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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 2010, there are a total of approximately 346,000 PERS members: 194,000 active, 39,000 inactive, and 113,000 retirees. The average retirement age is 59 with 22 years of service.

## Governing Structure

The Oregon State Legislature sets PERS policy, including benefit levels, membership requirements, and retirement payment options. Oregon courts have held that the statutes governing PERS constitute a contract between public employers and their employees. The court decisions restrict the legislature, limiting the scope of policy changes that can be made through legislative action.

The Public Employees Retirement Board (**PERB**) implements and administers the policy choices made by the legislature. As trustee of the Oregon Public Employees Retirement Fund (**OPERF**), the PERB has a fiduciary responsibility to administer the system in the best interest of the members contributing to the fund. The PERB'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 PERB consists of five members (trustees) 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 employee, 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 for a PERS-covered employer in a qualifying position requiring at least member hours per calendar year to be considered an active member. Membership in PERS is portable among participating Oregon employers.

PERS is a single retirement plan 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, adult parole and probation officers, the state and deputy state fire marshal, and persons employed by cities, counties, or districts whose duties involve firefighting<sup>1</sup>. All other qualifying positions are classified as *General Service*.

## Benefit Levels

For both classifications, the level of benefits differs depending on criteria such as their hiring date. An employee qualifies as a Tier One member if they began working for a PERS-participating employer on or before December 31, 1995, and worked six full calendar months in a qualifying position requiring at least 600 hours per calendar year. The 1995 Legislative Assembly established a different level of benefits (Tier Two) for employees 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, who can receive full retirement benefits at the age of 58, 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 eight 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 (General Service employees) or 2.0 percent (P&F employees); or Formula Plus Annuity<sup>2</sup>, 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. For all methods, members also receive an annual cost of living (COLA) adjustment of up to two percent.

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<sup>1</sup> 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.

<sup>2</sup> Available only to members who made contributions before August 21, 1981.

The FAS is defined as the higher of either the member's last 36 months of PERS-covered salary or the three calendar years in which the member was paid the largest total salary by a PERS-participating employer, divided by 36 months. In determining a member's FAS, "excess" overtime - overtime paid above the average paid to employees of that class during the time period being averaged, as established by PERS rule - is not included. 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 employer participates in the sick leave program, and member payroll contributions.

In contrast to Tier One, Tier Two members have a higher retirement age for receiving full benefits (generally, age 60 or after 30 years of service), and 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 (except for those who work for a local government) cannot include subject salary attributed to pay periods occurring before the first pay period included in the three calendar years or at the beginning of the last 36 calendar months of active membership, or lump sum payments received for accrued vacation time during the time period used to calculate the FAS.

Public employees hired on or after August 29, 2003 are a part of OPSRP, unless membership was previously established under Tier One or Tier Two. OPSRP is a hybrid pension plan (defined contribution/defined benefit) with two components: the Pension Program (defined benefit) and the Individual Account Program (IAP) (defined contribution). 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 (or 1.8 percent for qualified P&F members). The program has a normal retirement age of 65 or 58 with 30 years of retirement credit.

The IAP contains all member contributions made on and after January 1, 2004. OPSRP members contribute six percent of their salary, and 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. As a defined contribution plan, the IAP has no guaranteed benefit. Employees (or employers on behalf of employees) make contributions into the IAP and when a member retires, he or she receives the account balance (comprised of contributions and earnings or losses). 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.

The retirement age for P&F PERS members is different than for General Service members:

	Normal Retirement	Early Retirement
Tier One	55 or 50 with 25 years of qualifying service	50 or any age for 911 operators with more than 25 years of qualifying service
Tier Two	55 or 50 with 25 years of qualifying service	50 or any age for 911 operators with more than 25 years of qualifying service
OPSRP	60 or 53 with 25 years of qualifying service	55 if vested
IAP	55	55

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 the age of 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 the service date of retirement 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.

Tier One and Tier Two PERS members 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.

## **PERS Funding**

PERS benefits are funded by contributions from participating employers, their employees, and earnings from investments.

Employer contribution rates are set by the PERB, and are paid based on a percentage of employee salary. Each employer's individual rate varies based on recommendations of 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 determines general needs for the system and then calculates a contribution rate for each individual employer in order to fund projected needs.

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, 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 offset their pension liabilities. 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.

System wide, the average contribution rates for the 2011-2013 biennium average about 10.8 percent of PERS covered payroll after applying side account offsets. Net rates do not include the six percent IAP contributions or costs of debt service on Public Obligation Bonds.

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

The Oregon Investment Council (OIC) makes investment decisions for the OPERF in addition to all State of Oregon Funds. The OIC has six voting members: four appointed by the Governor and confirmed by the Senate who are qualified by training and experience in the field of investment and are not a state employee or elected public official, the State Treasurer, and the PERS Executive Director, who serves as an ex officio, nonvoting member. The OIC also employs private-sector money managers and contracts with private firms to carry out the Council's prescriptions. Funds are invested in common stocks, fixed income securities such as mortgages and corporate bonds, and a variety of other investments.

OPERF [returns](#) are available monthly. As of December 31, 2011, PERS was estimated to be 81 percent funded, including advance deposits from employers' side accounts, and the unfunded actuarial liability (UAL), when including side accounts, was estimated at \$11 billion.

## **PERS Retirees**

### *Data Verification*

All PERS members who are within two years of their earliest retirement date can request a Data Verification for purposes of ensuring that information is correct. Information in the verification includes accrued creditable service time and the member's FAS account balance. Verification data for Tier One and Tier Two members also includes Regular and Variable account balances and accumulated unused sick

leave. The Verification does not cover a member's P&F Unit account or their IAP. Information contained in the Data Verification is from the member's original hire date with each of their PERS-participating employers, excluding any forfeited or refunded time, up to the last calendar year for which annual earnings or losses have been credited. The normal processing time for a Data Verification is between four to six months, which includes a 60-day time period for the member's employer(s) to review data. Upon PERS providing the Data Verification, members have 60 days to dispute the data's accuracy.

Without a Data Verification, review and validation of data is completed when a member submits their retirement application. Otherwise, the information confirmed in the verification is used by PERS for compiling a requested benefit estimate. One Data Verification per members is provided at no cost; additional verifications cost \$100 each.

#### *Retirement Process*

The process for becoming a PERS retiree is essentially the same between [Tier One/Tier Two members](#) and [OPSRP members](#). While the only required steps for everyone is to complete and submit a service retirement application and notify their employer of their retirement, PERS recommends utilizing other steps such as reading publications that provide an overview of retirement and/or attending a Retirement Application Assistance Session. Another important 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](#). This is one of the steps recommended by PERS to be completed prior to submitting a service retirement application.

#### *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.

#### *Re-entering the Workforce*

If a retiree wishes to re-enter the workforce, the retiree's payments could be affected based on who their employer is and/or how many hours they work per year. Tier One, Tier Two, and OPSRP retirees who work for a private sector or non-PERS covered employer can work unlimited hours without any impact on their level of retirement benefits.

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 (known as the "1,040 rule"). [Exceptions](#) from 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. Examples include a registered nurse working as a nursing instructor, National Guard members on state active duty who are of normal retirement age, employees of a municipal police department of a city with a population of less than 15,000, and employees of the Legislative Assembly or the Oregon State Police for service during a legislative session. 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 on the non-exempted position work 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 is receiving a service retirement allowance and 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 an OPSRP retiree receiving a monthly pension becomes employed

in a non-qualifying position, they can remain in the Pension Program if they work no more than 599 hours in a calendar year. If the OPSRP retiree received a lump sum retirement, they will return to active membership if they become employed in a qualifying position or a non-qualifying position for more than 599 hours in the calendar year that the payment is received. If the date of employment was on or before the date payment was issued, the retiree must repay the benefit.

### **The PERS Reform and Stabilization Act of 2003**

The intent of House Bill 2003 (2003) was to reform PERS for the future in a way that generated savings for public employers while protecting the accrued benefits of employees. Reforms were also meant to resolve structural issues within the system. House Bill 2003 was primarily directed to the benefits payable to employees who became members of the system before the OPSRP went into effect (August 29, 2003). These employees are divided between Tier One members (those who became members before January 1, 1996) and Tier Two members (those who became members on or after January 1, 1996 and before August 29, 2003).

The three main reforms of House Bill 2003 were:

- Shifting the six percent employee contribution from the PERS account to a separate defined contribution account (IAP).
- Altering the mechanism for crediting interest to Tier One member accounts – essentially suspending guaranteed earnings during periods of low investment returns. The guarantee of the “assumed rate” of earnings for Tier One members was also changed to be over the course of a member’s career.
- Temporarily suspending future cost-of-living adjustments for members who retired between April 1, 2000 and March 1, 2004 who had excess interest credited to their accounts in 1999.

In combination with the use of updated mortality tables, these reforms have reduced the unfunded actuarial liability and lowered employer contribution rates.

Since the enactment of House Bill 2003, modifications to the original legislation have been enacted. House Bill 2285 (2007) retroactively eliminated the “break-in service” provision as established under the 2003 PERS reforms. Prior to House Bill 2003, a break-in service occurred when an active Tier One or Tier Two member performed no hours of service in a qualifying position for a period of six consecutive months or longer and were not exempt for reasons such as vacation, military duty, illness, or other authorized leave. If a break-in service was incurred, contributions were accrued under the OPSRP pension program. House Bill 2285 also equalized the accrual of retirement credit by OPSRP members by changing the retirement credit calculation to be the same as for Tier One and Tier Two members and established provisions for school employees to ensure they receive a full year’s worth of retirement credit if they were employed during the entire portion of an academic school year.

### **Litigation**

House Bill 2003 (2003) also established a process for expedited judicial review of any legal challenges to the legislatively approved PERS reforms. The Oregon Supreme Court had jurisdiction regarding challenges to the constitutionality of the changes made by the legislation or to claims of breach of contract. Since the PERS Reform and Stabilization Act of 2003 was enacted, a number of court cases have been filed.

*Strunk/City of Eugene: Strunk v. PERB* was a challenge to various provisions of the 2003 reforms. The Oregon Supreme Court ruled that the cost-of-living-adjustment (COLA) freeze enacted by the 2003 Legislative Assembly to recover overpayments from earnings crediting in 1999 was invalid. As a result of the 2003 legislation, PERS temporarily suspended the COLA for Tier One members who retired with an effective date on or after April 1, 2000 and

before April 1, 2004, under the Money Match calculation. The court also determined that PERS must annually credit the assumed rate, currently eight percent, to Tier One member's regular accounts. PERS credited zero percent to Tier One regular accounts in 2003 based on legislation passed that year.

*City of Eugene v. PERS* (also known as the *Lipscomb* case): Several employers and members sued to challenge PERS' policies on actuarial factors, variable match, and earnings crediting. The Marion County Circuit Court remanded the PERS Board's orders allocating 1999 earnings and setting employers rates for the petitioning employers. The board was directed to reissue these orders after the judge's final 2003 ruling on many PERS practices, such as actuarial factors, variable account calculations, and reserving. After the end of the 2005 Legislative Session, the Oregon Supreme Court issued its decision, ruling that the 2003 PERS reform legislation and a Settlement Agreement requiring PERS to reallocate 1999 earnings to Tier One benefit recipient accounts at 11.33 percent instead of 20 percent resolved the issues in the case.

The combined application of the *Strunk/City of Eugene* decisions varies on items such as when the Tier One member retired or will retire. In early 2006, the PERS Board issued an Order Adopting Repayment Methods for the recovery of overpayments under *Strunk* and *City of Eugene*. The board order affected Tier One members who retired on or after April 1, 2000 and before April 1, 2004 under the Money Match method and people who received or are receiving benefits based on 1999 account balances. The PERS Board has pursued repayment of benefit overpayments made as a result of 1999 earnings crediting.

The Oregon Supreme Court awarded fees and costs to the plaintiff's attorneys in the *Strunk* case to be paid from earnings that would otherwise be credited to Tier One members for 2007. The PERS Board will credit eight percent to Tier One regular accounts for 2007, with a portion of that eight percent being used to pay attorneys' fees and costs as directed by the court.

In February 2008, the board approved a preliminary 2007 earnings crediting rate of 7.97 percent after subtracting from Tier One regular account earnings for the plaintiff's attorney fees/costs. Final earnings crediting occurred in March 2008.

*Young v. State of Oregon*: Although *Young v. State of Oregon* focused on laws pertaining to exempt employees who were not due overtime for extra hours worked, it also affected PERS accounts. The state became liable for overtime hours worked by these employees during a 26-month period, July 1995 to August 1997. As a result of the court decision, approximately 1,850 current and former state employees are entitled to additional contributions to their PERS accounts. PERS is currently determining the overall project scope and securing project funding and anticipates account adjustments occurring from January 2008 to January 2009.

*Bell v. PERB*: The focus of the *Bell* case is on the calculation of benefits at the time of retirement. The plaintiff's estimated benefits differed by over \$1,100 per month from her actual retirement benefits, and the PERS member testified that if she received accurate information from PERS in a timely fashion, she would have modified her date of retirement. The plaintiff prevailed in Marion County Circuit Court, and the Oregon Court of Appeals modified the amount of the jury award, refused to award interest, but granted leave to reconsider the interest issue if the Oregon Supreme Court were to reverse the appeal court's decision. The case is the basis of the provision in enacted Senate Bill 897 (2009) to establish a formal benefit verification process.

*Murray v. PERB*: in May 2010, the Oregon Court of Appeals reversed the PERB on its decisions to charge the PERS variable account for administrative expenses in years of account loss. Such losses occurred in 2001 and 2002, and the account was charged just under \$2 million to cover losses. The court rejected the defendant's argument that Oregon statutes allowed the treatment of the variable account differently than the overall umbrella of the PERS system and charge the variable account against what was

termed as “negative interest.” If the decision is uncontested, it will result in a reconfiguration of affected members’ variable account amounts to reflect the amount that was taken to cover administrative expenses.

*Arken/Robinson v. PERS*: Both class action complaints were filed on behalf of Tier One members who retired between April 1, 2000 and April 1, 2004, alleging that the withholding members’ COLA from 2003 to 2006 constituted both a breach of their PERS contract and a violation of the state’s wage and hour laws in light of the *Strunk* decision. It also alleged that the PERS board’s intent to pursue collection actions against such retirees for alleged overpayment of 1999 earnings would also constitute a breach of their PERS contract.

*Robinson v. State of Oregon and PERS* challenged the board’s attempts to reduce retiree benefits to recover alleged overpayments resulting from PERS’ miscalculation of 1999 earnings to retirees’ regular accounts, arguing that the 2003 legislative reforms established that PERS is required to treat any overpayments as administrative expenses. In June 2007, the Multnomah County Circuit Court ruled in favor of both cases and ordered PERS to cease any collection activities against retirees. It further ordered PERS to immediately begin to pay back any money improperly collected from retirees as a result of the *Lipscomb* and the subsequent recalculation of 1999 PERS earnings. In October 2011, the Oregon Supreme Court ruled against the plaintiffs on both cases.

PERB has started [the process of recovering overpayments](#). All members or beneficiaries who received overpayments were first notified in January 2006, and will be receiving a first notice explaining the recovery process and second notice detailing the amount of the overpayment. The recovery process is anticipated to begin in summer 2012. Payment depends on whether the retiree or beneficiary receives benefits monthly, in a lump sum, or no ongoing monthly benefit.

*White v. PERB*: This is the last remaining court case in response to the *City of Eugene* litigation. The case challenges the legal authority of the

PERB from entering into a settlement of the court case without notification, involving, or engaging a key stakeholder in the litigation as it was decided in Marion County Circuit Court, as well as a number of PERS administrative actions taken as a result of the settlement. The Multnomah County Circuit Court ruled in favor of PERB on all issues; the Oregon Supreme Court determined that PERB’s actions were in line with its fiduciary duties, but transfer of earnings must be reviewed on demand to determine if it was consistent with those duties.

*Retiree Records*: In 2010, two Oregon newspapers requested, among other items, the names and benefit amounts for all PERS benefit recipients. Initially, the Attorney General’s Office advised PERS not to provide the newspapers with the requested information. However, after further review, the Attorney General decided the release of the requested information was in the public interest and this interest outweighed retirees’ privacy expectations. PERS sought court review of the Attorney General’s order; the court ordered PERS to disclose the names of every retiree receiving a PERS retirement benefit and the benefit amount, with the disclosure date set for November 21, 2011. The court also ordered PERS to disclose by March 2, 2012 the retirement plan and calculation method for determining the benefit for all retirees, as well as the member’s years of service and final salary, as well as the dollar amounts of benefits paid to survivor beneficiaries and alternative payees (i.e., former spouses). However, the names of these classes of recipients were not to be disclosed.

Legislation was drafted for the 2012 legislative session that would have expanded the public records disclosure exemptions to include employee and retirees’ names, but was not enacted.

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