

# COMPLIANCE AUDIT

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## City of McKeesport Firefighters Pension Plan Allegheny County, Pennsylvania For the Period January 1, 2017 to December 31, 2018

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July 2019



Commonwealth of Pennsylvania  
Department of the Auditor General

Eugene A. DePasquale • Auditor General



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**EUGENE A. DePASQUALE  
AUDITOR GENERAL**

The Honorable Mayor and City Council  
City of McKeesport  
Allegheny County  
McKeesport, PA 15132

We have conducted a compliance audit of the City of McKeesport Firefighters Pension Plan for the period January 1, 2017 to December 31, 2018. We also evaluated compliance with some requirements subsequent to that period when possible. The audit was conducted pursuant to authority derived from Section 402(j) of Act 205 and in accordance with the standards applicable to performance audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our conclusions based on our audit objective. We believe that the evidence obtained provides a reasonable basis for our conclusions based on our audit objective.

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

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

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

- We determined whether annual employee contributions were calculated, deducted, and deposited into the pension plan in accordance with the plan's governing document and applicable laws and regulations by testing total members' contributions on an annual basis using the rates obtained from the plan's governing document in effect for all years within the period under audit and examining documents evidencing the deposit of these employee contributions into the pension plan.
- We determined whether retirement benefits calculated for the plan lone 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 benefit due to the retired individual and comparing this amount to supporting documentation evidencing the amount determined and actually paid to the recipient.
- We determined whether the January 1, 2017 actuarial valuation report was prepared and submitted by March 31, 2018 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 all annual special ad hoc postretirement reimbursements received by the municipality were authorized and appropriately deposited in accordance with Act 147 by tracing information to supporting documentation maintained by plan officials.
- 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 and through the completion of our fieldwork procedures.
- We determined whether the terms and methodologies of the issuance of pension obligation bonds by the municipality, and any restrictions were in compliance with plan provisions and Act 205 through inquiry of plan officials and examination of supporting documentation.
- We determined whether provisions of the Deferred Retirement Option Plan (DROP) were in accordance with the provisions of Act 205 by examining provisions stated in the plan's governing documents.

The City of McKeesport contracted with an independent certified public accounting firm for an audit of its basic financial statements for the year 2017, which is available at the city's offices. These 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 McKeesport Firefighters 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 and as previously described, we tested transactions, assessed official actions, performed analytical procedures, and interviewed selected officials to provide reasonable assurance of detecting instances of noncompliance with legal and regulatory requirements or noncompliance with provisions of contracts, administrative procedures, and local ordinances and policies that are significant within the context of the audit objective.

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

The accompanying supplementary information is presented for purposes of additional analysis. We did not audit the information or conclude on it and, accordingly, express no form of assurance on it.

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

July 23, 2019



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 McKeesport Firefighters 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 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.

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.

The City of McKeesport Firefighters Pension Plan is a single-employer defined benefit pension plan locally controlled by the provisions of Ordinance No. 06-10, as amended, adopted pursuant to Act 67. The plan is also affected by the provisions of collective bargaining agreements between the city and its fighters. The plan was established September 6, 1889. Active members are required to contribute 5 percent of compensation to the plan. As of December 31, 2018, the plan had 20 active members, no terminated members eligible for vested benefits in the future, and 39 retirees receiving pension benefits from the plan.

## BACKGROUND – (Continued)

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

### Eligibility Requirements:

Normal Retirement	20 years of service.
Early Retirement	None
Vesting	100% vesting available after 12 years of service.

### Retirement Benefit:

Benefit equal 50% of average monthly compensation based on the greater of (a) highest 5 years of credited service or (b) annual rate of pay at termination plus a service increment equal to 1/40<sup>th</sup> of monthly benefit for each completed year in excess of 20 years (maximum \$500).

### Survivor Benefit:

Before Retirement Eligibility	Normal retirement benefit at the date of death as if the participant were eligible for retirement.
After Retirement Eligibility	A monthly benefit equal to 100% of the pension the member was receiving or was entitled to receive on the day of the member's death.

### Disability Benefit:

Service Related	Benefit equals 50% of the member's salary at the time the disability was incurred, offset by Social Security disability benefits received for the same injury.
Nonservice related	At least 5 years of service, a 50% benefit based on the lowest base salary paid during the year of disability, reduced for less than 20 years of service.

CITY OF MCKEESPORT FIREFIGHTERS PENSION PLAN  
SUPPLEMENTARY INFORMATION  
(UNAUDITED)

The supplementary information contained on Pages 3 through 5 reflects the implementation of GASB Statement No. 67, *Financial Reporting for Pension Plans*. The objective of this statement is to improve financial reporting by state and local governmental pension plans.

SCHEDULE OF CHANGES IN THE NET PENSION  
LIABILITY AND RELATED RATIOS  
FOR THE YEARS ENDED DECEMBER 31, 2014, 2015, 2016 AND 2017

	<u>2014</u>	<u>2015</u>	<u>2016</u>	<u>2017</u>
Total Pension Liability				
Service cost	\$ 175,180	\$ 178,965	\$ 185,923	\$ 180,306
Interest	869,838	860,316	910,294	934,941
Difference between expected and actual experience	(810,905)	-	-	72,976
Changes of assumptions	161,401	-	-	504,701
Benefit payments, including refunds of member contributions	<u>(744,515)</u>	<u>(711,210)</u>	<u>(716,073)</u>	<u>(744,976)</u>
Net Change in Total Pension Liability	(349,001)	328,071	380,144	947,948
Total Pension Liability – Beginning	<u>11,606,303</u>	<u>11,257,302</u>	<u>11,585,373</u>	<u>11,965,517</u>
Total Pension Liability – Ending (a)	<u>\$ 11,257,302</u>	<u>\$ 11,585,373</u>	<u>\$ 11,965,517</u>	<u>\$ 12,913,465</u>
Plan Fiduciary Net Position				
Contributions – employer *	\$ 578,118	\$ -	\$ 1,442,717	\$ 666,868
Contributions – member	65,825	73,445	73,276	78,134
Net investment income	172,404	(263,294)	511,404	1,211,235
Benefit payments, including refunds of member contributions	(744,515)	(711,210)	(716,073)	(744,976)
Administrative expense	(29,754)	(22,496)	(24,792)	(15,316)
Other	<u>2,843</u>	<u>-</u>	<u>-</u>	<u>-</u>
Net Change in Plan Fiduciary Net Position	44,921	(923,555)	1,286,532	1,195,945
Plan Fiduciary Net Position – Beginning	<u>7,900,024</u>	<u>7,944,945</u>	<u>7,021,390</u>	<u>8,307,922</u>
Plan Fiduciary Net Position – Ending (b)	<u>\$ 7,944,945</u>	<u>\$ 7,021,390</u>	<u>\$ 8,307,922</u>	<u>\$ 9,503,867</u>
Net Pension Liability – Ending (a-b)	<u>\$ 3,312,357</u>	<u>\$ 4,563,983</u>	<u>\$ 3,657,595</u>	<u>\$ 3,409,598</u>
Plan Fiduciary Net Position as a Percentage of the Total Pension Liability	70.58%	60.61%	69.43%	73.60%
Estimated Covered Employee Payroll	\$ 1,234,680	\$ 1,366,919	\$ 1,393,498	\$ 1,208,261
Net Pension Liability as a Percentage of Covered Employee Payroll	268.28%	333.89%	262.48%	282.19%

\* Employer contributions for 2016 include 2015 contributions with interest.



CITY OF MCKEESPORT FIREFIGHTERS 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, 2014, 2015 and 2016, calculated using the discount rate of 7.90%, 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:

	<u>1% Decrease (6.90%)</u>	<u>Current Discount Rate (7.90%)</u>	<u>1% Increase (8.90%)</u>
Net Pension Liability – 12/31/14	\$ 4,438,169	\$ 3,312,357	\$ 2,349,975
Net Pension Liability – 12/31/15	\$ 5,722,604	\$ 4,563,983	\$ 3,573,554
Net Pension Liability – 12/31/16	\$ 4,854,233	\$ 3,657,595	\$ 2,634,668

In addition, the following presents the net pension liability of the city as of December 31, 2017, calculated using the discount rate of 7.75%, 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:

	<u>1% Decrease (6.75%)</u>	<u>Current Discount Rate (7.75%)</u>	<u>1% Increase (8.75%)</u>
Net Pension Liability – 12/31/17	\$ 4,726,495	\$ 3,409,598	\$ 2,295,586

CITY OF MCKEESPORT FIREFIGHTERS PENSION PLAN  
SUPPLEMENTARY INFORMATION  
(UNAUDITED)

SCHEDULE OF CONTRIBUTIONS

Year Ended December 31	Actuarially Determined Contribution	Actual Contributions	Contribution Deficiency (Excess)	Covered- Employee Payroll *	Contributions as a Percentage of Covered- Employee Payroll
2009	\$ 340,440	\$ 340,440	\$ -	\$1,046,344	32.54%
2010	358,217	358,217	-	1,174,388	30.50%
2011	387,810	387,810	-	1,190,570	32.57%
2012	387,646	387,646	-	1,258,097	30.81%
2013	585,801	585,801	-	1,187,801	49.32%
2014	578,118	578,118	-	1,234,680	46.82%
2015**	661,449	-	661,449	1,366,919	0.00%
2016**	1,442,717	1,442,717	-	1,393,498	103.53%
2017	666,868	666,868	-	1,208,261	55.19%
2018	636,474	636,474	-		

\* Due to the timing of this audit, covered-employee payroll for 2018 was not provided in this schedule.

\*\* Due to severe financial distress, the city did not have funds available to pay its required obligation for 2015. However, the outstanding obligation, along with applicable interest, was added to the 2016 required obligation and deposited during 2016.

SCHEDULE OF INVESTMENT RETURNS

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

2017	15.67%
2016	8.03%
2015	(2.98%)
2014	2.79%
2013	13.51%
2012	13.35%
2011	0.21%
2010	13.07%
2009	20.35%
2008	(25.50%)

CITY OF MCKEESPORT FIREFIGHTERS PENSION PLAN  
 SUPPLEMENTARY INFORMATION  
 (UNAUDITED)

SCHEDULE OF FUNDING PROGRESS

Historical trend information about the plan is presented herewith as supplementary information. It is intended to help users assess the plan's funding status on a going-concern basis, assess progress made in accumulating assets to pay benefits when due, and make comparisons with other state and local government retirement systems.

The actuarial information is required by Act 205 biennially. The historical information, beginning as of January 1, 2013, is as follows:

	(1)	(2)	(3)	(4)
Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) - Entry Age (b)	Unfunded (Assets in Excess of) Actuarial Accrued Liability (b) - (a)	Funded Ratio (a)/(b)
01-01-13	\$ 8,253,504	\$ 11,329,516	\$ 3,076,012	72.8%
01-01-15	9,027,169	11,257,302	2,230,133	80.2%
01-01-17	9,969,506	12,543,194	2,573,688	79.5%

Note: The market values of the plan's assets at 01-01-13, 01-01-15 and 01-01-17 are valued using the smoothing method described in Section 210 of Act 205, as amended, subject to a ceiling of 120% of the market value of the 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 MCKEESPORT FIREFIGHTERS 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 MCKEESPORT FIREFIGHTERS PENSION PLAN  
SUPPLEMENTARY INFORMATION  
NOTES TO SUPPLEMENTARY SCHEDULES  
(UNAUDITED)

The information presented in the supplementary schedules was determined as part of the actuarial valuation at the date indicated. Additional information as of the latest actuarial valuation date follows:

Actuarial valuation date	January 1, 2017
Actuarial cost method	Entry age normal
Amortization method	Level dollar, closed
Remaining amortization period	6 years
Asset valuation method	Plan assets are valued using the method describe in Section 210 of Act 205, as amended, subject to a ceiling of 120% of the market value of assets.
Actuarial assumptions:	
Investment rate of return	7.75%
Projected salary increases	4.00%

CITY OF MCKEESPORT FIREFIGHTERS PENSION PLAN  
REPORT DISTRIBUTION LIST

**The Honorable Tom W. Wolf**  
Governor  
Commonwealth of Pennsylvania

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City Clerk

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CITY OF MCKEESPORT FIREFIGHTERS PENSION PLAN  
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