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## Summary

Oregon's Public Employees Retirement System suffers from a structural flaw that should be corrected for all new employees. A simplified 401K-style defined contribution plan would attract new workers, eliminate future debt liability, and help pay down the current unfunded liabilities.

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## Fix PERS for new hires

*By Angela Eckhardt*

Oregon's Public Employees Retirement System is finally getting the public scrutiny it deserves thanks in part to gubernatorial candidate Ron Saxton. Unfortunately that's only half the battle. For much of the past decade state and local elected officials have recognized the coming crisis in PERS. Some have even tried their hand at reform, but their efforts have left the system's flawed structure intact. Let's talk about real solutions.

Last year Cascade Policy Institute asked one of the nation's foremost experts on state pension reform, Peter J. Ferrara, J.D., to help devise a comprehensive reform plan for PERS. Because current employees claim a contractual right to the system in place when they were hired, Cascade asked Ferrara to propose reforms that would only apply to new hires.

After months of research and discussions with ranking PERS officials, Ferrara confirmed our fears: by his judgement, Oregon has the most complicated public employees pension system in the country. Even limiting reforms to new employees would be a dramatic improvement. A little background will show why.

The traditional model for retirement systems is the defined benefit plan, where the worker and employer agree on a benefit amount to be paid at retirement based on a formula of salary times years of service times some multiplier. Good investment years balance out bad investment years because the employer is only ever on the hook for a specified benefit regardless of how hot the economy is.

Over the last 25 years the private sector has moved sharply away from defined benefit plans to defined contribution plans, where contributions are made into 401K-style accounts and retirement checks are based on the accumulated funds in the worker's account at the end of his career.

The problem with PERS is that it is both a defined benefit and a defined contribution system. At retirement, workers receive benefits calculated under either the defined benefit "Full Formula" method, or the defined contribution "Money Match" method, whichever is higher. Ferrara calls this a "Heads workers win, tails PERS loses" formula.

PERS must wait for each worker's retirement before determining how to calcu-

late his benefits, which is why the total PERS shortfall—and therefore the budget of every city, county, school district and state agency—is covered in question marks. The most recent shortfall estimate is \$8.5 billion.

Ferrara recommends creating a simplified defined contribution plan for all new PERS-covered employees. Workers and employers would each contribute five percent of wages, for a total of ten percent, into a personal account for each worker. Workers would choose a mutual fund or money manager from a list approved by the state, for the investment of account funds. Benefits would be financed by the accumulated account funds at retirement, leaving no liabilities for government employers and taxpayers.

New hires would enjoy savings on their contribution portion, greater investment freedom, complete portability and no vesting requirement. Many current workers might opt into this system. PERS currently favors older, long-term workers at the expense of younger, short-term workers. For new employees who never envision themselves growing old, much less staying with one employer for 30 years, 401K-style reforms would make government employment more competitive with the private sector.

The five percent employer contribution would be less than the current average of 10.7 percent. This savings would initially be devoted to reducing and eliminating unfunded liabilities.

Other states have joined the private sector trend toward defined contribution retirement plans. Oregon should likewise immediately begin the transition to a fully funded defined contribution retirement system, starting with all new PERS covered employees.

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*Angela Eckhardt is director of publications at Cascade Policy Institute, a Portland, Oregon think tank. Professor Ferrara's report Pension liberation for Oregon is online at [www.cascadepolicy.org](http://www.cascadepolicy.org).*

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Please contact:

Angela Eckhardt  
Director of Publications  
Cascade Policy Institute  
813 SW Alder Street, Suite 450  
Portland, Oregon 97205

Phone: (503) 242-0900  
Fax: (503) 242-3822

[www.cascadepolicy.org](http://www.cascadepolicy.org)  
[angela@cascadepolicy.org](mailto:angela@cascadepolicy.org)