

COMPLIANCE AUDIT

Mechanicsburg Borough Police Pension Plan Cumberland County, Pennsylvania For the Period January 1, 2015 to December 31, 2018

June 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
Mechanicsburg Borough
Cumberland County
Mechanicsburg, PA 17055

We have conducted a compliance audit of the Mechanicsburg Borough Police Pension Plan for the period January 1, 2015 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. State Aid and Employer Contributions.

- 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 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 individuals 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 the terms of the contractual agreement with the Pennsylvania State Association of Boroughs were in accordance with the plan's governing document, if separately stated, and applicable laws and regulations by comparing the terms of the contractual agreement with the plan's governing document, if separately stated, and applicable laws and regulations.
- 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 Mechanicsburg 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 Mechanicsburg Borough 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 Mechanicsburg 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.

June 17, 2019



EUGENE A. DEPASQUALE
Auditor General

CONTENTS

	<u>Page</u>
Background.....	1
Supplementary Information	3
Report Distribution List	10

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 Mechanicsburg 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 Mechanicsburg Borough Police Pension Plan is a single-employer defined benefit pension plan locally controlled by the provisions of Ordinance No. 1093, 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, 1956. Active members are required to contribute 4.75 percent of compensation to the plan. As of December 31, 2018, the plan had 17 active members, 2 terminated members eligible for vested benefits in the future, and 11 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 completion 25 years of service.
Early Retirement	20 years of service.
Vesting	100% vesting available after 12 years of service.

Retirement Benefit:

A monthly pension equal to 50% of the average monthly compensation earned during the last 36 months of service. Hired on or after January 1, 1981, additional \$100 per month (maximum) for completing 26 or more years of service. Hired prior to January 1, 1981, additional \$100 per month for each completed year of service in excess of 25 years up to a maximum of 5 years (maximum \$500 per month).

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:

Greater of 75% of final average 36 monthly salary or 50% of the salary at time of disability offset by social security.

MECHANICSBURG BOROUGH POLICE PENSION PLAN
SUPPLEMENTARY INFORMATION
(UNAUDITED)

The supplementary information contained on Pages 3 through 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, AND 2016

	<u>2014</u>	<u>2015</u>	<u>2016</u>
Total Pension Liability			
Service cost	\$ 193,846	\$ 200,742	\$ 210,779
Interest	427,448	449,667	475,519
Difference between expected and actual experience	-	(157,490)	-
Changes of assumptions	-	140,491	-
Benefit payments, including refunds of member contributions	(288,694)	(298,872)	(283,385)
Net Change in Total Pension Liability	<u>332,600</u>	<u>334,538</u>	<u>402,913</u>
Total Pension Liability – Beginning	<u>6,056,904</u>	<u>6,389,504</u>	<u>6,724,042</u>
Total Pension Liability – Ending (a)	<u><u>\$ 6,389,504</u></u>	<u><u>\$ 6,724,042</u></u>	<u><u>\$ 7,126,955</u></u>
Plan Fiduciary Net Position			
Contributions – employer	\$ 434	\$ 8,585	\$ 35,088
Contributions – state aid	108,435	109,783	113,741
Contributions – member	51,808	62,722	50,448
Net investment income	361,157	(38,969)	273,892
Benefit payments, including refunds of member contributions	(288,694)	(298,872)	(283,385)
Administrative expense	(45,250)	(50,177)	(48,885)
Net Change in Plan Fiduciary Net Position	<u>187,890</u>	<u>(206,928)</u>	<u>140,899</u>
Plan Fiduciary Net Position – Beginning	<u>6,016,064</u>	<u>6,203,954</u>	<u>5,997,026</u>
Plan Fiduciary Net Position – Ending (b)	<u><u>\$ 6,203,954</u></u>	<u><u>\$ 5,997,026</u></u>	<u><u>\$ 6,137,925</u></u>
Net Pension Liability – Ending (a-b)	<u><u>\$ 185,550</u></u>	<u><u>\$ 727,016</u></u>	<u><u>\$ 989,030</u></u>
Plan Fiduciary Net Position as a Percentage of the Total Pension Liability	97.1%	89.2%	86.1%
Estimated Covered Employee Payroll	\$ 996,288	\$ 1,065,570	\$ 1,051,630
Net Pension Liability as a Percentage of Covered Employee Payroll	18.6%	68.2%	94.0%

MECHANICSBURG BOROUGH POLICE PENSION PLAN
SUPPLEMENTARY INFORMATION
(UNAUDITED)

SCHEDULE OF CHANGES IN THE NET PENSION
LIABILITY AND RELATED RATIOS
FOR THE YEARS ENDED DECEMBER 31, 2017, AND 2018

	<u>2017</u>	<u>2018</u>
Total Pension Liability		
Service cost	\$ 209,914	\$ 220,410
Interest	485,175	514,583
Difference between expected and actual experience	(446,197)	-
Changes of assumptions	195,041	-
Benefit payments, including refunds of member contributions	(309,289)	(261,638)
Net Change in Total Pension Liability	<u>134,644</u>	<u>473,355</u>
Total Pension Liability – Beginning	7,126,955	7,261,599
Total Pension Liability – Ending (a)	<u>\$ 7,261,599</u>	<u>\$ 7,734,954</u>
Plan Fiduciary Net Position		
Contributions – employer	\$ 21,573	\$ 44,707
Contributions – state Aid	119,295	121,794
Contributions – member	54,239	58,499
Net investment income	794,290	(319,098)
Benefit payments, including refunds of member contributions	(309,289)	(261,638)
Administrative expense	(52,185)	(49,331)
Net Change in Plan Fiduciary Net Position	<u>627,923</u>	<u>(405,067)</u>
Plan Fiduciary Net Position – Beginning	6,137,925	6,765,848
Plan Fiduciary Net Position – Ending (b)	<u>\$ 6,765,848</u>	<u>\$ 6,360,781</u>
Net Pension Liability – Ending (a-b)	<u>\$ 495,751</u>	<u>\$ 1,374,173</u>
Plan Fiduciary Net Position as a Percentage of the Total Pension Liability	93.2%	82.2%
Estimated Covered Employee Payroll	\$ 1,014,106	\$ 1,070,000
Net Pension Liability as a Percentage of Covered Employee Payroll	48.9%	128.4%

MECHANICSBURG 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 7.00%, 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:

	<u>1% Decrease (6.00%)</u>	<u>Current Discount Rate (7.00%)</u>	<u>1% Increase (8.00%)</u>
Net Pension Liability – 12/31/15	\$ 1,603,882	\$ 727,016	\$ (4,678)
Net Pension Liability – 12/31/16	\$ 1,911,277	\$ 989,030	\$ 218,804
Net Pension Liability – 12/31/17	\$ 1,439,614	\$ 495,751	\$ (289,513)
Net Pension Liability – 12/31/18	\$ 2,365,507	\$ 1,374,173	\$ 549,097

SCHEDULE OF CONTRIBUTIONS

<u>Year Ended December 31</u>	<u>Actuarially Determined Contribution</u>	<u>Actual Contributions</u>	<u>Contribution Deficiency (Excess)</u>	<u>Covered- Employee Payroll</u>	<u>Contributions as a Percentage of Covered- Employee Payroll</u>
2014	\$ 108,869	\$ 108,869	\$ -	\$ 996,288	10.93%
2015	118,368	118,368	-	1,065,570	11.10%
2016	148,829	148,829	-	1,051,630	14.15%
2017	140,868	140,868	-	1,014,106	13.89%
2018	166,501	166,501	-	1,070,000	15.56%

MECHANICSBURG BOROUGH POLICE PENSION PLAN
SUPPLEMENTARY INFORMATION
(UNAUDITED)

SCHEDULE OF INVESTMENT RETURNS

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

2018	(4.72%)
2017	12.94%
2016	4.57%
2015	(0.64%)
2014	6.13%

MECHANICSBURG 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	\$ 6,594,625	\$ 5,897,881	\$ (696,744)	111.8%
01-01-15	6,888,613	6,372,505	(516,108)	108.1%
01-01-17	7,365,510	6,875,799	(489,711)	107.1%

Note: The market values of the plan’s assets at 01-01-13, 01-01-15 and 01-01-17 have been adjusted to reflect the smoothing of gains and /or losses subject to a ceiling of 120 percent of the market value of assets. These method will lower contribution in years of less an 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.

MECHANICSBURG 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.

MECHANICSBURG 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	Plan assets are valued using the method described in Section 210 of Act 205, as amended, subject to a ceiling of 120% of the market value of assets.
Actuarial assumptions:	
Investment rate of return	7.0%
Projected salary increases	5.0%
Cost-of-living adjustments	In accordance with Act 600.

MECHANICSBURG BOROUGH POLICE PENSION PLAN
REPORT DISTRIBUTION LIST

This report was initially distributed to the following:

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