

COMPLIANCE AUDIT

City of Chester Officers and Employees Pension Plan Delaware County, Pennsylvania For the Period January 1, 2020 to December 31, 2022

February 2024



Commonwealth of Pennsylvania
Department of the Auditor General

Timothy L. DeFoor • Auditor General



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**TIMOTHY L. DEFOOR
AUDITOR GENERAL**

The Honorable Mayor and City Council
City of Chester
Delaware County
Chester, PA 19013

We have conducted a compliance audit of the City of Chester Officers and Employees Pension Plan for the period January 1, 2020 to December 31, 2022. We also evaluated compliance with some requirements subsequent to that period when possible. The audit was conducted pursuant to authority derived from the Municipal Pension Plan Funding Standard and Recovery Act (Act 205 of 1984, as amended, 53 P.S. § 895.402(j)). The Act requires the Auditor General, as deemed necessary, to audit every municipality which receives general municipal pension system state aid and every municipal pension plan and fund in which general municipal pension system state aid is deposited. The audit was not conducted, nor was it required to be, in accordance with Government Auditing Standards issued by the Comptroller General of the United States. We planned and performed the 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 report; and
2. To determine if the pension plan was administered in compliance with applicable state laws, regulations, contracts, administrative procedures, 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 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, local ordinances and policies, our methodology included the following:

- We determined whether state aid was properly calculated 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, applicable laws and regulations by examining the municipality's calculation of the plan's annual financial requirements and minimum municipal obligation¹ (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, applicable laws and regulations by testing total 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 plan members who retired, separated employment and received a lump-sum distribution or vested 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 benefits due to the retired individuals and comparing these amounts to supporting documentation evidencing amounts calculated and actually paid or payable to the recipients.
- We determined whether the January 1, 2019, and January 1, 2021, actuarial valuation reports were prepared and submitted by March 31, 2020, and 2022, 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 the pension plan is in compliance with Act 205 for distressed municipalities through inquiry of plan officials and evaluation of the recovery remedies implemented during the audit period.

¹ The minimum municipal obligation (MMO) is an annual calculation of the municipality's annual required contribution to the pension plan, prepared by the municipality pursuant to Act 205 provisions. The annual MMO is due by December 31 and is payable to the pension plan from the revenue of the municipality, which may include general fund contributions or general municipal pension system state aid received by the municipality. 53 P.S. §895.302.

City officials are responsible for establishing and maintaining effective internal controls to provide reasonable assurance that the City of Chester Officers and Employees Pension Plan is administered in compliance with applicable state laws, regulations, contracts, administrative procedures, local ordinances and policies. As previously described, we tested transactions, interviewed selected officials, and performed procedures to the extent necessary to provide reasonable assurance of detecting instances of noncompliance with legal and regulatory requirements or noncompliance with provisions of contracts, administrative procedures, 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 Chester Officers and Employees Pension Plan was administered in compliance with applicable state laws, regulations, contracts, administrative procedures, local ordinances and policies, except as noted in the following findings further discussed later in this report:

- Finding No. 1 – Noncompliance With Prior Audit Recommendation – Provision Of Benefits Inconsistent With Third Class City Code
- Finding No. 2 – Partial Compliance With Prior Audit Recommendation – Failure To Pay The Minimum Municipal Obligation Of The Plan

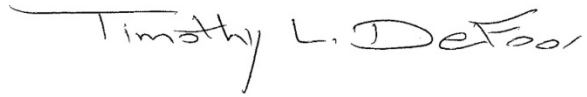
As previously noted, one of the objectives of our audit of the City of Chester Officers and Employees Pension Plan was to determine compliance with applicable state laws, regulations, contracts, administrative procedures, local ordinances and policies. Among several provisions relating to municipal pension plans, Act 205, which was amended on September 18, 2009, through the adoption of Act 44 of 2009, 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 funded status of the plan contained in the schedule of funding progress included in this report which indicates the plan’s funded ratio is 47.2% as of January 1, 2021, which is the most recent data available. Based in part on this information and when combined with the funded status of the city’s other pension plans, the Municipal Pension Reporting Program issued a notification that the aggregate funded status of the city’s plans places the city currently in Level III Severe Distress Status.**²

² It should be noted that the City of Chester filed for Chapter 9 Bankruptcy relief in November of 2022 during this audit period and proceedings are ongoing. The outcome of this filing on the City’s pension plans is unknown at this time.

The contents of this report were discussed with officials of City of Chester and, where appropriate, their responses have been included in the report.

A handwritten signature in black ink that reads "Timothy L. DeFoor". The signature is written in a cursive style with a long horizontal line extending to the left of the first letter.

Timothy L. DeFoor
Auditor General
November 21, 2023

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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.

Annual state aid allocations are provided from a two 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 Chester Officers and Employees Pension Plan is also governed by implementing regulations 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 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 362 - The Third Class City Code, Act of May 23, 1945 (P.L. 903, No. 362), Article XLIII-A, Optional Retirement System for Officers and Employees, as amended, 53 P.S. § 39371 et seq.

The City of Chester Officers and Employees Pension Plan is a single-employer defined benefit pension plan locally controlled by the provisions of Article 145, adopted pursuant to Act 362. The plan is also affected by the provisions of collective bargaining agreements between the city and its non-uniformed employees. The plan was established January 1, 1941. Active members are required to contribute six percent of compensation to the plan if hired prior to January 1, 1988, and three and one-half percent of compensation if hired on or after January 1, 1988. As of December 31, 2022, the plan had 71 active members, 4 terminated members eligible for vested benefit in the future, and 50 retirees receiving pension benefits.

CITY OF CHESTER OFFICERS AND EMPLOYEES PENSION PLAN
STATUS OF PRIOR FINDINGS

Compliance With Prior Recommendation

City of Chester has complied with the prior recommendation concerning the following:

- Deficiencies Relative To The City's Enactment Of The Special Taxing Provisions Of Act 205

During the current audit period, the city developed and implemented adequate procedures to account for the receipt and distribution of tax revenues collected under the special taxing authority afforded by Act 205 and maintained adequate, substantive documentation evidencing that funds collected under the special tax are used solely to defray the additional costs related to its pension plans in accordance with Act 205. City officials also implemented procedures to ensure that the city did not reduce its level of contributions to its pension plans from funding sources prior to the implementation of the special municipal tax in accordance with Act 205 for the years 2021 and 2022.

Partial Compliance With Prior Recommendation

City of Chester has partially complied with the prior recommendation concerning the following:

- Failure To Pay The Minimum Municipal Obligation Of The Plan

During the current audit period, the city fully paid the outstanding minimum municipal obligations (MMOs) for the years 2019 and 2020. However, a similar condition occurred during the current audit period as further discussed in Finding No. 2 of this report.

Noncompliance With Prior Recommendation

City of Chester has not complied with the prior recommendation concerning the following as further discussed in the Findings and Recommendations section of this report:

- Provision Of Benefits Inconsistent With The Third Class City Code

CITY OF CHESTER OFFICERS AND EMPLOYEES PENSION PLAN
FINDINGS AND RECOMMENDATIONS

**Finding No. 1 – Noncompliance With Prior Audit Recommendation – Provision Of Benefits
Inconsistent With The Third Class City Code**

Condition: As previously disclosed in prior audit reports, the city operates as 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.) and the plan’s governing document contains a benefit provision that is inconsistent with the Third Class City Code (Act 362), as noted below:

<u>Benefit</u>	<u>Governing Document</u>	<u>Third Class City Code</u>
Definition of salary	Salary includes regular wages, overtime wages, longevity wages, holiday pay, education benefits and any payments for reimbursement of health premiums.	Salary is the fixed amount of compensation paid at regular, periodic intervals by the city to the member and from which pension contributions have been deducted. ³

Criteria: As previously cited in prior reports, the Commonwealth Court of Pennsylvania issued its opinion on January 24, 2001, 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.” *Municipality of Monroeville v. Monroeville Police Department Wage Policy Committee*, 767 A.2d 596, 598 (Cmmw. Ct. 2001). The court’s holding was in accord with the position taken by this Department since at least January 1995.

Cause: Municipal officials again failed to take appropriate corrective action to comply with the prior audit recommendation.

Effect: Inconsistent benefit provisions may increase the plan’s pension costs and reduce the amount of funds available for investment purposes or the payment of authorized benefits or administrative expenses. Since the city received its state aid allocations based on unit value during the current audit period, it did not receive excess state aid allocations attributable to the benefits provided; however, the provision of inconsistent benefits could result in the receipt of excess state aid in the future or increase required municipal contributions to the plan.

³ 53 P.S. 42004(b)(3)(ii)(B). Part V. Cities of the 3rd Class, Chapter 84- Optional Retirement System.

CITY OF CHESTER OFFICERS AND EMPLOYEES PENSION PLAN
FINDINGS AND RECOMMENDATIONS

Finding No. 1 – (Continued)

Recommendation: The Department acknowledges that until *Monroeville*, there was no definitive decision as to whether home rule municipalities were obliged to comply with applicable pension law. The Department seeks, therefore, to implement the decision in as equitable a fashion as possible, while paying necessary deference to the court’s ruling. Accordingly, the Department will not penalize a home rule municipality for granting benefits not authorized by the Third Class City Code to existing retirees or to individuals who began full-time employment before January 24, 2001 (the date *Monroeville* was issued). However, the Department expects the city to restrict pension benefits to those authorized by the Third Class City Code for all employees who began full-time employment on or after that date.

Special note should be taken that the Department’s application of *Monroeville* only to employees hired on or after January 24, 2001, does not sanction: (1) a municipality’s granting excess benefits to existing or future employees when none had been granted as of January 24, 2001; 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: The city provided the following response:

The city is working with its legal team and the state appointed receivership team to update the governing document to comply with findings as stated.

Auditor’s Conclusion: We are concerned by the city’s continued failure to correct this previously reported audit finding and strongly encourage timely implementation of the recommendation noted in this audit report. Compliance will be evaluated during our next audit of the plan.

Finding No. 2 – Partial Compliance With Prior Audit Recommendation – Failure To Pay The Minimum Municipal Obligation Of The Plan

Condition: As disclosed in the Status of Prior Finding section of this report, the city partially complied with the prior recommendation by depositing the outstanding MMOs due the officers and employees pension plan for the years 2019 and 2020. However, a similar condition occurred during the current audit period. The city did not fully pay the MMOs due the plan for the years 2021 and 2022, in accordance with Act 205. The total MMO for 2021 calculated by the city was \$1,082,728; however, the city made only one deposit in the amount of \$34,362 on December 16, 2022. Additionally, the total MMO for 2022 calculated by the city was \$1,151,538 and remains outstanding as of the date of this report.

CITY OF CHESTER OFFICERS AND EMPLOYEES PENSION PLAN
FINDINGS AND RECOMMENDATIONS

Finding No. 2 – (Continued)

Additionally, although the city has made a formal commitment to pay the full MMOs due the plan by recording these amounts as receivables, thereby including amounts in plan assets, the city has a total unpaid MMO balance for its officers and employees pension plan in the total amount of \$2,426,819 (*\$1,198,160 (including interest) for 2021 and \$1,228,659 (including interest) for 2022*) as determined by the city as of December 31, 2022.

Criteria: With regard to the MMO, Section 302(c) of Act 205 states, in part:

Annually, the chief administrative officer of the pension plan shall determine the minimum obligation of the municipality with respect to the pension plan for the following plan year.

Section 302(d) of Act 205 states, in part:

Annually the municipality shall provide for the full amount of the minimum obligation of the municipality in the budget of the municipality. The minimum obligation of the municipality shall be payable to the pension plan from the revenue of the municipality.

Furthermore, Section 302(e) of Act 205 states:

Any amount of the minimum obligation of the municipality which remains unpaid as of December 31 of the year in which the minimum obligation is due shall be added to the minimum obligation of the municipality for the following year, with interest from January 1 of the year in which the minimum obligation was first due until the date the payment is paid at a rate equal to the interest assumption used for the actuarial valuation report or the discount rate applicable to treasury bills issued by the Department of Treasury of the United States with a six-month maturity as of the last business day in December of the plan year in which the obligation was due, whichever is greater, expressed as a monthly rate and compounded monthly.

Cause: The city could not properly budget for the drastic annual increases in its pension liability and allocate the necessary financial resources to meet its annual municipal pension obligation.

Effect: The failure to fully pay the MMOs could result in the plan not having adequate resources to meet current and future benefit obligations to its members.

CITY OF CHESTER OFFICERS AND EMPLOYEES PENSION PLAN
FINDINGS AND RECOMMENDATIONS

Finding No. 2 – (Continued)

Due to the city's failure to fully pay the 2021 and 2022 MMOs by the December 31, deadlines, the city must add the 2021 and 2022 MMO balances to the current year's MMO and include interest, as required by Act 205.

Furthermore, the city's future state aid allocations may be withheld until the recommendation is complied with.

Recommendation: We recommend that the city pay the outstanding MMOs due the officers and employees pension plan for the years 2021 and 2022 with interest, in accordance with Section 302(e) of Act 205. A copy of the interest calculation must be maintained by the city for examination during our next audit of the plan.

Furthermore, we recommend that in the future, the city determine and pay the full MMO due to the plan in accordance with Act 205 requirements.

Management's Response: The city provided the following response:

The city is continuing to work to fund the pension plans in a timely manner to bring the MMO payments up to date.

Auditor's Conclusion: Due to the potential withhold of state aid, the city's compliance with the finding recommendation will be evaluated subsequent to the release of the audit report and during our next audit of the plan.

CITY OF CHESTER OFFICERS AND EMPLOYEES PENSION PLAN
POTENTIAL WITHHOLD OF STATE AID

A condition of a repeat finding such as that reported by Finding No. 2 contained in this audit report may lead to a total withholding of state aid in the future unless that finding is corrected. However, such action will not be considered if sufficient written documentation is provided to verify compliance with this department's recommendation. Such documentation should be submitted to: Department of the Auditor General, Bureau of Municipal Pension & Liquor Control Audits, 314 Finance Building, Harrisburg, PA 17120.

CITY OF CHESTER OFFICERS AND EMPLOYEES PENSION PLAN
 SUPPLEMENTARY INFORMATION
 (UNAUDITED)

SCHEDULE 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, 2017, is as follows:

	(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)
01-01-17	\$ 2,019,149	\$ 8,350,535	\$ 6,331,386	24.2%
01-01-19	2,674,647	8,028,817	5,354,170	33.3%
01-01-21	4,116,668	8,715,193	4,598,525	47.2%

Note: The market values of the plan’s assets at 01-01-17 and 01-01-19 have been adjusted to reflect the smoothing of gains and/or losses subject to a maximum corridor of 120 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 CHESTER OFFICERS AND EMPLOYEES PENSION PLAN
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 CHESTER OFFICERS AND EMPLOYEES PENSION PLAN
 SUPPLEMENTARY INFORMATION
 (UNAUDITED)

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
2014	\$ 709,116	\$ 709,116	\$ -	\$4,493,142	15.78%
2015	1,010,694	1,010,694	-	4,800,000	21.06%
2016	1,027,873	1,027,873	-	4,836,136	21.25%
2017	754,857	754,857	-	4,920,000	15.34%
2018	638,153	638,153	-	5,206,666	12.26%
2019	810,917	810,917	-	4,974,178	16.30%
2020	1,041,780	1,041,780	-	5,200,000	20.03%
2021	1,082,728	(115,432)	1,198,160	3,200,000	N/A
2022	1,151,538	(77,121)	1,228,659	4,000,000	N/A

Note: The City's 12/31/2022 outstanding MMO balance including interest for 2021-2022 was \$2,426,819 (see Finding No. 2 contained in this report).

The 2021 and 2022 negative contributions made reflect the net imputed interest penalty applied under Act 205, which is the reason the contributions made are negative for 2021 and 2022.

N/A – Not applicable

CITY OF CHESTER OFFICERS AND EMPLOYEES PENSION PLAN
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:

Actuarial valuation date	January 1, 2021
Actuarial cost method	Entry age normal
Amortization method	Level dollar
Remaining amortization period	9 years
Asset valuation method	Market value
Actuarial assumptions:	
Investment rate of return	6.5%
Projected salary increases	5.0%
Cost-of-living adjustments	None assumed

CITY OF CHESTER OFFICERS AND EMPLOYEES PENSION PLAN
REPORT DISTRIBUTION LIST

This report was initially distributed to the following:

The Honorable Joshua D. Shapiro
Governor
Commonwealth of Pennsylvania

The Honorable Stefan Roots
Mayor

Ms. Portia West
Councilwoman

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Councilwoman

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Mr. Shy'Quan Davis
Councilman

Ms. Joy Taylor
City Controller

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