Secretary of State

State of Oregon

PUBLIC EMPLOYEES RETIREMENT SYSTEM

July 1, 1996, to June 30, 1997

Audits Division

-

Secretary of State

State of Oregon

PUBLIC EMPLOYEES RETIREMENT SYSTEM

July 1, 1996, to June 30, 1997

Audits Division

No. 98-04

February 12, 1998

The Honorable John Kitzhaber
Governor of Oregon
State Capitol
Salem, Oregon 97310

The Board of Trustees
Oregon Public Employees Retirement System
11410 SW 68th Parkway
Tigard, Oregon 97223

This audit was conducted for the purpose of reporting on the Oregon Public Employees Retirement System's financial statements as of and for the year ended June 30, 1997, and on the internal controls and compliance with applicable laws and regulations.

We conducted our audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement.

As also required by those standards, we reviewed the internal controls of the Oregon Public Employees Retirement System to determine the audit procedures necessary to gather sufficient competent evidence in support of our opinion on the financial statements. We also performed tests of the Oregon Public Employees Retirement System's compliance with applicable laws and regulations. Our comments regarding internal controls and compliance with legal requirements are presented in the Audit Results section of this report.

OREGON AUDITS DIVISION

John N. Lattimer
Director

Fieldwork Completion Date:
December 4, 1997

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T A B L E   O F   C O N T E N T S

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SUMMARY

BACKGROUND

The Oregon Public Employees Retirement System (PERS) is a statewide defined benefit retirement plan for units of state government, political subdivisions, community colleges, and school districts. As of June 30, 1997, there were 808 employers who were members of PERS, including 110 state agencies, 448 political subdivisions, 17 community colleges, and 233 school districts. There are more than 68,000 retirees and beneficiaries currently receiving PERS benefits and more than 185,000 current and terminated employees who are members who are not yet receiving benefits.

PERS is funded through member and employer contributions and investment earnings. For the fiscal year ended June 30, 1997, contributions and investment income of $5,596 million were reported. Deductions for the fiscal year ended June 30, 1997, totaled $945 million.

AUDIT PURPOSE

The audit was conducted for the purpose of reporting on PERS' financial statements for the year ended June 30, 1997, and on the internal controls and compliance with applicable laws and regulations.

AUDIT RESULTS

This audit concludes that PERS' financial statements for the year ended June 30, 1997, which are included in this report, are fairly presented. Additionally, we noted no matters involving internal controls that we consider to be material weaknesses, nor did our tests disclose instances of noncompliance that are required to be reported herein under Government Auditing Standards. Our report on internal control and compliance with applicable laws and regulations is included herein.

INTRODUCTION

ORGANIZATION AND FUNCTIONS

The Oregon Public Employees Retirement System (PERS) is a statewide defined benefit retirement plan for units of state government, political subdivisions, community colleges, and school districts. For state agencies, community colleges, and school districts, PERS is a cost-sharing, multiple-employer system. It is an agent multiple-employer system for political subdivisions. While participation by state government units, school districts, and community colleges is mandatory, participation by most political subdivisions is optional but irrevocable if elected.

The PERS is administered under Oregon Revised Statutes (ORS) Chapter 238 by the Public Employees Retirement Board (board). The board consists of eleven members, all of whom were appointed by the Governor and confirmed by the Senate. The board appoints a director and employs staff to administer PERS' activities. PERS' principal administrative office is located in Tigard, Oregon.

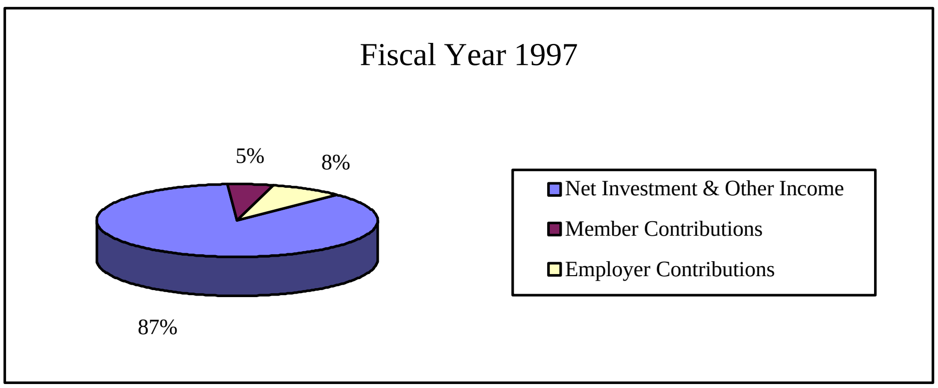
PERS, through its Member Services Division, provides counseling services at two external counseling centers as well as in the Tigard office. This division also provides services to employers and employee members relating to retirements, deaths, and disabilities. PERS also has a Fiscal Services Division and an Information Systems Division that provide administrative support for the agency. The Deferred Compensation plan, which is authorized under Internal Revenue Code Section 457 and ORS 243.400 to 243.507, is also administered through the board.

The board contracts for medical and hospital insurance on behalf of retired members. Members and their dependents are eligible for PERS health coverage if the member is receiving a retirement allowance or benefit under the PERS system. There are two health insurance subsidy programs, the Retirement Health Insurance Account (RHIA) that is available to all qualifying PERS retirees and dependents, and the Retirement Health Insurance Premium Account (RHIPA) that is available only for qualifying *state* retirees and dependents. These accounts subsidize qualifying retirees' and dependents' health insurance premiums.

FINANCIAL ACTIVITIES

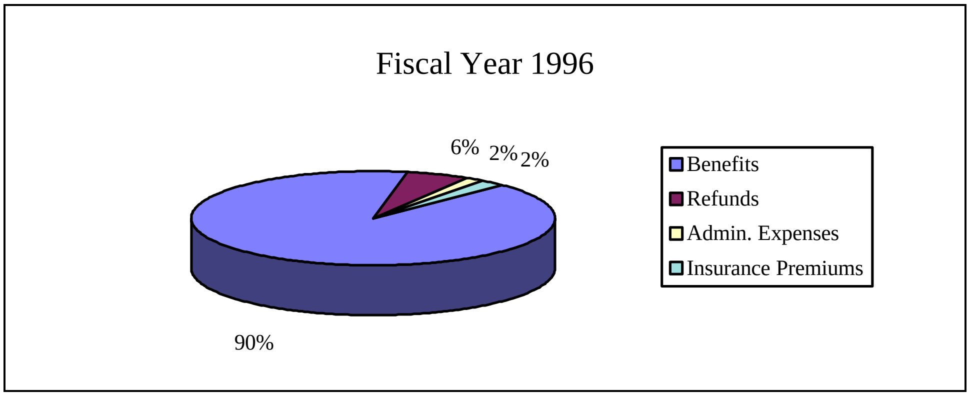
PERS' financial activities are accounted for in a Pension Trust Fund. The primary sources of additions to the fund are member and employer contributions and investment earnings.

Additions to Plan Net Assets



Member contributions totaled $304 million for fiscal year 1997. Employer contributions for the same period totaled $462 million. Investment earnings include interest earned on fixed-income securities, gains and losses on the disposal of investments, and changes in the market value of equity investments. Net income from investments for fiscal year 1997 totaled $4,829 million.

Deductions from Plan Net Assets



PERS benefits include service retirements, death, disability, and post-retirement health care benefits. Deductions from the fund for retirement, death, and disability benefits paid to retirees in fiscal year 1997 totaled $857 million. PERS also paid out approximately $53 million in refunds to members who decided to withdraw their accounts from PERS. Administration expenses were $14.7 million. Insurance premium subsidies paid by PERS for fiscal year 1997 were approximately $21.7 million.

AUDIT RESULTS

The Honorable John Kitzhaber
Governor of Oregon
State Capitol
Salem, Oregon 97310

The Board of Trustees
Oregon Public Employees Retirement System
11410 SW 68th Parkway
Tigard, Oregon 97223

BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS

We have audited the financial statements of the Oregon Public Employees Retirement System (PERS) as of and for the year ended June 30, 1997, and have issued our report thereon dated December 4, 1997.

We conducted our audit in accordance with generally accepted auditing standards and *Government Auditing Standards,* issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement.

Internal Controls

The management of PERS is responsible for establishing and maintaining a system of internal control. In fulfilling this responsibility, estimates and judgments by management are required to assess the expected benefits and related costs of controls. The objectives of an internal control system are to provide management with reasonable assurance regarding the reliability of financial reporting, the effectiveness and efficiency of operations, and compliance with laws and regulations. Because of inherent limitations in any system of internal control, errors or irregularities may nevertheless occur and not be detected. Also, projection of any evaluation of internal control to future periods is subject to the risk that controls may become inadequate because of changes in conditions or that the effectiveness of the design and operation of controls may deteriorate.

In planning and performing our audit of the financial statements of PERS for the year ended June 30, 1997, we obtained an understanding of internal control. With respect to the internal controls, we obtained an understanding of the design of relevant policies and procedures and

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whether they have been placed in operation, and we assessed control risk in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide an opinion on the internal controls. Accordingly, we do not express such an opinion.

Our consideration of internal control would not necessarily disclose all matters in internal controls that might be material weaknesses under standards established by the American Institute of Certified Public Accountants. A material weakness is a condition in which the design or operation of one or more of the specific internal control components does not reduce to a relatively low level the risk that errors or irregularities in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving internal control that we consider to be material weaknesses as defined above.

Compliance

Compliance with laws and regulations applicable to PERS is the responsibility of PERS' management. As part of obtaining reasonable assurance about whether the financial statements are free of material misstatement, we performed tests of PERS' compliance with certain provisions of laws and regulations. However, the objective of our audit of the financial statements was not to provide an opinion on overall compliance with such provisions. Accordingly, we do not express such an opinion.

The results of our tests disclosed no instances of noncompliance that are required to be reported herein under *Government Auditing Standards*.

OREGON AUDITS DIVISION

Sharron E. Walker, CPA, CFE
Deputy Director

December 4, 1997

FOLLOW-UP ON PRIOR AUDIT FINDINGS

This section reports follow-up action taken by PERS management on findings included in our prior audit report issued for the period from July 1, 1995, to June 30, 1996. The scope of the prior audit was to express an opinion on the Oregon Public Employees Retirement System's financial statements.

Prior Audit Findings	Disposition
1. Purchasing of Creditable Service: PERS is allowing members to retire with more service time credit and larger retirement benefits than allowed under Oregon Revised Statute 238.115(1)(a). A member was allowed to purchase and include their six month wait time as part of the amount of time worked as an active member.	1. RESOLVED. PERS received an Attorney General opinion stating that PERS should include the purchase of wait time performed *after* re-entry to covered employment and that under the specific circumstances noted in our previous audit, PERS does not have a duty to collect the overpayments or reduce future payments.
2. Information System Access: PERS is not removing employees' access to incompatible Retirement Information Management System (RIMS) screens to which they do not need access.	2. RESOLVED. PERS has implemented a new security matrix system. We observed testing of the new system, and it appears to be functioning properly. Employees no longer have access to screens that would allow them to perform functions incompatible with their job responsibilities.
3. Computer System Work Requests Backlog: There are 80 outstanding work orders to modify the Retirement Information Management System's (RIMS) screens or correct known RIMS errors, dating back as far as 1989.	3. PARTIALLY RESOLVED. A new screen was developed to process database-oriented work requests faster. A RIMS re-engineering project has begun, and systems staff are being reorganized for increased efficiency. There are still delays in processing work orders, and a comprehensive review of computer requests will not occur until June 30, 1998.
4. Policies and Procedures Manual: PERS' retirement services section does not have a current written procedure manual available to them that documents how pension benefits are calculated.	RESOLVED. All PERS policies and procedures manuals have been revised and input on the local area network so that employees may now access them in a usable format. Retirement services is approximately two-thirds complete with its revisions. Completion is expected by March 1, 1998.

Prior Audit Findings	Disposition
5. Financial Reporting: PERS misclassified cash and investments in the financial statements. Debt securities totaling $397 million and cash and cash equivalents totaling $4.5 million were classified as equity securities.	5. RESOLVED. PERS reclassified its securities in the fiscal year 1996 financial statements. Investments in the fiscal year 1997 financial statements are correctly classified. PERS is working with the State Treasury to determine information needed by PERS for financial reporting, and to review ways to improve financial information.

REPORT DISTRIBUTION

This report is a public record and is intended for the information of the Board of Trustees of the Oregon Public Employees Retirement System, the Retirement System's management, the governor of the state of Oregon, the Oregon Legislative Assembly, and all other interested parties.

COMMENDATION

The courtesies and cooperation extended by management and staff of the Oregon Public Employees Retirement System during the course of our audit were very commendable and sincerely appreciated.

AUDIT TEAM

Joel E. Leming, CPA, Audit Administrator
Craig M. Stroud, CPA
Anne S. Lawrence, CPA
Jason M. Stanley, CPA
Janice I. Richards

FINANCIAL SECTION

Secretary of State — Audits Division

Auditing for a Better Oregon

The Board of Trustees
Oregon Public Employees Retirement System
11410 SW 68th Parkway
Tigard, Oregon 97223

INDEPENDENT AUDITOR'S REPORT

We have audited the accompanying general purpose financial statements of the Oregon Public Employees Retirement System, an agency of the state of Oregon, as of and for the year ended June 30, 1997. These financial statements are the responsibility of the System's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with generally accepted auditing standards and *Government Auditing Standards* issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial status of the defined benefit pension plan and the postemployment healthcare plan, and the financial position of the deferred compensation fund and the health insurance administration fund of the Oregon Public Employees Retirement System as of June 30, 1997, and the changes in the financial status of the defined benefit pension plan and the postemployment healthcare plan, and the results of operations of the deferred compensation fund and the health insurance administration fund for the year then ended in conformity with generally accepted accounting principles.

Our audit was made for the purpose of forming an opinion on the general purpose financial statements taken as a whole. The accompanying financial information listed as supporting schedules in the foregoing table of contents is presented for purposes of additional analysis and is not a required part of the general purpose financial statements of the Oregon Public Employees Retirement System. Such information has been subjected to the auditing procedures applied in the audit of the general purpose financial statements and, in our opinion, is fairly presented in all material respects in relation to the general purpose financial statements taken as a whole.

A report in accordance with *Government Auditing Standards* on the System's internal control and its compliance with laws and regulations is separately presented in the AUDIT RESULTS section of this report.

OREGON AUDITS DIVISION

Sharron Walker

Sharron E. Walker, CPA
Deputy Director

December 4, 1997

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FINANCIAL STATEMENTS

Statements of Plan Net Assets - Defined Benefit Pension Plan and Postemployment Healthcare Plan and Balance Sheets - Agency Funds
June 30, 1997

			Agency Funds		
	Defined Benefit Pension Plan	Post-employment Healthcare Plan	Deferred Compensation Fund	Health Insurance Administration Fund	Totals (Memorandum Only)
Assets:					
Cash and Cash Equivalents	$ 792,171,907	$ 9,212,063	$ 129,667	12,378,925	$ 813,892,562
Receivables					
Employer	30,656,134	4,318,221			34,974,355
Employee	20,434,561				20,434,561
Interest and Dividends	118,299,191	16,458	,055	63,401	118,380,105
Investment Sales	389,195,616			-	389,195,616
Total Receivables	558,585,502	4,334,679	1,055	63,401	562,984,637
Due from Other Funds	9,858,098				9,858,098
Investments:					
U.S. Government Obligations	2,351,478,252				2,351,478,252
Domestic Corporate Obligations	1,894,296,145				1,894,296,145
Domestic Stocks	7,050,368,993				7,050,368,993
Domestic Mutual Funds	4,798,205,548				4,798,205,548
International Government & Corporate Obligations	1,422,248,351				1,422,248,351
International Stocks	2,652,758,567				2,652,758,567
International Mutual Funds	2,487,832,748				2,487,832,748
Mortgages	43,430,020				43,430,020
Real Estate	1,693,187,990				1,693,187,990
Limited Partnerships	692,136,161				692,136,161
Venture Capital	25,177,117				25,177,117
Leveraged Buy-Outs	2,047,552,171				2,047,552,171
Total Investments	27,158,672,063				27,158,672,063
Securities Lending Cash Collateral	2,223,552,615				2,223,552,615
Deferred Compensation Investments			388,659,480		388,659,480
Prepaid Expenses	131,930				131,930
Equipment and Fixtures, Cost Net of Accumulated Depreciation at 1997: $1,105,330	712,469				712,469
Land & Buildings, Cost Net of Accumulated Depreciation 1997: $15,247	8,247,767				8,247,767
Office Supplies Inventory, Cost	5,107				5,107
Total Assets	**30,751,937,458**	**13,546,742**	**$ 388,790,202**	**$ 12,442,326**	**31,166,716,728**
Liabilities and Fund Balance					
Liabilities:					
Investment Purchases and Accrued Expenses	332,054,239	648	$	$ 2,102,691	334,157,578
Deposits and Other Liabilities	11,420,260			10,339,635	21,759,895
Due to Other Funds	2,193,229	7,661,633	3,236		9,858,098
Bonds Payable	58,065,000				58,065,000
Deferred Compensation Due Participants			388,786,966		388,786,966
Securities Lending Collateral Due Borrowers	2,223,552,615				2,223,552,615
Total Liabilities	**2,627,285,343**	**7,662,281**	**388,790,202**	**12,442,326**	**3,036,180,152**
Net Assets held in trust for pension and postemployment benefits (Schedules of funding progress are presented on page 28)	$ 28,124,652,115	$ 5,884,461			**$ 28,130,536,576**
Fund Balance					
Total Liabilities and Fund Balance			**$ 388,790,202**	**$ 12,442,326**	

he accompanying notes are an integral part of the financial statements.

Statements of Changes in Plan Net Assets
Defined Benefit Pension Plan and Postemployment Healthcare Plan
For the Year Ended
June 30, 1997

	Defined Benefit Pension Plan	Post-employment Healthcare Plan	Totals (Memorandum Only)
Additions			
Contributions			
Employer	$ 433,289,222	$ 28,489,876	$ 461,779,098
Plan Member	303,723,333	-	303,723,333
Total Contributions	737,012,555	28,489,876	765,502,431
Investment Income			
Net Appreciation (Depreciation) in Fair Value of Investments	4,432,720,559		4,432,720,559
Interest, Dividends and Other Investment Income	571,382,419	1,423,356	572,805,775
Total Investment Income	5,004,102,978	1,423,356	5,005,526,334
Less Investment Expense	175,375,767	863,798	176,239,565
Net Investment Income	4,828,727,211	559,558	4,829,286,769
Other Income	749,047		749,047
Total Additions	5,566,488,813	29,049,434	5,595,538,247
Deductions			
Benefits	852,070,557	-	852,070,557
Death Benefits	4,437,394	-	4,437,394
Refunds of Contributions	52,542,067	-	52,542,067
Administrative Expense	13,227,283	1,449,323	14,676,606
Healthcare Premium Subsidies	-	21,726,518	21,726,518
Total Deductions	922,277,301	23,175,841	945,453,142
Net Increase	4,644,211,512	5,873,593	4,650,085,105
Net Assets held in trust for pension and postemployment healthcare benefits			
Beginning of Year - Restated (See note 12)	23,480,440,603	10,868	23,480,451,471
End of Year	$ 28,124,652,115	$	$ 28,130,536,576

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

Statement of Changes in Assets and Liabilities
Agency Funds
For the Year Ended
June 30, 1997

	Balance 7/1/96	Additions	Deductions	Balanc 6/30/9
Deferred Compensation Agency Fund				
Assets				
Cash	$ 90,006	$ 62,144	$ 22,483	$ 129,6
Accounts Receivable	8,667	1,055	8,667	1,0
Accrued Interest	15,721	48	15,769	
Investments	326,915,378	113,352,378	51,608,276	388,659,4
Total Assets	$ 327,029,772	$ 113,415,625	$ 51,655,195	$ 388,790,2
Liabilities				
Due Other Funds	$ 27,109	$ 8,444	$ 32,317	$ 3,2
Due to Participants	327,002,663	103,732,640	41,948,337	388,786,9
Total Liabilities	$ 327,029,772	$ 103,741,084	$ 41,980,654	$ 388,790,2

	Balance 7/1/96	Additions	Deductions	Balan 6/30/
Health Insurance Administration Agency Fund				
Assets				
Cash	$ 10,947,562	$ 49,562,513	$ 48,131,150	$ 12,378,9
Accrued Interest	58,285	63,401	58,285	63,4
Total Assets	$ 11,005,847	$ 49,625,914	$ 48,189,435	$ 12,442,3
Liabilities				
Accounts Payable	$ 447,894	$ 2,102,691	$ 447,894	$ 2,102,6
Trust Funds Payable	10,557,953	50,212,186	50,430,504	10,339,6
Total Liabilities	$ 11,005,847	$ 52,314,877	$ 50,878,398	$ 12,442,3

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

Notes to the Financial Statements
June 30, 1997

Employee and Retiree Members	
Retirees and beneficiaries currently receiving benefits:	
	6/30/97
General	64,685
Police and Fire	3,764
Total	68,449
Current employees and terminated employees entitled to benefits but not yet receiving them:	
Vested:	
General	124,251
Police and Fire	8,533
Nonvested:	
General	49,547
Police and Fire	2,780
Total	185,111

Employer Members	
	6/30/97
State Agencies	110
Political Subdivisions	448
Community Colleges	17
School Districts	233
Total	808

(1) Description of Plan

A. Plan Membership

The Oregon Public Employees Retirement System (PERS or "the System") is a statewide defined benefit retirement plan for units of state government, political subdivisions, community colleges, and school districts. PERS is administered under Oregon Revised Statutes (ORS) Chapter 238 by the Public Employees Retirement Board (PERB). For state agencies, community colleges, and school districts, PERS is a cost-sharing, multiple-employer system. It is an agent multiple-employer system for political subdivisions. Participation by state government units, school districts, and community colleges is mandatory. Participation by most political subdivisions is optional but irrevocable if elected.

For many years, retirement programs for Oregon judges were administered by special legislation and programs under the Judges Retirement Fund (JRF), established in 1963 under ORS 1.314 to 1.380. Effective August 1, 1991, the Judges Retirement Fund was merged into the Public Employees Retirement Fund.

The 1995 Legislature enacted Chapter 654, Section 3, Oregon Laws 1995 which has been codified into ORS 238.435. This legislation created a second tier of benefits for persons who established membership on or after January 1, 1996. The second tier provides a lower benefit structure than is available to Tier One members. Any potential reductions in employer contribution rates will not be realized until turnover has occurred and Tier Two members replace Tier One members. As of December 31, 1996, there were 13,499 Tier Two members in the system.

B. Plan Benefits

a. Pension Benefits

The PERS retirement allowance is payable monthly for life. It may be selected from 12 retirement benefit options. These options include survivorship benefits and lump-sum refunds. The basic benefit is based on years of service and final average salary. A percentage (2.00 percent for police and fire employees, 1.67 percent for general service employees) is multiplied by the number of years of service and the final average salary. Benefits may also be calculated under either a formula plus annuity (for members who were contributing before August 21, 1981) or a money match computation, if a greater benefit results. Monthly payments must be a minimum of $30 per month or the member will receive a lump sum payment of the actuarial equivalence of benefits to which they are entitled.

Police and fire members may purchase increased benefits that are payable between the date of retirement and age 65.

A member is considered vested and will be eligible at minimum retirement age for a service retirement allowance if he or she has had a contribution in each of five calendar years or has reached at least 50 years of age before ceasing employment with a participating employer (age 45 for police and fire members). General service employees may retire after reaching age 55. Police and fire members are eligible after reaching age 50. Members with 30 years of service (25 years for police and fire members at age 50) receive unreduced benefits. General service employee benefits are reduced if retirement occurs prior to age 58 with less than 30 years of service. Police and fire member benefits are reduced if retirement occurs prior to age 55 with less than 25 years of service.

Tier Two members are eligible for full benefits at age 60.

A judge member who has made contributions to the PERS Fund during each of five calendar years shall receive a retirement allowance, payable monthly, for life. Before reaching age 60, judge members must choose the calculation formula under which they will retire. The election is irrevocable after the member attains age 60. The two formulas, A and B, are described below.

The Plan A retirement allowance for judge members is computed by multiplying 2.8125 percent by the final average salary for the first 16 years of service, and 1.67 percent of the final average salary multiplied by the number of years of service as a judge in excess of 16. For most judge members the maximum amount is limited to 65 percent of final average salary.

The Plan B retirement allowance for judge members is computed by multiplying 3.0 percent by the final average salary for the first 16 years of service, and 1.75 percent of the final average salary multiplied by the number of years of service as a judge in excess of 16. For most judge members the maximum amount is limited to 65 percent of final average salary. Plan B requires a judge to serve up to 35 days per year for a period of five years as a pro-tem judge. There is no actuarial reduction for retirement prior to age 65.

Judges Retirement System (JRS) members were entitled to a monthly amount equal to one twelfth of final average salary upon reaching age 65 with 16 years of service or at age 70 with 12 years of service.

b. Death Benefits

Upon the death of a non-retired member, the beneficiary receives a lump-sum refund of the member's account balance (accumulated contributions and interest). In addition, the beneficiary will receive a lump-sum payment from employer funds equal to the account balance, provided that one or more of the following is true:

- The member was employed by a PERS employer at the time of death;
- The member died within 120 days after termination of PERS-covered employment;
- The member died as a result of injury sustained while employed in a PERS-covered job;
- The member is on an official leave of absence from a PERS-covered job at the time of death.

A member's beneficiary may choose a monthly payment for life instead of the lump sum, or a combination of lump sum and monthly payments, if eligible. The monthly payment must be a minimum of $30 per month.

Surviving spouses of JRS members and judge members of PERS receive benefits as provided in ORS 238.055 and ORS 238.565.

c. Disability Benefits

A member with ten or more years of creditable service who becomes disabled from other than duty-connected causes may receive a non-duty disability benefit. A disability resulting from a job-incurred injury or illness qualifies a member (including judge members of PERS) for disability benefits regardless of the length of PERS-covered service. Upon qualifying for either a non-duty or duty disability, service time is computed to age 58 (55 for police and fire members) when determining the monthly benefit.

Judge members of PERS who have served a minimum of six consecutive years and who become physically or mentally incapacitated are entitled to benefits as provided in ORS 238.555.

d. Benefit Changes After Retirement

Members may choose to continue participation in a "variable" stock investment account after retiring, and may experience annual benefit fluctuations due to changes in the market value of equity investments.

Monthly benefits are adjusted annually for cost-of-living changes. Two percent per year is the maximum cost-of-living adjustment. Periodically, the Oregon Legislature has granted ad hoc increases to post-retirement benefits.

e. Postemployment Healthcare Benefits

Under ORS 238.410 the PERB contracts for medical and hospital insurance on behalf of retired members. Members and their dependents are eligible for PERS healthcare coverage if the member is receiving a retirement allowance or benefit under the system. A surviving spouse of a PERS retiree is eligible to participate if he or she was covered under the health plan at the time of the retiree's death.

ORS 238.420 establishes a PERS Retirement Health Insurance Account (RHIA) and authorizes a payment of up to $60 from RHIA toward the monthly cost of health insurance for eligible PERS members.

To be eligible to receive this monthly payment toward the premium cost, the member must: (l) have eight years or more of qualifying service in the PERS system at the time of retirement, or receive a disability allowance as if the member had eight years or more of creditable service in the PERS system, (2) receive both Medicare Parts A and B coverage, and (3) enroll in a PERS-sponsored health plan.

A surviving spouse or dependent of a deceased PERS retiree who was eligible to receive the subsidy is eligible to receive the subsidy if he or she (1) is receiving a retirement benefit or allowance from PERS, or (2) was insured at the time the member died and the member retired before May 1, 1991.

All PERS employers currently contribute 0.58 percent of PERS-covered salaries to fund RHIA benefits. This is included in the employer contribution rates listed on page 18. The employer contribution rate covers the normal cost payment and an amount to amortize the unfunded actuarial accrued liability over a 30-year period. Based on the December 31, 1995 actuarial valuation, this rate will increase to 0.65 percent of PERS-covered salaries paid on or after July 1, 1997.

The employers' contributions are advance-funded on an actuarially determined basis. Employers' actual contributions for the fiscal year ended June 30, 1997, were $26.1 million.

The number of active plan RHIA participants was 29,746 for the fiscal year ended June 30, 1997.

ORS 238.415 establishes the Retirement Health Insurance Premium Account (RHIPA) and requires the PERB on or before January 1 of each year to calculate the average difference between the health insurance premiums paid by retired state employees under contracts entered into by the PERB and health insurance premiums paid by state employees who are not retired. ORS 238.415 authorizes payment of this average difference to qualified retired state employees. Retired state employees are qualified to receive this benefit if they had eight or more years of qualifying service in the system at the time of retirement or are receiving a disability pension calculated as if they had eight or more years of qualifying service, but are not eligible for federal Medicare coverage.

A surviving spouse or dependent of a deceased retired state employee is eligible to receive the subsidy if he or she (1) is receiving a retirement benefit or allowance from PERS, or (2) was insured at the time the member died and the member retired on or after September 29, 1991.

Currently state agencies contribute 0.18 percent of PERS-covered salaries to fund RHIPA benefits. Based on the December 31, 1995 actuarial valuation, this rate will decrease to 0.16 percent of PERS-covered salaries paid on or after July 1, 1997.

Based on the December 31, 1995 actuarial valuation, the actuarial accrued liability for postemployment healthcare benefits, using the entry age actuarial cost method, was $454.6 million and the actuarial value of assets was $(6.0) million. Therefore, the unfunded actuarial accrued liability, the excess of the actuarial accrued liability over the actuarial value of assets, totaled $460.6 million.

The postemployment benefit obligation was determined as part of an actuarial valuation prepared by the PERS consulting actuary at December 31, 1995. Significant assumptions used in the actuarial update include (1) a rate of return on the investment of present and future assets of 8.0 percent per year compounded annually, and (2) additional projected salary increases attributable to seniority and merit.

The inflation assumption for postemployment benefits is 0 percent because the RHIA payments amount is set by statute and is not adjusted for increases in healthcare costs.

The number of active plan RHIPA participants was 772 for the fiscal year ended June 30, 1997.

(2) Summary of Significant Accounting Policies and Investment Valuation Method

A. Basis of Presentation

The accompanying financial statements are prepared in accordance with Governmental Accounting Standards Board Statements 25 and 26, as well as generally accepted accounting principles that apply to governmental accounting for fiduciary funds. Fiduciary funds are used to account for assets held by a governmental unit in a trustee capacity (trust funds), or as an agent for another entity (agency funds).

The activities of PERS are accounted for in two fund types.

Pension Trust Fund

- Public Employees Retirement Fund

Agency Funds

- Deferred Compensation Agency Fund
- Retirement Health Insurance Administration Agency Fund

B. Basis of Accounting

The accrual basis of accounting is used for Pension Trust Funds. Revenues are recognized when earned. Expenses are recognized when incurred.

Agency funds are custodial in nature and do not measure the results of operations.

The modified accrual basis is used to record assets and liabilities of agency funds. Under the modified accrual basis, revenues are recognized when they are both available and measurable. Expenses are recognized when incurred.

C. Budgetary Data

Only administrative expenses are subject to biennial legislative budget control. The Legislature exercises this control at the agency level. Any unobligated balance lapses at the end of each biennium.

Encumbrance accounting is allowed only during the biennium. All encumbrances lapse at the end of the biennium except capital construction, capital improvements, and contested claims.

Budgetary accounting is not consistent with generally accepted accounting principles (GAAP) because the measurement focus is on decreases in financial resources rather than net income determination.

The accompanying schedule reconciles administrative expenses on the budgetary basis to administrative expenses presented on the Statements of Changes in Plan Net Assets. The Legislatively Approved Budget includes increases approved by the Legislative Emergency Board through June 1997.

	Legislatively Approved Budget Less Unscheduled Amts.	Actual	Favorable Variance
1995-1997 Biennium:			
Personal Services	$ 14,530,393	$ 13,563,845	$ 966,548
Services and Supplies	13,454,275	14,024,742	(570,467)
Capital Outlays	361,907	332,719	29,188
Debt Service	767,477	602,044	165,433
1995-1997 Totals	$ 29,114,052	$ 28,523,350	$ 590,702

Total Expenses July 1, 1995 - June 30, 1997	
Budgetary Basis (non GAAP)	$ 28,523,350
Biennium Adjustments to Administrative Expenses	
Add:	
Depreciation Expense	92,583
Decrease in Supplies Inventory	4,499
Increases in Compensated Absences	25,309
Adjustments from Prior Year	15,905
Amounts Expended in Capital Construction Budget	560,569
Deduct:	
Capitalization of COP Interest Expense per FASB 62	602,044
Capital Outlay, July 1, 1996 - June 30, 1997	241,825
Increase in Prepaid Expense	8,743
Expenditures from July 1, 1995 - June 30, 1996	13,692,997
Financial Statement Total for the year ended June 30, 1997	$ 14,676,606

D. Valuation of Investments

Investments are recognized at fair value, which is the amount at which financial instruments could be exchanged in a current transaction between willing parties, other than in a forced or liquidation sale. Open-end mutual funds, debt securities, and equity securities, option contracts, stock warrants, and stock rights are valued at the last reported sales price if there is an active market for the investment. If there is not an active market for investments, PERS relies on the Oregon Investment Council's consultants to establish the fair value of these investments. When attempting to value investments without active markets, the consultant determines if there is a market for similar investments. If a market price is not available, a forecast of expected cash flows may be used in estimating fair value, discounted at a rate commensurate with the risk involved.

E. Distribution of Earnings

Earnings distribution to members, by law, is made on a calendar year basis Members in Tier One are guaranteed to receive at least the assumed earning rate used in the most recent actuarial valuation. At this time that rate is 8.0 percent. Members participating in the Variable Account and Tier Two member receive actual earnings or losses.

(3) Contributions and Reserves

A. Contributions

	State Agencies and Community Colleges	Schools	Political Subdivisions: Police and Fire	Political Subdivisions: General	Judiciary
Employee Normal Cost	6.00%	6.00%	6.00%	6.00%	7.00%
Employer Normal Cost	7.10%	8.28%	9.91%	5.27%	14.25%
Unfunded Actuarial Liability	0.60	1.02	.85	1.85	5.46
Healthcare Benefits	0.76	0.58	0.58	0.58	0.76
Total Employer Rates	8.46%	9.88%	12.34%	7.70%	20.47%

a. Member Contributions

Member contributions are set by statute at fou to seven percent of salary. They are remitted b participating employers. The contributions ar either deducted from member salaries or paid b the employers. The Member Reserve represent member contributions and earnings allocation less refunds and amounts transferred to reserve for retirement and disability.

b. Employer Contributions

Employer contribution rates are determined b an actuarial formula known as the "entry age cos method." Under this method, a "normal cost" rat for each member is calculated. Normal cost is a level percentage of salary. Beginning at the member's entry into the system, it will accumulate ar amount sufficient to provide the member's retirement benefit. After the unfunded supplementa present value created by this method has been determined, the employer contribution rates are established as a level percentage of salary. The rates are set tc cover the normal cost and amortize the unfunded amount over a 30-year period commencing on the actuarial valuation date.

Based on the 1993 actuarial valuation, the Board decided to implement recommended contribution rate decreases, beginning July 1, 1995. Where contributior rate increases were required, beyond increases scheduled for July 1995, implementation will be effective July 1, 1997.

PERS funding policy provides for monthly employer contributions at actuarially determined rates. These contributions, expressed as a level percentage of annual covered payroll, coupled with employee contributions, accumulate sufficient assets to pay benefits when due.

Separate contribution rates are adopted by the Retirement Board for all state agencies and community colleges combined, all school districts combined, the state judiciary, and each individual political subdivision employer. The rates adopted by the Board and actually paid by the employers were those recommended by the actuary after each valuation and after legislative changes enacted subsequent to the valuations.

Employer aggregate contributions to the PERF for the calendar year ended December 31, 1996, were $462.5 million less $11.7 million for integration of prior plan assets by employers merging into the System and $2.0 million pertaining to prior year's salaries, for a total of $448.8 million attributable to calendar year 1996 activity. Employer contributions attributable to the period were equivalent to 8.77 percent of the members' aggregate annual salaries of $5,117.8 million. Employee contributions for the calendar year ended December 31, 1996, were $297.7 million less $0.4 million for integration of prior plan assets of employees merging into the system and $7.4 million of contributions pertaining to prior year's salaries for a total of $289.9 million employee contributions attributable to calendar year 1996 activity.

Employer contributions for the calendar year ended December 31, 1996, consisted of $359.2 million normal cost, $57.6 million amortization of the unfunded actuarial accrued liability, and $31.9 million to fund the Retirement Health Insurance Account.

Based on the actuarial valuation as of December 31, 1993, state agencies and certain political subdivisions received a lower employer contribution rate. The schools, judiciary, and other political subdivisions experienced an increase in their employer contribution rate. The PERB decided to implement the new employer contribution rates for those employers who experienced a decrease and to delay implementation of the new employer contribution rate for those employers who experienced an increase in their employer contribution rate.

The employer contribution rate for state agencies and community colleges is 8.46 percent and judiciary is 20.47 percent of PERS-covered salaries, effective July 1, 1995. New employer contribution rates for state agencies will be 8.20 percent and for schools will be 9.93 percent of PERS-covered salaries, effective July 1, 1997.

Amounts actually contributed by employers were in accordance with actuarially computed funding requirements of the December 31, 1993, actuarial valuation. Employer contributions consist of three components: a normal cost rate, an unfunded actuarial accrued liability rate, and a rate for postemployment healthcare benefits. Actual employer rates varied among the employer groups.

The rates for political subdivisions are presented in the aggregate. Actual rates for political subdivisions vary by employer.

B. Actuarial Cost Method and Assumptions

Employer contribution rates are set using the entry age actuarial cost method. This method produces an employer contribution rate consisting of (1) an amount for normal cost (the estimated amount necessary to finance benefits earned by the employees during the current service year), (2) an amount for amortization of the unfunded actuarial accrued liability over a period of 30 years, and (3) an actuarially determined amount for funding postemployment healthcare subsidies.

C. Reserves and Designations

a. Member Reserve

The Member Reserve of $6,914,751,167 as of June 30, 1997, represents member contributions and earnings allocations less refunds and amounts transferred to reserves for retirements and disabilities.

b. Employer Reserve

The Employer Reserve of $6,855,677,317 as of June 30, 1997, represents employer contributions and earnings allocations less amounts transferred to reserves for retirements and disabilities.

c. Benefit Reserve

The Benefit Reserve of $8,539,104,295 as of June 30, 1997, is the amount set aside to pay future benefits. The amount needed is determined by the PERS actuary. It includes funds initially included in the Employer and Member Reserves. The balance includes $343.8 million resulting from the change in accounting principle (see note 12).

d. Undistributed Investment Earnings Reserve

The Undistributed Investment Earnings Reserve may be credited with investment earnings in excess of required minimum distributions. As of June 30, 1997, the balance of this reserve was $2,749,435,189.

Oregon law requires individual accounts for Tier One members to be credited at the assumed rate of return on investments adopted by the PERB for use in actuarial valuations.

e. Unallocated Earnings Designation

The Unallocated Earnings Designation represents January through June investment earnings less administrative expenses which will be distributed after member accounts have been credited with contributions. This distribution takes place in March of the following year after Employer Annual Reports have been reconciled and contributions posted to individual member and employer accounts. As of June 30, 1997, the balance of this designation was $3,065,443,726. This balance includes $951,750,758 resulting from the change in accounting principle (see note 12).

f. Retirement Health Insurance Account

The RHIA plan net assets balance represents the debt assumed upon the dissolving of the Retirement Health Insurance Trust Fund (RHITF) pursuant to ORS 238.420, and RHIA's accumulation of employer contributions and interest earnings less premiums paid and administrative and interest expenses. Oregon law requires that the debt assumed from RHITF be satisfied on an amortization schedule established by the PERS Board out of employer contributions to the RHIA or earnings thereon. As of June 30, 1997, the balance of this account was $5,947,374.

g. Retirement Health Insurance Premium Account

The RHIPA plan net assets balance represents the program's accumulation of employer contributions and interest earnings, less premiums and administrative and interest expenses. As of June 30, 1997, the balance of this account was a $62,913 deficit.

D. Administrative Costs

Costs for administering the System come from investment earnings and are allocated to all plans and programs administered by the System.

(4) Reporting Entity

The Public Employees Retirement Board is the governing authority of the System. It consists of eleven persons appointed by the Governor and subject to confirmation by the State Senate. The Board appoints an executive director to act as the principal administrative officer of the System. The Board has independence in the operation and management of the System. The State Legislature has significant ability to influence funding, approve the System's budget, and pass laws governing the System.

PERS' financial statements are prepared on the basis of a fiscal year ended June 30. The Oregon State Treasury has statutory responsibility for custody and investment of PERS assets. As a result of this fiduciary responsibility, PERS is included as part of the primary government in the State of Oregon Comprehensive Annual Financial Report.

(5) Assets Used in Plan Operations

A. Building and Improvements

Capital construction of PERS headquarters in Tigard, Oregon was completed May 31, 1997. Land and buildings plus improvements are recorded at cost. PERS capitalized $179,869 of net interest expense in the current year as part of the project's construction costs. The depreciation of the building/improvements is computed on the straight-line method over the useful life of 40 years.

B. Equipment and Fixtures

Equipment and fixtures are recorded at historical cost, and are items which are not consumed in the normal course of operations, have a useful life of more than two years, and whose value is $5,000 or more. Depreciation is computed on the straight-line method over the estimated useful lives of the assets. Useful lives range from three to ten years.

C. Office Supplies Inventory

Office supplies inventory is reflected at cost, using the first-in/first-out (FIFO) method.

(6) Deposits and Investments

A. Cash

PERS cash and cash equivalents are considered to be cash on hand, demand deposits and deposits in the Oregon Short Term Fund, and are carried at cost.

The carrying amount is separately displayed on the balance sheet as cash. Statutes require that all monies received by the pension trust fund be deposited with the State Treasurer.

PERS deposits are classified in three categories of credit risk to give an indication of the level of risk assumed by PERS as of year end. The three categories of credit risk are:

1. Insured or collateralized with securities held by the State Treasurer or its custodian in the name of the state of Oregon;
2. Collateralized with securities held by the pledging financial institution's trust department or custodian in the name of the state of Oregon, and
3. Uncollateralized.

As of June 30, 1997, all PERS deposits held by the State Treasurer were in credit risk category "1," except for $15,392,750 of reinvested cash collateral in U.S. Government and agency securities, repurchase agreements and commercial paper, which are classified as investment risk category "3."

Investment managers' deposits with custodian banks consist of cash and cash equivalents that represent buying reserves. There is $332.4 million on deposit for the accounts of the Oregon Equity Fund and Real Estate Investment Fund investment managers and $237.4 million on deposit for the accounts of the International Equity Fund and Global Fixed Income investment managers. These deposits, with State Street Bank, are classified as uncollateralized, category "3."

B. Investments

By statute, the Oregon Investment Council (OIC) is responsible for investment policy. The State Treasurer is the investment officer. The law allows any kind of investment that is prudent. Common stock acquisitions are limited to 50 percent of the monies contributed. The State Treasurer is prohibited from investing in common stock. OIC common stock investments are made by independent investment managers selected and evaluated by the Council.

GASB Statement No. 3 requires that investments be categorized to give an indication of the level of risk assumed at year end. Certain investment types in the PERS portfolio, such as equity real estate, mutual funds, leveraged buy outs, and Deferred Compensation, cannot be categorized within the guidelines established by GASB Statement No. 3. These investments total approximately $14,298.8 million in carrying value.

In accordance with State investment policies, several outside investment managers retained by the Council may invest in the following types of derivative securities: futures contracts, forwards, option contracts, collateralized mortgages obligations, mortgage-backed securities, interest rate and currency swaps, or other financial instruments with similar characteristics. These transactions are generally made to manage the overall risk of the individual managers' portfolios to a level satisfactory to the investment management firm and in accordance with their contract with the Council. For the year ended June 30, 1997, the credit risk, market risk, and legal risk for these investments are not above and beyond those risks that are apparent in the financial statements or are otherwise disclosed in the notes to the financial statements. Information regarding the derivative holdings of mutual funds, which may be held by certain investment management firms as a component of their portfolio, is not available.

PERS investments are classified in three categories of credit risk to give indication of the level of risk assumed by PERS as of year end. The three ca gories of credit risk are:

1) Insured or registered, or securities held by the state of Oregon or its agent the state of Oregon's name for PERS;
2) Uninsured and unregistered with securities held by the counterparty's tr department or agent in the state of Oregon's name for PERS, and
3) Uninsured and unregistered with securities held by the counterparty, or by trust department or agent but not in the state of Oregon's name for PERS.

The schedule below presents the carrying value and market value of the inve ments that were held by the state of Oregon for PERS as of June 30, 1997.

		Risk Category		Total Carrying Amount	Total Fair Value Amount
		2	3		
Pension Trust Fund Investments					
Investment Type:					
U.S. Government Obligations	$ 1,280,611,147	$	$	$ 1,280,611,147	$ 1,280,611,147
Domestic Corporate Obligations	1,868,406,763			1,868,406,763	1,868,406,763
Domestic Stocks	6,300,725,115			6,300,725,115	6,300,725,115
International Government & Corporate Obligations	1,192,642,453			1,192,642,453	1,192,642,453
International Stocks	2,298,237,408			2,298,237,408	2,298,237,408
Investments on securities loan for securities and Tri Party agreement collateral:					
U.S. Government Obligations	243,340,287			243,340,287	243,340,287
Domestic Stocks	33,794,719			33,794,719	33,794,719
International Government & Corporate Obligations	30,753,969			30,753,969	30,753,969
Unclassified as to Risk:					
Real Estate				1,693,187,990	1,693,187,990
Real Estate Mortgages				43,430,020	43,430,020
Leveraged Buy-outs				2,047,552,171	2,047,552,171
Venture Capital				25,177,117	25,177,117
Limited Partnerships				692,136,161	692,136,161
Domestic Mutual Funds				4,798,205,548	4,798,205,548
Global Mutual Funds				2,487,832,748	2,487,832,748
Investments held by broker-dealers under securities loans with cash collateral:					
U.S. Government Obligations				827,526,818	827,526,818
Domestic & International Stocks				070,370,318	,070,370,318
Domestic Corporate Obligations				25,889,382	25,889,382
International Government & Corporate Obligations				198,851,929	198,851,929
Total Pension Plan Investments	$ 13,248,511,861	$ -	$ -	$ 27,158,672,063	$ 27,158,672,063
Deferred Compensation Fund Unclassified Risk:	$	$ -	$	$ 388,659,480	$ 388,659,480
Total Deferred Compensation Fund Investments				388,659,480	388,659,480
Total PERS Investments	$ 13,248,511,861	$ -	$	$ 27,547,331,543	$ 27,547,331,543

C. Securities Lending

In accordance with State investment policies, the Oregon Public Employees Retirement Fund (OPERF) participates in securities lending transactions. The Oregon State Treasury has, through Securities Lending Authorization Agreements, authorized its custodians to lend its securities pursuant to a form of loan agreement. Both OPERF and the borrowers maintained the right to terminate all securities lending transactions on demand. There have been no significant violations of the provisions of securities lending agreements during the period of these financial statements.

During the year, OPERF engaged four separate custodians, one of which currently remains as lending agent as of June 30, 1997. The custodians lent short-term, fixed income, and equity securities and received as collateral U.S. dollar and foreign currency cash, U.S. government and agency securities, letters of credit, and foreign sovereign debt of Organization of Economic Cooperation and Development (OECD) countries. Borrowers were required to deliver collateral for each loan equal to not less than 102% of the market value of the loaned security, or 105% in the case of international securities. The custodians did not have the ability to pledge or sell collateral securities absent a borrower default and OPERF did not impose any restrictions during the fiscal year on the amount of the loans the custodians made on its behalf, except that one custodian had a broker credit limitation. OPERF is fully indemnified against losses due to borrower default by its current custodian. There were no losses during the year from the failure of borrowers to return loaned securities and no recoveries of amounts from prior losses.

Securities Loaned Fair Value		
US Government Obligations	$ 1,083,150,420	
Domestic Equity	750,388,993	
Domestic Fixed Income	26,374,290	
International Equity	354,521,159	
International Fixed Income	238,586,597	
Total		**$ 2,453,021,459**
Collateral Fair Value		
Cash	$ 2,207,897,389	
Securities	210,119,989	
Tri Party Agreements	110,999,224	
Total		**$ 2,529,016,602**

The maturities of investments made with cash collateral generally matched the maturities of the securities loans for two custodians, but generally did not match for the other two custodians. The maturities of investments of cash collateral at June 30, 1997, averaged 46 days. Since the securities loans are callable on demand by either the lender or borrower, the life of the loans at June 30, 1997, is effectively one day. On June 30, 1997, OPERF had no credit risk exposure to borrowers. The market value of the collateral held and the securities on loan from OPERF as of June 30, 1997, including accrued income, was $2,529,016, 602 and $2,453,021,459, respectively.

OPERF's cash balances are invested in the Oregon Short Term Fund (OSTF), as is the cash of other state agencies. As of June 30, 1997, the market values of the collateral held and the securities on loan, including accrued income, from the OSTF was $272,531,250 and $266,331,457, respectively. OPERF's allocated portion of the collateral held and securities on loan was $15,655,226 and $15,299,086 respectively.

The total cash collateral of $2,223,552,615 is not categorized as to risk.

(7) Leases

Operating leases are rental agreements where the payments on these leases are chargeable as rent and recorded in the services and supplies expenditure account. Should the Legislature disallow the necessary funding for particular leases, all lease agreements contain termination clauses which provide for cancellation of the lease as of the end of a fiscal year. Lease obligations decrease each year because of various lease expirations. It is expected that ongoing leases will be replaced with leases which have higher rental rates due to inflation. A substantial reduction in lease payments was achieved by the construction of the PERS headquarters building. The building was completed in June 1997.

The schedule above summarizes the minimum lease payments for operating leases in effect as of June 30, 1997.

	Operating Leases
1998	$ 11,265
1999	11,500
2000	960
2001	0
2002	0
Thereafter	0
Total Future Minimum Lease Payments	$ 23,725

(8) Deferred Compensation Plan

Deferred compensation plans are authorized under Internal Revenue Code Section 457. ORS 243.400 to 243.507 establishes the state program. ORS 243.410(2) provides for PERS to administer the Deferred Compensation Program for the state of Oregon for the benefit of eligible employees. The plan is a benefit available to all state employees wherein they may execute an individual agreement with the state deferring current earnings to be paid at a future date. Participants in the plan are not required to pay federal and state income taxes on the deferred earnings until the earnings are received. Participants or their beneficiaries cannot receive the funds until at least one of the following circumstances occur: termination by reason of resignation, death, retirement, or unforeseeable emergency.

Payments to participants may be made over a period not to exceed the life expectancy of the participant and/or spouse. There are also other options available such as lump sum distributions or a specified payment amount until the deferred balance is exhausted. Employees of higher education institutions may participate in deferred compensation plans other than the plan described in this footnote.

Funds accumulated by the state under its plan have been invested with various financial institutions, insurance companies, and the State Treasury.

In November 1996, a single-source record keeper began maintaining all of the participant record keeping for a new restructured program. The investment providers of the prior program will continue to provide record keeping for those participants receiving a distribution who did not select to transfer funds to the restructured program. Under the new program, there are now nine asset classifications. Three or more financial institutions provide investment services for each asset classification. A participant will receive a blend of these funds within the asset class. The asset classes include Short Term Fixed Income Option, Stable Value Fund Option, Intermediate Term Fixed Option, Balanced Option, Value Equity Option, Stock Index Option, Growth Equity Option, International Equity Option, and Aggressive Growth Option.

The Oregon Legislature enacted Chapter 179, Oregon Laws 1997 which established the Deferred Compensation Fund. Assets of the Deferred Compensation Program will be transferred to the Deferred Compensation Fund and held in trust for the exclusive benefit of the participants. As of June 30, 1997, the assets of the program had not been transferred to the Deferred Compensation Fund.

The state has no liability for losses under the plan but does have the duty of due care that would be required of an ordinary prudent investor.

Activity of the plan is accounted for in an agency fund. The investments are valued at market and totaled approximately $388.7 million as of June 30, 1997.

PERS may assess a charge to the participants not to exceed two percent on amounts deferred to cover costs incurred administering the program.

Oregon Revised Statute 243.505 establishes a Deferred Compensation Advisory Committee to provide input from participants. This committee meets at least quarterly and has five members.

(9) Retirement Health Insurance Administration Agency Fund

Oregon Revised Statute 238.410 directs the PERS Board to provide healthcare insurance, collect premiums, and deliver premiums to carriers providing coverage. The Retirement Health Insurance Administration Agency Fund is established to allow for the monthly cost of the coverage to be deducted from the retirement benefit of eligible members who elect to participate in a healthcare insurance plan, and to pay the amount due to the carrier providing the coverage.

(10) Long Term Debt

In 1992, PERF entered into an agreement to guarantee $50 million in taxable special revenue obligation bonds issued by the Port of Portland on behalf of a start-up aircraft maintenance company at Portland International Airport. The company ceased operations at the end of October 1993. Initial interest payments were made from a reserve fund established from bond sale proceeds. This reserve fund was depleted and interest payments from the retirement trust fund commenced in October 1994.

PERS has purchased a lease-hold interest in the facility. The value of any recovery cannot be estimated because it will depend on whether PERS can release or sell the facility, and on what terms. In October 1996, the attorney general filed a lawsuit against the owners of the company and the consulting firm that advised the investment. The civil lawsuit is expected to go to trial in April 1998 and will attempt to recover losses, but the value of any recovery cannot be estimated at this time.

The first table describes taxable obligation revenue bonds issued and outstanding guaranteed by the retirement fund.

Pamcorp Taxable Special Obligation Revenue Bonds Issued and Outstanding

	Amount Issued and Outstanding	Interest Rate	Due Date	Issue Date
Series "A"	$ 12,700,000	8.350%	May 15, 2010	June 1, 1992
Series "B"	9,800,000	8.875	May 15, 2015	June 1, 1992
Series "C"	27,000,000	9.200	May 15, 2022	June 1, 1992

The next table summarizes the amounts necessary to pay all future long-term guaranteed debt principal and interest requirements as of June 30, 1997, for each fiscal year during the next five-year period ending June 30, 2002, and in total for the succeeding period July 1, 2002, to June 30, 2022.

Debt Service Requirements to Maturity

Fiscal Year	Series "A" Principal	Interest	Series "B" Principal	Interest	Series "C" Principal	Interest	Total Principal	Total Interest	Total Expenses
1998	$ 600,000	$ 1,060,450	$ -	$ 869,750	$ -	$ 2,484,000	$ 600,000	$ 4,414,200	$ 5,014,200
1999	600,000	1,010,350	-	869,750	-	2,484,000	600,000	4,364,100	4,964,100
2000	700,000	960,250	-	869,750	-	2,484,000	700,000	4,314,000	5,014,000
2001	700,000	901,800	-	869,750	-	2,484,000	700,000	4,255,550	4,955,550
2002	800,000	843,350	-	869,750	-	2,484,000	800,000	4,197,100	4,997,100
2003-2022	9,300,000	3,815,950	9,800,000	9,682,628	27,000,000	44,077,200	46,100,000	57,575,778	103,675,778
	$ 12,700,000	$ 8,592,150	$ 9,800,000	$ 14,031,378	$ 27,000,000	$ 56,497,200	$ 49,500,000	$ 79,120,728	$ 128,620,728

In 1996, PERF purchased the land and began construction on a new retirement system headquarters building in Tigard, Oregon. The financing for the new building was done by the sale of certificates of participation. The certificates of participation were sold on March 16, 1996, for $8,565,000 at 5.45 percent interest rate with the final repayment due April 10, 2017. The table below summarizes all future certificates of participation payments of principal and interest as of June 30, 1997, for each fiscal year during the next five-year period, and the total for the succeeding period from July 1, 2003, to April 10, 2017.

PERS Building Debt Service Requirements to Maturity

Fiscal Year	Principal	Interest	Total Expenses
1998	$ 265,000	$ 446,692	$ 711,692
1999	275,000	436,092	711,092
2000	285,000	424,542	709,542
2001	300,000	412,003	712,003
2002	315,000	398,503	713,503
2003-2017	7,125,000	3,544,095	10,669,095
	$8,565,000	$5,661,927	$ 14,226,927

(11) Contingent Liabilities

On August 29, 1996, the Oregon Supreme Court reversed the November 15, 1995, rulings on two Marion County Circuit Court cases. These rulings had prohibited the implementation of the 1995 House Bill 3349. The Supreme Court agreed with lower court rulings that taxes paid on benefits earned to 1991 constituted a breach of contractual obligation. The Supreme Court also ruled, however, that HB 3349 was a legitimate remedy for damages, that employers rather than the state were obligated to fund the remedy, and that the retroactive benefits could be paid from the PERS Fund, to be reimbursed by an increase in employer contribution rates.

As a result of the Supreme Court's decision, an estimated $343.8 million in annuities, death benefits, and refunds due as of June 30, 1996, were accrued for the fiscal year ended June 30, 1996. As a result of implementing GASB Statement number 25, the effect of this accrual has been reversed, and beginning plan net assets have been restated to reflect only deductions attributable to benefits due and payable under the plan as of June 30, 1996. 1997 House Bill 2034 amended provisions of 1995 HB 3349 and allowed retroactive benefits of $305.5 million due retired members to be paid on September 12, 1997. In addition to the retroactive payment, ongoing benefits were increased approximately $6.3 million in our monthly pension roll, beginning with the benefits paid February 1, 1997. Retroactive benefits due to refunded accounts or beneficiaries of deceased members are being calculated at this time and are estimated to amount to approximately $30 million. The total estimated cost to employers for these additional benefits will be 26 approximately $1,300 million. The effect of these additional benefits has not been included in the schedule of funding progress, and will be funded by increased employer contributions based on future actuarial valuations.

On June 21, 1996, the Oregon Supreme Court invalidated Article XI, Sections 10, 11, and 12 of the Oregon Constitution (1994 Ballot Measure 8). The effect of this ruling is to require the recalculation of retirement benefits for approximately 2,300 members. These recalculations are now being done, with 1,639 recalculations remaining. It is estimated that monthly retiree benefits will increase by only $3 to $5 dollars per month and will increase the annual pension roll by $138,000.

(12) Change in Accounting Principle

PERS has implemented GASB Statements 25 and 26 for the period ended June 30, 1997. The beginning balance of net assets available for plan benefits and postemployment healthcare benefits has been restated to reflect the change due to valuing all investments at fair value, rather than at amortized cost. Also, as explained in note 11, net assets and liabilities have been restated to reflect only benefits and refunds due and payable under the plan. The cumulative effect of restating net assets available for the defined benefits plan and postemployment plans was an increase of $1,295.6 million.

Required Supplementary Information
Schedules of Funding Progress
(Dollar amounts in millions)

Valuation Date	Actuarial Liability	Valuation of Assets	Unfunded Assets as a % of Actuarial Liabilities	Accrued Liabilities (UAL)	Annual Active Member Payroll	UAL as a % of Annual Active Member Payroll
Pension Benefits						
12/31/95	$ 22,794.0	$ 20,963.6	92.0%	$ 1,830.4	$ 4,848.1	37.8%
12/31/93	18,614.7	17,560.1	94.3	1,054.6	4,466.8	23.6
12/31/91	14,378.7	14,679.4	102.1	(300.7)	3,887.5	(7.7)
Postemployment Healthcare Benefits - Retirement Health Insurance Account*						
12/31/95	$ 428.1	$ (3.4)	(0.8)%	$ 431.5	$ 4,848.1	8.9%
12/31/93	360.7	(6.8)	(1.9)	367.5	4,466.8	8.2
12/31/91	263.2	(11.5)	(4.4)	274.7	3,887.5	7.1
Postemployment Healthcare Benefits - Retirement Health Insurance Premium Account**						
12/31/95	$ 26.5	$ (2.6)	(9.8)%	$ 29.1	$ 1,581.5	1.8%
12/31/93	25.9	(1.3)	(5.0)	27.2	1,498.1	1.8
12/31/91	29.3	0.0	0.0	29.3	1,440.6	2.0

*The Retirement Health Insurance Account provides postemployment healthcare benefits for eligible members for all participating employers.

**The Retirement Health Insurance Premium Account provides postemployment benefits only for eligible members whc retired from state of Oregon employers. Required annual contributions did not begin until 7/1/95.

Required Supplementary Information
Schedules of Employer Contributions
(Dollar amounts in millions)

	Year Ended	Annual Required Contribution	Percentage Contributed
Pension Benefits			
	12/31/96	$ 432.1	100.0%
	12/31/95	401.4	100.0
	12/31/94	402.7	100.0
	12/31/93	399.7	100.0
	12/31/92	409.1	100.0
	12/31/91	404.8	100.0
Postemployment Healthcare Benefits - Retirement Health Insurance Account*			
	12/31/96	$ 28.0	100.0%
	12/31/95	24.6	100.0
	12/31/94	21.8	100.0
	12/31/93	21.4	100.0
	12/31/92	22.0	100.0
	12/31/91	23.2	100.0
Postemployment Healthcare Benefits - Retirement Health Insurance Premium Account**			
	12/31/96	$ 2.4	100.0%
	12/31/95	1.2	100.0

*The Retirement Health Insurance Account provides postemployment healthcare benefits for eligible members for all participating employers.

**The Retirement Health Insurance Premium Account provides postemployment benefits only for eligible members whc retired from state of Oregon employers. Required Annual Contributions did not begin until 7/1/95.

The information presented in the required supplementary schedules was determined as part of the actuarial valuations at the dates indicated. Additional information as of the latest actuarial valuation follows.

	PERS
Valuation Date	12/31/95
Actuarial cost method	Entry Age
Amortization method	Level percent of salary
Actuarial assumptions:	
Investment rate of return	8.0%
Projected salary increases	5.0%
Includes inflation at	4.5%
Cost of living adjustments	2.0%
Method used to value assets	Fair Value
Amortization period	30 years
Selection of amortization approach	Open

Schedule of Plan Net Assets
Defined Benefit Pension Plan
For the Year Ended
June 30, 1997

	Regular Account	Variable Account	Totals Defined Benefit Pension Plan
Assets:			
Cash and Cash Equivalents	$ 752,606,866	$ 39,565,041	$ 792,171,907
Receivables			
Employer	30,656,134	-	30,656,134
Employee	15,666,152	4,768,409	20,434,561
Interest and Dividends	118,299,062	129	118,299,191
Investment Sales	382,626,209	6,569,407	389,195,616
Total Receivables	547,247,557	1,337,945	558,585,502
Due from Other Funds	7,664,869	2,193,229	9,858,098
Investments:			
U.S. Government Obligations	2,351,478,252	-	2,351,478,252
Domestic Corporate Obligations	1,854,374,915	39,921,230	1,894,296,145
Domestic Stocks	6,220,244,107	830,124,886	7,050,368,993
Domestic Mutual Funds	4,212,439,976	585,765,572	4,798,205,548
International Government & Corporate Obligations	1,422,248,351		1,422,248,351
International Stocks	2,652,758,567		2,652,758,567
International Mutual Funds	2,487,832,748		2,487,832,748
Mortgages	43,430,020		43,430,020
Real Estate	1,693,187,990		1,693,187,990
Limited Partnerships	692,136,161		692,136,161
Venture Capital	25,177,117	-	25,177,117
Leveraged Buy-Outs	2,047,552,171	-	2,047,552,171
Total Investments	25,702,860,375	1,455,811,688	27,158,672,063
Securities Lending Cash Collateral	2,223,552,615		2,223,552,615
Prepaid Expenses	131,930		131,930
Equipment and Fixtures, Cost Net of Accumulated Depreciation at 1997 $1,105,330	712,469		712,469
Land & Buildings, Cost Net of Accumulated Depreciation 1997 $15,247	8,247,767		8,247,767
Office Supplies Inventory, Cost	5,107		5,107
Total Assets	29,243,029,555	1,508,907,903	30,751,937,458
Liabilities:			
Investment Purchases and Accrued Expenses	325,115,134	6,939,105	332,054,239
Deposits and Other Liabilities	11,293,048	127,212	11,420,260
Due To Other Funds	2,193,229	-	2,193,229
Bonds Payable	58,065,000		58,065,000
Securities Lending Cash Collateral Due Borrowers	2,223,552,615		2,223,552,615
Total Liabilities	2,620,219,026	7,066,317	2,627,285,343
Net Assets held in trust for pension benefits	$ 26,622,810,529	$ 1,501,841,586	$ 28,124,652,115

Schedule of Changes in Plan Net Assets
Defined Benefit Pension Plan
For the Year Ended
June 30, 1997

	Regular Account	Variable Account	Totals Defined Benefit Pension Plan
Additions			
Contributions			
Employer	$ 433,289,222	$ -	$ 433,289,222
Plan Member	240,235,623	63,487,710	303,723,333
Total Contributions	673,524,845	63,487,710	737,012,555
Investment Income			
Net Appreciation (Depreciation) in Fair Value of Investments	4,094,189,413	338,531,146	4,432,720,559
Interest, Dividends and Other Investment Income	571,382,419	-	571,382,419
Total Investment Income	4,665,571,832	338,531,146	5,004,102,978
Less Investment Expense	172,352,503	3,023,264	175,375,767
Net Investment Income	4,493,219,329	335,507,882	4,828,727,211
Other Income	749,047	-	749,047
Total Additions	5,167,493,221	398,995,592	5,566,488,813
Deductions			
Benefits	827,632,313	24,438,244	852,070,557
Death Benefits	4,437,394	-	4,437,394
Refunds of Contributions	50,241,710	2,300,357	52,542,067
Administrative Expense	12,482,062	745,221	13,227,283
Interaccount Transfers	(56,529,913)	56,529,913	-
Total Deductions	838,263,566	84,013,735	922,277,301
Net Increase	4,329,229,655	314,981,857	4,644,211,512
Net Assets held in trust for pension benefits			
Beginning of Year - Restated	22,293,580,874	1,186,859,729	23,480,440,603
End of Year	**$ 26,622,810,529**	**$ 1,501,841,586**	**$ 28,124,652,115**

Schedule of Plan Net Assets
Postemployment Healthcare Plan
June 30, 1997

	Retirement Health Insurance Account	Retirement Health Insurance Premium Account	Totals Postemployment Healthcare Plan
Assets:			
Cash and Cash Equivalents	$ 5,581,973	$ 3,630,090	$ 9,212,063
Receivables			
Employer	3,953,414	364,807	4,318,221
Employee			-
Interest and Dividends		16,458	16,458
Total Receivables	3,953,414	381,265	4,334,679
Total Assets	**9,535,387**	**4,011,355**	**13,546,742**
Liabilities:			
Accounts Payable and Accrued Expenses	-	648	648
Deposits and Other Liabilities	-	-	-
Due To Other Funds	3,588,013	4,073,620	7,661,633
Total Liabilities	**3,588,013**	**4,074,268**	**7,662,281**
Net Assets held in trust for postemployment healthcare benefits	**$ 5,947,374**	**$ (62,913)**	**$ 5,884,461**

Schedule of Changes in Plan Net Assets
Postemployment Healthcare Plan
For the Year Ended
June 30, 1997

	Retirement Health Insurance Account	Retirement Health Insurance Premium Account	Totals Postemployment Healthcare Plan
Additions			
Contributions			
Employer	$ 26,119,088	$ 2,370,788	$ 28,489,876
Total Contributions	26,119,088	2,370,788	28,489,876
Investment Income			
Interest, Dividends and Other Investment Income	1,269,860	153,496	1,423,356
Total Investment Income	1,269,860	153,496	1,423,356
Less Investment Expense	303,846	559,952	863,798
Net Investment Income	966,014	(406,456)	559,558
Total Additions	27,085,102	1,964,332	29,049,434
Deductions			
Healthcare Premium Subsidies	21,070,901	655,617	21,726,518
Administrative Expense	1,387,505	61,818	1,449,323
Total Deductions	22,458,406	717,435	23,175,841
Net Increase	4,626,696	1,246,897	5,873,593
Net Assets held in trust for postemployment healthcare benefits			
Beginning of Year	1,320,678	(1,309,810)	10,868
End of Year	$ 5,947,374	$ (62,913)	$ 5,884,461

Schedule of Administrative Expenses
For the Year Ended June 30, 1997

Personal Services:		
Staff Salaries	$ 5,016,938	
Social Security	383,875	
Retirement	729,759	
Insurance	678,269	
Assessments	113,288	
Total Personal Services		$ 6,922,129
Professional Services:		
Actuarial	109,200	
Data Processing	1,965,084	
Systems Study	69,500	
Audit	178,100	
Legal Counsel	159,855	
Medical Consultant	78,832	
Accounting Services	870,983	
Health Care Fees	1,390,822	
Total Professional Services		4,822,376
Communication:		
Printing	121,832	
Telephone	185,989	
Postage	375,317	
Travel	71,706	
Total Communication		754,844
Rentals:		
Office Space	627,912	
Equipment	37,678	
Total Rentals		665,590
Miscellaneous:		
Supplies	381,614	
Maintenance	152,719	
Office Moving Expenses	96,690	
Non-Capitalized Equipment	788,061	
Depreciation	92,583	
Total Miscellaneous		1,511,667
Total Administrative Expenses		**$ 14,676,606**

Payments to consultants are summarized in "Professional Services.

Summary of Investment Fees, Commissions, and Expenses
For the Year Ended June 30, 1997

International Equity Fund Manager Fees		
Acadian Asset Management, Inc.	$ 1,523,878	
Barclay's Global Investors (EAFE)	715,086	
Baring Asset Management Ltd.	1,112,925	
Clay Finlay, Inc.	1,344,136	
Cursitor-Eaton Asset Management	1,099,443	
DSI International Management	918,397	
Genesis Investment Management Ltd.	1,302,222	
Marvin & Palmer Associates	1,311,055	
Nomura Capital Management	795,418	
Rowe, Price-Fleming, Inc.	3,213,456	
Total International Equity Fund Manager Fees		$ 13,336,016
Oregon Equity Fund Managers Fees		
Alliance Capital	795,701	
Barclay's Global Investors (all funds) Transition Fee	655,398	
Barclay's Global Investors (all funds)	512,534	
Becker Capital	289,071	
Brown Capital	501,059	
Columbia Management	1,438,434	
Equinox	1,487,741	
Fiduciary Trust	357,848	
Froley-Revy Investment Company	1,219,932	
Harris (Wanger) Associates	1,757,730	
Hotchkis & Wiley	1,942,663	
Nicholas Applegate	2,868,971	
Oak Associates	505,525	
Palisade Capital	392,302	
RCB Trust Company	541,152	
Sanford Bernstein	1,749,177	
Thompson/Rubenstein Investors	897,988	
Wellington	464,136	
Zesiger Capital Group	1,513,752	
Total Oregon Equity Fund Manager Fees		19,891,114
Global Fixed Income Managers Fees		
Mercury Asset Management	515,464	
Rogge Global Partners	563,968	
Total Global Fixed Income Managers Fees		,079,432
Real Estate Investment Fund		
La Salle Advisors (Alex Brown Realty)		835,190
Leveraged Buyout		
KKR		11,224,285
Custodial Fees for Investment Managers		
Oregon Equity - First Interstate Bank	221,077	
Oregon Equity - Morgan Stanley	216,673	
International Fund - Morgan Stanley	2,930,561	
Total Custodial Fees for Investment Managers		368,311
Alternative Equity Managers Fees		
Canterbury Mezz	370,227	
Castle Harlan	651,140	
CVC European	902,418	
Doughty Hanson	665,549	
Hicks Muse	1,697,890	
JLL Inc.	1,065,517	
Other Alternative Equity Fees	2,482,688	
Penman Partners	491,271	
Providence	1,521,458	
Stonington Ptr	492,972	
TCW/Crescent	39,590	
TPG Partners	884,856	
TSG Fund	799,784	
Zell Chilmark	256,071	
Total Alternative Equity Managers Fees		12,321,431
Real Estate Fees and Expenses		8,868,474
Real Estate Bond		4,986,790
State Treasury Fees		1,559,838
Securities Lending		79,550,979
Commission Recapture Expenses		1,274,267
Brokerage Commissions		15,394,339
Other Investment Fees and Expenses		1,685,301
Total Investment Fees, Commissions and Expenses Defined Benefit Plan		**$ 175,375,767**

Facts About the Secretary of State Audits Division

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Directory of Key Officials

Director	John N. Lattimer
Deputy Director	Sharron E. Walker, CPA, CFE
Deputy Director	Catherine E. Pollino, CGFM

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