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Statement of Position
Interest Earnings for Deferred Members of Volunteer Fire Relief Associations

About half of the volunteer fire relief associations in Minnesota have adopted bylaw provisions that allow interest or investment earnings to be credited to deferred members during the period of deferral.[1] Administering interest during periods of deferral can be complicated. Deferred service pensions must be calculated based on both state law and relief association bylaw provisions in effect on the date that each member separated from active service and membership. Deferred members of the same volunteer fire relief association could have interest that is calculated differently depending on when they separated from service.

Volunteer fire relief associations that elect in their bylaws to pay interest to deferred members must make three decisions: 1) the interest type; 2) the interest payment method; and 3) membership eligibility.

Interest Type

Minnesota Statutes provide various options for how interest will be paid, *i.e.*, the "interest type." The types of interest available for use by volunteer fire relief associations are 1) setting up a separate investment account; 2) setting up a separate investment vehicle; 3) allowing the board to set interest up to five percent, compounded annually; and 4) crediting full investment gains and losses.

1. Setting up a Separate Investment Account: Under this option, the volunteer fire relief association establishes a separate investment account for the amount payable to deferred members. The account is maintained separately from the other assets of the relief association, but is still governed by the relief association board of trustees and is still reported as an association asset. A member's deferred benefit amount is transferred to the separate investment account when the member separates from active service and membership. The volunteer fire relief association board of trustees determines how the account is invested. A deferred member with assets pooled in the separate investment account receives interest at the investment performance rate actually earned on the

[1] A deferred member is a member who is entitled to a deferred service pension. *See* Minn. Stat. § 424A.016, subd. 6 (defined contribution plans); Minn. Stat. § 424A.02, subd. 7 (defined benefit plans).

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account. The deferred member bears the full investment risk subsequent to transfer. When the member retires, the deferred service pension is equal to the member's portion of the separate investment account.

This option is available to all volunteer fire relief association plan types.

2. Setting up a Separate Investment Vehicle: Under this option, the volunteer fire relief association establishes a separate investment vehicle for the amount payable to each deferred member. The separate investment vehicle is held separately from the other assets of the relief association, but is still governed by the relief association board of trustees and is still reported as an association asset. A member's deferred benefit amount is invested in the separate investment vehicle when the member separates from active service and membership. The volunteer fire relief association board of trustees selects the separate investment vehicle for each deferred member. A deferred member receives interest at the investment performance rate actually earned on the investment vehicle. The deferred member bears the full investment risk subsequent to transfer. When the member retires, the deferred service pension is equal to the fair market value of the member's separate investment vehicle.

This option is available to all volunteer fire relief association plan types.

3. Allowing the Board to Set Interest up to 5%: Under this option, the volunteer fire relief association board of trustees determines the rate of interest for deferred members, between 0 and 5 percent, compounded annually. Any change in the interest rate set by the board of trustees must be ratified by the governing body of the affiliated municipality or by the independent nonprofit firefighting corporation.[2] Interest is payable beginning on the January 1 next following the date on which the interest rate was ratified.[3] The board of trustees has flexibility to change the interest rate annually, for example, based on actual investment performance, or it could choose to select an interest rate and leave it unchanged for several years.

This option is available to lump-sum plans and monthly/lump-sum combination plans only.

4. Crediting Full Investment Gains and Losses: Under this option, a deferred member of a defined contribution plan receives investment allocations in the same manner as an active member. Each deferred member's account balance is credited with net investment gains or losses at the rate actually earned on the investment of special fund assets.

This option is available to defined contribution plans only.

If a volunteer fire relief association has a deferred interest option in its bylaws that is not one of the options described above, the relief association must amend its bylaws to

[2] Minn. Stat. § 424A.02, subd. 7(d).
[3] Minn. Stat. § 424A.02, subd. 7(e).

comply with current statutory requirements. The bylaw changes will affect only those members who separate from active service and membership after the bylaw change.

Interest Payment Method

Volunteer fire relief associations that elect to pay interest to a deferred member must decide on an interest payment method, including the interest payment starting date and ending date. State law establishes payment methods for each deferred interest type. A relief association may choose to define a different payment method in its bylaws, but if a method is not defined in the bylaws, or if the bylaw definition does not include the payment starting date and ending date, the default established in state statute and described below applies.

<u>Lump-Sum and Monthly/Lump-Sum Combination Plans</u>
For relief associations with lump-sum or monthly/lump sum combination plans that choose interest type 1 (Setting up a Separate Investment Account) or type 3 (Allowing the Board to Set Interest up to 5%), the default payment method is to pay interest or additional investment performance beginning on the first day of the month following the date on which the member separates from active service and membership and ending on the last day of the month immediately before the month in which the deferred member begins to receive the deferred service pension. For example, a member of a lump-sum plan separates from active service on May 5, and elects to receive his or her deferred service pension on April 22 of the following year. The member receives interest starting on June 1 and continues to receive interest until March 31 of the following year.

For relief associations with lump-sum or monthly/lump sum combination plans that choose interest type 2 (Setting up a Separate Investment Vehicle), the default method is to pay interest or additional investment performance beginning on the date that the member separates from active service and membership and ending on the date that the separate investment vehicle is valued immediately before the date on which the deferred member begins to receive the deferred service pension. For example, a relief association sets up a separate investment vehicle for a deferred member that consists of several certificates of deposit. The deferred member separates from active service and membership, and commences receipt of the deferred service pension during the following year. The separate investment vehicle is valued at the end of each month. The member receives interest or additional investment performance from the date of separation through the last day of the month immediately before the month in which the deferred service pension is paid. The member’s deferred service pension is equal to the value of the separate investment vehicle on the most recent valuation date, which in this example is at the end of the preceding month.

<u>Defined-Contribution Plans</u>
For relief associations with defined-contribution plans that choose interest type 1 (Setting up a Separate Investment Account) or type 4 (Crediting Full Investment Gains and Losses), the default method is to pay interest or additional investment performance beginning on the date that the member separates from active service and membership and

ending on the "accounting date" immediately before the deferred member begins to receive the deferred service pension.

The "accounting date" is the date on which a defined-contribution allocation table is prepared. The "accounting date" can be set by the relief association in its bylaws. For example, if a deferred member notifies the relief association that the member intends to take distribution of his or her deferred service pension on May 5, and the most recent defined contribution allocation table available on that date was prepared as of the previous December 31, the member's deferred service pension would be equal to his or her account balance as of the previous December 31 accounting date.

For relief associations with defined-contribution plans that choose interest type 2 (Setting up a Separate Investment Vehicle), the default method is to pay interest or additional investment performance beginning on the date that the member separates from active service and membership and ending on the date that the separate investment vehicle is valued immediately before the date on which the deferred member begins to receive the deferred service pension. For example, a separate investment vehicle consisting of several mutual funds is set up for a deferred member. The deferred member separates from active service and membership, and commences receipt of the deferred service pension during the following year. The separate investment vehicle is valued daily. The member receives interest or additional investment performance from the date of separation through the day immediately before the date on which the deferred service pension is paid. The member's deferred service pension is equal to the value of the separate investment vehicle on the most recent valuation date, which in this example is at the end of the preceding day.

A relief association may choose to define its own payment method in its bylaws. For example, a relief association could specify that interest is paid to deferred members for each completed calendar month that a member is deferred, or for each completed calendar year that a member is deferred. Any definition must include the payment starting date and ending date in order for the bylaw definition to be effective.

Membership Eligibility

Volunteer fire relief associations should determine whether they want to place any limitations on eligibility for deferred interest. Similarly-situated members must be treated the same. Relief associations do have some ability, however, to differentiate between different types of deferred members. For example, volunteer fire relief associations can choose only to pay interest to fully-vested deferred members, rather than to both fully-vested and partially-vested deferred members. Volunteer fire relief associations choosing to place limitations on eligibility for deferred interest must make sure that the limitations are clearly reflected in the relief association's bylaws. Any changes to the bylaws will affect only deferred members who separate from active service and membership after the bylaw change.