

STATE OF MINNESOTA
OFFICE OF ADMINISTRATIVE HEARINGS

FOR THE PUBLIC EMPLOYEES RETIREMENT ASSOCIATION

In the Matter of the PERA Salary
Determinations Affecting Retired and Active
Employees of the City of Duluth,

SECOND AFFIDAVIT OF MARY VANEK

OAH Docket No. 4-3600-2080902

Allen Johnson, et al., Petitioners.

STATE OF MINNESOTA)
) ss.
COUNTY OF RAMSEY)

MARY VANEK, being first duly sworn, deposes and states:

1. I am the Executive Director of the Public Employees Retirement Association (“PERA”).

2. When the City of Duluth notified PERA that it had been reporting invalid salary amounts, PERA requested payroll data from the City in order to determine the amounts of invalid salary that had been reported, as required by Minn. Stat. § 353.27, subd. 11 (2008),.

3. PERA reasonably relied upon the extensive payroll abstracts the City of Duluth submitted to PERA.

4. The Determination Letters PERA sent to the City’s active and retired employees included individual charts for each employee/retiree setting forth on a year-by-year basis the amount of invalid salary reported by the City of Duluth. The charts informed the

employees/retirees that if the dollar amounts were disputed, that the City should be contacted in order to review those figures.

5. Several Duluth employees/retirees contacted PERA to question their numbers and staff referred them to the City of Duluth. It is my understanding that only one Petitioner contacted the City of Duluth to review payroll records.

6 It is my understanding the annual amounts the City reported to PERA vary depending upon when the payments were made, taking into account unsigned CBAs, the effective dates of the CBAs, and whether the employee/retiree received higher amounts due to participation in certain of the insurance plans offered by the City.

7. If any Petitioner challenges the figures determined by the City of Duluth, there is an easy remedy. The applicable CBAs set forth the amounts of employer contributions on an annual basis. It is reasonable to assume that those contributions were made in the amounts specified in the CBAs. Consequently, instead of relying upon payroll abstracts as the statute requires, the amounts of invalid salary can easily be determined by adding the applicable dollar amounts for each Petitioner set forth in the CBAs.

8. My review of the affidavits submitted in this proceeding show that none of the Petitioners are claiming that the amounts set forth in their charts are in excess of the total amounts provided under the applicable CBAs. Instead, they challenge the amounts because they are not identical with fellow fire fighters.

9. It is not PERA's intent to determine the amounts of invalid salary based upon data that may be questioned. When the legal issues in this proceeding are determined, PERA intends to meet with any individual Petitioner who might have a concern about the figures at issue and to review those figures based upon the amounts set forth in the collective bargaining agreements.

10. Attached to this Affidavit as Exhibit 1 are selective pages from the City of Duluth's Employee Benefits Handbook, 2009. The Handbook is available on the City's website. It explains the City's insurance programs, deferred compensation and its flexible benefit accounts.

11. I was an active participant in the 1992-1995 legislative sessions relating to the PERA law. At no time during those years did PERA propose legislation specifically excluding employer contributions to deferred compensation accounts from the definition of salary. There was no need for such a bill since PERA had historically excluded such contributions from PERA salary.

12. On March 9, 2010, the Legislative Auditor issued a follow-up Report to its February 13, 2009 PERA Report. Selective pages of that Report are attached hereto as Exhibit B. Based upon its Findings that the City of Duluth had incorrectly included some employer-paid benefits in its calculation of employee base salaries, the Auditor recommended that PERA should verify that participating employers properly calculate and report eligible salaries and contributions.

13. PERA's Response to the Legislative Auditor is included in Exhibit B. Four thousand political subdivisions participate in PERA. Requiring field audits of all four thousand entities would require an extensive increase in staffing and administrative expenses with questionable results. Under the state and federal "exclusive benefit rule" PERA pension money is held in trust for the exclusive benefit of its members. The necessary, reasonable and direct expenses of the plan are considered to be expenses for the exclusive benefit of PERA's members. Minn. Stat. § 356.001, subd. 2. Therefore PERA is seeking legislation to assure the authority to

conduct compliance audits, to affirm that the legislature considers the expenses thereof to be necessary and reasonable, and to have governmental subdivisions share in the costs of such audits.

Further Affiant sayeth not.

Mary Most Vanek
MARY MOST VANEK

Subscribed and sworn to before me on

this 15 day of March, 2010

Katie B. Olsen
NOTARY PUBLIC



AG: #2598815-v1



**City of Duluth
Legislative and Executive Department
Human Resources Division**

2009 Employee Benefits Handbook

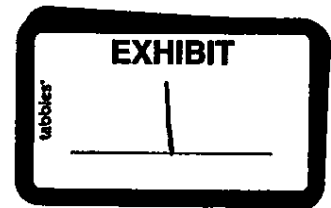


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Important Information –

The City of Duluth expects to continue its health insurance program indefinitely. However, it reserves the right to change or discontinue all or any part of the insurance programs or benefits, consistent with the City’s rights and obligations under the law and collective bargaining agreements. The City of Duluth’s employee group health insurance program is not liable for insurance plans that may become insolvent.

This booklet is a summary only. Please refer to each plan’s certificate of coverage / plan document for a complete description of all benefits and exclusions. Some of the certificates / plan documents are available online at:
<http://www.ci.duluth.mn.us/city/employment/Benefits/Benefits.htm>.

If there is any difference between the information provided in this booklet and any certificate of coverage / plan document, the certificate of coverage / plan document will govern.

In the event that some information changes, you will receive information about changes prior to Open Enrollment.

If you are a new employee, this information will help you to understand the benefit options available to you. If you’re already covered by any of the benefit plans, you may refer to this booklet throughout the year as you use your benefit plans. This booklet also provides information regarding your COBRA rights and responsibilities.

The benefits available through the City of Duluth are provided through a governmental plan which is not subject to ERISA.

Introduction to your benefits

Your benefits are carefully negotiated by representatives of employee unions and the City of Duluth. If you are not represented by a union, the City of Duluth may provide you with the same benefits that represented employees receive.

A broad base of programs has been developed in order to help you ensure your family's future health and security. Benefit-eligible employees are entitled to the following insurance and pre-tax benefits:

Automatic benefits provided by the City of Duluth

- ✓Employee Health Insurance
- ✓Employee Low-Option Dental Insurance
- ✓Retirement Plan (PERA)
- ✓Employee Basic Life Insurance
- ✓Employee Sick Leave & Long-Term Disability
- ✓Vacation / Holidays

Optional benefits provided by the City of Duluth

- ✓ Family Health Insurance
- ✓ Family or Single-plus-One or High-Option Dental Insurance
- ✓ Employee Supplemental Life Insurance
- ✓ Spouse Life Insurance
- ✓ Child Life insurance
- ✓ Group Decreasing Life Insurance through PERA
- ✓ Flexible Spending Accounts – Medical and/or Dependent Daycare
- ✓ Savings Plan (i.e., Deferred Compensation Plans)

Full-time employee benefits

The City of Duluth provides and pays the entire cost of single health and single Low-Option dental insurance for all eligible full-time employees. Employees may assign the monthly City Deferred Compensation contribution towards their family health care premium. Additionally, the City pays the premium for a Basic Life Insurance benefit for all eligible employees. Sick Leave and Long-term Disability benefits are also provided and paid for by the City of Duluth.

Part-time employee benefits

Eligible part-time employees, as defined by each of the Labor Agreements, may qualify for health, dental and life insurance benefits. Please refer to the specific Labor Agreement for further details.

Glossary of Benefit Terms

Please refer to this section for an explanation of certain terms used throughout this handbook.

Online access to benefits

Health and Dental Plan Materials

Information about your health and dental plan, premium information and summaries of the benefits, can be found on the City of Duluth's home page.

Certificates of Coverage, Plan Documents and Summaries of Benefits

Certificates of coverage and plan documents are legal documents that describe the plan benefits provided by the insurance companies and are mailed to the subscriber's homes. When available, the information is also posted on the City of Duluth's website.

Flexible Spending Accounts

A complete guide to enrollment and use of the medical and dependent daycare flexible spending accounts is available on the City of Duluth's website.

Labor Contracts and Plans

All non-appointed City employees are covered by labor contracts (also referred to as collective bargaining agreements). These contracts and plans define many of the key provisions of the benefits provided. For more information about your benefits, check the contract or plan that covers your position. These contracts are also available on the City of Duluth's website.

Open Enrollment

During the annual open enrollment period, all benefit-eligible employees will receive written benefit information from the Human Resources office. Information regarding the open enrollment process will also be available on the City of Duluth's website, www.duluthmn.gov, under Human Resources. Additionally, during the open enrollment period, employee meetings will be held periodically to discuss changes in benefits.

Forms

You will find the Employee Data Maintenance Form (EDMF) online. Use this form to enroll in health and dental benefits, or to change your current health and/or dental benefits due to a qualifying change in family status. You will also find enrollment/change forms for the employee basic and optional life insurance benefits as well as the Flexible Spending Account Plans.

Health Insurance

The City of Duluth offers all benefit-eligible employees a comprehensive health plan which is administered through Blue Cross Blue Shield Plan of Minnesota (BCBSMN). Employees may choose single or family coverage. The health plan includes prescription drug coverage administered through ClearScript, a nationally recognized Pharmacy Benefits Management company.

The City of Duluth provides single health care coverage at no cost to benefit-eligible employees. Once an employee elects coverage for the Plan Year (i.e., single or family coverage), the election is irrevocable for the remainder of the plan year. The only time an employee may change his or her coverage or add/drop dependents is during the open enrollment period unless the employee experiences a qualifying family status change (refer to page 26).

The Health Plan Summary of Benefits on the following pages provides an overview of the health and prescription drug benefits offered through the City of Duluth. A thorough description of the health plan is available in your BCBSMN Plan Document.

Health and prescription drug plan benefits can change through collective bargaining agreements reached by management and labor unions. Throughout the term of union contracts, the Health Insurance Labor-Management Committee discusses issues arising with health benefits – examining problems of rising health insurance costs, developing ways to evaluate the quality of health plans and promoting better labor-management relationships.

This handbook does not attempt to include the many procedures and requirements for ensuring quality and efficiency. For example, the handbook may state the level of benefits for a certain service, but the service may also require the plan's prior approval.

Eligibility

Eligible employees are those whose title and employment status satisfy the eligibility provision of a collective bargaining unit agreement or applicable City Council resolution. Each eligible employee selects one of these plans.

If you and your spouse are both employed by the City of Duluth and benefit eligible, you may cover each other as a dependent under your active employee health insurance benefit only. For further information regarding eligible dependents, please refer to page 33.

Enrollment

All newly hired benefit-eligible employees must complete a benefit election form to become enrolled in the health plan. Employees who fail to return the enrollment form (i.e., EDMF) within the first 30 days of their hire date will default to single health coverage under Health Plan Option 3A. Thereafter, an annual Open Enrollment period will be conducted for all benefit-eligible employees. The election made during the open enrollment period is for the entire plan year (i.e., January 1 through December 31). Employees may make benefit election changes only if they experience a qualifying family status change, as defined on page 26.

Health Insurance (continued)

Monthly Premiums

Premiums vary depending on the type of coverage you select. The amount of the City's contribution toward your health insurance premium is determined by your collective bargaining unit agreement or applicable City Council resolution. Eligible full-time and part-time employees are provided with single coverage health care benefits paid for by the City. The City pays for a portion of the family health insurance premiums and announces the next years' rates during the open enrollment period. During Open Enrollment or the special enrollment period, employees may designate their monthly Deferred Compensation contribution to be applied towards the family health insurance premium. The amount of the Deferred Compensation contribution may differ depending on the bargaining unit you belong to. Refer to your collective bargaining unit agreement to determine the amount of your Deferred Compensation contribution.

2009 Single Health Insurance Monthly Premium – Basic, Confidential, Fire, Police & Supervisory Units

	Plan 3A	
Total Single Premium paid by the City of Duluth	\$ 475.08	

2009 Family Health Insurance Monthly Premium – Basic, Fire, Police & Supervisory Units

	Plan 3A	
Total Family Premium	\$ 1,170.21	
City Premium Contribution	\$ 936.17	
Employee Premium Contribution*	\$ 234.04	
Per Paycheck Amount Without Deferred Comp Contribution	\$ 1,170.21	
Deferred Comp Contribution**	\$ 114.50	
Per Paycheck Amount With Deferred Comp Contribution	\$ 1,055.71	

2009 Family Health Insurance Monthly Premium – Confidential Unit

	Plan 3A	
Total Family Premium	\$ 1,170.21	
City Premium Contribution	\$ 936.17	
Employee Premium Contribution*	\$ 234.04	
Per Paycheck Amount Without Deferred Comp Contribution	\$ 1,170.21	
Deferred Comp Contribution**	\$ 122.50	
Per Paycheck Amount With Deferred Comp Contribution	\$ 1,047.71	

* The employee premium contribution listed above applies to full-time employees. Information regarding part-time employee premium contribution can be obtained from Human Resources at (218) 730-5210.

**The Deferred Comp Contribution may be applied towards family health insurance OR to a Deferred Compensation plan. This election may only be changed during the open enrollment period, special enrollment period or in the event of a qualifying family status change.

If you are a member in the Confidential Unit, you must complete a Deferred Compensation plan election form and assign \$5.48 as the employer contribution; otherwise the money will be forfeited because it will not be included in your regular pay.

Health Insurance (continued)

Monthly stipend for employees electing “Single” health coverage

Employees electing single health coverage will receive \$75 per month. The effective date of this benefit coincides with the health plan election. During the open enrollment period, special enrollment period or in the event of a qualifying family status change, employees may designate the \$75 monthly stipend to be applied to a flexible spending account and/or deferred compensation plan.

How the medical plan works

Health insurance benefits will become effective the first day of the month following the employee’s date of hire or benefit eligibility date provided that the employee completes and has the Benefit Enrollment Form to the City of Duluth Human Resources office within 31 days from their date of hire, or their benefit eligibility date. Thereafter, an annual open enrollment period will occur during the fall and the benefit elections made during the open enrollment period will become effective the following January 1st.

Plan documents describe the benefits available through the health plan. A plan document is provided to all newly hired employees with their new hire paperwork and benefit materials. (An electronic version of the Plan Document is also available in the City of Duluth’s website.) Thereafter, plan documents or a summary of benefit changes will be mailed to the members’ home whenever a change to a health insurance benefit occurs. Specific questions regarding health benefits or eligible services should be directed to the BCBS Customer Service Department. The phone number to Customer Service is located on the back of your health insurance identification card.

Choosing a Health Care Provider

Members enrolled in any one of the four health plan options sponsored by the City may choose an eligible provider of health services for the medical care needed. The plan will pay higher benefits when an “In-Network Provider” is chosen. A “provider” is any person, facility, or program that provides covered services which BCBSMN determines are within the scope of the provider’s license, certification, registration or training.

In-Network Providers

When you choose an in-network provider, you receive the maximum benefit allowable under the plan provisions. These providers send your claims directly to BCBSMN for services you receive. To locate an in-network provider near you, you may:

- 1) Reference your provider network booklet;
- 2) Contact the BCBSMN Customer Service Dept. at 1/800/382-2000 (TDD 1/888/878-0137); or
- 3) Visit the on-line member service center at www.bluecrossmn.com.

Please be aware that the provider directory lists in-network providers but it may change as providers enroll or terminate their agreements. It is your responsibility to confirm whether your provider is participating in the network at the time you receive medical services.

Out-of-Network Providers

In addition to paying more of the bill, non-participating providers may not take care of notification requirements or file claims on your behalf. Please refer to the Plan Document for a description of charges that are your responsibility.

Dental Insurance

All City of Duluth benefit-eligible employees will be offered a choice of two dental plan options, a Low-Option or High-Option. The dental benefits are administered through Delta Dental Plan of Minnesota. The City of Duluth provides excellent dental benefits, and employees may choose Single, Single Plus One, or Family coverage under one of the dental plan options. The City of Duluth provides single coverage in the Low-Option dental benefit at no cost to City employees. An employee may only elect Family dental coverage at the following times: 1) during the first 31 days of original date of hire; 2) during the open enrollment period; or 3) upon a qualifying change in family status (refer to page 26 for details). When an employee elects Family dental coverage, he/she will maintain Family dental coverage for not less than two (2) consecutive years. The employee may cancel Family dental coverage after the two (2) consecutive year period, and the change will be effective the first of the month following receipt of the change form. If the employee again elects Family coverage after canceling from a previous period, the employee must again maintain Family coverage for another two (2) consecutive year period.

Important Features

The City's dental plan is designed to provide benefits for most conditions requiring dental diagnosis and treatment, excluding orthodontia treatment. To encourage you to stay in good dental health, the dental benefits cover a broad range of preventive services, including:

- ✓ Regular exams
- ✓ X-rays
- ✓ Teeth cleanings
- ✓ Children's fluoride treatment

Benefits across the Low-Option and High-Option plans are similar, except for the annual maximum. For detailed information regarding benefits, please refer to your dental Plan Document.

For major dental procedures, we encourage you to have your dentist submit a pre-treatment estimate to Delta Dental for determination of benefits and financial responsibility prior to the service.

Choosing a Dental Provider

You have the freedom to see any dentist. However, dentists who participate in the DeltaPremier network have agreed not to charge more than Delta Dental's maximum allowable amount. This can result in lower out-of-pocket costs. As an added convenience, you never have to file a claim when you use a participating dentist – the dentist files the claim for you.

Finding a participating dentist is easy:

- 1) Visit www.deltadentalmn.org and use the interactive dentist search tool; or
- 2) Call Customer Service at 651/406-5916 or toll free at 1/800/553-9536.

Please be aware that providers enroll or terminate their agreements. It is your responsibility to confirm whether your provider is participating in the network at the time you receive dental services.

If dental services are received by a non-participating dentist, you will be responsible for paying the difference between the maximum allowable amount and what the dentist charges. You may be responsible for submitting your own claim and covered services will be paid directly to you.

Flexible Spending Accounts

Flexible Spending Accounts (FSAs) are voluntary plans that allow eligible employees to set aside money in two types of accounts (Medical and Dependent Daycare) to help pay for eligible health and/or dependent daycare expenses with pre-tax dollars. You decide how much money to contribute to the FSA, and the money is deducted from your paycheck before taxes are calculated. You then submit claims for your eligible health and/or dependent daycare expenses and are reimbursed from these accounts with your pre-tax contributions.

For all eligible employees who select single health care insurance under the BCBSMN Plan 3A (Comprehensive Plan), the City of Duluth will deposit a set amount each month towards the FSA of their choice and/or the Deferred Compensation Plan of their choice. To determine the amount the City of Duluth will deposit toward the FSA, please refer to your collective bargaining agreement. Employees who wish to participate in the FSA plan must complete an enrollment form designating their plan year election(s).

Important Note - Use it or Lose it Rule

If you decide to participate in the Flexible Spending Accounts, carefully consider your medical and/or dependent daycare eligible expenses. Once you determine the amount you wish to contribute and submit your enrollment form, your election is irrevocable. According to Federal law, any contributions to either of the FSAs that remain unclaimed by the end of the runoff period will be forfeited. Be sure you fully understand this risk and that you plan carefully when enrolling in the FSA.

How do I enroll?

You may participate in either or both of the Flexible Spending Accounts as follows:

- ❶ Complete and submit your FSA Enrollment Form to the Human Resources office by the annual open enrollment deadline;
- ❷ New hires or newly benefit-eligible employees must complete and submit the FSA Enrollment Form to the Human Resources office within 31 days from the date of hire or the benefit-eligibility date; or
- ❸ Employees experiencing a qualifying family status change must complete and submit the FSA Enrollment Form to the Human Resources office within 31 days of the qualifying event.

Flexible Spending Account - Annual Maximum Contributions

Medical: \$5,000
Dependent Daycare: \$5,000 (if you are married and filing a joint tax return)
\$2,500 (if you are married and filing separate tax returns)

SuperiorUSA is the administrator for the City's FSA plan. Additional information, examples and worksheets are provided on their website: www.superiorusa.com to help you determine if you can benefit from using a FSA and to help you estimate how much to set aside. The enrollment form you need to complete is available online on the City's website: <http://www.ci.duluth.mn.us/city/employment/Benefits/Benefits.htm>.

Flexible Spending Accounts (continued)

How Does it Work?

Medical Flexible Spending Account

The medical flexible spending account allows you to set aside money on a pre-tax basis to pay for qualifying medical and/or dental expenses you would otherwise pay for with after-tax dollars. You may use this account to pay for your health and dental plan deductibles, co-payments, co-insurance, and other qualifying expenses that cannot be reimbursed from any other source, such as another insurance plan. You may contribute up to \$5,000 per year to this account. If you lose your benefits eligibility, you may be eligible to continue your participation in the plan on an after-tax basis.

When you have an eligible health or dental service/expense, you pay the provider directly. You then submit copies of your documentation (e.g., explanation of benefits – EOBs) along with a completed claim form to SuperiorUSA. The services/expenses must be incurred during the time that you are a plan participant. In other words, if you are hired on May 5th and enroll in the medical FSA effective June 1st, only qualifying services/expenses incurred beginning June 1st are eligible for reimbursement; any services/expenses received prior to June 1st are not eligible for reimbursement.

Examples of Eligible Medical FSA Expenses

- ① Medical/Dental deductibles, co-payments and co-insurance;
- ② Prescription drug co-payments;
- ③ Prescription eyeglasses and/or contact lenses, cleaners and solution for contact lenses;
- ④ Lasik surgery;
- ⑤ Hearing aids;
- ⑥ Certain over-the-counter items (e.g., allergy medications, sinus medications, cough syrup, arthritis pain reliever, antacid tablets, etc.)

Examples of Ineligible Medical FSA Expenses

- ① Medical/Dental services/expenses that are not medically necessary;
- ② Cosmetic surgery, procedures and/or medications;
- ③ Dental bleaching;
- ④ Hair restoration;
- ⑤ Over-the-counter items that are not medically necessary;
- ⑥ COBRA payments

Visit www.superiorusa.com for a complete listing of eligible/ineligible services/expenses.

Dependent Daycare Flexible Spending Account

The dependent daycare flexible spending account allows you to pay for certain dependent daycare expenses with pre-tax dollars. To be eligible for reimbursement, the daycare expenses must be used to allow you to work and for the care of children under age 13, who qualify as dependents on your income tax return, or disabled family members or elderly parents who are incapable of self care and live with you. An example of an eligible expense includes fees for licensed day care or adult care facilities. The annual maximum benefit is \$5,000 per family per

Flexible Spending Accounts (continued)

year or \$2,500 per spouse if you and your spouse file taxes separately. *This account is for daycare expenses – not for medical/dental expenses for your dependents.*

When you have an eligible daycare expense, you pay the provider directly. You then submit your claim form and receipts to SuperiorUSA for reimbursement.

Definition of “Qualifying Dependents” for Dependent Daycare

- ✓ Children under age 13 who qualify as your dependents for income tax purposes
- ✓ A child, spouse or other dependent who is physically or mentally incapable of self-care, spends at least 8 hours a day in your household, and who qualifies as a dependent for income tax purposes

Examples of Eligible Dependent Daycare FSA Expenses

Expenses for care of a “qualifying dependent” are only eligible if the daycare enables you (and your spouse) to work, look for work, or go to school full-time. Eligible expenses include:

- ① In- and out-of-home daycare;
- ② Child or adult daycare center;
- ③ Before and after school care programs for dependents under age 13;
- ④ Pre-school daycare;
- ⑤ Summer day camp;
- ⑥ Payment to a relative (age 19 or older who is not your dependent) who cares for your qualified dependent.

Examples of Ineligible Dependent Daycare FSA Expenses

- ① Kindergarten fees;
- ② Elementary school expenses for a child in first grade or higher;
- ③ Food, transportation, and incidental expenses (e.g., diapers, activities, etc.) are not eligible if charged separately from dependent care expenses.

Visit www.superiorusa.com for a listing of eligible/ineligible services/expenses.

Disclaimer

If you have questions regarding the eligibility of a particular medical or daycare expense, resources that can be of assistance are IRS publications 502 and 503 (for health care and dependent daycare expenses, respectively) and are accessible through the IRS website at www.irs.gov, the library, or your tax advisor.

Please note that the City of Duluth does not provide tax advice to participants.

Flexible Spending Accounts (continued)

Tax Savings

An example of possible tax savings follows:

Terry is married and works for the City. Terry has a salary of \$30,000 per year and files a joint tax return. Terry's spouse works for another employer and earns an annual salary of \$20,000. Terry elects to contribute \$5,000 per year to one of the Flexible Spending Account Plans. Terry gets reimbursed for expenses equal to the amount contributed during the year. The chart below illustrates Terry's savings when using a FSA plan.

Sample Income Comparison

	Employee not enrolled in a Flexible Spending Account	Employee enrolled in a Flexible Spending Account
Gross Salary	\$ 30,000	\$ 30,000
Pre-tax contribution towards FSA - either the health or dental plan	\$ - 0	\$ - 5,000
Taxable Compensation	\$ 30,000	\$ 25,000
Estimated income tax (federal & Minnesota, based on 2003 rates)	\$ - 5,698	\$ - 4,595
Social Security (FICA) tax	\$ - 2,295	\$ - 1,913
Compensation after tax	\$ 22,007	\$ 18,492
Health care or Dependent daycare expenses paid with after tax dollars	\$ - 5,000	\$ - 0
Spendable income after expenses are paid	\$ 17,007	\$ 18,492

Using either of these accounts to pay for health and/or dependent daycare expenses on a pre-tax basis increases Terry's spendable income by \$1,485 per year. Of course, to the extent that some of the \$5,000 expenses represent dependent daycare cost, the illustration above would need to be adjusted by whatever amount of dependent care credit may be available on the individual's tax forms.

Estimated Impact on Social Security

Your social security benefits could be affected if your taxable earnings are less than the social security maximum covered wages. The laws affecting social security taxes and benefits are constantly changing, so there is really no way to predict how anyone might be affected. The decision becomes one of whether the current overall tax savings are more valuable to you than a possible reduction in social security benefits in the future.

Continuation of Your Coverage

Continuation Coverage Rights Under COBRA

Introduction

The right to COBRA continuation coverage was created by a federal law, the Consolidated Omnibus Budget Reconciliation Act of 1986 (COBRA), as well as by certain state laws. COBRA continuation coverage may become available to you when you would otherwise lose your group health coverage. It can also become available to other members of your family who are covered under the Plan when they would otherwise lose their group health coverage. For additional information about your rights and obligations under the Plan and under federal and state law, you should review the Plan Documents or contact the City of Duluth Human Resources office.

The following pages, "Initial Notice of COBRA Continuation Coverage Rights", contain important information about your right to COBRA continuation coverage, which is a temporary extension of coverage under certain benefit plans. This notice generally explains COBRA continuation coverage, when it may become available to you and your family, and what you need to do to protect the right to receive it.

The City of Duluth is responsible for administering continuation coverage.

Continuing Your Coverage

In most cases, you have 60 days from the date of the qualifying event to select continuation of coverage. Please read your Initial Notice of COBRA Continuation Coverage Rights on pages 36 – 39 which includes the following information:

- ✓ Terminology you need to know
- ✓ Circumstances which can trigger a COBRA qualifying event for you and/or your qualifying dependents;
- ✓ Steps required by you or your covered dependent to assure coverage continuation rights
- ✓ Employer responsibilities
- ✓ Length of COBRA Continuation Coverage

If a qualified dependent ceases to be eligible for coverage due to divorce or the loss of dependent status, notice must be provided to the City of Duluth within 60 days of the event.

Exception: Continuation is not available to any employee, spouse, ex-spouse or dependent that becomes covered under any other group health plan except as may otherwise be provided by law.

Employees Who Retire or Become Disabled

The labor agreements for each unit include the criteria which must be met to qualify for retiree medical and retiree life insurance. Likewise, each labor agreement outlines the application of benefits to employees who become disabled. Please reference the labor contract that applies to your job for further information.

Deferred Compensation Plans

As a City of Duluth employee, you can participate in a 457 Deferred Compensation plan. Under a deferred compensation plan, you can make pre-tax contributions bi-weekly through payroll deduction into a variety of investment options to save for retirement. By setting aside a portion of your income to accumulate on a tax-deferred basis, you pay fewer tax dollars now, and your savings and investment earnings accumulate tax-deferred until you start drawing from the plan at retirement. The City of Duluth offers five deferred compensation plans to choose from.

All five plans offer a wide range of investment options, each designed to pursue a different investment objective. Contact a plan representative or the Human Resources office for:

- ▶ Information describing the plan and its options.
- ▶ Prospectuses describing individual investments and their history.
- ▶ Help with enrollment and enrollment or change forms.
- ▶ Catch-up contribution rules.
- ▶ Hardship withdrawal information.
- ▶ Distribution upon termination information.

The City of Duluth provides a Deferred Compensation monthly allowance to eligible employees. The amount of the monthly contribution depends on the employee's union – please refer to your collective bargaining agreement to determine that amount. The monthly Deferred Compensation contribution can only be used in one of two ways: 1) to invest in the Deferred Compensation Plan(s); or 2) to apply toward the employee's monthly family health premium. It is the employee's responsibility to designate how the employer contribution will be assigned.

How Deferred Compensation Works

- You decide how much to defer and complete the appropriate participation / enrollment materials. You can contribute as little as \$10 per pay period or as much as the maximum of 100% of gross pay or \$16,500 annually – whichever is less. The 2009 IRS contribution level is \$16,500. If you're age 50 or over, you can set aside an even higher amount. ***Please submit your enrollment forms to the City of Duluth Human Resources office.***
- The City will deduct the contribution amount from your paycheck before state or federal income taxes are taken out, and forward them to the deferred compensation plan administrator on a regular basis.
- You choose how to invest your contributions from the investment options offered under the plan.
- Contributions and earnings accumulate tax-deferred. You are subject to state and federal income taxes only when you receive benefit payments.

Deferred Compensation Plans (continued)

- The plan has no effect on social security or PERA. Your social security and PERA benefits are based on your total pay, including the amounts paid into the deferred compensation plan.
- You can change your deduction amount or stop and start your deductions whenever you choose.
- You can change your allocation and investment options within the plan whenever you choose.

Reasons to Enroll

By deferring compensation, you have the opportunity to:

- ▶ Lower your current income taxes because you postpone paying taxes on contributions and investment earnings until you withdraw them.
- ▶ Enjoy the advantage of tax-deferred compounding.
- ▶ Accumulate more for retirement than you would with an after-tax retirement savings plan.

Plan Comparison

If you are interested in the deferred compensation plans, you can receive detailed information from either the Human Resources office or from the plan representatives. The materials you receive will include information on rate of returns, individual operating expenses, and total fund expenses.

The deferred compensation program is meant for long-term savings only. It should not be considered for short-term needs. Do not participate if you cannot afford to leave invested money untouched until retirement, or if you do not have other savings set aside for emergencies.

Deferred Compensation Plans (continued)

Deferred Compensation Plan Comparison

	Hartford Life Deferred Compensation Plan (Group # 107676)	ICMA Retirement Corporation Deferred Compensation Plan Plan # 302287	Minnesota State Deferred Compensation Plan MNDCP - (Great West)	Nationwide Deferred Compensation Program (Entity #2304UF)
Local Plan Administrator	Robert Farden	Tom Hilson Retirement Plans Specialist	Minnesota State Retirement System Medical Arts Building, Duluth 324 W. Superior Street, Suite 204	Steve Carlson Retirement Specialist
Local Representative Phone Numbers and Customer Service Hours	Robert Farden - (218) 624-2884, Monday - Friday 8:00 - 4:30	(866) 822-3631 8:00 a.m. to 6:00 p.m. Central Time	David Wright - (218) 740-3151 Kristen Kestly - (218) 740-3719 Weekdays: 8:00 am - 4:30 pm	1-877-677-3678, option 8, ext. 42094 Monday - Friday: 7 a.m. - 8 p.m. CT
National Representative Phone Numbers and Customer Service Hours	1-800-528-9009, 2 for Customer Service	(800) 669-7400 ext: 0 7:30 am to 8:00 pm Central Time	1-877-457-6466 (toll-free) Weekdays: 8:00 am - 4:30 pm Call center located in Minnesota.	1-877-677-3678, select *0 to speak with a representative or your assigned representative Neal Koenig at extension 4-3436.
Automated Telephone Voice Response System and Availability	1-800-528-9009, 1 for Automated System	(800) 669-7400 Available 24/7	"KeyTalk" automated system, 1-877-457-6466 Available 24 hours a day.	1-877-677-3678, select option 1 24 hours per day, seven days per week
E-mail Questions	robert.farden@edwardjones.com	E-mail questions to investorservices@icmarc.org	david.e.wright@state.mn.us	carlosos2@nationwide.com
Website	www.retire.hartfordlife.com	www.icmarc.org	www.mndcpplan.com Free 24 hour account access.	www.nrsforu.com
Investment Options	48 Fund Choices 2 stable value funds 5 bond funds 7 asset allocation 15 large Cap funds 4 mid cap funds 3 small cap funds 6 specialty funds 6 international funds	49 investment options: ✓ 8 time-based lifecycle funds ✓ 5 risk-based lifestyle funds ✓ 2 balanced funds ✓ 1 stable value fund ✓ 1 money market fund ✓ 4 U.S. bond funds ✓ 24 U.S. equity funds ✓ 4 international equity funds	14 mutual funds and investment options: 5 U.S. equity funds 2 international equity funds 2 balanced funds 2 U.S. bond funds 2 fixed interest funds 1 money market fund Plus hundreds of No Transaction Fee (NTF) mutual funds available through Ameritrade for an additional \$15 per quarter (optional).	26 investment options: ✓ 5 risk-based asset allocation funds ✓ 2 specialty funds ✓ 2 international funds ✓ 3 small cap funds ✓ 3 mid cap funds ✓ 6 large cap funds ✓ 3 bond funds ✓ 1 money market fund ✓ 1 fixed option
Quarterly Account Statements	Yes, mailed to participants, can also be viewed on-line	Yes. Mailed to participant's home 10 business days after quarter-end.	Yes. However, participants can opt-out of mailings and receive statements on-line.	Yes. Mailed to participant's address on file.
Financial Planning Services	Yes. Free financial assessment analysis retirement planning tools on website also available.	Fee-based financial plans available. Managed accounts available early 2007.	Free personalized online investment advice and fee-based managed accounts available in fall 2007.	Yes. Personal Retirement Consultants available.
Enrollment	Can be done any time during the year	Enrollment available any time of year.	Local licensed representatives available	Enroll any time at your convenience over the

Hartford Life Deferred Compensation Plan (Group # 107676)		ICMA Retirement Corporation Deferred Compensation Plan Plan # 302287		Minnesota State Deferred Compensation Plan MNDGP - (Great West)		Nationwide Deferred Compensation Program (Entity #2304UF)	
Annual Account Fees	No	No.	Retirement Plans Specialist on site quarterly for educational seminars with individual consultations available at anytime.	No	any time of the year to discuss investment options and enrollment.	No.	phone or face-to-face with Steve Carlson.
Daily Asset-Based Charges	75 - 90 bps	0.55% administration fees on all assets; additional 0.15% fee on assets in non-proprietary funds.	Fund expenses range from 0.46% to 1.40%	0.10% (1/10 th of 1%) annual administrative fee, charged only on the first \$100,000 in an account.	Varies by investment option from 0.01% to 1.01%. Six funds with operating expenses below 0.10% (1/10 th of 1%).	0.50% annual administrative fee on all variable fund assets. 0.25% annual administrative fee on fixed account option.	Fund expenses range from 0.00% to 1.40%.
Fund Operating Expenses	Varies by investment option, from 0.0% to 2.42%	None, other than those described above. No surrender charges or market value adjustments.	None, other than those described above. No surrender charges or market value adjustments.	None charged by MNDGP.	(Note: The Fidelity Diversified International Fund applies a 1% fee to all redemptions of only those shares held less than 30 days and the Vanguard Institutional Developed Markets Index Fund applies a 2% fee to all redemptions of only those shares held less than 60 days)	None.	
Expenses: Load, Risk & Mortality, Annuity Purchase, Transaction Fees, Surrender Charges	Load, Risk & Mortality, Annuity Purchase, Transaction Fees, Surrender Charges: CDSC - 5% - years 1 & 2 4% - years 3 & 4 3% - year 5 2% - year 6 1% - year 7 0% - year 8	None	None	None			
Fee for Minimum Distribution	None	None	None	None		None	
Compensation for Representatives	Included in fund operating expense.	Salaried with bonus. No compensation based on participant investment decisions.	Salaried. No commissions or bonuses.	Salaried. No commissions or bonuses.		Salary. No commissions.	

Health Care Savings Plan (HCSP)

The Health Care Savings Plan is a public employer-sponsored program administered by the Minnesota State Retirement System (MSRS) that allows employees to save pre-tax money to pay post employment medical expenses and/or health insurance premiums. Participation is determined during negotiations between the collective bargaining units and City of Duluth.

Employees will be able to choose among seven different investment options provided by the State Board of Investment. Assets in the account will accumulate *tax free*, and since payouts are used for approved health care expenses, they will remain tax-free.

Amounts to be put into the account must be negotiated or agreed to by both the bargaining unit and employer, and written into the collective bargaining agreement or Memorandum of Understanding (MOU).

The HCSP allows employees to set aside money to cover the ever-increasing costs of health insurance and out-of-pocket expenses after termination of public service. While deferred compensation plans or retirement accounts provide a tax-deferred benefit, amounts paid out are considered taxable income. Under the HCSP, amounts contributed are tax-free and no taxes are paid on amounts to pay health, dental and long-term care insurance premiums, as well as out-of-pocket medical expenses. This tax advantage could result in significant savings to you and your family!

Eligible employee participation is mandatory. For tax purposes, the IRS requires that eligible employees participate in the plan adopted by their bargaining unit. Employees may not opt out of the program except under specific situations including:

- The employee is a foreign national;
- The employee has full health care coverage through another documented source; or
- The employee participates in Tri-Care.

Requests to opt out of the plan must be accompanied by coverage documentation and any other supporting documentation available. Please note: if you waive participation you may not choose to participate in the future. Please contact MSRS directly to obtain the necessary paperwork to opt out of the plan.



OFFICE OF THE LEGISLATIVE AUDITOR
STATE OF MINNESOTA

Financial Audit Division Report

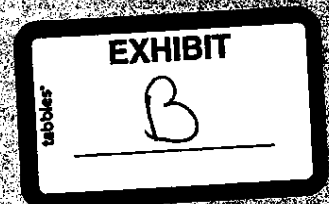
**Public Employees
Retirement Association**

Financial Statement Audit

Year Ended June 30, 2009

March 9, 2010

Report 10-06



Findings and Recommendations

Prior Finding Not Resolved: PERA did not have adequate controls to ensure that employers reported and remitted the correct amount of salaries and retirement contributions.

Finding 1

PERA did not have control procedures in place to ensure employers reported amounts based on statutory requirements. This internal control weakness increased the risk of pension contributions and retirement benefits being overstated or understated.

In our prior audit report for the year ended June 30, 2008, we noted that the City of Duluth had erroneously reported employee salaries to PERA dating back to January 1997.¹ The city had incorrectly included some employer-paid benefits in its calculation of employees' base salaries. The city used this overstated salary amount to determine both its employee and employer retirement contributions and also reported these incorrect base salaries to PERA. PERA used the incorrect base salaries to determine employees' pension benefits.

Employers are responsible to report members' eligible salaries in accordance with *Minnesota Statutes*.² According to statute, employer-paid fringe benefits, including employer contributions to flexible spending accounts, deferred compensation plans, and insurance coverage, are excluded from the definition of salary. Although PERA provided extensive training to employers on how to calculate and report salary information and pension contributions, it did not verify that employers reported the correct base salaries and pension contributions.

Recommendation

- *PERA should verify that participating employers properly calculate and report eligible salaries and contributions.*

PERA did not accurately report foreign currency risks in its financial statement footnote disclosures.

Finding 2

PERA did not accurately disclose \$32.8 million of cash and \$10.6 million of fixed income investments as investments held in foreign currencies in its foreign currency risk footnote. Instead, PERA erroneously reported that the funds were invested in other types of foreign currencies not specified in the disclosure. PERA relied on the State Board of Investment to provide the information included in the foreign currency investment disclosure since the board invests the pension's

¹ Office of the Legislative Auditor's Financial Audit Division Report 09-04, *Public Employees Retirement Association*, issued February 13, 2009.

² *Minnesota Statutes* 2009, 353.01, subd. 10.



March 3, 2010

James R. Nobles, Legislative Auditor
Office of the Legislative Auditor
Room 140, Centennial Office Building
658 Cedar Street
St. Paul, MN 55155-1603

Dear Mr. Nobles:

Thank you for the opportunity to review and respond to the audit your office conducted for fiscal year 2009. We take audit findings very seriously, and are either in the process of implementing your recommendations or have already implemented them. Our responses to your findings and recommendations are provided below.

1. ***Finding: PERA did not have adequate controls to ensure that employers reported and remitted the correct amount of wages and retirement contributions.***

Recommendation: PERA should verify that participating employers properly calculate and report eligible salaries and contributions.

Response: We have system controls in place that ensure the contributions we receive are calculated correctly based on the salary provided, but have not had authority in statute to conduct compliance audits. We have an extensive training program that includes online information, employer handbooks, quarterly newsletters and training sessions conducted throughout the state, and have introduced legislation that would give us authority to “establish reporting procedures and methods as required to review compliance by employers with the salary and contribution reporting requirements....” Should the legislation pass, we will be allowed to review payroll records of participating employers.

We have been working with the Teachers Retirement Association to jointly plan compliance audits of schools once we have authority in statute to do so. We will work with them for the next couple of years on schools, then will broaden our scope to include other employers. During this past year we also restructured the work done by staff so that we could free up the time of two employees to handle compliance audits.

Resolution Date: We will begin auditing schools during the summer of 2010, assuming legislation passes during the 2010 legislative session giving us that authority.

Person Responsible: Cheryl Keating