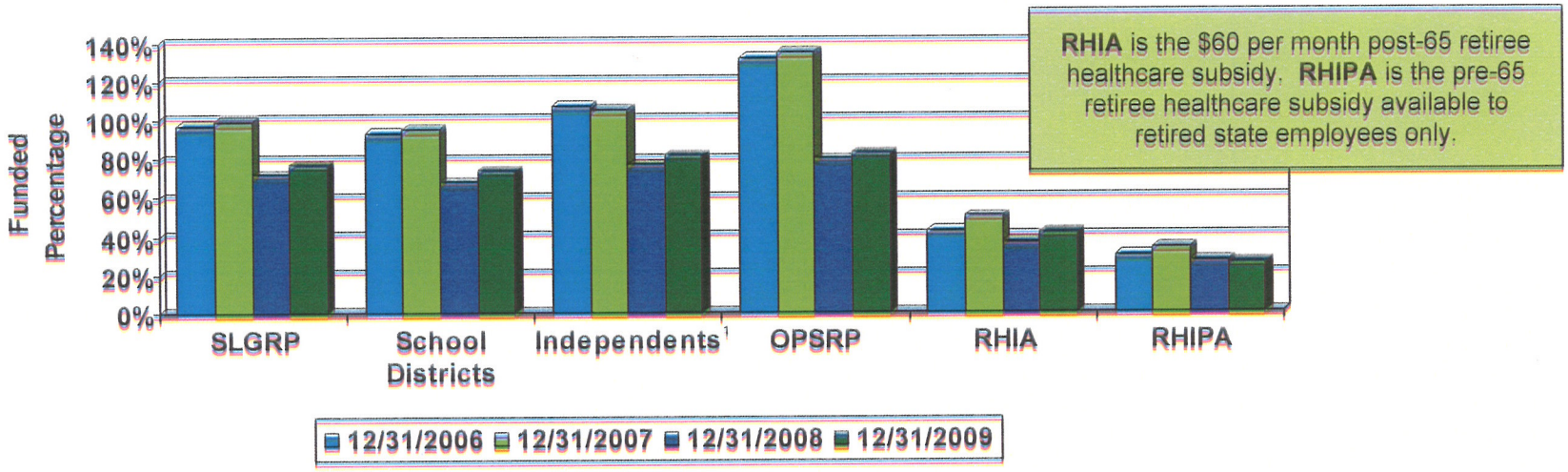
When comparing historical funded status, please note that there have been a number of changes including:

- Money Match benefits were not valued until 1997.
- A smoothed value of assets was used from 2000 through 2003.
- PERS reform was valued beginning in 2001.
- The entry age normal cost method was used until 2004 when projected unit credit (PUC) was adopted.



The 2001 valuation was revised to include the impact of PERS reform legislation enacted in 2003. Prior to the revision, the funded percentage was 88%.

Key Findings
Funded Status Excluding Side Accounts By Rate Pool



- Funded status for rate pools improved from 2003 through 2007, but dropped sharply due to 2008 investment losses. Investment returns during 2009 improved funded status, but all pools are still well below their 2007 levels.
- Side accounts account for a significant portion of assets, which are not included in the graph above
- RHIPA assets represent only 38 months of benefit payments. Participation in the RHIPA program is fairly low. An increase in the participation rate, an increase in the retiree population and/or an additional market downturn has the potential to drop the "months of available benefit payments" level even further.

[1] *Independent employers, including Judiciary, are treated as a single pool for purposes of this exhibit.*

Key Findings
Projection to Year-End 2010 Excluding Side Accounts

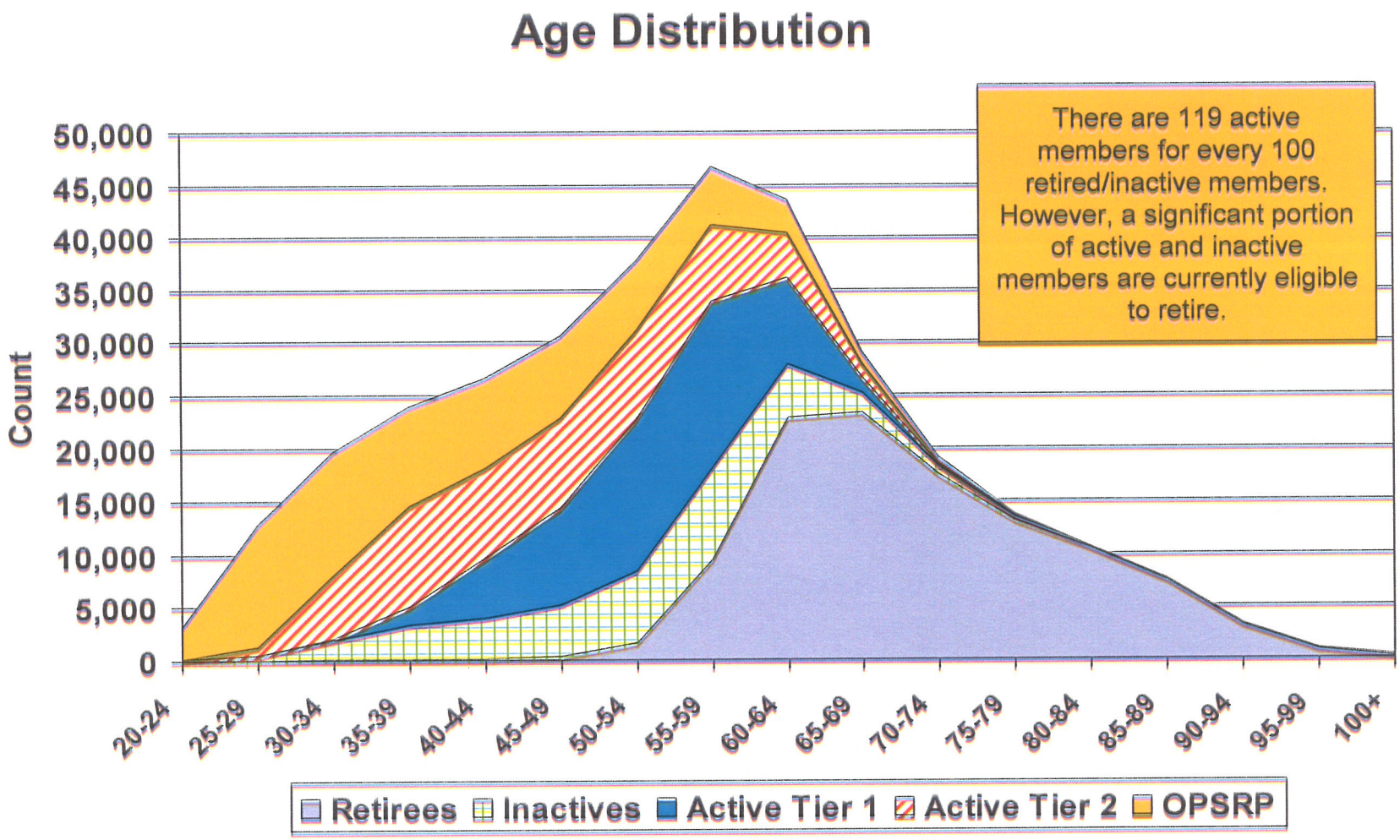
Percentile	2010 Asset Return	Projection to 12/31/2010		
		Funded Status (Excluding Side Accounts)	UAL Excluding Side Accounts (billions)	Advisory Uncollared Base Rate
5th	-6.5%	67%	$19.5	25.2%
10th	-4.2%	68%	$18.6	24.5%
25th	-0.4%	71%	$17.3	23.5%
50th	**3.8%**	**73%**	**$15.8**	**22.4%**
75th	7.8%	75%	$14.4	21.3%
90th	11.3%	78%	$13.2	20.3%
95th	13.4%	79%	$12.5	19.7%
Values at 12/31/2009:		***76%***	***$13.6***	***20.3%***

- This chart combines published investment experience through May 31 (-0.8% return) with forecast variability in returns for the last seven months of 2010
- Comparable amounts at year-end 2009 are shown at the bottom
- The system would need a return of approximately 8.8% to maintain the 12/31/2009 funded status of 76% (excluding side accounts)
- If experience after 2010 follows assumption, the collared base rate will move toward the uncollared base rate over a period of one biennium or more

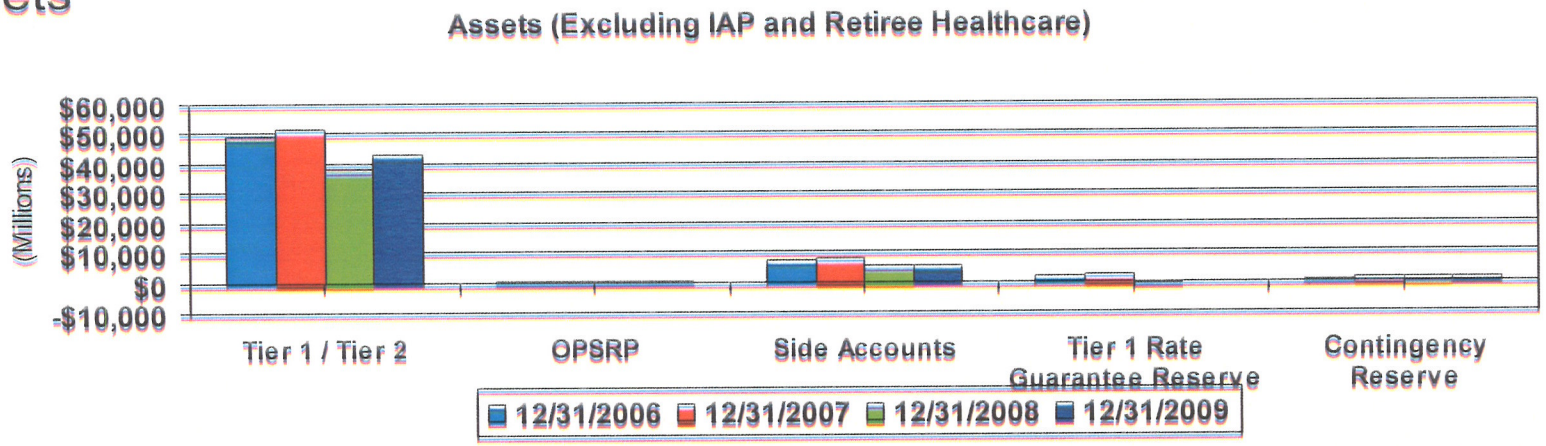
12/31/2009 Tier 1/Tier 2 & OPSRP Valuation

Oregon Public Employees Retirement System

12/31/2009 Tier 1/Tier 2 & OPSRP Valuation
Demographics



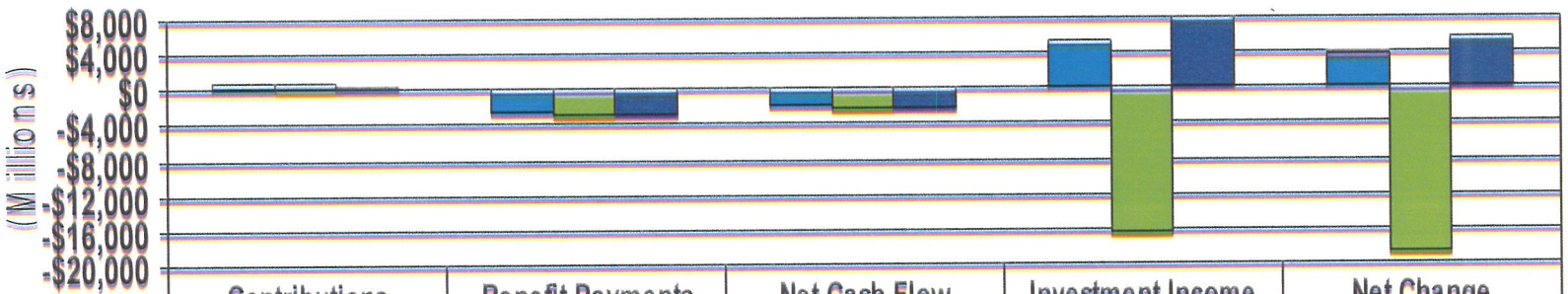
12/31/2009 Tier 1/Tier 2 & OPSRP Valuation
Assets



- Valuation assets used to set Tier 1/Tier 2 & OPSRP contribution rates exclude:
  - The Contingency and Tier 1 Rate Guarantee Reserves,
  - Side accounts,
  - Pre-SLGRP liabilities and surpluses, and
  - IAP and Retiree Healthcare (RHIA, RHIPA) assets
- Combined Tier 1/Tier 2, OPSRP and Side Account assets as reported by PERS increased from $44.0 billion to $49.2 billion during the year.
  - Tier 1/Tier 2 assets increased from $38.6 billion to $43.3 billion
  - Side Accounts increased from $5.1 billion to $5.5 billion.
  - OPSRP valuation assets increased from $270 million to $445 million in the last year
- The Rate Guarantee Reserve went from a negative $1.0 billion position to a negative $0.4 billion position. The Contingency Reserve was held constant at $653 million.

12/31/2009 Tier 1/Tier 2 & OPSRP Valuation
Assets

Changes in Tier 1/Tier 2 & OPSRP Assets (Including Side Accounts & Reserves)



	Contributions	Benefit Payments	Net Cash Flow	Investment Income	Net Change
2007	760.7	(2,668.4)	(1,907.7)	5,515.1	3,607.4
2008	646.5	(2,811.3)	(2,164.8)	(16,515.3)	(18,680.1)
2009	572.5	(2,842.0)	(2,269.5)	8,022.1	5,752.6

- Benefit payments are five times larger than 2009 net rate contributions, resulting in net negative cash flow before earnings
- Investment earnings and losses are the primary determinant of changes in Tier 1/Tier 2 & OPSRP assets. For 2009, investment gains were fourteen times greater than contributions.
- During 2008 and 2009 the cumulative net change was a $12.9 billion decrease
  - Over the same period valuation assets for the purposes of setting base rates, which exclude side accounts and reserves, decreased by $8.4 billion

12/31/2009 Tier 1/Tier 2 & OPSRP Valuation
Normal Cost Rate

- The average normal cost rate increased 52 basis points since the last valuation
- Active members projected to retire under Money Match have a 0% normal cost. As a result, Tier 1 general service members have the lowest normal cost rate.
- Tier 1 / Tier 2 normal cost rates are expected to continue to increase as benefits continue to shift to Full Formula and as active members age. For Tier 2 Members, this trend was accelerated by the 2008 market downturn.

	Valuation		
	12/31/2007	12/31/2008	12/31/2009
T-1, General	3.57%	5.02%	5.81%
T-1, P&F	13.14%	14.61%	15.79%
T-1, Average	**4.67%**	**6.12%**	**6.98%**
T-2, General	7.28%	9.52%	9.95%
T-2, P&F	12.81%	14.03%	14.67%
T-2, Average	**8.03%**	**10.13%**	**10.60%**
OPSRP, General	5.81%	5.90%	6.13%
OPSRP, P&F	8.52%	8.61%	8.84%
OPSRP, Average	**6.05%**	**6.16%**	**6.40%**
System Average	**6.07%**	**7.44%**	**7.96%**

12/31/2009 Tier 1/Tier 2 & OPSRP Valuation

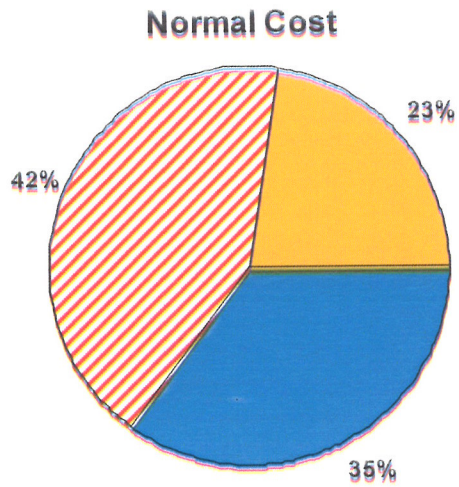
Actuarial Accrued Liabilities

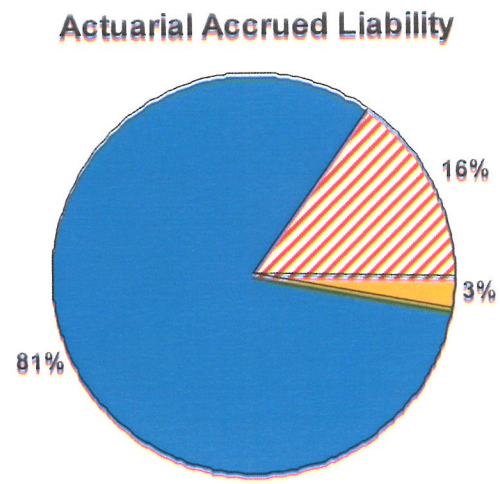
	Valuation		
	12/31/2007	12/31/2008	12/31/2009
T-1, General	$15,246	$14,666	$14,589
T-1, P&F	$1,810	$1,808	$1,863
T-1, Active Total	**$17,056**	**$16,474**	**$16,452**
T-2, General	$2,010	$2,177	$2,558
T-2, P&F	$415	$475	$563
T-2, Active Total	**$2,425**	**$2,652**	**$3,120**
OPSRP, General	$177	$290	$454
OPSRP, P&F	$25	$43	$70
OPSRP, Active Total	**$202**	**$333**	**$524**
Inactive	$4,421	$4,659	$4,666
Retiree	$28,767	$30,142	$32,074
Non-Active Total	**$33,188**	**$34,801**	**$36,741**
System Total	**$52,871**	**$54,260**	**$56,837**

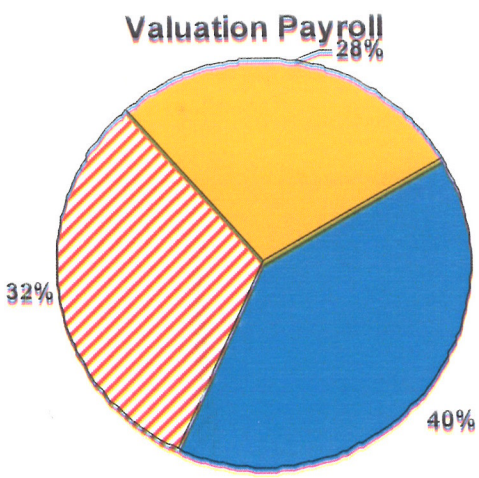
Amounts in millions

- System liabilities grew 4.7% since the prior valuation, with the above average increase caused by three factors in the active member liability
  - Fewer members commenced benefits than anticipated in 2009
    - Benefit payments not made are temporarily retained in liability
  - 37.57% crediting to variable accounts due to 2009 investment returns increased liabilities
  - 12/31/2008 systemwide normal cost rate was 1.37% of payroll higher than the 12/31/2007 normal cost rate (see prior slide)
    - Over time the system is migrating from Money Match to a normal cost level based on Full Formula and OPSRP
    - 2008 market returns accelerated that migration

12/31/2009 Tier 1/Tier 2 & OPSRP Valuation
Active Member Liabilities





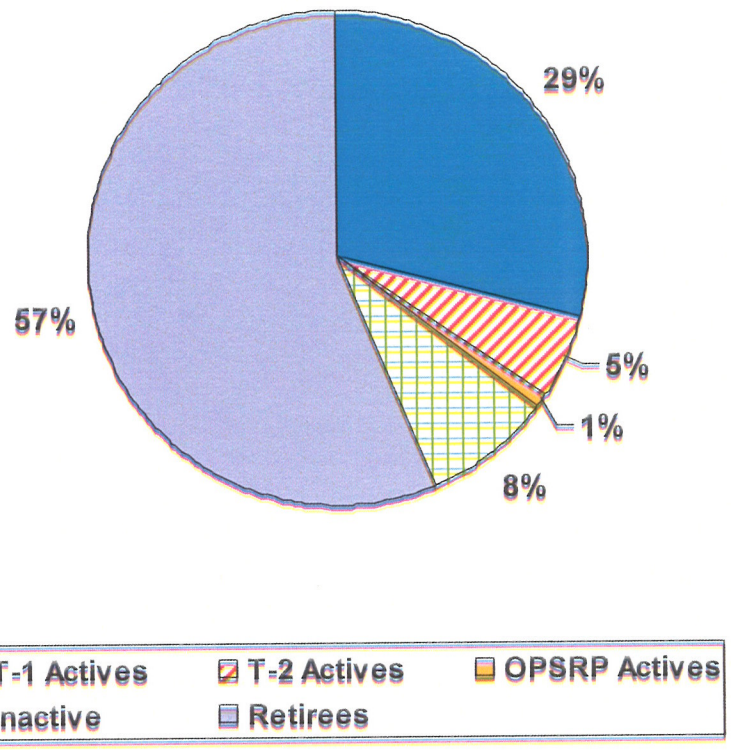


- While Tier 1 represents 81% of the accrued liability for active members, it is only 40% of the payroll and 35% of the normal cost
- Tier 2 represents 16% of the accrued liability, 32% of the payroll and 42% of the normal cost
- OPSRP represents 28% of the payroll and 23% of the normal cost, but only 3% of the active member liability

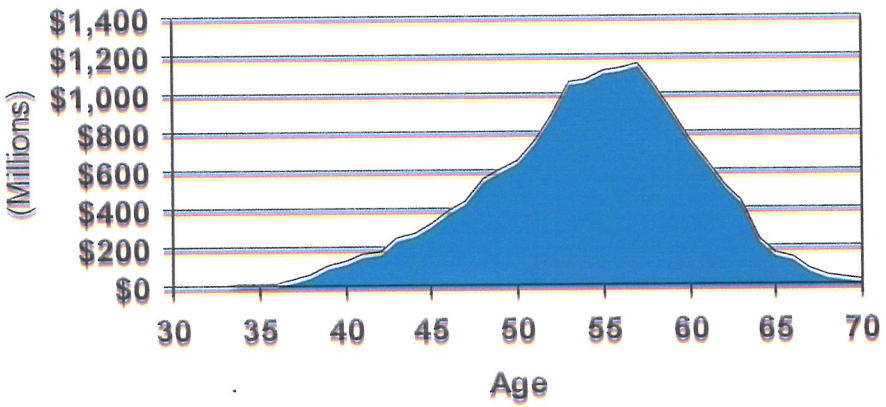
12/31/2009 Tier 1/Tier 2 & OPSRP Valuation
Actuarial Accrued Liabilities

- While Tier 1 members represent the predominant portion of the active member liability, 65% of the system's total accrued liability is for members who are no longer working in covered employment
- Over 44% of the Tier 1 active member liability is for members over age 55, and approximately 75% of the Tier 1 active member liability is for members over age 50

Actuarial Accrued Liability by Member Category



Distribution of Tier 1 Active Liability



12/31/2009 Tier 1/Tier 2 & OPSRP Valuation
Funded Status Measures

- **Unfunded Accrued Liability (UAL) Excluding Side Accounts**
  - The UAL excluding side accounts is used to calculate the employer contribution rates for the SLGRP and School District pools and for independent employers
  - The side accounts are treated as prepaid contributions for the individual employers who have made supplemental contributions
- **Unfunded Accrued Liability (UAL) Including Side Accounts**
  - The UAL including side accounts is used to report the funded status of the system as a whole
  - Side accounts are held within the PERS Trust and are available to pay PERS benefits
- **Employer Net Obligation**
  - The employer net obligation is the UAL including side accounts but adjusted for the outstanding principal on pension obligation bonds (POBs)
  - This measure is not used by PERS, but can be used in a broader financial context to understand the outstanding obligations related to PERS

12/31/2009 Tier 1/Tier 2 & OPSRP Valuation
Unfunded Accrued Liability (UAL)

	12/31/2009 Valuation					12/31/2008
	SLGRP	School Districts	Independ-ents	OPSRP	System-Wide[1]	System-Wide[1]
Accrued Liability	$29,058	$22,507	$4,674	$536	$56,837	$54,260
Assets	$22,476	$16,577	$3,840	$445	$43,239	$38,386
UAL Excluding Side Accounts	**$6,582**	**$5,929**	**$834**	**$90**	**$13,598**	**$15,873**
Side Accounts	$2,593	$2,811	$87	N/A	$5,490	$5,135
UAL Including Side Accounts	**$3,989**	**$3,119**	**$747**	**$90**	**$8,108**	**$10,739**
POBs	$3,264	$2,632	$213	N/A	$6,109	$6,187
Employer Net Obligations	**$7,254**	**$5,751**	**$959**	**$90**	**$14,217**	**$16,926**

The ratio of Side Accounts to outstanding Pension Obligation Bonds (POBs) went from 0.83 to 0.90 from 12/31/2008 to 12/31/2009

Amounts In Millions

[1] *System-wide results include Multnomah Fire District #10*

12/31/2009 Tier 1/Tier 2 & OPSRP Valuation
Unfunded Accrued Liability (UAL)

	12/31/2009 Valuation					12/31/2008
	SLGRP	School Districts	Independ-ents	OPSRP	System-Wide[1]	System-Wide[1]
Payroll (T1/T2 + OPSRP)	$4,850	$2,874	$788	$8,512	$8,512	$8,130
UAL Excluding Side Accounts	$6,582	$5,929	$834	$90	$13,598	$15,873
UAL Excluding Side Accounts as % of Payroll	**136%**	**206%**	**106%**	**1%**	**160%**	**195%**
UAL Including Side Accounts	$3,989	$3,119	$747	$90	$8,108	$10,739
UAL Including Side Accounts as % of Payroll	**82%**	**109%**	**95%**	**1%**	**95%**	**132%**
UAL Including Side Accounts Adjusted for POBs	$7,254	$5,751	$959	$90	$14,217	$16,926
Employer Net Obligations as % of Payroll	**150%**	**200%**	**122%**	**1%**	**167%**	**208%**

Amounts In Millions

[1] *System-wide results include Multnomah Fire District #10*

12/31/2009 Tier 1/Tier 2 & OPSRP Valuation
Employers Joining the State & Local Government Rate Pool (SLGRP)

- Effective 1/1/2010, eight previously independent employers joined the SLGRP
- SLGRP contribution rates in this valuation reflect the addition of these employers
- The SLGRP UAL rate is not affected by new employers joining the pool as a transition liability or surplus is established such that the pooled UAL rate remains unchanged
- All of the new employers had a transition surplus
- The addition of these employers to the pool increased the overall net transition surplus approximately $16 million

	Joining SLGRP	Current SLGRP
Primary Employers	8	353
Payroll (T1/T2 + OPSRP)	$29	$4,821
Tier 1/Tier 2 Assets	$109	$22,383
Tier 1/Tier 2 Accrued Liability	$133	$28,925
Tier 1/Tier 2 Normal Cost	$2	$306

Dollar Amounts In Millions

12/31/2009 Tier 1/Tier 2 & OPSRP Valuation
2011-2013 Contribution Rates (Excluding Retiree Healthcare and IAP)

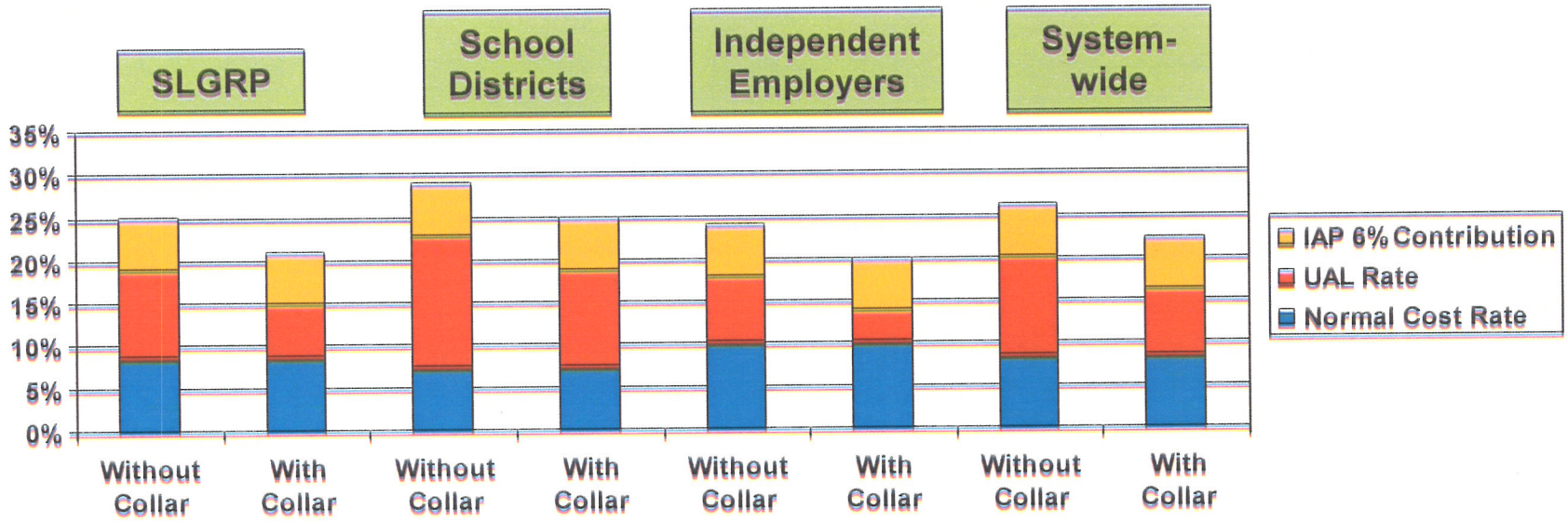
	SLGRP	School Districts	Indepen-dents[1]	OPSRP General	OPSRP P&F	System-Wide
Tier 1/Tier 2/OPSRP						
Normal Cost	8.89%	7.55%	10.35%	6.13%	8.84%	7.96%
T1/T2 UAL	6.16%	11.26%	3.56%	7.72%	7.72%	7.72%
OPSRP UAL	0.08%	0.08%	0.08%	0.08%	0.08%	0.08%
Base Rate, Excluding Retiree Healthcare & IAP	**15.13%**	**18.89%**	**13.99%**	**13.93%**	**16.64%**	**15.76%**
Adjustments[2]						
Side Accounts	(4.24%)	(7.75%)	(0.87%)	(5.11%)	(5.11%)	(5.11%)
Pre-SLGRP Liabs	(0.71%)	N/A	N/A	(0.40%)	(0.40%)	(0.40%)
Average Adjustment	(4.95%)	(7.75%)	(0.87%)	(5.51%)	(5.51%)	(5.51%)
Net Rate, Excluding Retiree Healthcare & IAP[2]	**10.18%**	**11.14%**	**13.12%**	**8.42%**	**11.13%**	**10.25%**

[1] *Independent employers, including Judiciary, are treated as a single pool for purposes of this exhibit.*

[2] *For this exhibit, adjustments are assumed not to be limited due to an individual employer reaching a 0.00% contribution rate.*

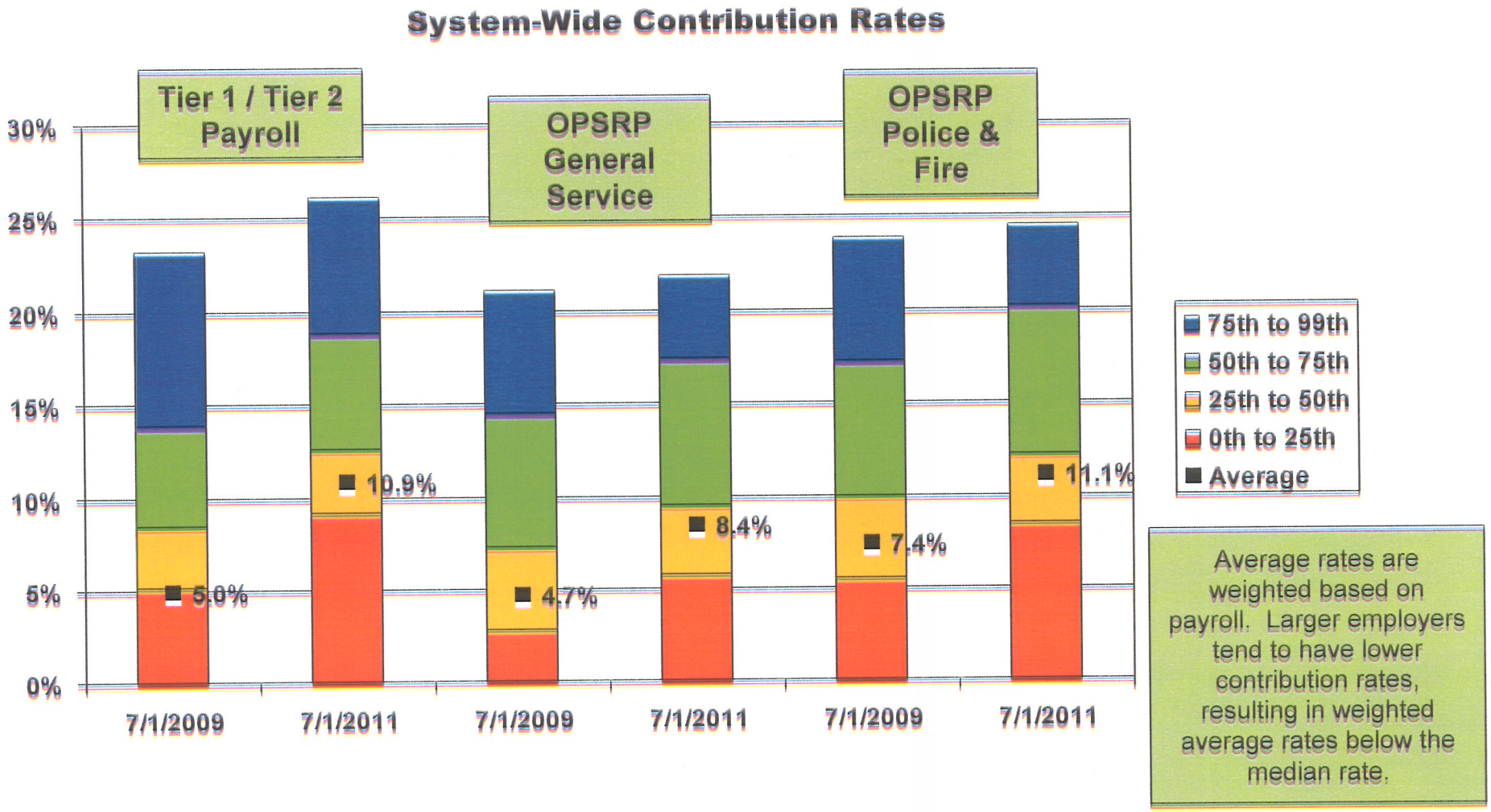
12/31/2009 Tier 1/Tier 2 & OPSRP Valuation

Impact of Collar on Base Rates for Tier 1/Tier 2 Payroll (Excluding Retiree Healthcare)



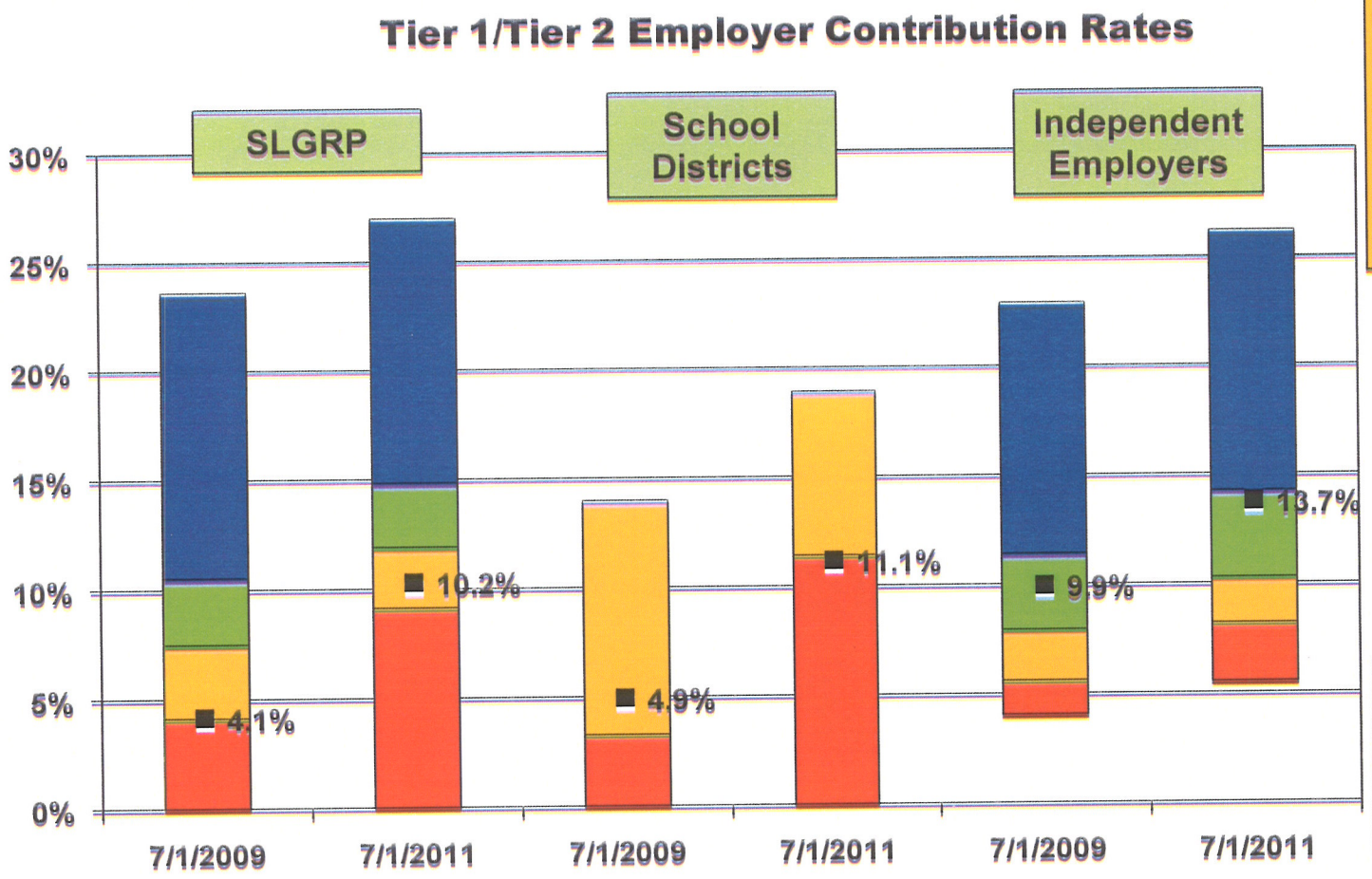
- Without the collar in place, the system-wide base rate on Tier 1/Tier 2 payroll excluding the IAP contribution would be 20.3% of payroll
- The rate collar limits the 2011-2013 base rate to 16.3% of payroll
- Independent employers are treated as a pool for purposes of this exhibit; rates for individual independent employers vary from the rate shown here

12/31/2009 Tier 1/Tier 2 & OPSRP Valuation
Distribution of Net Contribution Rates (Excluding Retiree Healthcare and IAP)



12/31/2009 Tier 1/Tier 2 & OPSRP Valuation

Distribution of Net Contribution Rates (Excluding Retiree Healthcare and IAP)



The Board's policy to require Independent Employers to contribute a minimum (excluding IAP) of 6% of payroll before side account adjustments affects 16 of the 130 independent employers. These employers could avoid this minimum if they joined the SLGRP.

Average rates are weighted based on payroll. Larger employers tend to have lower contribution rates, resulting in weighted average rates below the median rate.

12/31/2009 Retiree Healthcare Valuation

Oregon Public Employees Retirement System

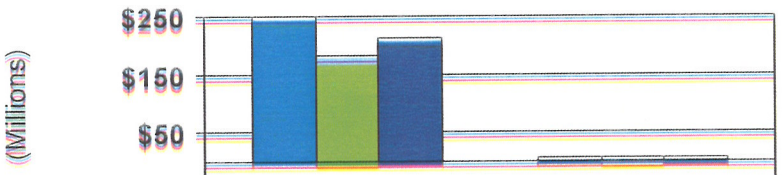
12/31/2009 Retiree Healthcare Valuation
Overview

- RHIA provides $60 per month subsidy toward healthcare premium for Tier 1/Tier 2 retirees who are eligible for Medicare. OPSRP retirees are not eligible for the RHIA subsidy.
- RHIPA provides Tier 1/Tier 2 State employees who retire prior to age 65 with an alternative to PEBB coverage until they reach Medicare eligibility. OPSRP retirees are not eligible for the RHIPA subsidy.
- These benefits are funded through 401(h) accounts within the PERS trust, but the funds are, by law, kept separate from the pension funds. Consequently, side accounts cannot be used to make RHIA or RHIPA contributions.
- RHIA and RHIPA are not as well-funded as the pension plan.
  - To address that, in July 2009 the Board approved a shortening of the amortization period to more rapidly improve funded status of those programs.
  - Effective July 2011, the unfunded actuarial liability (UAL) will be amortized over a 10-year period.
- Contribution rates for RHIA and RHIPA will increase effective 2011-2013 due to investment losses and the change from a 20-year amortization period to a 10-year period.

12/31/2009 Retiree Healthcare Valuation
Assets

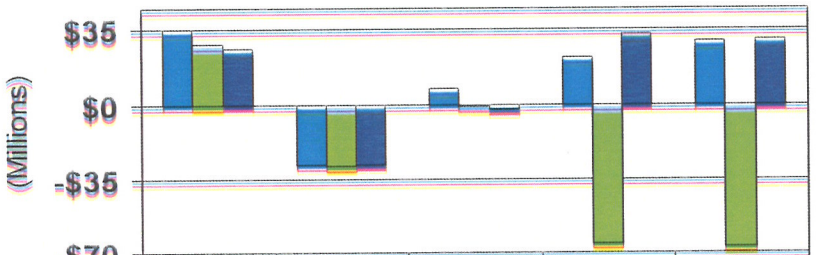
- During 2008 and 2009 the cumulative net change in retiree healthcare assets was a $38 million (or 15%) decrease
- For both programs, contributions are about equal to benefit payments, so the net decrease in assets is driven by investment losses

Retiree Healthcare Assets



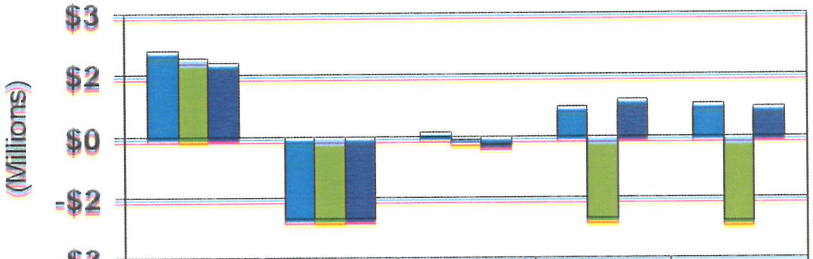
	RHIA	RHIPA
12/31/2007	250.8	7.8
12/31/2008	183.8	5.7
12/31/2009	214.1	6.4

Changes in RHIA Plan Assets



	Contributions	Benefit Payments	Net Cash Flow	Investment Income	Net Change
2007	35.5	(28.1)	7.4	22.1	29.4
2008	28	-28.9	-0.9	-66.1	-66.9
2009	25.9	-28.5	-2.6	33	30.4

Changes in RHIPA Plan Assets



	Contributions	Benefit Payments	Net Cash Flow	Investment Income	Net Change
2007	2.1	-2.0	0.1	0.7	0.8
2008	1.9	-2.0	-0.1	-2	-2.1
2009	1.8	-2.0	-0.2	0.9	0.7

12/31/2009 Retiree Healthcare Valuation
Normal Cost

	RHIA		RHIPA		Retiree Healthcare	
	12/31/2008	12/31/2009	12/31/2008	12/31/2009	12/31/2008	12/31/2009
Normal Cost	$5.6	$5.5	$0.8	$0.8	$6.4	$6.3
Normal Cost Payroll	$6,226	$6,123	$1,709	$1,705	$6,226	$6,123
Normal Cost Rate	**0.09%**	**0.09%**	**0.05%**	**0.05%**	**0.10%**	**0.10%**

Amounts In Millions

- Normal cost rates for RHIA and RHIPA have remained level
- These rates, however, are very sensitive to the participation assumption

12/31/2009 Retiree Healthcare Valuation
Unfunded Accrued Liability

Funded status lags significantly behind the funded status of Tier 1/Tier 2 and OPSRP.

	RHIA		RHIPA		Retiree Healthcare	
	12/31/2008	12/31/2009	12/31/2008	12/31/2009	12/31/2008	12/31/2009
Accrued Liability	$494	$511	$21	$25	$515	$536
Assets	$184	$214	$ 6	$ 6	$190	$220
UAL	$310	$297	$16	$18	$325	$315
Funded Percentage	**37%**	**42%**	**27%**	**26%**	**37%**	**41%**
Combined Valuation Payroll	$8,130	$8,512	$2,218	$2,372	$8,130	$8,512
UAL Rate	**0.50%**	**0.50%**	**0.10%**	**0.11%**	**0.53%**	**0.53%**

Amounts In Millions

- For comparison, the 12/31/2007 system-wide UAL rate was 0.20% of payroll
  - Both investment losses and a shortened amortization period increased the rate

12/31/2009 Retiree Healthcare Valuation
Contribution Rates for 2011-2013

- Contribution rates are higher than the rates in effect 2009-2011 by approximately 0.3% of payroll
  - The increase was driven by a change in the UAL rate
- Changes in actual participation rates can have a significant effect on the UAL

Payroll	Tier 1 / Tier 2	OPSRP General	OPSRP P&F
Normal Cost Rate	0.10%	N/A	N/A
UAL Rate	0.53%	0.53%	0.53%
2011-2013 Rates	**0.63%**	**0.53%**	**0.53%**
2009-2011 Rates	***0.32%***	***0.20%***	***0.20%***

Next Steps

- Board adopts individual employer rates for 2011-2013 biennium at September 24, 2010 Board meeting
- Individual employer reports are sent via e-mail to employers shortly after the rates are adopted

Actuarial Certification

Mercer has prepared this presentation exclusively for the Oregon PERS Board to present the system-wide results of a valuation of the Oregon Public Employees Retirement System as of December 31, 2009, and to provide information on system-wide employer contribution rates for the period beginning July 1, 2011. This presentation may not be used or relied upon by any other party or for any other purpose; Mercer is not responsible for the consequences of any unauthorized use.

A valuation report is a snapshot of a plan's estimated financial condition at a particular point in time; it does not predict a plan's future financial condition or its ability to pay benefits in the future.

Over time, a plan's total cost will depend on a number of factors, including the amount of benefits the plan pays, the number of people paid benefits, plan expenses and the amount earned on any assets invested to pay the benefits. These amounts and other variables are uncertain and unknowable at the valuation date, but are predicted to fall within a reasonable range of possibilities.

To prepare this report, various *actuarial assumptions*, as described in the Appendix, are used to select a single scenario from a range of possibilities . However, the future is uncertain, and the system's actual experience will differ from those assumptions; these differences may be significant or material. In addition, different assumptions or scenarios may also be within the reasonable range and results based on those assumptions would be different. Actuarial assumptions may also be changed from one valuation to the next because of changes in mandated requirements, plan experience, changes in expectations about the future and other factors. Due to the limited scope of our assignment, we did not perform, nor do we present, an analysis of the potential range of future possibilities and scenarios.

Because actual system experience will differ from the assumptions, decisions about benefit changes, investment policy, funding amounts, benefit security and/or benefit-related issues should be made only after careful consideration of alternative future financial conditions and scenarios and not solely on the basis of a valuation report or reports.

This report is based on data and system provisions as described in the Appendix. Oregon PERS is solely responsible for the validity, accuracy and comprehensiveness of this information. If the data or plan provisions supplied are not accurate and complete, the valuation results may differ significantly from the results that would be obtained with accurate and complete information; this may require a later revision of this report.

Actuarial Certification

Actuarial Calculations, Methods and Assumptions

To the best of our knowledge and belief, this report is complete and accurate and all costs, liabilities and other factors under the plan were determined in accordance with generally accepted actuarial principles and procedures using an actuarial cost method approved by the Board. Assumptions used are based on the last experience study, as adopted by the Board on July 16, 2009. This valuation is based on assumptions, plan provisions, methods and other parameters as summarized in this report. If this information is inaccurate or incomplete or does not reflect current statutes, regulations or Board directives, the reader of this report should not rely on the valuation results and should notify Mercer promptly. In our opinion, this report fully and fairly discloses the actuarial position of the plan on an ongoing basis.

Professional Qualifications

We are available to answer any questions on the material in this report or to provide explanations or further details as appropriate. The undersigned credentialed actuaries meet the Qualification Standards of the American Academy of Actuaries to render the actuarial opinion contained in this report. We are not aware of any direct or material indirect financial interest or relationship, including investments or other services that could create a conflict of interest, that would impair the objectivity of our work.

We are available to answer any questions on the material contained in the report, or to provide explanations or further details as may be appropriate.

July 23, 2010

Matthew R. Larrabee, FSA, EA, MAAA
Enrolled Actuary No. 08-6154

Date

July 23, 2010

Scott D. Preppernau, FSA, EA, MAAA
Enrolled Actuary No. 08-7360

Date

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The information contained in this document is not intended by Mercer to be used, and it cannot be used, for the purpose of avoiding penalties under the Internal Revenue Code that may be imposed on the taxpayer.

Appendix

Appendix
Actuarial Basis

Data

We have based our calculation of the liabilities on the data, methods, assumptions and plan provisions described in the forthcoming December 31, 2009, Actuarial Valuation ("2009 Valuation Report") for the Oregon Public Employees Retirement System.

Assets as of December 31, 2009, were based on values provided by Oregon PERS reflecting the Board's earnings crediting decisions for 2009. Assets and year-to-date returns as of May 31, 2010 as published by the Oregon Investment Council (OIC) were used as the basis for projecting December 31, 2010 assets, where applicable. Year-to-date 2010 returns as of that date on regular accounts are -0.83%.

Methods / Policies

Liabilities are based on the Projected Unit Credit method and are rolled forward according to the following rules:

UAL Amortization: The UAL for Tier 1/Tier 2, OPSRP, and Retiree Healthcare as of December 31, 2007 are amortized as a level percentage of combined valuation payroll over a closed period. For the Tier 1/Tier 2 UAL, this period is 20 years; for OPSRP, it is 16 years; for Retiree Healthcare, it is 10 years. Gains and losses between subsequent odd-year valuations are amortized as a level percentage of combined valuation payroll over the amortization period (20 years for Tier/Tier 1, 16 years for OPSRP, 10 years for Retiree Healthcare) from the odd-year valuation in which they are first recognized.

Contribution rate stabilization method: Contribution rates are confined to a collar based on the prior base contribution rate. The new base contribution rate will generally not increase or decrease from the prior contribution rate by more than the greater of 3 percentage points or 20 percent of the prior contribution rate. If the funded percentage excluding side accounts drops below 80% or increases above 120%, the size of the collar increases.

Expenses: OPSRP administration expenses are assumed to be equal to $6.6M and are added to the OPSRP normal cost.

Actuarial Value of Assets: Equal to Market Value of Assets excluding Contingency and Tier 1 Rate Guarantee Reserves

Appendix
Actuarial Basis

Assumptions

Assumptions for valuation calculations are as described in the 2009 Valuation Report.

Provisions

Provisions valued are as detailed in the 2009 Valuation Report.

Arken and Robinson Litigation

We have made no adjustment to these valuation results to reflect any interpretation of Judge Kantor's rulings in the *Arken and Robinson* cases.

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