SHARED RESPONSIBILITY, EQUITABLY APPLIED:
STABILIZING PERS FOR OREGON'S EDUCATION SYSTEM

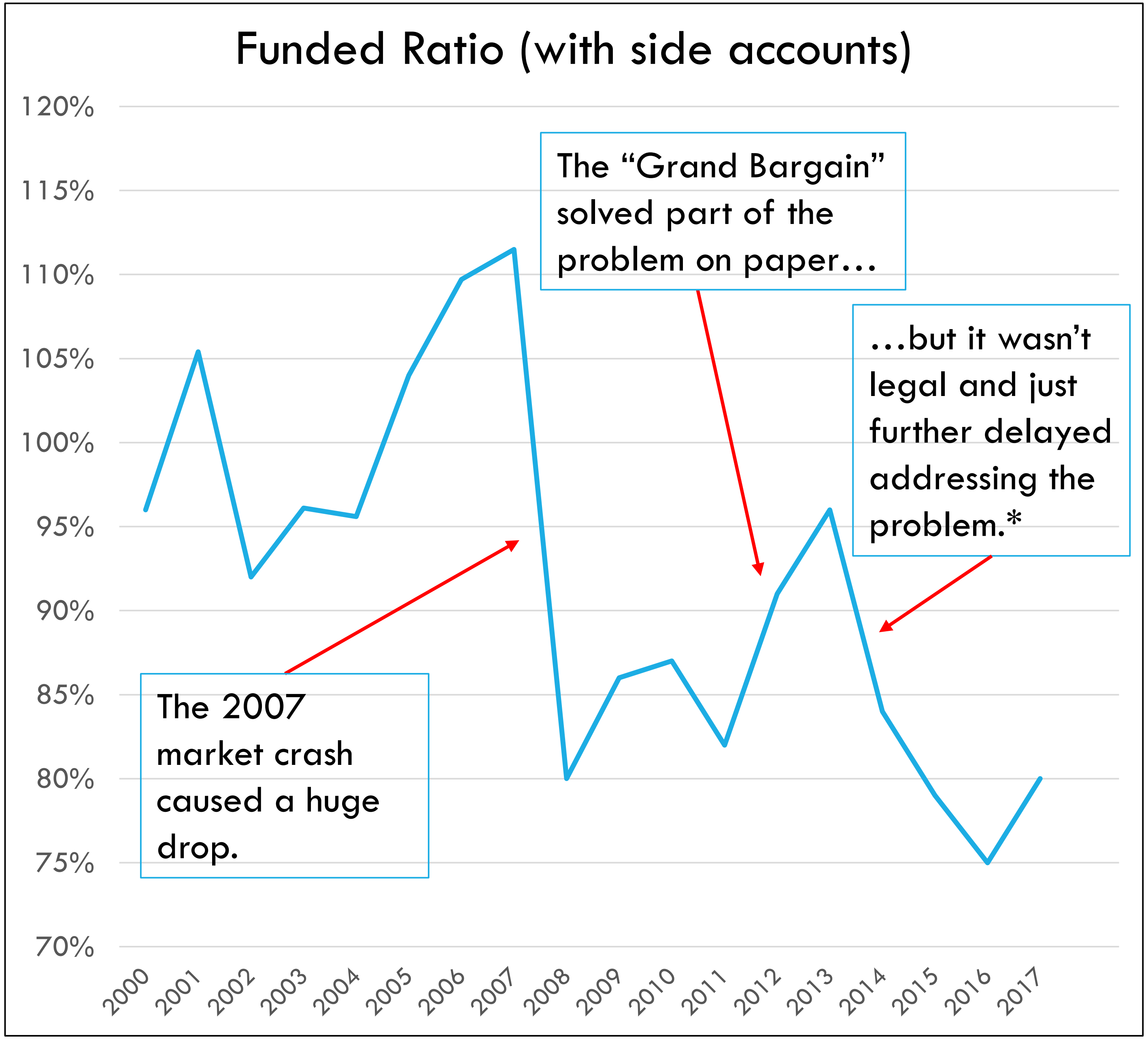
April 12, 2019

Nik Blosser, Chief of Staff
Governor Kate Brown

PERS WAS OVER 110% FUNDED BEFORE THE GREAT RECESSION, THEN DROPPED 31%

WE'VE NEVER RECOVERED, AND ANOTHER DROP WOULD BE CALAMITOUS AT OUR CURRENT FUNDED STATUS

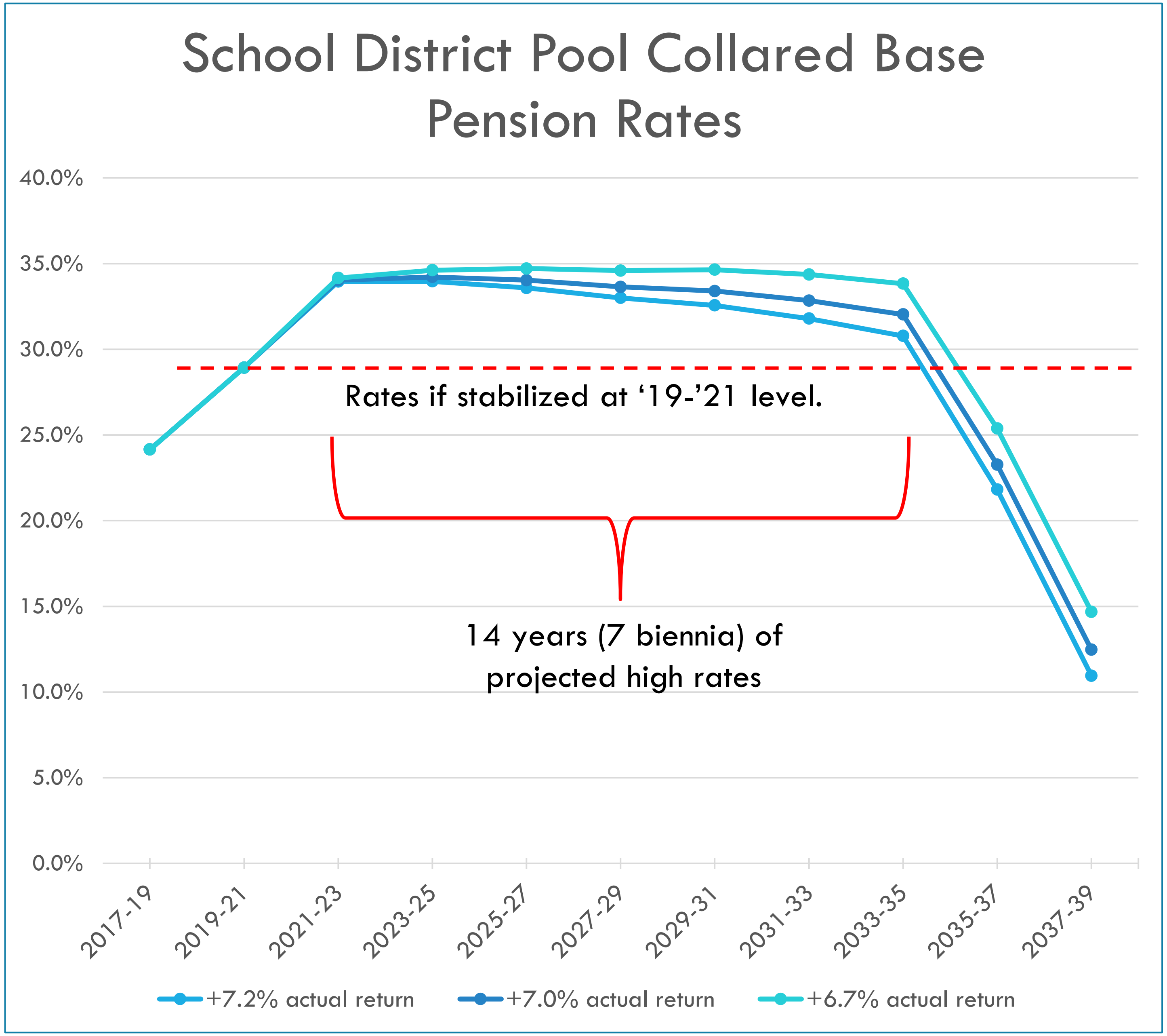
*2014 drop of 8% in funded status due to *Moro* Supreme Court decision ($5b impact), updated mortality assumptions ($1.8b), and lowered future assumed earnings rate ($1.7b).



Source: [PERS by the Numbers 2018]

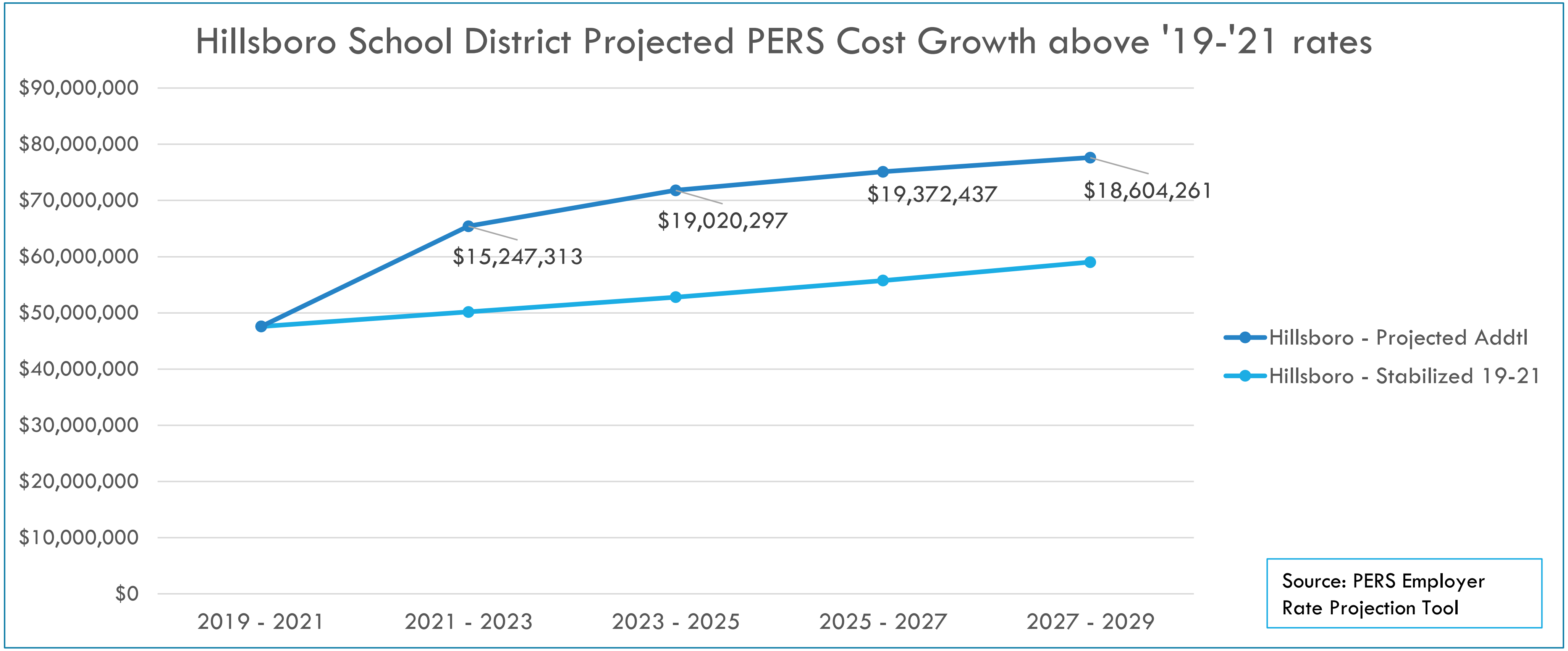
BECAUSE OF THE UAL, EMPLOYER RATES WILL INCREASE SIGNIFICANTLY

PERS ENFORCES A 20-YEAR PLAN TO MAINTAIN FUNDED STATUS



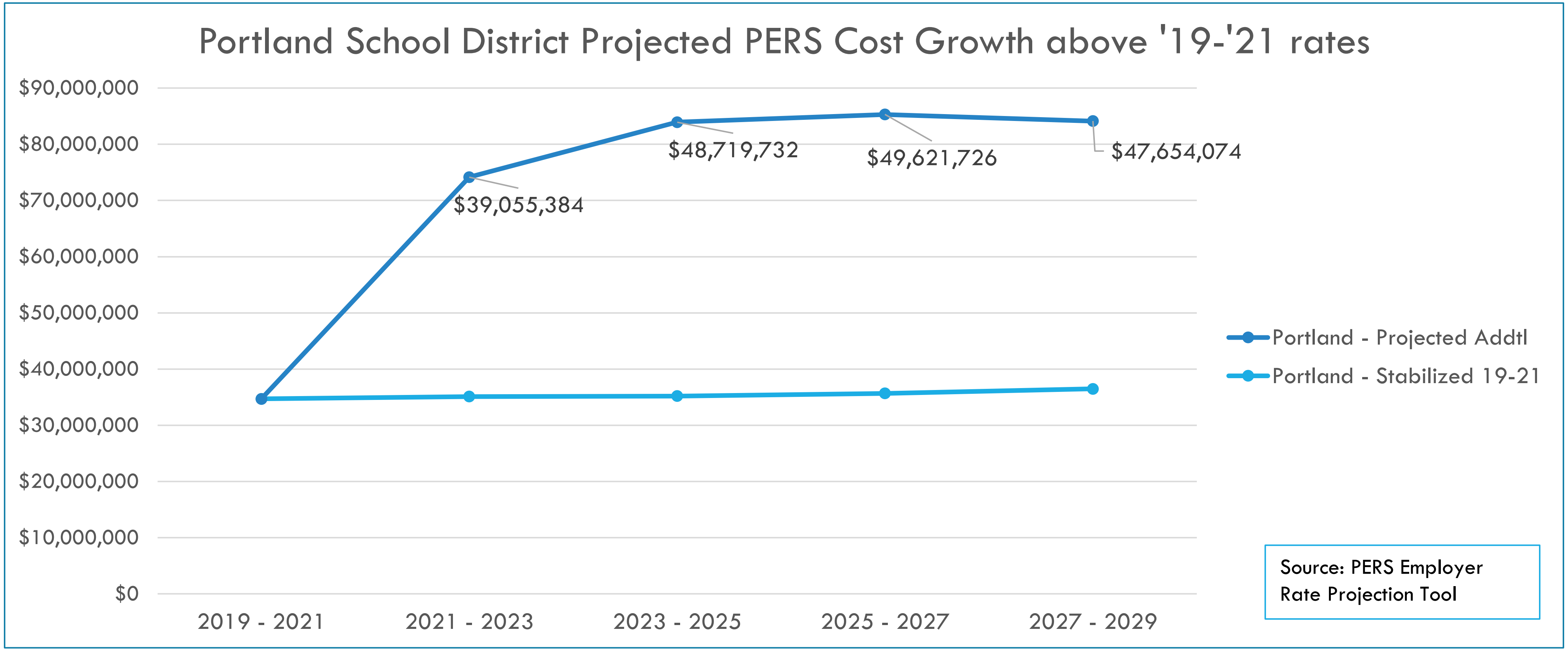
Source: PERS/Milliman Financial Modeling for School District Pool Request 2018-008

EXAMPLE 1: HILLSBORO
$15-19M IN INCREASED ANNUAL PERS COSTS ABOVE '19-'21 RATES



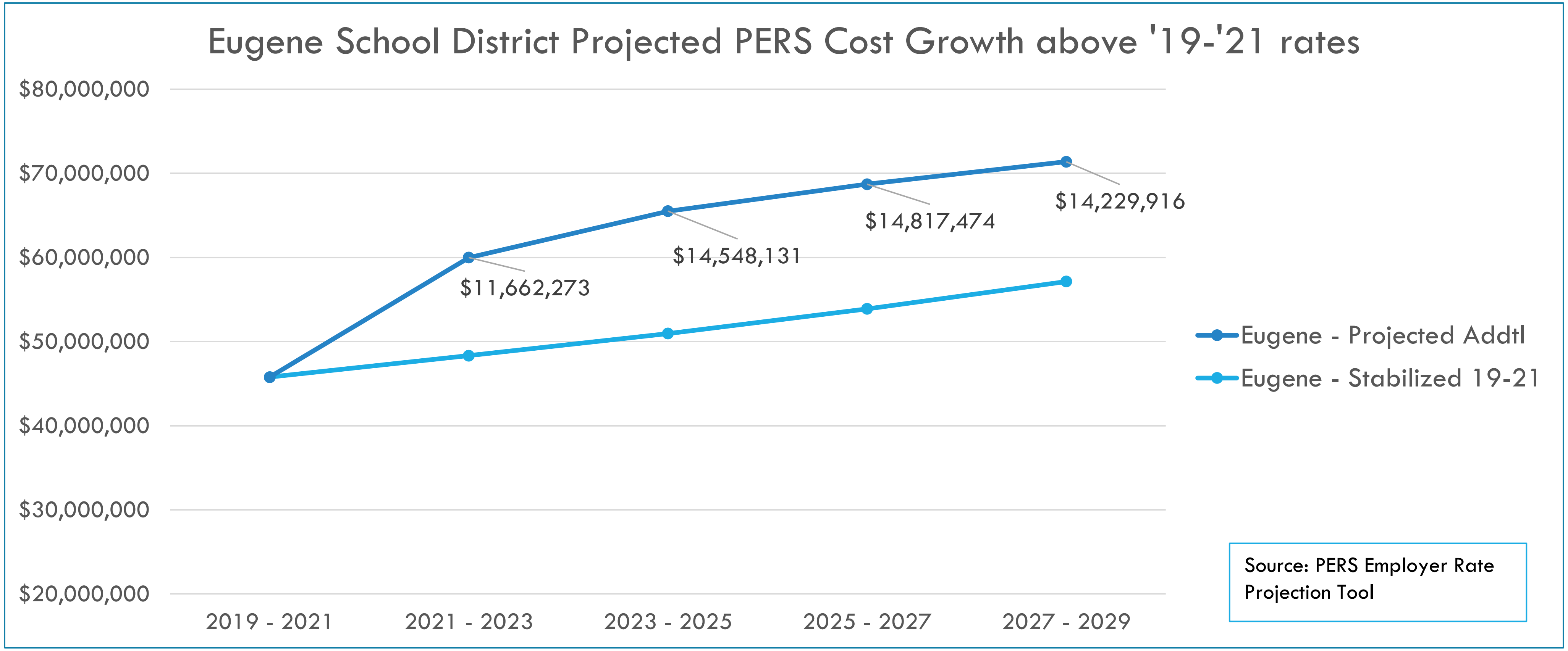
EXAMPLE 2: PORTLAND

$39-50M IN INCREASED ANNUAL PERS COSTS ABOVE ‘19-’21 RATES



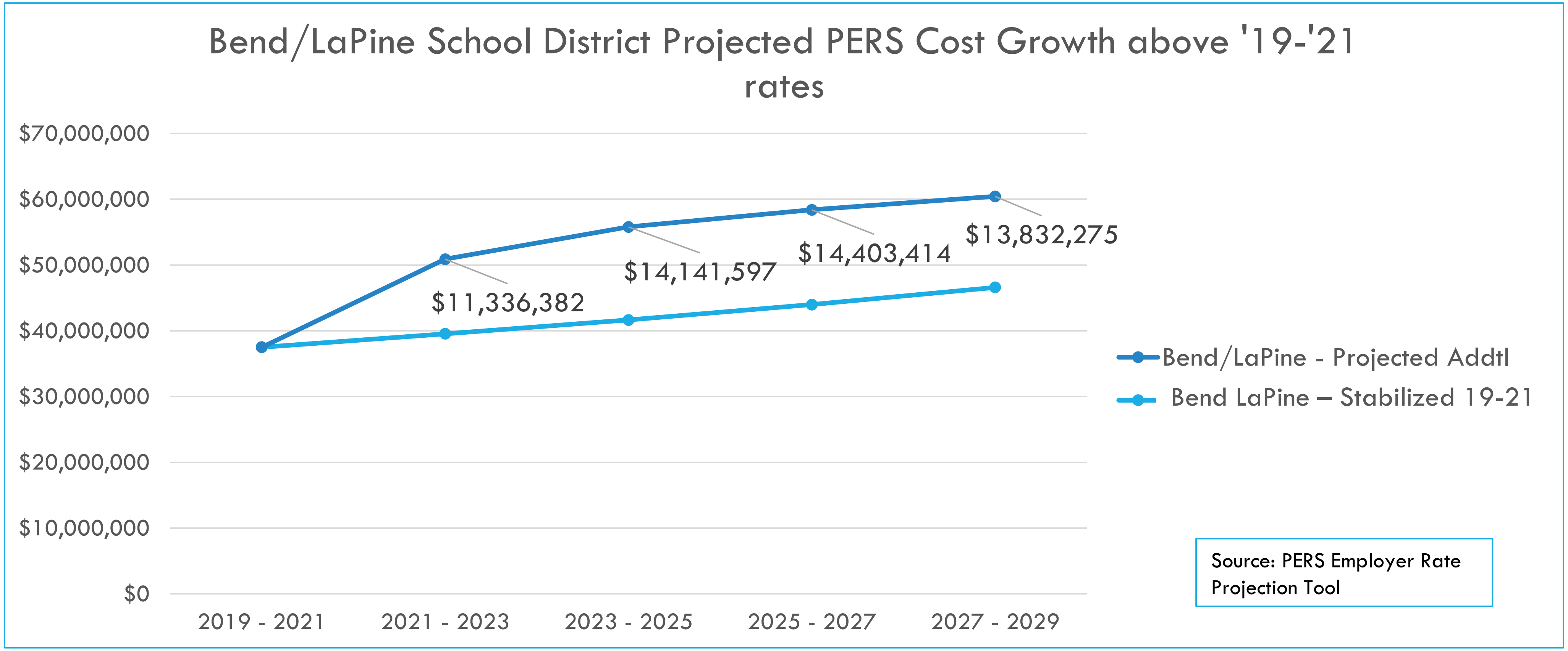
EXAMPLE 3: EUGENE

$39-50M IN INCREASED ANNUAL PERS COSTS ABOVE '19-'21 RATES

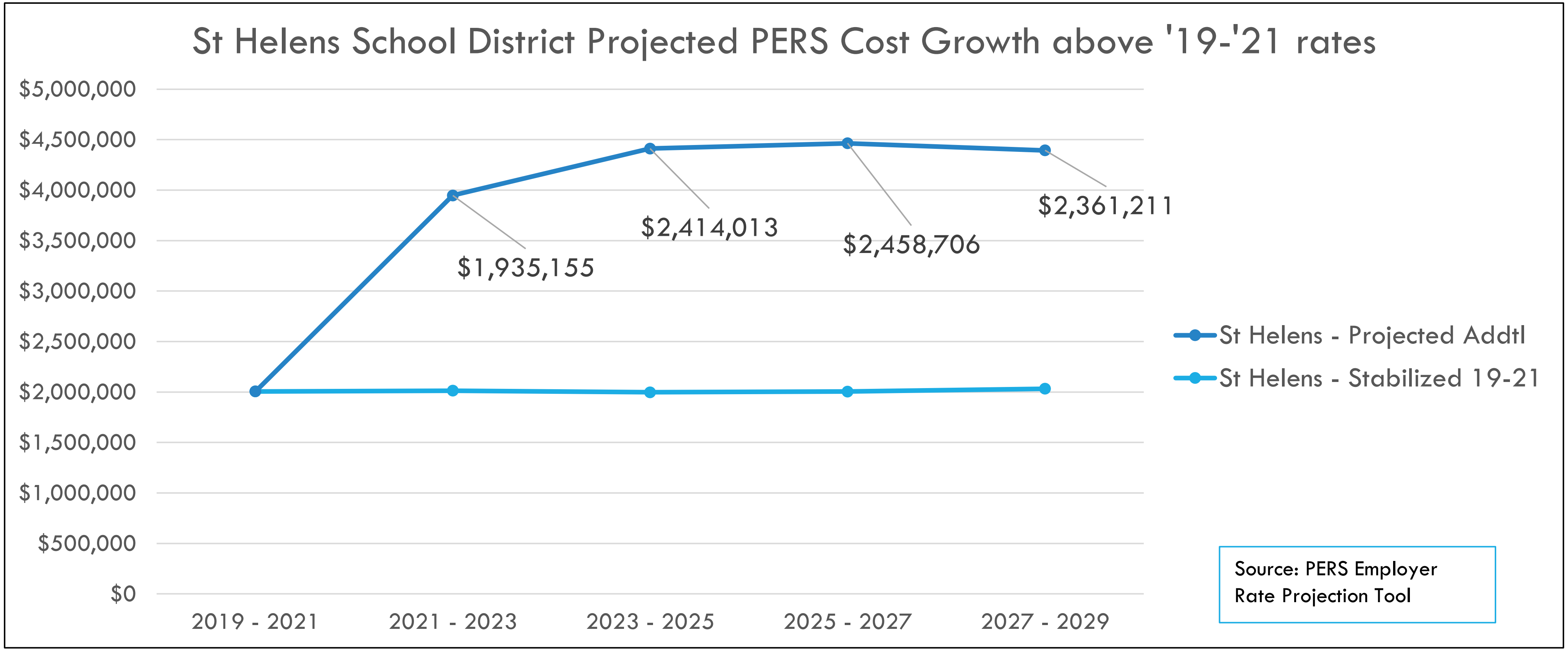


EXAMPLE 4: BEND

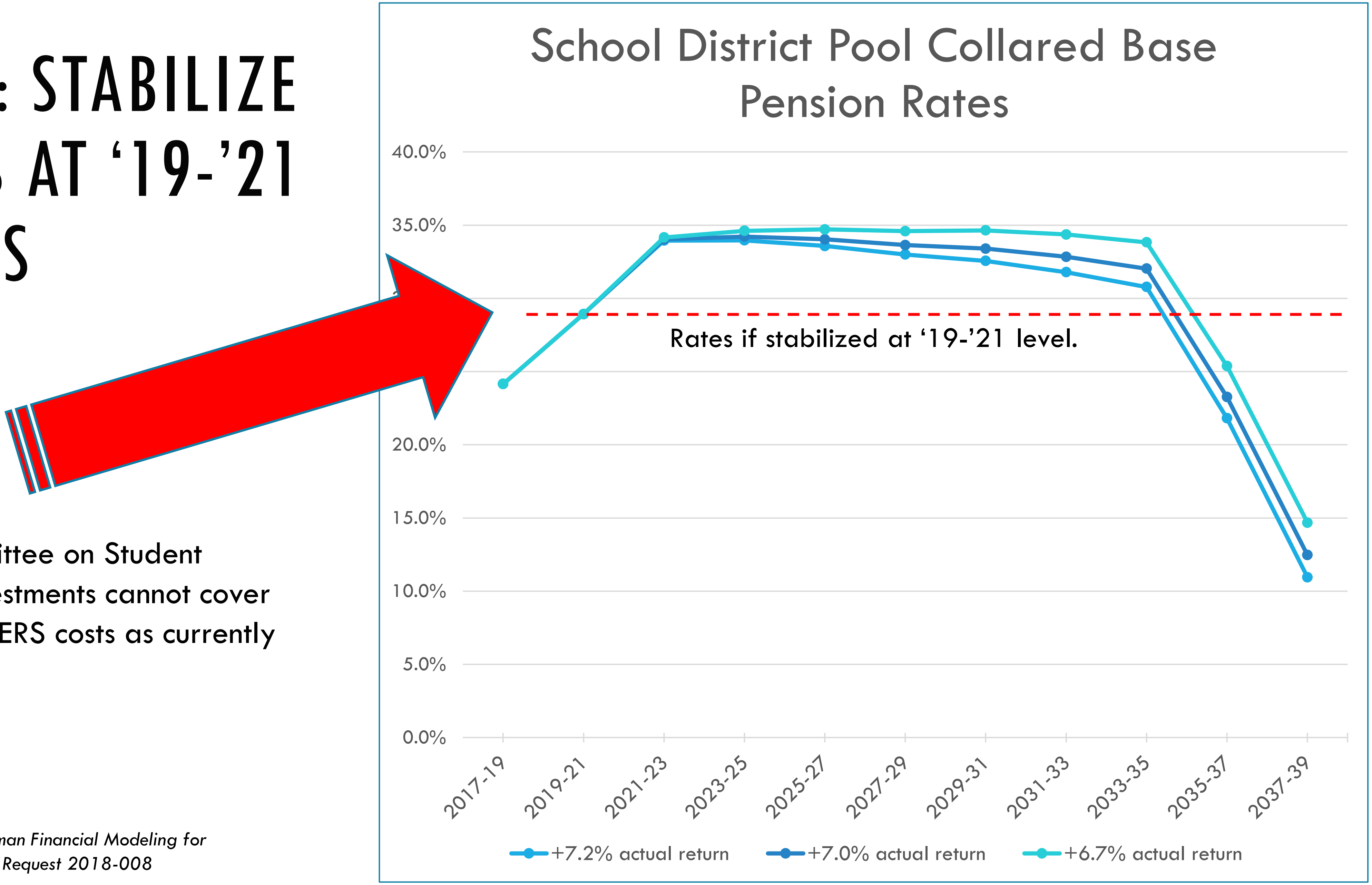
$11-14M IN INCREASED ANNUAL PERS COSTS ABOVE ‘19-’21 RATES



EXAMPLE 5: ST. HELENS
$2-2.5M IN INCREASED ANNUAL PERS COSTS ABOVE ‘19-’21 RATES



GOAL: STABILIZE RATES AT ‘19-’21 LEVELS



Joint Committee on Student Success investments cannot cover increased PERS costs as currently drafted.

Source: PERS/Milliman Financial Modeling for School District Pool Request 2018-008

TO ACHIEVE THIS WE NEED $2.5-$3.0 BILLION BETWEEN 2021 AND 2035

Estimated funds required over 7 biennia ('21-'23 thru '33-'35): $2.5-$3.0 billion

- 7.2% assumed earnings rate: $2.462 billion
- 7.0% assumed earnings rate: $2.927 billion

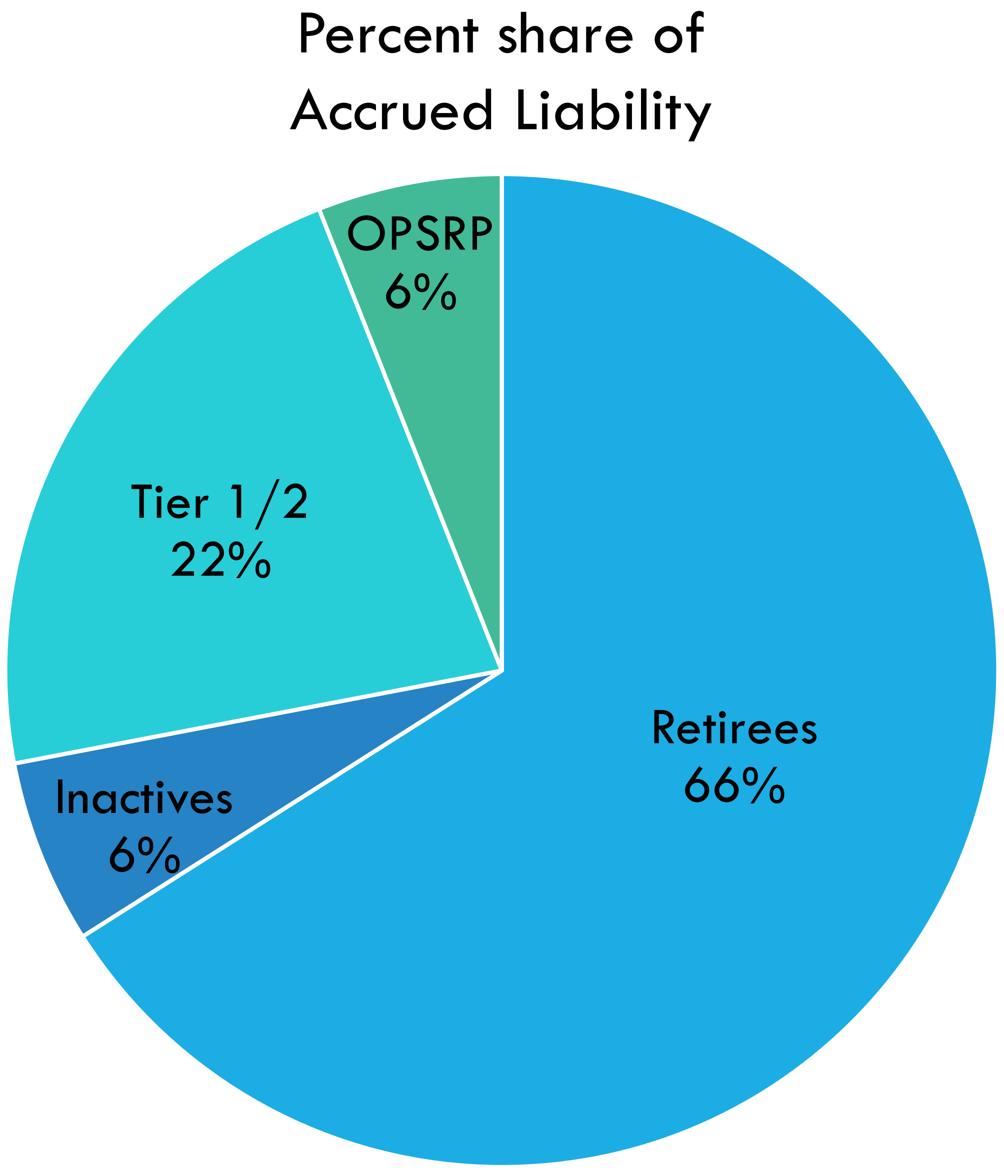
Estimated funds required per biennia (millions):

21-23	23-25	25-27	27-29	29-31	31-33	33-35	Total
$ 382	$ 410	$ 406	$ 380	$ 364	$ 307	$ 213	$ 2,462

Source: CFO financial model using data supplied by PERS

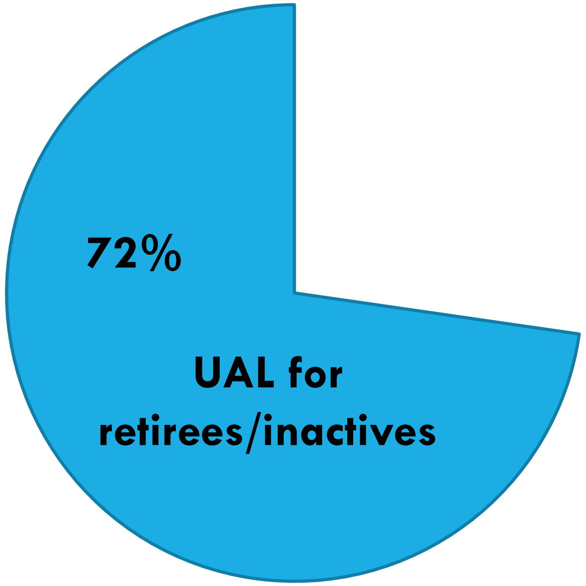
SOLUTION FRAMEWORK

IMPORTANT CONTEXT: 72% OF THE ACCRUED LIABILITY IS FROM RETIREES/INACTIVES, NOT CURRENT EMPLOYEES

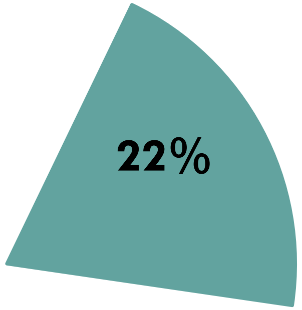


Source: *PERS by the Numbers 2018*

SHARED RESPONSIBILITY NEEDS TO BE EQUITABLE

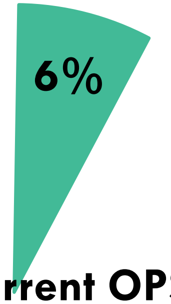


Employer
+
Major 15-year state commitment, including one-time funds and dedicated future revenues



UAL for current Tier 1/2 employees

Employer
+
PERS Stability Contribution and limited future risk sharing

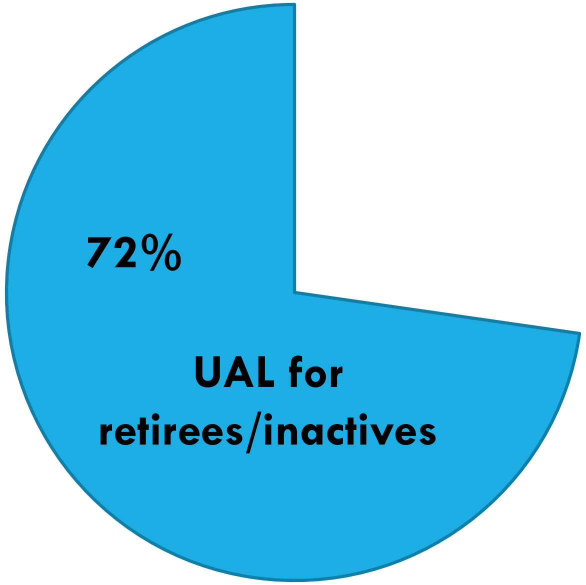


UAL for current OPSRP employees

Employer
+
PERS Stability Contribution and limited future risk sharing

Source: *PERS by the Numbers 2018*

PART 1: MAJOR STATE COMMITMENT



- Create a School PERS Offset Account (SPOA) for K-12 districts and a Higher Ed PERS Offset Account (HEPOA) for universities and community colleges.
- Seed SPOA with $800M in one-time funds;
- Dedicate roughly $1.6 billion in future state receipts over the next 15 years.

Source: PERS by the Numbers 2018

MUST SEED SPOA WITH $800M – SOME OPTIONS

I. 2017-19 personal kicker retention

- Preferred option: Return the first $100 to each eligible taxpayer and retain rest: $400-500M
- 2/3 vote

II. SAIF

- Transfer of excess surplus: $486M
- SAIF coverage of school district workers comp insurance + limited payment + "never again" independence provisions
- Simple majority vote

III. General/lottery funds

- Governor appropriated $100M in her budget (HB5032)
- Repatriation funds previously appropriated to school side account but not yet deposited ($83.3M)

IV. Temporary tax/fee/surcharge

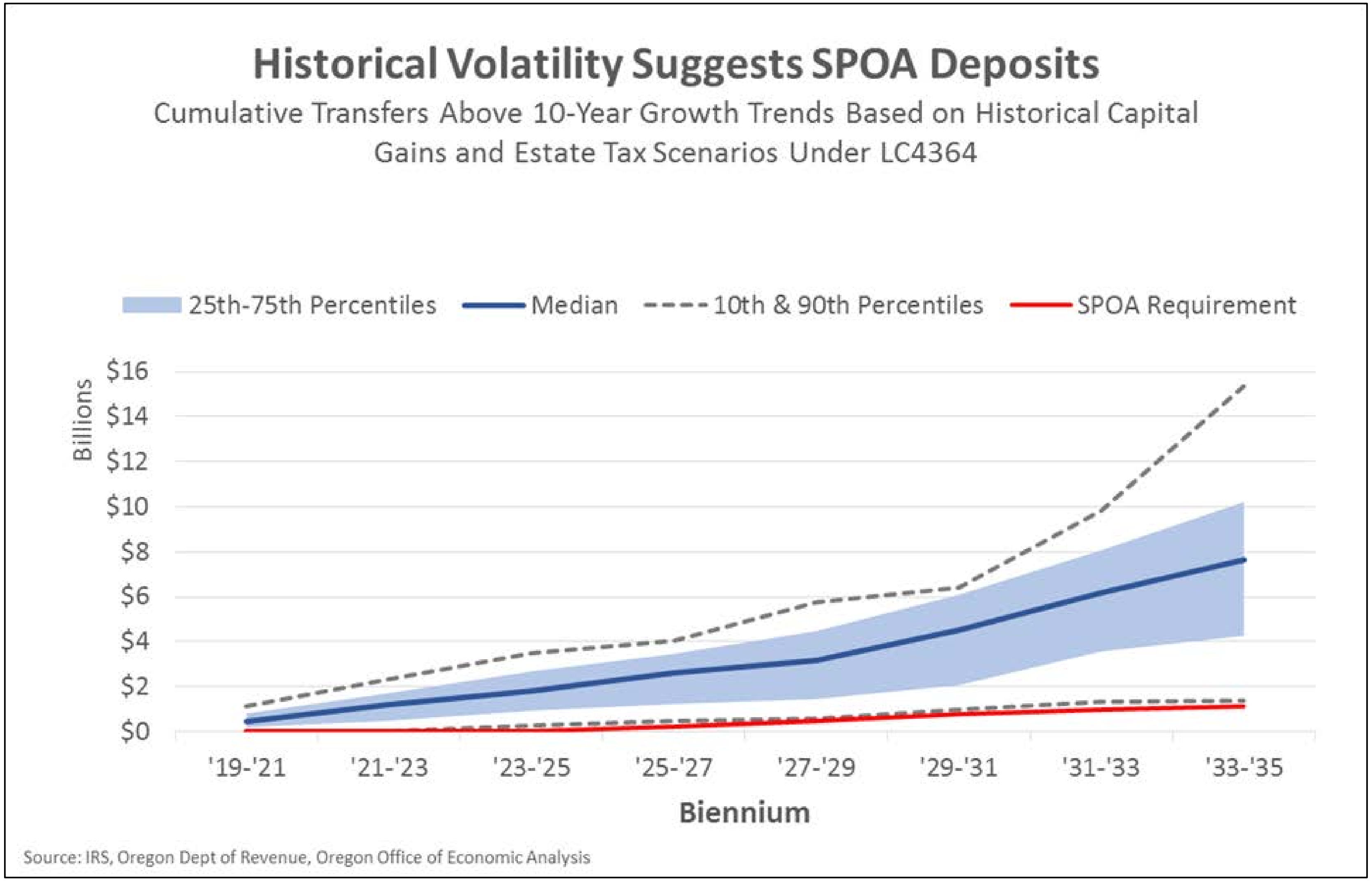
- i.e. surcharge on all state fees/licenses

DEDICATED REVENUES TO SPOA

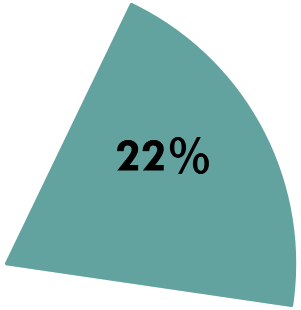
1. **Funds from SB1566: change dedication from side account to SPOA**
   - Unclaimed property
   - Excess debt collection
   - <u>Estimate: $332M over 15 years</u>

2. **Above-trend capital gains and estate taxes**
   - Capital gains and estate taxes flow into a new fund separate from the General Fund
   - Above-trend amounts go into SPOA, rest is at legislature's disposal
   - <u>Median estimate: $1.3 billion over 15 years</u>
   - Above-trend amounts are a) not at the legislature's disposal, and b) outside kicker calculation.

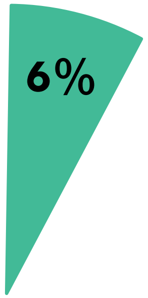
ABOVE-TREND CAPITAL GAINS AND ESTATE TAX RECEIPTS



PART 2: EMPLOYEE PERS STABILITY CONTRIBUTIONS



UAL for current Tier 1/2 employees



UAL for current OPSRP employees

1. Create a PERS Stability Contribution Program for current employees. Individual pension accounts are created for each employee and dedicated to their defined benefit plan, with contributions made as follows:
   - Tier 1/2: Exempt first $20,000 of salary, then contribute 3%. (Average of 2.1% contribution.)
   - OPSRP: Exempt first $20,000 of salary, then contribute 1.5%. (Average of 1% contribution.)
2. After the system is fully funded (it's currently at 80%) or after 14 years, whichever is earlier, cost-sharing will end. If the funded status subsequently drops below 90%, PERS Stability Contributions will re-start systemwide at 3% after the first $20,000 for all participants, again into individual employee pension accounts.

SCHOOL PERS OFFSET ACCOUNT FUNDING

	2019-21	2021-23	2023-25	2025-27	2027-29	2029-31	2031-33	2033-35	Total	%
One-time funds										
Repatriation[1]	83,300,000								**83,300,000**	**3%**
Kicker/SAIF/GF/Other	300,000,000	416,700,000							**716,700,000**	**22%**
Ongoing additions										
Unclaimed property[2]	38,000,000	38,000,000	38,000,000	38,000,000	38,000,000	38,000,000	38,000,000	38,000,000	**304,000,000**	**9%**
Debt collection[2]	3,500,000	3,500,000	3,500,000	3,500,000	3,500,000	3,500,000	3,500,000	3,500,000	**28,000,000**	**1%**
Above trend cap gains[3]			222,877,436	203,967,749	14,598,183	451,919,545	331,057,672	40,601,981	**1,265,022,566**	**38%**
Above trend estate taxes[3]	-		-	7,037,765	7,142,930	31,463,549	27,966,133	8,465,400	**82,075,777**	**3%**
School district employee contributions[4]	49,448,213	100,593,600	102,692,100	105,292,425	108,240,675	111,402,675	115,424,333	120,804,230	**813,898,250**	**25%**

TOTAL: $3,292,996,593

[1] *Source: Office of Economic Analysis projection, March 2019.*
[2] *Source: LRO estimated revenue impact for SB1566 (2018).*
[3] *Source: Cash Flow Estimates for Transfers of Proceeds from Capital Gains and Estate Taxes under LC4364, Office of Economic Analysis, April 2019.*
[4] *Source: Milliman correspondence 4/4/2019 using the following formula: Employees of employers in the school district PERS pool only, then a 3% contribution for Tier ½ and 1.5% for OPSRP employees after exemption of first $20,000 (indexed).*

A FEW OTHER SMART ITEMS

I. All prepayment of PERS contributions annually to increase investment returns

- Current payment schedule is monthly. Prepaying a full year at the beginning of the year will increase investment returns. Allow all other PERS employers to prepay as well to benefit their returns.

II. Employers pay full PERS rates on retired employees

- Starting 1/1/2020, PERS employers must pay net collared employer PERS rate for all employees working after retirement. The full amount goes toward the UAL. May contribute $100M per biennium.
- Expanding 1,039 hour limit is not recommended for Tier ½ as it will further exacerbate pay equity issues between retirees (primarily tier 1/2) and current employees (primarily OPSRP); OPSRP hour limit will be increased from 600 to 1,039.

III. Improved county assessment and taxation compliance

- Increased state investment in county assessment and taxation operations and DOR property tax division to improve collections for all taxing districts. (HB2104)
- Increased DOR support to ensure collection of local lodging taxes (HB3135, HB3136)

A FRAMEWORK FOR ADDRESSING THE PROBLEM EQUITABLY

- The only plan that stabilizes PERS employer rates for all K-12 school districts, providing certainty on budgeting and use of future investments. Protects school budgets and thus the jobs of many teachers, particularly newer, more diverse teachers.
- Maintains OPSRP as a strong defined benefit plan for current and future employees.
- Captures future above-trend volatile tax receipts and responsibly uses them to pay debt rather than putting them into the general fund.
- Provides improved long-term stability of the entire PERS system -- and greater financial alignment between all plan participants -- through limited future risk sharing.

SAIF BACKGROUND

SAIF OVERVIEW

- State-owned workers compensation insurer, governed by the Governor-appointed and Senate-confirmed SAIF Board of Directors. Very strong, competent management team led by CEO Kerry Barnett.
- Oregon ranks as one of the very best states in the country for workers comp costs (46th lowest in the U.S.).
- Writes $500 million of premium annually
- Operates as a virtual monopoly, covering over 70% of the addressable Oregon market for workers compensation insurance in 2017 (closest competitor is Liberty Mutual with 6.3%). This is up from 56% market share in 2008
- Has returned 27% of premium on average through dividends over the past 10 years. In 2017 average dividends returned across all U.S. states was 2.6%.
- SAIF contracts with business trade associations, including AGC, the Homebuilders, and the Association of Oregon Loggers, to run safety programs for their members.

Source: SAIF, DCBS

SAIF: RESERVES AND SURPLUS

Claims reserves: For each claim, SAIF calculates the lifetime cost and puts the entire amount into their claims reserves. This amount is not discounted. So, if estimated costs are $1 million for the lifetime of the claim, including expected medical cost growth, the full $1 million is put into claims reserves to pay future claims. Current claims reserves are $2.5 billion.

Surplus: In addition to claims reserves, SAIF maintains an additional buffer called a surplus. The targeted surplus is calculated in several ways using a risk-based capital approach. The board minimum is 4.0 times CAL-RBC ($1,215M) and the board target is 5.0 times CAL-RBC ($1,519M). The current SAIF surplus is $2,005M, $486M above the board target level.

Restating of claims reserves: every year claims reserves are re-analyzed to determine sufficiency. From 2014-2017 SAIF moved $933M out of claims reserves and into surplus due primarily to lower-than-expected medical cost growth.

Source: DCBS and SAIF annual filings