



H.F. 3895
(Murphy, M.)

S.F. 3630
(Saxhaug)

Executive Summary of Commission Staff Materials

Affected Pension Plan(s): Volunteer Firefighters
Relevant Provisions of Law: Minnesota Statutes, Chapters 69, 356, 356A, 356B, and 424C
General Nature of Proposal: Establishes voluntary statewide lump sum volunteer firefighter retirement plan
Date of Summary: March 27, 2008

Specific Proposed Changes

The bill creates a voluntary statewide lump sum volunteer firefighter retirement plan governed by a board primarily drawn from firefighters and municipal officials, administered by the Minnesota State Retirement System (MSRS), invested by the State Board of Investment, providing lump sum service pensions based on the fire department call level and fire state aid amounts, up to an overall maximum of \$4,000 per year of service credit, funded from transferred relief association assets, fire state aid, and prescribed municipal contribution amounts based on the service pension level and with an initial State General Fund appropriation.

Policy Issues Raised by the Proposed Legislation

- a. Attractiveness of a statewide retirement plan, reception by volunteer fire community.
- b. Appropriateness of restriction of statewide plan to lump sum volunteer plan.
- c. Appropriateness of MSRS administration.
- d. Appropriateness of crediting service based on "good time" service determinations by local fire chiefs.
- e. Appropriateness of representatives on statewide volunteer firefighter retirement plan board.
- f. Appropriateness of basing service pensions on fire calls and fire state aid levels.
- g. Appropriateness of municipal option to approve higher lump sum service pension level.
- h. Appropriateness of retaining current long vesting requirement.
- i. Adequacy of the funding of the statewide volunteer firefighter retirement plan.
- j. Appropriateness of the State General Fund appropriation and initial plan expenditures.

Potential Technical Amendments

An inconsistency in specified interest rates governing actuarial work and amortization contributions needs to be resolved at either 5.0 percent (**Amendment H3895-1A**) or at 8.5 percent (**Amendment H3895-2A**).



TO: Members of the Legislative Commission on Pensions and Retirement
FROM: Lawrence A. Martin, Executive Director *JAM*
RE: H.F. 3895 (Murphy, M.); S.F. 3630 (Saxhaug): Volunteer Firefighters; Statewide Lump Sum Volunteer Firefighter Retirement Plan
DATE: March 17, 2008

General Summary of H.F. 3895 (Murphy, M.); S.F. 3630 (Saxhaug)

H.F. 3895 (Murphy, M.); S.F. 3630 (Saxhaug) creates a new statutory chapter, Minnesota Statutes, Chapter 424C, and amends various portions of Minnesota Statutes, Chapters 69, 356, 356A, and 356B, to create a statewide lump sum voluntary volunteer firefighter retirement plan and to make conforming changes, as follows:

1. Coverage/Application (Article 1, Section 3). The statewide lump sum volunteer firefighter retirement plan would be open to any municipal fire department or nonprofit firefighting corporation that currently has a volunteer firefighter relief association providing a lump sum service pension or a defined contribution service pension or any firetown that has a fire department without an existing volunteer firefighter relief association. Coverage by the plan is elective with the agreement of the municipality and with the volunteer firefighter relief association, if any. The question of coverage by the statewide retirement plan can be raised either by the firefighters or by the municipality.
2. Governance (Article 1, Section 5). The voluntary statewide lump sum volunteer firefighter retirement plan would be governed by a seven-person board, with four firefighter representatives and three public sector/general public representatives. The firefighter members would be drawn from very small, small, medium, and large municipalities. The public sector/general public members would be from the League of Minnesota Cities, the Minnesota Association of Townships, and from the general public. All board members would be appointed by the governor. Board member terms would be for three years and would be staggered.
3. Plan Administration (Article 1, Section 5, Subdivision 1). The statewide plan would be administered by the executive director of the Minnesota State Retirement System (MSRS).
4. Fund and Investment (Article 1, Sections 6 and 7). The statewide lump sum volunteer firefighter retirement fund is a special dedicated retirement fund in the State Treasury. The statewide fund is invested by the State Board of Investment in the Combined Investment Funds, the investment vehicle for the various statewide retirement funds.
5. Service Credit (Article 1, Section 2, Subdivision 19). Past service credit in a volunteer firefighter relief association associated with a municipality or nonprofit firefighting corporation electing retirement coverage by the statewide retirement plan is transferred to the retirement plan. Future service is creditable on an annual or fractional (monthly) basis based on "good time" certification by the applicable fire department.
6. Benefit Levels (Article 1, Section 8). The retirement plan would provide one of 49 service pension levels, from a minimum of \$20,000 at 20 years, to a maximum of \$80,000 at 20 years, set based on the relative scoring level (to be developed) of the applicable municipality and fire department with one-half of the total service pension derived from seven levels associated with the fire state aid amount and one-half of the total service pension derived from seven levels associated with the average total call volume as reported on the Minnesota Fire Information Reporting System annual report. For fire departments closely approaching the fire calls and fire state aid levels for a higher benefit level, the applicable municipality is permitted to elect the higher level by filing a municipal resolution to that effect, thereby also incurring a higher municipal funding obligation for the higher benefit level. Other benefits (disability and survivorship) would be available if no service pension is payable and is in an amount equal to the accrued service pension. A service pension would be payable at age 50, unless the municipality set an older age, if the volunteer firefighter rendered at least five years of service covered by the plan and the vesting requirement would be set at five years of service, with a partial benefit, scaling up to a full non-forfeitable benefit at 20 years of service. A volunteer firefighter who

terminated active service before age 50 or the later age retirement age and with at least five years of active service would qualify for a deferred service pension, but without any interest or augmentation payable on the deferred service pension.

7. Relief Association Asset Transfer (Article 1, Section 4). Upon electing coverage by the statewide volunteer firefighter retirement plan, the assets of the special fund of the applicable volunteer firefighter relief association would be transferred to the statewide retirement fund after any accounts payable were resolved. If the transferred assets include investment securities that are impermissible or inappropriate for the State Board of Investment in the judgment of the executive director of the State Board of Investment, the executive director will liquidate the problematic investments immediately.
8. Funding (Article 1, Section 11). The statewide retirement plan is to be funded from fire state aid, regular municipal contributions, and additional municipal contributions. Fire state aid would be transmitted to the statewide fund directly rather than to the applicable municipality. The regular annual municipal contribution would be based on the applicable service pension level and set at \$200 per firefighter at the \$20,000 service pension amount, \$300 per firefighter at the \$30,000 service pension amount, \$400 per firefighter at the \$40,000 service pension amount, \$500 per firefighter at the \$50,000 service pension amount, \$600 per firefighter at the \$60,000 service pension amount, \$700 per firefighter at the \$70,000 service pension amount, and \$800 per firefighter at the \$80,000 service pension amount. If the transferred special fund assets are less than the actuarially calculated liability at the service pension level for a fire department electing plan coverage and the past service credit also transferred, the applicable municipality would be required to amortize the shortfall over five years on a level dollar amortization basis through the payment of an additional municipal contribution.
9. Impact on Volunteer Firefighter Relief Association (Article 1, Section 4). Upon the transfer of retirement coverage to the statewide volunteer firefighter retirement plan and the transfer of relief association special fund assets to the statewide retirement fund, the special fund of the applicable volunteer firefighter relief association is disestablished. A volunteer firefighter relief association following a transfer of retirement coverage could continue as a fraternal organization in the form of its prior general (non-pension) fund.
10. Plan Start-Up Costs (Article 1, Section 12). An unspecified appropriation is made to MSRS to cover the start-up costs of the new statewide retirement plan.
11. Conforming Changes (Article 2). The municipalities with firefighters covered by the statewide lump sum volunteer firefighter retirement plan would continue to be eligible to receive fire state aid (Article 2, Sections 1 through 7). The statewide lump sum volunteer firefighter retirement plan is required to prepare annual financial and actuarial reporting (Article 2, Sections 8 through 11). The statewide lump sum volunteer firefighter retirement plan is also to be covered by the general exemption from legal process statute (Article 2, Section 12), is included in the Public Pension Plan Fiduciary Responsibility Laws (Article 2, Section 13), and is required to make an early submission of administrative legislation (Article 2, Section 14).

Background Material

- **Attachment A** provides information on the number, the size, the financial health, and the benefit practices of the state's volunteer firefighter relief associations over the period 1974-2005.
- **Attachment B** gives a graphic presentation of the distribution of municipalities by population.

Technical/Clarification Amendment

- **Amendment H3895-1A** makes the interest rate used to determine the additional municipal contribution to amortize an unfunded actuarial accrued liability under Article 1, Section 11, Subdivision 6, consistent with the actuarial valuation interest rate assumption, setting the interest rate at five percent.
- **Amendment H3895-2A** addresses the same inconsistency as Amendment H3895-1A, but sets the interest rate at 8.5 percent.

Discussion and Analysis

H.F. 3895 (Murphy, M.); S.F. 3630 (Saxhaug) establishes and voluntary lump sum statewide volunteer firefighter retirement plan as an alternative to or replacement for local relief associations, to be governed

by a board appointed by the governor, to be administered by the executive director of the Minnesota State Retirement System (MSRS), and to provide a lump sum benefit based in part on the number of fire department fire calls and in part on the amount of fire state aid received.

The proposed legislation raises several pension and related public policy issues for Commission consideration and potential discussion, as follows:

1. Attractiveness; Reception by the Volunteer Fire Community. The policy issue is the attractiveness of a statewide lump sum volunteer firefighter retirement plan to the volunteer fire community and the reception that the plan is likely to have. Minnesota historically has utilized a decentralized public pension arrangement, especially for public safety employee retirement coverage. There are currently about 700 volunteer firefighter relief associations in the state, with most plans providing lump sum service pensions. If there is not substantial interest in the volunteer fire community in replacing their local relief associations with the statewide retirement plan, the legislative effort consumed in enacting it and the administrative effort expended in establishing it may be substantially in vain. A statewide plan has the potential of greater investment efficiencies, has the potential for administrative economics of scale, will utilize a greater risk pool for funding eventual retirement benefits, and will provide pension portability for firefighters who may move from place to place across the state. The statewide plan notion also has engendered some controversy among firefighters in the past and may be viewed by some portion of the volunteer fire community as a threat. The Commission may wish to take testimony from representatives of the volunteer fire community about its likely reception statewide.
2. Appropriateness of Restricting the Statewide Plan to Lump Sum Relief Associations Only. The policy issue is the appropriateness of the restriction of the proposed voluntary statewide volunteer firefighter retirement plan to the provision of lump sum service pensions and retirement benefits only. That excludes the five current volunteer firefighter relief associations that provide only monthly service pensions and excludes most or all combination (alternative lump sum or monthly service pension) volunteer firefighter relief associations. It also would likely eliminate from potential coverage the 86 volunteer firefighter relief associations that provide defined contribution service pensions, paid in a lump sum, but determined based solely on account balances. If the desirability from a policy standpoint of a statewide retirement plan lies in the large risk pool economics of scale and efficiencies that come with a statewide plan, those economics of scale and efficiencies also could benefit the members of monthly benefit, combination, and defined contribution volunteer firefighter relief associations. If there is a long-term goal with respect to monthly benefit, combination, and defined contribution relief associations on the part of the proponents of the statewide volunteer firefighter retirement plan, it may be helpful to the Commission if those plans were revealed. If there are no plans to ever include other volunteer firefighter relief association types in potential coverage by the statewide volunteer firefighter retirement plan, it would be appropriate to request from the proponents their thoughts about what improvements in the investment and administrative practices of monthly, combination, and defined contribution volunteer firefighter relief associations should be mandated or encouraged to make those relief associations function better.
3. Appropriateness of the Administration of the Statewide Plan by MSRS. The policy issue is the appropriateness of assigning the responsibility of performing the administrative duties related to the proposed statewide volunteer firefighter retirement plan to the executive director of the Minnesota State Retirement System (MSRS). Of the three statewide retirement plan administrations, MSRS has the smallest staff and has the widest variety of assignments, performing the administrative functions for nine retirement plans and two retirement-oriented savings programs:
 1. General State Employees Retirement Plan of the Minnesota State Retirement System (MSRS-General);
 2. Correctional Employees Retirement Plan of the Minnesota State Retirement System (MSRS-Correctional);
 3. State Patrol Retirement Plan;
 4. Legislators Retirement Plan;
 5. Elective State Officers Retirement Plan;
 6. Judges Retirement Plan;
 7. Transportation Department Pilots Retirement Plan;
 8. Military Affairs Department Retirement Plan;
 9. Fire Marshal/Arson Investigators Retirement Plan,
 10. the Minnesota Deferred Compensation Program; and
 11. the Health Care Savings Program.

Aside from tangential connections to local government through the Minnesota Deferred Compensation Program and the Health Care Savings Program, MSRS has no significant level of contact with local government and no direct contact with the volunteer fire community. Some testimony from the proponents of the proposed legislation and from MSRS should be considered about how these administrative duties will be fulfilled and at what level of cost.

4. Appropriateness of Crediting Firefighting Service Based on “Good Time” Service; Role of Fire Department Chiefs. The policy issue is the appropriateness of basing service credit for firefighters covered by the statewide retirement plan on undefined “good time” as certified by the fire chief of the fire department. “Good time” is not a statutory term of art, but apparently is a recognized concept in the fire service. The certification of “good time,” under Article 1, Section 2, Subdivision 19, is to be based on the requirements of the fire department, but the person or entity in or associated with the fire department setting those requirements is not specified and is not clear. For municipal fire departments, it is not clear whether or not the municipal governing body has any role in setting “good time” requirements. For fire departments that are not associated with one municipality, the body empowered to set the requirements is unclear. The “good time” certifications would be required at least monthly, since service credit is contemplated to be recorded monthly, but the reporting requirements that fire departments and fire chiefs would have to adhere to in certifying “good time” are not specified. The extent of judgment to be employed by the fire chief and the extent to which a fire chief could substitute the chief’s opinion for other methods of documenting service is an open question. When benefits are to be determined for an individual and a retiring firefighter disputes the service credit record, the manner in which the dispute and any appeal are to be resolved is unanswered. If the proponents have a clear vision of how fire chiefs and fire departments are to report to and interact with MSRS in determining service credit, it would be valuable to develop statutory language that captures those notions.
5. Appropriateness of the Representation on the Statewide Volunteer Firefighter Retirement Plan. The policy issue is the appropriateness of the composition, selection, and representation of the board of the proposed statewide volunteer firefighter retirement plan. The plan’s governing board includes a majority of firefighters, two municipal government representatives, and one public member with pension experience. The firefighter members represent firetowns under 5,000 in population, between 5,000 and 9,000 in population, between 9,000 and 20,000 in population, and over 20,000 in population. The municipal government representatives are to be selected from a group of three candidates each nominated by the League of Minnesota Cities and by the Minnesota Association of Townships. All board members are to be appointed to staggered terms by the governor. The firetown categories represented by firefighters may not be a good match for the actual distribution of small, medium, large, and very large firetowns. Although township and city data is not an exact replication of the size of firetowns, municipal data does suggest the general nature of the distribution of firetowns by population size. Of the 3,315 townships and cities in the state, 93.7 percent are under 5,000 in population, 2.3 percent are between 5,000 and 9,000 in population, 2.2 percent are between 9,000 and 20,000 in population, and 1.8 percent are over 20,000 in population. The representation in the proposed legislation thus would provide three firefighter representatives drawn from only 6.3 percent of the state’s municipalities. There is no requirement that firefighters on the board be members of the statewide plan. The attached map, Attachment B, gives a graphic presentation of the distribution of municipalities by population. No guidance is provided to the League of Minnesota Cities or the Association of Minnesota Townships about what qualifications should be emphasized in their selection of candidates. The criteria of “knowledgeable in pension matters” for the one public member of the board is very vague. Board service, which is uncompensated and which does not qualify for expense reimbursement or per diem allowance, will likely discourage potential board members who do not reside in the Twin City metropolitan area.
6. Appropriateness of Basing Service Pension Levels on Fire Call Levels and Fire State Aid Levels. The policy issue is the appropriateness of directly connecting service pension levels for the proposed voluntary lump sum statewide volunteer firefighter retirement plan to a fire department’s call level and to a firetown’s fire state aid level. According to the Commission’s Principles of Pension Policy, Minnesota public pension plans exist to assist in the recruitment, retention, and systematic periodic outtransitioning of personnel. Basing service pension levels on the performance level of the fire department and on the relative affordability of pension coverage as measured by fire state aid could assist in recruitment, retention, and outtransitions, but are not necessarily well designed to do so. The relative number of fire department calls will be greatly affected by whether or not the fire department provides emergency medical and related services as well as fire suppression services and will likely greatly influence the size of the fire department, but does not appear to account well for localized factors affecting recruitment patterns, such as the age distribution of the population of the firetown or

the competition for volunteers from other activities. Fire state aid is a very rough measure of fire service needs, as measured by total population of the firetown and by the value of the property protected in the firetown, but does not correct for other relevant factors, such as average building age, building material, extent of fire alarm and fire sprinkler utilization, and distribution of commercial and residential structures. While hardly optimal, the current flexible service pension maximums applicable to local volunteer firefighter relief associations can better adjust for localized needs than the proposed two-part benefit level determination by including local municipal contribution levels as a factor in setting the service pension amount, allowing firetowns with significant volunteer firefighter needs but modest fire state aid to produce larger firefighter service pension levels through the provision of additional municipal contributions. The proposed plan does not provide any comparable mechanism for localities with firefighting recruitment, retention, or outtransitioning problems amenable to solution through higher pension levels. Fire department calls are not specifically defined beyond the definition of the Minnesota Fire Information Report, which is an annual document filed with the State Fire Marshal. Some testimony may be necessary to ascertain whether or not the fire department call numbers can be manipulated.

7. Need to Specify the Fire Call and Fire State Aid Particulars of the Service Pension Formula. The policy issue is the need to supply the specific fire department call and fire state aid numbers for each service pension level. From the proposed legislation as currently constituted, the smallest service pension amount would be \$1,000 per year of service with the least number of fire department calls and the smallest amount of fire state aid, and the largest service pension amount would be \$4,000 per year of service with the greatest number of fire department calls and the largest amount of fire state aid, with 47 service pension levels in between the smallest and highest service pension amounts depending on the fire call and fire state aid break points ultimately utilized. The break points are apparently being developed by some other source. The benefit levels cannot be analyzed as to the appropriateness of their fit beyond the minimum and maximum service pension levels until those break points are developed.
8. Appropriateness of a Municipal Opt-Up for a Higher Lump Sum Service Pension Level for "On-the-Cusp" Firetowns. The policy issue is the appropriateness of a built-in deviation from the service pension level break point schedule for municipalities that are very close to the next highest service pension level. Article 1, Section 8, Subdivision 2, Paragraph (a), permits a municipality to elect to go to the next highest service pension level if the municipality has fire calls or fire state aid that is at least 85 percent of the next highest break point amount. The opt-up election potentially would require an additional \$100 per year per firefighter municipal contribution. The opt-up election presumably is in effect for one year at a time because the fire call and fire state aid amounts driving the amount of the service pension to be provided are recalculated annually before each April 1. It is unclear what factors compelled the proponents of the proposed legislation to add this opt-up provision to the bill.
9. Appropriateness of Continuing Long Vesting Period Before 100 Percent Accrued Service Pension is Payable. The policy issue is the appropriateness of the retention of a feature of the volunteer firefighter relief association benefit provisions, the vesting schedule, that only provides the full service pension amount with 20 years of service credit. The lengthy vesting schedule, providing 40 percent of the accrued benefit with five years of service credit and scaling up four percent per year until reaching 100 percent at 20 years, promotes the retention of firefighters once they have five years of service, but may discourage recruitment of new firefighters because of the lengthy commitment of time needed to obtain the full benefit. For defined contribution volunteer firefighter relief associations, a shorter vesting period is in place, at the request of representatives of those relief associations. The creation of a new pension plan provides an opportunity to reconsider whether or not very long vesting periods are still beneficial.
10. Adequacy of the Funding of the Statewide Volunteer Firefighter Retirement Plan. The policy issue is whether the funding provided for the statewide volunteer firefighter retirement plan will be sufficient to cover the actuarial liability of the benefits specified for the plan. The funding of the plan is the transferred assets of current volunteer firefighter relief associations that join the statewide plan, the fire state aid payable to the firetowns covered by the statewide plan, regular municipal contributions of between \$200 per firefighter and \$800 per firefighter annually, and additional municipal contributions by municipalities associated with relief associations transferring insufficient asset amounts upon joining the statewide plan, with a five-year amortization period based on an 8.5 percent interest rate assumption. Until the service pension determination formula is fully established and until some municipalities elect to be covered by the statewide plan, it is difficult to specifically assess the likely liability of the statewide plan and hence difficult to assess the adequacy of the proposed funding. However, the Commission staff has made some assessment of the proportion of potential

