SEWICKLEY BOROUGH POLICE PENSION PLAN

ALLEGHENY COUNTY

COMPLIANCE AUDIT REPORT

FOR THE PERIOD

JANUARY 1, 2008, TO DECEMBER 31, 2010

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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.

Pension plan aid is provided from a 2 percent foreign casualty insurance premium tax, a portion of the foreign 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 Sewickley Borough Police 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 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. § 761 et seq.

The Sewickley Borough Police Pension Plan is a single-employer defined benefit pension plan locally controlled by the provisions of Ordinance No. 1072, 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.

JACK WAGNER

AUDITOR GENERAL

The Honorable Mayor and Borough Council
Sewickley Borough
Allegheny County
Sewickley, PA 15143

We have conducted a compliance audit of the Sewickley Borough Police Pension Plan for the period January 1, 2008, to December 31, 2010. The audit was conducted pursuant to authority derived from Section 402(j) of Act 205 and in accordance with *Government Auditing Standards* applicable to performance audits 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 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. Sewickley 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 Sewickley 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 objective, and assessed whether those significant controls were properly designed and implemented. Additionally, we tested transactions, assessed official actions, performed analytical procedures and interviewed selected officials to the extent necessary to satisfy the audit objective.

The results of our tests indicated that, in all significant respects, the Sewickley Borough Police 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 finding further discussed later in this report:

Finding – Pension Benefit Not Authorized By Act 600 And The Plan's Governing Document

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

The contents of this report were discussed with officials of Sewickley Borough and, where appropriate, their responses have been included in the report.

June 27, 2011

JACK WAGNER
Auditor General

SEWICKLEY BOROUGH POLICE PENSION PLAN
FINDING AND RECOMMENDATION

Finding – Pension Benefit Not Authorized By Act 600 And The Plan's Governing Document

Condition: Plan officials provided a pension benefit in excess of what is authorized by Act 600 and the plan's governing document to a police officer who retired on April 5, 2011. Plan officials included accumulated unused sick leave that was not earned during the pension computation period. In addition, plan officials used overtime pay and court pay in the determination of final average salary which is prohibited by the plan's governing document.

Criteria: Section 5(c) of Act 600 states, in part:

> Monthly pension or retirement benefits other than length of service increments shall be computed at one-half the monthly average salary of such member during not more than the last sixty nor less than the last thirty-six months of employment.

Although Act 600 does not define "salary," the department has concluded, based on a line of court opinions, that the term does not encompass lump-sum payments for leave that was not earned during the pension computation period.

Furthermore, Section 1.10(b) of the pension plan's governing document, Ordinance No. 1072, as amended, states:

> "Final Monthly Average Salary" shall mean for Participants who were hired after August 30, 1983 the average monthly salary earned by the Participant and paid by the Employer during the final thirty-six (36) months immediately preceding retirement which are included in the averaging period. The term salary, as used herein, shall include the Employee's regular salary and other forms of compensation which are fixed amounts paid at periodic intervals such as longevity pay, holiday pay and night differential pay, but shall exclude any irregular or extra forms of compensation such as overtime or court pay.

Cause: Plan officials failed to establish adequate internal control procedures to ensure that the retirement benefit was determined in accordance with the provisions contained in Act 600 and the plan's governing document.

Effect: The plan is paying pension benefits to a retiree in excess of those authorized by Act 600 and the plan's governing document. The retiree is receiving excess benefits of $252 per month, or approximately $504 from the retirement date through the date of this audit report.

Finding – (Continued)

Providing unauthorized pension benefits increases the plan's pension costs and reduces the amount of funds available for investment purposes or for the payment of authorized benefits or administrative expenses. In addition, the increased costs to the pension plan as a result of the excess pension benefits could result in the receipt of excess state aid in the future and increase the municipal contributions necessary to fund the plan in accordance with Act 205 funding standards.

Recommendation: We recommend that the pension benefit of the retiree whose benefit was not determined in accordance with the provisions of Act 600 and the plan's governing document be adjusted prospectively. In addition, any excess benefit payments made from the plan will be deemed ineligible for funding with state aid. Accordingly, the pension plan's actuary may be required to determine the impact, if any, of the excess benefit payments on the plan's future state aid allocations and submit this information to the department.

We also recommend that plan officials establish and implement adequate internal control procedures to ensure that future pension benefits are determined and paid in accordance with Act 600 and the applicable provisions contained in the plan's governing document in effect at the time of a plan member's retirement.

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

SEWICKLEY 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, except for distressed pension plans, for which annual reporting was required through January 1, 2003. The historical information, beginning as of January 1, 2005, is as follows:

	(1)	(2)	(3)	(4)	(5)	(6)
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)	Covered Payroll (c)	Unfunded (Assets in Excess of) Actuarial Accrued Liability as a % of Payroll [(b-a)/(c)]
01-01-05	$ 2,259,677	$ 2,203,391	$ (56,286)	102.6%	$ 511,019	(11.0%)
01-01-07	2,809,523	2,596,123	(213,400)	108.2%	553,502	(38.6%)
01-01-09	3,030,980	2,977,795	(53,185)	101.8%	655,685	(8.1%)

Note: The market value of the plan's assets at 01-01-05 has been adjusted to reflect the smoothing of gains and/or losses over a 5-year averaging period. The market value of the plan's assets at 01-01-09 has been adjusted to reflect the smoothing of gains and/or losses over a 4-year averaging period subject to a minimum of 80% and a maximum of 120% of the market value of 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.

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.

Trends in unfunded (assets in excess of) actuarial accrued liability and annual covered payroll are both affected by inflation. Expressing the unfunded (assets in excess of) actuarial accrued liability as a percentage of annual covered payroll (Column 6) approximately adjusts for the effects of inflation and aids analysis of the plan's progress made in accumulating sufficient assets to pay benefits when due. Generally, where there is an unfunded actuarial accrued liability, the smaller this percentage, the stronger the plan. However, when assets are in excess of the actuarial accrued liability, the higher the bracketed percentage, the stronger the plan.

SEWICKLEY BOROUGH POLICE PENSION PLAN
SUPPLEMENTARY INFORMATION
(UNAUDITED)

SCHEDULE OF CONTRIBUTIONS FROM EMPLOYER
AND OTHER CONTRIBUTING ENTITIES

Year Ended December 31	Annual Required Contribution	Percentage Contributed
2005	$ 69,198	100.0%
2006	86,023	100.0%
2007	92,555	100.0%
2008	66,644	100.0%
2009	91,486	100.4%
2010	121,242	100.0%

SEWICKLEY BOROUGH POLICE PENSION PLAN
SUPPLEMENTARY INFORMATION
NOTES TO SUPPLEMENTARY SCHEDULES
(UNAUDITED)

The information presented in the required 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, 2009
Actuarial cost method	Entry age normal
Amortization method	N/A
Remaining amortization period	N/A
Asset valuation method	Market value, 4-year smoothing
Actuarial assumptions:	
Investment rate of return	7.0%
Projected salary increases	5.0%

SEWICKLEY BOROUGH POLICE PENSION PLAN
REPORT DISTRIBUTION LIST

This report was initially distributed to the following:

The Honorable Tom Corbett
Governor
Commonwealth of Pennsylvania

Sewickley Borough Police Pension Plan
Allegheny County
601 Thorn Street
Sewickley, PA 15143

The Honorable Brian F. Jeffe	Mayor
Mr. Robert G. Hague	Council President
Mr. Kevin M. Flannery	Borough Manager

This report is a matter of public record. Copies of this report may be obtained from the Pennsylvania Department of the Auditor General, Office of Communications, Room 318 Finance Building, Harrisburg, PA 17120. If you have any questions regarding this report or any other matter, you may contact the Department of the Auditor General by accessing our website at www.auditorgen.state.pa.us.