ANALYSIS

Public Employees Retirement System
SB 1566 (2018)

Analyst: John Borden

Request: Acknowledge receipt of a report on SB 1566 (2018).

Analysis: The Public Employee Retirement System (PERS) is directed by statute to report during each regular session to the Joint Committee on Ways and Means on the status of the School Districts Unfunded Liability Fund, Employer Incentive Fund, and the Unfunded Actuarial Liability Resolution Program that were established by SB 1566 (2018). SB 1049 (2019) made technical statutory changes to SB 1566, as well as provided funding for the Employer Incentive Fund and the Unfunded Accrued Liability Resolution program (discussed below).

Background
Employers have the option to make voluntary lump-sum payments to PERS that are in addition to the employer's required contribution. With few exceptions (i.e., payment of transition liability), lump-sum payments are deposited into "side accounts," and are used to offset a portion of the contributing employer's PERS contribution rate as of a date selected by the employer or July 1 of the year following publication of the actuarial valuation for the year in which the additional deposit is made, according to an amortization schedule. Side account balances are never entirely utilized in a single biennium. Employers without a side account pay the employer contribution rate without any offset.

Side accounts, which are tracked separately from other employer reserves in the Oregon Public Employees Retirement Fund, are assets of the PERS system and reduce a participating individual employer's net unfunded pension actuarial accrued liability. Once deposits are made into side accounts, employers are unable to withdraw or repurpose the funds. Employees have no vested interest in these side accounts as they are an asset of a participating employer not employee. The state also has no ability to access (or re-appropriate) side account balances, as they are held in statutory trust accounts.

School Districts Unfunded Liability Fund
SB 1566 established a School Districts Unfunded Liability Fund (SDULF). The PERS Board is required to create this pooled side account for school districts and proportionately distribute the side account among all school districts as an offset to employer contribution rates.

Since the SDULF was established (SB 1566, 2018), there have been no expenditures from the fund. The PERS Board has chosen not deploy deposits to offset school district pool rates until the balance reaches a threshold of one percent of the school district's payroll multiplied by an amortization factor of approximately 5.16%. For the 2023-25 biennium, the threshold would be a $466.5 million, based on the school district's payroll valuation ($9 billion or $90.4 million) multiplied by the 5.16% amortization factor. PERS reports that the balance of the SDULF is $46.3 million (as of October 2022); however, the balance does not take into account the anticipated transfer of $89 million in excess estate tax for the 2021-23 biennium. At present, no further deposits into the SDULF are forecasted, other than interest earnings. Based on an estimated balance of $135.3 million, the SDULF is $331.2 million short of the

PERS threshold and therefore no distribution or school district rate offset from the fund is anticipated for the 2023-25 biennium.

In addition, three SDULF revenue provisions are slated to repeal or sunset during the 2023-25 biennium: excess capital gains (limited to calendar years 2019, 2021, and 2023); excess estate tax (limited to calendar years 2019, 2021, and 2023); and excess debt collections (December 31, 2024). Of these revenue streams, only excess estate tax ($89 million) and the unclaimed property transfer ($45.5 million) have or are expect to produced revenue for the SDULF. There have been no revenues deposited into the account from either excess debt collection or capital gains other than account interest earnings. The unclaimed property transfer provision will sunset during the 2027-29 biennium on January 2, 2027. The SDULF itself has no sunset date.

Employer Incentive Fund

SB 1566 established an Employer Incentive Fund (EIF) to be used for a 25% match program for employer side accounts, which are for pre-paid employer contributions held in trust by PERS. Once deposited, side accounts funds may not be withdrawn except for the payment of employer contributions. All PERS entities, including school districts, community colleges, and public universities, are eligible to participate in the matching funds program. Employers must meet the following criteria: (a) deposits could only be cash and not from borrowed funds; (b) the minimum contribution of $25,000; (c) an employer must have no transition liability; and (d) an employer must participate in the Unfunded Actuarial Liability Resolution Program (discussed below). The EIF sunsets on July 1, 2042.

The revenue sources of the EIF is currently only Lottery Funds are from sports betting and one-time General Fund. The Department of Administrative Services - Office of Economic Analysis sports betting revenue forecast for the EIF (December 2022), is $15.3 million for the 2021-23 biennium, $21.7 million for the 2023-25 biennium, $27.8 million for the 2025-27 biennium, $29 million for the 2027-29 biennium, and $32 million for the 2029-31 biennium. PERS also is reporting a 2021-23 Lottery Funds ending balance of $341,000. Sports betting revenue for the EIF sunsets on December 31, 2041. One-time General Fund matching contributions have totaled $81.4 million. PERS made no 2023-25 request for General Fund for the EIF.

In contrast to the SDULF, the EIF has expended funds from the account. For the 2019-21 biennium, the EIF increased employer side accounts by $342.4 million, which includes $272.8 million in employer contributions, $64.8 million in state General Fund match, and $4.9 million for payment of transition liability payments. After the conclusion of the inaugural EIF application cycle in the 2019-21 biennium, there were 44 employers with $148 million in employer contributions that remained on a waitlist pending $36.6 million in state matching funds becoming available. After accounting for $19.5 million in forecasted sports betting revenue (March 2022), the 2022 Legislature appropriated $17.1 million in supplemental General Fund to fully fund the matching funds requirement for waitlisted entities.

PERS reports note the following:

> PERS does not anticipate opening a new round of EIF application until all waitlisted employers who participate are matched and the fund reaches a minimum of $25,000,000. Based on current budget projections, we plan to open the next application period in 2025.

Employer contributions and matching funds will be reflected in 2025-27 biennium, rather than the 2023-25 biennium, Board adopted employer contribution rates, due to the Board's rate setting and actuarial valuation schedules.

Unfunded Accrued Liability Resolution Program

The measure creates an Unfunded Actuarial Liability Resolution Program (UALRP) to assist an employer in the development of a plan to improve the employer's funded status. PERS has, after an initial slow start, completed implementation of this program. PERS employers had to meet the following criteria to participate in the UALRP: (a) identify their combined valuation payroll; (b) estimate the UAL amount and funded status using existing resources available online; and (c) use the web-based PERS' Employer Rate Projection tool to review the affect their intended lump sum payment and potential EIF match would have on their rates and contributions projected out over the next ten biennia. PERS completed the acquisition and deployment a more comprehensive and advanced Employer Rate Projection Tool that was funded as part of SB 1049 (2019). PERS is also now able to provide UAL information to state government agencies and entities as well as UAL educational guides.

Side Account Lump-Sum Payments

Apart from the reporting requirement, SB 1566 allows an entity making a lump sum cash payment of $10 million or higher into a side account to choose an amortization period of six years, 10-years, 16-years, or 20-years. There is also the option to defer when the side account takes effect; however, these become non-EIF matched side account contributions. After non-EIF contributions totaled $107 million during the 2019-21 biennium, there have been no further lumpsum payments under this provision of the law. Of additional note is that only the Port of Portland chose the rate deferral option with a rate offset date of July 1, 2029 and that is coupled with a ten-year amortization period.

Legislative Fiscal Office Recommendation: The Legislative Fiscal Office recommends acknowledging receipt of the report.

Request: Report on the status of the School Districts Unfunded Liability Fund, the Employer Incentive Fund, the unfunded Actuarial Liability Resolution program, and the extended amortization options from side accounts as stipulated in Senate Bill 1566 from the 2018 Session, by the Public Employees Retirement System.

Recommendation: Acknowledge receipt of report

Discussion: The Public Employees Retirement System (PERS), as directed by Senate Bill 1566 from the 2018 Legislative Session, is required to report by February 1 of each odd year the status of the unfunded liability fund accounts, the actuarial liability resolution program and the extended amortization options established in the bill.

School Districts Unfunded Liability Fund (SDULF) - is a pooled side account intended to provide rate relief to school districts, public charter schools and education service districts. There are four potential revenue sources if earnings are available to fund the SDULF. Of the four sources listed below:

- The Department of State Lands indicated that there would be no funds transferred from interest on unclaimed property for 2023,
- The Office of Economic Analysis (OEA) is forecasting a transfer of $89 million from estate taxes in 2023,
- The OEA is indicating no transfers are expected from Capital Gains taxes for 2023, and
- The Department for Administrative Services indicated no transfer expected from debt collections, because the provision is suspended in biennium with a projected kicker.

PERS has indicated that based on the existing SDULF fund balance of $46.4 million, plus the anticipated 2023 deposit of $89 million from estate taxes, funding will not be sufficient to provide an offset for the School District side account pool. In order for the school district pool to provide a one percent rate offset the fund would need a minimum of $580 million. Among the four revenue sources intended to provide rate relief, the dedication of excess estate tax and excess capital gains tax proceeds to the SDULF are scheduled to sunset in 2023.

The Employers Incentive Fund (EIF) - PERS is reporting that all employers (41 in total) on the first and second waitlists will be able to receive their EIF match totaling $36.4 million. In order for employers to fully utilize the match, they must make their full lump sum deposit by March 1, 2023. As of the 2022 Legislative Session, the EIF matching funds will come from the Lottery Funds, sports betting proceeds. PERS is not expecting another round of EIF matching funds to be available until 2025.

Unfunded Actuarial Liability (UAL) Resolution Program - PERS launched an Employer Rate Projection Tool in 2021. This tool provides employers the ability to modify payroll contributions rates and predict how these changes will affect their contributions. In addition, PERS created a series of guides to help employers better understand the system and provide more context to the resource they receive when forecasting and budgeting. The guide to “Understanding Pension Obligation Bonds” is expected to be published this year to assist employers.

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February 3, 2023

The Honorable Senator Elizabeth Steiner, Co-Chair
The Honorable Representative Tawna Sanchez, Co-Chair
Joint Committee on Ways and Means
900 Court St NE
H-178 State Capitol
Salem, OR 97301-4048

Nature of the Request

As required by Senate Bill 1566 (2018), PERS is providing the status of the School Districts Unfunded Liability Fund, the Employer Incentive Fund, the Unfunded Actuarial Liability Resolution Program, and extended amortization options for side accounts of $10 million or more as of December 2022.

Agency Action

School Districts Unfunded Liability Fund

The School Districts Unfunded Liability Fund (SDULF) is a pooled side account intended to provide rate relief to all public school districts, public charter schools, and education service districts. The SDULF has four defined revenue sources: interest on unclaimed property from the Department of State Lands, proceeds from estate taxes, proceeds from capital gains taxes, and proceeds from debt collection.

- Department of State Lands advises that there will be no funds transferred from interest on unclaimed property to the SDULF in 2023.
- The Office of Economic Analysis (OEA) forecasts a transfer of $89,000,000 from Estate taxes will occur in 2023.
- OEA advised no transfer is expected from proceeds of Capital Gains taxes as the growth did not exceed the 10-year trend, as required by statute.
- The Department of Administrative Services advised no transfer is expected from debt collection.

As of November 30, 2022, the SDULF has a balance of $46,366,763. Despite the anticipated deposits in 2023, the funding is not sufficient to provide an offset for the School District Pool. As of the December 31, 2021, valuation, the School Districts Pool has a combined valuation payroll of $4,141,800,000; $580,000,000 is the minimum amount the fund requires to provide a 1% rate offset to the pool.

Proceeds from estate taxes and capital gains taxes as an income source for the SDULF sunset in 2023. The transfer of proceeds from debt collection as an income source for the SDULF sunsets in 2024. The transfer of interest on unclaimed property as an income source for the SDULF sunsets in 2027.

Employer Incentive Fund

The Employer Incentive Fund (EIF) provides a 25% match to employers making a lump sum payment from non-borrowed funds of at least $25,000. This lump sum payment may be used to establish a new side account or as a payment into an existing side account and is subject to the limitations stated in the statute. The first 90 days of the application period are dedicated to employers whose UAL as a percentage of payroll that exceeds 200%; the application is subsequently open to all employers.

During the 2022 Regular Session, the Legislature apportioned an additional $17,250,000 in General Fund dollars to the EIF. The Legislature's intent is for PERS to use existing EIF funds of $19,500,000 (from sports-betting proceeds) and these new funds to offer matches to all EIF waitlisted employers and clear the EIF waitlist. In order to accomplish this objective, the prior EIF administrative rule was updated at the May 27, 2022, PERS Board meeting. This change extended the payment date to March 31, 2023.

Each waitlist employer is permitted, but not required, to deposit side account funds sufficient to receive their approved EIF match. In addition, any qualifying side account deposits made between the establishment of the waitlist and the availability of additional funds will receive an EIF match up to the lesser of the amount approved and 25% of the deposit.

PERS will provide matching funds to all employers on the waitlist who make their full deposit by March 31, 2023. (Any employers who miss this deadline will forfeit their matching funds.) As of December 31, 2022, PERS has distributed $30,118,738 from EIF to match 21 employers on the waitlist. Approved EIF matches totaling $6,317,842 remain to be distributed to the final 20 employers on the list.

PERS does not anticipate opening a new round of EIF application until all waitlisted employers who participate are matched and the fund reaches a minimum of $25,000,000. Based on current budget projections, we plan to open the next application period in 2025.

Unfunded Actuarial Liability (UAL) Resolution Program

Senate Bill 1049 modified the UAL Resolution Program (UALRP) to include the development of funding plans to improve the employers' funded status and to manage contribution rates. The bill also requires all PERS-participating employers to participate in the UALRP, whereas previously this was a requirement for employers only participating in EIF.

PERS launched an enhanced Employer Rate Projection Tool in 2021. This version of the tool provides employers the ability to modify payroll or contribution rates and predict how these changes will affect their contributions over time. The revised tool offers enhanced modeling of new side accounts as well. An ongoing maintenance plan provides annual update of projection factors that reflect the current actuarial valuation data for each employer.

PERS has created a series of guides to help employers understand the fundamentals of the system and provide context to the resources they receive when forecasting and budgeting.

Those guides are:

- *Guide to Understanding Your Rate*
- *Guide to Understanding Your Valuation*
- *Guide to Understanding Unfunded Actuarial Liability*
- *Guide to Understanding Pooling*
- *Guide to Financial Modeling*

The *Guide to Understanding Pension Obligation Bonds* will be published in 2023.

Extended Amortization Options

Senate Bill 1566 (2018) introduced additional amortization options for side accounts of at least $10,000,000. These include the ability to select a shortened amortization period of six, 10, or 16 years rather than the standard amortization period of 20 years. Employers also have the ability to select a deferred rate offset date.

Summary

Employer Programs have been well received by PERS-participating employers despite budgetary uncertainty. Employers appreciate incentives to proactively manage their contribution rates and appreciate the engaged role PERS has had in addressing knowledge gaps.

Action Requested

PERS requests the Committee acknowledge receipt of the report.

Legislation Affected

No legislation is affected by this request.

Sincerely,

Kevin Olineck, Director
Oregon Public Employees Retirement System