

COMPLIANCE AUDIT

City of Jeannette Firemen's Pension Plan Westmoreland County, Pennsylvania For the Period January 1, 2012 to December 31, 2013

March 2015



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 Jeannette
Westmoreland County
Jeannette, PA 15644

We have conducted a compliance audit of the City of Jeannette Firemen's Pension Plan for the period January 1, 2012 to December 31, 2013. 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. Our methodology addressed determinations about the following:

- Whether state aid was properly determined and deposited in accordance with Act 205 requirements.
- Whether employer contributions are determined and deposited in accordance with the plan's governing document and applicable laws and regulations.

- Whether employee contributions are required and, if so, are determined, deducted, and deposited into the pension plan and are in accordance with the plan provisions and applicable laws and regulations.
- Whether benefit payments, if any, represent payments to all (and only) those entitled to receive them and are properly determined in accordance with applicable laws and regulations.
- Whether obligations for plan benefits are accurately determined in accordance with plan provisions and based on complete and accurate participant data; and whether actuarial valuation reports are prepared and submitted to the Public Employee Retirement Commission (PERC) in accordance with state law and 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.
- Whether the special ad hoc postretirement adjustment granted to eligible pensioners is in accordance with applicable laws and regulations and whether the ad hoc reimbursement received by the municipality was treated in accordance with applicable laws and regulations.
- Whether benefit payments have only been made to living recipients, based on the Social Security numbers found in the pension records for retirees and beneficiaries.
- Whether refunds are made to eligible members in accordance with the plan provisions and applicable laws and regulations.
- Whether the pension plan is in compliance with state regulations for distressed municipalities.

City officials are responsible for establishing and maintaining effective internal controls to provide reasonable assurance that the City of Jeannette Firemen's Pension Plan 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, 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 tests indicated that, in all significant respects, the City of Jeannette Firemen’s Pension Plan 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:

Finding No. 1 – Noncompliance With Prior Recommendation - Failure To Implement Act 44 Mandatory Distressed Provisions

Finding No. 2 – Late Filing Of Certification Form AG 64 Resulting In A Loss Of Reimbursement For Special 2002 Ad Hoc Postretirement Adjustment

Finding No. 1 contained in this audit report repeats a condition that was cited in our previous audit report that has not been corrected by city officials. We are concerned by the city’s failure to correct this previously reported audit finding and strongly encourage timely implementation of the recommendation noted in this report.

As previously noted, one of the objectives of our audit of the City of Jeannette Firemen’s Pension Plan 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 schedule of funding progress included in this report which indicates a continued decline of assets available to satisfy the long-term liabilities of the plan. For example, **the plan’s funded ratio went from 67.6% as of January 1, 2009, to a ratio of 55.1% as of January 1, 2013, which is the most recent date available. Based in part on this information and when combined with the funded status of the city’s other pension plans, 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 the firemen’s pension plan to ensure its long-term financial stability.

As noted in the Comments section of this audit report, effective January 1, 2014, the City of Jeannette raised the Act 205 special municipal pension tax from .15% of earned income to .50% of earned income. The purpose of this tax is to enable municipalities to improve the funding status of its pension plans. Subsequent to this tax increase, on April 21, 2014, the city adopted Ordinance No. 14-03, which provided benefit increases to current and future retirees of the plan. These benefit increases will continue to exacerbate the plan's deteriorating funding status and increase the required municipal contributions necessary to fund the plan in accordance with Act 205 funding standards. We encourage city officials to make fiscally responsible decisions as plan fiduciaries that will benefit the City of Jeannette and its taxpayers to ensure the firemen's pension plan has adequate resources to meet current and future benefit obligations to the city's hard working firefighters.

The contents of this report were discussed with officials of City of Jeannette 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.



EUGENE A. DEPASQUALE
Auditor General

January 16, 2015

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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 Jeannette Firemen's Pension Plan 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 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 Jeannette Firemen's Pension Plan is a single-employer defined benefit pension plan locally controlled by the provisions of Ordinance No. 14-03, dated April 21, 2014, adopted pursuant to Act 317. The plan is also affected by the provisions of collective bargaining agreements between the city and its firefighters. The plan was established February 3, 1966. Active members are required to contribute 5 percent of compensation plus \$1 per month to the plan until age 65. As of December 31, 2013, the plan had 3 active members, no terminated members eligible for vested benefits in the future, and 5 retirees receiving pension benefits from the plan.

BACKGROUND – (Continued)

As of December 31, 2013, selected plan benefit provisions are as follows:

Eligibility Requirements:

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

Retirement Benefit:

A monthly benefit is payable for life equal to 50% of compensation (or Average Compensation averaged over any 5-year period prior to retirement which yields the highest average), plus a monthly service increment of 1/40 of regular pension for each year of completed service in excess of 20 years, prior to age 65, up to a maximum increment of \$500 per month.

Survivor Benefit:

Before Retirement Eligibility	Refund of member contributions will payable to the beneficiary.
After Retirement Eligibility	The surviving spouse will receive 100% of the amount the participant was receiving or entitled to receive payable for life. In the event of the spouse's death (for killed-in-service only), the participant's children under 18 will share the benefit.

Service Related Disability Benefit:

For total and permanent disablement, a monthly benefit for life equal to 50% of the greater of compensation or average compensation.

CITY OF JEANNETTE FIREMEN'S PENSION PLAN
STATUS OF PRIOR FINDING

Noncompliance With Prior Audit Recommendation

The City of Jeannette has not complied with the prior audit recommendation concerning the following as further discussed in the Finding and Recommendation section of this report:

- Failure To Implement Act 44 Mandatory Distressed Provisions

CITY OF JEANNETTE FIREMEN’S PENSION PLAN
FINDINGS AND RECOMMENDATIONS

Finding No. 1 – Noncompliance With Prior Audit Recommendation-Failure To Implement Act 44 Mandatory Distressed Provision

Condition: As disclosed in the prior audit report, the city failed to implement the mandatory distressed provisions of Act 205, as amended. Act 205 was amended on September 18, 2009, through the adoption of Act 44 of 2009, and 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%

Based on the plan’s funded ratio of 58.1% as of January 1, 2011, in aggregation with the funded ratios of the city’s other pension plans, the Public Employee Retirement Commission (PERC) issued a notification in 2012 that the city was in Level II moderate distress status. Based on the plan’s funded ratio of 55.1% as of January 1, 2013, in aggregation with the funded ratios of the city’s other pension plans, PERC issued another notification in 2014 that the city remains in Level II moderate distress status.

Included with the determination notices, PERC sent the city the Act 205 Recovery Program Election Form outlining the mandatory remedies that must be implemented and the voluntary remedies that the city could elect to implement. This form was required to be signed by the plan’s chief administrative officer and returned to PERC.

Although the city submitted the election forms to PERC, the city has not begun to take action to implement the mandatory remedies contained in Act 44 for municipalities in Level II distress regarding the aggregation of its 3 municipal pension funds and the submission of a plan for administrative improvement to PERC.

Criteria: Act 205, amended by Act 44, at Section 605(a), states:

Recovery program level II.

- (a) Mandatory remedies. Any municipality to which level II of the recovery program applies shall utilize the following remedies:
 - (1) The aggregation of trust funds pursuant to section 607(b).
 - (2) The submission of a plan for administrative improvement pursuant to section 607(i).

CITY OF JEANNETTE FIREMEN'S PENSION PLAN
FINDINGS AND RECOMMENDATIONS

Finding No. 1 – (Continued)

Cause: Plan officials failed to establish adequate internal control procedures to ensure that the mandatory distress remedies have been implemented.

Effect: The city is not in compliance with the Act 205, as amended by Act 44, regarding mandatory distress remedy provisions applicable to Level II pension plans which are designed to improve the funding status and administrative efficiency of its pension plans.

Recommendation: We again recommend that city officials contact PERC for guidance in the implementation of the mandatory distress remedies applicable to Level II pursuant to Act 44 of 2009.

Management Response: City officials agreed with the finding without exception.

Auditor Conclusion: We are concerned by the city's failure to correct this previously reported audit finding and strongly encourage timely implementation of the finding recommendation.

Finding No. 2 – Late Filing Of Certification Form AG 64 Resulting In A Loss Of Reimbursement For Special 2002 Ad Hoc Postretirement Adjustment

Condition: The city failed to file the Certification Form AG 64 by the April 1, 2014 deadline, as required by Act 147. This form is required to be annually submitted by municipalities to receive reimbursements for cost of living adjustments provided to retirees who meet the eligibility criteria.

Criteria: Section 502.1(a)(2) of Act 147 states, in part:

The determination of the reimbursable amount of the amortization contribution requirement attributable to the special ad hoc postretirement adjustment under Chapter 4 in any year shall be calculated as the amortization contribution requirement attributable to the special ad hoc postretirement adjustments under Chapter 4 and reflected in the determination of the financial requirements of the pension plan under Chapter 3 of the Municipal Pension Plan Funding Standard and Recovery Act for the immediate prior year less the product of that amortization contribution requirement multiplied by the ratio of the amount of general municipal pension system State aid allocated to the retirement system in the immediate prior year to the total amount of municipal contributions made to the retirement system from all sources other than employee contributions in the immediate prior year.

CITY OF JEANNETTE FIREMEN'S PENSION PLAN
FINDINGS AND RECOMMENDATIONS

Finding No. 2 – (Continued)

In addition, Section 502.1(b) of Act 147 states:

Limitation of eligibility.

- (1) The Commonwealth shall not reimburse any municipality for a special ad hoc adjustment paid under Chapter 4 if the information required under section 901(a)(2) either was not certified to the Auditor General or was certified after April 1 of the year the certification was due.
- (2) The Commonwealth shall not reimburse a municipality for the reimbursable amount of the amortization contribution requirement attributable to the special ad hoc postretirement adjustment under Chapter 4 if the municipality fails to submit a complete certification of the reimbursable amount of the amortization contribution requirement determined under subsection (a) to the Auditor General before April 1 of the year in which the reimbursement is payable.

Cause: Plan officials failed to establish adequate internal control procedures to ensure the Certification Form AG 64 was filed timely in accordance with Act 147 requirements.

Effect: The data submitted on this certification form is used to calculate the reimbursement due the city for ad hoc postretirement adjustments granted pursuant to Chapter 4 of Act 147. As a result of the late filing, the city did not receive a \$1,541 reimbursement from the Commonwealth for the Special 2002 Ad-Hoc Postretirement Adjustments paid in 2013.

Recommendation: We recommend that city officials implement adequate internal control procedures to ensure that future Certification Forms AG 64 are filed timely in accordance with Act 147 requirements.

Management Response: City officials agreed with the finding without exception.

Auditor Conclusion: Compliance will be subject to verification through our next audit.

CITY OF JEANNETTE FIREMEN'S 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, 2009, is as follows:

	(1)	(2)	(3)	(4)	(5)	(6)
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)	Covered Payroll (c)	Unfunded (Assets in Excess of) Actuarial Accrued Liability as a % of Payroll [(b-a)/(c)]
01-01-09	\$ 695,460	\$ 1,029,109	\$ 333,649	67.6%	\$ 176,661	188.9%
01-01-11	678,227	1,166,618	488,391	58.1%	180,563	270.5%
01-01-13	707,588	1,283,584	575,996	55.1%	171,271	336.3%

Note: The market values of the plan's assets at 01-01-09, 01-01-11 and 01-01-13, have been adjusted to reflect the smoothing of gains and/or losses over a 4-year averaging period. This method 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 JEANNETTE FIREMEN'S 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.

Trends in unfunded (assets in excess of) actuarial accrued liability and annual covered payroll are both affected by inflation. Expressing the unfunded (assets in excess of) actuarial accrued liability as a percentage of annual covered payroll (Column 6) approximately adjusts for the effects of inflation and aids analysis of the plan's progress made in accumulating sufficient assets to pay benefits when due. Generally, where there is an unfunded actuarial accrued liability, the smaller this percentage, the stronger the plan. When assets are in excess of the actuarial accrued liability, the higher the bracketed percentage, the stronger the plan.

CITY OF JEANNETTE FIREMEN'S PENSION PLAN
SUPPLEMENTARY INFORMATION
(UNAUDITED)

SCHEDULE OF CONTRIBUTIONS FROM EMPLOYER
AND OTHER CONTRIBUTING ENTITIES

Year Ended December 31	Annual Required Contribution	Percentage Contributed
2008	\$ 24,145	100.0%
2009	42,543	100.0%
2010	41,144	100.0%
2011	55,146	100.0%
2012	54,476	100.0%
2013	87,146	100.0%

CITY OF JEANNETTE FIREMEN'S PENSION PLAN
SUPPLEMENTARY INFORMATION
NOTES TO SUPPLEMENTARY SCHEDULES
(UNAUDITED)

The information presented in the required 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, 2013
Actuarial cost method	Entry age normal
Amortization method	Level dollar, closed
Remaining amortization period	14 years
Asset valuation method	Fair value, 4-year smoothing
Actuarial assumptions:	
Investment rate of return	7.0%
Projected salary increases	5.0%

CITY OF JEANNETTE FIREMEN'S PENSION PLAN
COMMENTS

On January 1, 2011, the City implemented the special municipal taxing authority pursuant to Section 607(f) of Act 205 to assist the city in funding its pension plans. The special earned income tax rate was initially .15% of earned income. During the current audit period, the city increased the rate to .50% effective January 1, 2014.

Subsequently, on April 21, 2014, the City adopted Ordinance No. 14-03 which provides for pension benefit increases to current and future retirees of the firemen's pension plan. The ordinance provides for an increase in the service increment benefit from \$100 to \$500 per month and grants cost of living allowances to members who retired after January 1, 2012.

The City did not obtain an actuarial cost study estimate for providing these pension benefit increases until May 30, 2014, after the benefit increases were formally adopted. This is contrary to Act 205 provisions which require a cost study to be performed prior to the adoption of revised pension benefits. The cost study revealed that the benefit modifications will result in a \$113,200 increase in the pension plan's unfunded actuarial accrued liability and will increase the City's minimum municipal obligation to properly fund the plan in accordance with Act 205 funding standards by \$25,500 annually.

Given the funded status of the firemen's pension plan and the City's imposition of a special municipal pension tax, we encourage City officials to obtain the required cost studies prior to the implementation of any future benefit modifications in order that the City may assess the long-term effects on the plan's funding status.

CITY OF JEANNETTE FIREMEN'S PENSION PLAN
REPORT DISTRIBUTION LIST

This report was initially distributed to the following:

The Honorable Tom W. Wolf
Governor
Commonwealth of Pennsylvania

City of Jeannette Firemen's Pension Plan
Westmoreland County
110 South Second Street
Jeannette, PA 15644

The Honorable Richard R. Jacobelli	Mayor
Mr. Jacob Milliron	City Controller
Mr. Bruce D. Jamison	City Manager

This report is a matter of public record and is available online at www.PaAuditor.gov. Media questions about the report can be directed to the Pennsylvania Department of the Auditor General, Office of Communications, 231 Finance Building, Harrisburg, PA 17120; via email to: news@auditorgen.state.pa.us.