OREGON PUBLIC EMPLOYEES RETIREMENT BOARD

Friday November 18, 2005 1:00 P.M.	PERS 11410 SW 68th Parkway Tigard, OR

	ITEM	PRESENTER
A.	**Administration**	
1.	October 21, 2005 Board Meeting Minutes	CLEARY
2.	Director's Report	
	a. Forward-Looking Calendar	
	b. OIC Investment Report	
	c. HB2020 Update	
	d. Miscellaneous	
B.	**Consent Action and Information Items**	
1.	Notice of Rulemaking of OAR 459-070-0001, OPSRP Definitions	RODEMAN
2.	First Reading of OAR 459-010-0003, PERS Membership Eligibility	RODEMAN
3.	First Reading of OAR 459-010-0014, Creditable Service	RODEMAN
4.	Earnings Crediting and Reserving Policy Update	RODEMAN
C.	**Action and Discussion Items**	
1.	Adoption of OAR 459-007-0015, Underpayment Interest Rate	RODEMAN
2.	Strunk / Eugene Policy Issues	RODEMAN
3.	Strunk / Eugene Implementation Plan Update	STROUD
D.	**Executive Session Pursuant to ORS 192.660(2)(f), (h), and/or ORS 40.225**	
1.	Litigation Update	LEGAL COUNSEL

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PUBLIC EMPLOYEES RETIREMENT BOARD

PERS Board Meeting
1:00 P.M.
October 21, 2005
Tigard, Oregon

MEETING DATE	11-18-05
AGENDA ITEM	A.1. 10-21-05 Minutes

MINUTES

Board Members:	**Staff:**		
Mike Pittman, Chair	Paul R. Cleary, Director	Steve Delaney	Dave Tyler
Brenda Rocklin, Vice-chair	Steve Rodeman	David Crosley	Joe Delillo
James Dalton	Stephanie Vaughn	Barbara Wahr	Rick Howitt
Thomas Grimsley	Brenda Pearson	Ricki Vang	Jim Schilmoeller
Eva Kripalani	Helen Bamford	Marsha Bacon	Dale Orr
	Brian DeForest	Bob Davis	Jeanette Zang
Others:	Gary A. Smith	Deborah Tremblay	Alan Stonewall
David Wimmer	Ross J. Williams	Steve Manton	Hasina Squires
Darel Glatt	Brenda Majdic	Bruce Adams	Bob Andrews
Gordon Allen	Angela Schiebout	E. Marie Laird	BethAnne Darby
Bill Hallmark	Sharon Mulligan	Dee Ann Hardt	Carol Samuels
Denise Zunker	Dirk Borges	Tricia Smith	Victor Nolan
Brooks Koenig	Janice Essenberg	Marc Feldesman	Pam Broadus
Linda Ely	Cathy Bloom	Greg Hartman	Myrnie Daut
Maria Keltner	Karen Artiaco	Michelle Deister	Duane Bales
Patricia Thomson-Wasover	Bob Andrews	Kurt Bonar	Keith Kutler

Board Chair Mike Pittman called the meeting to order at 1:00 P.M.

ADMINISTRATION

A.1. BOARD MEETING MINUTES OF SEPTEMBER 23, 2005

James Dalton moved and Tom Grimsley seconded to approve the minutes of the September 23, 2005 meeting. The motion passed unanimously.

A.2. DIRECTOR'S REPORT

Director Paul Cleary presented the Forward-Looking Calendar and noted that the primary focus for upcoming meetings will be on project plans, policies and rule making to implement recent court decisions. Cleary announced a stakeholder Legislative Advisory Committee meeting in Salem on Friday, November 4th. Cleary reviewed the October Budget Report noting continued vacancy savings and RIMS Conversion Project (RCP) payments that have been re-forcasted to better accommodate acceptance testing and invoice processing. Cleary provided updates on the HB2020 employer reporting program and the Individual Account Program (IAP) remediation plan. Cleary said that implementation of the IAP remediation and annual crediting process would allow PERS to make required prior-period adjustments to member IAP accounts. Cleary announced that Steve McElhaney of Mercer Human Resource Consulting will now be PERS primary actuary, along with Bill Hallmark who will continue as the Board's key actuarial contact and presenter. Cleary presented "PERS By-The-Numbers", a statistical document that contains facts and figures on system benefits, demographics, funding level and status, revenue, and reform legislation. Cleary said this document would be posted on PERS website for interested parties and stakeholders.

CONSENT ACTION AND INFORMATION ITEMS

B.1. <u>ADOPTION OF NON-SUBSTANSIVE CHANGES TO CHAPTER 459 ADMINISTRATIVE RULES</u>

Steve Rodeman, Policy, Planning and Legislative Analysis Division (PPLAD) administrator, presented proposed permanent rule modifications to various administrative rules to clean up non-substantive errors.

It was moved by Brenda Rocklin and seconded by Eva Kripalani to adopt the permanent rule modifications to the various Chapter 459 rules, as presented, to be effective upon filing. The motion passed unanimously.

B.2. <u>FIRST READING OF OAR 459-007-0015, UNDERPAYMENT INTEREST RATE</u>
B.3. <u>NOTICE OF OAR 459-020-0025, SOCIAL SECURITY REPORTING PENALTIES</u>
B.4. <u>NOTICE OF OAR 459-020-0003, PERS MEMBERSHIP ELIGIBILITY</u>
B.5. <u>NOTICE OF OAR 459-020-0014, CREDITABLE SERVICE</u>
B.6. <u>NOTICE OF OAR 459-005-0610, RECOVERY OF OVERPAYMENTS</u>

Rodeman presented the above rule making items, summarizing the key policy and procedural issues and describing the public comment process.

No Board action was required.

Chair Pittman asked if there were any members of the audience who wished to comment on the rule making items.

PERS Retiree Sharon Mulligan presented a letter to the Board and asked if they had made a final decision in addressing the recovery of overpayments to members due to 1999 earnings reallocation.

Chair Pittman said that the Board would review the letter and give Mulligan's recommendations the utmost consideration. Cleary noted that the staff was collecting *<u>Strunk / Eugene</u>* implementation comments and questions via the PERS website for use in developing a Frequently Asked Questions (FAQ) posting. Cleary also indicated that various *<u>Strunk / Eugene</u>* policy issues and staff recommendations would be presented for Board consideration at upcoming Board meetings.

ACTION AND DISCUSSION ITEMS

C.1. *STRUNK / EUGENE* IMPLEMENTATION PLAN UPDATE

Craig Stroud, Benefit Payments Division (BPD) administrator, presented a draft *Strunk* and *Eugene* Project Business Plan. The plan document includes a project overview, the core principles and success criteria, the project timeline, the planning team make-up and major workload components. Stroud said that adjustment of historical account information amplifies the complexity of the project and that every affected account will have 12 to 30 financial adjustments. Stroud stated that there are currently no automated processes to make the necessary financial adjustments and that these processes must be defined, built, tested and implemented. Stroud said that staff has reviewed and considered the various options, risks, consequences and contingencies for the project.

The Board asked questions about the project timeline, budget and staffing needs, and project oversight and accountability. The Board also emphasized the need to ensure accuracy and timeliness throughout the project. Cleary said that January 2006 is the target date for mailing 2004 member statements, and that other project timelines would extend into 2007 - 2008.

C.2. ADOPTION AND NOTICE OF EARNINGS CREDITING RULES

Rodeman presented a brief overview of the proposed earnings crediting rule modifications to address requirements of the 2003 PERS Reform Legislation that were subsequently voided by the Oregon Supreme Court in the *Strunk* case. Rodeman said the adoption of the rule modifications as temporary rules would allow the agency to move forward with earnings crediting in compliance with the court decision while permanent rule making was under way.

It was moved by Brenda Rocklin and seconded by Tom Grimsley to adopt modifications to OAR 459-007-0001, 459-007-0003, 459-007-0005 and 459-007-0090 as temporary rules and suspend OAR 459-007-0095 and 459-013-0300, as presented. The motion passed unanimously.

C.3. 2004 EARNINGS CREDITING AND RESERVING

Rodeman summarized the history and current status of the final 2004 earnings crediting and said that recent current court decisions have affected last February's preliminary 2004 earnings crediting. Rodeman reviewed the various *Strunk / Eugene* related revisions to the baseline for 2004 earnings crediting and related reserves. Given those baseline revisions, Rodeman said that staff does not recommend putting additional earnings in the capital preservation reserve at this time, but does recommend allocating 7.5% of available earnings to the contingency reserve. Rodeman noted that the longer the delay in allocation of 2004 earnings, the longer the delay in processing 2004 members statements and implementing the *Strunk / Eugene* project plan.

Steve Manton, representing the City of Portland recommended that the Board not attempt to reserve to establish a base return for Tier 2 accounts, because those accounts were intended to get market gains and losses with no guarantees.

PERS Coalition legal counsel Greg Hartman said that it is not necessary to reserve money in a Capital Preservation Reserve (CPR) to credit Tier 2 accounts or other accounts at some undetermined time. Hartman said that the CPR would serve no purpose unless the Board developed a complete plan that tracked the allocated amounts and specified how the reserved funds would be distributed in the future.

The Board discussed the pros and cons of allocating additional amounts to the CPR and also discussed whether it was appropriate to include Tier 2 account earnings in the CPR given the non-guaranteed market driven return on those accounts.

It was moved by James Dalton and seconded by Mike Pittman to accept staff recommendations with the exception of no crediting for the CPR, which was revised following Board discussion to allocate $27.55 million to reflect a reserving level of 75 basis points (0.75%). Mike Pittman and Tom Grimsley voted no. The motion passed.

C.4. FINANCIAL MODELING OF ACTUARIAL METHODS

Bill Hallmark, actuary from Mercer Human Resource Consulting provided a presentation on policy alternatives for Financial Modeling of Actuarial Methods. Hallmark reviewed the meeting with the Legislative Advisory Committee in September 2005 and subsequent feedback. Based on direction from the Board, Hallmark said Mercer would model the policy variations, analyze the outcomes and present the results at the December 2005 Board meeting. Hallmark said the analysis would provide the Board and stakeholders a clearer understanding of the long-term implications of Board decisions, such as reserving policies, and the financial modeling would provide system-wide projections for improved employer budgeting of PERS costs. The Board agreed with the value of the financial modeling and concurred with the recommended policy alternatives for modeling purposes.

Chair Pittman asked if there were any members of the audience who wished to address the Board.

PERS Retiree Darel Glatt requested a check for his COLA as restored by the ***Strunk*** ruling. Director Cleary said that staff was developing a one-touch adjustment that would offset the impact of the *Eugene* case with restoration of the COLA. Cleary said this would be the most cost-effective and efficient way to handle the necessary account balance and benefit payment adjustments.

Retiree Patricia Thompson-Washover asked if retirement election options, chosen at the time of retirement, could now be changed to offset the collection of overpayments to members and associated benefit reductions. Cleary said staff would review this question and other policy issues as part of the ongoing *Strunk/Eugene* implementation planning. Cleary said staff would present recommendations at the November Board meeting.

Retiree Kurt Bonar said that he believed the Board was trying to make the best decisions with the information that they have to work with. Bonar said retirees made the best retirement decisions based on the information they were given and now, due to court decisions, retiree decisions were wrong so they should be able to revisit those decisions.

EXECUTIVE SESSION

Pursuant to ORS 192.660 (2) (f), (h) and ORS 40.255, the Board went into executive session at 3:20 P.M.

The Board reconvened to open session.

Chair Pittman adjourned the meeting at 3:50 P.M.

Respectfully submitted,

Paul R. Cleary
Executive Director

Prepared by Donna R. Allen, Executive Assistant

MEETING DATE	**11-18-05**
AGENDA ITEM	**A.2.a. Forward Calendar**

PERS Board Meeting
Forward-Looking Calendar

December 2005

Meeting: 11:00 A.M. and 1:00 P.M. December 16, 2005

Appeal of Carolyn Bigelow
Notice of Rulemaking of Division 20 Old-Age and Survivors Insurance Rules
Notice of Rulemaking of OAR 459-017-0060, Reemployment of Retired Members
First Reading of OAR 459-005-0610, Recovery of Overpayments
Adoption of OAR 459-070-0001, OPSRP Definitions
Adoption of OAR 459-010-0003, PERS Membership Eligibility
Adoption of OAR 459-010-0014, Creditable Service
Mercer Financial Modeling Results
Strunk/Eugene Implementation Plan Update
Strunk/Eugene Policy Issues

January 2006

Meeting: 11:00 A.M. and 1:00 P.M. *January 20, 2006* *(tentative date)*

First Reading of OAR 459-017-0060, Reemployment of Retired Members
Adoption of OAR 459-005-0610, Recovery of Overpayments
2007 Legislative Process
Earnings Crediting and Reserving Policy Adoption
Strunk/Eugene Implementation Plan Update

February 2006

Meeting: 11:00 A.M. and 1:00 P.M. *February 17, 2005* (*tentative date)*

2004 Valuation Results
2005 Preliminary Earnings Crediting

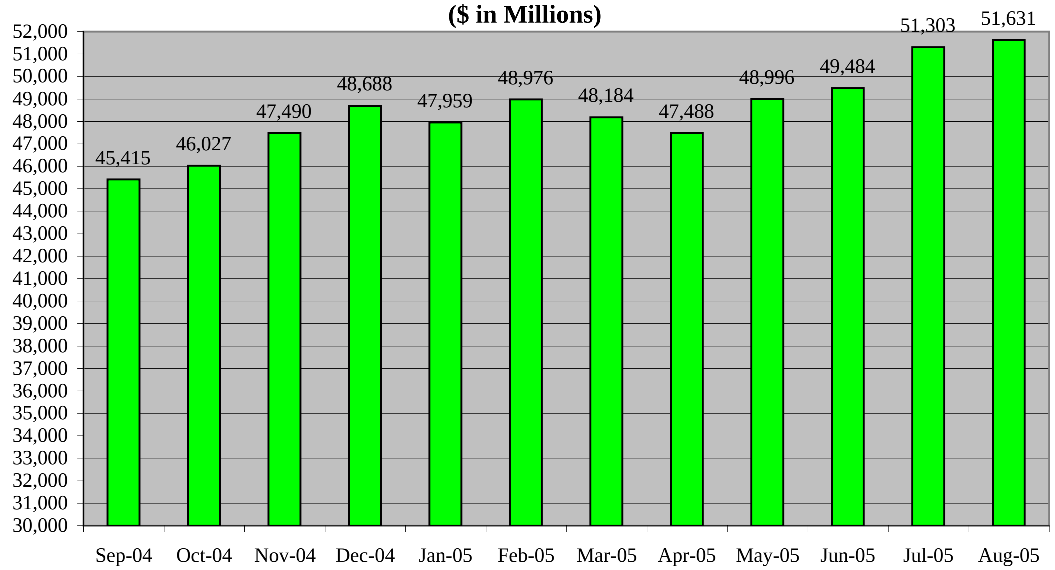
Returns for periods ending 9/30/05 **Oregon Public Employees Retirement Fund** 11-18-05 A.2.b.

OPERF	Policy[1]	Target[1]	$ Thousands	Actual	Year-To-Date	1 YEAR	2 YEARS	3 YEARS	4 YEARS	5 YEARS
	Regular Account				Historical Performance					
Domestic Equity	30-40%	35%	$ 18,094,781	35.5%	**5.08**	**16.35**	**15.60**	**19.29**	**8.77**	**-**
International Equity	15-25%	20%	11,705,115	23.0%	**13.28**	**29.96**	**26.75**	**27.48**	**16.32**	**5.33**
Alternative Equity	7-13%	10%	4,396,573	8.6%	**31.10**	**36.54**	**31.81**	**16.73**	**8.67**	**3.71**
Total Equity	**60-70%**	**65%**	**34,196,469**	**67.1%**						
Total Fixed	**22-32%**	**27%**	**13,255,821**	**26.0%**	**2.87**	**4.97**	**5.37**	**7.40**	**7.04**	**7.94**
Real Estate	**5-11%**	**8%**	**2,996,347**	**5.9%**	**22.16**	**32.40**	**25.24**	**20.72**	**17.74**	**15.79**
Cash	**0-3%**	**0%**	**506,009**	**1.0%**	**2.17**	**2.65**	**1.96**	**1.79**	**1.90**	**2.66**
TOTAL OPERF Regular Account		**100%**	**$ 50,954,646**	**100.0%**	**9.24**	**18.34**	**16.89**	**16.96**	**10.29**	**4.97**
OPERF Policy Benchmark					**6.97**	**14.61**	**14.38**	**15.65**	**9.23**	**4.20**
Value Added					**2.27**	**3.73**	**2.51**	**1.31**	**1.06**	**0.77**

Asset Class Benchmarks:

Benchmark	Year-To-Date	1 YEAR	2 YEARS	3 YEARS	4 YEARS	5 YEARS
Russell 3000 Index	4.00	14.57	14.41	18.13	7.55	(0.72)
MSCI ACWI Free Ex US	12.19	29.48	26.27	27.19	15.65	4.81
Russell 3000 Index + 300 bps--Quarter Lagged	13.05	12.42	18.84	14.81	7.59	4.31
LB Universal--Custom FI Benchmark	2.34	3.74	4.01	4.92	5.61	6.78
NCREIF Property Index--Quarter Lagged	14.12	18.02	14.37	12.08	10.40	10.63
91 Day T-Bill	2.13	2.62	1.86	1.68	1.76	2.49

TOTAL OPERF NAV
(includes variable fund assets)
One year ending September 2005
($ in Millions)



[1]OIC Policy 4.01.18

Oregon

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November 18, 2005

MEETING DATE	11-18-05
AGENDA ITEM	A.2.c. HB2020 Update

TO: Members of the PERS Board

FROM: Paul R. Cleary, Executive Director

SUBJECT: Update of HB2020 Employer Reporting and Accounts Receivable Plan

The agency is in its second year of administering the HB2020 program and using the new employer electronic reporting system. The Membership and Employer Relations Section (MERS) is working with 875 employer-reporting units to process outstanding 2004 employer reports and current 2005 reports. The table below shows the status of 2004 and 2005 employer reports and member records.

	Calendar Year 2004 (As of 11-07-05)	**Calendar Year 2005** (As of 11-07-05)
Reports due (estimated)	12,551	10,830
Outstanding reports	16	606
Reports fully posted at 100%	12,139	8,755
Records due (estimated)	3,065,374	2,528,873
Records not posted	2,459	40,411
Contributions posted	$ 387,824,465	$ 327,215,793

As of November 4, 2005, employers have submitted 99.9 % and 94.4 % of the reports due for 2004 and 2005, respectively. Of those reports submitted 96.7 % for 2004 and 80.8 % for 2005 are 100% accurate. These statistics indicate the major PERS educational effort and the progress employers have made to provide member demographic and wage information from 2004 to 2005. Last year at this time, only 90.7 % of reports due were submitted, and of the reports submitted only 68 % were 100% accurate.

To help employers complete their reports, PERS created semi-monthly payroll reporting classes. Since April 2005, staff has conducted 13 classes for 199 employers. In addition, PERS organized teams to work with employers who have outstanding 2004 data. Since the inception of the teams in May 2005, PERS has helped employer's post approximately 9,600 members' records from 2004 out of approximately 12,100 un-posted records.

Currently three employers are responsible for 16 outstanding 2004 reports (with 50 outstanding records). Staff who report information to PERS for two of these employers have legal problems that have resulted in reporting delays. PERS is working with these employers to identify other staff members who can report data to PERS to resolve the reporting delays. Finally, the remaining employer has committed to have its outstanding 2004 reports to PERS by the end of November 2005.

Besides assisting employers with overdue 2004 and 2005 data reports, PERS implemented an accounts receivable plan to proactively collect receivable balances that are more than 30 days overdue. The first action was to send letters in October to 54 employers who had an aggregate overdue receivable balance of approximately $6.8 million. One employer's receivable made up the largest portion of the total, approximately $4.73 million. The employer owing the $4.73 million paid its outstanding balance within days of receiving the letter. The remaining $2.11million is being actively collected. We intend to follow up with these employers by phone and letters this month.

Oregon

Theodore R. Kulongoski, Governor

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November 18, 2005

MEETING DATE	**11/18/05**
AGENDA ITEM	**B.1. OPSRP Definitions**

TO: Members of the PERS Board

FROM: Steven Patrick Rodeman, Administrator, PPLAD

SUBJECT: Notice of Rulemaking for OAR 459-070-0001, *OPSRP Definitions*

OVERVIEW

- **Action:** None. This is notice that staff has begun rulemaking.
- **Reason:** The current provisions for determining membership eligibility have proven to be administratively difficult for both the system and employers.
- **Subject:** Definition of “qualifying position” for the purposes of the OPSRP Pension Program and IAP.
- **Policy Issue:**
  - o Should the determination of qualifying position be modified to permit an employer to make the eligibility determination at the onset of employment?

BACKGROUND

Under the current rule, for the purposes of initial membership determination, an employee will be considered to be performing service in a qualifying position even if they perform less than 600 hours in the year of hire so long as they perform at least 600 hours in the following year. This provision may delay the determination of membership up to 2 years. Such delay prevents the timely remittance of required contributions and the granting of retirement credit and has proven to be very difficult to administer for both PERS and employers. The proposed amendments would make membership eligibility determination more efficient and easier to administer.

The OAR for the PERS Chapter 238 Program is currently also in rulemaking to address the same issue (see Agenda Item B.2. for this Board meeting).

POLICY ISSUE

- o *Policy Issue: Should the determination of qualifying position be modified to permit an employer to make the eligibility determination at the onset of employment?*

The statutory standard for a qualifying position is 600 hours in a calendar year. The current rule contains a special provision for employees hired too late in the calendar year to accumulate 600 hours. For the purposes of initial membership determination only, an employee will be considered to be in a qualifying position even if they perform less than 600 hours in the first year so long as they perform at least 600 hours in the following year.

This provision requires employers and employees to wait until then end of the following year, or until the employee performs 600 hours, whichever comes first, before knowing that the employee qualified for membership. Contributions can be delayed and retirement credit accruals miscalculated because of this time lag, so this standard has proven to be very difficult to administer for both PERS and employers.

The proposed amendments allow the employer to designate that the employee is in a qualifying position from the onset of employment. This will make membership eligibility determinations more efficient and easier to administer.

LEGAL REVIEW

The attached draft has been submitted to the Department of Justice for legal review and any comments or changes will be incorporated before the rules are presented for adoption.

PUBLIC COMMENT AND HEARING TESTIMONY

A rulemaking is scheduled for November 29 at 2:00 p.m. in PERS headquarters in Tigard. The public comment period ends on November 29, 2005 at 5:00 p.m.

On November 4, 2005, this proposed rule was discussed at a PERS Legislative Advisory Committee meeting. The committee recommended that, for the purposes of initial membership determination, the employer should make the determination of qualification and remit contributions on the “contribution begin date” as determined by the jClarety system.

IMPACT

Mandatory: No, but simplifying this process benefits plan administration and clarifies employee’s expectations.

Impact: Potentially, there may be some impact on the number of people that qualify for OPSRP membership, but those results will depend on individual circumstances and are not anticipated to have a significant impact.

Cost:

- *Members:* There will be no cost to members.
- *Employers:* There are no intrinsic costs to employers. These standards are not being developed with the thought that membership will increase or decrease, but to provide for membership determinations under a clear, consistent framework.
- *Administration:* Eligibility reviews will have to change to follow the established standards, but these processes already involve manual review and calculation so these standards will not substantially affect costs to review and process membership or eligibility issues.
- *Fund:* There will be no effect on the Fund.

RULEMAKING TIMELINE

October 14, 2005	Staff began the rulemaking process by filing Notice of Rulemaking with the Secretary of State.
November 1, 2005	*Oregon Bulletin* published the Notice.
November 18, 2005	PERS Board notified that staff began the rulemaking process.
November 29, 2005	Rulemaking hearing to be held at 2:00 p.m. in Tigard.
November 29, 2005	Public comment period ends at 5:00 p.m.
December 16, 2005	Staff will propose adopting the permanent rule modifications, including any amendments warranted by public comment or further research.

NEXT STEPS

A hearing is scheduled for November 29. The rule is scheduled to be brought before the PERS Board for adoption at the December 16 Board meeting.

OREGON ADMINISTRATIVE RULE
PUBLIC EMPLOYEES RETIREMENT BOARD
CHAPTER 459
DIVISION 070 – OREGON PUBLIC SERVICE RETIREMENT PLAN, GENERALLY

MEETING DATE	**11/18/05**
AGENDA ITEM	**B.1. OPSRP Definitions**

459-070-0001

Definitions

The words and phrases used in this Division have the same meaning given them in ORS 238A.005 unless otherwise indicated in this rule. Specific and additional terms for purposes of Divisions 70, 75 and 80 are defined as follows unless context requires otherwise:

(1) "Break in service" means a period concluding on or after August 29, 2003, during which a member of PERS performs no service, as defined below, with a participating public employer in a qualifying position for a duration of:

(a) Six or more consecutive calendar months; or

(b) 12 or more consecutive calendar months under one of the following circumstances:

(A) The member of PERS ceases performance of service for purposes that have qualified the member for family leave, as described in ORS 238A.025(3)(c), as determined by the employer; or

(B) The member of PERS ceases performance of service for career development purposes, as described in ORS 238A.025(3)(d).

(2) "Calendar month" means a full month beginning on the first calendar day of a month and ending on the last calendar day of the same month.

(3) "Calendar year" means 12 calendar months beginning on January 1 and ending on December 31 following.

(4) "Employee" has the same meaning as "eligible employee" in ORS 238A.005(4).

(5) "Employee class" means a group of similarly situated employees whose positions have been designated by their employer in a policy or collective bargaining agreement as having common characteristics.

(6) "Employee contributions" means contributions made to the individual account program by an eligible employee under ORS 238A.330, or on behalf of the employee under ORS 238A.335.

(7) "Member" has the same meaning given the term in ORS 238A.005(10).

(8) "Member account" means the account of a member of the individual account program.

(9) "Member of PERS" has the same meaning as "member" in ORS 238.005(12)(a), but does not include retired members.

(10) "OPSRP" means the Oregon Public Service Retirement Plan.

(11) "Overtime" means the salary or hours, as applicable, that an employer has designated as overtime.

(12) "PERS" means the retirement system established under ORS chapter 238.

(13)(a) "Qualifying position" means a position or positions in which an employee is expected to perform 600 or more combined hours of service in a calendar year.

(b) If an employee is employed in a position or positions not designated as qualifying and performs 600 or more total hours of service in a calendar year, the position or positions will be considered qualifying and the employee shall be considered to have performed service in a qualifying position from the date of employment or January 1 of the calendar year in which the employee performed more than 600 hours of service, whichever is later.

(c) Except as provided in subsection (d) of this section, if an employee is employed in a position or positions designated as qualifying and performs less than 600 hours of service in a calendar year, the position will be considered non-qualifying from the date of employment or January 1 of the calendar year in which the employee performed less than 600 hours of service, whichever is later.

[*(d) For purposes of determining qualification upon initial employment in a position or positions, but not for determining a break in service or any other purpose, if an employee is employed in a position or positions for less than a full calendar year and performs less than 600 hours of service in that calendar year, but would have performed 600 hours of service or more if the employee had performed service in the same position(s) for the full calendar year, and if the employee performs 600 or more hours of service in the following calendar year, the position or positions will be considered qualifying as of the date of employment.*]

[*(e)*] **(d)** For purposes of determining qualification upon separation from employment in a position or positions, but not for any other purpose, if an employee was employed in a position or positions for less than a full calendar year and performed less than 600 hours of service in that calendar year, but would have performed 600 hours of service or more if the employee had performed service in the same position or positions for the full calendar year, and if the employee performed 600 or more hours of service in the previous calendar year, the position or positions will be considered qualifying as of the date of separation.

(14)(a) "Salary" has the same meaning given the term in ORS 238A.005(16).

(b) Salary is considered earned when paid except as provided in subsection (c) of this section and as otherwise provided in ORS 238A.005(16)(b)(E).

(c) Salary is considered earned when earned for purposes of calculating final average salary.

(15) "School employee" has the meaning given the term in ORS 238A.140(6).

(16) "Service." Except as provided in subsection (c) of this section, a person is still providing "service," for purposes of determining whether a "break in service" has occurred under Section 2a, Chapter 733, Oregon laws 2003 (Enrolled HB 2020), during any calendar month that a member:

(a) Is in an employer/employee relationship; and

(b) Receives a payment of "salary," as that term is defined in ORS 238.005(20) or similar payment from workers compensation or disability.

(c) A member who is a school employee will be considered to provide "service" during any calendar month the institution is not normally in session so long as the member is in an employer/employee relationship both before and after the period the institution is not normally in session.

(17) The provisions of this rule are effective on January 1, 2004.

Stat. Auth.: 238A.450

Stats. Implemented: 238A.005, 238A.025, 238A.140, 238A.330, 238A.335

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November 18, 2005

MEETING DATE	**11/18/05**
AGENDA ITEM	**B.2. PERS Membership**

TO: Members of the PERS Board

FROM: Steven Patrick Rodeman, Administrator, PPLAD

SUBJECT: First Reading for OAR 459-010-0003, *PERS Membership Eligibility*

OVERVIEW

- **Action:** None. This is the First Reading of the rule.
- **Reason:** The current provisions for determining membership eligibility and concurrent employment have proven to be administratively difficult for both the agency and employers.
- **Subject:** Standards for determining membership and eligibility under the PERS Chapter 238 Plan.
- **Policy Issues:**
  - Should concurrent employment be defined as employment occurring within the same calendar year?
  - Should the determination of "qualifying position" be modified to permit an employer to make the eligibility determination at the onset of employment?

BACKGROUND

Under the current rule, a concurrent position is defined as two or more positions that occur within any given calendar month. This determination has always been problematic given the type and nature of information reported to PERS and usually has resulted in a manual review at retirement. This strict requirement has resulted in members being denied membership or service credit that they thought they had earned all along because the service doesn't meet this narrow window of concurrency. The new jClarety reporting system makes this concurrency issue a little easier to administer, but as the reports are tied to pay periods (which can span calendar months for some employers), the information is still not definitive.

Additionally, the current rule provides that for the purposes of initial membership determination, an employee will be considered to be performing service in a qualifying position even if they perform less than 600 hours in the year of hire so long as they perform at least 600 hours in the following year. This provision may push membership determinations out up to 2 years, delaying the timely remittance of required contributions and the granting of creditable service. The proposed amendments would make determining membership eligibility more efficient and easier to administer.

SUMMARY OF PROPOSED RULE AND POLICY ISSUES

The current rule provides that a “concurrent position” means employment segments that occur together in any given calendar month.

- *Policy Issue: Should concurrent employment be defined as employment occurring within the same calendar year?*

Under the PERS Chapter 238 Program, an employee is in a qualifying position if they perform 600 or more hours in a calendar year. For employees who work in two or more positions that may not be qualifying on their own, determining qualifying position becomes onerous. Currently, employers are reporting hours of service, with other information, on their pay date. There is not an administratively efficient way to determine what month the hours reported were actually worked. This makes determining membership and creditable service based on a monthly standard difficult to administer.

Accordingly, because a qualifying position is determined on a calendar year basis, amending the provision for concurrency from monthly to yearly makes administrative sense. Additionally, determining membership and creditable service will more closely align with the requirements of OPSRP as well, making employer reporting consistent throughout the system. Staff recommends these new provisions apply to any eligibility determination made on or after the effective date of the rule.

- *Policy Issue: Should the determination of qualifying position be modified to permit an employer to make the eligibility determination at the onset of employment?*

The statutory standard for a qualifying position is 600 hours in a calendar year. The current rule contains a special provision for employees hired too late in the calendar year to accumulate 600 hours. For the purposes of initial membership determination only, an employee will be considered to be in a qualifying position even if they perform less than 600 hours in the first year so long as they perform at least 600 hours in the following year.

This provision requires employers and employees to wait until then end of the following year, or until the employee performs 600 hours, whichever comes first, before knowing that the employee qualified for membership. Contributions can be delayed and retirement credit accruals miscalculated because of this time lag, so this standard has proven to be very difficult to administer for both PERS and employers.

The proposed amendments allow the employer to designate that the employee is in a qualifying position from the onset of employment. This will make membership eligibility determinations more efficient and easier to administer.

The rule has also been amended to correct citations that changed with adoption of new statutory provisions during the 2005 Legislative session.

LEGAL REVIEW

The attached draft has been submitted to the Department of Justice for legal review and any comments or changes will be incorporated before the rules are presented for adoption.

PUBLIC COMMENT AND HEARING TESTIMONY

A rulemaking hearing was held on October 25 at 2:00 p.m. in PERS headquarters in Tigard. No one attended the hearing.

On November 4, 2005, this proposed rule was discussed at a PERS Legislative Advisory Committee meeting. The committee agreed that a concurrent position should be measured on a calendar year basis rather than a monthly basis.

The committee recommended that, for the purposes of initial membership determination, the employer should make the determination of qualification and remit contributions on the appropriate starting date as determined by the jClarety system.

The comment period ends on November 29, 2005 at 5:00 p.m.

IMPACT

Mandatory: No, but bringing certainty to this process is necessary for simplification. Even though no new members will join the PERS Chapter 238 Plan, the agency handles numerous eligibility determination questions that should be decided under a consistent, reasonable structure.

Impact: Adopting these rule modifications will simplify administration of membership eligibility for PERS and employers. Potentially, there may be some impact on the number of people that qualify for PERS membership, but those results will depend on individual circumstances and are not anticipated to have a significant impact.

Cost:

- *Members:* There will be no cost to members.
- *Employers:* There are no intrinsic costs to employers. These standards are not being developed with the thought that membership will increase or decrease, but to provide for membership determinations under a clear, consistent framework.
- *Administration:* Eligibility reviews will have to change to follow the established standards, but these processes already involve manual review and calculation so these standards will not substantially affect costs to review and process membership or eligibility issues.
- *Fund:* There will be no effect on the Fund.

RULEMAKING TIMELINE

September 14, 2005	Staff began the rulemaking process by filing Notice of Rulemaking with the Secretary of State.

October 1, 2005	*Oregon Bulletin* published the Notice.
October 21, 2005	PERS Board notified that staff began the rulemaking process.
October 25, 2005	Rulemaking hearing held at 2:00 p.m. in Tigard.
November 18, 2005	First reading of the proposed rule.
November 28, 2005	Public comment period ends at 5:00 p.m..
December 16, 2005	Staff will propose adopting the permanent rule modifications, including any amendments warranted by public comment or further research.

NEXT STEPS

The comment period for this rulemaking extends beyond this November Board meeting to allow further reaction to any proposed changes. Adoption is currently scheduled for the Board's December 16, 2005 meeting

OREGON ADMINISTRATIVE RULE
PUBLIC EMPLOYEES RETIREMENT BOARD
CHAPTER 459
DIVISION 010 – MEMBERSHIP

MEETING DATE	**11/18/05**
AGENDA ITEM	**B.2.** **Membership Eligibility**

459-010-0003

Eligibility and Membership for the PERS Chapter 238 Program

(1) For the purpose of this rule:

(a) "Concurrent positions" means positions with two or more PERS participating employers where the positions occur together in any given calendar *[month]* **year**.

(b) "Qualifying position" **means:** *[means a position or concurrent positions in which an employee is expected to perform 600 or more hours of service in a calendar year.]*

[*(A) For purposes of initially determining qualification for membership, but not for any other purpose, if an employee was employed in a position or concurrent positions for less than a full calendar year and performed less than 600 hours of service in that calendar year, but would have performed 600 hours of service or more if the employee had performed service in the same position or concurrent positions for the full calendar year, and if the employee performs 600 or more hours of service in the following calendar year, the position or concurrent positions will be considered qualifying as of the initial date of employment.*]

[(*B*) *For purposes of determining qualification upon separation from employment, but not for any other purpose, if an employee was employed in a position or concurrent positions for less than a full calendar year and performed less than 600 hours of service in that calendar year, but would have performed 600 hours of service or more if the employee had performed service in the same position or concurrent positions for the full calendar year, and if the employee performed 600 or more hours of service in the* *previous calendar year, the position or concurrent positions will be considered qualifying up to the date of separation*.]

[(*C*)]**(A)** [*If*] **For** an employee **who** is employed in a position or in concurrent positions designated as non-qualifying and performs 600 or more total hours of service in a calendar year, the position or concurrent positions will be considered qualifying and the employee shall be considered to have performed service in a qualifying position from the date of employment or January 1 of the calendar year in which the employee performed more than 600 hours of service, whichever is later.

[(*D*)]**(B)** Except as provided in paragraph (A) [*and (B)*] of this subsection, [*if*] **for** an employee **who** is employed in a position or concurrent positions designated as qualifying and performs less than 600 hours of service in a calendar year, the position or concurrent positions will be considered non-qualifying from the date of employment or January 1 of the calendar year in which the employee performed less than 600 hours of service, whichever is later.

(C) For purposes of determining qualification upon separation from employment, but not for any other purpose, if an employee was employed in a position or concurrent positions for less than a full calendar year and performed less than 600 hours of service in that calendar year, but would have performed 600 hours of service or more if the employee had performed service in the same position or concurrent positions for the full calendar year, and if the employee performed 600 or more hours of service in the previous calendar year, the position or concurrent positions will be considered qualifying up to the date of separation.

(c) "Non-qualifying position" means:

(A) Any position that does not conform to the requirements set forth in subsection (b) of this section;

(B) Positions with two or more PERS participating employers in which there is an employee/employer relationship, as defined in OAR 459-010-0030, that do not meet the definition of "concurrent positions" even though each position, when added together, may total 600 or more hours of service in a calendar year.

(d) "Service" means any calendar month an employee:

(A) Is in an employer/employee relationship, as defined in OAR 459-010-0030; and

(B) Received a payment of "salary," as defined in ORS *[238.005(20)]* **238.005(21)** or similar payment from workers compensation or disability.

(2) An employee qualifies as a member of PERS under ORS 238.015 if the employee:

(a) Has completed a 6 month waiting period as defined in ORS 238.015(1);

(b) Has been employed in a qualifying position;

(c) Is not otherwise ineligible for membership; and

(d) Has not elected to participate in an optional or alternate retirement plan as provided in ORS Chapters 243 and 353.

(3) An employee shall remain an active member in PERS if the employee is employed in a qualifying position that totals 600 or more hours of service per calendar year.

(4) If an employee hired into a non-qualifying position completed service meeting the definition of "qualifying position" under section (1)(b) of this rule, the employee shall qualify as an active member for that calendar year.

(5)(a) If an active member in a qualifying position is terminated or they separate from employment prior to completing 600 hours of service in a year, the member shall not receive any service credit for that year unless they qualify under section (1)(b)(B) above.

(b) If an active member in a qualifying position is terminated or they separate from employment prior to completing 600 hours of service in a year and do not qualify under section (1)(b)(B), in addition to not receiving any service credit, all contributions for the year, employee and employer, shall be credited to the employer.

(6) The provisions of this rule are effective **for all eligibility determinations made on or after the effective date of this rule** *[on January 1, 2005]*.

Stat. Auth.: ORS 238.650

Stats. Implemented: ORS 238.015, 243.800 & 353.250

Oregon

Theodore R. Kulongoski, Governor

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November 18, 2004

MEETING DATE	**11/18/05**
AGENDA ITEM	**B.3. Creditable Service**

TO: Members of the PERS Board

FROM: Steven Patrick Rodeman, Administrator, PPLAD

SUBJECT: First Reading for OAR 459-010-0014, *PERS Creditable Service*

OVERVIEW

- **Action:** None. This is the First Reading of the rule.
- **Reason:** The current OAR provides for PERS Chapter 238 Program members to receive creditable service for "full months and major fractions of a month." This provision has proved to be very difficult for employers to report the necessary information. The proposed rule amendments simplify the standards by which creditable service would be granted to members in the PERS Chapter 238 Program and ease the reporting of the necessary information by employers.
- **Subject:** Determining creditable service under the PERS Chapter 238 Program.
- **Policy Issue:**
  - Whether creditable service should be granted based on a presumption that a "major fraction of a month" has been performed in any given calendar month.

BACKGROUND

Under ORS Chapter 238, members earn "creditable service" for any period of time during which the member is being paid a salary. Service credit is measured in full months and major fractions of a month; both of which add to full years of credit as one-twelfth of a year. Whether a member has performed a major fraction of a month proves difficult to determine given the current EDX reporting structure.

SUMMARY OF PROPOSED RULE AND POLICY ISSUE

Initially, the advisory committee on this issue concurred that the cleanest solution was to divide the 600-hour yearly requirement by the twelve months, which would result in 50 hours of service constituting a major fraction of each month. Currently, the administrative rule provides that creditable service will be granted for each month a member performs 50 hours of service, which is defined as constituting a major fraction of a month.

Under the jClarety reporting structure, employer reports are tied to payroll information, which can span across months for some employers. With this reporting structure, determining the number of hours a member actually worked in a month (and, therefore, has met the 50-hour minimum for the granting of creditable service) is not possible.

- *Policy Issue: Whether a "major fraction of a month" should be presumed if a member performs at least 600 hours in calendar year.*

The proposed rule amendments provide that if a member performs at least 600 hours of service in a calendar year, they will receive retirement credit for any month in which they are reported to have performed service. Adopting this presumption of hours, rather than have employers re-program their systems, keeps in place the yearly standard while avoiding administrative complications.

The proposed rule would have excluded any month during which a member has a period of leave without pay spanning more than 11 working days. The Legislative Advisory Committee, however, requested that provision be removed. They remarked that a person could still meet the 50-hour standard with the remaining working days and taking such a leave should not presumptively exclude a member from earning credit for that month.

LEGAL REVIEW

The attached draft has been submitted to the Department of Justice for legal review and any comments or changes will be incorporated before the rules are presented for adoption.

PUBLIC COMMENT AND HEARING TESTIMONY

A rulemaking hearing was held on October 25 at 2:00 p.m. in PERS headquarters in Tigard. No one attended the hearing.

On November 4, 2005, this proposed rule was discussed at a PERS Legislative Advisory Committee meeting. The committee understood the reporting issue and agreed that creditable service should be granted under the general provisions set forth in the proposed rule. They recommended that the 50-hour standard provision be removed as this provision was confusing. They also did not like the exception that removed creditable service if a member has a leave without pay period spanning more than 11 working days, so that provision has also been removed. Additionally, they recommended the effective date of the rule be January 1, 2006.

The comment period ends on November 29, 2005 at 5:00 p.m.

IMPACT

Mandatory: No, but bringing certainty to this process is necessary for simplification.

Impact: Adopting these rule modifications will simplify administration of creditable service for PERS and employers. Potentially, there may be some impact on the amount of service members are granted, but those results will depend on individual circumstances and are not anticipated to have a significant impact.

Cost:

- *Members:* There will be no cost to members.
- *Employers:* There are no intrinsic costs to employers. These standards are not being developed with the thought that membership will increase or decrease, but to provide for the granting of creditable service under a clear, consistent framework.

- *Administration:* Creditable service reviews will not have to change to follow the established standards since creditable service will continue to be granted under a major fraction of a month standard.
- *Fund:* There will be not effect on the Fund.

RULEMAKING TIMELINE

September 14, 2005	Staff began the rulemaking process by filing Notice of Rulemaking with the Secretary of State.
October 1, 2005	*Oregon Bulletin* published the Notice.
October 21, 2005	PERS Board notified that staff began the rulemaking process.
October 25, 2005	Rulemaking hearing held at 2:00 p.m. in Tigard.
November 18, 2005	First reading of the proposed rule.
November 28, 2005	Public comment period ends at 5:00 p.m..
December 16, 2005	Staff will propose adopting the permanent rule modifications, including any amendments warranted by public comment or further research.

NEXT STEPS

The comment period for this rulemaking extends beyond this November Board meeting to allow further reaction to any proposed changes. Adoption is currently scheduled for the Board's December 16, 2005 meeting.

OREGON ADMINISTRATIVE RULE
PUBLIC EMPLOYEES RETIREMENT BOARD
CHAPTER 459
DIVISION 010 – MEMBERSHIP

MEETING DATE	**11/18/05**
AGENDA ITEM	**B.3.** **Creditable Service**

459-010-0014

Creditable Service in PERS Chapter 238 Program

(1) For purposes of this rule*[:*

(a)]**"**Service credit" has the same meaning as "creditable service" in ORS 238.005(5).

[*(b)*](**2**) [*"Major fraction of a month" means a minimum of 50 hours in any calendar month in which an active member is being paid a salary by a participating public employer and contributions are due to the system either by or on behalf of the member*.] **An active member will be deemed to have performed service for a major fraction of a month and will be granted a month of creditable service if:**

(A) The member has performed at least 600 hours of qualifying service, as defined in OAR Chapter 459, in that calendar year; and

(B) The member's employer(s) have reported them as performing service in that calendar month.

[*(2) An active member, as defined in ORS 238.005(12)(b), shall accrue one full month of service credit if the employee:*

(a) Is employed in a qualifying position as defined in OAR Chapter 459; and

(b) Works a major fraction of a calendar month.]

(3) If the active member is a school employee, they may instead accrue one half year of service credit if the employee:

(a) Is or was employed in a qualifying position as defined in OAR Chapter 459; and

(b) Is employed for all portions of a school year when it is normally in session.

(4) Except as provided for under section (3) of this rule, an employee may not accrue more than one full month of service credit for any number of hours worked in a calendar month and no more than one year of service credit for any number of hours worked in a calendar year.

(5) The provisions of this rule are effective **for eligibility determinations made** on **or after** January 1, 200[*5*]**6**.

Stat. Auth.: ORS 238.650

Stats. Implemented: ORS 238.015

Oregon

Theodore R. Kulongoski, Governor

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MEETING DATE	11/18/05
AGENDA ITEM	B.4.

November 18, 2005

TO: Members of the PERS Board

FROM: Steven Patrick Rodeman, Administrator
Policy, Planning, & Legislative Analysis Division

SUBJECT: Earnings Crediting and Reserving Policy Update

Staff continues to develop a comprehensive earnings crediting policy with recommended reserving goals and objectives. The Legislative Advisory Committee (LAC) met on November 4, 2005 to consider the current status of earnings crediting rules and policies, in light of the significant changes to the system's dynamics and the shifting role that reserves have played over the plan's history.

Included with this memo are the key materials that were distributed at that meeting:

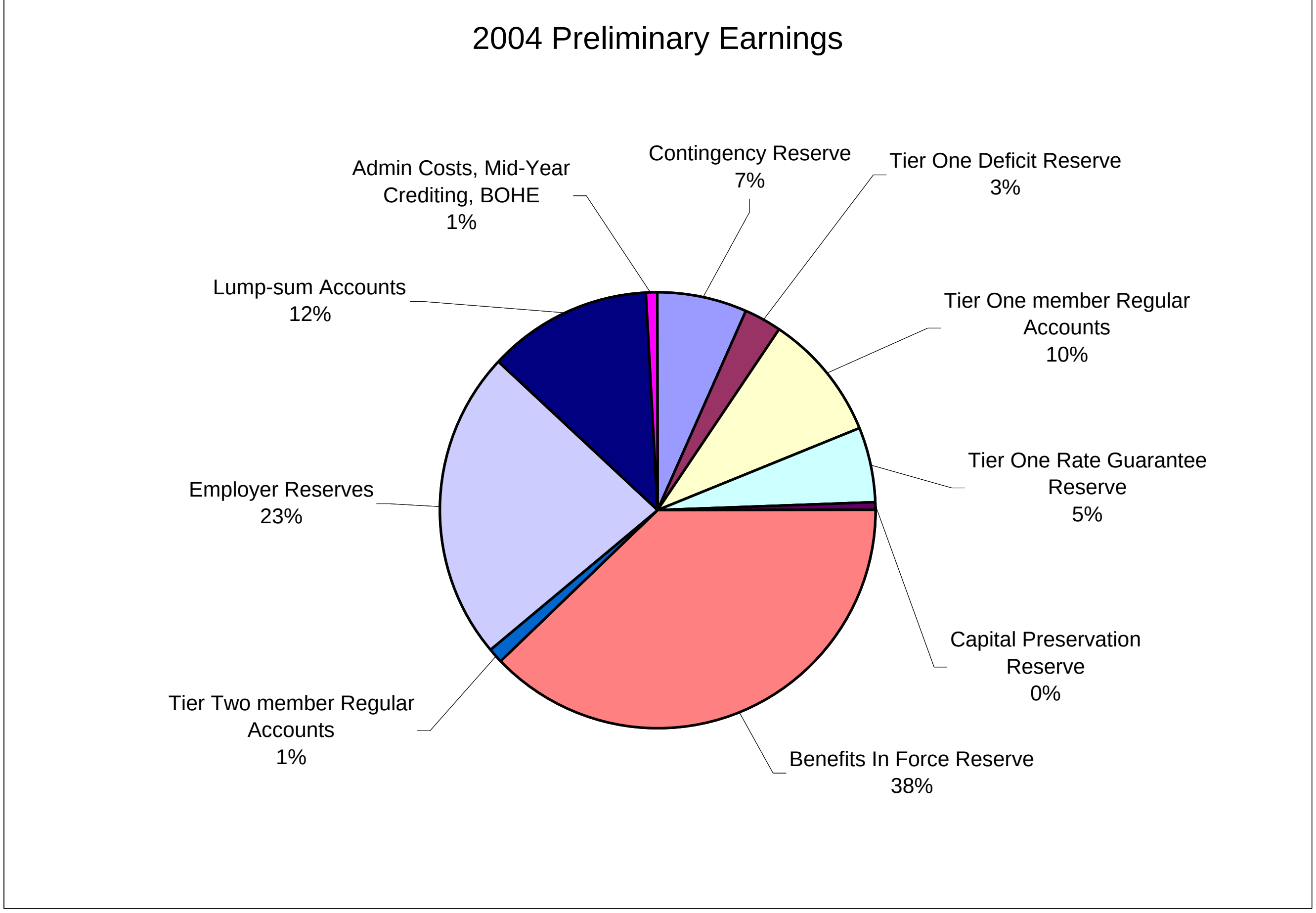
1. A summary table and pie chart showing the preliminary account and reserve balances as a result of the Board's 2004 earnings crediting decision in October, 2005;
2. A draft historical chart showing the transactions and balances in the Contingency, Gain/Loss, Tier One Deficit/Rate Guarantee, and other reserves over the plan's history. This chart was used to explain the shifting uses and policies applied to reserves over the plan's life. (Note that this chart is a draft and has not been updated to fully show the effects of the 1999 earnings reallocation.)
3. A memo summarizing the statutory provisions on PERS Fund reserves and some of the case law that has considered the Board's authority or use of the reserves.

The LAC employer and employee representatives requested an opportunity to return to their respective groups to discuss these materials and consider their recommendations. We expect to reconvene the LAC later this month or early next in the hopes of developing a final policy recommendation to present to the PERS Board at its December 2005 or January 2006 meeting. The delay to January may be caused by the LAC members wanting to see the results of Mercer's financial modeling (slated for the Board's December 2005 meeting) before recommending any direction on the earnings crediting and reserving policy.

2004 Earnings Crediting

(Based on 2004 Preliminary Earnings and *Eugene* Estimated Balances)
Contingency Reserve at 7.5%; Capital Preservation Reserve at $27.55M
(All dollar amounts in millions)

Reserve	2004 Crediting	Balance Before Crediting	Preliminary Earnings Distribution	Balance After Crediting
Contingency Reserve	7.50%	$1,106.4	$370.9	$1,477.3
Tier One Deficit Reserve	$162.3M	-162.3	162.3	0.0
Tier One member Regular Accounts	8.00%	6,762.0	540.9	7,302.9
Tier One Rate Guarantee Reserve	$307.0M	0.0	307.0	307.0
Capital Preservation Reserve	$27.55M	428.4	27.5	455.9
Benefits In Force Reserve	12.47%	17,198.8	2,142.3	19,341.1
Tier Two member Regular Accounts	13.27%	494.1	64.9	559.0
Employer Reserves	13.27%	9,806.4	1,304.4	11,110.8
Lump-sum Accounts	13.68% Avg.	5,092.7	691.3	5,784.0
Admin Costs, Mid-Year Crediting, BOHE	Various	0.0	54.3	0.0
Total		$40,726.5	$5,665.8	$46,338.0



Oregon Public Employees Retirement System
History of Contingency, Deficit, Gain-Loss, and Pending Reserve Activity
Through December 31, 2004

	ORS 238.670(1)		**ORS 238.255(2)**		**ORS 238.670(3)**		**ORS 238.670(4)**		
	Contingency Reserve		Employee Deficit / Tier One Rate Guaranty Reserve		Gain/Loss Reserve		Pending Reserve		
Date	Activity	Balance	Activity	Balance	Activity	Balance	Activity	Balance	Description for Activity
06/30/1952		90,541							
	61,929								Added from earnings
	-7,288								Transfer to retirement reserve to cover death benefit of an employee of a city which had withdrawn form the system..
06/30/1953		145,182							
	62,652								Added from earnings
06/30/1954		207,834							
	70,304								Added from earnings
06/30/1955		278,138							
	-19,308								Adjustment for the calendar year earnings from a fiscal year.
12/31/1955		258,830							
	127,058								Added from earnings
12/31/1956		385,889							
	150,951								Added from earnings
12/31/1957		536,840							
	177,366								Added from earnings
12/31/1958		714,206							
	138,045								Added from earnings
12/31/1959		852,251							
	177,659								Added from earnings
12/31/1960		1,029,910							
	217,378								Added from earnings
12/31/1961		1,247,289							
	269,598								Added from earnings
12/31/1962		1,516,887							
	309,217								Added from earnings
12/31/1963		1,826,104							
	288,338								Added from earnings
12/31/1964		2,114,441							
	78,843								Added from earnings
	-322,690								**Unknown change**
12/31/1965		1,870,594							
	181,314								Added from earnings
	-39,056								**Unknown change**
12/31/1966		2,012,852							
	211,788								Added from earnings

DRAFT
(Not fully adjusted for 1999 recrediting)

Date	ORS 238.670(1) Contingency Reserve Activity	ORS 238.670(1) Contingency Reserve Balance	ORS 238.255(2) Employee Deficit / Tier One Rate Guaranty Reserve Activity	ORS 238.255(2) Employee Deficit / Tier One Rate Guaranty Reserve Balance	ORS 238.670(3) Gain/Loss Reserve Activity	ORS 238.670(3) Gain/Loss Reserve Balance	ORS 238.670(4) Pending Reserve Activity	ORS 238.670(4) Pending Reserve Balance	Description for Activity
12/31/1967		2,224,640							
	189,343				189,343				Added from earnings
	-1,112,000				1,112,000				Transfer from contingency to capital gain loss
					-19,994				Capital Losses not amortized
12/31/1968		1,301,983				1,281,349			
					-1,778				Capital Losses not amortized
12/31/1969		1,301,983				1,279,571			
	207,922								Added from earnings
					-2,706				Capital Losses not amortized
12/31/1970		1,509,905				1,276,865			
	291,526								
					-52,172				Capital Losses not amortized
12/31/1971		1,801,431				1,224,693			
	700,215				**-700,215**				**Transfered. No documentation available.**
					-75,923				Capital Losses not amortized
12/31/1972		2,501,646				448,554			
					-12,169				Capital Losses not amortized
12/31/1973		2,501,646				436,385			
			-13,599,302						Distribution to Employee accounts to meet ORS 237.277 guaranty of 5.50%.
12/31/1974		2,501,646		-13,599,302					
	4,375,000		4,920,668						**Added from earnings (Note: Restated per 1975 financial statements)**
12/31/1975		6,876,646		-8,678,634		364,105			
	3,660,388		8,678,634						Added from earnings
					20,172				Gains or losses on sales of securitie
12/31/1976		10,537,034		**0**		384,277			**Note: Deficit Reserve Liquidated**
	-10,537,034								Employers, and Benefits-in-Force Reserves due to poor earnings year.
					71,833				Gains or losses on sales of securitie
			-9,012,290						accounts to meet 7.00% distribution requirments of ORS 238.255(2), in excess of earnings available.
12/31/1977		**0**		-9,012,290		456,110			
					153,787				Gains or losses on sales of securitie
			1,774,818						Partial liquidation of deficit reserve from 1978 earnings available to employees.
12/31/1978				-7,237,472		609,897			
					-609,897				Distributed to reserves.
			7,237,472						Liquidation of deficit reserve from 1979 earnings available to employees.
12/31/1979				**0**		**0**			**Deficit and Gain/Loss Reserves Liquidated**
12/31/1980					2,062,509	2,062,509			Amount reserved at option of PERS Board to offset future investment gains or losses

	ORS 238.670(1)		ORS 238.255(2)		ORS 238.670(3)		ORS 238.670(4)		
	Contingency Reserve		Employee Deficit / Tier One Rate Guaranty Reserve		Gain/Loss Reserve		Pending Reserve		
Date	Activity	Balance	Activity	Balance	Activity	Balance	Activity	Balance	Description for Activity
12/31/1981					-36,727,738	-34,665,229			Losses amortized over remaining life of Investments
					-63,754				Restatement - Correction in prior periods
					120,717,473				Amount reserved at option of PERS Board to offset future investment gains or losses
12/31/1982						85,988,490			
12/31/1983					196,499,125	282,487,615			Change in Accounting Principle. Accumulated loss distributed with 1982 earnings. Losses distributed in year recognized.
									Distribuion of 7.50% in excess of 1984 earnings of 7.33%.
					-2,062,509				Elimination of 1980 earnings accumulated.
12/31/1984					-4,227,226	276,197,880			Partial elimination of 1982 earnings accumulated.
12/31/1985					274,594,661	550,792,541			
					-3,134,250				Restatement to correct accounting for investment manager fees.
					4,448				Adjustment to 1983 earnings accumulated.
12/31/1986					222,806,110	770,468,849			
					-213,666,995				Residual equity transfer to fund legislatively mandated Retirement Health Insurance Trust Account
12/31/1987					53,692,788	610,494,642			
					-136,333,005				Residual equity transfer to fund legislatively mandated Retirement Health Insurance Trust Account
					388,655,846				Residual equity transfer to return to the PERF amounts previously transferred, as a result of Supreme Court ruling.
12/31/1988					231,941,243	1,094,758,726			
					16,805,496				Residual equity transfer to return to the PERF amounts previously transferred, as a result of Supreme Court ruling.
12/31/1989					505,762,007	1,617,326,229			
					1,207,956				Adjustment to 1989 earnings accumulated.
12/31/1990					-892,288,314	726,245,871			
12/31/1991					762,268,766	1,488,514,637			
12/31/1992					-126,481,650	1,362,032,987			Distribuion of 8.00% in excess of 1992 earnings of 6.94%.
12/31/1993					398,217,758	1,760,250,745			
12/31/1994					-851,211,756	909,038,989			Distribuion of 8.00% in excess of 1994 earnings of 2.16%.
12/31/1995					1,239,674,097	2,148,713,086			
12/31/1996					600,722,103	2,749,435,189			
12/31/1997					394,528,646	3,143,963,835			

	ORS 238.670(1)		ORS 238.255(2)		ORS 238.670(3)		ORS 238.670(4)		
	Contingency Reserve		Employee Deficit / Tier One Rate Guaranty Reserve		Gain/Loss Reserve		Pending Reserve		
Date	Activity	Balance	Activity	Balance	Activity	Balance	Activity	Balance	Description for Activity
12/31/1998					320,684,252	3,464,648,087			
12/31/1999					1,304,629,236	4,769,277,323			
12/31/2000					-2,272,170,177	2,497,107,147			Distribuion of 8.00% in excess of 2000 earnings of .63%.
12/31/2001			-610,227,886.00	-610,227,886.00	-2,497,107,146.86	0.00	-1,780,685,635.48	-1,780,685,635.48	Gain-Loss Reserve liquidated to Member, Employer and Benefit Reserves 2001 Deficit Reserve established for investment losses attributable to Tier One members. 2001 Pending Reserve established for investment losses attributable to Tier One Employer Accónts and Benefits Reserve.
12/31/2002			-1,320,795,495.94	-1,931,023,381.94			-2,238,497,961.00	-4,019,183,596.48	
					(Capital Preservation Reserve)				
12/31/2003	524,818,646.48	524,818,646.48	1,675,412,831.78	-255,610,550.16	428,436,521.57	428,436,521.57	4,019,183,596.48	0.00	
	201,669,946.07								Adjustment to Employer Accounts for 1999 OEF Crediting. Additional $321,703,074 from 1999 earnings will be credited to the Contingency Reserve when all accounts and reserves are recalculated for *Strunk/Eugene* .
12/31/2004	370,944,585.36	1,097,433,177.91		-255,610,550.16	27,550,000.00	455,986,521.57			The Employee Deficit Reserve is expected to be liquidated when 2004 annual earnings have been posted to Tier One accounts, and leaving a positive balance in the Tier One Rate Guaranty Reserve of approximately $300 million.

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November 1, 2005

To: Members of the Legislative Advisory Committee

From: Steven Patrick Rodeman, Administrator
Policy, Planning, and Legislative Analysis Division

Re: Statutory Reserve Provisions

To aid in our discussion of the PERS Board's earning crediting policy at the November 4, 2005 meeting, the following memo summarizes the statutory provisions on PERS Fund reserves and some recent related court rulings.

Contingency Reserve

Statutory Authority: ORS 238.670(1)

When Funded? When income for the calendar year equals or exceeds the assumed rate.

How Funded? "Interest and other income received through investment of the [PERF]."

Limit on Annual Funding: Cannot exceed 7.5% of income in a year.

Limit on Total Funding: Until the board determines the reserve is adequately funded for the purposes specified.

Permitted Uses:

1) Prevent any deficit of moneys available to pay retirement allowances;
2) Prevent any deficit caused by an employer's insolvency (reserves for this purpose must come from earnings on employer contributions);
3) Pay legal expenses or judgments that do not arise in the ordinary course of adjudicating an individual member's benefits or an individual employer's liabilities.
4) Any other contingency that the board may determine to be appropriate (so long as the use is in furtherance of the PERS Funds' trust purpose).

Capital Preservation Reserve

Statutory Authority: ORS 238.670(3)

When Funded? This reserve can be funded at any time.

How Funded? 1) "Interest and other income received through investment of the fund" or 2) Transfers from the Contingency Reserve of "such amount as the board determines to be unnecessary" for those purposes but necessary for the purposes of the Capital Preservation Reserve.

Limit on Annual Funding: None.

Limit on Total Funding: "Such part of the income as the board considers necessary."

Permitted Uses: "To offset gains and losses in invested capital." "Losses" can be construed to include current and prior year losses.

Benefits in Force Reserve

Statutory Authority: ORS 238.670(2)

When Funded? This reserve is credited at the close of each calendar year.

How Funded? "Interest and other income received during the calendar year."

Limit on Annual Funding: Judge Lipscomb specifically addressed this issue in his opinion accompanying the *City of Eugene* trial court decision:

> Specifically, the statute provides that "at the close of each calendar year the board shall set aside . . . a sufficient amount to credit (the Benefits-in-Force Reserve) varying percentage amounts adopted by the board as a result of periodic actuarial investigations." [Employers] contend that this language requires that the Benefits-in-Force Reserve must be "trued up" out of each calendar year's earnings in accordance with the investigations of the Board's actuary. It is only after the full needs of existing retirees have been met that the earnings of any calendar year may be allocated to the accounts of existing employees and their employers. The Board and the [members] contend that historically the "varying percentage amounts" language was intended to refer only to the current earnings assumption, which is presently 8%.
>
> It is apparent from this statute that each year the Board must appropriately credit the Benefits-in-Force Reserve before crediting other accounts. Little else is readily apparent from the statutory language. Accordingly, this Court cannot say, as a matter of law, that the Board has acted erroneously in failing to meet the full needs of the Benefits-in-Force Reserve before crediting other accounts. The wording of the statute supports the employers' view, but the statute's history does not.
>
> This provision cries out for legislative clarification, but until that occurs this Court is able to determine only that the requirements of this statute must be complied with before the other accounts of the system are addressed. Apparently, this has not been the Board's ordinary practice, but it must be. Therefore, upon remand of the March 2000 earnings allocation order, the Board must first comply with ORS 238.670(2) before allocating the remaining earnings in accordance with its discretionary authority and with the other provisions of this order.

Limit on Total Funding: Same as the above limit on annual funding. Note that the statute does require that if the PERF earns more than the assumed rate, the BIF is to "participate in such excess."

Permitted Uses: This reserve is used to pay retired members' pensions and annuities.

Tier One Member Deficit Reserve

Statutory Authority: ORS 238.255(1)

When Used? This reserve is debited whenever there are insufficient earnings to credit the assumed rate to Tier One member regular accounts.

How Funded? "Earnings in excess of the assumed rate…shall first be applied to reduce or eliminate" the Deficit Reserve.

Annual Limit on Use: Only debited in years where earnings or other reserves are inadequate to credit the assumed rate to Tier One member regular accounts.

Limit on Deficit Status: This reserve may not be maintained on a deficit basis for more than five years.

Tier One Rate Guarantee Reserve

Statutory Authority: ORS 238.255(1)

When Used? This reserve is the "positive balance" twin of the Tier One Member Deficit Reserve. When funded, the balance in this reserve can be reduced to fund crediting of the assumed rate to Tier One member regular accounts.

How Funded? By rule, earnings from Tier One member regular accounts are used to fund this reserve.

Limit on Total Funding: This reserve is to be funded "with amounts determined by the board, after consultation with the actuary…, to be necessary to ensure a zero balance in the account when all [Tier One members] have retired."

Other Conditions: Only when this reserve is fully funded to the limit described above for the three immediately preceding calendar years could the PERS Board credit more than the assumed rate to Tier One member regular accounts.

Allocating Earnings Among Accounts

In Judge Lipscomb's final opinion and order in the *City of Eugene* case, he stated the following as to the PERS Board's authority to allocate earnings among accounts:

> [T]his Court does find that the Board has discretion to respond to the apparent relative needs of each of its accounts with varying allocations of the available earnings of the Fund….[I]n exercising its discretion in accordance with the reallocation of the 1999 earnings upon remand on the other issues in this case, the Board should not feel constrained from discriminating among the various accounts on the basis of relative need. That authority plainly exists and it should be exercised when appropriate.

Judge Lipscomb also reviewed the Board's allocation of 1999 member account earnings to employers to make up for large returns on variable accounts. The judge opined:

> As a trustee, the Board had an absolute duty of loyalty to the beneficiaries of the trust funds. Interest earned on those employee funds should not have been diverted from the Fund to the accounts of employers whose funds had not participated in producing those earnings and who were not beneficiaries of the Fund.
>
> The statutorily unauthorized distribution of earnings on employee accounts held in the variable fund to the employer accounts conflicts with the overall statutory scheme established by the legislature for public employee retirement, and in particular, with ORS 238.250 and ORS 238.260. The statutes contemplate that all earnings on employee funds which are not needed for other enumerated statutory purposes should be credited to the employee accounts.

In the *Strunk v. PERB* case, the Oregon Supreme Court concluded that, "Tier One members have no contractual right … to the crediting of annual earnings in excess of the assumed earnings rate to their regular accounts." Rather, the legislature "has reserved for itself the ability to redirect any excess earnings."

Oregon

Theodore R. Kulongoski, Governor

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November 18, 2005

MEETING DATE	**11/18/05**
AGENDA ITEM	**C.1.** **Underpayment Interest Rate**

TO: Members of the PERS Board

FROM: Steven Patrick Rodeman, Administrator, PPLAD

SUBJECT: Adoption of OAR 459-007-0015, *Interest Rate Applied to Underpayment of Estimated Benefits*

OVERVIEW

- **Action:** Adopt permanent rule modifications to OAR 459-007-0015, Interest Rate Applied to Underpayment of Estimated Benefits
- **Reason:** 2005 SB 109 authorizes the PERS Board to determine the rate to be applied to the underpayment of estimated benefits.
- **Subject:** To determine which interest rate to apply to the underpayments of estimated benefits.
- **Policy Issue:**
  - What rate should be used to credit interest on underpaid estimated payments under ORS 238.455(5)?

BACKGROUND

Prior to the enactment of Senate Bill 109 by the 2005 Oregon Legislature, ORS 238.455(5) required that if an estimated payment results in an underpayment of $10 or more a month, the PERS Board shall pay interest on the underpaid balance “at the rate credited to the Public Employees Retirement Fund for the prior year” until the underpayment is paid. OAR 459-007-0015 set that rate as simple interest based on the rate credited to the member’s respective Tier for the prior year.

SUMMARY OF RULE AND POLICY ISSUES

SB 109, which went into effect on June 28, 2005, gives the Board authority to determine the rate to be applied to these underpaid estimated benefits. The rate is applicable to members who have effective dates of retirement that are on or after January 1, 2006. Those who retired prior to January 1, 2006 will receive the rates as provided under the current rule as described above.

- *Policy Issue: What rate should be used to credit interest on underpaid estimated payments under ORS 238.455(5)?*

There are several possible rates the Board could choose to apply to underpayments. These alternatives have been described in the prior memos on this rule. Briefly, they consist of:

1. The Assumed Rate (currently 8%).
2. A Tier One and Tier Two factor showing the latest year to date earnings (pro-rate of 8% for Tier One; actual overall fund gains and losses for Tier Two).
3. The Average Annualized Rate (short-term investment rate used by other earnings crediting rules to calculate distribution interest).
4. Other rates, such as the U.S. Treasury short-term rates, Oregon's 9.00% statutory rate on money owed (ORS 82.010) or a rate chosen by the Board that is not associated with a PERS Fund or external rate.

Based on the Board's prior policy decision to apply the Average Annualized Rate (AAR) to calculate distribution interest, staff recommends using that rate to credit interest on these underpayments. The proposed rule modification would use the AAR in effect at the time the final payment is calculated, to simplify the calculation. Using this rate would most closely approximate the actual return on those dollars while in the PERS Fund.

LEGAL REVIEW

The proposed rule amendments were submitted to the Department of Justice for review. Counsel had no substantive comments or changes.

PUBLIC COMMENT AND HEARING TESTIMONY

A rulemaking hearing was held on Tuesday, September 27, 2005. One person, Martha Sartain, appeared at the hearing to testify. A summary of her testimony, which was addressed in the October 18 first reading Board memo, is attached to this Board memo.

The comment period ended on November 1, 2005. PERS received written comments from five individuals. The comments from Martha Sartain and Paul Gornick were summarized in the October 21 first reading Board memo. PERS also received comments from Oregon PERS Retirees, Inc. Chairperson Kathleen Beaufait, John Goodson and David Onheibera. Copies of all written comments are attached to this Board memo.

Ms. Beaufait, Mr. Goodson and Mr. Onheibera commented that the Average Annualized Rate is too low. Ms. Beaufait believes the rate should be set at 9.00%, which is the rate specified in ORS 82.010 as the rate applied to transactions if parties have not otherwise agreed to a rate of interest, and the rate of interest on judgments for the payment of money. Mr. Onheibera believes the rate should be what is credited to the respective Fund for the members' accounts. Ms. Beaufait and Mr. Onheibera believe that a higher rate would provide a disincentive to underpayments.

PERS staff responds that the Average Annualized Rate is the closest measure to what those underpaid dollars earned while awaiting determination and payout. A higher rate would not provide any extra incentive for staff to try to clear these underpayments. In the normal course of business, these situations are rare and arise when some information is not available to complete processing the retirement application. PERS staff works diligently to close these situations by acquiring the necessary documentation from the employer or member (as the case may be) and the calculus of what rate may be applied to any amounts ultimately owed to the member does not diminish or enhance that effort.

Ms. Beaufait also states that it is difficult for the retiree to determine what the Average Annualized Rate is. Staff's response is that the rate is defined and used consistently in administrative rule. PERS communicates this rate every month to its staff and it can be readily obtained by contacting PERS Customer Service via e-mail or telephone.

IMPACT

Mandatory: No; the Board could retain the existing rule language. That rule, however, is imprecise and staff recommends the modifications explained above.

Impact: The rule modifications apply to underpayments of estimated benefits to members who have effective dates of retirement that are on or after January 1, 2006.

Cost:

- *Members*: There will be no new costs to members.
- *Employers*: There is no new cost to employers.
- *Administration*: There will be some costs in changing to the rate specified by the Board, but since estimated payment adjustments are ad-hoc calculations, the incremental costs of changing to whatever rate the Board selects is minimal.
- *Fund*: If the Board adopts the rate recommended by staff, the earnings rate paid should closely reflect the actual earnings on these dollars while they were in the fund, so there should be little or no cost to the Fund.

RULEMAKING TIMELINE

August 15, 2005	Staff began the rulemaking process by filing Notice of Rulemaking with the Secretary of State.
September 1, 2005	*Oregon Bulletin* published the Notice.
September 23, 2005	PERS Board notified that staff began the rulemaking process.
September 27, 2005	Rulemaking hearing held at 2:00 p.m. in Tigard.
October 21, 2005	First Reading
November 1, 2005	Public comment period ended at 5:00 p.m.
November 18, 2005	Rule is presented to the PERS Board for adoption with changes resulting from public comment or reviews by staff or further research.

BOARD OPTIONS

The Board may:

1. Pass a motion to "adopt the permanent rule modifications to OAR 459-007-0015, as presented."
2. Take no action and direct staff to make changes to the rules or take other action.

STAFF RECOMMENDATION

Staff recommends the Board choose Option #1.

Reason: The Average Annualized Rate is the most appropriate rate to apply to underpaid estimated benefits.

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.

OREGON ADMINISTRATIVE RULE
PUBLIC EMPLOYEES RETIREMENT BOARD
CHAPTER 459
DIVISION 007 – DIVISION TITLE

MEETING DATE	**11/18/05**
AGENDA ITEM	**C.1.** **Interest Rate**

459-007-0015

[Distribution of Earnings on Underpayment of Estimated Benefits] **Interest Rate Applied to Underpayment of Estimated Benefits**

In accordance with ORS 238.455(5), earnings credited to an underpayment of either Tier One or Tier Two estimated benefits shall be simple interest, prorated from date of underpayment to date of distribution by PERS of the underpaid amount based on**:**

(1) the rate credited to the respective tier in the Fund for the prior calendar year **for members who have effective dates of retirement prior to January 1, 2006;**

(2) the average annualized interest rate, as defined in OAR 459-007-0001(3), in effect as of the date of distribution for members who have effective dates of retirement on and after January 1, 2006.

Stat. Auth.: ORS 238.650
Stats. Implemented: ORS 238.455

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November 18, 2005

MEETING DATE	**11/18/05**
AGENDA ITEM	**C.2.** Strunk/Eugene Policy Issues

TO: Members of the PERS Board

FROM: Steven Patrick Rodeman, Administrator
Policy, Planning, & Legislative Analysis Division

SUBJECT: *Strunk/Eugene* Policy Issues

OVERVIEW

- **Subject:** As staff continues to develop and communicate its plans to reallocate 1999 earnings as required as a result of the *Eugene* case and correct accounts as directed by the Oregon Supreme Court's *Strunk* decision, policy issues are identified and staff is seeking the Board's guidance to resolve those issues.
- **Action:** Provide policy direction to PERS staff on the issues identified below.
- **Policy issues addressed in this memo:**
  - Can the PERS Board allow members to change their benefit option election?
  - Should members be allowed to purchase service credit, normally made at the time of retirement, in light of the adjusted accounts, benefits, and possible method changes?
  - Should the actuarial reduction end when a member has fully repaid the overpayment from the 1999 earnings allocation (calculated as of the benefit adjustment date)?
  - Should PERS accept repayment of the overpayment in some manner other than a lump sum or actuarial reduction (e.g. equal payments over 5 years)?
  - Should PERS help individual members with possible tax issues associated with the overpayment and potential tax consequences and penalties associated with repayments?

ANALYSIS OF POLICY ISSUES

PERS staff has conducted sufficient research on the following policy issues to present staff recommendations in these areas. Additional policy issues that are being researched are listed at the end of this memo. Based on how the PERS Board directs staff to proceed, these issues and their resolution will be incorporated into the *Strunk/Eugene* Frequently Asked Questions (FAQ) document that the agency will post and maintain on its web site.

- ***Can the PERS Board allow members to change their benefit option election?***

Members have inquired if they can change their benefit option election originally made at retirement since the amount of their benefit is changing. The PERS Chapter 238 Program allows retired members to select among several payment options, generally differentiating on survivorship features. Note that all the options are actuarially equivalent; in other words, the benefit payment under any option is calculated using actuarial factors that make the total value to be distributed consistent across all options.

The statute that allows a member to convert to an optional form of benefit payment (ORS 238.305) specifically limits that election to within 60 days after the member receives their first benefit payment. No statute provides the Board with the specific authority to waive or extend that election period. Since the statute provides for a specific period and no authority is granted to alter that period, staff's conclusion is that the PERS Board does not have the authority to allow members to change their election beyond the 60-day period. Keith Kutler at the Department of Justice concurred with this conclusion.

From a policy perspective, the optional forms of benefit payment are all actuarially equivalent so the member is receiving the same value regardless of the election. The election should therefore be based on a member's particular need to provide a survivorship benefit and the nature of that situation, which does not change as a result of the *Strunk/Eugene* adjustments.

Note that many of the affected retired members are receiving estimated benefit payments; they have not received their "first benefit payment" until PERS generates a Notice of Entitlement and converts them from an estimated to a final payment amount. In those circumstances, those retired members will have an opportunity to change their option election if they so choose.

STAFF RECOMMENDATION: Staff concludes that the PERS Board does not have the authority to allow members to change their benefit payment option election beyond the 60-day period provided in statute.

- ***Should members be allowed to purchase service credit, normally made at the time of retirement, in light of the adjusted accounts, benefits, and possible method changes?***

Members with qualifying service time may purchase credit for that time at retirement. The PERS Chapter 238 Program allows purchases for waiting, out of state teaching, or military service time. Such purchases are usually made to qualify for retirement (e.g., accumulate 30 years of creditable service) or increase benefits (e.g., a formula calculation based on creditable service).

Similarly to the policy issue above about benefit option elections, these purchases must be made around the time the member retires (generally, within 90 days of the member's effective retirement date). These time frames are specified in statute and the PERS Board has no authority to waive or extend them. Staff concludes, therefore, that members cannot be allowed to reconsider their purchase transactions that were or could have been made.

STAFF RECOMMENDATION: Staff concludes that the PERS Board does not have the authority to allow members to make purchases or change those made at retirement beyond the period provided in statute for making or changing that purchase.

- ***Should the actuarial reduction end when a member has fully repaid the overpayment from the 1999 earnings allocation (calculated as of the benefit adjustment date)?***

The Actuarial Reduction Method provided for in ORS 238.715(1)(b) reduces the member's payment by an amount actuarially determined to be adequate to recover the overpayment during the entire period the monthly payments are made to the recipient. The actuary's determination is based on average mortality. The reduction is therefore predicated on the member living the estimated life span; no longer and no shorter.

This same method is used to calculate a retired member's monthly benefit; although the benefit is payable for life, the actuary has to make some estimate of how long that payment will last. While no single member may exactly fit this estimate, the plan's entire population does on an aggregate, average basis. Those that live longer receive more total benefits than the actuary calculated; those that die sooner receive less.

This same theory applies to the Actuarial Reduction Method, meaning that the adjustment must continue until the benefit payment stream stops. Otherwise, PERS would have to track each repayment individually and collect from those who die sooner than expected while stopping the adjustment for those who live beyond expectations. If the same logic were applied to normal retirement payments, we would refund amounts that were not paid to members that died sooner and stop payments to those who live longer. Members who live beyond expectations are receiving "more" benefits than the actuary calculated they would have gotten; similarly, out of these "excess" benefits, their overpayment amount will continue to be recovered but, overall, the system should be in balance.

STAFF RECOMMENDATION: The actuarial reduction continue for as long as the affected member's benefit payment stream continues.

- ***Should PERS accept repayment of the overpayment in some manner other than a lump sum or actuarial reduction (e.g. equal payments over 5 years)?***

The volume of transactions involved in this effort is staggering: over 50,000 recipients. Each person may have particular circumstances or preferences that they want to negotiate with the agency. Simply put, PERS does not have the information system capability, the staffing, or the accounts receivable infrastructure to support setting up and tracking payment arrangements on this scale. Members that want to repay their overpayment in a lump sum, but under payment arrangements, can access various sources of outside credit to structure the repayment over time. Alternatively, the actuarial reduction option is a form of installment repayment if outside credit arrangements are not acceptable to the member.

STAFF RECOMMENDATION: That PERS not offer customized repayment plans to individual members but continue to offer two alternatives: repayment in a lump sum or actuarial reduction to future payments.

- ***Should PERS help individual members with possible tax issues associated with the overpayment and potential tax consequences and penalties associated with repayments?***

While the agency is not qualified to give individual tax advice, we can provide some information about how the benefit payments have been and will be reported to the state and federal government for taxation purposes. Under Revenue Ruling 2002-84, the effect of actuarially reducing future benefits is that PERS will report what the agency actually pays the recipient under this method, not what the recipient would have received absent the adjustment. For benefit payments after the adjustment date, therefore, PERS will report the taxable portion of the benefit the recipient actually receives so there should be no offset or deduction from what the recipient would have otherwise received but for the recovery. Similarly, for payments received prior to the adjustment, those are the amounts that the recipient actually received and should conform to the amounts reported as taxable.

If the recipient instead repaid PERS in a lump sum, PERS would report the recipient's future benefit amounts, again resulting in no special tracking or reporting requirements. Whether the recipient would receive a deduction or credit towards their current year tax return for the amount of the lump sum repayment depends on the recipient's individual tax situation and the amount of the repayment. Concerns that enter into consideration include whether the recipient itemizes their deductions; whether the repayment can be classified as a casualty loss under Internal Revenue Code §165(a)(1) (generally, a miscellaneous deduction of losses under $3000 subject to the two percent floor); or if the repayment qualifies for an immediate deduction or credit (generally, repayment of over $3000). IRS Publication 525, *Taxable and Nontaxable Income*, explains how the deduction or credit works when the repayment amount is greater than $3,000.

All these variables demonstrate how the tax implications of this transaction depend not only on the repayment option the recipient selects but also on their individual tax situation. For answers to those questions and to develop a specialized tax strategy, recipients need to consult their tax professional.

STAFF RECOMMENDATION: That PERS not offer individual tax advice but continue to direct affected members to consult their respective tax professionals.

POLICY ISSUES NOT ADDRESSED IN THIS MEMO

PERS staff is still researching the possible implications and alternatives to the following policy issues that have been identified. We anticipate having a staff recommendation on these matters at the PERS Board's December meeting.

- If the recalculation of a member's benefit results in a higher benefit under another method than originally used (Full Formula, Formula Plus Annuity and Money Match), should PERS recalculate the benefit and overpayment based on that method?
- Should PERS provide a way for members who rolled their PERS payment into a tax-qualified investment to roll the overpayment back to PERS, thus avoiding the consequences of a taxable disbursement or withdrawal?
- Should PERS review one-time variable transfer applications that were originally denied, now that the change in crediting for 1999 may result in those members being eligible for that transfer?
  - Should PERS only process the transfer if it benefits the member, or give them an opportunity to withdraw the request if the transfer harms them?

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November 18, 2005

MEETING DATE	11/18/05
AGENDA ITEM	C.3. Strunk / Eugene

TO: Members of the PERS Board

FROM: Craig M. Stroud, Administrator
Benefit Payments Division

SUBJECT: *Strunk* and *Eugene* Project Business Plan Update

At the November 18th, 2005 Board meeting, I am presenting the attached *Strunk* and *Eugene* Project Business Plan Update. The plan continues to be a work in progress. This version includes:

- Updates to the overall project timeline
- The 2004 member statement timeline
- A discussion as to how we plan to stage and address the "payment recipients" (those members that require a benefit adjustment).
- A variety of other minor revisions.

For ease of tracking revisions, we have added a bar to the left edge of each page to indicate where updates have been made since the previous version of the plan.

Strunk and ***Eugene*** Project Business Plan

Please note: The bar found on the left side of any page indicates updates made to this document since the version presented at the October Board meeting.

Table of Contents

Strunk & Eugene

Project Overview

The 2003 PERS Reform legislation and the Oregon Supreme Court decisions in the *Strunk* and *City of Eugene* cases have defined the parameters within which PERS can implement the Settlement Agreement. PERS is now required to implement the remainder of its obligations under that agreement and administer the law as it stands today. The project's goal is to implement these obligations.

The Court ruled that the Settlement Agreement and 2003 PERS Reform legislation have resolved the issues in the *Eugene* case. The Settlement Agreement requires PERS to reallocate 1999 earnings to Tier One member regular accounts at 11.33% instead of 20%. Other tenets of the Settlement Agreement have been met. PERS will also credit the assumed rate-- currently 8% -- to Tier One accounts for 2003 and 2004 as a result of the Oregon Supreme Court decision in the *Strunk* case. In addition, the Court held in *Strunk* that the Cost-of-Living Allowance (COLA) 'freeze' imposed by the 2003 PERS Reform Legislation was invalid. All members who retired between April 2000 and April 2004 that had their COLA 'frozen' are entitled to have those withheld amounts credited to them.

For those Tier One members who retired, withdrew, or received benefit payments after the 1999 earnings crediting was effective (April 1, 2000), PERS will:

- Pursue collection of overpaid amounts. This will correct past benefit overpayments and prevent future overpayments by adjusting benefits going forward.
- Use a recovery process that minimizes the effect on current monthly benefits and provides the longest possible repayment period.
    - Monthly benefit payments will be adjusted prospectively for the 1999 earnings allocation of 11.33%, and PERS will recover any overpayments that occurred up to the adjustment date. Comparing what should have been paid to a recipient against what was actually paid completes the adjustment. For those recipients who still owe a balance to the PERS Fund, PERS will calculate, based on each member's projected longevity and retirement option, the amount the benefit needs to be reduced to repay the balance over the remaining lifetime stream of payments. Benefit payments may be reduced in the short term, but would increase at the next, and subsequent, COLA dates.
    - Instead of this option, a recipient can opt to pay the entire amount owed in a lump-sum payment. The recipient's monthly payments will then only be adjusted going forward based on the 11.33% earnings reallocation for 1999 (and subsequent COLA adjustments).
    - For recipients who are no longer receiving PERS benefit payments (members, beneficiaries, or alternate payees who retired, withdrew, or received a death benefit), staff will calculate the lump-sum amount of their overpayment and pursue normal collection efforts and repayment plans to recover that amount.

- Waive collection of any overpayment that is less than $50 on an aggregate basis, as allowed by statute.
- Not charge interest or costs on the recovery of overpaid amounts.

Tier Two members could be minimally impacted if the Board re-credits different amounts to reserves as a result of the 1999 earnings re-crediting.

Core Principles

Core Principles

The following principles guide the planning and execution of this project:

- The negative adjustment on the retiree's current benefit payment is as small as possible.
- The account processing priority and order is transparent and communicated to stakeholders for input.
- Communications are complete, understandable, concise, and we proactively answer potential questions.
- The project is completed in the most efficient method that does not put undue burden on other business operations.
- The impact to the Rims Conversion Project (RCP) is planned and managed for success.
- Members of the core *Strunk* and *Eugene* team are dedicated 100% to the project.
- One touch per account. This means we attempt to push the account through the process in the most efficient means possible and present a final transaction to the impacted benefit recipient.

Success Criteria

The project is successful if:

- Recipients incur no disruption in the receipt of monthly PERS benefits.
- The identified population of accounts requiring adjustment includes all impacted accounts.
- All account balance and benefit payment adjustments are complete, accurate, and fully auditable so we can accurately report on the process and results. This means all underlying data issues must be resolved.
- The invoicing and accounts receivable processes optimize collections.
- 2004 member statements can be created from Phase I of this project.
- No data is corrupted or lost as a result of our processing.
- Completed within the approved budget.
- Completed within the approved timeline.

Planning Team

Description

The planning effort for a project of this size represents a significant project unto itself. The purpose of the planning is to ensure that: all activities needed to make the project successful have been defined; the correct project team is defined, built, housed, and trained; any setup work is planned and started; and the necessary contracts are constructed and executed.

To ensure the project's success, PERS would like to assemble a dedicated team to define and conduct a series of planning activities. The team would make use of some of the original *Strunk* allocated resources. However, due to the additional work represented by the *Eugene* decision, the management control structure of the project team needs to expand. The planning team needed for this phase consists of:

1 Primary Business Manager
2 Supporting Business Managers
1 Information Services Division Project Manager
1 Business Project Manager
1 Operations and Policy Analyst 2
1 Quality Assurance Position

Activities

The planning team is responsible for validating the types of impacted accounts. For each defined type, the team must:

- Determine the best order and time frame in which to process the adjustments.
- Identify and document the processes and procedures required to perform the adjustments.
- Validate the initial time estimates of the amount of work needed to complete the adjustments.
- Determine the tool set necessary to calculate the adjustments.
- Based on the defined process, tool set, and time estimates determine the resources, both internal and external, needed to complete the work.
- It is likely the amount of work to complete the adjustments is greater than current staff can accommodate. If so, the planning team must propose a solution to complete the work. To maximize project success, some account types may be outsourced.
- Determine if any pre-work can be started and if so when and by whom.

Project Timeline

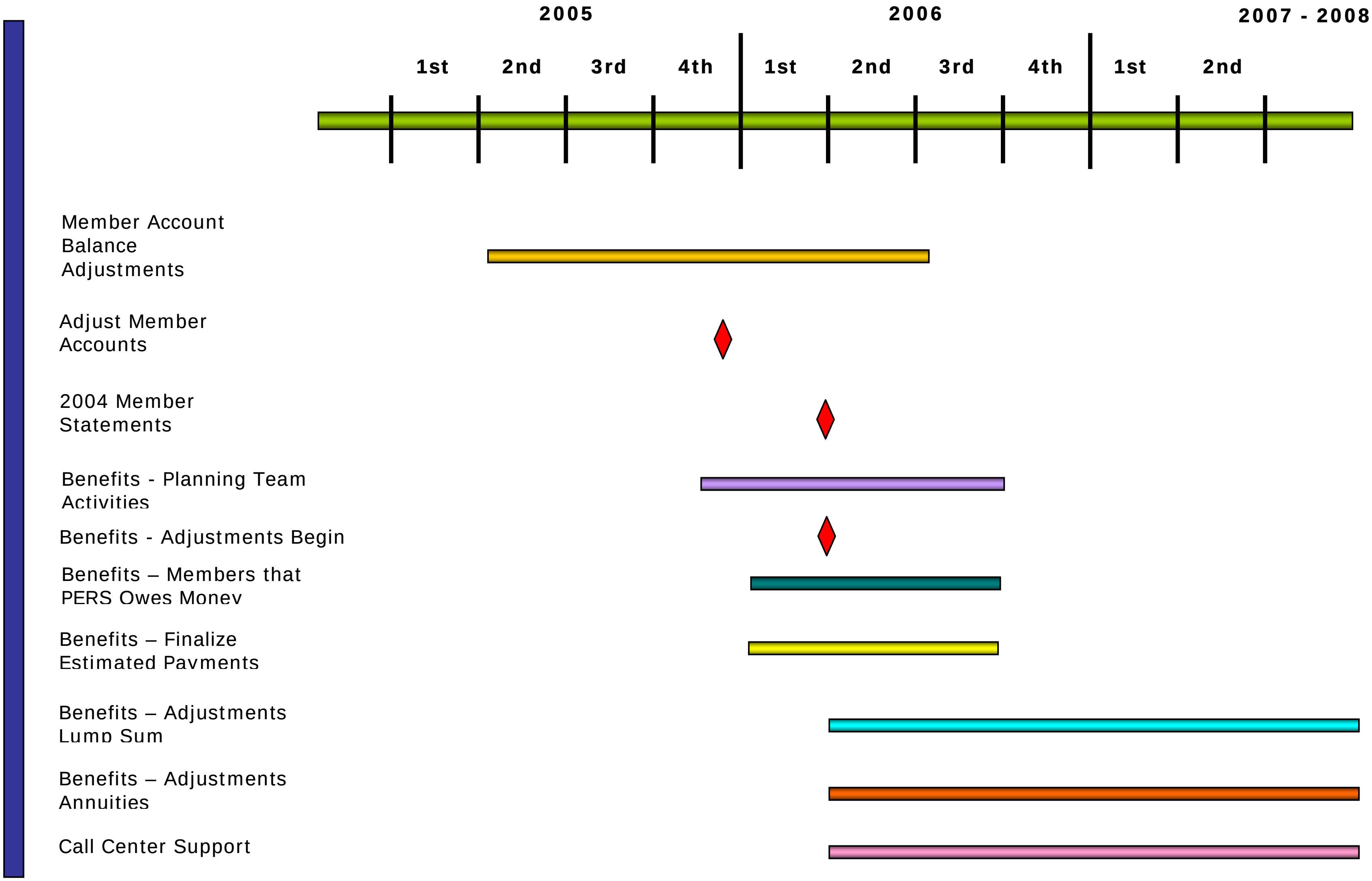
Major Milestones

The following chart shows the high-level milestones for this project. Please note - we continue to estimate the project work, therefore, the project end date is yet to be determined.

See the detailed timeline on the following page.

Strunk **and** ***Eugene*** **Project**

Project Timeline



Major Components

Complexity Factor

One of the overriding reasons this project is more complex than other RIMS related projects at PERS is that it adjusts historical member's account information rather than just system screens or reports. In so doing, PERS must create programs to back out (or void) transactions to member accounts, determine historical adjustments to each account (i.e., recreate the account as of the appropriate date in time, recalculate and apply credits accurately), and ensure that audit trails and logging files are created appropriately. In addition, since retired member benefits will change, PERS needs to develop ways to recalculate the benefits, notify members, and either collect or pay over/under payments:

Our analyses to date identified the following issues that need to be addressed:

- The *Strunk* decision impacts every PERS Tier One member that received 2003 interest earnings. This includes 105,000 members and 4,300 retirees.
- The *Eugene* decision impacts every PERS Tier One member that received 1999 interest earnings. This includes 100,000 members and 35,000 retirees.
- The decision to postpone 2004 earnings crediting impacted 180,000 members. As a result, Tier One and Tier Two Member Statements for 2004 are on hold.
- 21,563 Retired Members that are not receiving annual COLA increases are subject to COLA reinstatements and *Strunk/Eugene* adjustments. These adjustments must be communicated to the retiree and invoiced or paid.
- Every impacted recipient will have 12 to 30 financial adjustment transactions applied their account.
- Up to 60% of the original retirements were processed with manual interventions as they moved through the computer systems.
- No automated processes currently exist to make the above-mentioned adjustments. These processes must be defined, built, tested and implemented.
- Each of the following categories requires specialized processing rules. Many accounts are impacted by several of these categories and will require a combination of solutions:
    - Active/Dormant Member Accounts
    - Service Retirements
    - Disability Retirements
    - Police and Fire Units Retirements
    - Loss of Membership Accounts
    - Refunded Accounts

- o Deaths
- o Divorces
- o Lump Sum Settlements and Installments
- o Full Cost Purchases
- o AEF Estimated Payments
- o Police and Fire Units Purchases
- o One Time Variable Transfers
- o Re-Employed Accounts
- o COLA Frozen Benefits

Membership Adjustments (Active / Dormant / 2004 Statements)

- ♦ Description

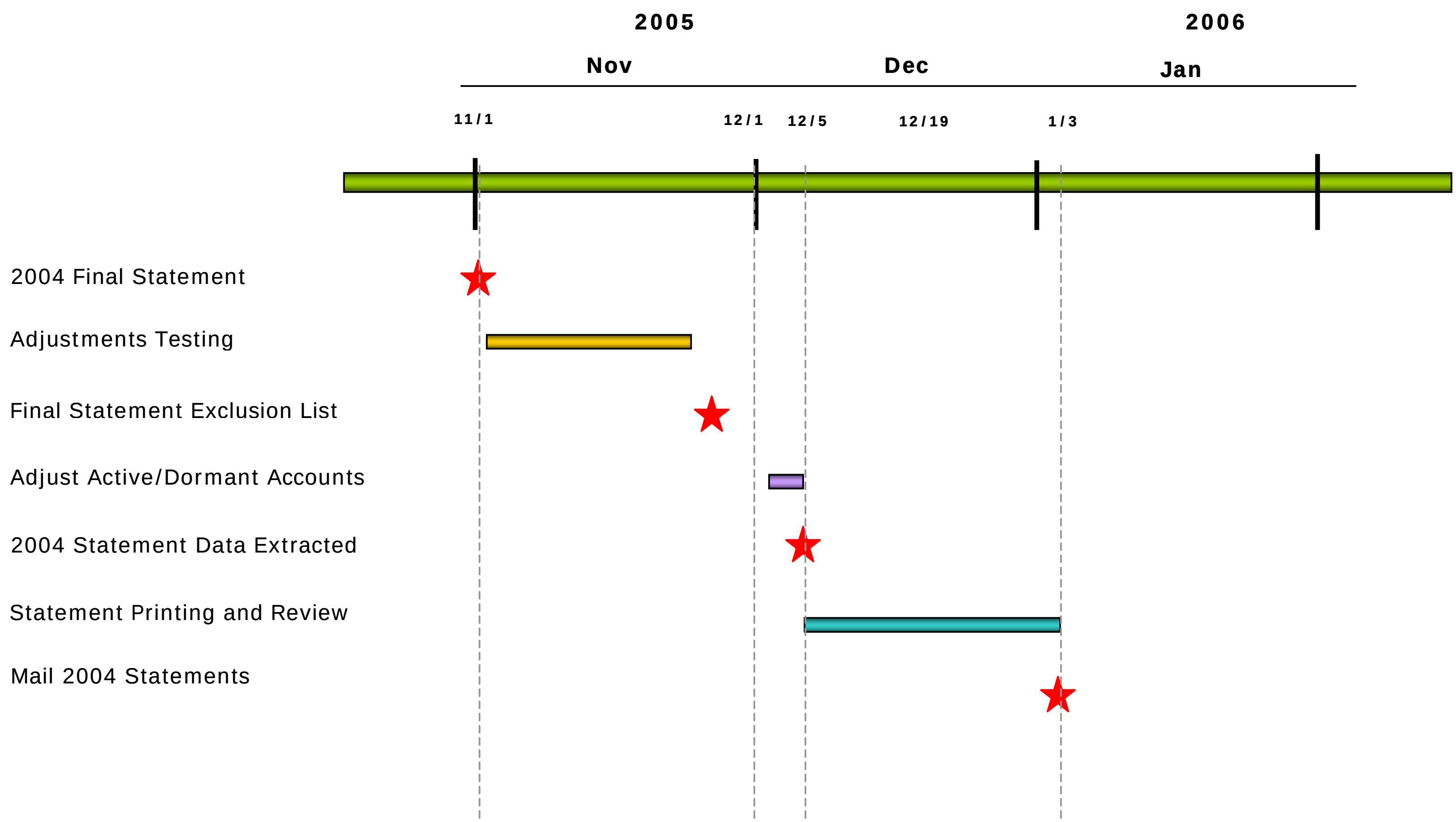
  This first phase of this project addresses the requirement to adjust all impacted Tier -One and Tier-Two member accounts. This phase has two goals: adjust the accounts so 2004 member statements can be created and, in the case where a member retires, stop unadjusted accounts from moving to the benefit calculation process. This action reduces the number of accounts that must be reviewed to ensure that the benefit amount previously calculated is correct.

- ♦ Timeline

  This phase started in the second quarter of 2005 and ends in the first quarter of 2006 when the last of the more difficult accounts has been adjusted.

  See the detailed timeline on the following page.

2004 Member Statements Timeline



- Dependencies

  Receive the 2004 final earnings crediting rates from the Board.
    - Complete - this issue was resolved at the October Board meeting.

  Resolve all testing issues in a timely fashion to produce 2004 statements.
    - To date we have not uncovered any major issues.

  Member and associated alternate payee accounts must be re-divided prior to completing account adjustments and producing applicable 2004 statements.
    - To credit *Strunk* and *Eugene* account earnings to these accounts, a manual effort must be completed to re-divide the account in accordance with the divorce decree on file with PERS. This effort cannot be completed in time for these accounts to be included on the 2004 member statements. We are studying alternatives for dealing with these accounts. There are 2,076 alternate payees and 2,266 members impacted by this decision.

Payment Recipients

This phase of this project addresses the requirement to adjust recipient's benefits. The phase has two goals: adjust the benefits according to the court cases and settlement agreement and complete this process in a manner that minimizes the impact to the recipient. The work in this phase has been divided into two categories: those recipients receiving monthly annuity payments and those recipients that received a lump sum payment.

The planning for this effort is underway. This effort involves:

1. Identify all impacted accounts. This list includes all accounts that must be reviewed because they required adjustment due to the *Strunk* and *Eugene* decisions. Please see the ***Impacted Accounts*** section in the Appendix for a detail breakdown of these accounts.
2. Classify the similar impacted accounts into workflow categories.
3. Define the workflows, including the steps in the processes, the tools needed to adjust the benefits, and the time required to complete each step.
4. Determine the staff required to adjust the accounts in each workflow.
5. Map the workflows and staff to a timeline to estimate the completion date and total costs of the project.

Our current plan is to generally stage the account adjustments on the project timeline in the following order:

1. Members that PERS owes money.
2. Members that are receiving estimated payments.
3. Members receiving annuity payments who also owe PERS money.
4. Members that received a lump sum payment and owe PERS money.

Annuity Accounts

- Description

  This category includes all recipients receiving a monthly annuity payment at the adjustment date.

- Impacted Accounts

  See high-level account breakdown table in Appendix.

- Timeline

  The timeline for this effort depends on the final estimates from the breakdown of the impacted accounts shown above and the availability of staff to perform the work. Further analysis needs to be performed on this information before a final timeline can be developed.

- Dependencies

  Create a plan to determine how to best complete the work.
  - This effort is underway and is to be presented at the January Board meeting.

  Identify and procure the resources necessary to perform the work.
  - This effort is underway and is to be presented at the January Board meeting.

  Receive the actuarial values to complete the Actuarial Reduction Method (ARM) calculations.
  - Request has been made to Mercer.

  Complete the tools necessary to complete the work.
  - This effort is underway. The completion date has not been determined. This is part of the planning team's responsibilities.

  Define the needed processes and procedures to complete the work.
  - This effort is underway. The completion date has not been determined. This is part of the planning team's responsibilities.

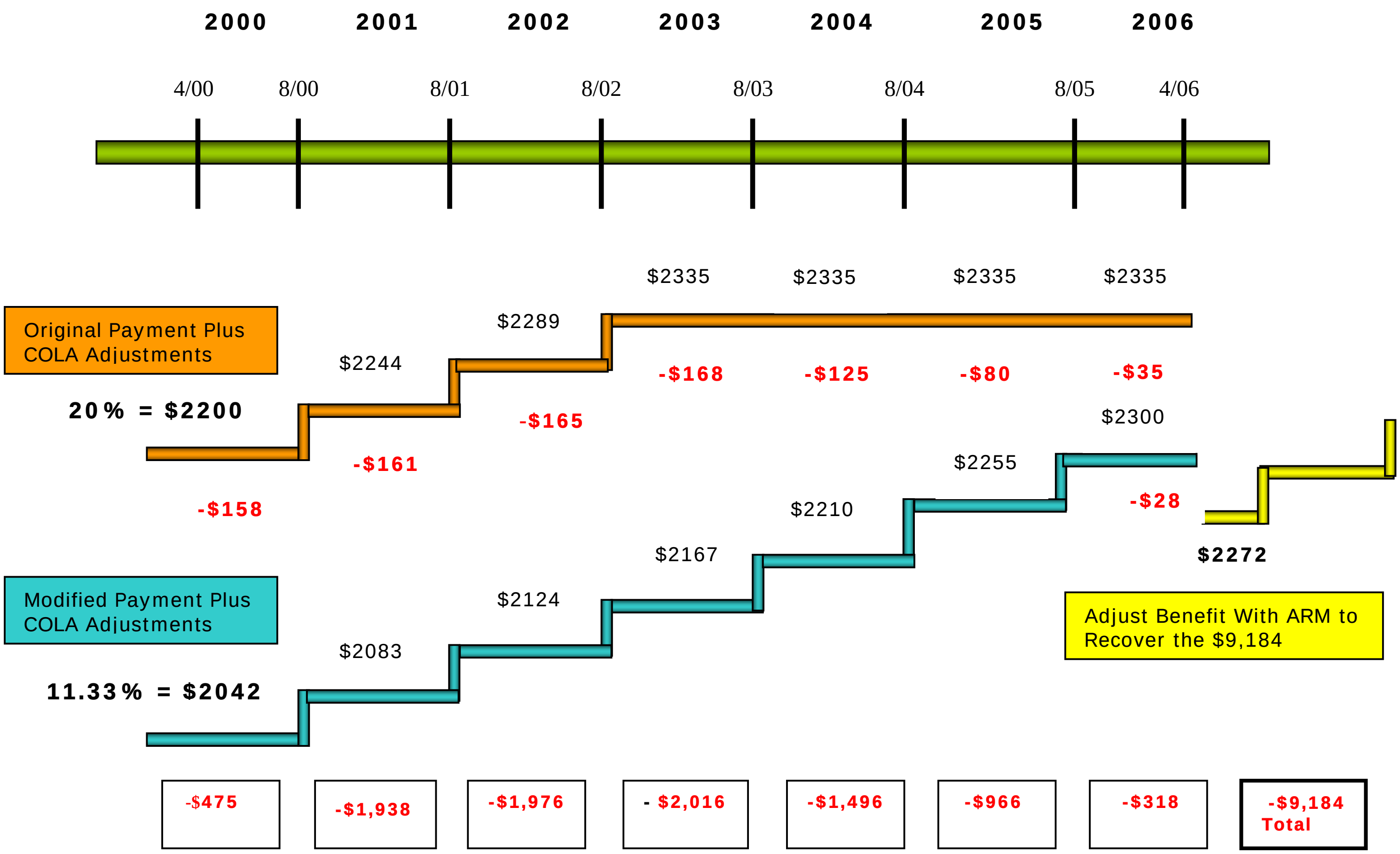
  Implement an invoicing and accounts receivable solution.
  - This effort is underway and is to be presented at the January Board meeting.

  Resolve the policy decisions associated with account adjustments.
  - This effort is underway and is to be presented at the November, December, and January Board meetings.

- Actuarial Reduction Method (ARM) Example

Example 1: The following example shows the effects of reducing the 1999 earnings rate from 20% to 11.33% and reapplying the Cost-of Living Allowance for 2003, 2004, and 2005. This example shows that the recipient's monthly payment is reduced by $35 plus the actuarial adjustment of $28 that is necessary to recover the $9,184 they owe the PERS Fund as of the adjustment date (April 1, 2006).

Strunk and Eugene Recalculation Example
Retirement Date of April 2000 and Member Had No Variable
The Benefit Adjustment Date is April 2006

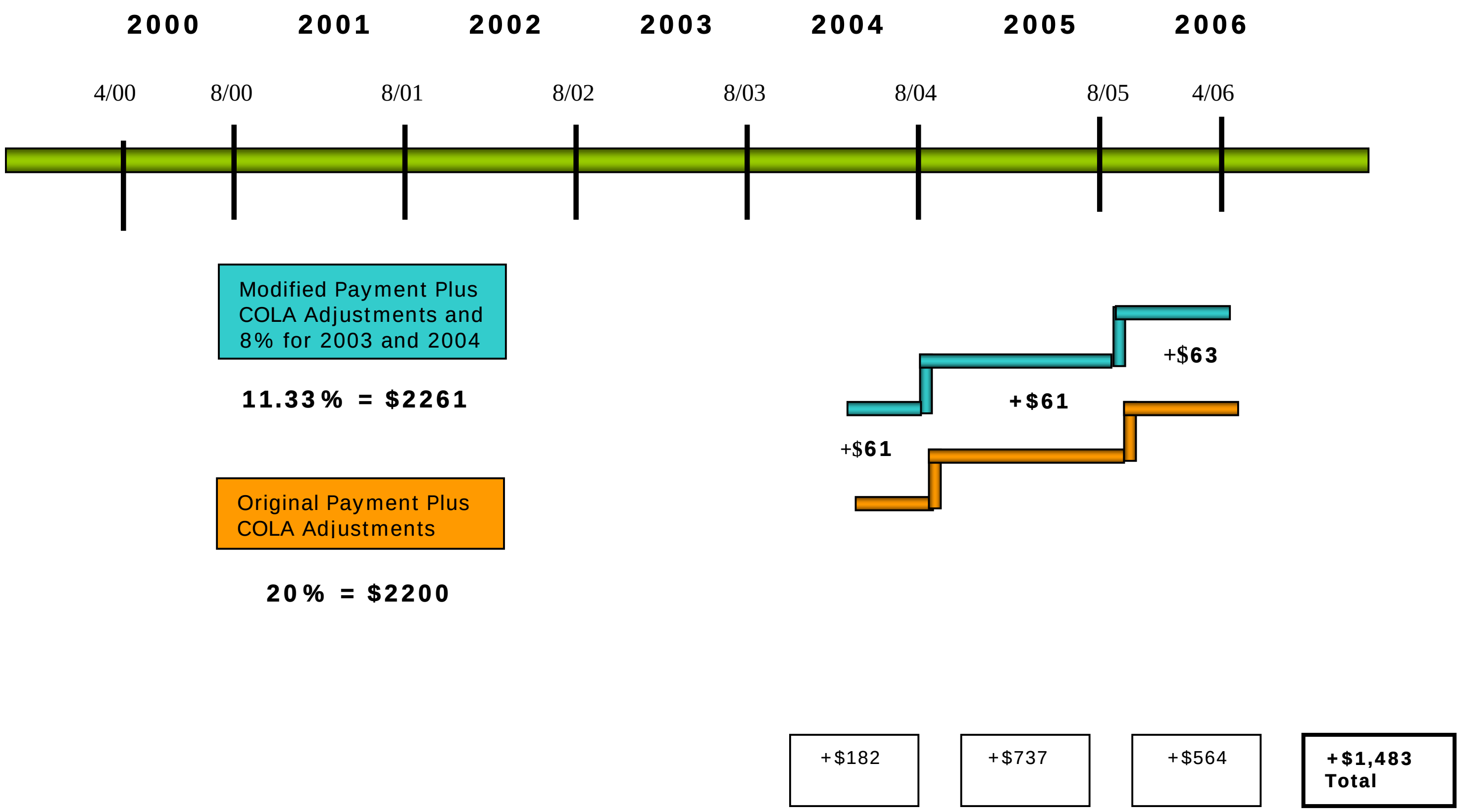


NET RESULT: The member's monthly benefit is reduced by $35. The PERS Fund must also collect the $9,184. We do this using an Actuarial Reduction Method. This adjustment results in an additional reduction of $28 a month for a total reduction of $63 a month as of the adjustment date.

The **negative** numbers represent the amount the member owes the PERS Fund for each year. The box on the bottom right is the sum total of all money owed as of the adjustment date.

Example 2: The following example shows the effects of reducing the 1999 earnings rate from 20% to 11.33%. The recipient's account balance was recalculated using the new rate and accruing 8% earnings for 2003 and 2004. This example shows that the recipient's monthly payment is increased by $63 plus PERS owes them $1,483 as of the adjustment date (April 1, 2006).

Strunk and Eugene Recalculation Example
Retirement Date of April 2004 and Member Had No Variable
The Benefit Adjustment Date is April 2006



NET RESULT: The member's monthly benefit is increased by $63 and the PERS fund must pay them an additional $1,483 as of the adjustment date.

The positive numbers represent the amount PERS owes the member for each year. The box on the bottom right is the sum total of all money owed as of the adjustment date.

Lump Sum Accounts

- Description

  This category includes all recipients that received a lump sum payment.

- Impacted Accounts

  See high-level account breakdown table in Appendix

- Timeline

  The timeline for this effort is dependent on the final estimates from the breakdown of the impacted accounts shown in the appendix and the availability of staff to perform the work. Further analysis needs to be performed on this information before a final timeline can be developed.

- Dependencies

  Build a plan to determine how to best complete the work.
  - This effort is underway and is to be presented at the January Board meeting.

  Identify and procure the resources necessary to perform the work.
  - This effort is underway and is to be presented at the January Board meeting.

  Complete the tools necessary to complete the work.
  - This effort is underway. The completion date has not been determined. This is part of the planning team's responsibilities.

  Define the needed processes and procedures to complete the work.
  - This effort is underway. The completion date has not been determined. This is part of the planning team's responsibilities.

  Implement an accounts receivable solution.
  - This effort is underway and is to be presented at the January Board meeting.

  Resolving the policy decisions associated with account adjustments.
  - This effort is underway and is to be presented at the November, December, and January Board meetings.

Appendix

Key Risks

This section describes the key risks to the project

1. **Risk:**

   Data Issues – We may uncover more data-related issues in system testing than we had originally thought.

   Consequence:

   If this occurs we may not be able to complete the member account balance adjustments in time to run the 2004 statements this year.

   Contingency Plan:

   We are doing our best to uncover as many issues as early in the process as possible. However, our only strategy is to either omit some accounts from our 2004 statement processing or delay the statements.

2. **Risk:**

   Rims Conversion Project Release – We are currently scheduled to complete our user acceptance testing to adjust member accounts one week before the last release of HB 2020 programming and the first release of RCP programming.

   Consequence:

   The two projects may conflict with each other during the testing phase. The release of two large projects into production simultaneously greatly increases the risk. It may be difficult to determine which project caused the underlying issues and, therefore, resolution may be difficult.

   Contingency Plan:

   Consider the possibility of moving the member account balance adjustments and 2004 annual statement production/distribution to early next year.

   We have rescheduled our implementation date to eliminate this risk. Please see the Member Statement timeline in the ***Membership Adjustments (Active / Dormant / 2004 Statements)*** section of this document.

3. **Risk:**

   Rims Conversion Project (RCP) – The *Strunk* and *Eugene* project is not be completed by the end of Stage 2 of RCP when all the job segments and related data are moved to jClarety.

Consequence:

The benefit recalculations can no longer be done in the RIMS system. This would end our *Strunk* and *Eugene* project as currently planned.

Contingency Plan:

We have three possible options:

- Extend the project and adjust the RCP schedule accordingly,
- Migrate the functionality to jClarety and continue the project in jClarety or
- Back bridge (send) job segments to RIMS from jClarety.

Meetings are currently underway to determine the impact and define a solution.

4. Risk:

Staff – The project plan and organization chart call for a team of 50+ people. It is very unlikely the agency can hire, train, and house a staff of this size.

Consequence:

The timeframe for the project must be extended and the functionality must be added to jClarety so the work can be completed there.

Contingency Plan:

We have three possible options:

- Extend the project and adjust the RCP schedule accordingly or
- Migrate the functionality to jClarety and continue the project in jClarety or
- Out source as much of this work as possible

The final plan will be presented at the January Board meeting.

5. Risk:

Contracts – Implementing contracts for consultants and/or out sourcing is a lengthy process with little flexibility.

Consequence:

The project timeline may have to be extended to account for the delay in this process.

Contingency Plan:

Perform the work using existing resources and attempt to address contracting bottlenecks.

6. Risk:

New Legislative or court actions – Future Legislative actions or court rulings could impact the scope of the project.

Consequence:

Scope and /or schedule change.

Contingency Plan:

Evaluate the impact and realign the plan.

Impacted Accounts

Accounts Impacted by *Strunk*/*Eugene* Re-crediting of Earnings

High-level Breakdown of Accounts

This table is a high level summary of the types of accounts impacted by *Strunk* and *Eugene*.

UNIQUE ACCOUNTS		(44,230)
Member & AP Retirements Post 3/1/00	33,792	
Account Withdrawals (Members & AP's)	4,967	
Final LSI for Retirements prior to 4/1/00	981	
Pre Retirement Death Benefits	1,395	
Non- Retired AP/Member Divisions	2,958	
Re-employed Retiree's	137	
ACCOUNTS THAT MAY OR MAY NOT BE PART OF ABOVE GROUP		(6,387)
Failed One Time Variable Transfers	4,928	
P & F Unit Benefits	1,459	
TOTAL ACCOUNTS		(50,617)

The 50,617 accounts have been further categorized into 74 unique workgroups. Each workgroup is identified by a unique 4-digit code. For each workgroup the code indicates:

- The business type (Retirement, Account Division, etc.). There are 9 such types.
- The relationship to the member (Owner, Beneficiary, etc). There are 6 such types.
- The type of payment (Monthly Annuity, Lump Sum, etc.). There are 10 such types.
- The original payment triggers (Service Retirement, Withdrawal, etc.). There are 9 such types.

Currently, we are in the process of reviewing the list of workgroups to ensure the completeness of the list. We will then define the tools and procedures for each workflow. From the procedures we will derive an accurate person-hour projection by workflow, which is fundamental to creating the staffing plan and final budget request.

05 – 07 Budget

Operations 110 – *Strunk* Implementation

As a result of the *Strunk* opinion, the HB 2003 COLA team request has been reconfigured to meet the staff needs to implement the opinion. The 22 positions originally requested have been increased by three. The positions provided in the budget are:

1	FTE Project Manager 1
2	FTE Program Technician 1
7	FTE Retirement Counselor 2
13	FTE Retirement Counselor 1
2	FTE Office Specialist 2
25	**TOTAL**

Anticipated Additional Staffing Needs

From the original estimates created 6 months ago, the number of additional staff needed to complete the adjustments required by the *Eugene* decision was 70 FTE. Although this estimate has not been verified, we are confident the 25 staff provided in the *Strunk* budget package is not sufficient to meet the workload and time frames of this project. We are working on the revised estimates and plan to have them available at future Board meetings.