

COMPLIANCE AUDIT

Ellwood City Borough Firemen's Pension Plan Lawrence County, Pennsylvania For the Period January 1, 2017 to December 31, 2018

September 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 Borough Council
Ellwood City Borough
Lawrence County
Ellwood City, PA 16117

We have conducted a compliance audit of the Ellwood City Borough Firemen's 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 the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our conclusions based on our audit objective. We believe that the evidence obtained provides a reasonable basis for our conclusions based on our audit objective.

The objective of the audit was to determine if the pension plan was administered in compliance with applicable state laws, regulations, contracts, administrative procedures, and local ordinances and policies.

Our audit was limited to the areas related to the objective identified above. To determine whether the pension plan was administered in compliance with applicable state laws, regulations, contracts, administrative procedures, and local ordinances and policies, our methodology included the following:

- We determined whether state aid was properly determined and deposited in accordance with Act 205 requirements by verifying the annual deposit date of state aid and determining whether deposits were made within 30 days of receipt for all years within the period under audit.
- We determined whether annual employer contributions were calculated and deposited in accordance with the plan's governing document and applicable laws and regulations by examining the municipality's calculation of the plan's annual financial requirements and minimum municipal obligation (MMO) and comparing these calculated amounts to amounts actually budgeted and deposited into the pension plan as evidenced by supporting documentation.

- We determined whether annual employee contributions were calculated, deducted, and deposited into the pension plan in accordance with the plan's governing document and applicable laws and regulations by testing 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.

Ellwood City Borough contracted with an independent certified public accounting firm for annual audits of its basic financial statements which are available at the borough's offices. Those financial statements were not audited by us and, accordingly, we express no opinion or other form of assurance on them.

Borough officials are responsible for establishing and maintaining effective internal controls to provide reasonable assurance that the Ellwood City Borough Firemen's Pension Plan is administered in compliance with applicable state laws, regulations, contracts, administrative procedures, and local ordinances and policies. In conducting our audit, we obtained an understanding of the borough's internal controls as they relate to the borough's compliance with those requirements and that we considered to be significant within the context of our audit objective, and assessed whether those significant controls were properly designed and implemented. Additionally and as previously described, we tested transactions, assessed official actions, performed analytical procedures, and interviewed selected officials to provide reasonable assurance of detecting instances of noncompliance with legal and regulatory requirements or noncompliance with provisions of contracts, administrative procedures, and local ordinances and policies that are significant within the context of the audit objective.

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

The accompanying supplementary information is presented for purposes of additional analysis. We did not audit the information or conclude on it and, accordingly, express no form of assurance on it. However, we are extremely concerned about the historical trend information contained in the schedule of funding progress included in this report which indicates a continued decline of assets available to satisfy the long-term liabilities of the plan. **The plan's funded ratio went from 77.9% as of January 1, 2013, to a ratio of 60.3% as of January 1, 2017**, which is the most recent data available. We encourage borough officials to monitor the funding of the firemen's pension plan to ensure its long-term financial stability.

The contents of this report were discussed with officials of Ellwood City Borough and, where appropriate, their responses have been included in the report. We would like to thank borough officials for the cooperation extended to us during the conduct of the audit.

September 10, 2019

A handwritten signature in black ink, appearing to read "Eugene A. DePasquale", with a long, sweeping horizontal line extending to the right.

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 Ellwood City Borough Firemen's 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.

The Ellwood City Borough Firemen's Pension Plan is a single-employer defined benefit pension plan locally controlled by the provisions of Chapter 296 of the borough's codified ordinances. The plan was established November 4, 1965. Active members are required to contribute 5 percent of participant's compensation to the plan. As of December 31, 2018, the plan had 1 active member, no terminated members eligible for vested benefits in the future, and 4 retirees receiving pension benefits from the plan.

BACKGROUND – (Continued)

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

Eligibility Requirements:

Normal Retirement	Age 46 and 21 years of service.
Early Retirement	None
Vesting	Member is 100% vested after 10 years of service.

Retirement Benefit:

Benefit equals 50% of final 36 months' average compensation.

Survivor Benefit:

Before Retirement Eligibility	Refund of member contributions plus 3.5% interest.
After Retirement Eligibility	A monthly benefit equal to 50% of the pension the member was receiving or was entitled to receive on the day of the member's death.

Service Related Disability Benefit:

Benefit equals 50% of the member's final 36 months' average compensation.

ELLWOOD CITY BOROUGH FIREMEN'S PENSION PLAN
SUPPLEMENTARY INFORMATION
(UNAUDITED)

The supplementary information contained on Pages 3 through 6 reflects the implementation of GASB Statement No. 67, *Financial Reporting for Pension Plans*. The objective of this statement is to improve financial reporting by state and local governmental pension plans.

SCHEDULE OF CHANGES IN THE NET PENSION
LIABILITY AND RELATED RATIOS
FOR THE YEARS ENDED DECEMBER 31, 2014, 2015, AND 2016

	<u>2014</u>	<u>2015</u>	<u>2016</u>
Total Pension Liability			
Service cost	\$ 10,588	\$ 11,476	\$ 12,336
Interest	47,461	46,896	46,217
Actual (gain)/loss	22,702	-	(25,948)
Assumption (gain)/loss	22,374	-	-
Benefit payments, including refunds of member contributions	(73,405)	(69,705)	(66,005)
Net Change in Total Pension Liability	29,720	(11,333)	(33,400)
Total Pension Liability – Beginning	624,672	654,392	643,059
Total Pension Liability – Ending (a)	<u>\$ 654,392</u>	<u>\$ 643,059</u>	<u>\$ 609,659</u>
Plan Fiduciary Net Position			
Contributions – employer	\$ 20,567	\$ 25,587	\$ 33,714
Contributions – member	2,380	2,549	2,657
Net investment income	14,921	(5,012)	14,686
Benefit payments, including refunds of member contributions	(73,405)	(69,705)	(66,005)
Actuarial costs	(425)	(5,885)	(1,735)
Other	(1,238)	(1,287)	(1,488)
Net Change in Plan Fiduciary Net Position	(37,200)	(53,753)	(18,171)
Plan Fiduciary Net Position – Beginning	415,677	378,477	324,724
Plan Fiduciary Net Position – Ending (b)	<u>\$ 378,477</u>	<u>\$ 324,724</u>	<u>\$ 306,553</u>
Net Pension Liability – Ending (a-b)	<u>\$ 275,915</u>	<u>\$ 318,335</u>	<u>\$ 303,106</u>
Plan Fiduciary Net Position as a Percentage of the Total Pension Liability	57.84%	50.50%	50.28%
Estimated Covered Employee Payroll	\$ 47,604	\$ 47,604	\$ 53,138
Net Pension Liability as a Percentage of Covered Employee Payroll	579.60%	668.71%	570.41%

ELLWOOD CITY BOROUGH FIREMEN'S PENSION PLAN
SUPPLEMENTARY INFORMATION
(UNAUDITED)

SCHEDULE OF CHANGES IN THE NET PENSION
LIABILITY AND RELATED RATIOS
FOR THE YEARS ENDED DECEMBER 31, 2017 AND 2018

	<u>2017</u>	<u>2018</u>
Total Pension Liability		
Service cost	\$ 12,845	\$ 13,808
Interest	43,731	43,060
Actual (gain)/loss	-	55,026
Assumption (gain)/loss	-	49,557
Benefit payments, including refunds of member contributions	(66,005)	(66,005)
Net Change in Total Pension Liability	(9,429)	95,446
Total Pension Liability – Beginning	609,659	600,230
Total Pension Liability – Ending (a)	<u>\$ 600,230</u>	<u>\$ 695,676</u>
Plan Fiduciary Net Position		
Contributions – employer	\$ 35,390	\$ 41,568
Contributions – member	2,953	3,830
Net investment income	30,400	(10,348)
Benefit payments, including refunds of member contributions	(66,005)	(66,005)
Administrative expense	(6,245)	-
Other	(1,648)	(1,618)
Net Change in Plan Fiduciary Net Position	(5,155)	(32,573)
Plan Fiduciary Net Position – Beginning	306,553	301,398
Plan Fiduciary Net Position – Ending (b)	<u>\$ 301,398</u>	<u>\$ 268,825</u>
Net Pension Liability – Ending (a-b)	<u>\$ 298,832</u>	<u>\$ 426,851</u>
Plan Fiduciary Net Position as a Percentage of the Total Pension Liability	50.21%	38.64%
Estimated Covered Employee Payroll	\$ 59,059	\$ 76,610
Net Pension Liability as a Percentage of Covered Employee Payroll	505.99%	557.17%

ELLWOOD CITY BOROUGH FIREMEN'S PENSION PLAN
SUPPLEMENTARY INFORMATION
(UNAUDITED)

Sensitivity Of The Net Pension Liability To Changes In The Discount Rate

The following presents the net pension liability of the borough as of December 31, 2015, 2016, and 2017 calculated using the discount rate of 7.5%, as well as what the borough's net pension liability would be if it were calculated using a discount rate that is 1 percentage-point lower or 1 percentage-point higher than the current rate:

	1% Decrease (6.5%)	Current Discount Rate (7.5%)	1% Increase (8.5%)
Net Pension Liability – 12/31/15	\$ 367,006	\$ 318,335	\$ 257,748
Net Pension Liability – 12/31/16	\$ 351,784	\$ 303,106	\$ 260,706
Net Pension Liability – 12/31/17	\$ 346,757	\$ 298,832	\$ 257,088

In addition, the following presents the net pension liability of the borough as of December 31, 2018, calculated using the discount rate of 7.0%, as well as what the borough's net pension liability would be if it were calculated using a discount rate that is 1 percentage-point lower or 1 percentage-point higher than the current rate:

	1% Decrease (6.0%)	Current Discount Rate (7.0%*)	1% Increase (8.0%)
Net Pension Liability – 12/31/18	\$ 491,546	\$ 426,851	\$ 371,491

* Auditor's Note: The discount rate of 7.0% was used in the schedule above for December 31, 2018 provided by the borough. This rate differs from the 7.5% investment rate of return reported in the Notes to Supplementary Schedules as of January 1, 2017 on page 9 of this report.

ELLWOOD CITY BOROUGH 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	\$ 20,567	\$ 20,567	\$ -	\$ 47,604	43.20%
2015	25,587	25,587	-	47,604	53.75%
2016	33,714	33,714	-	53,138	63.45%
2017	35,390	35,390	-	59,059	59.92%
2018*	47,258	41,568	5,690	76,610	54.26%

* Auditor's Note: The Actuarially Determined Contribution for 2018 in the schedule above provided by the borough appears to be in error and actually reflects the 2019 minimum municipal obligation (MMO) prepared by the borough for the plan. The 2018 MMO prepared by the borough is \$41,568, and there is actually no contribution deficiency for 2018.

SCHEDULE OF INVESTMENT RETURNS

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

2018	-3.75%
2017	10.82%
2016	4.95%
2015	-1.46%
2014	3.78%

ELLWOOD CITY BOROUGH 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, 2013, 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)
01-01-13	\$ 497,472	\$ 638,931	\$ 141,459	77.9%
01-01-15	452,633	654,392	201,759	69.2%
01-01-17	367,864	609,659	241,795	60.3%

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 limited to a maximum of 120 percent of market value. These methods 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.

ELLWOOD CITY BOROUGH 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.

ELLWOOD CITY BOROUGH 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, 2017
Actuarial cost method	Entry age normal
Amortization method	Level dollar, closed
Remaining amortization period	14 years
Asset valuation method	The actuarial value of assets will be limited to a maximum of 120% of the fair market value of assets.
Actuarial assumptions:	
Investment rate of return	7.5%
Projected salary increases	5.5%

ELLWOOD CITY BOROUGH FIREMEN'S PENSION PLAN
REPORT DISTRIBUTION LIST

This report was initially distributed to the following:

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