

# Oregon's public pension deficit comes under attack

By Ted Sickinger  
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PORTLAND, Ore. — Just how bad is Oregon's public pension funding crisis?

Bad enough that Rukaiyah Adams, the normally polished investment professional who is vice chair of the Oregon Investment Council, made an impassioned appeal for Oregon leaders to address the fund's \$22 billion deficit, not pass it to future taxpayers.

"My call to the Legislature and to the governor is for leadership on this, and I mean right now," Adams said during last Wednesday's joint meeting of the Oregon Public Employees Retirement System board and the citizen panel that oversees its investments. "This is becoming a moral issue. We can't just talk about numbers anymore."

The numbers are bleak. Oregon's pension system owes billions of dollars more to retirees than it has, and the last major attempt to fix the problem was shot down in courts.

This month, cities, school districts and others will find out how much more they'll pay to help prop up the system. Higher pension costs could come at the expense of funding for other needs, including social services, infrastructure investments and education programs.

Last week's meeting was extraordinarily candid. And it provided a brief, reality-based peek behind the financial charade taking place not only in Oregon's pension system, but also in systems across the country.

Experts openly acknowledged they're understating the magnitude of Oregon's problem. They're relying on optimistic assumptions about investment returns. And they're holding down required pension payments below what's needed to keep pace with the debt, to avoid eviscerating school and government budgets across Oregon.

"We're beyond crisis," Katy Durant, chair of the Oregon Investment Council, said in an interview after last week's meeting. "We should have been addressing this 20 years ago and it's just been building. It's a little bit like a Ponzi scheme. Sooner or later it's going to catch up with you."

A handful of lawmakers are set to meet Wednesday in hopes of jumpstarting a conversation on pension reforms in the 2017 legislative session. They have a list of ideas already vetted by state lawyers. They say the ideas could help plug an \$885 million budget hit looming over the next two years, fallout after the Oregon Supreme Court rejected most of a package of pension reforms negotiated in 2013.

But Democratic leaders, including Gov. Kate Brown, so far say they're not interested. In an interview this week, Brown said she saw pension costs as a very important issue, but

"from my perspective, that list is not legally viable and not likely to result in significant financial savings."

It's a similar story from Senate President Peter Courtney, D-Salem, and House Speaker Tina Kotek, D-Portland. They insist there are no more money-saving moves that could be both legally viable and economically significant.

Remaining pension reforms would also mean cutting pay and retirement benefits for current state workers — which would alienate Democratic benefactors in Oregon's public employee unions.

Kotek and Brown are both backing a controversial, union-backed proposed tax increase on large corporations on the fall ballot. Measure 97 would raise \$3 billion a year by taxing 2.5 percent of certain corporations' sales over \$25 million. But Brown also said that revenue should be spent as supporters have promised: to beef up spending on schools and social services.

So why is the pension debt becoming a bigger issue now?

There's the sheer size of the deficit - \$22 billion - at record heights even after a seven-year economic recovery. It's no longer a cyclical problem that a string of big investment returns could erase, board members agreed last week. The imbalance of assets and liabilities is now structural.

With interest rates at historical lows, financial markets aren't delivering the high returns needed to sustain the system. Public employers - financed by taxpayers - aren't contributing enough to make up the difference. And public employees are no longer required to contribute to their pensions.

"This problem is not going away," said John Thomas, a Eugene benefits consultant who chairs the pension system's board. "It is what it is. The math is the math...It's getting to a point now that it's difficult for people to accept what these numbers are."

As it stands, pension payments cost government agencies and school districts across the state about \$2 billion every two years, and they're panicking about the \$885 million, or 44 percent jump, in required payments over the next two years.

"That's just next biennium," PERS Director Steve Rodeman, said at the meeting. "There's going to be one just like that in the next biennium and very similar to that, under almost any scenario, in the one after that."

In other words, to pay down the debt over 20 years, the increase in pension payments over the next two years should be more than three times higher, or nearly \$2.7 billion.

But, Rodeman said, "You bump up against reality in terms of how quickly employers can adjust to the higher rates they're going to need to be charged."

So the pension board artificially "collars"

required contributions. In essence, by not making the needed minimum payments, the board is borrowing from the pension fund, adding interest costs and making the overall liability even larger.

The investment council, meanwhile, is bumping up against a different reality. Its members believe the system's assumptions for how much its investments will earn are unrealistic. The assumed rate of return is 7.5 percent a year. Over the last 10 years, pension fund investments have earned just 6.2 percent annually. Last year it was 2.1 percent. So far, this year, it's 4.6 percent.

"Can't we rip the band-aid off and deal with reality?" Durant, the outgoing chair of the council asked at the meeting. "We keep stacking more and more on because we're unwilling to deal with reality."

It's a math problem facing pension systems around the country. Pension payments are determined, in large part, by the income the system assumes from its investments.

If a pension system lowers its assumed returns, it has to make up the difference to keep its promise to retirees. That, in turn, requires higher payments — at the expense of other priorities — from government employers.

In Oregon, even a quarter-percentage-point reduction in the assumed rate would increase employers' payments by about \$400 million every two years. Oregon already made that change last year, lowering what had been a 7.75 percent rate.

Getting the rate to 7 percent would be painful, and 6.5 percent excruciating. But Thomas, the pension system's chair, said the rate would likely be reduced again next year.

The discussion during last week's meeting turned to how else the state could address the liability. Durant and Adams said Brown and lawmakers could make extra payments, worth billions of dollars, to pay down the liability.

Lawrence Furnstahl, a pension system board member and the chief financial officer of Oregon Health & Science University, said the state should consider refinancing its obligation.

Oregon State Treasurer Ted Wheeler said the pension board and investment council should both be more active in advising the Legislature on debt-solving strategies — though that would push them into the realm of policy making.

"We cannot solve this problem alone," Wheeler, who takes office as Portland's mayor Jan. 1, hastened to add. "There is leadership required outside of this room."

Sen. Tim Knopp, R-Bend, and Sen. Betsy Johnson, D-Scappoose, plan to get the conversation rolling at a special meeting in the Capitol. They'll kick off the session with a presentation from Rodeman, who's expected to share some of the same numbers he presented

last week.

The lawmakers have already submitted potential money-saving reforms to the Legislative Counsel's Office, which said many of the ideas would withstand a legal challenge. They include capping final salaries in pension calculations at \$100,000, changing the interest rate used to calculate benefits under the system's money-match formula, and requiring employees to help pay for their pensions.

Brown said the state could waste time and money pursuing reforms that could be thrown out in court. She said the best bet to solve Oregon's pension problems "is to increase investment returns."

She's focused on one major proposal in 2017, a plan to restructure the Oregon Treasury's investment management division that could potentially save fees paid to Wall Street firms.

Treasury estimates the overall savings over 20 years at \$1 billion. The idea has failed three times already and was opposed in 2015 by Courtney.

"This is something on my radar screen and I think it's critical," Brown said.

Johnson and Knopp, meanwhile are waiting for the pension system's actuary to analyze how much each of their ideas might save. They say their proposals could both cut the system's debt and save public employers big money each budget cycle.

"I'm not wed to any concept," Johnson said. "These are some ideas. There may be many other ideas. But the responsible thing to do is begin the conversation."



(Courtesy photo for The Illinois Valley News)  
Rukaiyah Adams, vice chair of the Oregon Investment Council.

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