CITY OF EASTON AGGREGATED PENSION TRUST FUND

NORTHAMPTON COUNTY

COMPLIANCE AUDIT REPORT

FOR THE PERIOD

JANUARY 1, 2011, TO DECEMBER 31, 2012

COMMONWEALTH OF PENNSYLVANIA

EUGENE A. DEPASQUALE - AUDITOR GENERAL

DEPARTMENT OF THE AUDITOR GENERAL

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EUGENE A. DEPASQUALE
AUDITOR GENERAL

The Honorable Mayor and City Council
City of Easton
Northampton County
Easton, PA 18042

We have conducted a compliance audit of the City of Easton Aggregated Pension Trust Fund for the period January 1, 2011, to December 31, 2012. 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 trust fund 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. Our methodology addressed determinations about the following:

- Whether state aid was properly determined and deposited in accordance with Act 205 requirements.

- Whether employer contributions are determined and deposited in accordance with the plan's governing document and applicable laws and regulations.

- Whether employee contributions are required and, if so, are determined, deducted and deposited into the pension plan and are in accordance with the plan provisions and applicable laws and regulations.

- Whether benefit payments, if any, represent payments to all (and only) those entitled to receive them and are properly determined in accordance with applicable laws and regulations.

- Whether obligations for plan benefits are accurately determined in accordance with plan provisions and based on complete and accurate participant data; and whether actuarial valuation reports are prepared and submitted to the Public Employee Retirement Commission (PERC) in accordance with state law and 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.

- Whether the special ad hoc postretirement adjustment granted to eligible pensioners is in accordance with applicable laws and regulations and whether the ad hoc reimbursement received by the municipality was treated in accordance with applicable laws and regulations.

- Whether benefit payments have only been made to living recipients, based on the Social Security numbers found in the pension records for retirees and beneficiaries.

- Whether the pension trust fund is in compliance with state regulations for distressed municipalities.

- Whether the terms and methodologies of the issuance of bonds by the municipality, and any restrictions are in compliance with plan provisions and state regulations.

- Whether Deferred Retirement Option Plan (DROP) participants' benefit payments are properly determined in accordance with the provisions of the DROP and any other applicable laws and regulations.

The City of Easton contracted with an independent certified public accounting firm for annual audits of the City of Easton Aggregated Pension Trust Fund's financial statements 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 Easton Aggregated Pension Trust Fund 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, 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 tests indicated that, in all significant respects, the City of Easton Aggregated Pension Trust Fund 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:

Aggregated Pension Trust Fund

Finding No. 1 - Partial Compliance With Prior Audit Recommendation – Incorrect Data On Certification Form AG 64 Resulting In An Excess Reimbursement Of Special 2002 Ad Hoc Postretirement Adjustment

Finding No. 2 - Failure To Appoint A Chief Administrative Officer

Police Pension Plan

Finding No. 3 - Noncompliance With Prior Audit Recommendation – Inconsistent Benefit Provisions And Provision Of Pension Benefits Not In Compliance With The Third Class City Code

Firemen's Pension Plan

Finding No. 4 - Noncompliance With Prior Audit Recommendation – Provisions Of Benefits Not In Compliance With The Third Class City Code

As previously noted, one of the objectives of our audit of the City of Easton Aggregated Pension Trust Fund was to determine compliance with applicable state laws, regulations, contracts, administrative procedures, and local ordinances and policies. Act 205 was amended on September 18, 2009, through the adoption of Act 44 of 2009. Among several provisions relating to municipal pension plans, the act provides for the implementation of a distress recovery program. Three levels of distress have been established:

Level	Indication	Funding Criteria
I	Minimal distress	70-89%
II	Moderate distress	50-69%
III	Severe distress	Less than 50%

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 respective schedules of funding progress included in this report which indicate a continued decline of assets available to satisfy the long-term liabilities of the fund. For example, **the police pension plan's funded ratio went from 92.1% as of January 1, 2007, to a ratio of 55.1%** as of January 1, 2011, which is the most recent date available. Similarly, **the firemen's pension plan's funded ratio went from 99.0% as of January 1, 2007, to 67.0%** as of January 1, 2011. Finally, **the officers' and employees' pension plan's funded ratio went from 99.7% as of January 1, 2007, to 64.4%** as of January 1, 2011. Based on this information, the Public Employee Retirement Commission issued a notification that the city is currently in Level II moderate distress status. We encourage city officials to monitor the funding of its pension plans to ensure their long-term financial stability.

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

Eugene A. DePasquale

September 26, 2013

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 Easton Aggregated Pension Trust Fund is also governed by implementing regulations adopted by the Public Employee Retirement Commission published at Title 16, Part IV of the Pennsylvania Code and applicable provisions of various other state statutes including, but not limited to, the following:

Act 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.

Act 317 - The Third Class City Code, Act of June 23, 1931 (P.L. 932, No. 317), as amended, 53 P.S. § 35101 et seq.

The City of Easton Aggregated Pension Trust Fund acts as a common investment and administrative agent for the city's police, firemen's and officers' and employees' defined benefit pension plans. The police pension plan is governed by Chapter 110, Article II of the city's codified ordinances. The firemen's pension plan is governed by Chapter 110, Article V of the city's codified ordinances. The officers' and employees' pension plan is governed by Chapter 100, Article III of the city's codified ordinances for non-uniformed employees hired prior to January 1, 1979. The plans are also affected by the provisions of collective bargaining agreements between the city and its police officers, firefighters and officers and employees.

BACKGROUND – (Continued)

As of December 31, 2012, the police pension plan had 60 active members and 78 retirees receiving pension benefits. As of December 31, 2012, the firemen's pension plan had 43 active members, 1 terminated member eligible for vested benefits in the future and 48 retirees receiving pension benefits. As of December 31, 2012, the officers' and employees' pension plan had 5 active members and 84 retirees receiving pension benefits.

CITY OF EASTON AGGREGATED PENSION TRUST FUND
STATUS OF PRIOR FINDINGS

Compliance With Prior Audit Recommendation

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

Aggregated Pension Trust Fund

- Incorrect Data On Certification Form AG 385 Resulting In A Net Overpayment Of State Aid

  The city reimbursed $16,788 to the Commonwealth for the overpayment of state aid.

Partial Compliance With Prior Audit Recommendation

The City of Easton has partially complied with the prior audit recommendation concerning the following:

Aggregated Pension Trust Fund

- Incorrect Data On Certification Form AG 64 Resulting In An Excess Reimbursement Of Special 2002 Ad Hoc Post Retirement Adjustment

  During the current audit period, the city reimbursed $13,504 to the Commonwealth for the excess reimbursements received in 2010 and 2011; however, plan officials failed to comply with the instructions that accompany Certification Form AG 64 to assist them in accurately reporting the required pension data for the year 2013 as further discussed in the Findings and Recommendations section of this report.

Noncompliance With Prior Audit Recommendations

The City of Easton has not complied with the prior audit recommendations concerning the following as further discussed in the Findings and Recommendations section of this report:

Police Pension Plan

- Inconsistent Benefit Provisions And Provision Of Pension Benefits Not In Compliance With The Third Class City Code

Firemen's Pension Plan

- Provision Of Benefits Not In Compliance With The Third Class City Code

CITY OF EASTON AGGREGATED PENSION TRUST FUND
STATUS OF PRIOR FINDINGS

Status Of Prior Audit Recommendation

Officers' And Employees' Pension Plan

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

The audit report for the period January 1, 2009, to December 31, 2010, contained a finding that the plan's governing document provided for an early retirement benefit that is not authorized by the Third Class City Code. There are currently no active members who would receive this excess benefit due to all active members being over the age of 55. However, excess benefits are still being paid to 1 retiree. Since the city received state aid based on unit value during the current audit period, it did not receive state aid attributable to the excess benefits provided. The Department will continue to monitor the impact of the excess benefits being paid to the existing retiree on the city's future state aid allocations.

Aggregated Pension Trust Fund

Finding No. 1 – Partial Compliance With Prior Audit Recommendation – Incorrect Data On Certification Form AG 64 Resulting In An Excess Reimbursement Of Special 2002 Ad Hoc Postretirement Adjustment

Condition: As disclosed in the prior audit report, the city did not accurately report the required pension data on the Certification Forms AG 64 filed for 2010 and 2011. During the current audit period, the city reimbursed $13,504 to the Commonwealth for the excess reimbursements received in 2010 and 2011; however, plan officials failed to comply with the instructions that accompany Certification Form AG 64 to assist them in accurately reporting the required pension data for the year 2013.

The city understated its state aid allocation received on the Certification Form AG 64 filed for the year 2013.

Criteria: Section 502.1(a)(2) of Act 147 states, in part:

> The determination of the reimbursable amount of the amortization contribution requirement attributable to the special ad hoc postretirement adjustment under Chapter 4 in any year shall be calculated as the amortization contribution requirement attributable to the special ad hoc postretirement adjustments under Chapter 4 and reflected in the determination of the financial requirements of the pension plan under Chapter 3 of the Municipal Pension Plan Funding Standard and Recovery Act for the immediate prior year less the product of that amortization contribution requirement multiplied by the ratio of the amount of general municipal pension system State aid allocated to the retirement system in the immediate prior year to the total amount of municipal contributions made to the retirement system from all sources other than employee contributions in the immediate prior year. (Emphasis added)

Cause: Plan officials failed to establish adequate internal control procedures to ensure the accuracy of the data certified and to ensure full compliance with the prior audit recommendation.

Effect: The data submitted on the Certification Form AG 64 is used to calculate the reimbursement due the city for ad hoc postretirement adjustments granted pursuant to Chapter 4 of Act 147.

Aggregated Pension Trust Fund – (Continued)

Finding No. 1 – (Continued)

The effect of the incorrect certification of pension data on the city's reimbursement is identified below:

Reimbursement Claimed	Reimbursement Due	Excess Reimbursement
$ 53,921	$ 51,977	$ 1,944

Recommendation: We recommend that the total excess state aid, in the amount of $1,944, 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, 320 Finance Building, Harrisburg, PA 17120. A copy of the interest calculation must be submitted along with the check.

In addition, we again recommend that plan officials comply with the instructions that accompany Certification Form AG 64 to assist them in accurately reporting the required pension data.

Management's Response: We recognize and accept the finding on 2013; however, we still believe that these matters would not be findings if the Auditor General's Office would provide advice or direct answers to our questions.

Auditor's Conclusion: Article VIII, Section 10 of the Pennsylvania Constitution and Section 404 of the Fiscal Code as amended, 72 P.S. 404, prohibit the Auditor General from giving pre-audit advice of any transaction which he has the subsequent duty to audit. Since the Department of the Auditor General has the responsibility to audit the City of Easton Aggregated Pension Trust Fund, the Department cannot provide such advice; therefore, the finding and recommendation remain as stated.

Aggregated Pension Trust Fund – (Continued)

Finding No. 2 – Failure To Appoint A Chief Administrative Officer

Condition: Municipal officials did not appoint a chief administrative officer (CAO) for the pension plans by ordinance, resolution or by a motion recorded in the minutes of a council meeting.

Criteria: Section 102 of Act 205 defines the CAO as "The person who has primary responsibility for the execution of the administrative affairs of the municipality in the case of the municipality, or of the pension plan in the case of the pension plan, or the designee of that person."

Municipal officials may appoint two CAOs - one for the pension plan and one for the municipality or appoint one person to fill both positions. Act 205 identifies specific duties for each position, as follows:

CAO Of The Municipality

- Supervise and direct the preparation of actuarial reports (Section 201(d));
- Certify and file actuarial valuation reports with the Public Employee Retirement Commission (Section 201(b)); and
- Make actuarial report information available to plan members (Section 201(e)).

CAO Of The Pension Plan

- Annually, determine and submit to the governing body of the municipality the financial requirements of the pension plan and minimum municipal obligation (Section 302(b), Section 302(c), Section 303(b), Section 303(c) and Section 304); and
- Provide the governing body of the municipality with a cost estimate of the effect of any proposed benefit plan modification (Section 305(a)).

Aggregated Pension Trust Fund – (Continued)

Finding No. 2 – (Continued)

Cause: Plan officials were unaware of the need to appoint a CAO for the pension plans in accordance with Act 205 provisions.

Effect: The failure to formally appoint a CAO could result in important filing deadlines being overlooked, state aid being adversely affected or delayed and investment opportunities being lost.

Recommendation: Because of the significance of the CAO's responsibilities to the municipality and its pension plans, we recommend that the CAO be formally appointed by ordinance, resolution or motion recorded in the minutes of a council meeting. Such ordinance, resolution or motion should detail the CAO's responsibilities and be filed with other plan documents.

Management's Response: The City Council of Easton has introduced for first reading an ordinance change to address this issue.

Auditor's Conclusion: Compliance will be evaluated during our next audit of the plans.

Police Pension Plan

Finding No. 3 – Noncompliance With Prior Audit Recommendation – Inconsistent Benefit Provisions And Provision Of Pension Benefits Not In Compliance With The Third Class City Code

Condition: As disclosed in the prior audit report, prior to January 2, 2008, the City of Easton operated pursuant to the Optional Third Class City Charter Law, Act of July 15, 1957 (P.L. 901, No. 399), as amended, 53 P.S. § 41101 et seq. Consequently, the city's aggregated pension trust fund was not subject to the constraints of the Third Class City Code. The city adopted 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.), effective January 2, 2008. Therefore, pursuant to this change, the city's pension plans must be in compliance with the Third Class City Code for employees hired after the adoption of the home rule charter. Our audit of the police pension plan has revealed that the city is providing benefits to police officers who were hired on or after the effective date noted above that are not in compliance with the Third Class City Code.

In addition, the police pension plan's governing document, City Codified Ordinances at Chapter 110, Article II, contains benefit provisions that conflict with the collective bargaining agreement between the police officers and the city. The inconsistent benefit provisions and the applicable Third Class City Code provisions are illustrated below:

Benefit Provision	Governing Document	Collective Bargaining Agreement	Third Class City Code
Minimum retirement benefit	The minimum pension payable under this section shall be $3,000 per year.	Not provided	Not provided
Service requirement	The later of the member's 50th birthday and the 20th anniversary of the date on which employment commenced.	Any covered employee may make application to retire at 20 years of service regardless of age.	A minimum service requirement of at least 20 years of continuous service for a normal retirement benefit and a minimum age of 50 years, if prescribed.

Police Pension Plan – (Continued)

Finding No. 3 – (Continued)

Benefit Provision	Governing Document	Collective Bargaining Agreement	Third Class City Code
Service-related disability	A service-related disability benefit for participants with 12 or fewer years of service… regardless of age of such participant, he shall be entitled to receive such portion of pension as his service up to the date of his termination bears to 20 years of service.	Not provided	A service-related disability benefit equal to the normal monthly pension benefit, regardless of the time served.
Member's contributions	A participant is required to contribute 6% of pensionable compensation. Each participant is required to contribute $1 per month for the service increment contribution until the member has reached age 60.	Pension contributions shall be deducted at 6% of pensionable wages plus fifty cents ($ .50) per week for survivor's benefits.	A member's contribution rate of up to 5% of the officer's compensation, plus service increment contributions. Service increment contributions are payable only to age 65.

Police Pension Plan – (Continued)

Finding No. 3 – (Continued)

Benefit Provision	Governing Document	Collective Bargaining Agreement	Third Class City Code
Monthly pension benefit	A participant shall receive an annual pension equal to 50% of the employee's pensionable compensation. (Pensionable compensation is defined as the annual salary plus degree pay, longevity pay, personal day buyback, holiday pay, scheduled shift differential, and acting rank pay for regularly scheduled shift of a participant on the date in question.)	Any covered employee with 20 years of service shall be entitled to 50% of pensionable compensation.	The basis of the apportionment of the pension shall be determined by the rate of the monthly pay of the member at the date of injury, death, honorable discharge, vesting under section 4302.1 or retirement, or the highest average annual salary which the member received during any five years of service preceding injury, death, honorable discharge, vesting under section 4302.1 or retirement, whichever is the higher, and except as to service increments provided for in subsection (b) of this section, shall not in any case exceed in any year one-half the annual pay of such member computed at such monthly or average annual rate, whichever is the higher.

Police Pension Plan – (Continued)

Finding No. 3 – (Continued)

Benefit Provision	Governing Document	Collective Bargaining Agreement	Third Class City Code
Service increments	The service increment shall be obtained by computing the number of whole years after 20 years of service, including credit for military service as provided in this plan, and multiplying the number of years so computed by 2.5% of pensionable compensation for each year of service to a maximum of 75% of pensionable compensation after 30 years of service. No employment after the participant has reached the age of 60 years shall be included.	Any covered employee with over 20 years of service shall be entitled to additional service increments of 2.5% of pensionable compensation for each additional year of service to a maximum of seventy-five (75%) of pensionable compensation after thirty (30) years of service.	A service increment provision, indicating that additional benefits accrue to age 65 for service exceeding the minimum required for retirement in an amount equal to 1/40th (2.5%) times the monthly pension benefit for each whole year over the minimum, not to exceed $500 per month. (Emphasis added)

Police Pension Plan – (Continued)

Finding No. 3 – (Continued)

Benefit Provision	Governing Document	Collective Bargaining Agreement	Third Class City Code
Nonservice-related disability	A participant who has not less than 15 years of service shall be eligible to receive a normal retirement benefit. If the participant has at least 12 years of service but less than 15 years of service, regardless of age of such participant, he shall be entitled to receive such portion of the normal retirement benefit as his service up to the date of termination bears to 20 years of service.	Not provided	For officers with less than 10 years of service, a pension equal to 25% of his annual compensation. For officers with more than 10 years of service, a pension equal to 50% of annual compensation.

Criteria: On January 24, 2001, the Commonwealth Court of Pennsylvania issued its opinion in *Municipality of Monroeville v. Monroeville Police Department Wage Policy Committee.* 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." The court's holding was in accord with the position taken by this department since at least January 1995. Therefore, for police officers hired on or after January 2, 2008, the pension plan's benefit structure should be in compliance with the provisions of the Third Class City Code.

Furthermore, a governing document which contains clearly defined and updated benefit provisions is a prerequisite for the consistent, sound administration of retirement benefits.

Cause: Plan officials failed to establish adequate internal control procedures to ensure compliance with the prior audit recommendation.

Police Pension Plan – (Continued)

Finding No. 3 – (Continued)

Effect: Inconsistent plan documents could result in inconsistent or improper benefit calculations and incorrect benefit payments from the pension plan. In 2011 a member began receiving a retirement benefit at the age of 45 because of the inconsistency between the governing document and the collective bargaining agreement.

Providing unauthorized pension benefits increases the plan's pension costs and reduces the amount of funds available for investment purposes or for the payment of authorized benefits or administrative expenses. Since the city received state aid based on unit value during the current audit period, it did not receive allocations attributable to the excess pension benefits provided. However, the increased costs to the pension plan as a result of the excess pension benefits could result in the receipt of excess state aid in the future and increase the municipal contributions necessary to fund the plan in accordance with Act 205 funding standards.

Furthermore, as previously noted, the plan's governing document contains provisions that could result in plan members receiving pension benefits that are less than what they would be entitled to under the provisions of the Third Class City Code.

Recommendation: We again recommend that the city provide pension benefits in accordance with the Third Class City Code for all police officers who began full-time employment on or after January 2, 2008. 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 police officers who began employment on or after January 2, 2008, 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, on the city's future state aid allocations and submit this information to the department.

Furthermore, to the extent that the city has failed to provide benefits which are mandated by the Third Class City Code, we again recommend that the city increase those benefits to the levels prescribed by the code at its earliest opportunity to do so.

We also recommend that municipal officials eliminate the inconsistencies between the plan's governing document and the collective bargaining agreement at their earliest opportunity to do so.

Police Pension Plan – (Continued)

Finding No. 3 – (Continued)

Special note should be taken that the department's application of *Monroeville* only to employees hired on or after January 2, 2008, does not sanction (1) a municipality's granting excess benefits to existing or future employees when none had been granted as of January 2, 2008, or (2) a municipality's increasing excess benefits for existing or future employees beyond those that had been granted as of that date.

Management's Response: The City of Easton was compliant with the Third Class City Optional Code for pension benefits until it changed to Home Rule in January of 2008. This is a matter for collective bargaining with Washington Lodge #17.

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

Firemen's Pension Plan

Finding No. 4 – Noncompliance With Prior Audit Recommendation – Provision Of Benefits Not In Compliance With The Third Class City Code

Condition: As disclosed in the prior audit report, prior to January 2, 2008, the City of Easton operated pursuant to the Optional Third Class City Charter Law, Act of July 15, 1957 (P.L. 901, No. 399), as amended, 53 P.S. § 41101 et seq. Consequently, the city's aggregated pension trust fund was not subject to the constraints of the Third Class City Code. The city adopted 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.), effective January 2, 2008. Therefore, pursuant to this change the city's pension plans must be in compliance with the Third Class City Code for employees hired after the adoption of the home rule charter.

Firemen's Pension Plan – (Continued)

Finding No. 4 – (Continued)

Our audit of the firemen's pension plan has revealed that the city is providing benefits to firefighters, who were hired on or after the January 2, 2008, effective date that are not in compliance with the Third Class City Code, as noted below:

Benefit Provision	Governing Document	Third Class City Code
Monthly pension benefit	The greater of the compensation at the date of retirement or 1/12 of the highest average annual salary during any five years of service preceding retirement. The multiplier percentage set forth correspondent to years of service; 20 years at 50%, 21 years at 52.5%, 22 years at 55%, 23 years at 57.5%, 24 years at 60%, 25 years at 62.5%, 26 years at 65%, 27 years at 67.5%, 28 years at 70%, 29 years at 72.5%, and 30 years at 75%.	A monthly pension benefit of 50% of the higher of the monthly salary at the date of termination or the highest average annual salary during any 5 years of service.
Definition of salary	A firefighter's total gross annual compensation, including, without limitation, position salary, longevity pay, degree pay, extra-duty pay, and birthday pay.	A definition of salary as "the fixed amount of compensation paid at regular, periodic intervals by the city to the member and from which pension contributions have been deducted.
Member's contributions	A monthly contribution equal to 4.5% of compensation, plus an additional 1% of compensation towards the survivor benefit and an additional $1 per month for the service increment contribution.	A member's contribution rate of up to 5% of the firefighter's compensation, plus service increment contributions.

Firemen's Pension Plan – (Continued)

Finding No. 4 – (Continued)

Benefit Provision	Governing Document	Third Class City Code
Minimum pension benefit	The pension benefit of any participant who becomes entitled to a pension benefit under the plan shall not be less than $3,000 annually.	Not provided
Survivor benefit	Nonservice-related death benefits where participant has 20 or more years of service. The surviving spouse of any participant who has retired or died while in service after having served for a minimum of 20 years, shall during their lifetime receive a pension benefit of the amount which would have been payable had the firefighter been retired and 50 years of age at the time of death.	A survivor's benefit to the surviving spouse of a deceased retiree or employee equal to the amount that the member was receiving or would have been receiving if he was retired, and continuing during the spouse's life.

Criteria: On January 24, 2001, the Commonwealth Court of Pennsylvania issued its opinion in *Municipality of Monroeville v. Monroeville Police Department Wage Policy Committee.* 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." The court's holding was in accord with the position taken by this department since at least January 1995.

Therefore, for firefighters hired on or after January 2, 2008, the pension plan's benefit structure should be in compliance with the Third Class City Code.

Cause: Plan officials failed to establish adequate internal control procedures to ensure compliance with the prior audit recommendation.

Firemen's Pension Plan – (Continued)

Finding No. 4 – (Continued)

Effect: Providing unauthorized pension benefits increases the plan's pension costs and reduces the amount of funds available for investment purposes or for the payment of authorized benefits or administrative expenses. Since the city received state aid based on unit value during the current audit period, it did not receive allocations attributable to the excess pension benefits provided. However, the increased costs to the pension plan as a result of the excess pension benefits could result in the receipt of excess state aid in the future and increase the municipal contributions necessary to fund the plan in accordance with Act 205 funding standards.

Recommendation: We again recommend that the city provide pension benefits in accordance with the Third Class City Code for all firefighters who began full-time employment on or after January 2, 2008, upon the renewal, extension, or renegotiation of the collective bargaining agreement. 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 firefighters who began employment on or after January 2, 2008, 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, on the city's future state aid allocations and submit this information to the department.

Special note should be taken that the department's application of *Monroeville* only to employees hired on or after January 2, 2008, does not sanction (1) a municipality's granting excess benefits to existing or future employees when none had been granted as of January 2, 2008, or (2) a municipality's increasing excess benefits for existing or future employees beyond those that had been granted as of that date.

Management's Response: The City of Easton was compliant with the Third Class City Optional Code for pension benefits until it changed to Home Rule in January of 2008. The City of Easton in 2012 was able to negotiate a new collective bargaining agreement with Easton Fire Fighters Local 713 to be in compliance with the Third Class City Code for new firefighters hired after January 1, 2013.

Auditor's Conclusion: The collective bargaining agreement for the years 2013 through 2016 addresses the monthly pension benefit and member contribution provisions for firefighters hired after January 1, 2013. Full compliance will be evaluated during our next audit of the plan.

CITY OF EASTON AGGREGATED PENSION TRUST FUND
SUPPLEMENTARY INFORMATION
(UNAUDITED)

SCHEDULES 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, 2007, is as follows:

POLICE PENSION PLAN

Actuarial Valuation Date	(1) Actuarial Value of Assets (a)	(2) Actuarial Accrued Liability (AAL) - Entry Age (b)	(3) Unfunded (Assets in Excess of) Actuarial Accrued Liability (b) - (a)	(4) Funded Ratio (a)/(b)	(5) Covered Payroll (c)	(6) Unfunded (Assets in Excess of) Actuarial Accrued Liability as a % of Payroll [(b-a)/(c)]
01-01-07	$ 21,007,068	$ 22,814,818	$ 1,807,750	92.1%	$ 3,231,885	55.9%
01-01-09	19,483,400	25,192,009	5,708,609	77.3%	3,006,049	189.9%
01-01-11	17,198,135	31,235,456	14,037,321	55.1%	3,454,626	406.3%

Note: The market value of the plan's assets at 01-01-09 has been adjusted to reflect the smoothing of gains and/or losses subject to a corridor between 70 to 130 percent of the market value of assets. The market value of the plan's assets at 01-01-11 has been adjusted to reflect the smoothing of gains and/or losses subject to a corridor between 90 to 110 percent of the market value of assets. 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.

CITY OF EASTON AGGREGATED PENSION TRUST FUND
SUPPLEMENTARY INFORMATION
(UNAUDITED)

SCHEDULES OF FUNDING PROGRESS – (Continued)

FIREMEN'S PENSION PLAN

	(1)	(2)	(3)	(4)	(5)	(6)
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)	Covered Payroll (c)	Unfunded (Assets in Excess of) Actuarial Accrued Liability as a % of Payroll [(b-a)/(c)]
01-01-07	$ 17,060,714	$ 17,240,727	$ 180,013	99.0%	$ 2,500,399	7.2%
01-01-09	16,463,283	18,209,105	1,745,822	90.4%	2,266,432	77.0%
01-01-11	15,393,967	22,975,675	7,581,708	67.0%	2,546,424	297.7%

Note: The market value of the plan's assets at 01-01-09 has been adjusted to reflect the smoothing of gains and/or losses subject to a corridor between 70 to 130 percent of the market value of assets. The market value of the plan's assets at 01-01-11 has been adjusted to reflect the smoothing of gains and/or losses subject to a corridor between 90 to 110 percent of the market value of assets. 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.

CITY OF EASTON AGGREGATED PENSION TRUST FUND
SUPPLEMENTARY INFORMATION
(UNAUDITED)

SCHEDULES OF FUNDING PROGRESS – (Continued)

OFFICERS' AND EMPLOYEES' PENSION PLAN

	(1)	(2)	(3)	(4)	(5)	(6)
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)	Covered Payroll (c)	Unfunded (Assets in Excess of) Actuarial Accrued Liability as a % of Payroll [(b-a)/(c)]
01-01-07	$ 11,643,036	$ 11,683,507	$ 40,471	99.7%	$ 420,982	9.6%
01-01-09	9,891,444	11,610,437	1,718,993	85.2%	326,105	527.1%
01-01-11	7,266,589	11,281,826	4,015,237	64.4%	307,184	13.1%

Note: The market value of the plan's assets at 01-01-09 has been adjusted to reflect the smoothing of gains and/or losses subject to a corridor between 70 to 130 percent of the market value of assets. The market value of the plan's assets at 01-01-11 has been adjusted to reflect the smoothing of gains and/or losses subject to a corridor between 90 to 110 percent of the market value of assets. 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.

CITY OF EASTON AGGREGATED PENSION TRUST 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.

Trends in unfunded (assets in excess of) actuarial accrued liability and annual covered payroll are both affected by inflation. Expressing the unfunded (assets in excess of) actuarial accrued liability as a percentage of annual covered payroll (Column 6) approximately adjusts for the effects of inflation and aids analysis of the plan's progress made in accumulating sufficient assets to pay benefits when due. Generally, where there is an unfunded actuarial accrued liability, the smaller this percentage, the stronger the plan. When assets are in excess of the actuarial accrued liability, the higher the bracketed percentage, the stronger the plan.

CITY OF EASTON AGGREGATED PENSION TRUST FUND
SUPPLEMENTARY INFORMATION
(UNAUDITED)

SCHEDULES OF CONTRIBUTIONS FROM EMPLOYER
AND OTHER CONTRIBUTING ENTITIES

POLICE PENSION PLAN

Year Ended December 31	Annual Required Contribution	Percentage Contributed
2007	$ 410,195	100.0%
2008	414,750	100.0%
2009	500,537	100.0%
2010	485,312	100.0%
2011	843,933	100.0%
2012	761,291	100.0%

CITY OF EASTON AGGREGATED PENSION TRUST FUND
SUPPLEMENTARY INFORMATION
(UNAUDITED)

SCHEDULES OF CONTRIBUTIONS FROM EMPLOYER
AND OTHER CONTRIBUTING ENTITIES – (Continued)

FIREMEN'S PENSION PLAN

Year Ended December 31	Annual Required Contribution	Percentage Contributed
2007	$ 286,227	100.0%
2008	290,276	100.0%
2009	405,504	100.0%
2010	434,626	100.0%
2011	434,219	100.0%
2012	441,521	100.0%

CITY OF EASTON AGGREGATED PENSION TRUST FUND
SUPPLEMENTARY INFORMATION
(UNAUDITED)

SCHEDULES OF CONTRIBUTIONS FROM EMPLOYER
AND OTHER CONTRIBUTING ENTITIES – (Continued)

OFFICERS' AND EMPLOYEES' PENSION PLAN

Year Ended December 31	Annual Required Contribution	Percentage Contributed
2007	$ 58,255	100.0%
2008	60,647	100.0%
2009	54,537	100.0%
2010	43,788	100.0%
2011	164,399	100.0%
2012	157,440	100.0%

CITY OF EASTON AGGREGATED PENSION TRUST FUND
SUPPLEMENTARY INFORMATION
NOTES TO SUPPLEMENTARY SCHEDULES
(UNAUDITED)

The information presented in the required 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, 2011
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 corridor between 90-110% of the market value of assets.
Actuarial assumptions:	
Investment rate of return	7.25%
Projected salary increases	5.0%

CITY OF EASTON AGGREGATED PENSION TRUST FUND
SUPPLEMENTARY INFORMATION
NOTES TO SUPPLEMENTARY SCHEDULES
(UNAUDITED)

FIREMEN'S PENSION PLAN

Actuarial valuation date	January 1, 2011
Actuarial cost method	Entry age normal
Amortization method	Level dollar
Remaining amortization period	15 years
Asset valuation method	Plan assets are valued using the method described in Section 210 of Act 205, as amended, subject to a corridor between 90-110% of the market value of assets.
Actuarial assumptions:	
Investment rate of return	7.25%
Projected salary increases	5.0%

CITY OF EASTON AGGREGATED PENSION TRUST FUND
SUPPLEMENTARY INFORMATION
NOTES TO SUPPLEMENTARY SCHEDULES
(UNAUDITED)

OFFICERS' AND EMPLOYEES' PENSION PLAN

Actuarial valuation date	January 1, 2011
Actuarial cost method	Entry age normal
Amortization method	Level dollar
Remaining amortization period	18 years
Asset valuation method	Plan assets are valued using the method described in Section 210 of Act 205, as amended, subject to a corridor between 90-110% of the market value of assets.
Actuarial assumptions:	
Investment rate of return	7.25%
Projected salary increases	5.0%

CITY OF EASTON AGGREGATED PENSION TRUST FUND
REPORT DISTRIBUTION LIST

This report was initially distributed to the following:

The Honorable Tom Corbett
Governor
Commonwealth of Pennsylvania

City of Easton Aggregated Pension Trust Fund
Northampton County
One South Third Street
Easton, PA 18042

The Honorable Salvatore J. Panto, Jr.	Mayor
Mr. Glenn Steckman	City Administrator
Mr. Chris Heagele	Director of Finance
Mr. Tony Bassil	City Controller
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