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STATE OF MICHIGAN
DEPARTMENT OF CONSUMER AND INDUSTRY SERVICES
EMPLOYMENT RELATIONS COMMISSION
COMPULSORY ACT 312 ARBITRATION

IN THE MATTER OF ACT 312 ARBITRATION

CITY OF MUSKEGON - EMPLOYER

-and-

MERC CASE NUMBER: L05 F-7001

POLICE OFFICERS LABOR COUNCIL - UNION

ACT 312 ARBITRATION PANEL

Richard E. Allen
Chair person

John C. Schrier, Employer Delegate
Fred LaMaire, Union Delegate

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APPEARANCES

FOR THE EMPLOYER:

John C. Schrier, Attorney

FOR THE UNION:

Thomas R. Zulch, Attorney

PRELIMINARY STATEMENT

The City of Muskegon (City) submitted a PETITION FOR ACT 312 ARBITRATION to the Michigan Employment Relations Commission stating "the parties have not succeeded in resolving disputed matters". The disputed matter listed by the Employer in it's PETITION stated as follows:

"The sole issue is the terms of a Defined Contribution Retirement Plan."

In Joint Exhibit #3. Tab #2, in a letter from the Employer, it was stated the City and Union agreed to the following "comparables":

Bay City
City of Holland
City of Kentwood
City of Muskegon Heights
City of Norton Shores
City of Saginaw
County of Muskegon

It was noted "Internal Comparables" will also be presented.

Joint Exhibit #3, Tab #3, listed the appropriate disputed sections of the Collective Bargaining Agreement. That Agreement contains Section 34 - PENSIONS, which defines the terms and conditions of the current "Defined Benefit" Pension Plan. Section 34 is summarized in Joint Exhibit #3, Tab #4, as follows:

Annuity Factor: 2.75 % x Years of Service

Maximum Benefit 75%

Eligibility Requirements Age 51 Year of Service 25

Employee Contribution: 6.00 %

Final Average Compensation: Highest 3 years out of last 5

Under Joint Exhibit #3, Tab # 4, the parties set forth their respective

"Proposed Modifications" as follows:

"Union Proposed Modifications:

The Union is proposing the current Retirement Systems remain status quo."

"Employer Proposed Modifications:

The Employer is requesting a two tiered pension system be established with "new" (emphasis added) hires participating in a Defined Contribution Plan with a 10% employer contribution and 6% employee contribution".

At dispute in this arbitration matter is the proper interpretation and application of Section 39 of the Collective Bargaining Agreement. That Section provides in part as follows:

"The contract will be reopened, at the City's request, within six (6) months for the limited purpose of negotiating a substantive modification to the retirement plan (including the possibility of a defined contribution plan instead of the present defined benefit plan) for employees hired after March 1, 2005. If the parties cannot agree on the modification to the retirement plan, the issue shall be subject to interest arbitration.

Subject to the above provision concerning a re-opener, this Agreement shall be binding upon the parties hereto, their successors and assigns. The Agreement shall commence as of the first day of January, 2004, and terminate as of the 31st day of December, 2006...."

EMPLOYER'S LAST BEST OFFER

"On the Single issue permitted by the re-opener provision (Collective Bargaining Agreement Section 39), the City proposes the following language:

SECTION 40 - DEFINED CONTRIBUTION RETIREMENT PLAN

SECTION 40.1 ELIGIBILITY. The Defined Contribution Retirement Plan shall be available to all members of this unit that entered the unit after March 1, 2005, and any current employee who has opted to quit the Defined Benefit Retirement Plan, and opted to join the Defined Contribution Retirement Plan. A decision to opt out of the Defined Benefit Retirement Plan and to join the Defined Contribution Retirement Plan is irrevocable. The Defined Benefit Retirement is available only to unit members hired on or before March 1, 2005, excluding unit members who have opted out.

SECTION 40.2 CONTRIBUTIONS. Members in this Plan shall contribute six (6%) percent of compensation. The City shall contribute ten (10%) percent of compensation. Compensation shall be Medicare taxable wages as reported on the employee's W-2.

SECTION 40.3 VESTING. Member contributions, including any member contributions transferred from the Defined Benefit Retirement Plan, shall be fully vested when made. City contributions, including any non-member contribution transferred from the Defined Benefit Retirement Plan, shall be vested according to the following schedule:

- 20% after the first full year of service;
- 40% after the second full year of service;
- 60% after the third full year of service;
- 80% after the fourth full year of service;
- 100% after the fifth full year of service.

A year of coverage will include time on the City's payroll and a member of the Defined Benefit Retirement Plan.

SECTION 40.4 LONG TERM DISABILITY Effective on the first day of the month after enrollment, a long term disability insurance policy shall be provided for members of this unit.

SECTION 40.5 TRANSFERS FROM DEFINED BENEFIT PLAN. With respect to money transferred from the defined benefit plan, the affirmative election made by the defined benefit plan participant will result in a transfer of the greater of the employee' contributions to the defined benefit plan or the present value of the individual accrued benefit payable at their deferred retirement date as a life annuity. If the defined benefit plan participant is eligible to receive an immediate benefit, the transfer will be based upon the present value of the individual's accrued benefit payable immediately as a life annuity.

The defined benefit plan participants will be notified of their right to transfer to the defined contribution plan. Defined benefit plan participants shall have until October 31, 2006 to elect to transfer. Failing to elect a transfer shall be deemed a refusal to transfer. A defined benefit plan participant who elects to transfer shall terminate their participation in the defined benefit plan effective November 18, 2006. Assets shall be transferred as soon as possible, and shall be based upon the values specified above as of November 30, 2006. Contributions shall commence in the defined contribution plan with the pay period commencing November 19, 2006, with first contribution occurring on December 8, 2006.

SECTION 40.6 INTERNAL REVENUE CODE COMPLIANCE. This plan shall fully comply with all Internal Revenue Code provisions, regulations and rulings. To the extent that there is a conflict, the Internal Revenue Code supersedes any collective bargaining agreement provision."

UNION'S LAST BEST OFFER

"1. PENSION - Section 34 (Employer) (Economic)

Maintain current defined benefit pension plan for all current and future members of the bargaining unit.

2. RETROACTIVITY -Section 34, 39 (Employer) (Economic)

If a defined contribution plan is awarded, current members, even those hired after March 1, 2005 should not be retroactively removed from the current defined benefit program. Such a defined contribution pension plan should only apply to new employees hired after the date of the award."

ISSUE

Is there reasonable justification for adopting the terms of the Employer's Proposed Defined Contributory Pension Plan? If so, when does the Defined Contributory Pension Plan become effective?

ANALYSIS AND OPINION

As the Employer points out, the "sole issue in dispute is the terms of a Defined Contribution retirement plan". This was so stated in the Act 312 Petition filed by the Employer. In the parties Agreement, effective January 2004, Section 39 provided for a contract re-opener, at the request of the Employer. This contract re-opener was for the limited purpose of negotiating a modification in the current retirement plan, including the possibility of a Defined Contribution Pension Plan, instead of the present Defined Benefit Pension Plan, for employees hired after March 1, 2005. The parties were unable to reach an agreement on the terms of a Contributory Pension Plan by March 1, 2005. The date of March 1, 2005 arrived, and passed, without any change in the current Defined Pension Plan.

Since the parties failed to successfully negotiate any modification to the current retirement plan, by March 1, 2005, that date is no longer applicable for the effective date and eligibility requirements for any future Contributory Pension Plan.

Now, the effective date of any pension modification must be determined via the arbitration process. This is so stated in the parties Agreement, which provides: "*If the parties cannot agree on the modification to the retirement plan, the issue shall be subject to interest arbitration.*" The new effective date, for any pension modification, must be determined by arbitration.

The terms of any pension modification, including a Contributory Pension Plan, must now be resolved by Act 312 Arbitration. The statutory considerations in resolving this matter are specified in MCLA 423.239. Of particular relevance and significance in this proposed pension modification is the financial ability of the governmental Employer to meet its pension obligations, both now, and in the future. The law applicable to the Act 312 Arbitration requires due consideration be given to "*The interests and welfare of the public and the financial ability of the unit of government to meet those costs*". (Act 312 MCLA 423.231, Section 9c).

Section 10 of the Act 312 Arbitration process requires the Arbitration Panel decision to be supported by competent, material and substantial evidence.

The Employer has proposed the Current Defined Benefit Pension Plan be replaced by a Contributory Pension Plan for all new hires. Those employees currently receiving a Defined Benefit are given the option to continue to participate in the Defined Benefit Plan, or convert to a new Contributory Benefit Plan. The Financial Director for the City of Muskegon explained the operational procedures of both the Defined Benefit Pension and and the Defined Contributory Pension. He testified as follows:

" Q. Would you explain for me what a defined benefit plan is and how that operates generally?

A. A Defined benefit plan is a -- I guess its the old traditional type of benefit pension plan where a benefit is guaranteed to an employee that stays for a certain length of service. The benefit is defined by the amount the employee made, usually at retirement or some average of final -- average compensation times a multiplier that in our case is negotiated in different contracts. So it's a mathematical formula which basically guarantees the employee--or retirant a set amount of money for the rest of their lives with different payment options. And whatever it takes to fund that benefit, whatever money is needed, comes from the City. I should say the benefit has a liability. Whatever -- the employees contribute some to that. The funds are set aside and earn investment earnings. Whatever else is needed come from the city's coffers.

Q. Would you describe generally how a defined contribution plan works?

A. A defined contribution is basically that. It defines the contribution for both the city and the employee. A fixed percentage of money is set aside in an account which the employee has control over -- gets total control over when they vest. If they quit, they can take the money with them after vesting. In the proposal here we have a graduated vesting schedule, but -- whereas within a defined benefit plan, if an an employee leaves before being fully vested, they're entitled to nothing other than the return of their contributions". (Transcript, pg 17-18).

The Financial Director further testified as to the reason and, need, for the City Employer to convert from the current Defined Benefit Pension Plan to the Defined Contribution Pension Plan. He said:

"Q. Why is it that the City is looking to switch to a defined contribution plan?

A. Well, like a lot of employers, public and private, you know, the City of Muskegon is feeling financial pressures obviously for a lot of different reason. And one of those pressures is the volatility of the defined benefit contributions. Defined benefit contributions go up and down dramatically, even though we take measures to try to smooth them. For example, we smooth the investment returns over time.

You know, the actuary tries to smooth things. The actuary's goal is actually to make a level percentage of payroll. But our practical experience is that it is not a level percentage by any means. And it tends to work counter-cyclical to the economy to some extent. In other words, pension -- the City's contributions for funding pension benefits tend to go up at the worst time; when the economy is bad, when our other revenue sources are down. And they tend to be lower when stocks are good, investment returns are good. So it really stings our budget.

*On top of health care cost increases, retiree health care, and everything else that's going on, we're looking to stabilize the City's cost in the pension arena. That was the main driving point. We're a City that faces a lot of financial issues, and this is a big one. And we need to stabilize over time how we're going to pay for this benefit."
(Transcript pg 18-19)*

The Employer points out the proposed Defined Contribution Pension Plan is consistent with the pension plan offered other City employees, and is identical to the pension plan afforded the City's fire department employees.

The Employer notes it is a current trend, among both public and private sector employers, to convert from defined benefit pension plans to defined contribution pension plans.

As to the costs of funding a defined contribution plan, the Employer produced evidence the City's 10% contribution is slightly greater than its pension contribution for the last 20 years.

The Union's opposition to the Defined Contribution Plan is mainly based upon their fear there is no guarantee as to the exact amount of a pension benefit an employee will receive when he/she retires. The Union is reluctant to require its members to become responsible for investing pension fund money. They point out ups and downs of stock market makes the pension fund vary from year to year. The employees want the protection offered in the Defined Benefit Plan, and knowing exactly the amount of their pension benefit at retirement.

By way of testimony and exhibits, the Employer has offered sufficient reason and justification to support converting, and replacing, the Defined Benefit Pension Plan with a Defined Contribution Pension Plan. This conclusion is based upon the apparent need for the Employer to face its financial obligations with a predictable annual pension cost. There is a sound business reason for fixing the Employer's pension costs at an established, and consistent 10% of the payroll per year. The enormous burdens of maintaining health care coverage, along with pension obligations, and other employee benefits has made it necessary to at least attempt to stabilize some of the employer's ever increasing employee benefit costs.

However, I find merit in the Union's concern about the need to provide, and maintain, the Defined Benefit Pension Plan for those employees who have been hired with the understanding that they would receive a specified amount of money on the date of their retirement. Those employees, including employees hired after March 1, 2005, were hired, and apparently understood they would receive an established, and set amount of money at retirement, based upon their years of service times a fixed multiplier. Those pension benefits should not be altered. Since the parties failed to reach an agreement by March 1, 2005, those employees hired after that date, and before the effective date of this Award should be entitled to continue accruing pension benefits under the Defined Benefit Pension Plan. The terms and conditions of eligibility for the newly established Defined Contribution Pension Plan are a proper contractual issue to be resolved in arbitration.

It is not fair to change the terms and conditions of a pension plan that existed at the time current employees were hired, and this time frame includes those employees hired after March 1, 2005. Any employee currently on the payroll should be entitled to make a choice between the existing Defined Benefit Plan, and the newly established Contributory Benefit Plan.

Therefore, the effective date of replacing the Defined Benefit Pension Plan, with the newly created Defined Contribution Pension Plan, must be the final effective date of this Award.

CONCLUSION

I find there is merit and persuasive proof the Employer needs to adopt, and implement, a Defined Contribution Pension Plan to become effective upon the final date of this Award. Any newly hired employee, commencing employment after the final date of this Award shall be eligible to enroll only in the Defined Contribution Pension Plan under the terms set forth in the Employer's Last Best Offer, as amended by this Act 312 Arbitration Award.

SECTION 40.1 ELIGIBILITY of the Employer's Last Best Offer must be amended to read as follows:

"SECTION 40.1 ELIGIBILITY. The Defined Contribution Retirement Plan shall be available to all members of this unit that entered the unit after the date of the Act 312 Arbitration Award, and any current employee who has opted to quit the Defined Benefit Retirement Plan, and opted to join the Defined Contribution Retirement Plan. A decision to opt out of the Defined Benefit Retirement Plan and to join the Defined Contribution Retirement Plan is irrevocable. The Defined Benefit Retirement Plan is available only to unit members hired on or before the date of this Act 312 Arbitration Award, excluding unit members who have opted out."

The language in all other Sections of the Employer's proposed Last Best Offer, including Sections 40.2, 40.3, 40.4, 40.5 and 40.6, shall remain unchanged, and as proposed by the Employer.

Date:

July 28, 2006 Richard E. Allen

Richard E. Allen, Arbitrator and
Chairman Act 312 Panel

THE CONTRACTUAL LANGUAGE OF THE EMPLOYER'S PROPOSED LAST BEST OFFER, (SECTIONS 40.2, 40.3, 40.4, 40.5, AND 40.6) ESTABLISHING A DEFINED CONTRIBUTORY PENSION PLAN SHALL BE ADOPTED BY THIS ARBITRATION PANEL.

CONCUR:

Date: _____

Employer Delegate

Date: _____

Union Delegate

DISSENT:

Date: _____

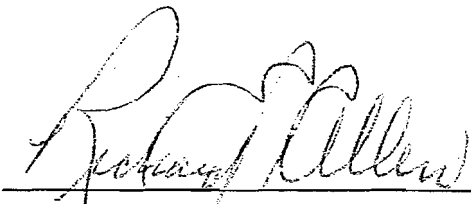
Employer Delegate

Date: 7/25/06

Joe LaMaie

Union Delegate

The language in all other Sections of the Employer's proposed Last Best Offer, including Sections 40.2, 40.3, 40.4, 40.5 and 40.6, shall remain unchanged, and as proposed by the Employer.

Date: July 28, 2006 
Richard E. Allen, Arbitrator and
Chairman Act 312 Panel

THE CONTRACTUAL LANGUAGE OF THE EMPLOYER'S PROPOSED LAST BEST OFFER, AS AMENDED BY THIS ACT 312 ARBITRATION AWARD, AND ESTABLISHING A DEFINED CONTRIBUTORY PENSION PLAN SHALL BE ADOPTED BY THIS ARBITRATION PANEL.

CONCUR:

Date: 7/27/06 
Employer Delegate

Date: _____
Union Delegate

DISSENT:

Date: _____
Employer Delegate

Date: _____
Union Delegate