

COMPLIANCE AUDIT

City of Lebanon Paid Firemen's Pension Plan Lebanon County, Pennsylvania For the Period January 1, 2014 to December 31, 2015

October 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 Lebanon
Lebanon County
Lebanon, PA 17042

We have conducted a compliance audit of the City of Lebanon Paid Firemen's Pension Plan for the period January 1, 2014 to December 31, 2015. 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 the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our conclusions based on our audit objective. We believe that the evidence obtained provides a reasonable basis for our conclusions based on our audit objective.

The objective of the audit was 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 objective identified above. 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 all 6 of the plan members who retired during the current audit period, and through the completion of our fieldwork procedures, 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, 2013 and January 1, 2015 actuarial valuation reports were prepared and submitted to the Public Employee Retirement Commission (PERC) by March 31, 2014 and 2016, 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 terms of the plan's 1 unallocated insurance contract, including ownership and any restrictions, were in compliance with plan provisions, investment policies, and state regulations by comparing the terms of the contract with the plan's provisions, investment policies, and state regulations.
- 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 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 Lebanon contracted with an independent certified public accounting firm for an audit of its basic financial statements for the year ending December 31, 2014 which is 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 Lebanon Paid 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 objective, 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 objective.

The results of our procedures indicated that, in all significant respects, the City of Lebanon Paid Firemen's Pension Plan was administered in compliance with applicable state laws, regulations, contracts, administrative procedures, and local ordinances and policies.

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.

The contents of this report were discussed with officials of the City of Lebanon 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.

September 29, 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 Lebanon Paid 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 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 November 24, 2015 (P.L. 242, No. 67), as amended, 11 Pa. C.S. § 10101 et seq.

The City of Lebanon Paid Firemen's Pension Plan is a single-employer defined benefit pension plan locally controlled by the provisions of Ordinance No. 22 of Sessions 2008-2009, as amended, adopted pursuant to Act 317. The plan is also affected by the provisions of collective bargaining agreements between the city and its paid firefighters. The plan was established January 23, 1961. Active members are required to contribute 5 percent of compensation to the plan. As of December 31, 2015, the plan had 16 active members, 1 terminated member eligible for vested benefits in the future, and 27 retirees receiving pension benefits from the plan.

BACKGROUND – (Continued)

As of December 31, 2015, selected plan benefit provisions are as follows:

Eligibility Requirements:

| | |
|-------------------|---|
| Normal Retirement | Hired before July 1, 1972: Age 50 and 20 years of service. Hired after July 1, 1972: Age 50 and 25 years of service. |
| Early Retirement | None |
| Vesting | A member is 100% vested after 12 years of service. |

Retirement Benefit:

Benefit equals 50% of average monthly pay based on last month of employment or highest 60 months of employment, if higher, plus an incremental monthly pension (maximum \$100) of 1/40th of such pension amount, times years of service in excess of 20 years and before age 65.

Survivor Benefit:

The surviving spouse receives 100% of the participant's pension at the time of death. If there is no surviving spouse, the surviving children under age 18 receive 50% of the pension.

Service Related Disability Benefit:

Benefit is 50% of average monthly pay.

Non-Service Related Disability Benefit:

After 10 years of service – 50% of average monthly pay, multiplied by the ratio of actual years of service to date to minimum required years of service for normal retirement.

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

The supplementary information contained on Pages 3 and 4 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
FOR THE YEAR ENDED DECEMBER 31, 2014 AND 2015

| | <u>2014</u> | <u>2015</u> |
|--|---------------------|---------------------|
| Total Pension Liability | | |
| Service cost | \$ 118,290 | \$ 130,055 |
| Interest | 554,125 | 586,986 |
| Difference between expected and actual experience | - | (13,754) |
| Changes of assumptions | - | 109,555 |
| Benefit payments, including refunds of member contributions | (358,004) | (380,418) |
| Net Change in Total Pension Liability | <u>314,411</u> | <u>432,424</u> |
| Total Pension Liability – Beginning | 6,987,269 | 7,301,680 |
| Total Pension Liability - Ending (a) | <u>\$ 7,301,680</u> | <u>\$ 7,734,104</u> |
| | | |
| Plan Fiduciary Net Position | | |
| Contributions – employer | \$ 198,453 | \$ 198,677 |
| Contribution – member | 57,192 | 56,219 |
| Net investment income | 334,395 | (55,148) |
| Benefit payments, including refunds of member contributions | (358,004) | (380,418) |
| Administrative expense | (4,500) | (6,200) |
| Net Change in Plan Fiduciary Net Position | <u>227,536</u> | <u>(186,870)</u> |
| Plan Fiduciary Net Position – Beginning | 6,347,862 | 6,575,398 |
| Plan Fiduciary Net Position - Ending (b) | <u>\$ 6,575,398</u> | <u>\$ 6,388,528</u> |
| | | |
| Net Pension Liability - Ending (a-b) | <u>\$ 726,282</u> | <u>\$ 1,345,576</u> |
| | | |
| Plan Fiduciary Net Position as a Percentage of the Total Pension Liability | 90.05% | 82.60% |
| | | |
| Estimated Covered Employee Payroll | \$ 1,439,664 | \$ 1,477,038 |
| | | |
| Net Pension Liability as a Percentage of Covered Employee Payroll | 50.45% | 91.10% |

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

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 8.0%, 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 (7.0%) | Current Discount Rate (8.0%) | 1% Increase (9.0%) |
|-----------------------|-----------------------|------------------------------------|-----------------------|
| Net Pension Liability | \$ 2,186,239 | \$ 1,345,576 | \$ 635,317 |

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 |
|---------------------------|---|-------------------------|--|---------------------------------|--|
| 2008 | \$ 112,004 | \$ 112,004 | \$ - | \$1,129,502 | 9.92% |
| 2009 | 117,357 | 117,357 | - | 1,291,602 | 9.09% |
| 2010 | 106,388 | 106,388 | - | 1,235,481 | 8.61% |
| 2011 | 177,369 | 177,369 | - | 1,254,922 | 14.13% |
| 2012 | 97,758 | 97,758 | - | 1,311,964 | 7.45% |
| 2013 | 102,870 | 102,870 | - | 1,365,404 | 7.53% |
| 2014 | 198,453 | 198,453 | - | 1,439,664 | 13.78% |
| 2015 | 198,677 | 198,677 | - | 1,477,038 | 13.45% |

SCHEDULE OF INVESTMENT RETURNS

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

| | |
|------|---------|
| 2015 | (0.87%) |
| 2014 | 5.36% |

CITY OF LEBANON PAID 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, 2011, 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) |
| 01-01-11 | \$ 5,879,517 | \$ 6,204,585 | \$ 325,068 | 94.8% |
| 01-01-13 | 5,689,875 | 6,681,630 | 991,755 | 85.2% |
| 01-01-15 | 6,575,398 | 7,397,481 | 822,083 | 88.9% |

Note: 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 over a 5-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 LEBANON PAID 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.

CITY OF LEBANON PAID FIREMEN'S 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, 2015 |
| Actuarial cost method | Entry age normal |
| Amortization method | Level dollar |
| Remaining amortization period | 10 years |
| Asset valuation method | Market value |
| Actuarial assumptions: | |
| Investment rate of return | 8.0% |
| Projected salary increases | 5.0% |
| Cost-of-living adjustments | Annual cost-of-living adjustment for members who retire between 1-1-2009 and 12-31-2017, with a maximum total cost-of-living increase of 10% of the initial pension. |

CITY OF LEBANON PAID FIREMEN'S PENSION PLAN
REPORT DISTRIBUTION LIST

This report was initially distributed to the following:

The Honorable Tom W. Wolf
Governor
Commonwealth of Pennsylvania

The Honorable Sherry Capello
Mayor

Mr. Wiley Parker
City Council Chairperson

Mr. Wayne Carey
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Mr. R. Anthony Matula
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Mr. Richard A. Wertz
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Mr. Cornell Wilson
Council Member

Ms. Debra Gates
Chief Administrative Officer

Ms. Cheryl Gibson
City Clerk

Ms. Helen Westphal
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