Ohio Police & Fire Pension Fund

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April 25, 2007

Aristotle Hutras
Ohio Retirement Study Council
88 East Broad St. Suite 1175
Columbus, OH 43215

Dear Mr. Hutras,

In the spring of 2006, the Ohio Police & Fire Pension Fund (OP&F) submitted a plan recommending several changes, which would result in the system complying with the state's 30-year funding requirement. Most of these recommendations relied on legislative action for implementation.

Since that time, the OP&F investment portfolio has achieved impressive returns, and our Board of Trustees developed a new retiree health care plan design that will result in additional cost savings compared to previous years, as we communicated in the original plan. Despite these achievements, OP&F's funding period remains outside the 30-year requirement. While we expect some additional savings when the 2008 health care plan design is implemented, we have reached the limit of what we can do regarding our previously submitted plan. Any further changes in the funding system must be addressed by the General Assembly.

The Board of Trustees remains committed to our recommendations of April 2006. If the gradual contribution increases for active members and employers are implemented, along with a cap for Medicare Part B reimbursements, we are confident that OP&F will be able to reach the 30-year goal within the next few years. Please keep in mind that our initial projections were based on the implementation of funding changes by January 1, 2007. These projections would differ somewhat by any legislation on OP&F's funding formula enacted after this date.

As we addressed during our presentation last April, the poor investment returns encountered from 2000-2002 are still actuarially accounted for due to the "smoothing" technique used when calculating our valuation report. We anticipate our funding status will gradually improve when the last of these negative investment years (2002) is accounted for.

If no action is taken in regards to the contribution recommendations presented last year, and assuming an actuarial rate of return of 8.25 percent annually, we project that our funding period will eventually drop to 48.6 years by 2016. While this is a marked improvement over the current "infinite" status, it still does not get us to the state-mandated 30 years.

Enclosed are the following materials:

- A copy of the funding recommendations presented to the ORSC in April 2006 (Exhibit A)
- A 10-year projection of our funding period and funded ratio if contribution rates remain unchanged and our current assumed investment rate of return (Exhibit B)
- A series of 10-year projections if contribution rates remain unchanged and using varying investment performance scenarios (Exhibit C, pages 1-3)
- Excerpts from *Standard & Poor's Public Finance Report*, released February 27, 2007 (Exhibit D)

If there are any questions concerning our recommendations, please do not hesitate to contact me. As always, we will reply promptly.

Sincerely,

William J. Estabrook

William J. Estabrook
Executive Director

cc: OP&F Board of Trustees

Enclosures

Exhibit A:
OP&F 30-year funding plan presented to the Ohio Retirement Study Council, April 12, 2006

Reaching the 30-year funding period
(recommendations and estimates)

Proposed Items Each item builds on the item before	**OP&F's UAL**	**Projected Funding Period**	**Funding Ratio**	**OP&F Health Care Expenses**	**Where employer contributions go:** Pensions	 To UAL	 Health Care	 Total	**Employer Contribution % required for a 15-year solvency period for health care**	**Funding Period if additional portion of employer contribution is allocated to UAL (year when 30-yr. funding achieved)**
Current	$2,207,588,000	Infinite	80.9%	$133,494,000	10.94%	2.87%	7.75%	21.56%	N/A	Infinite (NA)
HC Plan Implementation 1/1/2007	$2,207,588,000	Infinite	80.9%	$118,296,000	10.94%	2.87%	7.75%	21.56%	7.50%	Infinite (NA) (additional 0.25%)
Revised HC Subsidies -Pre-1986 retirees: 75% for members, 50% for dependents -Post-1986 retirees: 75% for members, 25% for dependents	$2,207,588,000	Infinite	80.9%	$99,701,000	10.94%	2.87%	7.75%	21.56%	6.90%	Infinite (NA) (additional 0.85%)
Medicare Part B Cap reimbursement at $115	$2,207,588,000	Infinite	80.9%	$99,701,000	10.94%	2.87%	7.75%	21.56%	6.75%	Infinite (NA) (additional 1.0%)
Increase Police Employer contribution rate 2007: to 20% 2008: to 21% 2009: to 22% 2010: to 23% 2011: to 24%	$2,207,588,000	Infinite	80.9%	$99,701,000	10.94% 10.94% 10.94% 10.94% 10.94%	3.14% 3.68% 4.22% 4.77% 5.31%	7.75% 7.75% 7.75% 7.75% 7.75%	21.83% 22.37% 22.91% 23.46% 24.00%	6.75%	54 yrs. (45 yrs. In 2015) (additional 1.0%)
Increase Active Member contribution rate 2007: to 10.5% 2008: to 11% 2009: to 11.5% 2010: to 11.75% 2011: to 12%	$2,229,227,000	41 (33 yrs: 2015	80.7%	$99,701,000	10.59% 10.09% 9.59% 9.34% 9.09%	3.49% 4.53% 5.57% 6.37% 7.16%	7.75% 7.75% 7.75% 7.75% 7.75%	21.83% 22.37% 22.91% 23.46% 24.00%	6.75%	31 yrs. (30 yrs. In 2008) (additional 1.0%)
Coverage for Medicare-eligibles These members receive subsidized medical coverage on a 3rd party basis only	$2,229,227,000	41 (33 yrs: 2015	80.7%	$99,701,000	9.09%	7.16%	7.75%	24.00%	6.75%	31 yrs. (30 yrs. In 2008) (additional 1.0%)

Shared Accountability

Ohio Police & Fire Pension Fund

Retirees

Health Care

Currently, 7.75 percent of the employers contributions are directed toward health care

- Health care plan changes reduce this percentage, directing more toward the unfunded liability

Additional plan changes include:

- Elimination of HMOs
- Medicare–eligible members will receive subsidized coverage on a 3rd party basis only (to be implemented Jan. 1, 2008)
- A revised health care subsidy percentage
- A lifetime maximum established at $2.5 million
- Health care plan changes are effective Jan. 1, 2007

2007 Health Care Plan

COVERAGES & OPTIONS REDUCED:

One option, one provider by 2008
(Previously, three option levels and five providers were available)
Annual Deductible—Individual
Annual Deductible—Family
Annual out of pocket—Individual
Annual out of pocket—Family
Physician Office Visit
Emergency Department
Urgent Care
Hospital In–patient Services:
- Prior Admission testing
- Scheduled in–patient admit
- Emergency in–patient admit

Ambulatory surgery center
Mental Health (no annual maximum):
- Scheduled in–patient admit
- Emergency in–patient admit
- Out–patient

Substance Abuse ($3,100 annual maximum):
- Scheduled in–patient admit
- Emergency in–patient admit
- Out–patient

Therapies
Chiropractor
Skilled nursing facility
Sub–acute rehabilitation center
Prescription Drugs, Retail
- Generic, Preferred and Non–preferred

Prescription Drugs, Mail
- Generic, Preferred and Non–preferred

NO CHANGES:

*Co–Insurance
*Diagnostic lab/x–ray
*Preventive Care
*Durable medical equipment
*Home health care services
*Private duty nursing

** In 2007, the only change for these items is the amount of the out-of-network reimbursement, which went from 70% to the current 50%.*

Active Members

Active Member Contributions

The OP&F Board recommends a contribution rate increase of two percent for all active members

- The current rate is 10 percent for active members
- The increase to 12 percent will be implemented gradually, over a five–year period, beginning Jan. 1, 2007

Retiree Medical Trust

The establishment of a Retiree Medical Trust will assist our active members in paying for health care expenses in retirement

- A cost–neutral benefit to OP&F members
- Provides a funding source for medical expenses in retirement
- Active members will contribute to their individual trusts through out their careers
- Funding for the Retiree Medical Trust requires an additional contribution from active members

General Assembly

Employer Contributions

The OP&F Board recommends equalizing the police and fire employer contribution rates

- Current Fire employer rate is 24 percent
- Current Police employer rate is 19.5 percent
- Equalize the Fire and Police rates at 24 percent
- The increase to 24 percent will be implemented over a five–year period, beginning Jan. 1, 2007

Cap On Medicare Part B Reimbursements

- The OP&F Board recommends capping Medicare Part B reimbursements at $115 per month
- The 2006 monthly premium is $88.50
- Annual increases have averaged 10 to 12 percent
- It is anticipated that the premium will surpass the cap amount by 2009

Exhibit B: 10 year projection with assumed investment return of 8.25%

OP&F Simplified 10-Year Projection of Pension Liability, Assets and Funding Period

($ amounts in billions)

	Actual	Projected									
	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016
Asset Performance During Year											
Actual investment return during the year	15.96%	8.25%	8.25%	8.25%	8.25%	8.25%	8.25%	8.25%	8.25%	8.25%	n/a
Contributions During Year											
Police - Employer Rate	19.50%	19.50%	19.50%	19.50%	19.50%	19.50%	19.50%	19.50%	19.50%	19.50%	19.50%
Fire - Employer Rate	24.00%	24.00%	24.00%	24.00%	24.00%	24.00%	24.00%	24.00%	24.00%	24.00%	24.00%
Health Care Allocation	7.75%	6.75%	6.75%	6.75%	6.75%	6.75%	6.75%	6.75%	6.75%	6.75%	6.75%
Valuation Results As of January 1											
Actuarial Accrued Liability	$ 12.2	$ 12.8	$ 13.4	$ 14.0	$ 14.7	$ 15.5	$ 16.2	$ 17.0	$ 17.9	$ 18.8	$ 19.7
Market-Related Value of Assets	9.6	10.2	11.2	12.0	12.8	13.6	14.3	15.1	15.9	16.7	17.6
Unfunded Accrued Liability	$ 2.6	$ 2.6	$ 2.2	$ 2.0	$ 1.9	$ 1.8	$ 1.9	$ 1.9	$ 2.0	$ 2.1	$ 2.1
Funded Ratio	78.3%	79.6%	83.7%	85.8%	87.1%	88.3%	88.5%	88.6%	88.8%	89.0%	89.1%
Funding Period (Years)	**Infinite**	**Infinite**	**Infinite**	**Infinite**	**80.1**	**52.8**	**51.9**	**51.1**	**50.3**	**49.4**	**48.6**
Extra Assets Needed	$ 1.8	$ 1.4	$ 0.9	$ 0.7	$ 0.5	$ 0.4	$ 0.4	$ 0.4	$ 0.4	$ 0.4	$ 0.4

Other Assumptions:

8.25% valuation interest rate

Service-related salary increase assumption first 4 years (11%, 9.5%, 8.5%, 6.5%), 5% thereafter

4% payroll growth for measuring funding period

No liability gains or losses

x:\orsc\2007 orsc funding letter\[orsc exhibit b & c, funding plan.xls]baseline

Exhbit C, page 1: 10 year projection with an assumed investment return of 9.25%

OP&F Simplified 10-Year Projection of Pension Liability, Assets and Funding Period

($ amounts in billions)

	Actual	Projected									
	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016
Asset Performance During Year											
Actual investment return during the year	15.96%	9.25%	9.25%	9.25%	9.25%	9.25%	9.25%	9.25%	9.25%	9.25%	n/a
Contributions During Year											
Police - Employer Rate	19.50%	19.50%	19.50%	19.50%	19.50%	19.50%	19.50%	19.50%	19.50%	19.50%	19.50%
Fire - Employer Rate	24.00%	24.00%	24.00%	24.00%	24.00%	24.00%	24.00%	24.00%	24.00%	24.00%	24.00%
Health Care Allocation	7.75%	6.75%	6.75%	6.75%	6.75%	6.75%	6.75%	6.75%	6.75%	6.75%	6.75%
Valuation Results As of January 1											
Actuarial Accrued Liability	$ 12.2	$ 12.8	$ 13.4	$ 14.0	$ 14.7	$ 15.5	$ 16.2	$ 17.0	$ 17.9	$ 18.8	$ 19.7
Market-Related Value of Assets	9.6	10.2	11.2	12.1	13.0	13.9	14.8	15.7	16.7	17.8	19.0
Unfunded Accrued Liability	$ 2.6	$ 2.6	$ 2.2	$ 1.9	$ 1.7	$ 1.5	$ 1.4	$ 1.3	$ 1.1	$ 1.0	$ 0.7
Funded Ratio	78.3%	79.6%	83.8%	86.3%	88.3%	90.2%	91.3%	92.5%	93.7%	94.9%	96.2%
Funding Period (Years)	**Infinite**	**Infinite**	**Infinite**	**Infinite**	**52**	**33.2**	**26.8**	**21.4**	**16.7**	**12.6**	**8.8**
Extra Assets Needed to Reach 30-Year Funding	$ 1.8	$ 1.4	$ 0.9	$ 0.6	$ 0.4	$ 0.1	$ (0.1)	$ (0.3)	$ (0.5)	$ (0.8)	$ (1.0)

Other Assumptions:
8.25% valuation interest rate
Service-related salary increase assumption first 4 years (11%, 9.5%, 8.5%, 6.5%), 5% thereafter
4% payroll growth for measuring funding period
No liability gains or losses

x:\orsc\2007 orsc funding letter\[orsc exhibit b & c, funding plan.xls]9.25% per year

Exhbit C, page 2: 10 year projection with an assumed investment return of 15% in 2007, and 8.25% thereafter

OP&F Simplified 10-Year Projection of Pension Liability, Assets and Funding Period

($ amounts in billions)

	Actual	Projected									
	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016
Asset Performance During Year											
Actual investment return during the year	15.96%	15.00%	8.25%	8.25%	8.25%	8.25%	8.25%	8.25%	8.25%	8.25%	n/a
Contributions During Year											
Police - Employer Rate	19.50%	19.50%	19.50%	19.50%	19.50%	19.50%	19.50%	19.50%	19.50%	19.50%	19.50%
Fire - Employer Rate	24.00%	24.00%	24.00%	24.00%	24.00%	24.00%	24.00%	24.00%	24.00%	24.00%	24.00%
Health Care Allocation	7.75%	6.75%	6.75%	6.75%	6.75%	6.75%	6.75%	6.75%	6.75%	6.75%	6.75%
Valuation Results As of January 1											
Actuarial Accrued Liability	$ 12.2	$ 12.8	$ 13.4	$ 14.0	$ 14.7	$ 15.5	$ 16.2	$ 17.0	$ 17.9	$ 18.8	$ 19.7
Market-Related Value of Assets	9.6	10.2	11.4	12.4	13.4	14.4	15.4	16.2	17.1	18.0	19.0
Unfunded Accrued Liability	$ 2.6	$ 2.6	$ 2.0	$ 1.6	$ 1.3	$ 1.0	$ 0.8	$ 0.8	$ 0.8	$ 0.8	$ 0.7
Funded Ratio	78.3%	79.6%	84.8%	88.3%	91.0%	93.5%	94.8%	95.1%	95.5%	95.9%	96.3%
Funding Period (Years)	Infinite	Infinite	Infinite	49.6	27.6	16.9	12.6	11.6	10.7	9.7	8.7
Extra Assets Needed to Reach 30-Year Funding	$ 1.8	$ 1.4	$ 0.8	$ 0.3	$ (0.1)	$ (0.4)	$ (0.7)	$ (0.8)	$ (0.8)	$ (0.9)	$ (1.1)

Other Assumptions:
8.25% valuation interest rate
Service-related salary increase assumption first 4 years (11%, 9.5%, 8.5%, 6.5%), 5% thereafter
4% payroll growth for measuring funding period
No liability gains or losses

x:\orsc\2007 orsc funding letter\[orsc exhibit b & c, funding plan.xls]15% in 2007

Exhbit C, page 3: 10 year projection with an assumed investment return of 15% in 2007, 4% in 2008, and 8.25% thereafter

OP&F Simplified 10-Year Projection of Pension Liability, Assets and Funding Period

($ amounts in billions)

	Actual	Projected									
	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016
Asset Performance During Year											
Actual investment return during the year	15.96%	15.00%	4.00%	8.25%	8.25%	8.25%	8.25%	8.25%	8.25%	8.25%	n/a
Contributions During Year											
Police - Employer Rate	19.50%	19.50%	19.50%	19.50%	19.50%	19.50%	19.50%	19.50%	19.50%	19.50%	19.50%
Fire - Employer Rate	24.00%	24.00%	24.00%	24.00%	24.00%	24.00%	24.00%	24.00%	24.00%	24.00%	24.00%
Health Care Allocation	7.75%	6.75%	6.75%	6.75%	6.75%	6.75%	6.75%	6.75%	6.75%	6.75%	6.75%
Valuation Results As of January 1											
Actuarial Accrued Liability	$ 12.2	$ 12.8	$ 13.4	$ 14.0	$ 14.7	$ 15.5	$ 16.2	$ 17.0	$ 17.9	$ 18.8	$ 19.7
Market-Related Value of Assets	9.6	10.2	11.4	12.3	13.2	14.0	14.8	15.5	16.3	17.2	18.1
Unfunded Accrued Liability	$ 2.6	$ 2.6	$ 2.0	$ 1.7	$ 1.6	$ 1.4	$ 1.4	$ 1.5	$ 1.6	$ 1.6	$ 1.7
Funded Ratio	78.3%	79.6%	84.8%	87.6%	89.3%	90.8%	91.3%	90.9%	91.1%	91.4%	91.6%
Funding Period (Years)	Infinite	Infinite	Infinite	62.4	39.8	29.1	26.8	29.8	28.8	27.9	27
Extra Assets Needed to Reach 30-Year Funding	$ 1.8	$ 1.4	$ 0.8	$ 0.4	$ 0.2	$ (0.0)	$ (0.1)	$ (0.0)	$ (0.0)	$ (0.1)	$ (0.1)

Other Assumptions:
8.25% valuation interest rate
Service-related salary increase assumption first 4 years (11%, 9.5%, 8.5%, 6.5%), 5% thereafter
4% payroll growth for measuring funding period
No liability gains or losses

x:\orsc\2007 orsc funding letter\[orsc exhibit b & c, funding plan.xls]15% in 2007 & 4% in 2008

Exhibit D:
Excerpts from S&P's Public Finance Report

STANDARD
&POOR'S

Improved U.S. state pension funding levels could be on the horizon

"Although U.S. state pension funding levels fell slightly in fiscal 2005, signs are pointing to a possible easing of pressures related to prior escalations in contribution rates. There is also reason to believe that funded ratios could stabilize and improve over the medium term if investment returns and liability growth meet expectations."

"From 1990-2000, the average annual increase of the S&P 500 index of domestic equities was 15% compared with an average actuarial return assumption of about 8%."

"...the S&P 500 fell 16% in fiscal 2001 and another 19% in fiscal 2002. In addition, and in conjunction with falling asset values, a number of factors led to upward pressure on liabilities, including demographic changes such as members living longer and the phasing in of previously granted benefit enhancements."

"...these negative effects on assets and liabilities resulted in average state pension funding levels falling to 83.5% as of June 30, 2004, from their previous high point four years earlier. The fiscal 2005 survey reports a further decline in funded rations to 81.8% despite solid investment returns... One possible explanation for this occurrence is that in fiscal 2005, with the five-year smoothing of asset values used by most public funds, the earlier investment losses of 2001 and 2002 were still acting as a brake on the actuarial value of assets."

"If we look at prospective public pension funding levels from the standpoint of one key variable – investment return performance – recent investment results would suggest that the funding climate should improve. With actual market returns exceeding investment return assumptions, on average, for the past three fiscal years, we should see an increase in the actuarial value of assets in fiscal 2006."

"Because about 60% of large public funds use five-year smoothing to value assets, the investment losses from 2002 will still be taking their toll on the June 30, 2006 actuarial valuations. It is only after fiscal 2006 that funds will be fully out of the woods from this drag on assets."