

In the Matter of the Interest Arbitration Between

The City of Hibbing

and

BMS Case # 11-PN-581

The Hibbing Police Federation

Before: Arbitrator Harley M. Ogata

Dates and Place of Hearing:

August 23, 2011
October 14, 2011
Hibbing Memorial Building
Hibbing, Minnesota

Date of Submission of Briefs:

November 10, 2011

Advocates:

For the City:

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This is a conventional interest arbitration certified by the Minnesota Bureau of Mediation Services (BMS) under Minn. Stat. §179A.16. The arbitrator conducted two days of hearings on this matter. Each party, represented by counsel, offered numerous pieces of evidence and testimony from witnesses. The parties filed post hearing briefs on November 10, 2011, at which time the arbitrator closed the record.

Issues

The Minnesota Bureau of Mediation Services certified seven issues for arbitration:

1. Duration
2. Wages for 2010
3. Wages for 2011
4. Wages for 2012
5. Employer/Employee health insurance premiums portions for 2010
6. Employer/Employee health insurance premiums portions for 2011
7. Employer/Employee health insurance premiums portions for 2012

The parties submitted the following final positions:

1. Duration **Union** - 3 year contract/remove all language in Article except for durational length, including language outlining notice requirements. **City** - Keep current language.

2. Wages for 2010 **Union** - 8% increase. **City** - 0%.
3. Wages for 2011 **Union** - 5% increase. **City** - 1/2% increase.
4. Wages for 2012 **Union** - 5% increase. **City** - 1% increase.
5. Employer/Employee health insurance premiums portions for 2010
Union - no change. **City** - no change.
6. Employer/Employee health insurance premiums portions for 2011
Union - no change. **City** - Reduce the city's contribution to the cost of health insurance premiums from 85% to 80%.
7. Employer/Employee health insurance premiums portions for 2012
Union - no change. **City** - no further change.

Arbitral Standards

Minn. Stat. §179A.16 requires an arbitrator to "consider the statutory rights and obligations of public employers to efficiently manage and conduct their operations within the legal limitations surrounding the financing of these operations." Minnesota public sector arbitrators have further refined the statutory requirements to include an analysis of four factors: external comparisons, internal comparisons, the employer's ability to pay and other relevant considerations. Finally, there is general agreement among Minnesota arbitrators that an interest award should reflect, to the extent possible, the settlement that the parties would have reached voluntarily had collective bargaining been concluded successfully between the parties.

This last consideration is somewhat skewed where, as here, the "normal" processes of the right to strike or lockout are removed from the playing field by state law and where the parties are miles apart in their final positions.

Wages

The testimony and evidence presented at hearing focused almost entirely on the issue of wages. As can be deduced by the widely disparate final positions of the parties on this issue, there is a breakdown in the collective bargaining process between the parties. Interest arbitration in Minnesota was never intended to be a substitute for collective bargaining itself. The circumstances in this matter most replicate the divergent viewpoints and divisions that lead to a strike in nonessential units. Under these circumstances, it makes it very difficult for an arbitrator to issue an award that replicates what the parties would have voluntarily agreed to in the absence of the arbitration, which is a primary goal of an interest arbitration award.

External Comparisons

The parties differed greatly on the comparison groups that should be used to assist in determining wage increases during the life of the contract. The city used three Iron Range cities and four Range Perimeter cities as

its comparison group. Those cities included Chisholm, Eveleth, Virginia, Bemidji, Brainerd, Cloquet and Grand Rapids. The city noted that this "historical grouping" had been used by arbitrators in the past in comparing Hibbing to other cities. (The historical group also included St. Cloud and Moorhead, but the parties generally agreed that those two cities had grown too large to be of much value here).

The city relied on actual, across the board increases in those cities in making its comparisons with its positions on wages. The comparative group was not used for any other purposes in the city's arguments other than to compare general wage increases and to argue that the city's proposal would maintain the union's relative pay ranking within the group and that the union's proposal would cause pay to leapfrog within the group.

The union argued that a more proper comparison group is the one used by a compensation study undertaken on behalf of the city in 2007 by Employer's Associates, Inc. (Gmach study). That comparison utilized cities across the state with populations between 10,000 and 25,000 that are not in close proximity to urban areas.

Implementation of the Gmach compensation study would have resulted in large increases for the members of the union. In fact, the city council determined that it would implement the recommended plan as a result of the study, but only if bargaining units agreed to the

implementation plan. Implementation of the plan would have cost the city about \$750,000. One bargaining unit, the city's largest, balked at implementation and the plans were never implemented.

Gmach testified at the hearing and indicated clearly that the comparison groups were not used for purposes of determining comparable wage comparisons between Hibbing and those cities. Rather, they were used to provide comparison cities with a similar breadth of job classifications and other factors for purposes of providing comparisons across the entirety of the city's job classifications so that some form of "linearity" could be established or maintained within Hibbing's compensation structure. In other words, the comparable cities were picked so that the job classifications at Hibbing would have some reasonable compensation levels in comparison with each other that would be based on objective criteria.

In this regard, the arbitrator finds this testimony to be persuasive and agrees with the city that using the historical group is a more proper external comparison group for our purposes.

The city used the historical group to provide support for two arguments. First, it noted that its wage proposals were consistent with those reported within the historical group with the exception of Grand Rapids, which it argued had settled before the Governor used unallotments

as a means of reducing state aid to cities and that those increases occurred before the recession.

The Range cities, generally, are much smaller than Hibbing. Chisholm has a population under 5,000, Eveleth under 4,000 and Virginia under 9,000, while Hibbing has a population of over 16,000. The Range perimeter cities all have populations over 10,000 and most closely match Hibbing's, which is the largest in the group. While a comparison of the whole group is appropriate, a closer look at the larger cities merits attention not only for pure population reasons, but also for purposes of trying to match up the size of the police force and range of duties that each city undertakes.

Second, the city argued that its wage proposals would maintain Hibbing's relative wage ranking within the historical group and noted that the union's position would greatly advance Hibbing's rankings within the group.

The arbitrator notes that something short of the union's position could be awarded in this conventional arbitration and still maintain Hibbing at the low end of the historical group. The city candidly admitted in its post hearing brief that Hibbing's officers pay is low, especially in comparison with the Range perimeter cities, but argued that Hibbing officers got better benefits.

The city's data on this issue is too incomplete to support a conclusion agreeing with the city's argument that the benefits make up for the loss in pay. The data shows that Hibbing actually receives a relatively equal amount of contribution to health insurance benefits in comparison to Range cities, but a better amount in comparison to most Range Perimeter cities. Missing are data indicating the scope of the plans and other issues. For instance, Grand Rapids shows a VEBA contribution of \$4,600, which is quite large, unless it has a very high deductible plan that is designed to bring down premiums. It could also indicate that it funds a retirement health benefit through its VEBA. As well, the VEBA plans could differ in that some might be recurring contributions and some might not. The point is that there is not enough data to reach good conclusions. Likewise, the data regarding vacations only includes some internal groups and the city listing excludes the Range perimeter cities. Again, the data is inconclusive.

Internal comparisons

A perusal of public sector interest arbitration awards in the last four years shows an increased reliance on internal comparisons, citing the economic hardships caused by the recessionary times we are currently experiencing. The city rightfully argued that internal consistency in general wage increases is especially important under the current conditions. All

the other employees, both represented and unrepresented, will be receiving general wage increases of 0% in 2010, 1% in 2011, and 1% in 2012.

The city did not make a concerted effort to explain its final position that the union here should receive less than the internal percentage wage pattern of 0%, 1% and 1% over the three years in question. However, it argued strenuously that the internal wage adjustments should be replicated in this arbitration, essentially conceding that its second year wage offer of 1/2% was too low. While internal consistency of the general wage percentage increase is a lead factor in determining interest arbitration awards, other internal issues need to be examined. To blindly follow that rule would essentially eliminate the need for collective bargaining in the first place. Having said that, a union or employer that proposes to attain something outside the pattern needs to show a compelling reason why it should be treated differently than other groups.

The Gmach study is enlightening on this issue. If the study would have been implemented, a number of things would have occurred. First, the compensation system would have changed from a "job rate" approach where everyone was paid the same rate within each classification regardless of years of service to a system where each classification would have steps that would increase pay based on years of service. As

indicated earlier, the system change would have cost the city about \$750,000 initially, but would have resulted in long term savings because new hires could be hired at lower entry rates.

Second, job classifications would have been compensated based on the results of the study, which evaluated the classifications and assigned a point value to each based on the methodology of the study. The union's classifications were determined to be undercompensated based on the study, and union members would have attained very large increases over the course of the implementation period.

George Gmach, the author of the study, testified that a core purpose of doing a compensation study such as the one in question is to provide some semblance of "linearity" within the various job classifications and to how they are compensated. This is another form of internal comparison that is relevant in an interest arbitration. If a union or employer can show that some classifications are so out of line within a reasonable range of compensation, adjustments might be called for, absent other overriding circumstances. According to Gmach, the internal relationships in Hibbing were cross-checked with internal relationships in the other comparative cities he chose to ensure validity.

The external and internal comparison analysis lead to the possibility that a wage adjustment in excess of the city's position may be warranted, if

it has the ability to pay for it and if other extenuating circumstances support it.

Ability to Pay

The parties differ greatly on this issue. The city generally states that the economic downturn has hit the Range cities and Hibbing in particular, especially hard. The city's economy is tied to taconite production, which it notes is at its lowest levels since the Great Depression of the 30's. Although taconite production is beginning to come back, Hibbing continues to suffer the effects of the recent recession, with high unemployment rates, low home values and related foreclosures. It notes that Hibbing is inordinately reliant on intergovernmental aids in the form of local government aid (LGA) and taconite aids. It asserts that 60% of its revenues come from these sources, 48% in the form of LGA. Finally, it notes that Hibbing has suffered over \$4 million dollars in reductions in LGA, taconite aids and market value homestead credits since 2008 because of low taconite production, unallotments and other cuts from the legislature.

As a result of these pressures, the city has undertaken an austerity plan that includes unfilled positions, a 10% reduction in the number of positions and high levies, all designed to help weather the economic storm. The result is that the city is currently in a relatively healthy economic status, the extent to which is in contest here.

The union asserts that the city has a more than healthy fund balance. Further, it asserts that the city deceptively under-budgets revenue and over-budgets expenditures. In particular, the union spent considerable time on asserting that the city maintains an excessive amount in unreserved fund balances, estimating that it holds approximately 70% of such funds (in relation to revenues), even though the state auditor recommends a reserve of only 35 to 50%.

The issue of the fund balances vis-à-vis the State Auditor's guidelines highlights the disparate positions of the parties to this arbitration. The parties spent so much time on the issue that it came to be an issue that exemplified the divisions between them. A close examination of this issue is thus warranted.

The city asserts that the fund balance at the end of 2009 equals 46%, in accordance with the standards set by the state auditor. The union asserts that the balance is actually at 70%. If the city is right, it asserts that the fund balance militates towards its position that it cannot afford an increase in wages beyond what it has offered as a final position, because the fund balance is minimally within the amount recommended by the state auditor. If the union is right, it asserts that it supports its position that the city can afford to pay the members of its union the fair wages it is seeking because it shows that the city has a surplus of available funds.

The relevant state auditor guidelines specifically recommend that:

"[A]t year-end local governments maintain an unreserved fund balance in their general fund and special revenue funds of approximately 35 to 50 percent of fund operating revenues or no less than five months of operating expenditures, . . ." Union exhibit 4.

The city maintains that at the end of 2009, it had "an unreserved, designated balance of \$9,134,964 (ER108), of which \$7,203,635 was for cash flow, which equals 46% of the 2010 general fund budget. (ER306)." City post hearing brief, p. 4. Page 306 of the city's exhibits outlines in greater detail how it reached the 46% figure. First, it assumes a budget of \$15,691,273 and then applies the amount of money designated for cash flow (\$7,203,273) to come to its 46% calculation.

The relevant fund balance figure to be applied is all unreserved fund balances that are not otherwise designated for something unchangeable, not simply that which has been designated as reserved for cash flow. Under the guidelines, all the unreserved designated line items could be included in the calculation. In an effort to forestall arguing over this, at a minimum, the amount would include the line items designated for cash flow, designated for state aid reductions and all unreserved undesignated amounts. Using these items in the formula indicates the city's calculation understates the percentage amount that is reserved under the state auditor's guidelines.

On December 31, 2009, if you include all unreserved fund balances enumerated above, the total amount to be used in the state auditor's calculations equal \$8,961,098. This amount is applied to the city's stated total expenditures (city exhibit, page 306) of \$15,691,273 results in a reserve ratio of 57%.

On December 31, 2010, if you include all unreserved fund balances enumerated above, the total amount to be used in the state auditor's calculations equal \$9,245,609. This amount is applied to the city's stated total expenditures (city exhibit, page 306) of \$15,637,417 results in a reserve ratio of 59%.

If the total amount of unreserved fund balances are applied to the formula, the percentage for the two years in question rises to the mid to upper 60 percents.

One final point. The fund balances described herein do not include \$2.2 million in 2010 and \$2.8 million in 2011 that the sewer fund owes the general fund, an amount that will be repaid by raising the sewer rate.

Having said all that, even though the parties spent an inordinate amount of time on this issue, it still is only one indicia of the economic health of the city and is not, by itself, determinative of the wage award that should be rendered herein.

The state auditor's guidelines discussed herein have much to do with the nature of local governmental revenue streams and should not be used as determinative of a city's financial health, standing alone. The guidelines

provide a snapshot view of a local government's finances. Cities like Hibbing receive their revenues mainly in two lump sum periods. A city is reliant on receiving revenues twice per year in property taxes and LGA. The guidelines presuppose an analysis on December 31 of a given year, immediately after receipt of LGA and property taxes for the year. It recommends an unreserved fund balance, therefore, of 35% to 50%, because it assumes that the city will not receive another lump sum payment of LGA or property taxes until 5 or 6 months from that date.

Thus, the whole import of the guidelines is to ensure that local governmental units reserve enough money to meet obligations between the influx of money. Therefore, it is one, and only one, indicia of the financial health of a local governmental unit. In accordance with the state auditor's guidelines, if a local unit of government exceeds the ratio, it should have a justifiable reason for doing so. None was provided here. This leads toward a conclusion that the city is not currently in dire financial shape.

However, there is no question that we are still in the midst of uncertain economic realities, both world-wide and especially state-wide. The city has undertaken numerous financial strategies designed to keep itself in fiscal health. As a result of these strategies, there have been no personnel layoffs and the citizenry will see a zero percent levy in the next year.

In order to get to this point, the city undertook an austerity strategy that included a no layoff provision, which is of benefit to the union. In order to reach its goals, it needed to reduce personnel, through attrition, by 10% over the last four years. Despite this, the union's membership was increased by 3 persons (over the objection of the union). Even though the levy for next year was set at zero per cent, the previous four years of economic hardship resulted in a cumulative 23.64% increase in the city's levy. Unemployment remains high in the city and home values are depressed. The loss in taconite aids and LGA/market value homestead credits unallotted in 2010 and 2011 totaled almost \$3.3 million. The city continues to face the likely possibility of further erosion of LGA and other state aids, but appears to face an optimistic outlook on local taconite aids, all of which it is inordinately reliant upon.

From the evidence and testimony at hearing, it is clear that Hibbing continues to "weather the storm" of economic hardship, due in large measure to the fiscal policies put in place by the city council on the recommendations of its staff for the last 4 years. The decisions made and implemented have obviously not been easy. To award the union's position in full would be counter to the fiscal prudence currently in place and would be irresponsible, given the continued economic outlook.

Having said that, something in excess of the city's position is warranted, given the discussion above. There are compelling facts here which

indicate that the union's job classifications are underpaid relative to the other job classifications within the city. Equally compelling is the clear need for fiscal prudence given the facts and circumstances presented by the city.

It should be noted that the union's arguments concerning the lack of good faith bargaining on the part of the city, meritorious or not, are more properly brought in a different forum. Essentially, it is making an argument that the city has committed unfair labor practices and such complaints belong in district court under PELRA, not in an interest arbitration. Further, as noted earlier, interest arbitration is not a substitute for collective bargaining itself. Successful collective bargaining results in the parties reaching a mutually arrived at decision as to terms and conditions of employment. In those circumstances, the parties live with its own decisions and accept responsibility for them. Interest arbitration can only simulate that agreement and substitutes the decision of an outsider for those of the parties themselves.

The principle that an arbitrator's objective in these matters is to render an award that is reflective of that which the parties would have reached on their own is generally credited to the arbitration book written by Elkouri and Elkouri.

"The fundamental objective of interest arbitration is to formulate awards from the evidence which represents the agreement the parties would have ultimately reached, mindful of whatever influence a work stoppage might theoretically have provided, had the parties

been able to continue negotiating to a successful conclusion." Elkouri and Elkouri, 105 (5th ed. 1997).

As indicated earlier, the parties here are so diametrically opposed in their positions, the circumstances here are akin to a strike situation in nonessential units. For this, and the reasons discussed above, an upward deviation from the internal pattern is warranted, but must be tempered by the ability to pay discussion contained herein.

Accordingly, wages will be adjusted across the board by 0% in 2010, 2% in 2011 and 2% in 2012. No wage adjustment is made for 2010 considering the fact that the public was required to contribute an additional 9.7% in a levy that year and the city was in the midst of its personnel reduction and austerity program. The adjustments will be applied to all employees covered by the collective bargaining unit at the time in question. In other words, the adjustments will apply to retired, severed, and otherwise separated employees covered by this agreement.

Duration

There was almost no discussion of this issue at the hearing or in the post hearing briefs. There being no compelling reason to change the current language, the city's position is awarded and the existing language will remain intact with a duration of three years, 2010, 2011, 2012.

Health Insurance Premiums

The city proposed a change in the amount it paid toward health insurance premiums from 85% to 80% in the second year of the contract. This would be a deviation from that amount that the employer pays for all other units and employees within its jurisdiction.

The parties generally agree that internal consistency is the most important factor when dealing with health insurance issues. They disagree over how that principle is applied. The city's position is that internal consistency is more important in the maintenance of common health care plans in order to avoid administrative burden. It argues that differing premium payments among units is not burdensome.

While the city's arguments here are generally true, it still has the burden of proving that there is a compelling reason to deviate from the pattern established in Hibbing. There is nothing in the record that would support reaching the conclusion that a deviation is called for here.

Accordingly, the union position is awarded its position on this issue and there will be no change in the health insurance article for the duration of the contract.

Summary of Award

The employer's position is awarded on the issue of the duration clause, meaning there will be a three year contract for 2010 through 2012, with no other changes to the current language. The union's position is awarded on the issue of health insurance for the life of the contract, meaning there will be no change to the employer's contribution to the insurance premiums or VEBA payments. Wages will be adjusted by 0% in 2010, 2% in 2011 and 2% in 2012.

Dated: November 23, 2011

A handwritten signature in black ink, appearing to read "Harley M. Ogata". The signature is stylized and cursive, with a long horizontal stroke extending to the right.

Harley M. Ogata
Arbitrator