

COMPLIANCE AUDIT

City of Sharon Police Pension Plan Mercer County, Pennsylvania For the Period January 1, 2017 to December 31, 2018

January 2020



Commonwealth of Pennsylvania
Department of the Auditor General
Eugene A. DePasquale • Auditor General



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City Council
City of Sharon
Mercer County
Sharon, PA 16146

We have conducted a compliance audit of the City of Sharon Police Pension Plan for the period January 1, 2017 to December 31, 2018. 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 all seven of the plan members who retired during the current audit period, and through 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 also determined whether retirement benefits calculated for the lone 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 benefits due to the retired individual and comparing these amounts to supporting documentation evidencing amounts determined.
- We determined whether the January 1, 2015 and January 1, 2017 actuarial valuation reports were prepared and submitted by March 31, 2016 and 2018, 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 all annual special ad hoc postretirement reimbursements received by the municipality were authorized and appropriately deposited in accordance with Act 147 by tracing information to supporting documentation maintained by plan officials.

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

City officials are responsible for establishing and maintaining effective internal controls to provide reasonable assurance that the City of Sharon 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 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 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 City of Sharon 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 City of Sharon 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.

November 6, 2019



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 City of Sharon 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 147 - Special Ad Hoc Municipal Police and Firefighter Postretirement Adjustment Act, Act of December 14, 1988 (P.L. 1192, No. 147), as amended, 53 P.S. § 896.101 et seq.
- 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.
- Act 67 - The Third Class City Code, Act of November 24, 2015 (P.L. 242, No. 67), as amended, 11 Pa. C.S. § 10101 et seq.

The City of Sharon Police Pension Plan is a single-employer defined benefit pension plan locally controlled by the provisions of Chapters 286 and 287 of the city's codified ordinances. The plan is also affected by the provisions of collective bargaining agreements between the city and its police officers. The plan was established April 12, 1967. Active members are required to contribute 4 percent of base and longevity pay, plus 1 percent for survivor benefits, plus \$3 per month to the plan. As of December 31, 2018, the plan had 29 active members, 1 terminated members eligible for vested benefits in the future, and 35 retirees receiving pension benefits.

BACKGROUND – (Continued)

As of December 31, 2018, selected plan benefit provisions are as follows:

Eligibility Requirements:

Normal Retirement	Age 50 and 20 years of service.
Early Retirement	None
Vesting	100% vesting available after 10 years of service. If hired on or after January 1, 2008, 100% vesting available after 12 years of service.

Retirement Benefit:

Benefit equals 50% of Final Monthly Average Salary plus a service increment equal to 1/40th of the retirement allowance times years of completed service over 20 years (service beyond age 65 is not counted) to a maximum increment of \$300 per month. Final Monthly Average Salary is defined as the greater of (a) the rate of the participant's monthly salary at retirement, death or termination of employment or (b) the sum of salary received during the five highest years prior to retirement, death or termination of employment, divided by 60.

Survivor Benefit:

Before Retirement Eligibility	Any police officer who has less than 10 years of service and who dies not in the line of duty, shall be entitled to 25% of the Final Monthly Average Salary computed as of the time of death. For death after 10 years of service, benefit equals 50% of Final Monthly Average Salary as of the time of death.
After Retirement Eligibility	100% to the surviving spouse during their lifetime. If the surviving spouse dies or already has died, then 50% (100% for disability pensioners) to a child or children of the officer under the age of 18.

BACKGROUND – (Continued)

Disability Benefit:

Service Related	Normal Retirement Benefit including Service Increment. If hired on or after January 1, 2008, the benefit is offset by Workers Compensation payments or Enforcement Officers Disability Benefit Law payments.
Non-Service Related	Benefit equals 25% of Salary at the time of disability for any police officer with less than 10 years of service who is disabled due to injury or illness not in the line of duty. After 10 years of service, an officer shall be entitled to 50% of Salary at the time of disability.

CITY OF SHARON POLICE PENSION PLAN
STATUS OF PRIOR FINDING

Compliance With Prior Audit Recommendation

The City of Sharon has complied with the prior audit recommendation concerning the following:

- Unauthorized Pension Benefit Provision

Municipal officials amended the plan's governing document in accordance with the benefit provisions of the Third Class City Code through the collective bargaining process.

CITY OF SHARON POLICE PENSION PLAN
SUPPLEMENTARY INFORMATION
(UNAUDITED)

The supplementary information contained on Pages 5 through 8 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	\$ 216,992	\$ 232,152
Interest	857,908	917,727
Changes in benefit terms	198,062	-
Changes in assumptions	293,665	-
Difference between expected and actual experience	-	-
Benefit payments, including refunds of member contributions	(735,399)	(774,710)
Net Change in Total Pension Liability	<u>831,228</u>	<u>375,169</u>
Total Pension Liability – Beginning	12,014,568	12,845,796
Total Pension Liability – Ending (a)	<u>\$ 12,845,796</u>	<u>\$ 13,220,965</u>
Plan Fiduciary Net Position		
Contributions – employer	\$ 449,131	\$ 709,590
Contributions – member	63,884	73,758
Net investment income	807,798	(2,811)
Benefit payments, including refunds of member contributions	(735,399)	(774,710)
Administrative expense	(12,078)	(16,437)
Net Change in Plan Fiduciary Net Position	<u>573,336</u>	<u>(10,610)</u>
Plan Fiduciary Net Position – Beginning	9,303,125	9,876,461
Plan Fiduciary Net Position – Ending (b)	<u>\$ 9,876,461</u>	<u>\$ 9,865,851</u>
Net Pension Liability – Ending (a-b)	<u>\$ 2,969,335</u>	<u>\$ 3,355,114</u>
Plan Fiduciary Net Position as a Percentage of the Total Pension Liability	76.88%	74.62%
Estimated Covered Employee Payroll	\$ 1,800,000	\$ 1,840,802
Net Pension Liability as a Percentage of Covered Employee Payroll	164.96%	182.26%

CITY OF SHARON POLICE PENSION PLAN
SUPPLEMENTARY INFORMATION
(UNAUDITED)

SCHEDULE OF CHANGES IN THE NET PENSION
LIABILITY AND RELATED RATIOS
FOR THE YEARS ENDED DECEMBER 31, 2016 AND 2017

	<u>2016</u>	<u>2017</u>
Total Pension Liability		
Service cost	\$ 226,396	\$ 292,989
Interest	945,052	938,101
Changes in assumptions	416,661	-
Differences between expected & actual experience	(15,402)	-
Benefit payments, including refunds of member contributions	(760,918)	(790,080)
Net change in total pension liability	<u>811,789</u>	<u>441,010</u>
Total Pension Liability – Beginning	<u>13,220,965</u>	<u>14,032,754</u>
Total Pension Liability – Ending (a)	<u>\$ 14,032,754</u>	<u>\$ 14,473,764</u>
 Plan Fiduciary Net Position		
Contributions – employer	\$ 687,357	\$ 698,224
Contributions – member	84,261	81,988
Net investment income	784,343	1,325,110
Benefit payments, including refunds of member contributions	(760,918)	(790,080)
Administrative expense	(24,223)	(10,601)
Net Change in Plan Fiduciary Net Position	<u>770,820</u>	<u>1,304,641</u>
Plan Fiduciary Net Position – Beginning	<u>9,865,851</u>	<u>10,636,671</u>
Plan Fiduciary Net Position – Ending (b)	<u>\$ 10,636,671</u>	<u>\$ 11,941,312</u>
Net Pension Liability – Ending (a-b)	<u>\$ 3,396,083</u>	<u>\$ 2,532,452</u>
 Plan Fiduciary Net Position as a Percentage of the Total Pension Liability	 75.80%	 82.50%
 Estimated Covered Employee Payroll	 \$ 1,924,063	 \$ 1,810,525
 Net Pension Liability as a Percentage of Covered Employee Payroll	 176.51%	 139.87%

CITY OF SHARON 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 city as of December 31, 2016 and 2017, calculated using the discount rate of 6.75%, 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 (5.75%)	Current Discount Rate (6.75%)	1% Increase (7.75%)
Net Pension Liability – 12/31/16	\$ 5,185,776	\$ 3,396,083	\$ 1,918,626
Net Pension Liability – 12/31/17	\$ 4,378,054	\$ 2,532,452	\$ 1,008,857

The discount rate used to measure the total pension liability at December 31, 2017 is 6.75%. This rate differs from the 7.25% reported in the Notes to Supplementary Schedules on page 12 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
2009	\$ 271,357	\$ 271,357	\$ -	\$1,463,732	18.54%
2010	238,845	238,845	-	1,469,378	16.25%
2011	390,577	340,929	49,648	1,612,551	21.14%
2012	398,236	348,588	49,648	1,667,397	20.91%
2013	447,617	447,617	-	1,720,856	26.01%
2014	449,131	449,131	-	1,640,835	27.37%
2015	709,590	709,590	-	1,800,000	39.42%
2016	687,357	687,357	-	1,840,802	37.34%
2017	698,224	698,224	-	1,924,063	36.29%
2018	679,947	679,947	-	1,810,525	37.56%

For 2011 and 2012, 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.

CITY OF SHARON POLICE PENSION PLAN
SUPPLEMENTARY INFORMATION
(UNAUDITED)

SCHEDULE OF INVESTMENT RETURNS

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

2018	(4.4%)
2017	12.40%
2016	8.00%
2015	0.00%
2014	8.80%

CITY OF SHARON 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, 2013, 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)
01-01-13	\$ 7,618,125	\$ 11,330,094	\$ 3,711,969	67.2%
01-01-15	9,001,269	12,845,796	3,844,527	70.1%
01-01-17	10,677,945	13,259,751	2,581,806	80.5%

Note: The market values of assets at 01-01-13, 01-01-15, and 01-01-17 have been adjusted to reflect the smoothing of gains and/or losses over a four-year averaging period. These methods will lower contributions in years of less 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 SHARON 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.

CITY OF SHARON 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, 2017
Actuarial cost method	Entry age normal
Amortization method	Level dollar, closed
Remaining amortization period	8 years
Asset valuation method	Fair value, 4-year smoothing
Actuarial assumptions:	
Investment rate of return	7.25%
Projected salary increases *	2.0%
Cost-of-living adjustments	None assumed

* Includes inflation at 2.5%

CITY OF SHARON POLICE PENSION PLAN
REPORT DISTRIBUTION LIST

This report was initially distributed to the following:

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