September 13 and 14, 1995
Room 10, State Office Building

11th Meeting

LEGISLATIVE COMMISSION ON PENSIONS AND RETIREMENT

MINUTES

September 13, 1995 Meeting

Representative Richard Jefferson, Chair of the Legislative Commission on Pensions and Retirement, called the meeting to order at 1:20 P.M.

Commission members present:

Representatives Jeff Bertram, Richard Jefferson, Bob Johnson, and Steve Smith
Senators Lawrence Pogemiller and Phil Riveness

Commission members with an excused absence:

Representative Phyllis Kahn; Senators Steven Morse and Roy Terwilliger

2. **Review of Small Volunteer Fire Plan Investment Performance Reporting Requirements** (First Consideration)
Judy Dutcher, the State Auditor, began her presentation regarding the views of the State Auditor on the reporting requirements for smaller relief associations. She stated that if changes in the reporting requirements are implemented, the entities impacted by the changes should be consulted and allowed an opportunity to discuss with the Commission how those changes would affect them. Auditor Dutcher provided copies of two volunteer firefighter reporting forms, the Annual Corporate Registration For 1995 reporting form and the Schedule I-II For Lump Sum Pension Plans State Fire Aid Year 1995 reporting form. Rep. Johnson questioned whether these forms are sent to all volunteer fire funds or just funds with assets above a certain level. Auditor Dutcher responded that these forms go to all volunteer fire funds required to report to the State Auditor.

Auditor Dutcher referred members to the Schedule I-II form, page 3, and noted that Section 1 requires relief associations to provide information relative to projected investment income, realized gains and losses, and unrealized gains and losses, and that this information affects the required municipal contribution. She also noted that on the back of the form the city clerk is required to certify that they have received a copy of this form.

Auditor Dutcher questioned whether additional information, beyond that provided in the forms referenced previously, is needed? She testified that 135 pension funds were included in the Investment Performance Report distributed recently and that the report took 3,500 staff hours to complete. In 1997, 600 funds will be required to provide data. Auditor Dutcher did not estimate the staff hours that might be required to complete that report. She testified that it comes down to an opportunity cost decision and stated that the question is how valuable is this information? She testified that ascertaining how the pension funds are performing and whether they are making good investment decisions is worthwhile but in reality, no one has asked to look at the detailed data collected other than Commission staff.

Rep. Jefferson questioned whether Auditor Dutcher had a recommendation for the Commission to review. Auditor Dutcher testified that the Commission should analyze the fact that volunteer fire relief associations are nonprofit corporations and therefore the state has no liability for these entities whereas the cities do have the liability to make contributions towards these funds. The Commission should ask the cities if they want this information. She questioned why the Legislature is mandating that all this information be provided if the information is not being looked at.

Rep. Johnson stated that he is concerned about the mandate to collect this information for 1997 and whether this is needless or redundant reporting. He noted that the discussion prior to passage of the investment performance law centered on providing a reduction mechanism through LGA or another aid program with regard to municipalities with relief associations that fall below a certain threshold of investment return since poor investment performance does have taxpayer implications.

Auditor Dutcher agreed that poor investment performance has taxpayer implications. She further stated that her office spent over $100,000 to compile the recent Investment Performance Report and that she was dissatisfied with the quality of the report and the information that report actually provided. Auditor Dutcher also stated that the information is unnecessary to the work the auditor does to certify that relief associations are eligible to receive state aid.

Rep. Bertram agreed with Auditor Dutcher that the investment performance report is an excessive reporting requirement.

Auditor Dutcher testified that she was not saying that the reporting requirements were excessive, she was raising the issue that the collected data is not being looked at.

Rep. Johnson referred to Minnesota Statutes, Section 69.772, Subdivision 3, which deals with a municipality's responsibility with regard to the investment performance of a relief association.

Lawrence A. Martin, LCPR Executive Director, referred members to Minnesota Statutes, Section 69.771 to 69.775, and stated that there is a five percent threshold that is calculated into the actuarial funding requirements for volunteer fire relief associations and if a relief association does not achieve a five percent investment return, an unfunded accrued liability occurs which may require a municipality to increase its contribution to the relief association in subsequent years.

Rep. Bertram questioned how many volunteer fire relief associations fell below that 5% investment return threshold. Discussion followed.

Auditor Dutcher testified that one positive outgrowth of the investment performance reporting law was that many relief associations now have investment policies that did not have them previously.

Sen. Riveness stated that he is appalled that municipalities are not requesting this information since municipalities are at risk to makeup the shortfall by potentially raising taxes if investment performance is poor. He further stated that if investment performance were higher, benefits could potentially be improved. He supports a report on investment performance returns.

Auditor Dutcher testified that the goal of the investment performance report is to provide information on how investments have performed over time and how management decisions have influenced investment performance. She testified that she does not know whether detailed information is being supplied to municipalities but that she would assume that it is not since the relief associations have had so much difficulty in providing the information to her office. She further questioned the State's interest in this issue since the 2% money comes from insurance premiums.

Rep. Johnson noted that two issues that arose prior to passage of the investment performance law were the issue of the underinvestment of relief association assets and the issue of whether underinvesting created an unfair tax burden. Discussion followed.

Sen. Riveness stated that some of the options that volunteer firefighter funds have are hiring a professional investment person, using the State Board of Investment, and investing in cash instruments at the local bank. He also stated that if in further testimony and review it is proven that municipalities do not use the investment performance information they receive, he would be open to other options. Discussion followed.

Stan Peskar, General Counsel for the League of MN Cities, began his presentation. He testified that cities are interested in a workable reporting requirement and that the beneficiaries of the reporting requirements are the firefighters relief associations, the cities, and the State. He also testified that the mayor, city financial officer, and fire chief in many cities attend relief association meetings and participate in reviewing reports. Rep. Johnson asked Mr. Peskar to differentiate between municipalities with relief association fund assets above $300,000 and those with assets below, and how the municipalities view that aspect of the reporting law. Mr. Peskar testified that there probably should be a difference in the reporting requirements for a large fund as opposed to a small fund. He testified that all funds should be required to provide an annual report to its members and should include the fund's investment policy in that report. He recommended that the Legislature should not require reporting that is duplicative. Rep. Bertram questioned whether the report that is filed with the State Auditor enabling relief associations to receive the 2% money is being provided to the municipalities. Mr. Peskar stated that municipalities do receive that report and suggested that investment performance and time-weighted rate of return also be included in that report so that there is only one report to deal with.

Gus Welter, representing MN State Fire Department Association, testified that quarterly returns do not seem to be of much value for relief associations which are invested for the long term. He believes that annual returns would provide adequate information to determine what the rate of investment return is for volunteer firefighter relief associations. He would like to see the reporting requirements simplified. The current forms and instructions are too complicated and many funds are paying a large amount to have the forms completed. Discussion followed.

Brian Holzer, Chairman of the MN State Fire Chiefs Association, testified that he supports the testimony provided by the MN State Fire Department Association representative. Discussion followed.

Nyles Zikmund, President MARAC and Chief of the Spring Lake Park Fire Department, testified that his organization represents approximately 170 fire relief associations, including 35 metro and 135 outstate associations, and those 170 fire relief associations have 60 to 65% of the state's volunteer fire relief association assets. Mr. Zikmund testified that MARAC has opposed the investment performance report in the past and continues its opposition as they do not see the value in the report. They are willing to work with the Commission toward making changes in the law. Mr. Zikmund suggested requiring investment performance reporting for relief associations with assets above a threshold of $500,000. He further suggested simplifying reporting requirements. In response to Rep. Johnson's question, Mr. Zikmund testified that the average relief association expense for preparation of the investment performance form was $700 to $800. Mr. Zikmund also testified that the cities he works with do not levy more when the fire relief association's expenses increase, he must reduce his budget in other areas to cover the increase.

Mr. Martin reviewed the staff memo and background information on this issue. He noted that investment income is the single largest component in funding pension plans. Mr. Martin referred members to a table on pages two and three of the memo which showed the 40 associations with the largest revenue and the 40 with the least revenue. He testified that the 40 associations with the largest revenue had an average investment income multiple of 1.6 times the revenue from other sources and the smaller 40, excluding the anomaly of Odessa, had an average investment income multiple of .74 times revenue from other sources. Discussion followed.

Sen. Riveness questioned what members learn from Edina's and Eden Prairie's investment income multiple shown in the table. Mr. Martin responded that the numbers could indicate that investments are underperforming in one fund and overperforming in the other or that something is going on with the contributions in the two plans or a combination of both. He stated, however, that one year's data is not enough to get the whole picture. Sen. Riveness stated that possibly it would be more effective to provide relief associations with a best practices report due to the skewed picture provided by just one report or one year's data.

Mr. Martin continued with his review of the staff memo and background information. Discussion regarding the reports continued.

Sen. Pogemiller referred to page six of the staff memo and asked whether there was a break down on which of relief associations failed to file the Investment Performance form or had data problems or processing problems? Mr. Martin responded that the memo included with the Auditor's report characterized those problems.

The meeting adjourned at 3:25 P.M.

September 14, 1995, LCPR Meeting

Representative Richard Jefferson, Chair of the Legislative Commission on Pensions and Retirement, called the meeting to order at 9:20 A.M.

<u>**Commission members present:**</u>

Representatives Jeff Bertram, Richard Jefferson, Bob Johnson, and Steve Smith
Senators Lawrence Pogemiller, Phil Riveness, and LeRoy Stumpf

<u>**Commission members with an excused absence:**</u>

Representatives Phyllis Kahn; Senators Steven Morse and Roy Terwilliger

3. **Review of Proposed Exclusive Defined Contribution Plan Coverage For Elected Officials** (First Consideration)
Lawrence A. Martin, LCPR Executive Director, reviewed the background and staff memo on this issue. He noted that this issue is the result of legislation introduced last session as H.F. 1080 (Jefferson); S.F. 972 (Morse) and sponsored by PERA. Mr. Martin noted that the memo provides information regarding the pension coverage options for elected officials as well as the differences between defined benefit and defined contribution plans. He stated that the two major factors related to pension plans are funding and benefits. If either of those two factors are fixed, the other factor becomes the variable.

1. **Approval of Meeting Minutes, Meetings of August 9 and 10, 1995**
Rep. Jeff Bertram moved approval of the meeting minutes. **MOTION PREVAILED.**

Mr. Martin continued with agenda item three and reviewed the side by side characteristics of defined benefit and defined contribution plans. Discussion followed. Mr. Martin then reviewed the advantages of membership for various elected officials in a defined benefit plan or a defined contribution plan.

Mr. Martin stated that the Commission's question in the 1996 Session when reviewing H.F. 1080; S.F. 972, is should there be exclusive defined contribution plan coverage for local elected officials.

Sen. Riveness questioned whether the biggest problem that the Commission is trying to solve is the issue of officials who move to higher office or shift to highly compensated positions. Mr. Martin responded that the argument for the bill does seem to be the abuse of the system that accompanies a low salaried official who has a late career move to a highly compensated position which creates a large liability for the pension plan. Discussion followed.

Rep. Johnson stated that he would like to see the Commission look at the windfall issue with regard to early career employees who subsidize the windfall benefits of late career employees.

Sen. Stumpf stated that the Commission has gained considerable knowledge with regard to the windfall issue and the early retirement incentive issue. He would like the Commission to target solutions to address those problems.

Mary Vanek, PERA representative, testified that in 1993, PERA did have a local official who became a PERA member prior to establishment of the salary threshold and who in the last five or six years of the member's career worked in a highly compensated position with PERA coverage and applied for the early retirement incentive. PERA sought the Attorney General's opinion in this case and as a result, the AG's office advised that governing body officials were not eligible for the early retirement incentive. Ms. Vanek testified that the PERA Board has taken the position that they would like to see PERA-General membership closed to future elected officials to avoid the public perception of abuse that arose after former Governor Perpich's pension situation was publicized. Ms. Vanek testified that the defined contribution plan now has 4,000 members. A big reason for the increase in membership was due to a 1991 change to the Social Security law which is that if an individual is participating in a governmental plan and the total combined employee and employer contribution are over 7%, the individual does not have to contribute to Social Security if the individual does not meet other requirements.

Sen. Riveness suggested computing a benefit for local officials in the situation the Commission has been discussing by calculating the benefit using a high five average for the years of service and salary received as a local government official and combining that with a calculation using the high five and years of service for the other employment position. Ms. Vanek testified that the solution suggested by Sen. Riveness would not be difficult to administer and is certainly another option to pursue. Discussion followed.

Rep. Bertram stated that he does not believe this is a big problem but recommended that if the Commission takes action on this issue it should be done on a statewide basis.

Rep. Johnson stated that the Commission should be aware that if the current law is changed, there may be court challenges. Discussion followed.

Rep. Bertram asked for an update on the LCPR pension policy principles issue.

Mr. Martin responded that letters have been sent to all the various employee organizations, employers, and pension funds, including the police and paid fire funds requesting their written input before October 30 and asking them to participate in the working groups. A calendar has been established setting meetings for every Tuesday in the months of November and December.

Rep. Bertram requested that members of the Legislature as well as Commission members also receive a copy of the letter on pension policy principles. He also requested that action be taken to permit confidential or anonymous input from all the groups contacted.

Rep. Bertram asked if the Chair had gone forward with any plans for a Commission meeting in greater Minnesota? Rep. Jefferson said that an outstate meeting is still under consideration. Rep. Johnson asked whether the Senate members would participate in outstate meetings? Discussion followed. Sen. Riveness stated that he would be willing to go outstate but he doesn't know if a case has been made that the Commission's work would benefit by going outstate. He further stated that if the agenda was based on issues of interest to the public outstate, there would be merit in holding an outstate meeting.

4. **Review of the Potential Options Available For Accommodating Benefit Increase Windfalls** (First Consideration)
Edward Burek, LCPR Deputy Executive Director, reviewed the staff memo and background on this issue. He noted that this issue came up as a result of the increase in the TRA, DTRFA, State Patrol, and PERA-P&F benefit accrual rate. Mr. Burek testified that older, long service employees retire without making the level of contributions necessary to fund the increase in their benefit and receive a windfall. He noted that in the case of TRA's 1993 accrual rate increase, the burden of the windfall to older employees who retire will be borne by younger and mid-career employees in the form of a 2% employee contribution increase. Mr. Burek then reviewed eight potential options to reduce the windfall to older employees.

Mr. Burek noted that in contrast to reducing windfalls after benefit increases, the purpose of early retirement incentive options is to provide a windfall that would induce older employees to retire and enable an employer to reduce the workforce. Any action taken to reduce windfalls should take into consideration early retirement incentive options to assure the continued ability to use that tool.

Sen. Stumpf cautioned the Commission to be sure that any policy established on this issue is fair to all employees.

5. **Other Items**
Rep. Jefferson tentatively set the next Commission meeting for October 11, to October 12, 1995.

The meeting adjourned at 11:25 A.M.

Jean Liebgott

Jean Liebgott, Secretary