

## Oregon Public Employee Retirement System

### Documenting the City of Grants Pass' participation in PERS



## Overview of the City's Participation in Oregon PERS

### Background

Approximately 57% of the City's current operating expenditures are personnel costs. This is followed by contractual services at 22.4%. As Oregon PERS (Public Employees Retirement System) is a major component of overall personnel costs, it's important to explain the budgetary impact of changes to PERS rates. Like almost all public agencies in Oregon, the City's participation in the Oregon PERS is mandatory. PERS is largely a defined benefit retirement system, and the largest revenue source for the system by far is investment returns. When investment returns temporarily fall well below projected averages, such as happened in 2008, differences between assets in the system and the actuarial liabilities of the system need to be made up over time in part through higher employer contributions. It's important to make sure the system is properly funded and continues to provide investment returns.

Public employees that participated in the PERS system prior to system changes made in 2003 receive slightly different benefits than those that started after 2003. PERS charges the City different rates for the different classes of employees and different rates for sworn personnel versus general service personnel. The City uses its insurance/benefits fund to charge slightly different rates to departments as compared to the rates paid into the PERS system to limit the drastic budgetary impact of the State's PERS rates changing every two years. There is currently a PERS reserve in the insurance fund that will be used in the future to offset the impact of rates that are set to increase every two years until the State system is fully funded again.

### Budget Considerations & PERS Reserve

For the City of Grants Pass, the impact of every 3% increase to PERS rates equates to nearly \$400,000 per year in additional benefit costs for the City. Absent additional legislation to change the benefit structure of the system, PERS rates are expected to increase at least 3% every two years again starting in FY'16 until the State PERS system is fully funded. PERS rates billed out to departments have been slightly different than rates paid into the system, with the difference accounted for in the Benefits Administration fund and the PERS reserve established in that fund. A City PERS reserve has been created over many past budget years by a slight difference between department charges and actual payments into the PERS system. This reserve will be drawn down starting a few years from now when actual PERS rates are expected to be even higher than they will be in FY'15. As the City's participation in PERS is mandatory, this is one of the few ways to manage the effects of large changes to PERS rates every two years.

Due to legislative changes made at the state level in 2013-2014, the City will be able to hold internally billed PERS rates the same for at least the next four fiscal years by using the PERS reserve. The following are the projected PERS reserve balances assuming the next rate changes will be similar to recent rate changes:

<u>DATE</u>	<u>PERS RESERVE BALANCE PROJECTION:</u>
End of FY'14	\$2.3 million
End of FY'15	\$2.7 million
End of FY'16	\$2.8 million
End of FY'17	\$2.8 million
End of FY'18	\$2.5 million

The PERS reserve can be found in the Support Services section of the budget and more specifically the Benefits Administration Fund. The next rate change will occur at the beginning of FY'16, followed by another rate change at the beginning of FY'18. According to the current plan and current projected rate

changes, the City will be charging out about the same rates as paid during FY’16 and FY’17, and the PERS rates paid into the system will exceed current internally billed rates starting in FY’18. On this plan, the City will start significant drawdowns of the PERS reserve starting in FY’18. If rates are kept the same and financial markets don’t perform well even more severe drawdowns of the reserve could begin in FY’20. Short-term financial market fluctuations play a big role in the rate setting cycle every two years and internal and external rates will continue to be evaluated on at least an annual basis.

Current Rates & Expectations

Like other Oregon public agencies, the City of Grants Pass experienced an increase in rates paid to PERS effective July 1, 2011 and another large rate increase was originally set to occur July 1, 2013. However, during the 2013 session, the legislature made some changes to the cost side of the system and made some changes to the rate increase cycle that essentially deferred the next potential rate increase for two more years to July 1, 2015. The City of Grants Pass assesses PERS rates to departments slightly different than the rate actually paid into the system to manage the large rate changes that can occur every two years. The change made by the legislature in 2013 will allow the City’s internally billed PERS rates to stay the same between Fiscal 2014 and Fiscal 2018 without having a large effect on the PERS reserves that have been established over the last ten years. Therefore, while large potential increases in PERS rates are still pending in the future, the City’s PERS reserves will allow internally billed rates that are accounted for in the operating budgets to stay the same for the next four years.

Total costs billed to departments and costs by major operating divisions are presented below and on the following pages. The total cost for PERS by the major categories is provided below to provide insight into the changes over time. Remember that “Budget” will appear to jump in comparison to “Actual” given that the City frequently has unfilled positions at different times throughout the year that result in temporary expenditure savings. PERS rates are assessed as a percentage of current gross salaries.

	<b>FY’12 Actual</b>	<b>FY’13 Actual</b>	<b>FY’14 Budget</b>	<b>FY’15 Recommend</b>	<b>FY’16 Projected</b>
PERS/OPSRP-Employee 6%	779,676	778,912	855,996	843,670	871,896
PERS/OPSRP-Employer	2,197,445	2,354,460	2,807,638	2,618,591	2,700,064

<b>Total PERS Expenditures by Program Area</b>					
	<b>FY’12 Actual</b>	<b>FY’13 Actual</b>	<b>FY’14 Budget</b>	<b>FY’15 Adopted</b>	<b>FY’16 Projected</b>
Policy & Legislation	5,239	19,641	0	0	0
Public Safety	1,931,478	2,038,679	2,281,406	2,215,435	2,274,109
Parks	68,241	65,306	72,881	75,066	76,670
Development	113,249	120,335	141,757	124,180	131,405
Transportation	64,369	63,294	83,329	85,577	87,977
Water	147,239	153,867	180,424	180,822	191,884
Wastewater	166,177	165,907	203,474	170,245	175,954
Solid Waste	1,329	1,473	1,556	2,577	2,708
Administrative Services	233,563	252,484	277,972	290,798	300,551
Support Services	246,207	252,386	420,835	317,561	330,702
Lands & Building	30	0	0	0	0
<b>TOTAL</b>	<b>2,977,121</b>	<b>3,133,372</b>	<b>3,663,634</b>	<b>3,462,261</b>	<b>3,571,960</b>

Department	FY'12 ACTUAL	FY'13 ACTUAL	FY'14 REVISED	FY'15 RECOMMEND	FY'16 PROJECTED
<b>01-Policy &amp; Legislation</b>					
GENERAL OPERATIONS	5,239	19,641	0	0	0
	5,239	19,641	0	0	0
<b>02-Public Safety</b>					
PS-FIRE RESCUE DIVISION	0	0	697,610	704,797	723,397
PS-POLICE DIVISION	1,527,231	1,602,961	1,230,077	1,175,543	1,204,295
PS-SUPPORT DIVISION	404,247	435,718	353,719	335,095	346,417
	1,931,478	2,038,679	2,281,406	2,215,435	2,274,109
<b>03-Parks</b>					
AQUATIC SERVICES	2,623	3,330	3,885	4,140	4,226
PARKS MAINTENANCE SERVICE	64,080	60,694	66,636	68,388	69,808
RECREATION SERVICES	1,538	1,282	2,360	2,538	2,636
	68,241	65,306	72,881	75,066	76,670
<b>04-Development</b>					
BUILDING AND SAFETY	27,651	29,086	34,009	34,476	35,745
DOWNTOWN DEVELOPMENT	15,635	15,174	16,832	17,065	17,667
ECONOMIC DEVELOPMENT	12,685	13,421	14,207	12,336	13,491
PLANNING	41,042	45,195	58,053	58,902	63,064
TOURISM PROMOTION SERVICE	16,236	17,459	18,656	1,401	1,438
	113,249	120,335	141,757	124,180	131,405
<b>05-Transportation</b>					
STREET & DRAINAGE MAINT	61,224	59,831	79,087	81,305	83,578
TRANSPORTATION PROJECTS	3,145	2,769	4,242	4,272	4,399
	64,369	62,600	83,329	85,577	87,977
<b>06-Storm Water and Open Space</b>					
STORM DRAIN SDCs	0	694	0	0	0
	0	694	0	0	0
<b>07-Water</b>					
WATER DISTRIBUTION	72,420	72,728	92,714	92,902	98,577
WATER PROJECTS	3,878	5,184	4,116	4,146	4,269
WATER TREATMENT	70,941	75,955	83,594	83,774	89,038
	147,239	153,867	180,424	180,822	191,884

Department	FY'12 ACTUAL	FY'13 ACTUAL	FY'14 REVISED	FY'15 RECOMMEND	FY'16 PROJECTED
<b>08-Wastewater</b>					
JO GRO	33,474	31,006	39,752	0	0
WASTEWATER COLLECTION	48,637	52,634	59,890	61,892	64,451
WASTEWATER PROJECTS	2,576	2,464	4,116	4,146	4,269
WASTEWATER TREATMENT	81,490	79,803	99,716	104,207	107,234
	166,177	165,907	203,474	170,245	175,954
<b>09-Solid Waste</b>					
SOLID WASTE CONSTRUCTION	164	89	0	0	0
SOLID WASTE OPERATIONS	1,165	1,384	1,556	2,577	2,708
	1,329	1,473	1,556	2,577	2,708
<b>10-Administrative Services</b>					
FINANCE	116,736	130,393	159,243	159,931	167,198
HUMAN RESOURCES	35,669	40,847	46,487	49,443	49,076
LEGAL SERVICES	2,709	411	444	3,591	3,867
MANAGEMENT SERVICES	78,449	80,833	71,798	77,833	80,410
	233,563	252,484	277,972	290,798	300,551
<b>11-Support Services</b>					
BENEFITS ADMINISTRATION	0	0	120,000	0	0
ENGINEERING	54,909	46,938	46,240	47,517	49,056
EQUIPMENT REPLACEMENT	5,819	7,284	9,050	9,105	8,919
GARAGE OPERATIONS	29,905	31,639	36,336	35,265	36,454
GENERAL INSURANCE	376	2,496	2,487	2,706	2,967
INFORMATION TECHNOLOGY	46,486	43,082	65,958	74,152	77,739
PARKS & CD MGMT SERVICES	84,118	94,684	111,682	114,435	119,600
PROPERTY MANAGEMENT	21,753	22,654	24,280	27,753	28,970
WORKERS COMP INSURANCE	2,841	3,609	4,802	6,628	6,997
	246,207	252,386	420,835	317,561	330,702
<b>13-Lands &amp; Buildings</b>					
LANDS AND BLDGS PROJECTS	30	0	0	0	0
	30	0	0	0	0
	2,977,121	3,133,372	3,663,634	3,462,261	3,571,960

### The 6% "Pick-Up"

PERS currently requires a payment of 6% of a public employee's gross wages into the system, paid either by the employee or by the employer. Most public employers, such as the City of Grants Pass, have elected to pay the 6% on behalf of the employee as part of the overall compensation package. This allows payroll taxes to be minimized (all things being equal in terms of the total compensation package). The costs shown above include both the main PERS rate and the 6% portion.

### Rate Drivers & PERS Reserve Impact

PERS rate changes are largely and directly correlated to the broad performance of financial markets, and rate changes tend to lag the actual performance of financial markets by at least two years. The FY'10 and FY'11 rates billed by PERS were reduced because of financial market performance that was healthy prior to 2008. However, knowing that 2008 was one of the worst financial market performances in many years, the City billed all departments at the same PERS rates as the previous two-year cycle and set aside additional reserves in the Benefits Administration program. Reserves have been set aside for many years by charging slightly different rates to operating departments as compared to the PERS system payment requirements, and at the peak of the PERS rate setting cycle these reserves will be used to lessen the impact of higher rates. Due to the PERS law change made by the State Legislature in last year's session, rates starting July 1<sup>st</sup>, 2013 have been similar to rates paid in the last two years and the City's PERS reserve will allow the City to hold internally billed rates at the same level for a number of years after FY'14.

The State PERS Board made a policy decision to spread unfunded liabilities, largely the result of retirement benefits for Tier 1/Tier 2 employees, to all groups. As the current employee membership in Tier 1/Tier 2 has declined due to retirements, the financial impact of liabilities and financial market losses in 2008 produced staggering rate projections for these remaining Tier 1/2 employees. Government agencies have found these impacts more manageable by allocating a portion of the liabilities across all groups of employees, and so under the State's rate setting rules the liabilities are spread across all categories of PERS employees. It is also noteworthy that the State has addressed the issue of Tier1/Tier2 benefits in that since 2003 new public employees do not have the same defined benefits. However, the system remains to be partially a defined benefit plan that sets retirement benefits based on time of service rather than by how much is earned in an employee's individual retirement account and how well investments perform. This type of retirement plan is challenging to manage when retirement portfolio returns come in well under average long-term expectations, as was the case in 2008.

Due to the historic losses in financial markets in 2008 and limited recovery of those losses in recent years, it is currently expected that at least 3% increases will be implemented by the state PERS program every two years starting again on July 1, 2015 until the losses are recovered and the retirement assets equal the actuarial liabilities. Over the next year, the City will bill all departments at rates slightly higher than what is paid into the system. The PERS reserve will grow slightly and be used to offset future rate increases. The financial plan at this time is to stop growing the reserve after FY'15 and use the reserve to help offset future increases.

Actuarial liabilities compared to growth in assets for the State operated PERS system will have to be monitored to predict the impact of future rate setting cycles. Ultimately the move to create PERS reserves will lessen the future impact of PERS rate hikes towards the end of the rate increase cycle and will help

smooth the potential volatility of City personnel and related benefit costs. While the City cannot control these rates and must follow the rules of the State’s system, the City has taken steps to prepare for future PERS cost increases.

Starting July 1, 2013, the rates paid in without the previously mentioned law changes would have increased by between 3.66% and 4.38% for the various classes of City of Grants Pass PERS employees (those rates are as a percentage of gross payroll, not the amount of change in the PERS rate itself). If the City was fully staffed for all funded positions in the adopted FY’14 budget, this increase would have amounted to increased costs of more than \$500,000 per year starting with the Fiscal 2014 budget year. In contrast, the City’s PERS reserve will only approach approximately \$2.7 million at the end of FY’15, and those reserves can only be used once before they would need to be built up again. This speaks to the continued need to build the reserve to prepare for future rate increases that are nearly certain unless other law changes are made. City Staff will continue to plan for additional rate increases in the future and discuss with Council the limited options we have at the local level on dealing with PERS rate changes every two years. Changes made to PERS by the legislature in the last year have also been appealed to the Oregon Supreme Court.

Absent above average investment returns, the City of Grants Pass and almost all other public agencies in Oregon currently have an actuarial unfunded liability related to participation in PERS. Each year, PERS engages an actuary to determine the proper measure of actuarial assets, actuarial liabilities, the system’s funded status, and each employer’s share of assets and liabilities. Below is one of the disclosures from the City of Grants Pass PERS annual report as of the end of calendar 2012 (Grants Pass’ share of the system only):

*Schedule of Funding Progress*

The Schedule of Funding Progress is required for the Tier 1/Tier 2 pension liabilities. The table below shows the schedule for the last several valuations. For employers with side accounts, the actuarial value of assets in this Schedule includes the value of the employer’s side accounts.

Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) (b)	Unfunded AAL (b - a)	Funded Ratio (a ÷ b)	Covered Payroll (c)	UAAL as a Percentage of Covered Payroll ((b-a) ÷ c)
12/31/2007	\$52,711,473	\$54,238,486	\$1,527,013	97%	\$11,433,157	13%
12/31/2008	39,663,782	56,472,774	16,808,992	70%	12,515,625	134%
12/31/2009	45,516,785	58,455,182	12,938,397	78%	11,981,543	108%
12/31/2010	49,311,239	61,438,085	12,126,846	80%	12,714,676	95%
12/31/2011	48,845,349	63,743,090	14,897,741	77%	13,468,530	111%
12/31/2012	54,287,992	65,439,529	11,151,537	83%	13,265,839	84%

Unfunded liabilities were reduced significantly during calendar 2013 due to both State law changes related to PERS and investment returns on the PERS portfolio that were significantly higher than the assumed return rate during 2013. The City’s share of the unfunded liabilities related to its participation in PERS will be significantly reduced in the next annual report. And again, the PERS investment performance will be the

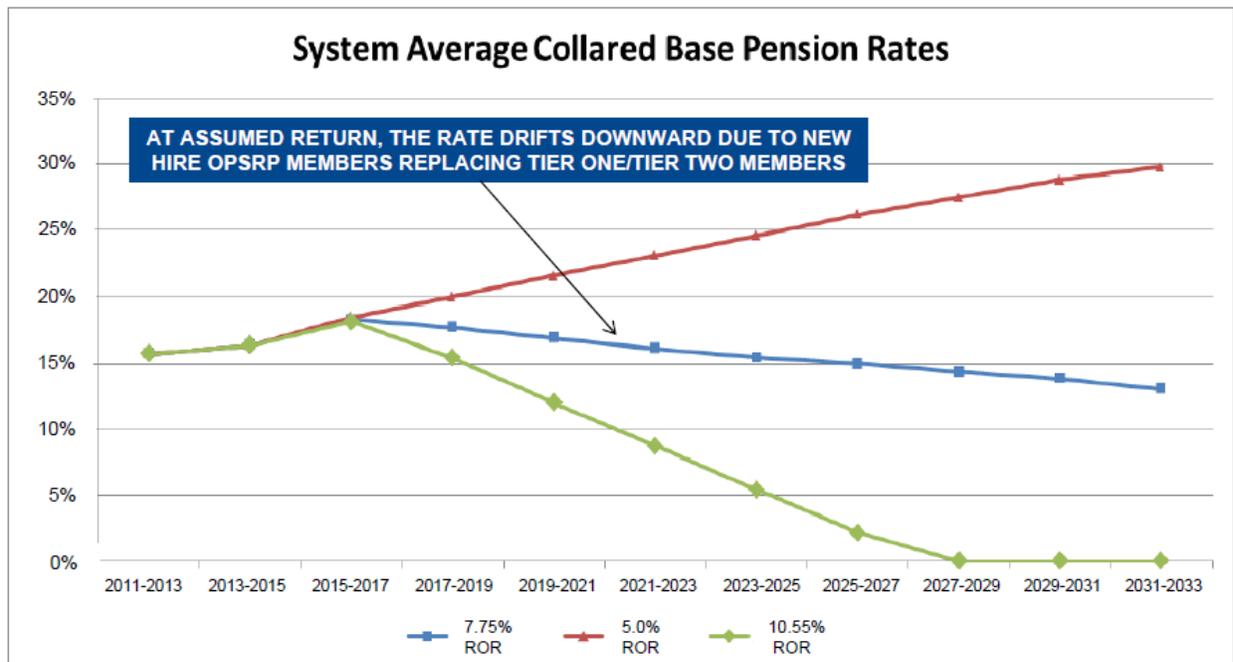
largest driver of future accrued liability reports and future PERS rate changes. The annual PERS report for each calendar year is typically available in the fall of the following year.

**Information directly from Oregon PERS**

The following charts and data points about Oregon PERS were copied from a presentation provided to the League of Oregon Cities on March 20, 2014. The first chart below highlights the importance of portfolio returns to the rate setting cycle for public agencies in Oregon.

## Steady Return Model Projections

Impact of consistently achieving the 7.75% assumed rate of return (ROR) compared to plus or minus 2.75% of that rate; includes effects of Senate Bills 822 and 861 and investment results through October 31, 2013



## PERS Membership, Retirements, and Benefits

- 167,000 active members; OPSRP (new program in 2003) now has the largest pool of active members (46%)
- 122,000 retirees/beneficiaries receiving monthly benefits
- 1 in 12 Oregonians is receiving or will receive a PERS benefit
- Average 6,000 retirements per year (peaked at 12,500 in 2003); about 9,500 retired in 2013; about 67,000 members are eligible to retire
- Average age at retirement for 2012 retirees: 61
- Average years of service at retirement for 2012 retirees: 22
- Average annual benefit for all current retirees: \$28,272
- Average annual benefit for 2012 retirees: \$29,235 (46% replacement rate of final salary)
- Average annual benefit for 2012 retirees with 30 years service: \$46,764 (70% replacement rate of final salary; still mostly Money Match)

## Benefit Component Comparisons

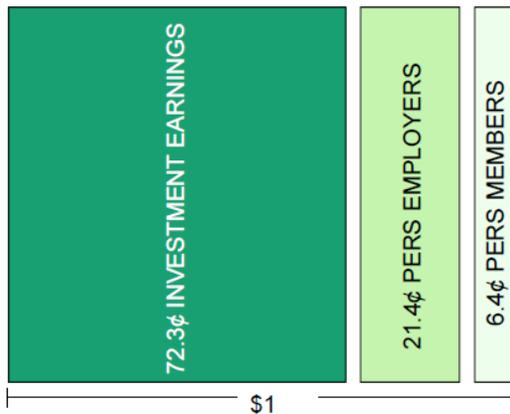
- Tier One: hired before January 1, 1996
- Tier Two: hired January 1, 1996 through August 28, 2003
- OPSRP: hired after August 28, 2003

	Tier One	Tier Two	OPSRP Pension	IAP
Normal retirement age	58 (or 30 yrs); P&F = age 55 or 50 w/ 25 yrs	60 (or 30 yrs) P&F = age 55 or 50 w/ 25 yrs	65 (58 w/ 30 yrs); P&F = age 60 or 53 w/ 25 yrs	Members retire from IAP when they retire from Tier One, Tier Two, or OPSRP
Early retirement	55 (50 for P&F)	55 (50 for P&F)	55, if vested	Members retire from IAP when they retire from Tier One, Tier Two, or OPSRP
Regular account earnings	Guaranteed assumed rate credited annually	No guarantee; market returns	Not applicable; no member account	No guarantee; market returns
Retirement calculation methods	<ul style="list-style-type: none"> <li>• Money Match</li> <li>• Full Formula</li> <li>• Formula + Annuity (hired before 8/21/1981)</li> </ul>	<ul style="list-style-type: none"> <li>• Money Match</li> <li>• Full Formula</li> </ul>	• Full Formula	Not applicable

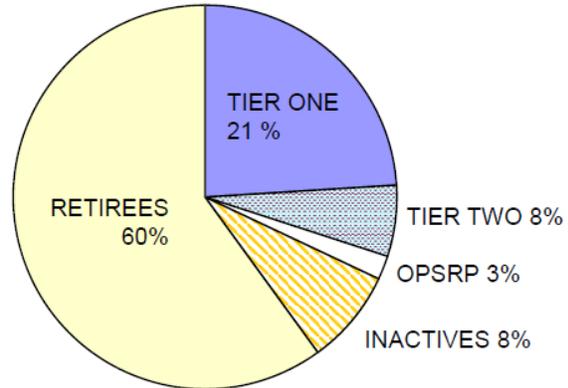
## Benefit Funding and Accrued Liabilities

### FUNDING SOURCES (1970-2012)

Money for benefit payments comes from three sources



### ACCRUED LIABILITIES



## 2007-2013 Funded Status and UAL

	Calendar Year (as of December 31)						
	2007	2008	2009	2010	2011	2012*	2013**
<b>Funded Status (%)</b>							
Including side accounts	112%	80%	86%	87%	82%	91%	96%
Excluding side accounts	98%	71%	76%	78%	73%	82%	87%
<b>Unfunded Actuarial Liability (UAL) (\$ billion)</b>							
Including side accounts	\$ -6.1***	\$11.0	\$8.1	\$7.7	\$11.0	\$5.6	\$2.2
Excluding side accounts	\$1.5	\$16.1	\$13.6	\$13.3	\$16.3	\$11.1	\$8.1

\* Includes liability reductions from Senate Bills 822 & 861 and Board-adopted changes to actuarial methods and assumptions.

\*\* 2013 is estimated.

\*\*\* This is a funding surplus. Side accounts are pre-payments made by employers.

## Employer Contribution Costs

- New contributions from PERS employers were approximately \$2 billion in the 2011-13 biennium; up from about \$1 billion in the 2009-11 biennium
  - Employer costs were projected to increase by about \$900 million in the 2013-15 biennium
    - \$224 million from state agencies,
    - \$330 million from K-12, and
    - \$352 million from local government and other entities
  - 2013 legislation (Senate Bill 822 as modified by Senate Bill 861) reduced PERS' unfunded actuarial liability by \$5 billion and reduced the 2013-15 biennium employer cost increase to about \$100 million
- 

Further information about Oregon PERS can be found on the State's website at the following address:

<http://www.oregon.gov/pers/Pages/index.aspx>

