

COMPLIANCE AUDIT

Dickson City Borough Police Pension Plan Lackawanna County, Pennsylvania For the Period January 1, 2016 to December 31, 2018

March 2020



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 Borough Council
Dickson City Borough
Lackawanna County
Dickson City, PA 18512

We have conducted a compliance audit of the Dickson City Borough Police Pension Plan for the period January 1, 2016 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 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 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 that there were no benefit calculations prepared for the years covered by our audit period.
- 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 provisions of the Deferred Retirement Option Plan (DROP) were in accordance with the provisions of Act 205 by examining provisions stated in the plan's governing documents.

Borough officials are responsible for establishing and maintaining effective internal controls to provide reasonable assurance that the Dickson City 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 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 Dickson City 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 - Incorrect Data On Certification Form AG 385 Resulting In An Overpayment Of State Aid

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 funded status of the plan contained in the schedule of funding progress included in this report, which indicates **the plan's funded ratio is 69.5% as of January 1, 2017**, which is the most recent data available. We encourage borough officials to monitor the funding of the police pension plan to ensure its long-term financial stability.

The contents of this report were discussed with officials of Dickson City 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.

February 4, 2020



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 Dickson City Borough 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 600 - Police Pension Fund Act, Act of May 29, 1956 (P.L. 1804, No. 600), as amended, 53 P.S. § 767 et seq.

The Dickson City Borough Police Pension Plan is a single-employer defined benefit pension plan locally controlled by the provisions of Ordinance No. 2 of 2008, 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. The plan was established December 4, 1959. Active members are required to contribute 2.25 percent of compensation in 2016, 2.50 percent of compensation in 2017, and 3.00 percent of compensation in 2018 to the plan. As of December 31, 2018, the plan had 8 active members, 1 terminated member eligible for vested benefits in the future, and 8 retirees receiving pension benefits from the plan.

BACKGROUND – (Continued)

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

Eligibility Requirements:

Normal Retirement	Age 50 and 25 years of service.
Early Retirement	None
Vesting	A member is 100% after 12 years of service.

Retirement Benefit:

Benefit equals 50% of final 36 months average salary, plus a service increment of \$100 per month for each year of service in excess of 25 years, up to a maximum of \$500 per month after 30 years.

Survivor Benefit:

Before Retirement Eligibility	Refund of member contributions plus 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.

Service Related Disability Benefit:

Police officers hired prior to June 1, 2009, 75% of salary, after June 1, 2009, 50% of salary.

DICKSON CITY BOROUGH POLICE PENSION PLAN
FINDING AND RECOMMENDATION

Finding - Incorrect Data On Certification Form AG 385 Resulting In An Overpayment Of State Aid

Condition: The borough certified an ineligible police officer (2 units) and overstated payroll by \$17,027 on the Certification Form AG 385 filed in 2019. The data contained on this certification form is based on prior calendar year information.

Criteria: Pursuant to Act 205, at Section 402(e)(2), in order to be eligible for certification, an employee must have been employed on a full-time basis for at least six consecutive months and must have been participating in a pension plan during the certification year.

Cause: The municipality believed that they were required to certify the employee on the Certification Form AG 385 filed during 2019 due to an arbitration award on September 10, 2018 which reinstated the employee, who was previously terminated by the borough on September 25, 2017, and granted him back pay to the date of separation.

Effect: The data submitted on this certification form is used, in part, to calculate the state aid due to the municipality for distribution to its pension plans. Because the borough’s state aid allocation was based on unit value, the incorrect certification of pension data affected the borough’s state aid allocation, as identified below:

<u>Year</u>	<u>Units Overstated</u>	<u>Unit Value</u>	<u>State Aid Overpayment</u>
2019	2	\$ 5,120.50	\$ 10,241

In addition, the borough used the overpayment of state aid to pay the minimum municipal obligation (MMO) due to the police pension plan; therefore, if the reimbursement to the Commonwealth is made from the pension plan, the plan’s MMO will not be fully paid.

Furthermore, the borough’s future state aid allocations may be withheld until the finding recommendation is complied with.

Recommendation: We recommend that the total excess state aid, in the amount of \$10,241, plus interest, be returned to the Commonwealth. A check in this amount, with interest compounded annually from date of receipt to date of repayment, at a rate earned by the pension plan, should be made payable to: Commonwealth of Pennsylvania and mailed to: Department of the Auditor General, Municipal Pension & Fire Relief Programs Unit, 321 Finance Building, Harrisburg, PA 17120. A copy of the interest calculation must be submitted along with the check.

DICKSON CITY BOROUGH POLICE PENSION PLAN
FINDING AND RECOMMENDATION

Finding - (Continued)

We also recommend that in the future, plan officials establish adequate internal control procedures, such as having at least two people review the data certified, to ensure compliance with the instructions that accompany Certification Form AG 385 to assist them in accurately reporting the required pension data.

Furthermore, if the reimbursement to the Commonwealth is made from police pension plan funds, we recommend that any resulting MMO deficiency be paid to the pension plan with interest, at a rate earned by the pension plan.

Management's Response: Borough officials disagreed with the finding as presented and provided a response from the plan consultant, which is included in its entirety as follows:

The officer in question was terminated in September 2017 and then reinstated in September 2018, as the result of an arbitration award. It is my understanding that the officer was given credit for service time towards pension retroactive to the date of termination and received back pay for earnings retroactive to the date of termination. Therefore, based on the arbitration award, the borough treats the officer as if he were never terminated and he was considered an employee and compensated for working during this period.

Just looking at the finding "criteria", it states that the employee must have been employed full-time for at least six consecutive months and was participating in a pension plan. The officer in question was reinstated and received back pay for being employed the entire year. In addition, as noted earlier, he was credited with service time for pension purposes for the entire year. In my opinion, the officer in question meets the criteria for being certified.

The finding mentions the amount received in 2018 does not equate to the officer working full-time for six consecutive months. The borough obviously disagrees as he was compensated as if he worked not only six months but the entire year.

In verbal conversations with the auditor, it was mentioned that because he was not reinstated until September 2018 he did not "work" six months in 2018 and thus not eligible. If this is the criteria then why is a municipality permitted to certify an employee on military leave the entire year? In military cases, not only does the employee not "work" the entire year but they also are not compensated by the municipality. The same can be said about employees on workers compensation, they are technically not "working" but are eligible for certification.

DICKSON CITY BOROUGH POLICE PENSION PLAN
FINDING AND RECOMMENDATION

Finding - (Continued)

I provided the auditor with a finding issued in one of my other accounts, the Borough of Wilkesburg, Allegheny County. It seems to me that this finding totally contradicts this audit finding.

In Wilkesburg, an officer was terminated in June of 2015 and because he did not work six months in 2015 he was not certified for state aid. The officer was then reinstated by an arbitration award on July 1, 2016, retroactive to June 2015 with all lost salary and benefits. The finding cited that because the officer was reinstated back to his termination date that he was now eligible for certification as if he worked all of 2015 and the borough was awarded additional state aid as such. The finding states “The reinstatement resulted in the employee being eligible for certification”.

The Wilkesburg finding goes on to “recommend” that, in the future, plan officials review any arbitration awards to determine if there is an effect on any previously filed Certification Form AG 385 which would necessitate an amendment of the form.

The Wilkesburg finding implies that the borough would have been cited by finding if they would “not” have certified the officer in question.

Auditor’s Conclusion: While we agree with plan officials that the officer in question was effectively reinstated during 2018 as a result of an arbitration award and granted credited service time towards his pension as well as back pay for earnings retroactive to the date of termination (September 25, 2017), facts and circumstances vary from one municipality to the next, and the scenario in Wilkesburg Borough should not be equated to the scenario in Dickson City Borough. In Wilkesburg Borough, the reinstated employee was reimbursed for all previous earnings and credited service time in the data year used for certification purposes. Conversely, Dickson City Borough elected to split the obligation for the prior accumulated earnings and service credit into two data years, 2018 and 2019, at the request and benefit of the employee for income tax purposes. Ultimately, the amount reimbursed to the employee during 2018, plus the service time actually earned by the employee from the date of reinstatement through the end of data year 2018 utilized for certification purposes on the Certification Form AG 385 filed in 2019, equated to less than the 6 months full-time employment required under Act 205 based on the employee’s annual compensation. The borough paid the remainder of the prior accumulated earnings and service credit obligation during 2019, which will be included in the data used for certification purposes on the borough’s Certification Form AG 385 that will be submitted during 2020. Therefore, the aforementioned recommendation remains as stated.

DICKSON CITY BOROUGH POLICE PENSION PLAN
POTENTIAL WITHHOLD OF STATE AID

The finding contained in this audit report cites an overpayment of state aid to the borough in the amount of \$10,241, plus interest. A condition of this nature may lead to a total withholding of state aid in the future unless that finding is corrected. A check in this amount with interest, at a rate earned by the pension plan, should be made payable to: Commonwealth of Pennsylvania, and mailed to: Department of the Auditor General, Municipal Pension & Fire Relief Programs Unit, 321 Finance Building, Harrisburg, PA 17120.

DICKSON CITY 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. 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	\$ 2,401,436	\$ 3,691,678	\$ 1,290,242	65.0%
01-01-15	2,795,512	3,815,473	1,019,961	73.3%
01-01-17	2,871,771	4,132,612	1,260,841	69.5%

Note: The market value of the plan's assets at 01-01-13 have been adjusted to reflect the smoothing of gains and/or losses over a four-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.

DICKSON CITY BOROUGH 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.

DICKSON CITY 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
2013	\$ 225,269	100.0%
2014	230,281	100.0%
2015	215,990	100.0%
2016	239,606	100.0%
2017	226,826	105.8%
2018	224,794	100.0%

DICKSON CITY BOROUGH 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
Remaining amortization period	12 years
Asset valuation method	Fair value
Actuarial assumptions:	
Investment rate of return	7.0%
Projected salary increases	4.75%

DICKSON CITY BOROUGH POLICE PENSION PLAN
REPORT DISTRIBUTION LIST

This report was initially distributed to the following:

The Honorable Tom W. Wolf
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Commonwealth of Pennsylvania

The Honorable Robert W. MacCallum
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