March 29, 2019

Testimony of Melissa Unger, Executive Director, SEIU Local 503 on behalf of the Oregon PERS Coalition to the Joint Ways and Means Committee on Capitol Construction

When you talk about PERS, you are talking about real people. Real people like Barbara, a low-wage administrative assistant in a southern Oregon child welfare office, who currently plans to work until she is 77.

When the business community talks about “PERS Reform,” they never talk about how much their proposals will impact the retirements that people have been working towards and counting on. But we should not ever - ever - lose sight of that. We did an actuarial analysis for a child welfare worker who is an OPSRP member and taking her 6% contribution from her individual account program slashes it by 58 percent. She can never hope to make that loss up out of her salary and will leave her and her husband - who is also a child welfare PERS member - financially insecure in their retirements. These are just two examples of teachers, firefighters or other public employees who work for the public--many who took that job for stability and a strong retirement. State and local governments, school districts, firehouses and other public employers rely on them to deliver services, protect our communities, and teach our kids. Today we have about one-third of the child welfare workers we need to take care of the children and they can’t hire enough people to fill the vacancies left behind by people leaving the profession, much less hire more people to meet the needs of the kids. Overall about 30% of public employees are eligible to retire. Not only do the proposals you heard about earlier today hurt real people, they hurt school districts, local governments, and the state. It would be a mistake to make it harder to recruit and retain a qualified workforce.

Who are our members:

Our public employee members are the classified staff at universities who support students, the people at DHS and OHA who help families access services, the ODOT crews who work all night to keep our roads clear and many more.

Many of the jobs our members do are really hard jobs, whether it is an ODOT worker that worked 7 days a week, 12 hours a day to manage the snow in February or a child welfare worker who gets called in the middle of the night to protect a child that has no safe place to go. The folks who do this job do it for a lot of reasons, but it not commonly talked about that to be able to recruit people to do the work the state asks of them, they need to be good jobs because they are hard jobs.

72% of our members make between under $60,000 and well over 70% of our members are now on the OPSRP plan

Nationally more than 50% of the people who make similar amounts of money have no savings and the average retirement savings is between $29,000 and $65,000 all together. That should not be what we are striving for because we know that people that retire with no savings and no retirement end up needing state assistance later on.

We really do believe the stories and the impacts on hundreds of thousands of people gets lost in this conversation. We know that there is a challenge paying the employer rates, but we hope that the people it impacts play into the calculations as well.

We really worry about a conversation that once again is focused on benefit reductions as led by Tim Nesbitt and Ted Kulongoski. We were hopeful when this committee started that it was not focused on benefits since it doesn't solve the problem we face, but it seems we always end up back here. Aruna laid out why we believe their plans won't legally work, but they also just don't represent the system that we have.

Here are some facts that I think are often left out of this conversation:

- Oregon spends significantly less of state and local government spending than the national average and neighboring states. We spend 2.83% of total revenue - including school districts. The national average is 4.74% Washington: 3.19%. Idaho: 3.14%. California: 6.39%
- Oregon's rate of increase as a percentage of revenue is significantly less than the national average and our neighboring states, and unlike many other states, has actually recently decreased. Our increase as a percent of revenue went up 11% between 2007 and 2016. National average was a 45% increase. Washington: 123% increase. Idaho: 7.9%, California: 44% increase. Both of these statistics reminded me that we are one of many states dealing with this challenge of past benefits.
- Average annual benefit is $31,097, median annual benefit is $24,692 and average years of service is 25 years. Those numbers include mostly tier 1 and tier 2 retirees because not very many OPSRP members have retired yet.
- The UAL we currently have is going to be paid off in within 20 years and rates will start declining within the decade as Tier 1 and 2 people retire. The reason employer rates are high is because we are moving through the plan to pay down the debt. 20 years is below the national average for amortization rates and the OPSRP amortization rate is at 17 years.
- The system was funded at 111% in 2007; it was not changes to plans or benefits that causes the decrease in our funded status, it was that wall street crashed.
- It is policies like our amortization rate and the fact that we pay down the debt that make sure that we have a strong system, which is why we are far above average funding for pensions. Nationally the national average funding level is 66%, according to a report from PEW Research, which takes the most conservative approach. Oregon is funded at 80%, the 11th best funded system in the country.

OPSRP as designed uses most of the best practices about designing benefits in the country:

- It sets a target percent you want people to retire at with their pension-- 45% of their final average salary. Setting a target is a recommendation from the National Association of State Retirement Administrators.
- It is a hybrid plan, so someone's retirement is not solely based on their pension, but they also have a defined contribution plan as well. As the National Association of State Retirement Administrators noted, hybrid plans are designed to transfer some risk from the employer to the employee and more states in recent years are moving to them, we moved to ours in 2003. Legislators were ahead of the curve. Our hybrid plan has it where the employer funded the pension and the employee funds the defined

contribution. So it is a revision of history to say that workers don't contribute to their retirement, the defined contribution is meant to make someone's retirement package complete.
- The normal rate for OPSRP is only 8.5%.
- The retirement age is set at 65, many pension plans in the country are set at lower retirement ages.

Other states are just catching up to our changes that you all made decades ago (which is why our system is more well-funded than theirs). For instance:

- Many are just making COLA changes to 2%, where Oregon lowered the COLA to 1.25%.
- Many are increasing their retirement age, but many are still not at 65 and Oregon has been at 65 since 2003.
- Some are adopting hybrid plans like the one the Legislature adopted in 2003
- Many are decreasing their multiplier, most are still higher than the 1.5% Oregon adopted in 2003.
- For instance, Colorado has made many changes to their pension over the years because they are 58% funded and they still have a 2.5% multiplier. The reason we can compete with these states with a lower multiplier is because of the hybrid plan that we have.

With all of that said, we are not here today to suggest nothing should be done to tackle the UAL or to deny that we are facing increasing employer rates. We, like all of you, recognize the strain it puts on our state's budget. But benefit design changes are not going to solve those problems alone.

We believe that we should look at amortization rates and ways to think about this debt differently as suggested by previous speakers.

The business community says they want a solution, but we keep talking about only benefits, which even in the most draconian cuts would not be a solution to the UAL. We believe looking at SAIF reserves is at minimum an idea worth exploring that could do more to help employer rates and the UAL immediately than any benefit changes. Here are some facts about SAIF that are detailed in the report we submitted:

- A 1990 study found SAIF was using bad assumptions when computing reserve needs, and thus overestimating the amount of reserves it needed. In 2017, Oregon state law required SAIF have a minimum reserve of about $420 million. Beyond those mandated reserves, SAIF has a surplus fund that now exceeds $2 billion, far beyond what is needed to hedge against economic uncertainty.
- SAIF has some of the lowest rates in the country, we rank 46th in worker compensation rates.
- Because SAIF is holding more money than it needs, it has been paying out generous dividends to policyholders — over $1 billion over the past 7 years (2012 - 2018). The dividends are not included in the rate calculation that has us ranking 46th in the country in rates.
- In 2018 SAIF earned $524 million worth of premiums, for a net underwriting gain of $186 million. The same year, their investment gains were $159 million. SAIF returned $160 million in dividends to policyholders, equivalent to a 30% discount on premiums.

Essentially, SAIF dispersed all its investment returns during the year, and still grew the surplus by $116 million

- It's time for a dividend that honors the public investment too. As reported in The Oregonian, the state could take $1.4 billion from the SAIF surplus without changing its operating model. Policyholders would still enjoy low rates and SAIF would still have sufficient reserves.

While I am sure there many calculations on this, we believe it should be explored just as much as benefit designs that won't have much if any immediate impacts without decreasing the salary of hundreds of thousands of middle income Oregonians.

Frankly, some of the conversation feels like Deja Vu - and I think it's important to reflect on what we've learned from the past and how we got to this moment. As an example, as Aruna shared, many employees pay the 6% employee contribution to the Individual Account Program themselves.

Why do these 6% employee contributions go to the IAP instead of the old employee regular account to pay for the pension? Because of the 2003 PERS Reforms.

Here is what Gov. Kulongoski's representative, Margaret Hallock, said to the legislature back in 2003:

"I want to be very clear today that the Governor opposes a 401k type defined contribution successor plan. He supports a defined benefit or a hybrid plan that includes both a guaranteed pension at a lower cost and a companion 401(k) type defined contribution component. We need a pension system that yields a dependable pension for public employees, one that will attract and retain quality employees at an affordable cost, and a shared-risk, hybrid plan meets those criteria."

"With respect to the 6 percent member contribution, we agree in general with the proposal in HB 2003 to prohibit the member contribution being added to the regular accounts in the future. We believe this money should be shifted to a separate defined contribution account. Removing it from the regular PERS accounts halts the compounding of these contributions which then must be matched in the future. But, this 6 percent is the members' money and should remain a part of their ultimate pension system. We should not provoke cries that we are taking it away from them but should retain these funds in a companion account."

Now, the business community, supported by Ted Kulongoski, is asking the legislature for the opposite—i.e., the creation of a new 401(k) type defined contribution plan and redirection of the 6% employee contribution back to pay for the cost of future pension accruals.

In 2003, the Governor and the Legislature made drastic changes to people's retirements to solve a problem. Those change fundamentally changed the plans and are bringing costs down as proposed the reason it did not solve the challenge facing the state regarding employer rates and the UAL is because nothing on benefits can solve that problem. Seventy-two percent of the debt is due to people that have already retired and 22% is due to closed plans; cutting benefits doesn't change the math that we must pay for that debt and by further decreasing the benefits of the people that are in the revised plan doesn't change it. The plan that was written in 2003 is having the intended impacts.

We need to learn from the past. On behalf of the PERS Coalition, I want to be clear that we see our role as reminding this committee about the humans behind the numbers, and at the same time work with you to solve the real financial problem. We, like all of you, recognize the strain it puts on our state's budget. But we also know that cutting member benefits creates more problems than it solves and is not the answer.

NASRA Issue Brief:
State and Local Government Spending on Public Employee Retirement Systems

Updated March 2019

State and local government pension benefits are paid not from general operating revenues, but from trust funds to which public retirees and their employers contributed during retirees' working years. These trusts pay out nearly $300 billion annually to retirees and their beneficiaries, benefits that reach virtually every city and town in the nation.[i] On a nationwide basis, contributions made by state and local governments to pension trust funds account for 4.7 percent of direct general spending (see Figure 1).[ii] Pension spending levels, however, vary widely among states, depending on various factors, and are sufficient for some pension plans and insufficient for others.

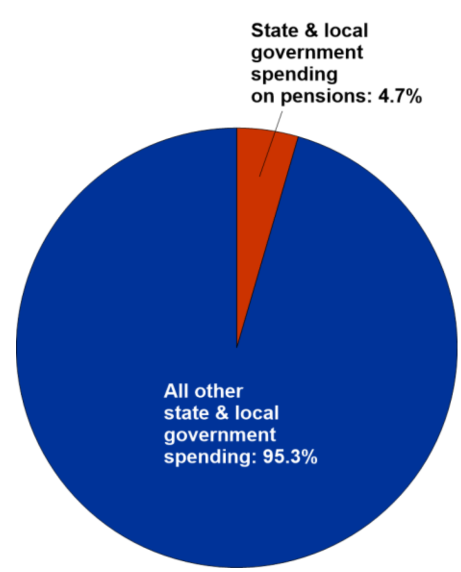
In the wake of the 2008-09 market decline, nearly every state and many cities have taken steps to improve the financial condition of their retirement plans and to reduce costs.[iii] States and cities changed their pension plans by adjusting employee and employer contribution levels, restructuring benefits, or both.

This update provides figures for public pension contributions as a percentage of state and local government direct general spending for FY 2016, and projects a rate of spending on pensions on an aggregate basis for FY 2017.

Nationwide Spending on Public Pensions

Based on the most recent information provided by the U.S. Census Bureau, 4.7 percent of all state and local government spending is used to fund pension benefits for employees of state and local government. As shown in Figure 2, pension costs rose sharply since FY 02 after falling equally sharply in the preceding years. These costs declined from 4.4 percent, in FY 88, to a low point of 2.3 percent in FY 02, and reached 4.7 percent in FY 16. State and local governments contributed, in aggregate, approximately $145 billion to pension funds in FY 17, a figure that is projected to decline slightly, from 4.74 percent to 4.73 percent of state and local direct general spending, as displayed in Figure 2.[iv]

Figure 1. State and local spending on public pensions as a percentage of total government direct general spending, FY 16

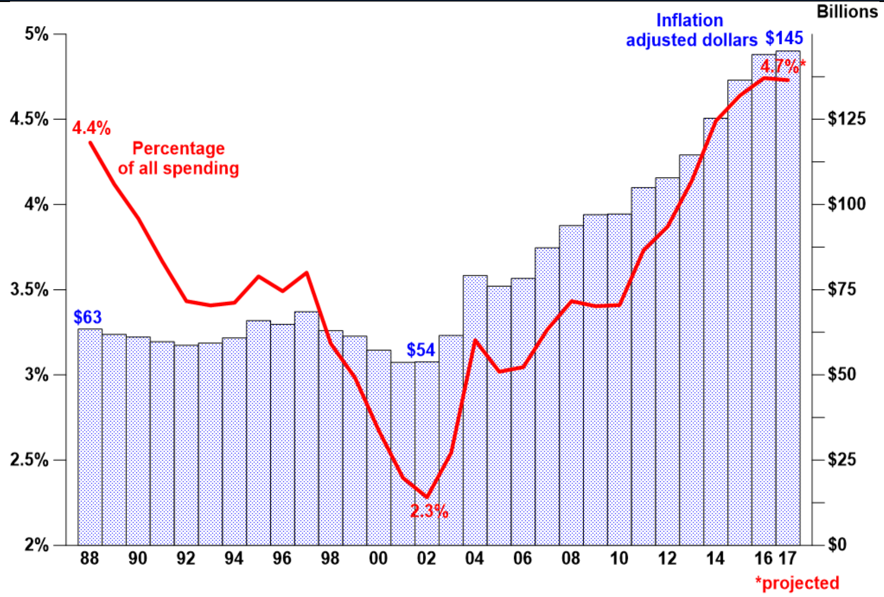


Compiled by NASRA based on U.S. Census Bureau data

The rate of spending in FY 16 increased by the smallest percentage since FY 10, and if the spending level projected for FY 17 is accurate, it will mark the first decrease—albeit slight—in the rate of pension spending since 2009. This development is notable especially when considering the improved effort among state and local governments in recent years to adequately fund their pension plans (see *NASRA Issue Brief: State and Local Government Contributions to Statewide Pension Plans: FY 16*).

Although pensions on average do not comprise a significant portion of aggregate state and local spending, as shown in Table 1, spending on pensions by states and political subdivisions varies widely among states, from 1.86 percent to nearly 10.0 percent. Some municipalities have reported higher pension costs as a percentage of their budget. One study estimates that total required spending on pensions could consume as much as 13 percent of one state's budget,[v] due mostly to historic underfunding of required pension costs and assuming a five percent investment return, which is considered by most investment experts to be conservative.

Figure 2. State and local pension contributions, in 2017 dollars, and as a percentage of state and local direct general spending, 1988-2017



Compiled by NASRA based on U.S. Census Bureau data
*Projected, based on estimated state and local government spending from National Association of State Budget Officers (NASBO) and U.S. Census Bureau data

Differences in Pension Cost Levels

The variation in pension spending levels among states is attributable to such factors as differences in benefit levels; variations in the size of unfunded pension liabilities; the level of commitment by the state and its local government plan sponsors to make required pension contributions; and the portion of the state's population that lives in an urban area. Most employees of state and local government participate in statewide retirement systems, which are the focus of this issue brief. In FY 17, state and local government contributions to statewide retirement systems accounted for 76 percent of total pension contributions, with the remaining 24 percent belonging to locally administered systems. As a percentage of total spending, cities have spent approximately 31 percent more than states on pensions over the 30-year period spanning 1987-2016.[vi] This higher commitment is largely attributable to the types of services delivered at the local level (i.e., more labor-intensive) and the resulting larger portion of local government spending goes toward salaries and related benefits compared to spending by states.

Differences in Benefit Levels

Pension benefit levels, and therefore required costs, vary among public pension plans, as plans in some states provide greater pension accrual rates than in others. As described below, this difference is particularly pronounced for the 25 percent to 30 percent of state and local government employees who do not participate in Social Security, as their pension benefit levels—and costs—generally are higher to compensate for all or part of the absence of Social Security benefits.

Size of Unfunded Liabilities

An unfunded pension liability is the projected difference between the pension benefits that have been accrued and the assets that have been set aside to pay for them. For a plan with a relatively large unfunded liability, the annual cost of paying down that liability can exceed the cost of benefits accrued each year. By contrast, the cost for a plan with no unfunded liability is simply the cost of benefits accrued each year. States with pension plans that have a relatively large unfunded liability will have higher pension plan spending levels, assuming the employer is making a good faith effort to pay its required contributions.

Social Security Coverage

Twenty-five to thirty percent of state and local governments and their employees make contributions to their retirement plan instead of to Social Security. This is the case for most to substantially all of the state and local government workforce in seven states, 40 percent of the nation's public school teachers, and a majority of firefighters and police officers.[vii] Pension benefits—and costs—for those who do not participate in Social Security are usually higher than for those who do participate, in order to compensate for the absence of Social Security benefits. This higher cost should be considered in the context of the 12.4 percent of payroll, or an estimated $2.6 billion annually,[viii] these employers and employees would otherwise be paying into Social Security.

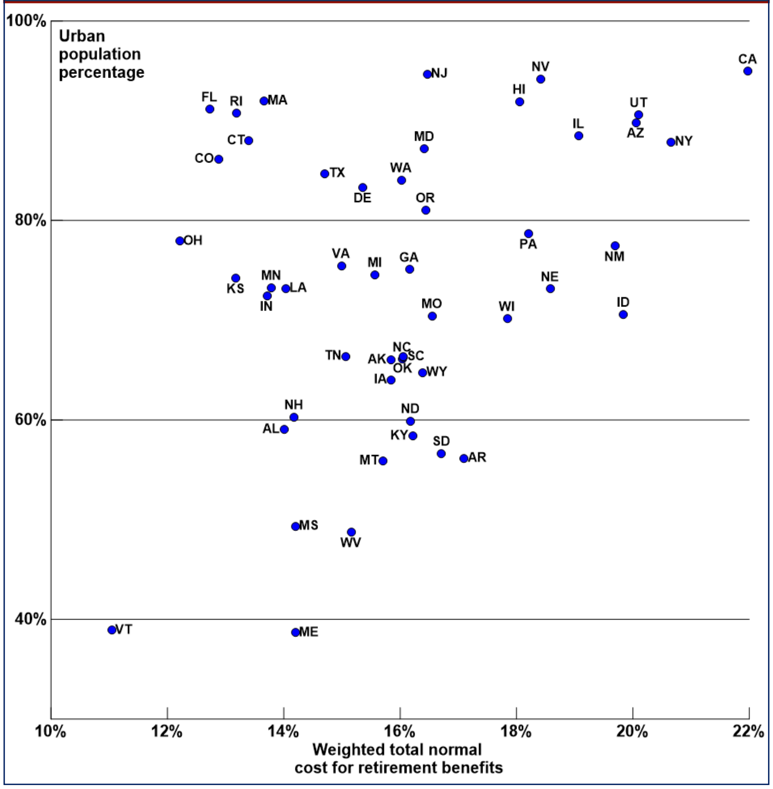
Level of Commitment to Pay Required Contributions

State and local government efforts to pay required contributions vary widely: some employers consistently pay the full Actuarially Determined Contribution, and others pay less.[ix] Whatever the cost of the pension plan, actual spending on pensions as a percentage of all spending is affected by employers' effort to fund the plan.

Urbanization

Another factor that appears to contribute to differences among states in pension costs is the extent to which the state's population resides in urban areas, or cities. Figure 3, which reflects analysis of state and local spending on pensions and the percentage of population residing in metropolitan areas within each state, suggests that, although not true in every case, states characterized by greater urban populations are more likely to experience higher costs for public pension benefits than states with lower urban populations.[x] This may be due to the fact that densely populated cities require more public services than are provided in less densely populated cities or rural areas. Also, tighter labor markets and higher cost of living – factors that may characterize densely populated cities – may also lead employers to offer higher retirement benefits in order to meet their workforce management objectives. Finally, pension benefits are just one component of total compensation, and other factors, such as salaries and health benefits for active and/or retired workers, may also be correlated with a state's degree of urbanization, and may also affect the difference in pension costs. Further research into the relationship of these factors may clarify these differences.

Figure 3. FY 17 State Retirement Benefit Costs and Urban Population Percentage



In addition to these causes of variation in pension costs among states, consistent comparisons of pension spending by local governments can be difficult to make because the fiscal relationship between each state and its political subdivisions is unique with respect to revenue, spending structure and taxing authority, and varies widely. For example, funding responsibility for K-12 education budgets ranges from primarily a state duty to one that is primarily a local responsibility. Likewise, revenue-sharing arrangements and the authority of local governments to tax and raise revenue also run a wide range. As with states, pension costs for municipalities also can vary widely.

Cost and Financing Factors

Public pensions are financed through a combination of contributions from public employers (state and local agencies) and public employees, and the investment earnings on those contributions. Since 1988, investment earnings have accounted for 62 percent of all public pension revenue; employer contributions, 26 percent; and employee contributions, 12 percent.[xi]

Employee Contributions

Because nearly all public employees are required both to participate in their employer-sponsored retirement plan and to contribute toward the cost of their pension benefit—typically four to eight percent of pay—most state and local government retirement plans are, in fact, mandatory savings programs. In recent years, many states have increased rates of required employee contributions. On a national basis, in fiscal year 2017, employee contributions accounted for nearly 28 percent of all public pension plan contributions, with employer contributions making up the remaining 72 percent.[xii]

Employer Contributions

A variety of state and local laws and policies guide governmental pension funding practices. Most require employers to contribute what is known as the Actuarially Determined Employer Contribution (ADEC), which is the amount needed to finance benefits accrued each year, plus the annual cost to amortize unfunded liabilities from past years, less required employee contributions. On a weighted basis, the average ADEC paid in recent years has been over 90 percent. Beneath this average contribution experience lies diversity: approximately 75 percent of plans in the Public Fund Survey[xiii] consistently receive 90 percent or more of their ADC.[xiv] This means that although a majority of plans have been receiving their required funding, some plans have not been adequately funded, which will result in higher future costs.

Leading national public sector associations established a Pension Funding Task Force, which in 2013 released its report *Pension Funding: A Guide for Elected Officials* urging policymakers to follow recommended guidelines for an actuarially determined contribution to government retirement systems.

Investments and Other Parts of the Financing Equation

The largest portion of public pension funding – over 60 percent for the 30-year period 1988-2017 – comes from investment earnings, which illustrates the major role this revenue source plays in determining pension costs (see *NASRA Issue Brief: Public Pension Plan Investment Return Assumptions*, February 2019).

In addition to the performance of pension fund investments, actuarial expectations regarding macro-economic and demographic events also affect the cost of the plan. These events include such changes as retirement rates, attrition and rates of hiring, and wage growth, which can be affected by salary cuts and layoffs. Additionally, legislatures in nearly every state have made changes to pension benefits and/or financing structures, in some cases reducing plan costs and long-term obligations.

Conclusion

Pension costs paid by state and local government employers vary widely and reflect multiple factors, including differing levels of public services, benefits, pension funding, and employer effort to pay required contributions, among other things. Employers in FY 17 contributed a total of $145 billion to pension benefits for employees, an amount that, in total, is a relatively small—but growing—part of state and local government spending.

Table 1: State and local government contributions to pensions as a percentage of all state and local government direct general spending, by state, FY 07 to FY 16

	FY 07 %	FY 07 to FY 16 %	FY 16 %
Alabama	2.84		3.26
Alaska	4.49		3.47
Arizona	2.38		3.94
Arkansas	3.48		3.56
California	4.42		6.39
Colorado	2.48		3.56
Connecticut	4.46		8.59
Delaware	2.17		3.04
District of Columbia	1.62		2.01
Florida	2.71		2.84
Georgia	2.33		4.24
Hawaii	4.21		5.55
Idaho	2.91		3.14
Illinois	3.55		9.97
Indiana	3.03		3.79
Iowa	1.91		2.61
Kansas	2.12		7.20[1]
Kentucky	2.80		4.06
Louisiana	4.46		6.48
Maine	3.22		3.07
Maryland	2.85		4.84
Massachusetts	3.41		4.90
Michigan	2.43		5.55
Minnesota	1.89		2.31
Mississippi	2.87		4.04
Missouri	3.62		5.36
Montana	2.53		3.75
Nebraska	1.89		2.66
Nevada[2]	6.08		7.69
New Hampshire	1.47		3.41
New Jersey	2.98		3.39
New Mexico	3.21		3.59
New York	4.63		6.78
North Carolina	1.10		2.27
North Dakota	1.55		2.23
Ohio	4.33		3.93
Oklahoma	4.23		4.64
Oregon	2.58		2.83
Pennsylvania	1.78		4.90
Rhode Island	5.13		6.28
South Carolina	2.47		3.13
South Dakota	1.87		1.86
Tennessee	2.78		3.15
Texas	2.44		2.85
Utah	3.19		4.94
Vermont	1.89		2.19
Virginia	3.92		4.47
Washington	1.43		3.19
West Virginia	13.99[3]		5.54
Wisconsin	1.59		2.13
Wyoming	1.40		1.99
US Average	**3.26**		**4.74**

Compiled by NASRA based on U.S. Census Bureau data

Table Notes

Charts in the FY 07 to FY 16 % column reflect the percentage spending for each of the 10 years within the timeframe.

Percent-of-spending is as of publication date; figures are subject to periodic revisions by the U.S. Census Bureau.

States where more than one-half of public employee payrolls are estimated to be outside of Social Security are italicized.

[1]Figure includes $1 billion in pension obligation bond proceeds from the State of Kansas' sale of a pension obligation bond to reduce the unfunded liability of the Kansas PERS.
[2]In addition to being a non-Social Security state, one-half of Nevada PERS employers' contribution is attributable to a non-refundable pre-tax salary reduction to fund the employees' portion of the contribution.
[3]In FY 07 the West Virginia Legislature committed $807 million in tobacco settlement funds to pay down the unfunded liability that had accumulated in the state's Teachers' Retirement System.

See also

National Governors Association, National Conference of State Legislatures, The Council of State Governments, National Association of Counties, National League of Cities, The U.S. Conference of Mayors, International City/County Management Association, National Council on Teacher Retirement, National Association of State Auditors, Comptrollers and Treasurers, Government Finance Officers Association, and National Association of State Retirement Administrators, "Pension Funding: A Guide for Elected Officials," 2013, https://www.nasra.org//Files/JointPublications/PensionFundingGuide(1).pdf

Center for Retirement Research at Boston College, "The Impact of Public Pensions on State and Local Budgets," October 2010, http://crr.bc.edu/briefs/impact-of-public-pensions-on-state-and-local-budgets/

Center on Budget Priorities and Policies, "Misunderstandings Regarding State Debt, Pensions, and Retiree Health Costs Create Unnecessary Alarm," January 2011, http://www.cbpp.org/cms/index.cfm?fa=view&id=3372

National Association of State Retirement Administrators, Issue Brief: Public Pension Plan Investment Return Assumptions, Updated February 2019, http://www.nasra.org/returnassumptionsbrief

National Association of State Retirement Administrators, Issue Brief: Employee Contributions to Public Pension Funds, September 2018, https://www.nasra.org/contributionsbrief

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[i] U.S. Census Bureau, Annual Survey of Public Pensions, https://www.census.gov/programs-surveys/aspp.html, 2017; see also "Economic Effects of Public Pensions," http://www.nasra.org/economiceffects

[ii] The U.S. Census Bureau defines direct general expenditures as all payments to employees, suppliers, contractors, beneficiaries, and other final recipients of governmental payments. Excluded from this category are expenditures for utilities, publicly owned liquor stores, employee retirement benefits paid from trust funds, and intergovernmental payments. Some state and local government spending is non-discretionary, and therefore not in competition for funds with other programs and services. Including non-discretionary spending would make the effect of pension spending appear smaller. In addition, some states and cities do not contribute the amount determined actuarially to adequately fund the plan.

[iii] Significant Reforms to State Retirement Systems, https://www.nasra.org/reforms & Selected Approved Changes to State and Selected Local Public Pensions, https://www.nasra.org/files/Compiled%20Resources/nasrapensionchanges.pdf

[iv] Projected spending for 2017 derived from actual state expenditures as reported by the National Association of State Budget Officers in the 2016-2018 State Expenditure Report (https://www.nasbo.org/mainsite/reports-data/state-expenditure-report p. 8 and projected increase in local government direct general spending, as provided by the U.S. Census Bureau https://www.census.gov/programs-surveys/gov-finances.html

[v] Center for Retirement Research at Boston College, "The Impact of Public Pensions on State & Local Budgets," supra

[vi] Author's calculations using public pension and state and local government finance data provided by the U.S. Census Bureau

[vii] Social Security Coverage @NASRA.org, http://www.nasra.org/socialsecurity

[viii] Author's calculation based on 30 percent of state and local government employees not participating in Social Security

[ix] The Annual Required Contribution Experience of State Retirement Plans, FY 01 to FY 13, https://www.nasra.org/arcspotlight and State and Local Government Contributions to Statewide Pension Plans: FY 14, http://www.nasra.org/adcbrief

[x] A moderate positive relationship is observed to exist between each state's weighted cost for pension benefits, with an adjustment for Social Security costs, and the percentage of residents in each state residing in Census-designated urban areas. Pension costs are sourced from Public Plans Data (https://publicplansdata.org/) , and are weighted for plans in each state and adjusted between 0-500 basis points depending on the percentage of public employees covered by Social Security in each state, based on expected present values of lifetime Social Security benefits and taxes paid as published in "Social Security and Medicare Lifetime Benefits and Taxes: 2018 Update," Urban Institute (October 2018). Urban density data are published by the U.S. Census Bureau and may be accessed at https://www.census.gov/geo/reference/ua/urban-rural-2010.html.

[xi] U.S. Census Bureau, Annual Survey of Public Pensions, https://www.census.gov/programs-surveys/aspp.html, 1988-2017

[xii] U.S. Census Bureau, Annual Survey of Public Pensions, https://www.census.gov/programs-surveys/aspp.html, 2017

[xiii] Public Fund Survey, http://www.nasra.org/publicfundsurvey

[xiv] The Annual Required Contribution Experience of State Retirement Plans, FY 01 to FY 13, https://www.nasra.org/arcspotlight

Oregon PERS Must Be Protected

By Tyler Bond ▪ September 2018

National Public Pension Coalition

NPPC

Executive Summary

- The median annual benefit for a PERS member is $24,062.
- Oregon made major structural changes to PERS in 2003 that have already reduced costs for employers.
- The current rising costs for PERS employers are the result of decisions made decades ago and are paying for benefits for employees who have already retired.
- Switching new hires to a defined contribution-only plan, like a 401(k), would do nothing to reduce the unfunded liability and would actually increase costs for taxpayers.
- Defined benefit pensions help recruit and retain public employees. Eliminating the pension component of PERS would make public employers less competitive.
- Few other states offer 401(k)-style plans to their public employees. The vast majority of states continue to offer defined benefit pensions.

History of the Public Employees Retirement System

Oregon has historically demonstrated a strong commitment to the retirement security of its public employees. This continues to be the case today. The Oregon Public Employees Retirement System (PERS) covers more than 168,000 active public employees[1] across the state. It also provides benefits to more than 136,000 retirees and other beneficiaries. The average annual benefit for a PERS member is $30,363 and the median annual benefit is $24,062.[2] These are modest amounts earned by public employees throughout a career in public service.

PERS was founded in direct response to the crisis of the Great Depression and the reality of elderly poverty. After a decade of debate, on March 26, 1945, Governor Earl Snell signed House Bill 344 establishing PERS. The legislation became effective more than a year later on July 1, 1946. PERS has not been frozen in time since 1946 though.

PERS currently follows the "three-legged stool" model of retirement: Social Security; an employer-provided defined benefit pension; and a defined contribution plan - similar to a 401(k) - funded by employee contributions. Oregon adopted this model following major legislation passed in 2003. As a result, pension benefits were reduced for Tier One and Tier Two employees and a third tier of benefits – the Oregon Public Service Retirement Plan -- was created. The 2003 legislation fundamentally changed the design of the plan to reduce costs for taxpayers while continuing to provide retirement security for public employees. Today, more than half of the public workforce earns this reduced benefit.

Pension funding, the current liability, and employer costs

From 1970 - 2015, Oregon PERS benefits were funded 73.4 percent by investment earnings, 21.1 percent by employer contributions, and 5.5 percent by employee contributions.[3] Following the 2003 plan changes, Oregon PERS reached a height of 111 percent of reserves needed to pay future pension liabilities in 2007, including employer side accounts.[4] After the recession hit, that number dropped to 80 percent in 2008.[5] This drop occurred because PERS earns such a high percentage of its revenues from investment earnings. PERS was more strongly impacted by the financial crisis as a result.

Today, Oregon has an unfunded pension liability of $22 billion.[6] It's important to note that Oregon does not allow employers to take "pension holidays" to stop payments, which has prevented some of the problems in other states. If investment assumptions are met, employer contribution rates to pay for the unfunded liability will rise over the next two biennia (two year budget cycles) then level out and start to decrease as more lower cost OPSRP members make up the retiree population.

There has been a very public debate in Oregon about the unfunded liability. Many of the proposals look to active public employees and future hires to pay the state's debt. For example, in 2013, the state reduced cost of living increases for future retirees. However, the majority of the unfunded liability - more than 70 percent - is to cover the cost of pensions for people already retired or who have left state service for other reasons.[7] The Oregon Supreme Court has been clear - those benefits cannot be reduced. Therefore, many of the proposals are centered on further reducing retirement benefits for today's workforce.

These proposals will not reduce the unfunded liability to any significant degree, will reduce the retirement security of current public employees, and will have unintended consequences, based on math and the experiences of other states.

Switching to 401(k)s for new hires is not the answer

Anti-pension ideologues have argued that more major changes are needed for PERS. Specifically, they have argued for switching to a defined contribution-only, 401(k)-style plan. This would be a mistake. Making additional significant changes is both unnecessary and potentially harmful. The changes made in 2003 are working and have reduced costs for the plan while still ensuring retirement security for public employees. One way to measure the cost of a public pension plan is by looking at the "normal cost", which is the cost to fund benefits earned in a single year by active employees. The normal cost for employees in OPSRP for the current biennium is only 8.56 percent of payroll and for the next biennium is only estimated to increase to 8.92 percent of payroll.[8]

Pension critics have pointed to increased costs for employers in PERS, but those costs need to be put in context. Current employees and future hires are not driving the cost increases for employers. The legacy debt from decisions made decades ago are a major driver of the current unfunded liability in PERS. Changes included in the 2003 legislation have been reducing costs for PERS employers.

Changes included in the 2003 PERS legislation:[9]

- Increasing the retirement age
- Decreasing the retirement formula
- Eliminating Money Match
- Eliminating guaranteed rate of return on all employee contributions made after January 1, 2004
- Eliminating inclusion of sick leave or vacation in Final Average Salary (FAS) calculation
- Capping salary at $200,000 with adjustments at the level set by the IRS

Switching to a 401(k)-style plan would not eliminate the costs PERS has already accrued. Closing a pension plan does not magically get rid of existing unfunded liability. Just like any other type of debt -a credit card, a mortgage, student loans- the debt already accrued by PERS in the form of unfunded liability must be paid. Switching to a 401(k)-style plan will just make it more difficult to do this.

Experience of other states on switching to a 401(k)-style plan

States that have moved public employees to a 401(k)-style, defined contribution plan have experienced harmful consequences, which is why so few states have done it. Only three states currently offer a defined contribution-only plan exclusively to their public employees. At least eight other states offer public employees some choice among defined benefit pension plans, defined contribution plans, or hybrid retirement plans. In these states, public employees overwhelmingly choose the pension plan.[10] For the states that only offer a defined contribution plan, these plans end up costing taxpayers more and leave public employees without retirement security.

West Virginia was the first state to make the switch - and the first to switch back. In 1991, West Virginia closed its defined benefit pension plan for teachers and placed all new teachers in a 401(k)-style plan. Over the course of the next fifteen years, teachers in the 401(k)-style plan failed to save enough to retire securely. As of April 30, 2005, the average account balance was just $41,478, and only 105 of the 1,767 teachers over age 60 had balances over $100,000.[11] This was largely because teachers saving in the defined contribution plan earned lower investment returns than those earned by the pension plan. Studies have shown that defined benefit pension plans consistently earn higher investment returns than 401(k) plans.[12]

In the early 2000s, West Virginia began to study a return to a defined benefit pension plan. These studies showed the state could provide equivalent benefits at half the cost under a pension plan, due to the inherent efficiencies of pensions, such as longevity risk pooling, a balanced investment portfolio, and lower fees.[13] The state reopened the closed teacher pension plan to new teachers beginning in 2006. Two years later, the state gave teachers in the 401(k)-style plan the option to switch to the reopened pension plan and more than 78 percent did.[14]

In the years since, the funding level for the teacher pension plan has steadily risen with new members paying into the fund and more consistent contributions from the state. The funded level has increased from just 25 percent in 2005 to 58 percent as of July 31, 2013.[15] Reopening the pension plan has also saved money for taxpayers. West Virginia is expected to save $22 million because so many younger participants in the 401(k)-style plan switched to the reopened pension plan.[16]

In 1997, Michigan closed its defined benefit pension plan for state employees. For the past two decades, all new state employees have participated in a 401(k)-style defined contribution plan. This has had at least two very serious consequences. First, it has failed to create retirement security for state employees. The state Office of Retirement Services reported in January 2017 that among state employees older than age 60 and with at least fifteen years of service, the median savings in the defined contribution plan is only $36,000.[17]

Second, closing the pension plan caused the unfunded liability in the plan to skyrocket. When the plan was closed, it was overfunded at 109 percent; fifteen years later, it was only 60 percent funded.[18] Without future contributions for new participants in the plan, it is difficult to maintain strong funding levels. Public pension plans can invest on an infinite time horizon because new members are joining and contributing to the plan as older members are retiring and collecting their benefits. This allows the plan managers to maintain an optimal investment portfolio that balances high- and low-risk investments. When a plan is closed and contributions from new members stop, the plan managers must shift to more conservative, low-risk and low-return investments. This lowers the overall returns for the pension fund. On average, pension plans earn anywhere from two-thirds to three-fourths of their revenue from investment earnings.

Were Oregon to follow a similar path as West Virginia and Michigan, it would experience similar negative consequences. Oregon PERS has historically received a significant percentage of its revenue from investment earnings (73.4 percent). This is a testament to the good work of the Oregon Investment Council (OIC) and the leaders of the plan. However, if new hires were switched to a defined contribution-only plan, that would cut off new revenue for the plan and would force the OIC to switch to more conservative, lower return investments. This would be the case even if current active employees were forced to contribute to the pension plan because eventually all of those employees would retire and the plan would lose that source of revenue while still paying out benefits to retired employees and other beneficiaries.

401(k)-style plans cause recruitment and retention problems

Closing a defined benefit pension plan doesn't only cause problems for retirement security and funding status. It also makes it more difficult for cities and states to recruit and retain public employees. Public pensions have long been an effective workforce management tool for public employers from school districts to fire departments to state governments. They are an attractive benefit for employees who are willing to commit to a career serving their communities. When public pensions are eliminated as a workplace benefit, it makes public employers less competitive and, therefore, less able to recruit and retain the most qualified employees.

Retaining public employees throughout their careers benefits taxpayers. Teachers, for example, dramatically increase their effectiveness during the first several years of teaching.[19] Studies have shown that most teachers do not reach their peak effectiveness until five years of teaching.[20] Teachers then maintain this effectiveness throughout their careers, so having more experienced teachers in the classroom raises the overall quality of teaching at a school.

When it comes to public safety professions such as policing and firefighting, there are large sunk costs that go into training new employees in these professions. One estimate suggested it costs a quarter million dollars to train a new police officer.[21] Taxpayers want to be sure they are getting a good return on their investment for paying for this training. Offering a defined benefit pension to career police officers and firefighters guarantees that the public will receive a return on investment for the money paid to train these professionals. It also means the public will be protected by experienced public safety officers who know how to handle dangerous situations.

Some states have learned these lessons the hard way. Oregon experienced more than 12,000 retirements in 2003, the year major pension changes took effect.[22] That was more than twice the number of retirements than the year before or the year after. Utah closed its pension plan in 2011 and placed new hires in a hybrid defined benefit-defined contribution plan. The state has struggled to hire new police officers and firefighters since the plan changed with hundreds of vacant positions statewide.[23]

A similar situation occurred in Palm Beach, Florida, when it moved from a pension plan to a hybrid plan. That change affected not just future hires, but current employees.[24] Since Palm Beach already had so many police officers eligible to retire, many of them left as soon as the changes passed since they would no longer be able to earn their full pension benefit.[25] Many police officers also received their training in Palm Beach, but then transferred to other departments where they could still receive a full pension. After four years of the hybrid plan, the Palm Beach City Council went back to a defined benefit pension for public safety officers to address the severe shortage. Despite this reversal, the damaging effects of the hybrid plan still linger. Palm Beach continues to experience high levels of attrition among its police officers and many point to the pension plan changes of the past decade as the cause.[26]

A harmful proposal: taking the current employee contribution to their individual account to fund the pension

Six percent of Oregon public employees' salaries go into their defined contribution account, also known as their Individual Account Program. Whether the 6 percent contribution is paid by the employee or the employer is part of the collective bargaining negotiations for unionized public employees. Most members of the state government workforce pay the 6 percent themselves, for example.

One of the most draconian proposals on the table takes away the 6 percent contribution from the employee's defined contribution account and moves it into the pension plan with no corresponding increase in pension benefits. Here's what that would mean:

- <u>Drastically reduced retirement benefits:</u>
  The effect of this proposal on the future retirement security of public employees would be devastating. It would, in effect, freeze the defined contribution accounts at their current level of funding to be only interest earning accounts. This would have the most devastating effect on employees with 10 or fewer years of service because there has not been enough time for them to significantly save in those accounts to generate adequate interest returns. During the 2017 legislative session, there was testimony from younger workers that showed their retirement accounts would be cut between 40 and 75 percent.

- <u>No reduction in the unfunded liability:</u>
  As noted above, the unfunded liability is driven by more than 70 percent from people already retired or no longer in state service. Taking money from today's workforce to pay the state's liability does not solve the problem because contributions from current employees cannot be used to pay down the unfunded liability.

Oregon should maintain its commitment to retirement security

The impact of the financial crisis and ensuing Great Recession must be considered in regards to PERS. Before the financial crisis, PERS was more than 100 percent funded. PERS took a major financial hit during the financial crisis as did so many others, both institutional and individual investors. The uneven economic recovery from the recession has made it difficult for PERS to return to its previously high funded status.

According to the most recent reports, PERS today is funded at 80 percent when including employer side accounts. These accounts were created in 2003 to allow employers to set aside money to pay down the unfunded liability in PERS. In 2017, the plan earned a 15.3 percent rate of return on its investments, more than double its expected rate of return.

PERS also delivers a great value for Oregon taxpayers. Historically, almost three-fourths of the revenue in the PERS fund comes from investment earnings. This is a great return on investment. According to the National Institute on Retirement Security, every taxpayer dollar invested in PERS supports $6.11 in total economic activity in Oregon.[27] This adds up to more than $5 billion annually in economic activity that supports more than 36,000 jobs.[28]

The National Conference on Public Employee Retirement Systems recently examined whether public pension plans are net revenue generators for state and local governments. Their analysis concluded that public pensions in Oregon generate significant amounts of tax revenue for state and local governments: more than $2 billion.[29] Public employers in Oregon are not just recouping what they spend on PERS pension benefits, they are receiving billions of dollars beyond what they contribute through tax revenue. This is because the investment returns for the PERS pension fund generate such high returns and fund the majority of the PERS pension benefit. A move to a 401(k)-style plan for public employees would eliminate this additional tax revenue because fewer investment returns would be generated and more money would be lost to fees and other costs of money managers and financial institutions.

Conclusion

The best path forward for Oregon is to continue to allow the reforms of 2003 to work. Additional changes and cuts to pension benefits would truly harm the retirement security of public employees. It would also harm local communities throughout the state by undercutting crucial economic activity and denying valuable tax revenue to local governments.

Forcing new public employees into a 401(k)-style defined contribution plan would have unintended consequences that would harm Oregon taxpayers and public employees. As the experiences of other states have shown, closing a pension plan and switching to a 401(k)-style plan increases the unfunded liability in the pension plan. This would actually increase the cost to employers as they would have to contribute more to pay down the unfunded liability. It also poses real challenges for recruiting and retaining qualified public employees.

Oregon's population keeps growing- it needs good public employees![30] Public pensions are valuable tools for recruiting and retaining quality public employees. Further unnecessary changes would harm the ability of state and local governments to attract the best and the brightest.

Endnotes

[1] These employees fall into three tiers: Tier 1 (members hired before January 1, 1996); Tier 2 (members hired between January 1, 1996 and August 28, 2003); and OPSRP (members hired on or after August 29, 2003). OPSRP members hired after 2003 now represent the majority (58 percent) of the total active member population in the system.

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[3] Ibid., Pg. 21.

[4] Ibid., Pg. 13.

[5] Ibid.

[6] Ibid.

[7] Ibid.

[8] Uncollared System-Wide OPSRP Normal Cost for this biennium is 8.56% and is projected to be 8.92% for the next biennium. PERS Board Packet, 8-3-18, Milliman Presentation p. 35.
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[10] Brown, Jennifer Erin and Matt Larrabee. *Decisions, Decisions: An Update on Retirement Plan Choices for Public Employees and Employers*. National Institute on Retirement Security. August 2017. Pg. 5.

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[12] Munnell, Alicia, Jean-Pierre Aubry, and Caroline Crawford. *Investment Returns: Defined Benefit vs. Defined Contribution Plans*. Center for Retirement Research. December 2015.

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[21] K. Ryals, 2017(Feb. 22), "City's move to 401(k) pensions is big mistake as Palm Beach showed," *Florida Times Union*, Jacksonville, FL.

[22] Oregon Public Employees Retirement System. *PERS: By The Numbers*. May 2017. Pg. 2.

[23] M. Shenefelt, 2018 (June 2), "Retention, recruitment 'killing' Utah police and fire departments," *Daily Herald*, Provo, UT.

[24] Oakley, Diane. *Retirement Reform Lessons: The Experience of Palm Beach Public Safety Pensions.* National Institute on Retirement Security. February 2018.

[25] This is similar to the situation in Oregon. 70,335 additional PERS active and inactive members are currently eligible to retire by age or service, according to *PERS: By the Numbers* (May 2017), p. 2.

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[27] Brown, Jennifer Erin. *Pensionomics 2016: Measuring the Economic Impact of Defined Benefit Pension Expenditures.* National Institute on Retirement Security. September 2016. Pg. 21.

[28] Ibid., Pgs. 18 and 22.

[29] *Unintended Consequences: How Scaling Back Public Pensions Puts Government Revenues at Risk.* National Conference on Public Employee Retirement Systems. May 2018. Pg. 17.

[30] S. DuBois, 2017 (November 17), "Oregon's Population Keeps Rising, Now at 4.1 Million," *U.S. News & World Report.*

Research Brief on SAIF's Surplus

Daniel Morris, MS, PhD • March 27, 2019

Improving workplace safety is one of the great public health achievements of the 20th century.(1) In 1913, the Bureau of Labor Statistics documented approximately 23,000 industrial deaths, equivalent to a rate of 61 deaths per 100,000 workers. In 2017, there were 3.5 deaths per 100,000 workers in the U.S., a remarkable decline.(2) Rates fell even more in Oregon. Oregon's State Industrial Accident Commission cataloged 543 worker deaths from 1915 to 1919, a rate of 265 per 100,000 workers.(3) In 2017, there were 60 fatal occupational injuries in Oregon, roughly 3 deaths per 100,000 workers.(4) **If Oregon's rates were the same today as they were 100 years ago, 5,000 more people would die from work-related injuries each year.**

Improved workplace safety is no accident. It took decades of work and legislative action to reduce rates of occupational injuries and illnesses. In addition to the efforts of workers, employers, and unions, taxpayers also invest a great deal to improve workplace safety, through the Occupational Safety and Health Administration (OSHA) and other state and local public health agencies. These gains are good for workers and their families, and profitable for employers.

In 1910, New York became the first state to pass a workers' compensation law. Instead of requiring workers or their families to sue employers for damages, these laws compensated injuries at a fixed rate.(5) Oregon workers' compensation law took effect in 1914, creating a state agency, the State Industrial Accident Commission, to run a workers' compensation insurance program.(6) Over time Oregon's workers' compensation laws were expanded to cover more employers; today Oregon requires most employers to carry workers' compensation insurance for their employees. Employers either purchase insurance or become self-insured.

In 1980 the state spun off its workers' compensation insurance program into a non-profit public corporation, the State Accident Insurance Fund (SAIF). As a non-profit, SAIF doesn't pay taxes—that helps it keep rates low and grow its market share. In 1987, SAIF had 37.9% of Oregon's workers' compensation market; in 2015, SAIF had 51.7%. The State of Oregon purchases insurance from SAIF.

In the mid-1980s, Oregon had the country's 6th highest workers' compensation premiums rates. But following the passage of workers' compensation insurance reform bill SB 1197 during a special session in 1990, premium rates fell rapidly. By 1994 Oregon's rates were below the U.S. median, and by 1998, Oregon ranked 38th highest in the country.(7)

Figure 2. Oregon's rate ranking among 51 jurisdictions, 1986-2018

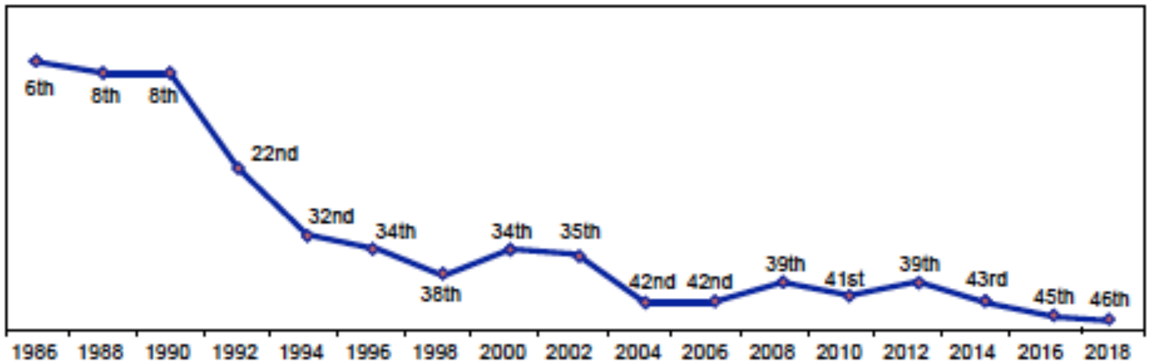
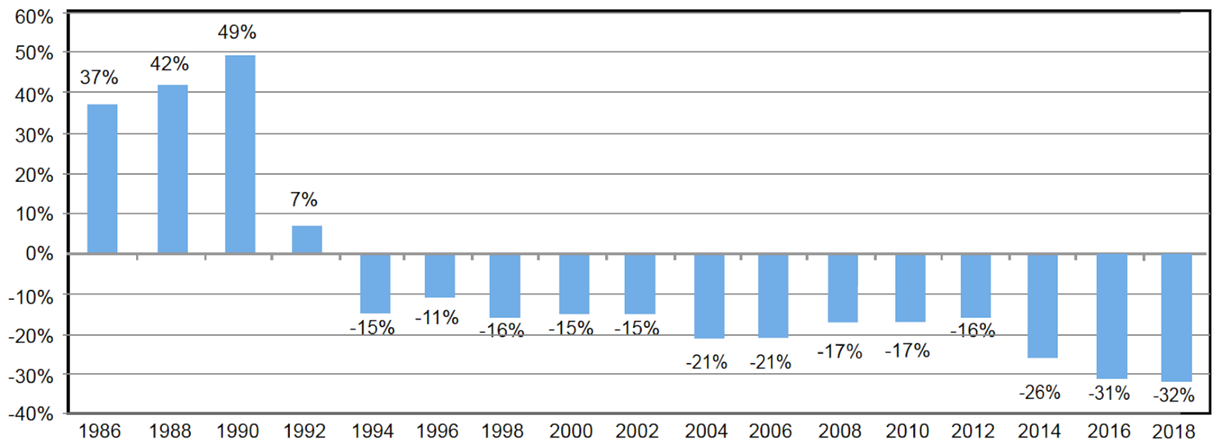


Figure 5. Oregon premium index rate relative to national median value, 1986-2018



Charts are from the DCBS Oregon Workers' Compensation Premium Rate Ranking Report for 2018

The 1990 reforms did many things, such as expanding requirements for safety committees and increasing OSHA staffing. But it also redefined which injuries would be compensated, by stating that the injury must be the major contributing cause of the need for treatment. In addition, SB 1197 stated that a claim was compensable only as long as the compensable condition remained the major contributing cause of the need for treatment.(8) The result was a significant reduction in the number of workers' comp claims. Subsequent legislation in 1995, SB 367, developed this even further. A study commissioned by DCBS in 2000 concluded these restrictions cut benefits to workers and costs to employers by over 13%.(9)

In 1987, there were 41,033 accepted workers' compensation claims in Oregon, 3.7 per 100 workers. By 2015 there were only 19,572 claims, 1.1 per 100 workers. In 1987, 44% of claims involved time off work; in 2015, only 35% did. With fewer compensated occupational injuries, and less time off when injuries do occur, SAIF doesn't have to pay out as much, and insurance premiums drop. Today, Oregon employers pay the 6th lowest workers' compensation premium rates in the nation.(7) That represents real cost savings, and makes Oregon a more attractive place to do business.

In 1987, Oregon employers averaged $4.36 in workers' comp premiums per $100 in payroll. In 2018, they averaged $1.15 per $100 in payroll, a huge decline. If rates were the same today as in 1987, Oregon employers would be paying billions of dollars more per year in premiums.

SAIF, like other insurance companies, is required to maintain financial reserves at certain levels. These funds create a cushion, guard against catastrophic events (such as financial market downturns or significant changes in claim costs), and ensure fiscal soundness. A 1990 study found SAIF was using bad assumptions when computing reserve needs, and thus overestimating the amount of reserves it needed.(9) In 2017, Oregon state law required SAIF have a minimum reserve of about $420 million. Beyond those mandated reserves, SAIF has a surplus fund that now exceeds $2 billion, far beyond what is needed to hedge against economic uncertainty.

Because SAIF is holding more money than it needs, it has been paying out generous dividends to policyholders — over $1 billion over the past 7 years (2012 - 2018), and $2.25 billion back to 1987. In 2018 SAIF earned $524 million worth of premiums, for a net underwriting gain of $186 million. The same year, investment gains were $159 million. SAIF returned $160 million in dividends to policyholders, equivalent to a 30% discount on premiums. Essentially, SAIF dispersed all its investment returns during the year, and still grew the surplus by $116 million.

It is important to note the state premium rankings do not account for dividend payments. Oregon's rates are low even without additional rebates.

In 1982 the Oregon legislature appropriated $81 million from the SAIF surplus to help deal with a budget crisis. After losing a lawsuit, the state had to repay the money. In response to the legal challenges, the legislature changed the law to make it legal to divert the SAIF surplus.(10) Today Oregon's legislature has the power to reallocate a portion of SAIF's surplus to other purposes without fear of lawsuits.

As reported in *The Oregonian*, the state could take $1.4 billion from the SAIF surplus without changing its operating model.(11) Policyholders would still enjoy low rates and SAIF would still have sufficient reserves.

Having a large surplus is no guarantee of low rates. California's State Compensation Insurance Fund has its origins in 1914, just like SAIF. California has the second highest workers' comp premiums in the country, though SCIF's surplus is larger, relative to net premiums earned, than SAIF (surplus is 5.1 times the amount of net premiums vs. 3.8 times).(12) On the other hand, North Dakota has the lowest premiums in the country. The surplus held by the North Dakota Workforce Safety & Insurance Workers Compensation Fund is less than three times the premiums earned.(13) SAIF doesn't need such a large surplus to keep premiums down.

SAIF has low rates and a surplus in large thanks to a century of public investment in workplace safety. The surplus has already generated a lot of extra payouts to businesses that already enjoy some of the lowest workers' comp rates in the country. It's time for a dividend that honors the public investment too.

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Governor considers taking $1.4 billion from SAIF workers comp surplus to reduce pension costs

Updated Feb 20, 2019;
Posted Feb 18, 2019

Gov. Kate Brown is considering tapping the state's workers compensation insurance corporation to defray pension costs for schools.

By Ted Sickinger| The Oregonian/OregonLive

Gov. Kate Brown is considering selling the state's workers compensation insurance corporation or tapping its substantial capital surplus to hold down future pension costs for money to accomplish the goal on its own. But if Brown moves forward with such a plan, it would be her boldest move yet to rein in the runaway costs of the Public Employees Retirement System. It's also one that would face substantial blowback from the business community.

Chris Pair, a spokesman for the governor's office, said Monday that "our office will not be providing comment."

The proposal to tap SAIF, the state's 100-year-old employer-funded workers compensation agency, was initially floated in 2017 by a task force Brown set up to look for ways to reduce PERS' mammoth unfunded liability**.** That liability now stands at about $26.6 billion.

At the time, the idea of selling SAIF or tapping its surplus was staunchly opposed in some quarters of the business community**.** Oregon businesses enjoy some of the cheapest workers compensation rates in the country, and employers who are policyholders of SAIF receive large annual dividends from investment earnings on the capital surplus that the governor may look to tap.

Transferring that surplus or selling the company might raise costs for workers compensation, erasing one of the few competitive advantages that Oregon offers business opponents have said.

At the same time, schools, municipalities and public agencies around the state are wallowing in pension debts and the relentless cost increases they are driving. Collectively, school districts have a funding deficit with PERS of more than $9 billion. They face a $375

This at a time when Brown has been promising to increase school funding to lengthen the school year, bring down class sizes and address Oregon's high school graduation rates, which are the second lowest in the country. Critics have said it would be a mistake to pump billions more into schools when much of that money would go to increased pension costs, not to the classroom.

Brown has already acted on one of the PERS debt-reduction task force's suggestions, setting up new "side accounts" at PERS that could, if adequately capitalized, offset some of the contribution increases employers are facing. One of the accounts is for the benefit of schools, which will be funded solely by the state. The other is designed as an incentive fund for all public employers that aims to provide a 25 percent match on new funds that employers deposit with the pension system.

The problem is that the side accounts are only minimally funded so far. And while Brown included another $100 million appropriation for the school fund in her proposed budget, that is really a drop in the bucket. PERS' actuary estimates that contribution rates will go up by about 7 percent of payroll in 2021 -- the systemwide equivalent of $1.6 billion -- if PERS' investments deliver their assumed rate of return of 7.2 percent this year.

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PERS has calculated that it will take a side account deposit of about $435 million to offset each percentage point increase in schools' contribution rates. That implies that Brown might need to inject about $3 billion into the school fund to hold pension costs constant in 2021. That comes on top of the $2 billion she's looking to provide in new funding for 2019-21 by raising corporate taxes.

SAIF was established as a state agency in 1914 and was made a public corporation in 1980, with a board appointed by the governor. Its non-taxable status gives it a big leg up in the marketplace, and it underwrites more than half the workers compensation market in Oregon. That competitive advantage irks competitors, but in 2004, voters decisively rejected a ballot measure supported by Liberty Northwest Insurance Corp. that would have abolished SAIF.

In 2017, SAIF took in almost $526 million in premiums and had $393 million in losses and underwriting expenses. Its $133 million underwriting profit, coupled with another $171 million in investment income, enabled the company to pay back policy holders 30 percent of their premiums - $160 million - while growing its already substantial capital surplus to nearly $1.9 billion.

In fact, SAIF has paid those "dividends" every year since 2010, returning more than $1 billion to policyholders while watching its surplus continue to grow.

SAIF is subject to minimum capital and surplus requirements established by the National Association of Insurance Commissioners. According to an annual independent audit, its minimum capital and surplus amount was $314.3 million at the end of 2017. That compares to an actual "net position" of $2.1 billion in the audit, or a $1.9 billion surplus listed in SAIF's annual report.

SAIF officials were not available Monday to explain the difference, but the surplus is a potentially attractive asset to backstop the struggling pension system. Records obtained by The Oregonian/OregonLive show that the governor, along with her chief of staff, Nik Blosser, and her legislative director, Elana Pirtle-Guiney, met on Jan. 10 with retired insurance executive and University of Oregon booster Pat Kilkenny as well as John von Schlegell, a founder of the Portland-based private equity firm Endeavour Capital, to discuss ways to reduce the pension system's unfunded liability.

Emails and Blosser's notes from the meeting show that those options included selling SAIF or tapping its capital surplus. (Emails from Von Schlegell also mentioned another option raised by the PERS task force – privatizing the state's liquor retailing monopoly.)

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Blosser’s notes indicate that based on SAIF’s current capital surplus and loss ratios, the state could take $1.4 billion from its surplus to fund PERS without changing its operating model. A sale of the company might garner a premium, the notes said.

Following the Jan. 10 meeting, Kilkenny also put the governor’s office in touch with Tony Ursano, president of TigerRisk Partners, an insurance mergers and acquisition specialist out of New York.

“We would love an opportunity to come out to Salem and introduce ourselves, our firm and our preliminary perspectives on SAIF,” Ursano said in a Jan. 17 email to Blosser. “I believe we are uniquely positioned to offer the State of Oregon insightful, thoughtful and objective advice about the strategic alternatives available to SAIF.”

Emails indicate that the follow-up meeting may have taken place in early February and included Oregon’s chief financial officer George Naughton and his team.

Business groups are prepared to push back on such a proposal.

Mike Salsgiver, executive director of the Associated General Contractors of Oregon, said his members would oppose any effort to use SAIF’s mandated reserves to pay down a structural deficit in the pension system.

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“We do not support sweeping accounts to pay off a debt the state has incurred” elsewhere, he said. “You could do that and you still wouldn’t solve the problem. It doesn’t make sense to use a program that’s working well to address a much deeper structural problem.”

Sandra McDonough, chief executive of the state’s biggest business organization, Oregon Business & Industry, said she met with the governor last week and asked about the strategy for containing pension costs, but got few details and no mention of SAIF.

“We would be concerned with any proposal that would undermine the fiscal integrity of SAIF,” she said. “We’ve told the governor we look forward to talking through what she’s thinking about. She indicated she’d have something relatively soon.”

Correction: An earlier version of this story said the new PERS side accounts for public employers were still empty. They have received only minimal funding so far.