

COMPLIANCE AUDIT

City of Carbondale Aggregate Pension Plan Lackawanna County, Pennsylvania For the Period January 1, 2017 to December 31, 2018

August 2019



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 Carbondale
Lackawanna County
Carbondale, PA 18407

We have conducted a compliance audit of the City of Carbondale Aggregate Pension Plan for the period January 1, 2017 to December 31, 2018. We also evaluated compliance with some requirements subsequent to that period when possible. The audit was conducted pursuant to authority derived from Section 402(j) of Act 205 and in accordance with the standards applicable to performance audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States. Those standards require that we plan and perform our audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

The objectives of the audit were:

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

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

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

- We determined whether annual employer contributions were calculated and deposited in accordance with the plan's governing document and applicable laws and regulations by examining the municipality's calculation of the plan's annual financial requirements and minimum municipal obligation (MMO) and comparing these calculated amounts to amounts actually budgeted and deposited into the pension plan as evidenced by supporting documentation.
- We determined whether annual employee contributions were calculated, deducted, and deposited into the pension plan in accordance with the plan's governing document and applicable laws and regulations by testing 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 that there were no benefit calculations prepared for the years covered by our audit period.
- We determined whether the January 1, 2015 and January 1, 2017 actuarial valuation reports were prepared and submitted by March 31, 2016 and 2018, respectively, in accordance with Act 205 and whether selected information provided on these reports is accurate, complete, and in accordance with plan provisions to ensure compliance for participation in the state aid program by comparing selected information to supporting source documentation.
- We determined whether all annual special ad hoc postretirement reimbursements received by the municipality were authorized and appropriately deposited in accordance with Act 147 by tracing information to supporting documentation maintained by plan officials.
- We determined whether the terms and methodologies of the issuance of pension obligation bonds by the municipality, and any restrictions were in compliance with plan provisions and Act 205 through inquiry of plan officials and examination of supporting documentation for pension obligation bonds issued during the current audit period and through the completion of our fieldwork procedures.

The City of Carbondale contracted with an independent certified public accounting firm for an audit of its basic financial statements for the year ended December 31, 2017, which are available at the city's offices. Those financial statements were not audited by us and, accordingly, we express no opinion or other form of assurance on them.

City officials are responsible for establishing and maintaining effective internal controls to provide reasonable assurance that the City of Carbondale Aggregate 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 and as previously described, we tested transactions, assessed official actions, performed analytical procedures, and interviewed selected officials to provide reasonable assurance of detecting instances of noncompliance with legal and regulatory requirements or noncompliance with provisions of contracts, administrative procedures, and local ordinances and policies that are significant within the context of the audit objectives.

The results of our procedures indicated that, in all significant respects, the City of Carbondale Aggregate 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 – Noncompliance With Prior Audit Recommendation – Failure To Properly Determine And Fully Pay The Minimum Municipal Obligations Of The Plans

The finding 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 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, express no form of assurance on it.

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

August 9, 2019



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 Carbondale Aggregate Pension Plan is also governed by implementing regulations adopted by the former 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 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 Carbondale Aggregate Pension Fund retains the assets and acts as a common investment and administrative agent for the city's police and firemen's pension plans. The police and firemen's pension plans are single-employer defined benefit pension plans locally controlled by the provisions of Chapter 27 of the city's code of ordinances, adopted pursuant to Act 67. The plans are also affected by the provisions of collective bargaining agreements between the city and its police officers and firefighters. The police pension plan was established August 7, 1950 and the firemen's pension plan was established December 19, 1949. Active members of both plans are required to contribute 5 percent of salary to their respective plans.

BACKGROUND – (Continued)

As of December 31, 2018, the police pension plan had 10 active members, no terminated members eligible for vested benefits in the future, and 19 retirees receiving pension benefits from the plan.

As of December 31, 2018, the firemen’s pension plan had 6 active members, no terminated members eligible for vested benefits in the future, and 5 retirees receiving pension benefits from the plan.

As of December 31, 2018, selected plan benefit provisions are as follows:

POLICE PENSION PLAN

Eligibility Requirements:

- Normal Retirement Age 50 and 20 years of service.
- Early Retirement None
- Vesting Member is 100% vested after 12 years of service.

Retirement Benefit:

Benefit equals 50% of average pay, plus 1.25% of pay per year of service in excess of 25 years (maximum \$100).

Survivor Benefit:

If retired or eligible to retire – 50% of benefit. If killed in service after 10 years - 40% of pay. Before 10 years – 20% of pay.

Service Related Disability Benefit:

Benefit equals 40% of pay after 10 years, 20% of pay before 10 years.

BACKGROUND – (Continued)

FIREMEN’S PENSION PLAN

Eligibility Requirements:

Normal Retirement	Hired before 1/1/87: 20 years of service. Hired after 1/1/87: Age 55 and 20 years of service.
Early Retirement	Hired before 1/1/87: None Hired after 1/1/87: Age 50 and 20 years of service.
Vesting	100% vesting after 12 years of service.

Retirement Benefit:

Hired before 1/1/87: Benefit equals 50% of final pay, plus 1.25% of pay per year of service in excess of 20 years (maximum \$100).

Hired after 1/1/87: Benefit equals 50% of final pay, plus 1.25% of pay per year of service in excess of 25 years (maximum \$100).

Survivor Benefit:

Hired before 1/1/87: If retired or eligible to retire – Benefit equals 100% of benefit.

Hired after 1/1/87: If retired or eligible to retire – Benefit equals 50% of benefit.

If killed in service after 10 years - 40% of pay. Before 10 years - 20% of pay.

Service Related Disability Benefit:

Hired before 1/1/87: Benefit equals 50% of pay.

Hired after 1/1/87: Benefit equals 40% of pay after 10 years, 20% of pay before 10 years.

CITY OF CARBONDALE AGGREGATE PENSION PLAN
STATUS OF PRIOR FINDINGS

Status Of Prior Audit Findings

Firemen's Pension Plan

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

As disclosed in the prior four audit reports, the collective bargaining agreement between the city and its firemen continues to provide a cost-of-living allowance to its firefighters in excess of the restrictions found in the Third Class City Code. During the current audit, it was determined that the City has continued to provide a cost-of-living allowance in excess of the restrictions found in the Third Class City Code. The city received its state aid based on unit value during the current audit period, therefore, the city did not receive any state aid attributable to the excess benefits provided. The Department will continue to monitor the effect of the excess benefit on the city's future state aid allocations during subsequent audits of the plan.

Police Pension Plan

· Pension Benefits In Excess Of The Third Class City Code

As disclosed in the prior three audit reports, the plan's governing document grants benefits that are not authorized by the Third Class City Code. The city created a "one-time" Retirement Incentive Program for full-time police officers with at least 20 years of service as of February 19, 2013. The city amended the incentive program in March 2013 to include an incentive for any full-time police officer eligible for a disability pension as of March 18, 2013. Under these incentives the city is paying pension benefits to four retirees in excess of those benefits authorized by the Third Class City Code. Additionally, as disclosed in the prior audit report, the city amended the incentive program in August 2016 for full-time police officers with at least 20 years of service as of July 16, 2016 and under this incentive the city is paying pension benefits to one retiree in excess of those authorized by the Third Class City Code. During the current audit, it was determined that these excess benefits are still being paid to existing retirees. Given the city's position on this matter and considering that the city received its state aid based on unit value during the current audit period and, therefore, did not receive any state aid attributable to the excess benefits provided, the finding will not be repeated in this audit report. The Department will, however, continue to monitor the effect of the excess benefits on the city's future state aid allocations during subsequent audits of the plan.

CITY OF CARBONDALE AGGREGATE PENSION PLAN
STATUS OF PRIOR FINDINGS

Noncompliance With Prior Audit Recommendation

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

Police Pension Plan

- Failure To Properly Determine And Fully Pay The Minimum Municipal Obligations Of The Plans

CITY OF CARBONDALE AGGREGATE PENSION PLAN
FINDING AND RECOMMENDATION

Finding – Noncompliance With Prior Audit Recommendation – Failure To Properly Determine And Fully Pay The Minimum Municipal Obligations Of The Plans

Condition: As disclosed in the prior audit report, plan officials did not properly determine or fully pay the minimum municipal obligation (MMOs) of the police and firemen’s pension plans for the years 2015 and 2016, as required by Act 205. The MMO determined by the city for the police pension plan for 2015 and 2016 understated payroll by \$72,411 and \$47,096, respectively. In addition, the MMO determined by the city for the firemen’s pension plan for 2015 and 2016 also understated payroll by \$69,817 and \$54,505, respectively. Based upon an estimate prepared by this department, the city had unpaid MMO balances of \$6,345 and \$4,271 for the police pension plan and outstanding MMO balances of \$3,454 and \$2,469 for the firemen’s pension plan for the years 2015 and 2016, respectively. In addition, the MMO determined by the city for the police pension plan for 2019 understated payroll by \$106,407 and based upon an estimate prepared by this department, the city had an underestimated MMO of \$9,176 for the police pension plan for the year 2019, which is due to be paid to the plan by December 31, 2019.

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.

With regard to the payroll estimate used in the preparation of the MMO, the Pennsylvania Code, Title 16, Section 204.1(c)(1) states, in part:

The payroll used in determining the minimum municipal obligation of a pension plan under section 302(c) of the act shall be based on the payroll to be reported on the Internal Revenue Service Form W-2 and shall be calculated as the total payroll for active members of the plan as of the date of the determination, plus the payroll for the same active members of the plan projected to the year’s end using the payroll rates in effect as of the date of the determination.

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.

CITY OF CARBONDALE AGGREGATE PENSION PLAN
FINDING AND RECOMMENDATION

Finding – (Continued)

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 again failed to establish adequate internal control procedures to ensure the accuracy of MMO calculations. City officials indicated the failure to comply with the prior audit recommendation was an oversight by the city.

Effect: The proper determination of the plan's MMO ensures plan officials can properly allocate the necessary resources to the pension plan for the upcoming year. The failure to fully pay the MMO could result in the plan not having adequate resources to meet current and future benefit obligations to its members.

Due to the municipality's failure to fully pay the police and firemen's MMOs by the December 31, 2015 and 2016 deadlines, the city must add the police and firemen's outstanding MMO balances to the current year's MMOs and include interest, as required by Act 205.

Recommendation: We again recommend that the city pay the outstanding MMOs due to the police and firemen's pension plans for the years 2015 and 2016, with interest, in accordance with Section 302(e) of Act 205. A copy of the interest calculations must be maintained by the city for examination during our next audit of the plan. We also recommend that the city's payment to the police pension plan for its 2019 MMO, due December 31, 2019, include the \$9,176 cited in the Condition above.

Furthermore, we again recommend that, in the future, plan officials properly determine the amount of payroll to be used in the MMO calculations and pay the full MMOs due the city's pension plans.

CITY OF CARBONDALE AGGREGATE PENSION PLAN
FINDING AND RECOMMENDATION

Finding – (Continued)

Management's Response: City officials agreed with the finding without exception and stated that the city will fund the shortfall and will review the MMOs annually to ensure they are prepared properly.

Auditor's Conclusion: Based on the management response, it appears municipal officials intend to comply with the finding recommendation. Compliance will be evaluated during our next audit of the plan.

CITY OF CARBONDALE AGGREGATE PENSION FUND
 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, 2013, is as follows:

POLICE PENSION PLAN

	(1)	(2)	(3)	(4)
Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) - Entry Age (b)	Unfunded (Assets in Excess of) Actuarial Accrued Liability (b) - (a)	Funded Ratio (a)/(b)
01-01-13	\$ 4,932,574	\$ 5,477,190	\$ 544,616	90.1%
01-01-15	5,203,029	6,420,726	1,217,697	81.0%
01-01-17	5,132,591	7,178,250	2,045,659	71.5%

Note: The market values of the plan's assets at 01-01-13, 01-01-15, and 01-01-17 have been adjusted to reflect the smoothing of gains and/or losses over a five-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.

Due to investment experience that was less than expected since the last valuation, the plan's unfunded actuarial accrued liability increased to \$2,045,659 as of January 1, 2017.

CITY OF CARBONDALE AGGREGATE PENSION FUND
 SUPPLEMENTARY INFORMATION
 (UNAUDITED)

SCHEDULE OF FUNDING PROGRESS – (Continued)

FIREMEN’S PENSION PLAN

	(1)	(2)	(3)	(4)
Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) - Entry Age (b)	Unfunded (Assets in Excess of) Actuarial Accrued Liability (b) - (a)	Funded Ratio (a)/(b)
01-01-13	\$ 3,084,629	\$ 3,336,363	\$ 251,734	92.5%
01-01-15	3,415,310	3,963,562	548,252	86.2%
01-01-17	3,387,847	4,372,788	984,941	77.5%

Note: The market values of the plan’s assets at 01-01-13, 01-01-15, and 01-01-17 have been adjusted to reflect the smoothing of gains and/or losses over a five-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.

Due to investment experience that was less than expected since the last valuation, the plan’s unfunded actuarial accrued liability increased to \$984,941 as of January 1, 2017.

CITY OF CARBONDALE AGGREGATE PENSION FUND
SUPPLEMENTARY INFORMATION
(UNAUDITED)

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

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

CITY OF CARBONDALE AGGREGATE PENSION FUND
 SUPPLEMENTARY INFORMATION
 (UNAUDITED)

SCHEDULE OF CONTRIBUTIONS FROM EMPLOYER
 AND OTHER CONTRIBUTING ENTITIES

POLICE PENSION PLAN

Year Ended December 31	Annual Required Contribution	Percentage Contributed
2013	\$ 237,597	100.0%
2014	202,527	100.0%
2015	207,980	*96.9%
2016	207,021	*97.9%
2017	341,478	100.0%
2018	93,253	100.0%

** See the finding contained in this report.*

CITY OF CARBONDALE AGGREGATE PENSION PLAN
 SUPPLEMENTARY INFORMATION
 (UNAUDITED)

FIREMEN’S PENSION PLAN

Year Ended December 31	Annual Required Contribution	Percentage Contributed
2013	\$ 59,970	100.0%
2014	63,881	100.0%
2015	85,434	*96.0%
2016	81,745	*97.0%
2017	130,880	100.0%
2018	44,441	100.0%

* See the finding contained in this report.

CITY OF CARBONDALE AGGREGATE PENSION FUND
SUPPLEMENTARY INFORMATION
NOTES TO SUPPLEMENTARY SCHEDULES
(UNAUDITED)

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

POLICE PENSION PLAN

Actuarial valuation date	January 1, 2017
Actuarial cost method	Entry age normal
Amortization method	Level dollar
Remaining amortization period	7 years
Asset valuation method	Fair value, 5-year smoothing
Actuarial assumptions:	
Investment rate of return	7.75%
Projected salary increases	4.75%
Cost-of-living adjustments	1.0% per year postretirement

CITY OF CARBONDALE AGGREGATE PENSION PLAN
SUPPLEMENTARY INFORMATION
NOTES TO SUPPLEMENTARY SCHEDULES
(UNAUDITED)

FIREMEN'S PENSION PLAN

Actuarial valuation date	January 1, 2017
Actuarial cost method	Entry age normal
Amortization method	Level dollar
Remaining amortization period	8 years
Asset valuation method	Fair value, 5-year smoothing
Actuarial assumptions:	
Investment rate of return	7.75%
Projected salary increases	4.75%
Cost-of-living adjustments	2.5% per year postretirement

CITY OF CARBONDALE AGGREGATE PENSION PLAN
REPORT DISTRIBUTION LIST

This report was initially distributed to the following:

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