



RETIREMENT SYSTEM

COMPREHENSIVE ANNUAL FINANCIAL REPORT

FOR THE YEAR ENDED DECEMBER 31, 1996

ORANGE COUNTY EMPLOYEES RETIREMENT SYSTEM

ORANGE COUNTY, CALIFORNIA



ORANGE COUNTY EMPLOYEES RETIREMENT SYSTEM

**COMPREHENSIVE
ANNUAL
FINANCIAL REPORT**

FOR THE YEAR ENDED DECEMBER 31, 1996

Raymond A. Fleming
Administrator

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I. INTRODUCTORY SECTION

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June 6, 1997

Board of Retirement
Orange County Employees Retirement System
2942 Daimler Street
Santa Ana, CA 92705

Dear Board Members:

It is with great pleasure that I submit the Comprehensive Annual Financial Report (CAFR) of the Orange County Employees Retirement System (OCERS) for the calendar year ended December 31, 1996, the System's 52nd year of operation. Information contained in this report is designed to provide a complete and accurate review of the year's operations and is the responsibility of the OCERS' management. The required financial statements have been prepared in accordance with generally accepted accounting principles, the reporting guidelines for government entities, and the County Employees Retirement Law of 1937. Ernst & Young LLP, independent auditors, have audited the financial statements. Management believes that internal control is adequate and that the accompanying statements, schedules and tables are fairly presented.

Structure of the Report

This report is presented in five sections:

- The Introductory Section describes the System's management and organizational structure, a summary of the plan provisions and a listing of the professional services used.
- The Financial Section contains the opinion of the independent auditor, Ernst & Young LLP, and the general purpose financial statements of the System.
- The Investment Section contains the investment consultant's statement produced by Callan Associates, OCERS' investment consulting firm, along with graphs and schedules regarding asset allocation, asset diversification, and history of performance.
- The Actuarial Section includes the certification letter produced by the independent actuary, Towers Perrin, along with supporting schedules and information.
- The Statistical Section contains graphs and schedules with comparative data related to active and deferred membership, retired membership, average monthly retirement benefits, revenues and expenses, and participating employers.

Board of Retirement

June 6, 1997

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Certificate of Achievement

The Government Finance Officers Association of the United States and Canada (GFOA) awarded a Certificate of Achievement for Excellence in Financial Reporting to OCERS for its Comprehensive Annual Financial Report for the fiscal year ended December 31, 1995. The Certificate of Achievement is a prestigious national award recognizing conformance with the highest standards for preparation of state and local government financial reports.

In order to be awarded a Certificate of Achievement, a government unit must publish an easily readable and efficiently organized Comprehensive Annual Financial Report, whose contents conform to program standards. Such comprehensive annual financial report must satisfy both generally accepted accounting principles and applicable legal requirements.

A Certificate of Achievement is valid for a period of one year only. We believe our current report continues to conform to the Certificate of Achievement program requirements, and we are submitting it to GFOA for evaluation.

Financial and Economic Summary

The past year has been another challenging one for OCERS. The Southern California economy is finally emerging from recession, although at a slow rate. Growth in the economy has come mainly from the technology and tourism areas, while various other industries also seem to be making progress. Tax revenues for the State of California have increased and it is anticipated that additional revenues will be made available to Counties, Cities and Special Districts.

Unemployment rates have trended down and in Orange County have gone below the national average rates. However, with the declaration of bankruptcy by the County in December 1994, the County government has had serious fiscal constraints requiring it to implement a significant layoff program as well as early retirement incentive programs. In addition, due to the effects of bankruptcy and resulting budgetary cutbacks, the County and OCERS negotiated a one-year agreement effective July 1, 1995 and subsequent agreement in 1996, whereby substantially all County employer retirement contributions would be paid from the reserve account established at OCERS resulting from the proceeds obtained from the issuance of the County's Pension Obligation Bonds in September 1994.

The effects of the County's personnel cutbacks had an impact on OCERS. The System's retired membership increased from 6,359 on December 31, 1995, to 6,631 at December 31, 1996. This represents an annual increase of 4% in the number of retirees. With this influx of recent retirements, the average monthly pension payment per member rose from \$1,210 to \$1,254. Also, mainly due to the County layoffs, the number of members in deferred status rose from 979 to 1,087. OCERS' active employee membership increased from 18,200 to 18,315.

Board of Retirement

June 6, 1997

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The reductions in employer contributions and the increasing number of retirees affect OCERS' cash requirements which has resulted in OCERS withdrawing moneys from the investments quarterly to meet cash flow needs.

OCERS' funding objective is to meet long-term benefit obligations through contributions and investment income. As of December 31, 1996, the funded ratio of the System was approximately at 135.4%. The System experienced a net increase in assets for the calendar year of \$346,143,000. Details of the components of this increase are included in the Statement of Changes in Net Assets Available for Benefits on page 24.

Investment Summary

OCERS' investments turned in a solid performance during 1996. For the calendar year, the portfolio earned a total return of 13.29%. Over long-term periods, the portfolio has earned total annualized returns of 10.45% over the past five years and 10.49% during the past ten years. These earnings have significantly outperformed the actuarially assumed rate of 8%. On a market value basis, the total net assets available for benefits grew from \$3,026,490,000 to \$3,372,633,000.

Conclusion

I would like to take this opportunity to thank each member of the System for their confidence in OCERS during the past year. I also want to express my thanks to the Board of Retirement for their dedicated effort in supporting the System through this past year. Likewise, I thank the consultants and staff for their commitment to OCERS and for their diligent work to assure the System's continued successful operation.

Respectfully submitted,



Raymond A. Fleming
Administrator

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Certificate of Achievement for Excellence in Financial Reporting

Presented to

Orange County Employees
Retirement System,
California

For its Comprehensive Annual
Financial Report
for the Fiscal Year Ended
December 31, 1995

A Certificate of Achievement for Excellence in Financial
Reporting is presented by the Government Finance Officers
Association of the United States and Canada to
government units and public employee retirement
systems whose comprehensive annual financial
reports (CAFRs) achieve the highest
standards in government accounting
and financial reporting.



Arthur R. Lynch
President

Jeffrey L. Esser
Executive Director

MEMBERS OF THE BOARD OF RETIREMENT
AS OF DECEMBER 31, 1996

Regular Members:

Mary K. Abbott	Elected Member - General Orange County Employees Retirement System Term expires December 30, 1997
Michael J. Carmody	Elected Member - Safety Vice-Chairperson 1996 Fire Department Term expires June 30, 1997
Keith L. Concannon	Elected Member - Retired Employees Term expires December 30, 1998
Thomas J. Lightvoet	Appointed Member Chairperson 1996 Appointed by Board of Supervisors Term expires May 1, 1998
Bruce Moore	Elected Member - General Probation Department Term expires December 30, 1998
John M.W. Moorlach	Ex-Officio Member County Treasurer
Bert Scott	Appointed Member Appointed by Board of Supervisors Term expires May 1, 1998
Chriss Street	Appointed Member Appointed by Board of Supervisors Term expires January 25, 1999
Supervisor Donald Saltarelli	Appointed Member Appointed by Board of Supervisors Term Expires December 31, 1996

Alternate Member:

Thomas N. Fox	Alternate for Safety Members (Alternate for all elected members) Elected by Safety Members (Sheriff) Term expires June 30, 1997
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SUMMARY OF PLAN PROVISIONS

1. Plan Description and History

OCERS was established in 1945 by the Board of Supervisors under the provisions of the County Employees Retirement Law of 1937, and provides members with retirement, death, disability, and cost-of-living benefits. It is a cost-sharing, multiple-employer defined benefit pension plan governed by a nine-member Board of Retirement.

Members employed prior to September 21, 1979, are designated as Tier I members. The Board of Supervisors amended the plan by adopting certain sections of the Government Code for members entering the plan after September 20, 1979, who are designated as Tier II members. All regular full-time employees or part-time employees, scheduled to work 20 hours or more per week for the County or other participating employers become members of the plan upon employment.

2. Monthly Salary Base for Benefits

Highest one-year average for Tier I members; three-year average for Tier II members.

3. Service Retirement

A. Eligibility

10 years of service and age 50, or 30 years of service and any age (20 years for safety members); age 70 with any service.

B. Benefit Formula per Year of Service

Tier I: $1/50 \times \text{Final Average Monthly Compensation} \times \text{Years of Service Credit} \times \text{Factor Based on Age at Retirement} = \text{Monthly Allowance}$.

Tier II: $1/60 \times \text{Final Average Monthly Compensation} \times \text{Years of Service Credit} \times \text{Factor Based on Age at Retirement} = \text{Monthly Allowance}$.

4. Non-Service Connected Disability

A. Eligibility

Five years of service.

B. Benefit Formula per Year of Service

Tier I: $1.8\% \times \text{Years of Service Credit} \times \text{Final Average Monthly Compensation}$. (If benefit is less than 1/3 of final average monthly compensation, years of service credit to age 62 can be added in order to pay up to a maximum of one-third of final average monthly compensation.)

Tier II: $1.5\% \times \text{Years of Service Credit} \times \text{Final Average Monthly Compensation}$. (If benefit is less than 1/3 of final average monthly compensation, years of service credit to age 65 can be added in order to pay up to a maximum of one-third of final average monthly compensation.)

5. **Service Connected Disability**

A. **Eligibility**

No age or service requirement.

B. **Benefit**

50% of final average monthly compensation.

6. **Active Member Death Before Completion of Five Years of Service**

Refund of employee contributions with interest plus one months' salary for each year of service to a maximum of six months' salary.

7. **Active Member Death After Completion of at Least Five Years of Service**

Qualified Surviving Spouse, or child, has the following options:

A. Refund of employee contributions with interest plus one month's salary for each year of service to a maximum of six months' salary; or

B. 60% of earned benefit payable to surviving eligible spouse; or

C. Combined benefit equal to a lump-sum payment plus a reduced monthly allowance.

If no eligible spouse or child exists, the named beneficiary receives refund of employee contributions with interest plus one month's salary for each year of service to a maximum of six months' salary.

8. **Service-Connected Death**

50% of final average monthly compensation payable to qualified spouse, or eligible child (if no qualified spouse).

9. **Death After Retirement**

A. **Non-Service Connected Disability Retirement**

60% of member's unmodified allowance continued to eligible spouse. (Member may elect a modified allowance at time of retirement.)

B. **Service-Connected Disability Retirement**

100% of member's allowance continued to eligible spouse or eligible child.

C. **\$1,000 Burial Benefit**

Payable to named beneficiary following death of original retiree.

10. **Withdrawal Benefits**

A. **Less than Five Years of Service**

Refund of accumulated employee contributions with interest.

B. **Five or More Years of Service**

If contributions are left on deposit, the member is entitled to the earned vested benefits commencing at any time after member would have been eligible to retire.

11. **Post-Retirement Cost-of-Living Benefits**

Based on changes in Consumer Price Index to a maximum of 3% per year; percentage in excess of 3% is "banked" for future increases.

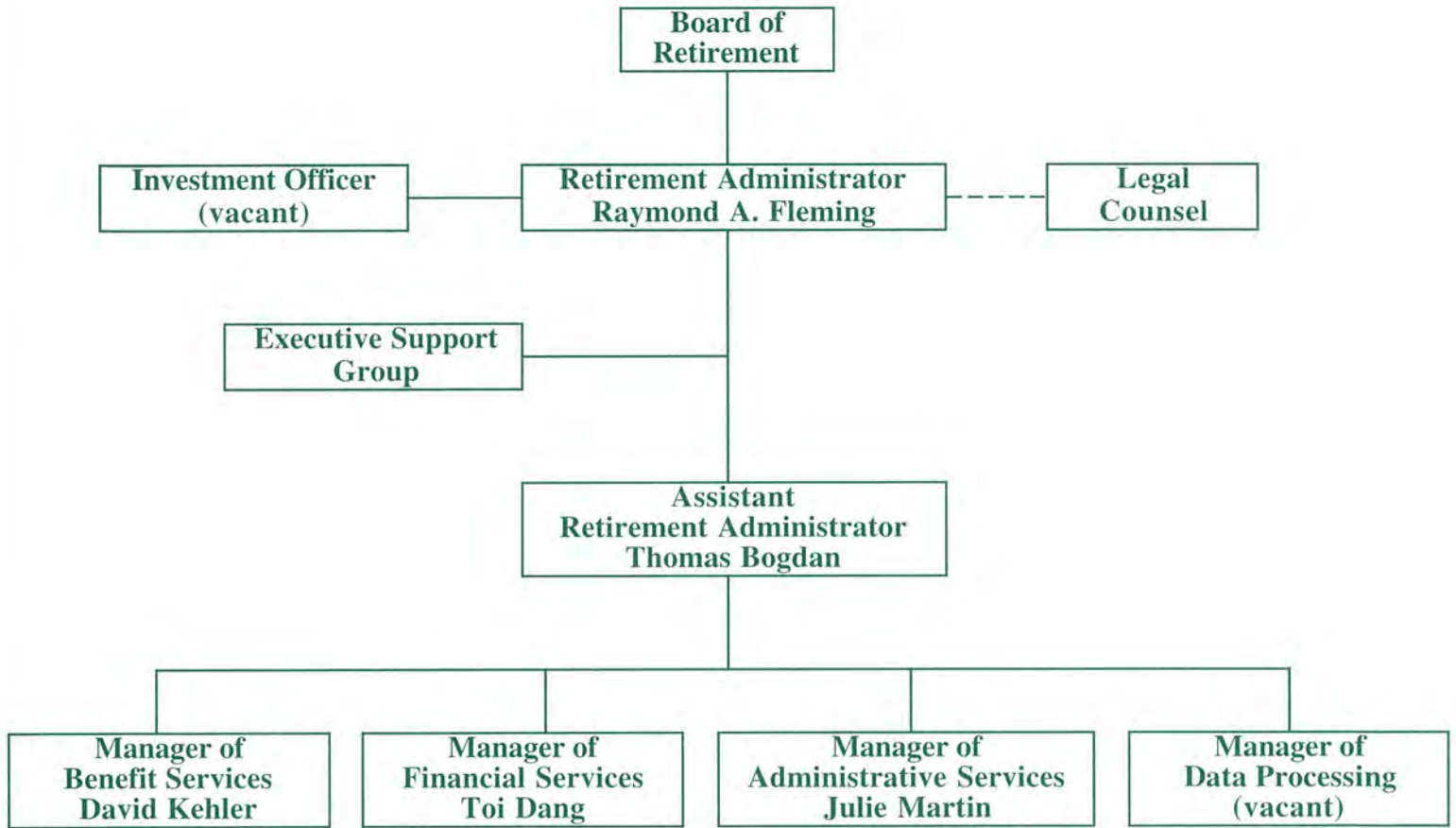
12. **County Contributions**

Determined by Projected Unit Credit funding method with a 30-year declining period amortization of Unfunded Actuarial Accrued Liability.

13. **Member Contributions - Tier I (Tier II in parentheses)**

Normal based on entry age, 1/200 (1/120) at 60 for General Members; 1/200 (1/100) at 50 for Safety Members. Cost-of-Living contributions equal to percentage of normal: 45.51% (25.89%) of General; 78.67% (39.55%) of Safety.

ORGANIZATION CHART



As of May 1, 1997

ORGANIZATION OF OCERS

EXECUTIVE: The Executive Section is responsible for the administration of the Orange County Employees Retirement System, including the management of the investment program, in accordance with the policies, regulations, and general guidelines of the Board of Retirement. It is also responsible for the interface with investment managers, the investment consultant, the actuary, legal counsel, and the County, as well as any other consultants authorized by the Board.

BENEFITS SERVICES: This Section is responsible for providing all benefit services to the members of the System. This includes benefit calculations, investigation of claims for disability retirement, preparation of data to support applications for retirement, preparation of the retiree payroll, and membership counseling.

FINANCIAL SERVICES: This Section is responsible for all of the financial records and reports including financial statements, control and balancing of payroll and members' contributions and reconciliation of investments. The Accounting Division also interfaces with the County Auditor-Controller and Treasurer's Office.

ADMINISTRATIVE SERVICES: This Section is responsible for providing administrative and clerical support services for OCERS, as well as for the maintenance of membership records of all OCERS members. In addition, Administrative Services is responsible for purchasing, building management, and for the internal payroll and personnel functions of OCERS.

DATA PROCESSING: Utilizing the HP 3000/937, this Section provides all of the computer and technical support for OCERS including production of the retiree payroll and Electronic Fund Transfer tapes.

LEGAL: This Section is responsible for providing legal advice to the Board of Retirement, Administrator, and staff in order to ensure compliance with all local, state and federal laws governing investments, operating procedures, and personnel issues. This Section also represents OCERS in all legal proceedings. A Deputy County Counsel is responsible for this Section.

PROFESSIONAL SERVICES
As of May 1, 1997

CONSULTING SERVICES

ACTUARY

Towers Perrin

Timothy J. Marnell, ASA (M.A.A.A.)
Chicago, IL

INVESTMENT CONSULTANT

Callan Associates, Inc.

Michael J. O'Leary, Jr., CFA
Denver, CO

INDEPENDENT AUDITOR

Ernst & Young LLP

Irvine, CA

LEGAL COUNSEL

County Counsel of Orange County
Santa Ana, CA

BANKRUPTCY COUNSEL

Katz, Hoyt, Seigel & Kapor
Los Angeles, CA

INVESTMENT COUNSEL

Stradling, Yocca, Carlson & Rauth
Newport Beach, CA

INVESTMENT MANAGERS

DOMESTIC EQUITY

Amerindo Investment Advisors, Inc.
San Francisco, CA

BZW Global Investors
San Francisco, CA

Columbus Circle Investors
Stamford, CT

Delaware Investment Advisers
Philadelphia, PA

Husic Capital Management
San Francisco, CA

STI Capital Management
Orlando, FL

GLOBAL FIXED INCOME

**Boston Partners Asset Management
Company, LP**
Boston, MA

Delaware International Advisers, Ltd.
London, England

Kennedy Associates, Inc.
Seattle, WA

LaSalle Street Capital Management, Ltd.
Chicago, IL

Loomis, Sayles & Company
Boston, MA

**Pacific Investment Management Company
(PIMCO)**
Newport Beach, CA

INTERNATIONAL EQUITY

Capital Guardian Trust Company
Los Angeles, CA

Capital Guardian International, Inc.
Los Angeles, CA

Schroder Capital Management International
London, England

REAL ESTATE

**Domestic
American Realty Advisors**
Glendale, CA

DA Management
Newport Beach, CA

Heitman/JMB Advisory Corporation
Chicago, IL

SSR Realty Advisors
San Francisco, CA

PMRealty Advisors
PMRA III
Newport Beach, CA

PROFESSIONAL SERVICES (Continued)
As of May 1, 1997

INVESTMENT MANAGERS (Cont.)

Sentinel Real Estate Corporation
New York, NY

International
GIM Capital Management, Inc.
Summit, NJ

PRICOA Property Investment Management, Ltd.
London, England

Timberland
Hancock Timber Resource Group
Boston, MA

Prudential Timber Investments, Inc.
Boston, MA

NON-TRADITIONAL INVESTMENTS

Managers
Brinson Partners, Inc.
Chicago, IL

Hancock Venture Partners, Inc.
Boston, MA

Hancock International Private Equity Partners LP (HIPEP)
Boston, MA

Limited Partnerships
American Industrial Partners
San Francisco, CA

Castle Harlan, Inc.
Mill Valley, CA

The Cypress Group L.L.C.
New York, NY

Energy Investors Funds
Mill Valley, CA

First Reserve Corporation
Greenwich, CT

The Gordon+Morris Group
Newport Beach, CA

IMR General, Inc.
Minneapolis, MN

Prudential Equity Investors, Inc.
New York, NY

Schroder Venture Managers, Inc.
New York, NY

TCW Asset Management Company
Los Angeles, CA

Torch Energy Advisors, Inc.
Houston, TX

Whippoorwill Associates, Inc.
White Plains, NY

CUSTODIAN

Boatmen's Trust Company
St. Louis, MO

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II. FINANCIAL SECTION

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REPORT OF INDEPENDENT AUDITORS



■ Suite 800
18400 Von Karman Avenue
Irvine, California 92612-1551

■ Phone: 714 252 2300

Report of Independent Auditors

Orange County Employees Retirement System Board of Retirement

We have audited the accompanying general purpose financial statements of the Orange County Employees Retirement System (System) as of and for the years ended December 31, 1996 and 1995, as listed in the table of contents. These general purpose financial statements are the responsibility of the System's management. Our responsibility is to express an opinion on these general purpose financial statements based on our audits.

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

In our opinion, the general purpose financial statements referred to above present fairly, in all material respects, the financial status of the Orange County Employees Retirement System at December 31, 1996 and 1995, and the changes in its financial status for the years then ended, in conformity with generally accepted accounting principles.

Our audits were conducted for the purpose of forming an opinion on the general purpose financial statements taken as a whole. The accompanying supplemental schedules included as "Other Supplementary Information," as listed in the table of contents, are presented for purposes of additional analysis and are not a required part of the general purpose financial statements. These schedules have been subjected to the auditing procedures applied in our audits of the general purpose financial statements and, in our opinion, are fairly stated in all material respects in relation to the general purpose financial statements taken as a whole.

Ernst & Young LLP

May 16, 1997

Ernst & Young LLP is a member of Ernst & Young International, Ltd.

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GENERAL PURPOSE FINANCIAL STATEMENTS

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ORANGE COUNTY EMPLOYEES RETIREMENT SYSTEM
STATEMENTS OF NET ASSETS AVAILABLE FOR BENEFITS
(in thousands)

	December 31	
	1996	1995
Assets		
Investments, at Fair Value (Notes B and F)		
United States Government Debt		
Securities and Corporate Bonds	\$ 1,018,542	\$ 890,911
Foreign Bonds	127,256	114,338
Domestic Equity Securities	1,216,221	1,148,498
Real Estate	400,770	332,046
International Equity		
Securities (Note F)	335,868	213,411
Venture Capital and		
Limited Partnership Interest (Note F)	110,099	77,978
Total Investments	<u>3,208,756</u>	<u>2,777,182</u>
Cash and Cash Equivalents (Note G)	176,617	258,267
Receivables		
Forward Currency Contracts, net (Note H)	227	128
Investment Income	21,899	23,892
Securities Sales	2,642	2,139
Employer/Employee Contributions	6,862	8,365
Total Receivables	<u>31,630</u>	<u>34,524</u>
Fixed Assets, Net (Note B)	2,655	261
Collateral Held for Securities Lent (Note F)	<u>273,947</u>	<u>180,784</u>
Total Assets	<u>3,693,605</u>	<u>3,251,018</u>
Liabilities		
Collateral Held for Securities Lent (Note F)	273,947	180,784
Securities Purchased	26,909	20,851
Mortgages Payable (Note J)	5,124	5,305
Miscellaneous Liabilities	<u>14,992</u>	<u>17,588</u>
Total Liabilities	<u>320,972</u>	<u>224,528</u>
Net Assets Available for Benefits	<u>\$ 3,372,633</u>	<u>\$ 3,026,490</u>

See accompanying notes to financial statements.

ORANGE COUNTY EMPLOYEES RETIREMENT SYSTEM
STATEMENTS OF CHANGES IN NET ASSETS AVAILABLE FOR BENEFITS
(in thousands)

	Years Ended December 31	
	1996	1995
Additions		
Investment Income:		
Net Appreciation in		
Fair Value of Investments (Note F)	\$ 240,675	\$ 414,557
Interest on:		
Domestic and International Securities	82,849	75,552
Cash with County Treasurer (Note G)	234	528
Short Term Investment Fund (Note G)	1,609	5,850
Domestic Dividends	26,333	32,874
Rental Income	25,161	21,926
International Dividends	5,576	2,956
Venture Capital and Limited Partnership	21,081	17,518
Securities Lending Revenues	740	542
 Total Investment Income	 404,258	 572,303
 Less Investment Counseling Fees	 (12,176)	 (10,851)
 Gain on Orange County		
Treasurer's Pooled Investment (Note G)	2,415	7,858
 Net Investment Income	 394,497	 569,310
 Contributions (Note C)		
Employer	16,463	20,814
Employee	48,461	47,953
 Total Contributions	 64,924	 68,767
 Total Additions	 459,421	 638,077
 Deductions		
Participants' Benefits	101,125	92,582
Member Withdrawals	7,166	12,523
Administrative Expenses (Note I)	4,987	4,971
 Total Deductions	 113,278	 110,076
 Increase in Net Assets Available for Benefits	 346,143	 528,001
 Net Assets Available for Benefits		
Beginning of Year	3,026,490	2,498,489
End of Year	\$ 3,372,633	\$ 3,026,490

See accompanying notes to financial statements.

ORANGE COUNTY EMPLOYEES RETIREMENT SYSTEM
STATEMENTS OF ACCUMULATED PLAN BENEFITS

(in thousands)

	December 31	
	<u>1996</u>	<u>1995</u>
Actuarial Present Value of Accumulated Plan Benefits		
Vested Benefits		
Retired	\$ 1,118,607	\$ 1,124,595
Terminated Vested	82,579	76,463
Active Vested	<u>917,033</u>	<u>806,970</u>
Total Vested Benefits	2,118,219	2,008,028
Nonvested Benefits	<u>272,423</u>	<u>237,826</u>
Actuarial Present Value of Accumulated Plan Benefits (Note B)	<u>\$ 2,390,642</u>	<u>\$ 2,245,854</u>

See accompanying notes to financial statements.

ORANGE COUNTY EMPLOYEES RETIREMENT SYSTEM
STATEMENTS OF CHANGES IN ACCUMULATED PLAN BENEFITS
(in thousands)

	Years Ended December 31	
	1996	1995
Actuarial Present Value of Accumulated Plan Benefits as of January 1	\$ 2,245,854	\$ 2,030,754
Increase (Decrease) During the Year Attributable to:		
Additional Benefits Accumulated	71,899	160,275
Benefits Paid	(108,291)	(103,572)
Increase for Interest Due to Decrease in Discount Period	175,420	158,397
Change in Actuarial Assumptions	5,760	0
Net Increase	144,788	215,100
Actuarial Present Value of Accumulated Plan Benefits as of December 31 (Note B)	\$ 2,390,642	\$ 2,245,854

See accompanying notes to financial statements.

ORANGE COUNTY EMPLOYEES RETIREMENT SYSTEM

DECEMBER 31, 1996

NOTES TO FINANCIAL STATEMENTS

A. Description of Plan

The following is a brief description of the Orange County Employees Retirement System (OCERS). Participants should refer to their Summary Plan Description for more complete information.

- 1. General.** OCERS is a cost-sharing multiple-employer, defined benefit pension plan covering substantially all employees of the County of Orange (County) and of the following agencies: Orange County Transportation Authority, Department of Education (closed to new members), City of San Juan Capistrano, UCI Medical Center (closed to new members), Foothill/Eastern Transportation Corridor Agency, San Joaquin Hills Transportation Corridor Agency, Cypress Recreation and Park District, County Sanitation Districts of Orange County, Capistrano Valley Water District, Capistrano Beach Sanitation District, Orange County Cemetery District, Santiago Library System, Orange County Vector Control District, Orange County Fire Authority, and Orange County Law Library.

The participating entities share proportionally in all risks and costs, including benefit costs. One actuarial valuation is performed for OCERS as a whole, and the same contribution rates apply to each participating entity.

OCERS was established in 1945 under the provisions of the County Employees Retirement Law of 1937, and provides members with retirement, death, disability, and cost-of-living benefits. OCERS is a related organization of the County of Orange, California. The Board of Retirement consists of nine members of which four are appointed by the County's Board of Supervisors, four are elected by the members of OCERS, and the County Treasurer is an ex-officio member. The County of Orange is not financially accountable for OCERS. During 1994, OCERS obtained a 100% interest in a subsidiary, OCRS Holding Corporation, which has been blended in these financial statements.

The Board of Supervisors adopted certain sections of the Government Code for members employed after September 20, 1979, designated as Tier II members. The establishment of Tier II resulted in reduced allowances to those members. Members employed prior to September 21, 1979, are designated as Tier I members. The differences between Tier I and Tier II benefits are discussed below.

- 2. Retirement Allowances.** An employee with ten or more years of service is entitled to an annual retirement allowance beginning at age 50. The amount of the retirement allowance is based upon the member's age at retirement, the member's "final compensation" as defined in Section 31462 of the Retirement Law of 1937, and the total years of service under OCERS.

Retirement Allowances for Tier I members are calculated using a fixed formula which will provide an allowance equal to 2 percent of the member's "final compensation" for each full year of service credit at age 57. Retirement allowances for Tier II members are calculated using a fixed formula which will provide the same allowance at approximately age 61 1/2.

If an employee terminates before rendering five years of service, the employee forfeits the right to receive benefits and is entitled to withdraw the employee contributions made, together with accumulated interest, unless the member enters a reciprocal retirement system and elects to keep these monies on deposit with OCERS.

If an employee terminates after five years of service, the employee may elect to leave the accumulated deposits in the retirement fund and be granted a deferred retirement allowance at the time the member would have been entitled to the allowance if service had been continued.

NOTES TO FINANCIAL STATEMENTS (Continued)

- 3. Death and Disability Benefits.** Upon the death of an active employee, a death benefit, equal to the deceased member's accumulated contributions, plus 1/12 of the annual compensation earnable by the deceased member during the 12 months immediately preceding death, multiplied by the number of completed years of service under OCERS, but not exceeding six months compensation, is paid to the employee's beneficiary. Upon the death of any member of OCERS who would have been entitled to retirement, the surviving spouse, as an option, may receive an annual allowance equal to 60 percent of the retirement allowance to which the deceased member would have been entitled as of the date of death. The death of a member due to service-connected injury or disease entitles the decedent's surviving spouse or child under 18 years of age to receive an annual allowance equal to one-half the member's "final compensation." In addition, the beneficiary of any member who dies before retirement with at least ten years of service under OCERS, or after retirement while receiving a retirement allowance from OCERS, is paid a death benefit of \$750 or \$1000, respectively.

An active employee who becomes totally disabled as a result of a service-connected injury or disease is paid an annual disability allowance equal to the larger of 50 percent of the employee's "final compensation" or the normal retirement benefits accumulated by the member as of the date the member became disabled. An active employee who becomes totally disabled as a result of nonservice-connected disease or injury is paid an annual allowance up to one-third of the employee's "final compensation," or the normal retirement benefits accumulated by the member as of the date of disability, whichever is the larger amount.

- 4. Active and Retired Members.** The following is a summary of OCERS' membership composition at December 31, 1996 and 1995:

Active Personnel (unaudited)

	December 31	
	1996	1995
<u>General Members</u>		
County and Agencies Paid by		
County Payroll	13,541	13,312
Outside Agencies	2,195	2,346
Pending (Retirement or Withdrawal)	213	174
Subtotal - General Members	<u>15,949</u>	<u>15,832</u>
<u>Safety Members</u>		
County and Agencies Paid by		
County Payroll	2,354	2,351
Pending (Retirement or Withdrawal)	12	17
Subtotal - Safety Members	<u>2,366</u>	<u>2,368</u>
<u>Deferred (General & Safety) Members</u>		
Regular	514	461
Employment with Other Agencies (Reciprocity)	<u>573</u>	<u>518</u>
Subtotal - Deferred Members	<u>1,087</u>	<u>979</u>
Total Active Personnel	<u><u>19,402</u></u>	<u><u>19,179</u></u>

At December 31, 1996 and 1995, 13,725 and 12,337 active members, respectively, had more than 5 years of service and were vested.

NOTES TO FINANCIAL STATEMENTS (Continued)

Retired Personnel Receiving Benefits (unaudited)

	<u>December 31, 1996</u>			<u>December 31, 1995</u>		
	<u>Gen.</u>	<u>Safety</u>	<u>Total</u>	<u>Gen.</u>	<u>Safety</u>	<u>Total</u>
Service Retirements	4,633	329	4,962	4,483	317	4,800
Continuances	484	44	528	469	34	503
Subtotal-Service Retirements	<u>5,117</u>	<u>373</u>	<u>5,490</u>	<u>4,952</u>	<u>351</u>	<u>5,303</u>
Service-Connected Disability	388	206	594	347	191	538
Continuances	36	14	50	37	13	50
Subtotal-Service Disability	<u>424</u>	<u>220</u>	<u>644</u>	<u>384</u>	<u>204</u>	<u>588</u>
Nonservice-Connected Disability	240	9	249	221	9	230
Continuances	239	9	248	230	8	238
Subtotal-Nonservice Disability	<u>479</u>	<u>18</u>	<u>497</u>	<u>451</u>	<u>17</u>	<u>468</u>
Total Retired Personnel	<u>6,020</u>	<u>611</u>	<u>6,631</u>	<u>5,787</u>	<u>572</u>	<u>6,359</u>

- 5. Employees Purchased Annuities.** OCERS provides accounts for additional member contributions as allowed under Government Code Section 31627. Contributions plus accumulated interest at the actuarial interest rate less 50 basis points are held in individual member accounts.

B. Summary of Significant Accounting Policies

- 1. Basis of Accounting.** OCERS' financial statements are prepared on the accrual basis of accounting in accordance with Financial Accounting Standards No.35. Contributions from employers and members are recognized as revenue in the period in which employees provide services. Investment income is recognized as revenue when earned. The net appreciation (depreciation) in fair value of investments held by OCERS is recorded as an increase (decrease) to investment income based on the valuation of investments at year end. Under GASB Statement No. 20, "Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities That Use Proprietary Fund Accounting", OCERS has elected not to apply Financial Accounting Standards Board pronouncements issued after November 30, 1989.

The accompanying financial statements include the accounts of OCERS and its wholly-owned subsidiary OCRS Holding Corp., incorporated March 1994. All intercompany accounts and transactions have been eliminated in consolidation.

NOTES TO FINANCIAL STATEMENTS (Continued)

In November 1994, the Governmental Accounting Standards Board (GASB) issued Statement No. 25, Financial Reporting for Defined Benefit Pension Plans and Note Disclosures for Defined Contribution Plans. This Statement establishes financial reporting standards for defined benefit plans and for the notes to the financial statements of defined contribution plans of state and local government entities. This Statement is effective for periods beginning after June 15, 1996. OCERS has elected not to early adopt this Statement as of December 31, 1996, and has not completed all of the complex analyses required to estimate the full impact of this new Statement.

2. **Fixed Assets.** Fixed assets are carried at cost less accumulated depreciation. Depreciation is calculated using the straight-line method with a 5 year useful life for computer software, 5 to 15 years for equipment and furniture, and 10 years for building improvements. The cost and accumulated depreciation of fixed assets at December 31, 1996 and 1995, were as follows:

	<u>1996</u>	<u>1995</u>
Furniture and Equipment	\$ 857,000	\$ 766,000
Computer Software	685,000	664,000
Building and Building Improvements	<u>2,405,000</u>	<u>53,000</u>
Total Fixed Assets (at cost)	3,947,000	1,483,000
Less Accumulated Depreciation	<u>(1,292,000)</u>	<u>(1,222,000)</u>
Total Fixed Assets - Net of Depreciation	<u>\$ 2,655,000</u>	<u>\$ 261,000</u>

3. **Valuation of Investments.** Quoted market prices are used to value United States Government securities, corporate and foreign bonds and debentures, and domestic and international common stocks. Mortgage notes are valued at an amount equal to the unpaid principal balance of the loans. Interest rates on the mortgage notes, discounted to reflect prepayment probabilities, do not differ significantly from market rates. Real estate equity investments are stated at market value, determined by independent appraisals performed on the properties held. The venture capital funds and limited partnership investments were determined by the investment managers based on the underlying financial statements and performance of the investments and acceptable valuation methodologies. At December 31, 1996, OCERS had investments in U.S. Treasury bonds and notes and in the Wells Fargo Nikko Equity Index Fund which individually represented more than 5 percent of OCERS' net assets available for benefits.
4. **Actuarial Present Value of Accumulated Plan Benefits.** Accumulated plan benefits are those future periodic payments, including lump-sum distributions, that are attributable, under OCERS' provisions, to the service employees have rendered. Accumulated plan benefits include benefits expected to be paid to (a) retired or terminated employees and their beneficiaries; (b) beneficiaries of employees who have died; and (c) present employees and their beneficiaries. Benefits under OCERS are based on employees' "final compensation". For Tier I members, a one-year average is used to calculate benefits, while for Tier II members, a three-year average is used to calculate benefits. The accumulated plan benefits for active employees are based on their average compensation. Benefits payable under all circumstances (retirement, death, disability, and termination of employment) are included to the extent they are deemed attributable to employee service rendered to the valuation date.

NOTES TO FINANCIAL STATEMENTS (Continued)

The actuarial present value of accumulated plan benefits is determined by the actuary and is that amount which results from applying actuarial assumptions to adjust the accumulated plan benefits to reflect the time value of money (through discounts for interest) and the probability of payment (by means of decrements such as for death, disability, withdrawal, or retirement) between the valuation date and the expected date of payment. Some of the actuarial assumptions used for financial statement purposes differ from those used for plan funding purposes. Such differences result from preparing the financial statements in accordance with the requirements of Statement of Financial Accounting Standards No. 35. The preparation of the general purpose financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts reported in the general purpose financial statements and accompanying notes. The significant actuarial assumptions as of December 31, 1996, were:

- a. Life expectancy of participants at December 31, 1996, and at December 31, 1995, is based on the 1983 Group Annuity Mortality Table.
- b. Retirement, disability, turnover, and mortality assumptions are based on OCERS' actual experience.
- c. The investment return, net of administrative expense, is assumed to be 8 percent at December 31, 1996, and at December 31, 1995.
- d. Retirees' benefits are assumed to increase 3 percent annually, once retired, in accordance with OCERS' cost-of-living provisions.
- e. Prior service cost is amortized over an initial 30-year period. The remaining period, as of December 31, 1996, was 11 years.
- f. Effective July 1, 1996, the Board of Retirement adopted a change in the Salary Scale Assumptions from 6% per annum per individual to 3.5% per annum per individual for the first five years and 5.5% per annum per individual thereafter. The effect of this change was an increase of \$5,760,000 in the Actuarial Present Value of Accumulated Plan Benefits.

C. Contributions Required and Contributions Made

As a condition of participation, employees are required to contribute a percentage of their annual compensation to OCERS. For Tier I members, the normal rate of contribution is based on the member's age of entry into OCERS, and is calculated to provide an annual annuity equal to 1/200 of the member's "final compensation" for each year of service rendered at age 60 for General Members, and at the age of 50 for Safety Members. For Tier II General Members, the rate of contribution is calculated to provide an annual annuity equal to 1/120 of the member's "final compensation" for each year of service rendered at age 60. For Tier II Safety Members, the rate of contribution is calculated to provide an annual annuity equal to 1/100 of the member's "final compensation" for each year of service rendered at age 50.

Present employees' accumulated contributions at December 31, 1996 and 1995, were \$511,278,000 and \$461,679,000, respectively, including interest credited at an interest rate of 5 percent per annum. Interest is credited as of June 30 on the balance of the members' accounts as of the prior December 31, and as of December 31 on the balance of the members' accounts as of the prior June 30. (Three percent, the balance of the assumed interest rate of 8 percent, is credited to the County Advance Reserve.)

The County's and participating agencies' funding policy is to make periodic contributions to OCERS in amounts such that, when combined with employees' contributions and with investment income, will fully provide for all employees' benefits by the time they retire.

In September 1994, the County of Orange issued \$320 million in Pension Obligation Bonds (POB) of which \$318.3 million in proceeds were paid to OCERS to fund the County's portion of the Unfunded Actuarial Accrued Liability (UAAL).

NOTES TO FINANCIAL STATEMENTS (Continued)

For accounting purposes, OCERS maintains the proceeds for the POB's in the County Investment Account. County Counsel, OCERS legal counsel, had previously issued an opinion which requires OCERS to charge all participating agencies the same employer contribution rate based upon type of membership, i.e. general, safety. Therefore, OCERS and the County of Orange, a single participating district, entered into an agreement which provides an offsetting credit based upon an amount actuarially determined to deplete the County Investment Account over the then remaining UAAL amortization period.

In 1995, the Board of Retirement of OCERS and the County of Orange, entered into an agreement modifying the previous agreement for the use of the County Investment Account (Investment Account). The modification provided, that for the year 1995, the employer contributions for the County of Orange would be paid entirely from the Investment Account.

Subsequently, in 1996, the Board of Retirement and the County of Orange entered into an agreement for the use of the Investment Account over a new funding period of 20 years. The agreement provides that the Investment Account will be used to fund the County's employer contribution in a decreasing percentage each year. In 1997, the Investment Account will fund approximately 90% of the County's employer contribution. Each subsequent year the funding by the Investment Account will decrease by 5% annually, while the County of Orange employer contribution will increase by a corresponding amount. As of December 31, 1996, the County Investment Account had a remaining balance of \$313,250,000.

Contributions for 1996 and 1995 approximate \$64,924,000 (\$16,463,000 employer and \$48,461,000 employee) and \$68,767,000 (20,814,000 employer and \$47,953,000 employee), respectively.

	<u>1996</u>	<u>1995</u>
Normal Cost	\$ 56,532,000	\$ 62,117,000
Amortization of Unfunded Actuarial Accrued Liability	<u>8,392,000</u>	<u>6,650,000</u>
Total	<u>\$ 64,924,000</u>	<u>\$ 68,767,000</u>

The contributions to OCERS for 1996 and 1995 were made in accordance with the actuarially determined requirements as follows:

	<u>Percent of Employees' Payroll</u>					
	<u>Jul '96 - Dec '96</u>		<u>Jul '95 - Jun '96</u>		<u>Jan '95 - Jun '95</u>	
	<u>Gen.</u>	<u>Safety</u>	<u>Gen.</u>	<u>Safety</u>	<u>Gen.</u>	<u>Safety</u>
Employer Contributions:						
Normal Cost	3.33%	5.59%	3.68%	6.58%	3.38%	6.20%
Amortization of Unfunded Actuarial Accrued Liability	<u>(0.97)%</u>	<u>18.34%</u>	<u>1.21%</u>	<u>21.35%</u>	<u>0.53%</u>	<u>18.56%</u>
Subtotal	2.36%	23.93%	4.89%	27.93%	3.91%	24.76%
Additional Contribution	<u>0.50%</u>	<u>0.50%</u>	<u>0.50%</u>	<u>0.50%</u>	<u>0.00%</u>	<u>0.00%</u>
Total	<u>2.86%</u>	<u>24.43%</u>	<u>5.39%</u>	<u>28.43%</u>	<u>3.91%</u>	<u>24.76%</u>

NOTES TO FINANCIAL STATEMENTS (Continued)

The Memorandum of Understanding (MOU) between OCERS and the County of Orange requires that Employer Contributions must increase by the lesser of .50% of pay and the amount necessary to increase OCERS' Unallocated Fund Balance (UFB) to 3% of OCERS' total assets. At December 31, 1994, and December 31, 1995, OCERS' UFB fell below 3% of OCERS' total assets. Therefore, the contribution rate increased by .50% effective with the pay period ending after June 30, 1995, and June 30, 1996, respectively. The .50% employer additional contribution is credited to the Unallocated Fund Balance.

	<u>1996</u>		<u>1995</u>	
	<u>Amount</u>	<u>Percent of Employees' Payroll</u>	<u>Amount</u>	<u>Percent of Employees' Payroll</u>
Employee Contributions	\$ 48,461,000	6.39%	\$ 47,953,000	6.58%
Employer Contributions	\$ 16,463,000	2.17%	\$ 20,814,000	2.85%

D. Funding Status and Progress

The amount shown in the following schedule as "pension benefit obligation" is a standardized disclosure measure of the actuarial present value of credited projected benefits adjusted for the effects of projected salary increases and any step-rate benefits, estimated to be payable in the future as a result of employee service to date. The measure is intended to help users assess the funding status on a going concern basis, assess progress made in accumulating sufficient assets to pay benefits when due, and make comparisons among public employees retirement systems. The measure is that used for the Analysis of Funding Progress on page 43 and is independent of the actuarial funding method used to determine contributions to OCERS. Ten-year historical trend information designed to provide information about OCERS' progress made in accumulating sufficient assets to pay benefits when due is presented on page 43.

The pension benefit obligation also differs from the present value of accumulated plan benefits (see Note B.4), used in the financial statements, which does not project future salary increases. The projections at December 31, 1996 and 1995, were determined using an 8 percent discount rate. The significant actuarial assumptions used to compute actuarially determined contribution requirements are the same as those used to compute the pension benefit obligation.

Year-end balances of the overfunded pension benefit obligation were as follows:

	<u>December 31</u>	
	<u>1996</u>	<u>1995</u>
	(in thousands)	
Pension benefit obligation:		
Retirees and beneficiaries currently receiving benefits and terminated employees not yet receiving benefits	\$ 1,201,186	\$ 1,201,057
Active participants:		
Provided by employee contributions including allocated investment income	484,459	438,949
Provided by employer contributions		
- Vested benefits	432,574	368,020
- Nonvested benefits	372,271	430,865
Total pension benefit obligation	2,490,490	2,438,891
Net assets available for benefits, at market value	3,372,633	3,026,490
Overfunded pension benefit obligation	\$ 882,143	\$ 587,599

NOTES TO FINANCIAL STATEMENTS (Continued)

The overfunded pension benefit obligation is based on GASB Statement No. 5 projected benefit obligations. The System continues to have an Unfunded Actuarial Accrued Liability.

E. Plan Termination

There are no plan termination provisions under the County Employees Retirement Law of 1937 which govern the operation of OCERS.

F. Investments

1. Investments Authorized

Government Code Section 31595 authorizes OCERS to invest in any form or type of investment deemed prudent, including security lending transactions, in the informed opinion of the Retirement Board, except as otherwise expressly restricted by California Constitution or by law.

2. Credit Risk

OCERS' investments are categorized below to give an indication of the level of risk assumed by OCERS at year-end. Category 1 includes investments that are insured or registered or for which the securities are held by OCERS or by its agent in its name. Category 2, of which OCERS has none, includes uninsured and unregistered investments for which the securities are held by the counterparty's trust department or agent in OCERS' name. Category 3, of which OCERS has none, includes uninsured and unregistered investments for which the securities are held by broker-dealers or by other counterparties, but not in OCERS' name.

The investment values (in thousands) are summarized as follows:

<u>Category 1 Classification</u>	<u>Cost</u>	<u>Market Value (Carrying Value)</u>
U.S. Government Debt Securities	\$ 375,379	\$ 381,427
Corporate Debt Securities	370,878	385,919
U.S. Government Bonds	52,972	50,640
Foreign Bonds	120,356	127,256
Domestic Equity Securities	611,928	770,911
International Equity Securities	221,519	261,598
Subtotal	1,753,032	1,977,751

Amounts Not Subject to Classification

Investments Held by Broker-Dealers Under Securities Loans with Cash Collateral

Corporate Debt Securities	17,484	17,456
U.S. Government Bonds	133,731	136,653
Domestic Equity Securities	70,076	81,565
International Equity Securities	26,331	34,673

NOTES TO FINANCIAL STATEMENTS (Continued)

<u>Amounts Not Subject to Classification (Continued)</u>	<u>Cost</u>	<u>Market Value (Carrying Value)</u>
Orange County Treasurer's Pooled Investment	50	50
Collateralized Mortgage Obligations	45,396	46,447
Real Estate Investments	434,462	400,770
Domestic Equity Index Fund	172,394	363,745
International Pooled Equity Funds	33,237	39,597
Non-Traditional Investment in Venture Capital and Limited Partnership	100,142	110,099
Subtotal	1,033,303	1,231,055
Less: Orange County Treasurer's Pooled Investment	50	50
Total Investments	\$ 2,786,285	\$ 3,208,756

A detailed report of the investment holdings is available for review at the OCERS location.

3. Net Appreciation

Investments in securities were held by Boatmen's Trust Company as custodian. During 1996 and 1995, OCERS' investments (including investments bought and sold, as well as held during each year) appreciated in values by \$240,675,000 and by \$414,557,000, respectively, as follows:

	<u>Years Ended December 31</u>	
	<u>1996</u>	<u>1995</u>
	(in thousands)	
Net Appreciation (Depreciation) in Fair Value as Determined by Quoted Market Prices:		
Domestic Equity Securities	\$ 197,340	\$ 280,603
United States Government Debt Securities, Corporate & Foreign Bonds & Debentures	(1,384)	125,760
International Equity Securities	32,991	11,315
Subtotal	228,947	417,678
Net Appreciation (Depreciation) in Fair Value as Determined by Estimated Fair Value:		
Real Estate	2,205	11,616
Non-Traditional	9,523	(14,737)
Total Net Appreciation	\$ 240,675	\$ 414,557

4. Financial Futures Contracts Held for Purposes Other than Trading

The net changes in market value of these contracts comprised \$3,180,000 of net depreciation and \$19,529,000 of the net appreciation during 1996 and 1995, respectively. As of December 31, 1996 and 1995, OCERS had open contracts of \$143,184,000 and \$161,710,000, respectively, for the purchase of U.S. Treasury bonds and notes, with delivery at specified future dates. Risks arise from the possible inability of counterparties to meet the terms of their contracts and from movements in securities values and interest rates.

OCERS is required to maintain a deposit with the broker as collateral to support open futures contracts. As of December 31, 1996 and 1995, OCERS had collateral deposits of \$2,107,000 and \$1,947,000, respectively, in cash equivalents, U.S. Treasury bills and notes.

5. Securities Lending Contracts

Included in the investment accounts for United States Government securities, international securities, corporate bonds and debentures, foreign bonds and debentures, and common stocks at December 31, 1996 and 1995 were securities with market values of \$270,347,000 and \$182,665,000, respectively, which had been lent by OCERS, through a securities lending agent, to various securities brokers in return for cash collateral equal to 102 percent (105 percent for international investments) of the market value (priced daily) of the securities lent, and additional collateral has to be provided by the next day if its value falls to less than 100 percent of the market of the value of the securities lent. OCERS invests the cash collateral in short term securities which cannot be pledged or sold by OCERS unless the borrower defaults. Securities on loan at year-end are presented as unclassified in the preceding schedule of custodial credit risk. In lending of both domestic and international securities, the term to maturity of the securities lent is matched with the term to maturity of the investment of collateral. Such matching existed at year-end. There were not any significant violations of the security lending provisions that occurred during 1996.

OCERS invested the cash collateral in short-term securities, which included certificates of deposit and commercial paper from certain domestic banks and savings and loans, repurchase agreements through certain brokers, and certain money market funds. Investments purchased with cash collateral are held by Boatmen's Trust Company in separate collateral accounts. The risks involved in a security lending program generally include: borrower bankruptcy, collateral deficiencies, problems with settlements, corporate actions, and dividends and interest.

Gross security lending revenues for 1996 and 1995 were \$740,000 and \$542,000, respectively. The costs of securities lending transactions are reported as expenses in the accompanying financial statements.

OCERS' securities lending agents are responsible for monitoring the market value of the securities lent to ensure that the value of the collateral equals or exceeds 100 percent of the market value of the securities lent as of the valuation date. At December 31, 1996 and 1995, OCERS held broker collateral with market values totaling \$273,947,000 and \$180,784,000, respectively.

6. International Investments

Specific investments in international securities are held by Bankers Trust Company, in accordance with a subcustodial agreement with Boatmen's Trust Company, and managed by three investment managers. Other investments are held in four pooled funds, all of which are invested in equities of companies located in international emerging markets.

NOTES TO FINANCIAL STATEMENTS (Continued)

7. Nontraditional Investments

OCERS' nontraditional investments represent investments made in private debt and equity securities through limited partnership and venture capital arrangements. OCERS has employed two investment methods. One method is the use of investment management firms to invest OCERS' assets in limited partnerships as well as direct private placements. OCERS has made five separate commitments of funds to two investment management firms. The second method of investment is OCERS' participation as a limited partner in limited partnership funds. To date, OCERS has made commitments of \$129,614,000 in 21 limited partnerships. These limited partnerships are diversified between venture capital, corporate finance, buyout, energy, and oil and gas investments.

8. Derivative Holdings Held for Trading Purposes

Of the total investments in OCERS' domestic fixed income portfolio of \$1,018,542,000 as of December 31, 1996, approximately \$427,875,000 are classified as derivative securities. The approximate annual income derived by OCERS from these securities is \$31,783,000. These holdings include asset-backed securities, mortgage-backed securities, collateralized mortgage obligations, zero coupon bonds and variable rate securities. These derivative securities offer favorable yields and advantageous risk/reward profiles with the vast majority of the holdings being guaranteed by either the U.S. Government or one of its agencies.

G. Cash and Cash Equivalents

OCERS' investments may not be entirely invested in securities at a given time. Those funds not in the form of securities are invested in short-term money market funds and cash equivalents, including the Orange County Investment Pool. At December 31, 1996, OCERS had money market funds of \$176,567,000, which were uninsured and uncollateralized, and pooled cash in the County of Orange Treasurer's Investment Pool of \$50,000. Interest in the Orange County Investment Pool is computed monthly on an average daily balance.

On December 6, 1994, the County of Orange and the Orange County Investment Pool (OCIP) filed for bankruptcy under Chapter 9 of the United States Bankruptcy Code. OCERS had three cash accounts invested in the OCIP which consisted of \$130,352,000 in principal and \$1,829,000 in unpaid accrued interest at December 6, 1994. As a result of the County's and OCIP's bankruptcies and based on subsequent information, the Board of Retirement valued the cash invested in the pool as of December 31, 1994, at 73% of its original principal.

During 1996 and 1995, OCERS received distributions from the OCIP of approximately 80% of its original principal, resulting in gains of \$2,415,000 and \$7,858,000, respectively. The current settlement agreement with the County provides that the remaining claims of approximately 20% of its original principal will be paid from litigation proceeds, if any. As additional proceeds are received, if any, the proceeds will be recognized as gains.

H. Forward Currency Contracts

OCERS' international investment managers invest in forward currency contracts. These are agreements to exchange different currencies at specified rates and settlement dates. Differences between the contract and market exchange rates at settlement result in gains or losses. Risks arise from the possible inability of counterparties to meet the terms of their contracts and from movements in exchange and interest rates. OCERS' balances for the forward currency receivables and payable accounts are based upon the currencies' contract exchange rates in relation to their market exchange rates at December 31, 1996 and 1995. An accounts receivable balance that is greater than the payable balance represents a net gain on the contracts. An accounts receivable balance that is less than the payable balance indicates a net loss.

NOTES TO FINANCIAL STATEMENTS (Continued)

I. Administrative Expenses

Section 31596.1 of the Government Code allows certain costs to be excluded from administrative expenses which are subject to statutory limitation. The excluded costs are not budgetary items but are included in the amounts classified as administrative expenses for OCERS' financial statements.

	Years Ended December 31	
	1996	1995
Expenses Subject to Statutory Limitation:		
Personnel Services:		
Board Members' Allowance	\$ 14,000	\$ 16,000
Employee Salaries and Benefits	2,222,000	1,904,000
Total Personnel Services	2,236,000	1,920,000
Office Operating Expenses:		
Operating Expenses	296,000	302,000
Professional Services	712,000	668,000
Rent/Leased Real Property	164,000	183,000
Depreciation/Amortization	70,000	152,000
Total Office Operating Expenses	1,242,000	1,305,000
Total Expenses Subject to Statutory Limitation	3,478,000	3,225,000
Expenses Not Subject to Statutory Limitation		
Commingled Interest Cost	5,000	1,000
Actuarial Costs	218,000	216,000
Custodian Services	935,000	1,046,000
Legal Costs	203,000	420,000
Additional Death Benefit Costs	148,000	63,000
Total Expenses Not Subject to Statutory Limitation	1,509,000	1,746,000
Total Administrative Expenses	\$ 4,987,000	\$ 4,971,000

J. Mortgage Payable

OCERS had mortgages payable at December 31, 1996, for two investment properties:

- La Sierra property, \$3,868,000 payable in equal monthly installments of \$43,000, at interest of 10% per annum, and maturing on May 1, 2001.
- North Torrance Shopping Center, \$1,256,000 in two notes payable due in equal monthly installments of \$15,000 and \$1,000 at interest rates of 8.875 and 10 percent, per annum, and maturing on August 1, 2007, and September 1, 2004, respectively.

NOTES TO FINANCIAL STATEMENTS (Continued)

K. Additional Retiree Benefit Account

The Additional Retiree Benefit results from a Memorandum of Understanding (MOU) with the County of Orange in which \$176,232,000 was used in 1993 to reduce the Unallocated Fund Balance (UFB). By the terms of the MOU, 75 percent (\$125,844,000) was transferred to the County Advance Reserve. The remaining 25 percent (\$50,388,000) was transferred to the Additional Retiree Benefit Account (ARBA). The amounts maintained in the ARBA are to be applied to health insurance or other supplemental benefits for OCERS' retirees. As of December 31, 1996, the balance of the ARBA Account was approximately \$82,596,000.

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REQUIRED SUPPLEMENTARY INFORMATION

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ORANGE COUNTY EMPLOYEES RETIREMENT SYSTEM
ANALYSIS OF FUNDING PROGRESS
FOR THE LAST TEN YEARS
(in thousands)

Year	Net Assets Available for Benefits	Pension Benefit Obligation	% Funded	Unfunded (Overfunded) Pension Benefit Obligation	Annual Covered Payroll	Unfunded (Overfunded) Benefit As % of Covered Payroll
1987	\$ 973,537	\$ 1,209,127	80.5	\$ 235,590	\$ 440,496	53.5
1988	1,142,190	1,255,075	91.0	112,885	481,919	23.4
1989	1,392,567	1,416,041	98.3	23,474	545,251	4.3
1990	1,452,337	1,564,142	92.9	111,805	624,088	17.9
1991	1,809,386	1,495,584	121.0	(313,802)	677,957	(46.3)
1992	1,945,122	1,844,738	105.5	(100,384)	701,526	(14.4)
1993	2,226,442	2,000,543	111.3	(225,899)	725,193	(31.2)
1994	2,498,489	2,214,161	112.8	(284,328)	769,175	(37.0)
1995	3,026,490	2,438,891	124.1	(587,599)	727,768	(80.7)
1996	3,372,633	2,490,490	135.4	(882,143)	758,897	(116.2)

Analysis of the dollar amounts of net assets available for benefits, pension obligation, and unfunded pension obligation in isolation can be misleading. Expressing net assets available for benefits as a percentage of pension benefit obligation provides one indication of OCERS' funding status on a going concern basis. Analysis of this percentage over time indicates whether the system is becoming financially stronger or weaker. Trends in unfunded (overfunded) pension benefit obligation and annual covered payroll are both affected by inflation. Expressing the unfunded (overfunded) pension benefit obligation as a percentage of annual covered payroll approximately adjusts for the effects of inflation and aids analysis of OCERS' progress made in accumulating sufficient assets to pay benefits when due.

Note: The pension benefit obligation for all years has been computed in accordance with GASB Statement No. 5.

ORANGE COUNTY EMPLOYEES RETIREMENT SYSTEM
REVENUES BY SOURCE AND EXPENSES BY TYPE
FOR THE LAST TEN YEARS
(in thousands)

Revenues By Source

<u>Year</u>	<u>Employee Contributions</u>	<u>Employer Contributions</u>	<u>Employer Contributions As % of Payroll</u>	<u>Investment* Income</u>	<u>Total Revenues</u>
1987	\$ 25,825	\$ 71,645	16.26	\$ 54,117	\$ 151,587
1988	28,476	77,854	16.15	61,679	168,009
1989	32,004	61,728	11.32	74,217	167,949
1990	37,700	84,466	13.53	83,143	205,309
1991	41,536	92,598	13.65	93,239	227,373
1992	42,349	59,664	8.50	85,837	187,850
1993	45,170	43,922	6.05	99,797	188,889
1994	47,442	369,382**	48.02	71,555	488,379
1995	47,953	20,814	2.85	154,753	223,520
1996	48,461	16,463	2.17	153,822	218,746

Expenses By Type

<u>Year</u>	<u>Benefits Paid</u>	<u>Administrative Expenses</u>	<u>Withdrawals</u>	<u>Total Expenses</u>
1987	\$ 34,128	\$ 1,258	\$ 5,409	\$ 40,795
1988	39,889	1,566	6,209	47,664
1989	44,254	2,200	7,124	53,578
1990	52,050	2,921	7,509	62,480
1991	58,249	3,283	5,679	67,211
1992	64,130	3,681	5,681	73,492
1993	74,238	3,854	5,928	84,020
1994	79,932	4,132	7,426	91,490
1995	92,582	4,971	12,523	110,076
1996	101,125	4,987	7,166	113,278

Contributions were made in accordance with actuarially determined contribution requirements.

* Net of investment manager fees. Does not include net appreciation in fair market value.

** Employer contributions include \$318,300,000 representing the County's funding of its portion of the unfunded actuarial accrued liability.

OTHER SUPPLEMENTARY INFORMATION

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ORANGE COUNTY EMPLOYEES RETIREMENT SYSTEM
SCHEDULE OF ADMINISTRATIVE EXPENSES
FOR THE YEARS ENDED DECEMBER 31, 1996 AND 1995

	<u>1996</u>	<u>1995</u>
Personnel Services:		
Board Members' Allowance	\$ 14,000	\$ 16,000
Employee Salaries and Benefits	<u>2,222,000</u>	<u>1,904,000</u>
Total Personnel Services	2,236,000	1,920,000
Office Operating Expenses:		
Operating Expenses	450,000	367,000
Professional Services	2,067,000	2,349,000
Rent/Leased Real Property	164,000	183,000
Depreciation/Amortization	<u>70,000</u>	<u>152,000</u>
Total Office Operating Expenses	<u>2,751,000</u>	<u>3,051,000</u>
Total Administrative Expenses	<u>\$ 4,987,000</u>	<u>\$ 4,971,000</u>

ORANGE COUNTY EMPLOYEES RETIREMENT SYSTEM
INVESTMENT SUMMARY
(in thousands)

<u>Type of Investment</u>	<u>December 31, 1995</u>				<u>December 31, 1996</u>		<u>% of Total Market Value</u>
	<u>Book Value</u>	<u>Market Value</u>	<u>Purchases</u>	<u>Sales and Redemption</u>	<u>Book Value</u>	<u>Market Value</u>	
U.S. Treasury Securities	\$ 176,301	\$ 185,659	\$ 404,218	\$ 205,140	\$ 375,379	\$ 381,427	11.88%
Corporate and Foreign Bonds	494,591	530,748	1,021,052	1,006,925	508,718	530,631	16.54%
U.S. Government Bonds	259,373	271,115	792,601	865,271	186,703	187,293	5.84%
Collateralized Mortgage Obligations	17,596	17,727	40,209	12,409	45,396	46,447	1.45%
Domestic Common Stocks	833,423	1,148,498	736,315	715,340	854,398	1,216,221	37.90%
Real Estate	367,904	332,046	68,458	1,900	434,462	400,770	12.49%
International Equity	173,790	213,411	304,744	197,447	281,087	335,868	10.47%
Non-Traditional	<u>77,544</u>	<u>77,978</u>	<u>33,020</u>	<u>10,422</u>	<u>100,142</u>	<u>110,099</u>	<u>3.43%</u>
Total Investments	<u>\$ 2,400,522</u>	<u>\$ 2,777,182</u>	<u>\$ 3,400,617</u>	<u>\$ 3,014,854</u>	<u>\$ 2,786,285</u>	<u>\$ 3,208,756</u>	<u>100.00%</u>

ORANGE COUNTY EMPLOYEES RETIREMENT SYSTEM
SCHEDULE OF CASH RECEIPTS AND DISBURSEMENTS
FOR THE YEARS ENDED DECEMBER 31, 1996 AND 1995
(in thousands)

	<u>1996</u>	<u>1995</u>
Cash and Cash Equivalents		
Balance at Beginning of Year	\$ 258,267	\$ 289,925
<u>Receipts:</u>		
Employee Contributions	48,461	47,953
Employer Contributions	16,463	20,814
Investments Matured and Sold	3,014,854	2,166,033
Investment Income	356,853	279,307
Miscellaneous	(929)	(23,021)
Total Cash Receipts	<u>3,435,702</u>	<u>2,491,086</u>
<u>Disbursements:</u>		
Benefits Payments	92,406	84,489
Refunds to Terminated Members	7,166	12,523
Administrative Expenses	4,987	4,971
Investments Purchased	3,400,617	2,409,910
Investment Expenses	12,176	10,851
Total Cash Disbursements	<u>3,517,352</u>	<u>2,522,744</u>
Cash and Cash Equivalents		
Balance at End of Year	<u>\$ 176,617</u>	<u>\$ 258,267</u>

ORANGE COUNTY EMPLOYEES RETIREMENT SYSTEM
SCHEDULE OF FEES AND OTHER INVESTMENT EXPENSES
FOR THE YEARS ENDED DECEMBER 31, 1996 AND 1995

	<u>1996</u>	<u>1995</u>
Equity:		
Domestic	\$ 3,484,000	\$ 3,172,000
International	1,581,000	1,035,000
Global Fixed Income	2,490,000	2,367,000
Real Estate	2,614,000	1,939,000
Venture Capital	917,000	939,000
Other Alternative Investments	<u>1,090,000</u>	<u>1,399,000</u>
Total Fees & Other Investment Expenses	<u>\$ 12,176,000</u>	<u>\$ 10,851,000</u>

III. INVESTMENT SECTION

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INVESTMENT CONSULTANT'S STATEMENT

CALLAN ASSOCIATES^{INC}

April 25, 1997

MICHAEL J. O'LEARY, JR., CFA
EXECUTIVE VICE PRESIDENT



SAN FRANCISCO

NEW YORK

CHICAGO

ATLANTA

DENVER

Mr. Raymond A. Fleming
Administrator
Orange County Employees Retirement System
2942 Daimler Street
Santa Ana, CA 92705

Dear Mr. Fleming:

Calendar 1996 was an excellent year for domestic stocks, a good year for international stocks, and a poor year for domestic bonds.

The economy performed well. Inflation as measured by the Consumer Price Index climbed 3.3% compared with 2.5% for 1995. Gross Domestic Product, based on preliminary estimates, exceeded 2.5% for all of 1996. Continued economic growth fueled strong earnings growth which supported extraordinary strength in the equity markets. From its recession low in the third quarter of 1990, the Callan Broad Market Index has climbed more than 188% to year-end 1996. During 1996, this index of the 2000 largest stocks enjoyed a total return of 21.91%. Large capitalization stocks performed better than smaller capitalization stocks. The S&P 500 Stock Index, a popular measure of large company stocks, returned 23.14% for the year while the Callan Small Cap Index returned 17.8%.

International stocks, as measured by the Morgan Stanley Capital International Index for Europe, Australia and the Far East (EAFE), returned 6.05% in dollar terms. This return masked the strength in most international markets. The European component of the Index returned a very attractive 21.08% in dollar terms. Similarly, most of the major Asian markets, with the notable exception of Japan, enjoyed reasonable returns. The Japanese market measured in dollar terms fell more than 11%, thereby accounting for EAFE's modest overall result.

After declining significantly in 1995, interest rates rose in 1996. Broad measures of the bond market, therefore, returned less than their income component. The Lehman Aggregate Bond Index returned 3.64% for the full year. The Lehman Government/Corporate Bond Index, owing to its slightly greater interest rate sensitivity, only returned 2.9%. Lower quality bonds fared better as did hedged international bonds.

The Orange County Employees Retirement System had an overall time-weighted return of 13.29% for the full year. This compared favorably with the fund's policy benchmark index return of 11.99%. The policy benchmark index is a customized index comprised of market

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INVESTMENT CONSULTANT'S STATEMENT (continued)

Mr. Raymond A. Fleming
Page Two
April 25, 1997

indices weighted in proportion to the System's strategic asset allocation policy. Over the trailing 5 and 9 year periods, OCERS' total fund has outperformed the policy index with compound annual returns of 10.45% and 11.36%, respectively versus 10.15% and 10.94% for the policy index.

OCERS' domestic equity managers slightly lagged their market benchmark, but the System's bond and international managers handsomely outpaced their target indices. Total fund returns also benefited from strong returns in the private equity area and improvement in the real estate arena.

In aggregate, OCERS' domestic equity managers returned 20.3% for the year. This was 1.6% below the Callan Broad Market Index and also lagged the Callan Equity database median return of 21.99%. Over the trailing 2 year period, OCERS' domestic equity composite has slightly exceeded the database median (27.94% compound return versus 27.91%) but trailed the broad market return of 28.8%.

OCERS' international stock managers produced very strong absolute and relative returns. The System's total international equity composite climbed 13.38% in 1996. This compared favorably with the EAFE Index return of 6.05% and the Callan Non-U.S. Style Group median manager return of 12.39%. Over longer-term periods, the System's international equity composite has consistently outperformed market indices.

OCERS' bond managers continued to produce very strong results in 1996. The System's domestic bond managers returned 6.19% for the year. While modest compared with equity returns, this result was more than twice that experienced by the Lehman Government/Corporate Bond Index (+2.90%). This return ranked in the top quartile of Callan's Total Fixed Income database. Results for longer cumulative periods exhibit similar patterns (i.e., better than market and top quartile).

In sum, 1996 was another strong year for the System. OCERS' broadly diversified investment program has produced results that are consistent with appropriate market benchmarks and the System's long-term earnings requirements.

Regards,



Michael J. O'Leary, Jr., CFA
Executive Vice President

MJO/dsb

ORANGE COUNTY EMPLOYEES RETIREMENT SYSTEM
STATEMENT OF INVESTMENT OBJECTIVES AND POLICIES
ADOPTED BY THE BOARD OF RETIREMENT MAY 11, 1992

General

This statement is intended to set forth the factors involved in the management of investment assets for the retirement system. The responsibility of the Board (with the participation of its Investment Committee, Staff and Advisors) is to establish broad investment policy, guidelines and objectives for the total fund and its component parts, to select independent investment managers and to monitor the activities of the investment managers. The responsibility of each investment manager is to develop and implement management strategies in accordance with the stated investment policies, guidelines and objectives, in a manner consistent with the "prudent man" rule for similar funds, i.e., with care, skill, prudence and diligence, with full discretion subject to the guidelines and applicable statutes. The investment manager is responsible for administration of the investment program within parameters established.

Strategic Asset Allocation Policy and Maintenance

The Board periodically undertakes strategic asset allocation studies. Such studies define the targeted level of diversification among the various major asset classes and the range in which they are permitted to fluctuate. When significant changes are made to the plan, a transition plan is adopted.

In normal circumstances, asset levels are permitted to fluctuate around targeted levels, and cash inflows are administered by staff in a manner that is consistent with maintenance of the desired level of diversification. When asset fluctuations and/or external cash flows take actual allocation outside the accepted range, cash inflows shall be directed toward the underallocated asset categories and cash outflows shall be directed from the overallocated asset classes.

Should expected external flows be judged by staff to be insufficient to bring the plan within permitted ranges within a 12 month period, staff shall inform the Investment Committee. The Investment Committee then will formulate a recommendation to shift assets that will be presented to the full Board.

Program Administration and Manager Structure

For each major asset class, the System shall diversify assets by employing managers with demonstrated skill in their particular areas of expertise. The System will retain managers who utilize varied investment approaches and allocate assets in a manner that is consistent with the overall strategic plan. So, for example, the sum of all domestic equity managers should exhibit characteristics that are similar, but not necessarily identical, to the overall equity market. When asset fluctuation causes the asset class to exhibit characteristics that are dissimilar from the plan, staff shall direct cash flows to or from the various managers so that actual characteristics are consistent with the plan. Should unusual circumstances create a significant imbalance that cannot be corrected through the routine allocation of external cash flows, the Investment Committee shall formulate a recommendation for Board consideration.

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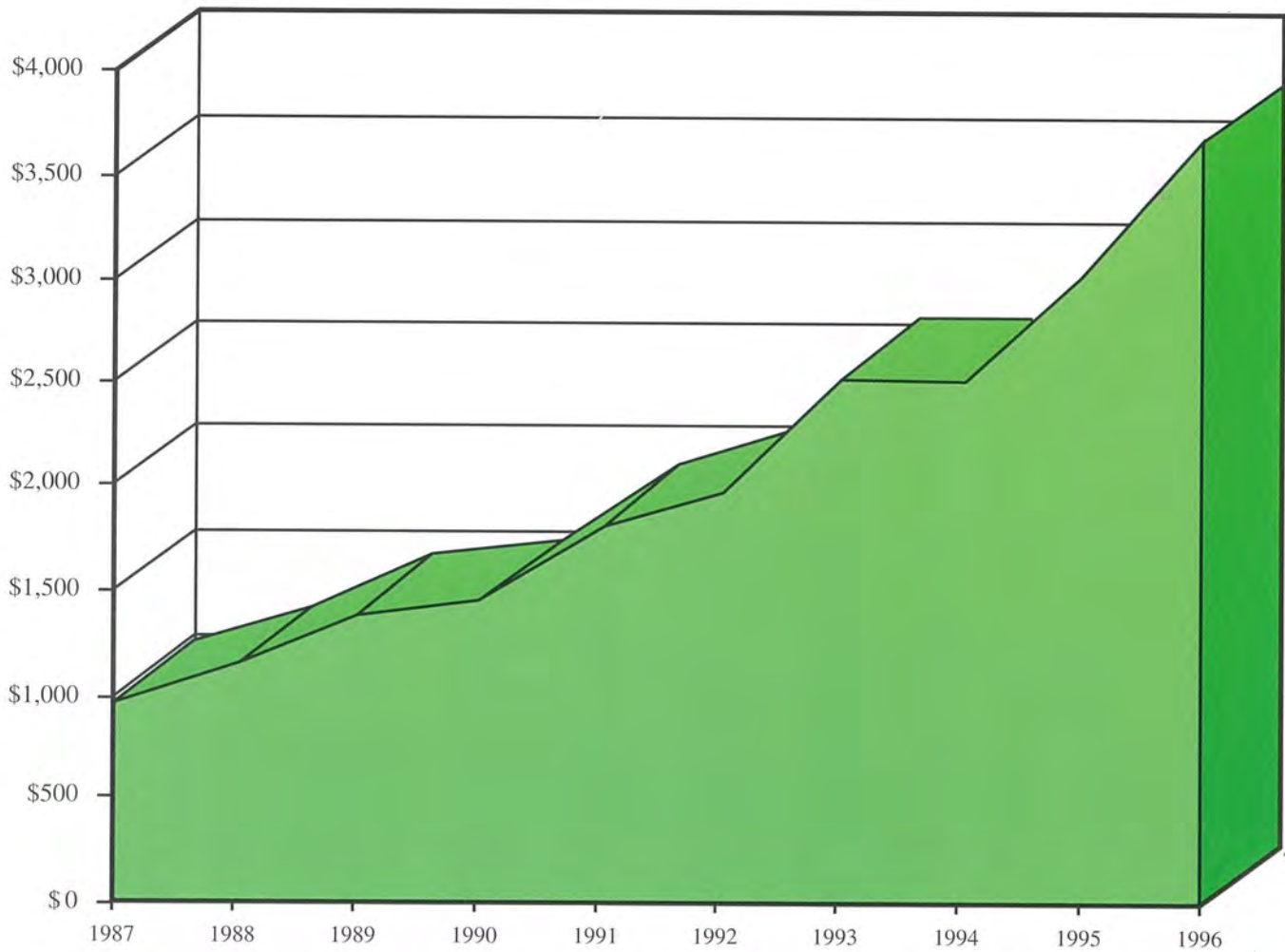
TARGET ASSET ALLOCATION RANGES

As of December 31, 1996

	<u>Lower End</u>	<u>Target As a % of Total Assets</u>	<u>Upper End</u>
Domestic Equity	<u>33%</u>	<u>40%</u>	<u>47%</u>
Core	<u>13%</u>	<u>15%</u>	<u>18%</u>
Growth	5%	10%	15%
Value	5%	10%	15%
Non-Traditional	3%	5%	7%
Non-traditional suballocation based on commitments, not actual investments.			
International Equity	<u>7%</u>	<u>10%</u>	<u>13%</u>
Growth	<u>3%</u>	<u>5%</u>	<u>8%</u>
Value	3%	5%	8%
Fixed Income	<u>29%</u>	<u>35%</u>	<u>41%</u>
Core	<u>12%</u>	<u>18%</u>	<u>24%</u>
Yield	4%	7%	10%
Intermediate	3%	5%	7%
International	3%	5%	7%
Real Estate	<u>12%</u>	<u>15%</u>	<u>18%</u>

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**Orange County Employees Retirement System
Growth of System Assets at Market Value
For Ten Years Ended December 31, 1996
(in Millions of Dollars)**

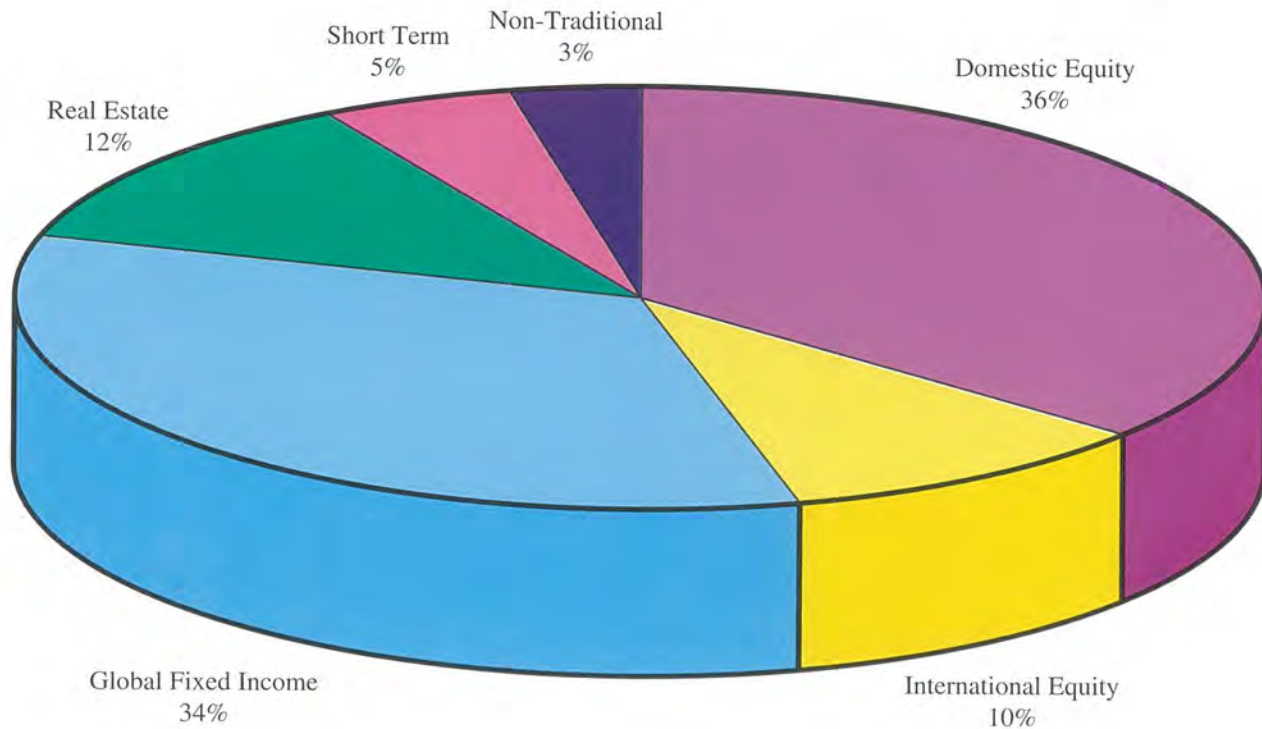


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Orange County Employees Retirement System

Asset Diversification

December 31, 1996

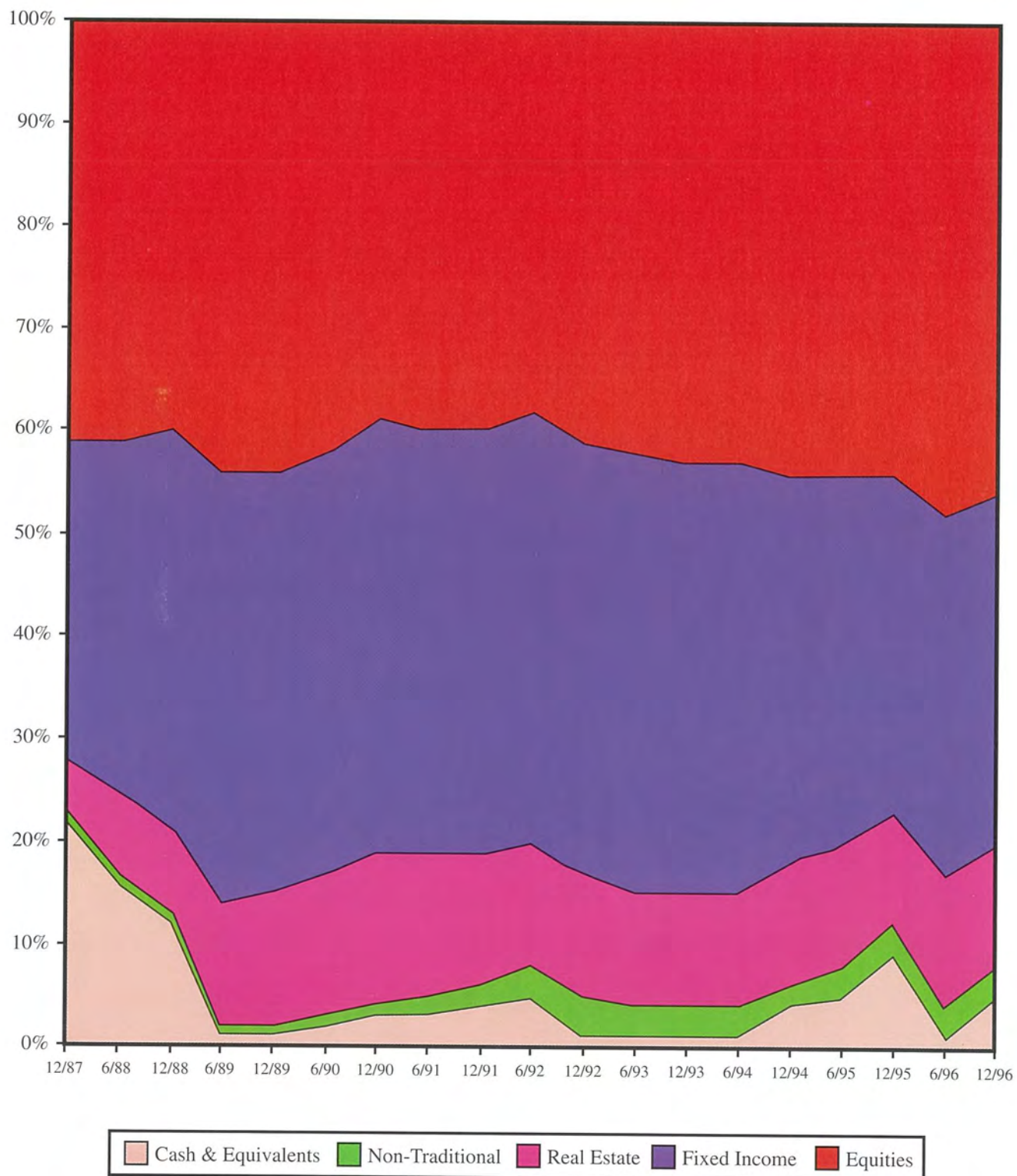


	Market (000's)
Domestic Equity	\$1,216,221
International Equity	335,868
Global Fixed Income	1,145,798
Real Estate	400,770
Short Term	176,617
Non-Traditional	110,099
Total	\$3,385,373

Note: The numbers included in this chart were obtained from the audited financial reports. The short term investments indicated above include all cash under the discretion of investment managers.

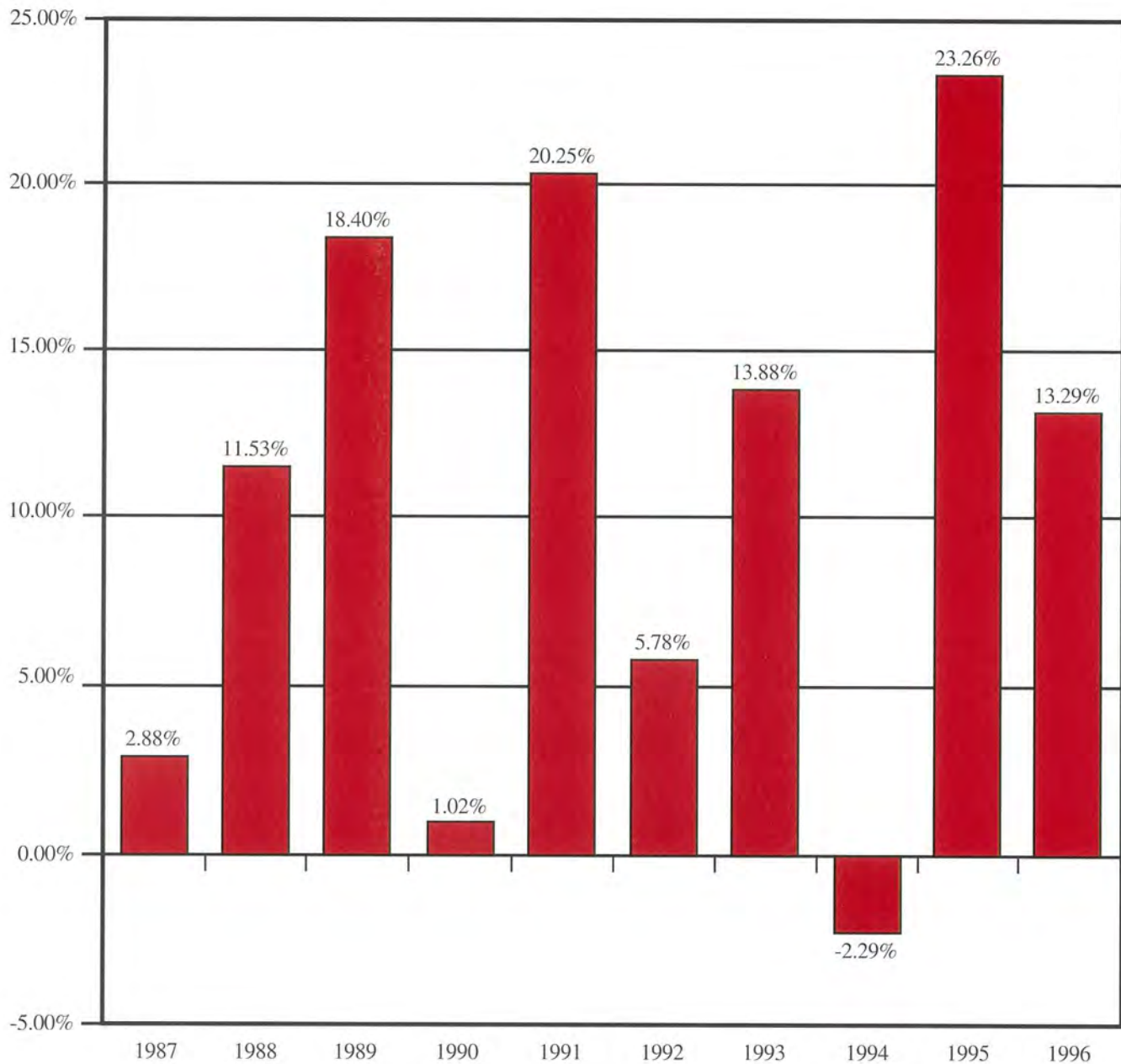
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Orange County Employees Retirement System Historical Asset Allocation (Actual) December 1987 – December 1996



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**Orange County Employees Retirement System
History of Performance
(Based on Market Value)
For Calendar Years 1987 – 1996**

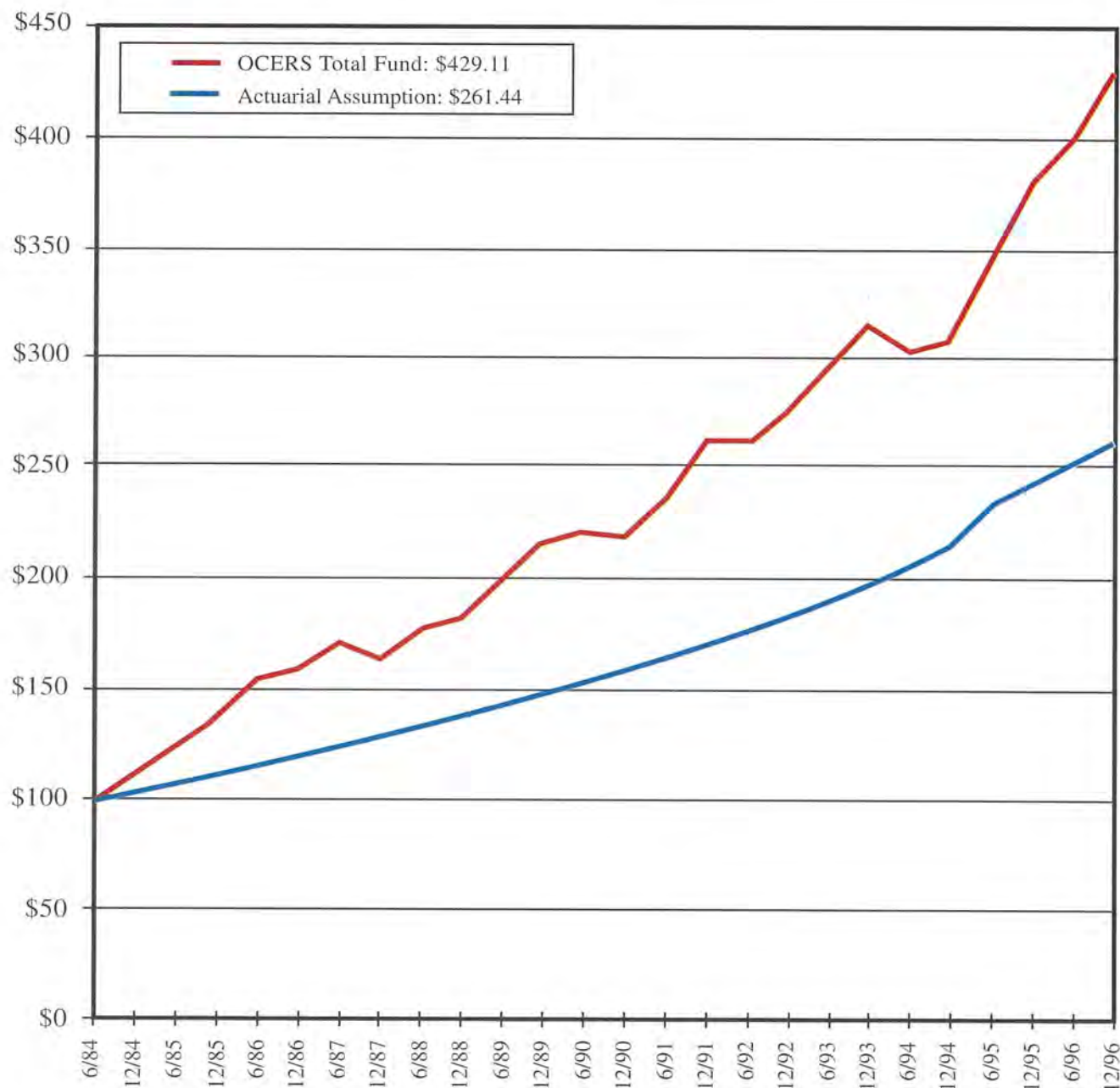


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Orange County Employees Retirement System

Growth of Fund vs. Actuarial Assumption Rate*

For Period June 1984 — December 1996



* Actuarial Assumption Rate was 7.25% through 6/89; 7.5% through 6/91 and 8% thereafter. An assumed basis of \$100 as of June 30, 1984 was adopted for the purpose of comparing the growth of the fund to the assumed actuarial rate.

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IV. ACTUARIAL SECTION

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ACTUARY CERTIFICATION LETTER

Timothy J. Marnell, ASA
Principal

200 West Madison Street, Suite 3300
Chicago, IL 60606-3414
312 609-9461
Fax: 312 609-9839

Towers Perrin

May 28, 1997

Members of the Board:

The financing objective of the plan has been to reduce the unfunded actuarial accrued liability to zero over a 28-year period commencing December 31, 1995, while maintaining contribution rates that remain approximately the same from generation to generation. Emerging gains and losses are amortized separately over individual 15-year periods. The progress being made toward the realization of the financing objectives through December 31, 1996, is illustrated in the attached Exhibits I and II.

An actuarial investigation is performed every three years, during which an analysis is made of the appropriateness of all economic and noneconomic assumptions. Recommendations for changes are presented to the Board for consideration. The last triennial investigation was performed as of December 31, 1995, at which time changes to the economic assumptions were recommended to the Board. The next triennial investigation will be performed as of December 31, 1998. Regular valuations are performed every year to comply with GASB requirements, to adjust contribution rates, and to monitor the plan's funded status.

The asset value used in determining employer contribution rates (the actuarial value of assets) is a five-year moving average of book and market values (Exhibit V). The data used in the actuarial valuation and investigation were provided by the Board. We have enclosed a summary of the employee data used in performing actuarial valuations over the past several years (Exhibits III and IV).

The actuarial assumptions used in the December 31, 1996, valuation are summarized in the attachments. All assumptions were determined by the actuary and were adopted by the Board. The employee census data and asset information were provided by the Retirement Office. The census data was reviewed, compared against the prior year and appeared to be reasonable. The asset information was accepted without further audit.

On the basis of the December 31, 1996, valuation, it is our opinion that OCERS continues to be in sound condition in accordance with the actuarial principles of level cost financing.

Respectfully submitted,



Timothy J. Marnell, A.S.A., M.A.A.A.
Principal

Orange County Employees Retirement System
HISTORY OF UNFUNDED ACTUARIAL ACCRUED LIABILITY
(In Thousands)

Valuation Date	Actuarial Accrued Liability	Actuarial Value of Assets	Unfunded Actuarial Accrued Liability	Ratio of Assets to Actuarial Accrued Liability	Annual Active Member Compensation	Ratio of Unfunded Actuarial Accrued Liability to Active Compensation
12/31/87	1,343,982	821,884	522,098	61.16%	440,496	118.53%
12/31/88	1,453,858	985,030	468,828	67.75%	481,919	97.28%
12/31/89	1,651,988	1,136,210	515,778	68.78%	545,251	94.59%
12/31/90	1,840,915	1,297,575	543,340	70.49%	624,088	87.06%
12/31/91	1,763,894	1,567,131	196,763	88.84%	677,957	29.02%
12/31/92	2,140,081	1,807,319	332,763	84.45%	701,596	47.43%
12/31/93	2,305,019	2,024,447	280,572	87.83%	725,193	38.69%
12/31/94	2,550,059	2,177,673*	372,386	85.40%	769,175	48.41%
12/31/95	2,633,884	2,434,406*	199,478	92.43%	727,768	27.41%
12/31/96	2,851,894	2,675,632*	176,262	93.82%	758,897	23.23%

Notes:

- The 12/31/95 valuation included a change in the salary scale from 6.0% to 3.5% per annum through the year 2000, and 5.5% thereafter. The aggregate payroll increase assumption was also changed from 5.0% to 4.5% per annum.
- The 12/31/91 valuation included a change in funding method from Entry Age Normal to Projected Unit Credit, a change in asset accounting concerning the unallocated fund balance, and changes in discount rate from 7.5% to 8.0%, salary scale from 5.5% to 6.0%, and payroll increases from 4.5% to 5.0%.
- The 12/31/88 interest rate increased from 7.25% to 7.50%, salary scale from 5% to 5.5%, and payroll from 4.0% to 4.5%. Asset method changed from book to five-year-average of book and market.

* The 12/31/94, 12/31/95 and 12/31/96 assets exclude \$311,022,000, \$329,064,000 and \$313,250,000, respectively, of the County's unamortized 1994 funding of its portion of the Unfunded Actuarial Accrued Liability, which funding for 1995 is being amortized over a fourteen year period beginning July 1, 1994 and for 1996 and later is being amortized over a 28-year period beginning July 1, 1996.

Orange County Employees Retirement System
HISTORY OF EMPLOYER CONTRIBUTION RATES

Employer Contribution Rate

Valuation Date	
12/31/87	
General	
Normal	7.13
UAAL	6.59
Total	13.72
Safety	
Normal	14.28
UAAL	15.97
Total	30.25
12/31/88	
General	
Normal	5.06
UAAL	5.57
Total	10.63
Safety	
Normal	15.13
UAAL	14.95
Total	30.08

Valuation Date	
12/31/89	
General	
Normal	5.04
UAAL	5.77
Total	10.81
Safety	
Normal	15.26
UAAL	14.03
Total	29.29
12/31/90	
General	
Normal	4.75
UAAL	4.60
Total	9.35
Safety	
Normal	13.91
UAAL	10.42
Total	24.33
12/31/91	
General	
Normal	2.40
UAAL	0.15
Total	2.55
Safety	
Normal	4.15
UAAL	13.78
Total	17.93

Valuation Date	
12/31/92	
General	
Normal	3.56
UAAL	1.30
Total	4.86
Safety	
Normal	6.42
UAAL	17.92
Total	24.34
12/31/93	
General	
Normal	3.38
UAAL	0.53
Total	3.91
Safety	
Normal	6.20
UAAL	18.56
Total	24.76
12/31/94	
General	
Normal	3.68
UAAL	1.71
Total	5.39
Safety	
Normal	6.58
UAAL	21.85
Total	28.43

Valuation Date	
12/31/95	
General	
Normal	3.33
UAAL	(0.47)
Total	2.86
Safety	
Normal	5.59
UAAL	18.84
Total	24.43
12/31/96	
General	
Normal	3.38
UAAL	(1.06)
Total	2.32
Safety	
Normal	5.77
UAAL	17.77
Total	23.54

Orange County Employees Retirement System
SUMMARY OF ACTIVE MEMBERSHIP

Valuation Date	Number	Annual Salary	Annual Average Salary	% Increase in Average Salary
12/31/87				
General	13,147	\$371,715,434	\$28,274	4.04%
Safety	1,853	68,780,426	37,118	2.49
Total	15,000	\$440,495,860	\$29,366	4.09
12/31/88				
General	13,839	\$407,356,604	\$29,435	4.11%
Safety	1,904	74,562,254	39,161	5.50
Total	15,743	\$481,918,858	\$30,612	4.24
12/31/89				
General	14,587	\$459,324,832	\$31,489	6.98%
Safety	1,985	85,926,444	43,288	10.54
Total	16,572	\$545,251,276	\$32,902	7.48
12/31/90				
General	15,969	\$523,453,762	\$32,779	4.10%
Safety	2,214	100,633,832	45,453	5.00
Total	18,183	\$624,087,594	\$34,323	4.32
12/31/91				
General	16,426	\$571,527,088	\$34,794	6.15%
Safety	2,175	106,429,952	48,933	7.66
Total	18,601	\$677,957,040	\$36,447	6.19
12/31/92				
General	16,432	\$590,453,256	\$35,933	3.27%
Safety	2,144	111,142,980	51,839	5.94
Total	18,576	\$701,596,236	\$37,769	3.63
12/31/93				
General	16,611	\$610,095,632	\$36,728	2.21%
Safety	2,186	115,097,702	52,652	1.57
Total	18,797	\$725,193,334	\$38,580	2.15
12/31/94				
General	17,084	\$645,117,097	\$37,761	2.81%
Safety	2,289	124,058,327	54,198	2.94
Total	19,373	\$769,175,424	\$39,703	2.91
12/31/95				
General	15,658	\$597,800,535	\$38,179	1.11%
Safety	2,351	129,967,110	55,282	2.00
Total	18,009	\$727,767,645	\$40,411	1.78
12/31/96				
General	15,736	623,682,535	39,634	3.81%
Safety	2,354	135,214,811	57,440	3.90
Total	18,090	758,897,346	41,951	3.81

Orange County Employees Retirement System

SUMMARY OF RETIRED MEMBERSHIP

Year	Number of Members				Annual Allowance (In Thousands)	% Increase in Annual Allowance	Average Monthly Allowance
	At Beginning of Year	Added During Year	Removed During Year	At End of Year			
1/87 to 12/87	3,870	N/A	N/A	4,138	\$35,890,628	13.34%	\$723
1/88 to 12/88	4,138	N/A	N/A	4,355	40,000,809	11.45	765
1/89 to 12/89	4,355	N/A	N/A	4,565	44,295,200	10.74	809
1/90 to 12/90	4,565	371	(158)	4,778	49,560,031	11.89	864
1/91 to 12/91	4,778	400	(149)	5,029	54,804,848	10.58	908
1/92 to 12/92	5,029	326	(51)	5,304	61,805,646	12.77	971
1/93 to 12/93	5,304	267	(59)	5,512	69,241,800	12.03	1,047
1/94 to 12/94	5,512	504	(200)	5,816	77,629,436	12.11	1,112
1/95 to 12/95	5,816	690	(147)	6,359	92,332,920	18.94	1,210
1/96 to 12/96	6,359	426	(154)	6,631	99,751,438	8.03	1,254

Orange County Employees Retirement System
DEVELOPMENT OF ACTUARIAL VALUE OF ASSETS
 As of December 31, 1996

Plan Year Ending	Market Value	Book Value	Ratio of Market Value to Book Value
1996	\$2,829,039,344	\$2,408,673,997	1.174521
1995	2,573,558,176	2,197,035,693	1.171377
1994	2,080,529,097	2,016,613,313	1.031695
1993	2,029,589,351	1,848,968,933	1.097687
1992	1,797,613,093	1,666,184,666	1.078880

(1) Average ratio in five years preceding December 31, 1996	1.110832
(2) Book value on December 31, 1996	2,408,673,997
(3) Actuarial value of assets: (1) x (2)	2,675,632,153

Orange County Employees Retirement System

SHORT-TERM SOLVENCY TEST

(\$ Amounts in Thousands)

Valuation Date	(1) Active Member Contributions	(2) Liability for Inactive Participants	(3) Liability for Active Members (Employer Financed Portion)	Valuation Assets	Portion of Accrued Liability Covered by Valuation Assets		
					(1)	(2)	(3)
12/31/87	\$173,793	\$511,586	\$658,603	\$ 821,884	100%	100%	61.15%
12/31/88	194,642	555,494	703,722	985,030	100	100	67.75
12/31/89	217,796	625,449	808,743	1,136,210	100	100	68.78
12/31/90	245,591	674,000	903,324	1,279,575	100	100	70.19
12/31/91	292,868	650,365	820,661	1,567,131	100	100	88.84
12/31/92	327,402	807,213	1,005,467	1,807,319	100	100	84.45
12/31/93	369,199	899,240	1,036,580	2,024,447	100	100	87.83
12/31/94	413,058	1,002,300	1,134,701	2,177,673	100	100	85.40
12/31/95	438,949	1,201,057	993,878	2,434,406	100	100	92.43
12/31/96	484,451	1,295,334	1,072,109	2,675,632	100	100	93.82

Orange County Employees Retirement System
ACTUARIAL METHODS AND ASSUMPTIONS

The Projected Unit Credit method was used in conjunction with the following actuarial assumptions:

1. *Interest:* 8% per annum.
2. *Salary scale:* 3.5% per annum per individual through year 2000, 5.5% per annum thereafter; the aggregate salary increase assumed for the entire system is 4.50% per annum. The number of active employees is assumed not to increase.
3. *Consumer Price Index:* Increase of 4.5% per annum subject to tier maximums.
4. *Spouses and dependents:* 80% of male employees and 50% of female employees assumed married at retirement, with wives assumed four years younger than husbands.
5. *Rehire of former employees:* Assumed not to be rehired.
6. *Asset valuation:* Asset values taken directly from statements furnished by OCERS. See Exhibit V for a description of the development of the actuarial value of assets.
7. *Rates of termination of employment:* As shown in Table I, which follows.
8. *Expectation of life after retirement:* As shown in Table II.
9. *Expectation of life after disability:* As shown in Table III.

The above assumptions were adopted effective December 31, 1995. The unfunded actuarial accrued liability as of December 31, 1995, is amortized as a level dollar amount over 28 years. Actuarial gains and losses for each year are amortized over separate 15-year periods on a level dollar basis.

Orange County Employees Retirement System

PROBABILITY OF OCCURRENCE

(Includes Eligibility)

Age Nearest	Ordinary Withdrawal	Vested Withdrawal	Ordinary Death	Ordinary Disability	Service Retire.	Service Disability	Service Death
General Members – Male							
20	0.2500	0.0000	0.0001	0.0000	0.0000	0.0000	0.0000
30	0.1110	0.0028	0.0003	0.0001	0.0000	0.0004	0.0000
40	0.0540	0.0097	0.0007	0.0004	0.0000	0.0010	0.0000
50	0.0330	0.0068	0.0010	0.0011	0.0460	0.0022	0.0000
60	0.0000	0.0000	0.0011	0.0052	0.0840	0.0050	0.0000
70	0.0000	0.0000	0.0000	0.0000	1.0000	0.0000	0.0000
General Members – Female							
20	0.2090	0.0000	0.0001	0.0000	0.0000	0.0000	0.0000
30	0.1280	0.0033	0.0002	0.0001	0.0000	0.0000	0.0000
40	0.0790	0.0102	0.0004	0.0006	0.0000	0.0000	0.0000
50	0.0450	0.0062	0.0009	0.0015	0.0390	0.0003	0.0000
60	0.0270	0.0000	0.0016	0.0026	0.0950	0.0000	0.0000
70	0.0000	0.0000	0.0000	0.0000	1.0000	0.0000	0.0000
Safety Members							
20	0.1376	0.0000	0.0004	0.0000	0.0000	0.0011	0.0002
30	0.0454	0.0026	0.0005	0.0001	0.0000	0.0013	0.0006
40	0.0099	0.0052	0.0010	0.0004	0.0000	0.0066	0.0005
50	0.0000	0.0029	0.0036	0.0023	0.1230	0.0174	0.0030
60	0.0000	0.0000	0.0000	0.0000	1.0000	0.0000	0.0000
70	0.0000	0.0000	0.0000	0.0000	1.0000	0.0000	0.0000

Orange County Employees Retirement System

EXPECTATION OF LIFE**Age and Service Retirees**

1983 Group Annuity Mortality

Age	Male	Female
20	57.86	64.15
30	48.11	54.29
40	38.46	44.52
50	29.19	34.92
60	20.64	25.67
70	13.18	17.13
80	7.64	10.20
90	4.28	5.41
100	2.28	2.36

Orange County Employees Retirement System

EXPECTATION OF LIFE**Disabled Retirees**

1981 Disabled Mortality

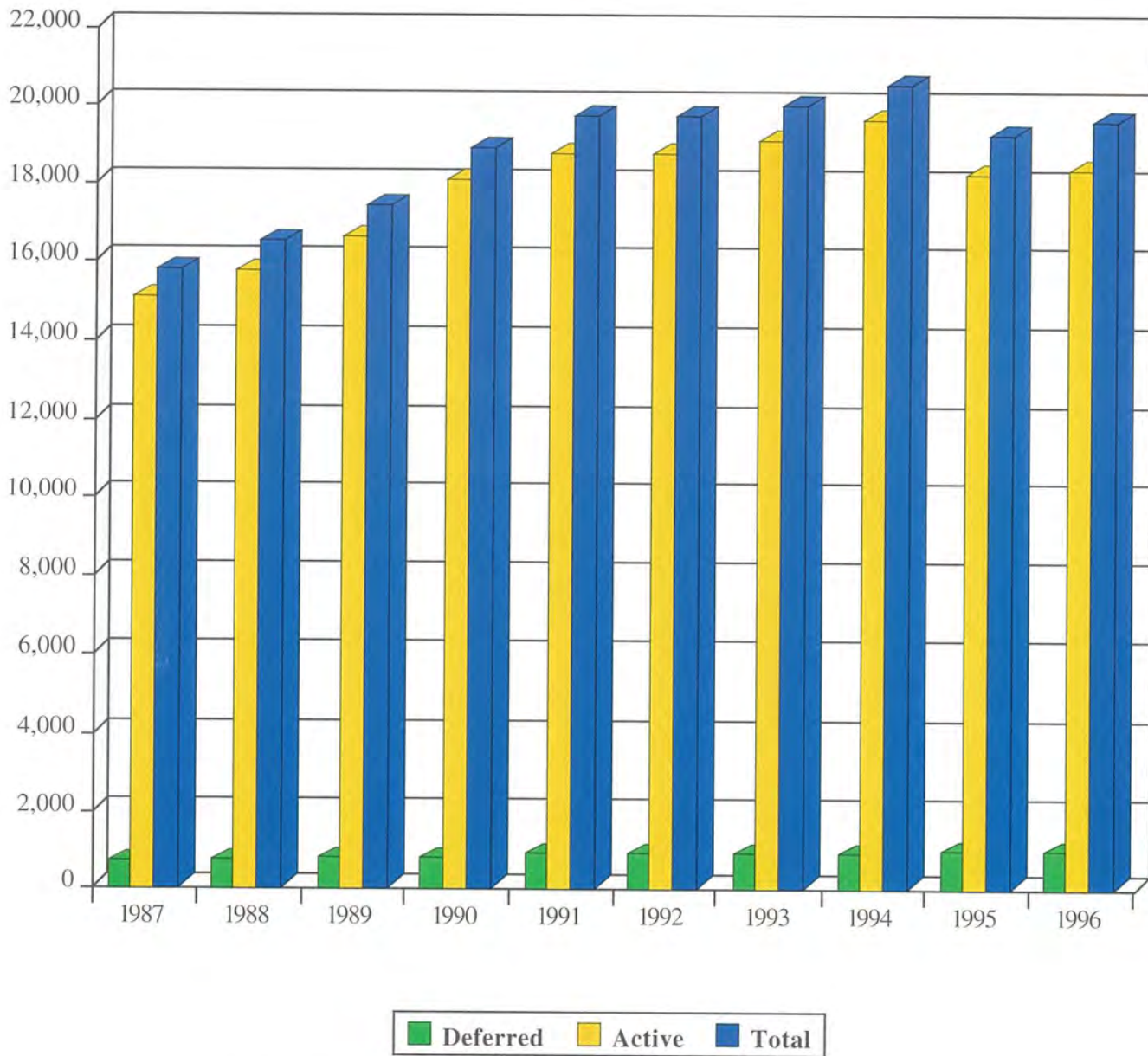
Age	General	Safety
20	38.73	49.29
30	31.98	40.36
40	26.21	31.77
50	21.08	23.59
60	16.37	16.64
70	11.70	11.70
80	7.00	7.00
90	4.09	4.09
100	2.20	2.20

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V. STATISTICAL SECTION

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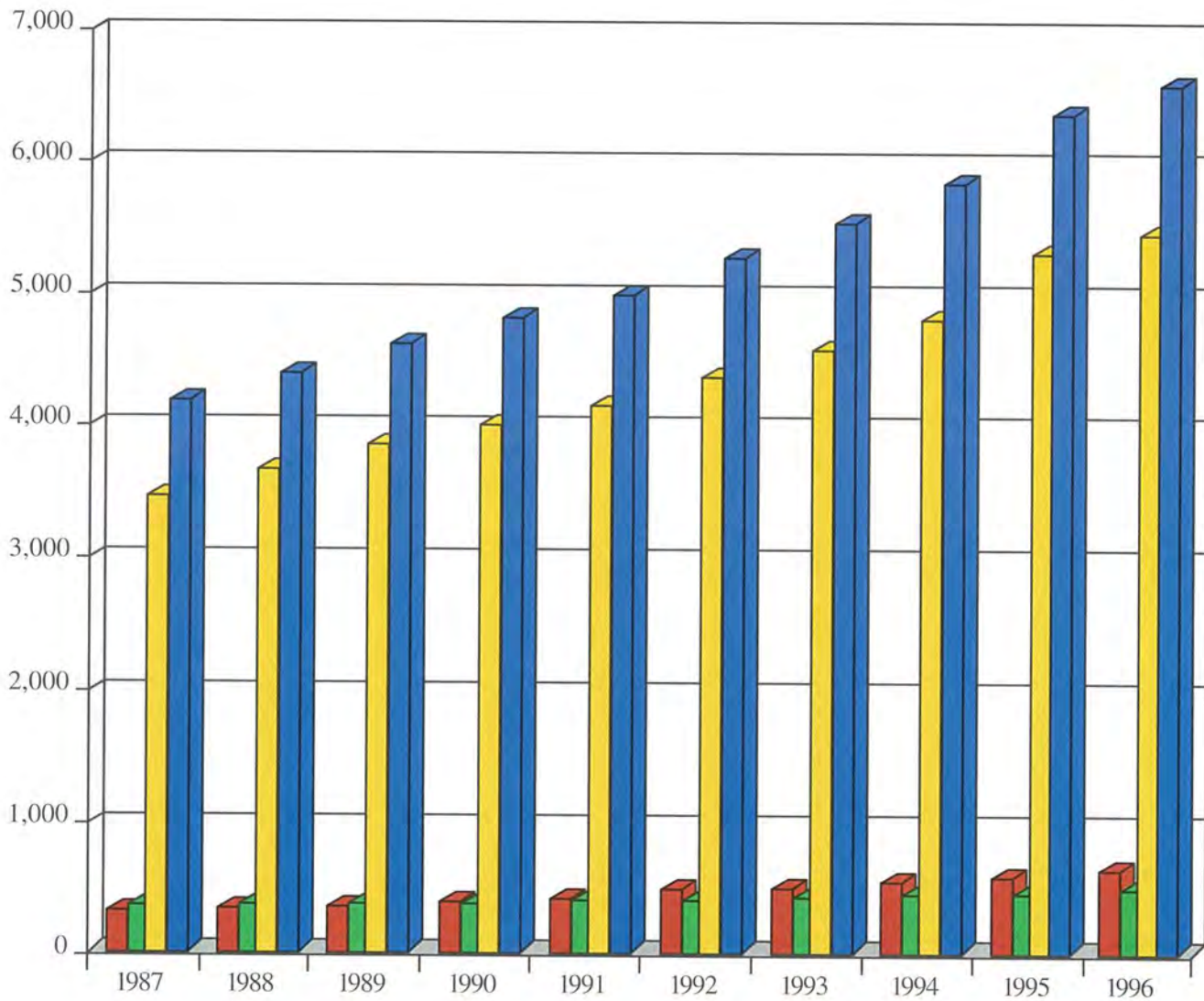
Membership History 1987-1996 (Active and Deferred)



	1987	1988	1989	1990	1991	1992	1993	1994	1995	1996
Deferred	689	748	797	798	936	932	903	908	979	1,087
Active	15,050	15,744	16,573	18,066	18,702	18,735	19,073	19,589	18,200	18,315
Total	15,739	16,492	17,370	18,864	19,638	19,667	19,976	20,497	19,179	19,402

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Membership History 1987-1996 (Retired)

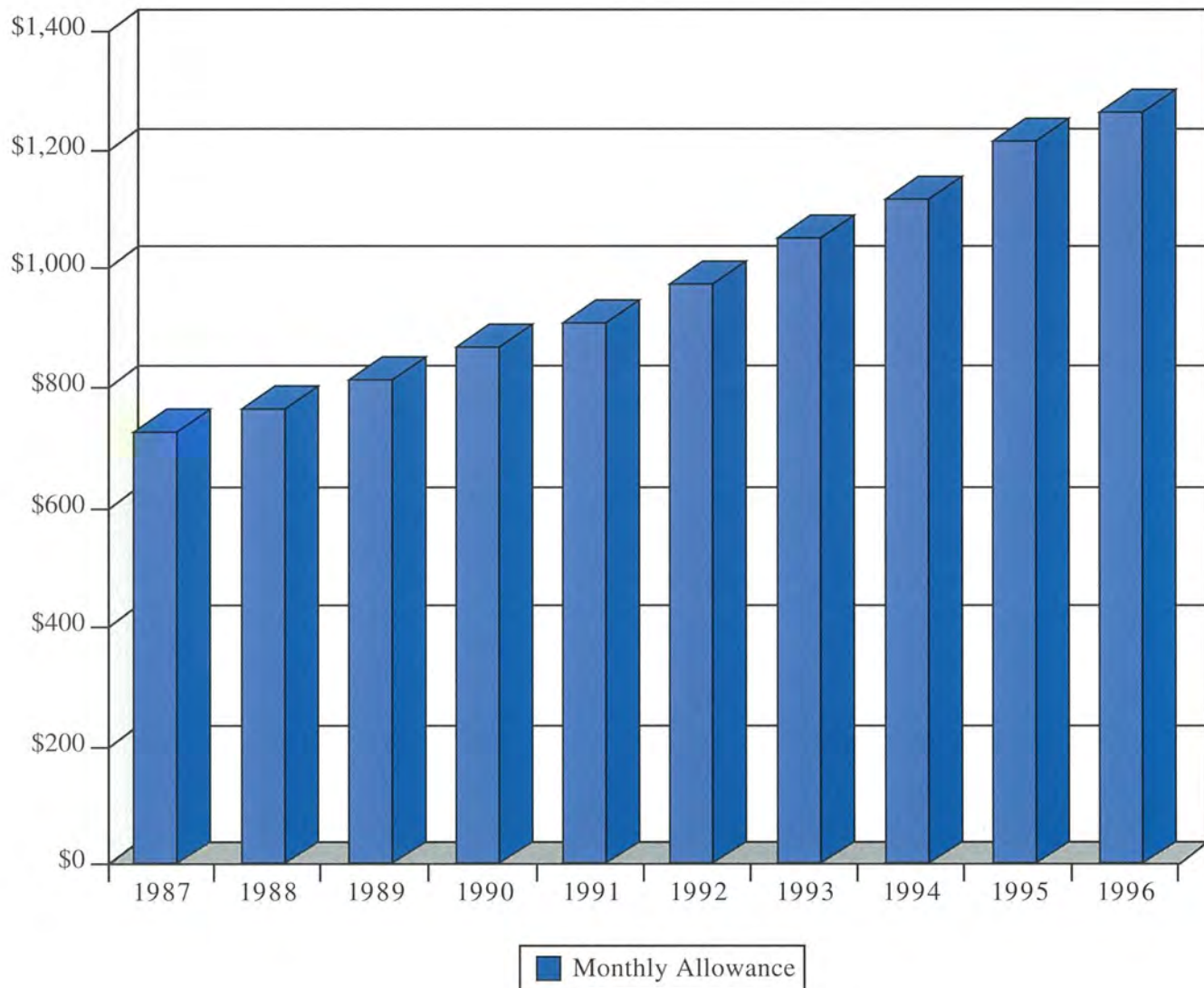


■ Serv. Conn. Disab.
 ■ Non-Serv. Conn. Disab.
 ■ Service
 ■ Total

	1987	1988	1989	1990	1991	1992	1993	1994	1995	1996
Serv. Conn. Disab.	335	354	366	400	424	487	508	548	588	644
Non-Serv Conn. Disab.	374	376	391	398	400	411	437	461	468	497
Service	3,464	3,661	3,852	4,001	4,149	4,354	4,579	4,807	5,303	5,490
Total	4,173	4,391	4,609	4,799	4,973	5,252	5,524	5,816	6,359	6,631

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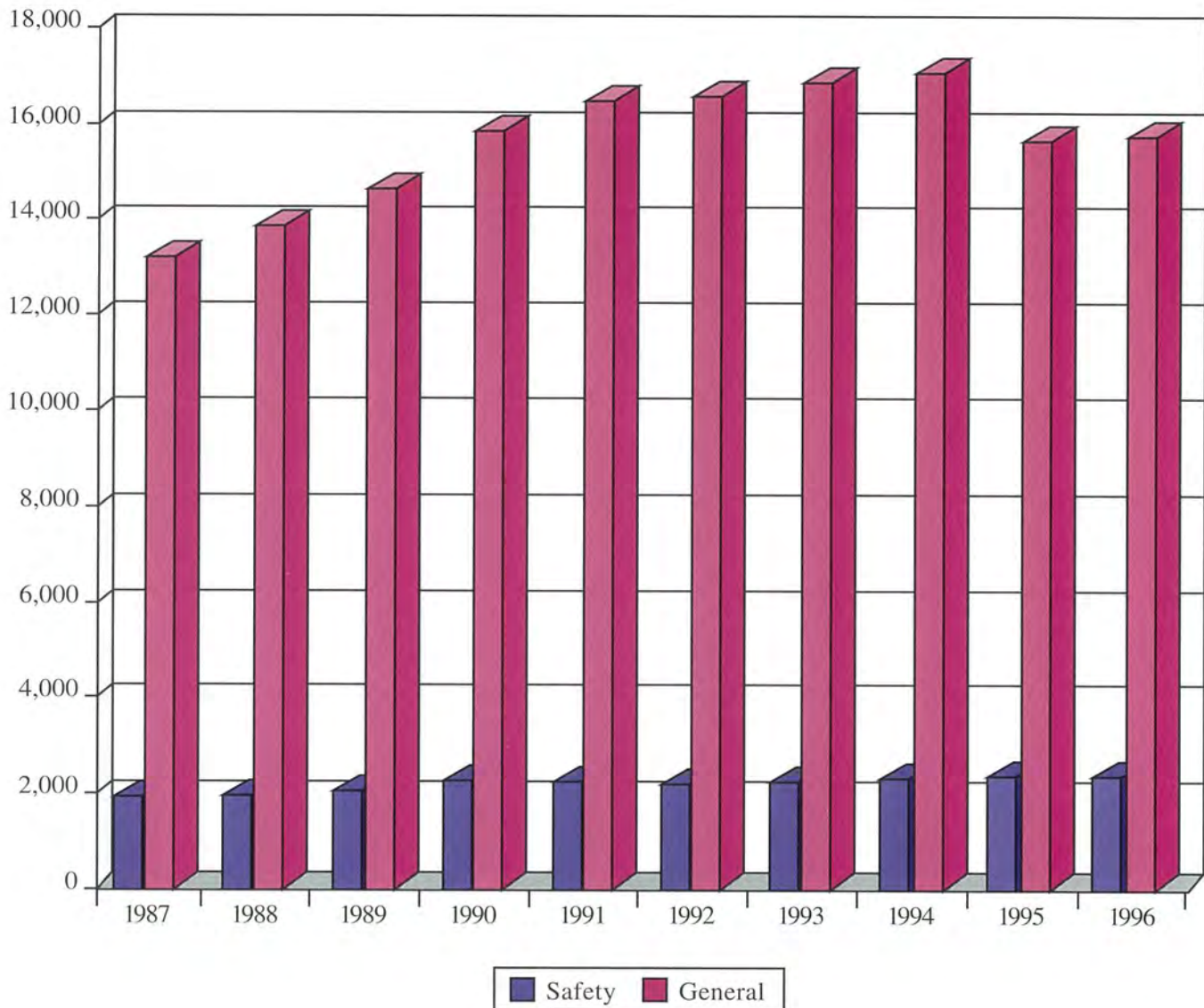
Average Monthly Retirement Benefits



	1987	1988	1989	1990	1991	1992	1993	1994	1995	1996
Monthly Allowance	\$723	\$765	\$809	\$864	\$908	\$971	\$1,047	\$1,112	\$1,210	\$1,254

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Membership Classification

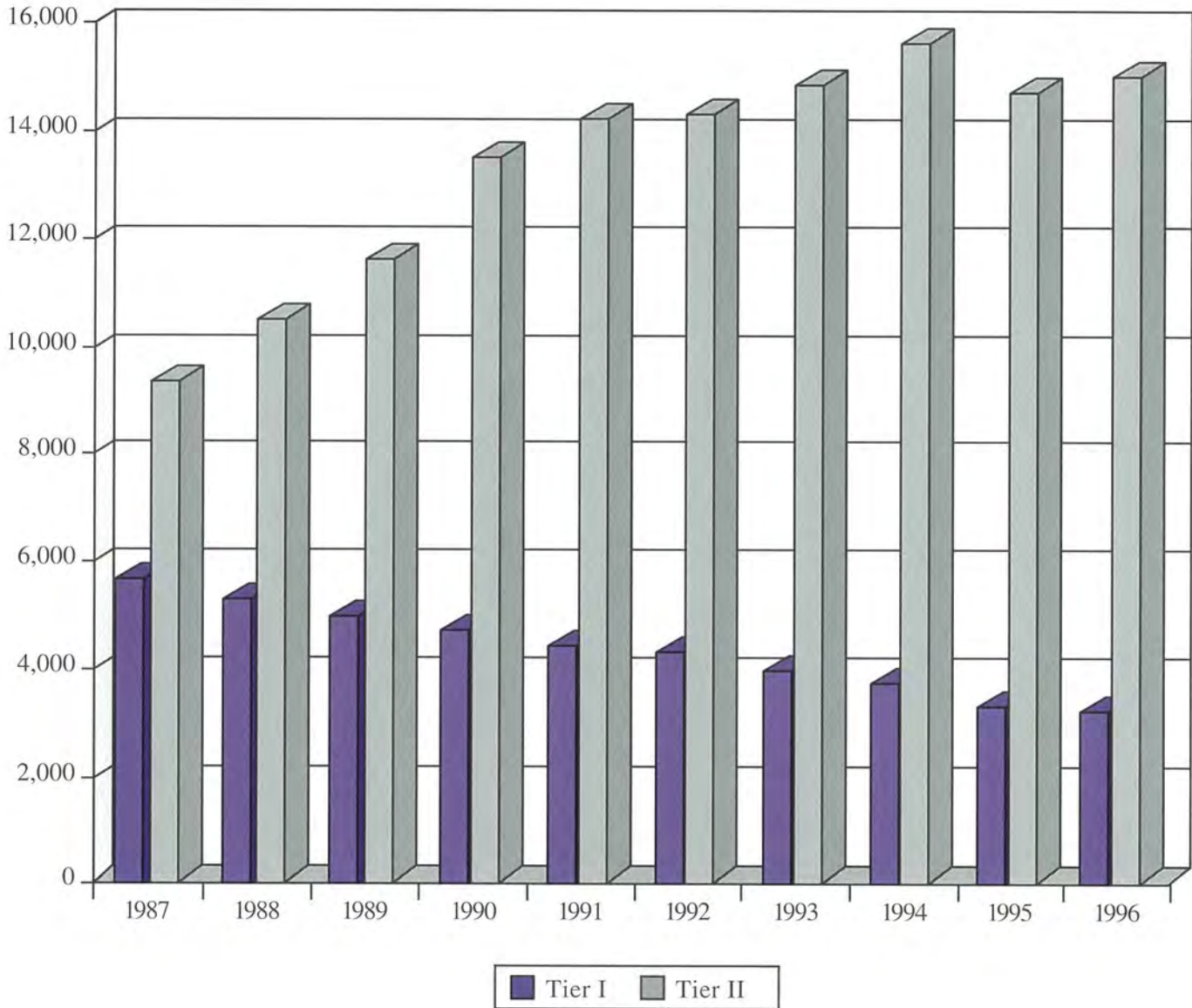


* Excludes members with Pending Statuses.

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Membership by Tier

(Active Members)

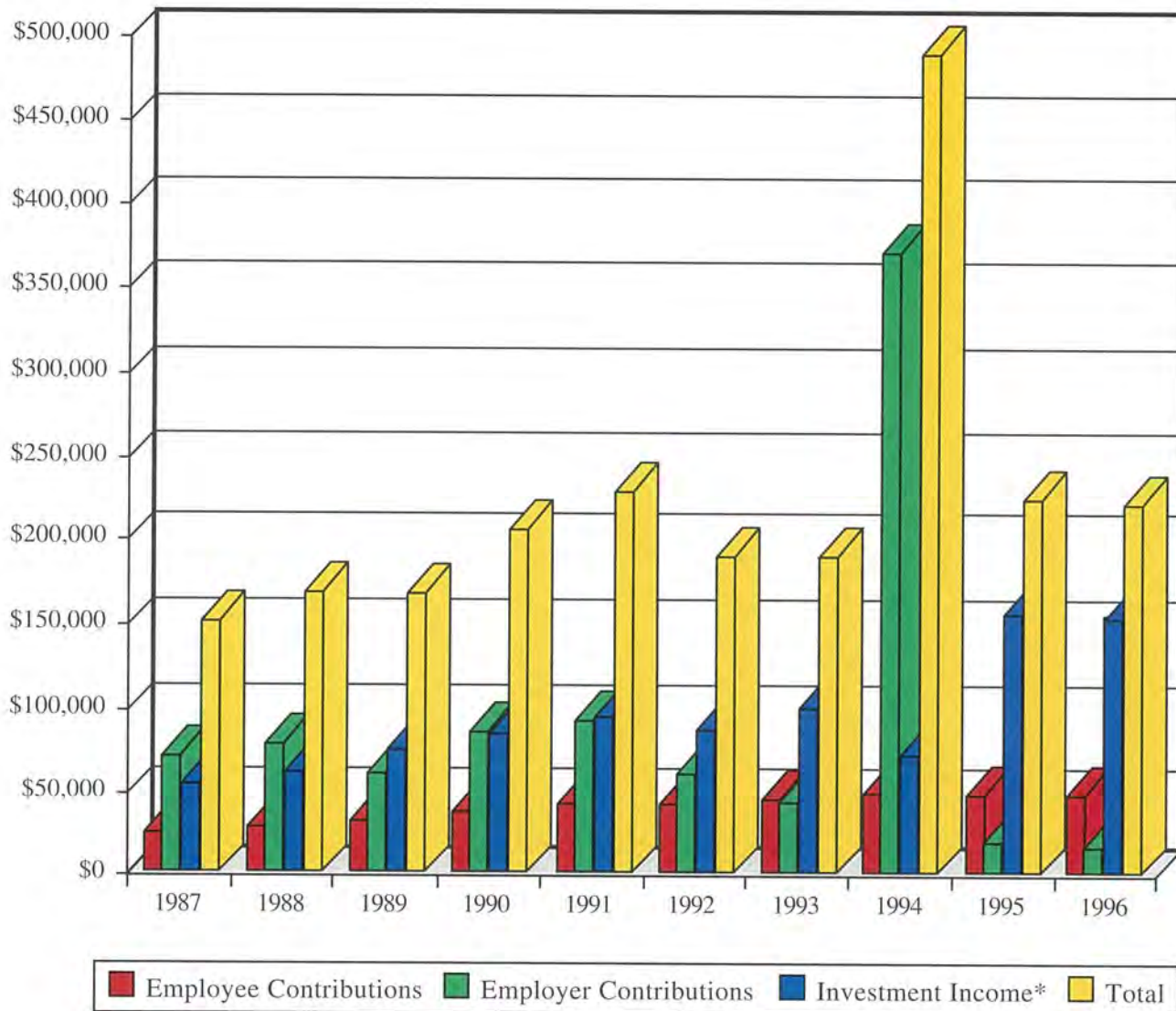


	1987	1988	1989	1990	1991	1992	1993	1994	1995	1996
Tier I	5,650	5,269	4,973	4,702	4,399	4,265	3,948	3,714	3,303	3,172
Tier II	9,350	10,474	11,599	13,481	14,202	14,311	14,849	15,659	14,706	14,918

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Revenues by Source

(in thousands)



	1987	1988	1989	1990	1991	1992	1993	1994	1995	1996
Employee Contributions	\$25,825	\$28,476	\$32,004	\$37,700	\$41,536	\$42,349	\$45,170	\$47,442	\$47,953	\$48,461
Employer Contributions	\$71,645	\$77,854	\$61,728	\$84,466	\$92,598	\$59,664	\$43,922	†\$369,382	†\$20,814	†\$16,463
Investment Income*	\$54,117	\$61,679	\$74,217	\$83,143	\$93,239	\$85,837	\$99,797	\$71,555	\$154,753	\$153,822
Total	\$151,587	\$168,009	\$167,949	\$205,309	\$227,373	\$187,850	\$188,889	\$488,379	\$223,520	\$218,746

* Net of investment manager fees. Does not include net appreciation fair market value.

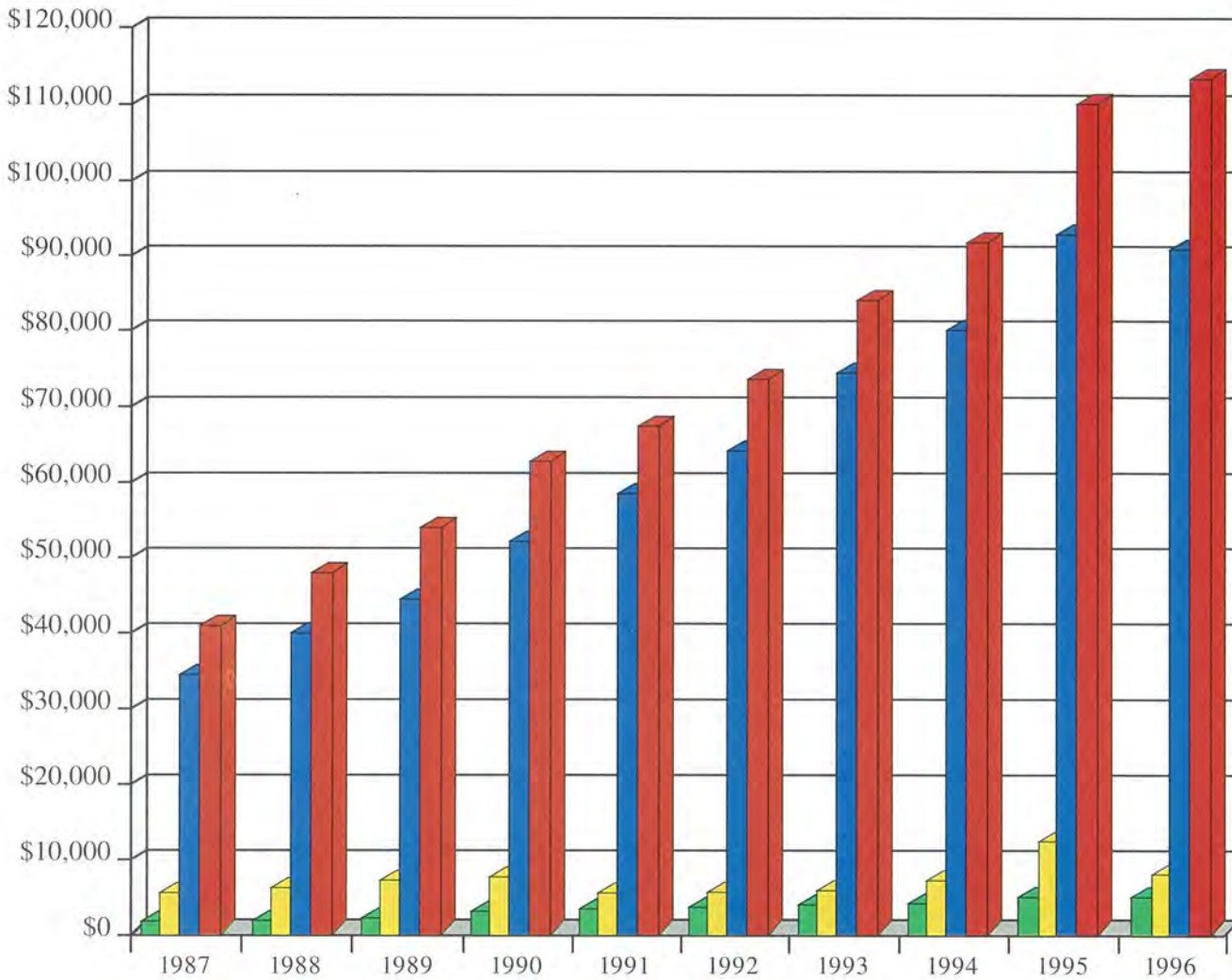
† Employer contributions include \$318,300,000 of County's 1994 funding of its portion of the Unfunded Actuarial Accrued Liability.

In subsequent years, agreements between OCERS and the County provided that employer's contributions would be paid from this funding.

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Expenses by Type

(in thousands)



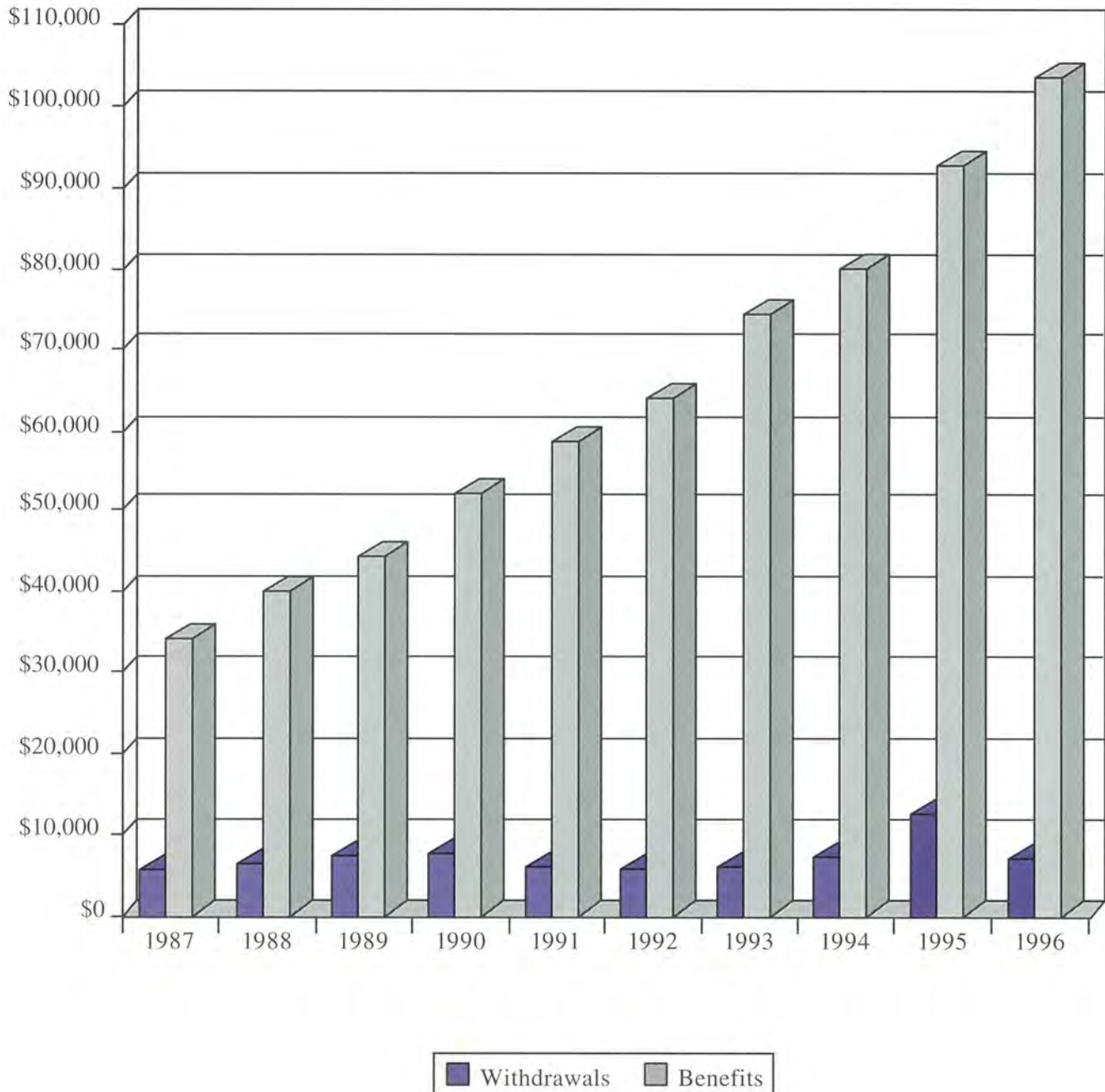
■ Administrative Expenses
 ■ Withdrawals
 ■ Benefits
 ■ Total

	1987	1988	1989	1990	1991	1992	1993	1994	1995	1996
Administrative Expenses	\$1,258	\$1,566	\$2,200	\$2,921	\$3,283	\$3,681	\$3,854	\$4,132	\$4,971	\$4,987
Withdrawals	\$5,409	\$6,209	\$7,124	\$7,509	\$5,679	\$5,681	\$5,928	\$7,426	\$12,523	\$7,166
Benefits	\$34,128	\$39,889	\$44,254	\$52,050	\$58,249	\$64,130	\$74,238	\$79,932	\$92,582	\$101,125
Total	\$40,795	\$47,664	\$53,578	\$62,480	\$67,211	\$73,492	\$84,020	\$91,490	\$110,076	\$113,278

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Benefits and Withdrawals Paid

(in thousands)



	1987	1988	1989	1990	1991	1992	1993	1994	1995	1996
Withdrawals	\$5,409	\$6,209	\$7,124	\$7,509	\$5,679	\$5,681	\$5,928	\$7,426	\$12,523	\$7,166
Benefits	\$34,128	\$39,889	\$44,254	\$52,050	\$58,249	\$64,130	\$74,238	\$79,932	\$92,582	\$101,125

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ORANGE COUNTY EMPLOYEES RETIREMENT SYSTEM
SCHEDULE OF BENEFIT EXPENSES BY TYPE
(in thousands)

	1987	1988	1989	1990	1991	1992	1993	1994	1995	1996
Retirement Benefits	\$33,863	\$39,655	\$44,005	\$51,749	\$57,910	\$64,035	\$73,544	\$79,280	\$92,335	\$101,074
Death Benefits	265	234	249	301	339	95	694	652	247	51
Withdrawals and Refunds	5,409	6,209	7,124	7,509	5,679	5,681	5,928	7,426	12,523	7,166
Total	\$39,537	\$46,098	\$51,378	\$59,559	\$63,928	\$69,811	\$80,166	\$87,358	\$105,105	\$108,291

HISTORY OF EMPLOYER CONTRIBUTION RATES BY EFFECTIVE DATE

<u>Effective Date</u>	<u>Recommended Rates</u>		<u>Implemented Rates</u>	
	<u>General</u>	<u>Safety</u>	<u>General</u>	<u>Safety</u>
7/1/85	14.40%	28.74%	14.40%	28.74%
7/1/86	13.95%	30.40%	13.95%	30.40%
7/1/87	13.73%	29.87%	13.73%	29.87%
7/1/88	13.72%	30.25%	13.72%	30.25%
7/1/89	11.48%	31.39%	11.48%	31.39%
7/1/90	10.81%	29.29%	10.81%	29.29%
7/1/91	10.80%	27.77%	10.80%	27.77%
12/1/91	9.35%	24.33%	9.35%	24.33%
7/1/92	2.55%	17.93%	2.55%	17.93%
7/1/93 *	4.86%	24.34%	2.55%	17.93%
7/1/94	3.91%	24.76%	3.91%	24.76%
7/1/95 **	5.39%	28.43%	5.39%	28.43%
7/1/96 **	2.86%	24.43%	2.86%	24.43%

* Recommended Contribution Rates for 1993 were not implemented.

** Include .50% of Additional Contribution credited to Unallocated Fund Balance.

ORANGE COUNTY EMPLOYEES RETIREMENT SYSTEM
HISTORY OF ACTUARIAL ASSUMPTION RATES
FOR THE PERIOD JANUARY, 1945 - DECEMBER, 1996

The table shown below is a comprehensive history of the interest rate assumption and the salary assumption rates corresponding to the Orange County Employees Retirement System since the inception of the system. These rates are adopted by the Board of Retirement and used by the consulting actuary in the creation of the actuarial valuation of the system.

Specifically, the interest rate assumption estimates the rate at which the funds of the system's investment portfolio will realize earnings over many years into the future. The salary assumption rate estimates the relative increases in the salary of a member from the date of the valuation to the estimated date of separation of the member from active service.

HISTORY OF OCERS ACTUARIAL ASSUMPTION RATES

<u>EFFECTIVE DATE</u>	<u>INTEREST RATE</u>	<u>SALARY ASSUMPTION RATE</u>
1/1/45	2.50%	0.00%
7/1/62	3.50%	0.00%
12/31/65	4.00%	0.00%
7/1/69	4.50%	0.00%
6/30/70	5.00%	0.00%
8/31/73	5.75%	0.00%
7/1/75	6.00%	0.00%
7/1/81	7.25%	5.00%
7/1/89	7.50%	5.50%
7/1/91	8.00%	6.00%
7/1/96	8.00%	3.50%

LIST OF PARTICIPATING EMPLOYERS

Capistrano Beach Sanitation District

Capistrano Valley Water District

City of San Juan Capistrano

County of Orange

Cypress Recreation and Park District

Foothill/Eastern Transportation Corridor Agency

Orange County Cemetery District

Orange County Employees Retirement System

Orange County Fire Authority

Orange County Law Library

Orange County Transportation Authority

Orange County Vector Control District

San Joaquin Hills Transportation Corridor Agency

Sanitation Districts of Orange County

Santiago Library System

Orange County Department of Education (closed to new members)

UCI Medical Center (closed to new members)

Orange County Employees Retirement System
2942 Daimler Street
Santa Ana, CA 92705
(714) 975-1962
