

# COMPLIANCE AUDIT

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## City of Easton Aggregated Pension Trust Fund Northampton County, Pennsylvania For the Period January 1, 2013 to December 31, 2014

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August 2016



Commonwealth of Pennsylvania  
Department of the Auditor General

Eugene A. DePasquale • Auditor General



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**EUGENE A. DePASQUALE  
AUDITOR GENERAL**

The Honorable Mayor and City Council  
City of Easton  
Northampton County  
Easton, PA 18042

We have conducted a compliance audit of the City of Easton Aggregated Pension Trust Fund for the period January 1, 2013 to December 31, 2014. We also evaluated compliance with some requirements subsequent to that period when possible. The audit was conducted pursuant to authority derived from Section 402(j) of Act 205 and in accordance with the standards applicable to performance audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States. Those standards require that we plan and perform our audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

The objectives of the audit were:

1. To determine if municipal officials took appropriate corrective action to address the findings contained in our prior audit report; and
2. To determine if the pension plan was administered in compliance with applicable state laws, regulations, contracts, administrative procedures, and local ordinances and policies.

Our audit was limited to the areas related to the objectives identified above. To determine if municipal officials took appropriate corrective action to address the findings contained in our prior audit report, we inquired of plan officials and evaluated supporting documentation provided by officials evidencing that the suggested corrective action has been appropriately taken. To determine whether the pension plan was administered in compliance with applicable state laws, regulations, contracts, administrative procedures, and local ordinances and policies, our methodology included the following:

- We determined whether state aid was properly determined and deposited in accordance with Act 205 requirements by verifying the annual deposit date of state aid and determining whether deposits were made within 30 days of receipt for all years within the period under audit.

- We determined whether annual employer contributions were calculated and deposited in accordance with the plan's governing document and applicable laws and regulations by examining the municipality's calculation of the plan's annual financial requirements and minimum municipal obligation (MMO) and comparing these calculated amounts to amounts actually budgeted and deposited into the pension plan as evidenced by supporting documentation.
- We determined whether annual employee contributions were calculated, deducted, and deposited into the pension plan in accordance with the plan's governing document and applicable laws and regulations by testing members' contributions on an annual basis using the rates obtained from the plan's governing document in effect for all years within the period under audit and examining documents evidencing the deposit of these employee contributions into the pension plan.
- We determined whether retirement benefits calculated for the 1 police pension plan member and for the 1 non-uniformed pension plan member who retired during the current audit period represent payments to all (and only) those entitled to receive them and were properly determined and disbursed in accordance with the plan's governing document, applicable laws and regulations by recalculating the amount of the monthly pension benefit due to the retired individuals and comparing these amounts to supporting documentation evidencing amounts determined and actually paid to the recipients.
- We determined whether the January 1, 2011 and January 1, 2013 actuarial valuation reports were prepared and submitted to the Public Employee Retirement Commission (PERC) by March 31, 2012 and 2014, respectively, in accordance with Act 205 and whether selected information provided on these reports is accurate, complete, and in accordance with plan provisions to ensure compliance for participation in the state aid program by comparing selected information to supporting source documentation.
- We determined whether all annual special ad hoc postretirement reimbursements received by the municipality were authorized and appropriately deposited in accordance with Act 147 by tracing information to supporting documentation maintained by plan officials.
- We determined whether the terms and methodologies of the issuance of pension obligation bonds by the municipality, and any restrictions were in compliance with plan provisions and Act 205 through inquiry of plan officials and examination of supporting documentation for pension obligation bonds issued during the current audit period and through the completion of our fieldwork procedures.
- We determined whether provisions of the Deferred Retirement Option Plan (DROP) were in accordance with the provisions of Act 205 by examining provisions stated in the plan's governing documents.

The City of Easton contracted with an independent certified public accounting firm for annual audits of its basic financial statements which are available at the city's offices. Those financial statements were not audited by us and, accordingly, we express no opinion or other form of assurance on them.

City officials are responsible for establishing and maintaining effective internal controls to provide reasonable assurance that the City of Easton Aggregated Pension Trust Fund is administered in compliance with applicable state laws, regulations, contracts, administrative procedures, and local ordinances and policies. In conducting our audit, we obtained an understanding of the city's internal controls as they relate to the city's compliance with those requirements and that we considered to be significant within the context of our audit objectives, and assessed whether those significant controls were properly designed and implemented. Additionally and as previously described, we tested transactions, assessed official actions, performed analytical procedures, and interviewed selected officials to provide reasonable assurance of detecting instances of noncompliance with legal and regulatory requirements or noncompliance with provisions of contracts, administrative procedures, and local ordinances and policies that are significant within the context of the audit objectives.

The results of our procedures indicated that, in all significant respects, the City of Easton Aggregated Pension Trust Fund was administered in compliance with applicable state laws, regulations, contracts, administrative procedures, and local ordinances and policies, except as noted in the following findings further discussed later in this report:

Police Pension Plan

Finding No. 1 - Noncompliance With Prior Audit Recommendation – Inconsistent Benefit Provisions And Provision Of Pension Benefits Not In Compliance With The Third Class City Code

Firemen's Pension Plan

Finding No. 2 - Noncompliance With Prior Audit Recommendation – Provisions Of Benefits Not In Compliance With The Third Class City Code

The findings contained in this audit report repeat conditions that were cited in our previous audit report that have not been corrected by city officials. We are concerned by the city's failure to correct these previously reported audit findings and strongly encourage timely implementation of the recommendations noted in this audit report.

As previously noted, one of the objectives of our audit of the City of Easton Aggregated Pension Trust Fund was to determine compliance with applicable state laws, regulations, contracts, administrative procedures, and local ordinances and policies. Act 205 was amended on September 18, 2009, through the adoption of Act 44 of 2009. Among several provisions relating to municipal pension plans, the act provides for the implementation of a distress recovery program. Three levels of distress have been established:

<u>Level</u>	<u>Indication</u>	<u>Funding Criteria</u>
I	Minimal distress	70-89%
II	Moderate distress	50-69%
III	Severe distress	Less than 50%

The accompanying supplementary information is presented for purposes of additional analysis. We did not audit the information or conclude on it and, accordingly, express no form of assurance on it. However, we are extremely concerned about the historical trend information contained in the respective schedules of funding progress included in this report which indicate a continued decline of assets available to satisfy the long-term liabilities of the fund. For example, **the police pension plan's funded ratio went from a high of 77.3% as of January 1, 2009, to a ratio of 52.1% as of January 1, 2013**, which is the most recent data available. Similarly, **the firemen's pension plan's funded ratio went from 90.4% as of January 1, 2009, to 66.5% as of January 1, 2013**. Finally, **the officers' and employees' pension plan's funded ratio went from 85.2% as of January 1, 2009, to 56.4% as of January 1, 2013**. Based on this information, and the funded status of the city's Officers' and Employees' PMRS Pension Plan, the Public Employee Retirement Commission issued a notification that the city is currently in Level II moderate distress status. We encourage city officials to monitor the funding of its pension plans to ensure their long-term financial stability.

The contents of this report were discussed with officials of the City of Easton and, where appropriate, their responses have been included in the report. We would like to thank city officials for the cooperation extended to us during the conduct of the audit.

This report is a revision of a previously issued report dated November 19, 2015. The report has been revised due to the elimination of the finding that was contained in that report entitled "Incorrect Data On Certification Form AG 64 Resulting In An Excess Reimbursement Of Special 2002 Ad Hoc Postretirement Adjustment."

August 8, 2016

  
EUGENE A. DEPASQUALE  
Auditor General

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## BACKGROUND

On December 18, 1984, the Pennsylvania Legislature adopted the Municipal Pension Plan Funding Standard and Recovery Act (P.L. 1005, No. 205, as amended, 53 P.S. § 895.101 et seq.). The act established mandatory actuarial reporting and funding requirements and a uniform basis for the distribution of state aid to Pennsylvania's public pension plans. Section 402(j) of Act 205 specifically requires the Auditor General, as deemed necessary, to make an audit of every municipality which receives general municipal pension system state aid and of every municipal pension plan and fund in which general municipal pension system state aid is deposited.

Annual state aid allocations are provided from a 2 percent foreign (out-of-state) casualty insurance premium tax, a portion of the foreign (out-of-state) fire insurance tax designated for paid firefighters and any investment income earned on the collection of these taxes. Generally, municipal pension plans established prior to December 18, 1984, are eligible for state aid. For municipal pension plans established after that date, the sponsoring municipality must fund the plan for three plan years before it becomes eligible for state aid. In accordance with Act 205, a municipality's annual state aid allocation cannot exceed its actual pension costs.

In addition to Act 205, the City of Easton Aggregated Pension Trust Fund is also governed by implementing regulations adopted by the Public Employee Retirement Commission published at Title 16, Part IV of the Pennsylvania Code and applicable provisions of various other state statutes including, but not limited to, the following:

- Act 147 - Special Ad Hoc Municipal Police and Firefighter Postretirement Adjustment Act, Act of December 14, 1988 (P.L. 1192, No. 147), as amended, 53 P.S. § 896.101 et seq.
- Act 177 - General Local Government Code, Act of December 19, 1996 (P.L. 1158, No. 177), as amended, 53 Pa.C.S. § 101 et seq.
- Act 317 - The Third Class City Code, Act of June 23, 1931 (P.L. 932, No. 317), as amended, 53 P.S. § 35101 et seq.

The City of Easton Aggregated Pension Trust Fund acts as a common investment and administrative agent for the city's police, firemen's and officers' and employees' defined benefit pension plans. The police pension plan is governed by Chapter 110, Article II of the city's codified ordinances. The firemen's pension plan is governed by Chapter 110, Article V of the city's codified ordinances. The officers' and employees' pension plan is governed by Chapter 110, Article III of the city's codified ordinances for non-uniformed employees hired prior to January 1, 1979. The plans are also affected by the provisions of collective bargaining agreements between the city and its police officers, firefighters and non-uniformed employees. The police pension plan was established July 1, 1923. The firemen's pension plan was established June 23, 1931. The officers' and employees' pension plan for non-uniformed employees hired prior to January 1, 1979, was established May 23, 1945.

## **BACKGROUND – (Continued)**

Active members of the police pension plan are required to contribute 6 percent of compensation to the plan. Active members of the firemen's pension plan are required to contribute 5.5 percent of compensation to the plan. Active members of the officers' and employees' pension plan are required to contribute 6.5 percent of compensation to the plan. As of December 31, 2014, the police pension plan had 62 active members, 1 terminated member eligible for vested benefits in the future, and 76 retirees receiving pension benefits from the plan. As of December 31, 2014, the firemen's pension plan had 43 active members, 1 terminated member eligible for vested benefits in the future, and 45 retirees receiving pension benefits from the plan. As of December 31, 2014, the officers' and employees' pension plan had 4 active members, no terminated members eligible for vested benefits in the future, and 78 retirees receiving pension benefits from the plan.

As of December 31, 2014, selected plan benefit provisions for the police pension plan are as follows:

### Eligibility Requirements:

Normal Retirement	Eligible with 20 years of service.
Early Retirement	None
Vesting	A member is 100% vested after 12 years of service.

### Retirement Benefit:

Benefit equals 50% of final rate of pay plus an incremental pension of 2.5% times final pay for each year of service in excess of 20 years. Maximum pension of 75% of final pay after 30 years of service.

### Survivor Benefit:

If retired, eligible for retirement or killed in service – 100% of benefit to surviving spouse or child under 18.

### Service Related Disability Benefit:

Greater than 15 years of service, benefit based on normal retirement formula. With 12 to 15 years of service, normal retirement pension prorated to 15 years. Less than 12 years of service, normal retirement pension prorated to 20 years.

## **BACKGROUND – (Continued)**

As of December 31, 2014, selected plan benefit provisions for the firemen's pension plan are as follows:

### Eligibility Requirements:

Normal Retirement	Age 50 and 20 years of service.
Early Retirement	None
Vesting	A member is 100% vested after 12 years of service effective January 1, 2009.

### Retirement Benefit:

Benefit equals 50% of highest yearly compensation during the last 5 years (or final pay rate if higher) plus 2.5% of compensation per year of service in excess of 20 years (maximum 75% of compensation) plus an incremental pension (maximum \$100 per month) of 1.25% times compensation for each year of service (before age 65) in excess of 20 years. For members hired after January 1, 2013, 50% of average monthly compensation.

### Survivor Benefit:

If a member with 20 years of service dies or is killed in service, 100% of monthly pension.  
If a member has 12 to 20 years of service, 25% of compensation.

### Service Related Disability Benefit:

The disabled participant will receive full benefits provided by the plan.

## **BACKGROUND – (Continued)**

As of December 31, 2014, selected plan benefit provisions for the officers' and employees' pension plan are as follows:

### Eligibility Requirements:

Normal Retirement	Age 55 and 20 years of service.
Early Retirement	None
Vesting	A member is 100% vested after 12 years of service.

### Retirement Benefit:

Benefit equals 50% of average compensation over the last five years (or final compensation rate if higher), plus an incremental pension of 1.25% of average compensation for each year of service in excess of 20 years.

### Survivor Benefit:

If member has 12 or more years of service, a death benefit is payable to his spouse. Benefit equals 50% of pension prorated for less than 20 years.

### Service Related Disability Benefit:

If a member is vested, disability pension is the accrued benefit to the date of disability.

CITY OF EASTON AGGREGATED PENSION TRUST FUND  
STATUS OF PRIOR FINDINGS

Compliance With Prior Audit Recommendations

The City of Easton has complied with the prior audit recommendations concerning the following:

Aggregated Pension Trust Fund

- Incorrect Data On Certification Form AG 64 Resulting In An Excess Reimbursement Of Special 2002 Ad Hoc Postretirement Adjustment

The city reimbursed \$1,951 to the Commonwealth for the excess ad hoc postretirement adjustment reimbursement received in 2013.

- Failure To Appoint A Chief Administrative Officer

City officials formally appointed the Chief Administrative Officer (CAO) by ordinance.

Officers' And Employees' Pension Plan

- Provision Of Benefits In Excess Of The Third Class City Code

The audit report for the period January 1, 2009, to December 31, 2010, contained a finding that the plan's governing document provided for an early retirement benefit that is not authorized by the Third Class City Code. There are currently no active members who would receive this excess benefit due to all active members being over the age of 55. However, excess benefits are still being paid to 1 retiree. Since the city received state aid based on unit value during the current audit period, it did not receive state aid attributable to the excess benefits provided. The Department will continue to monitor the impact of the excess benefits being paid to the existing retiree on the city's future state aid allocations.

Noncompliance With Prior Audit Recommendations

The City of Easton has not complied with the prior audit recommendations concerning the following as further discussed in the Findings and Recommendations section of this report:

Police Pension Plan

- Inconsistent Benefit Provisions And Provision Of Pension Benefits Not In Compliance With The Third Class City Code

Firemen's Pension Plan

- Provision Of Benefits Not In Compliance With The Third Class City Code

CITY OF EASTON AGGREGATED PENSION TRUST FUND  
FINDINGS AND RECOMMENDATIONS

Police Pension Plan

**Finding No. 1 – Noncompliance With Prior Audit Recommendation – Inconsistent Benefit Provisions And Provision Of Pension Benefits Not In Compliance With The Third Class City Code**

Condition: As disclosed in the prior audit report, prior to January 2, 2008, the City of Easton operated pursuant to the Optional Third Class City Charter Law, Act of July 15, 1957 (P.L. 901, No. 399), as amended, 53 P.S. § 41101 et seq. Consequently, the city’s aggregated pension trust fund was not subject to the constraints of the Third Class City Code. The city adopted a home rule charter pursuant to the Home Rule Charter and Optional Plans Law, 53 Pa. C.S. § 2901 et seq. (previously 53 P.S. § 1-101 et seq.), effective January 2, 2008. Therefore, pursuant to this change, the city’s pension plans must be in compliance with the Third Class City Code for employees hired after the adoption of the home rule charter. Our audit of the police pension plan has revealed that the city is providing benefits to police officers who were hired on or after the effective date noted above that are not in compliance with the Third Class City Code.

In addition, the police pension plan’s governing document, City Codified Ordinances at Chapter 110, Article II, contains benefit provisions that conflict with the collective bargaining agreement between the police officers and the city. The inconsistent benefit provisions and the applicable Third Class City Code provisions are illustrated below:

<u>Benefit Provision</u>	<u>Governing Document</u>	<u>Collective Bargaining Agreement</u>	<u>Third Class City Code</u>
Minimum retirement benefit	The minimum pension payable under this section shall be \$3,000 per year.	Not provided	Not provided
Service requirement	The later of the member’s 50 <sup>th</sup> birthday and the 20 <sup>th</sup> anniversary of the date on which employment commenced.	Any covered employee may make application to retire at 20 years of service regardless of age.	A minimum service requirement of at least 20 years of continuous service for a normal retirement benefit and a minimum age of 50 years, if prescribed.

CITY OF EASTON AGGREGATED PENSION TRUST FUND  
FINDINGS AND RECOMMENDATIONS

Police Pension Plan – (Continued)

**Finding No. 1 – (Continued)**

<u>Benefit Provision</u>	<u>Governing Document</u>	<u>Collective Bargaining Agreement</u>	<u>Third Class City Code</u>
Service-related disability	A service-related disability benefit for participants with 12 or fewer years of service... regardless of age of such participant, he shall be entitled to receive such portion of pension as his service up to the date of his termination bears to 20 years of service.	Not provided	A service-related disability benefit equal to the normal monthly pension benefit, regardless of the time served.
Member's contributions	A participant is required to contribute 6% of pensionable compensation. Each participant is required to contribute \$1 per month for the service increment contribution until the member has reached age 60.	Pension contributions shall be deducted at 6.5% of pensionable wages plus \$2 per pay for survivor's benefits.	A member's contribution rate of up to 5% of the officer's compensation, plus service increment contributions. Service increment contributions are payable only to age 65.

CITY OF EASTON AGGREGATED PENSION TRUST FUND  
FINDINGS AND RECOMMENDATIONS

Police Pension Plan – (Continued)

**Finding No. 1 – (Continued)**

<u>Benefit Provision</u>	<u>Governing Document</u>	<u>Collective Bargaining Agreement</u>	<u>Third Class City Code</u>
Monthly pension benefit	A participant shall receive an annual pension equal to 50% of the employee's pensionable compensation. (Pensionable compensation is defined as the annual salary plus degree pay, longevity pay, personal day buyback, holiday pay, scheduled shift differential, and acting rank pay for regularly scheduled shift of a participant on the date in question.)	Any covered employee with 20 years of service shall be entitled to 50% of pensionable compensation.	The basis of the apportionment of the pension shall be determined by the rate of the monthly pay of the member at the date of injury, death, honorable discharge, vesting under section 4302.1 or retirement, or the highest average annual salary which the member received during any five years of service preceding injury, death, honorable discharge, vesting under section 4302.1 or retirement, whichever is the higher, and except as to service increments provided for in subsection (b) of this section, shall not in any case exceed in any year one-half the annual pay of such member computed at such monthly or average annual rate, whichever is the higher.

CITY OF EASTON AGGREGATED PENSION TRUST FUND  
FINDINGS AND RECOMMENDATIONS

Police Pension Plan – (Continued)

**Finding No. 1 – (Continued)**

<u>Benefit Provision</u>	<u>Governing Document</u>	<u>Collective Bargaining Agreement</u>	<u>Third Class City Code</u>
Service increments	The service increment shall be obtained by computing the number of whole years after 20 years of service, including credit for military service as provided in this plan, and multiplying the number of years so computed by 2.5% of pensionable compensation for each year of service to a maximum of 75% of pensionable compensation after 30 years of service. No employment after the participant has reached the age of 60 years shall be included.	Any covered employee with over 20 years of service shall be entitled to additional service increments of 2.5% of pensionable compensation for each additional year of service to a maximum of seventy-five (75%) of pensionable compensation after thirty (30) years of service. Any employee hired after January 1, 2015 with 20 years of service shall be entitled to a maximum of 50% pensionable compensation with no additional increases.	A service increment provision, indicating that additional benefits accrue to age 65 for service exceeding the minimum required for retirement in an amount equal to 1/40 <sup>th</sup> (2.5%) times the monthly <u>pension benefit</u> for each whole year over the minimum, not to exceed \$500 per month. (Emphasis added)

CITY OF EASTON AGGREGATED PENSION TRUST FUND  
FINDINGS AND RECOMMENDATIONS

Police Pension Plan – (Continued)

**Finding No. 1 – (Continued)**

<u>Benefit Provision</u>	<u>Governing Document</u>	<u>Collective Bargaining Agreement</u>	<u>Third Class City Code</u>
Nonservice-related disability	A participant who has not less than 15 years of service shall be eligible to receive a normal retirement benefit. If the participant has at least 12 years of service but less than 15 years of service, regardless of age of such participant, he shall be entitled to receive such portion of the normal retirement benefit as his service up to the date of termination bears to 20 years of service.	Not provided	For officers with less than 10 years of service, a pension equal to 25% of his annual compensation.  For officers with more than 10 years of service, a pension equal to 50% of annual compensation.

Criteria: On January 24, 2001, the Commonwealth Court of Pennsylvania issued its opinion in *Municipality of Monroeville v. Monroeville Police Department Wage Policy Committee*. Therein, the court held that Section 2962(c)(5) of the Home Rule Charter and Optional Plans Law, 53 Pa. C.S. § 2962(c)(5), “clearly precludes home rule municipalities from providing pension benefits different from those prescribed in general law including Act 600.” The court’s holding was in accord with the position taken by this department since at least January 1995. Therefore, for police officers hired on or after January 2, 2008, the pension plan’s benefit structure should be in compliance with the provisions of the Third Class City Code.

Furthermore, a governing document which contains clearly defined and updated benefit provisions is a prerequisite for the consistent, sound administration of retirement benefits.

Cause: Plan officials failed to establish adequate internal control procedures to ensure compliance with the prior audit recommendation.

CITY OF EASTON AGGREGATED PENSION TRUST FUND  
FINDINGS AND RECOMMENDATIONS

Police Pension Plan – (Continued)

**Finding No. 1 – (Continued)**

Effect: Inconsistent plan documents could result in inconsistent or improper benefit calculations and incorrect benefit payments from the pension plan. In 2011, a member began receiving a retirement benefit at the age of 45 because of the inconsistency between the governing document and the collective bargaining agreement.

Providing unauthorized pension benefits increases the plan's pension costs and reduces the amount of funds available for investment purposes or for the payment of authorized benefits or administrative expenses. Since the city received state aid based on unit value during the current audit period, it did not receive allocations attributable to the excess pension benefits provided. However, the increased costs to the pension plan as a result of the excess pension benefits could result in the receipt of excess state aid in the future and increase the municipal contributions necessary to fund the plan in accordance with Act 205 funding standards.

Furthermore, as previously noted, the plan's governing document contains provisions that could result in plan members receiving pension benefits that are less than what they would be entitled to under the provisions of the Third Class City Code.

Recommendation: We again recommend that the city provide pension benefits in accordance with the Third Class City Code for all police officers who began full-time employment on or after January 2, 2008. To the extent that the city is not in compliance with the Third Class City Code and/or is contractually obligated to provide benefits in excess of those authorized by the Third Class City Code to police officers who began employment on or after January 2, 2008, the excess benefits must be reflected in the Act 205 actuarial valuation reports for the plan and funded in accordance with Act 205 funding standards. Furthermore, such benefits will be deemed ineligible for funding with state pension aid. In such case, the plan's actuary may be required to determine the impact, if any, on the city's future state aid allocations and submit this information to the department.

Furthermore, to the extent that the city has failed to provide benefits which are mandated by the Third Class City Code, we again recommend that the city increase those benefits to the levels prescribed by the code at its earliest opportunity to do so.

We also recommend that municipal officials eliminate the inconsistencies between the plan's governing document and the collective bargaining agreement at their earliest opportunity to do so.

CITY OF EASTON AGGREGATED PENSION TRUST FUND  
FINDINGS AND RECOMMENDATIONS

Police Pension Plan – (Continued)

**Finding No. 1 – (Continued)**

Special note should be taken that the department's application of *Monroeville* only to employees hired on or after January 2, 2008, does not sanction (1) a municipality's granting excess benefits to existing or future employees when none had been granted as of January 2, 2008, or (2) a municipality's increasing excess benefits for existing or future employees beyond those that had been granted as of that date.

Management's Response: At our exit conference held on October 28, 2015, management indicated that they would provide a written response to this finding within 10 days; however, as of November 19, 2015, no such response has been provided.

Auditor's Conclusion: Compliance will be evaluated during our next audit of the plan.

CITY OF EASTON AGGREGATED PENSION TRUST FUND  
FINDINGS AND RECOMMENDATIONS

Firemen’s Pension Plan

**Finding No. 2 – Noncompliance With Prior Audit Recommendation – Provision Of Benefits Not In Compliance With The Third Class City Code**

Condition: As disclosed in the prior audit report, prior to January 2, 2008, the City of Easton operated pursuant to the Optional Third Class City Charter Law, Act of July 15, 1957 (P.L. 901, No. 399), as amended, 53 P.S. § 41101 et seq. Consequently, the city’s aggregated pension trust fund was not subject to the constraints of the Third Class City Code. The city adopted a home rule charter pursuant to the Home Rule Charter and Optional Plans Law, 53 Pa. C.S. § 2901 et seq. (previously 53 P.S. § 1-101 et seq.), effective January 2, 2008. Therefore, pursuant to this change the city’s pension plans must be in compliance with the Third Class City Code for employees hired after the adoption of the home rule charter.

Our audit of the firemen’s pension plan has revealed that the city is providing benefits to firefighters, who were hired on or after the January 2, 2008, effective date that are not in compliance with the Third Class City Code, as noted below:

<u>Benefit Provision</u>	<u>Governing Document</u>	<u>Third Class City Code</u>
Monthly pension benefit	<p>The greater of the compensation at the date of retirement or 1/12 of the highest average annual salary during any five years of service preceding retirement. The multiplier percentage set forth correspondent to years of service; 20 years at 50%, 21 years at 52.5%, 22 years at 55%, 23 years at 57.5%, 24 years at 60%, 25 years at 62.5%, 26 years at 65%, 27 years at 67.5%, 28 years at 70%, 29 years at 72.5%, and 30 years at 75%.</p> <p><i>(Collective bargaining agreement modified provision for members hired after January 1, 2013, to 50% of average monthly compensation.)</i></p>	A monthly pension benefit of 50% of the higher of the monthly salary at the date of termination or the highest average annual salary during any 5 years of service.

CITY OF EASTON AGGREGATED PENSION TRUST FUND  
FINDINGS AND RECOMMENDATIONS

Firemen’s Pension Plan – (Continued)

**Finding No. 2 – (Continued)**

<u>Benefit Provision</u>	<u>Governing Document</u>	<u>Third Class City Code</u>
Definition of salary	A firefighter’s total gross annual compensation, including, without limitation, position salary, longevity pay, degree pay, extra-duty pay, and birthday pay.	A definition of salary as “the fixed amount of compensation paid at regular, periodic intervals by the city to the member and from which pension contributions have been deducted.
Member’s contributions	A monthly contribution equal to 4.5% of compensation, plus an additional 1% of compensation towards the survivor benefit and an additional \$1 per month for the service increment contribution.	A member’s contribution rate of up to 5% of the firefighter’s compensation, plus service increment contributions.
Minimum pension benefit	The pension benefit of any participant who becomes entitled to a pension benefit under the plan shall not be less than \$3,000 annually.	Not provided
Survivor benefit	Nonservice-related death benefits where participant has 20 or more years of service. The surviving spouse of any participant who has retired or died while in service after having served for a minimum of 20 years, shall during their lifetime receive a pension benefit of the amount which would have been payable had the firefighter been retired and 50 years of age at the time of death.	A survivor’s benefit to the surviving spouse of a deceased retiree or employee equal to the amount that the member was receiving or would have been receiving if he was retired, and continuing during the spouse’s life.

CITY OF EASTON AGGREGATED PENSION TRUST FUND  
FINDINGS AND RECOMMENDATIONS

Firemen's Pension Plan – (Continued)

**Finding No. 2 – (Continued)**

Criteria: On January 24, 2001, the Commonwealth Court of Pennsylvania issued its opinion in *Municipality of Monroeville v. Monroeville Police Department Wage Policy Committee*. Therein, the court held that Section 2962(c)(5) of the Home Rule Charter and Optional Plans Law, 53 Pa. C.S. § 2962(c)(5), “clearly precludes home rule municipalities from providing pension benefits different from those prescribed in general law including Act 600.” The court’s holding was in accord with the position taken by this department since at least January 1995.

Therefore, for firefighters hired on or after January 2, 2008, the pension plan’s benefit structure should be in compliance with the Third Class City Code.

Cause: Plan officials failed to establish adequate internal control procedures to ensure compliance with the prior audit recommendation.

Effect: Providing unauthorized pension benefits increases the plan’s pension costs and reduces the amount of funds available for investment purposes or for the payment of authorized benefits or administrative expenses. Since the city received state aid based on unit value during the current audit period, it did not receive allocations attributable to the excess pension benefits provided. However, the increased costs to the pension plan as a result of the excess pension benefits could result in the receipt of excess state aid in the future and increase the municipal contributions necessary to fund the plan in accordance with Act 205 funding standards.

Recommendation: We again recommend that the city provide pension benefits in accordance with the Third Class City Code for all firefighters who began full-time employment on or after January 2, 2008, upon the renewal, extension, or renegotiation of the collective bargaining agreement. To the extent that the city is not in compliance with the Third Class City Code and/or is contractually obligated to provide benefits in excess of those authorized by the Third Class City Code to firefighters who began employment on or after January 2, 2008, the excess benefits must be reflected in the Act 205 actuarial valuation reports for the plan and funded in accordance with Act 205 funding standards. Furthermore, such benefits will be deemed ineligible for funding with state pension aid. In such case, the plan’s actuary may be required to determine the impact, if any, on the city’s future state aid allocations and submit this information to the department.

Special note should be taken that the department’s application of *Monroeville* only to employees hired on or after January 2, 2008, does not sanction (1) a municipality’s granting excess benefits to existing or future employees when none had been granted as of January 2, 2008, or (2) a municipality’s increasing excess benefits for existing or future employees beyond those that had been granted as of that date.

CITY OF EASTON AGGREGATED PENSION TRUST FUND  
FINDINGS AND RECOMMENDATIONS

Firemen's Pension Plan – (Continued)

**Finding No. 2 – (Continued)**

Management's Response: At our exit conference held on October 28, 2015, management indicated that they would provide a written response to this finding within 10 days; however, as of November 19, 2015, no such response has been provided.

Auditor's Conclusion: Compliance will be evaluated during our next audit of the plan.

CITY OF EASTON AGGREGATED PENSION TRUST FUND  
SUPPLEMENTARY INFORMATION  
(UNAUDITED)

The supplementary information contained on Pages 17 through 22 reflect the implementation of GASB Statement No. 67, *Financial Reporting for Pension Plans*. The objective of this statement is to improve financial reporting by state and local governmental pension plans.

SCHEDULE OF CHANGES IN THE NET PENSION  
LIABILITY AND RELATED RATIOS  
POLICE PENSION PLAN  
FOR THE YEAR ENDED DECEMBER 31, 2014

Total Pension Liability	
Service cost	\$ 753,083
Interest	2,506,321
Benefit payments, including refunds of member contributions	(2,085,465)
Net Change in Total Pension Liability	1,173,939
Total Pension Liability - Beginning	33,707,264
Total Pension Liability - Ending (a)	\$ 34,881,203
 Plan Fiduciary Net Position	
Contributions - employer	\$ 1,703,854
Contribution - member	258,853
Net investment income	1,512,997
Benefit payments, including refunds of member contributions	(2,085,465)
Administrative expense	(14,805)
Other	1,020
Net Change in Plan Fiduciary Net Position	1,376,454
Plan Fiduciary Net Position - Beginning	16,889,268
Plan Fiduciary Net Position - Ending (b)	\$ 18,265,722
 Net Pension Liability - Ending (a-b)	\$ 16,615,481
 Plan Fiduciary Net Position as a Percentage of the Total Pension Liability	52.37%
 Estimated Covered Employee Payroll	\$ 4,648,695
 Net Pension Liability as a Percentage of Covered Employee Payroll	357.42%

CITY OF EASTON AGGREGATED PENSION TRUST FUND  
 SUPPLEMENTARY INFORMATION  
 (UNAUDITED)

POLICE PENSION PLAN

Sensitivity of the Net Pension Liability to Changes in the Discount Rate

The following presents the net pension liability of the city, calculated using the discount rate of 7.5%, as well as what the city's net pension liability would be if it were calculated using a discount rate that is 1 percentage-point lower or 1 percentage-point higher than the current rate:

	1% Decrease (6.5%)	Current Discount Rate (7.5%)	1% Increase (8.5%)
Net Pension Liability	\$ 20,404,389	\$ 16,615,481	\$ 12,452,236

SCHEDULE OF CONTRIBUTIONS

Year Ended December 31	Actuarially Determined Contribution	Actual Contributions	Contribution Deficiency (Excess)	Covered- Employee Payroll*	Contributions as a Percentage of Covered- Employee Payroll
2006	\$ 454,129	\$ 454,129	\$ -		
2007	410,195	410,195	-		
2008	414,750	414,750	-		
2009	500,537	500,579	(42)		
2010	485,312	485,312	-		
2011	843,933	843,934	(1)		
2012	761,291	761,291	-		
2013	1,684,086	1,684,086	-		
2014	1,703,854	1,703,854	-	\$4,648,695	36.65%

\* Due to GASB Statement No. 67, *Financial Reporting for Pension Plans*, being implemented only recently, the amount of Covered-Employee Payroll was not provided for years prior to 2014.

SCHEDULE OF INVESTMENT RETURNS

Annual Money-Weighted Rate of Return, Net of Investment Expense:

2014                      6.28%

CITY OF EASTON AGGREGATED PENSION TRUST FUND  
 SUPPLEMENTARY INFORMATION  
 (UNAUDITED)

SCHEDULE OF CHANGES IN THE NET PENSION  
 LIABILITY AND RELATED RATIOS  
 FIREMEN'S PENSION PLAN  
 FOR THE YEAR ENDED DECEMBER 31, 2014

Total Pension Liability	
Service cost	\$ 571,789
Interest	1,900,331
Benefit payments, including refunds of member contributions	(1,120,697)
Net Change in Total Pension Liability	<u>1,351,423</u>
Total Pension Liability – Beginning	25,326,303
Total Pension Liability - Ending (a)	<u><u>\$ 26,677,726</u></u>
Plan Fiduciary Net Position	
Contributions – employer	\$ 1,061,666
Contribution – member	201,891
Net investment income	1,483,012
Benefit payments, including refunds of member contributions	(1,120,697)
Administrative expense	(14,084)
Other	920
Net Change in Plan Fiduciary Net Position	<u>1,612,708</u>
Plan Fiduciary Net Position – Beginning	16,291,120
Plan Fiduciary Net Position - Ending (b)	<u><u>\$ 17,903,828</u></u>
Net Pension Liability - Ending (a-b)	<u><u>\$ 8,773,898</u></u>
Plan Fiduciary Net Position as a Percentage of the Total Pension Liability	67.11%
Estimated Covered Employee Payroll	\$ 3,081,522
Net Pension Liability as a Percentage of Covered Employee Payroll	284.73%

CITY OF EASTON AGGREGATED PENSION TRUST FUND  
 SUPPLEMENTARY INFORMATION  
 (UNAUDITED)

FIREMEN'S PENSION PLAN

Sensitivity of the Net Pension Liability to Changes in the Discount Rate

The following presents the net pension liability of the city, calculated using the discount rate of 7.5%, as well as what the city's net pension liability would be if it were calculated using a discount rate that is 1 percentage-point lower or 1 percentage-point higher than the current rate:

	1% Decrease (6.5%)	Current Discount Rate (7.5%)	1% Increase (8.5%)
Net Pension Liability	\$ 11,852,327	\$ 8,773,898	\$ 6,166,213

SCHEDULE OF CONTRIBUTIONS

Year Ended December 31	Actuarially Determined Contribution	Actual Contributions	Contribution Deficiency (Excess)	Covered- Employee Payroll*	Contributions as a Percentage of Covered- Employee Payroll
2006	\$ 300,816	\$ 300,816	\$ -		
2007	286,277	286,277	-		
2008	290,276	290,276	-		
2009	405,504	405,504	-		
2010	434,626	434,626	-		
2011	434,219	434,219	-		
2012	441,521	441,521	-		
2013	1,073,905	1,073,905	-		
2014	1,061,666	1,061,666	-	\$3,081,522	34.45%

\* Due to GASB Statement No. 67, *Financial Reporting for Pension Plans*, being implemented only recently, the amount of Covered-Employee Payroll was not provided for years prior to 2014.

SCHEDULE OF INVESTMENT RETURNS

Annual Money-Weighted Rate of Return, Net of Investment Expense:

2014                      6.28%

CITY OF EASTON AGGREGATED PENSION TRUST FUND  
SUPPLEMENTARY INFORMATION  
(UNAUDITED)

SCHEDULE OF CHANGES IN THE NET PENSION  
LIABILITY AND RELATED RATIOS  
OFFICERS' AND EMPLOYEES' PENSION PLAN  
FOR THE YEAR ENDED DECEMBER 31, 2014

Total Pension Liability	
Service cost	\$ 17,966
Interest	713,728
Benefit payments, including refunds of member contributions	(1,081,524)
Net Change in Total Pension Liability	<u>(349,830)</u>
Total Pension Liability – Beginning	10,039,171
Total Pension Liability - Ending (a)	<u><u>\$ 9,689,341</u></u>
Plan Fiduciary Net Position	
Contributions – employer	\$ 524,433
Contribution – member	20,384
Net investment income	411,644
Benefit payments, including refunds of member contributions	(1,081,524)
Administrative expense	(10,590)
Other	920
Net Change in Plan Fiduciary Net Position	<u>(134,733)</u>
Plan Fiduciary Net Position - Beginning	5,103,621
Plan Fiduciary Net Position - Ending (b)	<u><u>\$ 4,968,888</u></u>
Net Pension Liability - Ending (a-b)	<u><u>\$ 4,720,453</u></u>
Plan Fiduciary Net Position as a Percentage of the Total Pension Liability	51.28%
Estimated Covered Employee Payroll	\$ 242,604
Net Pension Liability as a Percentage of Covered Employee Payroll	1945.74%

CITY OF EASTON AGGREGATED PENSION TRUST FUND  
 SUPPLEMENTARY INFORMATION  
 (UNAUDITED)

OFFICERS' AND EMPLOYEES' PENSION PLAN

Sensitivity of the Net Pension Liability to Changes in the Discount Rate

The following presents the net pension liability of the city, calculated using the discount rate of 7.5%, as well as what the city's net pension liability would be if it were calculated using a discount rate that is 1 percentage-point lower or 1 percentage-point higher than the current rate:

	1% Decrease (6.5%)	Current Discount Rate (7.5%)	1% Increase (8.5%)
Net Pension Liability	\$ 5,369,517	\$ 4,720,453	\$ 4,144,186

SCHEDULE OF CONTRIBUTIONS

Year Ended December 31	Actuarially Determined Contribution	Actual Contributions	Contribution Deficiency (Excess)	Covered- Employee Payroll*	Contributions as a Percentage of Covered- Employee Payroll
2006	\$ 51,594	\$ 51,594	\$ -		
2007	58,255	58,255	-		
2008	60,647	60,647	-		
2009	54,537	54,537	-		
2010	43,788	43,788	-		
2011	164,399	164,399	-		
2012	157,440	157,440	-		
2013	516,830	516,830	-		
2014	524,433	524,433	-	\$242,604	216.17%

\* Due to GASB Statement No. 67, *Financial Reporting for Pension Plans*, being implemented only recently, the amount of Covered-Employee Payroll was not provided for years prior to 2014.

SCHEDULE OF INVESTMENT RETURNS

Annual Money-Weighted Rate of Return, Net of Investment Expense:

2014                      6.28%

CITY OF EASTON AGGREGATED PENSION TRUST FUND  
 SUPPLEMENTARY INFORMATION  
 (UNAUDITED)

SCHEDULES OF FUNDING PROGRESS

Historical trend information about the plan is presented herewith as supplementary information. It is intended to help users assess the plan’s funding status on a going-concern basis, assess progress made in accumulating assets to pay benefits when due, and make comparisons with other state and local government retirement systems.

The actuarial information is required by Act 205 biennially. The historical information, beginning as of January 1, 2009, is as follows:

POLICE PENSION PLAN

	(1)	(2)	(3)	(4)
Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) - Entry Age (b)	Unfunded (Assets in Excess of) Actuarial Accrued Liability (b) - (a)	Funded Ratio (a)/(b)
01-01-09	\$ 19,483,400	\$ 25,192,009	\$ 5,708,609	77.3%
01-01-11	17,198,135	31,235,456	14,037,321	55.1%
01-01-13	17,016,919	32,634,045	15,617,126	52.1%

The Actuarial Accrued Liability as of 01-01-11 reflects increases due to changes in the actuarial assumption modification and an actuarial loss.

The market value of the plan’s assets at 01-01-09 has been adjusted to reflect the smoothing of gains and/or losses subject to a corridor between 70 to 130 percent of the market value of assets. The market values of the plan’s assets at 01-01-11 and 01-01-13 have been adjusted to reflect the smoothing of gains and/or losses subject to a corridor between 90 to 110 percent of the market value of assets. These methods will lower contributions in years of less than expected returns and increase contributions in years of greater than expected returns. The net effect over long periods of time is to have less variance in contribution levels from year to year.

CITY OF EASTON AGGREGATED PENSION TRUST FUND  
 SUPPLEMENTARY INFORMATION  
 (UNAUDITED)

SCHEDULES OF FUNDING PROGRESS – (Continued)

FIREMEN’S PENSION PLAN

	(1)	(2)	(3)	(4)
Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) - Entry Age (b)	Unfunded (Assets in Excess of) Actuarial Accrued Liability (b) - (a)	Funded Ratio (a)/(b)
01-01-09	\$ 16,463,283	\$ 18,209,105	\$ 1,745,822	90.4%
01-01-11	15,393,967	22,975,675	7,581,708	67.0%
01-01-13	16,029,344	24,115,633	8,086,289	66.5%

The Actuarial Accrued Liability as of 01-01-11 reflects increases due to changes in the actuarial assumption modification, an actuarial loss and a benefit plan modification.

The market value of the plan’s assets at 01-01-09 has been adjusted to reflect the smoothing of gains and/or losses subject to a corridor between 70 to 130 percent of the market value of assets. The market values of the plan’s assets at 01-01-11 and 01-01-13 have been adjusted to reflect the smoothing of gains and/or losses subject to a corridor between 90 to 110 percent of the market value of assets. These methods will lower contributions in years of less than expected returns and increase contributions in years of greater than expected returns. The net effect over long periods of time is to have less variance in contribution levels from year to year.

CITY OF EASTON AGGREGATED PENSION TRUST FUND  
 SUPPLEMENTARY INFORMATION  
 (UNAUDITED)

SCHEDULES OF FUNDING PROGRESS – (Continued)

OFFICERS’ AND EMPLOYEES’ PENSION PLAN

	(1)	(2)	(3)	(4)
Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) - Entry Age (b)	Unfunded (Assets in Excess of) Actuarial Accrued Liability (b) - (a)	Funded Ratio (a)/(b)
01-01-09	\$ 9,891,444	\$ 11,610,437	\$ 1,718,993	85.2%
01-01-11	7,266,589	11,281,826	4,015,237	64.4%
01-01-13	5,868,994	10,414,324	4,545,330	56.4%

Note: The market value of the plan’s assets at 01-01-09 has been adjusted to reflect the smoothing of gains and/or losses subject to a corridor between 70 to 130 percent of the market value of assets. The market values of the plan’s assets at 01-01-11 and 01-01-13 have been adjusted to reflect the smoothing of gains and/or losses subject to a corridor between 90 to 110 percent of the market value of assets. These methods will lower contributions in years of less than expected returns and increase contributions in years of greater than expected returns. The net effect over long periods of time is to have less variance in contribution levels from year to year.

CITY OF EASTON AGGREGATED PENSION TRUST FUND  
SUPPLEMENTARY INFORMATION  
(UNAUDITED)

The comparability of trend information is affected by changes in actuarial assumptions, benefit provisions, actuarial funding methods, accounting policies, and other changes. Those changes usually affect trends in contribution requirements and in ratios that use the actuarial accrued liability as a factor.

Analysis of the dollar amount of the actuarial value of assets, actuarial accrued liability, and unfunded (assets in excess of) actuarial accrued liability in isolation can be misleading. Expressing the actuarial value of assets as a percentage of the actuarial accrued liability (Column 4) provides one indication of the plan's funding status on a going-concern basis. Analysis of this percentage, over time, indicates whether the system is becoming financially stronger or weaker. Generally, the greater this percentage, the stronger the plan.

CITY OF EASTON AGGREGATED PENSION TRUST FUND  
SUPPLEMENTARY INFORMATION  
NOTES TO SUPPLEMENTARY SCHEDULES  
(UNAUDITED)

The information presented in the supplementary schedules was determined as part of the actuarial valuation at the date indicated. Additional information as of the latest actuarial valuation date follows:

POLICE PENSION PLAN

Actuarial valuation date	January 1, 2013
Actuarial cost method	Entry age normal
Amortization method	Level dollar
Remaining amortization period	16 years
Asset valuation method	Plan assets are valued using the method described in Section 210 of Act 205, as amended, subject to a corridor between 90-110% of the market value of assets.
Actuarial assumptions:	
Investment rate of return	7.5%
Projected salary increases	5.0%

CITY OF EASTON AGGREGATED PENSION TRUST FUND  
SUPPLEMENTARY INFORMATION  
NOTES TO SUPPLEMENTARY SCHEDULES  
(UNAUDITED)

FIREMEN'S PENSION PLAN

Actuarial valuation date	January 1, 2013
Actuarial cost method	Entry age normal
Amortization method	Level dollar
Remaining amortization period	14 years
Asset valuation method	Plan assets are valued using the method described in Section 210 of Act 205, as amended, subject to a corridor between 90-110% of the market value of assets.
Actuarial assumptions:	
Investment rate of return	7.5%
Projected salary increases	5.0%

CITY OF EASTON AGGREGATED PENSION TRUST FUND  
SUPPLEMENTARY INFORMATION  
NOTES TO SUPPLEMENTARY SCHEDULES  
(UNAUDITED)

OFFICERS' AND EMPLOYEES' PENSION PLAN

Actuarial valuation date	January 1, 2013
Actuarial cost method	Entry age normal
Amortization method	Level dollar
Remaining amortization period	8 years
Asset valuation method	Plan assets are valued using the method described in Section 210 of Act 205, as amended, subject to a corridor between 90-110% of the market value of assets.
Actuarial assumptions:	
Investment rate of return	7.5%
Projected salary increases	5.0%

CITY OF EASTON AGGREGATED PENSION TRUST FUND  
REPORT DISTRIBUTION LIST

This report was initially distributed to the following:

**The Honorable Tom W. Wolf**  
**Governor**  
Commonwealth of Pennsylvania

City of Easton Aggregated Pension Trust Fund  
Northampton County  
123 South Third Street  
Easton, PA 18042

<b>The Honorable Salvatore J. Panto, Jr.</b>	<b>Mayor</b>
<b>Mr. Glenn Steckman</b>	<b>City Administrator</b>
<b>Ms. Cassandra Williams</b>	<b>Director of Finance</b>
<b>Mr. Tony Bassil</b>	<b>City Controller</b>
<b>Mr. Thomas A. Hess</b>	<b>City Clerk</b>
<b>Mr. Ken Brown</b>	<b>City Council</b>
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