

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 55% of the City's current operating expenditures are personnel costs. This is followed by contractual services at about 25%. 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 most state and local 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 to keep up with the retirement system's contractual and legal obligations.

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 approximately \$400,000 per year in additional benefit costs for the City. Absent additional legislation to change the benefit structure or rate setting process of the system, PERS rates are expected to increase at least 3% every two years again starting on July 1, 2017 until rates approach a total of close to 30% of gross payroll costs (according to PERS rate advisory and other presentations). Rates the City pays also increased modestly starting in FY'16 but internal billed rates are scheduled to remain the same until at least the end of FY'18 in combination with the use of the established PERS reserve.

PERS rates billed out to City departments have been slightly different than rates paid into the system, with the difference accounted for in the Benefits Administration fund (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. It is estimated that this reserve will be drawn down starting in FY'18 when actual PERS rates are adjusted for the next two-year rate cycle. And unless internally billed PERS rates change over the years, the drawdowns are expected to be much more severe and PERS reserves will begin significant declines when PERS rates change again in FY'20. 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 through at least FY'19 by using the PERS reserve. FY'20 would be the year where drawdowns would become much more severe without changes to internally billed rates. The following are the actual and projected PERS reserve balances assuming the next rate changes are close to expectations:

<u>DATE</u>	<u>PERS RESERVE BALANCE PROJECTION:</u>
End of FY'15 (actual)	\$2.8 million
End of FY'16	\$3.2 million
End of FY'17	\$3.6 million
End of FY'18	\$3.5 million
End of FY'19	\$3.4 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'18, followed by another rate change at the beginning of FY'20. Because the FY'16 rate increase came in slightly less than previous expectations, FY'16 and FY'17 years will continue to build on the reserve. The plan at this point is the City would begin drawing on the reserve starting in FY'18 and it's possible the City could extend well past FY'18 without having to adjust internally billed PERS rates. If rates are kept the same and financial markets don't perform well even more severe drawdowns of the reserve would likely 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 that 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 at least 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 at least the next three years.

There were some legal challenges pending in early 2015 for the PERS changes made by the state legislature in 2013-2014. In the end, a large portion of the cost savings measures implemented by the legislature were overturned by the Supreme Court, meaning the increases in PERS rates in the next two rate setting cycles will be even higher than they would have been otherwise (and actuarial PERS liabilities will be higher). In addition, December 31, 2015 was the measurement date for the next PERS rate cycle and the PERS portfolio returned far less than assumed returns in 2015. This means the PERS unfunded liability amounts are greater than the previous year and there will be a large rate increase on July 1, 2017.

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.

	FY'14 Actual	FY'15 Actual	FY'16 Budget	FY'17 Budget	FY'18 Projected
PERS/OPSRP-Employee 6%	771,419	772,893	878,405	903,780	929,691
PERS/OPSRP-Employer	2,452,920	2,445,407	2,691,863	2,750,271	2,830,164

Total PERS Expenditures by Program Area					
	FY'14 Actual	FY'15 Actual	FY'16 Budget	FY'17 Budget	FY'18 Projected
Public Safety	2,131,211	2,108,694	2,312,946	2,361,613	2,441,964
Parks	71,044	68,748	77,992	79,483	81,416
Development	108,461	100,093	125,480	121,550	123,473
Transportation	65,703	73,766	80,062	88,072	91,877
Storm Water/Open Space	728	607	0	0	0
Water	153,603	159,193	188,639	187,949	191,191
Wastewater	159,812	154,818	172,673	180,721	181,177
Solid Waste	1,614	2,607	2,598	2,562	2,629
Administrative Services	260,073	262,575	285,783	290,553	297,449
Support Services	272,086	285,988	323,818	341,548	348,679
Lands & Building	4	1,211	0	0	0
TOTAL	3,224,339	3,218,300	3,569,991	3,654,051	3,759,855

Department	FY14 Actual	FY15 Actual	FY16 Adopted	FY16 Revised	FY17 Recommend	FY18 Projected
Public Safety						
PS-FIRE RESCUE DIVISION	703,418	724,663	728,976	728,976	720,542	738,436
PS-POLICE DIVISION	1,099,448	1,089,621	1,205,640	1,205,640	1,259,949	1,308,303
PS-SUPPORT DIVISION	328,345	294,409	378,330	378,330	381,122	395,225
	<u>2,131,211</u>	<u>2,108,694</u>	<u>2,312,946</u>	<u>2,312,946</u>	<u>2,361,613</u>	<u>2,441,964</u>
Parks						
PARKS MAINTENANCE SERVICE	65,409	63,020	71,159	71,159	73,098	74,942
RECREATION SERVICES	2,050	2,456	2,548	2,548	2,633	2,633
AQUATIC SERVICES	3,585	3,272	4,285	4,285	3,752	3,841
	<u>71,044</u>	<u>68,748</u>	<u>77,992</u>	<u>77,992</u>	<u>79,483</u>	<u>81,416</u>
Development						
BUILDING AND SAFETY	30,701	30,822	33,928	33,928	35,025	35,108
PLANNING	40,735	49,249	58,283	58,283	53,092	53,742
ECONOMIC DEVELOPMENT	480	3,180	12,084	12,084	11,590	12,007
TOURISM PROMOTION SERVICE	18,675	1,016	1,075	1,075	992	1,008
DOWNTOWN DEVELOPMENT	17,870	15,826	20,110	20,110	20,851	21,608
	<u>108,461</u>	<u>100,093</u>	<u>125,480</u>	<u>125,480</u>	<u>121,550</u>	<u>123,473</u>
Transportation						
STREET & DRAINAGE MAINT	61,821	69,935	75,762	75,762	83,790	87,570
TRANSPORTATION PROJECTS	3,881	3,831	4,300	4,300	4,282	4,307
	<u>65,703</u>	<u>73,766</u>	<u>80,062</u>	<u>80,062</u>	<u>88,072</u>	<u>91,877</u>
Storm Water & Open Space						
STORM DRAIN SDCs	<u>728</u>	<u>607</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>
Water						
WATER TREATMENT	75,673	82,705	90,387	90,387	85,188	87,192
WATER DISTRIBUTION	72,441	72,938	94,078	94,078	98,605	99,817
WATER PROJECTS	5,489	3,550	4,174	4,174	4,156	4,182
	<u>153,603</u>	<u>159,193</u>	<u>188,639</u>	<u>188,639</u>	<u>187,949</u>	<u>191,191</u>
Wastewater						
WASTEWATER COLLECTION	58,590	60,892	64,928	64,928	69,282	68,999
WASTEWATER TREATMENT	84,645	89,961	103,571	103,571	107,283	107,996
JO GRO	14,218	0	0	0	0	0
WASTEWATER PROJECTS	2,360	3,965	4,174	4,174	4,156	4,182
	<u>159,812</u>	<u>154,818</u>	<u>172,673</u>	<u>172,673</u>	<u>180,721</u>	<u>181,177</u>
Solid Waste						
SOLID WASTE OPERATIONS	1,472	2,196	2,598	2,598	2,562	2,629
SOLID WASTE CONSTRUCTION	142	412	0	0	0	0
	<u>1,614</u>	<u>2,607</u>	<u>2,598</u>	<u>2,598</u>	<u>2,562</u>	<u>2,629</u>
Administrative Services						
HUMAN RESOURCES	46,558	41,219	42,044	42,044	38,955	40,918
MANAGEMENT SERVICES	75,242	73,693	78,147	78,147	79,954	80,891
LEGAL SERVICES	327	381	3,627	3,627	3,957	3,995
FINANCE	137,947	147,282	161,965	161,965	167,687	171,645
	<u>260,073</u>	<u>262,575</u>	<u>285,783</u>	<u>285,783</u>	<u>290,553</u>	<u>297,449</u>
Support Services						
GARAGE OPERATIONS	28,638	31,603	42,228	42,228	44,158	45,000
EQUIPMENT REPLACEMENT	7,696	7,252	0	0	0	0
INFORMATION TECHNOLOGY	60,487	71,961	77,371	77,371	80,597	82,432
PROPERTY MANAGEMENT	22,943	22,901	24,268	24,268	24,924	25,232
ENGINEERING	44,704	45,096	72,243	72,243	79,325	80,234
PARKS & CD MGMT SERVICES	100,222	99,368	98,025	98,025	101,026	103,776
WORKERS COMP INSURANCE	4,824	5,073	6,947	6,947	7,586	7,921
GENERAL INSURANCE	2,572	2,733	2,736	2,736	3,932	4,084
	<u>272,086</u>	<u>285,988</u>	<u>323,818</u>	<u>323,818</u>	<u>341,548</u>	<u>348,679</u>
Lands & Buildings						
LANDS AND BLDGS PROJECTS	<u>4</u>	<u>1,211</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>
	3,224,339	3,218,300	3,569,991	3,569,991	3,654,051	3,759,855

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.

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, 2017 and for the next couple rate cycles unless the losses are recovered in that time. Investments must return well over the assumed returns of slightly less than 8% in order for the unfunded liability to decrease in a given year. Over the 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'17 and use the reserve to help offset future increases starting in FY'18.

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.

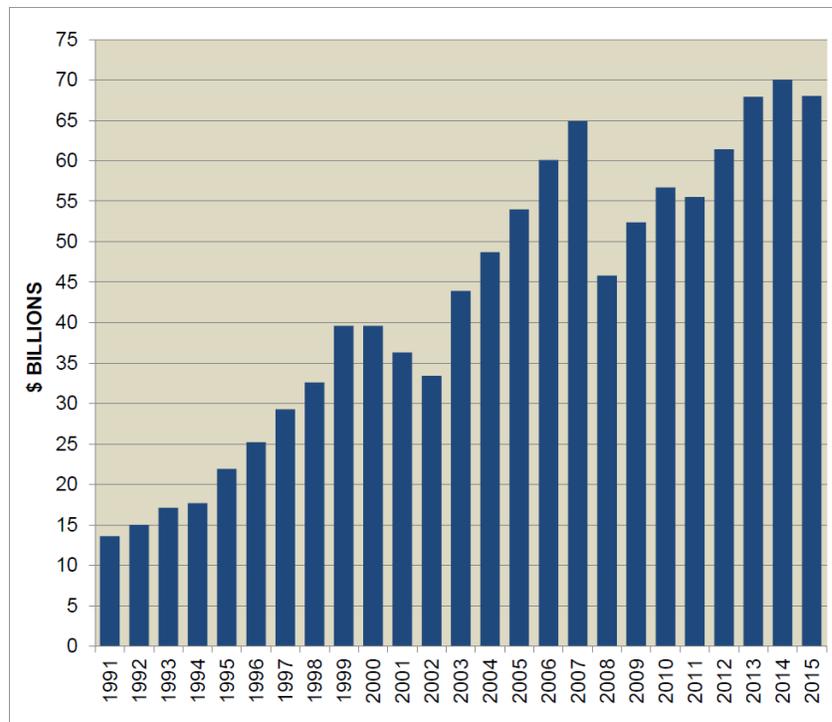
The rate increases that the City experienced starting July 1, 2015, were less than previous expectations. This is due in part to the City now being part of the State & Local Government Rate Pool for its Tier 1 and Tier 2 liabilities for the first time. Grants Pass is no longer an independent employer for the calculated liabilities for the PERS Tiers previous to OPSRP (2003), and the difference between the funded status of Grants Pass and the pool at the point where Grants Pass joined the rate pool recently, is set to be amortized over many years into the future. PERS rate changes every two years might be slightly less volatile in the future due to this change that was made in the last cycle.

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 some information directly from PERS for a better understanding of this retirement system.

Information directly from Oregon PERS

The following charts and data points about Oregon PERS were copied from a presentation created by PERS dated April 1, 2015, titled “PERS by the Numbers.” The charts that follow highlight the importance of portfolio returns to the rate setting cycle for public agencies in Oregon.

PERS fund value (calendar years ending December 31)



3. System Funding Level and Status (continued)

Unfunded actuarial liability history and funded ratio*

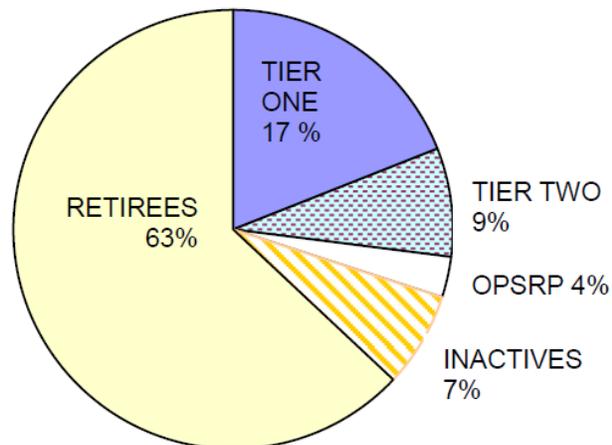
Valuation** Date	With Side Accounts*** (starting in 2002)		Without Side Accounts	
	UAL (\$M)	Funded Ratio (%)	UAL (\$M)	Funded Ratio (%)
2000	1,545	96.4	1,545	96.4
2001	-2,031	105.4	-2,031	105.4
2002	3,204	92.0	3,983	89.9
2003	1,751	96.1	6,227	86.0
2004	2,122	95.6	7,678	84.0
2005	-1,751	104.0	4,919	91.0
2006	-5,019	109.7	2,229	95.7
2007	-6,120	111.5	1,538	97.1
2008	10,998	80.0	16,133	70.4
2009	8,108	86.0	13,598	76.0
2010****	7,700	87.0	13,300	78.0
2011	11,030	82.0	16,255	73.0
2012*****	5,600	91.0	11,100	82.0
2013	2,600	96.0	8,500	86.0
2014*****	12,100	84.0	18,000	76.0
2015 (estimated)	-----	-----	21-22	71.0-72.0

- * Includes RHIA/RHIPA.
- ** 2000-2003 UALs were calculated using actuarial value of assets (AVA) based on year-to-year changes in asset values smoothed over four-year periods. All other UALs since 1997 were calculated using an AVA based on fair market value.
- *** The official PERS valuation UAL and funded ratio are based on accepted actuarial standards and methodologies. These methodologies are subject to review and revision every two years. A negative UAL amount represents a surplus.
- **** 2010 and after includes the OPSRP Pension Program, 2000-2009 reflects only Tier One/Tier Two.
- ***** Includes liability reductions from Senate Bills 822 & 861 and new Board-adopted actuarial assumptions and methods from the 2012 Experience Study.
- ***** Includes the *Moro* decision and new Board-adopted actuarial assumptions and methods from the 2014 Experience Study.

Actuarial accrued liabilities

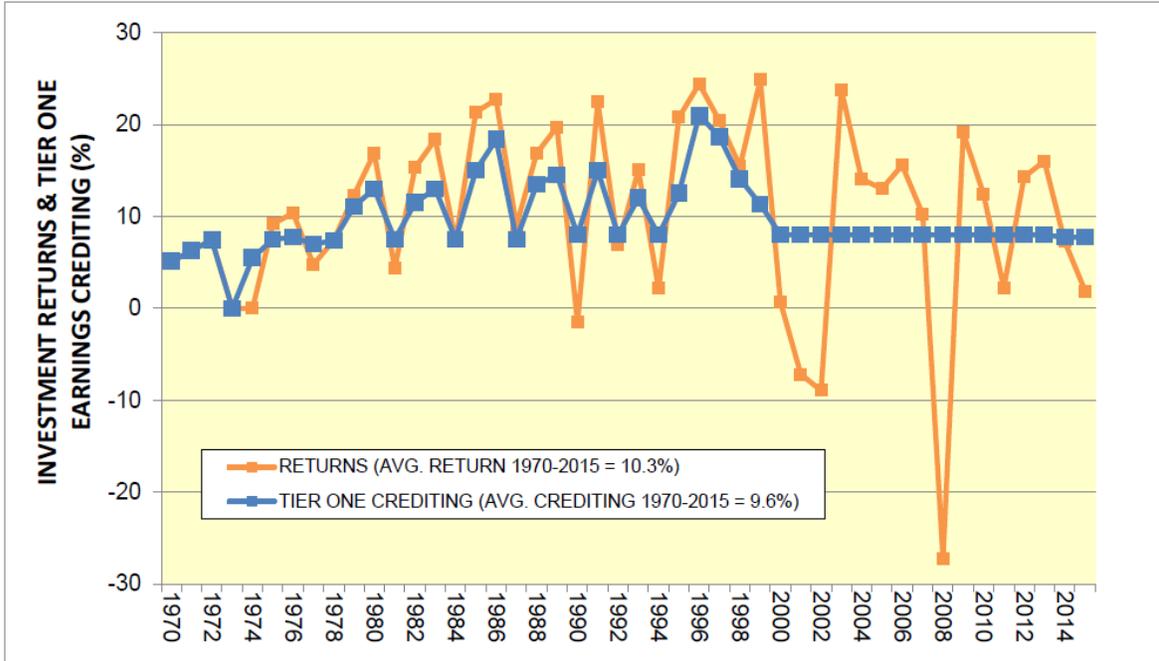
Before PERS reform in 2003, PERS’ liabilities were growing by about 12% annually. Reform reduced liability growth to an expected average of 3 to 4% annually over the long-term, which is close to the system’s annual inflation rate assumption of 2.5% (for the December 31, 2014 and December 31, 2015 valuations).

Approximately 70% of PERS’ total accrued liability is for members who are no longer working in PERS-covered employment (retirees and inactives). As a result, more than 40% of an employer’s total contribution rate is associated with these groups.



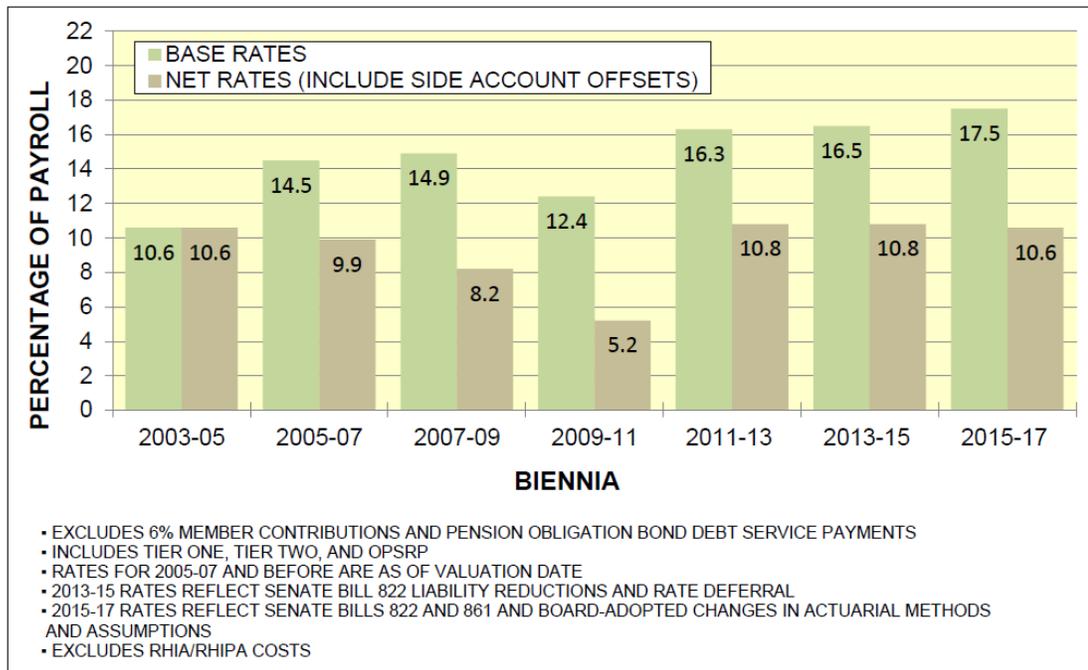
4. System Revenue (continued)

Regular account earnings available for crediting and actual distributions to Tier One member regular accounts based on 2015 earnings



4. System Revenue (continued)

System-wide average employer contribution rates as a percent of covered salary (net rates include side account offsets).



2017-2019 employer contribution rate increase projections

(\$ millions)	Projected 2015-17 Payroll*	(A) Projected 2015-17 Contribution	Projected 2017-19 Payroll*	(B) Projected 2017-19 Contribution	(B) - (A) Projected Contribution Increase
State Agencies	\$5,580	\$575	\$5,980	\$800	\$225
School Districts	\$5,950	\$560	\$6,370	\$850	\$290
All Others	<u>\$7,350</u>	<u>\$870</u>	<u>\$7,870</u>	<u>\$1,155</u>	<u>\$285</u>
Total	\$18,880	\$2,005	\$20,220	\$2,805	\$800

- Projected 2017-19 contributions are determined by applying collared net advisory rates calculated in the 12/31/2014 valuation
- Projections do not reflect the effects of actual 2015 investment returns

Investment income provided 73.8% of total PERS' revenues from 1970-2014, with member contributions providing 5.6% and employer contributions providing 20.6%.

Money for PERS benefit payments comes from three sources (1970-2014)



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>