COMPLIANCE AUDIT

City of Chester
Firemen's Pension Plan
Delaware County, Pennsylvania
For the Period
January 1, 2018 to December 31, 2019

May 2021

Commonwealth of Pennsylvania
Department of the Auditor General

Timothy L. DeFoor • Auditor General

Commonwealth of Pennsylvania
Department of the Auditor General
Harrisburg, PA 17120-0018
Facebook: Pennsylvania Auditor General
Twitter: @PAAuditorGen
www.PaAuditor.gov

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 Firemen's Pension Plan for the period January 1, 2018 to December 31, 2019. 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)), which 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 finding 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, 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 finding 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, 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[1] (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 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 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 benefits 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, 2017 and January 1, 2019 actuarial valuation reports were prepared and submitted by March 31, 2018 and 2020, 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 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.

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[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.

- 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.

City officials are responsible for establishing and maintaining effective internal controls to provide reasonable assurance that the City of Chester Firemen's Pension Plan is administered in compliance with applicable state laws, regulations, contracts, administrative procedures, and 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, 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 Chester 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 Audit Recommendation – Provision Of Benefits Inconsistent With The Third Class City Code
Finding No. 2	–	Deficiencies Relative To The City's Enactment Of The Special Taxing Provisions Of Act 205
Finding No. 3	–	Failure To Pay The Minimum Municipal Obligation Of The Plan

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

The accompanying supplementary information is presented for purposes of additional analysis. We did not audit the information or conclude on it and, accordingly, we express no form of assurance on it. **We would like to point out that although the funded status of the plan contained in the schedule of funding progress included in this report indicates a funded ratio of 83.4% as of January 1, 2019, 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.**

As noted in the Comments section of this audit report, the City maintains a practice of determining pension benefits for its firefighters based on their final 12 months accumulated earnings or the highest average annual salary during any 5 years (whichever is higher) which includes overtime. During the current audit period, this practice resulted in the average pension benefit determination being approximately 60.9% of the retirees' final average annual base pay. Furthermore, as previously noted, while the current funding ratio of the plan as of January 1, 2019 is 83.4%, this represents a marked decline from the plan's January 1, 2015 funding ratio which was 96.3%. Therefore, we encourage city officials to make fiscally responsible decisions as plan fiduciaries that will benefit the City of Chester and its taxpayers to ensure the city's firemen's pension plan continues to have adequate resources to meet current and future benefit obligations to the city's hard working firefighters that are determined in accordance with the provisions and the intent of the Third Class City Code.

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

Timothy L. DeFoor

April 12, 2021

Timothy L. DeFoor
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.

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 Chester Firemen's 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 67	-	The Third Class City Code, Act of November 24, 2015 (P.L. 242, No. 67), as amended, 11 Pa. C.S. § 10101 et seq.
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.

The City of Chester Firemen's Pension Plan is a single-employer defined benefit pension plan locally controlled by the provisions of Article 147 of the city's codified ordinance, adopted pursuant to Act 67 (formerly 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 December 26, 1972. Active members are required to contribute 5 percent of compensation to the plan. As of December 31, 2019, the plan had 46 active members, no terminated members eligible for vested benefits in the future, and 69 retirees receiving pension benefits.

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

Noncompliance With Prior Audit Recommendation

The City of Chester has not complied with the prior audit 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

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

Condition: 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.). As previously disclosed in the last nine prior audit reports, the city continues to provide pension benefits to its firefighters which are inconsistent with the Third Class City Code. In addition, the collective bargaining agreement between the firefighters and the city contains benefit provisions that are inconsistent with the pension plan's governing document, as follows:

Benefit Provision	Governing Document	Collective Bargaining Agreement	Third Class City Code
Definition of Salary	Salary includes regular wages, overtime wages, longevity wages, holiday pay, education benefits and any payments for reimbursement of health premiums.	For all employees hired on or after December 12, 2011, the term "salary" will be defined as "base pay plus longevity."	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.
Survivor benefit	The widow of any paid fireman, so long as she does not remarry, shall receive a pension benefit of the amount payable to the paid fireman or which would have been payable had he retired at the time of his death.	No provision	Upon the death of a member who retires on pension or is killed in service on or after January 1, 1960, or who dies in the service on or after January 1, 1968, payments as provided under this subchapter shall be made to the member's surviving spouse during the life of the spouse.

Finding No. 1 – (Continued)

Benefit Provision	Governing Document	Collective Bargaining Agreement	Third Class City Code
Normal retirement eligibility	Hired pre 1-1-88, age 50 and 20 years of service; Hired on or after 1-1-88, age 55 and 25 years of service.	Effective 1-1-02, all members eligible after 20 years of service, with no minimum age requirement. All employees hired on or after December 12, 2011, will be eligible to retire after 25 years of service and age 50. All employees hired before December 12, 2011 shall be grandfathered.	At least 20 years of service and, when a minimum age is prescribed, a minimum age of 50.
Calculation of vested benefit	No provision	The number of years of completed service times 2.5% at the time of termination. Pension shall vest at 12 years of service with receipt of pension benefits at age 50.	Benefit is determined by applying to the base amount the percentage that the member's years of service rendered bears to the years of service that would have been rendered had the member continued to be employed by the department until the member's minimum retirement date.

In addition, the actuarial valuation report for the firemen's pension plan, with a valuation date of January 1, 2019, submitted to the Municipal Pension Reporting Program, reported the benefit provisions included in the collective bargaining agreement.

Finding No. 1 – (Continued)

Criteria: As previously disclosed in prior audit reports, the Commonwealth Court of Pennsylvania issued its opinion in *Municipality of Monroeville v. Monroeville Police Department Wage Policy Committee* on January 24, 2001. 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: City officials were again unable to implement compliance with the prior audit recommendation through the collective bargaining process.

Effect: The provision of unauthorized benefits could 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 unauthorized benefits provided; however, the provision of unauthorized benefits could result in the receipt of excess state aid in the future, or increase required municipal contributions to the plan. Furthermore, inconsistent plan documents could result in inconsistent or improper benefit calculations and incorrect benefit payments from the pension plan.

Recommendation: We again recommend that the city restrict pension benefits to those authorized by the Third Class City Code for all employees who began full-time employment on or after January 24, 2001 (the effective date *Monroeville* was decided) at its earliest opportunity to do so.

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 employees who began employment on or after January 24, 2001, 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, of the unauthorized benefits on the city's future state aid allocations and submit this information to the department. If it is determined the unauthorized benefits had an impact on the city's future state aid allocations after the submission of this information, the plan's actuary would then be required to contact the department to verify the overpayment of state aid received. Plan officials would then be required to reimburse the overpayment to the Commonwealth.

In addition, we again recommend that city officials ensure the plan's governing document and the collective bargaining agreement contain consistent benefit provisions at their earliest opportunity to do so.

Finding No. 1 – (Continued)

Management's Response: At our exit conference held on March 23, 2021, municipal officials indicated that a written response to this finding would be provided within 10 days; however, as of May 20, 2021, no such response has been provided.

Auditor's Conclusion: This finding repeats a condition that was cited in our previous nine audit reports that has not been corrected by city officials. 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. Any response to the finding provided by officials subsequent to report issuance will be given due consideration upon receipt and compliance will be evaluated during our next audit of the plan, accordingly.

Finding No. 2 – Deficiencies Relative To The City's Enactment Of The Special Taxing Provisions Of Act 205

Condition: The City of Chester's pension plans were determined to be Level III Distressed by the former Pennsylvania Employee Retirement Commission (PERC). Act 44 of 2009 provides short-term fiscal relief to local governments operating public pension plans and includes discretionary remedies available for distressed municipalities to assist with the funding of their pension plans. Utilizing a special tax provision provided in Act 44, the city adopted Ordinance No. 8-2018 *(effective January 1, 2019)* increasing its Earned Income Tax rate for non-residents of the city for the sole purpose of defraying the additional costs required to be paid pursuant to Act 205 directly related to the city's pension plans. In addition, the city's recovery coordinator prepared the calculation necessary to determine the appropriate funding levels mandated by Act 205 after enacting the special taxing legislation. The city subsequently modified its tax rate by enacting Ordinance No. 5-2020 which effectively re-established its Earned Income Tax rates for both residents (3.75 percent of earnings) and non-residents (2.0 percent of earnings) of the city *(effective January 1, 2021)*. However, this department identified the following deficiencies relative to the city's enactment of the special taxing provisions of Act 205:

- Ordinance No. 8-2018 enacted special taxing authority for non-residents of the city; however, such enactment was contrary to provisions of Act 199.

- Although it appears that the city attempted to rectify the aforementioned inconsistency through the passage of Ordinance No. 5-2020 by re-establishing the city's earned income tax rates for residents and non-residents effective 2021, the ordinance does not specify the amount of tax imposed specifically for the sole purpose of defraying the additional costs required to be paid pursuant to Act 205 directly related to the city's pension plans.

Finding No. 2 – (Continued)

- The city did not establish procedures to adequately account for tax revenues received under the special taxing provisions of Act 205 or to differentiate the amount of tax collected and received from the taxing agent generated pursuant to Act 205 for its distressed pension plans, as opposed to tax revenue generated under Act 511 which can be used for general government purposes during 2019 and 2020.

- The city did not maintain adequate supporting documentation evidencing that amounts received under the special taxing authority of Act 205 and designated for its distressed pension plans were appropriately deposited into the pension plans during 2019 and 2020.

- The city failed to implement procedures to effectively monitor and evidence that required contributions under the special taxing provisions of Act 205 were made by the city to its pension plans during the years 2019 and 2020 from funds in existence prior to implementation of the special tax, in amounts determined by the coordinator.

Additionally, it was further noted that based on records provided during the audit by the taxing entity responsible for collecting local taxes, the city reportedly received tax revenues amounting to $7 million and $3.5 million during 2019 and 2020, respectively. However, the department was unable to determine whether the amounts received under the special taxing provisions of Act 205 were deposited into the city's pension plans and, accordingly, whether the city continued to meet the special tax provisions under Act 205 for the years 2019 and 2020.

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:

> The minimum obligation of the municipality shall be payable to the pension plan from the revenue of the municipality.

Finding No. 2 – (Continued)

Furthermore, relative to the additional remedies available to distressed municipalities to assist with the funding of their pension plans, Section 607(f) of Act 205 further states:

(f) Special municipal taxing authority.

(1) If the tax rates set by the municipality on earned income or on real property are at the maximum provided by applicable law, the municipality may increase its tax on either earned income or real property above those maximum rates. The proceeds of this special municipal tax increase shall be used solely to defray the additional costs required to be paid pursuant to this act, which are directly related to the pension plans of the municipality. The municipality utilizing this special municipal taxing authority shall not reduce the level of municipal contributions to the pension plans prior to the implementation of the special municipal taxing authority. [Emphasis added.]

(2) The average level of municipal contributions to the pension plans from all revenue sources for the three years immediately prior to the implementation of the special municipal taxing authority shall be expressed as a percentage of the average covered payroll for that same three-year period: Provided, however, that any supplemental contributions made to the plans pursuant to any pension recovery legislation enacted by the municipalities shall be excluded for purposes of determining the level of municipal contribution to the pension plans prior to the implementation of the special municipal taxing authority. In each year subsequent to the implementation of the special municipal taxing authority, the municipal contributions to the pension plan from all revenue sources existing prior to the implementation of the special existing municipal taxing authority, reduced by any supplemental pension recovery contributions, shall equal or exceed this average percentage of the current covered payroll. [Emphasis added.] A municipality utilizing the provisions of section 404 may levy or continue to levy the special municipal tax increase under this subsection provided that the municipality does not reduce the level of municipal contributions to the pension plans prior to the implementation of the special municipal taxing authority. In executing the procedure prescribed in this subsection to determine the level of municipal contributions, the debt service payments for bonds or notes issued under section 404 shall be considered municipal contributions.

Finding No. 2 – (Continued)

Moreover, Section 34 of Act 199 of 2014 pertaining to distressed municipalities, states:

> For tax years beginning after the effective date of this section, a financially distressed municipality shall be prohibited from using the special taxing authority in section 607(f) of the act of December 18, 1984 (P.L. 1005, No. 205), known as the Municipal Pension Plan Funding Standard and Recovery Act, to impose an increase in the rate, over the rate imposed as of June 30, 2014, of taxation on nonresident income unless an equal or greater increase in the rate of taxation on resident income, over the highest rate levied in the previous fiscal year, is imposed in the same tax year. [Emphasis added.]

Cause: Although the city's recovery coordinator prepared the calculation necessary to determine the appropriate funding levels mandated by Section 607(f) of Act 205 after enacting the special taxing legislation, the city lacked adequate internal control procedures to ensure that the city did not reduce its level of contributions to its pension plans and from funding sources in effect prior to the implementation of the special municipal tax. Nor did the city maintain appropriate substantive evidence to ensure that funds received under distress provisions of Act 205 were used for their intended purpose.

Effect: The failure to properly apply the provisions of Section 607(f) of Act 205 and fund the pension plans accordingly resulted in less annual funding towards the city's distressed pension plans than afforded under the provisions of Act 205 during 2019 and 2020 and could result in the plans not having the necessary resources to meet current and future benefit obligations to its members. In addition, the failure to maintain the levels of contribution prior to enacting the additional special tax reduced the net overall contributions to the plan, potentially negating benefits of the additional tax. Furthermore, since the city failed to maintain a separate accounting for the tax designated for distressed pension payments, it could not be determined how much was actually received by the city and deposited into its pension plans pursuant to Act 205 for the sole purpose of defraying the additional costs directly related to the city's pension plans during 2019 and 2020.

Recommendation: We recommend that the city develop and implement adequate procedures to account for the receipt and distribution of tax revenues collected under the special taxing authority afforded by Act 205 and maintain 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.

Finding No. 2 – (Continued)

We also recommend that city officials implement adequate internal control procedures to ensure that the city does 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 periods subsequent to this report. Such procedures should include maintaining appropriate supporting documentation identifying the sources of its annual contributions to its pension plans as well as an annual reconciliation evidencing that funding requirements were properly met in accordance with Section 607(f) of Act 205.

Furthermore, we recommend that the city, along with its solicitor, review the ordinance enacting the special taxing authority by the city and ensure compliance with provisions of Act 205 and Act 199.

Finally, we recommend that the city provide documentation that funds previously collected under provisions of Section 607(f) of Act 205 during 2019 and 2020 were used for their intended purpose under the act.

Management's Response: At our exit conference held on March 23, 2021, municipal officials indicated that a written response to this finding would be provided within 10 days; however, as of May 20, 2021, no such response has been provided.

Auditor's Conclusion: Although the municipality did not provide a written response as of the issuance of this report, any response to the finding provided by officials subsequent to report issuance will be given due consideration upon receipt and compliance will be evaluated during our next audit of the plan, accordingly.

Finding No. 3 – Failure To Pay The Minimum Municipal Obligation Of The Plan

Condition: The city did not pay the minimum municipal obligation (MMO) due the firemen's pension plan for the years 2019 and 2020, as required by Act 205. The total MMO for 2019 for the firemen's pension plan as determined by the city amounted to $953,353 and the total MMO for 2020 was $953,107; however, the city did not make any deposits towards the 2019 and 2020 MMOs.

Although the city has made a formal commitment to pay the full amount of the MMOs due the pension plan by recording amounts as receivables, thereby including amounts in plan assets, the city has an unpaid 2019 MMO balance for the firemen's pension plan of $1,107,121 (including interest) and an unpaid 2020 MMO balance for the firemen's pension plan of $1,027,099 (including interest). The interest calculations were provided by the city as of December 31, 2020.

Finding No. 3 – (Continued)

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

Due to the city's failure to pay the 2019 and 2020 MMOs by the December 31, 2019 and 2020 deadlines, the city must add the 2019 and 2020 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 finding recommendation is complied with.

Finding No. 3 – (Continued)

Recommendation: We recommend that the city pay the outstanding MMOs due to the firemen's pension plan for the years 2019 and 2020 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, city officials pay the full MMO due to the plan in accordance with Act 205 requirements.

Management's Response: At our exit conference held on March 23, 2021, municipal officials indicated that a written response to this finding would be provided within 10 days; however, as of May 20, 2021, no such response has been provided.

Auditor's Conclusion: Although the municipality did not provide a written response as of the issuance of this report, any response to the finding provided by officials subsequent to report issuance will be given due consideration upon receipt. 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 FIREMEN’S PENSION PLAN
POTENTIAL WITHHOLD OF STATE AID

A condition such as that reported by Finding No. 3 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 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, 2015, 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)
01-01-15	$ 33,100,351	$ 34,356,625	$ 1,256,274	96.3%
01-01-17	32,822,001	37,679,820	4,857,819	87.1%
01-01-19	33,275,475	39,891,425	6,615,950	83.4%

Note: The market values of the plan's assets at 01-01-15, 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. This method will lower contributions in years of less than expected returns and increase contribution 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 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 CHESTER FIREMEN'S 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	$ 207,303	$ 207,303	$ -	$4,871,554	4.26%
2015	111,792	111,792	-	3,800,000	2.94%
2016	118,972	118,972	-	3,878,908	3.07%
2017	561,281	561,281	-	4,200,000	13.36%
2018	547,892	547,892	-	4,072,364	13.45%
2019	953,353	(74,011)	1,027,364	4,202,254	N/A

Note: The City's 12/31/19 outstanding MMO balance including interest for 2019 was $1,027,364. The City calculated the outstanding 2019 MMO balance including interest to be $1,107,121 as of 12/31/20. See Finding No. 3 contained in the Findings and Recommendations section of this report.

The 2019 negative contribution made reflects the net imputed interest penalty applied under Act 205, which is the reason the contribution made is negative for 2019.

N/A – Not applicable

CITY OF CHESTER 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, 2019
Actuarial cost method	Entry age normal
Amortization method	Level dollar
Remaining amortization period	17 years
Asset valuation method	Plan assets are valued using the method described in Section 210 of Act 205, as amended, subject to a ceiling of 120% of the market value of assets.
Actuarial assumptions:	
Investment rate of return	7.5%
Projected salary increases	5.0%
Cost-of-living adjustments	None assumed

As previously noted in this audit report, the City of Chester Firemen's Pension Plan is governed by local ordinances adopted pursuant to Act 177 and Act 67 (formerly Act 317), the Third Class City Code. With regard to the determination of pension benefits for firefighters, Section 14322 of the Third Class City Code states, in part:

> **§ 14322. Pensions and service increments.**
> **(a) Payments.--**The following apply:
> (1) Payments of pensions shall only be a charge on the firefighters pension fund and shall not be a charge on any other fund under the control, or in the treasury, of the city.
> (2) The basis of the pension of a member shall be determined by the monthly salary of the member at the date of vesting under section 14320.1 (relating to limited vested benefit for firefighters) or retirement or the highest average annual salary which the member received during any five years of service preceding retirement, whichever is higher, whether for disability or by reason of age or service, and, except as to service increments provided for in subsection (b), shall be one-half the annual salary of the member at the time of vesting under section 14320.1 or retirement computed at the monthly or average annual rate, whichever is higher.
> (3) For payment of pensions to members for permanent injury incurred in service and to families of members killed or who die in service, the amount and commencement of the payment of pensions shall be fixed by regulations of the board of managers. These regulations shall not take into consideration the amount and duration of workers' compensation allowed by law. Payments to surviving spouses of members retired on pension or killed in service on or after January 1, 1960, or who die in service on or after January 1, 1968, shall be the amount payable to the member or which would have been payable had the member been retired at the time of the member's death.

Section 14319 of the Third Class City Code defines the term salary as follows:

> **"Salary."** The fixed amount of compensation paid at regular, periodic intervals by the city to the member and from which pension contributions have been deducted.

The city's practice has been to calculate the firefighters' pension benefits based on the amount of the firefighter's final 12 months of salary or the highest average annual salary which the firefighter received during any five years of service preceding retirement, whichever is higher. This includes regular monthly earnings plus overtime that a firefighter accumulates in his or her final 12 months of employment, or the five year period, as applicable. As disclosed in prior audit reports, 11 firefighters retired between January 1, 2013 and December 31, 2017 with non-disability normal retirement pensions which included overtime earnings rather than their regular monthly base pay in the determination of their final 12 month earnings or highest five years used in the calculation of their monthly pension benefits.

CITY OF CHESTER FIREMEN'S PENSION PLAN
COMMENTS

During the current audit period, 5 additional firefighters retired on non-disability normal retirement pensions based on their final 12 months' earnings, or the highest average annual salary during any 5 years, whichever was higher, which included overtime earnings. The city's practice of including these additional overtime earnings for these 16 firefighters since 2013 had a significant impact on not only the individual pension calculations but ultimately the pension plan and the amount of money needed to fund it. The excess payments for these retired firefighters increased the amount needed to fund the plan by approximately $21,348 per month or $256,176 annually, at the time of this audit.

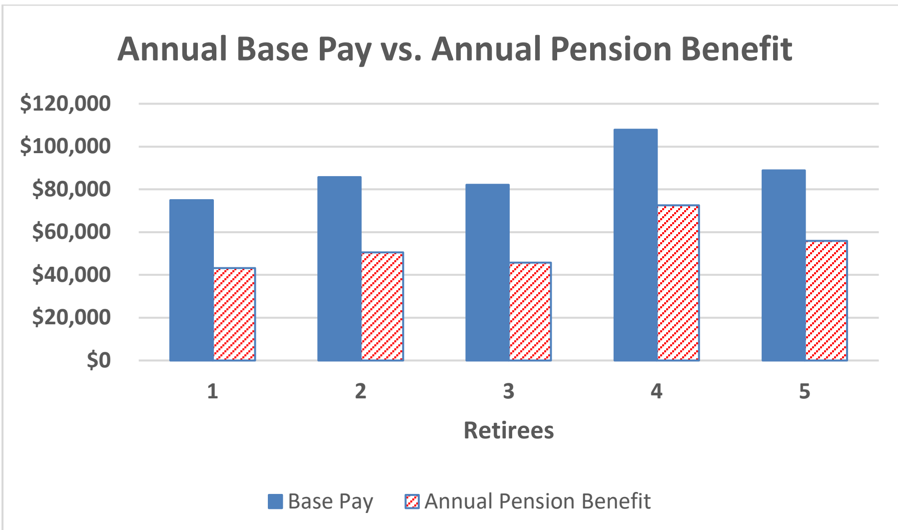
For the 5 aforementioned firefighters who retired during the current audit period, the following chart illustrates the effect that the inclusion of the overtime earnings rather than using the retiree's regular monthly base pay had on the pension calculations, and ultimately, the pension plan and the amount of money required to fund it.

Retiree – Full Years of Service	Overtime Hours	Additional Final 12 Month or 5 Year Earnings For Overtime	Annual Base Pay per contract (including longevity)	Annual Pension Benefit	Monthly Pension Benefit (includes Additional Overtime)	Monthly Pension Benefit (excludes Additional Overtime)	Excess Monthly Pension Benefit Due to Additional Earnings
1 – 25*	907.5**	$ 27,306**	$ 74,954	$ 43,204*	$ 3,600*	$ 3,513*	$ 87
2 – 23*	2,201.75**	82,078**	85,726	50,484*	4,207*	3,840*	367
3 – 20	93.25	4,167	82,106	45,727	3,811	3,637	174
4 – 20	4,912.83**	242,360**	107,801	72,495	6,041	4,786	1,255
5 – 20	503	22,862	88,850	55,856	4,655	3,702	953

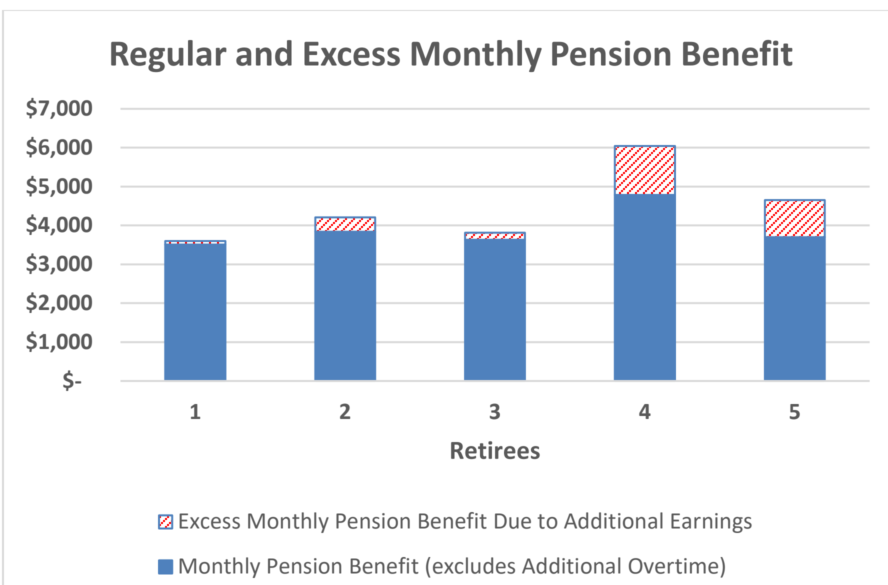
* The final annual pension benefits and monthly pension benefits include service increments determined pursuant to the Third Class City Code, which authorizes additional pension benefits based upon completed years of service in excess of 20 years, not to exceed $500 per month.

** Overtime included for highest 5 year average since pension calculated based on highest 5 year average.

As illustrated in this audit report, through the inclusion of additional earnings, which primarily consisted of overtime, in these 5 retirees' final 12 month earnings (or in the highest average annual salary during any 5 years, as applicable), the retirees are receiving pension benefits that approximate on average 60.9% of the amount of the total base pay earned during the final year of employment with the city. The annual pension benefits compared to the base pay for individual retirees is illustrated below:



The effect of the inclusion of additional earnings on the monthly pension benefits for individual retirees is illustrated below:



CITY OF CHESTER FIREMEN'S PENSION PLAN
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As previously noted in this audit report, the City of Chester is a home rule municipality, and until *Monroeville*, there was no definitive decision as to whether home rule municipalities were obliged to comply with applicable pension law. Consequently, the Department seeks 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 effective date *Monroeville* was decided). 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 the date of that decision.

Although the city's firemen's pension plan is sufficiently funded currently (83.4% as of the most recent valuation), the plan's funding ratio percentage has been declining. We continue to encourage city officials to review the methodology used to calculate pension benefits for its firefighters. The city's practice of allowing firefighters the opportunity to accumulate large amounts of overtime during their last 12 months of employment and including that compensation in the calculation of pension benefits has created apparent windfalls for retirees, thwarted actuarial projections and potentially jeopardizes the fiscal soundness of the pension plan.

CITY OF CHESTER FIREMEN'S PENSION PLAN
REPORT DISTRIBUTION LIST

This report was initially distributed to the following:

The Honorable Tom W. Wolf
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Commonwealth of Pennsylvania

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Councilwoman

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Councilwoman

Mr. William A. Jacobs
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City Controller

Mr. Michael T. Doweary
Receiver, Commonwealth of Pennsylvania

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