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Legislative Committee Services
State Capitol Building
Salem, Oregon 97301
(503) 986-1813

Background Brief on …

Public Employees Retirement System (PERS)

Oregon's Public Employees Retirement System **(PERS)** enables public employers to provide their employees with retirement benefits. PERS has administered benefits since 1946, providing service and disability retirement income, death benefits, and retiree health insurance. PERS also administers the Oregon Savings Growth Plan **(OSGP)**, which is a separate deferred compensation program for state and local government employees.

State government, public schools, community colleges, and many local governments (cities, counties, and special districts) participate in PERS. There are approximately 900 public employers currently participating in PERS, covering about 95 percent of all public employees in Oregon and with a total PERS-covered annual salary of $9.2 billion. As of December 2012, there were approximately 331,000 PERS members: 167,000 active, 42,000 inactive, and 122,000 retirees. For those who retired between 1990 and 2012, the average retirement age was 59 with 22 years of service, and the average monthly benefit at the time of retirement was $2,172, which represents 54 percent of final average salary.

Governing 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 and rules constitute a contract between public employers and their employees when the legislature has unambiguously shown their intent for the statute to be a contract term. Recent court decisions have found some provisions to be contract terms, while others have not been, so the limit of the legislature's scope of available policy changes is not clear.

The Public Employees Retirement Board implements and administers the policy choices made by the legislature. As trustee of the Oregon Public Employees Retirement Fund **(OPERF)**, the Board has a fiduciary responsibility to administer the system in the best interest of the members contributing to the fund. The Board's main role is to administer the system as required in statute and monitor the plan for compliance with federal laws. They appoint an executive director and retain consultants in areas such as legal counsel, actuarial services, and medical advisors, to assist in the administration of the system.

The Board consists of five members who are 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.

Membership

In order to qualify for PERS membership, an individual must work at least 600 hours per calendar year in a qualifying position for a PERS-covered employer to be considered an active member. Membership in PERS is portable among participating Oregon employers.

PERS is a single retirement system with three primary plans: Tier One, Tier Two, and the Oregon Public Service Retirement Plan **(OPSRP)**. They also maintain the separate PERS Judge Member Program that includes any judge of the Oregon Supreme Court, Court of Appeals, Oregon Tax Court, and Circuit Courts.

There are two types of classifications for all primary PERS plans. Examples of qualified positions for the *Police and Fire* **(P&F)** classification include Oregon Department of Corrections employees, Oregon State Police officers, local government police officers, parole and probation officers, the state and deputy state fire marshal, and persons employed by cities, counties, or districts whose duties involve firefighting[1]. All other qualifying positions are classified as *General Service*.

Benefit Levels

For both General Service and P&F, the level of benefits differs depending on their hire date. An employee is a Tier One member if they began working for a PERS-participating employer before January 1, 1996. Tier Two employees are those who were first employed on or after January 1, 1996 and before August 29, 2003. All other employees are members of the OPSRP Pension Program.

Tier One members can receive full retirement benefits at age 58 or 30 years of service; they have a guaranteed annual rate of return on their account balances that is equal to the system's assumed earnings rate, which is currently at 7.75 percent. Retirement benefits can be calculated by one of three methods: Money Match, in which the amount in a member's regular account is matched by the employer and converted into an annuity for the lifetime of the employee; Full Formula, which multiplies the member's final average salary **(FAS)** by their years of creditable service, multiplied by either 1.67 percent for General Service employees or 2.0 percent for P&F employees; or Formula Plus Annuity[2], which annuitizes the member's account balance, and adds one percent of their FAS (or 1.35 percent for legislators and P&F members) multiplied by their years of creditable service.

The FAS is defined as 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 will include any lump-sum payments for accrued vacation and compensatory time, adjusted value of accumulated unused sick leave if their

[1] Firefighters and police officers that work for the City of Portland and were hired before January 1, 2007 receive retirement benefits through the Portland Fire and Police Disability and Retirement Fund instead of PERS.

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

employer participates in the sick leave program, and member payroll contributions (typically referred to as the 6 percent pick up).

In contrast, Tier Two members have a higher retirement age for receiving full benefits (age 60 or 30 years of service) and they receive market returns versus guaranteed returns. Members have the option of calculating retirement benefits either by Money Match or Full Formula. A Tier Two member's FAS calculation cannot include lump sum payments received for accrued vacation time.

Public employees hired on or after August 29, 2003, are part of OPSRP which is a hybrid pension plan with two components: the Pension Program (formula benefit) and the Individual Account Program **(IAP)**. The Pension Program provides a life pension funded by employer contributions and benefits are calculated by the member's FAS multiplied by their years of qualified service multiplied by a factor of 1.5 percent for General Service and 1.8 percent for P&F members. OPSRP members have a higher retirement age (65, or 58 with 30 years of service) than Tier One or Tier Two.

The IAP contains all member contributions made on and after January 1, 2004. OPSRP members contribute six percent of their salary, but employers may agree to pay the six percent contribution. Beginning on January 1, 2004, Tier One and Tier Two member contributions were redirected into the IAP portion of OPSRP, but members retain their existing PERS accounts. The IAP has no guaranteed benefit or earnings; benefits are based on the member's account at retirement or withdrawal and continue to be adjusted for market earnings or losses until paid out. At retirement, the member may receive the IAP as a lump-sum payment or in equal installments over a five, 10, 15, or 20-year period, or over the member's anticipated life span.

Police and Fire PERS members operate under slightly different rules. The normal and early retirement age for P&F members is less than General Service members. Tier One and Tier Two P&F PERS members have the option of purchasing what is known as 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 member is less than age 65, or a lump sum payment within 60 days of their retirement date and before reaching 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 paid in a lump sum with the member's first monthly unit benefit payment.

Any Tier One and Tier Two PERS member can voluntarily purchase service credit for a number of circumstances, such as paying back forfeited service due to prior withdrawal, service time for teaching in a public school or employment as a public safety officer in another state, or for military service. These purchases may impact the member's benefit or allow the member to retire earlier.

PERS Funding

PERS benefits are funded by contributions from participating employers, their employees, and earnings from investment of those contributions.

Employer contribution rates are set by the Board, and are based on a percentage of the employer's PERS -covered payroll. Each employer's individual rate varies based on determinations by PERS actuaries to ensure that the system has adequate long-term funding. When determining employer rates, actuaries consider 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 that is expected to fund projected needs within a limited amount of time.

To limit volatility of Tier One and Tier Two individual employer rates, state agencies and community colleges are pooled for PERS funding purposes. Local government employers are allowed to join the state agency pool on a voluntary basis (called 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 experience. School districts are separately pooled and all school districts have the same base employer contribution rate. Actual rates vary as the majority of school districts have purchased bonds to pre-pay their pension liabilities (called side accounts). Each pool and each unpooled local government employer is assigned a separate employer contribution rate. All participating public employers are pooled for OPSRP funding purposes.

The system-wide, uncollared average base contribution rate for the 2015-2017 biennium is 18.18 percent of PERS covered payroll (down from 23.08 in the previous biennium). Base rates do not include the six percent IAP contributions, retiree health insurance, rate collar impacts, or side accounts.

The member contribution is fixed in statute at six percent of covered salary. Statutes allow employers to agree to pay the member contribution; approximately 70 percent of PERS members have their IAP contribution picked up in this fashion.

The Oregon Investment Council **(OIC),** staffed by the Oregon State Treasury, makes investment decisions for the OPERF in addition to all funds of the State of Oregon. 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, and a variety of other investments.

As of December 31, 2013, PERS was estimated to be 96 percent funded when side account deposits are included, 86 percent funded if side accounts are not included. The unfunded actuarial liability (UAL), when including side accounts, was estimated to be $2.6 billion, down from $11 billion at the close of 2011.

PERS Retirees

Retirement Process

The process for becoming a PERS retiree is essentially the same between Tier One/Tier Two members and OPSRP members. Everyone is required to complete and submit a service retirement application and notify their employer of their retirement. PERS recommends taking other steps such as reading publications that provide an overview of retirement and attending a Retirement Application Assistance Session. Another step recommended by PERS is obtaining a benefit estimate. Members can estimate their retirement benefits by using the Online Member Services **(OMS)** website, or request an estimate in writing.

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. Retired state employees are eligible for higher monthly premium subsidies based on their years of service.

Work After Retirement

If a retiree wishes to re-enter the workforce, their benefit could be affected based on who their employer is and how many hours they work per year. Any retiree who works for a private sector or non-PERS covered employer may work unlimited hours without any impact on their level of retirement benefit.

A Tier One/Tier Two retired member working for a participating public employer can continue to receive retirement benefits as long as the period or periods of employment with one or more participating public employers do not total 1,040 hours or more in a calendar year. Exceptions to the 1,040 rule are established via statute for Tier One and Tier Two retirees in a number of qualified positions for PERS-covered members. Overall, the retiree must be receiving normal retirement benefits in order to qualify for the exception. If a retiree works concurrently for a PERS employer under an exemption and a non-PERS employer and the position is not exempted, only the hours worked in the non-exempted position count towards the 1,040-hour limit. Unless specified, the exceptions do not apply if a member chooses to retire early.

Retirement benefit payments will cease for an OPSRP retired member who becomes employed in a qualifying position by a participating employer or works a total of more than 600 hours in a calendar year for one or more participating employers; they will also become an active member of the Pension Program upon employment. If the OPSRP retiree received a lump-sum payment upon retirement, they will return to active membership if they become employed in a qualifying position or work more than 599 hours in a non-qualifying position in the calendar year that the payment was made. If the date of employment was on or before the date the lump sum payment was made, the retiree must repay the benefit.

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). The end result is an annual cost of living adjustment capped at 1.25 percent for those whose yearly benefit is less than $60,000 and 0.15 percent for those with a yearly benefit exceeding $60,000. Senate Bill 861 provided for an annual supplementary payment of 0.25 percent to all benefit recipients, capped at $150. Those who have a yearly benefit of less than $20,000 will receive a second supplementary payment of 0.25 percent. The supplementary payments are scheduled to end in 2019.

Senate Bill 822 also eliminated the increased retirement benefits resulting from Oregon income taxation of payments if the person receiving the payments does not pay Oregon income tax because they are not an Oregon resident.

Senate Bill 822 and Senate Bill 861 were challenged and are now under expedited review by the Oregon Supreme Court. The challenge should be fully briefed and argued before the 2015 legislative session convenes.

Staff and Agency Contacts

Jan Nordlund
Legislative Committee Services
503-986-1557
jan.nordlund@state.or.us

Marjorie Taylor, Senior Policy Advisor
Public Employees Retirement System
503-431-8902

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