

# COMPLIANCE AUDIT

---

## Mercersburg Borough Non-Uniformed Pension Plan Franklin County, Pennsylvania For the Period January 1, 2012 to December 31, 2015

---

October 2016



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  
Mercersburg Borough  
Franklin County  
Mercersburg, PA 17236

We have conducted a compliance audit of the Mercersburg Borough Non-Uniformed Pension Plan for the period January 1, 2012 to December 31, 2015. 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 findings 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 findings 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 that there were no employee contributions required by the plan's governing document and applicable laws and regulations for the years covered by our audit period.
- 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 benefit due to the retired individual and comparing this amount to supporting documentation evidencing the amount determined and actually paid to the recipient. We also determined whether retirement benefits calculated for the plan member who elected to vest during the current audit period represent payments to all (and only) those entitled to receive them and were properly determined in accordance with the plan's governing document, applicable laws and regulations by recalculating the amount of the pension benefit due to the retired individual and comparing this amount to supporting documentation evidencing the amount determined.
- We determined whether the January 1, 2011, January 1, 2013, and January 1, 2015 actuarial valuation reports were prepared and submitted to the Public Employee Retirement Commission (PERC) by March 31, 2012, 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 plan's unallocated insurance contract, including ownership and any restrictions, were in compliance with plan provisions, investment policies, and state regulations by comparing the terms of the contract with the plan's provisions, investment policies, and state regulations.

Mercersburg 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 Mercersburg Borough Non-Uniformed 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 Mercersburg Borough Non-Uniformed 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 Mercersburg 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.

October 18, 2016



EUGENE A. DEPASQUALE  
Auditor General

## CONTENTS

	<u>Page</u>
Background.....	1
Status of Prior Findings .....	3
Supplementary Information .....	4
Report Distribution List .....	10

## **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 Mercersburg Borough Non-Uniformed 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.

The Mercersburg Borough Non-Uniformed Pension Plan is a single-employer defined benefit pension plan locally controlled by the provisions of Ordinance No. 5-8. The plan was established January 1, 1986. Active members are not required to contribute to the plan. As of December 31, 2015, the plan had 7 active members, 5 terminated members eligible for vested benefits in the future, and 3 retirees receiving pension benefits from the plan.

## **BACKGROUND – (Continued)**

As of December 31, 2015, selected plan benefit provisions are as follows:

### Eligibility Requirements:

Normal Retirement	Attained age 62
Early Retirement	Attained age 55 with 10 years of vesting service
Vesting	20% after 3 years of service plus 20% per year for each year thereafter up to 100%

### Retirement Benefit:

1.75% of average compensation times accrual service (maximum 35 years). Average Compensation is the monthly average of compensation received for the 5 consecutive years out of the 10 latest years prior to retirement which gives the highest average, excluding overtime.

### Survivor Benefit:

The greater of, the transfer value (from previous defined contribution plan), or the vested accrued benefit payable as a 50% joint and survivor annuity to the spouse of a married participant deferred until the participant's earliest retirement age.

### Disability Benefit:

None

MERCERSBURG BOROUGH NON-UNIFORMED PENSION PLAN  
STATUS OF PRIOR FINDINGS

Compliance With Prior Audit Recommendations

Mercersburg Borough has complied with the prior audit recommendations concerning the following:

· Restated Plan Document Not Adopted By Ordinance Or Resolution

The borough formally adopted the restated plan document through Ordinance No. 5-8.

· Failure To Appoint A Chief Administrative Officer

The borough adopted Resolution No. 09-15 which appointed a new Chief Administrative Officer for the pension plan.



MERCERSBURG BOROUGH NON-UNIFORMED 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, 2014 AND 2015

	<u>2014</u>	<u>2015</u>
Total Pension Liability		
Service cost	\$ 23,597	\$ 22,632
Interest	44,134	47,275
Difference between expected and actual experience	-	(79,501)
Changes of assumptions	-	34,696
Benefit payments, including refunds of member contributions	(24,100)	(15,389)
Net Change in Total Pension Liability	<u>43,631</u>	<u>9,713</u>
Total Pension Liability - Beginning	<u>642,291</u>	<u>685,922</u>
Total Pension Liability - Ending (a)	<u><u>\$ 685,922</u></u>	<u><u>\$ 695,635</u></u>
Plan Fiduciary Net Position		
Contributions – employer *	\$ 58,706	\$ 55,747
Net investment income	40,131	(9,539)
Benefit payments, including refunds of member contributions	(24,100)	(15,389)
Administrative expense	(5,375)	(7,250)
Other	-	781
Net Change in Plan Fiduciary Net Position	<u>69,362</u>	<u>24,350</u>
Plan Fiduciary Net Position - Beginning	<u>517,713</u>	<u>587,075</u>
Plan Fiduciary Net Position - Ending (b)	<u><u>\$ 587,075</u></u>	<u><u>\$ 611,425</u></u>
Net Pension Liability - Ending (a-b)	<u><u>\$ 98,847</u></u>	<u><u>\$ 84,210</u></u>
Plan Fiduciary Net Position as a Percentage of the Total Pension Liability	85.59%	87.89%
Estimated Covered Employee Payroll	\$ 259,094	\$ 272,117
Net Pension Liability as a Percentage of Covered Employee Payroll	38.15%	30.95%

\* The 2014 Employer Contributions reflect a receivable for the 2014 minimum municipal obligation (MMO) plus interest for late payment.

MERCERSBURG BOROUGH NON-UNIFORMED 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, calculated using the discount rate of 6.25%, 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 (5.25%)	Current Discount Rate (6.25%)	1% Increase (7.25%)
Net Pension Liability	\$ 177,313	\$ 84,210	\$ 6,175

The discount rate of 6.25% was used in the preparation of the borough's December 31, 2015 GASB 67 report. This rate differs from the 6.75% reported in the Notes to Supplementary Schedules on page 9 of this report.

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
2006	\$ 41,746	\$ 44,341	\$ (2,595)	\$ 193,386	22.93%
2007	44,341	44,341	-	213,154	20.80%
2008	43,550	43,550	-	209,655	20.77%
2009	44,952	44,952	-	224,556	20.02%
2010	50,249	50,448	(199)	233,721	21.58%
2011	51,327	51,835	(508)	245,643	21.10%
2012	48,786	48,786	-	254,502	19.17%
2013	49,523	49,523	-	262,137	18.89%
2014	54,994	-	54,994	259,094	0.0%
2015	55,747	115,234	(59,487)	266,867	43.18%

Note: The 2014 MMO was paid in 2015 including interest for the late payment.

MERCERSBURG BOROUGH NON-UNIFORMED PENSION PLAN  
SUPPLEMENTARY INFORMATION  
(UNAUDITED)

SCHEDULE OF INVESTMENT RETURNS

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

2015	(1.64%)
2014	8.10%

MERCERSBURG BOROUGH NON-UNIFORMED 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	\$ 349,793	\$ 496,956	\$ 147,163	70.4%
01-01-13	424,536	603,180	178,644	70.4%
01-01-15	561,678	639,505	77,827	87.8%

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 subject to a corridor between 80 to 120 percent of market value. 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.

MERCERSBURG BOROUGH NON-UNIFORMED 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.

MERCERSBURG BOROUGH NON-UNIFORMED 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	5 years
Asset valuation method	5-year smoothing, subject to a corridor between 80-120% of market value
Actuarial assumptions:	
Investment rate of return	6.75%
Projected salary increases	4.0%
Cost-of-living adjustments	None assumed

MERCERSBURG BOROUGH NON-UNIFORMED PENSION PLAN  
REPORT DISTRIBUTION LIST

This report was initially distributed to the following:

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

**The Honorable Roger Defibaugh**  
Mayor

**Mr. Thomas Suddeth**  
Council President

**Mr. Jeff Main**  
Council Vice-President

**Ms. Lisa McCoy**  
Council Member

**Ms. Amy Burkot**  
Council Member

**Mr. Jonathan Kittredge**  
Council Member

**Mr. Donald Stoner**  
Council Member

**Ms. Dawn Scheller**  
Borough Manager

**Ms. Catalin Bonciu**  
Borough Treasurer

This report is a matter of public record and is available online at [www.PaAuditor.gov](http://www.PaAuditor.gov). Media questions about the report can be directed to the Pennsylvania Department of the Auditor General, Office of Communications, 229 Finance Building, Harrisburg, PA 17120; via email to: [news@PaAuditor.gov](mailto:news@PaAuditor.gov).