



**CITY OF JEANNETTE POLICE PENSION PLAN  
WESTMORELAND COUNTY  
COMPLIANCE AUDIT REPORT  
FOR THE PERIOD  
JANUARY 1, 2010, TO DECEMBER 31, 2011**

**COMMONWEALTH OF PENNSYLVANIA**

**EUGENE A. DEPASQUALE - AUDITOR GENERAL**

**DEPARTMENT OF THE AUDITOR GENERAL**



**CITY OF JEANNETTE POLICE PENSION PLAN**

**WESTMORELAND COUNTY**

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### ABBREVIATION

PERC - Public Employee Retirement Commission

## 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.

Pension plan aid is provided from a 2 percent foreign casualty insurance premium tax, a portion of the foreign 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 Jeannette Police Pension Plan 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 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 Jeannette Police Pension Plan is a single-employer defined benefit pension plan locally controlled by the provisions of Ordinance No. 00-10, as amended, adopted pursuant to Act 317. The plan is also affected by the provisions of collective bargaining agreements between the city and its police officers.



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**EUGENE A. DePASQUALE**  
**AUDITOR GENERAL**

The Honorable Mayor and City Council  
City of Jeannette  
Westmoreland County  
Jeannette, PA 15644

We have conducted a compliance audit of the City of Jeannette Police Pension Plan for the period January 1, 2010, to December 31, 2011. 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 findings and conclusions based on our audit objective. We believe that the evidence obtained provides a reasonable basis for our findings and 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. 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.

City officials are responsible for establishing and maintaining effective internal controls to provide reasonable assurance that the City of Jeannette Police 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 objective, 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 objective.

The results of our tests indicated that, in all significant respects, the City of Jeannette 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 – Failure To Pay The Minimum Municipal Obligation Of The Plan
- Finding No. 2 – Failure To Implement Act 44 Mandatory Distressed Provisions

As previously noted, the objective of our audit of the City of Jeannette Police Pension Plan 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:

<u>Level</u>	<u>Indication</u>	<u>Funding Criteria</u>
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 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. For example, **the plan's funded ratio went from 82.1% as of January 1, 2007, to a ratio of 58.9% as of January 1, 2011**, which is the most recent date available. 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 the police pension plan to ensure its long-term financial stability.

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



April 26, 2013

EUGENE A. DEPASQUALE  
Auditor General

CITY OF JEANNETTE POLICE PENSION PLAN  
FINDINGS AND RECOMMENDATIONS

Finding No. 1 – Failure To Pay The Minimum Municipal Obligation Of The Plan

Condition: Plan officials did not pay the minimum municipal obligation (MMO) of the police pension plan for the year 2012, as required by Act 205. The city had an unpaid 2012 MMO of \$414,406.

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.

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.

Cause: Plan officials did not comply with the Act 205 requirements because the city is in financial distress and lacked the funds to pay the MMO.

Effect: The failure to 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 city's failure to pay the 2012 MMO by the December 31, 2012, deadline, the city must add the 2012 MMO to the current year's MMO and include interest, as required by Act 205.



CITY OF JEANNETTE POLICE PENSION PLAN  
FINDINGS AND RECOMMENDATIONS

Finding No. 1 – (Continued)

Recommendation: We recommend that the city pay the MMO due to the police pension plan for the year 2012, 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.

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

Finding No. 2 – Failure To Implement Act 44 Mandatory Distressed Provisions

Condition: 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:

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

Based on the plan’s funded ratio of 66.3% as of January 1, 2009, in aggregation with the funded ratios of the city’s other pension plans, the Public Employee Retirement Commission (PERC) issued a notification in 2010 that the city was in Level II moderate distress status. Based on the plan’s funded ratio of 58.9% as of January 1, 2011, in aggregation with the funded ratios of the city’s other pension plans, PERC issued another notification in 2012 that the city is currently in Level II moderate distress status.

Included with the determination notices, PERC sent the city the Act 205 Recovery Program Election Form outlining the mandatory remedies that must be implemented and the voluntary remedies that the city could elect to implement. This form was required to be signed by the plan’s chief administrative officer and returned to PERC.

Although the city submitted the election forms to PERC, the city has not begun to take action to implement the mandatory remedies contained in Act 44 for municipalities in Level II distress regarding the aggregation of pension funds and the submission of a plan for administrative improvement to PERC.

CITY OF JEANNETTE POLICE PENSION PLAN  
FINDINGS AND RECOMMENDATIONS

Finding No. 2 – (Continued)

Criteria: Act 205, amended by Act 44, at Section 605(a), states:

Recovery program level II.

- (a) Mandatory remedies. Any municipality to which level II of the recovery program applies shall utilize the following remedies:
  - (1) The aggregation of trust funds pursuant to section 607(b).
  - (2) The submission of a plan for administrative improvement pursuant to section 607(i).

Cause: City officials failed to establish adequate internal control procedures to ensure that the mandatory distress remedies have been implemented.

Effect: The city is not in compliance with the Act 44 mandatory distress remedy provisions applicable to Level II which are designed to improve the funding status and administrative efficiency of its pension plans.

Recommendation: We recommend that city officials contact PERC for guidance in the implementation of the mandatory distress remedies applicable to Level II pursuant to Act 44 of 2009.

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

CITY OF JEANNETTE POLICE PENSION PLAN  
POTENTIAL WITHHOLD OF STATE AID

A condition such as that reported by Finding No. 1 contained in this audit report may lead to a total withholding of state aid in the future unless that finding is corrected. However, such action will not be considered if sufficient written documentation is provided to verify compliance with this department's recommendation. Such documentation should be submitted to: Department of the Auditor General, Bureau of Municipal Pension Audits, 402-D Finance Building, Harrisburg, PA 17120.

CITY OF JEANNETTE 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, 2007, is as follows:

	(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	\$ 6,332,222	\$ 7,709,913	\$ 1,377,691	82.1%	\$ 893,985	154.1%
01-01-09	5,794,711	8,739,050	2,944,339	66.3%	1,042,985	282.3%
01-01-11	5,796,039	9,847,386	4,051,347	58.9%	1,014,282	399.4%

Note: The market values of the plan's assets at 01-01-07, 01-01-09 and 01-01-11, have been adjusted to reflect the smoothing of gains and/or losses over a 4-year averaging period. This method will lower contributions in years of less than expected returns and increase contributions in years of greater than expected returns. The net effect over long periods of time is to have less variance in contribution levels from year to year.

CITY OF JEANNETTE 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.

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. However, when assets are in excess of the actuarial accrued liability, the higher the bracketed percentage, the stronger the plan.

CITY OF JEANNETTE POLICE PENSION PLAN  
SUPPLEMENTARY INFORMATION  
(UNAUDITED)

SCHEDULE OF CONTRIBUTIONS FROM EMPLOYER  
AND OTHER CONTRIBUTING ENTITIES

Year Ended December 31	Annual Required Contribution	Percentage Contributed
2006	\$ 129,377	100.0%
2007	231,493	100.0%
2008	217,836	100.0%
2009	254,809	100.2%
2010	255,258	100.0%
2011	347,276	100.0%

CITY OF JEANNETTE POLICE PENSION PLAN  
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:

Actuarial valuation date	January 1, 2011
Actuarial cost method	Entry age normal
Amortization method	Level dollar, closed
Remaining amortization period	18 years
Asset valuation method	Fair value, 4-year smoothing
Actuarial assumptions:	
Investment rate of return	7.0%
Projected salary increases *	5.0%
* Includes inflation at	3.0%

CITY OF JEANNETTE POLICE PENSION PLAN  
COMMENTS

Automatic Promotions Granted Prior To Retirement

The City of Jeannette has maintained a practice of promoting police officers to the next higher grade in rank for a period of at least one month immediately prior to retirement.

Ordinance No. 66-9 established a past practice, which the city continues to follow at Section II, which states, in part:

...Any Participant in the Plan before retiring shall be promoted to the next higher grade in rank for a period of at least one month immediately prior to his retirement and said next higher grade in rank shall be at least that of a Lieutenant.

Section 4303(a) of the Third Class City Code states, in part:

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.

While the city's practice is not considered to be in noncompliance with the Third Class City Code, it does serve to inflate the pension benefits of retirees from the city's police pension plan and increases the municipal contributions required to fund the plan in accordance with Act 205 funding standards. The additional unfunded liability resulting from the pre-retirement promotions contributes to the city's inability to meet its funding obligations to the plan as cited in Finding No. 1 contained in this report.



CITY OF JEANNETTE POLICE PENSION PLAN  
REPORT DISTRIBUTION LIST

This report was initially distributed to the following:

The Honorable Tom Corbett  
Governor  
Commonwealth of Pennsylvania

City of Jeannette Police Pension Plan  
Westmoreland County  
110 South Second Street  
Jeannette, PA 15644

The Honorable Robert M. Carter	Mayor
Mr. William Bedont	Director of Accounts and Finance
Mr. Michael J. Minyon, Jr.	City Clerk

This report is a matter of public record and is available online at [www.auditorgen.state.pa.us](http://www.auditorgen.state.pa.us). Media questions about the report can be directed to the Pennsylvania Department of the Auditor General, Office of Communications, 231 Finance Building, Harrisburg, PA 17120; via email to: [news@auditorgen.state.pa.us](mailto:news@auditorgen.state.pa.us).