



**ELLWOOD CITY BOROUGH POLICE  
PENSION PLAN**

**LAWRENCE COUNTY**

**COMPLIANCE AUDIT REPORT**

**FOR THE PERIOD**

**JANUARY 1, 2010, TO DECEMBER 31, 2012**

**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  
Ellwood City Borough  
Lawrence County  
Ellwood City, PA 16117

We have conducted a compliance audit of the Ellwood City Borough Police Pension Plan for the period January 1, 2010, to December 31, 2012. 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.
- Whether refunds are made to eligible members in accordance with the plan provisions and applicable laws and regulations.
- Whether disability/killed-in-service insurance premiums are proper and in accordance with plan provisions and applicable laws, regulations, and policies.
- Whether Deferred Retirement Option Plan (DROP) participants' benefit payments are properly determined in accordance with the provisions of the DROP and any other applicable laws and regulations.

Ellwood City Borough contracted with an independent certified public accounting firm for audits of its basic financial statements for the years ended December 31, 2010 and 2011, and an audit 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 for the year ended December 31, 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 Ellwood City 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.

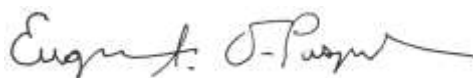
The results of our tests indicated that, in all significant respects, the Ellwood City Borough Police Pension Plan was administered in compliance with applicable state laws, regulations, contracts, administrative procedures, and local ordinances and policies, except as noted in the following findings further discussed later in this report:

Finding No. 1 – Noncompliance With Prior Audit Recommendation - Pension Benefit Not Authorized By Act 600

Finding No. 2 – Noncompliance With Prior Audit Recommendation – Unauthorized Disability Benefit Provision

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 Ellwood City Borough and, where appropriate, their responses have been included in the report.



EUGENE A. DEPASQUALE  
Auditor General

August 21, 2013

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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 Ellwood City 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 Ellwood City Borough Police Pension Plan is a single-employer defined benefit pension plan locally controlled by the provisions of Chapter 294 of the borough's codified ordinances. The plan is also affected by the provisions of collective bargaining agreements between the borough and its police officers. As of December 31, 2012, the plan had 10 active members, 1 terminated member eligible for vested benefits in the future and 18 retirees receiving pension benefits.

ELLWOOD CITY BOROUGH POLICE PENSION PLAN  
STATUS OF PRIOR FINDINGS

Noncompliance With Prior Audit Recommendations

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

- Pension Benefit Not Authorized By Act 600
- Unauthorized Disability Benefit Provison

ELLWOOD CITY BOROUGH POLICE PENSION PLAN  
FINDINGS AND RECOMMENDATIONS

Finding No. 1 - Noncompliance With Prior Audit Recommendation - Pension Benefit Not  
Authorized By Act 600

Condition: As disclosed in the prior audit report, Chapter 294 of the borough's codified ordinances grants a benefit that is not authorized by Act 600. Section 294.01(18) states:

“Final monthly average salary” means the average monthly salary earned by the participant and paid by the employer during the final thirty-six months immediately preceding termination of active employment. Salary shall include payments made for unused vacation, earned vacation (calculated from employee's anniversary date to the date of retirement), unused personal days, longevity (based on years of service at the time of retirement), accumulated unused sick leave (in accordance with the maximum allowed under the police contract), holiday pay (based on the number of holidays beginning with January 1 of the current year to the date of retirement at the rate of pay stated in the police contract).

In addition, the collective bargaining agreements (CBAs) covering the periods January 1, 2006, to December 31, 2008, and January 1, 2009, to December 31, 2012, provide for the payment of accumulated unused sick leave up to a maximum of 250 days, which given the definition of salary contained in the plan's governing document could result in pension benefit determinations in excess of Act 600 provisions.

Criteria: Section 5(c) of Act 600 states, in part:

Monthly pension or retirement benefits other than length of service increments shall be computed at one-half the monthly average salary of such member during not more than the last sixty nor less than the last thirty-six months of employment.

Although Act 600 does not define “salary,” the department has concluded, based on a line of court opinions, that the term does not encompass lump-sum payments for leave that was not earned during the pension computation period.

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

Effect: The plan is paying pension benefits to two retirees in excess of those authorized by Act 600. The retirees are receiving excess benefits of \$539 per month, which have totaled approximately \$40,490 from the dates of their respective retirements through the conclusion of our audit fieldwork procedures.



## ELLWOOD CITY BOROUGH POLICE PENSION PLAN FINDINGS AND RECOMMENDATIONS

### Finding No. 1 – (Continued)

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 received 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 borough amend the plan's governing document to ensure that all future pension benefits are determined in compliance with Act 600 at its earliest opportunity to do so. To the extent that the borough is not in compliance with Act 600 and/or is contractually obligated to pay benefits to existing retirees in excess of those authorized by Act 600, the excess benefits must be reflected in the Act 205 actuarial valuation reports for the plan and funded in accordance with Act 205 funding standards. Furthermore, such benefits will be deemed ineligible for funding with state pension aid. In such case, the plan's actuary may be required to determine the impact, if any, of the excess benefits on the borough's future state aid allocations and submit this information to the Department. If it is determined the excess benefits 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.

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

Auditor's Conclusion: We are concerned by the borough's failure to correct this previously reported audit finding and strongly encourage timely implementation of the recommendation contained in this audit report.

ELLWOOD CITY BOROUGH POLICE PENSION PLAN  
FINDINGS AND RECOMMENDATIONS

Finding No. 2 – Noncompliance With Prior Audit Recommendation – Unauthorized Disability Benefit Provision

Condition: As disclosed in the prior audit report, the collective bargaining agreement (CBA) between the police officers and the borough contains a disability benefit provision that is not in compliance with Act 600. The collective bargaining agreement states:

Police officers retiring due to disability shall receive annual COLA adjustments regardless of the total percentage increase of his pension benefit or Final Average Salary. There shall be no Social Security Offset or Worker's Compensation offset applied to any retiree.

Criteria: Act 600 at Section 5(g)(1), states:

The ordinance or resolution establishing the police pension fund may provide for a cost of living increase for members of the police force receiving retirement benefits. The cost of living increase shall not exceed the percentage increase in the Consumer Price Index from the year in which the police member last worked, shall not cause the total police pension benefits to exceed seventy-five per centum of the salary for computing retirement benefits and shall not cause the total cost of living increase to exceed thirty per centum. No cost of living increase shall be granted which would impair the actuarial soundness of the pension fund.

Therefore, Act 600 does not provide any exceptions that cost-of-living adjustments (COLAs) for disability pension benefits can exceed authorized limitations.

In addition, Act 600 at Section 5(e)(1), states:

In the case of the payment of pensions for permanent injuries incurred in service, the amount and commencement of the payments shall be fixed by regulations of the governing body of the borough, town, township or regional police department and shall be calculated at a rate no less than fifty per centum of the member's salary at the time the disability was incurred, provided that any member who receives benefits for the same injuries under the Social Security Act (49 Stat. 620, 42 U.S.C. § 301 et. seq.) shall have his disability benefits offset or reduced by the amount of such benefits. (Emphasis added)

ELLWOOD CITY BOROUGH POLICE PENSION PLAN  
FINDINGS AND RECOMMENDATIONS

Finding No. 2 – (Continued)

Cause: The disability benefit provision contained in the CBA is subject to the collective bargaining process.

Effect: The unauthorized benefit provision could result in improper benefit calculations and excess payments from the pension plan.

Recommendation: We again recommend that municipal officials take appropriate action to ensure that the CBA contains a disability benefit provision that is in compliance with Act 600 at their earliest opportunity to do so.

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

Auditor's Conclusion: We are concerned by the borough's failure to correct this previously reported audit finding and strongly encourage timely implementation of the recommendation contained in this audit report.

ELLWOOD CITY 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, 2007, 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)]
01-01-07	\$ 5,559,416	\$ 5,747,878	\$ 188,462	96.7%	\$ 885,549	21.3%
01-01-09	5,459,637	6,394,396	934,759	85.4%	803,518	116.3%
01-01-11	5,888,028	6,903,443	1,015,415	85.3%	746,448	136.0%

Note: The market value of the plan's assets at 01-01-09 has been adjusted to reflect the smoothing of gains and/or losses at 130 percent of market value. The actuarial value of the plan's assets 01-01-11 represents an adjusted market value computed by the plan's actuary. These methods 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.

ELLWOOD CITY 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.

ELLWOOD CITY 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
2007	\$ 223,143	100.0%
2008	133,092	100.0%
2009	144,506	100.0%
2010	136,078	100.0%
2011	266,559	100.0%
2012	275,007	100.0%

ELLWOOD CITY 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	6 years
Asset valuation method	Plan assets are valued using the method described at Section 210 of Act 205.
Actuarial assumptions:	
Investment rate of return	8.0%
Projected salary increases *	5.5%

\* Includes inflation at 4.0%

ELLWOOD CITY BOROUGH POLICE PENSION PLAN  
REPORT DISTRIBUTION LIST

This report was initially distributed to the following:

The Honorable Tom Corbett  
Governor  
Commonwealth of Pennsylvania

Ellwood City Borough Police Pension Plan  
Lawrence County  
525 Lawrence Avenue  
Ellwood City, PA 16117

The Honorable Anthony J. Court	Mayor
Mr. Anthony DeCarbo	Council President
Mr. Domenic A. Viccari	Borough Manager
Ms. Linda M. List	Borough Secretary

This report is a matter of public record and is available online at [www.auditorgen.state.pa.us](http://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](mailto:news@auditorgen.state.pa.us).