

# COMPLIANCE AUDIT

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## Municipality of Kingston Non-Uniformed Employees Pension Plan Luzerne County, Pennsylvania For the Period January 1, 2015 to December 31, 2016

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January 2018



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 Municipal Council  
Municipality of Kingston  
Luzerne County  
Kingston, PA 18704

We have conducted a compliance audit of the Municipality of Kingston Non-Uniformed Employees 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 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 2 plan members who retired during the current 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 retired individuals and comparing these amounts to supporting documentation evidencing amounts determined and actually paid to recipients.
- 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.
- 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 for pension obligation bonds issued during the current audit period.

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

Municipal officials are responsible for establishing and maintaining effective internal controls to provide reasonable assurance that the Municipality of Kingston Non-Uniformed Employees 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 municipality's internal controls as they relate to the municipality'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 Municipality of Kingston Non-Uniformed Employees Pension Plan was administered in compliance with applicable state laws, regulations, contracts, administrative procedures, and local ordinances and policies.

As previously noted, the objective of our audit of the Municipality of Kingston Non-Uniformed Employees 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. **The plan's funded ratio went from 71.4% as of January 1, 2011, to a ratio of 64.4% as of January 1, 2015**, which is the most recent data available. Based on this information, **the former Public Employee Retirement Commission issued a notification that the municipality is currently in Level II moderate distress status**. We encourage municipal officials to monitor the funding of the non-uniformed employees pension plan to ensure its long-term financial stability.

The contents of this report were discussed with officials of the Municipality of Kingston and, where appropriate, their responses have been included in the report. We would like to thank municipal officials for the cooperation extended to us during the conduct of the audit.



EUGENE A. DEPASQUALE  
Auditor General

January 3, 2018

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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 Municipality of Kingston Non-Uniformed Employees 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 177 - General Local Government Code, Act of December 19, 1996 (P.L. 1158, No. 177), as amended, 53 Pa.C.S. § 101 et seq.

The Municipality of Kingston Non-Uniformed Employees Pension Plan is a single-employer defined benefit pension plan locally controlled by the provisions of an ordinance dated March 14, 1988, as amended. The plan was established March 3, 1972. Active members are required to contribute 5 percent of compensation to the plan. As of December 31, 2016, the plan had 29 active members, 1 terminated member eligible for vested benefits in the future, and 29 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 55; Municipal Administrator – Age 60
Early Retirement	Voluntary – 22 years of service; Involuntary – 8 years of service
Vesting	Member is 100% vested after 8 years of service

**Retirement Benefit:**

Benefit equals 2.0% of final average salary based on last 3 years of employment times years of service up to 25 years.

**Survivor Benefit:**

If a member is eligible for retirement, a death benefit is payable according to the election filed by the member.

**Service Related Disability Benefit:**

Benefit equals 80% of final average salary, reduced by Workers' Compensation benefits received by the member.

**Non-Service Related Disability Benefit:**

After ten or more years of service, the benefit is equal to 50% of final average salary, reduced by Workers' Compensation benefits received by the member.

**MUNICIPALITY OF KINGSTON NON-UNIFORMED EMPLOYEES 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, 2015 AND 2016

	<u>2015</u>	<u>2016</u>
Total Pension Liability		
Service cost	\$ 153,590	\$ 161,270
Interest	428,039	446,706
Difference between expected and actual experience	(305,176)	-
Benefit payments, including refunds of member contributions	(340,703)	(356,166)
Net Change in Total Pension Liability	(64,250)	251,810
Total Pension Liability - Beginning	5,845,016	5,780,766
Total Pension Liability - Ending (a)	<u>\$ 5,780,766</u>	<u>\$ 6,032,576</u>
Plan Fiduciary Net Position		
Contributions - employer	\$ 289,991	\$ 2,148,228
Contribution - member	64,822	68,192
Net investment income	(103,510)	126,632
Benefit payments, including refunds of member contributions	(340,703)	(356,166)
Administrative expense	-	(10,550)
Net Change in Plan Fiduciary Net Position	(89,400)	1,976,336
Plan Fiduciary Net Position - Beginning	2,974,773	2,885,373
Plan Fiduciary Net Position - Ending (b)	<u>\$ 2,885,373</u>	<u>\$ 4,861,709</u>
Net Pension Liability - Ending (a-b)	<u>\$ 2,895,393</u>	<u>\$ 1,170,867</u>
Plan Fiduciary Net Position as a Percentage of the Total Pension Liability	50.0%	80.6%
Estimated Covered Employee Payroll	\$ 1,261,354	\$ 1,390,868
Net Pension Liability as a Percentage of Covered Employee Payroll	229.5%	84.2%

MUNICIPALITY OF KINGSTON NON-UNIFORMED EMPLOYEES 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 municipality as of December 31, 2015 and 2016, calculated using the discount rate of 7.75%, as well as what the municipality'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 (6.75%)	Current Discount Rate (7.75%)	1% Increase (8.75%)
Net Pension Liability - 12/31/15	\$ 3,464,424	\$ 2,895,393	\$ 2,406,412
Net Pension Liability - 12/31/16	\$ 1,759,960	\$ 1,170,867	\$ 667,400

**MUNICIPALITY OF KINGSTON NON-UNIFORMED EMPLOYEES 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	\$ 61,556	\$ 61,556	\$ -		
2008	44,258	44,258	-		
2009	56,927	56,927	-		
2010	49,231	52,296	(3,065)		
2011	110,114	138,868	(28,754)		
2012	101,488	101,488	-		
2013	238,076	238,076	-		
2014	240,115	240,115	-	\$1,248,739	19.23%
2015	289,991	289,991	-	1,261,354	22.99%
2016**	287,102	2,148,228	(1,861,126)	1,390,868	154.45%

\* 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 years prior to 2014.

\*\* 2016 actual contributions include bond proceeds of \$1,970,113.

MUNICIPALITY OF KINGSTON NON-UNIFORMED EMPLOYEES 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) Actuarial Valuation Date	(2) Actuarial Value of Assets (a)	(2) Actuarial Accrued Liability (AAL) - Entry Age (b)	(3) Unfunded (Assets in Excess of) Actuarial Accrued Liability (b) - (a)	(4) Funded Ratio (a)/(b)
01-01-11	\$ 3,643,679	\$ 5,100,880	\$ 1,457,201	71.4%
01-01-13	3,348,182	5,394,348	2,046,166	62.1%
01-01-15	3,569,727	5,539,840	1,970,113	64.4%

Note: The market value of the plan's assets at 01-01-11 have been adjusted to reflect the smoothing of gains and/or losses subject to a corridor between 70 to 130 percent of the market value of assets. The market values of the plan's assets at 01-01-13 and 01-01-15 have been adjusted to reflect the smoothing of gains and/or losses subject to a corridor between 80 to 120 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.

MUNICIPALITY OF KINGSTON NON-UNIFORMED EMPLOYEES 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.

MUNICIPALITY OF KINGSTON NON-UNIFORMED EMPLOYEES 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	13 years
Asset valuation method	Plan assets are valued using the method described in Section 210 of Act 205, as amended, subject to a corridor between 80-120% of the market value of assets.
Actuarial assumptions:	
Investment rate of return	7.75%
Projected salary increases	5.0%

MUNICIPALITY OF KINGSTON NON-UNIFORMED EMPLOYEES PENSION PLAN  
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