

# COMPLIANCE AUDIT

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## City of Easton Officers' and Employees' PMRS Pension Plan Northampton County, Pennsylvania For the Period January 1, 2015 to December 31, 2016

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December 2017



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 Easton  
Northampton County  
Easton, PA 18042

We have conducted a compliance audit of the City of Easton Officers' and Employees' PMRS Pension Plan for the period January 1, 2015 to December 31, 2016. 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 finding and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our finding 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 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 whether retirement benefits calculated for all 7 of the plan members who retired during the current audit period, and through the completion of our fieldwork procedures, represent payments to all (and only) those entitled to receive them and were properly determined and disbursed in accordance with the plan's governing document, applicable laws and regulations by recalculating the amount of the monthly pension benefit due to the retired individuals and comparing these amounts to supporting documentation evidencing amounts determined and actually paid to the recipients.
- We determined whether the January 1, 2013 and January 1, 2015 actuarial valuation reports were prepared and submitted to the former Public Employee Retirement Commission (PERC) by March 31, 2014 and 2016, 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 the terms of the contractual agreement with the Pennsylvania Municipal Retirement System were in accordance with the plan's governing document, if separately stated, and applicable laws and regulations by comparing the terms of the contractual agreement with the plan's governing document, if separately stated, and applicable laws and regulations.

The City of Easton Officers' and Employees' PMRS 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 Comprehensive Annual 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 Easton Officers' and Employees' PMRS 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 Easton Officers' and Employees' PMRS 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 finding further discussed later in this report:

Finding – Incorrect Data On Certification Form AG 385 Resulting In An  
Overpayment Of State Aid

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 Easton 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.

November 17, 2017



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 Officers' and Employees' PMRS 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 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 Easton Officers' and Employees' PMRS Pension Plan is a single-employer defined benefit pension plan for non-uniformed employees hired after January 1, 1979, locally controlled by the provisions of Article 143 of the city's codified ordinances, adopted pursuant to Act 15. The plan is also affected by the provisions of collective bargaining agreements between the city and its non-uniformed employees. The plan was established January 1, 1979. Active members are required to contribute 3 percent of compensation to the plan. As of December 31, 2016, the plan had 118 active members, 3 terminated members eligible for vested benefits in the future, and 72 retirees receiving benefits.

## **BACKGROUND – (Continued)**

As of December 31, 2016, selected plan benefit provisions are as follows:

### Eligibility Requirements:

Normal Retirement	Available upon attainment of age 65 or upon attainment of age 55 with 12 years of credited service.
Early Retirement	A voluntary early retirement available after 24 years of service. An involuntary early retirement is available after 8 years of service.
Vesting	A member is 100% vested after 12 years of service.

### Retirement Benefit:

Benefit equals 1.0% times credited service times Final Average Salary (FAS). A separate annuity is provided by the member contributions. FAS based upon final 5 years annualized salary.

### Survivor Benefit:

If eligible to retire at the time of death, beneficiary receives present value of accrued benefit. At retirement, member may select a survivor benefit.

### Disability Benefit:

Service Related	A 50% disability benefit is provided to a member who is unable to perform gainful employment regardless of age or service.
Non-service Related	A 30% disability benefit is provided to a member who has at least 10 years of service and who is unable to perform gainful employment.

CITY OF EASTON OFFICERS' AND EMPLOYEES PMRS PENSION PLAN  
STATUS OF PRIOR FINDING

Compliance With Prior Audit Recommendation

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

- Failure To Appoint A Chief Administrative Officer

The city adopted Resolution No. 23-2016 appointing a chief administrative officer for the pension plan.

CITY OF EASTON OFFICERS' AND EMPLOYEES PMRS PENSION PLAN  
FINDING AND RECOMMENDATION

**Finding – Incorrect Data On Certification Form AG 385 Resulting In An Overpayment Of State Aid**

Condition: The city certified 3 ineligible non-uniformed employees (3 units) and overstated payroll by \$35,896 on the Certification Form AG 385 filed in 2016. A similar condition occurred subsequent to the audit period. The city certified 2 ineligible non-uniformed employees (2 units) and overstated payroll by \$18,742 on the Certification Form AG 385 filed in 2017. 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 to ensure the accuracy of the data certified.

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 for 2016 and 2017 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</u>	<u>Unit Value</u>	<u>State Aid Overpayment</u>
2016	O&E PMRS	3	\$ 4,375	\$ 13,125
2017	O&E PMRS	2	\$ 4,588	<u>9,176</u>
Total Overpayment of State Aid				<u><u>\$ 22,301</u></u>

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

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

CITY OF EASTON OFFICERS' AND EMPLOYEES PMRS PENSION PLAN  
FINDING AND RECOMMENDATION

**Finding – (Continued)**

**Recommendation:** We recommend that the total excess state aid, in the amount of \$22,301, 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 2 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 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:** At the audit exit conference held on October 25, 2017, management indicated that they would provide a written response to this finding within 10 days; however, as of November 17, 2017, no such response has been provided.

**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 EASTON OFFICERS' AND EMPLOYEES PMRS PENSION PLAN  
POTENTIAL WITHHOLD OF STATE AID

The finding contained in this audit report cites an overpayment of state aid to the city in the amount of \$22,301, plus interest. A condition of this nature may lead to a total withholding of state aid in the future unless the 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 EASTON OFFICERS' AND EMPLOYEES PMRS PENSION PLAN  
SUPPLEMENTARY INFORMATION  
(UNAUDITED)

The supplementary information contained on Pages 7 and 8 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 AND 2015

	<u>2014</u>	<u>2015</u>
Total Pension Liability		
Service cost	\$ 824,389	\$ 816,351
Interest	1,110,052	1,132,977
Change of benefit terms	-	-
Difference between expected and actual experience	(445,874)	-
Changes of assumptions	-	145,747
Benefit payments, including refunds of member contributions	(612,033)	(1,522,955)
Net Change in Total Pension Liability	<u>876,534</u>	<u>572,120</u>
Total Pension Liability - Beginning	<u>19,748,649</u>	<u>20,625,183</u>
Total Pension Liability - Ending (a)	<u><u>\$20,625,183</u></u>	<u><u>\$21,197,303</u></u>
Plan Fiduciary Net Position		
Contributions - employer	\$ 314,675	\$ 405,999
Contribution - member	422,268	427,351
Net investment income	505,847	133,787
Benefit payments, including refunds of member contributions	(612,033)	(1,522,955)
Administrative expense	(44,805)	(43,476)
Net Change in Plan Fiduciary Net Position	<u>585,952</u>	<u>(599,294)</u>
Plan Fiduciary Net Position - Beginning	<u>19,353,945</u>	<u>19,939,897</u>
Plan Fiduciary Net Position - Ending (b)	<u><u>\$19,939,897</u></u>	<u><u>\$19,340,603</u></u>
Net Pension Liability - Ending (a-b)	<u><u>\$ 685,286</u></u>	<u><u>\$ 1,856,700</u></u>
Plan Fiduciary Net Position as a Percentage of the Total Pension Liability	96.68%	91.24%
Estimated Covered Employee Payroll	\$ 6,261,571	\$ 6,194,675
Net Pension Liability as a Percentage of Covered Employee Payroll	10.94%	29.97%

CITY OF EASTON OFFICERS' AND EMPLOYEES PMRS 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 city as of December 31, 2016, calculated using the discount rate of 5.5%, as well as what the city'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 (4.5%)	Current Discount Rate (5.5%)	1% Increase (6.5%)
Net Pension Liability	\$ 3,629,852	\$ 1,856,700	\$ 365,097

CITY OF EASTON OFFICERS' AND EMPLOYEES PMRS 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, 2011, 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)
01-01-11	\$ 15,965,646	\$ 15,590,694	\$ (374,952)	102.4%
01-01-13	18,432,385	18,482,683	50,298	99.7%
01-01-15	20,366,862	20,625,183	258,321	98.7%

CITY OF EASTON OFFICERS' AND EMPLOYEES PMRS 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 EASTON OFFICERS' AND EMPLOYEES PMRS PENSION PLAN  
 SUPPLEMENTARY INFORMATION  
 (UNAUDITED)

SCHEDULE OF CONTRIBUTIONS FROM EMPLOYER  
 AND OTHER CONTRIBUTING ENTITIES

Year Ended December 31	Annual Required Contribution	Percentage Contributed
2011	\$ 290,556	100.0%
2012	288,585	100.0%
2013	273,801	100.0%
2014	302,232	104.1%
2015	405,659	100.1%
2016	391,711	100.0%

CITY OF EASTON OFFICERS' AND EMPLOYEES PMRS 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, 2015
Actuarial cost method	Entry age normal
Amortization method	Level dollar
Remaining amortization period	10 years
Asset valuation method	Fair value
Actuarial assumptions:	
Investment rate of return	5.5%, net of expenses
Projected salary increases *	Age-related scale for merit/ seniority (e.g. age 30 - 6.4%; age 40 - 5.0%; age 50 - 4.1%; age 60 - 3.7%)
Cost-of-living adjustments	3.0%, where applicable

\* Includes inflation at 3.0%

CITY OF EASTON OFFICERS' AND EMPLOYEES PMRS PENSION PLAN  
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This report was initially distributed to the following:

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Pennsylvania Municipal Retirement System

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