

COMPLIANCE AUDIT

Mahanoy City Borough Police Pension Plan Schuylkill County, Pennsylvania For the Period January 1, 2015 to December 1, 2018

July 2019



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
Mahanoy City Borough
Schuylkill County
Mahanoy City, PA 17948

We have conducted a compliance audit of Mahanoy City Borough Police Pension Plan for the period January 1, 2015 to December 1, 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 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. 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 sole plan member 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 benefits due to the retired individual and comparing these amounts to supporting documentation evidencing amounts determined and actually paid to the recipient.
- 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 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.

Borough officials are responsible for establishing and maintaining effective internal controls to provide reasonable assurance that Mahanoy 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 Mahanoy 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 – Failure To Implement Act 205 Mandatory Distressed Provisions

As previously noted, the objective of our audit of the Mahanoy City Borough Police Pension Plan was to determine compliance with applicable state laws, regulations, contracts, administrative procedures, and local ordinances and policies. Among several provisions relating to municipal pension plans, Act 205 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 funded status of the plan contained in the schedule of funding progress included in this report which indicates a decline of assets available to satisfy the long-term liabilities of the plan. **The plan's funded ratio went from 72.0% as of January 1, 2013, to a ratio of 62.8% as of January 1, 2017**, which is the most recent data available. Based on this information, the Municipal Pension Reporting Program issued a **notification that the borough is currently in Level II moderate distress status**. 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 Mahanoy 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.

July 3, 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, Mahanoy 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.

Mahanoy City Borough Police Pension Plan is a single-employer defined benefit pension plan locally controlled by the provisions of Ordinance No. 395, 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 January 1, 1962. Active members are required to contribute 6.75% percent of compensation to the plan. As of December 31, 2018, the plan had 4 active members, no terminated members eligible for vested benefits in the future, and 9 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	20 years of service.
Vesting	100% vesting available 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 participant who completed 26 or more 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:

A monthly benefit equal to 50% of the member's salary at the time the disability was incurred, offset by Social Security disability benefits received for the same injury.

MAHANoy CITY BOROUGH POLICE PENSION PLAN
FINDING AND RECOMMENDATION

Finding – Failure To Implement Act 205 Mandatory Distressed Provisions

Condition: Among several provisions relating to municipal pension plans, Act 205 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%

Based on the plan’s funded ratio of 72.0% as of January 1, 2013, the borough was considered in Level I minimal distress status. However, the plan’s funded ratio has subsequently declined to 62.8% as of its January 1, 2017 valuation and the borough is now currently in Level II moderate distress status.

Included with the determination notices, the Municipal Pension Reporting Program (MPRP) (formerly PERC) sent the municipality the Act 205 Recovery Program Election Form outlining the mandatory remedies that must be implemented along with the voluntary remedies available that the municipality could additionally elect to implement based on its distress status. This form was required to be signed by the plan’s Chief Administrative Officer and returned to MPRP.

Although the municipality submitted the required election form to MPRP, as of the date of this audit report, the borough has not complied with the mandatory remedy under Act 205 requiring the submission of a plan for administrative improvement.

Criteria: Act 205, amended by Act 44, at Section 605(a), states:

Recovery program level II.

- (a) Mandatory remedies. Any municipality to which level II of the recovery program applies shall utilize the following remedies:
 - (1) The aggregation of trust funds pursuant to section 607(b).
 - (2) The submission of a plan for administrative improvement pursuant to section 607(i).

Cause: Municipal officials failed to establish adequate internal control procedures to ensure that the mandatory distress remedies have been implemented.

Effect: The municipality is not in compliance with the Act 44 mandatory distress remedy provisions applicable to Level II, which are designed to improve the funding status and administrative efficiency of its pension plans.

MAHANOEY CITY BOROUGH POLICE PENSION PLAN
FINDING AND RECOMMENDATION

Finding – (Continued)

Recommendation: We recommend that municipal officials contact MPRP for guidance regarding the submission of its plan for administrative improvement as required under the mandatory remedies applicable to Level II of the recovery program of Act 205.

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

Auditor's Conclusion: Compliance will be evaluated during our next audit of the plan.

MAHANAY CITY BOROUGH POLICE PENSION PLAN
SUPPLEMENTARY INFORMATION
(UNAUDITED)

The supplementary information contained on Pages 5 and 6 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, 2015, 2016, 2017, AND 2018

	<u>2014</u>	<u>2015</u>	<u>2016</u>	<u>2017</u>	<u>2018</u>
Total Pension Liability					
Service cost	\$ 31,811	\$ 23,947	\$ 25,025	\$ 21,194	\$ 22,148
Interest	131,506	139,663	141,850	141,223	143,093
Difference between expected and actual experience	-	63,435	-	(73,474)	-
Changes of assumptions	-	-	-	52,766	-
Benefit payments, including refunds of member contributions	(105,662)	(114,596)	(156,445)	(144,947)	(131,936)
Net Change in Total Pension Liability	<u>57,655</u>	<u>112,449</u>	<u>10,430</u>	<u>(3,238)</u>	<u>33,305</u>
Total Pension Liability – Beginning	1,774,430	1,832,085	1,944,534	1,954,964	1,951,726
Total Pension Liability – Ending (a)	<u>\$ 1,832,085</u>	<u>\$ 1,944,534</u>	<u>\$ 1,954,964</u>	<u>\$ 1,951,726</u>	<u>\$ 1,985,031</u>
Plan Fiduciary Net Position					
Contributions – state aid	\$ 50,345	\$ 50,971	\$ 52,496	\$ 55,059	\$ 46,844
Contributions – employer	6,335	18,125	16,581	34,765	43,215
Contributions – member	15,135	12,088	10,404	7,739	13,657
Net investment income	45,978	(25,931)	61,137	115,761	(76,003)
Benefit payments, including refunds of member contributions	(105,662)	(114,596)	(156,445)	(144,947)	(131,936)
Other	1,310	-	-	-	-
Net Change in Plan Fiduciary Net Position	<u>13,441</u>	<u>(59,343)</u>	<u>(15,827)</u>	<u>68,377</u>	<u>(104,223)</u>
Plan Fiduciary Net Position – Beginning	1,277,380	1,290,821	1,231,478	1,215,651	1,284,028
Plan Fiduciary Net Position – Ending (b)	<u>\$ 1,290,821</u>	<u>\$ 1,231,478</u>	<u>\$ 1,215,651</u>	<u>\$ 1,284,028</u>	<u>\$ 1,179,805</u>
Net Pension Liability – Ending (a-b)	<u>\$ 541,264</u>	<u>\$ 713,056</u>	<u>\$ 739,313</u>	<u>\$ 667,698</u>	<u>\$ 805,226</u>
Plan Fiduciary Net Position as a Percentage of the Total Pension Liability	70.46%	63.33%	62.18%	65.79%	59.44%
Estimated Covered Employee Payroll	\$ 201,000	\$ 164,621	\$ 164,368	\$ 167,631	\$ 170,984
Net Pension Liability as a Percentage of Covered Employee Payroll	269.29%	433.15%	449.79%	398.31%	470.94%

MAHANAY CITY BOROUGH 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 borough as of December 31, 2015, 2016, 2017, and 2018, calculated using the discount rate of 7.5%, as well as what the borough'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 (6.5%)	Current Discount Rate (7.5%)	1% Increase (8.5%)
Net Pension Liability – 12/31/15	\$ 915,138	\$ 713,056	\$ 543,079
Net Pension Liability – 12/31/16	943,071	739,313	568,011
Net Pension Liability – 12/31/17	852,013	667,698	511,231
Net Pension Liability – 12/31/18	988,463	805,226	649,772

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
2014	\$ 56,680	\$ 56,680	\$ -	\$ 201,000	28.20%
2015	69,096	69,096	-	164,621	41.97%
2016	69,077	69,077	-	164,368	42.03%
2017	89,824	89,824	-	167,631	53.58%
2018	90,059	90,059	-	170,984	52.67%

MAHANAY 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	\$ 1,214,685	\$ 1,687,701	\$ 473,016	72.0%
01-01-15	1,290,821	1,895,520	604,699	68.1%
01-01-17	1,215,651	1,934,256	718,605	62.8%

The primary reason for the decrease in the plan’s funding percentage from 01-01-13 to 01-01-17 is attributable to asset losses incurred during the period 1-1-2013 to 1-1-2017. In addition, the plan experienced increases in the actuarial accrued liability from 2013 to 2017 as a result of changes in actuarial assumptions involving the mortality tables. The combination of the asset losses along with increases in the accrued liability decreased the plan’s funding percentage from 72.0% as of 1-1-2013 valuation to 62.8% as of 1-1-2017 valuation.

MAHANOEY 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.

MAHANoy 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
Amortization method	Level dollar
Remaining amortization period	11 years
Asset valuation method	Fair value
Actuarial assumptions:	
Investment rate of return	7.5%
Projected salary increases	4.5%
Cost-of-living adjustments	3.0%

MAHANAY CITY BOROUGH POLICE PENSION PLAN
REPORT DISTRIBUTION LIST

This report was initially distributed to the following:

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