

# COMPLIANCE AUDIT

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## McKees Rocks Borough Police Pension Plan Allegheny County, Pennsylvania For the Period January 1, 2015 to December 31, 2017

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September 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 Borough Council  
McKees Rocks Borough  
Allegheny County  
McKees Rocks, PA 15136

We have conducted a compliance audit of the McKees Rocks Borough Police Pension Plan for the period January 1, 2015 to December 31, 2017. 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 findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and 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 findings 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 findings 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 both of the 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 the retired individuals and comparing these amounts to supporting documentation evidencing amounts determined and actually paid to the recipients.
- 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.
- 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 McKees Rocks 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 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 McKees Rocks 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 findings further discussed later in this report:

Finding No. 1 – Partial Compliance With Prior Audit Recommendation – Incorrect Data On Certification Form AG 385 Resulting In An Overpayment Of State Aid

Finding No. 2 – Untimely Deposit Of State Aid

Finding No. 1 contained in this audit report repeats a condition that was cited in our previous audit report that has not been corrected by borough officials. We are concerned by the borough's failure to correct this previously reported audit finding and strongly encourage timely implementation of the recommendation noted in this audit report.

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 McKees Rocks 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.

September 7, 2018



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 McKees Rocks 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 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 600 - Police Pension Fund Act, Act of May 29, 1956 (P.L. 1804, No. 600), as amended, 53 P.S. § 761 et seq.

The McKees Rocks Borough Police Pension Plan is a single-employer defined benefit pension plan locally controlled by the provisions of Ordinance No. 1710, 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 August 1, 1963. Active members are required to contribute 5 percent of compensation to the plan. As of December 31, 2017, the plan had 7 active members, 1 terminated member eligible for vested benefits in the future, and 9 retirees receiving pension benefits from the plan.

## **BACKGROUND – (Continued)**

As of December 31, 2017, selected plan benefit provisions are as follows:

### Eligibility Requirements:

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

### Retirement Benefit:

Benefit equals 50% of final 36 months average salary, plus a service increment of \$100 for service in excess of 26 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. The monthly survivor benefits are payable to the participant's spouse for life. If there is no spouse or the spouse later dies, the benefit will be paid to the participant's dependent children, if any until age 18, or age 23 if attending college.

### Service Related Disability Benefit:

Benefit equals 50% of the participant's final monthly average salary at disablement/retirement, but no less than 50% member's salary at the time the disability was incurred, offset by Social Security disability benefits received for the same injury.

## MCKEES ROCKS BOROUGH POLICE PENSION PLAN STATUS OF PRIOR FINDINGS

### Compliance With Prior Audit Recommendations

McKees Rocks Borough has complied with the prior audit recommendations concerning the following:

- Incorrect Data On Certification Form AG 490 Resulting In Excess Reimbursement For Special 1989 Ad Hoc Postretirement Adjustments

On November 9, 2016, borough officials returned \$550 to the Commonwealth for the excess reimbursement; and subsequently on July 31, 2018, reimbursed an additional \$34 representing interest due on the excess reimbursement.

- Late Filing Of Actuarial Valuation Report

Borough officials filed their latest Actuarial Valuation Report in a timely manner in accordance with Act 205.

### Partial Compliance With Prior Audit Recommendation

McKees Rocks Borough has partially complied with the prior audit recommendation concerning the following:

- Incorrect Data On Certification Form AG 385 Resulting In A Net Overpayment Of State Aid

On November 9, 2016, borough officials reimbursed \$11,143 to the Commonwealth for the net overpayment of state aid received in 2014. Subsequently on July 31, 2018, borough officials returned an additional \$694 representing the interest due on the state aid overpayment; however, plan officials again failed to comply with the instructions that accompanied Certification Form AG 385 to assist them in accurately reporting the required pension data of the police pension plan in the year 2017, as further discussed in Finding No. 1 of this report.



MCKEES ROCKS BOROUGH POLICE PENSION PLAN  
FINDINGS AND RECOMMENDATIONS

**Finding No. 1 – Partial Compliance With Prior Audit Recommendation – Incorrect Data On Certification Form AG 385 Resulting In An Overpayment Of State Aid**

Condition: As disclosed in the Status of Prior Findings section of this report, the borough partially complied with our prior audit recommendation by reimbursing the Commonwealth for the overpayment of state aid received in 2014 and including interest on the overpayment. However, a similar condition occurred during the current audit period. Plan officials again failed to comply with the instructions that accompany Certification Form AG 385 to assist them in accurately reporting the required pension data of the police pension plan. The borough certified 2 ineligible police officers (4 units) on Certification Form AG 385 filed during 2017. The data contained on these certification forms 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: Plan officials again failed to implement adequate internal control procedures to ensure the accuracy and consistency of the data certified and to ensure full compliance with the prior audit recommendation.

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 plan. The township's state aid for 2017 was based on the plan's unit value in the amount of \$114,706 (25 units at \$4,588). However, based on the corrected information, the township was only entitled to an allocation based on the plan's pension costs in the amount of \$91,122. Therefore, the township received an overpayment of state aid in the amount of \$23,584 in 2017. Additionally, the borough used the overpayment of state aid to pay the minimum municipal obligation (MMO) due to the 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 \$23,584 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.

## MCKEES ROCKS BOROUGH POLICE PENSION PLAN FINDINGS AND RECOMMENDATIONS

### **Finding No. 1 – (Continued)**

We also again recommend that in the future, plan officials establish adequate internal control procedures, such as having at least 2 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.

In addition, 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 Response:** Municipal officials agreed with the finding without exception.

**Auditors Conclusion:** Due to the potential withhold of state aid, the borough's compliance with the finding recommendation will be monitored subsequent to the release of the audit report and through our next audit of the plan.

### **Finding No. 2 – Untimely Deposit Of State Aid**

**Condition:** The municipality did not deposit its 2016 and 2017 state aid allocations into an eligible pension plan within the 30 day grace period allowed by Act 205. The borough received its state aid allocations in the amounts of \$118,115 and \$114,706, respectively, on September 27, 2016, and September 27, 2017, respectively, but did not deposit these funds into one of the borough's eligible pension plans until December 19, 2016 and December 27 and 28, 2017, respectively.

**Criteria:** Section 402(g) of Act 205 states, in part:

. . . the total amount of the general municipal pension system State aid received by the municipality shall, within 30 days of receipt by the treasurer of the municipality, be deposited in the pension funds or the alternate funding mechanisms applicable to the respective pension plans.

**Cause:** Due to turnover in municipal officials responsible for the administration of the borough's pension plans who were unaware of the requirements of Act 205, the borough's 2016 and 2017 state aid allocations were not deposited timely into the borough's pension plans.

**Effect:** Although the state aid was eventually deposited into the plans, the interest earned beyond the 30 day grace period was not deposited into the plans. When state aid is not deposited into a pension plan account in a timely manner, the funds are not available to pay operating expenses or for investment and the risk of misapplication is increased.

MCKEES ROCKS BOROUGH POLICE PENSION PLAN  
FINDINGS AND RECOMMENDATIONS

**Finding No. 2 – (Continued)**

Recommendation: We recommend that plan officials determine and pay the interest earned during the period beyond the 30 day grace period allowed by Act 205 compounded annually, into its non-uniformed management and police pension plans, accordingly. A copy of the interest calculation must be maintained by the borough for examination during our next audit of the plan.

We also recommend that plan officials develop and implement adequate internal control procedures to ensure that future state aid allocations are deposited timely in accordance with Act 205 requirements.

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

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

MCKEES ROCKS BOROUGH POLICE PENSION PLAN  
POTENTIAL WITHHOLD OF STATE AID

Finding No. 1 contained in this report cites an overpayment of state aid to the borough in the amount of \$23,584 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.

MCKEES ROCKS 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	\$ 3,497,158	\$ 3,492,052	\$ (5,106)	100.1%
01-01-15	4,333,187	3,736,381	(596,806)	116.0%
01-01-17	4,529,302	4,334,132	(195,170)	104.5%

MCKEES ROCKS 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.

MCKEES ROCKS 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
2012	\$ 95,108	100.0%
2013	113,019	100.0%
2014	112,253	100.0%
2015	114,914	100.0%
2016	47,411	249.1%
2017	63,533	100.0%

MCKEES ROCKS 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	N/A
Remaining amortization period	N/A
Asset valuation method	Fair value
Actuarial assumptions:	
Investment rate of return*	7.25%
Projected salary increases*	5.0%

\* *Includes inflation at 2.75%*



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