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REVIEW OF PROPOSED AMENDMENTS

SENATE BILL 1049

On behalf of the PERS Coalition of Unions, we reviewed the amendments to Senate Bill 1049 being proposed by the legislative leadership.¹ The proposed amendments raise: (1) legal concerns in light of the *Moro* case's command that benefits attributable to service already performed must be protected and the *Strunk* case's interpretation of the concept of "actuarial equivalency;"² (2) new questions not addressed by the court in *Strunk*; and (3) equity concerns in calling for further cuts for workers who are not the major source of the PERS unfunded actuarial liability and who are already receiving lower and affordable benefits.³ We discuss some of these concerns in greater detail below.

Reinstate Employee Contributions to the Pension Plan

- The reason that the 6% employee contributions currently go to the Individual Account Program (IAP) instead of the old employee regular account to pay for the pension benefit is because of the 2003 PERS cuts. The consequence of that change was known to then Governor Kulongoski and the 2003 Legislative Assembly—i.e., the reduced benefit pension plan would thereafter be funded by employer contributions and the IAP by employee contributions.
- Now, the proposed amendments to SB 1049 change that existing "shared responsibility" for retirement benefits and call for active Tier 1, Tier 2, and OPSRP employees to also fund the reduced benefit pension plan.
- The proposed amendments call for the creation of a new "employee pension stability account" for each active PERS member and require that PERS divert 2.5% of active Tier 1 and Tier 2 members' IAP contribution and 0.75% of active OPSRP members' IAP contribution to the new employee pension stability account. The proposal exempts employees earning less than \$2,500

¹ See [April 29, 2019 Letter from Milliman to PERS re. Legislative Fiscal Office Combined Concepts](#).

² See *Moro v. State*, 357 Or 167, 351 P3d 1 (2015) and *Strunk v. PERB*, 338 Or 145, 108 P3d 1058 (2005).

³ As a result of the 2003 and 2013 legislative changes, the majority of active Tier 1 and Tier 2 members now retire on a Full Formula pension and will be receiving a lower COLA, and OPSRP members, who now comprise a majority of the active members of the system, receive a lower formula at a higher retirement age and a reduced COLA. See [PERS By the Numbers October 2018](#). The vast majority of the unfunded liability relates to retirees. See [Charts from PERS](#).

per month (\$30,000 annually) in salary. The contributions continue to be required so long as the “funded status” of PERS is below 90%.⁴

- Presumably because even legislative counsel agrees that it would be unconstitutional under *Moro* to apply any of these required contributions toward the existing unfunded actuarial liability (UAL),⁵ the proposed amendments provide that the contributions should only be applied to benefits that accrue after July 1, 2021. However, the requirement of a contribution is imposed on all employees regardless of whether they will actually accrue any additional retirement benefits after July 1, 2021. For example, as discussed further below, members who retire on money match will not accrue any additional benefits after July 1, 2021.
- Furthermore, to the extent the employee contributions are applied solely to cover the cost of future accruals of pension benefits, the PERS Actuary has explained that it would do nothing directly to reduce the UAL.⁶ Therefore, the proposed amendments would only be reducing future “normal cost” which is already fairly reasonable for the vast majority of the system and doing so to the detriment of workers who are already receiving a lower level of benefits.
- It is also important to recognize that although the Supreme Court in *Strunk*, approved the diversion of the 6% contribution to the IAP account for Tier One and Tier Two members, that diversion moved the money to an account that accrued earnings as a new benefit for members. The diversion of the employee contributions from the IAP to the new “employee account” comes with no new benefit to members. Whether that is legal is a question that the Supreme Court has not addressed.
- In addition, by requiring the creation of a new account for each active member of the system, the proposed amendments create an administratively cumbersome system for PERS to track. According to PERS by the Numbers, there are 175,997 active employees and growing. PERS will have to track yet an additional account for each of these employees, moving it even closer to the top of the list of most complex retirement systems in the country.
- Finally, any estimates of savings would also be reduced by salary increases which would inevitably be bargained by employees to make-up for any diversion of the contribution from their IAP and by mass retirements. Approximately 30.5% of all active/inactive members are eligible to retire by age and service.⁷

Changes to Final Average Salary

- The legislative leadership proposed amendments calls for capping “salary” used to calculate “final average salary” for service on or after January 1, 2020 at \$195,000 with an index for inflation. Currently, Tier 2 and OPSRP members’ salary is already subject to a cap tied to

⁴ With regard to the “funded status” issue, it is important to note that PERS consists of over 900 participating employers with different levels of funded status and different employer rates.

⁵ [August 31, 2016 Letter from Legislative Counsel to Sen. Johnson.](#)

⁶ [Milliman Combined Concepts Analysis Letter, May 9, 2019.](#)

⁷ See page 3, [PERS By the Numbers October 2018.](#)

amounts set by the IRS (\$280,000 in 2019). The proposal is unclear whether it properly allows for benefits attributable to service already provided to be calculated under the current cap for Tier 2 and OPSRP members and uncapped for Tier 1 members, including salary increases through the date of retirement.

- As we have previously explained, to fully protect benefits based on service performed before the change, within the meaning of the majority opinion in *Moro*, the PERS Actuary would still have to account for increases in salary through the date of retirement. It is unclear whether this occurred because as the PERS Actuary acknowledges they are not analyzing the concepts for legality or consistency with any cases. Legislative Counsel has also acknowledged that if a proposal were to cap the use of salary earned before the effective date of the change, it would likely be unconstitutional under *Moro* because it would affect accrued benefits.

Changes to Annuitization Rate for Money Match Benefits

- The legislative leadership proposed amendments also calls for the Money Match retirement benefit to be calculated using a rate which is half the assumed interest rate of the system, which is currently 7.20%. In other words, under the proposed amendments, if the system's assumed interest rate remained at its current level, Money Match benefits would be calculated using 3.6% instead of 7.2% after July 1, 2021.
- With regard to the Money Match benefit, it is important to highlight that it is exclusively attributable to service provided and contributions made prior to January 1, 2004. Under the court's decision in *Moro*, benefits attributable to service already provided cannot be reduced. In addition, in the *Strunk* case, the court set-aside the "career guarantee" proposal because it effectively reduced the benefits based on service already provided and contributions made before the effective date of the change. This proposal would do the same. That is why the PERS Actuary's analysis shows only a reduction in the UAL rate.
- In addition, as the retiree funds in the benefits in force reserve are assumed to be growing at the assumed interest rate recommended by the PERS Actuary and adopted by the PERS Board, decoupling that assumed rate from the rate used to annuitize money match benefits would also violate the interpretation of the term "actuarial equivalency" by the Supreme Court in *Strunk*.
- Even the legislative counsel acknowledges that if the rates were decoupled, "[o]ne could argue that this difference in rates is unreasonable, especially because the use of the higher assumed interest rate would lower employer contribution rates, while the use of the lower assumed interest rate would reduce benefit payments.

- Finally, the PERS Actuary's analysis acknowledges that the savings attributable to this change could be greatly reduced as many money match recipients might be eligible to retire prior to the effective date of the change.

Extension of the Amortization Period

- The legislative leadership proposed amendments call for extension of the amortization period of the current unfunded actuarial liability for Tier 1 and Tier 2 members from 20 years to 22 years for the year 2019 and thereafter returns to the current rate effective January 2, 2020.
- Whatever amortization period is selected, the legislature must obtain assurance from the PERS Actuary that the period selected is within the range considered acceptable by the actuarial community to maintain the actuarial soundness of the plan. There are good and sound reasons why the choice of selecting the appropriate amortization period is delegated to the PERS Board with advice from the PERS Actuary.

Finally, as we have noted before, in both *Moro v. State*, 357 Or 167, 230-31, 351 P3d 1 (2015) and *Strunk v. PERB*, 338 Or 145, 207-08, 108 P3d 1058 (2005), the Oregon Supreme Court rejected the argument that "economic necessity or hardship" required the State of Oregon to reduce promised retirement benefits to public employees in order to fund other services like public safety and education. The Oregon legislature, therefore, must be cautious of any invitation to misuse our shared public responsibility to properly fund schools and public safety as an excuse for why PERS benefits "must" be cut. It should address other sources of revenue first.