



H.F. 45

(Murphy, M., by request)

S.F. 215

(Bakk)

Executive Summary of Commission Staff Materials

<i>Affected Pension Plan(s):</i>	Proctor Volunteer Firefighters Relief Association
<i>Relevant Provisions of Law:</i>	Minnesota Statutes, Section 424A.03, Subdivision 1
<i>General Nature of Proposal:</i>	Exemption from the service pension uniformity provision
<i>Date of Summary:</i>	March 4, 2015

Specific Proposed Changes

- Permits the Proctor Volunteer Firefighters Relief Association to increase lump-sum service pensions for prospective years of service only after December 31, 2013, without being required to uniformly apply that increase to such pensions for years of service rendered before the date of increase.

Policy Issues Raised by the Proposed Legislation

1. Appropriateness of legislative action as compared to possible internal solutions.
2. Appropriateness of special legislation rather than general legislation.
3. Extent of administrative burden for the Proctor Volunteer Firefighters Relief Association and for the State Auditor.
4. Prospect for local law approval by the city.

Potential Amendments

Technical Amendments:

H0045-1A eliminates the Subdivision 1 reference to exempt the Proctor Volunteer Firefighters Relief Association from all of Minnesota Statutes, Section 424A.03, specifically the penalties of noncompliance imposed in Subdivision 2.

H0045-2A amends the proposed legislation's headnote and title for clarity, specifies what years the exemption applies to, and amends the effective date by removing the "day following enactment" option because the city of Proctor cannot knowledgeably approve the legislation prior to enactment.

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TO: Members of the Legislative Commission on Pensions and Retirement

FROM: Rachel Thurlow, Deputy Director *RT*

RE: H.F. 45 (Murphy, M., by request); S.F. 215 (Bakk): Permitting the Proctor Volunteer Firefighters Relief Association to Limit Application of an Increase in Service Pensions

DATE: March 4, 2015

Summary of H.F. 45 (Murphy, by request); S.F. 215 (Bakk)

Summary of H.F. 45 (Murphy, M., by request); S.F. 215 (Bakk) creates an exception to Minnesota Statutes, Section 424A.03, Subdivision 1, the general volunteer firefighters relief association law that requires uniformity in volunteer firefighter service persons and retirement benefits, by permitting the Proctor Volunteer Firefighters Relief Association to increase lump-sum service pensions for prospective years of service only after December 31, 2013, without being required to uniformly apply that increase to such pensions for years of service rendered before the date of increase.

Proctor Volunteer Firefighter Relief Association Request

The Proctor fire chief is requesting an exemption from the service pension uniformity provision. In 2014, the Proctor Volunteer Firefighters Relief Association raised its lump-sum service pension from \$1,100 per year of service to \$2,200 for prospective service only. However, Proctor was unaware that the increase was statutorily required to be uniformly applied to every firefighters' past service years, which it cannot afford. Proctor now requests an exemption from Minnesota Statutes, Section 424A.03, Subdivision 1, in order to afford the increase to attract new recruits and encourage underperforming, longer-service firefighters to retire.

Background Information on Relevant Topics

The following attachments provide background information on topics relevant to the proposed legislation:

- **Attachment A:** Volunteer firefighter relief association service pension uniformity provision and calculations.

Discussion and Analysis

H.F. 45 (Murphy, M., by request); S.F. 215 (Bakk) creates an exception to the general requirement in Minnesota Statutes, Section 424A.03, Subdivision 1, that each volunteer firefighter relief association must uniformly calculate firefighter service pensions, by permitting the Proctor Volunteer Firefighters Relief Association to increase lump-sum service pensions for prospective years of service after December 31, 2013 without having to apply that increase to years of service rendered before the date of increase.

The proposed legislation raises several pension and related public policy issues for consideration by and possible discussion between members of the Commission, including the following:

1. Appropriateness of Legislative Action. The policy issue is whether legislative action is an appropriate solution to the Proctor Volunteer Firefighters Relief Association's participation and financial problems as compared to possible internal solutions. The proposed legislation would exempt the Proctor Volunteer Firefighters Relief Association from complying with the uniformity provision in calculating pensions in the hopes of attracting new recruits, maintaining the \$2,200 service pension increase, and encouraging retirement.

An alternative would be for the Proctor Volunteer Firefighters Relief Association to gradually increase the service pensions under the statutory guidelines over several years to eventually reach the \$2,200 increase, while still complying with the uniformity provision, and for the Proctor fire station to also create and enforce minimum service requirements all firefighters must meet in order to continue receiving service credit.

The proposed legislation would allow the Proctor Volunteer Firefighters Relief Association to keep the \$2,200 service pension increase, but it may not be appropriate to base recruitment solely on pension amounts and may raise a question of equity. Longer service firefighters, who are still very active, will be excluded from the large impact of the increase because the majority of their service years will be computed under the \$1,100 amount while the newer firefighters will have their years calculated under the \$2,200 amount and any other service pension increase in the future. The alternative would address this question of equity by uniformly increasing the active longer service firefighters' pensions and closing the disparity between longer service and newer firefighters' pensions. A gradual increase may also be more appealing to new recruits rather than one large increase that may stay the same for many years. The Proctor Volunteer Firefighters Relief Association would still be able to increase service pensions without opening the door for the hundreds of other relief associations to petition for a special legislation exemption. The alternative would also directly and effectively deal with underperforming longer service firefighters by requiring all firefighters to meet established minimum requirements to continue receiving service credit. This approach does not target a specific demographic but instead applies to everyone, avoiding equity or age discrimination disputes.

2. Appropriateness of Special Legislation. The policy issue is whether it would be more appropriate for the proposed legislation to be general instead of special legislation. The Proctor Volunteer Firefighters Relief Association hopes that the exemption will reduce the amount of liability otherwise to be incurred by a uniform service pension increase, attract new recruits with affordable higher service pensions, and encourage longer service firefighters, who may remain minimally active solely to be included in the next service pension increase, to retire. However, other relief associations in the state experience similar problems and would therefore benefit from a uniformity requirement exemption as well. To more efficiently and effectively address these statewide problems, it may be more appropriate to do so through general legislation. Principle III.B of the Commission's Principles of Pension Policy addresses the preference for general legislation:

III.B. Preference for General Legislation

No pension legislation of local or special limited application should be recommended by the Legislative Commission on Pensions and Retirement if the purpose and the intent of the proposed legislation would be better served by legislation of general statutory application or if the proposed legislation constitutes a significant departure from previously established uniform pension policy. Pension legislation affecting local police or salaried firefighters may be recommended by the Legislative Commission on Pensions and Retirement in light of any special circumstances that are unique to the relief association.

The proposed legislation's intent is to solve participation and financial problems in one fire department and volunteer firefighter relief association. Because these problems likely are statewide, if the proposed legislation is the optimal resolution, the intent would be better served through general legislation, avoiding the time-consuming special legislation process for each relief association seeking an exemption. An exemption from the uniformity requirement would also be a significant departure from an established law that has been in place since 1933. An exclusive exemption also presents the issue of equity among the state's relief associations. The problems of the Proctor Volunteer Firefighters Relief Association's are not unique and may not be sufficient in demonstrating an equitable basis for the Commission to allow an exclusive exemption. General legislation removing the uniformity provision would equitably address the participation and financial problems of all relief association.

3. Extent of Administrative Burden. The policy issue is the administrative burden that a uniformity provision exemption will create for the Proctor Volunteer Firefighters Relief Association and for the State Auditor and whether each entity is able to take on this additional burden. The premise behind the uniformity provision is to make calculating volunteer firefighter pensions as easy as possible. The equation used under Minnesota Statutes, Section 424A.092, Subdivision 2, is a simple process that only requires multiplying each firefighter's cumulative years of service and the current service pension amount ratio. A uniformity exemption will require the Proctor Volunteer Firefighters Relief Association to keep detailed records tracking the dates of each service pension increase, the amount of each increase, which firefighter received it, and the number of years each increase covered. The State Auditor, which performs yearly audits for the state's relief associations, will also have to shoulder some of the additional administrative burden in calculating non-uniform service pensions. As demonstrated, the calculations to determine non-uniform service pensions are far from simple. The State Auditor will have to calculate each pension amount through a complex equation that takes into consideration each service pension increase during each firefighter's career, the number of years each increase covered, and the time value of money for each increase. The State Auditor will have to take extra time and care in calculating the Proctor Volunteer Firefighters Relief Association's accrued liability, raising administrative expenses which comes directly out of the Proctor Volunteer Firefighters Relief Association's fire state aid. Currently, the State Auditor has a computerized

program to efficiently calculate each relief association’s accrued liability. If the proposed legislation is enacted, the State Auditor will face an additional burden of either having to update the entire system or calculate the Proctor Volunteer Firefighters Relief Association’s audit manually. These additional and complex factors greatly increase the administrative expenses, responsibilities, and likelihood of errors in recordkeeping and calculating. Although the proposed legislation would make the Proctor Volunteer Firefighters Relief Association’s service pension increase from \$1,100 to \$2,200 affordable, that large of an increase will have a significant financial impact.

The following summarizes the most recent actuarial condition of the Proctor Volunteer Firefighters Relief Association as of December 31, 2012:

	FY2012
Membership	
Active Membership	25
Retired Membership	0
Deferred Membership	<u>1</u>
Total Membership	26
Funded Status	
Accrued Liability	\$218,881
Current Assets	<u>\$360,337</u>
Unfunded Accrued Liability	\$141,456
Funding Ratio	165.00%
Financing Requirements	
Service Pensions Payable	\$0
Normal Cost	\$27,039
Administrative Expenses	\$0
Amortization	<u>(\$14,146)</u>
Total Requirements	\$12,893
Fire State Aid	\$15,427
Municipal Contribution	<u>\$5,000</u>
Total Support	\$20,427
Total Requirements	\$12,893
Total Support	<u>\$20,427</u>
Deficiency (Surplus)	(\$7,534)

The impact of the service pension increase can only be fully assessed by using more detailed demographic records, but that large of an increase will decrease the surplus and potentially lead to an unfunded accrued liability in the near future. The additional complexities may require the Proctor Volunteer Firefighters Relief Association to hire outside clerical or accounting assistance, increasing the administrative expenses. The Proctor Volunteer Firefighters Relief Association may also need to determine how often and how much it will increase the service pensions, since too many increases defeats the purpose of the exemption and too few increases will not solve the current participation and financial problems, which would require advanced financial planning.

4. Prospect for Local Law Approval by the City. The policy issue is the likelihood that the special legislation has the support of the city of Proctor and that, if the potential legislation proceeds, it would be approved by the city council. The city of Proctor approved the 2014 service pension increase from \$1,100 to \$2,200 without knowing that the increase would be subject to the uniform service pension provision. The Proctor fire chief has indicated that the city does currently support the special legislation. That may change if the city is presented with other options that raise the service pension levels while still complying with the uniform service pension provision. If the special legislation is not supported by the Proctor City Council and mayor, the Commission and the Legislature would not be well advised to spend legislative time processing the potential legislation during a legislative session.

Technical Amendments

- **Amendment H0045-1A** eliminates the subdivision 1 reference to exempt the Proctor Volunteer Firefighters Relief Association from all of Minnesota Statutes, Section 424A.03, specifically the penalties of noncompliance imposed in subdivision 2.
- **Amendment H0045-2A** amends the proposed legislation’s headnote and title for clarity, specifies what years the exemption applies to, and amends the effective date by removing the “day following enactment” option because the city of Proctor cannot knowledgeably approve the legislation prior to enactment.

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Background Information on the Volunteer Firefighter Relief Association Service Pension Uniformity Provision

Minnesota Statutes, Chapter 424A.23, the service pension uniformity provision, applies to every volunteer firefighter relief association in Minnesota. The uniformity provision has a long legislative history. The uniformity requirement was first added in 1933 (Laws 1933, Chapter 124), the only change to Mason's Minnesota Statutes 1927, Section 3728, and the current provision is a recodification of Minnesota Statutes 1978, Section 69.06.

Under the uniformity provision, when a volunteer firefighter retires, the established yearly service pension amount at the time of retirement applies to every year of service rendered by the firefighter. The service pension amount for each relief association is based on the available financing per firefighter and the corresponding allowable maximum service pension amount established by the flexible service pension maximum chart in Minnesota Statutes 424A.02, Subdivision 3, Clause (d). The service pension amount may not exceed the applicable allowable maximum amount. Both the respective relief association and municipality must approve any service pension increase.

The uniformity provision underlies the procedure that is used to annually determine the relief association's accrued liability. The table in Minnesota Statutes, Section 424A.092, Subdivision 2, is used to calculate the accrued liability for each active member. The statutory table is a present value table assuming a lump sum service pension payable immediately after 20 years of service, is based on a 3% interest assumption, and assumes no pre-retirement turnover or mortality. The table specifies the accrued liability for a \$100 per year lump sum service pension and is scalable for service pensions greater than \$100 per year:

<u>Cumulative Year</u>	<u>Accrued Liability</u>
1	\$ 60
2	124
3	190
4	260
5	334
6	410
7	492
8	576
9	666
10	760
11	858
12	962
13	1,070
14	1,184
15	1,304
16	1,428
17	1,560
18	1,698
19	1,844
20	2,000
21 and thereafter	\$100 additional per year

To determine the actual accrued liability, the relief association must calculate the applicable accrued liability for each active member based on cumulative years of service and corresponding accrued liability and multiply that number by the ratio of the current service pension amount to the table's assumed \$100 service pension amount. So for example, in 2012, the Proctor VFRA's service pension was a \$1,100 per year service benefit, so the ratio used would be 11 (\$1,100 divided by \$100). Therefore, if an active Proctor volunteer firefighter had 6 years of service at the end of 2012, the firefighter's individual accrued liability would be \$4,510 (\$410 multiplied by 11).

To better demonstrate the financial implications of the proposed legislation, Table 1 illustrates the difference in accrued liabilities between a uniform service pension increase and a non-uniform service pension increase. The chart also shows the relative simplicity of calculating the total accrued liability under the uniformity provision and the complexity of calculating the total accrued liability without applying the uniformity provision.

The table represents a 10-person fire department, with a service pension increase from \$1,100 to \$2,200 starting calendar year 2014 and continuing thereafter per year. The current years of service include 2015.

The prospective non-uniform calculations takes into consideration each firefighters' years of service at the \$1,100 service pension amount and then two years of service (2014 & 2015) at the \$2,200 service pension amount. The accrued liability table is used to calculate the liability for the years of service performed at the \$1,100 service pension amount and the two years of service at the \$2,200 service pension are calculated using the difference in accrued liability from the table between the previous year and the current year.

So for example, Firefighter A has three years of service at the \$1,100 service pension amount, so using the accrued liability table that would be 190 x 11. The 2014 accrued liability would be the difference between the table's accrued liability at year 3, \$190, and the table's accrued liability at year 4, 260, leaving 70, which would be multiplied by 22. The 2015 accrued liability amount would use the same method, so the difference between the fourth year, 260, and the fifth year, 334, leaving 74, which would be multiplied by 22. All three totals would then be added together to get the non-uniform accrued liability. Each row represents a single active member:

Table 1
Service Pension Liability Calculations

Firefighter	Current Years of Service	Current \$1,100 Service Pension	Uniform \$2,200 Service Pension	Prospective Non-Uniform \$2,200 Service Pension
A	5	\$334 x 11 = \$3,674	\$334 x 22 = \$7,348	(\$190x11) + (70x22) + (74x22) = \$5,258
B	6	\$410 x 11 = \$4,510	\$410 x 22 = \$9,020	(\$260x11) + (74x22) + (76x22) = \$6,160
C	7	\$492 x 11 = \$5,412	\$492 x 22 = \$10,824	(\$334x11) + (76x22) + (82x22) = \$7,150
D	8	\$576 x 11 = \$6,336	\$576 x 22 = \$12,672	(\$410x11) + (82x22) + (84x22) = \$8,162
E	9	\$666 x 11 = \$7,326	\$666 x 22 = \$14,652	(\$492x11) + (84x22) + (90x22) = \$9,240
F	10	\$760 x 11 = \$8,360	\$760 x 22 = \$16,720	(\$576x11) + (90x22) + (94x22) = \$10,384
G	11	\$858 x 11 = \$9,438	\$858 x 22 = \$18,876	(\$666x11) + (94x22) + (98x22) = \$11,550
H	12	\$962 x 11 = \$10,582	\$962 x 22 = \$21,164	(\$760x11) + (98x22) + (104x22) = \$12,804
I	13	\$1,070 x 11 = \$11,770	\$1,070 x 22 = \$23,540	(\$858x11) + (104x22) + (108x22) = \$14,102
J	14	\$1,184 x 11 = \$13,024	\$1,184 x 22 = \$26,048	(\$962x11) + (108x22) + (114x22) = \$15,466
		Total: \$80,432	Total: \$160,864	Total: \$100,276

- 1.1 moves to amend H.F. No. 45; S.F. No., as follows:
- 1.2 Page 1 line 7, delete "subdivision 1,"

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- 1.1 moves to amend H.F. No. 45; S.F. No., as follows:
- 1.2 Page 1, line 5, after "ASSOCIATION" insert a semicolon
- 1.3 Page 1, line 6, before "PENSION" insert "PROSPECTIVE SERVICE " and delete "LIMIT"
- 1.4
- 1.5 Page 1, line 10, before "for" insert "only"
- 1.6 Page 1, line 12, delete "on or"
- 1.7 Page 1, line 13, delete everything after "effective "
- 1.8 Page 1, line 16, delete ", whichever is later"
- 1.9 Amend the title as follows:
- 1.10 Page 1, line 3, before the period insert " to prospective service"

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State of Minnesota
HOUSE OF REPRESENTATIVES

EIGHTY-NINTH SESSION

H. F. No. 45

01/08/2015 Authored by Murphy, M., by request

The bill was read for the first time and referred to the Committee on Government Operations and Elections Policy

1.1 A bill for an act
1.2 relating to pensions; permitting the Proctor Volunteer Firefighters Relief
1.3 Association to limit application of an increase in service pensions.

1.4 BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF MINNESOTA:

1.5 Section 1. **PROCTOR VOLUNTEER FIREFIGHTERS RELIEF ASSOCIATION**
1.6 **PENSION INCREASE LIMIT.**

1.7 Notwithstanding Minnesota Statutes, section 424A.03, subdivision 1, the Proctor
1.8 Volunteer Firefighters Relief Association may, if consistent with the association's
1.9 governing bylaws, increase a lump-sum service pension under Minnesota Statutes, section
1.10 424A.02, for years of service rendered after an effective date of the service pension
1.11 increase that is after December 31, 2013, without increasing the lump-sum service pension
1.12 for years of service rendered on or before the effective date of the service pension increase.

1.13 **EFFECTIVE DATE.** This section is effective the day following final enactment or
1.14 the day after the governing body of the city of Proctor and its chief clerical officer timely
1.15 complete their compliance with Minnesota Statutes, section 645.021, subdivisions 2
1.16 and 3, whichever is later.