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Annual Report 2010

Evaluations and Recommendations Regarding the Operations of the State Retirement Systems and Their Funds

128th General Assembly
January 1, 2009 – December 31, 2010

January 2011

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ANNUAL REPORT

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Introduction

The Ohio Retirement Study Council (ORSC) is pleased to submit this report on the five state retirement systems and the fund for volunteer firefighters for the period beginning January 1, 2009 and ending December 31, 2010. This report is submitted pursuant to section 171.04(B) of the Revised Code, which requires the ORSC to *"make an annual report to the governor and the general assembly covering its evaluation and recommendations with respect to the operations of the state retirement systems and their funds"*.

The State of Ohio has a long and successful track record regarding its five statewide retirement systems. The oldest of these retirement systems is the State Teachers Retirement System (STRS), which was created in 1920 for teachers in the public schools, colleges, and universities. The Public Employees Retirement System (PERS) was created in 1935 for state employees, with local government employees added in 1938. The School Employees Retirement System (SERS) was created in 1937 for non-teaching employees of the various local school boards. The Highway Patrol Retirement System (HPRS) was created in 1944 by the withdrawal of all state troopers from PERS. The Ohio Police and Fire Pension Fund (OP&F) was created in 1967 after the abolition of 454 local police and fire relief and pension funds, many of which predated the Social Security System created in 1935 and many of which were on the verge of financial insolvency. A special retirement program administered by PERS was subsequently created in 1975 for certain law enforcement officers, including sheriffs, deputy sheriffs, township police and various others. Today the five systems have combined assets of approximately $149.5 billion (as of January 1, 2010) and approximately 705,000 active contributing members, 664,000 inactive members, and 398,000 beneficiaries and recipients. The February 8, 2010 issue of Pensions and Investments included a list of the top 200 public and private pension funds in the nation. Four of Ohio's five public retirement systems are listed in the top 200. PERS ranked 16th out of all public and private; STRS ranked 18th out of all public and private funds; OP&F ranked 113th; while SERS ranked 125th among all public and private pension funds.

Created in 1968, ORSC was one of the first permanent pension oversight commissions in the nation. The Council was designed to develop legislative leadership in the area of retirement pensions for public employees. Legislators are accustomed to dealing in two-year budgetary cycles, whereas decisions about public pension plans typically involve significant long-term costs, such as 30-year pension obligations. The Council is empowered to make an impartial review of the laws governing the administration and financing of Ohio's five public retirement systems and to recommend to the General Assembly any changes it may find desirable with respect to the allowances and benefits, the sound financing of the cost of benefits, the prudent investments of funds, and the improvement of the language, structure and organization of the laws. It must report to the Governor and the General Assembly concerning its evaluation and recommendations with respect to the operations of the systems. The Council is required to study all statutory changes in the retirement laws proposed to the General Assembly and report to the General Assembly on their probable cost, actuarial implications, and desirability as a matter of public policy.

The Council evaluates the operations of the systems on a continuing basis. During the past year the Council also reviewed the retirement systems' investment performance, operating budgets, and compliance with various provisions of S.B. 133 (eff. 9-15-04). In addition, ORSC staff presented to the Council analyses of legislation and updates on administrative rules filed by the systems. The analyses of legislation always contain staff recommendations and staff makes recommendations regarding changes in proposed administrative rules as needed.

All of the Council's reports and legislative analyses can be found on the Council's website at www.orsc.org. In addition, the website contains links to all five retirement systems, their laws, and various pension-related organizations. Staff recently archived all legislative changes to the laws affecting the ORSC and each retirement system. These archived laws are now available on our website.

This report is a compilation of the evaluations and recommendations the Council made throughout the year. It provides a summary of the ORSC reports completed during 2009 and 2010, pending public retirement issues, and staff recommendations. In addition, it provides a historical record of legislative action taken by the 128th Ohio General Assembly on bills affecting PERS, STRS, SERS, OP&F, HPRS and the Volunteer Fire Fighters' Dependents Fund (VFFDF).

The report is divided into nine sections: Systems' Investment Performance; 30-Year Funding Plans; Status of Health Care Funds; Actuarial Reviews; Reports on Enacted Pension Legislation; Pending Pension-Related Issues; Documents Submitted by the Retirement Systems; Subject Index of Pension Bills Introduced; and Status of Pension Legislation.

The Systems' Investment Performance section provides a summary of the investment performance reviews completed by Evaluation Associates, LLC (a subsidiary of Milliman), during 2009 and 2010. The full reports can be obtained from the ORSC office or on the ORSC website: www.orsc.org.

The 30-Year Funding Plans section details the board-approved funding plans presented by each system to the ORSC. The complete plans can be obtained from the ORSC office or found on the ORSC's website.

The Status of the Health Care Funds provides a summary of the major changes made to the systems' health care benefits for 2011. The summaries of health care plan changes include an overview of changes the systems made relative to prescription drugs, benefits, premiums, eligibility, and plan design. In addition, it provides information regarding the amount of employer contributions that will be allocated to healthcare during 2011.

The Actuarial Reviews section provides a summary of the actuarial reviews completed during 2009 and 2010. The full reports can be obtained from the ORSC office or on the ORSC website.

The Reports on Enacted Pension Legislation section provides a detailed examination of each pension bill enacted into law during the 128th Ohio General Assembly, including the name of the principal sponsor, a description of its contents, its fiscal impact, the ORSC position and its effective date. These reports are intended to give the reader an awareness and understanding of all substantive changes made to the state retirement plans; they are not intended to serve as a substitute for the statutory laws governing these plans.

The Pending Pension-Related Issues section provides a summary of relevant public retirement issues and prior staff recommendations that have been made, but not acted upon by the legislature. It includes a brief summary of the issues and whether any legislation has been introduced this session that addresses the issue.

The Documents Statutorily Required of the Retirement Systems section provides information on all reports that the retirement systems are required by law to submit to the ORSC.

The Subject Index of Pension Bills Introduced provides a listing of legislation under subject headings and a key word description within the subject heading. Bills that cover more than one subject area are listed under all appropriate headings. All subject headings are listed at the beginning of the index for quick reference.

The Status of Pension Legislation provides a record of the legislative action taken on pension bills at each step of the legislative process from the date of introduction to the date of enactment, including the committee assignments in each house of the Ohio General Assembly, the date reported by the committees, the date passed by each house and the date reported by a conference committee and/or concurred in by the other house. Also provided are a brief description of the subject of the pension bill and the ORSC position on the bill. A key to all abbreviations used in the Status of Pension Legislation is found on the last page.

SYSTEMS' INVESTMENT PERFORMANCE

THE 128TH GENERAL ASSEMBLY

JANUARY 1, 2009 – DECEMBER 31, 2010

Section 171.04(D) of the Revised Code requires the ORSC to conduct a semiannual review of the policies, objectives, and criteria of the systems' investment programs. The ORSC has hired Evaluation Associates, LLC to conduct the reviews. These reports are submitted to the Governor and General Assembly. The following is a summary of the investment reviews completed during 2009 and 2010:

Investment Performance Review (Fourth Quarter 2008), April 8, 2009 -
This report, which was presented at the April 8, 2009 ORSC meeting, reflects the investment performance for all five retirement systems over the ten-year period beginning January 1, 1999 and ending December 31, 2008. The findings of this report are summarized as follows:

- During the third and fourth quarters of 2008, every area of the financial markets was plagued by the credit crisis that began over a year earlier. As a result, all of the systems posted severe declines in the second half of 2008. Returns for the six-month period ranged from -21.73% (PERS DB) to -23.76% (STRS). The systems benefited from relatively strong fixed income markets during the six months ending December 31, 2008.

- Four of the five systems lagged their respective policy index for the six-month period. HPRS outpaced its benchmark by 216 basis points. OP&F trailed its benchmark index by six basis points. PERS DB and STRS trailed their benchmarks by 27 and 44 basis points, respectively. SERS underperformed its policy benchmark by 225 basis points.

- In comparison to a broad universe of other public retirement systems (the Mellon All Public Total Fund Universe), four of five plans ranked below median for the six-month period ending December 31, 2008. PERS ranked in the 46th percentile among its peers, SERS ranked in the 59th percentile, HPRS ranked in the 64th percentile, OP&F ranked in the 75th percentile and STRS ranked in the 77th percentile.

- For the one-year period, two of the five plans outperformed their respective policy benchmark returns. HPRS outpaced its policy index by 306 basis points, OP&F outperformed its benchmark by 84 basis points, PERS HC lagged its benchmark by 160 basis points. Relative to their peers in the Mellon All Public Total Fund Universe, all five plans fell below the median, with PERS placing in the 58th percentile among its peers. The remaining four funds placed in the 69th, 72nd, 77th and 85th percentiles (SERS, OP&F, HPRS and STRS, respectively).

- On a three-year basis, all systems posted negative returns. HPRS, OP&F and STRS outperformed their policy benchmarks by 144, 90 and 30 basis points, respectively. SERS lagged its benchmark by 59 basis points, while PERS DB and HC trailed their benchmarks by 3 and 82 basis points, respectively.

- Comparing the three-year returns of the systems to the Mellon All Public Total Fund Universe, only one plan ranked above the median. OP&F ranked in the 37th percentile followed by PERS, SERS, STRS and HPRS which ranked in the 52nd, 52nd, 56th and 78th percentiles, respectively.

- For the five-year period, all systems posted positive returns, and four of the five systems outpaced their respective policy benchmarks with HPRS outperforming by 105 basis points. In comparison to the Mellon All Public Total Fund Universe, STRS (+2.87%), OP&F (+2.64%), SERS (+2.48%) and PERS (+2.33%) ranked in the second quartile. HPRS (+1.34%) ranked in the third quartile.

- Over the ten-year period, all five plans posted positive returns, but underperformed their actuarial interest rate assumption. The ten-year returns were greatly impacted by poor equity markets in 2000, 2001, 2002, and 2008. However, all five plans outperformed their respective policy benchmarks over ten years. HPRS outpaced its benchmark by 114 basis points, OP&F returned +3.33%, while STRS returned +3.30% and SERS returned +3.00% over a ten-year period. For the ten-year period, performance results versus the Mellon All Public Total Fund Universes are mixed. OP&F ranked in the 53rd percentile, STRS (56th percentile), SERS (77th percentile), PERS DB (78th percentile), and HPRS (92nd percentile).

- During the ten years that we have been reviewing the results of the systems on behalf of the Council, the asset allocation targets became more similar and were reasonably close to each other. The obvious exception is PERS HC. The retirement plans all have actuarial return assumptions of 8.00% to 8.25% while PERS HC has a lower actuarial interest rate assumption than the others, at 6.7%. As a result, PERS HC has a lower equity and higher fixed income allocation than the retirement plans. This similarity in policy makes comparing one system's results to the other a more meaningful exercise over the more recent time periods. Changes to asset allocation policy by HPRS, PERS DB and PERS HC, will likely cause some comparison differences in the near future. HPRS has decreased its domestic equity exposure while PERS DB has slightly decreased domestic equity exposure and slightly increased alternatives exposure. PERS HC has decreased fixed income exposure and increased its equities exposure.

- Please note that comparing investment performance relative to the plans' actuarial interest rate assumption and policy benchmark are of primary importance, while peer group comparisons, although useful, should be of secondary importance in evaluating investment performance. In addition, since the plans have long-term funding schedules and investment time horizons, more emphasis should be placed on evaluating performance over longer holding periods.

- Appendix 1.1 and 1.2 at the end of this report compares the current and target asset allocation of each of the systems to two public fund universes, the total universe of public funds and the universe of public funds in excess of $1 billion. The following observations are based on a review of the systems' asset allocation in comparison to those peer universes:
    1. The actual and target asset allocation of PERS DB, STRS, OP&F, and HPRS domestic equity rank above the median plan's allocation to domestic equity (33.73%) in the Mellon All Public Total Fund Universe. The SERS actual (26.94%) and target (29.00%) allocation, as well as the PERS HC actual (25.20%) and target (29.00%) allocation to domestic equity are below that of

the median plan. The same holds true when the systems are compared to the median (32.87%) of the Mellon Billion Dollar Public Total Fund Universe.

2. The systems' actual and target asset allocation to fixed income are below the median plan (30.09%) of the Mellon All Public Total Fund Universe. PERS HC is the exception with a target (42.00%) and actual allocation (45.30%) well above the median.
3. The median plan allocation of the Mellon All Public Total Fund Universe to non-U.S. equity as of December 31, 2008 was 15.79%. The target allocation for HPRS is slightly below the median at 15.00%, and its actual allocation was about 13.42%. The target allocations for the remaining plans were well above the median, with the actual allocations following suit.
4. The universe median allocation to real estate of the Mellon All Public Total Fund Universe was 7.83%. The target allocation of each of the systems besides HPRS (5.00%) and PERS HC (6.00%) is above the median allocation. All plans except HPRS and PERS HC are maintaining a current allocation above their respective targets.
5. HPRS has actual and target allocations to alternatives above the peer median of 10.26%. All other plans have lower target allocations to alternative assets.

- We have made a number of changes to this report. First and foremost, we outlined the report such that each plan's information is grouped together and easily accessible. In addition, you will notice that a former section of this report titled Appendix: ORSC Performance Attribution has been removed. In our goal to provide the most appropriate and precise information possible, we have determined that revisiting this section of the report with regard to the methodology of the underlying calculations is warranted and the format in which the data is presented could be enhanced. This section will be included in the June 30, 2009 report. Additionally, we will be re-examining the report in more detail to determine if there are any additional enhancements that should be made. Overall, we believe this report provides the ORSC with a consolidated source of valuable information to assist in its oversight of the five Ohio Statewide pension funds. These reports have provided important high level information to enable the ORSC to evaluate the performance of the plans, and to better understand the impact of the plans' investment policy, and the effectiveness of the implementation of those policies, on total fund performance. In other words, have the investment policies and the implementation of those policies met the objectives of the plans? In order to assist in the oversight duties of the ORSC, we continue to work with the HPRS in this regard.

- Looking forward, the current global financial crisis may have a protracted effect on the pension funds. Our economic outlook does not bode well for the financial markets and pension funds in the foreseeable future. A global economic recovery may not begin until 2010 and it may be sluggish. This economic outlook may exacerbate the funding challenges for the plans. In light of the low investment returns experienced over the past ten years, combined with our economic outlook, the systems should re-evaluate investment, funding, and benefits policies. Potential changes to the Boards' long-term investment policies may include further diversification into alternative investments including real estate, hedge funds, private equity, commodities, and infrastructure. Changes to funding policies may include raising the contribution rates. Changes to benefits policies may include changes in plan eligibility or plan design.

Investment Performance Review (Second Quarter 2009), October 14, 2009 – This report, which was presented at the October 14, 2009 ORSC meeting, reflects the investment performance for all five retirement systems over the ten-year period beginning July 1, 1999 and ending June 30, 2009. The findings of this report are summarized as follows:

- During the first and second quarters of 2009, the financial markets experienced mixed results. During the first two months of the new year, the market continued its freefall. Unexpectedly, March 9th saw markets show signs of life, with low quality, high beta companies leading the market into recovery. Since March, the equity markets have experienced sustained growth in connection with improving consumer sentiment. Equities performed well, as the MSCI EAFE Index gained 7.95% and the Wilshire 5000 Index rose 4.45% over the last six months. Plan returns for the six-month period ranged from +6.61% (PERS HC) to +1.06% (SERS).

- Three of six systems lagged their respective policy index for the six-month period. The best relative performers were PERS DB and HPRS, outpacing their benchmarks by 83 and 43 basis points, respectively. PERS HC was the best absolute performer, gaining 6.61% over the last two quarters, and outpacing its benchmark by 31 basis points. OP&F gained 3.99%, STRS gained 2.76% and SERS gained 1.06%, but each lagged their custom benchmark by 83, 102 and 52 basis points, respectively.

- In comparison to a broad universe of other public retirement systems (the Mellon All Public Total Fund Universe), two of six plans ranked ahead of the median for the six-month period ending June 30, 2009. PERS HC ranked in the 16th percentile among its peers and HPRS ranked in the 19th percentile. Ranking below the median were OP&F (51st percentile), PERS DB (62nd percentile), STRS (67th percentile) and SERS (89th percentile).

- For the one-year period ending June 30, 2009, PERS DB outpaced its benchmark by 38 basis points. PERS HC had the best absolute performance, returning -16.96% but lagging its benchmark by 58 basis points. Against their peers in the Mellon All Public Total Fund Universe, five of six plans fell below the median, with PERS HC placing in the 40th percentile among its peers. The remaining five funds placed in the 56th, 67th, 80th, 85th and 86th percentiles (HPRS, PERS DB, OP&F, STRS and SERS, respectively).

- On a three-year basis, OP&F and PERS DB bested their policy benchmarks by 42 and 34 basis points, respectively. STRS, PERS HC, SERS and HPRS lagged their benchmarks by five, 78, 97 and 150 basis points, respectively. Comparing the three-year returns of the systems to the Mellon All Public Total Fund Universe, only one plan ranked above the median. PERS HC ranked in the 48th percentile, followed by OP&F, PERS DB, HPRS, STRS and SERS, which ranked in the 61st, 66th, 73rd, 79th and 85th percentiles, respectively.

- For the five-year period, three of the five systems outpaced their respective policy benchmarks with STRS and OP&F each outperforming their benchmark by 39 basis points. In comparison to the Mellon All Public Total Fund Universe, STRS (+2.69%) and OP&F (+2.66%) ranked in the second quartile. PERS DB (+2.32%), SERS (+2.02%), and HPRS (+1.76%) ranked in the third quartile.

- Over the longer-term, ten-year period, all five plans have trailed their actuarial interest rate. The ten-year numbers have suffered greatly due to recent market conditions. Nevertheless, when compared to each system's respective policy benchmark all five plans have outperformed their individual benchmarks, except HPRS. Over the ten-year period, HPRS underperformed their respective policy benchmark by 1.14%. OP&F returned +3.11%, while PERS DB returned +2.79%, STRS returned +2.71%, SERS returned +2.40% and HPRS returned +2.31% over a ten-year stretch.

- During the ten years that we have been reviewing the results of the systems on behalf of the Council, the asset allocation targets became more similar and were reasonably close to each other. The obvious exception is PERS HC. It is important to note that they have a lower actuarial interest rate target than the others, at 6.7%. The retirement plans all have actuarial return assumptions of 8.00% to 8.25%. As a result, PERS HC has a lower equity and higher fixed income allocation than the retirement plans. This similarity in policy makes comparing one system's results to the other a more meaningful exercise over the more recent time periods. Changes to asset allocation policy during the most recent six-month period by STRS and SERS, will likely cause some comparison differences in the near future. STRS has slightly decreased its equity exposure and increased exposure to alternative investments. Likewise SERS has decreased its equity exposure, and increased its allocation to alternatives.

  Please note that comparing investment performance relative to the plans' actuarial interest rate and policy benchmark are of primary importance, while peer group comparisons, although useful, should be of secondary importance in the performance evaluation process. In addition, since the plans have long-term funding schedules and investment time horizons, more emphasis should be placed on evaluating performance over longer holding periods.

- Appendix 1.1 and 1.2 at the end of this report compares the current and target asset allocation of each of the systems to two public fund universes, the total universe of public funds and the universe of public funds in excess of $1 billion. The following observations are based on a review of the systems' asset allocation in comparison to those peer universes:
  1. The actual and target asset allocation of PERS DB, STRS, OP&F, and HPRS domestic equity rank above the median plan's allocation to domestic equity (38.02%) in the Mellon All Public Total Fund Universe. The actual (27.40%) and target (27.50%) allocation of SERS, as well as the actual (27.74%) and target (29.00%) allocation of PERS HC to domestic equity are below that of the median

plan. The same holds true when the systems are compared to the median (36.34%) of the Mellon Billion Dollar Public Total Fund Universe.

2. Five of the six systems' actual and target asset allocation to fixed income are below the median plan (29.23%) of the Mellon All Public Total Fund Universe. PERS HC is the exception with a target (42.00%) and actual allocation (39.59%) well above the median.
3. The median plan allocation of the Mellon All Public Total Fund Universe to non-U.S. equity as of June 30, 2009 was 17.21%. The target allocation for HPRS is slightly below the median at 15.00%, and its actual allocation was slightly less at 13.93%. The target allocations for the remaining plans were well above the median, with the actual allocations following suit.
4. The universe median allocation to real estate of the Mellon All Public Total Fund Universe was 7.99%. The target allocation of each of the systems besides HPRS (5.00%) and PERS HC (6.00%) is above the median allocation. Following their target allocations, all plans except HPRS and PERS HC are maintaining a current allocation near their respective targets.
5. HPRS has actual and target allocations to alternatives above the peer median of 8.52%. While SERS has an above-median target (10.00%), the actual allocation (7.74%) falls below. The remaining plans have lower target allocations to alternative assets.

- For performance reporting purposes, the asset allocation benchmarks are consistent with investment policy asset allocations for all plans, except for HPRS. The HPRS asset allocation benchmarks in this report were changed by HPRS on January 1, 2009 and do not reflect the actual asset allocation of the plan assets. Alternative investments and real estate were included in the U.S. equity allocations, which we do not believe is appropriate. As a result, the relative performance of the HPRS fund is inaccurate. If the asset allocation benchmarks of the HPRS plan (page 56) were consistent with the investment policy allocations (page 8), the plan would have outperformed the policy benchmark by 90 basis points (versus 43 basis points) for the past two quarters, and underperformed by 196 basis points (versus underperforming by 204 basis points) for the one year period ending June 30, 2009. We recommend that HPRS follow best practices along with the other plans by keeping consistency between the asset allocation benchmarks and policy allocations.

- One of the primary purposes of this report is to provide an accurate representation of plan performance of the Ohio Retirement Systems and to provide an "apples to apples" comparison of the Retirement Systems' investment results. In order for this performance report to fulfill this purpose, it is necessary that each plan provide accurate information over a rolling ten-year period. During this review we discovered inaccuracies in the data provided and reviewed by HPRS. The accuracy of the data provided by each plan consultant or custodian, and the thorough review of data presented by plan sponsors are fundamental to the integrity of this performance report. In light of these issues, we recommend a fiduciary audit of the HPRS investment program to evaluate current policies and procedures relative to industry best practices be made pursuant to section R.C. 171.04 (F), which requires a fiduciary audit once every ten years.

- Overall, we believe this report provides the ORSC with a consolidated source of valuable information to assist in its oversight of the five Ohio Statewide pension funds and ensure that investment policies are consistently and effectively implemented. While the report does not provide very specific underlying portfolio detail, it does provide the necessary information to allow the ORSC to ask the right questions and act as an early indicator of potential issues that should be delved into in more detail. Any modifications to the report will only serve to enhance that ability.

<u>Investment Performance Review (Fourth Quarter 2009, April 14, 2010)</u> -
This report, which was presented at the April 14, 2010 ORSC meeting, reflects the investment performance for all five retirement systems over the ten-year period beginning January 1, 2000 and ending December 31, 2009. The findings of this report are summarized as follows:

- During the third and fourth quarters of 2009, the financial markets continued their strong rebound. As a gauge of the strength of the rally, the Wilshire 500 finished +22.8% and the MSCI EAFE gained 22.1% for the last two quarters of 2009. However, unemployment (roughly 10.0%) and housing statistics remain a concern despite an increase in existing home sales. In non-U.S. markets, unemployment is also an issue in spite of rapid GDP growth in emerging markets countries. Japan's central bank acknowledged the beginning of a deflationary period while other nations began discussing means to combat inflation. The Ohio Statewide pension fund returns for the six-month period ranged from +15.15% (SERS) to +17.06% (PERS HC).
- Three of six systems lagged their respective policy index for the six-month period. The best relative performers were HPRS and STRS, outpacing their benchmarks by 122 and 50 basis points, respectively. PERS HC was the best absolute performer, gaining 17.06% over the last two quarters, and outpaced its benchmark by 30 basis points. OP&F gained 16.09%, PERS DB gained 15.61% and SERS gained 15.15%, but each lagged their custom benchmark by 120, 182 and 148 basis points, respectively.
- In comparison to a broad universe of other public retirement systems (the BNY Mellon All Public Total Fund Universe), five of six plans ranked ahead of the median for the six-month period ending December 31, 2009. PERS HC ranked in the 23rd percentile, HPRS ranked in the 39th percentile, STRS ranked in the 40th percentile, OP&F ranked in the 44th percentile and PERS DB ranked in the 47th percentile among its peers. Ranking below the median was SERS, which placed in the 55th percentile.
- For the one-year period ending December 31, 2009, HPRS (+23.22%) outpaced its benchmark by 223 basis points. PERS HC had the best absolute performance, returning +24.80% and had the second-best relative performance, outperforming its benchmark by 69 basis points. Against their peers in the BNY Mellon All Public Total Fund Universe, three of six plans placed above the median, with PERS HC placing in the 14th percentile among its peers. The remaining five funds placed in the 26th, 41st, 51st, 54th and 78th (HPRS, OP&F, STRS, PERS DB and SERS, respectively).

- On a three-year basis, OP&F and STRS were the best relative performers, despite lagging their benchmarks by six and 17 basis points, respectively. PERS DB, PERS HC, HPRS and SERS lagged their benchmarks by 20, 71, 121 and 138 basis points, respectively. Comparing the three-year returns of the systems to the BNY Mellon All Public Total Fund Universe, only one plan ranked above the median. PERS HC ranked in the 32nd percentile, followed by OP&F, HPRS, PERS DB, STRS and SERS, which ranked in the 58th, 62nd, 68th, 77th and 79th percentiles, respectively.
- For the five-year period, three of the six systems outpaced their respective policy benchmarks with STRS and OP&F outperforming their benchmark by 36 and six basis points, respectively. In comparison to the BNY Mellon All Public Total Fund Universe, STRS (+3.99%), OP&F (+3.98%) and PERS HC (+3.82%) ranked in the second quartile. PERS DB (+3.51%), SERS (+3.33%), and HPRS (+3.13%) ranked in the third quartile.
- Over the longer-term, ten-year period, all five plans trailed their actuarial interest rate. When compared to each system's respective policy benchmark three of five plans have outperformed their individual benchmarks. Over the ten-year period, OP&F, STRS and HPRS outperformed their benchmarks by 38, 29 and 19 basis points, respectively. PERS DB and SERS trailed their benchmarks by one and eight basis points, respectively.
- During the ten years that we have been reviewing the results of the systems on behalf of the Council, the asset allocation targets became more similar and were reasonably close to each other. The obvious exception is PERS HC. It is important to note that they have a lower actuarial interest rate target than the others, at 6.7%. The retirement plans all have actuarial return assumptions of 8.00% to 8.25%. As a result, PERS HC has a lower equity and higher fixed income allocation than the retirement plans. This similarity in policy makes comparing one system's results to the other a more meaningful exercise over the more recent time periods. Changes to asset allocation policy during the most recent six-month period by PERS HC, PERS DB, STRS and OP&F will likely cause some comparison differences in the near future.
- Please note that comparing investment performance relative to the plans' actuarial interest rate and policy benchmark are of primary importance, while peer group comparisons, although useful, should be of secondary importance in the performance evaluation process. In addition, since the plans have long-term funding schedules and investment time horizons, more emphasis should be placed on evaluating performance over longer holding periods.
- Appendix 1.1 and 1.2 at the end of this report compares the current and target asset allocation of each of the systems to two public fund universes, the total universe of public funds and the universe of public funds in excess of $1 billion. The following observations are based on a review of the systems' asset allocation in comparison to those peer universes:
    1. The actual and target asset allocation of PERS DB and HPRS domestic equity rank above the median plan's allocation to domestic equity (40.96%) in the BNY Mellon All Public Total Fund Universe. The actual (29.76%) and target (27.50%) allocation of SERS, the actual (29.62%) and target (29.40%) allocation of PERS HC, as well as the actual (38.47%) and target (39.00%) allocation of STRS to domestic equity are below that of the median plan. For

OP&F, the actual (42.63%) was above the median, while the target (39.00%) was below.

2. Five of the six systems' actual and target asset allocation to fixed income are below the median plan (28.38%) of the BNY Mellon All Public Total Fund Universe. PERS HC is the exception with a target (40.00%) and actual allocation (38.30%) well above the median.
3. The median plan allocation of the BNY Mellon All Public Total Fund Universe to non-U.S. equity as of December 31, 2009 was 18.14%. The target allocation for HPRS is slightly below the median at 15.00%, and its actual allocation was slightly less at 14.98%. The target allocations for the remaining plans were well above the median, with the actual allocations following suit.
4. The universe median allocation to real estate of the BNY Mellon All Public Total Fund Universe was 5.93%. The target allocation of each of the systems with the exception of HPRS (5.00%) is above the median allocation. In addition, the HPRS actual allocation (1.69%) was below the median while the actual allocations for the remaining systems were above.
5. HPRS has actual (17.74%) and target (15.00%) allocations to alternatives above the peer median of 9.03%. While SERS has an above-median target (10.00%), the actual allocation (7.74%) falls below. The remaining plans have lower target allocations to alternative assets.

- Overall, we believe this report provides the ORSC with a consolidated source of valuable information to assist in its oversight of the six Ohio Statewide funds and ensure that investment policies are effectively implemented. While the report does not provide very specific underlying portfolio detail, it does provide the necessary information to allow the ORSC to ask the right questions and act as an early indicator of potential issues that should be delved into in more detail. Any modifications to the report will only serve to enhance that ability.
- For performance reporting purposes, the asset allocation benchmarks in this report are generally consistent with investment policy asset allocations for all plans. As we previously stated, one of the primary purposes of this report is to provide an accurate representation of plan performance of the Ohio Retirement Systems and to provide an "apples to apples" comparison of the Retirement Systems' investment results. In order for this performance report to fulfill this purpose, it is necessary that each plan provide accurate information. In light of the increased complexity of the plans' portfolios, in part due to diversification into alternative investments, we will review current performance benchmarking practices and make recommendations to ensure consistent and transparent reporting for all plans in subsequent performance reports.
- Despite strong investment returns in 2009 and some early signs of positive economic development in 2010, we are cautiously optimistic on the global financial markets in the foreseeable future. In light of the low investment returns experienced over the past ten years, combined with our economic outlook, the Systems should continue to re-evaluate investment, funding, and benefits policies. Potential changes to the Boards' long-term investment policies may include further diversification into alternative investments including hedge funds, private equity, commodities, and infrastructure. Changes to funding policies may include raising the contribution rates. Changes to benefits policies may include changes in plan eligibility or plan design.

- The Systems' investment policies are changing and we will, of course, continue to review any changes and proposed changes to the Systems' investment policies and report them to the ORSC in subsequent performance reports.

Investment Performance Review (Second Quarter 2010, November 10, 2010) - This report, which was presented at the November 10, 2010 ORSC meeting, reflects the investment performance for all five retirement systems over the ten-year period beginning July 1, 2000 and ending June 30, 2010. The findings of this report are summarized as follows:

- During the first and second quarters of 2010, the financial markets experienced mixed results. As a gauge of the marketplace, the Wilshire 5000 finished -5.83% and the MSCI EAFE fell -13.23% for the first two quarters of 2010. Domestically, the second quarter was the most volatile period since March 2009 as the VIX peaked at 45.8 in May. Retail markets were sluggish and housing activity dropped due to the expiration of the first time buyers tax credit. Internationally, Europe's sovereign debt crisis continues to rattle investors, despite the nearly $1 trillion rescue package; the euro slid 9.42% against the U.S. dollar. In fixed income, interest rates declined and the yield curve flattened on investor risk aversion and flight to quality flows on concerns over the sustainability of economic growth. Short-term rates remained anchored near zero and longer term rates fell; the Federal Reserve has indicated it is still committed to keeping rates low and has not yet signaled the start of the rate-raising cycle.
- The Ohio Statewide fund returns for the six-month period ranged from -1.95% (HPRS) to -2.78% (PERS HC). Four of six systems outperformed their respective policy index for the six-month period. The best relative performers were OP&F (-2.38%) and PERS HC (-2.78%), outperforming their benchmarks by 100 and 33 basis points, respectively. HPRS was the best absolute performer, falling -1.95% over the last two quarters, and outpaced its benchmark by 28 basis points. PERS DB fell -2.51% and outperformed its benchmark by six basis points, STRS fell -2.39% and trailed its benchmark by 20 basis points and SERS lost -2.47% and trailed its benchmark by 82 basis points.
- In comparison to a broad universe of other public retirement systems (the BNY Mellon All Public Total Fund Universe), all of the plans ranked in the third quartile for the six-month period ending June 30, 2010. HPRS ranked in the 53rd percentile, OP&F and STRS ranked in the 66th percentile, SERS ranked in the 68th percentile, PERS DB ranked in the 71st percentile and PERS HC ranked in the 77th percentile.
- For the one-year period ending June 30, 2010, HPRS (+14.09%) outperformed its benchmark by 153 basis points. PERS HC (+13.81%) outperformed its benchmark by 68 basis points, STRS (+13.54%) outperformed its benchmark by 26 basis points, and OP&F (+13.33%) was in line with its benchmark. Against their peers in the BNY Mellon All Public Total Fund Universe, three of six plans placed above the median, with HPRS placing in the 40th percentile among its peers. The remaining five funds placed in the 45th, 48th, 53rd, 62nd and 66th percentiles (PERS HC, STRS, OP&F, PERS DB and SERS, respectively).
- On a three-year basis, OP&F and STRS were the best relative performers, despite lagging their benchmarks by eight and 30 basis points, respectively. PERS DB, PERS HC, HPRS and SERS lagged their benchmarks by 36, 68, 110 and 208 basis points,

respectively. Comparing the three-year returns of the systems to the BNY Mellon All Public Total Fund Universe, only one plan ranked above the median. PERS HC ranked in the 33rd percentile, followed by HPRS, OP&F, PERS DB, STRS and SERS, which ranked in the 66th, 72nd, 73rd, 82nd and 88th percentiles, respectively.

- For the five-year period, three of the six systems outpaced their respective policy benchmarks with STRS, OP&F and PERS DB outperforming their benchmark by 28, 22 and four basis points, respectively. In comparison to the BNY Mellon All Public Total Fund Universe, OP&F (+3.12%) and PERS HC (+3.01%) ranked in the second quartile while STRS (+2.92%) was in-line with the median manager in the Universe. PERS DB (+2.73%), HPRS (+2.59%), and SERS (+2.35%) ranked in the third quartile.
- Over the three, five and ten-year periods, all five plans trailed their actuarial interest rate. When compared to each system's respective policy benchmark, four of five plans outperformed their individual benchmarks. Over the ten-year period, OP&F (+3.57%), STRS (+3.00%), HPRS (+3.34%) and PERS DB (+3.16%) outperformed their benchmarks by 41, 28, 22 and six basis points, respectively and SERS trailed its benchmarks by 30 basis points. Relative to the peer group universe, OP&F, HPRS, PERS DB, STRS and SERS placed in the 37th, 47th, 59th, 66th, and 90th percentiles, respectively over the ten-year period.
- Please note that comparing investment performance relative to the plans' actuarial interest rate and policy benchmark are of primary importance, while peer group comparisons, although useful, should be of secondary importance in the performance evaluation process. In addition, since the plans have long-term funding schedules and investment time horizons, more emphasis should be placed on evaluating performance over longer holding periods.
- During the ten-plus years that we have been reviewing the results of the systems on behalf of the Council, the asset allocation targets have became more similar and are reasonably close to each other. The obvious exception is PERS HC. It is important to note that they have a lower actuarial interest rate target than the others, at 6.7%. The retirement plans all have actuarial return assumptions of 8.00% to 8.25%. As a result, PERS HC has a lower equity and higher fixed income allocation than the retirement plans. This similarity in policy makes comparing one system's results to the other a more meaningful exercise over the more recent time periods. Changes to asset allocation policy during the most recent six-month period by PERS HC, PERS DB, STRS and OP&F will likely cause some comparison differences in the near future.
- Appendix 1.1 and 1.2 at the end of this report compares the current and target asset allocation of each of the systems to two public fund universes, the total universe of public funds and the universe of public funds in excess of $1 billion. The following observations are based on a review of the systems' asset allocation in comparison to those peer universes:
    1. The actual and target asset allocation of HPRS domestic equity ranks above the median plan's allocation to domestic equity (40.32%) in the BNY Mellon All Public Total Fund Universe. For OP&F, the actual domestic allocation (41.30%) was above the median, while the target domestic allocation (39.00%) was below the median. The actual (23.85%) and target (27.50%) allocation of SERS, the actual (36.90%) and target (39.61%) allocation of PERS DB, the actual (30.14%) and target (31.90%) allocation of PERS HC, as

well as the actual (38.31%) and target (39.00%) allocation of STRS to domestic equity are below that of the median plan. As an important note, SERS has 10.3% allocated to Hedge Funds included in its U.S. Equity and Fixed Income policy target.

2. Five of the six systems' actual and target asset allocation to fixed income are significantly below the median plan (32.36%) of the BNY Mellon All Public Total Fund Universe. PERS HC is the exception with a target (34.00%) and actual allocation (32.92%) above the median.
3. The median plan allocation of the BNY Mellon All Public Total Fund Universe to non-U.S. equity as of June 30, 2010 was 15.87%. The target allocation for HPRS is slightly below the median at 15.00%, and its actual allocation was slightly less at 13.91%. The target allocations for the remaining plans were significantly above the median, with the actual allocations following suit.
4. The universe median allocation to real estate of the BNY Mellon All Public Total Fund Universe was 5.36% as of June 30, 2010. The target allocation of each of the systems, with the exception of HPRS (5.00%), is above the median allocation. In addition, the HPRS actual allocation (2.58%) was below the median while the actual allocations for the remaining systems were above.
5. HPRS has actual (19.23%) and target (15.00%) allocations to alternatives above the peer median of 10.54%. While SERS has target (10.00%) close to the median, its actual allocation, which includes Hedge Funds from its U.S. Equity and Fixed Income allocations, is well ahead of the median (19.34%). The remaining plans have lower target allocations to alternative assets.

- Overall, we believe this report provides the ORSC with a consolidated source of valuable information to assist in its oversight of the six Ohio Statewide funds and ensure that investment policies are effectively implemented. While the report does not provide very specific underlying portfolio detail, it does provide the necessary information to allow the ORSC to ask the right questions and act as an early indicator of potential issues that should be delved into in more detail. Any modifications to the report will only serve to enhance that ability.
- For performance reporting purposes, the asset allocation benchmarks in this report are generally consistent with investment policy asset allocations for all plans. As we previously stated, one of the primary purposes of this report is to provide an accurate representation of plan performance of the Ohio Retirement Systems and to provide an "apples to apples" comparison of the Retirement Systems' investment results. In order for this performance report to fulfill this purpose, it is necessary that each plan provide accurate information. In light of the increased complexity of the plans' portfolios, we have divided the "alternative investment" performance table into separate and distinct categories including private equity, hedge funds, and "other." Footnotes have been added to provide clarity. We will continue to review current performance benchmarking practices and make recommendations to ensure consistent and transparent reporting for all plans in subsequent performance reports.
- In light of the low investment returns experienced over the past three, five and ten-year year periods, the Systems should continue to re-evaluate investment, funding, and benefits policies. Potential changes to the Boards' long-term investment policies may include further diversification into alternative investments including hedge

funds, private equity, commodities, and infrastructure. Changes to funding policies may include raising the contribution rates. Changes to benefits policies may include changes in plan eligibility or plan design. (Please see page 12 for investment returns and actuarial interest rate assumptions.)

30-YEAR FUNDING PLANS

THE 128TH GENERAL ASSEMBLY

JANUARY 1, 2009 – DECEMBER 31, 2010

Pursuant to S.B. 82 (eff. 12-6-1996), each retirement system whose funding period exceeds 30 years in any given year is required to submit to the ORSC and the standing committees of the house and senate with primary responsibility for pension legislation a plan approved by the retirement board that reduces the funding period to no more than 30 years, along with any progress made by the board in meeting the 30-year funding period. This standard was modeled after the national standard adopted by the Governmental Accounting Standards Board for all governmental pension plans. The change was intended to maintain inter-generational equity among taxpayers and system members by limiting the ability to fund benefit costs by extending the funding period beyond 30 years. The following table summarizes the funding period and funded ratio of each retirement system as reported in its last actuarial valuation[1]:

Retirement System	Funding Period	Funded Ratio
PERS	30	75.0%
STRS	Infinity	59.1%
SERS	29	72.6%
OP&F	Infinity	72.8%
HPRS	Infinity	66.0%

Given the severe decline in investment market values since the end of fiscal year 2008 and the need to begin evaluating options to address this situation proactively, all five systems, in consultation with the ORSC, developed legislative proposals that would reduce their unfunded actuarial accrued liability periods. Under the current contribution and benefit levels, SERS and PERS, as a whole, are expected to exceed the 30-year funding period as they begin recognizing investment losses in each of the next four years due to the actuarial smoothing technique used. The Council approved a motion to have staff work with OP&F on December 10, 2008, on March 11, 2009 with STRS, and on April 8, 2009 with PERS, SERS, and HPRS.

STRS, SERS, OP&F, and HPRS presented their board-approved funding plans at the September 9, 2009 ORSC meeting. PERS presented its board-approved plan at the December 9, 2009 ORSC meeting. Once legislation is introduced, ORSC staff will review it and make recommendations. Failure to implement a viable plan that will reduce the funding period to no more than 30 years, as certified by the retirement system's actuary, could be potentially very costly in the long run with the gradual disfunding of these retirement systems.

The following chart summarizes the plans presented to the ORSC.

[1] The most recent actuarial valuations for PERS, OP&F, and HPRS are as of 12/31/09; STRS and SERS as of 6/30/10.

	PERS[i]	STRS	SERS	OP&F	HPRS
Contributions (Legislation required)	No proposed changes.	Employee rate increased from 10% to 12.5% beginning 7/1/2011 phased in by 0.5% per year. Employer rate increased from 14% to 16.5% beginning 7/1/2016 phased in by 0.5% per year.	No proposed changes.	Employee rate increased from 10% to 12% phased in by 0.5% increments from 2010 to 2013. Employer rate for police increased from 19.5% to 24% phased in by 0.5% in 2010, 2% in 2011 and 2% in 2012. Employer rate for police and fire increased from 24% to 25% (1/1/2013).	Employee rate increased from 10% to 11%. (Employer rate increased from 25.5% to 26.5% pursuant to board action effective 7/1/2009; H.B. 1 capped the employer rate at 26.5%.)
Retirement Eligibility (Legislation required)	Normal retirement increased from 65 to 67 with 5 YOS and from 30 to 32 YOS at age 55; Early retirement increased from 60 to 62 with 5 YOS and from 55 to 57 with 25 YOS, with actuarially-reduced benefits.[ii]	Normal retirement increased from 30 to 35 YOS at any age (retains age 65 with 5 YOS); 30 YOS at age 60. Early retirement increased from 25 to 30 YOS at age 55 (retains age 60 with 5 YOS), with actuarially-reduced benefits.	Normal retirement increased from 65 to 67 with 10 YOS and from 55 to 57 with 30 YOS. Early retirement retained at age 62 with 10 YOS and age 60 with 25 YOS, with actuarially-reduced benefits, and applied to members hired prior to S.B. 148 (eff. 5/14/08)	Normal retirement increased from 48 to 52 with 25 YOS for *new* hires only. Early retirement available at age 48 with 25 YOS, with actuarially-reduced benefits for *new* hires.	No proposed changes.
Benefit Accrual Rate	Benefit formula changed to 2.2% for the first 35 YOS, plus	Benefit formula changed to flat 2.2% for the first 30	No proposed changes.	No proposed changes.	No proposed changes.

	PERS[i]	STRS	SERS	OP&F	HPRS
(Legislation required)	2.5% for YOS after 35 (instead of 30). Minimum benefit of $86 per YOS eliminated.	YOS, plus flat 2.5% for YOS after 30. 35-year incentive of 88.5% of FAS eliminated.[iii]			
FAS (Legislation required)	FAS changed from average 3 to 5 years.	FAS changed from average 3 to 5 years.	No proposed changes.	FAS changed from average 3 to 5 years for members with < 15 YOS.	FAS changed from average 3 to 5 years.
COLA (Legislation required)	Lesser of actual change in CPI-W or 3% for *future* retirees only.	COLA reduced from 3% to 2% for *current* retirees and to 1.5% for *future* retirees.	No proposed changes.	COLA deferred until age 55 for *current* and *future* retirees, except surviving beneficiaries (12 months after effective date of benefit).	COLA decreased from 3% to 2% for *current* and *future* retirees, except for retirees who are age 65 and receiving a pension of less than 185% of federal poverty level ($26,000). COLA deferred until age 60 for benefit recipients (currently age 53). Board authority to increase COLA up to 3% when funds are available.
Allocation to Retiree Health Care Benefits (Board may determine amount	Reduced from 7% to 5.5% in 2009 and, in 2010, to 4%.	No proposed changes.	Reduced from 4.16% to estimated 0.31%, *excluding* employer health care surcharge of 1.5%.	Reduced from 6.75% to 4.8%. (Ties health care premium subsidy to years of service for new retirees up to a	Reduced from 5.5% to an amount necessary to bring plan to a 30-year funding period (estimated 0.3%

	PERS[i]	STRS	SERS	OP&F	HPRS
allocated to retiree health care.)				maximum 75% of monthly premium.)	reduction)
Part-Time/Full-Time Service Credit (Legislation required)	Increased from $250 to $1,000 per month to earn one month of credit, indexed to wage inflation.	No proposed changes.	No proposed changes.	Not applicable	Not applicable
Purchased Service Credit (Legislation required)	Require member to pay 100% of liability resulting from purchase.	Require member to pay 100% of liability resulting from purchase.	Require member to pay 100% of liability resulting from purchase.	Require member to pay 100% of liability resulting from purchase.	Require member to pay 100% of liability resulting from purchase.
DROP Plans (Legislation required, *except Board may determine interest rate.)*	Not applicable	Not applicable	Not applicable	Interest reduced from 5% to 3%; minimum period (no penalty) increased from 3 to 5 years.	Additional 1% employee contribution paid to HPRS, not DROP account.
Disability Modifications (Legislation required)	Change from "own occupation" to "any occupation" standard after three years on disability (up to maximum five years if continued treatment though active case management).[iv] Exclude disabilities that were the result of a voluntary commission of a felony or elective	No proposed changes.	No proposed changes.	No proposed changes.	No proposed changes.

	PERS[i]	STRS	SERS	OP&F	HPRS
	cosmetic surgery. Prohibit post-separation eligibility unless disability began during employment or is work-related. Mandate application for Social Security Disability and offset any benefits received from SSDI, except for those who maintained two jobs for at least five years prior to disability.[v] Limit employer duty to reinstate member to former job to 3 years after disability, *except if member is on continued treatment, then up to maximum 5-year period*. Limit service credit while on disability to matching years of service based on the actual time member returned to covered public employment, with a minimum of 2				

	PERS[1]	STRS	SERS	OP&F	HPRS
Disability Modifications (Legislation required)	years and a maximum of 5 years. Make members ineligible for disability benefits who are working at their own job after approval of disability benefits, *except for members with modified duties or hours or with future-dated treatment that will create incapacity.*	No proposed changes.	No proposed changes.	No proposed changes.	No proposed changes.
Membership Determination (Legislation required)	Establish a five-year limit for individuals to initiate a request for membership determination in PERS.	No proposed changes.	No proposed changes.	No proposed changes.	No proposed changes.
Retroactive Benefits (Legislation required)	Limit retroactive benefit payments for inactive members to within 90 days of application (currently retroactive to date member first eligible for retirement)	No proposed changes.	No proposed changes.	No proposed changes.	No proposed changes
Inter-System Transfers (Legislation	Actuarially-determined cost for inter-system transfers, with credit	No proposed changes.	No proposed changes.	No proposed changes.	No proposed changes.

	PERS[i]	STRS	SERS	OP&F	HPRS
required)	either prorated or purchased by member.				
Mitigating Rate for Participants in DC Plan (Legislation required)	Authorize the board rather than the actuary to determine the rate to mitigate any negative impact upon the DB plan as a result of participants electing the DC plan.	No proposed changes.	No proposed changes. (SERS Board has not yet established a DC Plan as required by statute.)	Not applicable	Not applicable

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[i] The PERS Board recommended the following three group phase-in once legislation is enacted: Group A – Must be eligible to retire within five years after the effective date of the legislation – grandfathered in under the current plan, except for COLA provision; Group B – must have 20 or more years of service by the effective date of the legislation or be eligible to retire within 10 years after the effective date of the legislation – grandfathered in under the current plan, except for the COLA provision and the actuarial reduction factors for early retirement; and Group C – all others - all elements of the new plan design apply.

[ii] The law enforcement and public safety divisions represent only 2.3% of the active members in PERS. PERS generally recommends increases in the age of retirement by two years, but suggests that the ORSC may wish to consider consistency with any proposed changes made in OP&F and HPRS retirement ages.

[iii] STRS members who have 30 years of service, who are age 55 with 25 years of service, or who are age 60 with 5 years of service as of July 1, 2015 would receive the greater of the following: The benefit as of July 1, 2015 under the current formula; OR the benefit upon retirement under the new formula.

[iv] Definition of "any occupation" is that the employee is not capable of gainful employment that would replace 75% of FAS, that could reasonably be found in the employee's regional job market, and for which the employee is qualified by experience, education and station in life.

[v] Increase FAS by CPI in calculation of income before taking offset.

STATUS OF HEALTH CARE FUNDS

THE 128th GENERAL ASSEMBLY

JANUARY 1, 2009 - DECEMBER 31, 2010

In 1974, the five state retirement boards were given broad discretionary authority to provide health care coverage to retirees and their dependents. Unlike pension benefits, which become vested upon retirement, health care benefits are not a vested right under Ohio's public pension laws. Therefore, the boards are authorized to change the premiums, eligibility and level of health care benefits at any time. A 2004 ruling by the Tenth District Court of Appeals (Ohio Association of Public School Employees, et al. v. School Employees Retirement System Board, et al.) upheld the discretionary nature of health care benefits in a lawsuit that had attempted to prevent the SERS Board from making changes to its health care plan. The Ohio Supreme Court let this decision stand in May 2005 when it declined to review the case.

Since 1974 each system has provided some level of comprehensive hospital, medical and prescription drug coverage. In 1977, the systems were required statutorily to reimburse benefit recipients for Medicare Part B premiums (medical). Retirees who do not qualify for Medicare Part A (hospital) are provided equivalent coverage under the systems' health care plans. All employees hired on or after April 1, 1986 are required by federal law to contribute to Medicare.

Beginning in 2006, Medicare began offering a prescription drug benefit known as Medicare D. For most retirees, the prescription drug benefit provided by the systems is superior to the benefit offered by Medicare. However, low income retirees who qualify for a government subsidy for their Medicare prescription drug benefit may fare better under Medicare D so they will need to determine which drug plan is better for them.

January 1, 2011 marks the implementation date of the Patient Protection and Affordable Care Act (federal health care reform act). Beginning on that date, federal law will require health care plans to offer health care for enrollees' children until age 26 if they do not have access to employer-sponsored health care, provide an unlimited maximum lifetime benefit, and cover 100% of preventive services without any member cost sharing.

Controlling health care costs has been and continues to be a major concern for Ohio's retirement systems. In 2009, the total retiree health care costs paid by the retirement systems were approximately $2.5 billion. By law, any health care costs borne by the retirement systems must be financed by employer contributions only. The retirement systems' actuaries review annually the amount of contributions required to fund vested pension benefits. Contributions in excess of what is needed to support those benefits can be allocated to health care. The following charts indicate the percentage of employer contribution each system intends to allocate to health care during 2011 and the projected solvency period for each system's health care fund.

Ohio Retirement System	Percentage of Employer Contribution Allocated to Health Care in 2011
OPERS	4.00%
STRS	1.00%
SERS	1.43%*
OP&F	6.75%
HPRS	3.50%

*Does not include employer health care surcharge of up to 1.5% of total active member payroll.

Projected Solvency Period for Health Care Funds	
OPERS	2020 (as of 12/09)
STRS	2021 (as of 1/10)
SERS	2018 (as of 6/10)
OP&F	2040 (as of 10/10)
HPRS	2026 (as of 12/09)

Each year the retirement systems review their health care plans and make adjustments as needed. Below is a description of the changes to each system's health care plan effective January 1, 2011.

OPERS

PREMIUMS
Effective in 2011, OPERS will no longer subsidize the monthly premium of a retiree's spouse who is under the age of 55.

OPERS will continue to reimburse retirees $96.40 each month for Medicare Part B premiums in 2011.

ELIGIBILITY
Retirees will be able to cover eligible children up to age 26 regardless of marital status or enrollment as a full-time student.

BENEFITS
There will no longer be a lifetime maximum for medical/pharmacy coverage for retirees not yet eligible for Medicare. Preventive services will be covered at 100% with no member cost sharing.

For detailed information on the PERS health plan in general, please visit the system's website at www.opers.org.

STRS

PREMIUMS

In 2011, individuals age 26 or older who became incapacitated in childhood will no longer be eligible for the child premium rate.

STRS will continue to reimburse Medicare Part B monthly premiums on a sliding scale from $29.90 for those with 16 or fewer years of service to a maximum of $52.83 for those with 30 or more years of service.

ELIGIBILITY

Retirees will be able to cover eligible children up to age 26 regardless of marital status or enrollment as a full-time student. The waiting period for late enrollees will be reduced to 90 days.

BENEFITS

There will no longer be a lifetime maximum for medical/pharmacy coverage for retirees not yet eligible for Medicare. Preventive services will be covered at 100% with no member cost sharing. Additionally, Aetna, Medical Mutual, Paramount, and AultCare enrollees will be covered by a Medicare Part D plan.

For detailed information on the STRS health plan, please visit the system's website at www.strsoh.org.

SERS

PREMIUMS

Premiums will increase for all groups. Retirees who retired with less than 10 years of service before August 1989 will begin paying 50% of the premium cost, up from the 17.5% of the cost they paid in 2010. Retirees who retired between August 1989 and July 1993 will begin paying the same percentages as those who retired between August 1993 and July 2008. Disability retirees with less than 10 years of service will begin paying 50% of the premium cost, while disability retirees with 10 years but less than 25 years of service will pay 33% of the cost, and those with 25 or more years of service will pay 17.5%.

The amount that SERS reimburses for Medicare Part B premiums remains set in statute at $45.50 per month.

ELIGIBILITY

Retirees will be able to cover eligible children up to age 26 regardless of marital status or enrollment as a full-time student.

BENEFITS

There will no longer be a lifetime maximum for medical/pharmacy coverage for retirees not yet eligible for Medicare. Preventive services will be covered at 100% with no member cost sharing. MetLife will be the administrator of the dental program beginning January 1, 2011.

For detailed information on the SERS health plan, please visit the system's website at www.ohsers.org.

<u>OP&F</u>

<u>PREMIUMS</u>
OP&F will continue to subsidize 75% of the health care premium for retirees who retired on or before July 24, 1986 and 50% for their dependents. If benefits began being paid on or after July 25, 1986, OP&F will subsidize 75% of the retiree's premium and 25% for dependents.

OP&F will continue to reimburse retirees $96.40 each month for Medicare Part B premiums in 2011.

<u>ELIGIBILITY</u>
Retirees will be able to cover eligible children up to age 26 regardless of marital status or enrollment as a full-time student.

<u>BENEFITS</u>
There will no longer be a lifetime maximum for medical/pharmacy coverage for enrollees. Preventive services will be covered at 100% with no member cost sharing. Additionally, OP&F will begin offering a Diabetes Health Plan benefit to all participants enrolled in the UnitedHealthcare medical plan effective January 1, 2011.

For detailed information on the OP&F health care plan, please visit the system's website at www.op-f.org.

<u>HPRS</u>

<u>PREMIUMS</u>
Monthly premiums for all groups except Medicare eligible retirees will be increased. For example, the monthly premium for non-Medicare eligible retirees will increase from $25 to $39. Beginning in 2011 a plan participant will be considered to have Medicare if he or she has Medicare Part A and Part B coverage. In the past only Medicare Part B coverage was required.

The monthly premiums for secondary coverage through HPRS will increase as well. HPRS also will begin charging a premium for surviving children. The tobacco use monthly surcharge will increase from $35 to $39 and will be applicable to dependent children beginning in January 2011.

HPRS will continue to reimburse retirees $96.40 each month for Medicare Part B premiums in 2011.

ELIGIBILITY

Retirees will be able to cover eligible children up to age 26 regardless of marital status or enrollment as a full-time student.

BENEFITS

Effective January 1, 2011, EyeMed will be the sole administrator of vision benefits. There will no longer be a lifetime maximum for medical/pharmacy coverage for enrollees. Additionally, preventive services will be covered at 100% with no member cost sharing.

For detailed information on the HPRS health care plan, please visit the system's website at www.ohprs.org.

ACTUARIAL REVIEWS

THE 128th GENERAL ASSEMBLY

JANUARY 1, 2009 - DECEMBER 31, 2010

<u>Actuarial Audit of the State Teachers Retirement System, Completed by Milliman, November 18, 2009</u> – The Ohio Retirement Study Council is required by statute to conduct an actuarial audit of each statewide retirement system at least once every ten years. The Council contracted with Milliman to complete this audit of STRS. Milliman presented their report at the November 18, 2009 ORSC meeting.

Milliman made five major recommendations for possible changes in current procedures resulting from the review. Four would affect the determination of the System's liabilities and costs and the fifth would affect future Actuarial Experience Reviews.

Recommendation #1: Post-retirement Mortality Assumption

As discussed in *Section III – Actuarial Valuation Assumptions*, actuarial standards indicate that the mortality assumption used in determining pension obligations should provide appropriate margin for future mortality improvements. This can be done either by specifying a "static" mortality table with a margin built in (e.g. – a mortality assumption that generates fewer expected deaths than has occurred in the recent past), or by specifying a "projected" mortality table (e.g. – starting with a mortality assumption that matches current mortality rates and projects annual decreases in mortality rates into each future year modeled in the valuation). PwC (PricewaterhouseCoopers, LLC) used a static mortality table in the July 1, 2008 valuation of STRS. Based on our review of the mortality assumption, we find some age/gender combinations that appear to allow a reasonable margin for future improvement in mortality, while other age/gender combinations that have a negative margin (i.e. – the assumption anticipates a *greater* number of expected deaths than indicated by recent experience). We recommend that the mortality assumption be revised to provide sufficient margin across all age and gender combinations, and thus in total.

Recommendation #2: Investment Return Assumption

As discussed in *Section III – Actuarial Valuation Assumptions*, we believe that, while the STRS current investment return assumption complies with the requirements of Actuarial Standard of Practice No. 27 (ASOP27), *Selection of Economic Assumptions for Measuring Pension Obligations*, that 8.0% is in the optimistic end of the acceptable range as specified in ASOP27. We believe that a net rate of return assumption of 7.5% will provide an unbiased or more neutral estimate of future returns over the period during which STRS will pay benefits to the current participants. We recommend that STRS consider reducing the current 8.0% investment return assumption.

Recommendation #3: Reflection of Contribution Timing

As discussed in *Section III – Actuarial Valuation Methods and Procedures*, we recommend that the calculation of the Normal Cost Rate be revised to better reflect the actual timing of the receipt of contributions to the System. Currently, this Rate is determined by dividing (a) the amount of the normal cost for the coming plan year by (b) the prior year annualized salaries of active members included in the Actuarial Valuation increased by one-half of a year's assumed payroll growth. The dollar amount of the normal cost for a plan year is being determined as if it would be paid at the beginning of the plan year. Since contributions are received on a monthly basis throughout the plan year, with an average receipt at mid-year, we recommend that the dollar amount of the normal cost applied to determine the Normal Cost Rate be increased by one-half year of interest to reflect this delay in the receipt of contributions after the beginning of the plan year. Also, the prior year annualized salaries used to determine this rate are being increased by one-half year of payroll growth to approximate the payroll upon which contributions will be made. Based on our understanding that teachers' pay increases occur predominantly at the beginning of the school year, we recommend increasing the prior year annualized salary by a full year of payroll growth to better reflect the expected payroll in the upcoming plan year.

Recommendation #4: Service in Multiple Systems

As discussed in *Section I – Data Validity*, in our review of individual member benefit calculations provided to us by the System versus valuation data provided by the System to the actuary for the valuation, we identified one transferred member whose actual benefit calculation was based on service and pay with both OPERS and STRS, but whose valuation liability was based only on the service and pay within STRS. The result was a significant understatement of this member's liability. Due to the large number of members who have earned service in more than one of the five Ohio Retirement Systems, we recommend that STRS compile information from the other Ohio Retirement Systems regarding active and inactive members who have service in one or more of those systems and provide information to PwC so that all service and pay may be taken into account in the valuation of such members.

Recommendation #5: Presentation of Proposed Actuarial Assumptions

As discussed in *Section III – Actuarial Valuation Assumptions*, when conducting an experience review, the actuary will tabulate the actual number of occurrences of a particular decrement over the study period, and will compare the actual number of decrements with the number expected based on a combination of the prior census data and actuarial assumption. Dividing the actual occurrences by the expected occurrences results in an actual to expected ratio ("A/E ratio"). Deviations in actual versus expected results (e.g. – A/E ratios above or below 1.0) provide a basis for the actuary to modify assumptions prospectively. Once a new assumption is proposed it is possible to calculate A/E ratios for the prior period as if the new assumption had been in place during the prior period. Calculating A/E ratios on the proposed new assumption is a powerful way to review the appropriateness of the new assumption. We recommend that PwC include A/E ratios in future experience review reports based on both the prior and the proposed new assumptions in order summarize the extent to which the new assumption matches actual experience relative to the prior assumption. Please see our discussion of post-retirement mortality in Section III for more detail.

REPORTS ON ENACTED PENSION LEGISLATION

THE 128th GENERAL ASSEMBLY

JANUARY 1, 2009 - DECEMBER 31, 2010

Am. Sub. H.B. 1 – Rep. Sykes

Am. Sub. H.B. 1 generally makes operating appropriations for the biennium beginning July 1, 2009 and ending June 30, 2010 and provides authorization and conditions for the operation of state programs. This analysis is limited to those provisions of the bill that pertain to the Ohio retirement systems.

The bill would make the following appropriations to Ohio Police & Fire Pension Fund (OP&F):

Appropriation Item	Fiscal Year 10	Fiscal Year 11
GRF 090-524 Police and Fire Disability Pension Fund	$8,000	$7,500

This state subsidy is authorized by R.C. §742.374 and funds the ad hoc increase enacted in H.B. 284 (109th General Assembly - 1971). Persons who were receiving a pension prior to July 1, 1968 were eligible for an additional monthly payment of two dollars for each year between their effective date of retirement and December 31, 1971.

Appropriation Item	Fiscal Year 10	Fiscal Year 11
GRF 090-534 Police and Fire Ad Hoc Cost of Living	$95,000	$90,000

This state subsidy is authorized by R.C. §742.3712 and funds the ad hoc increase first granted in H.B. 204 (113th General Assembly - 1979) and later codified in H.B. 638 (114th General Assembly - 1981). Persons who were receiving an age and service or disability pension prior to July 1, 1974 were eligible for a supplemental payment of five percent of the first 5,000 dollars of their annual pension. Persons receiving a survivor benefit prior to July 1, 1981 were also eligible for a supplemental payment of five percent of the first 5,000 dollars of their annual benefit.

Appropriation Item	Fiscal Year 10	Fiscal Year 11
GRF 090-554 Police and Fire Survivor Benefits	$720,000	$680,000

This state subsidy is authorized by R.C. §742.361 and funds the survivor benefit increases enacted in H.B. 215 (108th General Assembly - 1970), S.B. 48 (110th General Assembly - 1974) and H.B. 268 (111th General Assembly - 1976). This state subsidy was limited by H.B. 694 (114th General Assembly - 1981) to persons who first received survivor benefits prior to July 1, 1981. For survivors first receiving benefits on or after July 1, 1981, OP&F is required to make payment from its own resources.

Appropriation Item	Fiscal Year 10	Fiscal Year 11
090-575 Police and Fire Death Benefits	$20,000,000	$20,000,000

This state subsidy is authorized by R.C. §742.62 and funds benefits payable under the Ohio Public Safety Officers Death Benefit Fund to the surviving spouses and dependent children of law enforcement officers and fire fighters who die in the line of duty or from injuries sustained in the line of duty. OP&F administers the Death Benefit Fund; the State of Ohio funds the benefits payable thereunder.

Additionally, the bill sets the employer contribution rate at 26.5%. When the bill was amended, however, prior language allowing the Highway Patrol Retirement System (HPRS) board to establish the employer contribution rate at no more than three times the employee contribution rate was not removed. Therefore, current law contains a conflict as to what the employer contribution rate is at HPRS.

ORSC Position – The ORSC took no action on this bill.

Effective Date - July 17, 2009 (Emergency)

PENDING PENSION-RELATED ISSUES

THE 128th GENERAL ASSEMBLY

JANUARY 1, 2009 - DECEMBER 31, 2010

The ORSC staff keeps legislators abreast of relevant public retirement issues and of prior recommendations that have been made but not acted upon by the legislature. There remain a number of issues and recommendations that continue to warrant legislative consideration. What follows is a brief summary of each issue and of action taken by the legislature, if any, in 2009 and 2010. Further background and detail is available through the ORSC website www.orsc.org.

Actuarial Funding of Pension Benefits - There are generally three sources of revenue for the Ohio retirement systems to fund, on an actuarial basis, their defined benefit pension benefits: (1) employee contributions; (2) employer contributions; and (3) investment earnings. The legislature guarantees the defined benefit pension benefits that are paid to participants and determines the maximum contribution rates. Investment earnings are typically the largest source of revenue for the Ohio retirement systems, funding up to 75 percent of the benefits paid.

The last semi-annual investment review required by law and presented at the ORSC meeting on November 10, 2010, indicates that all five systems have ten-year returns that are below their current actuarial interest rate assumptions due to recent market conditions.

In 2004 Milliman reviewed the adequacy of the contribution rates in OP&F and concluded that the current rates were not adequate to support **both** the mandated pension benefits within the maximum 30-year funding period and the discretionary health insurance benefits provided by OP&F to retirees, beneficiaries and their dependents. One or more of the following actions will need to occur: statutory contribution rates must be increased between 5 and 5.5% of payroll; state subsidies must be provided to OP&F; mandated pension benefits must be reduced; and/or discretionary health care benefits must be reduced significantly or eliminated. Milliman further found that an infinite funding period in OP&F should be deemed to be an unacceptable situation and that the cost of bringing the funding period into compliance with the maximum 30-year funding limit will continue to grow the longer corrective action is delayed. It is important to note that all five statewide retirement systems in Ohio have sufficient funds on hand to pay the statutorily mandated pension benefits for the next two to three decades.

The section of this report titled "30-Year Funding Plans" provides further details on the systems' plans to reduce their funding periods.

Cost and Funding of Retiree Health Care Benefits - Faced with double-digit increases for the foreseeable future, particularly in the area of prescription drugs, all of the retirement systems face significant challenges of controlling costs while maintaining meaningful coverage. Contributing factors to the double-digit increases include: the advent of "baby boomer" retirements, improved life expectancy of retirees, higher drug utilization, advances in medical technology, direct consumer advertising, and the general declining ratio of active members to retirees. The significant investment losses experienced from March 2000 to March 2003 as well as during the great recession of 2008-2009 by all investors have also exacerbated the health care funding problem since the retirement systems must first fund guaranteed pension benefits, which will likely require a reduction in or elimination of the amount currently allocated to discretionary retiree health care benefits, given the current caps on contribution rates. The early retirement ages for many public employees create a significant cost for each retirement system's health care program.

<u>Joint Legislative Committee to Study Ohio's Public Retirement Plans</u> - In 1995, the Joint Legislative Committee to Study Ohio's Public Retirement Plans (JLC) was created to complete a comprehensive review of the laws and operations of all five retirement systems. It consisted of six senators and six representatives (including members of the ORSC), and was supported by the ORSC staff. The JLC reviewed each system, concentrating on the following major areas: disability statutes, procedures, and experience; cost and funding of retiree health care benefits; retirement eligibility and benefit provisions; investment authority and performance; and the level of contributions in relation to the level of benefits provided. In 1996, JLC issued a report in which ORSC staff made a number of recommendations. Many, but not all, of the recommendations have been acted upon by the legislature over the years. The following recommendations were made by staff as part of the report, but have not been implemented:

- "That the normal retirement age be increased in the uniformed employee systems from 48 to 52 with a four-year phase-in and that benefits be reduced prior to normal retirement age."

- "That the normal retirement age of 65 in the non-uniformed employee systems be increased in tandem with Social Security and that the 30-year service requirement be increased at the same rate and that benefits be reduced prior to normal retirement age or service."

  S.B. 148 (eff. 5-14-08) increased the retirement age and the minimum number of years of service new members of SERS need to be eligible for retirement.

- "That the statutory reduction rates for early retirement be repealed and that reduction rates for early retirement be determined on an actuarial basis in all five systems."

  S.B. 148 (eff. 5-14-08) changed the reduction factors for new SERS members opting for early retirement. The reduced benefit is based on actuarial factors.

- "That disproportionate increases in salary prior to retirement be limited to a maximum percentage for purposes of determining final average salary in PERS, SERS, PFDPF and HPRS unless such increase results from employment with another employer or promotion to a position previously held by another employee." (H.B. 180 (eff. 10-29-91) established a percentage limit in STRS.)

- "That the statutory authority to grant an annual lump sum supplemental benefit check (i.e., 13th check) be repealed in STRS and that ad hoc post-retirement increases be enacted on an as-needed basis by the legislature."

- "That non-law enforcement service credit be excluded for purposes of determining eligibility for service retirement under PFDPF." (H.B. 648 (eff. 9-16-98) requires members who establish membership in OP&F on or after 9-16-98 to pay the difference between both the employee and employer contributions that were made and the employee and employer contributions that would have been made had the member rendered the service in OP&F, plus annual compound interest thereon. Members who do not pay the difference receive pro-rated credit for their non-law enforcement service.)

- "That the five systems have prepared a study to determine the feasibility of pooling active members and retirees for purposes of health care coverage and submit their findings and recommendations to the standing committees of both houses of the Ohio General Assembly with primary responsibility for retirement and health care legislation and ORSC no later than December 31, 1996."

Defined Contribution Plan for SERS Members - Another staff recommendation included in the JLC final report was "that an alternative defined contribution plan be established, in conjunction with the existing defined benefit plan, in the three non-uniformed employee systems to provide greater portability and options for employees." Alternative defined contribution (DC) plans have been established in STRS pursuant to S.B. 190 (eff. 7-13-00) and in PERS pursuant to H.B. 628 (eff. 9-21-00). No alternative DC plan has been established in SERS, though S.B. 270 (eff. 4-9 01) requires the SERS board to establish such plan.

According to SERS staff, the SERS board commissioned The Segal Company to statistically verify member interest and identify the costs of implementing a defined contribution plan in 2002. Segal surveyed 10,000 SERS members who had less than five years of service and would be eligible for the DC plan. They found that 1% of new SERS members were interested in a DC option based solely on their own investments and 89% of new members preferred a guaranteed retirement. However, there appeared to be considerable interest in a hybrid plan that combined features of a DB and DC plan (46%). Segal completely outsourced the development and maintenance of the option. According to Segal this would require about $1 million in start-up costs and $1.3 million annually to operate. In February 2003, the SERS board decided that it was not in the best interest of its members to develop a DC option; however, the board requested that staff revisit the studies at a later time, and in the interim, request a language change making the current statute permissive rather than mandatory. However, there has been no such request this session.

Contributing Service Credit in PERS - H.B. 232 (eff. 2-16-84) increased the minimum amount of earnable salary required per month from $150 to $250 to receive one month's credit in PERS. A PERS member who earns $250 per month for twelve consecutive months ($3,000) is granted one year of service credit. This raises the public policy issue of whether the minimum monthly salary amount used to determine service credit in PERS should be increased and indexed to annual wage inflation.

Deferred Retirement Option Plans (DROP) - Popular throughout the country, these plans are intended to encourage members to continue working beyond normal retirement and are often designed to be cost-neutral to the retirement system. Generally, participation in a DROP is limited to members who are eligible for normal service retirement. The member continues to be employed for some defined period, such as three to eight years, during which period the member's monthly service retirement benefit is credited to the member's DROP account, along with annual compound interest at some specified rate. Upon termination of employment, the member receives a lump sum distribution of the member's DROP account or some alternative distribution thereof, and begins receiving a monthly service retirement benefit based on the member's final average salary and service credit calculated at the time the member elects participation in the DROP. S.B. 134 (eff. 7-23-02) granted the OP&F board the authority to establish a DROP for its members. A recent review of OP&F's DROP revealed that 85% of members who do not retire when first eligible for retirement elect to participate in the DROP. In the analysis of S.B. 134, the ORSC staff raised the public policy issue of whether the other four retirement boards should be granted similar authority to establish DROPs for their respective memberships. S.B. 206 (eff. 6/15/06) established a DROP for members of HPRS last year.

University of Akron Non-Teaching Employees - With the single exception of the University of Akron, all non-teaching employees of Ohio's state universities are members of PERS. Employees of the University of Akron are currently members of SERS. In the interest of maintaining parity in retirement benefits, there continues to be some legislative interest to transfer these employees from SERS to PERS. The ORSC actuary provided several options to address the actuarial impact upon both retirement systems of such a transfer in its report Transfer of University of Akron Active Members from SERS to PERS dated March 11, 2002. Based upon that report, the ORSC staff recommended "the transfer of the University of Akron non-teaching employees from SERS to the PERS state division in order to provide uniform benefits and representation for all non-teaching employees at state universities, provided:

1. PERS receives from SERS an amount equal to the member's actuarial accrued liability to the extent funded by SERS under the third option described above which would minimize any actuarial loss to PERS and have no actuarial gain or loss to SERS;

2. PERS serves as a pass-through or conduit for health care contributions received from the University of Akron (A PERS employer after enactment) to pay SERS for the net cost of providing health care benefits to University of Akron retirees still remaining in SERS until the last University of Akron retiree ceases to be covered under the SERS health care plan. This is consistent with the current pay-as-you-go financing of retiree health care benefits in all five retirement systems, and would hold SERS harmless as well as avoid any windfall to PERS on account of the proposed transfer; and

3. The current differential in the contribution rates under SERS and PERS, including the employer health care surcharge, remains payable by the University of Akron and its non teaching employees for 25 years (the current funding period under SERS), with the excess in contributions used to provide a supplemental contribution to SERS. This is consistent employees who elect the alternative defined contribution plan, and would mitigate any adverse impact upon the SERS health care plan and would eliminate any perceived financial incentive for potential groups of employers and employees to "shop" among the state retirement systems for benefits. In the alternative, the University of Akron makes a lump sum payment to SERS that is the actuarial equivalent of the above supplemental contribution payable over 25 years as determined by the SERS actuary and reviewed by the ORSC."

The ORSC did not take any action upon the staff recommendation.

Reemployment Provisions - There continues to be legislative interest in the reemployment provisions of the Ohio retirement systems that allow members who have been retired for at least two months to return to public employment while continuing to receive their pension. H.B. 84 (eff. 7 31-01) requires elected officials who retire and are reelected or appointed to the same office from which they retired to notify the board of elections or appointing authority of their retirement in order to continue receiving their pension. H.B. 95 (eff. 6-30-03) included language that requires a hearing before certain retirants can be reemployed and changes the deadline for elected officials to file notice of intent to retire and run for reelection to the same office.

Health Care for Reemployed Retirees - H.B. 151 (eff. 2-9-94) required PERS reemployed retirants to receive primary health insurance coverage through the retirant's public employer if the employer provides coverage to other employees performing comparable work. PERS health care coverage becomes secondary. It is important to note that health care coverage is a discretionary retiree benefit. Effective January 1, 2004 the OP&F board amended its health care policy relative to reemployed retirees. In OP&F, reemployed retirees who are eligible for health care coverage through their employer must pay the full premium cost should they choose to enroll in the OP&F health care plan. The STRS board adopted a rule, which became effective January 2009, that requires reemployed retirees to receive health care coverage from their public or private employer if the employer offers health care. HPRS also has a policy, which became effective January 1, 2008, that requires surviving spouses who are not eligible for Medicare and who are working and have medical coverage available through their employers to obtain their primary medical coverage through that employer. This raises a public policy issue of whether similar requirements should be adopted in the other state retirement systems with respect to reemployed retirants. Moreover, it raises a public policy issue of whether such requirements should include reemployment with a private employer that provides health insurance coverage as well.

Annual 3% COLA - In its analysis of H.B. 157 (eff. 2-1-02), which provides for an annual 3% COLA in all five retirement systems, regardless of the actual percentage change in the CPI-W, the ORSC staff recommended against the COLA changes under the bill and suggested that "any additional resources of these retirement systems be allocated to the provision of discretionary retiree health care benefits that are neither taxable nor subject to the Social Security offset and/or the provision of ad hoc increases, such as a "purchasing parity" adjustment of some target ratio of either 75% or 85%, to retirees whose benefits have been eroded the most by inflation over the years." The ORSC rejected the staff recommendation and recommended instead that the legislature approve H.B. 157. Between 1992 and 2010, the CPI-W has increased by less than 3% in 14 of those years.

Workers' Compensation Offset - In its Analysis of Police and Firemen's Disability and Pension Fund Disability Plan, Procedures and Experience, November 8, 1996, William M. Mercer recommended that the legislature "consider offsetting the disability retirement benefit by any periodic benefit being received by the disabled member through workers' compensation." A subsequent study prepared by the ORSC actuary Milliman & Robertson pursuant to a legislative mandate concluded that "Based on the data collected in this study, M&R believes it is feasible for the State of Ohio to coordinate public retirement systems disability benefits and workers' compensation benefits. We clearly recognize that the decision to do so rests with the Ohio General Assembly. If such a decision is made, we recommend that the benefit coordination be structured as follows:

1. Offsets should affect the following benefits:

    a. Periodic Wage Replacement Benefits;

    b. Lump Sum payments to close workers' compensation cases;

    c. Cost of living adjustments.

2. Offset should not affect lump sum scheduled benefits.

3. Maximum income from combined disability and workers' compensation benefits should be set at 100% of final average salary.

4. If offsets are introduced in Ohio, they should be made applicable to all 5 public retirement systems at the same time."

(<u>Report to the Ohio Retirement Study Council: Feasibility Study on Disability and Workers' Compensation Coordination</u>, Milliman & Robertson, November 23, 1999)

<u>Review of Adequacy of the Contribution Rates</u> - Current law requires the ORSC to conduct an annual review of the police and fire contribution rates and make recommendations to the legislature that it finds necessary for the proper financing of OP&F benefits. In 2003 the Council voted to have Milliman review the adequacy of the contribution rates for PERS, STRS, SERS, and HPRS. The legislature should consider amending the law to require the ORSC to conduct similar actuarial reviews of the adequacy of the contribution rates for the other four retirement systems as well.

<u>Mandatory Social Security</u> - The State of Ohio has a long and successful record of opposing mandatory Social Security coverage for its public employees. This issue continues to resurface in the context of various Social Security reform proposals as a means of generating additional revenues which are estimated to extend the solvency of Social Security by a mere two years.

<u>Submission of Annual Actuarial Valuation</u> - Each system is required to submit annually an actuarial valuation to the ORSC and the standing committee of the House of Representatives and Senate with primary responsibility for retirement legislation. The due date for each system is different: PERS must submit theirs by September 1, OP&F must submit theirs by November 1, STRS must submit theirs by January 1, SERS must submit theirs by May 1, and HPRS must submit theirs by July 1 following the year for which the valuation was made. This raises the issue of whether the due date should be the same for PERS, OP&F, and HPRS, all of whom operate on the calendar year and whether the due date should be the same for STRS and SERS, both of whom are on fiscal years beginning July 1 and ending June 30.

Purchase of Service Credit – Pursuant to the ORSC's request, Milliman, Inc. completed a report on the cost of purchasing service credit this year. The report noted that with regard to health care benefits, if they are reduced in the future, some of the additional health liabilities could be eliminated. Additionally, if service purchases did not count toward eligibility for or the amount of health care benefits, then the additional health care liabilities would be eliminated. The report revealed that the retirement systems subsidized the purchase of credit in nearly every case in 2005. This was true even for service credit for which the member was required to pay the full actuarial cost. This report raised the public policy issue of whether a member's purchase of service credit should be subsidized by the retirement system. ORSC staff made the following recommendations, which the Council approved: (1) The purchase price for all types of service should be the full actuarial liability resulting from the purchase of service credit, except as prohibited by federal law, and members should be required to retire within 90 days of purchasing service and (2) purchased credit should be prohibited from being counted for purposes of health care eligibility or subsidy.

Independent Legal Counsel – The ORSC contracted with Independent Fiduciary Services to complete fiduciary audits of STRS and OP&F. These reports were completed in 2006. One of the recommendations was that Ohio law should be amended to authorize the retirement systems' boards to retain independent outside legal counsel without the prior approval of the State Attorney General. This recommendation has not been acted upon.

Custodian – Another recommendation from the 2006 fiduciary audits of STRS and OP&F that has not been acted upon was that the applicable Ohio statutes should be amended to grant authority to select, contract with, manage, and terminate the financial institution(s) that will provide master custody services to the retirement systems, which are subject to the oversight jurisdiction of the ORSC.

DOCUMENTS STATUTORILY REQUIRED OF THE RETIREMENT SYSTEMS

THE 128th GENERAL ASSEMBLY

JANUARY 1, 2009 - DECEMBER 31, 2010

The retirement systems are required by statute to submit various documents to the ORSC to assist the Council in its evaluation of the systems. The following is a listing of each report the retirement systems are required to submit to the ORSC along with a brief summary of the contents of the report. Copies of the reports can be obtained at the ORSC office.

Annual Actuarial Valuation - (R.C. §§145.22(A), 742.14(A), 3307.51(A), 3309.21(A), 5505.12(A)) This annual report is an actuarial valuation of the pension assets, liabilities, and funding requirements of the retirement systems. The report must include (1) a summary of the benefit provisions evaluated; (2) a summary of the census data and financial information used in the valuation; (3) a description of the actuarial assumptions, actuarial cost method, and asset valuation method used in the valuation, including a statement of the assumed rate of payroll growth and assumed rate of growth or decline in the number of members contributing to the retirement system; (4) a summary of findings that includes a statement of the actuarial accrued pension liabilities and unfunded actuarial accrued pension liabilities; a schedule showing the effect of any changes in the benefit provisions, actuarial assumptions, or cost methods since the last annual actuarial valuation; and (6) a statement of whether contributions to the retirement system are expected to be sufficient to satisfy the funding objectives established by the board.

The actuarial valuation must be submitted annually to the ORSC and the standing committees of the House of Representatives and Senate with primary responsibility for retirement legislation. PERS must submit theirs by September 1, OP&F must submit theirs by November 1, STRS must submit theirs by January 1, SERS must submit theirs by May 1, and HPRS must submit theirs by July 1 following the year for which the valuation was made.

Annual Report on Health Care - (R.C. §§145.22(E), 742.14(E), 3307.51(E), 3309.21(E), 5505.12(E)) This report provides a full accounting of the revenues and costs relating to health care benefits. The report must include (1) a description of the statutory authority for the benefits provided; (2) a summary of the benefits; (3) a summary of the eligibility requirements for the benefits; (4) a statement of the number of participants eligible for the benefits; (5) a description of the accounting, asset valuation, and funding method used to provide the benefits; (6) a statement of the net assets available for the provision of the benefits as of the last day of the fiscal year; (7) a statement of any changes in the net assets available for the provision of benefits, including participant and employer contributions, net investment income, administrative expenses, and benefits provided to participants, as of the last day of the fiscal year; (8) for the last six consecutive fiscal years, a schedule of the net assets available for the benefits, the annual cost of benefits, administrative expenses incurred, and annual employer contributions allocated for the provision of benefits; (9) a description of any significant changes that affect the comparability of the report required under this division; and (10) a statement of the amount paid for Medicare Part B reimbursement.

The report on health care must be submitted annually to the ORSC and the standing committees of the House of Representatives and Senate with primary responsibility for retirement legislation. PERS, OP&F, and HPRS must submit theirs by June 30, whereas STRS and SERS must submit theirs by December 31, following the year for which the report was made.

Quinquennial Evaluation - (R.C. §§145.22(B), 742.14(C), 3307.51(B), 3309.21(B), 5505.12(B)) This report must be completed at least once every five years. It is an actuarial investigation of the mortality, service, and other experience of the members, retirants, contributors, and beneficiaries of the system to update the actuarial assumptions used in the actuarial valuation. The report must include (1) a summary of relevant decrement and economic assumption experience observed over the period of the investigation; (2) recommended changes in actuarial assumptions to be used in subsequent actuarial valuations; (3) a measurement of the financial effect of the recommended changes in actuarial assumptions.

The quinquennial evaluation must be submitted to the ORSC and the standing committees of the House of Representatives and Senate with primary responsibility for retirement legislation. PERS, OP&F and HPRS must submit theirs by November 1, STRS and SERS must submit theirs by May 1 following the last fiscal year of the period the report covers.

Annual Report on Disability Experience - (R.C. §§145.351, 742.381, 3307.513, 3309.391, 5505.181) The report details the preceding fiscal year of the disability retirement experience of each employer. The report must specify the total number of disability applications submitted, the status of each application as of the last day of the fiscal year, total applications granted or denied, and the percentage of disability benefit recipients to the total number of the employer's employees who are members of the public employees retirement system.

The report on the disability experience must be submitted to the Governor, the ORSC, and the chairpersons of the standing committees and subcommittees of the Senate and House of Representatives with primary responsibility for retirement legislation.

30-Year Funding Period - (R.C. §§145.221, 742.16, 3307.512, 3309.211, 5505.121) This report is required if the system's funding period exceeds thirty years. The report must include the number of years needed to amortize the unfunded actuarial accrued pension liability as determined by the annual actuarial valuation and a plan approved by the board that indicates how the board will reduce the amortization period of unfunded actuarial accrued liability to not more than thirty years. The report submitted by OP&F must also include whether the board has made any progress toward meeting the 30-year amortization period.

The report on the thirty-year funding period must be submitted to the ORSC and the standing committees of the House of Representatives and Senate with primary responsibility for retirement legislation not later than ninety days after the retirement system board receives the actuarial valuation in which the funding period exceeds thirty years.

STRS, SERS, OP&F, and HPRS presented their board-approved funding plans at the September 9, 2009 ORSC meeting. PERS presented its board-approved plan at the December 9, 2009 ORSC meeting.

Actuarial Analysis of Legislation - (R.C. §§145.22(D), 742.14(D), 3307.51(D), 3309.21(D), 5505.12(D)) These reports are required when any introduced legislation is expected to have a measurable financial impact on the retirement system. The actuarial analysis must include (1) a summary of the statutory changes that are being evaluated; (2) a description of or reference to the actuarial assumptions and actuarial cost method used in the report; (3) a description of the participant group or groups included in the report; (4) a statement of the financial impact of the legislation, including the resulting increase, if any, in the employer normal cost percentage; the increase, if any, in actuarial accrued liabilities; and the per cent of payroll that would be required to amortize the increase in actuarial accrued liabilities as a level per cent of covered payroll for all active members over a period not to exceed thirty years; (5) a statement of whether the scheduled contributions to the system after the proposed change is enacted are expected to be sufficient to satisfy the funding objectives established by the board.

The actuarial analysis must be submitted to the ORSC, the Legislative Service Commission, and the standing committees of the House of Representatives and Senate with primary responsibility for retirement legislation within sixty days from the date of introduction of the legislation.

Investment Managers and Brokers - (R.C. §§145.114(E), 145.116(C), 742.114(E), 742.116(C), 3307.152(E), 3307.154(C), 3309.157(E), 3309.159(C), 5505.068(E), 5505.0610(C)) Each system is required to submit an annual report to the ORSC containing the following information: (1) the name of each agent designated as an Ohio-qualified agent; (2) the name of each agent that executes securities transactions on behalf of the board; (3) the amount of equity and fixed-income trades that are executed by Ohio-qualified agents, expressed as a percentage of all equity and fixed-income trades executed by agents; (4) the compensation paid to Ohio-qualified agents, expressed as a percentage of total compensation paid to all agents that execute securities transactions; (5) the amount of equity and fixed-income trades that are executed by agents that are minority business enterprises (i.e., owned and controlled by Ohio residents who are Black, American Indian, Hispanic, or Oriental), expressed as a percentage of all equity and fixed-income trades executed by all agents; and (6) any other information requested by the ORSC regarding the board's use of agents.

Budgets – (R.C. §§145.092, 742.102, 3307.041, 3309.041, 5505.062) Each retirement system is required to submit to the ORSC its proposed operating budget, along with the administrative budget for the board, for the next immediate fiscal year at least sixty days before adoption of the budget.

STRS and SERS operate on fiscal years beginning July 1 and ending June 30. They presented their proposed operating budgets for fiscal year 2010 at the May 13, 2009 ORSC meeting and for fiscal year 2011 at the May 12, 2010 ORSC meeting. PERS, OP&F, and HPRS submitted their budgets for calendar year 2010 at the November 18, 2009 ORSC meeting and their budgets for calendar year 2011 at the November 10, 2010 ORSC meeting.

Audit Committee Report – (R.C. §§145.095, 742.105, 3307.044, 3309.044, 5505.111) Each retirement system is required annually to submit to the ORSC a report of the actions taken by its Audit Committee.

Rules - The systems are required to submit to the ORSC a copy of the full text, rule summary, and fiscal analysis of each rule they file with the Joint Committee on Agency Rule Review pursuant to R.C. §111.15.

SUBJECT INDEX OF PENSION BILLS INTRODUCED

THE 128TH GENERAL ASSEMBLY

JANUARY 1, 2009 - DECEMBER 31, 2010

The Subject Index of Pension Bills Introduced provides a listing of pension bills under subject heading and a key word description within the main heading. Bills that cover more than one subject are listed under all appropriate headings.

The pension systems affected by the bill are also indicated. "All systems" means the Public Employees Retirement System (PERS), the State Teachers Retirement System (STRS), the School Employees Retirement System (SERS), the Ohio Police and Fire Pension Fund (OP&F), and the Highway Patrol Retirement System (HPRS). "VFFDF" and "DBF" respectively refer to the Volunteer Fire Fighters' Dependents Fund and the Ohio Public Safety Officers Death Benefit Fund.

The main subject headings are listed at the beginning of the index for quick reference. The bills that were enacted are marked with an asterisk.

Subject Headings

Appropriations
Subsidies – OP&F – HB 1*

Benefits
Forfeiture of – ALL SYSTEMS – SB 219

Contributions
Employer rate – HPRS – HB 1*

Disability
On-duty presumptions – OPF – HB 246; SB 94

Early Retirement Incentives
Employer report – PERS – HB 30

Health Care
Volunteer firefighters killed in line-of-duty – VFFDF, OPF – SB 66

Membership
Public high school law enforcement officers – PERS-LE – HB 164; SB 122

Reemployment
Early retirement incentive – PERS – HB 30

Salary
Bonuses prohibited – SERS – HB 177
Certain compensation excluded – PERS – SB 83

Taxation
Volunteer firefighter credit – HB 255

*Enacted

STATUS OF PENSION LEGISLATION

THE 128th GENERAL ASSEMBLY

JANUARY 1, 2009 - DECEMBER 31, 2010

HOUSE BILLS

HSE BILL	INTRO	Actuarial Received	Subject, Sponsor, and System	Cont Pers	ORSC Pos	Hse Cmte	Testimony – Reported Out – Floor Vote	INTRO SEN	Sen Cmte	Testimony – Reported Out – Floor Vote	Conf Cmte	Concur-rence	Eff Date
1	02-12-09		Biennial budget bill; early retirement incentive plans; contribution rate freeze Sykes – PERS; OP&F; HPRS	BI	N	FA Sykes 02-17-09	02-24-09 Sub----02-25-09----02-26-09----03-10-09----03-11-09----03-12-09----03-24-09----03-25-09----03-26-09----03-31-09----04-01-09----04-02-09----04-21-09 Sub----04-27-09 Amend----04-29-09 Amend; Fl Vo: Y=53 N=45	04-30-09	FFI Carey 05-05-09	04-14-09----04-15-09----04-21-09----04-22-09----04-23-09----04-28-09----04-29-09----04-30-09----05-05-09----05-06-09----05-07-09----05-12-09----05-13-09----05-14-09----05-15-09----05-19-09----05-20-09----05-21-09----05-29-09 Sub----06-01-09----06-02-09 Amend----06-03-09 Amend; Fl Vo: Y=20 N=11	06-10-09	7-13-09	7-17-2009
30	02-18-09		Regarding early retirement incentive plans Combs - PERS	AE		FRS Koziura 02-24-09	06-10-09----						
118	04-01-09		Changes name of Department of Mental Retardation and Developmental Disabilities Newcomb, Phillips – PERS	BI	N	LGP Chandler 04-16-09 RR Book 06-10-09	Rereferred to RR 06-10-09						
164	04-29-09	07-02-09	Creates public high school law enforcement officers Miller – PERS-LE			PSH 05-05-09							
177	05-12-09		Prohibits investment bonuses under certain circumstances Huffman, Bubp - STRS	AE	D 07-08-09	ADS Newcomb 05-19-09	06-02-09----						
246	06-30-09	07-23-09	Changes on-duty disability presumptions Yuko, Stewart – OP&F			ADS Newcomb 07-01-09	11-19-09----03-02-10----03-09-10----05-18-10						
255	07-23-09		To allow $400 tax credit for volunteer firefighters Balderson	BI	N	WM Letson 09-15-09							

SENATE BILLS

SEN BILL	INTRO	Actuarial Received	Subject, Sponsor, and System	Cont Pers	ORSC Pos	Sen Cmte	Testimony – Reported Out – Floor Vote	INTRO HSE	Hse Cmte	Testimony – Reported Out – Floor Vote	Conf Cmte	Concur-rence	Eff Date
66	03-04-09		Health care for dependents of volunteer firefighters killed in line of duty Faber – VFFDF, OP&F	GK		ICL Buehrer 03-10-09	03-24-09----03-31-09----						
79	03-11-09		Changes name of Department of Mental Retardation and Developmental Disabilities Stewart - PERS	BI	N	SLV Hughes 03-17-09	04-22-09 Fl Vo: Y=32 N=0	04-23-09	LGP Chandler 05-06-09	06-10-09 Fl Vo: Y=99 N=0		06-17-09	10-06-2009
83	03-19-09	05-14-09	Excludes certain compensation from FAS Faber - PERS	GK		HHA Coughlin 03-24-09	03-31-09----04-21-09----04-28-09----						
94	04-07-09	07-23-09	Changes on-duty disability presumptions Patton – OP&F			ICL Buehrer 04-21-09	06-09-09----02-09-10----						
122	04-30-09	07-02-09	Creates public high school law enforcement officers Turner – PERS-LE			ED Cates 05-05-09	10-20-09----						
134	06-16-09		Creates Department of Health Care Administration R. Miller – ALL SYSTEMS	BI	N	FFI Carey 06-17-09							
189	10-20-09		Makes changes to adoption laws Goodman – ALL SYSTEMS	BI	N	JCV Seitz 10-22-09							
219	12-08-09	PERS:03-30-10	Forfeiture of disability benefits based on conviction of certain felonies Grendell – ALL SYSTEMS	AE	A 04-14-10	HHA Coughlin 12-09-09 Re-referred GO Husted 12-09-09	12-16-09----02-17-10----02-24-10 Amend; Fl Vo: Y=33 N=0	02-25-10	FRS Koziura 03-02-10	05-19-10----05-26-10----			

HOUSE COMMITTEES

ADS	Aging & Disability Services
ANR	Agriculture & Natural Resources
AE	Alternative Energy
CC	Civil & Commercial Law
CL	Commerce & Labor
CEP	Consumer Affairs & Economic Protection
CRJ	Criminal Justice
ED	Economic Development
EDU	Education
EE	Elections & Ethics
EBD	Environment & Brownfield Development
FBI	Faith-Based Initiatives
FA	Finance & Appropriations
AD	Agriculture & Development Subcommittee
HE	Higher Education Subcommittee
HS	Human Services Subcommittee
PSE	Primary & Secondary Education Subcommittee
TJ	Transportation & Justice Subcommittee
FRS	Financial Institutions, Real Estate & Securities
HLT	Health
HAA	Healthcare Access and Affordability
HUR	Housing & Urban Revitalization
INS	Insurance
JUD	Judiciary
JFL	Juvenile & Family Law
LGP	Local Government/Public Administration
PSH	Public Safety & Homeland Security
PU	Public Utilities
RR	Rules & Reference
SGE	State Government
TI	Transportation & Infrastructure
VA	Veterans Affairs
WM	Ways & Means

SENATE COMMITTEES

AG	Agriculture
ED	Education
ENE	Energy & Public Utilities
ENR	Environment & Natural Resources
FFI	Finance & Financial Institutions
GO	Government Oversight
HHA	Health, Human Services & Aging
HT	Highways & Transportation
ICL	Insurance, Commerce & Labor
JCV	Judiciary - Civil Justice
JCR	Judiciary - Criminal Justice
REF	Reference
RUL	Rules
SLV	State & Local Government & Veterans Affairs
WME	Ways & Means & Economic Development

LEGISLATIVE ACTION

A	Amended
S	Substitute
P	Postponed Indefinitely
R	Rereferred
V	Vetoed
E	Emergency
CR	Concurrence Refused

ORSC POSITION

A	Approved
D	Disapproved
AA	Approved with Amendment
AD	Action Deferred
N	No Action Necessary

ORSC CONTACT PERSON

GK	Glenn Kacic
AE	Anne Erkman
BI	Bill of Interest