



CASCADE POLICY INSTITUTE

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## Summary

The pension plan for Portland's police and fire employees currently has a \$1.1 billion unfunded liability. The city's politicians have not moved to reform the system, instead relying on a Ponzi-like funding scheme that will require future taxpayers to pay the costs of today's fire and police services. The City should fix the plan for new hires and get its fiscal house in order.

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***“The plan’s funding relies on a bizarre notion of equity that says tomorrow’s taxpayers should pay for the costs of police and fire services enjoyed by today’s residents.”***

## No accountability: Portland’s Mini PERS

By *Matt Roehr, CFA*

Accountability is the buzzword being used by advocates of a three-year income tax hike in Portland. City and Multnomah County officials say trust us, give us more money, and we will hold the schools accountable. It's hard to believe local officials when they talk about "accountability." For years, Portland City Commissioners have sat on a Mini PERS problem and done nothing about it. This unfunded fiscal time-bomb has now grown to nearly \$1.1 billion, or over \$2,000 for each man, woman, and child living in Portland.

While the Oregon Public Employee Retirement System is hogging the limelight, the growing unfunded liability of Portland's Fire and Police Disability and Retirement Fund (FPD&R) deserves closer attention. This plan is not a conventional, actuarial-based plan that is supposed to be fully funded at all times, rather the FPD&R uses "pay-as-you-go" funding—charging taxpayers for retiree benefits on-the-fly, as they are incurred.

Like the similarly financed Social Security System, this is the quintessential pension-Ponzi scheme, whereby today's politicians make grand promises of benefits to police and fire employees, leaving future generations of taxpayers to pay the costs. City Commissioners are well aware of the problem, but have not acted. In 1998, when talk of reforming the pension plan came before the city council, Commissioner Jim Francesconi said, "Is there anyone in the room willing to raise \$350,000 to educate the public on this? Absent that, I just can't see it."

The current liability is large and growing. According to the latest report by EFI Actuaries, the current unfunded liability is approximately \$1.1 billion; it has grown at about a five percent rate over the last ten years. Expenses are forecasted to increase at about four percent per year for the next 60 years (including new hires)—pushing the present value of the projected liability to about \$1.4 billion.

To put this in perspective, if the projected liability were added in one lump sum to today's property tax bills, property tax rates would have to more than quadruple. Bonding the deficit would spread the burden out over future years, but

would still add to property tax rates—putting upward pressure on rental rates, downward pressure on home values and pushing the city closer to state property tax rate limitations.

The current pension funding system makes little economic sense. Financed by property taxes, if the fund levy cannot cover the plan's annual expenses, the city's general fund makes up the difference. The plan's funding relies on a bizarre notion of equity that says tomorrow's taxpayers should pay for the costs of police and fire services enjoyed by today's residents. There is no logical basis for this approach; it is simply a politically expedient way to tax people who haven't been born yet or who cannot yet vote. For a city that constantly parrots that "our children are our future," the current policy is particularly callous.

A solution is available. The city should move to cap the existing liability, move the plan to a more fiscally sound footing, and provide more freedom to plan members. To do so, the city should terminate the defined benefit plan for new hires and set up a defined contribution plan; this would effectively cap the existing unfunded liability at the \$1.1 billion figure. New hires would have the freedom and responsibility to save a portion of their salary, likely with an employer match and within the limits of both their personal and the City's current budgets, and invest the funds according to their own risk tolerance. An employee's retirement nest egg, like most in the private sector, would depend on their savings and performance of their investments. If workers retire or move, they can take their accumulated savings with them.

Current workers and retirees would remain under the old plan, but reform would at least begin to move some of the burden off of future taxpayers and force some long overdue fiscal discipline within the city's budget. Portland taxpayers are faced with an unaddressed Mini PERS. Before the city embarks on another grand scheme to get into businesses it has little experience managing (such as sports arenas and public utilities), Portland ought to sell money-losing assets and put its current financial house in order. Perhaps taxpayers would then have reason to trust the promises of accountability.

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