

COMPLIANCE AUDIT

City of Farrell Police Pension Plan Mercer County, Pennsylvania For the Period January 1, 2020 to December 31, 2022

February 2024



Commonwealth of Pennsylvania
Department of the Auditor General

Timothy L. DeFoor • Auditor General



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**TIMOTHY L. DEFOOR
AUDITOR GENERAL**

The Honorable Mayor and City Council
City of Farrell
Mercer County
Farrell, PA 16121

We have conducted a compliance audit of the City of Farrell Police Pension Plan for the period January 1, 2020 to December 31, 2022. We also evaluated compliance with some requirements subsequent to that period when possible. The audit was conducted pursuant to authority derived from the Municipal Pension Plan Funding Standard and Recovery Act (Act 205 of 1984, as amended, 53 P.S. § 895.402(j)), 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 (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 the plan member who retired during the current audit period represent payments to all (and only) those entitled to receive them and were properly determined and disbursed in accordance with the plan's governing document, applicable laws, and regulations by recalculating the amount of the monthly pension benefits due to the retired individual and comparing these amounts to supporting documentation evidencing amounts determined and actually paid to the recipient.
- We determined whether the January 1, 2021 actuarial valuation report was prepared and submitted by March 31, 2022 in accordance with Act 205 and whether selected information provided on this report 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.

The City of Farrell Police Pension Plan participates in the Pennsylvania Municipal Retirement System (PMRS), which is an agent multiple-employer public employee retirement system that acts as a common investment and administrative agent for participating municipal pension plans. PMRS issues a separate Annual Comprehensive Financial Report, copies of which are available from the PMRS accounting office. PMRS's 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 Farrell Police 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.

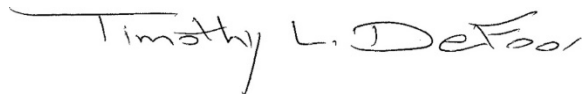
The results of our procedures indicated that, in all significant respects, the City of Farrell Police Pension Plan was administered in compliance with applicable state laws, regulations, contracts, administrative procedures, and local ordinances and policies, except as noted in the following findings further discussed later in this report:

Finding No. 1 – Incorrect Data On Certification Form AG 385 Resulting In A Net Overpayment Of State Aid

Finding No. 2 – Failure To Properly Determine And Fully Pay The Minimum Municipal Obligation Of The Plan

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 City of Farrell 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.



Timothy L. DeFoor
Auditor General
February 9, 2024

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BACKGROUND

On December 18, 1984, the Pennsylvania Legislature adopted the Municipal Pension Plan Funding Standard and Recovery Act (P.L. 1005, No. 205, as amended, 53 P.S. § 895.101 et seq.). The Act established mandatory actuarial reporting and funding requirements and a uniform basis for the distribution of state aid to Pennsylvania's public pension plans.

Annual state aid allocations are provided from a two percent foreign (out-of-state) casualty insurance premium tax, a portion of the foreign (out-of-state) fire insurance tax designated for paid firefighters and any investment income earned on the collection of these taxes. Generally, municipal pension plans established prior to December 18, 1984, are eligible for state aid. For municipal pension plans established after that date, the sponsoring municipality must fund the plan for three plan years before it becomes eligible for state aid. In accordance with Act 205, a municipality's annual state aid allocation cannot exceed its actual pension costs.

In addition to Act 205, the City of Farrell Police 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 15 - Pennsylvania Municipal Retirement Law, Act of February 1, 1974
(P.L. 34, No. 15), as amended, 53 P.S. § 881.101 et seq.

The City of Farrell Police Pension Plan is a single-employer defined benefit pension plan locally controlled by the provisions of Ordinance No. 0-2-2020, effective January 1, 2020, as amended, and a separately executed plan agreement with the plan custodian, adopted pursuant to Act 15. The plan is also affected by the provisions of collective bargaining agreements between the city and its police officers. The plan was established November 19, 1953. Active members are required to contribute five percent of compensation, plus \$1 per month to the plan. As of December 31, 2022, the plan had 9 active members, 3 terminated members eligible for vested benefits in the future, and 21 retirees receiving pension benefits.

CITY OF FARRELL POLICE PENSION PLAN
STATUS OF PRIOR FINDING

Compliance With Prior Recommendation

The City of Farrell has complied with the prior recommendation concerning the following:

- Failure To Maintain An Adequate Record-Keeping System To Effectively Monitor Activity Of The Pension Plan

During the current audit period, the city provided annual financial statements of transactions of the custodial account of the police pension plan for all years under audit.

CITY OF FARRELL POLICE PENSION PLAN
FINDINGS AND RECOMMENDATIONS

Finding No. 1 – Incorrect Data On Certification Form AG 385 Resulting in A Net Overpayment Of State Aid

Condition: The city certified two ineligible police officers on the Certification Form AG 385 filed in 2022. In addition, the city certified five ineligible police officers, one ineligible employee in the nonuniformed pension plan and failed to include one eligible police officer and one eligible firefighter on the Certification Form AG 385 filed in 2023. The city included employees who were not enrolled into the police pension plan, excluded a police officer who retired in July 2022 but satisfied the requirements for certification prior to separation, and incorrectly classified an eligible firefighter as a non-uniformed employee. The data contained on these certification forms is based on prior calendar year information.

Criteria: Pursuant to Act 205, at Section 402(e)(2), in order to be eligible for certification, an employee must have been employed on a full-time basis for at least six consecutive months and must have been participating in a pension plan during the certification year.

Cause: Plan officials failed to establish adequate internal control procedures, such as having another individual review the data certified, to ensure the accuracy of the reported data prior to submission.

Effect: The data submitted on these certification forms is used, in part, to calculate the state aid due to the municipality for distribution to its pension plans. Because the city’s state aid allocations were based on unit value, the incorrect certification of pension data affected the city’s state aid allocations, as identified below:

<u>Year</u>	<u>Type Of Plan</u>	<u>Units Overstated (Understated)</u>	<u>Unit Value</u>	<u>State Aid Overpayment (Underpayment)</u>
2022	Police	4	\$ 5,180	\$ 20,720
2023	Police	10	5,828	\$ 58,280
	Police	(2)	5,828	(11,656)
	Non-Uniformed	1	5,828	5,828
	Firemen’s	(2)	5,828	(11,656)
			2023 Subtotal	<u>\$ 40,796</u>
			Total Net Overpayment of State Aid	<u>\$ 61,516</u>

CITY OF FARRELL POLICE PENSION PLAN
FINDINGS AND RECOMMENDATIONS

Finding No. 1 – (Continued)

In addition, the city used the overpayments of state aid to pay the minimum municipal obligations (MMOs) due to the police, non-uniformed and firemen's pension plans; therefore, if the reimbursement to the Commonwealth is made from the pension plans, the plans' MMOs will not be fully paid.

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

Recommendation: We recommend that the total excess state aid, in the amount of \$61,516, plus interest, be returned to the Commonwealth. A check in this amount, with interest compounded annually from date of receipt to date of repayment, at a rate earned by the pension plan, should be made payable to: Commonwealth of Pennsylvania and mailed to: Department of the Auditor General, Municipal Pension & Fire Relief Programs Unit, 321 Finance Building, Harrisburg, PA 17120. A copy of the interest calculation must be submitted along with the check.

We also recommend that in the future, plan officials establish adequate internal control procedures, such as having at least two people review the data certified, to ensure compliance with the instructions that accompany Certification Form AG 385 to assist them in accurately reporting the required pension data.

In addition, if the reimbursement to the Commonwealth is made from police, non-uniformed or firemen's pension plan funds, we recommend that any resulting MMO deficiencies be paid to the pension plan with interest, at a rate earned by the pension plan.

Management's Response: Municipal officials agreed with the finding without exception.

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

CITY OF FARRELL POLICE PENSION PLAN
FINDINGS AND RECOMMENDATIONS

Finding No. 2 – Failure To Properly Determine And Fully Pay The Minimum Municipal Obligation Of The Plan

Condition: Plan officials did not properly determine or fully pay the minimum municipal obligation (MMO) of the police pension plan for the year 2022, as required by Act 205. The MMO determined by the municipality understated payroll by \$98,736 on the 2022 MMO calculation. Based upon an estimate prepared by this department, the city had an unpaid balance of \$13,365 for the year 2022.

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

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

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.

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.

CITY OF FARRELL POLICE PENSION PLAN
FINDINGS AND RECOMMENDATIONS

Finding No. 2 – (Continued)

Cause: The city did not comply with the Act 205 requirements because officials failed to account for authorized wage increases and overtime applied during 2022 and procedures were not adequate to ensure the accuracy of payroll amounts used in the MMO calculation.

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 2022 MMO by the December 31, 2022, deadline, the municipality must add the \$13,365 MMO balance to the current year’s MMO and include interest, as required by Act 205.

Recommendation: We recommend that the municipality pay the MMO due to the police pension plan for the year 2022, with interest, in accordance with Section 302(e) of Act 205. A copy of the interest calculation must be maintained by the city for examination during our next audit of the plan.

In addition, we recommend that, in the future, the city properly determine the amount of payroll to be used in the MMO calculation in accordance with Act 205 and the Pennsylvania Code.

Management’s Response: Municipal officials agreed with the finding without exception.

Auditor’s Conclusion: Compliance will be evaluated during our next audit of the plan.

CITY OF FARRELL POLICE PENSION PLAN
POTENTIAL WITHHOLD OF STATE AID

Finding No. 1 contained in this audit report cites an overpayment of state aid to the city in the amount of \$61,516, plus interest. A condition of this nature may lead to a total withholding of state aid in the future unless that finding is corrected. A check in this amount with interest, at a rate earned by the pension plan, should be made payable to: Commonwealth of Pennsylvania, and mailed to: Department of the Auditor General, Municipal Pension & Fire Relief Programs Unit, 321 Finance Building, Harrisburg, PA 17120.

CITY OF FARRELL POLICE PENSION PLAN
 SUPPLEMENTARY INFORMATION
 (UNAUDITED)

SCHEDULE OF FUNDING PROGRESS

Historical trend information about the plan is presented herewith as supplementary information. It is intended to help users assess the plan’s funding status on a going-concern basis, assess progress made in accumulating assets to pay benefits when due, and make comparisons with other state and local government retirement systems.

The actuarial information is required by Act 205 biennially. The historical information, beginning as of January 1, 2017, is as follows:

	(1)	(2)	(3)	(4)
Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) - Entry Age (b)	Unfunded (Assets in Excess of) Actuarial Accrued Liability (b) - (a)	Funded Ratio (a)/(b)
01-01-17	\$ 7,123,601	\$ 7,283,180	\$ 159,579	97.8%
01-01-19	7,205,155	7,366,506	161,351	97.8%
01-01-21	7,252,354	7,083,741	(168,613)	102.4%

CITY OF FARRELL POLICE 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 FARRELL POLICE PENSION PLAN
 SUPPLEMENTARY INFORMATION
 (UNAUDITED)

SCHEDULE OF CONTRIBUTIONS

<u>Year Ended December 31</u>	<u>Actuarially Determined Contribution</u>	<u>Actual Contributions</u>	<u>Contribution Deficiency (Excess)**</u>	<u>Covered- Employee Payroll*</u>	<u>Contributions as a Percentage of Covered- Employee Payroll</u>
2014	\$ 53,254	\$ 62,075	\$ (8,821)		
2015	49,083	54,332	(5,249)		
2016	197,507	197,507	-	\$ 576,647	34.3%
2017	14,218	14,705	(487)	712,622	2.1%
2018	11,518	12,365	(847)	706,015	1.8%
2019	113,797	114,528	(731)	752,803	15.21%
2020	118,193	118,515	(322)	760,068	15.59%
2021	115,898	116,215	(317)	685,195	16.96%
2022	110,539	110,798	(259)	741,933	14.93%

* Prior to 2016, active police officers were members of the Southwest Mercer County Regional Pension Plan; therefore, no covered-employee payroll was provided for 2014 and 2015.

** Information provided by the plan custodian and not reconciled to determine the cause of deviations from the Actuarially Determined Contribution.

CITY OF FARRELL POLICE PENSION PLAN
 SUPPLEMENTARY INFORMATION
 NOTES TO SUPPLEMENTARY SCHEDULES
 (UNAUDITED)

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

Actuarial valuation date	January 1, 2021
Actuarial cost method	Entry age normal
Amortization method	Not applicable
Remaining amortization period	None
Asset valuation method	Not available
Actuarial assumptions:	
Investment rate of return *	5.25%, compounded annually, net of investment and administration expenses.
Projected salary increases *	4.1%
* Includes inflation at	2.2%
Cost-of-living adjustments	2.2% per year, subject to plan limitations.

The information reported above was extracted from the Pennsylvania Municipal Retirement System Experience Study Results Report dated September 2020, which is the basis for the 01-01-2021 actuarial valuation. The report did not specify the actuarial or market value methodologies often contained in the Notes to Supplementary Schedules and will be added going forward when readily available.

CITY OF FARRELL POLICE PENSION PLAN
REPORT DISTRIBUTION LIST

This report was initially distributed to the following:

The Honorable Joshua D. Shapiro
Governor
Commonwealth of Pennsylvania

The Honorable Kimberly Doss
Mayor

Mr. Albert Rock
Deputy Mayor

Ms. Barbara Mosley
Acting City Manager

Mr. Robert Renner
Acting City Manager

Ms. Melissa Cannone
City Treasurer

Mr. Richard Cardamone, CPA, CGMA
Pennsylvania Municipal Retirement System

This report is a matter of public record and is available online at www.PaAuditor.gov. Media questions about the report can be directed to the Pennsylvania Department of the Auditor General, Office of Communications, 229 Finance Building, Harrisburg, PA 17120; via email to: news@PaAuditor.gov.