2019-21 Budgeted PERS Contribution Rates for State Government

Oregon’s state government participates in the Public Employees Retirement System (PERS) to provide a retirement plan for employees. PERS is funded by a combination of employer and employee contributions. The purpose of this brief is to explain why the budgeted employer contribution rate for state government agencies will increase from the 2017-19 budgeted rate of 13.09% to 16.97%, or by an additional 3.88% (a change of +29.66%), of PERS-eligible payroll for the 2019-21 biennium’s budget development process.¹

Key Definitions

The PERS budgeted rate for state government agencies is synonymous with the Position Inventory Control System (PICS) budgeted rate used in the calculation of Other Payroll Expenses (OPE). The budgeted rate is sometimes referred to as the “blended” rate as the rate blends the costs of Tier 1/Tier 2 and Oregon Public Service Retirement Plan (OPSRP) together. An important distinction is that the PERS Board also publishes “advisory” rates for all employers. The difference between the state’s budgeted rate and advisory rates is that advisory rates are specific to Tier 1/Tier 2 and OPSRP benefit plans (i.e., unblended). For this budget brief, the focus will be on explaining the “budgeted” rate used in the PICS system for state government agency OPE budgeting.

State government is defined as only the statutorily-established state agencies in the Executive, Judicial, and Legislative branches of government or those agencies whose positions are budgeted in PICS. This is opposed to the PERS term “State Agencies,” which includes the agencies in state government plus some statutorily-authorized public corporations, semi-independent agencies, boards, and commissions, as well as Oregon’s public universities. Excluded from this definition are school districts, community colleges, and local governments.

PERS Budgeted Rate and the Budget Schedule for State Government

In the fall of odd-numbered years, the PERS actuary produces advisory employer contribution rates for all employers for the upcoming biennium. For state government, the PERS actuary also produces a budgeted rate in the spring of even-numbered years to budget the personal services costs of state government agencies for the following biennium. In the fall of even-numbered years, the PERS Board officially adopts final employer contribution rates for the upcoming biennium. Contribution rates are based on the most recently completed actuarial

¹ In absence of actuarially-provided budgeted rate information, and in order to attempt to explain the budgeted rate and the drivers of the rate increase, the Legislative Fiscal Office has estimated the impact by relying on information from advisory rates, blended rate(s), and the 2016 actuarial valuation.
valuation. For example, 2019-21 advisory rates are based on the calendar year 2016 valuation and 2019-21 adopted rates will be based on the calendar year 2017 actuarial valuation. The budgeted rate used by agencies in budget development may later be updated during the Governor’s budget or legislatively adopted budget cycles based upon the materiality of the change in the rates. Legislatively enacted PERS reform may also produce changes to the budgeted rate.

**Budgeted PERS Rate for State Government**

The PERS actuary provides state government with estimated budgeted employer contribution rates for use in budget development. The budgeted rate is a composite or blended rate based on the proportionate share of individual benefit program costs weighted by PERS-eligible payroll costs for each program. Benefit programs are the combined Tier 1/Tier 2 pension plans, the OPSRP, and two post-retirement health insurance plans: the Retirement Health Insurance Account (RHIA) and the Retiree Health Insurance Premium Account (RHIPA). Employees of most state government agencies are classified as General Service and all agencies with General Service employees use the same single blended rate provided by PERS. State government agencies with a material number of police and fire-eligible employees are provided a budget rate unique to that agency. It should be noted that while agencies budget based on budgeted rate, actual PERS charges to agencies are ultimately based on an adopted employer contribution rate specific to individual employees and their associated benefit program and which could understate, or overstate, an agency’s budgeted line-item for PERS contributions. Details of the budgeted rate are summarized in Appendix A.

**PERS-Eligible Payroll Costs for State Government**

PERS-covered or -eligible salary is defined by law generally as taxable salary and wages, which includes overtime and any stipends or differentials (e.g., shift times, second language, or training certification). PERS-covered payroll is estimated to increase from $4.5 billion for the 2017-19 biennium to a projected $4.6 billion for the 2019-21 biennium (a difference of $136.9 million, or 3.05%). The PERS-eligible payroll data in each valuation comes from actual calendar year amounts reported to PERS for each participating state agency by the Department of Administrative Services (DAS). This data is inflated by 3.5% per year to develop estimates for future payroll and is based on 2.5% for assumed inflation and 1% real wage growth. The 3.5% is also the payroll growth factor that is adopted by the PERS Board every two years as part of actuarial methods and assumptions and assumed by the PERS actuary. Two observations about payroll data are of note:

1) There continues to be a decline in Tier 1 and Tier 2 member payroll due largely to retirements with a corresponding increase in OPSRP payroll. This shift represents only a modest cost reduction as a portion of the OPSRP rate includes an Unfunded Accrued Liability (UAL) factor for not only OPSRP itself, but primarily Tier 1/Tier 2 legacy costs.

2) The assumed rate of payroll growth is based on system-wide and national experience, not the experience of individual PERS employers, and therefore does not account for the atypical increase in compensation (+6.95%) that occurred as part of the shift from an employer-paid to an employee-paid employee contribution to the Individual Account Program (discussed in more detail under the Employee Contribution/Individual Account Program section). In other words, the PERS-covered payroll estimate may be understated;
however, it will be factored into future payroll estimates and PERS charges will be based on actual payroll.

**Normal Cost for State Government**

Normal cost is the biennial contribution needed each year to fully fund the retirement benefits earned over a member’s working career. Normal costs are generally driven by the statutory benefit structure as well as assumed earnings rate decisions of the PERS Board. Normal costs decreased from 10.93% of payroll for the 2017-19 biennium to 10.02% for the 2019-21 biennium, or by 0.91% of payroll (-8.3%). This reduction is explained by the fact that as the proportion of employees in the less costly OPSRP pension plan grow, and the number of the costlier Tier 1/Tier 2 members decline, normal costs fall. In the future, the increase in compensation (+6.95%) that occurred as part of the shift from employer to employee-paid employee contribution to the IAP will drive a higher benefit for OPSRP members, thereby marginally increasing overall normal cost contributions for employers.

**Unfunded Liability for State Government**

The UAL is the excess of the actuarial accrued liability over the actuarial value of assets. The largest part of the UAL is the cost of benefits attributable to the now closed Tier 1 and Tier 2 benefit plans. There is also a UAL in the OPSRP pension and retiree healthcare programs. Liabilities were calculated based on the 2016 actuarial valuation, which has the system-wide UAL at $19.9 billion. The state government share of the system-wide UAL is $5.3 billion (26.6%), after accounting for $1.8 billion in pre-paid side account contributions (discussed in more detail under the Side Account Offset for State Government Agencies section).

The UAL is not a stagnant amount, but changes based on a number of factors. In general, changes in the UAL are driven by: (a) changes in the assumed earnings rate; (b) prior biennia rate deferrals (i.e., rate collaring); (c) actual investment earnings or changes to asset values; (d) changes to other actuarial methods and assumptions; and (e) prospective legislative changes to PERS benefits.

The Tier 1/Tier 2 UAL rate increased from 14.43% of payroll for the 2017-19 biennium to an estimated 16.13% for the 2019-21 biennium, or by an additional 1.7% of payroll (a change of +11.8%). The OPSRP UAL rate increase from 1.18% of payroll for the 2017-19 biennium to an estimated 1.31% for the 2019-21 biennium, or by an additional 0.13% of payroll (a change of +11.0%). These increases are explained by:

1) A decision by the PERS Board to lower the assumed [investment] earnings rate from 7.5% to 7.2% per annum beginning retroactively with the December 31, 2016 actuarial valuation. Of the $3.7 billion net increase in the system-wide UAL, $2.4 billion (or 66%) is attributable to the reduction in the assumed earnings rate. (The specific UAL impact to state government agencies was not determined.)

2) Another $1.1 billion in the UAL’s system-wide increase is attributable to previous rate collaring or the deferral of a portion of a prior biennium’s required employer contribution.
However, the final UAL rate is adjusted by rate collaring, which is the single most material change in the budgeted employer contribution rates (discussed in more detail under the Rate Collar section).

Additionally, although not technically part of the UAL rate calculation, the employer contribution rate for state agencies includes a component rate for the state’s experience prior to the formation of the State and Local Government Rate Pool (SLGRP). The SLGRP is a risk-sharing pool of state government and some local entities that reduces employer rate fluctuations due to an individual employer’s unexpected demographic changes (school districts are not part of the SLGRP, but instead participate in their own rate pool). The pre-SLGRP rate is attributable to a liability that existed prior to the formation of the SLGRP, when the state and community colleges were pooled by statute. The pre-SLGRP rate is expected to increase from 1.17% of payroll for the 2017-19 biennium to an estimated 1.73% for the 2019-21 biennium, or by an additional 0.56% of payroll (a change of +47.86%).

**Rate Collar for State and Local Government Rate Pool**

By PERS Board policy, and as calculated by the PERS independent actuarial firm, a rate collar limits the amount by which the SLGRP’s base rate can change from one biennium to the next based on the SLGRP’s funded status on the valuation date. For the 2019-21 biennium, as with the prior three biennia, the practical effect of the rate collar is to lower the Tier 1/Tier 2 UAL rate. The advisory rate for OPSRP remains uncollared, but the rate does include the collared Tier 1/Tier 2 UAL rate. The OPSRP rate is included as part of the budgeted rate.

Rate collaring for state government agencies is calculated at the SLGRP level rather than at the individual employer level. The rate collar is applied only to the base rate. The base rate includes the normal cost and UAL for the given pension program; it does not include employer-specific rate components such as side accounts or pre-SLGRP liabilities (discussed in more detail under the Side Account Offset for State Government Agencies section). The rate collar also does not include retiree healthcare rates or employee contributions, even if employer-paid.

The UAL for the SLGRP totaled $9.9 billion out of a system-wide total UAL of $19.9 billion (50%), including side accounts. The SLGRP’s pre-side account funded status used in budgeted rates fell from 72.1% in 2015 to 69.5% in 2016. The SLGRP’s funded status, with side accounts, is 75.4%; however, the rate collar is calculated using the SLGRP’s funded status prior to any side account offset. The OPSRP funded status is 64.1% with a UAL of $1.7 billion, which is included in the $19.9 billion system-wide UAL.

At a funded level of 70% or above, a single rate collar of the greater of 3% of payroll or 20% of the current base employer contribution rate is used. At a funded level of 60% or below, the rate collar doubles. At funded levels between 70% and 60%, the collar increases gradually from the single collar limit until it reaches the double collar limit. For the 2019-21 advisory rates, with the funded status of the SLGRP below 70%, a graduated double rate collar is in effect, resulting in a 5.58% reduction to employer contribution rates. For the 2017-19 biennium, a
single rate collar was in effect and reduced contribution rates by 8.35% based upon a SLGRP funded percentage of 72%.^2^3

The decline in funded status and the resulting graduated double rate collaring is primarily attributable to the decision by the PERS Board to lower the assumed earnings rate from 7.5% to 7.2% per annum and to previous rate collaring. This is also the single most significant factor driving the 2019-21 blended rate increase. The lowering of the assumed rate increased the UAL and reduced the funded status of the system and various pools within the system. The lowering of the funded status to just below 70% triggered graduated double rate collaring.

The other significant driver of the UAL and rate collaring is actual investment returns. The calendar year 2016 actual earnings were 7.1%, which was below the 2016 assumed earnings rate of 7.5% (retroactively changed to 7.2% with the 2016 actuarial valuation). Calendar year 2017 earnings of 15.12%, were also factored into the blended rate. In other words, assets were calculated based on the 2017 preliminary actuarial valuation, while, as noted, liabilities were calculated on the 2016 actuarial valuation.

The value of the rate collar, or the contribution amount deferred by the rate collar, for state government agencies for the 2019-21 biennium is estimated to be $346.6 million. Ultimately, the amount of required employer contributions deferred by the rate collar adds to the UAL at the carrying cost of the assumed earnings rate; however, this impact will not be reflected in employer contribution rates until the 2021-23 biennium and beyond.

Retiree Healthcare Rate for State Government

Another component of employer rates is for retiree health insurance benefit(s), which for state government employees includes the following benefits for Tier 1 and Tier 2 members:

- Retiree Health Insurance Premium Account – Provides an insurance premium subsidy for eligible pre-Medicare state agency retirees and beneficiaries.
- Retirement Health Insurance Account – Provides a $60 health insurance premium subsidy for eligible retired members who had eight or more years of qualifying service with any PERS employer and who are eligible and enrolled in the federal Medicare program.

It is estimated that the combined retiree health insurance benefit will decrease from 0.89% of payroll for the 2017-19 biennium to an estimated 0.86% for the 2019-21 biennium, or by 0.03% of payroll (a change of -3.1%). These rates include the retiree health insurance UAL. There is no significant change in the employer rates for retiree health insurance benefit(s) other than perhaps a reduction to the healthcare-related UAL.

Side Account Offset for State Government

Employers have the option to make voluntary lump-sum payments to PERS that are in addition to the employer’s required contribution. With few exceptions, such lump-sum payments are deposited into “side accounts,” and are used to offset a portion of the contributing employer’s future PERS contribution rate, according to an amortization schedule.

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2 An actuarial rate collar calculation unique to the budgeted rate was not made available. Therefore, this brief has had to rely upon the standard SLGRP rate collar calculation from the 2016 actuarial valuation.
State government has a side account comprised of the proceeds from a 2003 Pension Obligation Bond (POB) issuance plus annual investment earnings, minus the amount used each year for contribution rate relief. POBs are a debt financing mechanism that allow the state, school districts, and local governments to borrow funds long-term to offset all or a portion of a retirement system’s UAL. Of the state’s original $2 billion POB issuance, a balance of $1.8 billion remains. The employer rate contribution drivers for side accounts are the assumed earnings rate (used to project future earnings), new deposits, actual investment earnings or losses, the individual employer’s payroll, and the amortization schedule.

There was a marginal improvement in the state government side account offset, which is estimated to increase from a 7.16% offset during the 2017-19 biennium to a 7.50% offset for the 2019-21 biennium. This is due to actual earnings for calendar year 2017 exceeding the assumed rate ($10.1 billion, which is the single largest amount of earnings credited in PERS history for a 15.12% increase, exceeding the assumed rate of 7.2% by 8%). The value of the side account offset, or pre-payment, is estimated to be $491.4 million. The amortization schedule remained consistent with prior biennia.

**Police and Fire Contribution Rates for State Government**

PERS members who are classified as Police and Fire are eligible to retire at an earlier date and with a higher benefit calculation factor than General Service employees. Six state agencies with a significant amount of Police and Fire payroll have uniquely blended rates that reflect that payroll. While these blended rates are higher than the blended rate for other state agencies, the factors explaining the increase in rates are generally the same. The average projected 2019-21 blended Police and Fire rate across the six state agencies is 20.49%, a 3.96% of payroll rate increase (+23.94%) from the prior biennium. These rates compare to the General Service rate of 16.97%. Appendix B provides a summary of Police and Fire agencies and their individual blended rates.

**Statutory Judgeships**

There are 196 judgeships authorized in statute. These include 175 circuit court judges (upon increase from the current 173, in January 2019), 1 tax court judge, 13 Court of Appeals justices, and 7 Supreme Court justices. Statutory judgeships have their own retirement plan, which is as a non-pooled independent employer (i.e., not part of the SLGRP). The 2019-21 budgeted employer contribution rate for statutory judgeships will increase from a rate of 25.06% to 28.46%, or by an additional 3.41% of payroll (a change of +13.6%). The increase in the UAL is the primary driver of the rate increase.

**Employee Contribution/Individual Account Program**

A mandatory employee contribution is required by statute to fund the Individual Account Program (IAP), which is an account-based benefit in addition to a member’s pension benefit. The employee contribution, whether made by the member or employer on behalf of the member, is a uniform 6%. The only exception is for statutory judges, whose employee contributions go toward their pension benefits rather than into an IAP account and whose contribution rate is set at 7%. Employers collect and remit the employee’s contribution to PERS each pay period as a percentage of an employee’s PERS-covered salary. As noted previously, PERS-covered salary is defined by law generally as taxable salary and wages, which includes
overtime and any stipends or differentials (e.g., shift times, second language, or training certification).

For the 2019-21 biennium, state government will no longer budget the 6% employee contribution as an employer-paid expense; the employer “pickup” will be fully eliminated for state government by the end of the 2017-19 biennium. Employees will be responsible for paying the 6% employee contribution but will receive a comparable increase in compensation. The overall cost for the 2019-21 biennium is projected to increase to $277.3 million from $269.1 million for the 2017-19 biennium, or by $8.2 million (a change of +3.1%). This is another major change to the state government PERS rates for some agencies, which is the complete elimination of the employer “pickup.”

**Pension Obligation Bonds Debt Service for State Government**

The contribution rates calculated by the PERS actuary and used in the blended rate calculation exclude debt service on POBs. If an employer has issued POBs, an employer must also pay the PERS employer contribution rate in addition to debt service on the POBs. State POB principal and interest payments, or debt service, are assessed by DAS and budgeted as a percentage of PERS-eligible payroll expenses for each state government agency. Important to the understanding of POB debt service is that debt service is budgeted separate from the PERS employer contribution rate. For state agencies, the current percentage of payroll that is charged for the POB debt service for the 2017-19 biennium is 6%; the rate is expected to remain around this level for the 2019-21 biennium.

For the 2019-21 biennium, the debt service on POBs will cost state agencies, the university system, and other participating semi-independent agencies, public corporations, boards, and commissions $407.7 million, of which state government will pay $307.9 million (76% of the total). Additional POB issuances for state government are not anticipated.

**Net Budgeted Contribution Rate for State Government**

For development of the 2019-21 current service level, state government agencies can expect the blended employer contribution rate to increase from 13.09% to 16.97%, or by an additional 3.88% of payroll (a change of +29.66%). This collared rate excludes both the employee contribution and debt service on state-issued POBs. For the 2019-21 biennium, total estimated PERS employer contributions will increase from $636 million to $840 million, or by $204 million (a change of +32%). Of the total $839.6 million in costs, an estimated $409.1 million will be paid by the General Fund, $9.8 million by Lottery Funds, $298.7 million by Other Funds, and $122 million by Federal Funds. In addition, estimated PERS employer contributions for statutory judgeships will increase from $5.9 million to $6.7 million General Fund, or by $786,842 (a change of +13.3%). These estimates will be refined as the state’s budget system produces official estimates.

**Net Adopted Contribution Rate for State Government**

In the fall of 2018, the PERS Board will adopt and publish final employer contribution rates for the 2019-21 biennium, which will be based on the 2017 actuarial valuation. The overall funded status of PERS is expected to improve due to 2017 actual earnings (+15.12%). Since the state government budgeted rate already includes the impact of 2017’s actual earnings, there will likely be no major change to the budgeted rate. With that said, there may be some need for
state government employer contribution rates to be adjusted during the Governor's budget cycle due to three factors: (a) updated payroll costs; (b) updated retiree health insurance costs (i.e., Retirement Health Insurance Account); and (c) recalculation of the SLGRP rate collar based on actual earnings crediting for calendar year 2017 and an improved funded status, which may lead to the return of a single rate collaring due to the funding status moving above 70%. The amount of change, if any, by these or other factors could result in a change to the budgeted rate, but only if the change is material.

2021-23 Biennium Contribution Rates

State government should be prepared, and plan accordingly, for further employer rate increases in the 2021-23 biennium. The PERS actuary notes that “...if actual experience is near assumption we anticipate system-average collared rate increases similar to the increase calculated in this valuation [2016] not only for the 2019-2021 biennium, but also for the 2021-2023 biennium...” The key variables to watch will be actual investment earnings for calendar years 2018 and 2019, any possible administrative change by the PERS Board to the assumed earnings rate or other significant actuarial methods or assumptions, and any enacted benefit reform. State government agencies, per the direction of SB 1067 (2017), may want to consider pre-funding future employer contributions by establishing and funding an employer side account using cash proceeds.

Additional Resources

The Legislative Fiscal Office website (oregonlegislature.gov/lfo/Pages/Publications.aspx) contains several PERS-related resources such as budget information briefs explaining rate collaring, side accounts, employee contributions, and POBs, among others.
### Appendix A: State Government Budgeted Employer Rate Comparison

#### PERS Rate Summary - State Government Budgeted Contribution Rate

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<td>PERS-Eligible Wages - Estimated*</td>
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<td>$ 4,622,050,797</td>
<td>$ 136,850,068</td>
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**Budgeted Employer Contribution Rate(s)**

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<td>T1/T2 Pre-SLGRP Rate</td>
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*Figures exclude Oregon’s Public Universities.
**Figures may not foot due to rounding.

### Appendix B: Police and Fire State Government Agencies

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<td>OLCC</td>
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*Forestry and Oregon Youth Authority SEIU collective bargaining agreements beginning in the 2017-19 biennium reflect that the employer no longer budgeting for the 6% employee contribution as an employer-paid expense (“pickup”).