COMPLIANCE AUDIT

City of Aliquippa Firefighter Pension Plan

Beaver County, Pennsylvania

For the Period

January 1, 2018 to December 31, 2019

December 2020

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 Aliquippa
Beaver County
Aliquippa, PA 15001

We have conducted a compliance audit of the City of Aliquippa Firefighter Pension Plan for the period January 1, 2018 to December 31, 2019. We also evaluated compliance with some requirements subsequent to that period when possible. The audit was conducted pursuant to authority derived from the Municipal Pension Plan Funding Standard and Recovery Act (Act 205 of 1984, as amended, 53 P.S. § 895.402(j), which requires the Auditor General, as deemed necessary, to audit every municipality which receives general municipal pension system state aid and every municipal pension plan and fund in which general municipal pension system state aid is deposited. The audit was not conducted, nor was it required to be, in accordance with Government Auditing Standards issued by the Comptroller General of the United States. We planned and performed the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our finding and conclusions based on our audit objective. We believe that the evidence obtained provides a reasonable basis for our finding 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. To determine whether the pension plan was administered in compliance with applicable state laws, regulations, contracts, administrative procedures, and local ordinances and policies, our methodology included the following:

- We determined whether state aid was properly determined and deposited in accordance with Act 205 requirements by verifying the annual deposit date of state aid and determining whether deposits were made within 30 days of receipt for all years within the period under audit.

- We determined whether annual employer contributions were calculated and deposited in accordance with the plan's governing document and applicable laws and regulations by examining the municipality's calculation of the plan's annual financial requirements and minimum municipal obligation (MMO) and comparing these calculated amounts to amounts actually budgeted and deposited into the pension plan as evidenced by supporting documentation.

- We determined whether annual employee contributions were calculated, deducted, and deposited into the pension plan in accordance with the plan's governing document and applicable laws and regulations by testing total members' contributions on an annual basis using the rates obtained from the plan's governing document in effect for all years within the period under audit and examining documents evidencing the deposit of these employee contributions into the pension plan.

- We determined whether retirement benefits calculated for the plan member who retired during the current audit period represent payments to all (and only) those entitled to receive them and were properly determined and disbursed in accordance with the plan's governing document, applicable laws, and regulations by recalculating the amount of the monthly pension benefits due to the retired individual and comparing these amounts to supporting documentation evidencing amounts determined and actually paid to the recipients.

- We determined whether the January 1, 2019 actuarial valuation report was prepared and submitted by March 31, 2020, in accordance with Act 205 and whether selected information provided on this report is accurate, complete, and in accordance with plan provisions to ensure compliance for participation in the state aid program by comparing selected information to supporting source documentation.

- We determined whether the pension plan is in compliance with Act 205 for distressed municipalities through inquiry of plan officials and evaluation of the recovery remedies implemented during the audit period.

City of Aliquippa contracted with an independent certified public accounting firm for annual audits of its basic 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 Aliquippa Firefighter Pension Plan is administered in compliance with applicable state laws, regulations, contracts, administrative procedures, and local ordinances and policies. As previously described, we tested transactions, interviewed selected officials, and performed procedures to the extent necessary to provide reasonable assurance of detecting instances of noncompliance with legal and regulatory requirements or noncompliance with provisions of contracts, administrative procedures, and local ordinances and policies that are significant within the context of the audit objective.

The results of our procedures indicated that, in all significant respects, the City of Aliquippa Firefighter 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 Maintain Required Documentation And Evidence Of Required Annual Funding Of The City's Pension Plans In Accordance With Special Taxing Provisions Of Act 205

Finding No. 2 – Failure To Maintain Vested Pension Benefit Calculation

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.

During the current audit period, the City has continued to contribute more than the required minimum municipal obligation (MMO) to the city firefighter pension plan. These additional contributions are due, to the City's implementation of an Act 205 earned income pension funding tax *(referred to later in Finding No. 1 contained in this report)*. These deposits have had a dramatic effect on the city firefighter pension plan's funding ratios. The plan's funded ratio increased to 102.4% as of January 1, 2019, which is the most recent data available, and we commend the city for their continuing efforts in improving the financial position of the city's police pension plan.

The contents of this report were discussed with officials of City of Aliquippa 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.

December 1, 2020

EUGENE A. DEPASQUALE
Auditor General

CONTENTS

Page

BACKGROUND

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

Annual state aid allocations are provided from a 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 Aliquippa Firefighter Pension Plan is also governed by implementing regulations published at Title 16, Part IV of the Pennsylvania Code and applicable provisions of various other state statutes

Act 67 - The Third Class City Code, Act of November 24, 2015 (P.L. 242, No. 67), as amended, 11 Pa. C.S. § 10101 et seq.

The City of Aliquippa Firefighter Pension Plan is a single-employer defined benefit pension plan locally controlled by the provisions of Ordinance 4 of 2008, as amended, adopted pursuant to Act 67. The plan is also affected by the provisions of collective bargaining agreements between the city and its firefighters. The plan was established July 1, 1964. Active members are required to contribute 5 percent of compensation to the plan, plus $1 per month until age 65. As of December 31, 2019, the plan had 9 active members, 3 terminated members eligible for vested benefits in the future, and 8 retirees receiving pension benefits.

CITY OF ALIQUIPPA FIREFIGHTER PENSION PLAN
FINDING AND RECOMMENDATION

Finding No. 1 – Failure To Maintain Required Documentation And Evidence Of Required Annual Funding Of The City's Pension Plans In Accordance With Special Taxing Provisions Of Act 205

Condition: Between 2001 and 2003, the City's pension plans experienced actuarial investment losses of almost $4,000,000 and were classified by the state as Level III Distress. In 2002 and for 2003, the City assessed a 0.1% special Earned Income Tax (EIT) levy under Act 205 dedicated to the pension funds. The City Council, in the 2004 budget, voted to increase the EIT special levy to 0.6% for pension purposes. In 2005, the City conducted a pension study with the assistance from a Department of Community Economic Development (DCED) Act 47 grant that studied the pension funding deficits and made recommendations for dealing with pension liabilities. As a result, this study recommended, in part, a continuation of the dedicated 0.6% levy for the purposes of addressing delinquent Minimum Municipal Obligation (MMO) payments to the funds. This levy was reduced to 0.5% beginning in 2007 because delinquent MMO payments were completely addressed by that time.[1] The city however, failed to provide supporting documentation evidencing the determination of its level of contributions to its pension plans prior to the implementation of the special tax and its continued monitoring over current contribution levels to ensure that the city met its annual funding requirements during 2018 and 2019 in accordance with the distress provisions of Act 205.

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.

[1] 2018 City of Aliquippa Financial Condition Evaluation of Designated Status Under Act 47; Filed December 12, 2018.

<u>Finding No. 1 – (Continued)</u>

Furthermore, relative to the additional remedies available to distressed municipalities to assist with the funding of their pension plans, Section 607(f) of Act 205 further states:

(1) If the tax rates set by the municipality on earned income or on real property are at the maximum provided by applicable law, the municipality may increase its tax on either earned income or real property above those maximum rates. The proceeds of this special municipal tax increase shall be used solely to defray the additional costs required to be paid pursuant to this act, which are directly related to the pension plans of the municipality. <u>The municipality utilizing this special municipal taxing authority shall not reduce the level of municipal contributions to the pension plans prior to the implementation of the special municipal taxing authority.</u> (Emphasis added.)

(2) The average level of municipal contributions to the pension plans from all revenue sources for the three years immediately prior to the implementation of the special municipal taxing authority shall be expressed as a percentage of the average covered payroll for that same three year period: Provided, however, that any supplemental contributions made to the plans pursuant to any pension recovery legislation enacted by the municipalities shall be excluded for purposes of determining the level of municipal contribution to the pension plans prior to the implementation of the special municipal taxing authority. In each year subsequent to the implementation of the special municipal taxing authority, the municipal contributions to the pension plan from all revenue sources existing prior to the implementation of the special existing municipal taxing authority, reduced by any supplemental pension recovery contributions, shall equal or exceed this average percentage of the current covered payroll.

A municipality utilizing the provisions of section 404 may levy or continue to levy the special municipal tax increase under this subsection provided that the municipality does not reduce the level of municipal contributions to the pension plans prior to the implementation of the special municipal taxing authority. In executing the procedure prescribed in this subsection to determine the level of municipal contributions, the debt service payments for bonds or notes issued under section 404 shall be considered municipal contributions.

<u>Cause</u>: The city failed to establish adequate internal control procedures to assist them in complying with the special tax provisions of Act 205. Current officials were unable to locate or provide substantive documentation evidencing whether previous plan officials appropriately determined the city’s required funding levels prior to enacting the special tax and/or whether the city previously performed procedures necessary to ensure and evidence that annual funding levels mandated by Act 205 since implementation of the special tax were met.

Finding No. 1 – (Continued)

Effect: The failure to establish adequate internal control procedures to apply the distress provisions of Section 607(f) of Act 205 and fund the city's pension plans accordingly could result in the plans not having the necessary resources to meet current and future benefit obligations to its members; however, we were unable to determine the impact on the city's pension plans for 2018 and 2019 because as noted in the Cause section above, the city was unable to provide the original determination of its level of municipal contributions to its plans or its revenue sources existing prior to implementation of the special tax. The failure to maintain the levels of contribution prior to enacting the additional special tax reduces the net overall contributions to the plan, potentially negating benefits of the additional tax. Furthermore, the special tax that is being collected is the only contribution that is being deposited into the pension plan in addition to state aid.

Recommendation: We recommend that the city, with assistance from its actuary, determine or locate the prior determination of the city's required level of annual contributions under Section 607(f) of Act 205. Copies of these calculations must be maintained by the city for examination during our next audit of the plans.

In addition, we recommend that city officials establish and implement adequate internal control procedures to ensure that the city does not reduce its level of contributions to its pension plans from funding sources prior to the implementation of the special municipal tax in accordance with Act 205 for periods subsequent to this report beginning with the city's 2021 budgetary process. Such procedures should include maintaining appropriate supporting documentation identifying the sources of its annual contributions to its pension plans as well as an annual reconciliation evidencing that funding requirements are appropriately met in accordance with Section 607(f) of Act 205.

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

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

Finding No. 2 – Failure To Maintain Vested Pension Benefit Calculations

Condition: The city failed to determine and maintain vested pension benefit calculations for three plan members who terminated employment with the city during the audit period.

Criteria: Sound internal control procedures dictate that vested pension benefits should be determined in a timely manner following a plan member's termination of employment and that the city should maintain adequate supporting documentation to substantiate the accuracy of vested pension benefit determinations to avoid discrepancies occurring in the future when the former employees are eligible to begin receiving their pension benefits.

Finding No. 2 – (Continued)

Cause: Plan officials failed to engage its pension plan consultant to prepare the vested pension benefit calculations.

Effect: The failure of plan officials to maintain vested pension benefit calculations could result in inconsistent or improper benefit calculations and incorrect benefit payments from the pension plan.

Recommendation: We recommend that plan officials prepare and/or provide the vested benefit calculations for the three members who separated from employment with the city during the current audit period and met the requirements for a deferred vested pension benefit under the plan document. We also recommend that plan officials establish adequate internal control procedures to ensure that all vested pension benefits are determined timely, supported by adequate documentation, and maintained by the city.

Management's Response: The city is going to contact their plan consultant about the vested calculations for the members.

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

CITY OF ALIQUIPPA FIREFIGHTER 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, 2015, 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)
01-01-15	$ 3,857,519	$ 4,376,750	$ 519,231	88.1%
01-01-17	4,659,516	4,703,977	44,461	99.1%
01-01-19	5,507,271	5,380,783	(126,488)	102.4%

Note: The market values of the plan's assets at 01-01-15, 01-01-17, and 01-01-19 have been adjusted to reflect the smoothing of gains and/or losses over a 4-year averaging period subject to a corridor between 90 to 110 percent of the market value of assets. 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.

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 ALIQUIPPA FIREFIGHTER PENSION PLAN
SUPPLEMENTARY INFORMATION
(UNAUDITED)

SCHEDULE OF CONTRIBUTIONS FROM EMPLOYER
AND OTHER CONTRIBUTING ENTITIES

Year Ended December 31	Annual Required Contribution	Percentage Contributed
2014	$ 265,463	141.6%
2015	202,220	140.5%
2016	202,766	143.4%
2017	210,590	151.7%
2018	191,864	188.1%
2019	174,007	175.5%

CITY OF ALIQUIPPA FIREFIGHTER 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, 2019
Actuarial cost method	Entry age normal
Amortization method	N/A
Remaining amortization period	N/A
Asset valuation method	Fair value, 4-year smoothing, subject to a corridor between 90-110% of the market value assets.
Actuarial assumptions:	
Investment rate of return	7.00%
Projected salary increases *	5.00%

* Includes inflation at 2.50%

CITY OF ALIQUIPPA FIREFIGHTER PENSION PLAN
REPORT DISTRIBUTION LIST

This report was initially distributed to the following:

The Honorable Tom W. Wolf
Governor
Commonwealth of Pennsylvania

The Honorable Dwan B. Walker
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Mr. Samuel L. Gill
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Ms. Cheryl McFarland
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