

# COMPLIANCE AUDIT

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## Forest Hills Borough Police Pension Plan Allegheny County, Pennsylvania For the Period January 1, 2015 to December 31, 2016

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July 2017



Commonwealth of Pennsylvania  
Department of the Auditor General

Eugene A. DePasquale • Auditor General



**Commonwealth of Pennsylvania  
Department of the Auditor General  
Harrisburg, PA 17120-0018  
Facebook: Pennsylvania Auditor General  
Twitter: @PAAuditorGen  
www.PaAuditor.gov**

**EUGENE A. DePASQUALE  
AUDITOR GENERAL**

The Honorable Mayor and Borough Council  
Forest Hills Borough  
Allegheny County  
Pittsburgh, PA 15221

We have conducted a compliance audit of the Forest Hills Borough Police 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 conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our 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 the plan member who retired subsequent to the 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 individual and comparing this amount to supporting documentation evidencing the amount determined and actually paid to the recipient.
- 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.

Forest Hills Borough contracted with an independent certified public accounting firm for annual audits of its basic financial statements which are available at the borough's offices. Those financial statements were not audited by us and, accordingly, we express no opinion or other form of assurance on them.

Borough officials are responsible for establishing and maintaining effective internal controls to provide reasonable assurance that the Forest Hills Borough 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 borough's internal controls as they relate to the borough'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 Forest Hills Borough Police 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 Forest Hills Borough and, where appropriate, their responses have been included in the report. We would like to thank borough officials for the cooperation extended to us during the conduct of the audit.

July 11, 2017

A handwritten signature in black ink, appearing to read "Eugene A. DePasquale", with a long, sweeping horizontal line extending to the right.

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 Forest Hills Borough Police 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 600 - Police Pension Fund Act, Act of May 29, 1956 (P.L. 1804, No. 600), as amended, 53 P.S. § 767 et seq.

The Forest Hills Borough Police Pension Plan is a single-employer defined benefit pension plan locally controlled by the provisions of Ordinance No. 974, as amended, adopted pursuant to Act 600. The plan is also affected by the provisions of collective bargaining agreements between the borough and its police officers. The plan was established January 1, 1958. Active members are required to contribute 5 percent of compensation to the plan. As of December 31, 2016, the plan had 9 active members, no terminated members eligible for vested benefits in the future, and 11 retirees receiving pension benefits from the plan.

## **BACKGROUND – (Continued)**

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

### Eligibility Requirements:

Normal Retirement	Age 50 and 25 years of service.
Early Retirement	None
Vesting	A member is 100% vested after 12 years of service.

### Retirement Benefit:

Benefit equals 50% of final 36 months average salary, plus a service increment of \$100 per month for completion of 26 or more years of service.

### Survivor Benefit:

Before Retirement Eligibility	Refund of member contributions plus interest.
After Retirement Eligibility	A monthly benefit equal to 50% of the pension the member was receiving or was entitled to receive on the day of the member's death.

### Service Related Disability Benefit:

The greater of (a) 100% of final monthly average salary at the time the disability was incurred, payable until normal retirement date, after which the benefit is reduced to 50% of final monthly average salary or (b) 50% of the member's salary at the time the disability was incurred, offset by Social Security disability benefits received for the same injury.

FOREST HILLS BOROUGH POLICE PENSION PLAN  
STATUS OF PRIOR FINDING

Status Of Prior Audit Recommendation

· Failure To Implement Act 44 Mandatory Distressed Provisions

The borough received a notification from the former Public Employee Retirement Commission indicating that based on the aggregate funding level of the borough's pension plans as of January 1, 2015, the borough is currently in Level 1 minimal distress status; therefore, the mandatory Level 2 moderate distress remedies are no longer required.



FOREST HILLS BOROUGH POLICE PENSION PLAN  
SUPPLEMENTARY INFORMATION  
(UNAUDITED)

The supplementary information contained on Pages 4 through 6 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, 2015 AND 2016

	<u>2015</u>	<u>2016</u>
Total Pension Liability		
Service cost	\$ 122,748	\$ 128,579
Interest	573,931	595,163
Difference between expected and actual experience	(130,201)	-
Benefit payments, including refunds of member contributions	(419,102)	(419,715)
Net Change in Total Pension Liability	147,376	304,027
Total Pension Liability - Beginning	7,865,627	8,013,003
Total Pension Liability - Ending (a)	<u>\$ 8,013,003</u>	<u>\$ 8,317,030</u>
Plan Fiduciary Net Position		
Contributions - employer*	\$ 355,733	\$ 332,739
Contribution - member	48,724	42,181
Net investment income	(30,725)	368,810
Benefit payments, including refunds of member contributions	(419,102)	(419,715)
Administrative expense	(47,652)	(31,882)
Other	-	(31,206)
Net Change in Plan Fiduciary Net Position	(93,022)	260,927
Plan Fiduciary Net Position - Beginning	6,153,258	6,060,236
Plan Fiduciary Net Position - Ending (b)	<u>\$ 6,060,236</u>	<u>\$ 6,321,163</u>
Net Pension Liability - Ending (a-b)	<u>\$ 1,952,767</u>	<u>\$ 1,995,867</u>
Plan Fiduciary Net Position as a Percentage of the Total Pension Liability	75.6%	76.0%
Estimated Covered Employee Payroll	\$ 803,415	\$ 843,612
Net Pension Liability as a Percentage of Covered Employee Payroll	243.1%	236.6%

\* 2016 Employer contributions includes a funding deficiency in the amount of \$534 plus interest paid in 2017.

FOREST HILLS BOROUGH POLICE 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 borough as of December 31, 2015 and 2016, calculated using the discount rate of 7.5%, as well as what the borough'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 (6.5%)	Current Discount Rate (7.5%)	1% Increase (8.5%)
Net Pension Liability - 12/31/15	\$ 2,893,639	\$ 1,952,767	\$ 1,167,155
Net Pension Liability - 12/31/16	\$ 2,952,681	\$ 1,995,867	\$ 1,195,992

FOREST HILLS BOROUGH POLICE 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
2007	\$ 40,946	\$ 40,946	\$ -		
2008	90,706	90,706	-		
2009	89,898	89,898	-		
2010	84,368	84,368	-	\$ 895,881	9.4%
2011	183,690	183,690	-		
2012	194,209	194,209	-	805,051	24.1%
2013	268,617	268,617	-		
2014	265,625	265,625	-	861,056	30.8%
2015	436,200	355,733	80,467	803,415	44.3%
2016	409,897	332,164	77,733	843,612	39.4%

\* Due to GASB Statement No. 67, *Financial Reporting for Pension Plans*, being implemented only recently, the amount of Covered-Employee Payroll was not provided for any years prior to 2010 nor any odd years prior to 2015.

For 2015 and 2016, the contribution deficiency reflects the 25 percent reduction to the plan's amortization contribution elected by the municipality under Act 44 for distressed municipalities which allows for such reduction.

SCHEDULE OF INVESTMENT RETURNS

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

2016	6.21%
2015	(0.51%)
2014	9.80%

FOREST HILLS BOROUGH 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, 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	\$ 5,069,490	\$ 6,352,695	\$ 1,283,205	79.8%
01-01-13	4,762,498	7,327,523	2,565,025	65.0%
01-01-15	5,632,457	7,735,426	2,102,969	72.8%

Note: The market values of the plan's assets at 01-01-11, 01-01-13, and 01-01-15 have been adjusted to reflect the smoothing of gains and/or losses over a 5-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.

FOREST HILLS BOROUGH 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.

FOREST HILLS BOROUGH POLICE 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, closed
Remaining amortization period	9 years
Asset valuation method	Fair value, 5-year smoothing
Actuarial assumptions:	
Investment rate of return	7.5%
Projected salary increases *	4.75%

\* Includes inflation at 3.0%

FOREST HILLS BOROUGH POLICE PENSION PLAN  
REPORT DISTRIBUTION LIST

This report was initially distributed to the following:

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