LPRO: Legislative Policy and Research Office

PUBLIC EMPLOYEES RETIREMENT SYSTEM (PERS)

BACKGROUND BRIEF

The Oregon Public Employees Retirement System (PERS) administers retirement benefits for approximately 213,000 active/inactive members, 135,000 retired members, and 925 public employers that include state agencies, public schools and many local governments. PERS also provides service and disability retirement income, death benefits, and retiree health insurance. In addition, PERS administers the Oregon Savings Growth Plan (OSGP), a separate 457(b) deferred compensation program for state and local government employees. PERS was created by the Legislative Assembly in 1945.

For those who retired in 2015, the average retirement age was 62 with 24 years of service. The average monthly benefit for that group at the time of retirement was $2,692, which represents 44% of final average salary.

PERS is one retirement system with three primary programs: Tier One, Tier Two, and the Oregon Public Service Retirement Plan (OPSRP). PERS also administers a separate Judge Member Program for judges of the Oregon Supreme Court, Court of Appeals, Oregon Tax Court, and Circuit Courts.

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GOVERNANCE STRUCTURE

The Oregon Legislative Assembly sets PERS policy, including benefit levels, membership requirements, and retirement payment options. Oregon courts have held that portions of the PERS statutes constitute a contract between public employers and their employees. Recent court decisions have found some provisions to be contract terms, while others have not been.

The Public Employees Retirement Board implements and administers the policies made by the legislature. As trustee of the Oregon Public Employees Retirement Fund (**OPERF**), the PERS Board has a fiduciary responsibility to administer the system in the best interest of PERS members. The Board is required by statute to "adequately fund the benefits to be provided." The Board administers the system as required by statute and ensures compliance with federal laws.

The five-member PERS Board is appointed by the Governor and confirmed by the Senate for three-year terms unless specified otherwise. One member must be a state employee in a management position or a person who holds office in the governing body of a participating public employer, other than the state. One member must be a current or retired public employee in an appropriate bargaining unit. The remaining three members must have experience in business management, pension management, or investing and may not be a PERS member or beneficiary.

The Board appoints an executive director and retains consultants including legal counsel, actuarial services, and medical advisors.

PERS FUNDING

PERS' basic funding equation can be summarized as:

B = C + E
(Benefits = Contributions + Earnings).

PERS benefits are currently funded by contributions from participating employers and investment earnings on those contributions. Employer contribution rates increase when investment earnings on the PERS Fund are insufficient to pay for retirement benefits.

Employer contribution rates have two components:

1. Normal Cost – the annual cost assigned to service provided in the current year; and
2. Unfunded Actuarial Liability (**UAL**) – the shortfall in revenue to pay for benefits already accrued.

Employer contribution rates are set by the PERS Board every two years, or as directed by the legislature, and are applied as a percentage of employers' PERS-covered payroll. When determining employer contribution rates, the PERS actuary, Milliman, considers employee demographics, wages, inflation, projected retirements, investment yields, and broad assumptions about trends affecting the system. Based on those assumptions, the actuary calculates a contribution rate for each employer, with the UAL portion of the rate calculated over a 20-year amortization period as a level percentage of payroll.

To limit volatility of individual employer rates, state agencies and community colleges are pooled for Tier One and Tier Two funding purposes. Local government employers can join the State and Local Government Rate Pool (**SLGRP**), and rates for employers who choose not to participate in a pool are based on their individual actuarial experience.

All school districts are in a separate rate pool for Tier One and Tier Two.

All participating public employers are in a single pool for OPSRP.

The PERS Board has instituted a "rate collar" that limits the increase of employer contribution rates in any biennium. Generally, the collar limits the change in rates to 20% of the previous biennium's rate.

Individual employer contribution rates vary as some PERS employers made lump-sum payments to pre-pay their PERS future contributions. These payments, typically financed with pension obligation bonds, are put into side accounts that are invested as part of the PERS Fund and receive actual earnings and losses.

When setting individual employer rates, side accounts are excluded. However, since the funds have already been contributed to PERS, they must be used exclusively to pay benefits owed, so the system's funded status is best reflected when including the side account balances.

Base employer contribution rates do not include side account offsets; net rates include the offsets.

The system-wide employer contribution rate summary is:

Contribution Rate	Percent of Payroll		
	15-17	17-19	Change
Uncollared base	18.18%	29.08%	10.90%
Collared base	17.46%	20.85%	3.39%
Collared net	10.61%	14.23%	3.62%

The rates shown above do not include the 6% IAP contributions or retiree health insurance.

PERS' funded status and UAL for the 2013 and 2015 system valuations (as of December 31) is shown below:

Funded status	2013	2015
Including side accounts	96%	79%
Excluding side accounts	86%	71%
UAL ($ billions)		
Including side accounts	$2.6	$16.2
Excluding side accounts	$8.5	$21.8

The decrease in funded status and increase in UAL from 2013 to 2015 is due to:

- Investment performance in 2014 and 2015 came in below assumption,
- Impact of the 2015 Supreme Court decision in the *Moro* case,
- Decrease in assumed rate of return to 7.50%,
- New mortality assumptions, and
- All other assumption changes and actual experience.

PERS FUND INVESTMENTS

The Oregon Investment Council (**OIC**), staffed by the Oregon State Treasury, makes investment decisions for the OPERF. The OIC has six members: four appointed by the Governor and confirmed by the Senate, the State Treasurer, and the PERS Executive Director, who serves as an ex officio, nonvoting member. The OIC also employs private-sector investment managers and contracts with private firms to carry out the Council's directives. Funds are invested in common stocks, fixed income securities such as mortgages and corporate bonds, private equity, real estate, and a variety of other investments.

EMPLOYEE MEMBERSHIP

An employee must work at least 600 hours per calendar year in a qualifying position for a PERS-covered employer to qualify for PERS membership. PERS membership is portable among participating Oregon public employers.

An employee is a Tier One member if they worked for a PERS-participating employer before January 1, 1996. Tier Two members are those who were first employed on or after January 1, 1996 and before August 29, 2003. Newer employees are OPSRP members.

There are two membership classifications for the primary PERS programs: General Service and Police and Fire (**P&F**). Some examples of qualified positions for the P&F classification include Oregon State Police officers; local government police officers; parole and probation officers; Oregon Department of Corrections employees; and persons employed by cities, counties, or districts whose duties include firefighting.

Of the 213,000 non-retired members, 24% were in Tier One, 28% in Tier Two, and 48% were OPSRP members.

RETIREMENT BENEFITS

Tier One members receive full retirement benefits at age 58 or with 30 years of service and their account balances are guaranteed to be credited annually with the assumed earnings rate (currently 7.5%). Retirement benefits are calculated by up to three methods for Tier One members (and the member is entitled to the calculation method that provides the highest benefit):

- Money Match - the amount in a member's regular account is matched by the employer and converted into a lifetime annuity for the employee;
- Full Formula - multiplies a member's final average salary (**FAS**) by years of creditable service, multiplied by either 1.67% for General Service employees or 2.0% for P&F employees; or
- Formula Plus Annuity[1], which annuitizes the member's account balance, and adds one percent of their FAS (or 1.35% for legislators and P&F members) multiplied by their years of creditable service.

FAS is the higher of either the salary from the last 36 months divided by the number of months worked in that period, or the average salary earned in the top three calendar years. A Tier One member's FAS calculation includes any lump-sum payments for accrued vacation and compensatory time, adjusted value of accumulated unused sick leave if their employer participates in the sick leave program, and member payroll contributions (typically referred to as the 6% pick up).

In contrast, Tier Two members have a higher retirement age to receive full benefits (age 60 or with 30 years of service) and they receive market returns versus guaranteed returns annually. Retirement benefits are calculated using either Money Match or Full Formula. A Tier Two member's FAS calculation cannot include lump- sum payments received for accrued vacation time, but does include the adjusted value of accumulated unused sick leave if their employer participates in the sick leave program, and it includes member payroll contributions (the 6% pick up).

The normal and early retirement age for P&F members is less than General Service members. Additionally, the Full Formula factor is higher for years of service as a P&F member. Tier One and Tier Two P&F members can purchase Police Officer and Firefighter Units, which provide additional benefits between their date of retirement and age 65. Up to eight units can be purchased, either via payroll deduction if the qualified, active P&F member is less than age 65, or a lump-sum payment within 60 days of their retirement date and before reaching age 60.

Each purchased unit provides a $20 monthly benefit paid by PERS for five years, $10 from member contributions and $10 from employer contributions. Accrued earnings on unit benefits above the amount purchased are

[1] Available only to members who made contributions before August 21, 1981.

paid in a lump- sum with the member's first monthly unit benefit payment.

Tier One and Tier Two members can purchase service credit for a number of circumstances, such as waiting time (the 6-month period between being hired into a PERS-covered position and establishing PERS membership), buying back forfeited service due to prior withdrawal, service time for teaching in a public school, employment as a public safety officer in another state, and military service. These purchases may increase the member's benefit or allow the member to retire earlier. Some purchases require 10 years of accrued service time. OPSRP members cannot purchase service credit.

Public employees hired on or after August 29, 2003, are OPSRP members. OPSRP members have a higher retirement age (65, or 58 with 30 years of service) than Tier One or Tier Two. Retirement benefits are calculated using the member's FAS multiplied by their years of qualified service multiplied by a factor of 1.5% for General Service and 1.8% for P&F members. Accrued vacation time, accumulated unused sick leave and the member payroll contributions (the 6% pick up) are not included in an OPSRP member's FAS.

INDIVIDUAL ACCOUNT PROGRAM (IAP)

The IAP is a separate but additional retirement account and can have earnings or losses. The member contribution is fixed in statute at 6% of covered salary and the law allows employers to pay the member contribution. Approximately 70% of PERS members have their IAP contribution paid by their employer (the 6% pick up).

Through reforms made in 2003, as of January 1, 2004, a member's 6% of payroll contribution has been directed to the member's IAP account instead of their Tier One or Tier Two account. An OPSRP member's 6% contribution is also placed in their IAP account. By directing the member's 6% contribution to the IAP, Tier One and Tier Two account balances stopped growing as rapidly and many Tier One members are now retiring under the Full Formula calculation instead of Money Match. For members who retired in 2003, the average retirement benefit replaced 66% of FAS; for those who retired in 2015, it was 44%.

At retirement, a member may receive the IAP account balance as a lump-sum payment or in installments over a five, 10, 15, or 20-year period, or over the member's anticipated life span.

PERS RETIREES

Retirement Process

In the years before retirement, members are encouraged to get an estimate of their benefits using PERS' Online Member Services **(OMS)** or via a written benefit estimate.

Members must complete and submit a service retirement application and separate from employment to retire. PERS recommends taking additional steps such as reading publications that provide an overview of retirement and attending a Retirement Application Assistance Session. In these one-hour sessions, PERS staff reviews the retirement application and answers questions.

Work After Retirement

A PERS retiree who works for a private sector or non-PERS covered employer may work unlimited hours without affecting their retirement benefit. If a retiree returns to work for a PERS-covered employer, their PERS benefit could be affected based on who their employer is and the hours they work in a calendar year.

A Tier One or Tier Two retiree working for a PERS-covered employer can continue to receive retirement benefits as long as their employment with one or more participating public employers does not total more than 1,040 hours in a calendar year. Exceptions to the 1,040 limit are established in statute for Tier One and Tier Two retirees in a number of circumstances. Overall, the retiree must be receiving normal retirement benefits to qualify for an exception. If a retiree works concurrently for a PERS employer under an exception and in a non-exempt position with another PERS employer, only the hours worked in the non-exempted position count towards the 1,040-hour limit. Unless specified in statute, exceptions do not apply if a member retired before normal retirement age.

Retirement benefit payments cease if a retired OPSRP member becomes employed in a qualifying position with a PERS-participating employer or works more than 600 hours in a calendar year for one or more participating employers; and the member will become an active member of the OPSRP Pension Program upon re-employment.

Once any retired member reaches full retirement age based on Social Security guidelines, the member can work unlimited hours for a PERS-covered employer and continue to receive PERS retirement benefits.

PERS Health Insurance

Retirees, their spouses, and eligible dependents can participate, at their own expense, in the PERS Health Insurance Program. The program includes options for medical and dental insurance, including Medicare supplemental plans, as well as long-term care insurance plans. Retirees are eligible for a monthly premium subsidy which varies based on their employer or years of service.

RECENT LEGISLATIVE REFORMS

In 2013, the Legislative Assembly modified the cost-of-living adjustment (**COLA**) in its regular session (Senate Bill 822) and a special session (Senate Bill 861). After an Oregon Supreme Court ruling (*Moro* decision) issued in April 2015, retired members receive a maximum 2% COLA annually for service on or before October 1, 2013. For service after October 1, 2013, the COLA is 1.5% for the first $60,000 of the annual benefit and 0.15% on the benefit amount above $60,000.

Senate Bill 822 also eliminated the tax remedy benefit payment increase to benefit recipients who do not pay Oregon income taxes because they do not live in Oregon. Only specific Tier One members are eligible for the tax remedy payment.

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