

## 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 about 23%. 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 currently set to increase every two years until the State system is closer to 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. On July 1, 2017, the average rate increase for Grants Pass for all the different classes of PERS staff was an estimated 3.86% of gross wages. Tier 1/2 rates increased 4.83% while other classes increased between 2.81% and 3.47%. Absent additional legislation to change the benefit structure or rate setting process of the system, PERS rates are expected to increase at least 3% on average every two years again starting on July 1, 2019 until rates approach a total of close to 30% of gross payroll costs (according to PERS rate advisory and other presentations). This means rates are likely to go up again in 2019 and 2021 and remain high for many years after 2021. Rates the City pays into the reserve fund will need to be increased slightly each year in FY'19 and a number of years beyond FY'19 to keep up with the increased external PERS rates every two years. Thanks to actions in the past in building up a PERS reserve, the City's operating budget won't be as severely impacted by PERS rate changes for at least a few more years.

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 slightly starting in FY'18 when actual PERS rates were adjusted for the current two-year rate cycle. And unless internally billed PERS rates are slightly adjusted over the years, the drawdowns are expected to be much more severe and PERS reserves will likely begin additional 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.

The following are the actual and projected PERS reserve balances assuming internally billed PERS rates are adjusted by 1.5% of gross payroll each year through FY'21:

<u>DATE</u>	<u>PERS RESERVE BAL.PROJECTION:</u>
End of FY'16 (actual)	\$3.2 million
End of FY'17 (actual)	\$3.5 million
End of FY'18	\$3.3 million
End of FY'19	\$3.3 million
End of FY'20	\$2.9 million
End of FY'21	\$2.8 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'20, followed by another potential rate change at the beginning of FY'22. At this time the FY'20 rate increases are expected to be slightly larger than the percentage increases in FY'18 based on preliminary PERS rate advisories. The plan at this point is the City will begin drawing on the reserve slightly starting in FY'18 and small incremental annual increases to internally billed rates would happen in each of the few years in combination with the use of some of the reserves. It would be preferable to use the reserves incrementally over at least the next 10 years since rates are set to increase through 2021 and remain very high for at least 10 years after 2021. 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.

There is a new PERS program approved by the State Legislature in 2018 that might allow the City to use a portion of the PERS reserve in the next year. The State has set aside \$25 million for local governments and school districts across the state to use to pay down some of the actuarial liability of the system. Each local government is either an independent employer with its own share of the system's assets and liabilities or is pooled with the state and other local governments and is still responsible for a certain portion of the system's liabilities. Each local government that qualifies and has assets to pay down part of its share of the unfunded liability may apply to receive a 25% matching portion from the \$25 million in the new State program. For example, if Grants Pass was granted participation in this program, the state would pay \$25,000 towards the Grants Pass liability for every \$100,000 that Grants Pass paid into the system. Over the next year the City will likely make an application to this new program to receive the potential benefit of a 25% match, however the maximum amount of potential benefit and use of the PERS reserve is limited as the \$25 million has to be shared across all eligible public employers throughout the State. The majority of the PERS reserve will remain with the City even if the City is allowed to participate in this new State program.

Current Rates & City Department Costs

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>Total PERS Current Rates</b>					
	<b>FY'16 Actual</b>	<b>FY'17 Actual</b>	<b>FY'18 Budget</b>	<b>FY'19 Budget</b>	<b>FY'20 Projected</b>
PERS/OPSRP-Employee 6%	795,892	842,978	989,227	998,312	1,027,287
PERS/OPSRP-Employer	2,517,001	2,614,867	3,166,244	3,256,890	3,604,001
<b>TOTAL</b>	<b>3,312,893</b>	<b>3,457,845</b>	<b>4,155,471</b>	<b>4,255,202</b>	<b>4,631,288</b>

<b>Total PERS Expenditures by Program Area</b>					
	<b>FY'16 Actual</b>	<b>FY'17 Actual</b>	<b>FY'18 Budget</b>	<b>FY'19 Budget</b>	<b>FY'20 Projected</b>
Public Safety	2,121,308	2,253,042	2,557,879	2,750,974	2,992,508
Parks	71,709	70,609	85,246	91,334	99,134
Development	103,263	102,061	158,589	190,497	209,141
Transportation	71,060	65,961	88,221	80,796	88,713
Storm Water/Open Space	539	763	0	14,767	16,622
Water	194,408	161,337	200,376	220,829	239,650
Wastewater	175,518	180,913	194,722	209,843	226,020
Solid Waste	2,853	3,148	3,803	4,066	4,557
Administrative Services	260,755	285,936	310,425	314,337	343,302
Support Services	310,896	333,203	556,210	377,759	411,641
Lands & Building	584	872	0	0	0
<b>TOTAL</b>	<b>3,312,893</b>	<b>3,457,845</b>	<b>4,155,471</b>	<b>4,255,202</b>	<b>4,631,288</b>

Department	FY16 Actual	FY17 Actual	FY18 Adopted	FY19 Recommend	FY20 Projected
<b>PUBLIC SAFETY</b>					
PS-FIRE RESCUE DIVISION	708,236	692,521	758,284	825,675	900,140
PS-POLICE DIVISION	1,104,679	1,212,943	1,376,425	1,460,833	1,587,189
PS-SUPPORT DIVISION	308,394	347,578	423,170	464,466	505,179
	2,121,308	2,253,042	2,557,879	2,750,974	2,992,508
<b>PARKS</b>					
AQUATIC SERVICES	3,114	2,051	3,606	3,714	3,990
PARKS MAINTENANCE SERVICES	66,028	65,930	78,987	85,192	92,717
RECREATION SERVICES	2,566	2,628	2,653	2,428	2,427
	71,709	70,609	85,246	91,334	99,134
<b>DEVELOPMENT</b>					
BUILDING AND SAFETY	32,461	34,638	49,480	61,156	64,262
DOWNTOWN DEVELOPMENT	17,446	21,001	26,667	28,379	31,888
ECONOMIC DEVELOPMENT	2,087	11,811	12,379	17,812	20,111
PLANNING	50,389	33,573	68,988	80,525	89,914
TOURISM PROMOTION SERVICES	880	1,038	1,075	2,625	2,966
	103,263	102,061	158,589	190,497	209,141
<b>TRANSPORTATION</b>					
STREET & DRAINAGE MAINT	68,147	64,152	88,221	80,796	88,713
TRANSPORTATION PROJECTS	2,913	1,809	0	0	0
	71,060	65,961	88,221	80,796	88,713
<b>STORM WATER &amp; OPEN SPACE</b>					
STORM DRAIN SDCs	539	763	0	0	0
STORM WATER MAINTENANCE	0	0	0	14,767	16,622
<b>WATER</b>					
WATER DISTRIBUTION	84,158	80,017	108,107	117,631	129,722
WATER PROJECTS	3,540	3,174	6,427	10,032	7,424
WATER TREATMENT	106,710	78,146	85,842	93,166	102,504
	194,408	161,337	200,376	220,829	239,650
<b>WASTEWATER</b>					
WASTEWATER COLLECTION	65,850	66,954	79,311	81,707	89,802
WASTEWATER PROJECTS	5,173	6,502	6,426	10,032	7,423
WASTEWATER TREATMENT	104,495	107,457	108,985	118,104	128,795
	175,518	180,913	194,722	209,843	226,020
<b>SOLID WASTE</b>					
SOLID WASTE CONSTRUCTION	355	535	0	0	0
SOLID WASTE OPERATIONS	2,498	2,613	3,803	4,066	4,557
	2,853	3,148	3,803	4,066	4,557
<b>ADMINISTRATIVE SERVICES</b>					
FINANCE	152,314	162,810	181,689	195,390	213,294
HUMAN RESOURCES	38,103	42,265	40,741	47,690	52,786
LEGAL SERVICES	225	132	4,083	410	463
MANAGEMENT SERVICES	70,112	80,729	83,912	70,847	76,759
	260,755	285,936	310,425	314,337	343,302
<b>SUPPORT SERVICES</b>					
BENEFITS ADMINISTRATION	0	0	172,900	0	0
ENGINEERING	70,397	75,533	88,393	98,277	104,746
EQUIPMENT REPLACEMENT	0	0	0	0	0
GARAGE OPERATIONS	35,115	35,477	52,635	56,531	62,349
GENERAL INSURANCE	2,740	3,345	3,934	4,671	5,151
INFORMATION TECHNOLOGY	77,308	80,167	85,582	89,134	97,211
PARKS & CD MGMT SERVICES	94,137	104,022	111,700	87,986	96,847
PROPERTY MANAGEMENT	25,899	26,830	30,445	31,777	34,858
WORKERS COMP INSURANCE	5,300	7,829	10,621	9,383	10,479
	310,896	333,203	556,210	377,759	411,641
<b>LANDS &amp; BUILDINGS</b>					
LANDS AND BLDGS PROJECTS	584	872	0	0	0
	3,312,894	3,457,847	4,155,471	4,255,202	4,631,288

### 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 in the chart, 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 the unfunded liability since that time, 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, 2019 and for at least the following rate cycle unless the portfolio returns come in significantly higher than assumed earning rates. Investments must return well over the assumed returns of 7.2% in order for the unfunded liability to decrease in a given year. Over the FY18 year, the City is billing departments at rates slightly lower on average than what is paid into the system and begin small incremental annual increases to internally billed rates will begin again in FY19.

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.

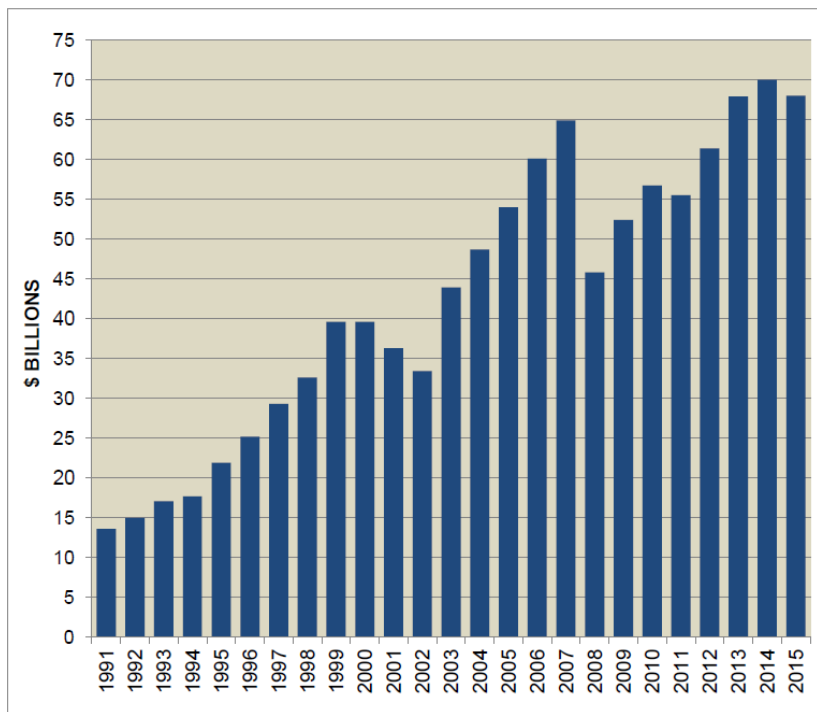
Since 2015 Grants Pass is no longer an independent employer for the calculated liabilities for the PERS Tiers previous to OPSRP (2003), and the difference between the funded status of Grants Pass and the pool at the point where Grants Pass joined the rate pool recently, is set to be amortized over many years into the future. PERS rate changes every two years for Grants Pass might be slightly less volatile in the future due to this change that was made in the cycle ending in 2015. Rate changes every two years will be closer to that experienced by the overall pool participants on average.

Without 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 presentations created by PERS dated September 2016, titled “PERS by the Numbers” and “PERS Facts.” Much of the following information is expected to be updated again later in 2018 as the State prepares for the July 1, 2019 rate changes. 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)

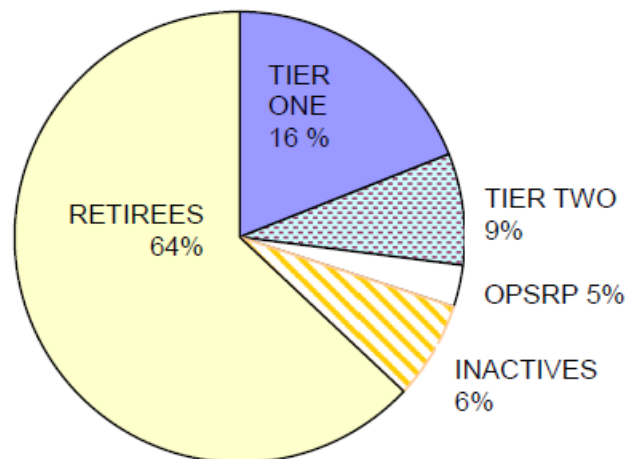
Unfunded actuarial liability history and funded ratio<sup>1</sup>

Valuation <sup>2</sup> Date	With Side Accounts <sup>3</sup> (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 <sup>4</sup>	7,700	87.0	13,300	78.0
2011	11,030	82.0	16,255	73.0
2012 <sup>5</sup>	5,600	91.0	11,100	82.0
2013	2,600	96.0	8,500	86.0
2014 <sup>6</sup>	12,100	84.0	18,000	76.0
2015	16,200	79.0	21,800	71.0

- 1 Includes RHIA/RHIPA.
- 2 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.
- 3 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.
- 4 2010 and after includes the OPSRP Pension Program, 2000-2009 reflects only Tier One/Tier Two.
- 5 Includes liability reductions from Senate Bills 822 & 861 and new Board-adopted actuarial assumptions and methods from the 2012 Experience Study.
- 6 Includes the *Moro* decision and new Board-adopted actuarial assumptions and methods from the 2014 Experience Study.

Actuarial accrued liabilities (as of December 31, 2015)

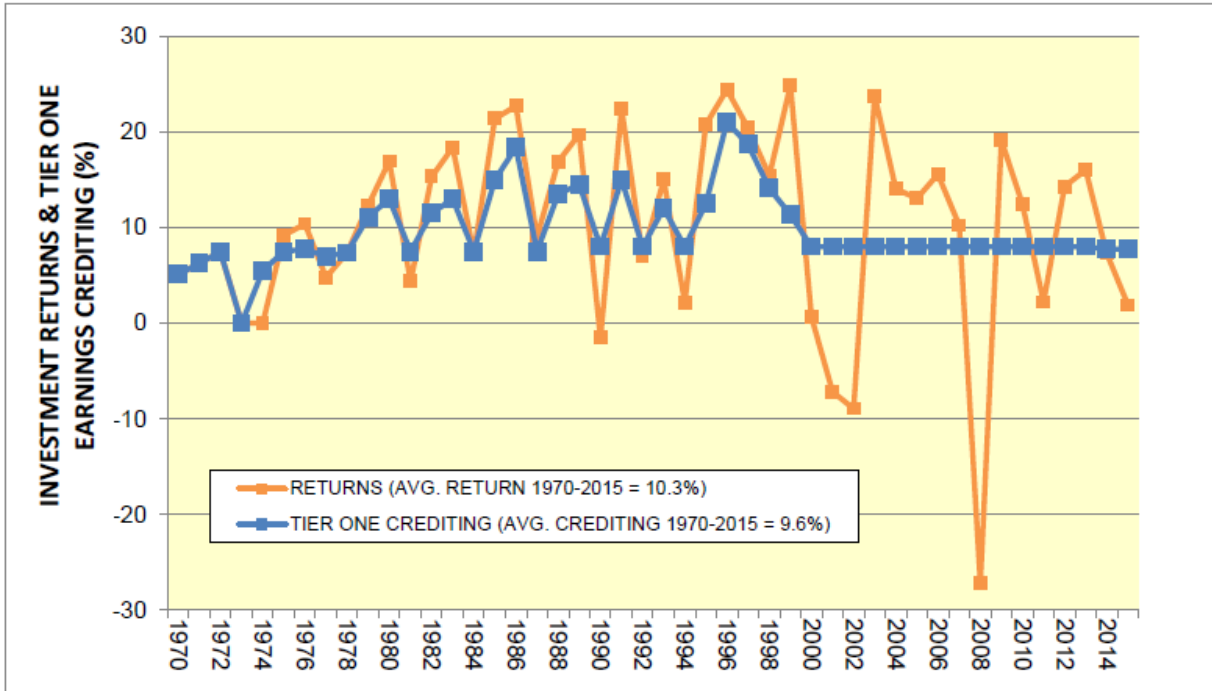
Approximately 70% of PERS' total accrued liability is for members who are no longer working in PERS-covered employment (retired and inactive members).





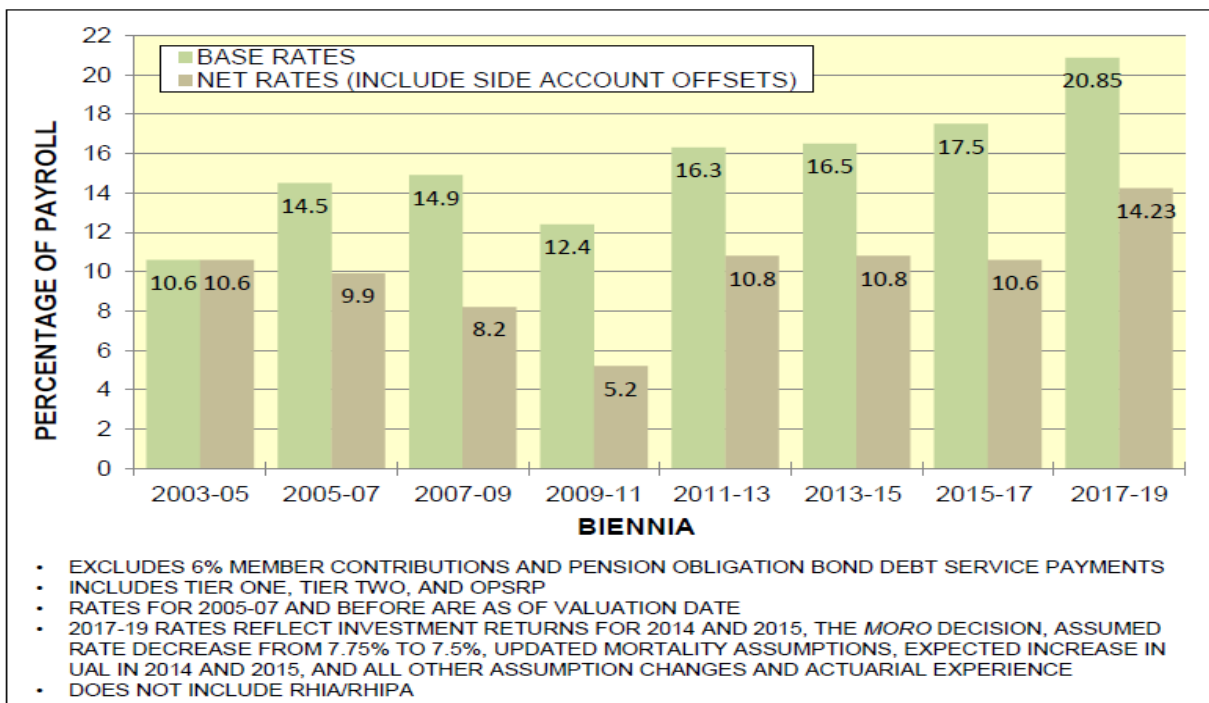
4. System Revenue (continued)

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).



## 2017-19 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	\$5,620	\$575	\$6,020	\$835	\$225
School Districts	\$6,120	\$560	\$6,560	\$910	\$335
All Others	<u>\$7,350</u>	<u>\$875</u>	<u>\$7,880</u>	<u>\$1,165</u>	<u>\$290</u>
<b>Total</b>	<b>\$19,090</b>	<b>\$2,025</b>	<b>\$20,460</b>	<b>\$2,910</b>	<b>\$885</b>

\* Assumes payroll growth at 3.5% annually based on 12/31/2015 active member census, reflecting proportional payroll composition (Tier One/Tier Two vs. OPSRP) as of 12/31/2015.

\*\* Collared net rates are used to project 2017-19 employer contributions.

## Funding sources (1970-2015)

Money for benefit payments comes from three sources



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>