

COMPLIANCE AUDIT

City of Shamokin Officers' and Employees' Pension Plan Northumberland County, Pennsylvania For the Period January 1, 2015 to December 31, 2016

January 2018



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 City Council
City of Shamokin
Northumberland County
Shamokin, PA 17872

We have conducted a compliance audit of the City of Shamokin Officers' and 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 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 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.

City officials are responsible for establishing and maintaining effective internal controls to provide reasonable assurance that the City of Shamokin Officers' and 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 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 Shamokin Officers' and 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 City of Shamokin Officers' and 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 100.3% as of January 1, 2011, to a ratio of 51.1% as of January 1, 2015, which is the most recent data available. Based on this information and the funded status of the city's police pension plan, the former Public Employee Retirement Commission issued a notification that the city is currently in Level II moderate distress status.** We encourage city officials to monitor the funding of the officers' and employees' pension plan to ensure its long-term financial stability.

The contents of this report were discussed with officials of the City of Shamokin 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.

January 12, 2018



EUGENE A. DEPASQUALE
Auditor General

CONTENTS

	<u>Page</u>
Background.....	1
Supplementary Information	3
Report Distribution List	9

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 Shamokin Officers' and 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 362 - The Third Class City Code, Act of May 23, 1945 (P.L. 903, No. 362), Article XLIII-A, Optional Retirement System for Officers and Employees, as amended, 53 P.S. § 39371 et seq.

The City of Shamokin Officers' and Employees' Pension Plan is a single-employer defined benefit pension plan locally controlled by the provisions of Chapter 25 of the city code, adopted by Ordinance No. 02-02, pursuant to Act 362. The plan is also affected by the provisions of collective bargaining agreements between the city and its non-uniformed employees. The plan was established November 1, 1969. Active members are required to contribute 4.5 percent of compensation to the plan. As of December 31, 2016, the plan had 11 active members, 1 terminated member eligible for vested benefits in the future, and 12 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 60 and 20 years of service.
Early Retirement	None
Vesting	A member is 100% vested after 12 years of service.

Retirement Benefit:

Benefit equals 50% of the highest average yearly salary earned during any 5 years of service or the rate of monthly pay at the time of retirement, whichever is higher.

Survivor Benefit:

Before Retirement Eligibility	Refund of member contributions without 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.

Disability Benefit:

If under age 55 and 15 years of service, the benefit is based on the normal retirement formula.

CITY OF SHAMOKIN OFFICERS' AND EMPLOYEES' PENSION PLAN
SUPPLEMENTARY INFORMATION
(UNAUDITED)

The supplementary information contained on Pages 3 and 4 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	\$ 53,884	\$ 56,309
Interest	71,994	75,226
Difference between expected and actual experience	161,375	-
Changes of assumptions	71,407	-
Benefit payments, including refunds of member contributions	(79,919)	(84,353)
Net Change in Total Pension Liability	<u>278,741</u>	<u>47,182</u>
Total Pension Liability - Beginning	781,782	1,060,523
Total Pension Liability - Ending (a)	<u><u>\$ 1,060,523</u></u>	<u><u>\$ 1,107,705</u></u>
Plan Fiduciary Net Position		
Contributions – employer	\$ 28,923	\$ 30,171
Contributions – state aid	39,208	43,746
Contribution – member	21,136	22,183
Net investment income	(15,135)	24,863
Benefit payments, including refunds of member contributions	(79,919)	(84,353)
Net Change in Plan Fiduciary Net Position	<u>(5,787)</u>	<u>36,610</u>
Plan Fiduciary Net Position - Beginning	518,607	512,820
Plan Fiduciary Net Position - Ending (b)	<u><u>\$ 512,820</u></u>	<u><u>\$ 549,430</u></u>
Net Pension Liability - Ending (a-b)	<u><u>\$ 547,703</u></u>	<u><u>\$ 558,275</u></u>
Plan Fiduciary Net Position as a Percentage of the Total Pension Liability	48.36%	49.60%
Estimated Covered Employee Payroll	\$ 430,114	\$ 500,583
Net Pension Liability as a Percentage of Covered Employee Payroll	127.34%	111.52%

CITY OF SHAMOKIN OFFICERS' AND 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 city as of December 31, 2015 and 2016, calculated using the discount rate of 7.0%, 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:

	1% Decrease (6.0%)	Current Discount Rate (7.0%)	1% Increase (8.0%)
Net Pension Liability - 12/31/15	\$ 642,087	\$ 547,703	\$ 465,661
Net Pension Liability - 12/31/16	\$ 658,786	\$ 558,275	\$ 471,058

SCHEDULE OF INVESTMENT RETURNS

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

2016	5.12%
2015	-3.10%

CITY OF SHAMOKIN OFFICERS' AND 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)	(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	\$ 676,068	\$ 673,728	\$ (2,340)	100.3%
01-01-13	560,908	782,299	221,391	71.7%
01-01-15	518,607	1,014,564	495,957	51.1%

Note: The market values of the plan's assets at 01-01-11 and 01-01-13 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.

CITY OF SHAMOKIN OFFICERS' AND EMPLOYEES' PENSION PLAN
SUPPLEMENTARY INFORMATION
(UNAUDITED)

The Actuarial Accrued Liability went from \$673,728 as of 01-01-11 to \$1,014,564 as of 01-01-15 for the following reasons:

- 1) Demographic liability loss of \$98,306 during the period 01-01-11 to 12-31-12
- 2) Demographic liability loss of \$161,376 during the period 01-01-13 to 12-31-14
- 3) Change in interest rate assumption as of 01-01-15 from 8% to 7% resulting in added liability of \$71,407

The market value of assets decreased from \$676,068 as of 01-01-11 to \$518,607 as of 01-01-15 primarily due to an asset loss of \$136,324 during the period 01-01-11 to 12-31-12.

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 SHAMOKIN OFFICERS' AND EMPLOYEES' PENSION PLAN
SUPPLEMENTARY INFORMATION
(UNAUDITED)

SCHEDULE OF CONTRIBUTIONS FROM EMPLOYER
AND OTHER CONTRIBUTING ENTITIES

Year Ended December 31	Annual Required Contribution	Percentage Contributed
2011	\$ 9,371	173.9%
2012	10,416	100.0%
2013	12,992	100.0%
2014	13,193	111.5%
2015	68,131	100.0%
2016	73,917	100.0%

CITY OF SHAMOKIN OFFICERS' AND 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	12 years
Asset valuation method	Fair value
Actuarial assumptions:	
Investment rate of return	7.0%
Projected salary increases	4.5%

CITY OF SHAMOKIN OFFICERS' AND EMPLOYEES' PENSION PLAN
REPORT DISTRIBUTION LIST

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