

**Minutes of the Regular Meeting of the Board of Directors of the
Sunshine Fire Protection District
August 10, 2021**

Call to Order

The meeting was held at Station 1.

The meeting was called to order at 7:34 PM and quorum was established. See Agenda below.

Attendance

Board Members Present: Alan Kirton, Cathy Shoenfeld, Dan Fischer, Dick Smith, Jean Gatz

Board Members Absent:

Others Present: Chief Michael Schmitt

Approval of Minutes

- Minutes from the July Board meeting were reviewed, no issues were found.

MOTION: To approve July Board Meeting Minutes was seconded and carried unanimously.

Treasurer's Report

- Treasurer's report was reviewed.
- There was discussion regarding contract fire payments, capital expense budget, uniforms.

MOTION: To approve July Treasurer's Report was seconded and carried unanimously.

Fire Chief's Report (see attached)

- There is another firefighter going to the academy this fall. That will make about 10 that have gotten that certification. It is the highest level and a great benefit to our community that we have that many certified at that level.
- Celebration of life for Aaron Beltz will be Saturday. Masks will be required. We have a training at the same day.
- Boulder County and fire service have rescinded the fire restrictions in the front range.
- There continue to be improvements made to the station; century link to fix phone, repair to doors. A. Kirton will reach out to address door seals and other maintenance.
- Previously identified landing zones are being evaluated and identified. This will improve the process and save time, giving us more flexibility to call for medical helicopters when needed.

Other Business (see agenda below)

- Update on grant awards and levels; we did not get awarded the 2021 Forest Restoration and Wildfire Risk Mitigation grant.
- Check-in on the financing for the new engine to determine if there were any new information about financing \$100,000. D. Fischer will follow up to confirm. Timing for the new engine is likely December-January.

- Revisit rescinding the emergency declaration for COVID. Board members agreed to keep it in place for the near-term.
- Community fest gathering will be put on hold until COVID rates are down and CDC and county guidance deems in-person gathering appropriate. J. Gatza and C. Shoenfeld will reach out to team from last year about hosting the virtual fund-raising. Messaging can include high rates of volunteering, high rates for training, costs for training and new truck equipment.
- Lynn Ballard is stepping down as medical officer. David Begleiter will be taking over that position.
- Board discussed research from D. Smith on Pension options for Firefighters that was presented at the July meeting.
- Options include:
 1. Contract with Fire fighter pension fund (FPPA) – state program. Current moratorium – expected to last at least 1-2 years.
 2. Establishing district own independent pension plan (e.g. Gold Hill)
 3. Length of Service Awards Program (LOSAP) (also called Heroes program)
- Group discussed pros and cons of each of the options. Cost, amount of work involved will be key factors. FPPA seems like the favored option with state matching, outside agency to help structure and guide. Additional analysis would be needed to determine the amounts to contribute; based on a target for monthly payments. (e.g. \$100 per month based on 10 yr service; \$200 per mo at 20 years service – Sugarloaf example). D. Smith suggested we could budget some funds until the FPPA option becomes available to be able to join.
- Discussion included eliminating option 2 for further analysis, focus on option 1.
- D. Smith will continue to gain information regarding the FPPA option, holding on LOSAP option for now.

Adjourned at 8:52 PM

Attest:



 Jean Gatza, Board Secretary

Board Meeting August 10th, 2021, 7:30 PM

Meeting will be held at Station 1

Based on the new CDC guidelines we should plan on wearing masks.

Agenda

Review/Approve Minutes

Review/Approve Treasurer's Report

Review Chief's Report

Other Business

1. We did not get awarded the 2021 Forest Restoration and Wildfire Risk Mitigation grant that we applied for in May. We are typically running between 50% and 60% success rate on CWPP grants. So not unusual that we didn't get awarded but still disappointing.
2. Discuss status on financing for the new engine. In the last meeting we had settled on \$100,000 as the amount to finance.
3. Last meeting we had discussed if we wanted to rescind SFPD's emergency declaration. Given what's going on with the Delta variant we will probably want to leave it in place.
4. Further discussion on Dick Smith's findings regarding a Firefighter's Pension for the fire district.
5. Other business?



Sunshine Fire Protection District
311 County Rd 83
Boulder, CO 80302
www.sunshine-fpd.org

Chief Report, Board Meeting 08/10/2021

1. Firefighter Newton will be attending fire academy this fall. This will put our number of structure (+MVA, Hazmat etc) certified firefighters at about double of comparable departments and even in line with combination (career/volunteer) departments.
2. Beltz Memorial Service. The service will be on 08/14 from 1400 to 1700hrs. A crew of volunteers will be there at 0800 to get instructions, and a larger training will occur between the stations that morning (with Gold Hill and Fourmile in attendance). Its ensured that there are no conflicts or safety issues.
As for the use of the stations for memorial service, the policy is that as long as the person was involved one way (helping, supporting) or another (volunteering) it is okay to use the station as long as operations are not affected (for which we meet in the morning to communicate with the group).
3. Boulder County and USFS have rescinded fire restrictions in the front range. In my opinion prematurely as the decision is based on the monsoon moisture we received. However, there is only sporadic moisture that is isolated in the forecast.
4. Our station group continues to make improvements and repairs to the stations.
5. After SFPD's effort in improving medical response with the creation of a new landing zone protocol and pre-determined LZ's numerous other districts are adopting the same system, and we are no in discussion with dispatch centers and OEM as well as Sheriff offices to create a setup that allows every district in the State to adopt this template. As of now already 5 districts including SFPD have adopted this new system.

Calls

Incident	Units	Problem	Response Date
BFD210726-008022	4561, 2501, 2503, 2505, 2570, AMR17, 2505, AMR400, AMR12	Injury / MVA	7/26/2021 23:20
BCFD210711-007852	4501, 4532, 4661, A5, AMRA, FM1, SS3	INACCR-Injury or Rollover	7/11/2021 15:39
BCFD210712-007910	5461, GH1	FICAMR-Illeg/Unattend Campfire	7/12/2021 22:24
BCFD210716-008052		FICONR-Controlled Burn	7/16/2021 13:30
BCFD210716-008062	2301, 2321, BR2	EMSR-Medical Call	7/16/2021 15:48
BCFD210716-008076	2301, 4532, 4561, 4565, 4566, 4662, A21, AMRC, FM2, GH1, SS3	EMSR-Medical Call	7/16/2021 20:44
BCFD210716-008078	4532, 4562, 4602, 4661, 4662, 5666, FM2, SS2	FIALCMR-Commercial Fire Alarm	7/16/2021 21:01
BCFD210717-008084	4532, 4662, A21, AMRC, FM2, SS2	EMSR-Medical Call	7/17/2021 0:52
BCFD210718-008165	4661, BCFDO2, FM3, SS3	FISMOR-Smoke Report	7/18/2021 20:51

<u>BCFD210720-008260</u>	4566, 4632, 4652, 4661, 6561, BCFDO1, FM1, SS2	FISMOR-Smoke Report	7/20/2021 16:51
<u>BCFD210723-008386</u>		FICONR-Controlled Burn	7/23/2021 22:11
<u>BCFD210724-008433</u>	4661, FM1, SS3	FICAMR-Illeg/Unattend Campfire	7/24/2021 20:10
<u>BCFD210724-008435</u>		FISMOR-Smoke Report	7/24/2021 20:38
<u>BCFD210728-008597</u>	4632, FM4, SS3	FIODOR-Odor Inv Outside	7/28/2021 8:16
<u>BCFD210801-008787</u>	4603, A5, AMRD, FM2, SS2	EMSR-Medical Call	8/1/2021 13:12
<u>BCFD210801-008791</u>	2204, 2260, 2331, 2332, BCFDO2, BR3	FIWILR-Wildland/Grass Fire	8/1/2021 14:41
<u>BCFD210801-008809</u>	2301, BR3	FINONR-Fire Non Structure	8/1/2021 22:19
<u>BCFD210802-008815</u>		FICONR-Controlled Burn	8/2/2021 8:37
<u>BCFD210802-008816</u>	2301, BR2	FIALRSR-Residential Fire Alarm	8/2/2021 8:43
<u>BCFD210802-008825</u>	4602, 4661, A5, SS2	INACCR-Injury or Rollover	8/2/2021 14:02
<u>BCFD210805-008933</u>	5461, GH2	FICAMR-Illeg/Unattend Campfire	8/5/2021 20:56
<u>BCFD210806-008978</u>	5404, A21, AMRA, GH1, 4535	zSick (AE/EE)	8/6/2021 21:34
<u>BCFD210807-008980</u>	2301, 4501, 4561, 4566, FM3, GH1, SS3	FIALRSR-Residential Fire Alarm	8/7/2021 2:13

BCFD210807-
008997

4532, 4561, 4566,
4602, 4651, 4662,
A7, AMRB, FM2,
SS3

EMSR-Medical
Call

8/7/2021 13:05

Pension Plan/Service Award Options for Volunteer Firefighters

1) Contract with Firefighter and Police Pension Association (FPPA)

FPPA is the primary central pension plan administrator for established volunteer fire departments. It provides a centralized service that works closely with DOLA to manage pension funds, actuarial audits of a district's finances and demographics, and pension payments. Departments make yearly contributions to their individual plans within FPPA. Requirements include establishing an SFPD Pension Board of Directors, adherence to DOLA rules and regulations (see Appendix), and whatever additional requirements and/or modifications that we would choose to add.

FPPA contact: Jacquette Tara 720-479-2310

Example fire district: Sugarloaf. Chief Goldman indicated that they contribute about \$20K/yr, which is matched by DOLA, based on a force of 56 volunteers. Monthly pension payment is about \$110 for 10 yr. volunteers and about \$200 for 20 yr. volunteers.

Advantages: A) Central Pension fund manager, SFPD not responsible for pension administration or investments (though we would have to track and verify that participants qualify each year and can be vested). B) Eligible for DOLA matching contributions. C) FPPA works with the district to ensure that the pension fund remains solvent down the road.

Disadvantage: FPPA currently has a moratorium on accepting additional Fire Districts into their pension program. The FPPA Board is awaiting introduction and passage of new legislation in the Colorado Legislature. The earliest possible time that SFPD could apply to this program would be 2024, if the legislation were to become law, and if FPPA then lifts the moratorium.

2) Establish our own independent pension plan

It is possible for a Fire District to setup and run our own pension plan. This would require consultation with an attorney, establishing bylaws, investing and managing the funds, and handling the pension payments. DOLA does support this option, thus all of DOLA rules and regulations would apply, including establishing a Pension Board of Directors.

Example fire district: GoldHill established an 'in-house' pension fund in 2017. They contribute about \$2K/yr into a money market fund at a local bank. To date, they have no one receiving pension money. Chief Finn provided a copy the GoldHill Bylaws (see attached file). The bylaws give them the option of contracting with FPPA in the future, if they so choose.

Advantages: This option is probably the only currently available mechanism to establish a pension fund. It is eligible for DOLA matching contributions (with a yearly grant application).

Disadvantage: The amount of in-house work required would be substantial. We would need a fair bit of legal advice and document preparation. There is a higher risk of inadequate funding down the road if the fund is not carefully tailored to SFPD demographics and anticipated long-term volunteer participation.

3) Use Length of Service Awards Program (LOSAP)

This is also called the Heroes program. It is a nationally-authorized program, but the rules and function vary a bit from state to state. It is not a pension program, per se, but is specifically designed to offer financial rewards to fire and law enforcement volunteers, based on length of service. LOSAP offers both defined contribution and defined benefit programs. The defined contribution portion is by far the most popular (according to Chad Alevras, the CO LOSAP representative). The latter involves setting up individual accounts for each volunteer. SFPD would contribute tax-deferred funds to those accounts based on pre-established criteria that we choose. The fund then becomes the property of the individual. From the Hero brochure: "A defined contribution plan defines the contribution the plan sponsor (sponsoring agency) makes to the participant's plan. The plan sponsor makes a contribution annually. The plan can be established as either a fixed LOSAP contribution or a variable LOSAP contribution, as determined by the plan sponsor. The plan sponsor contribution amount is based on the volunteer's annual qualifying activity. The plan sponsor is responsible only for the contribution amount, which is placed in the participant's LOSAP account. The LOSAP participant selects the investments from available investment options. The outcome of the defined contribution LOSAP retirement account is dependent upon the performance of the investments selected by the participant."

From the LOSAP representative:

What makes the HEROPLUS Program a preferred choice is:

- Incentive based account for your new and existing volunteers
- Fiduciary protection through Morningstar
- Mutual Funds with fully disclosed fees
- No Surrender Charges, custodian charges or sponsor charges
- Independent actuarial services
- Defined Contribution plan investment support provided by Morningstar Associates
- A stable value option for participants
- Personal Web-based fund performance

LOSAP Contact: Chad Alevras, 303-793-9319.

Example fire district: Estes Valley. Dave Wolff (Chief) and Erika Goetz, 970-577-0900.

See also example County Hill LOSAP plan as example.

Advantages: Criteria for service earned and amount of individual contribution would be determined by SFPD. LOSAP can be discriminatory, i.e., it can be used to award current volunteers who have already put in 20 years, or whatever length of time we determine, and the contribution does not need to be equal to contributions to others. For example, it could be used for a one time reward for a retiring volunteer.

Actuarial service is provided.

Disadvantage: Program is not eligible for DOLA matching funds.

Appendix (from the DOLA web page)

DOLA Volunteer Firefighter Pension Fund

As of July 1, 2004, the Department of Local Affairs (DOLA) became responsible for administering and disbursing the state contribution for state matching funds for the Volunteer Firefighter Pension Fund (VFP) state match program (CRS 31-30-1112). The Fire and Police Pension Association (FPPA) previously administered the program. This program is designed to help local governments provide a retirement benefit to attract volunteers. All volunteer firefighting entities, which provide a volunteer firefighter pension, are eligible to receive a state match. The entities must contribute funds generated from taxes (property, sales, S.O., etc.) which the state will match based on a statutory calculation.

Application Information

Applications from eligible entities (see "Eligibility") are accepted annually from September 1 - October 31, to request a state match based on the entity tax contribution as described above.

The VFP online application will be available via the "Apply and Manage Application" button below during the application period.

Please contact program staff if you have questions, contact information is below.

Eligibility

- Municipalities with a population under 100,000 that maintain a regularly organized volunteer fire department and that offer fire protection services
- Fire protection districts having volunteers and offering fire protection services
- County improvement districts having volunteer fire department members and offering fire protection services
- Counties contributing to a volunteer pension fund at one of the above

The eligible entities must have:

- Active, pension-eligible volunteer firefighters
 - "Active volunteer": A volunteer firefighter shall maintain a minimum training participation in the fire dep't of 36 hours each year to qualify for benefits (31-30-1122(1)).
 - "Pension-eligible": A retired volunteer firefighter who has served twenty years and is over 50 years of age is eligible for pension benefit. If the firefighter is not yet 50, they may take a leave of absence until they reach that age. The local board may decide to pay a retirement benefit with less than 20 years of service if the municipality/District is actuarially sound. No matter what, you're not eligible for funds until after 10 years.
- Contributed tax revenue to the volunteer firefighter pension fund in the year prior to the application year.

Other Attachments

FPPA Employer guide for volunteer fire departments, GoldHill Pension Fund Bylaws, HeroPlus Program Brochure, Country Hill LOSAP Plan.

**STUDY OF
VOLUNTEER FIREFIGHTER PENSION PLANS
IN COLORADO**

September 2016

LEGISLATIVE AUDIT COMMITTEE

Representative Dan Nordberg – Chair Representative Dianne Primavera – Vice-Chair

Senator Rollie Heath
Senator Chris Holbert
Senator Cheri Jahn

Representative Tracy Kraft-Tharp
Senator Tim Neville
Representative Lori Saine

OFFICE OF THE STATE AUDITOR

Dianne E. Ray

State Auditor

Monica Bowers

Deputy State Auditor

Andrew Knauer

Contract Monitor

Duane Morris LLP
Pension Trustee Advisors

Contractor
Sub-Contractor

AN ELECTRONIC VERSION OF THIS REPORT IS AVAILABLE AT
WWW.STATE.CO.US/AUDITOR

A BOUND REPORT MAY BE OBTAINED BY CALLING THE
OFFICE OF THE STATE AUDITOR
303.869.2800

PLEASE REFER TO REPORT NUMBER 1550P WHEN REQUESTING THIS REPORT

September 19, 2016

Members of the Legislative Audit Committee:

This report contains the results of a study of the Volunteer Firefighter Pension Plans in Colorado. The study was conducted pursuant to Section 31-31-1002, C.R.S., which requires the State Auditor, with the concurrence of the Fire and Police Pension Association (FPPA) and the Department of Local Affairs (Department) to retain a nationally recognized law firm with experience in federal tax law as it relates to public sector pension plans and an actuary if necessary to conduct a study of various issues pertaining to the plans.

The work presented in this study relies on the actuarial work conducted by FPPA's actuaries, and incorporates the actuarial assumptions approved by the FPPA Board of Trustees. As with any actuarial study which engages in the prediction of future outcomes, to the extent future experience differs from the assumptions, then the actuarial outcomes will similarly differ.

No statements made in this study should be construed as legal advice or as pertaining to specific factual situations.

William Fornia is a member of the American Academy of Actuaries and meets all of the Qualification Standards of the American Academy of Actuaries to render the actuarial opinion contained herein.

Respectfully Submitted,



John A. Nixon
Duane Morris, LLP



William B. Fornia, FSA, EA
Pension Trustee Advisors

Table of Contents

Report Highlights	1
Volunteer Firefighter Pension Plans – Background	2
Funding of Volunteer Firefighter Pension Plans	3
The Fire and Police Pension Association.....	3
The Department of Local Affairs.....	4
Purpose, Scope, and Methodology of the Study	4
Section I: Current Structure of Volunteer Firefighter Pension Plans	6
A. Tax Qualified Status under the Internal Revenue Code.....	6
B. Compliance with the Fair Labor Standards Act (FLSA)	10
C. Funding and Best Practices	13
D. Administrative Issues.....	19
Section II: Plan Design Implications	21
Alternatives to the Current Structure of Maintaining Separate Local Defined Benefit Plans	22
A. Adoption of Master and Prototype Plan Document under a Central Administrator	23
B. Length of Service Plan Under Section 457(e)(11).....	25
C. Convert all Pension Act Plans to a Single DB System Administered by a Central Organization	27
D. Privatization – Annuitize Current Benefits through a Private Vendor	28
E. Adopt a Traditional Defined Benefit Plan with an “Offset” Formula (Umbrella Plan).....	29
F. Establish a “Cash Balance” DB Plan with Future Service Accruals	32

List of Tables

Table 1	Volunteer Firefighter Pension Plans – Monthly Benefit Levels	3
Table 2	Actuarial Assumptions.....	11
Table 3	Association Affiliated Volunteer Pension Plans	14
Table 4	Non-FPPA-Affiliated Volunteer Pension Plans.....	15

KEY FACTS AND FINDINGS

- There is a high risk that the Plans do not comply with the tax qualification requirements of the Internal Revenue Code (IRC).
- While the vast majority of Plans comply with the Fair Labor Standards Act (FLSA), as many as 33 Plans may warrant further analysis to assure compliance.
- The majority of the \$4.1 million of annual State funding toward Plans is going toward those which are fully funded or to provide benefits in excess of \$300 per month.
- The structure of the current Plans may not provide adequate incentives to encourage firefighters to serve as volunteers;
- While a majority of the Plans do not have any unfunded liability and generally follow best practices with respect to actuarial calculations and plan contributions, at least 101 of the Plans are underfunded, with a majority of these providing benefits in excess of \$300 per month. Policymakers should consider benefit levels and funding practices in relation to state funding for plans.
- Alternatives exist which would allow the Plans to comply with the IRC and FLSA, and could also address funding and administrative concerns. Most of these alternatives would require an amendment to the Pension Act.

BACKGROUND

In Colorado, pension plans for volunteer fire departments (Plans) are established under the Volunteer Firefighter Pension Act (Pension Act).

Normal Retirement Pensions may be granted to a volunteer firefighter who has maintained a minimum training participation in the fire department of thirty-six hours each year during twenty years of active service and is at least 50 years of age. Certain other benefits may also be provided.

At least 235 Plans currently operate in the State. The Fire and Police Pension Association (FPPA) administers 174 of these plans. The others are administered locally. 210 of the 235 Plans receive funding from the State.

ALTERNATIVES TO THE CURRENT PLAN STRUCTURE

- A. Master and Prototype Plan Document under a Central Administrator – Makes available an IRS compliant plan document that each volunteer firefighter department would adopt. Plans would be pooled and managed by a state entity such as FPPA (pursuant to its own master and prototype document) or an outside vendor (pursuant to the vendor's master and prototype document).
- B. Length of Service Plan – Converts all plans to a DC approach through a Length of Service program, which qualifies under section 457(e)(11) of the IRC rather than 401.
- C. Single DB System Administered by a Central Organization – The various Plans would be merged into a single defined benefit "system" operated by a central organization, such as the FPPA.
- D. Annuitize Current Benefits through a Private Vendor – Requires each volunteer firefighter department to purchase annuities from the private market for benefits accrued to date plus benefits earned each year.
- E. New Traditional Defined Benefit Plan with an "Offset" Formula – Develops an IRS compliant master plan document that each current Plan would adopt. The current Plans would be frozen and act as an offset to the new plan benefit levels. The new plan would be sponsored and solely administered by a central organization, such as the FPPA.
- F. New "Cash Balance" DB Plan with Future Service Accruals – A cash balance plan operates under many of the same principles as a defined contribution plan but is considered a defined benefit plan under the IRC. Current Plans would be frozen or terminated. For current Plans that are terminated, funds could be "rolled over" into the new the cash balance plan.

Volunteer Firefighter Pension Plans – Background

In Colorado, pension plans for volunteer fire departments are established under the Volunteer Firefighter Pension Act (Pension Act) [Section 31-30-1101, et seq., C.R.S.]. The Pension Act allows for a volunteer pension fund to pay the following retirement benefits:

- Normal Retirement Pension [Section 31-30-1122, C.R.S.]. Normal Retirement Pension may be granted to a volunteer firefighter who has maintained a minimum training participation in the fire department of thirty-six hours each year during twenty years of active service and is at least fifty years of age.
- Supplemental Retirement Pension – Extended Service [Section 31-30-1125, C.R.S.]. A supplemental monthly pension payment may be granted to a volunteer of at least fifty years of age who volunteered for more than twenty years.
- Vested Retirement Benefit [Section 31-30-1122, C.R.S.]. A vested retirement benefit may be provided to any volunteer who is at least fifty years old and terminates service with ten or more years of service, but less than twenty years of service, provided the relevant pension fund is actuarially sound. This benefit amount will be the Normal Retirement Pension pro-rated based on the volunteer's number of years of service.

In addition, the Pension Act requires volunteer fire departments to offer disability and funeral benefits, and also allows for them to offer survivor benefits. [Sections 31-30-1121, 1126, and 1129, C.R.S.]

Section 31-30-1103, C.R.S., requires each local government that maintains a volunteer fire department to have a board of trustees that manages and disperses money in the pension fund. Each board consists of various members, typically including local government officials and fire department representatives who are elected to the boards by their constituents. The boards are required by statute [Section 31-30-1108, C.R.S.] to adopt necessary rules to discharge their duties and are responsible for setting the local district's contribution level and the per month retirement benefit level for volunteers.

There is no single entity that is responsible for oversight of volunteer firefighter pension plans (Plans) in the State. As such, there is no central entity with comprehensive information about volunteer Plans, including the total number of Plans, their financial situations, or the number of retirees and volunteers they serve. However, as discussed in more detail later in this section, the Fire and Police Pension Association (FPPA) and the Colorado Department of Local Affairs (Department) have involvement with the volunteer Plans. According to information from the Department and FPPA, there are at least 235 Plans currently operating in the State. Each of the local governments determines which of the retirement pension benefits it will offer its volunteers and sets the benefit level. There is a wide range of plan sizes, from covering fewer than 10 participants to more than 150. The following chart provides a breakdown of the monthly retirement benefits offered by the known Plans.

TABLE 1.

Volunteer Firefighter Pension Plans – Monthly Benefit Levels		
Monthly Benefit Level	Number of Plans	Percentage of Total Plans
Less than \$100	37	16%
\$100 - \$300	87	37%
\$301 - \$650	78	33%
\$651 - \$999	26	11%
\$1000 and Up	7	3%
Total	235	100%

Funding of Volunteer Firefighter Pension Plans

Counties, county improvement districts, fire improvement districts, and municipalities with volunteer fire departments are statutorily allowed to levy a tax of not more than one mill (which is equal to one tenth of a cent) on the taxable property of the area [Section 31-30-1110, C.R.S.] to fund the volunteer firefighter pension plans. Those with populations under 100,000 can also contribute moneys to the volunteer pensions from any other tax that is levied in the county, district, or municipality. In addition, the State makes annual contributions available to volunteer firefighter pension plans whose boards choose to participate in the state assistance program. The total number of plans and the amount of the State contribution has remained stable over the past few years. In 2015, the State's total contribution was \$4.1 million and these contributions went to 210 of the 235 Plans (89 percent).

The Fire and Police Pension Association

If the local volunteer firefighter pension board decides to, it can enter into an affiliation agreement with FPPA to administer its Plan and manage the investments of the Plan's funds [Section 31-30-1108, C.R.S.]. FPPA is a public instrumentality and political subdivision of the state governed by a nine-member board of directors [Section 31-31-201, C.R.S.]. FPPA acts as the trustee of the fire and police members' benefit investment fund which includes funds from paid police and fire department pensions as well as funds from affiliated volunteer firefighter plans [Section 31-31-302, C.R.S.].

FPPA currently has agreements with local governing bodies to administer 174 volunteer firefighter pension plans. According to Section 31-31-705(2), C.R.S., FPPA's responsibilities for each of these Plans includes:

- Investing the assets of the Plan.
- Collecting and accounting for the contributions to the Plan.
- Disbursing benefits to retirees as outlined by the local pension board.

- Conducting an actuarial valuation and financial audit of the Plan on at least a biannual basis, or as required by regulatory bodies or law.
- Maintaining records and reporting the investments, assets, and benefits of the Plan as required by statute or regulatory bodies.
- Authorizing the payment of Plan expenses from the assets of the Plan, including the expenses incurred by FPPA for administration of the Plan.

According to FPPA, it manages about \$173 million in investments for the volunteer firefighter pension plans covering about 3,200 active volunteer firefighters and 3,600 retirees as of December 2015.

The Department of Local Affairs

In accordance with Section 31-30-1112, C.R.S., the Department's primary responsibility related to Plans is to determine the state's annual contribution to each Plan that chooses to participate in the state assistance program. The Department calculates the contribution amounts in accordance with a statutory formula (described in more detail in Section I of the report) and distributes the funds to the Plans. Additionally, the Department is responsible for administering the short-term disability program for volunteers.

Purpose, Scope, and Methodology of the Study

In accordance with statute, [Section 31-31-1001, C.R.S.], the Police Officers' and Firefighters' Pension Reform Commission (Commission) has the responsibility to study and propose legislation related to the funding of police officers' and firefighters' pensions in the State, including volunteer firefighters' pensions. The Commission is made up of five senators appointed by the president of the Senate and 10 representatives appointed by the speaker of the House of Representatives. During its 2014 meeting, the Commission discussed concerns over the regulatory and financial adequacy of the volunteer firefighter pension plans in the State, which led to the statutory requirement for this study.

The key objectives of this study were to evaluate the current structure of volunteer firefighter plans in Colorado and consider alternatives, as required by Senate Bill 15-029 enacted by the General Assembly in 2015. Specifically, the bill required the Office of the State Auditor (OSA) to conduct a study of specific issues and also consider other matters (the required issues are **bolded**):

1. The current structure of the local volunteer firefighter pension plans in Colorado, including:
 - a. **Whether the federal Internal Revenue Service (IRS) recognizes the volunteer firefighter Plans created pursuant to Section 31-31-1100 and 1200 et seq., C.R.S.**
 - b. **If the current Plans are not recognized by the IRS, how such Plans can be brought into compliance with federal law.**

- c. **Whether volunteer firefighter Plans have provided benefits in excess of what is allowed under federal law, primarily the Fair Labor Standards Act (FLSA).**
- d. Whether the local volunteer firefighter Plans should undergo periodic actuarial valuations.
- e. Whether volunteer fire departments should make contributions to their volunteer pension Plans.
- f. Whether state assistance should be provided to fully funded Plans or instead be based on a Plan's need for additional funding, including a comparison of the State's current costs with the costs of state assistance if it were based on need and an analysis of the impact on Plan benefits if state assistance were based on need.
- g. The difficulties and burdens inherent in operating local Plans, such as: separate recordkeeping; coordinating information and benefits when volunteers have worked at multiple departments; complying with regulatory requirements including GASB reporting requirements; and maintaining separate boards.

These issues are discussed in Section I of the report.

2. Alternatives to maintaining separate local volunteer plans as currently structured, including the benefits and drawbacks of such alternatives:

How alternative plans are compliant with federal law:

- a. Whether the state should close current local Plans or convert them to alternative benefit plans, such as annuities, lump sum, or defined contribution (DC) style Plans.
- b. Whether firefighters and volunteer departments are best served by pension Plans that require 10 to 20 years of service before paying a benefit at age 50.
- c. If a cost-sharing multiple employer Plan would be more efficient than individual local Plans.
- d. Whether a central administrator should be authorized or directed to administer a Plan other than the current local Plan.

Alternatives to the current structure along with discussion of the questions above are discussed in Section II of the report.

In accordance with Senate Bill 15-029, the OSA, with the concurrence of FPPA and the Department, retained a nationally recognized law firm with experience in federal tax law as it relates to public sector pension plans to conduct this study. The OSA contracted with Duane Morris, LLP, a law firm with extensive experience in the design, compliance, and legal issues impacting governmental pension Plans. Duane Morris engaged the actuarial services of Pension Trustee Advisors, Inc., a nationally recognized actuarial firm with expertise in government pension systems, including firefighter pensions (collectively, the "Contractors").

The above notwithstanding, no statements made in this study should be construed as legal advice or as pertaining to specific factual situations.

To complete the study, the Contractors:

- Reviewed applicable state and federal laws, legal decisions, and other federal legal guidance related to volunteer pension Plans;
- Examined Plan information, and summary actuarial data for all Plans that receive state funding;
- Performed actuarial calculations and analysis related to the Plans, including actuarial analysis related to Plans' funded status and current contribution levels;
- Obtained information from FPPA for the 174 Plans affiliated with FPPA and surveyed the 61 locally administered plans to determine whether the Plans had a "plan document" and whether they felt the current system was serving their needs. Only two Plans responded;
- Researched other states with similar volunteer pension Plans, and
- Discussed issues with and gathered data from FPPA and the Department.

Section I: Current Structure of Volunteer Firefighter Pension Plans

A. Tax Qualified Status under the Internal Revenue Code

Section 31-30-1133(2), C.R.S., provides, in relevant part, as follows:

Any volunteer firefighter pension plan established by this part 11 [of the Pension Act] to provide retirement benefits for volunteer firefighters shall satisfy the qualification requirements specified in section 401 of the Internal Revenue Code, as applicable to governmental plans.

In order to attain and maintain tax qualified status as required by the Pension Act, a retirement plan must satisfy both documentation and operational requirements of the Internal Revenue code (IRC). Based on our review of IRC tax qualification requirements and the Pension Act, there is a high risk that Colorado's Plans are not in compliance with applicable IRC requirements. This is because (i) there are several tax-qualification language requirements that are not incorporated in the Pension Act, and (ii) our review indicates that few if any individual Plans maintain written plan documents that incorporate such requirements.

As a threshold matter, any Plan established pursuant to the Pension Act would be deemed a "governmental plan" pursuant to Section 414(d) of the IRC. Therefore, the Pension Act Plans are not subject to many of the tax qualification documentation requirements applicable to private sector plans. Nonetheless, there are several language requirements applicable to governmental

plans that are not satisfied by the Pension Act. Specifically, the Pension Act, standing alone without supplement by a plan document, would not be deemed tax qualified due to its failure to include the following required provisions:

- Section 401(a)(7) – Minimum Vesting Standards. Governmental plans are required to include a written statement of the applicable “vesting rules” (i.e., the conditions under which a participant’s benefit under the plan becomes non-forfeitable). With respect to governmental plans, in the event of a plan termination, a participant must be vested to the extent that benefits are “funded” under the trust. Thus, for example, if the plan is 60% funded at termination, a participant, regardless of the amount of service, would be 60% vested in his or her accrued benefit. This requirement regarding vesting upon plan termination must be included in the plan document. The failure to include such a provision is a tax qualification defect.
- Section 401(a)(9) – Required Minimum Distributions. This section requires that a participant must commence benefits on the later of April 1 of the calendar year following: (i) the calendar year in which the employee attains age 70½; or (ii) the calendar year in which the employee retires. The plan document must include a specific reference to comply with Section 401(a)(9) of the IRC. There is no reference to Section 401(a)(9) of the IRC in the Pension Act nor is there any language which implies that a volunteer must begin the benefit in a timely fashion that complies with Section 401(a)(9) of the IRC. See 26 CFR § 1.401(a)(9), Q&A-3.
- Section 401(a)(17) – Limitation on Compensation. Section 401(a)(17) of the IRC provides that a Plan must state the limitation on compensation that is includable for purposes of determining the Plan benefit. The 2016 limitation is \$265,000 per year. Obviously, this provision does not impact a volunteer firefighter Plan under which there is no base compensation utilized for purposes of determining the accrued benefit. Nonetheless, the applicable IRS guidance provides that the limitation on compensation must be included in the written plan document. See 26 CFR § 1.401(a)(17)-1(a)(1).
- Section 401(a)(31) - Automatic Rollovers. This section of the IRC provides that any distribution from a participant’s account that is an “eligible rollover distribution” must provide applicable language authorizing the rollover from the participant’s account. The Pension Act does not contain eligible rollover language. See 26 CFR § 1.401(a)(31)-1, Q&A-1(a) & Q&A-3.
- Section 415(b) – Limitations on Benefits. Section 415(b) of the IRC provides that with respect to governmental plans, such plans cannot pay a benefit in excess of \$210,000 per year. While this is obviously much greater than the benefit that would be paid under any Pension Act Plan, the tax qualification requirements of the IRC mandate that the dollar limitation, or reference to the statutory provision, be included in the plan document. See Section 415(a)(1)(A) of the IRC.

The IRC requires the above provisions be included in a written plan document, however we have not identified a single Plan that operates pursuant to a written plan document meeting the tax qualification requirements. Specifically, FPPA does not believe that any of their affiliates’ Plans

have a qualified written document, and none of the non-FPPA Plans provided a written plan document in response to our request. Accordingly, absent a complete plan document properly incorporating these requirements, Plans established under Pension Act would likely not satisfy the tax qualification provisions under the IRC and could be subject to disqualification.

Lastly, we note that even if the tax qualification rules were incorporated into the Pension Act, an individual Plan would only meet all IRC qualifications if it maintained its own plan document detailing its operations including, (1) the specific volunteers covered; and (2) the benefit formula utilized to calculate the benefit of such volunteer. The Pension Act's current structure as an "enabling" statute is consistent with allowing for different localities to enact different Plan levels by individual document. It would be extremely difficult to incorporate the operative terms of over 200 plans into a state statute.

Potential Liability for Tax-Qualification Failure

The IRS is authorized to audit the documentation and operation of any retirement plan that purports to be tax-qualified. While we are not aware of cases in which the IRS has disqualified volunteer firefighter plans, the non-compliant Plans could lose tax-qualified status under the IRC based upon the lack of documentation. Disqualification could result in severe consequences, including (i) immediate taxation of Plan participants on the present value of the vested accrued benefit under the Plan irrespective of whether such amounts have been distributed to the participant; (ii) the assessment of interest on the tax liability (assuming that the amounts were deemed "earned" in previous tax years) and (iii) potential payroll taxes under Social Security, Medicare, and Unemployment.

Additionally, if income and payroll taxes and interest are triggered upon Plan disqualification, a participant could assert a cause of action against the local government for its failure maintain a tax-qualified Plan as required under the Pension Act. One possible claim would be that the local government failed to provide a benefit consistent with the intended federal tax treatment under the Pension Act and the IRC.

Achieving Compliance within the Current Plan Structure: Adopting a Tax-Compliant Plan Document

To bring the existing local plans into compliance with the IRC documentation requirements without making any other change to the structure or funding of the plans, a "template" document could be developed that meets the various tax qualification rules. The template would be adopted by the individual departments with appropriate eligibility, benefit accrual formula, and vesting requirements.

This alternative should not require legislative action because the Pension Act currently requires departments to adopt a plan compliant with IRC Section 401(a). The principal concerns would be: (1) the cost of having an outside attorney develop a template plan that could be tailored for all of the individual plans would be at least \$75,000; (2) there would a significant burden on FPPA or any agency charged with assisting the individual departments in completing the template; and (3) the possibility that the IRS could examine one or more of the volunteer plans and find non-compliance for the tax periods **prior** to the adoption of the template.

Because this approach does not have the benefit of IRS review and approval, consideration should be given to filing for prior period correction under the IRS “Employee Plans Compliance Resolution System” (EPCRS). EPCRS allows plan sponsors to correct operational or plan document defects with IRS approval and avoid disqualification. The Voluntary Correction Program is an option within the EPCRS that allows employers to submit the correction pursuant to a specified procedure and specifically request that the IRS approve the correction methodology. After approving the proposed correction, and any changes in a plan's administrative practices and procedures to help ensure compliance, the IRS issues a “Compliance Statement” which requires that the error be corrected in the manner approved by the IRS. The Compliance Statement addresses the identified errors, the terms of required correction (including any revision of administrative procedures to help ensure compliance) and the time period within which the proposed corrections must be implemented. The advantage of filing under EPCRS is that the Compliance Statement is binding upon the IRS and the plan sponsor and provides that the IRS will not treat the plan as failing to satisfy the applicable tax qualification requirements as long as the conditions listed in that statement are satisfied.

Typically, Voluntary Correction Program filings are made with respect to individual plans that currently have IRS determination letters. Moreover, the IRS guidance under EPCRS does not specifically address the current situation in which the Plans never adopted formal plan documents. However, EPCRS includes a “group submission” process through which an “eligible organization” may make a Voluntary Correction Program filing for at least 20 plans for which it provides regular administrative services. FPPA qualifies as an eligible organization for this purpose. It is arguable that the group submission process is appropriate in light of the unique nature of the plans involved (governmental, volunteer plans) and the relatively limited resources of individual departments to file separately.

We have reached out to the IRS on an informal, anonymous basis regarding the availability of a group submission with respect to the current situation and its representatives have been non-committal. Nonetheless, it may still be advantageous to file a group submission as the IRS is prohibited from initiating a plan examination while a Voluntary Correction Program submission is pending.

The primary disadvantage of filing under EPCRS is the possibility that the IRS would reject group submission status and the individual plans would have been disclosed and therefore exposed to potential audit. The filing would also generate additional costs. Specifically, the Voluntary Correction Program group submission filing fee is \$50,000 payable to the IRS (\$50,000 is the maximum fee assuming the defects are uniform across all plans). Additionally, there are associated legal fees in preparing the Voluntary Correction Program application (which would likely require the inclusion of a template document as discussed above) and negotiation of the Compliance Statement. We estimate these professional fees to be between \$85,000 and \$120,000. If successful in obtaining the Compliance Statement, FPPA or the appropriate state agency would be charged with the implementation of the Compliance Statement by the individual departments.

Section II of this Report discusses a number of alternatives to the current structure. An EPCRS filing is compatible with each of these alternatives and should be considered as part of a comprehensive solution.

B. Compliance with the Fair Labor Standards Act (FLSA)

Pursuant to the FLSA, an employer must pay employees at least the minimum hourly wage for work performed, 29 U.S.C. § 206, and one and one half times the employer’s regular wage for hours worked in excess of forty hours per week, 29 U.S.C. § 207. The FLSA does not apply to individuals who volunteer to perform services for a public agency. Organizations that use volunteer services must determine if an individual is an employee or a volunteer in determining FLSA compliance. For purposes of this report, the key factor in this determination is whether the amount of retirement benefits payable under a Plan is “reasonable”. As discussed in the next section, based on our review of the FLSA, analogous provisions of the IRC, and the level of benefits provided by each of the Plans, the retirement benefits under at least 202 of the 235 Plans (86 percent) are reasonable. We further conclude that it is highly likely that the retirement benefits under the remaining Plans would be deemed reasonable. However, as discussed in the next section, further analysis of the benefits and payments offered by some volunteer Plans may be warranted to assure compliance.

Provision of Retirement Benefits to Volunteers

The Department of Labor (DOL) has regulations [29 U.S.C. 2003(e)(4)(A) of the FLSA and 29 C.F.R. §§ 553.101 and 553.103] defining a “volunteer” within the meaning of the FLSA as an individual who:

1. Provides their services for civic, charitable, or humanitarian reasons without promise, expectation, or receipt of compensation for the services rendered, although a volunteer can be paid expenses, reasonable benefits, or a nominal fee to perform such services;
2. Offers their services freely and without coercion, direct or implied, from the employer; and
3. Is not otherwise employed by the same public agency to perform the same services as those for which they propose to volunteer; in other words, individuals can qualify as volunteers if they either volunteer for different agencies or perform services different from those they are otherwise employed to perform.

Those who volunteer as firefighters will fall within this definition — provided those individuals do not additionally perform paid firefighter services for the same department for which they “volunteer.” See 29 C.F.R. § 553.104(a)-(b); 29 C.F.R. § 553.101 for exceptions to this definition.

According to federal regulations [29 C.F.R. § 553.106(d),(f)], “reasonable benefits” expressly include “inclusion of individual volunteers in group insurance plans (such as liability, health, life, disability, workers’ compensation) or *pension plans* or ‘*Length of Service*’ awards, commonly or traditionally provided to volunteers of State and local government agencies” provided, however, that the “economic realities” of a particular situation, determined by examining the total amount of payments made (expenses, benefits, fees), do not warrant the loss of volunteer status (emphasis added). Accordingly, the provision of retirement benefits under the Pension Act would not jeopardize the volunteer status of the firefighters provided that the amount paid constitutes a “reasonable benefit” for purposes of the FLSA.

The FLSA does not provide an expressed “safe harbor” on the amount of retirement benefits that is deemed “reasonable” and as such permitted for volunteers. We believe, however, that reasonableness can be inferred by reference to standards established under the Internal Revenue Code for “bona fide volunteers” under “Length of Service award programs” (Length of Service programs) pursuant to Section 457(e)(11) of the IRC.

Under Section 457(e)(11), a Length of Service benefit is not deemed reasonable if “the aggregate amount of Length of Service awards accruing with respect to any year of service for any bona fide volunteer exceeds \$3,000.” We have concluded that the \$3,000 limit in Section 457(e)(11) of the IRC actuarially converts to a life annuity benefit of approximately \$650 per month or \$7,800 per year using the Pension Act provision qualifying a firefighter for a Normal Retirement Pension upon completion of 20 years of service. (A Supplemental Retirement Pension based upon 21 or more total years of service would have a higher equivalent annuity.) Our calculation of the \$3,000 limit is as shown below.

TABLE 2.

Actuarial Assumptions	
<ul style="list-style-type: none"> Pre-Retirement Accumulation Factor of 43.30 years based on: <ul style="list-style-type: none"> 20-year career (Normal Retirement Pension) 7.5% annual investment return, based on assumptions used by FPPA actuary for volunteers Annuity Factor of 16.4325 based on: <ul style="list-style-type: none"> Average Age of 53.4 years Male retiree Female spouse 50% Joint and Survivor Annuity RP-2014 Mortality Table with fully generational mortality improvement, using Scale MP-2014 	
	<p>Calculation</p> <ul style="list-style-type: none"> \$3,000 per year accumulates to \$129,914 after 20 years <ul style="list-style-type: none"> $\\$3,000 \times 43.30 = \\$129,914$ \$129,914 can purchase a monthly annuity of \$659 <ul style="list-style-type: none"> $\\$129,914 / 16.4325 / 12 = \\659
<p>Conclusion: \$3,000 per year is actuarial equivalent to a monthly benefit of \$659 assuming a Normal Retirement Pension based upon at least 20 years of service.</p>	

Accordingly, we conclude that \$650 per month should be deemed “reasonable” and should not jeopardize the voluntary status of such firefighter. Currently 202 of the 235 Plans (86 percent) provide a monthly benefit of \$650 or less, and therefore are consistent with voluntary status under the FLSA.

If a retirement benefit exceeds \$650 per month, the payment of such does not automatically convert the firefighter from a volunteer to an employee. The determination of volunteer status in such cases must be made based on a case-by-case analysis of the total economic realities of the volunteer relationship accounting for all expenses, benefits, and fees provided to the volunteer by examining the total amount of payments made.

While there are 33 Plans with benefits above \$650, the risk that the DOL would disallow volunteer status is extremely low. We have only identified one somewhat analogous case, which determined that payments to volunteer firefighters at an hourly rate substantially similar to the hourly rates paid to full-time employed firefighters were not “nominal” and destroyed the firefighters’ volunteer status rendering them “employees” under the FLSA. Employing a similar logic to retirement benefits, even the highest pension benefit paid under a Plan (\$1,400 per month) is substantially less than the \$3,317 average monthly pension benefit offered to a paid full time firefighter retiring after 20 to 25 years of service under FPPA.

Potential Liability for FLSA Violation

A violation of FLSA could result in several consequences:

- **Potential liability of the local government to the employee for wage payments.** If a benefit is deemed unreasonable, and a firefighter is found to be an employee rather than a volunteer, the local government deemed to be the employer of the firefighter may be required to pay back wages and payroll taxes. When the DOL encounters violations, it recommends changes in employment practices to bring the employer into compliance, and requests the payment of any back wages due to employees. In addition to the back wages, the employer could be held liable for both the employer and employee portion of Social Security, Medicare, and Unemployment payroll taxes.
- **Penalties against the local government.** The DOL may bring suit for back pay and seek injunctions to restrain persons from violating the Act. The potential financial exposure would be equal to the estimated number of hours worked by the individual multiplied by \$7.25 (the current Federal minimum wage as of July 24, 2009) plus an equal amount in liquidated damages. In addition to the DOL, a firefighter may bring a private right of action under the FLSA. Employers who violate FLSA provisions are liable not only to the employee affected in the amount of their unpaid wages, but also for an additional equal amount as liquidated damages” [29 U.S.C. § 216(b)]. Further, if a private plaintiff is the prevailing party in an FLSA case, the court is required to award reasonable attorneys’ fees and costs, which would then be paid by the defendant (the local government) [29 U.S.C. § 216(b)]. The statute of limitations related to FLSA violations is generally two years, however, if the cause of action arises out of a “willful violation,” the statute of limitation is extended to three years.

If a pension benefit of a Plan exceeds \$650 per month, the local government should document the nature of the relationship in a manner that supports voluntary status. Additionally, the local government should be prepared to support the position that the total economic benefit provided to volunteers is not commensurate with the economic benefits (salary plus benefits) provided to its actual employees.

The probability of finding a FLSA violation as a result of retirement benefits being *too generous* is unlikely and completely inconsistent with the goals and objectives of the FLSA. As noted by the DOL in evaluating the status of volunteers for purposes of the FLSA:

The FLSA recognizes the generosity and public benefits of volunteering and does not seek to pose unnecessary obstacles to bona fide volunteer efforts for charitable and public purposes. The Department of Labor is committed to ensuring that individuals are able to volunteer their services freely for charitable and public purposes within the legal constraints established by Congress.

This language strongly suggests that historically, the DOL has been flexible in its review of voluntary status, particularly in the public sector.

C. Funding and Best Practices

Actuarial Valuations

We reviewed the practices of all of the 174 Plans under FPPA and a sample of 5 of the 61 individually administered Plans with respect to conducting routine actuarial valuations, employer contributions, and state funding to determine if the Plans are following best practices in these areas and to assess the impact if state funding was changed to be directed to Plans that need additional funding.

Periodic actuarial valuations are required under Governmental Accounting Standards for any local government which reports its financial position under generally accepted accounting principles. Under Governmental Accounting Standard Number 68 (GASB 68), employers with defined benefit programs are required to perform an actuarial valuation and report certain information on their financial statements. Conducting routine actuarial valuations is also best practice under the Government Finance Officers Association (GFOA) Committee on Retirement Benefit Administration best practices.

The primary purpose of a periodic actuarial valuation is to determine a recommended contribution amount for a Defined Benefit (DB) pension plan. Because DB plans define the ultimate retirement benefit, a series of contributions is calculated which would fund the DB plan over an appropriate period of time.

FPPA contracts to perform actuarial valuations of all of the affiliated Plans every two years, and all Plans that apply for state assistance are required to provide actuarial valuation information every two years. In Calendar Year 2015 there were 210 Plans that received state assistance. All of the Plans administered by FPPA and all 5 of the individually administered plans we reviewed complied with these requirements and best practices. Biennial actuarial valuations can continue to be the appropriate basis and are consistent with GFOA best practices.

Contributions

It is a shift of costs onto future taxpayers if volunteer firefighter departments do not make appropriate contributions to their Plans. It is also considered actuarial best practice for organizations to make contributions to their Plans at least at the level of an actuarial required contribution (ARC) which includes the normal cost (value of the benefits earned), plus an amortization of the unfunded actuarial accrued liability. In other words, a Plan that is fully funded only needs a contribution sufficient pay each year's pensions while a Plan that is

underfunded needs a contribution sufficient to pay each year's pension plus enough to get the Plan fully funded by some future time (often 20 years). Under the current structure, each volunteer department contributes based on the millage, and may also receive state funding.

There is no statutory requirement that the local governments make contributions based on those actuarial valuations or their ARC, as described above. While FPPA Plans are required by statute [Section 31-31-705(2)(d), C.R.S.] to perform periodic actuarial valuations, there is no such requirement for non-FPPA Plans, although all Plans or their sponsors who report under GASB 68 are required to have periodic actuarial valuations. While many Plans are being funded (through a combination of local contribution plus state contribution) at a level at least as great as their ARC based on their benefit level, we found that 14 of the 174 FPPA affiliated Plans (8 percent) did not receive contributions at that level in Calendar Year 2015 (although 7 of these 14 received 89% or more of the actuarially determined contributions). The failure to make adequate contributions can lead to poorly funded Plans.

FPPA and the Department provided us with actuarial information for all 174 of FPPA-affiliated Plans. This includes actuarial calculations based on the Plans' actual benefit levels and based on a benefit level of no more than \$300/month. The information for a \$300/month maximum benefit were provided because the General Assembly uses this benefit amount as a threshold for determining the amount of the state contribution. The following table compares the funded status of all FPPA affiliated plans based on a benefit level of no more than \$300/month with the status based on the actual benefit levels each plan offers. The calculations show that the majority of plans (more than 80 percent) would be fully funded or overfunded if they paid benefits of no more than \$300/month, but fewer than half (47 percent) are fully funded or overfunded at their actual benefit levels. As discussed in the next section: *State Funding Assistance*, almost 90 percent of all the Plans receive some state assistance but the following tables show, the vast majority of both FPPA and non-FPPA plans would be fully funded or overfunded if they paid a benefit of no more than \$300/month. Currently, 111 of the 235 plans (47 percent) provide a benefit of more than \$300/month. Of these, 88 are FPPA Plans and 23 are non-FPPA Plans.

TABLE 3.

FPPA Affiliated Volunteer Pension Plans ¹		
	Based on lesser of \$300 benefit or actual benefit level	Based on actual benefit level
Number of Plans fully funded or overfunded	143 (82%)	81 (47%)
Number of Plans underfunded	31 (18%)	93 (53%)
Number of Plans less than 80% funded	n/a	63 (36%)
Number of Plans less than 50% funded	n/a	9 (5%)
Source: Based on data provided by the Fire and Police Pension Association and the Department of Local Affairs.		
¹ There were 174 volunteer pension plans affiliated with FPPA in 2015.		

For the 61 non-FPPA Plans, the Department provided consolidated actuarial information based on the lesser of their current benefit level or a \$300/month benefit level. In 2015, all of these Plans received combined local and state contributions of at least the lesser of their \$300-level ARC or their actual-benefit-level ARC. However, the data provided by the Department does not allow us to determine whether they are funded at their actual-benefit-level ARC if their benefits are above \$300/month. The funded status for these plans is shown below.

TABLE 4.

Non-FPPA-Affiliated Volunteer Pension Plans ¹	
	Based on lesser of \$300 benefit level or actual benefit level
Number of Plans reported	61
Number of Plans fully funded or overfunded	53 (87%)
Number of Plans underfunded	8 (13%)
Source: Based on data provided by the Department of Local Affairs.	
¹ There were 61 volunteer pension plans that were not affiliated with FPPA in 2015.	

Of the 93 FPPA Plans which were underfunded at their actual benefit levels, we find that the total unfunded liability is \$37 million, giving them an average funded ratio of 73%. Because of the large number of Plans which are fully funded or stronger, the overall aggregate funded ratio for all FPPA Plans is 92%. However, the FPPA states in its Comprehensive Annual Financial Report (Financial Report), “Each employer participating in the system is financially responsible for its own liabilities. Accordingly, the aggregate numbers ... are indicative only of the overall condition of the system and are not indicative of the status of any one employer.”

State Funding Assistance

Until 1978, all fire and police pension funds, both paid and volunteer, were administered and funded by local governments. A 1977 study conducted by the General Assembly found that all of the plans in total were underfunded by over \$500 million. In 1978 and 1979, the General Assembly adopted legislation to reform the pension system. The purpose of the reforms was to help facilitate all local pension plans, both paid and volunteer in becoming actuarially sound, and included state financial assistance conditioned on increases in both employer and employee contributions for paid plans and increases in volunteer firefighter department contributions for volunteer plans. These reforms also allowed volunteer plans to affiliate with FPPA to relieve some administrative burdens.

Currently, state funding assistance for volunteer firefighter departments is based on two formulae under Section 31-30-1112, C.R.S., as follows:

- A. For those Plans with benefit levels of \$300 per month or less, the State contribution is the lesser of:
 - a. 90% of the amount contributed by the local government in the prior year, and
 - b. One-half mill of the previous assessed valuation.
- B. For those Plans with benefit levels of more than \$300, the State contribution is the lesser of the amount determined for Plans with benefit levels of \$300 per month or less as described in (A) above, and the greater of:
 - a. The actuarially required contribution for a \$300 benefit, and
 - b. The highest annual contribution provided by the state during calendar year 1998, 1999, 2000 or 2001.

In 2015, the majority of the Plans (210 of the 235 or 89 percent) received some state assistance. The statutory formula suggests that State funding support is based on a combination of the amount necessary to fund benefits up to \$300 and at a level consistent with that provided from 1998 to 2001. Our analysis finds that 86 volunteer firefighter departments receive state funding based on the state's contributions in the 1998-2001 period, irrespective of the need for state funding support for \$300 benefits. Of the 196 Plans (143 FPPA administered + 53 locally administered) that are fully funded or overfunded at the \$300 per month benefit level, as shown in the tables above, 183 receive state assistance. Of those receiving state assistance, 68 (37 percent) have improved benefits beyond the \$300 threshold with the State sharing nearly half the cost. The General Assembly may wish to consider whether it is an appropriate use of State funds to provide financial assistance to Plans that offer more than a specified amount, such as \$300 per month.

Each Plan that desires State funding must provide the Department with actuarial calculations including the ARC of the Plan if it provided benefits at the \$300 per month (for 20 years of service) level. In the discussion below, we will refer to this figure as the “\$300-basis-ARC”. As previously discussed, an ARC is the actuarially determined contribution to the Plan, which is the “Normal Cost” or value of benefit earned, plus a payment toward the unfunded liability. The unfunded liability is the shortfall of assets to the actuarial liability, or amount of prior Normal Costs which should have accumulated. So the \$300-basis-ARC is the actuarially calculated amount that would need to be contributed to a Plan to maintain benefits at the \$300 level, based on the assets in the Plan and the value of \$300 per month benefits. For most of the Plans, this number is zero or a negative number. A negative ARC means that the Plan is so well funded that an amortization of the surplus exceeds the “Normal Cost” of the benefits being earned in the year.

Based on data from the Department, we found the following key information for calendar year 2015:

1. 216 Plans report their \$300-basis-ARC to the Department
 - a. 183 of these have a \$300-basis-ARC of zero or less (meaning that no contribution would be necessary to provide for a \$300 per month benefit).

- b. 33 have a positive \$300-basis-ARC. In other words, at most 33 Plans would be underfunded if their benefit levels were limited to \$300. The actual benefit amounts for these 33 Plans range from \$350 to \$900 with an average of \$451.
2. 210 of the 235 total Plans reviewed are receiving State funding
 - a. The total state funding was \$4.1 million for calendar year 2015.
 - b. Most of that \$4.1 million is being paid to Plans for amounts in excess of the \$300-basis-ARC, as illustrated in the next two numbered items.
3. If the state were to limit the state funding amount to the \$300-basis-ARC, the state funding would fall by \$3.6 million to \$536,000 per year.
 - a. Only the 33 Plans with a positive \$300-basis-ARC would receive state funding.
 - b. This is comparable to eliminating provision (B)(b) in the state funding formulae above
4. If the State were to limit the state funding further so that the State would only match 90 percent up to the amounts necessary to fund the \$300-basis-ARC, the state funding would fall by a further \$202,000 to \$334,000.
 - a. Only the 33 Plans with a positive \$300-basis-ARC would receive State Funding, and only the amount necessary to pay that \$300-basis-ARC
5. If the State were to limit the state funding so that the combination of the amounts were designed to fund the current-basis-ARC (i.e., the ARC calculated based on the actual benefit level provided by the plan), the state funding for FPPA Plans would fall by nearly \$1 million from \$2.9 million to \$2.0 million
 - a. The Department does not collect data on the current-basis-ARC. So this data for the non-FPPA Plans was not available.

If the only goal for state funding is to provide a 90% match as necessary to fund a \$300 Plan, then the approach identified in #4 above would be appropriate. Some examples may clarify the situation.

- Plan A has a benefit level of \$700 per month, but is overfunded with a negative \$300-basis-ARC of \$695,000. In other words, at the current time, the plan has assets that are \$695,000 more than are needed to cover its existing pension obligations. Based on the current formula, however, which uses the volunteer firefighter department's 2000 state funding level, the department is making contributions of \$55,000 and receiving 90% matching funds of \$49,500.
 - At this strong funding level, the department might be able to afford to increase its benefit well above \$700 at no additional cost to the department.

- Plan B provides \$1,400 per month. It was overfunded at the \$1,400 level with assets of \$1.7 million and liabilities of \$1.1 million. As a result of the overfunding, the ARC for \$1,400-per-month benefits was only \$4,500 per year, while the \$300-basis-ARC calculation would not require any department contribution.
 - Despite the large overfunded position, the State is matching the \$3,500 department contribution with \$1,200 contributions based on the current formula which uses its 2001 payment. This resulted in total contributions of \$4,700, slightly more than the \$4,500 ARC.
 - This year, the contribution requirement has increased to \$14,000, (due to a year of reduced investment income), but the state funding will remain at \$1,200, meaning that the department will need to fund nearly \$13,000 in order to maintain actuarial soundness.
 - Although the state funding levels are small for this small department, the Plan is so overfunded that this Plan provides an illustration of why the State may wish to change policies to not provide state funding for Plans that pay benefits over the \$300 in statute and that are fully funded or better.
- Plan C is nearly \$1 million under-funded with benefits at a level of \$400. Assets are \$1.8 million and liabilities are \$2.7 million for a funded ratio of 66%. The \$400-basis-ARC was \$122,000 while the \$300-basis-ARC is \$92,000. The department contributed \$123,000 while the State contribution was \$92,000.
 - This department has kept benefit levels modest
 - This department is maximizing state funding by making a contribution large enough that the state is funding its full \$300-basis-ARC even though the combination of the department's contribution and the state match is more than its benefit-level-ARC.
 - This department's 1998-2001 maximum contribution was only \$36,000
- Plan D is only 60% funded and has closed its Plan to new members. Its benefits are \$615 per month. The \$615-basis-ARC was \$250,000 and its \$300-basis-ARC is less than zero.
 - This can be considered intuitively: If a Plan has 60 cents for every dollar of \$615 liabilities, it would have 60 cents for about 50 cents of \$300 liabilities. So it is overfunded on a \$300 basis, but only 60% funded on a \$615 basis.
 - This department last year contributed \$120,000, with the State contributing \$78,000 based on the 2001 contribution levels.
 - These contributions are \$56,000 short of the actuarially required contribution, totaling only 78% of that amount.

Conclusion

Our analysis finds that of the more than \$4 million paid by the state in the form of assistance to volunteer Plans, more than \$3 million goes to Plans which do not have an actuarially required contribution based on a \$300 benefit level. This suggests that most of the state funds are going toward Plans which are more than fully funded on a \$300 benefit basis.

Many of these Plans have improved benefits over the years. If this is not consistent with State objectives, it may be appropriate to phase-out or eliminate the provision which allows volunteer firefighter departments to continue to receive state funding for benefit levels at the amount specified in statute.

D. Administrative Issues

Implications of GASB 68

Under Governmental Accounting Standard Number 68 (GASB 68), employers with defined benefit programs are required to have an actuarial valuation performed and report certain information on their financial statements. GASB 68 addresses reporting by employers. Each employer is required to report pension costs and liabilities. Whether local Plans are separate or combined, the locality is required to report specific actuarial values relative to their specific Plan. Where GASB 68 does generate additional administrative costs on separate local Plans as opposed to combined Plans in large part, is the requirement that each Plan have an audit report of the census data controlled by the plan, including verification that internal controls are suitably designed and operating effectively. This cumbersome reporting would be significantly reduced if plans are combined.

Coordination of Benefits

Under current Colorado Law, volunteers who move from one volunteer firefighter department to another may receive a combined benefit based on service from both departments. This requires a specific calculation to determine the combined benefit. For FPPA Plans, the records from prior departments are maintained and the calculation can be performed or reviewed by FPPA. For non-FPPA Plans, the burden is on the retiring firefighters to alert their current and prior departments if they believe they should have benefits from both departments.

Each department has a unique defined benefit Plan with unique costs and benefits. When a volunteer moves from one department to another, benefit calculations can be somewhat complex and actuarial calculations can be even more complex, in order to properly assign costs to each employer.

Based on current FPPA data, 21 of 3,916 of those currently receiving benefits (less than 1%) had portable service, meaning that they have moved among departments. Additionally, 221 out of 4,320 volunteers who are not currently receiving benefits (5 percent) have portable service. Of the 221 not yet receiving benefits, 156 are still active volunteer firefighters and 65 are no longer active volunteer firefighters. 24 of these 65 who are no longer active are waiting to attain age 50 to begin collecting benefits, while the remaining 41 do not currently qualify for a benefit but

FPPA is retaining their records in case they later join a department and get enough service to qualify for a benefit.

There is no data available on the specific administrative costs of tracking volunteers with portable service because it is not tracked as a separate administrative cost. However, it is certainly an administrative burden. For example, FPPA has indicated that the major problem from an administrative perspective is that even though only 21 volunteers are currently receiving benefits based on portable service, every single volunteer who terminates with five or more years must remain monitored in perpetuity in case he or she returns to another department. Complying with this law requires cumbersome processes, including more complex actuarial systems, even though a very small number of firefighters will ever benefit from the provisions.

Under a DC approach, the calculation would be very straight-forward: the benefit is simply based on the account balance and the annual contribution from each employer. This would be the most transparent and equitable manner of coordinating benefits with very little in terms of administrative costs. The only other solution would be to have a single administrated Plan which would alleviate some of the administrative burden by making it easier to track volunteers when they move between departments and allow for simpler actuarial calculations.

Administrative Costs

State contributions for calendar year 2015 were \$4.1 million; local employer contributions were \$9.8 million. FPPA Plans had annual state and local contributions of \$2.9 million and \$7.6 million respectively, for a total of \$10.5 million. According to its 2015 Financial Report, FPPA's total administrative costs charged to volunteer Plans were \$460,000. This means that the total administrative costs for FPPA Plans are only about 4% of the annual costs of the program. It is likely that the administrative costs of the non-FPPA Plans would be higher proportionately because they do not have the economies of scale of a multi-billion dollar pension fund.

Some of the common administrative costs associated with the Plans include those for tracking beneficiaries, complying with regulatory requirements, and maintaining records. Costs for these activities will be incurred whether separate Plans are maintained or Plans are combined but the use of a central administrator such as FPPA could limit the costs because it can more efficiently establish procedures for each of these critical tasks. FPPA's administrative costs for affiliated volunteer Plans averages 0.3% of year-end assets, or \$66 per participant. Although the actual costs charged by FPPA to each Plan it administers varies based on assets, special services requested, and number of participants, it is safe to conclude that such administrative costs are much lower than would be borne by separate self-administered Plans. For example, one self-administered Plan for which we had actuarial valuation information had total expenses of 0.6% of Plan assets, or \$175 per participant, more than twice the average for FPPA Plans.

Maintaining a local pension board is another function that creates some administrative costs that could likely be reduced if local Plans were abolished. For FPPA Plans, the administrative cost of a local board is generally low because the local board has outsourced Plan administration and investment authority to FPPA. Non-FPPA plans have made a conscious decision that they want local control more than administrative savings from using FPPA. However, the local board is made up of volunteers. The only administrative costs are typically borne by the local department

and board meetings are often held in tandem with other volunteer firefighter administrative functions. So while the costs are certainly borne, they are not specifically allocated to the pension fund. Actuarial valuation costs are typically about \$5,000 to \$10,000 per biennium. Although it would be reasonable to expect that non-FPPA all-in administrative costs are well above the 0.3% of assets/ \$66 per head FPPA costs, the amounts may still be small enough to not be of concern to the departments. There are likely other benefits of including pension duties for the board members. Particularly for the departments who have not elected to join FPPA, these may include:

- Greater involvement and understanding of the recruiting and retention benefits of the pension program
- Interest in and appreciation of the investment management aspect of pension funds
- Appreciation and understanding of the impact of the pensions on the department finances

In addition to the likely higher minor administrative costs of the local board, two disadvantages arise. One is the potential for inappropriate financial activities. Although well beyond the scope of this study, any time there is a separate pool of assets, there is some potential for failure to act in accordance with fiduciary standards. We have seen no evidence of such behavior and in our experience, such activity is rare. Because of the small size of the volunteer pension Plans relative to the department budgets, the incentive for such malfeasance is low.

A second disadvantage is that small locally administered pensions will likely have lower long run investment returns than a large sophisticated fund such as FPPA. This is because larger funds:

- (1) have economies of scale which drive down fees,
- (2) have access to asset classes which are expected to have higher risk-adjusted returns, and
- (3) have more sophisticated investment professionals on staff.

Another reason that FPPA plans would tend to have higher investment returns is that under the Pension Act [Section 31-30-1113(3) C.R.S.], locally administered Plans are subject to strict restrictions regarding investments that do not apply to FPPA plans.

Studies of public pensions generally demonstrate this correlation between size and investment performance. One such study, by researchers from the University of Toronto, found that larger plans outperformed smaller ones due to efficiencies in management and greater latitude in investment decisions.

Section II: Plan Design Implications

Section II discusses alternative structures for providing pension benefits to volunteer firefighters in Colorado. We discuss in Section II the frequency of actuarial valuations that would be needed for each alternative and the degree of employer contribution that might be required.

Alternatives to the Current Structure of Maintaining Separate Local Defined Benefit Plans

In weighing alternatives to the current structure of Pension Act Plans in Colorado, policy makers should give consideration to the objectives of a volunteer pension benefit in light of the changing nature of volunteer service. Depending on their firefighter needs, there may be a desire to revise the 10 to 20 year service requirements as well as consider different structures. It is important that departments balance the recruiting advantages of a program with short vesting with the retention advantages of a program with longer vesting requirements.

Incentivizing and Retaining Younger Volunteers

Younger volunteers (and younger workers in general) are more mobile, from both a geographic and occupational standpoint. Accordingly, consideration should be given to how the following structural elements may incentivize and retain such volunteers while facilitating more efficient and cost-effective administration:

- Defined benefit (DB) vs. defined contribution (DC) structure. DB gives the security of a life-long income stream but only to long-serving volunteers, therefore prioritizing retaining current volunteers. DC plans, in the form of a Length of Service program, tend to have shorter vesting periods which would incentivize new volunteers even if they are more mobile. The DC option would need to be in the form of a Length of Service program because a traditional DC plan cannot be established for volunteers. Specifically, the IRC limits contributions to a traditional DC plan to *the lesser* of (i) \$53,000 or (ii) 100% of the employee's compensation. In operation, the volunteers have no compensation and therefore the applicable dollar limitation would be \$0. However, the \$3,000 Length of Service program limit might make a DC approach less viable for a department that needs to provide benefits at a higher level. The value of benefits under DC plans is very transparent as compared to DB because the value of a volunteer's DC account is always known. Additionally, studies show that individually directed DC plans tend to have investment returns about 1.0% per year lower than professionally managed pooled DB plans. Investment return and longevity risk are borne by participant under DC and by employer under DB. In terms of administrative costs, a DC alternative would be more efficient than a DB approach, in part because no actuarial valuations are required. Also, administrative complications of DC tend to be lower, particularly when concerns for portability of benefits between departments are considered.
- Longer vs. shorter vesting periods. Shorter vesting facilitates recruiting goals because a new volunteer can be assured of some level of retirement benefit without having to commit to volunteering for 10 or 20 years. However, shorter vesting can hamper retention goals because volunteers can leave at any time after they are vested without forfeiting retirement benefits. Further, shorter vesting periods are more expensive because more volunteers are likely to end up receiving benefits.

Employer Concerns

In general, employers who have an emphasis on retention will tend to prefer a DB approach, while employers who have more needs for recruitment would prefer a DC approach. Similarly,

recruitment suggests a shorter vesting requirement, while retention would be consistent with a longer vesting period such as the 10- or 20-year vesting options available to the Plans currently. Finally, it is important to also consider that although these Plans are characterized as pensions, it would be expected that the volunteers are saving separately for retirement based on their earned income. These levels of benefits are not adequate for a meaningful retirement benefit.

Other Concerns

- Individual Plan administration vs. state-entity administration. Individual Plan administration allows for local control over fund investments but requires that local Plans be able to provide actuarial studies and track volunteers who may have served multiple departments. State-entity administration has cost benefits and provides for centralized actuarial services and tracking of benefits. If a pooled plan alternative is implemented, then all departments would share in the cost of the new the plan, and those which continue to maintain a frozen Plan would have an additional actuarial valuation to determine their costs and liabilities. The actuarial valuation for a pooled cost-sharing multiple-employer plan would allocate costs and liabilities based on the value of the monthly benefit provided and number of active and retired firefighters on a unitized basis. If there were a cost-sharing multiple employer plan, the costs would be less because the benefit calculation and recordkeeping is more simple. However, it is still necessary to properly assign actuarial costs to each department.
- Maintain, freeze or terminate existing Plans. Some of the options below would require that current Plans be frozen and/or terminated. Maintaining current Plans would limit the options available for improving the pension system.

Strong preferences on these items will determine the best alternative or combination of alternatives to be implemented. We note in advance that these alternatives are designed to mitigate the risk of non-compliance with IRC tax-qualification issues requirements. For each alternative, however, there remains some risk with respect to the previous years of non-compliance. Additionally, it is possible that a volunteer could raise a challenge to any proposed alternative that arguably represents a diminution in the rate or manner in which benefits are accrued.

The above notwithstanding, aside from item D below, none of these alternatives would necessarily require changes that would affect the contribution levels required by Plans or the level of benefits paid to current volunteers and retirees. Additionally, with the exception of the Length of Service option (item B below), issues such as state funding and actuarial funding requirements can be resolved in ways independent of the structure chosen.

A. Adoption of Master and Prototype Plan Document under a Central Administrator

The first option would be the adoption of a master and prototype “volume submitter” plan document and submission of same to the IRS. This alternative would bring the existing local Plans into compliance with the IRC documentation requirements and would require all Plans to be centrally administered (i.e., similar to the current FPPA affiliated Plans). Under this option, the General Assembly would need to assign responsibility to a sponsor organization, such as

FPPA, to become the sponsor and administrator of a master and prototype program which each local government or district could join for purposes of establishing its qualified pension Plan. The sponsor organization would adopt a “base plan” document and each participating entity would complete an “adoption agreement” detailing the terms of its individual Plan. The base plan document and the adoption agreement would each be drafted consistent with the terms of the Pension Act and contain all necessary tax compliance language.

The sponsor organization would file to secure an advisory letter ruling on the documents from the IRS. This would assure that any entity that adopts the documents would have Section 401(a) tax qualified status for its Plan.

If the state chose to sponsor and administer a master and prototype program, the IRS application fee for the required advisory letter would be \$16,000 for the base Plan plus an additional \$11,000 for each adoption agreement. Additionally, the documentation of the base Plan and adoption agreement(s) could range in cost from \$75,000 to \$125,000. Lastly, there would be some administrative burden in transitioning all plans to the sponsor organization.

As part of this option, the sponsor organization could contract with a vendor to maintain the tax-compliant master and prototype volume submitter documents. While such vendors often require determination letters before accepting new Plans, a vendor, particularly those focusing on the governmental plan sector, may be willing to accept a group transfer without an existing determination letter.

Advantages

There would clearly be administrative cost savings resulting from the uniform and centralized administration of the Plans. The unitized plans, items C, E, and F below, would have most of the same efficiencies.

Disadvantages

The Pension Act Plans collectively represent “low asset, high participation” Plans. Such Plans are not particularly attractive to outside vendors. Moreover, the transition costs assessed by an outside vendor to duplicate over 200 individual Plans could make this infeasible. A vendor may be more willing to accept the Plans if the current Plans were “frozen” and it were only responsible for future operations and benefit accruals.

It should be noted that unless legislation made adoption of the master and prototype mandatory, it is likely that some non-FPPA Plans would continue to be out of compliance with IRC. This master and prototype approach does not affect the fundamental Plan design or actuarial funding, although changes to these areas could be addressed within the same legislation.

Lastly, with this approach, there is some risk that the IRS, in reviewing the filing, could inquire regarding the “current” tax qualified status of the Plans. As such, there is some risk that the IRS would threaten action against the individual entities operating non-compliant Plans for the period prior to the adoption of the master and prototype Plan form.

Alternative A:	
This alternative develops or makes available a “Master and Prototype” plan document that each volunteer firefighter department would adopt. Plans would be pooled and managed by a state entity such as FPPA (pursuant to its own master and prototype document) or an outside vendor (pursuant to the vendor’s master and prototype document). There would be an IRS advisory letter filing if the master and prototype is developed by the state.	
Would this alternative combine the Plans funds or administration?	Plans would be combined for administrative purposes.
Would this alternative maintain local control over benefit levels?	Yes
Would this alternative: <ul style="list-style-type: none"> • Address IRC compliance issues? • Affect Plan funding? • Affect administrative costs? 	This alternative would significantly address IRC issues as the documents would be reviewed and approved by the IRS. It would not affect the funding of the Plans. Administrative costs of the Plans would be expected to increase if a private vendor is used.
Would this alternative require contributions or benefits to change?	No

B. Length of Service Plan Under Section 457(e)(11)

Under this alternative, benefits payable under Pension Act Plans would be converted to Length of Service programs (commonly known as LOSAP) under Section 457(e)(11) of the IRC. Section 457(e)(11) of the IRC provides that a Length of Service program may be established for volunteers who render service in an emergency employee capacity. Section 31-30-1203(2), C.R.S., includes language allowing for the establishment of a Length of Service program by a governmental body. Because Length of Service programs are not subject to IRC Section 401, the current qualification deficiencies under 401 would no longer be of concern.

Currently, the Pension Act does not provide for state funding of a Length of Service program. If the Plans were converted to Length of Service programs, the Pension Act could be amended to authorize state contributions to supplement local funding. It should be noted, however, that a Length of Service plan will not satisfy Section 457(e)(11) of the IRC if “the aggregate amount of accruing with respect to any year of service for any bona fide volunteer exceeds \$3,000.” Section 457(e)(11)(A)(iii) of the IRC.

Although Length of Service programs are designed to be DC plans, they can also be structured as defined benefit plans. The current Pension Act Plans are structured as defined benefit plans. Therefore, the Length of Service program limit of Section 457(e)(11) has to be converted to a defined benefit rate of accrual if the DB structure is to be maintained. As noted above, we have concluded that the \$3,000 limit in the IRC converts to a life annuity of approximately \$650 per month or \$7,800 per year. Since 14% of the Plans currently offer a monthly benefit in excess of \$650, this alternative would not be viable for those Plans. Moreover, the dollar limit in the IRC is not indexed for inflation. Therefore, converting to Length of Service programs may make it more

difficult over time to provide substantial benefits. Many volunteer firefighter departments have increased their DB benefit levels partly due to inflation. This is not possible with Length of Service programs above \$3,000.

A variation on this alternative would be to convert past benefits to a Length of Service program and for future benefits to accrue as a defined contribution Length of Service program. In this case, the accrued benefit under the existing Plans would be converted to its actuarial single sum equivalent. As long as this is consistent with the actuarial equivalent of a career of \$3,000 Length of Service program contributions, the benefit should comply with Section 457(e)(11) of the IRC. Regardless of form, if the Length of Service program approach is pursued, the enabling legislation would need to specifically expand state funding to these Plans and provide for them as an alternative.

This discussion contemplates Length of Service programs designed and administered either individually by each department, or by a central organization, such as FPPA, if there is a desire for central state administration. The transition from a DB approach to DC approach is complex, requiring actuarial calculations, particularly for plans which offer benefits in excess of the \$650 per month DB actuarial equivalent to a \$3,000 DC accrual.

Advantages

One advantage of the Length of Service program approach is that in the long run it greatly reduces the administrative complexities. Under the Length of Service program alternative, no actuarial valuations would be necessary because contributions are defined and do not need to be calculated based on future benefits. Additionally, there would be no need to track portable service because Length of Service would only apply to individual employers. Shorter vesting periods are more common in Length of Service programs and other DC plans than in DB plans. As discussed above, a shorter vesting period could help address recruiting issues.

Another advantage is that all Plans will always be 100 percent funded and there will be no unfunded liabilities. For those Plans that provide benefits of less than \$650 per month, the Length of Service program characterization would eliminate the need to comply with the tax qualification rules for the previously accrued benefits.

Disadvantages

Distribution options under a Length of Service program may not be as favorable as those under traditional qualified Plans. For example, rollovers would not be permitted. Also the IRC appears to prohibit a Length of Service program from allowing multiple distribution forms (e.g., lump sum or annuity) without adverse tax consequences. Additionally, as with all alternatives discussed herein, there remains some risk that the IRS could challenge the tax qualified status of the Plans prior to the Length of Service program conversions. Finally, this approach must be used in connection with one of the other alternatives to address those Plans with benefits in excess of \$650 per month. Thus a single entity could be required to operate a Length of Service program for accruals of less than \$650 per month and run a parallel DB for amounts in excess of \$650. The parallel DB would be necessary because only the DB structure allows for benefits in excess of \$650 per month.

Alternative B:	
Converts all plans to a DC approach through a Length of Service program, which qualifies under section 457(e)(11) of the IRC rather than 401.	
Would this alternative combine the Plans funds or administration?	Plans could be administered separately or centrally, similar to the current framework.
Would this alternative maintain local control over benefit levels?	Yes
Would this alternative: <ul style="list-style-type: none"> • Address IRC compliance issues? • Affect Plan funding? • Affect administrative costs? 	This substantially resolves IRC issues. Plan funding could be structured to be similar to current funding practices. Administrative costs and complexities would be reduced.
Would this alternative require contributions or benefits to change?	Yes. For those with benefits above \$650, either a supplemental DB plan would have to be implemented, or benefits would be reduced.

C. Convert all Pension Act Plans to a Single DB System Administered by a Central Organization

Under this alternative, the various Pension Act Plans would be merged into a single defined benefit “system” operated by a central organization. The Pension Act could be amended as necessary to allow for single system funding by the State, municipalities, and districts. The central administrator may then elect to pursue a single determination letter from the IRS for a “system-wide” Plan.

In instituting this alternative, one decision that would have to be made by policy makers would be whether to offer local governments full flexibility in determining their benefit levels or whether benefit levels would be limited to certain pre-defined tiers. For example, the single Plan could only offer benefit tiers of \$300, \$600, \$900, and \$1,200. Limiting employer options to only certain defined tiers could improve the administrative efficiency for the central administrator. If structured properly, the “cost” for the elected tier can be unitized and the funding required at each tier can be actuarially calculated. A unitized basis means that benefits and employer costs are in terms of units. The central administrative organization will determine an annual actuarial cost per unit. An employer which provided benefits at the \$600 level would have twice as much cost (and benefit) as one which provided benefits at the \$300 level.

This approach is somewhat similar to the approach taken by the state of Minnesota. The Public Employees Retirement Association of Minnesota operates a multiple employer plan that covers over 700 individual volunteer firefighter plans. The plan is documented via a single state statute that received a favorable determination letter from the IRS in 2012. The plan provides for multiple benefit formulas ranging from \$500 to \$7,500 per year of service as selected by the individual municipality. We have been unable to locate any other similar state-wide programs for volunteer firefighters.

Advantages

A single merged system should be easier to administer, and the central administrator could pursue a determination letter from the IRS which would solve the IRC issues.

Disadvantages

There could be significant policy concerns. Such a system, commonly referred to as a “cost-sharing multiple employer plan,” requires that all assets contributed by the multiple employers be available to pay the benefits accrued by any retiree. There are significant disparities in the funded status of the individual Plans. There may be ways to address this policy concern, such as modifying statute to reallocate the state funding subsidy in a manner that levels out the deficiency of the lesser funded Plans. However, unless there is required leveling of the funded status (either by state or mandated local government contributions), certain Plan sponsors would be “subsidizing” the funding deficiencies of other sponsors. Moreover, even if the Plans were merged, the IRS could still challenge the tax-qualified status of the Plans prior to the merger.

Alternative C:	
All plans would merge. The merged plan would be IRS compliant, and may choose a determination letter filing.	
Would this alternative combine the Plans funds or administration?	The plans would be combined.
Would this alternative maintain local control over benefit levels?	Yes, but limited.
Would this alternative: <ul style="list-style-type: none"> • Address IRC compliance issues? • Affect Plan funding? • Affect administrative costs? 	This addresses IRC issues and would likely reduce administrative costs following transition.
Would this alternative require contributions or benefits to change?	To a limited extent both contributions and benefits might change based on the options in the tiered structure of the plan.

D. Privatization – Annuitize Current Benefits through a Private Vendor

Under this approach, each Plan would solve its tax qualification issues by purchasing benefits from a private sector vendor such as an insurance company or investment company specializing in public pensions (a practice commonly referred to as “annuitization”).

If this alternative were selected, it may be worthwhile for the General Assembly to charge a state entity to do the research of finding appropriate private sector vendors. It would probably be more cost effective to have each of the Plans choose one of the selected vendors rather than give them each a full choice. However, the volunteer firefighter departments may prefer to have local authority to choose their own vendor.

Advantages

The main advantage of this approach is that it would eliminate any administrative complexity associated with the current structure by transferring responsibility for tasks such as GASB 68 compliance and tracking retirees to a vendor

Disadvantages

The primary disadvantage is cost. Actuarial liabilities would generally increase by 20% or more, because the private vendors would not expect to have earnings as strong as FPPA Plans or even many of the non-FPPA Plans, due to their restrictions on investments imposed on insurance companies. In addition, the private vendors need to be compensated for their administrative services and the risks which they bear.

The total actuarial liability for FPPA Plans is currently \$186 million. We roughly estimate the liability would increase by at least \$40 million if this approach were taken. In other words, for this approach to work, and annuities to be purchased, at the time of transition to this alternative, the volunteer firefighter departments would need to come up with an additional \$40 million plus whatever unfunded liabilities currently exist. Moreover, these costs would only fund the benefit liabilities accrued to date. The state would still have to adopt one of the other alternatives for future accruals. Accordingly, we did not make detailed estimates as this would appear to be a cost-prohibitive alternative for the Plans and the State.

Alternative D:	
This alternative requires each volunteer firefighter department to purchase annuities from the private market for benefits accrued to date plus benefits earned each year.	
Would this alternative combine the Plans funds or administration?	Plans can remain separate.
Would this alternative maintain local control over benefit levels?	Yes.
Would this alternative: <ul style="list-style-type: none"> • Address IRC compliance issues? • Affect Plan funding? • Affect administrative costs? 	<p>This option addresses IRC noncompliance. All Plans would have to be fully funded at the time of transition, requiring a substantial upfront investment.</p> <p>Administrative complexities are borne by the private sector, but at a higher cost to the Plans.</p>
Would this alternative require contributions or benefits to change?	Contribution costs would likely increase to cover higher administrative costs.

E. Adopt a Traditional Defined Benefit Plan with an “Offset” Formula (Umbrella Plan)

Another alternative is to adopt a new state-sponsored agency multiple employer defined benefit pension plan via statute (the “New Plan”) with a “traditional” defined benefit formula that includes all of the pertinent tax qualification language. The New Plan would be sponsored and

solely administered by a central organization but funded by the individual municipalities and limited state contributions. Similar to alternative C above, the statute could permit all municipalities to elect from pre-determination formula tiers rather than allowing the local government unlimited discretion to design benefit formulas. Moreover, the statute could impose limitations on the available tier based on the funded status of the local government's current Plan.

The current individual Plans would be frozen ("Frozen Plan") so that there would be no additional accruals or new participants as of the freeze date. The New Plan's accrued benefit formula would take into account all of the volunteer's service with the local government. However, the benefits paid under the New Plan would be "offset" by the benefit accrued and paid under the Frozen Plan. This means that the new umbrella multiple-employer plan will essentially be providing benefits on a future or prospective basis only. The actuarial costs would be based on that assumption which facilitates a continually fully-funded Plan with costs primarily based on the benefit accruals only with minimal past-service cost. Such costs would be consistent with the current Normal Costs that the individual Plans are bearing.

There are multiple potential design formulas, such as:

New Plan Benefit =

(Total Years of Service times Multiplier) minus Frozen Accrual Benefit

or

New Plan Benefit =

**[(Years of Services under New Plan times Multiplier) + (Greater of:
Years of Service under Frozen Plan times Multiplier, or Frozen Accrued Benefit)]
minus Frozen Accrued Benefit.**

There are pros and cons of each benefit formula that would need to be weighed before selecting one.

Advantages

The advantage of the New Plan approach is that a single uniform Plan can be created or authorized by statute that (1) allows for the standardization of administration; (2) incorporates necessary tax qualification language and can therefore receive a favorable determination letter from the IRS; (3) creates a fixed range of benefit accrual formulas that can be more easily administered; and (4) allows for eventual phase out of the various individual local Plans.

The last point is particularly significant in that any alternative based upon the continuance of the current Plans will have some risk of tax disqualification. While none of the proposed alternatives is perfect, a remedy that sunsets the existing Plans (rather than attempting to "fix" them) may be preferable from both a legal and administrative standpoint. From a legal perspective the IRS is less inclined to audit a frozen Plan than an ongoing active Plan. We cannot represent that the IRS would never audit the Frozen Plans; however, we do note that (1) governmental sector audits are rare, (2) we are unaware of any instance in which the IRS has audited a plan covering volunteer firefighters; and (3) the New Plan statute could apply and receive a determination letter on its tax qualified status. From an administrative standpoint, post-transition administrative costs for this

alternative should be lower than current administrative costs in part because the Plans are pooled as a cost-sharing multiple employer plan, which requires a single actuarial valuation and allows for some economies of scale in other administrative costs.

This option seems to be the most practical in terms of the objectives of:

- Complying with federal requirements;
- Maintaining the employer's flexibility to set their own benefits or providing flexibility to choose from among defined benefit tiers; and
- Minimizing administrative burden on the central organization by ultimately replacing administration of many individual Plans (i.e. 235, if all current Plans were included in the umbrella plan) with one pooled Plan, and on non-FPPA volunteer firefighter departments by shifting administration to the central organization.

Accordingly, we believe that this alternative presents the optimal solution if the desire is to remain in a traditional defined benefit format.

Disadvantages

There are several caveats to this approach. First, the central administrator would be required to administer the Frozen Plans to determine the offset amount. Because the Plans will be frozen however, the administrative burden should not be as great as with an ongoing Plan. Second, if the Frozen Plan is underfunded, the local government will be required to fund two Plans simultaneously. Third, for those Plans which are not close to fully funded, the frozen Plan will continue in force until it becomes fully funded and can buy-in to the multiple employer plan. Mathematically, the costs will be the same as under the current arrangement, with the possible exception of future administration fees of the central organization which would probably be significantly higher for the frozen individual employer Plans than for the pooled multiple employer umbrella plan.

Alternative E:	
This alternative develops a master plan document that each plan would adopt, which would provide full target benefit levels and be IRS compliant. The prior plans would be frozen and act as an offset to the target benefit levels.	
Would this alternative combine the Plans funds or administration?	The plans would be combined for funding and administration.
Would this alternative maintain local control over benefit levels?	Yes.
Would this alternative: <ul style="list-style-type: none"> • Address IRC compliance issues? • Affect Plan funding? • Affect administrative costs? 	This option lessens IRC exposure and reduces administrative costs following a transition.
Would this alternative require contributions or benefits to change?	No, but departments may wish to pay down their unfunded liabilities more rapidly.

F. Establish a “Cash Balance” DB Plan with Future Service Accruals

A final alternative is to establish a statewide “cash balance” defined benefit plan. A cash balance plan operates under many of the same principles as a defined contribution plan but is considered a defined benefit plan under the IRC. Each participant in a cash balance plan has a “hypothetical account” that accumulates annual credits. These credits are: (1) annual “principal credits” which would be a specified dollar amount for each participating employer; and (2) annual “interest credits” based upon a fixed or variable interest rate applied to the hypothetical account balance (The interest rate cannot be subject to the discretion of the employer.). Similar to the Length of Service program option, a cash balance plan would offer many of the same features as a traditional “defined contribution” plan, which cannot be established for volunteers because they have no “compensation”, as explained previously.

Cash balance plans are technically treated as defined benefit plans because the hypothetical account is a recordkeeping account only and the interest credits are fixed based on the Plan’s provisions, not the actual returns on Plan assets. At no time can the hypothetical account balance be less than the aggregate principal credits. To the extent that there is a deficiency in the principal and interest credits at the time of distribution (due to poor investment return or otherwise) the employers collectively are responsible for the deficiency. The benefit payable upon termination or retirement is the value of the hypothetical account. The following is an illustration of a typical cash balance formula calculation that could apply.

1. Opening hypothetical account balance as of January 1, 2017: \$20,000
2. Interest credit at 5% ($5\% \times \$20,000$), which is credited at the end of the year: \$1,000
3. Principal credit (as selected by volunteer fire department): \$3,000
4. Hypothetical account balance account at end of 2017 ($1+2+3$): \$24,000

Upon retirement, the hypothetical account balance may be paid as a single sum or converted to an actuarially equivalent annuity form. Because cash balance plans are classified as defined benefit plans, the only limitation on the benefits payable is the annual limit under Section 415(b), which is currently \$210,000 per year. At benefit levels comparable to those provided for volunteers, this limit is not likely to be approached.

The state legislation could contain a range of “benefit tiers” such that the individual local government can elect the level of principal and interest credits and fund accordingly.

Advantages

The cash balance plan can replace the current Plan which would be frozen or terminated. If the current Plans are terminated, the cash balance plan could allow for the “rollover” of funds from the terminated plan and then convert the rolled over amounts into additional benefits under the cash balance formula. In either case (freeze or termination) the cash balance plan would be deemed a “new” plan and could seek a determination letter untainted by deficiencies of the current Plan. This plan is similar to a Defined Contribution approach, but does not have the \$3,000 Length of Service program limit, and maintains the advantages of the Offset approach

described above. **Consequently, if there is a desire to move to a “defined contribution” type format, implementation of a cash balance plan could be the preferred option.**

Disadvantages

This approach has the same potential issues as adopting a traditional defined benefit plan with and offset formula (item E above). These include: (1) maintenance of the old Plans (unless terminated or outsourced); (2) funding of any deficiencies of the old Plans; and (3) the lingering tax-qualification defects of the current Plans.

Alternative F:	
This alternative develops a master plan document that each plan would adopt, which would provide full target benefit levels and be IRS compliant. The prior plans would be frozen and act as an offset to the target benefit levels.	
Would this alternative combine the Plans funds or administration?	The plans would be combined for funding and administration.
Would this alternative maintain local control over benefit levels?	Yes.
Would this alternative: <ul style="list-style-type: none"> • Address IRC compliance issues? • Affect Plan funding? • Affect administrative costs? 	This lessens IRC exposure and reduces administrative costs following a transition.
Would this alternative require contributions or benefits to change?	No, but departments may wish to pay down their unfunded liabilities more rapidly.