



TO: Members of the Legislative Commission on Pensions and Retirement
FROM: Rachel Barth, Deputy Director
RE: LCPR16-025: Eden Prairie VFRA; Special Legislation to Raise Service Pension Maximum and Lower Lump-Sum Service Pension Vesting Period for Returning Firefighters
DATE: February 19, 2016

Summary of LCPR16-025

Bill draft LCPR16-025 implements the special provisions supported by the Eden Prairie Fire Department, the Eden Prairie Volunteer Firefighters Relief Association (VFRA), and the city of Eden Prairie. The bill is intended to address recruitment issues and aid the Eden Prairie VFRA in transitioning to a total lump-sum defined benefit plan. The main components of the bill are as follows:

1. Increase the Maximum Lump-Sum Service Pension Amount. The maximum lump-sum service pension amount that the Eden Prairie VFRA may provide in its bylaws is increased from the current \$10,000 maximum to \$15,000, which is increased through \$100 increments. The current maximum monthly benefit service pension amount in Minn. Stat. § 424A.02, subd. 3, para. (c), remains in effect.
2. Lower Vesting Period for Firefighters Returning to Eden Prairie VFRA Active Service. The required vesting period for Eden Prairie volunteer firefighters who have collected a service pension and are returning to active service is lowered from ten years to three years.

The legislation is effective upon local approval.

Background Information

The Eden Prairie VFRA is a defined benefit relief association that provides both a lump-sum service pension and a monthly benefit service pension. The proposed legislation's increase in the maximum lump-sum service pension amount is intended to incentivize Eden Prairie VFRA members to choose a lump sum over a monthly benefit service pension upon retirement. Minn. Stat. § 424A.02, subd. 3, para. (d), sets the applicable maximum lump-sum service pension amount a relief association is able to provide for its members per year of service based on the minimum average amount of available financing per firefighter. The lump-sum amount set by the relief association's bylaws at the time a firefighter retires, is the amount applied to every year of service the firefighter is credited for. The highest lump-sum amount a relief association is able to offer per year of service is currently set at \$10,000 as long as the relief association has an average of at least \$5,397 of available financing per active firefighter. As of 2015, the Eden Prairie VFRA had an average available financing per firefighter of \$10,512, almost double the required amount, and was therefore eligible to, and did, provide the \$10,000 lump-sum maximum.

The proposed legislation does not increase the maximum amount that Eden Prairie VFRA may provide for monthly benefit service pensions. The Eden Prairie VFRA has not increased its monthly benefit maximum of \$56 per month since 2009, despite having enough financing per firefighter to provide the highest maximum of \$100 per month (Minn. Stat. § 424A.02, subd. 3, para. (c)). Lump-sum service pensions are easier to administer than monthly benefit service pensions, so the Eden Prairie VFRA believes that increasing the lump-sum maximum amount will lead to more members choosing the lump-sum service pension option upon retirement. The Eden Prairie City Council passed a resolution on January 20, 2015, stating its support for any legislation that would increase the lump-sum maximum amount.

The proposed legislation is also intended to address current recruitment and retention problems related to vesting. Under Minn. Stat. § 424A.02, subd. 2, defined benefit relief association members are required to complete 20 years of active service to be eligible to receive a full service pension. A majority of these relief associations provide partial vesting, which means a member with less than 20 years of service is only eligible for a service pension that has been reduced by a certain percentage. Each relief association's bylaws defines the requirements to be partially vested, with about half requiring at least five years of service and the other half requiring ten years. The Eden Prairie VFRA is the only defined benefit relief association that provides fully-vested service pensions after a member has completed ten years of active service, which is authorized by special legislation (Laws 1995, Ch. 262, Art. 10, Sec. 5). Therefore, members are not eligible to receive any portion of a service pension until they have completed ten years, after which they are eligible to receive the full service pension.

Also, under Minn. Stat. § 424A.01, subd. 6, firefighters returning to active service after taking a service pension may become eligible for a second service pension if the relief association's vesting requirements are satisfied. This provision therefore requires that the returning members of nearly all relief associations must provide either five or ten years to be eligible for a partially vested service pension. Returning members of the Eden Prairie VFRA must provide another ten years to be eligible for a fully vested service pension and are not eligible for a partially vested service pension. This additional ten-year service requirement has created a disincentive for EDEN PRAIRIE VFRA members to return to active service. Eden Prairie VFRA's vesting requirements have provided an incentive for firefighters to retire after ten years of service and to remain inactive after retirement, which has resulted in retention problems for the fire department.

Policy Considerations

Bill draft LCPR16-025 raises the following pension and public policy issues:

1. Cost. Increasing the maximum lump-sum service pension from \$10,000 to \$15,000 provides a service pension increase as well a cost to the relief association. Members with ten years of service at the time of retirement will see a \$50,000 increase in their service pensions if the maximum limit is increased. An additional \$5,000 per year of service could provide an incentive for EP firefighters to serve more than ten years. In order to provide a \$15,000 maximum, the Eden Prairie VFRA must have an average available financing per firefighter of at least \$8,097. As of 2015, the Eden Prairie VFRA had an average available financing per firefighter of \$10,512, which is above the requirement to provide a \$15,000 maximum.

2. Special Law versus General Application. The proposed legislation only affects the Eden Prairie VFRA and would not apply to the other relief associations in the state. Currently, all relief associations must comply with the \$10,000 lump-sum service pension amount maximums set in statute. Very few relief associations are able to offer the \$10,000 maximum. In the most recent relief association financial data report from the Office of the State Auditor, only nine relief associations offered lump-sum amounts above \$7,000. If the lump-sum maximum was increased on a statewide level, very few relief associations would be impacted by the change. However, there are a few relief associations offering the \$10,000 maximum, or getting close, that may be also be interested in an increased maximum. Only increasing Eden Prairie VFRA's maximum amount could result in other relief associations coming to the Commission with special legislation to increase their maximum amounts. Increasing the maximum does not mean that a relief association will be able to provide that amount. The relief association must still satisfy the applicable average financing per firefighter amount in order to legally offer a higher amount.

As discussed above, the Eden Prairie VFRA has a unique vesting requirement that has created recruitment and retention problems. Although other relief associations in the state have recruitment and retention problems, they are not experiencing the same problem of large numbers of members retiring when they complete ten years of service. Other relief associations provide an incentive for their members to stay a full 20 years. The proposed legislation provides a potential solution to Eden Prairie VFRA's distinctive problem that may cause issues if it were adopted on a statewide level.

VFRAs must annually calculate their total accrued liability to determine the financial status and requirements of the relief association's special fund. Because the Eden Prairie VFRA provides both lump-sum and monthly benefit service pensions, they are statutorily required to have an actuarial valuation performed to determine the relief association's liabilities and minimum financial requirements. An actuary can ensure that the valuation includes liability projections for firefighters returning to service. However, the other 535 lump-sum only relief associations must determine their liabilities using the table in Minn. Stat. § 424A.092, subd. 2, which is basically a present value table assuming a lump-sum benefit payable immediately after 20 years of service. So, paying members a fully vested service pension before completing 20 years of service will result in an unfunded liability. Municipalities would be required to contribute more money to their affiliated relief associations to cover those unfunded liabilities under Minn. Stat. § 424A.092, subd. 3. Here is an example:

The accrued liability for a member with three years of service at a \$1,800 benefit level is \$3,420. If the member is paid the full pension for three years of service, as is proposed in the bill, the pension distribution would be \$5,400, which is \$1,980 more than what has been pre-funded. The impact will be more significant if a number of members in the same relief association take the option around the same time or if the relief association has a small pool of assets.

3. Appropriateness of Proposed Legislation. Reducing the vesting requirement and increasing the lump-sum service pension maximums are attempts by the Eden Prairie VFRA to mitigate certain issues. No relief association has a vesting period shorter than five years. Introducing a three year vesting requirement would set a new precedent that could result in other VFRAs seeking special legislation to lower their vesting requirements for firefighters returning to active service. Implementing partial vesting as well as increasing the service requirement for full vesting to 15 or 20 years are other options the Eden Prairie VFRA could utilize to try and solve the recruitment and

retention issues. However, increasing the vesting period could backfire and result in even more retention problems.

4. Local Approval. The proposed legislation requires the City Council of Eden Prairie and its chief clerical officer to approve the legislation before it can become effective. The City Council supported the Eden Prairie VFRA's legislative efforts to increase the maximum lump-sum service pension amount in a resolution dated January 20, 2015. The City Council has also supported the vesting requirement change for retired firefighters returning to service in a letter from February 2016. The higher lump-sum amount and new vesting requirement must also be approved by the Eden Prairie VFRA membership in order for the bylaws to be amended to reflect the changes. Eden Prairie VFRA members requested the proposed legislation, indicating their support for the changes.