

# COMPLIANCE AUDIT

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## Zelienople Borough Police Pension Plan Butler County, Pennsylvania For the Period January 1, 2017 to December 31, 2018

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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  
Zelienople Borough  
Butler County  
Zelienople, PA 16063

We have conducted a compliance audit of the Zelienople Borough Police Pension Plan for the period January 1, 2017 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 finding 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 lone 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 benefit 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, 2017 actuarial valuation report was prepared and submitted by March 31, 2018, in accordance with Act 205 and whether selected information provided on this report 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 Zelienople 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 Zelienople 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 Pension Benefits Paid To Retiree

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 Zelienople 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 12, 2019

A handwritten signature in black ink, appearing to read "Eugene A. DePasquale". The signature is fluid and cursive, with a long horizontal stroke 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 Zelienople 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 Zelienople Borough Police Pension Plan is a single-employer defined benefit pension plan locally controlled by the provisions of Ordinance No. 803-10, 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 April 10, 1958. Active members are required to contribute 8 percent of compensation to the plan. As of December 31, 2018, the plan had 8 active members, no terminated members eligible for vested benefits in the future, and 7 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. Age 55 and 25 years of service for participants hired after January 1, 2017.
Early Retirement	Age 60 and 20 years of service between January 1, 2017 and November 30, 2020.
Vesting	100% vesting available after 12 years of service.

### Retirement Benefit:

A monthly benefit equal to 50% of the final 48 months average salary, plus a service increment of \$100 for service of 26 years or more.

### 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:

Benefit equals 50% of the member's salary at the time the disability was incurred, offset by Social Security disability benefits received for the same injury.

ZELIENOPLE BOROUGH POLICE PENSION PLAN  
FINDING AND RECOMMENDATION

**Finding – Incorrect Pension Benefits Paid To Retiree**

Condition: The pension plan is paying an incorrect monthly benefit to a retiree in excess of the benefit amount calculated at retirement. Beginning in June 2018, a retiree began receiving \$200 more per month than entitled, which went undetected by borough officials until brought to the borough's attention during the conduct of our audit of the police pension plan.

Criteria: Ordinance No. 803-10, at Section 4.02, states, in part:

Normal Retirement Benefit - Each Participant who shall become entitled to a benefit pursuant to Section 4.01 shall receive a benefit paid monthly in an amount equal to fifty percent (50%) of the Participant's Final Monthly Average Salary as determined herein.

Ordinance No. 854-17, at Section 4.15, states, in part:

A benefit equal to the actuarial equivalent of the participant's accrued benefit calculated on final monthly average salary multiplied by a fraction, the numerator of which shall be the Participant's Aggregate Service determined as of such date and the denominator of which shall be the projected Aggregate Service of the Participant as if the Participant continues in Employment until attainment of Normal Retirement Age.

Our review of the original pension benefit determination evidenced that the calculation was significantly correct and in accordance with the plan document.

Cause: Although plan officials correctly determined the original monthly pension benefit, a typographical error was made by the plan's custodian during 2018 that went undetected by officials because internal control procedures, such as reconciling pension payments due to payments paid, were not effective to ensure that the correct monthly benefit was being paid to the retiree.

Effect: The retiree is receiving \$2,453 per month instead of the \$2,253 amount authorized by the plan document (\$200 in excess monthly benefits), and a total overpayment of \$2,800 was made from the pension plan from June 1, 2018 to the date of this report.

Recommendation: We recommend that municipal officials adjust the retiree's pension benefit prospectively, to the correct monthly amount due the retired member. In addition, we recommend the pension plan be reimbursed for the overpayments made from the plan retroactive to June 2018.

We also recommend that plan officials establish adequate internal control procedures, such as reconciling pension payments due to payments paid, to ensure correct amounts are being paid from the plan.

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.



ZELIENOPLE BOROUGH POLICE PENSION PLAN  
SUPPLEMENTARY INFORMATION  
(UNAUDITED)

The supplementary information contained on Pages 4 through 7 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 AND 2015

	<u>2014</u>	<u>2015</u>
Total Pension Liability		
Service cost	\$ 81,873	\$ 94,329
Interest	266,453	282,822
Difference between expected and actual experience	-	66,733
Benefit payments, including refunds of member contributions	<u>(207,669)</u>	<u>(210,940)</u>
Net Change in Total Pension Liability	140,657	232,944
Total Pension Liability – Beginning	3,572,807	3,713,464
Total Pension Liability – Ending (a)	<u>\$ 3,713,464</u>	<u>\$ 3,946,408</u>
Plan Fiduciary Net Position		
Contributions – employer	\$ 158,709	\$ 173,968
Contributions – employee	42,786	45,416
Net investment income	234,599	14,602
Benefit payments, including refunds of member contributions	<u>(207,669)</u>	<u>(210,940)</u>
Administrative expense	<u>(25,451)</u>	<u>(25,493)</u>
Net Change in Plan Fiduciary Net Position	202,974	(2,447)
Plan Fiduciary Net Position – Beginning	2,994,387	3,197,361
Plan Fiduciary Net Position – Ending (b)	<u>\$ 3,197,361</u>	<u>\$ 3,194,914</u>
Net Pension Liability – Ending (a-b)	<u>\$ 516,103</u>	<u>\$ 751,494</u>
Plan Fiduciary Net Position as a Percentage of the Total Pension Liability	86.1%	81.0%
Estimated Covered Employee Payroll	\$ 643,864	\$ 680,353
Net Pension Liability as a Percentage of Covered Employee Payroll	80.2%	110.5%

ZELIENOPLE BOROUGH POLICE PENSION PLAN  
SUPPLEMENTARY INFORMATION  
(UNAUDITED)

SCHEDULE OF CHANGES IN THE NET PENSION  
LIABILITY AND RELATED RATIOS  
FOR THE YEARS ENDED DECEMBER 31, 2016 AND 2017

	<u>2016</u>	<u>2017</u>
Total Pension Liability		
Service cost	\$ 99,045	\$ 114,040
Interest	295,643	309,454
Difference between expected and actual experience	-	(82,614)
Change of assumptions	-	210,376
Benefit payments, including refunds of member contributions	(210,940)	(210,940)
Net Change in Total Pension Liability	<u>183,748</u>	<u>340,316</u>
Total Pension Liability – Beginning	3,946,408	4,130,156
Total Pension Liability – Ending (a)	<u>\$ 4,130,156</u>	<u>\$ 4,470,472</u>
Plan Fiduciary Net Position		
Contributions – employer	\$ 180,769	\$ 180,169
Contributions – employee	50,772	50,764
Net investment income	164,871	528,926
Benefit payments, including refunds of member contributions	(210,940)	(210,940)
Administrative expense	(23,175)	(28,682)
Net Change in Plan Fiduciary Net Position	<u>162,297</u>	<u>520,237</u>
Plan Fiduciary Net Position – Beginning	3,194,914	3,357,211
Plan Fiduciary Net Position – Ending (b)	<u>\$ 3,357,211</u>	<u>\$ 3,877,448</u>
Net Pension Liability – Ending (a-b)	<u>\$ 772,945</u>	<u>\$ 593,024</u>
Plan Fiduciary Net Position as a Percentage of the Total Pension Liability	81.3%	86.7%
Estimated Covered Employee Payroll	\$ 675,209	\$ 668,645
Net Pension Liability as a Percentage of Covered Employee Payroll	114.5%	88.7%

ZELIENOPLE 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 and 2016 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:

	<u>1% Decrease (6.5%)</u>	<u>Current Discount Rate (7.5%)</u>	<u>1% Increase (8.5%)</u>
Net Pension Liability – 12/31/15	\$ 1,185,008	\$ 751,494	\$ 382,819
Net Pension Liability – 12/31/16	\$ 1,221,066	\$ 772,945	\$ 391,604

In addition, the following presents the net pension liability of the borough as of December 31, 2017, calculated using the discount rate of 7.25%, 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 (6.25%)</u>	<u>Current Discount Rate (7.25%)</u>	<u>1% Increase (8.25%)</u>
Net Pension Liability – 12/31/17	\$ 1,094,815	\$ 593,024	\$ 169,496

ZELIENOPLE BOROUGH POLICE PENSION PLAN  
 SUPPLEMENTARY INFORMATION  
 (UNAUDITED)

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	\$ 130,476	\$ 130,476	\$ -		
2010	133,792	133,792	-	\$ 643,523	20.8%
2011	177,711	177,711	-		
2012	159,714	159,714	-	606,412	26.3%
2013	161,784	161,784	-		
2014	158,709	158,709	-	631,344	25.1%
2015	173,968	173,968	-	680,353	25.6%
2016	180,769	180,769	-	675,209	26.8%
2017	180,169	180,169	-	668,645	26.9%
2018	232,567	232,567	-		

\* Due to GASB Statement No. 67, *Financial Reporting for Pension Plans*, being implemented only recently, the amount of Covered-Employee Payroll was not provided for odd years prior to 2014. In addition, due to the timing of this audit, covered-employee payroll for 2018 was not provided in this schedule.

SCHEDULE OF INVESTMENT RETURNS

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

2017	16.04%
2016	5.24%
2015	0.47%
2014	8.00%

ZELIENOPLE 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	\$ 2,488,898	\$ 3,411,166	\$ 922,268	73.0%
01-01-15	3,018,686	3,780,197	761,511	79.9%
01-01-17	3,517,819	4,257,918	740,099	82.6%

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 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.

ZELIENOPLE 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.

ZELIENOPLE 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, closed
Remaining amortization period	7 years
Asset valuation method	Market value, 4-year smoothing
Actuarial assumptions:	
Investment rate of return *	7.25%
Projected salary increases *	4.50%
Cost-of-living adjustments	None assumed

\* Includes inflation at 2.75%

ZELIENOPLE BOROUGH POLICE PENSION PLAN  
REPORT DISTRIBUTION LIST

This report was initially distributed to the following:

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