



**AVALON BOROUGH POLICE
PENSION PLAN**

ALLEGHENY COUNTY

COMPLIANCE AUDIT REPORT

FOR THE PERIOD

JANUARY 1, 2011 TO DECEMBER 31, 2013

COMMONWEALTH OF PENNSYLVANIA

EUGENE A. DEPASQUALE - AUDITOR GENERAL

DEPARTMENT OF THE AUDITOR GENERAL



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**EUGENE A. DePASQUALE
AUDITOR GENERAL**

The Honorable Mayor and Borough Council
Avalon Borough
Allegheny County
Pittsburgh, PA 15202

We have conducted a compliance audit of the Avalon 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 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. 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 the special ad hoc postretirement adjustment granted to eligible pensioners is in accordance with applicable laws and regulations and whether the ad hoc reimbursement received by the municipality was treated in accordance with applicable laws and regulations.

Avalon Borough contracted with an independent certified public accounting firm for audits of its basic financial statements for the years ended December 31, 2011 and 2012 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 Avalon 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, 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 tests indicated that, in all significant respects, the Avalon 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:

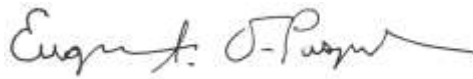
- Finding No. 1 – Noncompliance With Prior Audit Recommendation - Excess Pension Payments
- Finding No. 2 – Noncompliance With Prior Audit Recommendation - Pension Benefit Not Authorized By The Plan's Governing Document

Finding No. 3 – Partial Compliance With Prior Audit Recommendation -
Failure To Fully Pay The Minimum Municipal Obligation Of
The Plan

The findings contained in this audit report repeat conditions that were cited in our previous audit report that have not been corrected by borough officials. We are concerned by the borough's failure to correct those previously reported audit findings and strongly encourage timely implementation of the recommendations 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 Avalon 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.



EUGENE A. DEPASQUALE
Auditor General

May 21, 2014

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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 Avalon 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 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 Avalon Borough Police Pension Plan is a single-employer defined benefit pension plan locally controlled by the provisions of Ordinance No. 1293, 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 March 7, 1958. Active members are required to contribute 5 percent of compensation to the plan. As of December 31, 2013, the plan had 6 active members, no terminated members eligible for vested benefits in the future and 6 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 55 and 25 years of service.

Early Retirement 20 years of service.

Vesting 100% after 12 years of service.

Retirement Benefit:

50% of gross pay averaged over the last 36 months of employment, plus a service increment of \$100 per month 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:

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

AVALON BOROUGH POLICE PENSION PLAN
STATUS OF PRIOR FINDINGS

Compliance With Prior Audit Recommendation

Avalon Borough has complied with the prior audit recommendation concerning the following:

- Failure To Pay Benefits To Surviving Spouse

The surviving spouse was paid a lump-sum of \$56,614 for retroactive pension payments due. In addition, the borough commenced paying monthly benefit payments to the surviving spouse.

Partial Compliance With Prior Audit Recommendation

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

- Failure To Fully Pay the Minimum Municipal Obligation Of The Plan

The borough paid the balance of the 2009 minimum municipal obligation due to the police pension plan in accordance with the provisions of Act 205; however, during the current audit period, the 2012 minimum municipal obligation was not fully paid as further discussed in the Findings and Recommendations section of this report.

Noncompliance With Prior Audit Recommendations

Avalon Borough has not complied with the prior audit recommendations concerning the following as further discussed in the Findings and Recommendations section of this report:

- Excess Pension Payments

- Pension Benefit Not Authorized By The Plan's Governing Document

AVALON BOROUGH POLICE PENSION PLAN
FINDINGS AND RECOMMENDATIONS

Finding No. 1 - Noncompliance With Prior Audit Recommendation – Excess Pension Payments

Condition: As disclosed in the prior audit report, the police pension plan paid duplicate monthly pension benefits to 5 retirees in October of 2005.

Criteria: According to the plan’s governing ordinance, retired members are entitled to receive a benefit paid monthly in an amount equal to 50 percent of the member’s final monthly average salary and shall be payable the first day of each month.

Cause: Plan officials failed to establish adequate internal control procedures to ensure compliance with the prior audit recommendation.

Effect: The 5 retirees received excess pension benefits totaling \$8,506. In addition, these funds have not been available for investment purposes, for the payment of authorized benefits or to pay administrative expenses of the plan.

Recommendation: We again recommend that municipal officials review this finding with their solicitor to determine the appropriate course of action to ensure the plan is reimbursed for the duplicate pension benefits paid from the plan, plus appropriate interest.

Management’s Response: Municipal officials agreed with the finding without exception. Municipal officials stated that appropriate action to reimburse the police pension plan will be taken once the plan’s actuary has prepared a calculation to determine the amount of interest.

Auditor’s Conclusion: We are concerned that the municipality has not complied with the prior audit recommendation and encourage compliance at the earliest opportunity to do so.

Finding No. 2 - Noncompliance With Prior Audit Recommendation – Pension Benefit Not Authorized By The Plan’s Governing Document

Condition: As disclosed in the prior audit report, municipal officials provided a \$500 per month service increment benefit to a member who retired on October 1, 2010, with over 33 years of service. While Act 600 does allow for a \$500 monthly service increment for members with at least 30 years of service, the plan’s governing document only provides for a \$100 service increment benefit.

AVALON BOROUGH POLICE PENSION PLAN
FINDINGS AND RECOMMENDATIONS

Finding No. 2 – (Continued)

Criteria: Section 4.06 of the pension plan’s governing document, Ordinance No. 1293, states, in part:

Such Service Increment shall be an amount equal to one-hundred dollars (100.00), and shall be paid monthly in addition to the amount of Normal Retirement Benefit calculated pursuant to section 4.02.

In addition, the collective bargaining agreement between the borough and its police officers, at Article 10, provides for a service increment of \$100 per month after 26 full years of service.

Cause: Municipal officials failed to establish adequate internal control procedures to ensure compliance with the service increment provision contained in the plan’s governing document and to ensure compliance with the prior audit recommendation.

Effect: The plan is paying pension benefits to a retiree in excess of those authorized by the plan’s governing document. The retiree is receiving excess benefits of \$400 per month, which totaled approximately \$17,200 from the date of retirement through the date of the audit report.

Providing unauthorized pension benefits increases the plan’s pension costs and reduces the amount of funds available for investment purposes or for the payment of authorized benefits or administrative expenses. Since the borough receive state aid based on unit value during the current audit period, it did not receive allocations attributable to the excess pension benefits provided. However, the increased costs to the pension plan as a result of the excess pension benefits could result in the receipt of excess state aid in the future and increase the municipal contributions necessary to fund the plan in accordance with Act 205 funding standards.

Recommendation: We again recommend that the pension benefit of any retiree whose benefit was not determined in accordance with the provisions of the plan’s governing document be adjusted prospectively. In addition, any excess benefit payments made from the plan will be deemed ineligible for funding with state aid. Accordingly, the pension plan’s actuary may be required to determine the impact, if any, of the excess benefit payments on the borough’s future state aid allocations and submit this information to the department. If it is determined the excess benefit payments had an impact on the borough’s future state aid allocations after the submission of this information, the plan’s actuary would then be required to contact the Department to verify the overpayment of state aid received. Plan officials would then be required to reimburse the overpayment to the Commonwealth.

AVALON BOROUGH POLICE PENSION PLAN
FINDINGS AND RECOMMENDATIONS

Finding No. 2 – (Continued)

We further recommend that future service increment benefits be determined and paid in accordance with the applicable provisions contained in the plan’s governing document in effect at the time of a plan member’s retirement.

Management’s Response: Municipal officials indicated they would provide a written response to this finding, however no response was received.

Auditor’s Conclusion: We are concerned that the municipality has not complied with the prior audit recommendation and encourage compliance at the earliest opportunity to do so.

Finding No. 3 – Partial Compliance With Prior Audit Recommendation - Failure To Fully Pay The Minimum Municipal Obligation Of The Plan

Condition: As disclosed in the prior audit report, the borough did not pay the full amount of the minimum municipal obligation (MMO) that was due to the police pension plan for 2009. On December 31, 2012, the borough paid the balance of the MMO due to the plan for 2009, with applicable interest.

However, during the current audit period, the borough did not fully pay the 2012 MMO that was due to the police pension plan. The borough had an unpaid MMO balance of \$33,000 for the year 2012.

Criteria: With regard to the MMO, Section 302(c) of Act 205 states, in part:

Annually, the chief administrative officer of the pension plan shall determine the minimum obligation of the municipality with respect to the pension plan for the following plan year.

Section 302(d) of Act 205 states, in part:

The minimum obligation of the municipality shall be payable to the pension plan from the revenue of the municipality.

AVALON BOROUGH POLICE PENSION PLAN
FINDINGS AND RECOMMENDATIONS

Finding No. 3 – (Continued)

Furthermore, Section 302(e) of Act 205 states:

Any amount of the minimum obligation of the municipality which remains unpaid as of December 31 of the year in which the minimum obligation is due shall be added to the minimum obligation of the municipality for the following year, with interest from January 1 of the year in which the minimum obligation was first due until the date the payment is paid at a rate equal to the interest assumption used for the actuarial valuation report or the discount rate applicable to treasury bills issued by the Department of Treasury of the United States with a six-month maturity as of the last business day in December of the plan year in which the obligation was due, whichever is greater, expressed as a monthly rate and compounded monthly.

Cause: Plan officials failed to establish adequate internal control procedures to ensure full compliance with the prior audit recommendation.

Effect: The failure to fully pay the MMO could result in the plan not having adequate resources to meet current and future benefit obligations to its members.

Due to the municipality's failure to fully pay the 2012 MMO by the December 31, 2012, deadline, the municipality must add the 2012 MMO balance to the current year's MMO and include interest, as required by Act 205.

Recommendation: We recommend that the municipality pay the balance of the 2012 MMO due to the police pension plan, with interest, in accordance with Section 302(e) of Act 205. A copy of the interest calculation must be maintained by the borough for examination during our next audit of the plan.

Furthermore, we recommend that plan officials establish adequate internal control procedures to ensure that future MMOs are fully paid in accordance with Act 205 requirements.

Management's Response: Municipal officials agreed with the finding without exception. Municipal officials stated that appropriate action to deposit the remaining balance for the MMO due to the police pension plan will be taken once the plan's actuary has prepared a calculation to determine the amount of interest.

Auditor's Conclusion: We are concerned that the municipality has not fully complied with the prior audit recommendation and encourage compliance at the earliest opportunity to do so.

AVALON 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	\$ 1,516,590	\$ 1,926,461	\$ 409,871	78.7%	\$ 424,415	96.6%
01-01-11	1,619,506	1,874,734	255,228	86.4%	415,253	61.5%
01-01-13	1,624,661	2,219,245	594,584	73.2%	389,145	152.8%

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 4-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.

AVALON 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.

AVALON 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	\$ 71,132	100.0%
2009	54,758	100.0%
2010	58,746	100.0%
2011	88,000	100.0%
2012	95,731	65.5%
2013	117,582	100.0%

AVALON 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, 2011
Actuarial cost method	Entry age normal
Amortization method	Level dollar, closed
Remaining amortization period	11 years
Asset valuation method	Fair value, 4-year smoothing
Actuarial assumptions:	
Investment rate of return	7.0%
Projected salary increases *	5.0%

* Includes inflation at 3.0%

AVALON BOROUGH POLICE PENSION PLAN
REPORT DISTRIBUTION LIST

This report was initially distributed to the following:

The Honorable Tom Corbett
Governor
Commonwealth of Pennsylvania

Avalon Borough Police Pension Plan
Allegheny County
640 California Avenue
Pittsburgh, PA 15202

The Honorable David C. Haslett Mayor

Mr. Joshua Klicker Council President

Mr. Ralph Cortese Councilman

Mr. Harry W. Dilmore Borough Manager

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