

OREGON PUBLIC EMPLOYEES RETIREMENT SYSTEM BOARD MEETING

**Monday
April 3, 2017
1:00 P.M.**

**PERS
11410 SW 68th Parkway
Tigard, OR**

ITEM	PRESENTER
A. Administration	
1. January 27, 2017 Board Meeting Minutes	RODEMAN
2. Director's Report	
a. Forward-Looking Calendar	
b. OPERF Investment Report	SKJERVEM
c. Budget Execution Report	
B. Administrative Rulemaking	
1. Notice of Insolvent Employer Rule	VAUGHN
2. Notice of Restoration of Forfeited Service Credit Rule	
3. Disability Rules Update	
C. Action and Discussion Items	
1. <i>Moro</i> Attorney Fees and Costs	VAUGHN
2. <i>Moro</i> Implementation Project Update	ELLEDGE-RHODES
3. Legislative Update	TAYLOR
4. Preliminary Contingency Reserve Allocation	DUNN
5. 2016 Final Earnings Crediting and Reserving	DUNN, MARBLE

There will be an Audit Committee meeting immediately following the regular Board meeting.

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<http://www.oregon.gov/PERS/>

2017 Meetings: May 26 July 28* September 29 November 17* * Audit Committee

Stephen Buckley Lawrence Furnstahl Krystal Gema John Thomas, Chair Pat West, Vice Chair Steve Rodeman, Executive Director
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OREGON PUBLIC EMPLOYEES RETIREMENT SYSTEM BOARD MEETING MINUTES

January 27, 2017

Board members present:

Chair John Thomas, Stephen Buckley, Lawrence Furnstahl, Krystal Gema, and Vice-chair Pat West were present.

Staff present:

Brandon Armatas, Linda Barnett, Dean Carson, Melanie Chandler, David Crosley, Mary Dunn, Yvette Elledge-Rhodes, Brian Harrington, Debra Hembree, Neil Jones, Kyle Knoll, Amanda Marble, Jordan Masanga, Louise Plata, Steve Rodeman, Jason Stanley, Marjorie Taylor, Stephanie Vaughn, Anne Marie Vu, Joli Whitney, and Yong Yang.

Others present:

Teresa Brennan, Nancy Brewer, Bob Burket, Janice Essenberg, Debra Grabler, Henry Groepper, Jeff Gudman, Greg Hartman, David Lacy, Matt Larrabee, Elizabeth McCann, Ken Olsen, Scott Preppernau, David Short, Del Stevens, James Strong, Debra Tremblay, Trudy Vidal, Linnea Wittekind, and Peter Wong.

Chair John Thomas called the meeting to order at 1:00 P.M.

ADMINISTRATION

A.1. MEETING MINUTES OF NOVEMBER 18, 2016

Board member Furnstahl moved and Board member Krystal Gema seconded approval of the minutes submitted from the November 18, 2016 Board meeting. The motion passed unanimously.

A.2. DIRECTOR'S REPORT

Executive Director Steve Rodeman reviewed the Forward Looking Calendar and highlighted the important items to be considered by the Board in the coming year. Of note, he added that the 2018 meeting schedule may be adjusted to allow for financial results to be reflected by moving to having meetings early in the following month instead of late in the month.

Rodeman reviewed the OIC Investment Report of the Oregon Public Employees Retirement Fund (OPERF) for the period ending December, 2016. He reviewed the different rate setting processes for Treasury and PERS. Furnstahl asked about the difference in the crediting and the benchmarks.

Rodeman presented the Budget Execution Report. He noted the 2017-19 budget presentation has been scheduled for March 13-16, 2017, before the Joint Ways & Means General Government Subcommittee. He provided an overview of the process and noted that the committee is comprised of several new legislators who we are planning to meet with to provide an educational groundwork on the system and an opportunity for questions in advance of the meeting. Thomas noted and praised the agency's continued recognition for achievement of excellence in financial reporting as awarded by the Government Finance Officers Association which PERS has received for the last 25 years as described in the latest Comprehensive Annual Financial Report (CAFR).

Rodeman presented the Annual Report of Executive Director's Financial Transactions. This report was submitted to the PERS Audit Committee in November and is now officially submitted to the PERS Board in compliance with OAM 10.90.00 PO.

Member Account Adjustment Team Manager Brandon Armatas, Central Data Coordinator Matthew Rickard, and Business Solutions Analyst MaryMichelle Sosne presented the Board Scorecard Report on Agency Performance Measures.

Chair Thomas asked why the benefit estimate completion within 30 days score was so far below the target. Various circumstances which result in spikes in benefit estimate requests and items which complicate the benefit estimate themselves were discussed, as well as what could be done to increase the team's output volume. Rodeman shared the difficulty in onboarding staff in this area as there is significant lag time before new staff are trained and ready to perform these functions.

Thomas asked if the benefit estimator was widely used and how accurate the benefit estimator is. Rickard reviewed the differences between the two estimates provided by the two processes. The written estimate is vastly more comprehensive. Vice-chair West noted that improvements in the verification process will eventually yield positive results in some of these areas which are currently underperforming. Board member Buckley clarified the frequency of benefit estimate requests. Armatas said that members may request two free benefit estimates per year, with a fee for additional requests. Furnstahl asked how aware front line staff are of the impacts of their efforts on the performance measures. Sosne reviewed the efforts to create the PERS Outcome Based Management Council and how they intend this council to more fully integrate the importance of the measures into the day-to-day performance of front line staff.

Thomas expressed his appreciation for the scorecard report.

ADMINISTRATIVE RULEMAKING

Stephanie Vaughn, Policy Analysis and Compliance Section Manager, presented.

B.1. NOTICE OF DISABILITY RULES

Vaughn presented notice of rulemaking for Disability Rules, OAR 459-015-0001, -0010, -0020, -0025, -0040, -0050; -076-0001, -0010, -0020, -0025, -0040, and -0050. These rules are being modified to update and add definitions; update specialist requirements; address effect of unemployment benefits on determining disability eligibility; clarify when PERS may request evaluations or exams; add physical capacity to independent evaluations; clarify periodic review standard; and clarify the burden of proof for OPSRP disability. A rulemaking hearing has been scheduled for February 22, 2017, at PERS Headquarters. The public comment period ends March 1, 2017. No Board action was required.

There was one policy question included in the rulemaking package: Should PERS adopt a standard of considering only the last 15 years of employment experience when considering what work for which an applicant is qualified? The Board concurred that this was a reasonable and consistent standard.

B.2. ADOPTION OF IRC LIMITATIONS RULE

Vaughn presented the modifications to the IRC Limitations Rule OAR 459-005-0545; and -080-0500. These revisions incorporate federal adjustments and are necessary to ensure compliance with the IRC's limits on the amount of annual compensation allowed for determining contributions and benefits, annual benefits and annual additions to PERS.

A rulemaking hearing was held December 22, 2016, at PERS headquarters. No members of the public attended. The public comment period ended December 30, 2016. No public comment was received.

West moved to adopt modifications to the IRC Limitations rules as presented. Furnstahl seconded. The motion passed unanimously.

ACTION AND DISCUSSION ITEMS

C.1. MORO IMPLEMENTATION PROJECT UPDATE

Chief Operations Officer Yvette Elledge-Rhodes presented an update on the status of the *Moro* Implementation Project. She noted the steady progress on processing the deceased population. As of today, they are just over halfway complete. Also included in her presentation was an update on the COLA restoration payments which are coming from the Contingency Reserve. Gema asked if there was an estimate for the additional charge. She thought it was about 6,000 benefit recipients out of 7,400 due payments. She will update that information at the next board meeting.

No Board action was required.

C.2. LEGISLATIVE UPDATE

Senior Policy Director Marjorie Taylor presented. She reviewed upcoming legislative committees and groups which have requested presentations from PERS in the near future. She provided a list of bills which she is tracking so far. Also included in her presentation were three policy papers which were developed to help educate stakeholders on important recurring issues: Police and Fire classification, public employment after retirement, and tax remedy payments.

Taylor reviewed the general process for how bills are drafted and assigned to committees.

C.3. PRELIMINARY 2016 EARNINGS AND CREDITING

Assistant Chief Administration Officer Mary Dunn presented preliminary earnings allocations for 2016. In addition, based on a decision at the March 28, 2016 Board meeting to fund the Contingency Reserve at .25% of the system's accrued liability, this fund is currently over-funded by \$345.8 million. She reviewed the options available to the Board to reduce the allocation in this fund. Staff recommends that the Board solicit stakeholder input on a proposed allocation. Input would need to be received by March 15, 2017, to be included in the final earnings crediting materials. The Board agreed that the staff recommendation would be the best method to develop a strategy for addressing the excess funds in the Contingency Reserve. A discussion on how some of the options might work followed. Thomas asked if there was anyone in the audience today who would like to add their ideas to how this should be distributed. Greg Hartman of the PERS Coalition came forward and noted that he will have some comments, but he will provide those in writing in advance for consideration at the next meeting.

West noted when considering redistributing Contingency Reserve dollars it would be important to be mindful of how Death Benefits are funded and may be impacted if money is returned to a different account from which it originated. Furnstahl noted that it would be helpful to have a review of typical orders of magnitude to help inform that decision in the future. Rodeman noted that in an order of magnitude, there are not a significant number of these circumstances.

Gema moved to adopt the preliminary crediting of earnings as presented for calendar year 2016, subject to final adoption at the April 3, 2017 PERS Board meeting. Furnstahl seconded. The motion passed unanimously.

Del Stevens of the Portland Retired Firefighters Association addressed the Board. A discussion regarding equal to or better than responsibilities and the scope of those responsibilities followed. Thomas adjourned the Board meeting at 2:30 PM.

Respectfully submitted,

A handwritten signature in black ink, appearing to read "S. Rodeman", written over a light gray rectangular background.

Steven Patrick Rodeman
Executive Director

PERS Board Meeting Forward-Looking Calendar

Friday, May 26, 2017

Adoption of Insolvent Employer Rule
Adoption of Restoration of Forfeited Service Credit Rule
Adoption of Disability Rules
Board Scorecard Report on Agency Performance Measures
2018 Retiree Health Insurance Plan Renewals and Rates
Overview of Methods and Assumptions for 2016 Valuation

Friday, July 28, 2017

2017 Legislative Session Review
Adoption of 2016 Valuation Methods and Assumptions Including Assumed Return Rate
Audit Committee Meeting

Friday, September 29, 2017

2016 Valuation Results

Friday, November 17, 2017

2016 Valuation Update and Financial Modeling Results
Board Scorecard Report on Agency Performance Measures
Audit Committee Meeting

Returns for periods ending FEB-2017

Oregon Public Employees Retirement Fund

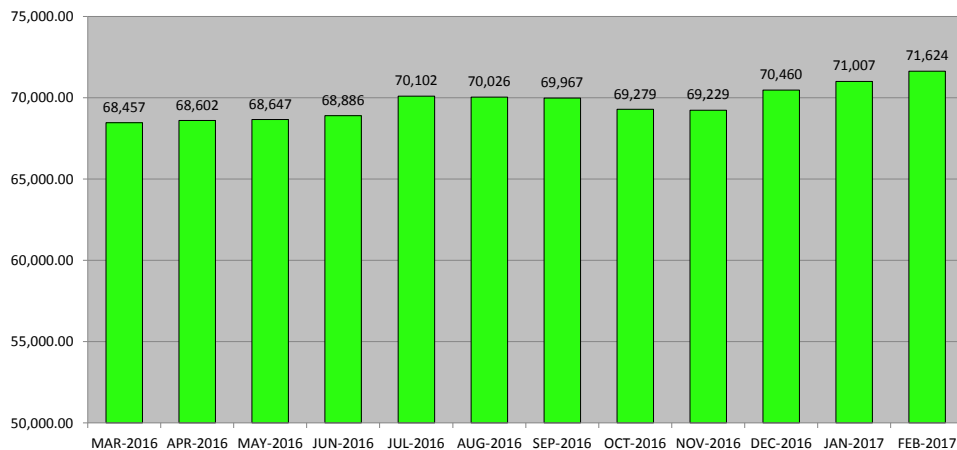
Item A.2.b

OPERF	Regular Account				Historical Performance (Annual Percentage)							
	Policy ¹	Target ¹	\$ Thousands ²	Actual	Year-To-Date ³	1 YEAR	2 YEARS	3 YEARS	4 YEARS	5 YEARS	7 YEARS	10 YEARS
Public Equity	32.5-42.5%	37.5%	\$ 27,649,451	38.9%	5.24	24.11	4.45	5.06	9.03	9.30	9.68	4.66
Private Equity	13.5-21.5%	17.5%	\$ 13,785,572	19.4%	(0.16)	6.08	6.94	9.84	11.40	11.99	12.48	9.60
Total Equity	50.0-60.0%	55.0%	\$ 41,435,023	58.4%								
Opportunity Portfolio	0-3%	0%	\$ 1,462,727	2.1%	(0.33)	4.46	2.48	3.84	6.50	8.39	8.32	6.52
Total Fixed	15-25%	20.0%	\$ 15,386,263	21.7%	1.09	3.87	1.75	2.22	2.18	3.28	4.81	5.22
Real Estate	9.5-15.5%	12.5%	\$ 8,615,059	12.1%	0.85	8.65	8.17	10.14	10.93	11.19	9.98	5.09
Alternative Investments	0-12.5%	12.5%	\$ 4,092,955	5.8%	0.31	6.12	0.47	1.97	3.22	2.42		
Cash w/Overlay	0-3%	0%	\$ 6,520	0.0%	0.26	1.27	0.89	0.77	0.75	0.82	0.78	1.38
TOTAL OPERF Regular Account		100.0%	\$ 70,998,547	100.0%	2.33	12.49	4.60	5.87	7.92	8.52	9.05	5.62
OPERF Policy Benchmark					2.49	14.69	5.53	6.88	8.58	9.39	9.40	6.13
Value Added					(0.15)	(2.20)	(0.93)	(1.01)	(0.66)	(0.87)	(0.35)	(0.51)
TOTAL OPERF Variable Account			\$ 625,733		5.57	22.92	4.15	5.16	8.50	8.81	9.21	3.74

Asset Class Benchmarks:

Russell 3000	5.67	26.29	7.88	9.92	13.91	13.85	13.87	7.64
OREGON MSCI ACWI EX US IMI NET	5.38	19.33	(0.10)	0.08	3.15	3.86	4.76	1.79
MSCI ACWI IMI NET	5.54	22.65	3.73	4.78	8.17	8.43	8.84	4.32
RUSSELL 3000+300 BPS QTR LAG	0.00	18.37	10.15	13.73	16.49	19.80	16.55	10.99
OREGON CUSTOM FI BENCHMARK	0.92	2.60	1.29	1.81	1.66	2.58	3.63	4.29
OREGON CUSTOM REAL ESTATE BENCHMARK	0.00	9.62	11.53	11.44	11.33	11.26	11.15	7.26
CPI +4%	1.56	6.84	5.94	5.28	5.25	5.41	5.70	5.85
91 Day Treasury Bill	0.09	0.39	0.23	0.16	0.14	0.14	0.13	0.73

Total OPERF NAV
(includes Variable Fund asset)
One year ending FEB-2017
(\$ in Millions)



¹OIC Policy revised June 2015.

²Includes impact of cash overlay management.

³For mandates beginning after January 1 (or with lagged performance), YTD numbers are "N/A". Performance is reflected in Total OPERF. YTD is not annualized.

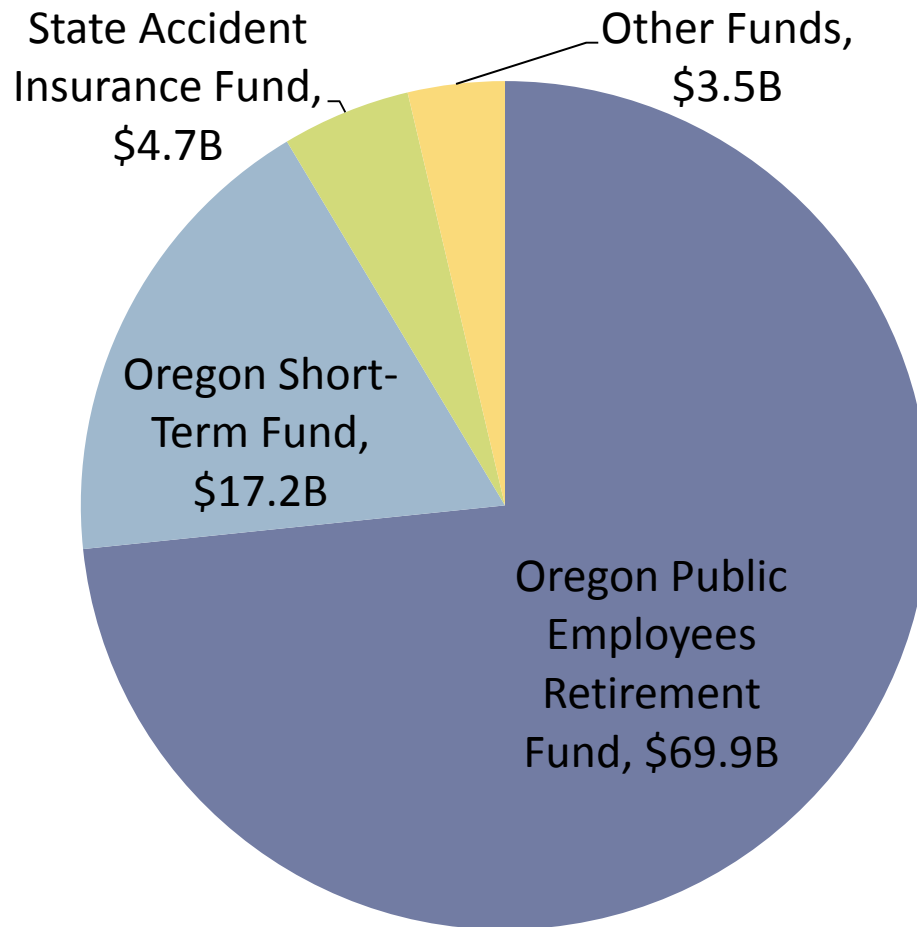


Oregon Investment Program Overview and Best Practice Remarks

John D. Skjervem, CFA
Chief Investment Officer
Oregon State Treasury

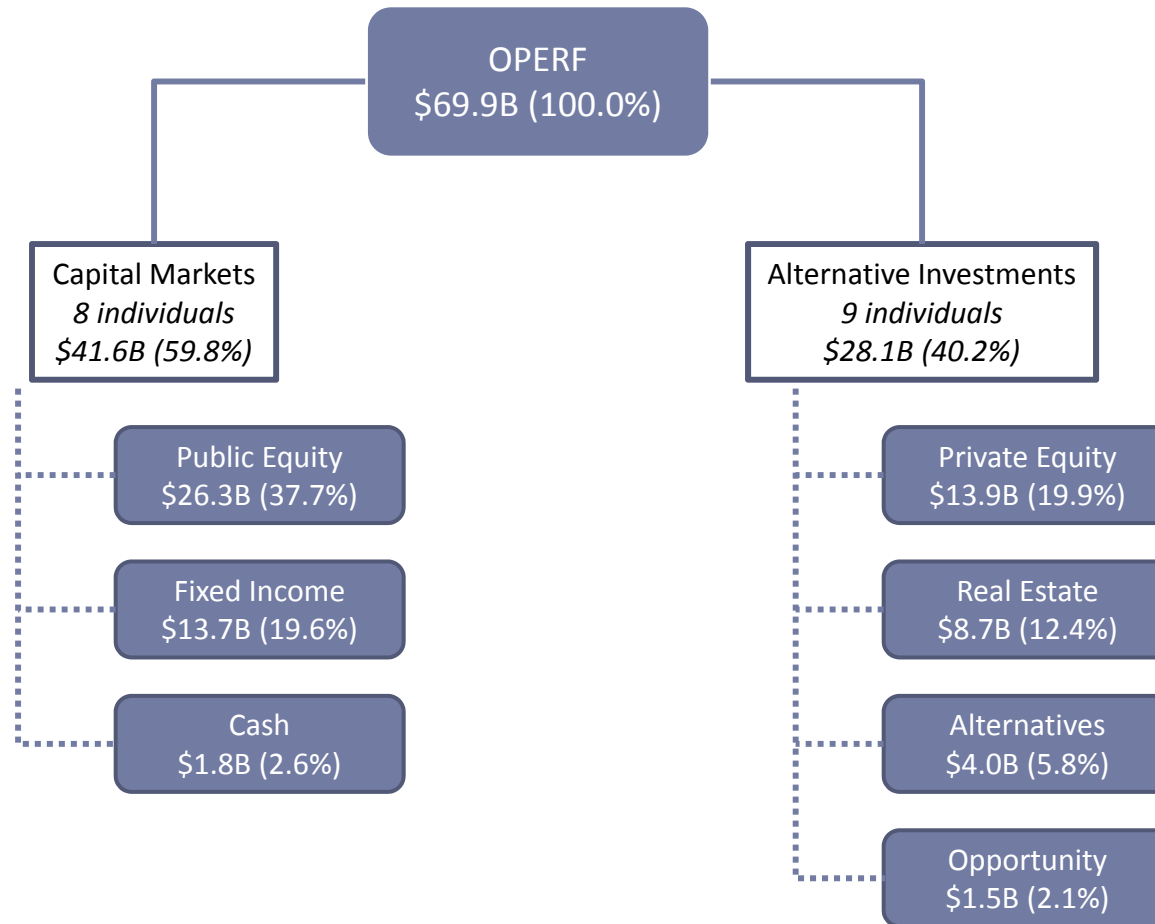
April 3, 2017

OST Investment Division Assets Under Management (at December 31 2016)



Total Assets: \$92.7 billion

Oregon Public Employees Retirement Fund Asset Allocation (at Dec 31 2016)



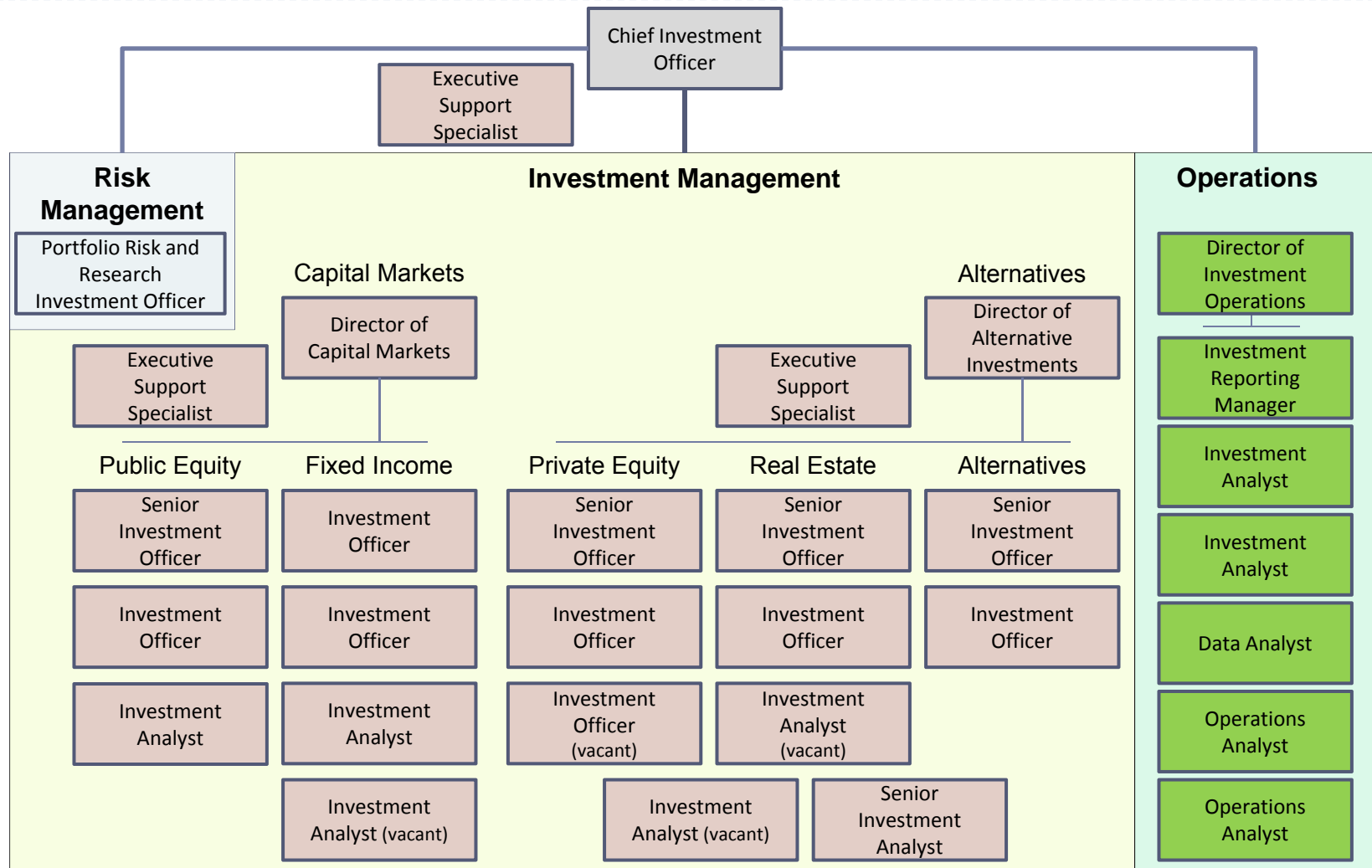
OPERF Performance & Peer Rankings (as of December 31, 2016)

Annualized Return¹	1-Year	3-Year	5-Year	7-Year	10-Year
Russell 3000	12.74%	8.43%	14.67%	12.92%	7.07%
S&P 500	11.96%	8.87%	14.66%	12.83%	6.95%
Russell 2000	21.31%	6.74%	14.46%	13.24%	7.07%
MSCI ACWI ex-US IMI	4.41%	-1.44%	5.35%	3.28%	1.22%
MSCI Emerging Markets	11.19%	-2.55%	1.28%	0.47%	1.84%
Bloomberg Barclays U.S. Aggregate	2.65%	3.03%	2.23%	3.62%	4.34%
Fund Performance (Ranking²)	1-Year	3-Year	5-Year	7-Year	10-Year
OPERF	6.88% (47)	5.40% (9)	9.11% (5)	8.59% (1)	5.47% (1)
Domestic Equity	14.81% (10)	7.73% (61)	14.51% (27)	12.81% (28)	6.94% (21)
International Equity	4.59% (20)	-0.35% (20)	6.90% (16)	4.70% (13)	2.51% (5)
Fixed Income	3.07% (84)	2.37% (78)	3.64% (22)	4.99% (17)	5.27% (13)
Private Equity	6.26% (36)	9.90% (11)	12.03% (1)	12.51% (1)	9.62% (1)
Real Estate	6.58% (78)	10.17% (64)	11.38% (35)	9.81% (66)	5.20% (30)

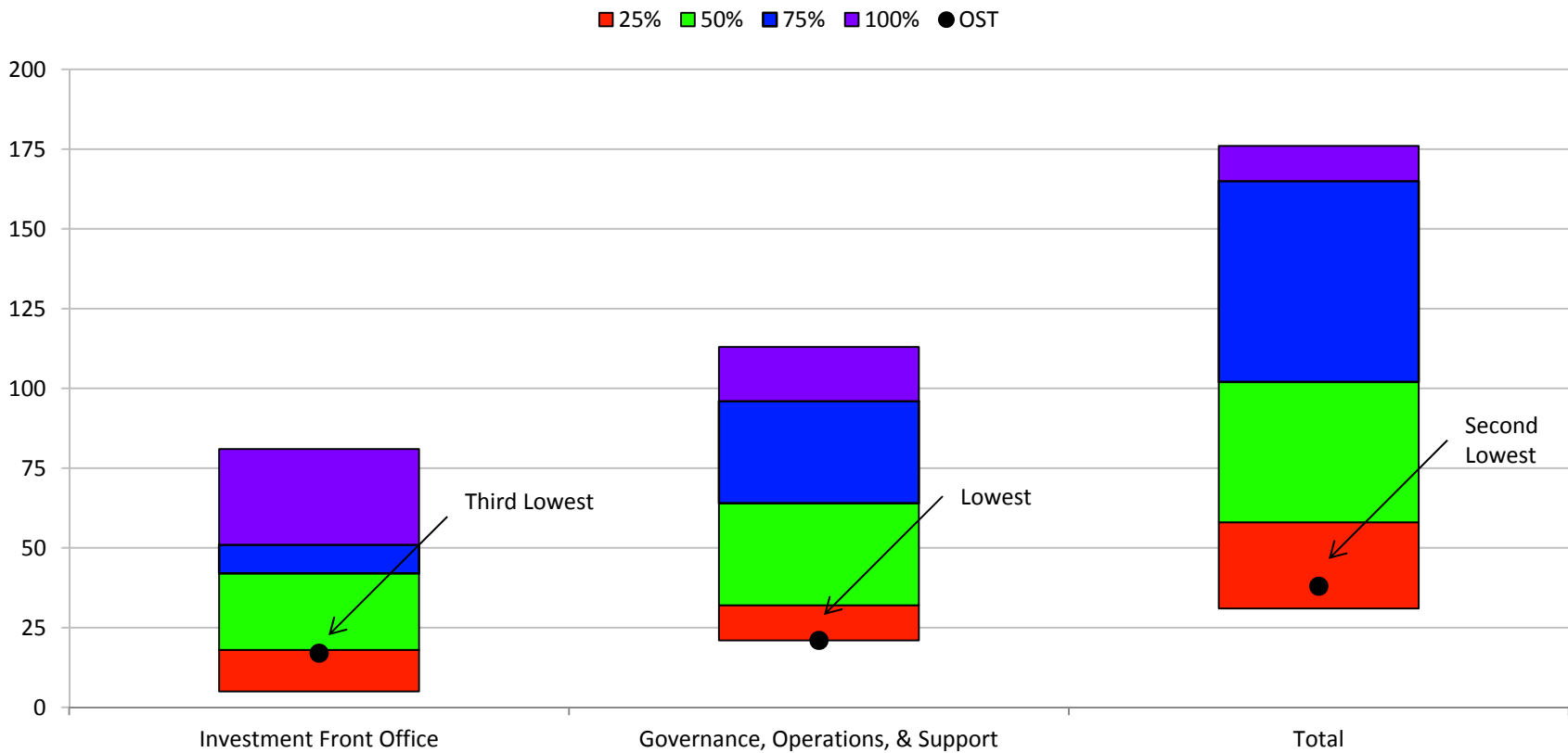
● ¹ Bloomberg for index returns & levels.

● ² Relative to Wilshire Trust Universe Comparison Service (TUCS) Public Funds > \$10 Billion peer group.

OST Investment Division Org Chart



OST Staffing Compared to Peers



Rankings based on custom peer group of 13 global asset owners of similar size and portfolio composition.

Source: CEM Benchmarking, November 2016 report.



Thank You

John D. Skjervem, CFA
Chief Investment Officer
Oregon State Treasury

April 3, 2017



Oregon

Kate Brown, Governor

Public Employees Retirement System

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April 3, 2017

TO: Members of the PERS Board
FROM: Linda M. Barnett, Budget Officer
SUBJECT: April 3, 2017 Budget Execution Report

2015-17 OPERATIONS BUDGET

Operating expenditures for January 2017 and preliminary expenditures for February 2017 were \$3,926,628 and \$3,468,542, respectively. Final expenditures for February closed on March 17, 2017, in the Statewide Financial Management System (SFMS), and will be included in the May 26, 2017, report to the Board. To date, through the first 20 months (or 83%) of the 2015-17 biennium, the Agency has expended a total of \$78,092,577 or 73.02% of PERS' legislatively approved operations budget of \$106,949,449. The current projected positive variance is \$3,571,210 or approximately 3.34% of the operations budget. The Agency's goal is to maintain a positive variance of at least \$2.1 million (2%).

As of February 2017, PERS' budget contains \$3,466,176 unscheduled budget which was approved during the 2015 Legislative Session to do the following:

- \$1,659,976 Pkg. 104 – IT Maintenance & Enhancements
- \$1,581,200 Pkg. 105 – to further develop the agency's Disaster Recovery and Business Continuity technology infrastructure in support of the Oregon Retirement Information Online Network (ORION).
- \$225,000 Pkg. 840 – to implement SB 370; this established a new benefit that allows an ex-spouse of an Oregon Public Service Retirement Plan (OPSRP) member to receive a death benefit if the member, who is vested, dies pre-retirement.

The 2017-19 PERS' Governor's Budget consists of \$109,143,993 in limited or operating budget and \$10,993,982,999 in non-limited budget which represents benefit payments made, health insurance premiums, and third-party administration payments for both the PERS Health Insurance Program and the Individual Account Program. PERS has completed Phase 1 of its budget presentation to the General Government Subcommittee of the Joint Ways & Means Committee. PERS may be asked to conduct a more in-depth discussion of the agency's major budget issues in Phase 2. Phase 3, Work Sessions, may occur as soon as late May, but usually occur in June.

Attachment:

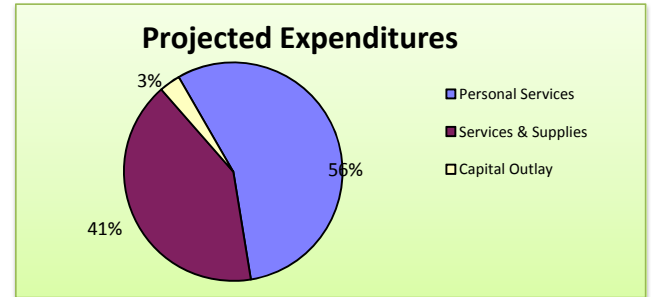
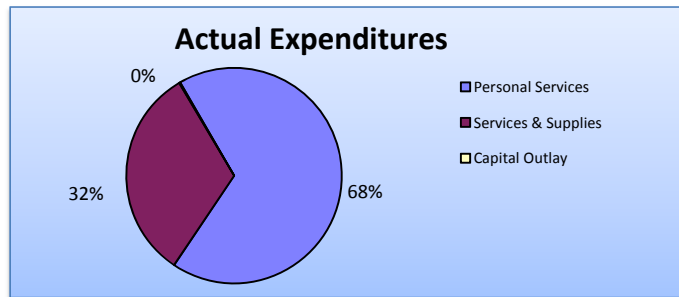
A.2.c. Attachment 1 – 2015-17 Agency-wide Budget Execution Summary Analysis

**2015-17 Agency-wide Budget Execution
Summary Budget Analysis
Preliminary for the Month of: February 2017**

Limited - Operating Budget

2015-17 Biennial Summary

Category	Actual Exp. To Date	Projected Expenditures	Total Est. Expenditures	2015-17 LAB	Variance
Personal Services	52,893,109	12,168,728	65,061,837	69,268,743	4,206,906
Services & Supplies	25,044,662	8,973,811	34,018,473	33,118,723	(899,750)
Capital Outlay	154,806	676,948	831,754	1,095,807	264,053
Unscheduled	0	3,466,176	3,466,176	3,466,176	0
Total	78,092,577	25,285,663	103,378,240	106,949,449	3,571,210



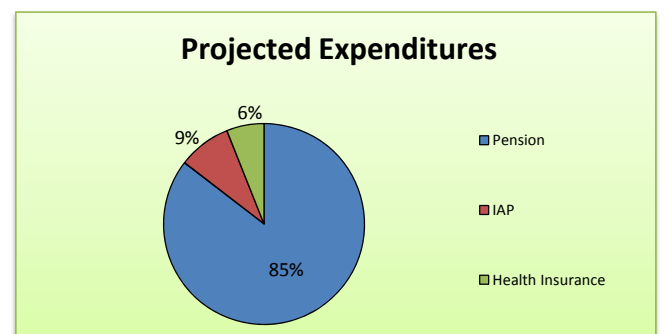
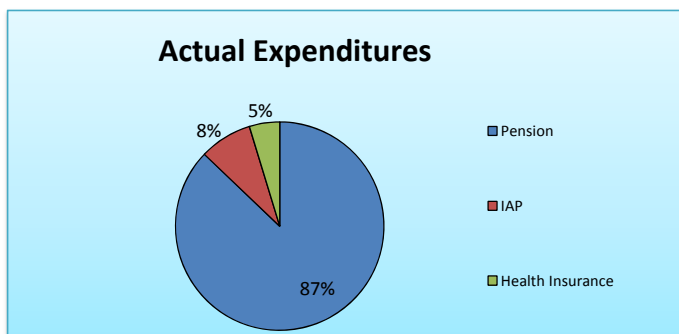
Monthly Summary

Category	Actual Exp.	Projections	Variance	Avg. Monthly Actual Exp.	Avg. Monthly Projected Exp.
Personal Services	2,778,624	3,043,375	264,751	2,644,655	3,042,182
Services & Supplies	689,918	947,211	257,293	1,252,233	2,243,453
Capital Outlay	0	0	0	7,740	169,237
Total	3,468,542	3,990,586	522,044	3,904,629	5,454,872

Non-Limited Budget

2015-17 Biennial Summary

Programs	Actual Exp To Date	Projected Expenditures	Total Est. Expenditures	Non-Limited LAB	Variance
Pension	6,805,146,794	1,426,881,608	8,232,028,402	8,291,874,726	59,846,324
IAP	637,712,034	142,295,980	780,008,014	873,488,891	93,480,877
Health Insurance	368,968,172	100,575,485	469,543,657	558,094,445	88,550,788
Total	7,811,827,000	1,669,753,073	9,481,580,073	9,723,458,062	241,877,989





Oregon

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April 3, 2017

TO: Members of the PERS Board
FROM: Stephanie Vaughn, Manager, Policy Analysis & Compliance Section
SUBJECT: Notice of Rulemaking for Insolvent Employer Rule:
OAR 459-009-0400, *Insolvent Employer*

OVERVIEW

- Action: None. This is notice that staff has begun rulemaking.
- Reason: Define “insolvent employer” and establish that the PERS Board has the authority to take action to satisfy some or all outstanding liability of an insolvent employer to the PERS Fund through the Contingency Reserve.
- Policy Issue: None identified.

BACKGROUND

ORS 238.670(1)(a) authorizes the PERS Board to use funds in the Contingency Reserve established under ORS 238.670(1) to “prevent any deficit in the fund by reason of the insolvency of a participating public employer.” Note that the funding for this purpose can only be from earnings from employers; \$25 million has currently been set aside in the reserve for this purpose.

The Board has not previously used the Contingency Reserve to address the liabilities of insolvent employers, principally because there has never been a framework to determine that an employer is insolvent. There are a number of PERS employers that have ceased to exist as ongoing entities; many of them have remaining PERS liabilities, whether outstanding invoices or unfunded actuarial liabilities.

The new administrative rule provides a definition of insolvent employer to assist in assessing whether the Contingency Reserve should be for this purpose. A simple balance sheet analysis is not sufficient to determine solvency; PERS should also determine whether there are other potential sources for payment of the liabilities, such as successor entities, or other entities that may have received assets or assumed liabilities of the dissolved entity. Once PERS determines, after making all reasonable efforts to collect as required by OAR 459-005-0620, that there is no resource from which to collect, then PERS will consider whether the employer is insolvent.

PUBLIC COMMENT AND HEARING TESTIMONY

A rulemaking hearing will be held April 25, 2017, at 3:00 p.m. at PERS headquarters in Tigard. The public comment period ends May 3, 2017, at 5:00 p.m.

LEGAL REVIEW

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

IMPACT

Mandatory: Yes. Without a clear definition of “insolvent employer,” the Board would not be able to carry out its discretion in the use of the reserve account money as specified in the statute.

Impact: This rule sets the definition for an “insolvent employer” so that once an employer is determined to be insolvent, the Board may then exercise its discretion under ORS 238.670(1)(a) to use the reserve account money to satisfy any outstanding PERS liability the insolvent employer may have left behind.

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

RULEMAKING TIMELINE

March 15, 2017	Staff began the rulemaking process by filing a Notice of Rulemaking with the Secretary of State.
April 1, 2017	<i>Oregon Bulletin</i> publishes the Notice. Notice is sent to employers, legislators, and interested parties. Public comment period begins.
April 3, 2017	PERS Board notified that staff began the rulemaking process.
April 25, 2017	Rulemaking hearing to be held at 3:00 p.m. at PERS in Tigard.
May 3, 2017	Public comment period ends at 5:00 p.m.
May 26, 2017	Staff will propose adopting the rule modifications, including any changes resulting from public comment or reviews by staff or legal counsel.

NEXT STEPS

A rulemaking hearing will be held April 25, 2017, at 3:00 p.m. at PERS headquarters in Tigard. The rule is scheduled to be brought before the PERS Board for adoption at the May 26, 2017 Board meeting.

B.1. Attachment 1 - 459-009-0400, *Insolvent Employer*

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

1 **459-009-0400**

2 **Insolvent Employer**

3 **(1) For the purposes of this rule, an “insolvent employer” is an employer that**
4 **meets all of the following requirements:**

5 **(a) The employer has dissolved either by statute or administrative action as an**
6 **on-going entity;**

7 **(b) There are no assets from which PERS can collect to cover the dissolved**
8 **employer’s PERS liability or there are inadequate assets to cover all PERS liability;**
9 **and**

10 **(c) There is no entity either by operation of law or contractual agreement that is**
11 **responsible for the dissolved employer’s remaining liability, or PERS is unable to**
12 **assign the remaining liability to an entity.**

13 **(2) If PERS determines an employer is insolvent, the board may take action to**
14 **satisfy some or all of the outstanding liability of an insolvent employer to the fund**
15 **through the Contingency Reserve established under ORS 238.670(1).**

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

17 **Stats. Implemented: ORS 238.670**



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April 3, 2017

TO: Members of the PERS Board
FROM: Stephanie Vaughn, Manager, Policy Analysis & Compliance Section
SUBJECT: Notice of Rulemaking for Restoration of Forfeited Service Credit Rule:
OAR 459-011-0050, *Forfeiture and Restoration of Service Rights*

OVERVIEW

- Action: None. This is notice that staff has begun rulemaking.
- Reason: Clarify administration of membership termination and restoration of forfeited credit by reason of withdrawal, including how membership forfeiture impacts other PERS statutes. Specifies that the five-year clock for separation from service begins from the date of last separation from employment in a “qualifying position” and clarifies what types of membership forfeiture may be restored under ORS 238.105 and 238.115.
- Policy Issue: None identified.

BACKGROUND

There are two ways a Tier One/Tier Two member ceases to be a member: through withdrawal or through loss of membership (LOM). Withdrawal occurs under ORS 238.265, when a member withdraws their account and terminates their membership. The withdrawal terminates all of the member’s rights in the system; if that person later returns to PERS membership (after serving another six-month waiting period in a qualifying position), their rights for the employment before the withdrawal remain forfeited. ORS 238.105 provides one way for such persons to restore the rights forfeited by the withdrawal: if the reemployment is within five years from when they left the PERS-covered employment that preceded the withdrawal, the member repays the amount previously withdrawn plus interest that would have accrued on the withdrawn amount within the first year of reemployment (commonly known as a “voluntary redeposit”). If the member does not restore their account through a voluntary redeposit and is an active member for 10 or more years (on subsequent employment), they can purchase some or all of their forfeited time at retirement under ORS 238.115.

A member also loses their membership if they leave PERS-covered employment before becoming vested and does not work for a PERS participating employer for five or more years (commonly known as “Loss of Membership” or “LOM”). After the member goes into LOM status, all rights in the system are terminated under ORS 238.095(2), and their account ceases to accrue additional earnings under ORS 238.095(4). If they return to PERS-covered employment, they must serve another six-month waiting period and establish new membership; there is no statutory provision that allows for this time to be restored or purchased.

OAR 459-011-0050 was adopted to address PERS administration of membership forfeiture and restoration. However, that rule only addresses the voluntary redeposit under ORS 238.105. That

rule does not address the restoration of forfeited time by the purchase that is available under ORS 238.115 nor does it clarify that restoration under ORS 238.115 is not available to those who lost their membership rights through LOM. The proposed rule modifications provide these clarifications. Given that these statutes do not use consistent terminology, staff have been inconsistent in applying these provisions to members who are trying to restore their prior service and accounts so the rule modifications draw these distinctions more clearly. Members' expectations about whether they can restore these rights have also been inconsistently communicated, so the rule modifications will provide that clarity as well. Given the inconsistencies in the statutes, PERS does not intend to review prior purchases but has directed staff to follow these strictures on a going-forward basis.

PUBLIC COMMENT AND HEARING TESTIMONY

A rulemaking hearing will be held April 25, 2017, at 3:00 p.m. at PERS headquarters in Tigard. The public comment period ends May 3, 2017, at 5:00 p.m.

LEGAL REVIEW

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

IMPACT

Mandatory: No, the Board need not adopt the rule modifications.

Impact: Clarification of procedures and administration will benefit members and staff.

Cost: There are no discrete costs attributable to the rule. Statute requires the administration of voluntary redeposits and forfeited time purchases as provided under ORS 238.095, 238.105, 238.115, and 238.265.

RULEMAKING TIMELINE

March 15, 2017	Staff began the rulemaking process by filing a Notice of Rulemaking with the Secretary of State.
April 1, 2017	<i>Oregon Bulletin</i> publishes the Notice. Notice is sent to employers, legislators, and interested parties. Public comment period begins.
April 3, 2017	PERS Board notified that staff began the rulemaking process.
April 25, 2017	Rulemaking hearing to be held at 3:00 p.m. at PERS in Tigard.
May 3, 2017	Public comment period ends at 5:00 p.m.
May 26, 2017	Staff will propose adopting the rule modifications, including any changes resulting from public comment or reviews by staff or legal counsel.

Notice – Restoration of Forfeited Service Credit Rule

04/03/17

Page 3 of 3

NEXT STEPS

A rulemaking hearing will be held April 25, 2017, at 3:00 p.m. at PERS headquarters in Tigard. The rule is scheduled to be brought before the PERS Board for adoption at the May 26, 2017 Board meeting.

B.2. Attachment 1 - 459-011-0050, *Forfeiture and Restoration of Service Rights*

**OREGON ADMINISTRATIVE RULE
PUBLIC EMPLOYEES RETIREMENT BOARD
CHAPTER 459
DIVISION 011 – RETIREMENT CREDIT**

1 **459-011-0050**

2 **Forfeiture and Restoration of Service Rights**

3 (1) A member who, pursuant to ORS 238.265, withdraws the amount credited to the
4 member's account ceases to be a PERS Chapter 238 Program member and forfeits all
5 membership rights accrued under ORS Chapter 238 before the effective date of *[the]*
6 withdrawal, including any service rights attributable to employment before the effective
7 date of *[the]* withdrawal.

8 (2) Any such person may elect to restore credit forfeited by the withdrawal of
9 the member account as provided in ORS 238.105 or 238.115.

10 ~~[(2)]~~(3) Pursuant to ORS 238.105, [A]any such person who reenters the service of
11 a participating employer in a qualifying position within five years from the date of the
12 last separation from employment in a qualifying position that preceded the member's
13 withdrawal may, at any time during the one-year period immediately following the date
14 of reemployment, repay to PERS, in a single lump sum payment, an amount equal to the
15 amount withdrawn plus the earnings the amount withdrawn would have accumulated
16 from the effective date of withdrawal to the date of repayment.

17 ~~[(3)]~~(a) Upon repayment as described in section ~~[(2)]~~(3) of this rule, the PERS
18 Chapter 238 Program membership and service rights forfeited by the withdrawal will be
19 restored. The former member will reestablish membership in the PERS Chapter 238
20 Program on the first day of the month following the date of the repayment. Service by the
21 former member from date of reemployment to the date membership is reestablished shall

1 be attributed to the PERS Chapter 238 Program. The withdrawn member account will be
2 reestablished in the amount of the repayment.

3 ~~[(4)]~~**(b)** An employee who is terminated from employment, withdraws the member
4 account under ORS 238.265, and is reinstated to employment in connection with a
5 retroactive payment may restore membership and service rights within the time period
6 described in section ~~[(2)]~~**(3)** of this rule or within one year from the date the employee
7 actually returns to employment, whichever is later. A retroactive payment must be
8 allocated pursuant to ORS 238.008. So allocated, the payment must be used in the
9 determination of employee and employer contributions and in the calculation of benefits.

10 **(4) Pursuant to ORS 238.115, a person described in section (1) of this rule who**
11 **reenters the service of a participating employer in a qualifying position and serves as**
12 **an active member for 10 years after such reentry may obtain restoration of**
13 **creditable service forfeited by the withdrawal if the member repays to PERS, in a**
14 **single lump sum payment, an amount equal to the amount withdrawn plus the**
15 **earnings the amount withdrawn would have accumulated from the effective date of**
16 **withdrawal to the date of repayment.**

17 **(5) Restoration of credit forfeited by withdrawal of the member account under**
18 **section (4) of this rule is not available to persons who already restored membership**
19 **and service rights under section (3) of this rule.**

20 **(6) A person whose membership is terminated under ORS 238.095(2) may not**
21 **restore forfeited credit under ORS 238.115.**

22 ~~[(5)]~~**(7)** Notwithstanding the provisions of this rule, a member who withdraws
23 pursuant to ORS 238.265 and receives an additional amount pursuant to section 2, chapter

1 276, Oregon Laws 2003, may not reestablish membership under section ~~[(2)]~~(3) of this
2 rule.

3 Stat. Auth.: ORS 238.650

4 Stats. Implemented: ORS 238.008, 238.095, 238.105, 238.115, 238.125, 238.265,
5 2003 OL Ch. 276 *[2007 OL Ch. 769]*



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April 3, 2017

TO: Members of the PERS Board
FROM: Stephanie Vaughn, Manager, Policy Analysis & Compliance Section
SUBJECT: Disability Rules Update

At the January 27, 2017 Board meeting, we presented modifications to the Disability Rules and indicated we anticipated presenting them for adoption at the April 3, 2017 Board meeting.

The modifications are the result of meeting with a focus group comprised of staff and employer representatives. We received public comment on the rules and anticipate additional modifications to them. However, with the legislature in session, we have not had sufficient time to properly vet any additional changes to the rules to have them ready for adoption at this meeting.

We hope to present the rules for adoption at the May 26, 2017 meeting.



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April 3, 2017

TO: Members of the PERS Board
FROM: Stephanie Vaughn, Manager, Policy Analysis & Compliance Section
SUBJECT: *Moro* Attorney Fees and Costs

BACKGROUND

On June 11, 2015, petitioners in the *Moro* case filed claims for attorney fees, seeking fees and costs of \$2,426,459. On October 27, 2016, the Oregon Supreme Court awarded attorney fees and costs in the amount of \$943,792.95, directing that the PERS Board determine, within its statutory authority and fiduciary obligations, how best to allocate the burden of the fee award among the PERS Fund's accounts. The appellate judgment was issued on February 24, 2017, and includes post-judgment interest from the date of the judgment to date of payment. The post judgment interest as currently around \$8,900.00.

DISCUSSION

The Supreme Court awarded attorney fees based on the common-fund and substantial-benefit doctrines. These are not “prevailing party” fees meant to make the plaintiffs whole, but are meant to avoid unjust enrichment by spreading the litigation costs among those who benefited from the case. The Court’s decision explains these concepts:

The common-fund doctrine applies when a plaintiff’s “legal efforts create, discover, increase, or preserve a fund of money to which others also have a claim.” *Strunk II*, 341 Or at 181. A party who litigates such a case may recover the costs of those legal efforts, including attorney fees, from the created or preserved fund. *Id.* The substantial-benefit doctrine, on the other hand, ordinarily applies when a party’s legal efforts create nonliquidated benefits—whether or not pecuniary—that are held in common with others, such as when a union member’s lawsuit benefits other union members, *Gilbert v. Hoisting & Port. Engrs.*, 237 Or 130, 137, 384 P2d 136 (1963), or a shareholder’s lawsuit benefits the corporation and thus other shareholders, *Crandon Capital Partners*, 342 Or at 562-63.

Moro v. State of Oregon, 360 Or 467 (2016). Those who will benefit from the *Moro* decision, theoretically, include PERS members (retired, active, and inactive) and beneficiaries whose increased cost-of-living adjustments (COLAs) were restored by this decision. That population is constantly changing as members withdraw, die, elect the total lump sum retirement option, etc. The Court recognized the administrative challenges in determining the source from which to pay the fees, particularly given that there is no segregated fund holding the COLAs that PERS members will receive in the future, and decided the best course was to allow the Board to determine how best to allocate the fee award obligation.

Staff evaluated a number of options to pay the fees, including:

1. Reduce earnings credited to the Benefits-in-Force Reserve (BIF). This would be done via the annual earnings crediting process. However, it would only affect retired members.
2. One-time reduction to all benefit payments. This option would require either a manual process using temporary resources, or program changes to the system. This option would only affect retired members.
3. Invoicing all members. Based on 346,400 members (as of December 31, 2015), the amount per member would be \$2.72; if only retirees were invoiced (132,000 retirees), the amount per retiree would be \$7.15. Based on PERS' experience with invoicing, the cost to invoice just the retirees would be approximately \$2,800,000 and would take 46 months to complete.
4. Reduce earnings crediting to member accounts. This would be done via the annual earnings crediting process. However, this would only affect active and inactive Tier One/Tier Two members and would eventually cost the members more than the amount of the attorney fees over time. Members would be crediting fewer earnings in the calendar year affected and lose the future earnings on that amount.
5. Reduce earnings crediting to IAP accounts. This would be done via the annual earnings crediting process. This would affect only active and some inactive members; members who have been inactive since before 2004 would not be affected. Similarly, this option would eventually cost the members more as they lose the future earnings on the amount not credited.
6. Use Contingency Reserve funds. ORS 238.670(1)(b) allows the board to use Contingency Reserve funds "To pay any 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." Other than the \$25 million set aside for insolvent employers, the funds in the Contingency Reserve are not allocated to any particular group.

Since options #1, 2, 4, and 5 each affect only a portion of the target population, they would have to be used in some combination to affect all groups. Of all the options considered, only two affect active, inactive, and retired members: invoicing (#3) and using the Contingency Reserve (#6). Invoicing does not seem a feasible option, as the cost of invoicing would exceed the amount of the attorney fees.

Considering the amount of the attorney fee award comparative to the cost of implementing one or more of the other options described above, using the Contingency Reserve is the least expensive and most efficient way to pay the attorney fees. For these reasons, staff recommends using the Contingency Reserve to pay the attorney fees. Use of the Contingency Reserve was contemplated by the Court, which specifically stated that the "authority to operate the system includes making decisions related to litigation, and, as long as PERB acts reasonably and consistently with statutory requirements and its fiduciary duty to members, such decisions ordinarily will be upheld, unless PERB has abused its discretion." (Citing the *White* case.)

BOARD OPTIONS

The Board may:

1. Pass a motion to “pay attorney fees awarded by the court in the *Moro* case from the Contingency Reserve.”
2. Direct staff to implement one or more of the other options presented.
3. Direct staff to explore other options.

RECOMMENDATION

Staff recommends the Board choose Option #1.

- Reason: Using Contingency Reserve funds is the most efficient option to pay the attorney fees and it is within the Board’s statutory authority to do so.



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April 3, 2017

TO: Members of the PERS Board
FROM: Yvette Elledge-Rhodes, Chief Operations Officer
SUBJECT: *Moro* Implementation Project Update

PROJECT ACTIVITIES

For the *Moro* project, we are in the process of resolving the final population which represents all benefit recipients (about 7,400) who passed away before their cost-of-living adjustment (COLA) was restored. About 300 benefit recipients pass away every month, so this population is comprised of people who did so between the time that the 2013 legislation was implemented (which was partially reversed when Oregon Supreme Court's decision in the *Moro* case was issued) and we adjusted the COLA in accordance with that decision. We are resolving these by researching whether an authorized representative was established for the recipient's estate and, if not, attempting to notify the recipient's survivors of the amount of unclaimed benefits. Our goal is to complete this work by the end of June 2017.

- As of March 10, 2017, we have sent out 4,868 letters to this population, which is 77% of the population that we need to notify. PERS has received forms from 784 representatives and paid out 673 accounts.
- If we continue to send weekly mailings of 250-300 letters, we will reach our goal of 100% notification by the end of April.
- We have paid out 11% of the population for a total dollar amount of \$122,597.13

At the January Board meeting, the Board expressed interest in the total amount that could potentially be paid out for the deceased population. That information is captured in the table below:

Population	Action	Accounts	Total
Negative COLA Retro	Invoice	57	\$(960.88)
Outstanding Invoice > Retro	Apply to Invoice	498	\$93,603.21
<\$5.00 Retro	Waive	591	\$1,493.12
>\$5.00 Retro	Pay Retro	6,306	\$934,734.00
Total Population		7,452	

There will be additional charges to the Contingency Reserve for the remaining populations of deceased accounts, which we will include in our project closeout report at the Board's July 2017 meeting.



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April 3, 2017

TO: Members of the PERS Board
FROM: Marjorie Taylor, Senior Policy Director
SUBJECT: Legislative Update

2017 REGULAR LEGISLATIVE SESSION

The 2017 Regular Legislative Session convened on Wednesday, February 1, and PERS has been a topic of discussion in committees since that time. About 2,700 bills have been introduced for consideration so far, and the deadline for work sessions on most first chamber bills is Tuesday, April 18. The deadline for work sessions on most second chamber bills is Friday, June 2. The Constitutional deadline for the end of session is Monday, July 10.

LEGISLATION IMPACTING PERS

The Senate Workforce Committee has taken the lead in holding public hearings on a variety of bills impacting PERS. First, the committee heard extensive background testimony about system dynamics and how the plan has evolved over time, from PERS staff and a variety of stakeholders. The committee then sought recommendations from the public regarding ideas for PERS reform. A “technical team” including PERS and staff from Legislative Counsel, Legislative Fiscal, and the DAS Chief Human Resources Office, shared high-level reaction to those public ideas.

Other committee discussions have centered on provisions in Senate Bill 559, Senate Bill 560, Senate Bill 913, and various amendments that could change: the calculation of Final Average Salary (extend the number of years used in the calculation, cap the amount, eliminate vacation and sick leave, reduce the calculation factor); redirection of member contributions from the Individual Account Program to offset the costs for the member’s pension benefit; extending the waiting time period to establish membership and increasing the hours required to be in a qualifying position; mandating an assumed rate of return for certain purposes; and others.

In addition to hearing about PERS reform proposals, the Senate Workforce Committee engaged in a discussion about the Contingency Reserve and current over-funded status. Ultimately, the committee sent the Board a letter recommending that funds be redeployed to reserves and accounts to reduce the unfunded actuarial liability. (Item C.4. Attachment 2)

The House Committee on Business and Labor holds most PERS bills in the House, and has not scheduled hearings on this topic.

PERS BUDGET BILL

The PERS budget bill, Senate Bill 5534, was heard in the Joint Ways and Means Subcommittee on General Government during the week of March 6. The committee heard a one-day summary about PERS, the system, followed by two days about agency operations including the strategic plan, outcome and performance measures, and Policy Option Package requests. On the fourth

day, the committee heard brief public testimony in support of the budget and a report on 2016 preliminary earnings crediting.

The subcommittee was interested in how the over-funding of the Contingency Reserve may be redeployed. Similar to a recommendation from the Senate Workforce Committee, the General Government subcommittee requests that, prior to final action, the Board report to the Joint Committee on Ways and Means regarding which accounts the Reserve funds may be redeployed to and the associated rationale.

We anticipate that the PERS budget will receive further consideration during “Phase II” of the budget process, and may again be scheduled for discussion in late April.



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April 3, 2017

TO: Members of the PERS Board
FROM: Mary Dunn, Assistant Chief Administration Officer
SUBJECT: Preliminary Contingency Reserve Allocation

OVERVIEW

As first explained in the 2016 Preliminary Earnings Crediting agenda item at the PERS Board's January 27, 2017 meeting, the Contingency Reserve is currently over-funded by \$345.8 million based on the funding level adopted by the PERS Board at its March 2016 meeting of 0.25% of the system's accrued liability. Staff described several options for deployment of this excess funding, and stakeholder input was sought on those options (or others to be suggested). Note that the Contingency Reserve is part of the PERS Fund, and that ORS 238.660(2) provides that "assets of the fund may not be diverted or otherwise put to any use that is not for the exclusive benefit of members and their beneficiaries."

STAKEHOLDER INPUT

Three letters were submitted in response to the request for stakeholder input: one from Greg Hartman (Attachment 1); another from Senators Kathleen Taylor and Tim Knopp, the Chair and Vice-Chair of the Senate Committee on Workforce (Attachment 2); and from the Senate Republican Caucus (Attachment 3).

The response from the Senate Committee on Workforce states "It is our strong recommendation that the Board allocate the excess Contingency Reserve funds to other reserve accounts where the funds will be credited toward the unfunded liability." Mr. Hartman, representing the PERS Coalition, states that "funds should be distributed...on a pro-rata basis back to the funds from which they derived." He goes on to state, "From a system-wide perspective a pro-rata distribution would ultimately be virtually indistinguishable from a distribution directly to the benefits-in-force." The letter from the Senate Republican Caucus concludes, "...the Board should mindfully devote the \$345.8 million surplus to paying down the unfunded liability." PERS staff has evaluated these recommendations and offers the following options for consideration.

PRELIMINARY REALLOCATION OPTIONS:

- *Deploy excess funds in the Contingency Reserve in relative proportion to the member and employer reserves and accounts that contributed to the funding of the reserve.*

Since the Contingency Reserve balance is derived from revenue from the Tier One and Tier Two member reserves, Employer Reserves, and the Benefits in Force Reserve, then when the Contingency Reserve is over-funded, an option is to return revenue to its source. Historically, there are two occasions where the PERS Board reallocated Contingency Reserve funds in this manner, but system dynamics have also driven particular allocations that vary from this model.

- *Deploy excess funds in the Contingency Reserve to the Benefits in Force Reserve.*

The Benefits in Force Reserve, established under ORS 238.670(2), is the source from which all Tier One and Tier Two member benefits are paid. This reserve is funded through transfers of contributions and accumulated earnings from member accounts and employer reserves at the time of the member's retirement.

Based on the December 31, 2015 system valuation, PERS has an unfunded actuarial liability (UAL) of \$21.8 billion, excluding side accounts. Retired members, or their beneficiaries, currently account for 64% of the system's liabilities, or approximately \$13.9 billion of the UAL if that same proportion is applied. Compared to the system's liability for retired member benefits and the current funding level of this reserve, a direct infusion of these excess Contingency Reserve funds would incrementally improve the amount of funds available to satisfy these benefit payments as they come due.

This allocation would be consistent with the direction from the Senate Workforce Committee and the Senate Republican Caucus. Functionally, this allocation would also accomplish much of the result advocated by the PERS Coalition, as the bulk of the funding would be allocated to the Benefits in Force Reserve and employer reserves, as those two accounts generate the vast majority of earnings that have been credited to the Contingency Reserve. Only a small fraction would not be paid back to Tier Two member accounts (Tier One member accounts would not increase, as they cannot receive earnings in excess of the assumed rate; any extra crediting would go into the Tier One Rate Guarantee Reserve, which is currently in surplus). Tier Two members would benefit from the increase in the Benefits in Force Reserve's funding because that reserve's funding balance will be used to pay their benefits when they ultimately retire.

For these reasons, staff recommends that the PERS Board allocate the excess Contingency Reserve funds to the Benefits in Force Reserve.

WAYS AND MEANS SUBCOMMITTEE RECOMMENDATION

At its March 9, 2017 meeting, the Joint Committee on Ways and Means Subcommittee on General Government adopted a recommendation that the PERS Board report back to the Joint Committee on Ways and Means as to which accounts the Contingency Reserve funds would be reallocated to and the associated rationale for the decision. Although the full Joint Ways and Means Committee has not adopted this recommendation as of this date, staff recommends that we adopt preliminary direction on the allocation and await further legislative action before finalizing the allocation.

Executive Director Steve Rodeman responded to this direction in a letter to the Senate Committee on Workforce (Attachment 4). He outlined that the Board would continue action on 2016 earnings crediting at this meeting, but the delay in reallocating the Contingency Reserve means 2016 earnings crediting will not be impacted. Director Rodeman clarified that an allocation of the Contingency Reserve that is finalized in the 2017 calendar year will be reflected in the 2017 system valuation and recognized during the subsequent employer rate setting cycle (to take effect July 1, 2019).

BOARD ACTION – PRELIMINARY CONTINGENCY RESERVE ALLOCATION

The Board’s options for the Preliminary Contingency Reserve Allocation include:

1. Pass a motion, contingent on legislative reporting and review, to “adopt the preliminary allocation of excess funds in the Contingency Reserve to the Benefits in Force Reserve, subject to adoption at a future PERS Board meeting.”
2. Pass a motion, contingent on legislative reporting and review, to “adopt the preliminary allocation of excess funds in the Contingency Reserve proportionality back to the accounts from which they were derived, subject to adoption at a future PERS Board meeting.”
3. Pass a motion, contingent on legislative reporting and review, to allocate excess Contingency Reserve funds in a different proportion, subject to adoption at a future PERS Board meeting.

STAFF RECOMMENDATION

Staff recommends the Board choose Option 1.

NEXT STEPS

Contingency Reserve allocation: When the Board makes its preliminary allocation, staff will prepare and present the required report to the Joint Legislative Committee on Ways and Means. Any comments received from the committee will be presented to the Board prior to the final decision at a future meeting.

Attachments:

- C.4. Attachment 1 – Greg Hartman Memo (February 12, 2016)
- C.4. Attachment 2 – Senator Taylor and Senator Knopp Letter (March 7, 2017)
- C.4. Attachment 3 – Senate Republican Caucus Letter (March 20, 2017)
- C.4. Attachment 4 – Director Rodeman Letter (March 10, 2017)

BENNETT, HARTMAN, MORRIS & KAPLAN, LLP

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February 12, 2016

BY EMAIL ONLY

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

Re: Contingency Fund ORS 238.670(1)
Our File No.: 5415-237

Dear Steve:

At the upcoming PERB meeting the board will consider issues relating to the contingency reserve including how to determine adequate funding as well as appropriate uses of the contingency reserve. The purpose of this letter is both to make some observations about the contingency reserve and offer some hopefully helpful thoughts on both topics.

While the funding of the contingency reserve has been the topic of recent litigation, particularly in the *City of Eugene* case, none of those cases have offered any specific guidance on the related issue of how to appropriately size the contingency funds nor any guidance on the appropriate uses of the contingency fund. In addition the trial court opinion by Judge Paul Lipscomb in the *City of Eugene* was later vacated by the Supreme Court, so that decision should not play a major role in the board's discussions.

Prior to any specific discussion about the contingency reserve some historical perspective is appropriate. ORS 238.670(1), which authorizes the contingency fund, is currently part of a five-part statute and should be analyzed in the context of that overall statutory scheme. ORS 238.670(1) as well as ORS 238.670(2) were passed in 1951, shortly after the initiation of the system, and for the most part the operative language of these two reserve statutes has not changed. The contingency statute provides that it is to be used to prevent any "deficit of monies available for the payment of retirement allowances" arising from interest fluctuations, changes in mortality rates, loss of investment capital, or other unforeseen contingency. Though there is no legislative history to give any insight on the meaning of this language, contemporaneous PERS documents indicate that at that time there was a substantial concern that the newly-established system would not have sufficient money to pay benefits. It is reasonable to understand the "deficit of monies" language to mean exactly what it says and that initially the primary purpose of the contingency fund was to guard against not having the money to pay

benefits. This interpretation is further supported by ORS 238.670(2), which provides a preferential allocation of income to the fund which we currently call the benefits in force reserve. Clearly the legislature wanted to make certain that the fund set up to pay benefits would receive adequate earnings to carry out its statutory purpose.

The first major amendment to ORS 238.670 took place in 1967 with the addition of sections (3) and (4), which provide for the establishment of additional reserves “to offset gains and losses of invested capital” or alternatively for the amortization of gains or losses if that is preferable. At that same time the contingency reserve language of subsection (1) was amended to delete the reference to loss of investment capital (as well as “unforeseen” contingencies), with new cross-references to sections (3) and (4). Clearly in 1967 the legislature authorized new reserves to address loss of investment capital rather than assigning that responsibility to the contingency reserve. The reserve authorized by subsection (3) has provided the basis for the establishment of the reserve formerly known as the gain/loss reserve, now known as the Tier One rate guarantee reserve. I don’t recall that it has ever been used for another purpose as it is clear that the board has decided to use the authority under subsection (4) to deal with investment issues through amortization rather than by utilization of special reserves. In 1987 the legislature added subsection (5) which requires the board to report proposed earning creditings to the legislature.

In 2001 the legislature amended ORS 238.670(1) by adding three new provisions, subsections (a), (b), and (c), to add potential additional uses of a contingency reserve. A review of the 2001 legislative history of HB 134 which added these new provisions shows that there were multiple changes proposed to PERS, largely by those employers who were participating in the *City of Eugene* litigation which was pending at that time. Among these many changes were a number of proposed changes which would have allowed contingency fund reserves to be used in various ways for the benefit of the employers. During the course of multiple hearings on the bill both Bob Muir, then DOJ counsel to PERS, and David Heynderickx, then legislative counsel, testified at length on the impropriety of using the contingency reserve to pay expenses which were otherwise assigned to employers. Both argued that this was a breach of elementary trust law as well as potentially placing PERS’ IRS qualification in jeopardy. The legislature ultimately rejected all of those proposed changes to the contingency statute with the exception of subsections (a), (b), and (c), which are part of today’s statute. The limitation in subparagraph (a) which requires that only the portion of the reserve which is funded by employer fund earnings be used to address insolvency of participating public employers is clearly as a result of the Muir and Heynderickx testimony. While (c) gives the board authority to utilize the fund that discretion is subject to the board’s fiduciary obligation to members and that discretion should not be used to pay expenses otherwise assigned to employers consistent with the testimony of Muir and Heynderickx in 2001.

With that background it should be clear that the uses of the contingency reserve under the current statute should be focused on subsections (a), (b), and (c), as given the current size of the fund there is not likely to be a lack of money to pay benefits, which is the focus of subsection (1). With the recent allocation of 2015 earnings the benefits in force reserve has in excess of \$22 billion with an additional \$23 billion in employer accounts available to pay benefits. This should lead to the

conclusion that the current contingency fund is substantially overfunded and that a much smaller fund would be sufficient to meet the needs of subsections (a), (b), and (c).

If the board determines that the current reserve is overfunded, then the historical practice would be to return those funds to the accounts from which they were derived. An exception to that is the specific authorization in ORS 238.670(3) which permits excess funds in the contingency reserve to be paid to a reserve established under subsection (3). Though there has been no recent analysis of the appropriate funding level of the Tier One rate guarantee reserve there would appear to be little question that at the current time it is underfunded. After payment to the Tier Two employee accounts the board should consider whether any additional funds should be paid to the Tier One rate guarantee reserve to assure that it is adequately funded. Certainly at a minimum any funds which would otherwise be returned to Tier One employee accounts should be used to increase the funding of the rate guarantee reserve.

The January 29, 2016 memo to the board on the contingency reserve notes one recent use of the reserve and one pending request for the use of the reserve. The first use of the reserve was the payment of back COLA benefits to retirees as a result of the *Moro* decision. Consistent with basic trust principles that payment should ultimately be charged to the portion of the contingency reserve funded by earnings from the benefits in force reserve as the payment of COLA benefits is specifically assigned by statute to the employers (ORS 238.360(3)).


In settlement of the *City of Eugene* litigation a payment was made from the contingency reserve to certain employers to satisfy a judgment against PERS. In the *White* case the court approved the settlement agreement including a payment from the contingency reserve to satisfy the judgment against PERS, presumably under the authority of ORS 238.670(1)(b). In contrast, in *Moro* the court did not enter a judgment against PERS but only ruled that certain portions of the 2013 legislation were breaches of PERS contracts and set those portions of the legislation aside. There was no judgment against PERS and ORS 238.670(1)(b) provides no authority for the payment from the contingency reserve of COLA benefits. If the board decides that there should be a distribution of funds because the contingency reserve is overfunded then a lower distribution to the benefits in force reserve to take into account the monies already paid would be consistent with the statute and consistent with the board's fiduciary obligation.

The pending request is for an allocation from the contingency reserve to a small group of employers who argue that there was confusion on the appropriate start date for new members of the OPSRP system. They argue that PERS actions added to this confusion and that these confused employers should not be required to fully fund the benefits as required under OPSRP statutes. The board should reject that request if for no other reason than it relates to the OPSRP system which is a separate and distinct part of ORS Chapter 238. It is clear that the contingency fund established by ORS 238.670(1) was never meant to deal with issues relating to the OPSRP system. In addition, to the extent that this request is to compensate employers who did not properly comply with the statute that would run afoul of the board's fiduciary obligation not to use these funds simply to cover expenses otherwise assigned to employers within the system.

Steve Rodeman
February 12, 2016
Page 4

I trust that these comments will be helpful as the board addresses these contingency fund issues.

Yours very truly,



Gregory A. Hartman

GAH:kaj

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cc: Clients

**OREGON STATE SENATE**

Steve Rodeman
Executive Director
Public Employees Retirement System
P.O. Box 23700
Tigard, OR 97281-3700

March 7, 2017

Dear Mr. Rodeman:

In your January 31, 2017, letter to the Joint Committee on Ways and Means you wrote that the system's Contingency Reserve includes \$536.3 million, more than twice what is needed to maintain the fund at the Board's approved level.

Specifically, the letter states that the "Contingency Reserve is currently over-funded by \$345.8 million."

As the chair and vice-chair of the Senate Workforce Committee, we want to ensure that these funds will be used to best improve the health of the PERS system into the future. Toward that end, we request that PERS prioritize the application of the excess funding in the system's Contingency Reserve to the unfunded actuarial liability.

It is our understanding that the Board is scheduled to consider the issue of the excess funds in the Contingency Reserve at its April meeting. It is our strong recommendation that the Board allocate the excess Contingency Reserve funds to other reserve accounts where the funds will be credited toward the unfunded liability.

Sincerely,

Senator Kathleen Taylor
Senate Committee on Workforce
Chair

Senator Tim Knopp
Senate Committee on Workforce
Vice-Chair

cc: John Thomas, Oregon PERS Board, Chair
President Peter Courtney, President of the Senate
Speaker Tina Kotek, Speaker of the House
Senator Ted Ferrioli, Senate Republican Leader
Representative Mike McLane, House Republican Leader
Senator Richard Devlin, Joint Committee on Ways Means, Co-Chair
Representative Nancy Nathanson, Joint Committee on Ways and Means, Co-Chair



OREGON STATE SENATE

PERS
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March 20, 2017

Steve Rodeman
 Executive Director
 Public Employees Retirement System
 P.O. Box 23700
 Tigard, OR 97281-3700

Dear Mr. Rodeman,

On January 31, 2017, the Public Employees Retirement System (PERS) sent a letter to the Co-Chairs of the Joint Committee on Ways and Means stating that the PERS Contingency Reserve has a \$345.8 million surplus.

In the letter, PERS requested input from stakeholders on a proposed reallocation of the surplus funds in advance of the April 3, 2017, PERS Board meeting where suggestions will be compiled and evaluated for the PERS Board's consideration. Below is the Senate Republican Caucus's direction for the PERS Board with respect to the Contingency Reserve surplus.

The \$345.8 million surplus funds must be used in the most meaningful and effective manner possible to both preserve the health of the PERS system and help protect current and future retirees. To that end, the Contingency Reserve surplus should be reallocated to prudently address the PERS unfunded liability and to buy down rates for school districts and local governments. PERS's fiscal solvency requires the Board to do as much.

With these surplus funds, the Board has an opportunity to be proactive and bend down the cost curve on PERS. Inflated PERS costs continue to cause otherwise unnecessary cuts to essential funding for students and teachers, public safety, mental health, health care, seniors, and veterans. Oregonians want to see solutions and this is a judicious way to help maintain funding for these essential services.

It is the Senate Republican Caucus's position that the Board should mindfully devote the \$345.8 million surplus to paying down the unfunded liability. Thank you.

Sincerely,

A handwritten signature in blue ink that reads "Ted Ferrisoli".

Ted Ferrisoli
 Senate Republican Leader
 District 30

A handwritten signature in blue ink that reads "Tim Knopp".

Tim Knopp
 Senate Republican Deputy Leader
 District 27



Oregon

Kate Brown, Governor

Public Employees Retirement System

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Tigard, OR 97281-3700
(503) 598-7377
TTY (503) 603-7766
www.oregon.gov/pers

March 10, 2017

The Honorable Senator Kathleen Taylor, Chair
The Honorable Senator Tim Knopp, Vice-Chair
Senate Committee on Workforce
900 Court St NE, Room 453
Salem, OR 97301

Dear Chair Taylor and Vice Chair Knopp:

Thank you for your letter of March 7, 2016, regarding the PERS Board's pending decision on the allocation of the Contingency Reserve. Your strong recommendation that the Board allocate the excess funding to be credited towards the system's unfunded actuarial liability ("UAL") will be a prominent element in the PERS Board's deliberations on this policy issue.

I must also bring to your attention a Legislative Fiscal Office recommendation that was approved by the Joint Committee On Ways and Means Subcommittee on General Government at their meeting on March 9, 2017. The LFO's recommendation was to direct the PERS Board to report to the Joint Committee on Ways and Means on the Board's specific recommendation as to which accounts the Contingency Reserve funds should be deployed to and the associated rationale.

To comply with LFO's recommendation, the PERS Board will not be able to allocate the Contingency Reserve funds at its upcoming April 3, 2017 meeting but will instead need to adopt an allocation that is contingent to allow for the requested legislative reporting and review. Consequently, any allocation of the Contingency Reserve will not affect system earnings for the 2016 calendar year, as that final crediting decision must be made at the April meeting to allow for member annual statements to proceed and the actuary to begin their work on the 2016 system valuation.

So long as a final decision on allocating the Contingency Reserve funds is made during the 2017 calendar year, and if that allocation is consistent with your recommendation, the delay in implementing that allocation (caused by complying with LFO's recommendation) just means that any unfunded actuarial liability reduction will be recognized in calendar year 2017 instead of calendar year 2016.

As the next cycle of employer rates, to be effective July 1, 2019, will be based on the 2017 system valuation, the UAL reduction will have the same effect as those rates are based on earnings in both calendar year 2016 and 2017.

Please let me know if you have any further questions or would like me to elaborate further on this change in timing of the Contingency Reserve allocation as a result of LFO's recommendation. We appreciate all the attention and deliberation your committee has given to

SLI

Senate Committee on Workforce

March 10, 2017

Page 2 of 2

PERS issues in this session, and your time and effort in developing your recommendation on this issue.

Sincerely,



Steven Patrick Rodeman
Executive Director

cc John Thomas, Oregon PERS Chair
 President Peter Courtney, President of the Senate
 Speaker Tina Kotek, Speaker of the House
 Senator Ted Ferrioli, Senate Republican Leader
 Representative Mike McLane, House Republican Leader
 Senator Richard Devlin, Joint Committee on Ways and Means, Co-Chair
 Representative Nancy Nathanson, Joint Committee on Ways and Means, Co-Chair



Oregon

Kate Brown, Governor

Public Employees Retirement System

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April 3, 2017

TO: Members of the PERS Board

FROM: Mary Dunn, Assistant Chief Administration Officer
Amanda Marble, Financial Reporting Coordinator

SUBJECT: 2016 Final Earnings Crediting and Reserving

OVERVIEW

- Action: Allocate 2016 Final Earnings Crediting

The PERS Board is charged with crediting the earnings from the PERS Fund each calendar year. Some of those allocations are directed by statute or rule; the balance are at the PERS Board's discretion. At the January 27, 2017 meeting, the PERS Board adopted preliminary earnings allocations.

EARNINGS ALLOCATIONS DIRECTED BY STATUTE OR RULE

The following reserves and accounts are allocated earnings by applicable statute or rule. In compliance with these restrictions, the preliminary earnings allocation reflects the following:

1. **Administrative Expenses:** PERS administrative costs are funded by earnings when they are sufficient, as they were in 2016 (ORS 238.610(1)). As directed by House Bill 4155 (2014 Regular Session), the administrative costs to comply with Governmental Accounting Standards Board (GASB) 68 reporting standards were \$190,533, and will be recovered from earnings on employer's contributions.
2. **Heath Insurance Accounts:** These accounts are created as part of the PERS Fund and directed by statute to be credited with actual earnings or losses, less the expense related to the administration of the programs (ORS 238.410(7); 238.415(4); 238.420(4)). For 2016, the final crediting rate for these accounts is 7.07% for RHIA, 3.69% for RHIPA, and 0.62% for SRHIA (invested in the Treasury Short-Term Fund).
3. **Employer Lump Sum Payment Accounts:** These accounts are credited with actual earnings or losses of the PERS Fund Regular Account less administrative expenses, as authorized by ORS 238.225. For 2016, the final crediting rate for these accounts averages 7.65%.
4. **Variable Annuity Account:** This account is credited with earnings and losses on its distinct asset allocation of the PERS Fund. The Variable Annuity Account is only invested in equities and therefore its earnings are discrete from those of the more diversified PERS Fund Regular Account. For 2016, final Variable Annuity Account earnings are 8.76%.
5. **Individual Account Program (IAP):** These member accounts are credited with actual earnings or losses of the PERS Fund Regular Account as required by ORS 238A.350 (1). Final IAP earnings for 2016 are calculated to be 7.13% after deducting IAP expenses.

- 6. Tier One Rate Guarantee Reserve:** This reserve, established under ORS 238.255(1), is used to fund crediting of the assumed rate to Tier One member regular accounts when earnings are less than the assumed rate. A transfer of \$2.4 million from the existing reserve will be credited to Tier One member regular accounts for 2016 earnings crediting, resulting in a remaining balance of \$180.8 million. Over the last two calendar years, this reserve has decreased by 60%.

CONTINGENCY RESERVE ALLOCATION

When the PERS Fund's calendar year earnings exceed the assumed rate, the PERS Board can make an allocation to the Contingency Reserve. Because 2016 earnings did not exceed the assumed earnings rate of 7.50%, the PERS Board cannot allocate any earnings to the Contingency Reserve, but there is an existing balance of \$583.7 million.

At the January 27, 2017 board meeting the PERS Board was presented with the question of excess funding in the Contingency Reserve, and solicited stakeholder feedback. The analysis of that feedback and staff recommendations is addressed in agenda item C.4., Contingency Reserve Excess Funding, and any decision on the options presented under that item will not impact 2016 final earnings crediting.

2016 FINAL ALLOCATIONS

The PERS Board's Annual Earnings Crediting rule (OAR 459-007-0005) directs the crediting to the Judge and Tier Two member regular accounts, as well as the OPSRP Pension Program, Benefits-in-Force, and Employer reserves. Staff recommends the following allocations be adopted by the PERS Board:

Non-Discretionary Allocations

Credit administrative expenses, health insurance accounts, employer lump sum accounts, variable annuity accounts, and accounts in the Individual Account Program in the manner described above. Credit Tier One member regular accounts with the assumed earnings rate (7.50%) in effect during 2016.

Judge Member Accounts

Credit Judge Member Accounts with the assumed earnings rate (7.50%) in effect during 2016.

Tier Two Member Regular Accounts

Tier Two member regular accounts usually are credited with a proportional share of available PERS Fund Regular Account earnings, which results in a rate of 7.15%.

Benefits-in-Force and Employer Reserves

Credit the Benefits-in-Force and Employer Reserves evenly with the remaining available PERS Fund Regular Account earnings. The crediting rate to those accounts is 7.15%.

BOARD ACTION – FINAL EARNINGS CREDITING

The Board's options for 2016 final earnings crediting include:

1. Pass a motion to "adopt the final crediting of earnings as presented for calendar year 2016."
2. Pass a motion adopting an alternative final allocation for 2016.

STAFF RECOMMENDATION

Staff recommends the Board choose Option #1.

Attachment:

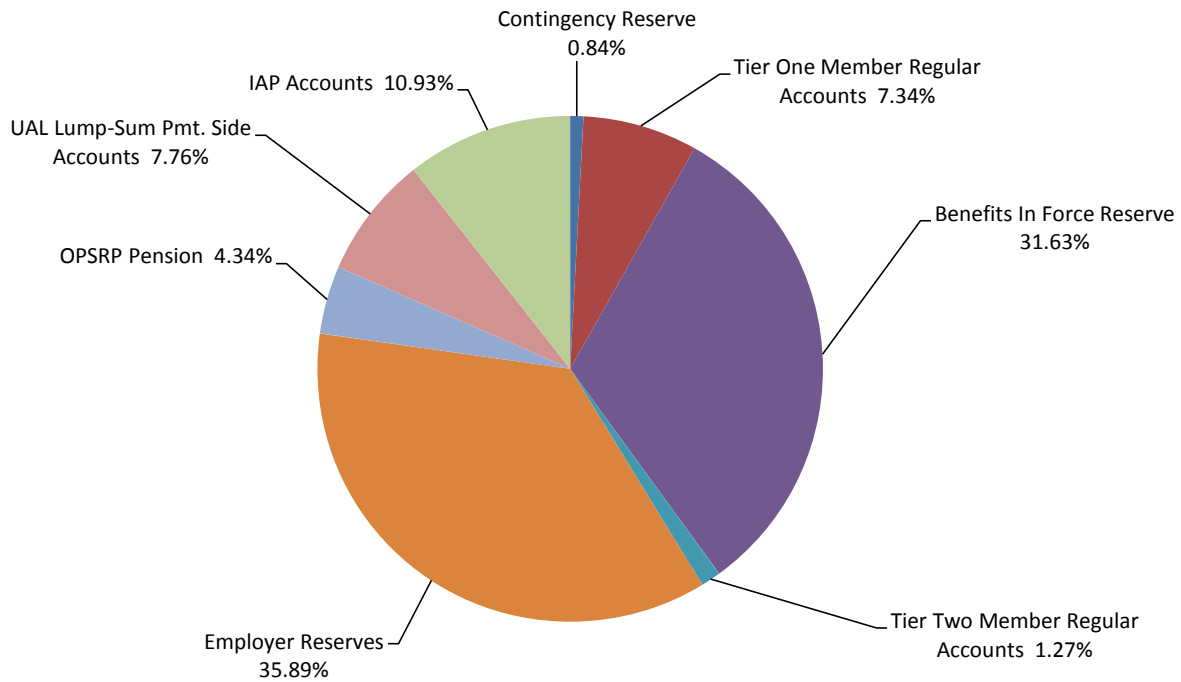
C.5. Attachment 1 – Final 2016 Accounts and Reserves Crediting

Oregon Public Employees Retirement System Final 2016 Crediting and Reserving

(All dollar amounts in millions)

	Reserves Before Crediting	2016 Crediting	Reserves After Crediting	2016 Rates
Contingency Reserve	\$583.7	-	\$583.7	N/A
Tier One Member Regular Accounts	4,547.0	341.0	4,888.0	7.50%
Tier One Rate Guarantee Reserve	183.2	(2.4)	180.8	N/A
Benefits In Force Reserve	20,550.4	1,461.3	22,011.7	7.15%
Tier Two Member Regular Accounts	816.8	58.4	875.2	7.15%
Employer Reserves	23,235.6	1,663.0	24,898.6	7.15%
OPSRP Pension	2,807.8	198.8	3,006.6	7.08%
*UAL Lump-Sum Pmt. Side Accounts	5,005.8	383.2	5,389.0	Various
*IAP Accounts	6,858.5	489.3	7,347.8	7.13%
Total	\$64,588.8	\$4,592.6	\$69,181.4	

2016 Reserve Balances After 2016 Crediting



*Informational only. Not affected by Board reserving or crediting decisions.
IAP accounts receiving installments have already received 2016 earnings.

**ADDITIONAL ITEMS FOR PERS BOARD
April 3, 2017**

Agenda Item C.4.

Letter received from Governor Kate Brown



KATE BROWN
Governor

March 31, 2017

Public Employees Retirement Board
11410 SW 68th Parkway
Tigard, OR 97223

Dear PERS Board Members:

As you know, I have had a number of conversations over the past two years about PERS and how we might address the current Unfunded Actuarial Liability while also ensuring the system is strong moving forward. I appreciate all your work, and the conversations you and your staff have engaged in with me and with my staff on these issues. Thank you for your service to Oregonians.

As I have talked to a number of PERS stakeholders, including public employees and employers, two things have stood out to me as potential changes which, while small, will strengthen the PERS system and may lead to increased rate stability. The first relates to a decision I hope you will make today. The second relates to a structural change I hope you will consider addressing at your May 26, 2017 Board meeting.

Today, you will decide how to allocate excess funds from the Contingency Reserve. Rather than allocating these funds equally across accounts, as you have done at times in the past, I urge you to instead allocate them exclusively to the Benefits in Force Reserve. Given the historic imbalance between the assets in that reserve and the present liability to retired members, your action to bolster that reserve seems to be the most prudent action.

At your next meeting, please discuss options for easing the requirements around the creation of employer side accounts. These accounts offer employers the opportunity to pre-pay for their future obligations to PERS. I have heard from a number of employers that there are barriers to creation of these accounts which force them to hold reserves for predicted PERS rate increases in their own internal accounts. Their own accounts are not always interest bearing, and those that are rarely see the returns gained by the PERS fund.

Public Employees Retirement Board

March 31, 2017

Page 2

Increasing flexibility for public employers to dedicate their resources most efficiently to satisfy their future PERS obligations would maximize their options to resolve this difficult financial situation. Please work with staff to determine how side accounts could be made more accessible to public entities wishing to set aside smaller amounts of funds or to set aside funds on a more frequent basis.

Thank you for your work. I know that you all take seriously your responsibility to oversee our state's public retirement system and I appreciate your diligent work.

Sincerely,

A handwritten signature in black ink that reads "Kate Brown" with a long horizontal flourish extending to the right.

Governor Kate Brown

KB/epg

Cc: Steve Rodeman, Executive Director, Oregon PERS