

COMPLIANCE AUDIT

Slippery Rock Borough Police Pension Plan Butler County, Pennsylvania For the Period January 1, 2011 to December 31, 2013

October 2014



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
Slippery Rock Borough
Butler County
Slippery Rock, PA 16057

We have conducted a compliance audit of the Slippery Rock Borough Police Pension Plan for the period January 1, 2011 to December 31, 2013. 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 findings and conclusions based on our audit objective. We believe that the evidence obtained provides a reasonable basis for our findings 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. Our methodology addressed determinations about the following:

- Whether state aid was properly determined and deposited in accordance with Act 205 requirements.
- Whether employer contributions are determined and deposited in accordance with the plan's governing document and applicable laws and regulations.
- Whether employee contributions are required and, if so, are determined, deducted and deposited into the pension plan and are in accordance with the plan provisions and applicable laws and regulations.
- Whether benefit payments, if any, represent payments to all (and only) those entitled to receive them and are properly determined in accordance with applicable laws and regulations.

- Whether obligations for plan benefits are accurately determined in accordance with plan provisions and based on complete and accurate participant data; and whether actuarial valuation reports are prepared and submitted to the Public Employee Retirement Commission (PERC) in accordance with state law and 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.
- Whether benefit payments have only been made to living recipients, based on the Social Security numbers found in the pension records for retirees and beneficiaries.

Slippery Rock Borough contracted with an independent certified public accounting firm for annual audits of its financial statements prepared in conformity with the accounting practices prescribed or permitted by the Department of Community and Economic Development of the Commonwealth of Pennsylvania, which are available at the borough's offices. Those financial statements were not audited by us and, accordingly, we express no opinion or other form of assurance on them.

Borough officials are responsible for establishing and maintaining effective internal controls to provide reasonable assurance that the Slippery Rock 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, 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 tests indicated that, in all significant respects, the Slippery Rock 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:

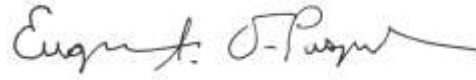
Finding No. 1 – Incorrect Data On Certification Form AG 385 Resulting In A Net Underpayment Of State Aid

Finding No. 2 – Pension Benefit Not In Compliance With Act 600 Provisions

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 Slippery Rock Borough and, where appropriate, their responses have been included in the report.

October 9, 2014

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

CONTENTS

	<u>Page</u>
Background.....	1
Findings and Recommendations:	
Finding No. 1 – Incorrect Data On Certification Form AG 385 Resulting In A Net Underpayment Of State Aid.....	3
Finding No. 2 – Pension Benefit Not In Compliance With Act 600 Provisions.....	4
Supplementary Information	6
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 Slippery Rock Borough Police Pension Plan is also governed by implementing regulations adopted by the 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. § 761 et seq.

The Slippery Rock Borough Police Pension Plan is a single-employer defined benefit pension plan locally controlled by the provisions of Ordinance No. 590-RSTUV, effective January 1, 2014, adopted pursuant to Act 600. Prior to January 1, 2014, the plan was locally controlled by the provisions of Ordinance No. 590, 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 December 29, 1975. Active members are required to contribute not less than 5 percent and not more than 8 percent of compensation to the plan; however, member contributions were waived during the current audit period. As of December 31, 2013, the plan had 2 active members, 1 terminated member eligible for vested benefits in the future and 2 retirees receiving pension benefits from the plan.

BACKGROUND – (Continued)

As of December 31, 2013, selected plan benefit provisions are as follows:

Eligibility Requirements:

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

Retirement Benefit:

Benefit equals 50% of final 36 months average compensation, plus a service increment of \$100 per month for each year of service in excess of 25 years, up to a maximum of \$100 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:

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

SLIPPERY ROCK BOROUGH POLICE PENSION PLAN
FINDINGS AND RECOMMENDATIONS

Finding No. 1 – Incorrect Data On Certification Form AG 385 Resulting In A Net Underpayment Of State Aid

Condition: The borough failed to certify 1 eligible police officer (2 units) who terminated employment on October 26, 2012, and understated payroll by \$35,329 on the Certification Form AG 385 filed in 2013. In addition, the borough certified 1 ineligible non-uniformed employee (1 unit) who was employed part-time and overstated payroll by \$12,249 on the Certification Form AG 385 filed in 2013. The data contained on this certification form is based on prior calendar year information.

Criteria: Pursuant to Act 205, at Section 402(e)(2), an employee who has been employed on a full-time basis for at least six consecutive months and has been participating in a pension plan during the certification year is eligible for certification.

Cause: Plan officials failed to establish adequate internal control procedures to ensure the accuracy of the data certified.

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 plans.

The borough's state aid allocation for 2013 was based solely on police pension costs in the amount of \$23,467. However, based on the corrected information, the borough was entitled to a unit value allocation of \$31,072 (6 police units and 2 non-uniformed units); therefore, the borough received an underpayment of state aid in the amount of \$7,605 in 2013.

Although the borough will be reimbursed for the underpayment of state aid due to the borough's certification errors, the full amount of the 2013 state aid allocation was not available to be deposited timely and therefore was not available to pay operating expenses or for investment.

Since the borough made a 2013 contribution of \$5,698 to the police pension plan in order to satisfy the 2013 minimum municipal obligation, upon receipt of the \$7,605, \$5,698 may be reimbursed to the borough, and the remaining balance deposited into the police pension plan.

Recommendation: We 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.

SLIPPERY ROCK BOROUGH POLICE PENSION PLAN
FINDINGS AND RECOMMENDATIONS

Finding No. 1 – (Continued)

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

Auditor’s Conclusion: Compliance will be subject to verification through our next audit.

Finding No. 2 – Pension Benefit Not In Compliance With Act 600 Provisions

Condition: The pension plan’s governing document, Ordinance No. 590-RSTUV, effective January 1, 2014, contains a service-related disability benefit provision that is not in compliance with Act 600 as illustrated below:

<u>Benefit Provision</u>	<u>Governing Document</u>	<u>Act 600 (as amended)</u>
Service-related disability benefit	A benefit of 50% of final 36 month average compensation as of the disability date multiplied by the ratio of completed years of service at the disability date to the total years of service the member would have attained at normal retirement age. (Section 5.02)	The benefit must be in conformity with a uniform scale and fixed by the plan’s governing document at no less than 50% of the member’s salary at the time the disability was incurred.

Criteria: A governing document which contains clearly defined and updated benefit provisions is a prerequisite for the consistent, sound administration of retirement benefits. In addition, the police pension plan’s benefit structure should be in compliance with Act 600, as amended.

Cause: Plan officials failed to establish adequate internal control procedures to ensure the plan’s service-related disability benefit provision contained in the amended ordinance is in compliance with Act 600, as amended.

Effect: Maintaining a benefit structure which is not in compliance with Act 600 could result in plan members or their beneficiaries receiving incorrect benefit amounts.

SLIPPERY ROCK BOROUGH POLICE PENSION PLAN
FINDINGS AND RECOMMENDATIONS

Finding No. 2 – (Continued)

Recommendation: We recommend that plan officials take whatever action is necessary to bring the police pension plan's benefit structure into compliance with Act 600, as amended, at their earliest opportunity to do so.

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

Auditor's Conclusion: Compliance will be subject to verification through our next audit.

SLIPPERY ROCK 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, 2009, is as follows:

	(1)	(2)	(3)	(4)	(5)	(6)
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)	Covered Payroll (c)	Unfunded (Assets in Excess of) Actuarial Accrued Liability as a % of Payroll [(b-a)/(c)]
01-01-09	\$ 1,389,296	\$ 1,279,253	\$ (110,043)	108.6%	\$ 265,526	(41.4%)
01-01-11	1,559,455	1,539,628	(19,827)	101.3%	137,771	(14.4%)
01-01-13	1,672,751	1,628,964	(43,787)	102.7%	114,114	(38.4%)

Note: The market values of the plan's assets at 01-01-09, 01-01-11 and 01-01-13, have been adjusted to reflect the smoothing of gains and/or losses over a 3-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.

SLIPPERY ROCK 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.

Trends in unfunded (assets in excess of) actuarial accrued liability and annual covered payroll are both affected by inflation. Expressing the unfunded (assets in excess of) actuarial accrued liability as a percentage of annual covered payroll (Column 6) approximately adjusts for the effects of inflation and aids analysis of the plan's progress made in accumulating sufficient assets to pay benefits when due. Generally, where there is an unfunded actuarial accrued liability, the smaller this percentage, the stronger the plan. When assets are in excess of the actuarial accrued liability, the higher the bracketed percentage, the stronger the plan.

SLIPPERY ROCK 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
2008	None	N/A
2009	None	N/A
2010	None	N/A
2011	\$ 19,688	127.4%
2012	10,663	299.9%
2013	29,165	100.0%

SLIPPERY ROCK BOROUGH POLICE PENSION PLAN
SUPPLEMENTARY INFORMATION
NOTES TO SUPPLEMENTARY SCHEDULES
(UNAUDITED)

The information presented in the required 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, 2013
Actuarial cost method	Entry age normal
Amortization method	N/A
Remaining amortization period	N/A
Asset valuation method	Fair value, 3-year smoothing
Actuarial assumptions:	
Investment rate of return	7.0%
Projected salary increases	4.5%
Cost-of-living adjustments	3.0%

SLIPPERY ROCK BOROUGH POLICE PENSION PLAN
REPORT DISTRIBUTION LIST

This report was initially distributed to the following:

The Honorable Tom Corbett
Governor
Commonwealth of Pennsylvania

Slippery Rock Borough Police Pension Plan
Butler County
306 East Water Street
Slippery Rock, PA 16057

The Honorable Ronald Fodor	Mayor
Mr. David K. Miller	Council President
Ms. Lucinda G. Lipko	Borough Administrator

This report is a matter of public record and is available online at www.auditorgen.state.pa.us. Media questions about the report can be directed to the Pennsylvania Department of the Auditor General, Office of Communications, 231 Finance Building, Harrisburg, PA 17120; via email to: news@auditorgen.state.pa.us.