TO: Members of the Legislative Commission on Pensions and Retirement

FROM: Lawrence A. Martin, Executive Director

RE: S.F. 259 (Betzold); H.F. 1706 (Smith): Volunteer Firefighter Relief Associations; Implementing Legislation for Recommendations of the State Auditor's Volunteer Fire Working Group

DATE: March 30, 2005

General Summary of the Bill

S.F. 259 (Betzold); H.F. 1706 (Smith) amends various provisions of Minnesota Statutes, Chapters 69, 356A, and 424, the statutory chapters governing various aspects of the regulation of volunteer firefighter relief associations, to implement the recommendations of a working group on volunteer fire issues assembled by the Office of the State Auditor, by making the following changes:

1. Refines the Trigger for the Required Filing of Financial Reports. (Sections 1 and 2) The imposition of the more stringent requirement of a volunteer firefighter relief association financial report and audit, rather than a financial statement, would occur in the year after the relief association achieves $200,000 in either assets or liabilities, rather than during the same year, and the more stringent financial reporting requirement would continue thereafter, irrespective of the subsequent asset or accrued liability size of the volunteer firefighter relief association.

2. Specifically Enumerates the Reporting, Funding and Investment Requirements for Compliance Determination by the State Auditor. (Section 3) The generic specification of the responsibility for the Office of the State Auditor to determine compliance by volunteer firefighter relief associations for qualification for fire state aid receipt is augmented with a specific enumeration of the reporting, funding, and investment requirements on which a compliance determination will be based, including filing a financial report or statement, meeting treasurer bonding requirements, filing an actuarial valuation that meets minimum contents requirements, failure to obtain a sufficient municipal contribution, failure to obtain municipal ratification of a benefit improvement, investing in an unauthorized investment security, making an unauthorized special fund administrative expense, failure to provide investment portfolio and performance reporting, failure to obtain broker acknowledgements of investment restrictions, permitting or failing to correct a prohibited transaction, or paying a service pension in excess of the applicable service pension maximum.

3. Requires the Amortization of Experience Losses in Volunteer Firefighter Relief Associations. (Sections 4 and 6) The amortization requirement is clarified to match the procedure represented for several years in the applicable State Auditor's forms, with the original benefit increase-related unfunded liabilities required to be retired by one-tenth of the amount annually and a ten-year amortization requirement is extended to relief association investment losses and experience (mortality, retirement age, or investment) losses, which previously were not required to be amortized.

4. Requires Disclosure of Relief Association Financial Requirements and Minimum Obligation in Relief Association Financial Reporting and Authorizes the State Auditor to Obtain 1971 Guidelines Act Funding Certifications Upon the Determination of Insufficient Funding. (Sections 5 and 7) The annual financial reporting or financial statement of a volunteer firefighter relief association is required to include disclosure of the most recent relief association financial requirements and minimum municipal obligation. The Office of the State Auditor is authorized to obtain copies of the relief association financial requirements and minimum municipal obligation certification documents under Minnesota Statutes, Sections 69.771 through 69.775, from the relief association and the applicable municipality if insufficient funding of the relief association is disclosed in the relief association annual financial reporting.

5. Clarification of Deduction of Reasonably Anticipated Fire State Aid. (Sections 4 and 7) The deduction of expected fire state aid in determining the minimum municipal contribution is limited to a reasonable estimate and a maximum on the reasonably expected fire state aid is set at the prior year's fire state aid increased by 3.5 percent.

6. Relaxes the 75 Percent Maximum on Volunteer Firefighter Relief Association Mutual Fund Investments. (Section 8) The amount of any investment of money market mutual funds is excluded from the calculation of the 75 percent market value maximum on investments in mutual funds by volunteer firefighter relief associations.

7. Clarifies the Corporate Stock and Exchange-Traded Funds as Authorized Volunteer Firefighter Relief Association Investments. (Section 9) The authorized corporate stock investments are expanded from stocks listed on the New York Stock Exchange or the American Stock Exchange to stocks listed on any exchange regulated by the United States federal government or the Canadian national government and the authorized investment security list is expanded to specifically include exchange-traded funds.

8. Average Financial Support Per Firefighter Required for Monthly Benefit Volunteer Firefighter Relief Associations Service Pension Maximum Adjusted. (Section 10) The amount of the three-year average annual financing required per firefighter for a given monthly benefit volunteer firefighter relief association service pension level is reduced from $84 for each dollar of service pension per month per year of service to $81.

9. Accommodates Defined Contribution Volunteer Firefighter Relief Associations Deferred Service Pension Investment Return Crediting Procedure. (Sections 11 and 12) Defined contribution volunteer firefighter relief associations are permitted to credit proportional amounts of investment gains or losses along with active members as of the most recent post date for determining and crediting investment return investment and restricts the current deferred service pension interest provision to lump sum defined benefit volunteer firefighter relief associations.

10. Revises Defined Benefit Volunteer Firefighter Relief Association Fixed Rate Deferred Service Pension Interest Crediting Option. (Section 12) The current five percent interest option is eliminated and an option is added for interest at a rate up to five percent per annum, as set by the board of trustees of the relief association and if approved by the applicable municipality, and payable from the first of the month next following the separation from active service until the last day of the month preceding the application for the deferred service pension upon a former active member attaining the normal retirement age.

11. Requires Volunteer Firefighter Relief Association Service Credit for Military Service Break-In-Service. (Section 13) Allows up to five years of service credit in a volunteer fire relief association for a break in firefighter service to provide military service if the firefighter provides notice to the fire department of the break in service to provide uniformed service, and promptly returns to firefighter service covered by the same relief association (or its successor) upon return from uniformed service, and the discharge from military service is not less than honorable.

12. Revises the Municipal Representation on Volunteer Firefighter Relief Association Boards of Trustees. (Section 14) Makes the municipal representation on the board of a volunteer firefighter relief association more flexible by replacing the current ex-officio members with one elected and one elected or appointed municipal officer appointed by the municipal council, reduces the municipal representation on relief association boards of trustees associated with an independent nonprofit firefighting corporation from three board members to two board members, and clarifies the municipal representation for joint powers entities and townships.

Section-By-Section Summary of the Bill

A section-by-section summary of S.F. 259 (Betzold); H.F. 1706 (Smith) is attached.

Background Information on the Regulation of Volunteer Firefighter Relief Associations

Appendix A sets forth background information on the state law regulation of volunteer firefighter relief associations contained in Minnesota Statutes, Chapters 69, 356A, and 424B.

Background Information on the Number, Size, Financial Health, and Benefit Practices of Volunteer Firefighter Relief Associations 1974-2002

The following presents aggregate information on volunteer firefighter relief associations as assembled by the staff of the Legislative Commission on Pensions and Retirement (1974 and 1977) from fire state aid qualification information obtained by the Insurance Department and by the Office of the State Auditor (1980 through 2002):

Number of Plans

Year:	1974	1977	1980	1982	1984	1986	1987	1988	1989	1990	1991
Lump Sum											
Under $50/yr	134	110	72	28	23	11	12	8	10	10	9
$50-$100/yr	122	116	79	68	60	39	33	28	25	23	19

$100-$200/yr	122	118	131	133	132	99	88	85	62	50	55
$200-$300/yr	5	45	81	83	88	115	123	108	114	108	99
$300+/yr	7	57	124	18	237	277	293	331	355	379	396
Total Lump Sum	390	446	487	330	540	541	549	560	566	570	578
Monthly Benefit											
Under $2/mo/yr	41	16	3	0	6	8	--	--	--	--	--
Over $1.99/mo/yr	10	32	26	24	23	22	33	30	28	27	26
Total Monthly	51	48	29	24	29	30	33	30	28	27	26
Mo/Lump Sum Comb.											
Total Combined	--	--	--	--	--	--	--	--	--	--	--
Defined Contribution											
Total Def. Contrib.	52	54	45	56	68	66	66	72	68	67	66
No Benefits											
Total No Benefits	42	27	33	8	5	7	2	1	2	--	--
Total	535	575	594	580	642	641	650	663	664	664	671

Year:	**1992**	**1993**	**1994**	**1995**	**1996**	**1997**	**1998**	**1999**	**2000**	**2001**	**2002**
Lump Sum											
Under $50/yr	13	12	10	10	8	7	--	--	--	--	--
$50-$100/yr	17	16	16	13	13	10	13	13	10	6	7
$100-$200/yr	60	59	55	49	39	45	36	26	20	19	16
$200-$300/yr	84	79	78	74	67	61	51	42	35	30	24
$300+/yr	419	429	439	453	445	470	492	512	530	539	549
Total Lump Sum	593	595	598	599	572	593	592	593	595	594	596
Monthly Benefit											
Under $2/mo/yr	--	--	--	--	--	--	--	--	--	--	--
Over $1.99/mo/yr	29	27	12	10	7	8	7	5	5	5	5
Total Monthly	29	27	12	10	7	8	7	5	5	5	5
Mo/Lump Sum Comb.											
Total Combined	--	2	15	15	16	16	16	23	18	18	18
Defined Contribution											
Total Def. Contrib.	72	73	74	76	76	80	84	85	87	88	89
No Benefits											
Total No Benefits	--	--	--	--	--	--	--	--	--	--	--
Total	694	697	699	700	671	697	699	706	705	705	708

The numbers presented depend on filings by the applicable volunteer firefighter relief associations as part of the fire state aid program and, because there is a cut-off publication date for the reports from the Office of the State Auditor, there is some potential slippage in the information over time. There is a significant trend in volunteer firefighter relief association growing from low benefit amounts to higher benefit amounts over the 28-year period, with 62.61 percent of volunteer firefighter relief associations either under $200 per year of service lump sum or $40 per month with 20 years of service monthly annuity in 1977 and with 92.11 percent of lump sum volunteer firefighter relief associations providing a service pension over $300 per year of service and with 100 percent of monthly benefit volunteer firefighter relief associations providing a service pension in excess of $40 per month with 20 years of service. Over the period 1974-2002, the number of volunteer firefighter relief associations providing lump sum service pensions has been reasonable consistent but there has been a significant drop in the number of volunteer firefighter relief associations providing monthly benefit service pensions, the emergence of volunteer firefighter relief associations providing a combination of monthly benefit and lump sum service pensions, a modest growth in the number of volunteer firefighter relief associations providing “split-the-pie” or defined contribution service pensions, and the apparent elimination of volunteer firefighter relief associations which provide no service pension coverage.

Membership

Year:	**1974**	**1977**	**1980**	**1982**	**1984**	**1986**	**1987**	**1988**	**1989**	**1990**	**1991**
Members											
Actives											
Lump Sum	9,052	10,915	10,834	12,523	12,980	12,859	13,179	13,406	13,720	14,112	14,049
Monthly	1,549	1,592	745	812	1,092	1,125	1,305	1,252	1,178	1,174	1,200
Combination	--	--	--	--	--	--	--	--	--	--	--
Defined Contrib.	1,042	1,256	401	1,207	1,449	1,345	1,411	1,520	1,460	1,434	1,407
No Benefits	820	558	278	114	63	83	35	20	37	--	--

Total Actives	12,463	14,321	12,258	14,656	15,584	15,412	15,930	16,198	16,395	16,720	16,656
Deferreds											
Lump Sum		139	170	296	381	451	609	520	558	639	718
Monthly		117	68	32	39	50	61	67	76	92	78
Combination		--	--	--	--	--	--	--	--	--	--
Defined Contrib.,		12	3	9	18	29	26	29	36	68	39
No Benefits		--	8	0	0	0	0	0	0	--	--
Total Deferreds		268	249	337	438	530	696	616	670	799	835
Retirees											
Lump Sum		--	527	363	410	177	124	177	173	165	214
Monthly		400	249	302	413	444	547	493	483	472	494
Combination		--	--	--	--	--	--	--	--	--	--
Defined Contrib.		--	38	3	20	1	1	18	19	23	23
No Benefits		--	67	0	0	0	0	0	0	--	--
Total Retirees		400	881	668	843	622	672	688	675	660	731
Total Members											
Lump Sum		11,054	11,531	13,182	13,771	13,487	13,912	14,103	16,395	14,916	14,981
Monthly		2,109	1,062	1,146	1,544	1,619	1,913	1,812	1,737	1,738	1,772
Combination		--	--	--	--	--	--	--	--	--	--
Defined Contrib.		1,268	442	1,219	1,487	1,375	1,438	1,567	1,515	1,525	1,469
No Benefits		558	353	114	63	83	0	20	37	--	--
Total Members		14,989	13,388	15,661	16,865	16,564	17,263	17,502	19,684	18,179	18,222

Year:	**1992**	**1993**	**1994**	**1995**	**1996**	**1997**	**1998**	**1999**	**2000**	**2001**	**2002**
Members											
Actives											
Lump Sum	13,583	14,051	14,187	14,189	13,655	14,022	13,854	12,612	13,244	13,691	13,767
Monthly	1,210	1,218	525	464	307	313	324	208	208	206	159
Combination	--	100	735	726	807	775	746	879	840	790	847
Defined Contrib.	1,594	1,565	1,647	1,721	1,727	1,972	2,033	2,039	2,106	2,182	2,222
No Benefits	--	--	--	--	--	--	--	--	--	--	--
Total Actives	16,387	16,934	17,094	17,100	16,496	17,082	16,957	15,738	16,398	16,869	16,995
Deferreds											
Lump Sum	841	945	1,074	1,222	1,333	1,538	1,640	1,660	1,801	1,948	2,042
Monthly	88	100	62	57	45	44	56	34	29	31	19
Combination	--	1	64	80	89	79	90	114	157	196	216
Defined Contrib.	122	150	171	188	166	508	266	528	666	722	738
No Benefits	--	--	--	--	--	--	--	--	--	--	--
Total Deferreds	1,051	1,196	1,371	1,547	1,633	2,169	2,052	2,336	2,653	2,897	3,015
Retirees											
Lump Sum	148	173	187	184	90	76	56	36	316	538	507
Monthly	527	566	312	261	198	207	206	153	164	178	149
Combination	--	26	271	267	312	349	344	424	413	400	392
Defined Contrib.	14	8	6	7	5	5	11	17	62	58	64
No Benefits	--	--	--	--	--	--	--	--	--	--	--
Total Retirees	689	773	776	719	605	637	617	630	955	1,174	1,112
Total Members											
Lump Sum	14,572	15,169	15,448	15,595	15,078	15,636	15,550	14,308	15,361	16,177	16,316
Monthly	1,825	1,884	899	782	550	564	586	395	401	415	327
Combination	--	127	1,070	1,073	1,208	1,203	1,180	1,417	1,410	1,386	1,455
Defined Contrib.	1,730	1,723	1,824	1,916	1,898	2,485	2,310	2,584	2,834	2,962	3,024
No Benefits	--	--	--	--	--	--	--	--	--	--	--
Total Members	18,127	18,903	19,241	19,366	18,734	19,888	19,626	18,704	20,006	20,940	21,122

Over the period 1977-2002, there has been considerable consistency in the share of the total volunteer firefighter relief association active membership covered by lump sum relief associations (76.22 percent in 1977 as compared to 81.01 percent in 2002), but a huge decline in the share of the total volunteer firefighter relief association active membership covered by a monthly benefit relief association (11.11 percent in 1977 as compared to 0.94 percent without considering combination relief associations or to 5.92 percent with the inclusion of combination relief associations), and a rough doubling the share of the total volunteer firefighter relief association active membership covered by a defined contribution relief association. There has been a huge growth in the number of deferred volunteer firefighter relief association members over the period 1977-2002, especially between 1996-1997, 2000-2001, and 2001-2002, and with the biggest growth in the number of deferred members in defined contribution volunteer firefighter relief associations. The small number of total deferred volunteer firefighter relief association members in 1977 is consistent with the modest attention shown to deferred volunteer firefighter issues in the 1979 recodification of volunteer firefighter relief association laws (see Laws 1979, Chapter 201), but the growth in the number of deferred volunteer firefighters correlates with the greater demands for changes in the regulation of deferred volunteer firefighter relief association service pensions. Because retired members in volunteer firefighter relief association providing lump sum service pensions are not always tracked, the retired membership and total membership results are not wholly reliable.

Liabilities, Assets, Fire State Aid, and Municipal Contributions

Year:	1974	1977	1980	1982	1984	1986	1987	1988	1989	1990	1991
Accrued Liabilities											
Lump Sum		14,278,898	29,501,934	40,937,006	52,985,939	59,057,471	60,643,988	68,071,179	78,070,344	86,588,461	92,771,460
Monthly		9,041,863	7,547,661	10,621,672	46,490,469	25,044,975	34,347,349	35,320,800	37,432,078	39,749,215	44,543,835
Combination		--	--	--	--	--	--	--	--	--	--
Defined Contrib.		1,444,286	1,219,645	2,094,808	4,417,375	5,927,094	6,449,852	8,704,595	9,581,000	10,434,995	11,349,299
Total Accr. Liab.		24,765,047	38,269,240	53,653,486	103,893,783	90,029,540	101,441,189	112,096,574	125,083,422	136,772,671	148,664,594
Assets											
Lump Sum		15,054,337	29,791,110	40,565,620	51,654,774	61,032,069	62,395,065	69,774,320	80,004,613	86,825,688	95,265,007
Monthly		8,211,852	7,250,784	9,900,259	31,055,648	23,220,944	31,624,291	32,759,213	34,603,998	36,463,717	40,225,667
Combination		--	--	--	--	--	--	--	--	--	--
Defined Contrib.		1,444,286	1,219,645	2,094,808	4,417,375	5,927,094	6,449,852	8,704,595	9,581,000	10,434,995	11,349,299
Total Assets		24,710,475	38,261,539	52,560,687	87,127,797	90,180,107	100,469,208	111,238,128	124,189,611	133,724,400	146,839,973
Normal Cost											
Lump Sum		1,470,015	498,536	3,926,658	5,212,341	5,058,195	5,273,113	4,994,302	5,964,120	8,224,582	9,004,068
Monthly		463,651	337,988	515,211	1,503,450	934,147	957,484	859,673	755,699	1,355,894	1,575,915
Combination		--	--	--	--	--	--	--	--	--	--
Defined Contrib.		151,019	500	8,769	32,776	504,008	539,181	632,067	616,205	611,359	603,678
Total Normal Cost		2,084,685	837,024	4,450,638	6,748,567	6,496,350	6,769,778	6,486,042	7,336,024	10,191,835	11,183,661
Fire State Aid											
Lump Sum		1,419,035	2,912,095	3,690,695	4,047,173	4,512,805	4,552,052	4,733,327	4,881,199	4,805,462	4,929,212
Monthly		602,368	581,600	693,007	1,276,954	1,320,346	1,700,437	1,684,158	1,609,808	1,620,559	1,667,813
Combination		--	--	--	--	--	--	--	--	--	--
Defined Contrib.		143,460	166,375	205,638	334,357	430,992	436,382	550,993	533,395	517,789	504,419
Total Fire State Aid		2,164,863	3,660,070	4,589,340	5,658,484	6,264,143	6,688,871	6,968,478	7,024,402	6,943,810	7,101,444
Municipal Contribution											
Lump Sum		357,973	664,700	834,832	1,197,277	1,299,731	1,176,333	1,246,509	1,557,416	1,842,447	1,858,245
Monthly		277,370	164,259	284,988	2,434,045	441,115	751,488	620,926	633,533	739,970	849,286
Combination		--	--	--	--	--	--	--	--	--	--
Defined Contrib.		21,569	11,296	26,879	36,797	73,016	102,799	81,074	82,810	93,570	99,259
Total Mun. Contr.		656,912	840,255	1,146,699	3,668,119	1,813,862	2,030,620	1,948,509	2,273,759	2,675,987	2,806,790

Year:	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002
Accrued Liabilities											
Lump Sum	94,145,127	102,546,702	107,486,014	113,855,616	119,936,745	130,642,738	145,966,781	150,761,568	171,611,378	186,795,976	192,569,597
Monthly	47,327,072	52,161,236	28,830,599	24,678,407	14,839,392	17,085,291	20,340,226	14,338,052	15,008,219	16,915,086	12,923,387
Combination	--	2,454,593	27,615,459	28,819,704	38,743,123	39,644,188	42,204,240	54,526,028	54,173,717	57,952,711	62,876,598
Defined Contrib.	16,586,370	18,095,687	17,590,749	25,919,681	28,832,841	38,390,049	44,757,368	50,606,325	47,427,772	47,259,294	43,432,178
Total Accr. Liab.	158,058,569	175,258,218	181,522,821	193,273,408	202,352,101	225,762,266	253,268,615	270,231,973	288,221,086	308,923,067	311,801,760
Assets											
Lump Sum	95,375,295	105,920,681	105,073,259	122,226,938	133,172,234	153,037,774	172,113,829	179,343,843	183,279,497	179,424,046	165,317,015
Monthly	46,002,578	47,765,817	27,362,519	22,953,953	13,813,247	16,602,144	20,504,773	14,132,149	13,960,203	13,385,232	9,532,988
Combination	--	2,196,505	21,609,884	25,008,817	37,619,149	40,851,421	43,579,741	59,072,419	55,443,773	51,172,825	47,442,209
Defined Contrib.	16,586,370	18,095,687	17,590,749	25,919,681	28,832,841	38,390,049	44,757,368	50,606,325	47,427,772	47,259,294	43,432,178
Total Assets	157,964,243	173,978,690	171,636,411	196,109,389	213,437,471	248,881,388	280,955,711	303,154,736	300,111,245	291,241,397	265,724,390
Normal Cost											
Lump Sum	8,965,833	9,921,518	10,211,254	10,869,651	11,214,171	12,219,929	13,311,487	13,514,162	15,189,092	16,483,865	16,892,504
Monthly	1,600,109	1,625,173	875,806	686,563	346,433	358,792	470,770	284,860	312,019	340,067	261,434
Combination	--	120,725	939,552	981,755	1,322,315	1,269,951	1,307,322	1,515,019	1,662,901	1,674,601	1,844,560
Defined Contrib.	919,866	855,696	928,280	1,411,551	2,098,195	2,684,271	2,553,138	2,640,890	2,753,206	3,004,038	3,288,331
Total Normal Cost	11,485,808	12,523,112	12,954,892	13,949,520	14,981,114	16,532,943	17,642,717	17,954,931	19,917,218	21,502,571	22,286,829
Fire State Aid											
Lump Sum	4,739,140	4,242,494	4,950,397	5,211,582	8,060,595	7,140,394	7,731,336	7,391,107	7,937,916	8,644,841	9,378,276
Monthly	1,801,399	1,548,161	858,681	689,483	512,496	554,859	643,057	379,802	395,685	426,640	418,469
Combination	--	154,328	934,346	995,205	1,486,949	1,434,117	1,386,971	1,765,592	1,753,859	1,789,869	2,148,174
Defined Contrib.	774,684	707,024	782,147	1,172,687	1,536,620	1,855,313	2,038,308	2,091,608	2,212,814	2,385,099	2,639,147
Total Fire State Aid	7,315,223	6,652,007	7,525,571	8,068,957	11,596,660	10,984,683	11,799,672	11,628,109	12,300,274	13,246,449	14,584,066
Municipal Contribution											
Lump Sum	2,281,421	2,613,573	2,691,177	2,803,095	3,276,302	2,680,940	2,442,795	2,360,961	2,375,285	2,732,044	4,202,331
Monthly	1,085,807	1,223,934	613,418	724,911	341,465	305,466	353,220	273,287	279,476	309,149	176,255
Combination	--	37,957	680,895	870,130	1,029,153	1,010,042	1,029,535	1,113,773	1,069,335	1,106,226	1,351,792
Defined Contrib.	145,182	148,672	146,133	238,864	561,575	828,958	514,830	549,282	540,392	618,939	649,184
Total Mun. Contr.	3,512,410	4,024,136	4,131,623	4,637,000	5,208,495	4,825,406	4,340,380	4,297,303	4,264,488	4,766,358	6,379,562

Over the period 1977-2002, there has been a significant increase in volunteer firefighter relief association accrued liabilities, with a 7.75 percent annual compound increase rate for lump sum volunteer firefighter relief associations, a 2.20 percent annual compound increase rate for monthly benefit/combination volunteer firefighter relief associations, and a 16.00 percent annual compound increase rate for defined contribution volunteer firefighter relief associations. For defined contribution volunteer firefighter relief associations, the relief association accrued liability is equal to the relief association assets. There has been a general growth in volunteer firefighter relief association assets over the period 1977-2002, until 2000-2001, when there was a general decline in the size of volunteer firefighter relief association assets. There also has been a significant increase in the normal cost of volunteer firefighter relief associations, especially in lump sum volunteer firefighter relief associations. For defined contribution volunteer firefighter relief associations, the normal cost figure is the sum of the relief association's fire state aid and municipal contributions. Fire state aid for volunteer firefighter relief associations has grown considerably over the period 1977-2002, at a 9.75 percent annual compound increase rate. However, the fire state aid pays a smaller portion of the normal cost of volunteer firefighter relief association in 2002 than it did in 1977, 55.5 percent of the total normal cost in 2002 as compared to 96.5 percent of the total normal cost in 1977. The average amount of fire state aid per active member in 2002, with combination volunteer firefighter relief associations an average of $2,536.21 in fire state aid per active member in 2002, with lump sum volunteer firefighter relief associations receiving an average of $1,227.03 in fire state aid per active member in 2002, and with defined contribution volunteer firefighter relief associations receiving an average of $4,187.73 in fire state aid per active member in 2002. The average per active member fire state aid amounts in 1977 were $378.37 for monthly benefit volunteer firefighter relief associations, $130.01 for lump sum volunteer firefighter relief associations, and $114.22 for defined contribution volunteer firefighter relief associations. Although total municipal contributions to volunteer firefighter relief associations also grew at a 9.75 percent annual compound increase rate over the period 1977-2002, the portion of the volunteer firefighter relief association normal cost paid by the municipal contribution has dropped from 31.5 percent of the normal cost in 1977 to 28.6 percent of normal cost in 2002. The average amount of municipal contribution per active firefighter in 2002 varies, following essentially the same pattern as with the average amount of fire state aid, with combination volunteer firefighter relief associations receiving an average of $1,595.98 in municipal contributions, with monthly benefit volunteer firefighter relief associations receiving an average of $1,108.52 in municipal contributions, with lump sum volunteer firefighter relief associations receiving an average of $305.25 in municipal contributions, and with defined contribution volunteer firefighter relief associations receiving an average of $292.16 in municipal contributions.

Specific Volunteer Firefighter Relief Association Information

Appendix B provides specific funded status, annual financial requirements, financial support, and membership information for the various volunteer firefighter relief associations for the period 1993-2002, the most recent compilation information available from the Office of the State Auditor. Column (7) of the appendix presents the funded ratio of each volunteer firefighter relief association, with defined contribution volunteer firefighter relief associations indicated as 100.00 percent funded. Column (11) of the appendix indicates the financial requirements of the volunteer firefighter relief association under Minnesota Statutes, Section 69.772 or 69.773, which are the normal cost of column (8), any amortization requirement indicated in column (9), the administrative expenses of the volunteer firefighter relief association indicated in column (10) increased by 3.5 percent, and a credit of one-tenth of any funded surplus indicated in column (6). Column (14) of the appendix indicates the minimum municipal obligation towards the volunteer firefighter relief association under Minnesota Statutes, Section 69.772 or 69.773, which are the annual financial requirements of the relief association indicated in column (11) reduced by the fire state aid indicated in column (12) and the expected investment income on assets for lump sum volunteer firefighter relief associations indicated in column (13). Column (15) of the appendix sets forth the municipal contribution to the volunteer firefighter relief association, which can be compared with column (14). Columns (16), (17), and (18) indicate the investment returns of the volunteer firefighter relief association, although the classification criteria between the three columns is not clear. Column (19) of the appendix indicates the total of columns (12), (15), (16), (17), and (18), as well as any miscellaneous (i.e., donations, supplemental benefit reimbursements, etc.) receipts. Columns (20), (21), (22), (23), and (24) of the appendix set forth membership information. Column (25) indicates the amount of fire state aid per active firefighter calculated by dividing the total reported fire state aid amount by the total reported number of active members.

Appendix C provides specific investment portfolio mix and investment return information for the various volunteer firefighter relief associations for the period 1993-2002, the most recent compilation information available from the Office of the State Auditor. Column (2) of the appendix indicates the type of benefit plan of the volunteer firefighter relief association (lump sum, monthly benefit, defined contribution, or combination monthly benefit and lump sum). Column (7) of the appendix indicates the portion of the investment portfolio investment in cash, cash equivalents, or money market investments, totaling columns (5) and (6) and expressing that figure as a percentage of the total assets indicated in column (4). Column (15) of the appendix indicates the portion of the investment portfolio invested in debt-related securities, totaling columns (8), (9), (10), (11), (12), (13), and (14), and treasury bills and bonds, and expressing that figure as a percentage of the total assets indicated in column (4). Column (17) indicates the portion of the investment portfolio invested in annuities, column (16), expressed as a percentage of the total assets indicated in column (4). Column (21) indicates the portion of the investment portfolio invested in stocks and other direct ownership investments, totaling columns (18), (19), and (20), and expressing the figure as a percentage of the total assets indicated in column (4). Column (24) of the appendix indicates the portion of the investment portfolio invested in mutual funds or in an investment mechanism akin to a mutual fund family operated by the State Board of Investment, the Minnesota Supplemental Investment Fund, totaling columns (22) and (23), and expressing that figure as a percentage of the total assets indicated in column (4). Column (25) of the appendix indicates a rough approximation of the dollar-weighted annual rate of return of the volunteer firefighter relief association, calculated as the total of the interest, gains, and investment earnings indicated as columns (16), (17), and (18) appearing in Appendix B, as a percentage of the mean amount of total assets for the year, inherently assuming the bulk of cash flows occurred either evenly throughout the year or on July 1, annually.

Background Information on Common Stock Investment Securities and Exchanges

Appendix D sets forth background information on common stock investment securities and exchanges.

Background Information on Exchange-Traded Funds

Appendix E sets forth background information on exchange-traded funds.

Background Information on the Federal Uniformed Services Employment and Reemployment Rights Act (USERRA)

Appendix F sets forth the background information on the federal Uniformed Services Employment and Reemployment Rights Act (USERRA).

Discussion and Analysis

S.F. 259 (Betzold); H.F. 1706 (Smith) amends various portions of the laws governing volunteer firefighter relief associations, refining the trigger for the required filing of financial reports, specifically enumerates the reporting, funding and investment requirements for compliance determination by the state auditor, requiring the amortization of experience losses in volunteer firefighter relief associations, requiring disclosure of relief association financial requirements and minimum obligation in relief association financial reporting and authorizes the state auditor to obtain 1971 guidelines act funding certifications upon the determination of insufficient funding, clarifying of deduction of reasonably anticipated fire state aid, relaxing the 75 percent maximum on volunteer firefighter relief association mutual fund investments, clarifying the corporate stock and exchange-traded funds as authorized volunteer firefighter relief association investments, adjusting the average financial support per firefighter required for monthly benefit volunteer firefighter relief associations service pension maximum, accommodating defined contribution volunteer firefighter relief associations deferred service pension investment return crediting procedure, revising defined benefit volunteer firefighter relief association fixed rate deferred service pension interest crediting option, requiring volunteer firefighter relief association service credit for military service break-in-service, and revising the municipal representation on volunteer firefighter relief association boards of trustees.

S.F. 259 (Betzold); H.F. 1706 (Smith) raises several pension and related public policy issues that may merit Commission consideration and discussion, as follows:

a. Financial Reporting Trigger.

   1. Appropriate Liability or Asset Breakpoint for Requiring Annual Financial Reports and Audits. The policy issue is the appropriate breakpoint in the amount of assets or liabilities for the imposition of the requirement for the use of greater professional accounting help and the preparation of annual financial reports and audits. Currently, the breakpoint is set at $200,000 in either liabilities or assets. As of the December 31, 2002, compilation of volunteer firefighter relief association information prepared by the State Auditor, 383 volunteer firefighter relief associations, or 54.71 percent of the total number of volunteer firefighter relief associations, had

assets and liabilities under $200,000. By not being required to prepare and file a financial report and audit by an accountant rather than prepare and file a financial statement, these volunteer firefighter relief associations are not gaining the professional assistance that many likely need. These volunteer firefighter relief associations also avoid the several hundreds of dollars in accounting fees that would accompany that professional assistance. Minnesota, with the second largest number of public employee pension plans of the 50 states, has decided to utilize a decentralized approach to pension plan coverage and administration. With that decentralization, there is a substantial risk of substandard or unprofessional activities. Public pension plans function as specialized insurance companies and the operation of an insurance program requires a certain degree of sophistication and attention to detail. With volunteer fire departments, the foremost goal presumably is to achieve a significant degree of competence and professionalism in firefighting. If firefighters also happen to be competent pension plan managers, that is a policy benefit, but attempting to gain pension plan administrative competence could be competing effort or a distraction. Since greater pension plan administrative competence and professionalism can be gained through a contracted consultant, consideration should be given to encouraging that trend by lowering the breakpoint trigger amount that requires the use of a public accountant and the preparation of a full annual financial report.

2. Impact of Reporting Requirements on the Reviews by the Office of the State Auditor for Fire State Aid Qualification. The policy issue is the impact of the financial reporting deadlines on the determination of fire state aid qualification by the Office of the State Auditor and the appropriateness of reconsidering those deadlines. The 1986 financial reporting legislation (Laws 1986, Chapter 359) that required the filing of a financial report and audit by the larger volunteer firefighter relief associations included a change in the deadline date for the review of the Office of the State Auditor and the determination of qualifications for fire state aid. Before 1986, all volunteer firefighter relief associations were required to be file on or before June 1, annually. In 1986, the financial statements by volunteer firefighter relief associations with assets or liabilities under $200,000 were required to be filed by April 1, annually and the financial reports and audits by volunteer firefighter relief associations with assets or liabilities equal to or in excess of $200,000 were required to be filed by July 1, annually. For 2003, the twin reporting deadlines resulted in 55 percent of the volunteer firefighter relief associations obligated to file before April 1 (90 days after the fiscal year end) and 45 percent of the volunteer firefighter relief associations obligated to file before July 1 (180 days after the fiscal year end). The Commission file on the 1986 legislation does not shed light on the specific rationale for the two particular reporting dates. The 2004 filings with the Office of the State Auditor indicate a potential trend for later and later volunteer firefighter relief association filings, which undoubtedly negatively impacts on the scheduling of the workload of that office. If a better allocation of the workload of the State Auditor’s office is desired by policymakers or by volunteer firefighter relief association community, that improved allocation can be accomplished either by volunteer firefighter relief association self-help efforts or by further revisions in the filing deadlines.

3. Appropriateness of Pursuing a Collective Approach for Improved Volunteer Firefighter Relief Association Financial Reporting. The policy issue is whether or not it would be appropriate for volunteer firefighter relief associations to pursue a more collective approach to providing financial reporting. Both municipal governments and local pension plans have engaged in collective arrangements for the performance of functions in the past and some collective approach may be appropriate in this instance. In the late 1970s, when required to improve their actuarial reporting, the then 48 local police and paid firefighter relief associations collectively retained a consulting actuarial firm to prepare the necessary reporting with greater cost efficiency. Minnesota cities have entered into collective arrangements to gain or provide services, such as the League of Minnesota Cities Insurance Trust to provide property and casualty insurance coverage and workers’ compensation coverage. Several Pennsylvania municipal pension plans contract with a common third party pension plan administrator for plan administration, financial reporting, and actuarial reporting. Under the auspices of the Minnesota Fire Department Association, the Minnesota Area Relief Association Coalition, the Minnesota Fire Chiefs Association, and the League of Minnesota Cities, volunteer firefighter relief associations could engage one accounting firm statewide or several accounting firms regionally to prepare the required financial reports and audits, presumably with greater expertise than is available with the myriad collection of accountants currently providing these services and at a more competitive cost.

b. Collected Enumeration of Fire State Aid Eligibility Requirements (Section 3).

1. Appropriateness of Specifically Enumerating Fire State Aid Qualification Requirements. The policy issue is the appropriateness of replacing the general fire state aid qualification standard statement for the Office of the State Auditor in Minnesota Statutes, Section 69.771, with a detailed list of fire state aid qualification requirements. The replacement of a generalized review requirement with a specific set of compliance requirements will assist both volunteer firefighter relief associations and the Office of the State Auditor and will provide clarity to the fire state aid qualification process. The Legislature has used fire state aid as a tool to attempt to improve fire department capabilities, to improve volunteer firefighter relief association funding, to insure appropriate volunteer firefighter relief association investment practices, to insure compliance with the flexible service pension maximums, and to discourage inappropriate administrative expenditures and practices. To further these goals and to provide both the regulator and the regulated with the standards by which compliance is to be determined, the replacement of a generic statement of the State Auditor's responsibility with the specific requirements is likely to be a more effective provision of law.

2. Appropriateness of Evaluating Monthly Benefit Volunteer Firefighter Relief Association Funding in Gross. The issue is the appropriateness of determining municipal compliance with the volunteer firefighter relief association funding requirement in gross rather than in components for monthly benefit volunteer firefighter relief associations. Proposed Minnesota Statutes, Section 69.771, Subdivision 3, Paragraph (c), Clause (5), relating to monthly benefit volunteer firefighter relief associations, specifies a funding level compliance standard that compares the total volunteer firefighter relief association funding requirement with the total relief association financial support, rather than focusing on the minimum municipal requirement and the actual municipal contribution. The proposed "funding in gross" requirement is an accommodation to the greater professionalism and greater presumed accuracy of the monthly benefit volunteer firefighter relief association funding requirement determination process that was recommended by one of the actuarial consulting firms retained by Minnesota monthly benefit volunteer firefighter relief associations. Use of actuarial valuations by monthly volunteer firefighter relief associations rather than the simpler liability table process used by lump sum volunteer firefighter relief associations does involve a pension expert in the process and should involve more rigorous determinations. Comparing the funding requirements and total financial support at large achieves the Commission's pension funding goal without requiring the Office of the State Auditor to spend the extra effort to chase the component funding elements.

c. Appropriateness of Requiring the Filing of 1971 Volunteer Firefighter Relief Association Financing Guidelines Act Certification Upon Insufficient Funding (Sections 5 and 7). The policy issue is the appropriateness of requiring volunteer firefighter relief associations and municipal officials to file their annual funding certifications with the Office of the State Auditor upon request. The 1971 Volunteer Firefighter Relief Association Financing Guidelines Act sets forth a process that, if followed, will result in a volunteer firefighter relief association being properly and timely funded. The process, currently, is wholly local, depending on certifications by the relief association officers to the municipalities, without the direct involvement by the Office of the State Auditor. The proposed change would permit the Office of the State Auditor to validate whether or not the 1971 Guidelines Act process was being followed when the annual financial report of the relief association indicates a funding shortfall, but would not burden the relief association and municipal officials unless there is evidence of a problem and would not burden the Office of the State Auditor with the collection of a greater volume of paper. There is anecdotal information that compliance with the 1971 Guidelines Act certification requirements and timing is lacking in a number of volunteer firefighter relief associations and the trend may be increasing. Clarifying that the Office of the State Auditor can request the 1971 Guidelines Act certification may help reverse that trend.

d. Lump Sum Volunteer Firefighter Relief Association Experience Loss Amortization Requirements (Sections 4 and 6).

1. Appropriateness of Clarifying the Lump Sum Volunteer Firefighter Relief Association Amortization Procedure. The policy issue is the appropriateness of modifying the lump sum volunteer firefighter relief association amortization period so Minnesota Statutes, Section 69.772, reflects the longstanding practice utilized in the Department of Commerce, State Auditor's Office forms. Minnesota Statutes, Section 69.772, Subdivision 3, provides that the 1971 unfunded liability be amortized over ten years, with one-tenth of the 1971 unfunded liability amount paid per year, and that the unfunded liability from post-1971 benefit increases also be amortized over ten years from the year of the service pension increase, with one-tenth of

the original benefit increase unfunded liability amount paid per year. The schedules that have been used by the Department of Commerce previously and the State Auditor's Office currently require the remaining unfunded liability amount from the last nine years and any new unfunded liability amount from the current year to be totaled, with one-tenth of that total amount required to be paid in the year following the calculation. The two procedures appear to result in a lump sum volunteer firefighter relief association amortizing its unfunded liability over ten years with an essentially similar stream of municipal contributions, so having the law reflect the actual practice used by most volunteer firefighter relief associations, even if implemented without prior legislative authority, achieves the policy end intended. The year in which the departure from the precise strategy procedure first occurred has not been determined and may not be determinable.

2. Appropriateness of Amortizing Experience Losses. The policy issue is the appropriateness of adding a requirement that all lump sum, monthly benefit, and combination volunteer firefighter relief associations amortize their experience losses. For lump sum volunteer firefighter relief associations, the sole experience loss will be investment losses. For monthly benefit and combination volunteer firefighter relief associations, experience losses can be investment losses, mortality losses, and retirement age losses. For an undeterminable reason, because few contemporaneous records remain from the 1970-1971 Commission deliberations on the issue, the Volunteer Firefighter Relief Association Financing Guidelines Act of 1971 (Laws 1971, Chapter 261) did not require the amortization of these experience losses. Since experience losses can, and do, occur and the policy end is to insure that volunteer firefighter relief associations do become fully funded over a reasonable period of time, the experience loss amortization requirement appears appropriate.

3. Appropriateness of Ten-Year Amortization Period for Both Lump Sum and Monthly Benefit Volunteer Firefighter Relief Associations. The policy issue is the appropriateness of specifying a ten-year amortization period for all defined benefit plan volunteer firefighter relief associations.

4. Appropriateness of Setting an Annual Limit on the Lump Sum Volunteer Firefighter Relief Association Amortization Contribution. The policy issue is the appropriateness of limiting the annual amortization contribution requirement of a lump sum volunteer firefighter relief association at the amount of the remaining unfunded liability. The staff of the Pension Oversight Division of the State Auditor's Office indicate that in some unusual instances, under the current lump sum volunteer firefighter relief association amortization procedures used in the State Auditor's forms, a large unfunded amount in one prior year and nominal unfunded amounts in the balance of the ten years can result in a computed amortization contribution that is greater than the total unfunded liability, making the city required contribution larger than it otherwise needs to be in order to achieve the policy goal of lump sum volunteer firefighter relief associations working towards full funding.

e. Deduction of Reasonably Anticipated Fire State Aid Amounts (Sections 4 and 7).

1. Appropriateness of a Statutory Requirement of Including "Reasonably Anticipated" Fire State Aid in Volunteer Firefighter Relief Association Funding Determination. The policy issue is the appropriateness of requiring volunteer firefighter relief association officials to use a "reasonably anticipated" fire state aid amount in calculating minimum municipal obligations towards volunteer firefighter relief associations. The State Auditor's Office has required for some period of time the use of a reasonably anticipated fire state aid amount in reviewing the minimum city contribution to its volunteer firefighter relief associations, without absolute statutory clarity on the requirement. The proposed change would be to add a very specific requirement that the fire state aid deduction amount be a "reasonably anticipated" amount. The use of unreasonably determined anticipated fire state aid amounts appears difficult to defend, since any short-term advantage produced by such manipulation will damage the volunteer firefighter relief association over the longer term.

2. Appropriateness of the Proposed Definition of the Maximum Amount of Reasonably Anticipated Fire State Aid. The policy issue is the appropriateness of defining the maximum amount of the reasonably anticipated fire state aid as the prior year's aid multiplied by the factor 1.035. Fire state aid amounts do vary over time, but generally increase modestly year to year. The following compares the fire state aid amounts for 11 years for four volunteer firefighter relief associations somewhat randomly:

Ada	Finland	Montevideo	Zumbo Falls

Year	$	% Incr.	$	% Incr.	$	% Incr.	$	% Incr.
1993	6,860	--	3,058	--	12,797	--	4,870	--
1994	7,206	+5.04	3,222	+5.36	13,691	+6.98	5,177	+6.30
1995	7,713	+7.04	2,549	-20.89	14,406	+5.22	5,545	+7.11
1996	9,803	+27.10	5,820	+128.3	18,812	+30.58	7,173	+29.41
1997	9,307	-5.10	5,769	-0.88	18,393	-2.22	6,961	-3.00
1998	9,427	+1.29	6,889	+18.37	19,168	+4.21	7,361	+5.75
1999	9,641	+2.27	7,068	+2.60	19,886	+3.75	7,556	+2.65
2000	9,746	+3.38	7,245	+2.50	20,437	+2.77	7,820	+3.49
2001	8,856	-9.13	7,185	-0.01	20,504	+0.33	7,838	+0.20
2002	9,683	+9.34	6,200	-13.71	23,035	+12.34	9,005	+14.89
2003	11,383	+17.56	7,758	+25.13	27,628	+19.94	11,091	+23.16
Annual Compound Rate		4.70%		9.00%		7.25%		7.75%

The 3.5 percent increase rate incorporated into the reasonableness maximum is an expansion of the historic view of the State Auditor's Office, which was the prior fire state aid amount without any increase and parallels the inflation factor used in calculating an anticipated administrative expense figure.

f. Volunteer Firefighter Relief Association Mutual Fund Investment Maximum (Section 8).

1. Appropriateness of the 75 Percent Mutual Fund Investment Limitation. The policy issue is the appropriateness of the current 75 percent market value maximum on mutual fund investments by volunteer firefighter relief associations under Minnesota Statutes, Section 69.775. The volunteer firefighter relief association mutual fund investment maximum replicates the maximum applicable to the local police and paid fire relief association maximum enacted in 1969 in Minnesota Statutes, Section 69.77. In 1969, Minnesota Statutes 1969, Section 11.16, governing the authorized investments for the State Board of Investment, did not appear to permit mutual fund investments by the State Board of Investment. A de facto family of mutual funds operated by the State Board of Investment, the Minnesota Supplemental Investment Fund, was created in 1967 and the 1969-1971 local police and fire relief association guidelines acts included authority of the local relief association to utilize the Minnesota Supplemental Investment Fund. The 75 percent mutual fund investment maximum was part of the 1969-1971 enactments and has not been modified since 1971. The Commission's records on the 1969 and 1971 Sessions do not include anything that sets forth the sense of the policy discussion or discussions that resulted in the specific percentage. The provision was clearly intended, along with the Minnesota Supplemental Investment Fund authority, to encourage local relief associations to utilize available investment management services rather than engaging in active investment management themselves. The selection of a limit lower than 100 percent probably reflected both diversification and liquidity considerations, although this is Commission staff conjecture.

2. Appropriateness of the Exception for Money Market Mutual Fund Investments. The policy issue is the appropriateness of the proposed exception in calculating the 75 percent mutual fund investments for money market mutual fund investments. The proposal attempts to address a practical problem of some volunteer firefighter relief associations which utilize mutual funds heavily, including money market mutual fund investments for liquidity purposes, and hit the current maximum periodically as market values change. By excluding money market mutual fund investments, these volunteer firefighter relief associations will have some additional margin for error before they reach the maximum. These relief associations, however, have a non-legislative remedy to the problem if the relief association utilized the State Board of Investment's Minnesota Supplemental Investment Fund for either its money market needs, since the Minnesota Supplemental Investment Fund has a money market account, or its other mutual fund-like investment needs, since the Minnesota Supplemental Investment Fund has six other accounts (Income, International, Fixed Interest, Bond Market, Common Stock, and Growth). The Minnesota Supplemental Investment Fund provides a mutual fund-like investment approach, but does not count against the 75 percent mutual fund investment maximum. A number of volunteer firefighter relief associations, however, have been disinclined to invest with the State Board of Investment.

3. Appropriateness of Providing an Incentive for Money Market Mutual Fund Investments Beyond Liquidity Needs. The policy issue is the potential that the proposed change would induce some volunteer firefighter relief associations to change their asset mix and invest in money market mutual fund exposure in excess of the maximum and not for liquidity needs. The optimal use of money market mutual fund investments would be to meet liquidity needs, either because of

impending retirements that necessitate holding a certain amount of cash or because of the need to amass cash when changing its portfolio mix or when reacting to investment market fluctuations. Cash equivalents, including money market mutual fund investments, have an appropriate role in pension fund investments, but rarely would that role be as a long-term investment. The proposed change could become an unintended incentive to increase long term investments in money market mutual funds. To clarify that the proposed exception is not to provide this unintended incentive, Amendment LCPR05-016 would specify that the proposed exception is limited to money market mutual fund investments to those necessitated by liquidity needs. The amendatory language would indicate a policy perspective and would not be readily enforceable however.

g. Expanded Volunteer Firefighter Relief Association Investment Security Authorization (Section 9).

1. Appropriateness of the Potential Corporate Stock Expansion. The policy issue is the appropriateness of modifying the corporate stock authorized investment provision to expand to stocks listed on any exchange regulated by an agency of the U.S. government or an agency of the Canadian national government. The potential change replicates a change enacted for the State Board of Investment in Minnesota Statutes, Section 11A.24, Subdivision 5, in 2000 (Laws 2000, Chapter 392, Section 1). The 2000 State Board of Investment corporate stock change, however, was a portion of a bill primarily related to the medical education endowment fund and the tobacco use prevention and local public health endowment fund and was not reviewed or recommended by the Commission. Under the proposed change, the number of corporate stocks available for investment, if they also meet the prudent person rule, would increase from those listed on two exchanges to those listed on at least seven exchanges. While the number of additional corporate stocks authorized under the potential change is unclear, the additional corporate stocks will generally be capitalized to a lesser extent and will generally be more recently issued. Both characteristics would increase the risk of corporate failure beyond the risk of a loss of corporate stock value.

2. Appropriateness of the Specific Authorization of Exchange-Traded Funds. The policy issue is the appropriateness of specifically authorizing the investment of Minnesota public pension plan assets in exchange-traded funds (ETFs). ETFs are derivatives, representing primarily corporate stocks, but not having a net asset value. According to the Securities and Exchange Commission (SEC), the chief benefits of ETFs for individual investors are to provide trading flexibility, which is important for investment strategies that include market timing, to allow for purchases of ETF shares on margin, and to be able to sell ETF shares short. The chief benefits to ETFs for institutional investors, according to the SEC, are to gain the advantages of an index derivative where investment restrictions may preclude index derivatives, to use ETFs as substitutes for index futures without margins or expiration dates, to use in hedging strategies, or to invest cash in a broad market segment during temporary investment management or strategy transitions. Commentators also note that ETFs have lower expense ratios than mutual funds, but incur broker commissions on their purchase and sale, which make them unattractive compared to mutual funds, and that ETFs can trade at a premium or discount in relation to the net asset value of the underlying securities, opening up arbitrage opportunities. From the available information on ETFs, they appear to be a security generated more as a marketing tool than as a result of investor need or demand and they do not appear to provide any discernible investment portfolio advantage to volunteer firefighter relief associations. The Legislative Commission on Pensions and Retirement would be well advised to take testimony from volunteer firefighter relief associations and other similar institutional investors about ETFs' place in pension plan investing before recommending the change.

3. Need to Consider Other 2000 State Board of Investment Recommended Changes. The policy issue is the question of whether or not the other investment authority changes of Laws 2000, Chapter 392, proposed by the State Board of Investment would also be appropriate for volunteer firefighter relief associations. Laws 2000, Chapter 392, Sections 1 and 2, chiefly expanded various segments of the "other investments" portion of the State Board of Investment authorized investment law, Minnesota Statutes, Section 11A.24. The 2000 State Board of Investment recommended changes in question are the following:

    a. 20 Percent Limit on Closed-End Mutual Fund Shares. A limit of 20 percent of the shares of a closed-end mutual fund was added to the corporate stock investment authorization.

b. Venture Capital Investments. Investments in venture capital investment businesses were expanded beyond limited partnership and corporations to include trusts, private placements, limited liability corporations, limited liability companies, and limited liability partnerships.

c. Regional and Mutual Funds. Investments in regional and mutual funds through bank sponsored collective funds and open-end investment companies were expanded to include closed-end mutual funds listed on an exchange regulated by a governmental agency.

d. Resource Investments. Investments in resource investments through limited partnership, private placements, and corporations were expanded to include trusts, limited liability corporations, limited liability companies, and limited liability partnerships.

These changes were deemed to be appropriate for the State Board of Investment in 2000, but as of yet have not been considered for all other Minnesota public pension plan investment operations. If the primary argument for the expansion of exchanges for authorized corporate stocks is the precedent of the State Board of Investment in 2000, some consideration should also be given to the wisdom of these changes. To fully replicate the 2000 State Board of Investment changes, Amendment LCPR05-017 would add the items specified in points a. through d. above.

4. Appropriate Extent of Volunteer Firefighter Relief Association "Other Investments." The policy issue is the appropriate portion of a volunteer firefighter relief association's portfolio should be permitted to be in "other investments" under Minnesota Statutes, Section 356A.06, Subdivision 7, paragraph (g). Current law permits investment in a large number of historically non-traditional securities with a 35-percent of market value limit on the aggregate amount of "other investments," a requirement of a minimum of four other unrelated owners in the investment other than international securities with a 20-percent maximum on the investment by a covered pension plan in an investment vehicle, other than international securities, and with a requirement that the covered pension plan in a limited partnership not be general partner or have general liability. The whole category of "other investments" was created for the State Board of Investment and only emerged in 1981 (Laws 1981, Chapter 208, Section 6), when the State Board of Investment was seeking higher rates of return in response to prior criticism leveled by State Auditor Arne Carlson. The volunteer firefighter relief associations gained the "other investment" authority by being indexed to the investment authority of the State Board of Investment before 1994, not by having volunteer firefighter relief associations independently argue for that special legislative authority. The "other investment" category for volunteer firefighter relief associations appears to have created marketing opportunities for investment security sales personnel, but does not appear to be generally suitable for most volunteer firefighter relief associations or to have contributed to good volunteer firefighter relief association investment performance. According to the 2002 State Auditor's Investment Disclosure Report, only two percent of volunteer firefighter relief association assets (excluding the Eden Prairie Volunteer Firefighter Relief Association) are invested in "other" assets (although the statutory category "other investments" is not purely synonymous with the "other" category) and volunteer firefighter relief associations produced a 9.6 percent total time-weighted rate of return investment loss in 2002. Arguments can be made that investments in "other investments" as a kind are inappropriate for volunteer firefighter relief associations or that investments in "other investments" with outside vendors are inappropriately driven by marketing concerns and marketing pressures. Amendment LCPR05-018 would prohibit all new investments in "other investments" by volunteer firefighter relief associations. Amendment LCPR05-019 would prohibit the investment by volunteer firefighter relief associations in "other investments" except through the Minnesota Supplemental Investment Fund operated by the State Board of Investment. Amendment LCPR05-020 clarifies that the unrelated investor restrictions of the "other investments" provision requires investors other than the State Board of Investment and all Minnesota covered pension plans.

5. Appropriateness of a Specific Prohibition of Volunteer Firefighter Relief Association Investments in Junk Bonds. The policy issue is the potential need for and the appropriateness of a specific prohibition of investments in junk bonds by volunteer firefighter relief associations. In 1994 (Laws 1994, Chapter 604, Article 2, Section 3), the current legal list of authorized investments for Minnesota retirement plans other than those invested by the State Board of Investment replaced a cross-reference to Minnesota Statutes, Section 11A.24, accompanying an expansion of the investment authority of the State Board of Investment (see Laws 1994, Chapter 604, Article 1, Sections 7, 8, 9, 10, and 11), in which the State Board of Investment gained authority to invest in unrated corporate obligations (i.e., junk bonds). The intent of the specific legal list for non-State Board of Investment retirement plans was to exclude those plans from the

expansion in investment authority for the State Board of Investment. That intent is clear from the legislative history of Minnesota Statutes, Section 356A.06, Subdivision 7, compared to Minnesota Statutes, Section 11A.24, but the intent may not be conveyed by a reading of Minnesota Statutes, Section 356A.06, Subdivision 7, alone. For a clearer statement of the investment authority of retirement plans which are not invested by the State Board of Investment, specific prohibitions of junk bonds and similar investment securities should be added to Minnesota Statutes, Section 356A.06, Subdivision 7. Amendment LCPR05-021 specifically bans junk bonds for volunteer firefighter relief associations. Amendment LCPR05-022 specifically bans junk bonds for all retirement plans that are not invested by the State Board of Investment. Amendment LCPR05-023 bans for volunteer firefighter relief associations all investment securities which are permitted for the State Board of Investment under Minnesota Statutes, Section 11A.24, and are not specifically authorized under Minnesota Statutes, Section 356A.06. Amendment LCPR05-024 bans for all retirement plans which are not invested by the State Board of Investment all investment securities which are permitted for the State Board of Investment under Minnesota Statutes, Section 11A.24, and are not specifically authorized under Minnesota Statutes, Section 356A.06.

h. Monthly Benefit Service Pension Average Financing Per Firefighter Modification (Section 10).

1. Appropriateness of a Reduction in the Required Funding for Monthly Service Pensions. The policy issue is the appropriateness of a reduction in the funding required for a given monthly service pension amount under the flexible service pension maximums. The proposed $81 required average per firefighter financing requirement is based on Commission staff research. The Office of the State Auditor provided the Commission staff with data from the monthly benefit volunteer firefighter relief association actuarial valuations. The Commission staff reviewed the data and removed a few cases which would distort results, such as data which claimed that a plan was providing a monthly benefit but the indicated normal cost was zero, and examined the relationship between normal cost per member as determined from the actuarial valuations, and benefit levels per month per year of service provided by these plans and that information suggests that for every one-dollar increase in monthly benefit per year of service, the normal cost of the plan will increase by $77.70. The Commission staff found that there is little justification for suggesting that a different relationship exists at lower levels than at higher levels. The variability is higher at higher benefit levels and that revised statistical approach produced a similar result, suggesting that for each dollar increase in monthly benefits, the normal costs increases by $78.40. The proposed change would split the difference between the flexible service pension maximum schedule in existing law, which generally requires a support level increase of $84 for each one dollar increase in monthly benefits, and the approximately $78 increase in support for each one dollar increase in benefits suggested by the Commission staff study, or a requirement of an $81 increase in support for each one dollar increase in monthly benefit per year of service to produce a result that is reasonably conservative.

2. Appropriateness of Encouraging Monthly Benefit Volunteer Firefighter Relief Association Benefit Increases. The policy issue is the appropriateness of the encouragement for immediate monthly benefit volunteer firefighter relief association benefit increases that a reduction in the required average financing requirement per firefighter will likely produce. By virtue of the change, every monthly benefit volunteer firefighter relief association could increase its benefit by at least one dollar per month per year of service without any increase in the current level of the relief association average financing per firefighter. Any benefit increase, however, would require municipal approval unless the relief association is exceedingly well funded before and after the benefit increase. While the current flexible service pension maximum three-year average financing requirement for any given level of benefits is clearly very conservative, promoting a benefit increase without a showing for each relief association that the current benefit level is insufficient to recruit new firefighters, to retain existing firefighters, and to systematically out-transition senior firefighters.

3. Appropriate Timing for Implementation. The policy issue is the appropriateness of the proposed timing for implementing the proposed change in the monthly benefit volunteer firefighter relief association flexible service pension maximums average financing requirements. The proposed timing for implementation would be July 1, 2005. Alternative effective dates could be an accelerated date, the day following enactment, or could be a delayed date, either December 31, 2005, or some later date.

4. Appropriateness of Grandparenting the Immediately Prior Service Pensions Amount as a Maximum Service Pension Amount. The related policy issue is the appropriateness of

reinstating language from the original 1979 volunteer firefighter relief association recodifications and revisions that retains the prior service pension amount as the maximum service pension amount if the prior amount I s greater than the calculated maximum amount under the flexible service pension sliding scale procedure. The provision was eliminated in 1993 (Laws 1993, Chapter 244), when vetoed 1992 volunteer firefighter relief association legislation was reenacted by the Legislature, in favor of current Minnesota Statutes, Section 424A.02, Subdivision 3, Paragraph (f). Apparently, there are instances when the average amount of financing per firefighter drops for reasons unrelated to a relation ship of fire state aid or an increase in the number of firefighters and the post-1993 statute would cause an unintended benefit reduction by a volunteer firefighter relief association. The reincorporation of the pre-1993 language would avoid this hardship. Amendment LCPR05-025 adds the pre-1993 language.

i. Defined Contribution Volunteer Firefighter Relief Association Deferred Service Pension (Sections 11 and 12).

1. Appropriateness of Special Defined Contribution Volunteer Firefighter Relief Association Deferred Service Pension Interest Rule. The policy issue is the appropriateness of augmenting the general volunteer firefighter relief association deferred service pension interest rules for defined contribution volunteer firefighter relief associations. The current general deferred service pension rules include options that are entirely workable for defined contribution volunteer firefighter relief associations, either no interest, interest at the rate equal to the time-weighted total rate of investment return as reported by the State Auditor's office, or the investment performance earned by a separate investment account or by a separate investment vehicle, and one option that is not workable fore defined contribution volunteer firefighter relief associations, interest set at a five percent rate. The philosophy of the volunteer firefighter community appears to have changed over the 25 years since the passage of Minnesota Statutes, Chapter 424A, the volunteer firefighter relief association law recodification, from minimal or nominal interest in providing any reward to deferred members in 1979 to considerable interest in rewarding deferred members in 2004. The policy goal of the Legislature in the 1979 recodification was to permit interest on deferred service pensions where a volunteer firefighter relief association is interested in doing so, but also to protect the actuarial health of the relief association. In the 2000 amendments to Minnesota Statutes, Section 424A.02, Subdivision 7, the Minnesota Area Relief Association Coalition (MARAC) sought to allow deferred service pensioners to share in investment returns greater than the five percent interest assumption that underlies volunteer firefighter relief association actuarial work. The resulting 2000 legislation recommended by the Commission provided the separate account/separate investment vehicle as a means to provide greater investment return consistent with actuarial concerns and limitations. The proposed change, allowing defined contribution volunteer firefighter relief associations to include deferred members in the allocation of investment returns with active members as an additional deferred service pension option, minimizes the administrative complexity of the interest crediting practice for defined contribution volunteer firefighter relief associations while avoiding any threat to the actuarial condition of the relief association or the allocation of benefits within the relief association.

2. Need for a Clarification of the Timing of Interest Return Crediting. The policy issue is the need for a clarification in the manner in which a defined contribution volunteer firefighter relief association recognizes and credits investment performance to active member accounts and deferred service pension accounts. The 1979 volunteer firefighter relief association recodification specifically authorized the existing "split-the-pie" volunteer firefighter relief associations and future defined contribution volunteer firefighter relief associations, but the defined contribution volunteer firefighter relief association provision, Minnesota Statutes, Section 424A.02, Subdivision 7, did not regulate the totality of defined contribution retirement plan operations and practices. Defined contribution volunteer firefighter relief associations existed before 1979, with an active membership range of a low of 14 active members (Milroy) and a high of 42 active members (Hopkins) and an average number of active members of 25, an average asset size of $28,886, an average annual fire state aid amount of $2,848, a frequency of municipal contributions of 40 percent, and an average annual municipal contribution of $431. In 2002, defined contribution volunteer firefighter relief associations have grown in number, to 88, with an active membership range of a low of 10 active members (Crane Lake and Ellsburg) and a high of 98 active members (Eagan) and an average number of active members of 25, an average asset size of $493,547, an average annual fire state aid amount of $29,990, a frequency of municipal contributions of 52.3 percent, and an average annual municipal contribution of $7,377. Some growth in defined contribution volunteer firefighter relief associations has been from new

relief associations, such as the Gunflint Trail Volunteer Firefighter Relief Association and the Vermilion Lake Volunteer Firefighter Relief Association, but the growth in defined contribution volunteer firefighter relief associations also has come from relief associations that did so in order to exceed the uppermost limit of the service pension maximums, such as the Anoka-Champlin Volunteer Firefighter Relief Association and the Eagan Volunteer Firefighter Relief Association. With the growth of defined contribution volunteer firefighter relief associations, their funding and assets, and their active membership, the operation of these plans has become more complicated in investing and in crediting investment returns. The proposed change would allow defined contribution volunteer firefighter relief associations to establish specific dates for and procedures for crediting investment performance and would require deferred retirees to recognize those dates. Thus, if a defined contribution volunteer firefighter relief association only credits investment performance as of the first of each month, a retiring deferred service pensioner would sacrifice a portion of a month's investment performance if the person desires to receive the service pension payment on their birthday mid-month.

j. Deferred Service Pension Interest (Section 12).

1. Appropriate Role of Deferred Service Pensions and the Extent of Relief Association Encouragement of Deferrals. The policy issue is the question of the appropriate role of deferred service pensions and interest on deferred service pensions and the extent of desirable encouragement by relief associations of service pension deferrals. The philosophy of the volunteer firefighter community appears to have changed over the 25 years since the passage of Minnesota Statutes, Chapter 424A, the volunteer firefighter relief association law recodification, from minimal or nominal interest in providing any reward to deferred members in the past to considerable interest in rewarding deferred members currently. The policy goal of the Legislature in the 1979 recodification was to permit interest on deferred service pensions where a volunteer firefighter relief association was interested in doing so, but to do so in a manner that would protect the actuarial health of the relief association. In the 2000 amendments to Minnesota Statutes, Section 424A.02, Subdivision 7, the Minnesota Area Relief Association Coalition (MARAC) sought to allow deferred service pensioners to share in investment returns greater than the five percent interest assumption that underlies volunteer firefighter relief association actuarial work. The resulting 2000 legislation recommended by the Commission provided the separate account/separate investment vehicle as a means to provide a greater investment return on deferred service pensions and reward deferred service pensioners in a manner consistent with actuarial concerns and limitations. If the volunteer firefighter community desires to encourage volunteer firefighters to defer a service pension prior to reaching age 50 rather than to attempt to half-heartedly continue in active fire department service, deferred service pensions can be encouraged by providing interest on the pension amount during the deferral period. Greater interest on a deferred service pension will presumably provide a greater degree of encouragement, but the amount of interest should be consistent with the actuarial design of the volunteer firefighter relief association. Deferred service pension interest that does not exceed five percent is consistent with the actuarial design of volunteer firefighter relief associations.

2. Appropriateness of Eliminating the Flat Five Percent Interest Option. The policy issue is the appropriateness of eliminating the current flat five percent deferred volunteer firefighter service pension interest rate. The flat five percent rate option was introduced in 2000 (Laws 2000, Chapter 461, Article 15, Section 6), when the two prior options (i.e. no interest and interest at the relief association's actual investment performance rate up to five percent) were also expanded to include investment of the deferred service pension amount in a separate account or a separate investment vehicle where the deferred service pensioner bears the full investment risk of gain and loss. The five percent deferred service pension rate matches the five percent interest assumption that underlies the funding of volunteer firefighter relief associations, meaning that a volunteer firefighter relief association does not take on any extraordinary risk of an unexpected funding loss by implementing the flat five percent interest rate.

3. Appropriateness of Setting Deferred Service Pension Interest at a Board-Established Rate. The policy issue is the appropriateness of permitting the volunteer firefighter relief association boards to set the interest rate on deferred service pensions at the discretion of the boards, subject to a five percent interest rate maximum. Since five percent is the underlying interest rate assumption, an interest rate on deferred service pensions set at less than five percent is not required to maintain the actuarial soundness of volunteer firefighter relief associations. The decision of a relief association board to credit deferred lump sum service pensions with less than

a five percent interest rate logically must be driven by some other motivation, either a lack of confidence in the relief association's investment operation or a lack of commitment to deferred service pensioners. If a relief association's investments are unlikely to achieve a five percent average rate of investment performance, when the State's statewide and major local pension plans are expected to achieve an 8.5 percent average return, the efficiency and prowess of the relief association's investment program is seriously challenged. If the relief association lacks a commitment to deferred service pensioners, it raises the question of the rationale for the provision of any interest on deferred service pensions.

4. Appropriateness of Potentially Fluctuating Deferred Service Pension Interest Rates. The policy issue is the appropriateness of permitting volunteer firefighter relief associations to change the interest rate on deferred service pensions biannually, annually, semi-annually, or even monthly. If a relief association attempts to change the deferred service pension interest rate on a relatively frequent basis, the frequency of the potential changes will become administratively burdensome for the relief association and for the applicable municipality. Frequent changes in the interest rate creditable to deferred service pensions also will make the decision by a firefighter to defer a service pension more uncertain and potentially undesirable in achieving the overall goal of having a volunteer firefighter relief association service pension program.

k. Military Service Credit (Section 13).

1. Need to Address Defined Contribution Volunteer Firefighter Relief Associations. The policy issue is the question of whether or not it is necessary to include comparable membership inclusion language for defined contribution volunteer firefighter relief associations. Roughly 50 volunteer firefighter relief associations are defined contribution plans, where the principal benefit of volunteer firefighter relief association membership is inclusion in the allocation of fire state aid, any municipal contribution, and any investment return. The current language applies only to defined benefit plans. Amendment LCPR05-026 attempts to add language for defined contribution volunteer firefighter relief associations with a comparable coverage effect.

2. Proper Effective Date for Provision. The policy issue is the question of the date on which the provision will apply. The provision currently is limited to military service breaks in service occurrences that conclude on or after July 1, 2005. As such, the provision is not retroactive back to uniformed service periods that have already concluded. If the provision is determined to be required to have more retroactivity, Amendment LCPR05-027 would allow for an earlier effective date.

l. Volunteer Firefighter Relief Association Municipal Representation (Section 14).

1. Appropriateness of the Shift from Ex-Officio Municipal Representation to City Council-Appointed Municipal Representation. The policy issue is the appropriateness of shifting from ex-officio municipal representatives on volunteer firefighter relief association boards of trustees to elected or appointed municipal officials appointed by the municipal governing board. Currently, there are three municipal representatives on most volunteer firefighter relief association boards of trustees, the mayor, the finance director/city clerk, and the fire chief. The change would replace the mayor and the finance director/city clerk with two elected or appointed officials of the municipality who are appointed by the city council. The change is intended to provide greater flexibility to municipalities and to improve interest and participation in relief association affairs by municipal representatives. Although the municipal representation on volunteer firefighter relief association boards of trustees has remained unchanged since 1907, when first regulated by State law, the process appears to have problems. As municipal mayors have become busier in official duties and volunteer firefighter relief association laws become less problematic by virtue of significant increases in fire state aid, participation by mayors and city finance directors apparently has become more sporadic. The proposal would utilize the same process that municipalities currently employ to fill positions on municipal advisory and regulatory commissions, with city council appointment of representatives to the volunteer firefighter relief association board of trustees. The representatives are required to be municipal officials, either elected or appointed.

2. Appropriateness of One-Year Terms for Municipal Representatives on Volunteer Firefighter Relief Association Boards of Trustees. The policy issue is the appropriateness of limiting the term of the municipal representatives on a volunteer firefighter relief association board of trustees to one year. Currently, the term of office of the ex-officio municipal representative on the volunteer firefighter relief association board of trustees is the term of office of the mayor or the duration in office of the municipal finance director or the city clerk. The change in the term

could result in a musical chairs situation on the municipal representative portion of the volunteer firefighter relief association board of trustees. Since the municipality is less well represented quantitatively than the volunteer firefighter relief association active membership, any further impairment of city representation by having those representatives constantly changing may leave the city with no effective representation.

3. Appropriateness of a Reduction in the Municipal Representation for Volunteer Firefighter Relief Associations Associated with Nonprofit Firefighting Corporations. The policy issue is the appropriateness of a proposed reduction in municipal representatives from three to two on the board of trustees of volunteer firefighter relief associations associated with independent nonprofit firefighting corporations. The current municipal representation for independent nonprofit firefighting corporation volunteer firefighter relief associations was incorporated into the volunteer firefighter relief association recodification in 1979 and did not have any earlier rendition. If the change for independent nonprofit firefighting corporations, paralleling the proposed procedure for municipalities, results in a volunteer firefighter relief association board that has a full complement of interested and competent members, the change is valuable. If the reduction in municipal representation results in some municipalities becoming unrepresented, the change may harm overall firefighting-related operations in local government.

4. Appropriateness of Proposed Joint Powers Entity and Township Representation on Volunteer Firefighter Relief Associations. The policy issue is the appropriateness of the extension of the municipal representation procedures to joint powers entities and townships. In 2000, Minnesota Statutes, Section 424A.04, Subdivision 1, was amended to add a procedure for county board appointment of municipal representatives from the fire department service area if the volunteer firefighter relief association was not associated with a city or an independent nonprofit firefighting corporation. Presumably, that 2000 procedure should have covered volunteer firefighter relief associations associated with townships and volunteer firefighter relief associations associated with joint powers entities. Little or no information has been assembled on the actual practice since 2000 with respect to townships and joint powers entities.

Appendix A

Background Information on the Regulation of Volunteer Firefighter Relief Associations

A. In General. Fire coverage in Minnesota is provided through approximately 800 firetowns. Pension coverage for paid firefighters is provided by the Public Employees Police and Fire Plan (PERA-P&F), three paid firefighter relief associations (Bloomington, Minneapolis, and Virginia), and 18 former paid firefighter consolidation accounts that were merged into PERA-P&F in 1999 (Albert Lea, Austin, Chisholm, Columbia Heights, Crookston, Duluth, Faribault, Hibbing, Mankato, Red Wing, Richfield, Rochester, St. Cloud, St. Louis Park, St. Paul, South St. Paul, West St. Paul, and Winona).

Coverage for volunteer firefighters in the state's roughly 800 firetowns is provided by approximately 700 volunteer firefighter relief associations. Although the Bloomington Firefighters Relief Association provides retirement coverage to firefighters in a volunteer fire department, the coverage is based on the salary of a salaried (police) position and is thus considered a paid firefighters relief association for statutory regulation purposes.

In Minnesota, volunteer firefighters typically have pension coverage as part of their compensation package and that pension coverage is provided by the various local volunteer firefighter relief associations located in the state. These volunteer firefighter relief associations are creatures of state law and are subject to various statutory regulations.

B. Legal Status and Structure. Under Minnesota Statutes, Section 424A.001, Subdivision 4, volunteer firefighter relief associations are required to be nonprofit corporations organized under Minnesota Statutes, Chapter 317A, the Minnesota Nonprofit Corporation Act. Minnesota Statutes, Chapter 317A, applies to all Minnesota nonprofit corporations and contains numerous requirements on the manner of incorporation, general powers, scope of bylaws, function of the board and officers, rights and obligations of members, processes of consolidation, merger, or dissolution, and corporate registration. In several areas, Minnesota Statutes, Chapter 424A, contains additional regulation or conflicting regulation, and the more particularized regulatory provisions of that chapter apply. For instance, Minnesota Statutes, Section 317A.203, provides for a board of directors of at least three individuals, but Minnesota Statutes, Section 424A.04, Subdivision 1, provides for a board of trustees generally comprised of nine members. Also, Minnesota Statutes, Sections 317A.701 through 317A.791, generally governs the dissolution of a nonprofit corporation, but Minnesota Statutes, Section 424A.02, Subdivision 11, specifically governs the dissolution of a volunteer firefighter relief association.

A volunteer firefighter relief association under Minnesota Statutes, Chapter 424A, can exist in one of three ways:

1. Separate Corporation. As a separate nonprofit corporation directly associated with a municipal fire department established by municipal ordinance;

2. Division of Another Relief Association. As a volunteer division or account of a part paid and part volunteer firefighter relief association directly associated with a municipal fire department established by municipal ordinance; or

3. Subsidiary Corporation. As a separate nonprofit corporation subsidiary to an independent nonprofit firefighting corporation also organized under Minnesota Statutes, Chapter 317A, and operating exclusively for firefighting purposes.

A volunteer firefighter relief association, under Minnesota Statutes, Section 424A.001, Subdivision 4, has the status of a governmental entity, receiving public money, and providing benefit coverage for individuals providing the governmental services of firefighting and emergency first response.

C. Volunteer Firefighter Relief Association Governance. Minnesota Statutes, Section 424A.04, Subdivision 1, requires either a nine-member board of trustees or a ten-member board of trustees. The board composition differs depending on whether the relief association is associated with a municipal fire department or is subsidiary to an independent nonprofit firefighting corporation, as follows:

Relief Association Associated With Municipal Fire Department	Relief Association Subsidiary to Independent Nonprofit Firefighting Corporation
Six trustees elected from the relief association membership (one can be a retiree receiving a monthly benefit, at relief association's discretion).	Six trustees elected from the relief association membership (one can be retiree receiving a monthly benefit, at relief association's discretion).
Three trustees from municipal officials (the mayor, clerk, the clerk-treasurer or finance director, and the municipal fire chief).	Three trustees from municipal officials (if one municipality served, three officials designated by municipality; if two municipalities served, two officials from largest municipality and one official from other municipality, designated by municipalities; if three or more municipalities served, one official from each of the three largest municipalities, designated by municipalities).
	One trustee, who is the fire chief of the independent nonprofit firefighting corporation.

If a fire department is not located in or associated with an organized municipality, the County Board of Commissioners must appoint the ex-officio board members from the fire department service area.

Ex-officio trustees have the same rights and duties as elected trustees, except that ex-officio trustees may not serve as an officer of the board of trustees. Elected trustees have a term length as specified in the relief association bylaws, but it may not be longer than three years and it must be staggered if it is more than one year in length.

Minnesota Statutes, Section 424A.04, Subdivision 1, provides for at least three officers of a volunteer firefighter relief association. The three officers must include a president, a secretary, and a treasurer. The officers must be drawn from the relief association board of trustees, from the elected board membership. The officers can be elected by the board of trustees or by the relief association membership as the bylaws specify. No person is allowed to occupy more than one officer position at one time. Officers have a term length as specified in the relief association bylaws, but the term may not be longer than three years.

D. <u>Volunteer Firefighter Relief Association Fund Structure</u>. Minnesota Statutes, Section 424A.05, requires that every relief association establish and maintain a special fund. The special fund is the fund from which volunteer firefighter pension benefits are payable and into which state aid, municipal contributions, and other public money is deposited. Beyond fire state aid and municipal tax revenue, the special fund also must receive all money or property donated by any person if so designated. Investment income on special fund assets also must be deposited in the special fund. Beyond the payment of service pensions, the special fund can also be disbursed for disability benefits, survivor benefits, funeral benefits, Minnesota State Fire Department Association and State Volunteer Firefighters' Benefit Association dues, and authorized administrative expenses. A survivor benefit may be paid to a designated beneficiary (which must be a natural person) if there is no surviving spouse or children. The payment of fees or assessments is permitted to the Minnesota Area Relief Association Coalition (MARAC). All benefit payments are required to be in accord with the requirements of law and the relief association bylaws.

The relief association treasurer is required to be the custodian of the special fund and recipient on behalf of the special fund of its revenue. The treasurer is required to maintain records documenting any transaction affecting the assets or revenues of the special fund. The records of the treasurer, as well as the relief association bylaws, are public and open for public inspection.

The assets of the special fund must be invested in authorized securities, which are either a limited list of securities for small relief associations, or a separate codified list which represents the pre-1994 list of authorized investment securities for the State Board of Investment for larger relief associations.

Relief associations under Minnesota Statutes, Section 69.775, also have authority to invest in mutual funds that are restricted to the same authorized securities, or to invest in the Minnesota Supplemental Investment Fund administered by the State Board of Investment.

Minnesota Statutes, Section 424A.06, allows a volunteer firefighter relief association to establish and maintain a general fund. The general fund is the fund into which non-tax or non-public funds are deposited and from which moneys can be expended as the relief association sees fit, as governed by its bylaws. The general fund traditionally is supported by member dues and by revenues raised from community fundraising events.

E. Volunteer Firefighter Relief Association Membership Inclusions and Exclusions. State law is largely silent on the question of which persons are required to be or may be included in the membership of or coverage by a volunteer firefighter relief association. Except for a definition of the term "volunteer firefighter" in Minnesota Statutes, Section 353.01, Subdivision 36, existing for purposes of providing an exclusion of volunteer firefighters from the Public Employees Retirement Association or Public Employees Police and Fire (PERA-P&F) coverage, the term "volunteer firefighter" is not defined in state law. Under Minnesota Statutes, Chapters 317A and 424A, each volunteer firefighter relief association sets its own qualifications or requirements for membership, subject to certain statutory membership exclusions. The determination of volunteer firefighter status occurs in conjunction with the municipal fire department or the independent nonprofit firefighting corporation membership requirements, since Minnesota Statutes, Section 424A.02, Subdivision 1, sets certain benefit qualifications in terms of active membership with the fire department in addition to relief association membership. Volunteer firefighters are not always individuals who donate their time for free to assist in fire suppression activities. Many volunteer firefighters are reimbursed for their out-of-pocket expenses, or are paid a minimum fire run amount, or are paid an hourly rate when engaged in fire department duties. Some volunteer firefighter relief associations cover salaried firefighters who also have PERA-P&F coverage. Fire department duties can include activities beyond strict fire suppression activities, including fire equipment maintenance, firefighters training, fire department administration, fire prevention, and emergency first response services. When the fire department is the sponsoring entity for ambulance services, the activities can include paramedic or other ambulance and emergency medical duties. Because service pensions from a volunteer firefighters relief association are a function in large measure of the amount of fire state aid per relief association member, which is an amount determined independent of volunteer firefighter relief association requirements, there is an economic incentive for a relief association to be selective or restrained in fashioning the local definition or classification of a volunteer firefighter.

Minnesota Statutes, Section 424A.01, sets forth several exclusions from volunteer firefighter relief association membership or coverage. Minnesota Statutes, Section 424A.01, Subdivision 1, prohibits municipalities or independent nonprofit firefighting corporations from employing minors as volunteer firefighters, hence also excluding minors from volunteer firefighter relief association membership. Minnesota Statutes, Section 424A.01, Subdivision 2, excludes substitute volunteer firefighters from volunteer firefighter relief association membership. Minnesota Statutes, Section 424A.01, Subdivision 3, provides that members of the fire department who also decline to be members of the volunteer firefighter relief association are ineligible for volunteer firefighter relief association benefit coverage. Minnesota Statutes, Section 424A.01, Subdivision 4, allows a volunteer firefighter relief association board of trustees to exclude applicants for membership in the volunteer firefighter relief association from membership if they have a pre-existing physical or mental impairment or condition that would constitute a predictable and unwarranted risk of ancillary (disability or death) benefit liability, and if the relief association makes that determination based on medical evidence.

F. Benefit Coverage Provided By Volunteer Firefighter Relief Associations.

1. In General. The state law regulating the benefit coverage provided to volunteer firefighters by volunteer firefighter relief associations from the relief association special fund is primarily Minnesota Statutes, Sections 424A.02, 424A.03, and 424A.10. Minnesota Statutes, Chapter 424A, was enacted in 1979. Unlike most public employee pension coverage, where state law specifies all or most aspects of the benefit plan, the statutory regulation of volunteer firefighter relief associations largely consists of specifying certain minimum eligibility requirements and certain benefit maximums, with the actual benefit plan assembled in the articles of incorporation or the bylaws of the particular volunteer firefighter relief association. The primary benefit coverage provided by a volunteer firefighter relief association is the service pension coverage, and most minimum eligibility requirements and benefit maximums relate to the service pension coverage.

   The primary benefit payable from a volunteer fire relief association is a service pension. Most volunteer fire relief associations provide a lump sum service pension, with a minority providing a monthly benefit service pension (some with an alternative lump sum service pension). Service pensions are not payable before age 50, and usually are payable in full only with 20 years of service. Some volunteer fire relief associations have casualty (disability and death) benefit coverage if a service pension is not otherwise payable.

The funding of volunteer fire relief associations is primarily the annual fire state aid, which is allocated to cities based half on population compared to statewide totals, and half on their property value compared to the statewide total. The aid is dedicated for pension purposes. Additionally, if the actuarial cost of the volunteer firefighters relief association exceeds the fire state aid, the municipality must levy a property tax to support the volunteer fire relief association.

2. Service Pension Eligibility Requirements. Minnesota Statutes, Section 424A.02, Subdivision 1, authorizes a volunteer firefighter relief association to provide a service pension to a member of the relief association if certain conditions are met by the volunteer firefighter. The volunteer firefighter must meet the following conditions:

   i. Terminate Active Service. The person must separate from active service as a firefighter with the fire department, defined as the cessation of the performance of fire suppression duties and the cessation of the supervision of fire suppression activities. In 2002, certain retirees were authorized to receive and retain a volunteer firefighter pension although subsequently employed full-time within the fire department by the applicable city or independent nonprofit firefighting corporation, providing that the employer determines the position would be difficult to fill with another similarly qualified applicant, and providing the relief association bylaws permit it. If a firefighter resumes service, no additional service pension accrues and the individual must repay any previously received service pension.

   ii. Attain at Least Age 50. The person must reach at least age 50.

   iii. Have Credit for at Least Five Years Fire Department Service. The person must have credit for at least five years of service as an active member of the fire department with which the relief association is associated.

   iv. Have Credit for at Least Five Years Relief Association Membership. The person must have credit for at least five years of active membership in the relief association before separating from service (open to modification for a new relief association covering an existing volunteer fire department, with firefighters having prior service).

   v. Compliance with Additional Conditions. The person must comply with any additional age, service or membership conditions prescribed in the relief association bylaws.

3. Partial Vesting With Less Than 20 Years Service Credit. A vesting requirement is a requirement for a public pension plan member or beneficiary to obtain an enforceable entitlement to a pension benefit, typically the acquisition of credit for a specific minimum period of allowable service. Vesting requirements exist in defined benefit plans to provide a minimum threshold to be achieved before the pension plan member gains a non-forfeitable entitlement to an eventual retirement benefit. Vesting requirements can contribute significantly to the actuarial turnover gain that funds the retirement benefits payable to other public pension plan members.

   Vesting requirements also reflect the contribution that public pension plan coverage is intended to provide to the public employing unit's personnel system. The minimum vesting requirement for any retirement benefit and the minimum vesting requirement for a full retirement benefit will generally induce many public employees to continue in public employment for at least one of those periods of time.

   The volunteer firefighter personnel system varies considerably in the 700+ localities in Minnesota with volunteer fire department coverage, with some localities providing a considerable compensation package to volunteer firefighters and other localities providing no compensation beyond the volunteer firefighters relief association service pension. A vesting period for the volunteer firefighters relief association service pension will allow a locality to recover any resources that it expended in training a volunteer firefighter and will reduce the turnover of firefighters which consequentially demands efforts to recruit new firefighters.

   Volunteer firefighter relief associations have traditionally required 20 years of service for a person to become eligible to receive a service pension. Before 1977, the minimum vesting period permitted by statute was 20 years of firefighting service. A shorter vesting period that was not necessarily supported by the volunteer fire community (as represented by the League of Minnesota Cities) was added in 1977, at the instigation of the then Pension Commission chair, but it was not widely implemented. As part of the 1979 revision of volunteer firefighters relief association laws assembled jointly by the Pension Commission staff, the Minnesota Fire Department Association, and the League of Minnesota Cities, the current vesting provision replaced the 1977 early vesting provision. Between 1979 and 1989, ten years of service were required as the minimum service requirement for entitlement to a partial service pension. In 1989, the ten years service requirement was reduced to five years. Under state law, the maximum service pension payable with less than 20 years of service is limited to a portion of the service pension earned or accrued. The applicable statutory provision is Minnesota Statutes, Section 424A.02, Subdivision 2. The percentage of the accrued or earned benefit must be set forth in the articles of incorporation or the bylaws of the relief association. The 2004 Legislature permitted defined contribution volunteer firefighter relief associations to utilize a different vesting schedule than the vesting schedule applicable to lump sum volunteer firefighter relief associations.

The vesting schedule for lump sum volunteer firefighter relief associations and monthly benefit volunteer firefighter relief associations is as follows:

Completed Years of Service	Non-Forfeitable Percentage of Pension Amount
5	40 percent
6	44 percent
7	48 percent
8	52 percent
9	56 percent
10	60 percent
11	64 percent
12	68 percent
13	72 percent
14	76 percent
15	80 percent
16	84 percent
17	88 percent
18	92 percent
19	96 percent
20 and thereafter	100 percent

The vesting schedule for defined contribution volunteer firefighter relief associations authorized by the 2004 Legislative Session is as follows:

Completed Years of Service	Non-Forfeitable Percentage of Pension Amount
5	40 percent
6	52 percent
7	64 percent
8	76 percent
9	88 percent
10 and thereafter	100 percent

Five volunteer firefighter relief associations have special laws from before 1979 that provide vesting earlier than 20 years (Brooklyn Park (1975), Caledonia (1963), Dassel (1969), Golden Valley (1973), and Rockford (1976)). Only two volunteer firefighter relief associations have had special legislation enacted to provide early vesting since 1979, Minnetonka (Laws 1989, Chapter 319, Article 11, Section 5) and Eden Prairie (Laws 1995, Chapter 262, Article 10, Section 5).

The Minnetonka Volunteer Firefighters Relief Association early vesting was full proportional vesting at five years of service (i.e., for a $500 pension, a pension of $2,500 with five years and $5,000 with ten years). The Eden Prairie Volunteer Firefighters Relief Association early vesting was 40 percent of the accrued amount at five years up to 100 percent of the accrued amount at ten years (i.e., for a $500 pension, $1,000 at five years and $5,000 at ten years).

4. <u>Flexible Service Pension Maximums</u>.

   i. <u>Service Pension Maximums Before 1979</u>. Volunteer firefighter service pensions have always been subject to a benefit maximum, either under Minnesota Statutes, Section 69.06 (1905-1979) or Minnesota Statutes, Section 424A.02, Subdivision 3 (1979 to present). In the system used before 1979, a single-benefit maximum was stated in law, but without any mention of the financing needed to support that benefit level, and without any guidance for reasonable benefit levels that could be supported in municipalities where funding support was low. Prior to 1957, the maximum service pension payable to a retiring volunteer firefighter was a $40 monthly benefit (plus two dollars per month per year of service beyond 20 years to a maximum of $60 per month) or $100 per year of service credit lump sum benefit. In 1957, the lump sum benefit maximum was increased to $200 per year of service credit. In 1973, the lump sum benefit maximum was increased to $300 per year of service credit. In 1976, the monthly benefit maximum was increased to $80 per month (plus four dollars per month per year of service beyond 20 years to a maximum of $120 per month) or $600 per year of service credit lump sum benefit.

ii. Service Pension Maximums 1979 and After. In 1979, with the passage of Minnesota Statutes, Chapter 424A, recodifying the law governing volunteer fire pension coverage, the single dollar amount service pension maximums were eliminated in favor of flexible service pension maximums. The flexible service pension maximums established a sliding scale of benefit maximums based on the level of funding per firefighter for the previous three-year period, with the greatest monthly benefit service pension of $15 per month per year of service up to 30 years of service if the funding per firefighter was at least $744 per year and with the greatest lump sum benefit service pension of $2,000 per year of service if the funding per firefighter was at least $960 per year. In 1983, the upper end of the monthly benefit service pension flexible maximum sliding scale was increased to $22.50 per year of service credit up to 30 years of service with at least $1,678 funding per firefighter per year, and the upper end of the lump sum service pension flexible maximum sliding scale was increased to $3,000 per year of service credit with at least $1,440 funding per firefighter per year. In 1990, the monthly benefit service pension flexible maximum sliding scale was increased from $22.50 per month per year of service to $30.00 per month per year of service credit. In 1993, the maximum permitted lump sum pension was increased from $3,000 per year of service to $4,000 per year of service, to be phased in by 1996.

In 1997, the maximum permitted service pension was increased from $30 per month per year of service to $40 per month per year of service and from $4,000 per year of service lump sum to $5,500 per year of service lump sum.

The flexible service pension maximums were again increased by the 2000 Legislature. The 2000 Session changes increased the maximum monthly pension from $40 per month per year of service to $56, to be phased in by the end of calendar 2003. The maximum lump sum pension was increased from $5,500 to $7,500 per year of service, with a similar phase-in.

iii. Current Service Pension Maximums. Minnesota Statutes, Section 424A.02, Subdivision 3, establishes a maximum service pension payable to a retiring former volunteer firefighter. Before 1979, the predecessor provision (Minnesota Statutes 1978, Section 69.06) set a single dollar amount maximum on volunteer fire service pensions. With the enactment of Minnesota Statutes, Section 424A.02, Subdivision 3, the service pension maximum has been a sliding scale depending on the financial resources of the relief association on a per firefighter basis. If a volunteer firefighter relief association has a substantial portion of the funding required to support a given level of service pension under the 1971 Volunteer Firefighter Relief Association Guidelines Act, Minnesota Statutes, Sections 69.771 through 69.776, the relief association is allowed to provide in its articles of incorporation or bylaws that service pension level.

The service pension can be a monthly benefit service pension (a specified dollar level per month per year of service credit, payable for life) or a lump sum service pension (a specified dollar level per year of service credit, payable in a lump sum or in a number of installment payments). If a relief association provides both a monthly benefit service pension and a lump sum service pension as an alternative, the amount of each type of service pension must comply with the flexible service pension maximum. The funding amount on which the flexible service pension maximum scale is based is the amount of funding available per firefighter, computed on a three-year average. The funding used in the computation is the amount of fire state aid received, the amount of any municipal funding provided, and one-tenth of the amount of any funding surplus (assets in excess of actuarial accrued liability).

5. Defined Contribution Lump Sum Service Pension Coverage. Minnesota Statutes, Section 424A.02, Subdivision 4, allows a volunteer firefighter relief association to provide a defined contribution (or split-the-pie) service pension in lieu of a defined benefit monthly benefit or

lump sum service pension. The defined contribution service pension coverage necessitates that the volunteer firefighter relief association establish a separate account for each member, to which an equal share of any fire state aid, municipal contributions or turnover gain (forfeited amounts upon early terminations under Minnesota Statutes, Section 424A.02, Subdivision 2) must be credited to each individual account. Investment income based on the account balance also must be credited to each individual account.

6. Benefit Calculation Uniformity. Minnesota Statutes, Section 424A.02, Subdivision 6, provides that the method of calculating service pensions must be applied uniformly for all years of active service. It also provides that credit must be given for all years of service other than those covered by the 30-year service credit maximum and the partial early vesting provisions. The provision also prohibits the payment of a service pension to a person who remains an active firefighter, prohibits the payment of other special fund benefits to a person receiving a service pension, exempts volunteer firefighter relief association pensions and benefits from garnishment, judgement, execution or legal process other than marriage dissolution or child support obligations, and prohibits the assignment of any service pension or benefit from a volunteer firefighter relief association.

7. Deferred Service Pensions. For a volunteer firefighter who has completed the length of service credit required for vesting, has at least five years of relief association active membership, but separates from active volunteer firefighter service and volunteer firefighter relief association membership before age 50, Minnesota Statutes, Section 424A.02, Subdivision 7, provides for a deferred service pension payable when the former firefighter reaches at least age 50. The service pension is calculated based on the law in effect when active service terminated, but a lump sum service pension may be credited with interest.

   Minnesota Statutes 1978, Section 69.06, and its predecessor provisions, Revised Laws of 1905, Section 1655, General Statutes of Minnesota 1913, Section 3347, and Mason's Minnesota Statutes of 1927, Section 3728, set the minimum age (age 50) and the minimum service (20 years active fire department membership, 10 years active relief association membership) requirements for a service pension and set maximum service pension amounts ($40 per month initially, or $100 per year of service after 1944). Minnesota Statutes 1978, Section 69.06, and precursor provisions did not specifically address the topic of deferred service pensions or what benefit rights a firefighter who terminates active firefighting service with the minimum service period before attaining age 50 has. Attachment A contains Minnesota Statutes 1978, Section 69.06, and its various predecessor formulations.

   The historic practice in private sector/corporate pension plans before the 1974 enactment of the Employee Retirement Income Security Act (ERISA) was to require plan membership until and termination of employment at the normal retirement age for the pension plan in order to receive a retirement benefit, without any deferred pension eligibility. Until relatively recently, pension plans were established to encourage the retention of employees, penalizing employment mobility by having break-in-service rules, where past service credit could be cancelled when the plan member terminated covered employment.

   Minnesota Statutes, Section 424A.02, Subdivision 7, affirmatively establishes the right of a volunteer firefighter who leaves active firefighting service before attaining age 50 to a deferred service pension and clarifies that a deferred service pension is to be calculated under the provisions of law and the bylaws in effect when the firefighter separated from active service. Thus, if the service pension amount has increased since the deferred member terminated active service, the deferred service pensioner does not benefit from the service pension amount increase.

   Before 2000 (Laws 2000, Chapter 461, Article 15, Section 6), the relief association was permitted to pay interest on a deferred lump sum service pension at the rate actually earned by the relief association, but not to exceed the five percent interest rate actuarial assumption underlying lump sum volunteer firefighter relief association funding. In 2000, in legislation initially requested by the Minnesota Area Relief Association Coalition (MARAC), an educational organization representing volunteer firefighter relief associations, the lump sum deferred service pension interest provision was modified, to encompass three options. If the relief association bylaws so provide, interest can be provided on a lump sum deferred service pension at the actual rate of interest earned if the deferred pension amount is placed in a separate relief association account established for that purpose, at the actual rate of interest earned if the deferred pension amount is invested in a separate investment vehicle held by the relief association, or at a flat five percent interest rate.

In 2003, displeased with the 2000 deferred service pension legislation, the Marshall Volunteer Firefighter Relief Association sought a legislative change to replicate the pre-2002 law change. Ultimately, the Marshall Volunteer Firefighter Relief Association general law request was converted into a special law demonstration project (First Special Session Laws 2003, Chapter 12, Article 12, Section 3), which included the additional specification of the manner in which the relief association investment earnings are to be calculated. The Marshall Volunteer Firefighter Relief Association was permitted to pay interest on its lump sum deferred service pensions based on the actual investment performance of the relief association special fund, up to five percent annually. The actual investment performance is that reported by the Office of the State Auditor under Minnesota Statutes, Section 356.219.

In 2004 (Laws 2004, Chapter 267, Article 14, Section 2), an additional option for providing interest on deferred lump sum service pensions was authorized, in force, until December 31, 2008. The additional deferred service pension interest option is an amount equal to the actual time-weighted rate of investment return of the pension plan as reported by the State Auditor, up to five percent per annum, if the volunteer firefighter relief association bylaws so provide.

8. Installment Payments for Lump Sum Service Pensions. Volunteer firefighter relief associations that pay lump sum service pensions are authorized by Minnesota Statutes, Section 424A.02, Subdivision 8, to pay the lump sum service pension in installments. No limit in the number of installments is specified. The installments are to have the same present value as the lump sum service pension, based on a five percent interest assumption.

9. Conversion of Lump Sum Service Pensions Into Annuities Through Single Premium Insurance Annuity Purchase. Minnesota Statutes, Section 424A.02, Subdivision 8a, allows a volunteer firefighter relief association that pays a lump sum service pension to purchase a single premium insurance annuity for the retiring volunteer firefighter from an insurance company approved to do this type of business by the state Commerce Commissioner.

10. Ancillary Benefit Limits. Minnesota Statutes, Section 424A.02, Subdivision 9, places limits on ancillary retirement benefit coverage. Ancillary benefits are those benefits provided by a volunteer firefighter relief association other than the service pension, such as disability benefits, death benefits, or survivor benefits. In 1873, with the creation of fire state aid, municipalities were permitted to pay relief to disabled firefighters and to survivors of deceased firefighters from fire state aid if no relief association is located in the municipality. In 1909, firefighter relief associations were specifically permitted to make payments for the relief of sick, injured, and disabled firefighters and to make payments to widows and orphans of deceased firefighters. The term “widow” was not defined until 1937, requiring three years of marriage before the occurrence of death and dependency for eligibility. The provision became Minnesota Statutes 1978, Section 424.31. The limitations are needed to protect the financial solvency regulation of volunteer firefighter relief associations, which is built around determining the accrued liability and financial requirements for the level of the service pension coverage provided by the volunteer firefighter relief association. The limitations are:

    i. No Post-Retirement Benefit Beyond the Lump Sum Service Pension. Volunteer firefighter relief associations that provide lump sum service pensions are prohibited from paying any additional benefit to a retired firefighter or on behalf of a retired firefighter once payment of the service pension commences; and

    ii. Maximum Ancillary Benefit Available. All volunteer firefighter relief associations are limited in the payment of pre-retirement and post-retirement ancillary benefits to the amount of the accrued service pension of the volunteer firefighter, except that the survivor benefit payable on behalf of a deceased short service firefighter may be based on a five years of service accrued benefit if that produces a larger accrued service pension amount.

11. Post-Retirement Increases. A volunteer firefighter relief association paying a monthly service pension may, if it chooses, provide a post-retirement increase to service pension and benefit recipients upon providing a benefit increase to active firefighters, under Minnesota Statutes, Section 424A.02, Subdivision 9.

12. Municipal Approval of Benefit Changes; State Filing Requirements. Minnesota Statutes, Section 424A.02, Subdivision 10, requires municipal approval of any benefit changes or amendments to the relief association articles of incorporation or bylaws impacting on benefits unless the volunteer firefighter relief association has authority under the 1971 Volunteer

Firefighter Relief Association Financing Guidelines Act to implement the benefit increase without local approval. The benefit change approval request must be accompanied by an estimate of the actuarial impact of the benefit change. Upon making a benefit change, the volunteer firefighter relief association must file a copy of the revised articles of incorporation or bylaws with the Commissioner of Commerce in order to retain eligibility for fire state aid.

13. Volunteer Firefighter Relief Association Dissolution and Consolidation. Minnesota Statutes, Chapter 424B, governs the dissolution and consolidation of volunteer firefighter relief associations. With approval of the governing bodies of each municipality, two or more relief associations servicing contiguous fire districts may initiate consolidation. Initiation involves proposing a consolidation resolution to the relief association board of trustees, notification of members, and a public hearing. If adopted by the majority of the board, a copy of the resolution must be filed with other relief associations which may be part of the consolidation. If two or more of the applicable relief associations adopt a consolidation resolution, those relief associations are consolidated as of the following January 1. If the subsequent relief association following the consolidation is a new relief association, the association must incorporate as a nonprofit corporation and the new board must include at least one board member from each prior association. If the consolidation retains one association and dissolves the others, the articles of incorporation of the remaining association must be revised as necessary. The president, secretary, and treasurer of the consolidated relief association must be elected by the association membership. On the effective date of the consolidation, the assets of the prior relief association special funds transfer to the consolidated special fund, and all liabilities, fund management and plan administration, and all records transfer to the new board of trustees. The consolidated relief association is the successor in interest in all claims for and against the special funds of the prior relief associations. Before consolidation, the secretaries of the prior relief associations must settle all accounts payable from the respective general fund. Remaining balances transfer to the general fund of the consolidated relief association. Following transfer of administration, records, special and general fund assets and liabilities, the prior relief associations cease to exist. The Secretary of State, State Auditor, Commissioner of Revenue, and the Commissioner of the federal Internal Revenue Service are to be notified of the termination. Administrative expenses consistent with Minnesota Statutes, Section 69.80 (authorized special fund administrative expenses) may be paid from the consolidated special fund. All other expenses must be paid from the general fund. The service pension of the consolidated relief association is the highest service pension amount payable by any of the relief associations that were included in the consolidation. Subsequent benefit increases after that date must conform to general law applicable to volunteer fire benefit levels. Unless the municipalities agree in writing to another procedure, the minimum annual financial obligation to the consolidated relief association must be allocated between the applicable municipalities in proportion to their fire state aid. If a municipality fails to pay its share, contributions must be covered by the remaining municipalities. The municipality which is delinquent or deficient in its payments must reimburse the other municipalities plus a 25 percent surcharge.

    If a relief association is dissolved without consolidation, prior to the effective date of the dissolution the board must pay all accounts payable against the special fund other than the accrued liabilities for pensions and other benefits. The remainder of the special fund assets after settling those non-benefit-related obligations are transferred, in cash or securities, to the municipal finance officer. The board also transfers any records needed to settle future benefit-related claims. The assets of the prior special fund create a municipal trust fund to be invested according to investment and fiduciary law applicable to volunteer fire plans. The municipality and the trust fund are responsible for any remaining liabilities of the prior special fund, including any unfunded liabilities. The board must notify the Commissioner of Revenue, the State Auditor, and the Secretary of State of the dissolution action within 30 days of the effective date of the dissolution.

    In lieu of the asset transfer to the municipality mentioned above, the board of the dissolving relief association may purchase annuity contracts. Payment of the annuity for which the contract is purchased may not begin before the retirement age specified in law and bylaw. Legal title to the annuity contract transfers to the municipality in trust.

14. Combined Volunteer Firefighter Relief Association Service Pensions. If the volunteer firefighter relief association elects to do so, the relief association under Minnesota Statutes, Section 424A.02, Subdivision 13, can recognize total service rendered for any other participating volunteer firefighter relief association in meeting its vesting requirement and can pay a prorated service pension based on the accrual service rendered in that relief association.

15. Supplemental Benefit for Lump Sum Volunteer Firefighter Relief Associations. Minnesota Statutes, Section 424A.10, requires a volunteer firefighter relief association that pays a lump sum service pension to pay a supplemental benefit from the relief association special fund to retiring firefighters who receive a lump sum service pension. The supplemental benefit is an amount equal to ten percent of the lump sum service pension paid, up to $1,000. The supplemental benefit is reimbursable to volunteer firefighter relief associations annually, in March, from the state general fund by the Commissioner of Revenue, for the volunteer firefighter relief associations that apply for the reimbursement in the preceding February. The supplemental benefit was intended to offset the impact of a federal Internal Revenue Code ten percent income tax surcharge on pre-age 59-1/2 non-annuity pension distributions. The supplemental benefit is in lieu of a state income tax exclusion for lump sum retirement benefit distributions.

G. Background Information on Relief Association Financial Reporting. Since 1965 (Laws 1965, Chapter 359, Section 1), Minnesota public pension plans have been required to prepare annual financial reporting. The statutory requirement is codified as Minnesota Statutes, Section 356.20. For volunteer firefighter relief associations, a financial report under Minnesota Statutes, Section 69.051, is considered to meet the reporting requirements of Minnesota Statutes, Section 356.20.

The financial reporting requirement under Minnesota Statutes, Section 69.051, was first imposed as part of the fire state aid revisions of 1969 (Laws 1969, Chapter 1001, Section 5). From 1969 to 1986, all volunteer firefighter relief associations filed the same reporting form, which was initially prescribed by the Commissioner of Insurance and then by the Commissioner of Commerce. The 1969-1986 form was required to include the information needed by the Commissioner to reveal the true financial condition of the relief association and to reveal the extent of compliance by the relief association with the regulatory, financing, and funding provisions of the applicable state law. The financial report was to be prepared as of December 31 for the prior calendar year, was required to be countersigned by the municipal clerk, and was to be certified by an independent accountant or auditor, who was required to provide an opinion on the condition of the relief association and any exceptions.

In 1986, after the discovery of a significant fraud and misappropriation of funds involving the secretary of the Winona Police Relief Association, the local relief association financial reporting requirements to qualify for state aid under 69.051 were modified. The 1986 financial reporting law amendments gave the State Auditor authority and responsibility to audit all relief associations and centralized the receipt and certification of financial statements of all relief associations in the Office of the State Auditor, provided that the Commissioner of Revenue process the distribution of state aid only after notification by the State Auditor that a relief association's financial reports and actuarial valuations are complete, and provided more municipal oversight of the relief associations by requiring annual reports to the municipality of relief association financial affairs. The 1986 legislation also gave the Commission authority to request information from the various funds and the funds are authorized and directed to promptly furnish any data requested and required the State Auditor in performing an audit or examination of a pension plan to notify the Commission if the audit or examination reveals malfeasance, misfeasance, or nonfeasance in office and requires the Commissioner of Revenue to notify the Commission if the State Auditor has not filed with the Commissioner of Revenue the required financial compliance reports by the July 1 deadline. The State Auditor was required to oversee the completion and auditing of financial statements of fire relief associations rather than the Commissioner of Revenue and was required to notify the Commissioner of Revenue by July 1 in any year which relief associations that with the financial reporting requirements necessary to qualify for fire state aid, and the primary administration of the fire and police state aid program was transferred from the Department of Revenue to the State Auditor. The deadline for fire state aid applications was moved from June 1 to July 1.

The requirements for the preparation and submission of financial reports is based on the size of the relief association, and for volunteer associations with assets or liabilities of at least $200,000, the relief association must:

i. Prepare its annual financial reports on forms prescribed by the State Auditor;
ii. File the report in its office for public inspection and present it to the city council; and
iii. Submit audited financial statements to the State Auditor within 180 days after the close of the fiscal year.

For volunteer associations with assets and liabilities less than $200,000, the relief association must:

i. Prepare annually a detailed financial statement on a form prescribed by the State Auditor;

ii. Have the detailed financial statement certified by an independent public accountant or auditor or the auditor that regularly examines the books of the municipality;
iii. File the statement in its office for public inspection and present it to the city council within 45 days of the close of the fiscal year; and
iv. Send a copy of the statement to the State Auditor within 90 days of the end of the fiscal year.

The surety bond of the volunteer firefighter relief association treasurer must be at least 10 percent of the assets, but is not required to exceed $500,000.

H. Volunteer Firefighter Relief Association Funding Requirements.

1. Volunteer Firefighter Relief Association Financing Guidelines Act of 1971. Minnesota Statutes, Sections 69.771 through 69.776, the Volunteer Firefighter Relief Association Financing Guidelines Act of 1971, governs the calculation of the actuarial accrued liability and annual funding requirement of volunteer firefighter relief associations, the determination of the financial requirements of volunteer firefighter relief associations, the determination of the minimum obligation of municipalities or independent nonprofit firefighting corporations toward the volunteer firefighter relief association, the requirement for municipal ratification of volunteer firefighter relief association plan amendments, and the investment of volunteer firefighter relief association special fund assets.

2. Calculation of Volunteer Firefighter Relief Association Actuarial Accrued Liability and Annual Funding Requirement. State law differentiates in the calculation of volunteer firefighter relief association actuarial accrued liabilities or its equivalent and the annual funding requirements. For volunteer firefighter relief associations providing monthly benefit service pensions, because there is a mortality risk and the need for making complicated computations, the relief association is required by Minnesota Statutes, Section 69.773, to utilize an approved actuary and have a quadrennial actuarial valuation prepared. For volunteer firefighter relief associations providing lump sum service pensions, because there is no mortality risk and the liability and funding calculations are less complicated, the relief association officers are required by Minnesota Statutes, Section 69.772, to estimate the association's actuarial liabilities and its annual funding requirement by using a simplified statutory valuation procedure.

   The monthly benefit volunteer firefighter relief association actuarial work is governed essentially by the same requirements applicable for other Minnesota public pension plans, Minnesota Statutes, Sections 356.215, and 356.216. The actuarial valuations will disclose the relief association's actuarial accrued liability, the assets, unfunded actuarial accrued liability, normal cost, and amortization of the unfunded actuarial accrued liability (typically using a 20-year amortization period.) The financial requirement of the monthly benefit relief association is the combination of four items:

   i. The normal cost;
   ii. The amortization requirement if the relief association has an unfunded actuarial accrued liability;
   iii. The prior year's administrative expenses, multiplied by a factor of 1.035; and
   iv. One-tenth of the relief association's funding surplus, if the relief association has assets in excess of its actuarial accrued liability.

   The lump sum volunteer firefighter relief association computations are required to follow simplified calculation procedures set forth in Minnesota Statutes, Section 69.772, Subdivision 2. The table and related provisions in Minnesota Statutes, Section 69.772, Subdivision 2, were developed by the Commission and its consulting actuary in 1970-1971. The statutory table is basically a present value table assuming a lump sum benefit payable immediately after 20 years of service, based on a three percent interest assumption, and assuming no pre-retirement turnover or mortality. The following is the statutory pension liability table, applicable for a $100 per year of service lump sum benefit:

Cumulative Year	Accrued Liability
1	$60
2	124
3	190
4	260
5	334

Cumulative Year	Accrued Liability
6	410
7	492
8	576
9	666
10	760
11	858
12	962
13	1070
14	1184
15	1304
16	1428
17	1560
18	1698
19	1844
20	2000
21 and thereafter	100 additional per year

The relief association's accrued liability is calculated annually using the table, after being multiplied by a factor to adjust the $100 lump sum per year of service table to the actual lump sum service pension amount provided by the volunteer firefighter relief association. Thus, for a volunteer firefighter relief association paying a $1,000 per year of service lump sum service pension, the factor would be 10 ($1,000 divided by $100.) The calculated accrued liability is compared to the special fund assets to determine whether or not the relief association has an unfunded accrued liability. The following year's projected accrued liability is then calculated, based on an additional year of service per member, and the increase in the accrued liability over the current year's accrued liability is the annual accruing liability of the relief association, which is the functional equivalent of the normal cost calculation in an actuarial valuation prepared by an actuary under Minnesota Statutes, Section 356.215. The financial requirements of the relief association are the combination of three or four items:

i. The computed annual accruing liability;
ii. One-tenth of the computed current year's unfunded accrued liability, if the relief association has an unfunded accrued liability;
iii. The prior year's administrative expense, multiplied by a factor of 1.035; and
iv. One-tenth of the relief association's funding surplus, if the relief association has assets in excess of the accrued liability.

3. <u>Calculation of the Minimum Municipal Obligation</u>.

Prior to the enactment of the 1971 Volunteer Firefighter Relief Association Financing Guidelines Act, under Minnesota Statutes 1969, Section 424.30, various municipalities were required to provide funding to its associated volunteer firefighter relief association equal to one-tenth of one mill on all taxable property in the municipality and were authorized to provide additional volunteer firefighter relief association funding to a maximum of one and nine-tenths mill on all taxable property of the municipality. If the municipality failed to make the required levy, the volunteer firefighter relief association board of trustees was authorized to certify the levy to the county auditor.

In 1971 (Laws 1971, Chapter 261), the Volunteer Firefighter Relief Association Financing Guidelines Act was enacted and was deemed to implicitly repeal Minnesota Statutes 1969, Section 424.30. Minnesota Statutes 1978, Section 424.30, was formally repealed by Laws 1979, Chapter 201. The 1971 Volunteer Firefighter Relief Association Financing Guidelines Act requires that municipalities fund their associated volunteer firefighter relief association based on the actuarial requirements of the relief association and establishes a procedure for determining the annual financial requirements of the special fund of the volunteer firefighter relief association and the minimum municipal obligation to the relief association. For relief associations providing monthly defined benefit service pensions, the relief association financial requirements are based on periodic actuarial valuations (required quadrennially under statute, more frequently under generally accepted accounting principles (GAAP)). For relief associations providing lump sum defined benefit service pensions, the financial relief association financial requirements are based on a statutory liability table that had been developed by Dr. Franklin Smith, the consulting actuary then retained by the Legislative Commission on Pensions and Retirement. The minimum municipal obligation is the annual financial requirements of the relief association reduced by the anticipated amount of fire state aid, one-tenth of any funding surplus (assets in excess of calculated accrued liability), and, for lump sum volunteer firefighter relief associations, an amount equal to five percent of the current assets of the special fund.

The officers of the volunteer firefighter relief association are required under the 1971 Volunteer Firefighter Relief Association Financing Guidelines Act to certify their calculations of the financial requirements of the relief association and the minimum municipal obligation each August. The municipality, after verifying those calculations, is required to include the minimum municipal obligation in the municipal budget and if the municipality fails to budget for the minimum municipal obligation, the volunteer firefighter relief association officers are obligated to certify the minimum municipal obligation as a tax levy to the applicable county auditor, who is required to spread the levy over the taxable property of the municipality.

The Volunteer Firefighter Relief Association Financing Guidelines Act of 1971, Minnesota Statutes, Sections 69.771 through 69.776, requires municipal support of a relief association if the main other revenue source, the fire state aid program under Minnesota Statutes, Sections 69.011 through 69.051, is insufficient. Specifically, Minnesota Statutes, Section 69.772, Subdivision 3, for lump sum volunteer firefighter relief associations, and Minnesota Statutes, Section 69.773, Subdivision 5, for monthly benefit volunteer firefighter relief associations, require that the municipality include in its budget, levy for, and pay over to the relief association the amount of the financial requirements of the relief association, reduced by the amount of the fire state aid anticipated to be received in the following year. For lump sum volunteer firefighter relief associations, the relief association financial requirement also are reduced by an amount equal to five percent of the assets of the relief association, to adjust for the next year's future expected interest earnings. The determination of the minimum municipal obligation must be made by the officers of the relief association, and must be certified to the municipality as part of the municipal budget preparation process.

4. Compliance with Municipal Funding Requirement. If the municipality fails to include the minimum municipal obligation in its budget or fails to spread the obligation in its property tax levy, Minnesota Statutes, Section 69.772, Subdivision 4, for lump sum volunteer firefighter relief associations, and Minnesota Statutes, Section 69.773, Subdivision 5, for monthly benefit volunteer firefighter relief associations, require that the relief association officers certify the required municipal obligation amount to the county auditor, who is required to levy that amount as part of the property taxes of that municipality

5. Applicable Actuarial Funding and Procedures, Relief Association Discontinuing Monthly Pensions, Or Purchasing Annuities to Finance Monthly Pensions. If a volunteer fire relief association discontinues providing monthly pensions or purchases annuities to cover the monthly pensions, the funding procedures and minimum municipal obligation requirements applicable to lump sum plans apply, rather than those applicable to monthly benefit plans.

I. Volunteer Firefighter Relief Association Investment Authority. In Minnesota, the assets of the local retirement plans (i.e., the first class city teacher retirement fund associations, the Minneapolis Employees Retirement Fund (MERF), and the local police, paid fire, and volunteer fire relief associations) are invested by the particular retirement plan board and the assets of the statewide retirement plans are invested by the State Board of Investment.

Prior to 1961, the responsibility to invest statewide public pension plan assets lay with the State Board of Investment (see Minnesota Statutes 1953, Sections 135.04, Subdivision 4; 352.06; and 353.06), but neither the retirement plan governing laws nor the State Board of Investment governing laws specifically regulated the types of investment securities in which those assets could be invested. In 1961 (Laws 1961, Chapter 380), the investment authority over state retirement funds was first delineated, with the legislation coded in the Minnesota State Retirement System (MSRS) governing law. The 1961 enactment set the prudent person rule as the general investment standard and included a “legal list” of authorized types of investment securities, which included the following:

1. U.S. Government bonds or notes;
2. Minnesota or other U.S. state bonds;
3. Dominion of Canada or Canadian province bonds;
4. Minnesota municipal bonds, notes, or obligations;

5. Other U.S. state municipal bonds;
6. Canadian municipal bonds;
7. International Bank for Reconstruction and Development obligations;
8. U.S. agency insured obligations;
9. Minnesota public housing obligations;
10. Other state, municipal, or public authority obligations with income for each of the prior five years at least equal to 120 percent of its average annual debt service;
11. U.S. or Canadian corporate bonds, if Canadian bond debt service is payable in U.S. dollars, and if the corporation has assets of at least $10 million and has capital stock equal to at least 50 percent of its debt, has pretax earnings over each of the prior five years of 150 percent of annual interest charges, and has gross operating revenues of at least $1 million, and the bond issue is rated at least "A" by a recognized commercial rating agency. Total corporate bond investments were limited to 40 percent of the total assets of the fund;
12. U.S. corporate stock of a corporation with at least $10 million, with corporate earnings equal to the prior five-year average of interest and preferred dividend requirements for preferred stock, and with the payment of cash dividends for at least five years before the purchase. Investment in any one corporation was limited to one percent of the assets of the fund. The total corporate stock investments were limited to 25 percent of the assets of the fund, with a maximum increase in the stock investment in any year of five percent of the assets of the fund. The investment of all Minnesota public pension plans in any one corporation was limited to five percent of its voting stock;
13. Bank certificates of deposit and savings account if insured by a federal agency and if needed for liquidity; and
14. Commercial paper of less than 270-day maturity if the corporation has assets equal to 150 percent of current liabilities and long-term debt, and has average annual income over the past five years of at least $1 million. Commercial paper in total cannot exceed five percent of the book value of the fund and in any one corporation cannot exceed two percent of the book value of the fund.

In 1961, the State Board of Investment created the predecessor the current Investment Advisory Council to advise the board on the entry of statewide Minnesota public pension plans into corporate stock investments.

In 1967 (Laws 1967, Chapter 404), the authorized retirement plan investment specification was moved out of the MSRS statutes and was added to the State Board of Investment statutes. During the 1970s and 1980s, the investment authority of the State Board of Investment was expanded and the requirements and maximums relaxed. In 1989, a separate public pension plan fiduciary responsibility law was enacted for the State's statewide and local retirement plans, including a "prudent person" rule as a general fiduciary standard and legal lists of authorized investments. Initially, the fiduciary law legal list for larger or professionally managed local retirement plans replicated the legal list applicable to the State Board of Investment. In 1993-1994, in connection with the issue of authorizing non-investment grad corporate bonds for the State Board of Investment, the fiduciary law legal list retained the pre-1994 authority of the State Board of Investment.

Volunteer firefighter relief associations are either subject to a limited list of authorized investment securities or to an expanded list of authorized investment securities.

Minnesota Statutes, Section 356A.06, Subdivision 6, provides that a relief association that has less than $1 million in assets based on book value is a limited list plan unless the relief association:

1. Invests at least 60 percent of its assets based on book value using the services of an investment advisor registered with the securities and exchange commission in accordance with the federal Investment Advisors Act of 1940 or uses a licensed investment advisor under state law; or
2. Invests at least 60 percent of its assets based on book value through the State Board of Investment; or
3. Uses a combination of a registered/licensed investment advisor and the State Board of Investment to invest at least 75 percent of its assets based on book value.

A relief association which has more than $1 million in assets based on book value or which meets one or more of the above requirements is an expanded list plan and is permitted to invest according to the expanded list of authorized investment securities under Minnesota Statutes, Section 356A.06, Subdivision 7.

Section 356A.06, Subdivision 6, includes the following investment securities in the limited list of authorized investment securities:

1. Insured certificates of deposit and savings accounts.
2. Fixed income government obligations which have yield and quality comparable to non-tax exempt issues, and which have been issued by government units which back the securities by full taxing authority and which have not defaulted on any interest and principal during the preceding ten years (revenue bonds must be self supporting for the last five years).
3. Domestic corporate obligations, including bonds, notes, debentures, or other regularly issued and readily marketable forms of indebtedness, providing that average pre-tax earnings for the past five years are at least 150 percent of total interest and principal payments, and providing that the debt is in the top three quality ratings of Moody's Investors Service or Standard and Poor's ratings.
4. Mutual fund shares, providing that the securities the mutual fund holds comply with (1) through (3) above.

Section 69.775 permits stock investing through a mutual fund. Section 69.775 indicates that, notwithstanding Section 356A.06, Subdivision 6, volunteer firefighter relief associations can invest up to 75 percent of the market value of their assets in open end mutual funds if the investments of those funds are consistent with the expanded list of authorized investments.

Those volunteer firefighter relief associations that are not subject to the limited list are permitted by Section 356A.06, Subdivision 7, to invest in the full range of acceptable investments for the State Board of Investment prior to 1994. This creates a difference between the relief associations that are subject to the limited list and those which are not. The difference concerns the form of the investments. Limited list relief associations can invest through mutual funds in securities of the types applicable to expanded list volunteer firefighter relief associations. Those associations subject to the expanded list and not subject to the limited list can invest in these assets without use of a mutual fund.

The expanded list of authorized investment securities includes the following:

1. Government obligations, including notes, bills, bonds, and mortgages backed by the full faith and credit of the issuer and with a rating within the top four quality rating categories of a nationally recognized rating agency. Acceptable investments include guaranteed and insured issues of the United States and its agencies, the states and their political subdivisions, Canadian issues and those of the International Bank for Reconstruction and Development, the Inter-American Development Bank, the Asian Development Bank, the African Development Bank, or any other United States Government sponsored organization of which the United States is a member, provided that the principal and interest is payable in United States dollars;
2. Domestic corporate debt, including bonds, notes, debentures, and transportation equipment obligations, providing the obligations are rated among the top four quality categories by a nationally recognized rating agency, and Canadian debt meeting these quality requirements, providing the principle and interest payments are in United States dollars;
3. Various other forms of investments, including bankers acceptances, certificates of deposit, commercial paper, mortgage participation certificates and pools, guaranteed investment contracts, savings accounts, guaranty fund certificates, surplus notes, and mutual insurance company debt, providing various quality and insurance requirements regarding these various investments as specified in detail in the statutes are met;
4. Stocks and convertibles of any domestic corporation, Canadian corporation, or any corporation whose stock trades on the New York or American Stock Exchanges; and
5. Venture capital, real estate and resource limited partnerships, below investment grade debt, and international securities, with limits regarding the minimum number of other unrelated owners of the limited partnership investments and the maximum portion of a portfolio that can be devoted to these types of investments, in order to limit the risk exposure.

Finally, Minnesota Statutes, Section 356.71, permits any public pension plan whose assets are not invested by the State Board of Investment to invest in Minnesota situs non-farm real estate ownership interests or loans secured by mortgages or deeds of trust.

J. Fiduciary Obligations. The fiduciary obligations of volunteer firefighter relief association administrators and the standards which they must follow in conducting those duties are codified in Minnesota Statutes, Chapter 356A, the Public Pension Fiduciary Responsibility Law. This regulation includes:

1. Fiduciary Status. Board members and the chief administrating officer of volunteer firefighter relief associations are fiduciaries. As fiduciaries, they have a duty to active members, deferred retirees, and benefit recipients, to the state, and to local taxpayers.

2. Fiduciary Activities. The activities of volunteer firefighter plan fiduciaries include, but are not limited to:

   i. Determination of Plan Benefits. Administrators must correctly compute benefits and provide only authorized benefits to plan members;

   ii. Determining Funding Requirements and Contributions. Funding requirements must be properly determined;

   iii. Maintaining Membership and Financial Records. Accurate, well maintained membership data and financial information must be maintained;

   iv. Plan Administrative Expenses. Administrative expenses must be reasonable and necessary; and

   v. Investment of Plan Assets. Investments should be properly diversified, prudent, and consistent with laws indicating authorized investments for the particular fund.

   All fiduciary activities must be conducted in accordance with the purpose and intent of the by-laws and relevant laws, and must be conducted faithfully and without prejudice. No fiduciary or relative of a fiduciary may receive anything more than nominal compensation in consideration for a pension plan disbursement. The administrators are also bound in all their actions by the prudent person standard, which requires the fiduciary to act in good faith and to exercise the degree of judgement and care that persons of prudence, discretion, and intelligence would exercise in the management of their own affairs, and, for investments, not undertaken for speculation, considering the probable safety of the plan capital as well as the probable investment return to be derived from the assets.

3. Specific Investment Requirements. Section 356A.06 details investment-related fiduciary requirements, as follows:

   i. Financial control of assets. Plan assets may be held only by the plan treasurer, the depository agent of the plan, or the State Board of Investment or its depository agent;

   ii. Diversification. Investment must be properly diversified among investment types to minimize the risk of substantial investment losses;

   iii. Sufficient Liquidity. Plans must invest sufficient assets in cash equivalent securities to meet immediate liquidity needs, thus avoiding losses due to forced early liquidation of other securities;

   iv. Collateralization. Plans are required to designate a financial institution as the depository for plan assets not held by the plan's custodian bank and is subject to the applicable federal government insurance limits unless collateralized by the institution.

   v. Investment Authority Disclosure. Before using any investment broker, the plan is required to provide the broker with a written statement of the applicable state law and plan policy investment restrictions and the broker must acknowledge receipt of the statement and must agree to comply with those restrictions.

   vi. Conflicts of Interest. Any conflict of interest must be avoided and no fiduciary may personally profit, directly or indirectly, from the investment of plan assets;

   vii. Prohibited Transactions. Certain transactions are explicitly prohibited, which include, but are not limited to, sales, exchanges, or leases of real estate between the pension plan and a fiduciary of the plan, lending of money or extensions of credit by the plan to a fiduciary, transfers of assets between a fiduciary and the plan, and sales of services by a fiduciary to a plan;

   viii. Economic Interest Statement. To help identify actual or potential conflicts of interest, members of the governing board and the chief administrative officer of the relief association must file an annual economic interest statement which is available for public inspection, which must identify ownership interests in investment brokerage businesses, real estate sales, insurance agencies, banks, or other financial institutions, and which must identify any relationship or financial arrangement that can lead to a conflict of interest;

ix. Investment Business Recipient Disclosure. The chief administrative officer must annually disclose the recipients of investment business or investment commissions paid to brokers, banks, or other investment managers; and

x. Authorized Investments. Volunteer fire relief associations are either "limited list" associations, or "expanded list" associations, depending on the size of their asset base or whether the plan uses professional investment advisors. Plans with more than $1 million in assets, or smaller plans that use professional investment advisors are expanded list associations, enabling them to invest following essentially the same investment authorization as the State Board of Investment had prior to 1994. In addition, under other statutes, these plans are given broader real estate investment authorization than the State Board of Investment. Limited list plans are somewhat more restricted, although they share the same real estate investment authorization as the expanded list plans. In all cases, investments must meet prudent investment standards.

4. Required Disclosure to the Membership. The chief administrating officer of the volunteer firefighter relief association must provide a benefit summary to all plan participants. A copy of all financial reports and actuarial reports required of volunteer fire plans, or a summary of these reports, must be provided to relief association members.

5. Adverse Determination Review Procedure. A review procedure covering adverse determination of eligibility, benefits, or other rights under the plan must be available to volunteer firefighter relief association members. Members must be given timely notice and a reasonable opportunity to be heard in the review process. If a specific review procedure is not specified by other law, the volunteer firefighters relief association must develop and adopt a review procedure.

6. Fiduciary Continuing Education Requirement. Fiduciaries must make a reasonable effort to obtain the knowledge and skills necessary to perform their obligations effectively. The governing boards of the volunteer firefighter relief associations must develop continuing education programs for relief association board of trustee members who are not proficient in all areas of their fiduciary responsibilities.

7. Consultant Certificate of Insurance. Before hiring or contracting with a consultant, a volunteer fire relief association must obtain a copy of the consultant’s certificate of insurance. A consultant is an individual or firm providing legal or financial advice, including an actuary; attorney; accountant; investment advisor, manager, counselor, or investment manager selection consultant; pension benefit design advisor or consultant; or any other financial consultant.

K. Background Information on Fire State Aid.

1. Establishment. The Fire State aid program was initially established in 1885 (Laws 1885, Chapter 187). The program is codified in Minnesota Statutes, Sections 69.011 through 69.051.

   The Fire State aid was initially intended to assist municipal and other fire departments in obtaining firefighting equipment and in providing firefighter pension coverage. In 1943, for municipalities and nonprofit firefighting corporations with fire pension coverage, the Fire State aid was dedicated to fire pension funding. Fire State aid is payable to municipalities and fire department with paid or volunteer firefighters or with a combination of paid and volunteer firefighters.

2. Source of Fire State Aid Revenue. The Fire State aid program is funded from a premium tax on various types of minimum coverage, primarily fire insurance. The 1885 law established a one-half of one percent tax on insurance premiums for property located in municipalities having a fire protection service. Laws 1903, Chapter 20, raised the tax to the two percent premium tax level and specified uses for the money raised. The funds were to be used to provide retirement and disability benefits to fire department members and their survivors, and to help maintain the fire department, including covering purchase and maintenance costs of fire equipment.

   After 1903, the most fundamental changes in the Fire State aid laws were to restrict the use of the aid to providing pension and disability related benefits, and to change the nature of the aid distribution system. Authority to use the aid to purchase fire equipment and to cover other costs of operating the fire service existed from 1885 until 1943, when Laws 1943, Chapter 323, Section 2, deleted the language authorizing this use. Laws 1945, Chapter 225, provided for the use of fire State aid for firefighting equipment purposes only if no firefighter relief association is associated with the fire department.

Before 1995, the Fire State aid program was financed from the dedicated proceeds of a generally applicable two percent premium tax on fire, lightning, sprinkler damage, and extended coverage insurance on property located within the State. Minnesota Statutes, Section 60A.15, Subdivision 1, imposed a premium tax on fire and related insurance of two percent for most insurance companies, and one-half of one percent for town and farmer's mutual insurance companies and mutual property and casualty insurance companies with assets less than $1.6 billion. The Fire State aid under Minnesota Statutes, Section 69.021, Subdivision 5, Paragraph (b), was funded by an appropriation equal to the amount of fire and related insurance premium taxes collected. Half of the total Fire State aid amount was distributed in proportion to the population according to the last federal census and half was distributed in proportion to property market values, excluding mineral values but including tax-exempt property. This allocation method reflected an assumption that local property values and population relative to the whole State reflect the relative need for fire protection services. Before 1995, the last major revision in the insurance premium tax rates underlying the fire State aid program occurred in 1988 (Laws 1988, Chapter 719, Article 2, Sections 1 through 5) when the fire and related insurance premium tax rates were reduced for certain mutual insurance companies. Before 1995, the last major revision in the amount of State tax revenue available for allocation as Fire State aid occurred in 1991 (Laws 1991, Chapter 291, Article 13) when the appropriation for the Fire State aid program was reduced to the amount of the insurance premium taxes raised.

The 1995 Omnibus Tax Bill, Laws 1995, Chapter 264, increased the various insurance premium taxes and also increased the revenue available for the fire State aid program. Laws 1995, Chapter 264, Article 9, Section 3, amending Minnesota Statutes, Section 60A.15, Subdivision 1, increased the insurance premium tax rates for town and farmers' mutual insurance companies and for mutual property casualty companies with assets no greater than $1.6 billion. The pre-1995 insurance premium tax rate for these mutual insurance companies was one-half of one percent of the amount of all premiums. The rate was increased by the 1995 Legislature to two percent of all life insurance premiums, one percent of all other insurance premiums for all town and farmers' mutual insurance companies and for the smaller mutual property and casualty companies (assets of no more than $5 million) and 1.26 percent of all other insurance premiums for the larger mutual property and casualty companies (assets over $5 million and no greater than $1.6 billion). Laws 1995, Chapter 264, Article 9, Section 5, amending Minnesota Statutes, Section 69.021, Subdivision 5, increases the insurance premium tax revenue dedicated to the fire State aid program and the police State aid program. For the fire State aid program, the dedicated revenue is increased from the amount of insurance premium taxes collected on fire, lightning, sprinkler leakage, and extended coverage insurance, to the greater of either 107 percent of the fire, lightning, sprinkler leakage, and extended coverage insurance premium taxes collected or an amount equal to one percent of the fire, lightning, sprinkler leakage, and extended coverage premiums written by town and farmers' mutual insurance companies and by mutual property and casualty companies with assets not exceeding $5 million and to two percent of the fire, lightning, sprinkler leakage, and extended coverage premiums written by all other fire risk insurers.

In 1996, Minnesota Statutes, Sections 69.021, Subdivision 7, and 423A.02, were amended to implement a minimum Fire State aid floor for volunteer firefighter relief associations that would otherwise receive a disproportionately small amount of Fire State aid on a per-active-member basis.

Total Fire State aid has increased over time, as follows:

Year	Total Fire State Aid	Aid to Volunteer Firefighters	Aid to Paid Firefighters
1988	$10,840,404	$7,528,581	$3,311,823
1989	10,923,145	7,601,263	3,321,882
1990	10,872,111	7,508,647	3,363,464
1991	10,491,446	7,650,439	2,841,532
1992	10,530,014	7,716,007	2,814,007
1993	9,997,957	7,349,215	2,648,742
1994	10,665,543	7,869,847	2,795,696
1995	11,336,631	8,405,060	2,931,571
1996	14,797,126	11,006,256	3,790,870
1997	15,148,160	11,476,519	3,671,641
1998	16,088,768	11,976,222	4,112,546
1999	16,682,376	12,419,342	4,263,034
2000	17,265,502	12,879,980	4,385,522
2001	17,964,376	13,595,203	4,369,173
2002	19,912,608	14,930,886	4,981,722

3. Qualification Requirements for Receipt of Fire State Aid. Before 1969, Fire State aid was provided to municipalities that had an organized fire department upon the filing of a certificate by the municipal clerk stating that the fire department exists, stating that the fire department does not employ any minor under age 18, and indicating the fire department's water supply, the number of fire department organized companies, the number of fire department engines and trucks, the number of hose carts in use, and the number of hose feet in use.

   In 1969, the qualifications for Fire State aid were increased. Municipalities and independent nonprofit firefighting corporations using paid, volunteer, or a combination of paid and volunteer firefighters can qualify to receive the aid. To determine which municipalities and independent nonprofit firefighting corporations qualify for the aid, the municipal clerk or the secretary of the nonprofit firefighting corporation, if appropriate, and fire chief certify by March 15 of each year to the Department of Revenue that a municipal fire department or nonprofit firefighting corporation exists which meets minimum required standards for the aid.

   Under Minnesota Statutes, Section 69.771, and other volunteer firefighter relief association statutes, the initial qualification for fire state aid by a municipality and its associated volunteer firefighter relief association and the retention of fire state aid is conditioned on compliance with several requirements. Those requirements, in the view of the staff of the Legislative Commission on Pensions and Retirement, are the following:

   i. Fire Department Existence Certification. The clerk of a municipality or the secretary of an independent nonprofit firefighting corporation must certify the existence of the fire department on or before March 15 (Minnesota Statutes, Section 69.011, Subdivision 2);

   ii. Fire Department Minimum Requirements. A municipal fire department must have been officially established and organized for at least one year. An independent nonprofit firefighting corporation must operate exclusively for firefighting purposes and must provide retirement benefits to firefighters. Fire department or firefighting corporation must have at least ten firefighters, have regular meetings and frequent drills, a motorized fire truck with equipment, has suitable housing for apparatus, have alarm system, have second piece of motorized apparatus if service area exceeds municipal limits, and meet other Department of Revenue requirements, with compliance determined by the State Fire Marshal (Minnesota Statutes, Sections 69.011, Subdivisions 4 and 5, and 69.021, Subdivision 4);

   iii. Relief Association Financial Report or Statement. The volunteer firefighter relief association must file a financial statement (liabilities or assets under $200,000) by March 31 or a financial report (liabilities or assets of at least $200,000) by July 1 (Minnesota Statutes, Section 69.051, Subdivisions 1, 1a, 1b, 3, and 4);

   iv. Relief Association Treasurer Bond. The volunteer firefighter relief association treasurer must be bonded to a minimum amount (Minnesota Statutes, Section 69.051, Subdivision 2);

   v. Relief Association Financial Requirements Determination. The volunteer firefighter relief association officers must determine relief association funding requirements, based on liability calculations or actuarial valuation, whichever is required (Minnesota Statutes, Sections 69.771, 69.772, and 69.773);

vi. Relief Association Minimum Municipal Contribution. The municipality or the independent nonprofit firefighting corporation must budget for the minimum contribution and the municipality must budget for that contribution amount (Minnesota Statutes, Sections 69.772 and 69.773);

vii. Municipal Ratification of Plan Amendments. Unless the volunteer firefighter relief association is fully funded before and after the plan amendment, the municipality must ratify plan amendments affecting benefits (Minnesota Statutes, Sections 693772, Subdivision 6; 69.773, Subdivision 6; and 424A.02, Subdivision 10);

viii. Authorized Relief Association Investments. Volunteer firefighter relief association special fund assets must be investment in authorized investment securities (Minnesota Statutes, Sections 69.775 and 356A.06, Subdivisions 6 or 7);

ix. Authorized Relief Association Administrative Expenses. The volunteer firefighter relief association or the municipality must limit administrative expenses to authorized expenses (Minnesota Statutes, Section 69.80 or 424A.05, Subdivision 3);

x. Relief Association Investment Performance Reporting. The volunteer firefighter relief association must make investment portfolio and investment performance report (Minnesota Statutes, Section 356.219);

xi. Investment Authority Statement. The volunteer firefighter relief association must provide all investment brokers with written statement of investment restrictions and receive acknowledgement and compliance agreement from the broker annually (Minnesota Statutes, Section 356A.06, Subdivision 8b);

xii. No Prohibited Transactions. The volunteer firefighter relief association must not permit a prohibited transaction to occur or must correct a prohibited transaction that did occur (Minnesota Statutes, Section 356A.06, Subdivision 9); and

xiii. No Excessive Service Pension Amount. The defined benefit volunteer firefighter relief association must not provide a service pension that is in excess of the applicable service pension maximum (Minnesota Statutes, Section 424A.02, Subdivision 3).

4. Allocation of Fire State Aid. Initially, Fire State aid was allocated to the various municipalities and independent nonprofit firefighting corporations based on the amount of fire insurance written in that firetown, as identified by the various insurance agents and insurance companies. The allocation method eventually proved problematic, in part because of errors made by insurance company agents in identifying applicable firetowns.

   In 1969, the allocation method was shifted to a combination of population ranking and property value ranking. One half of the Fire State aid was distributed in proportion to the population according to the last federal census and one half was distributed in proportion to property market values, excluding mineral values but including tax-exempt property. This allocation method reflected an assumption that local property values and population relative to the whole State reflect the relative need for fire protection services.

   In 1996, for municipalities and independent nonprofit firefighting corporations with wholly volunteer fire departments, an additional allocation of aid is made to bring the municipal or corporation total up to the minimum volunteer firefighter fire State aid amount multiplied by the total number of active volunteer firefighters to a maximum of 30 firefighters.

5. Permissible Use of Fire State Aid. Initially, in 1885, fire State aid could be used to pro-vide firefighters with pension coverage or to maintain the fire department, including the purchase of fire equipment. In 1943, the Fire State aid was dedicated solely to firefighter pension funding if the firefighters have pension coverage. For municipalities and non-profit firefighting corporations where the associated firefighters do not have pension coverage, Fire State aid must be used to maintain the fire department or purchase fire equipment.

6. Source of Additional Revenues if Shortfall Occurs. If a relief association funding requirements exceed all applicable revenue sources, including tax revenues derived from taxes on life insurance providers and town and farmers' mutual insurance companies and mutual property and casualty companies, any shortfall or additional revenue needs must be paid from the state's general fund if appropriated by the Legislature. The provision is not to be interpreted as relieving any municipality of its obligations to a relief association.

L. Background Information on the Minimum Volunteer Fire State Aid Program.

1. Establishment. The minimum volunteer Fire State aid program was enacted in 1996 (Laws 1996, Chapter 438, Article 4, Section 2). The program is codified as Minnesota Statutes, Sections 69.021, Subdivision 7, Paragraph (d), and 423A.01, Subdivision 7, Paragraph (a). The minimum Fire State aid program was an effort to address a long-standing concern that the State fire tax aid provides unreasonable low aid amounts per firefighter in many communities in the State. Many jurisdictions were receiving well under $100 per firefighter. After the minimum Fire State aid program was introduced, the floor aid per eligible firefighter was increased to slightly over $260 per firefighter.

2. Source of Minimum Fire State Aid. Thirty percent of any unallocated amortization or supplemental amortization State aid is dedicated as a minimum Fire State aid amount for volunteer fire relief associations. Amortization State aid and supplemental amortization State aid becomes unallocated when there is the payment of a thirteenth check by the Minneapolis Fire Relief Association or by the Minneapolis Police Relief Association or when a former local police or paid firefighter consolidation account became fully funded.

   The amount of amortization State aid and supplemental amortization State aid dedicated to the minimum fire State aid (and added to the fire insurance premium tax equivalent amount dedicated to pension purposes and already included in the total fire State aid in the preceding section) is as follows:

Year	Total Additional Aid Dedicated to Volunteer Firefighters
1996	$ 663,788
1997	667,610
1998	974,076
1999	1,034,608
2000	1,210,366
2001	1,065,323
2002	1,846,119

3. Qualification Requirements for the Receipt of Minimum Fire State Aid. The minimum volunteer firefighter Fire State aid is payable to municipalities with volunteer firefighters and with Fire State aid calculated on the basis of relative property value and relative population that is modest, with these minimum receipt municipalities brought up to the minimum fire State aid amount for firefighters, not to exceed 30, until the funding dedicated for the program is exhausted. Roughly half of the municipalities with volunteer firefighter relief associations receive some minimum Fire State aid amount.

4. Allocation of Minimum Fire State Aid. The minimum Fire State aid program is targeted to volunteer fire relief associations that receive low aid per firefighter under the State fire tax aid program. The firefighter count used in the allocation procedure is the number of firefighters, not to exceed 30, in each relief association in 1993. The minimum floor Fire State aid program brings the funding for those associations receiving the least aid per firefighter up to a higher, uniform level. Volunteer fire relief associations established after 1999 also are eligible for inclusion in the minimum floor fire aid distribution. The member count the association will use in the distribution is the member count, up to a limit of 20 firefighters, reported in the first annual financial reporting submitted to the State Auditor by the association.

5. Permissible Uses of Minimum Fire State Aid. Minimum Fire State aid is included in the Fire State aid allocation and is subject to the same permissible use as fire State aid.

M. Background Information on the First Class City Fire Insurance Premium Tax Surcharge.

1. Establishment. The first class city fire insurance premium tax surcharge was enacted in 1934 (Extra Session Laws 1934, Chapter 53, Sections 1 through 3). It is codified in Minnesota Statutes, Section 297I.10.

   The first class city fire insurance premium tax surcharge was enacted to assist the three first class city fire department relief associations in paying the service pensions and other retirement benefits that are payable. The provisions were enacted at a time when the Duluth Fire Department Relief Association, the Minneapolis Fire Department Relief Association, and the St. Paul Fire Department Relief Association were funded in virtually a current disbursements (or "pay-as-you-go") manner, when there were substantial statutory limits on the amount of municipal taxes that could be levied in support of the relief associations, and before the enactment of the 1969 Police and Paid Fire Relief Association Financing Guidelines Act mandating some measure of actuarial funding.

2. Source of Program Revenue. The first class city fire insurance premium tax surcharge is funding from the dedicated proceeds of a surcharge on the premiums paid on fire insurance written in a city of the first class. The surcharge is an amount equal to two percent of those premiums. The surcharge is collected by the Commissioner of Commerce and deposited in the State General Fund.

3. Qualification Requirement for Receipt of Surcharge Amounts. There are no qualification requirements for the receipt of the first class city fire insurance premium tax surcharge proceeds.

4. Allocation of First Class City Fire Insurance Premium Tax Surcharge. The first class city insurance premium tax surcharge is allocated based on the geographical source of the insurance premium tax surcharge. Thus, the fire insurance premium tax surcharge proceeds collected from Duluth are payable to the Duluth Fire Consolidation Account, the fire insurance premium tax surcharge proceeds collected from Minneapolis are payable to the Minneapolis Firefighters Relief Association, and the fire insurance premium tax surcharge proceeds collected from St. Paul are payable to the St. Paul Fire Consolidation Account.

N. Background on the Volunteer Fire Lump Sum Supplemental Benefit and State Reimbursement.

1. Establishment. In 1988 (Laws 1988, Chapter 719, Article 19, Section 22), as part of that legislative session's tax bill, the Legislature mandated that volunteer firefighter relief associations that pay a lump sum service pension also pay a supplemental benefit equal to ten percent of the amount of the lump sum service pension payable to retiring members, to a maximum of $1,000 per lump sum service pension. The provision is coded as Minnesota Statutes, Section 424A.10. The supplemental benefit was intended to reimburse retiring volunteer firefighters for a change in Minnesota tax law, enacted in the late 1980s, which caused Minnesota public pensions to be taxable under Minnesota law. Given the relatively modest level of volunteer fire pensions, at least as of the late 1980s, the 1988 enactment of the volunteer fire lump sum supplemental benefit may have been intended to offset the impact of that new Minnesota taxation, so that the new tax treatment did not discourage individuals from providing volunteer fire services.

2. Source of the Volunteer Fire Lump Sum Supplemental Benefit State Reimbursement. The volunteer fire lump sum supplemental benefit State reimbursement is payable from a State General Fund appropriation to the Department of Revenue.

3. Qualification Requirements for Receipt of the Volunteer Fire Lump Sum Supplemental Benefit State Reimbursement. The supplemental benefit is reimbursable by the State if the volunteer firefighter relief association that paid the supplemental benefit applies with the Commissioner of Revenue by the subsequent February 15, with the reimbursement paid on March 15 from a State General Fund appropriation for that purpose.

4. Amount of the Volunteer Fire Lump Sum Supplement Benefit State Reimbursement. The amount of the State General Fund appropriation to the Department of Revenue for payment by the Department of Revenue of volunteer fire lump sum supplemental benefits is as follows:

Fiscal Year	Supplemental Benefit Reimbursement Appropriation	Fiscal Year	Supplemental Benefit Reimbursement Appropriation
1989	not available	1996	$400,000
1990	not available	1997	378,000
1991	not available	1998	375,000
1992	not available	1999	370,000
1993	not available	2000	378,000
1994	not available	2001	420,000
1995	$400,000	2002	420,000

5. Permissible Uses for Reimbursement Amounts. The State reimbursement of volunteer fire lump sum supplemental benefits are required to be deposited into the special fund of the applicable volunteer firefighter relief association and may be expended for any lawful purpose for the relief association.

Appendix D

Background Information on Common Stock Investment Securities and Exchanges

Minnesota public pension plans are permitted to invest in corporate stocks. Under Minnesota Statutes, Section 11A.24, Subdivision 5, the State Board of Investment may invest funds in stocks or convertible issues of any corporation that is organized under the laws of the United States or the states thereof, any corporation that is organized under the laws of the Dominion of Canada or its provinces, or any corporation listed on an exchange regulated by an agency of the United States or Canadian national government, if the aggregate value of corporate stock investments, as adjusted for realized profits and losses does not exceed 85 percent of the market or book value, whichever is less, of a fund, less the aggregate value of alternative investments and if the investment does not exceed five percent of the total outstanding shares of any one corporation, or exceed 20 percent of the shares of a real estate investment trust, or exceed 20 percent of the shares of a closed-end mutual fund. Under Minnesota Statutes, Section 356A.06, Subdivision 7, Paragraph (f), any Minnesota public pension plan with assets over $1 million or is not invested through the State Board of Investment or a professional investment manager for at least 60 percent (75 percent combined) of the book value of assets can invest in the same corporate stocks, except that the exchange listing requirement is limited to the New York Stock Exchange or the American Stock Exchange.

Corporate stocks are a form of equity investment and represent a degree of ownership of a corporation. Stocks are divided into common stocks and preferred stocks. Common stocks and preferred stocks both represent ownership in a corporation, but common stocks have voting rights in the corporation while preferred stocks do not have voting rights in the corporation, and common stocks may receive dividends based on the proportionate ownership while preferred stocks received a fixed dividend year after year and have a preference in receiving distributions from the corporation over the claims of common shareholders if the corporation is liquidated.

Common stock sometimes has different classes. The most common reason for different classes of stock is that the corporate board wants a significant portion of the voting power with respect to the corporation to remain with a particular group. For example, one class of shares could be held by a select group who are given ten votes per share while a second class could issued to the majority of investors who are given one vote per share.

Common stocks are generally traded on an exchange. An exchange is a place where buyers of corporate stocks and sellers of corporate stocks meet and decide on a transaction price. Some exchanges are physical locations where transactions are carried out on a trading floor. The other type of exchange is a virtual kind, composed of a network of computers where trades are made electronically. A stock market is intended to facilitate the exchange of securities between buyers and sellers, thus reducing the risks of investing.

Stock markets are either primary markets or secondary markets. The primary market is where securities are created through an initial public offering while, in the secondary market, investors trade previously issued securities without the involvement of the issuing companies. If a corporate stock is not traded on an exchange, the security can be traded on an “over the counter” market. These markets have no central location or floor brokers whatsoever and trading is done through a computer and telecommunications network of dealers.

Securities market regulation is premised on a belief that investors are more likely to trade on a market when prices are current and reflect the value of securities, when they are confident that they will be able to buy and sell securities easily and inexpensively, and when they believe that they can trade on a market without being defrauded or without other investors having an unfair advantage. Appropriate regulation is often necessary to protect these interests, by helping to ensure fair and orderly markets, to prevent fraud and manipulation, and to promote market coordination and competition for the benefit of all investors. Commercial incentives alone are insufficient to protect investors adequately and ensure fair markets. The U.S. Congress, in 1934, noted that, however zealously exchange authorities may supervise the business conduct of their members, the interests with which they are connected frequently conflict with the public interest.

The United States Securities and Exchange Commission (SEC) regulates securities markets, primarily under the Securities Exchange Act of 1934. Congress created the Securities and Exchange Commission in the Securities Exchange Act of 1934, which gives the SEC broad authority overall aspects of the securities industry, including the power to register, regulate, and oversee brokerage firms, transfer agents, and clearing agencies as well as the nation's securities self regulatory organizations (SROs). A self-regulatory organization is a member organization that creates and enforces rules for its members based on the federal securities laws. The various stock exchanges, such as the New York Stock Exchange, and American Stock Exchange are SROs. The National Association of Securities Dealers, which operates the NASDAQ (National Association of Securities Dealers Automated Quotation System) system, is also an SRO.

In 1975, Congress gave the exchanges authority to enforce their members' compliance with the goals of the securities laws and, in 1983, required every broker-dealer to become a member of an exchange or securities association. As SROs, every registered exchange and securities association is required to assist the SEC in assuring fair and honest markets, to have effective mechanisms for enforcing the goals of regulation, and to submit their rules for SEC review. This statutory structure has given the SEC ample authority to oversee securities markets and ensure compliance with the securities laws. Although regulation cannot prevent all manipulation, fraud, or collusion, it has proven effective in ridding markets of the most egregious of these practices and consequently in inspiring a high degree of investor confidence.

The Division of Market Regulation of the SEC establishes and maintains standards for fair, orderly, and efficient markets. It does this primarily by regulating the major securities market participants: broker-dealer firms; self-regulatory organizations (SROs), which include the stock exchanges and the National Association of Securities Dealers (NASD), Municipal Securities Rulemaking Board (MSRB), and clearing agencies (SROs that help facilitate trade settlement); transfer agents (parties that maintain records of stock and bond owners); and securities information processors.

There are currently nine securities exchanges registered with the SEC under Section 6(a) of the Securities Exchange Act of 1934 as national securities exchanges:

- American Stock Exchange
- Boston Stock Exchange
- Chicago Board Options Exchange
- Chicago Stock Exchange (includes the former Minneapolis-St. Paul Stock Exchange)
- International Securities Exchange
- National Stock Exchange (formerly the Cincinnati Stock Exchange)
- New York Stock Exchange
- Pacific Exchange
- Philadelphia Stock Exchange

The NASDAQ Stock Market is not a registered national securities exchange. NASD, Inc., is a registered national securities association under Section 15A of the Securities Exchange Act of 1934 that oversees the operations of the NASDAQ Stock Market. The NASDAQ Stock Market is comprised of the NASDAQ National Market, which trades the largest and most active securities, and the NASDAQ Small Cap Market, which lists a smaller number of emerging growth companies. The NASDAQ Stock Market electronically provides real-time quotes for over-the-counter securities and many New York Stock Exchange listed companies.

Appendix E

Background Information on Exchange-Traded Funds

Exchange-traded funds (ETFs) are investment companies that are registered under the Investment Company Act of 1940 as open-end funds or unit investment trusts (UITs). Unlike typical open-end funds or UITs, however, ETFs do not sell or redeem their individual shares ("ETF shares") at net asset value. Instead, ETFs sell and redeem ETF shares at net asset value only in large blocks (such as 50,000 ETF shares). In addition, national securities exchanges list ETF shares for trading, which allows investors to purchase and sell individual ETF shares among themselves at market prices throughout the day. ETFs therefore possess characteristics of traditional open-end funds and UITs, which issue redeemable shares, and of closed-end funds, which generally issue shares that trade at negotiated prices on national securities exchanges and are not redeemable. A fundamental characteristic of all existing ETFs traded in the United States is that they are based on specific domestic and foreign market indices. An "index-based ETF" seeks to track the performance of an index by holding in its portfolio either the contents of the index or a representative sample of the securities in the index.

During the year 2000, the number of ETFs increased from 30 to 80, and the amount of assets held by ETFs nearly doubled from $34 billion to $66 billion. While the total amount of ETF assets at the end of 2000 was still relatively small when compared to the approximately $4 trillion of assets in equity open-end investment companies ("open-end funds" or "mutual funds"), ETF assets were much closer to the $89 billion of total assets invested in unit investment trusts and the $135 billion of total assets invested in closed-end investment companies ("closed-end funds"). The following provides information on the assets and the number of exchange-traded index funds over an 11-year period, by type of fund:

Year	Total	Domestic Equity	Global/ International Equity	Bond
Assets *(millions of dollars, end of year)*				
1993	$464	$464	--	--
1994	424	424	--	--
1995	1,052	1,052	--	--
1996	2,411	2,159	$252	--
1997	6,707	6,200	506	--
1998	15,568	14,542	1,026	--
1999	33,873	31,881	1,992	--
2000	65,585	63,544	2,041	--
2001	82,993	79,977	3,016	--
2002	102,143	92,904	5,324	$3,915
2003	150,983	132,332	13,984	4,667
Number of Funds *(end of year)*				
1993	1	1	--	--
1994	1	1	--	--
1995	2	2	--	--
1996	19	2	17	--
1997	19	2	17	--
1998	29	12	17	--
1999	30	13	17	--
2000	80	55	25	--
2001	102	68	34	--
2002	113	66	39	8
2003	119	72	41	6

Note: Components may not add to the total because of rounding
Sources: Strategic Insight and Investment Company Institute

In 1993, a subsidiary of the AMEX introduced the first ETF – the SPDR Trust, organized as a unit investment trust. The SPDR Trust, which issues ETF shares referred to as SPDRs (pronounced "spiders"), is a UIT that tracks the Standard & Poor's 500 Composite Stock Price Index ("S&P 500 Index") by holding substantially all of the securities in the S&P 500 Index in substantially the same weightings as in the S&P 500 Index. The trustee adjusts the portfolio of the SPDR Trust only to reflect changes in the composition of the S&P 500 Index. In order to offer SPDRs, the SPDR Trust obtained exemptions from various provisions of the Investment Company Act of 1940. Among other things, the exemptions allow the SPDR Trust to redeem SPDRs in large aggregations only, SPDRs to trade at negotiated prices in the secondary market, dealers to sell SPDRs to purchasers in the secondary market unaccompanied by a prospectus (when prospectus delivery is not required by the Securities Act of 1933), and certain affiliated persons of the SPDR Trust to deposit securities into, and receive securities from, the SPDR Trust in connection with the purchase and redemption of large aggregations of SPDRs.

In 1996, ETF sponsors introduced the first two ETFs organized as open-end funds. The CountryBaskets Index Fund, Inc., consisted of different portfolios that tracked various country indices of the Financial Times/S&P Actuaries World Indices. The Foreign Fund, Inc., offers series that track various Morgan Stanley Capital International ("MSCI") country indices. These ETFs obtained exemptions from various provisions of the Act that were generally analogous to the exemptions obtained by the ETFs organized as UITs. Many ETFs organized as open-end funds replicate the holdings of their corresponding indices to track the performance of the indices. However, because ETFs organized as open-end funds employ investment advisers, some of these ETFs instead may use "sampling strategies" to track the performance of an index. Using a sampling strategy, an investment advisor can construct a portfolio that is a subset of the component securities in the corresponding index, rather than a replication of the index. The investment adviser also may acquire securities for the ETF portfolio that are not included in the corresponding index. While these ETFs still seek to track the performance of their respective indices, they have greater flexibility in accomplishing that goal. In addition, ETFs that are open-end funds are not prohibited from participating in securities lending programs or from using futures and options in achieving their investment objectives.

ETFs issue shares only in large aggregations or blocks (such as 50,000 ETF shares) called "Creation Units." An investor, usually a brokerage house or large institutional investor, may purchase a Creation Unit with a "Portfolio Deposit" equal in value to the aggregate net asset value of the ETF Shares in the Creation Unit. The investment adviser or sponsor of the ETF announces the contents of the Portfolio Deposit at the beginning of each business day. The Portfolio Deposit generally consists of a basket of securities that mirrors the composition of the ETF's portfolio. Because the purchase price of the Creation Unit must equal the net asset value of the underlying ETF shares, the required Portfolio Deposit generally also includes a small amount of cash to account for the difference between the value of the basket of securities and the net asset value of the ETF shares. The value of a Creation Unit typically exceeds several million dollars. After purchasing a Creation Unit, the investor may hold the ETF shares, or sell some or all of the ETF shares to investors in the secondary market.

ETFs register offers and sales of shares under the Securities Act of 1933 and list their ETF shares for trading on a national securities exchange under the Securities Exchange Act of 1934. As with any listed security, investors also may trade ETF shares in off-exchange transactions. In either case, ETF shares trade at negotiated prices. The development of the secondary market in ETF shares depends upon the activities of the exchange specialist assigned to make a market in the ETF shares and upon the willingness of Creation Unit purchasers to sell ETF shares in the secondary market.

ETF shares purchased in the secondary market are not redeemable from the ETF except in Creation Unit aggregations. If an investor purchases a Creation Unit to the ETF for redemption, the redeeming investor receives a "Redemption Basket," the contents of which are identified by the ETF investment advisor or sponsor at the beginning of the day. The Redemption Basket (usually the same as the Portfolio Deposit) consists of securities and a small amount of cash. An investor holding fewer ETF shares than the amount needed to constitute a Creation Unit may dispose of those ETF shares only by selling them in the secondary market. The investor receives market price for the ETF shares, which may be higher or lower than the net asset value of the ETF shares. The investor also pays customary brokerage commissions on the sale.

Appendix F

Background Information on the Federal Uniformed Services Employment and Reemployment Rights Act (USERRA)

The federal Uniformed Services Employment and Reemployment Rights Act (USERRA), passed in 1994, has the stated purpose to:

1. Encourage non-career service in the uniformed services by eliminating or minimizing the disadvantage to civilian careers and employment which can occur due to that uniformed service;
2. Provide for the prompt reemployment of individuals who provide uniformed service upon the completion of that service; and
3. Prohibit discrimination against persons because of the performance of uniformed service.

USERRA provisions apply to virtually all employers in the United States *in situations where there is an employee/employer relationship*. The Volunteer Fire Relief Association Working Group may wish to consider what Minnesota law changes, if any, that it should recommend. In a pure volunteer setting, presumably USERRA would not apply because there is no employee/employer relationship. To the extent that some volunteer fire plans cover individuals who do have an employment situation with the fire department, it is reasonable to conclude that these plans will need to comply with USERRA. While many other volunteer fire plans may provide coverage to individuals who can be properly viewed as volunteers (and who therefore are not employees of the city or fire department), the situation will be far more consistent and fair if comparable treatment is provided in all volunteer fire plans.

For purposes of USERRA, uniformed service includes service in the Army, Navy, Marine Corps, Air Force, Coast Guard, the reserve components of any of these organizations, the Commissioned Corps of the Public Health Service, and any other category of persons so designated by the President in time of war or emergency.

With few exceptions, USERRA requires the employer of the individual who provided the uniformed service to rehire that individual at the end of that uniformed service. To be covered by this reemployment right, or any other provisions of USERRA including the pension-related provisions of the act:

1. The individual must provide notice to the employer that the person is leaving to provide uniformed service (unless providing that notice is not possible due to the emergency nature of the situation);
2. The period of uniformed service must not exceed five years;
3. The person must not be released from uniformed service under dishonorable or other punitive conditions; and
4. The person must report back to the civilian employer in a reasonable time period.

“Reasonable time period” depends upon the length of uniformed service provided. If service is less than 31 days, the individual can be required to return to employment within eight hours of returning home. If the length of service is between 31 and 180 days, the employee must apply for reemployment no later than 14 days after completion of uniformed service. If the length of uniformed service is 180 days or longer, the individual must return to employment no later than 90 days after completion of uniformed service.

Regarding pension rights, USERRA states (USC Section 4318) that “a person reemployed under this chapter shall be treated as not having incurred a break in service with the employer or employers maintaining the plan by reason of such person’s period or periods of service in the uniformed services.” In a plan that requires employee contributions (which is not relevant in Minnesota volunteer fire plans since no employee contribution is made to these plans) the individual must make the same contributions that the individual would have made if the individual had continued to work for the employer during the uniformed service period.

Section-By-Section Summary of S.F. 259 (Betzold); H.F. 1706 (Smith)

Sec.	Page, Lines	Statute Section	Summary
1	Page 1, Lines 27-35; Page 2, Lines 1-32	Section 69.051, Subdivision 1	Resets the trigger for the requirement for a volunteer firefighter relief association to file a financial report rather than a financial statement, requiring a financial report in the calendar year after a relief association has liabilities or assets in excess of $200,000 and in every subsequent calendar year.
2	Page 2, Lines 33-36; Page 3, Lines 1-36; Page 4, Lines 1-6	Section 69.051, Subdivision 1a	Makes a conforming change as a result of Section 1, making the financial statement requirement applicable to volunteer firefighter relief associations which are not required to file a financial report.
3	Page 4, Lines 7-36; Page 5, Lines 1-36; Page 6, Lines 1-36; Page 7, Lines 1-25	Section 69.771	Augments the generic specification of the responsibility for the Office of the State Auditor to determine compliance by volunteer firefighter relief associations for qualification for fire state aid receipt with a specific enumeration of the reporting, funding, and investment requirements on which a compliance determination will be based, including filing a financial report or statement, meeting treasurer bonding requirements, filing an actuarial valuation that meets minimum contents requirements, failure to obtain a sufficient municipal contribution, failure to obtain municipal ratification of a benefit improvement, investing in an unauthorized investment security, making an unauthorized special fund administrative expense, failure to provide investment portfolio and performance reporting, failure to obtain broker acknowledgements of investment restrictions, permitting or failing to correct a prohibited transaction, or paying a service pension in excess of the applicable service pension maximum.
4	Page 7, Lines 26-36; Page 8, Lines 1-36; Page 9, Lines 1-36; Page 10, Lines 1-22	Section 69.772, Subdivision 3	Eliminates an obsolete 1971-related amortization references and clarifies the amortization requirement to match the procedure represented for several years in the applicable State Auditor's forms, with the original benefit increase-related unfunded liabilities required to be retired by one-tenth of the amount annually. Extends the revised lump sum volunteer firefighter relief association ten-year amortization requirement to lump sum volunteer firefighter relief association investment losses which previously were not required to be amortized. Caps the amortization amount at the remaining total unfunded liability amount, so the late in the period amortization contribution requirement does not exceed the actual principal unfunded amount remaining after having been reduced by other investment or contribution gains. Limits the deduction of expected fire state aid in determining the minimum municipal contribution to a reasonable estimate and a maximum on the reasonably expected fire state aid is set at the prior year's fire state aid increased by 3.5 percent.
5	Page 10, Lines 23-36; Page 11, lines 1-27	Section 69.772, Subdivision 4	Requires the annual financial reporting or financial statement of a volunteer firefighter relief association to include disclosure of the most recent relief association financial requirements and minimum municipal obligation. Authorizes the State Auditor to obtain copies of the relief association financial requirements and minimum municipal obligation certification documents under Minnesota Statutes, Sections 69.771 through 69.775, from the relief association and the applicable municipality if insufficient funding of the relief association is disclosed in the relief association annual financial reporting.
6	Page 11, Lines 28-36; Page 12, Lines 1-36; Page 13, Lines 1-36; Page 14, Lines 1-36; Page 15, Lines 1-4	Section 69.773, Subdivision 4	Adds a ten-year amortization requirement for monthly benefit volunteer firefighter relief association experience (mortality, retirement age, or investment) losses, which previously were not required to be amortized.

Sec.	Page, Lines	Statute Section	Summary
7	Page 15, Lines 5-36; Page 16, Lines 1-28	Section 69.773, Subdivision 5	Limits the deduction of expected fire state aid in determining the minimum municipal contribution to a reasonable estimate and a maximum on the reasonably expected fire state aid is set at the prior year's fire state aid increased by 3.5 percent. Requires the annual financial reporting or financial statement of a volunteer firefighter relief association to include disclosure of the most recent relief association financial requirements and minimum municipal obligation. Authorizes the State Auditor to obtain copies of the relief association financial requirements and minimum municipal obligation certification documents under Minnesota Statutes, Sections 69.771 through 69.775, from the relief association and the applicable municipality if insufficient funding of the relief association is disclosed in the relief association annual financial reporting.
8	Page 16, Lines 29-36; Page 17, Lines 1-24	Section 69.775	Excludes the amount of any investment of money market mutual funds from the calculation of the 75 percent market value maximum on investments in mutual funds by volunteer firefighter relief associations.
9	Page 17, Lines 25-36; Page 18, Lines 1-36; Page 19, Lines 1-36; Page 20, Lines 1-36; Page 21, Lines 1-36; Page 22, Lines 1-11	Section 356A.06, Subdivision 7	Expands the authorized corporate stock investments from stocks listed on the New York Stock Exchange or the American Stock Exchange to stocks listed on any exchange regulated by the United States federal government or the Canadian national government and adds as a specific authorized investment security exchange traded funds.
10	Page 22, Lines 12-36; Page 23, Lines 1-36; Page 24, Lines 1-36; Page 25, Lines 1-36; Page 26, Lines 1-36; Page 27, Lines 1-36; Page 28, Lines 1-27	Section 424A.02, Subdivision 3	Reduces the minimum three-year average amount of available financing per firefighter for monthly benefit service pensions from $84 per firefighter to $81 per firefighter for each $1 of monthly benefit service pension per year of service.
11	Page 28, Lines 28-36; Page 29, Lines 1-32	Section 424A.02, Subdivision 4	Clarifies that the provision applies to active members solely and clarifies the investment return crediting period.
12	Page 29, Lines 33-36; Page 30, Lines 1-36; Page 31, Lines 1-36; Page 32, Lines 1-5	Section 424A.02, Subdivision 7	Eliminates the current five percent interest option and adds an option for interest at a rate up to five percent per annum, set by the board of trustees of the relief association and if approved by the applicable municipality, and payable from the first of the month next following the separation from active service until the last day of the month preceding the application for the deferred service pension upon a former active member attaining the normal retirement age. Permits defined contribution volunteer firefighter relief associations to credit proportional amounts of investment gains or losses along with active members as of the most recent post date for determining and crediting investment return investment and largely restricts the current deferred service pension interest provision to lump sum defined benefit volunteer firefighter relief associations.
13	Page 32, Lines 6-29	New Section 424A.021	Allows a volunteer firefighter returning from a break in service to render military service up to five years of service credit in a volunteer fire relief association, providing that the individual provides notice to the fire department of the break in service to provide uniformed service, and promptly returns to firefighter service covered by the same relief association (or its successor) upon return from uniformed service, and the discharge from military service is not less than honorable.
14	Page 32, Lines 30-36; Page 33, Lines 1-36; Page 34, Lines 1-36; Page 35, Lines 1-6	Section 424A.04, Subdivision 1	Makes the municipal representation on the board more flexible by replacing ex-officio members with one elected and one elected or appointed municipal officer appointed by the municipal council, to reduce the municipal representation on relief association boards of trustees associated with an independent nonprofit firefighting corporation from three board members to two board members, and to clarify the municipal representation for joint powers entities and townships.
15	Page 35, Lines 7-10	Effective Date	Makes the changes effective on July 1, 2005.