Request for City Council Committee Action from the Department of Finance

Date: Tuesday, July 24, 2007
To: Council Member Betsy Hodges, Chair
Referral to: Intergovernmental Relations Committee

Subject: Local Approval Requirements; MFRA State Pension Legislation

Act on local approval clause related to changes to benefits for the Minneapolis Fire Relief Association (MFRA) enacted as part of state omnibus pension legislation (*Laws of Minnesota* 2007, Chapter 134, Article 9, Section 2).

Recommendation:

- Do not approve legislation increasing the MFRA's supplemental retirement benefits by up to one half of excess investment income.

Previous Directives:

Prepared by: June Mathiowetz, 612-673-2027
Approved by: Patrick Born, Chief Financial Officer ______________________________
Steven Bosacker, City Coordinator ______________________________
Presenters in Committee: Patrick Born, Chief Financial Officer
Heather Johnston, Director, Management and Budget

Reviews

- Permanent Review Committee (PRC): Approval ___ Date ________________
- Policy Review Group (PRG): Approval ___ Date ________________

Financial Impact

- Other financial impact

Supporting Information

Increase in MFRA Retirement Benefits by One Half of Excess Investment Income

This legislation, passed as part of the omnibus pension bill during the 2007 legislative session, contains a local approval clause. If it receives local approval, the result will be an increase in postretirement benefit payments (or what is commonly called "13th checks") to MFRA retirees and beneficiaries by up to an additional one half of excess investment income. There will also be an equivalent decrease in MFRA assets. This legislation is not retroactive.

Excess investment income is the amount, if any, by which the average time weighted total rate of return earned by the fund in the most recent prior five fiscal years, has exceeded the actual average percentage increase in the current salary of a top grade firefighter in the most recent prior five fiscal years plus two percent **or 1% of assets**, whichever is lower. The following section from the MFRA's 12/31/06 Actuarial Report depicts how excess investment income is calculated:

Excess Investment Income Determination Calculation

1. Salary increases and time-weighted rate of return on assets

Fiscal Year	Salary Increase	Asset Return	Market Value of Assets
2002	3.491%	-9.650%	$226,580,976
2003	1.887%	20.000%	$250,352,620
2004	6.296%	10.047%	$255,076,595
2005	1.524%	5.890%	$253,180,944
2006	2.576%	12.460%	$263,951,959
Average of past 5 years:	**3.155%**	**7.749%**	

2. Determination of excess investment income

a. Arithmetic average of previous 5 years salary increases	3.155%
b. Arithmetic average of previous 5 years of asset returns	7.749%
c. Excess of asset return over salary increase	4.594%
d. Excess minus 2%	2.594%
e. Excess investment income-minimum of 1% or 2.d., x market value	$2,639,520
f. Post-retirement benefit - minimum of 0.5% or 2.d., x market value	**$1,319,760**

Under current law, MFRA can distribute one half of excess investment income of the fund – if there is any – to the payment of annual postretirement benefit payments to members. The MFRA recently provided a determination notice indicating that all members are eligible to receive a postretirement benefit on June 1, 2007. With excess investment income totaling $2.6 million on 12/31/06, MFRA can distribute half of this amount ($1.3 million). Retirees with forty-three units[1] are scheduled to receive a check worth $2,586 (estimate provided by MFRA).

Current law also states that the second half of excess investment income is to be applied to reduce state basic and supplemental amortization aids otherwise due to the MFRA. Procedurally, this means that before the state sends the appropriate amortization aids to MFRA it subtracts half of the fund's excess investment income. In 1998, however, MFRA achieved full funding for the first time making it permanently ineligible under state law to receive any further state basic and supplemental amortization aids.

MFRA's testimony at the legislature indicated that if this legislation had been in place this year, the additional average increase per member with forty-three units would have resulted in an additional $900 per member, approximately. This would have resulted in total additional

[1]As of 1/1/06, the benefits calculation for retirees with at least twenty-five years of service is based on forty-three units.

postretirement benefits for each individual in this group of approximately $3,500 in 2007. (Payments to each eligible member are capped to an amount equal to the total monthly benefits that the member was entitled to in the prior year or each member's proportionate share of the excess investment income, whichever is less.)

Increasing benefits when the MFRA fund is not fully funded is not consistent with the Council's adopted policies on pension issues. On 12/31/06, the MFRA was 87.5% funded. Every time supplemental payments are made to members before the plan is fully funded, it takes away from future investment earnings; shortfalls in investment earnings are then required to be made up by payments from City taxpayers.

As of 12/31/06, the MFRA had 31 active members, 374 retirees and 218 beneficiaries. The average annual benefit for a MFRA retiree for 2006 was $41,100. The chart below summarizes the additional postretirement benefit amounts that have been distributed to retirees and beneficiaries in recent years, City contributions during those years and the funding levels.

MFRA Historical Post Retirement Benefits, City Contributions and Funding Ratios

Year	Average Annual Benefit Amount Per Person	Average PRB Amounts Per Person	Average Annual Benefit and PRB Amount	City Levy Contributions	Percent Funded on December 31st	
1993	$24,088	$1,777	$25,865	$7,006,477	79%	
1994	$27,252	$1,836	$29,088	$6,265,048	78%	
1995	$27,252	-	$27,252	$5,604,274	83%	
1996	$27,252	$2,127	$29,379	$5,636,100	83%	
1997	$29,105	$2,253	$31,358	$3,675,000	90%	
1998	$31,265	$2,637	$33,902	$4,312,500	**105%**	←Fully Funded
1999	$32,712	$9,196	$41,908	$3,175,000	**109%**	←Fully Funded
2000	$34,242	$10,195	$44,437	$1,147,000	**108%**	←Fully Funded
2001	$35,494	$8,698	$44,192	$310,000	**104%**	←Fully Funded
2002	$36,797	$7,612	$44,409	$0	87%	
2003	$36,797	$0	$36,797	$0	81%	
2004	$38,074	$0	$38,074	$0	90%	
2005	$40,626	$0	$40,626	$4,737,705	86%	
2006	$41,100	$0	$41,100	$1,385,000	88%	
2007	tbd	$2586*	tbd	$3,086,000	tbd	

NOTES:
The 2005 amount listed under City Levy Contributions is bonds issued in lieu of levy.
MFRA is the source of the "per person" amounts listed.

* This amount is for retirees with forty-three units only; average across all members was not available.

Proposed Resolution

Of the

City of Minneapolis

By Hodges

Opposing Law of Minnesota 2007 Legislative Session; Chapter 134, Article 9, Section 2.

Whereas, the Minnesota State Legislature has passed legislation relating to the Minneapolis Fire Relief Association doubling the excess investment income amount available for distribution to members in the form of postretirement benefit increase checks; and

Whereas, the City of Minneapolis has shown its commitment to meeting its obligations to retirees by fully funding all contributions to these funds as required by statute; and

Whereas, the MFRA is currently only 88% funded; and

Whereas supplemental excess investment income checks are being issued to retirees at the same time the City is levying $3.1 million for MFRA; and

Whereas, MFRA's members have received ten distributions of excess investment distribution checks since 1992 in average annual amounts ranging from $1,800 to over $10,000 per member; and

Whereas, on June 1, 2007 postretirement benefit checks for retirees with forty-three units were estimated at $2,586; and

Whereas, in the future event of a market down turn, the taxpayers of the City of Minneapolis will bear the full responsibility for any liabilities created by increases to short-term payouts to members; and

Whereas, the City maintains its position that the most appropriate use of these taxpayer dollars would accelerate MFRA's return to full funding; and

Whereas, said legislation, by its terms requires an affirmative vote of a majority of the members of the City Council by the first day of the next regular session of the legislature before it may become effective; and

Now, therefore, Be It Resolved by the City Council of Minneapolis:

That the Council not approve said legislation.

CHAPTER 134
ARTICLE 9
MINNEAPOLIS POLICE AND FIREFIGHTERS
RELIEF ASSOCIATIONS CHANGES

Sec. 2. Minnesota Statutes 2006, section 423C.06, subdivision 2, is amended to read:

Subd. 2. **Actuarial assets of special fund less than 102 percent.** (a) When the actuarial assets of the special fund in any year are less than 102 percent of its accrued liabilities according to the most recent annual actuarial valuation of the special fund prepared in accordance with sections 356.215 and 356.216, investment-related postretirement adjustments shall be determined and paid pursuant to this subdivision. Payment of the annual postretirement adjustment may be made only if there is excess investment income.

(b) The board shall determine by May 1 of each year whether or not the special fund has excess investment income. The amount of excess investment income, if any, must be stated as a dollar amount and reported by the executive secretary to the mayor and governing body of the city, the state auditor, the commissioner of finance, and the executive director of the Legislative Commission on Pensions and Retirement. The dollar amount of excess investment income up to one percent of the assets of the special fund must be applied for the purpose specified in paragraph (c). Excess investment income must not be considered as income to or assets of the special fund for actuarial valuations of the special fund for that year under this section and sections 69.77, 356.215, and 356.216 , except to offset the annual postretirement adjustment. Additional investment income is any realized or unrealized investment income other than the excess investment income and must be included in the actuarial valuations performed under this section and sections 69.77, 356.215, and 356.216.

(c) The amount determined under paragraph (b) must be applied as follows: the association shall apply ~~the first one-half of~~ one percent of assets that constitute excess investment income to the payment of an annual postretirement adjustment to eligible members ~~and the second one-half of one percent of assets which constitute excess investment income shall be applied to reduce the state amortization state aid or supplementary amortization state aid payments otherwise due the association under section 423A.02 for the current calendar year~~. The amounts of all payments to eligible members shall not exceed ~~one-half of~~ one percent of the assets of the fund. The amount of each eligible member's postretirement adjustment shall be calculated by dividing the total number of units to which eligible members are entitled into the excess investment income available for distribution to eligible members, and then multiplying that result by the number of units to which each eligible member is entitled. If this amount exceeds the total monthly benefit that the eligible member was entitled to in the prior year under the terms of this chapter, the association shall pay the eligible member the lesser amount. Payment of the annual postretirement adjustment must be in a lump-sum amount on June 1 following the determination date in any year. In the event an eligible member dies prior to the payment of the annual postretirement adjustment, the executive secretary shall pay the eligible member's estate the amount to which the member was entitled.

EFFECTIVE DATE; LOCAL APPROVAL. This section is effective the day after the city council of the city of Minneapolis and its chief clerical officer timely complete their compliance with section 645.021, subdivisions 2 and 3.