

# COMPLIANCE AUDIT

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## Watsonstown Borough Non-Uniformed Pension Plan Northumberland County, Pennsylvania For the Period January 1, 2015 to December 31, 2018

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September 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  
Watsontown Borough  
Northumberland County  
Watsontown, PA 17777

We have conducted a compliance audit of the Watsontown Borough Non-Uniformed 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.

- We determined that there were no employee contributions required by the plan's governing document and applicable laws and regulations for the years covered by our audit period.
- We determined whether retirement benefits calculated for the two 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 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 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 benefit due to the retired individual and comparing this amount to supporting documentation evidencing the amount determined.
- We determined whether the January 1, 2013, January 1, 2015, and January 1, 2017 actuarial valuation reports were prepared and submitted by March 31, 2014, 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.
- We determined whether transfers were properly authorized, timely, and appropriately recorded by plan officials by examining supporting documentation for the transfer made during the audit period.

Borough officials are responsible for establishing and maintaining effective internal controls to provide reasonable assurance that the Watson town Borough Non-Uniformed 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 Watsontown Borough Non-Uniformed 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 Watsontown 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 11, 2019

A handwritten signature in black ink, appearing to read "Eugene A. DePasquale", with a long horizontal flourish extending to the right.

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 Watsonstown Borough Non-Uniformed 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.

The Watsonstown Borough Non-Uniformed Pension Plan is a single-employer defined benefit pension plan locally controlled by the provisions of Ordinance No. 1995-6, and a separately executed plan agreement with custodian. The plan was established January 1, 1988. Active members are not required to contribute to the plan. As of December 31, 2018, the plan had 7 active members, 2 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 62 and 25 years of service (maximum age 70).
Early Retirement	Age 52 with 10 years of service.
Vesting	100% after 5 years of service.

### Retirement Benefit:

Benefit equals 50% of average compensation times the accrued benefit adjustment times the short service percentage. Average Compensation equals the average of total pay received 3 years prior to normal retirement date. The accrued benefit adjustment equals service as of a given date divided by the later of service as of normal retirement date or age 65. The short service percentage equals the months of service at normal retirement date divided by 300 (maximum equals 100%).

### Survivor Benefit:

If participant is fully or partially vested, an accrued benefit payable immediately to the spouse equal to amount that would have been had employment terminated on date of death and participant had survived to earliest retirement age with a 50% survivor annuity and then died the next day.

### Service Related Disability Benefit:

None

WATSONTOWN BOROUGH NON-UNIFORMED PENSION PLAN  
SUPPLEMENTARY INFORMATION  
(UNAUDITED)

The supplementary information contained on Pages 3 through 5 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	\$ 26,316	\$ 30,962	\$ 32,278	\$ 39,240	\$ 40,908
Interest	88,237	90,175	92,618	88,290	90,362
Difference between expected and actual experience	-	(46,661)	-	(99,294)	-
Changes of assumptions	-	38,600	-	4,759	-
Benefit payments, including refunds of member contributions	(80,962)	(83,902)	(88,624)	*(114,268)	(82,711)
Net Change in Total Pension Liability	33,591	29,174	36,272	(81,273)	48,559
Total Pension Liability – Beginning	1,321,385	1,354,976	1,384,150	1,420,422	1,339,149
Total Pension Liability – Ending (a)	<u>\$ 1,354,976</u>	<u>\$ 1,384,150</u>	<u>\$ 1,420,422</u>	<u>\$ 1,339,149</u>	<u>\$ 1,387,708</u>
Plan Fiduciary Net Position					
Contributions – employer	\$ 90,524	\$ 90,648	\$ 106,708	\$ 70,474	\$ 112,664
Contributions – state aid	4,477	2,070	-	36,706	-
Net investment income	30,170	(15,988)	34,341	94,298	(47,262)
Benefit payments, including refunds of member contributions	(80,962)	(83,902)	(88,624)	*(114,268)	(82,711)
Administrative expense	(5,375)	(5,875)	-	(13,695)	(9,800)
Net Change in Plan Fiduciary Net Position	38,834	(13,047)	52,425	73,515	(27,109)
Plan Fiduciary Net Position – Beginning	839,588	878,422	865,375	917,800	991,315
Plan Fiduciary Net Position – Ending (b)	<u>\$ 878,422</u>	<u>\$ 865,375</u>	<u>\$ 917,800</u>	<u>\$ 991,315</u>	<u>\$ 964,206</u>
Net Pension Liability – Ending (a-b)	<u>\$ 476,554</u>	<u>\$ 518,775</u>	<u>\$ 502,622</u>	<u>\$ 347,834</u>	<u>\$ 423,502</u>
Plan Fiduciary Net Position as a Percentage of the Total Pension Liability	64.8%	62.5%	64.6%	74.0%	69.5%
Estimated Covered Employee Payroll	\$ 286,030	\$ 262,610	\$ 308,415	\$ 312,417	\$ 315,728
Net Pension Liability as a Percentage of Covered Employee Payroll	166.6%	197.5%	163.0%	111.3%	134.17%

\* Includes annuity purchase of \$30,795 before transfer to new custodian.



WATSONTOWN BOROUGH NON-UNIFORMED 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 6.75%, 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 (5.75%)	Current Discount Rate (6.75%)	1% Increase (7.75%)
Net Pension Liability – 12/31/15	\$ 659,720	\$ 518,775	\$ 396,750
Net Pension Liability – 12/31/16	\$ 646,482	\$ 502,622	\$ 377,972
Net Pension Liability – 12/31/17	\$ 484,082	\$ 347,834	\$ 230,285
Net Pension Liability – 12/31/18	\$ 563,981	\$ 423,502	\$ 302,198

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	\$ 73,095	\$ 73,095	\$ -	\$ 285,073	25.64%
2010	92,405	95,003	(2,598)	294,953	32.21%
2011	93,950	93,950	-	310,896	30.22%
2012	92,041	92,041	-	317,595	28.98%
2013	87,084	87,084	-	260,743	33.40%
2014	95,001	95,001	-	286,030	33.21%
2015	92,718	92,718	-	262,610	35.31%
2016	106,708	106,708	-	308,415	34.60%
2017	107,180	107,180	-	312,417	34.31%
2018	112,664	112,664	-	315,728	35.68%

WATSONTOWN BOROUGH NON-UNIFORMED PENSION PLAN  
SUPPLEMENTARY INFORMATION  
(UNAUDITED)

SCHEDULE OF INVESTMENT RETURNS

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

2018	-4.77%
2017	12.21%
2016	3.11%
2015	-1.84%
2014	3.79%

WATSONTOWN BOROUGH NON-UNIFORMED 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	\$ 826,026	\$ 1,292,246	\$ 466,220	63.9%
01-01-15	926,081	1,346,915	420,834	68.8%
01-01-17	1,001,176	1,325,887	324,711	75.5%

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 over a five-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.

WATSONTOWN BOROUGH NON-UNIFORMED 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.

WATSONTOWN BOROUGH NON-UNIFORMED 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	6 years
Asset valuation method	Fair value, 5-year smoothing
Actuarial assumptions:	
Investment rate of return	6.75%
Projected salary increases	4.25%

WATSONTOWN BOROUGH NON-UNIFORMED PENSION PLAN  
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