



**NESQUEHONING BOROUGH POLICE
PENSION PLAN**

CARBON 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



Commonwealth of Pennsylvania
Department of the Auditor General
Harrisburg, PA 17120-0018
Facebook: Pennsylvania Auditor General
Twitter: @PAAuditorGen

EUGENE A. DePASQUALE
AUDITOR GENERAL

The Honorable Mayor and Borough Council
Nesquehoning Borough
Carbon County
Nesquehoning, PA 18240

We have conducted a compliance audit of the Nesquehoning 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 conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our 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 benefit payments have only been made to living recipients, based on the Social Security numbers found in the pension records for retirees and beneficiaries.

Nesquehoning Borough contracted with an independent certified public accounting firm for annual audits of its basic financial statements 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 Nesquehoning 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 Nesquehoning 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 – Noncompliance With Prior Audit Recommendation – Improper Disposition
Of Insurance Policy

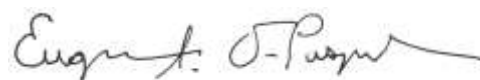
As previously noted, one of the objectives of our audit of the Nesquehoning Borough Police Pension Plan was to determine compliance with applicable state laws, regulations, contracts, administrative procedures, and local ordinances and policies. Act 205 was amended on September 18, 2009, through the adoption of Act 44 of 2009. Among several provisions relating to municipal pension plans, the act provides for the implementation of a distress recovery program. Three levels of distress have been established:

<u>Level</u>	<u>Indication</u>	<u>Funding Criteria</u>
I	Minimal distress	70-89%
II	Moderate distress	50-69%
III	Severe distress	Less than 50%

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. However, we are extremely concerned about the funded status of the plan contained in the schedule of funding progress included in this report which indicates the plan's funded ratio is 56.4% as of January 1, 2011, which is the most recent date available. Based on this information, the Public Employee Retirement Commission issued a notification that the borough is currently in Level II moderate distress status. We encourage borough officials to monitor the funding of the police pension plan to ensure its long-term financial stability.

The contents of this report were discussed with officials of Nesquehoning 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 4, 2013



EUGENE A. DEPASQUALE
Auditor General

CONTENTS

	<u>Page</u>
Background.....	1
Status of Prior Findings	2
Finding and Recommendation:	
Finding – Noncompliance With Prior Audit Recommendation – Improper Disposition Of Insurance Policy	3
Supplementary Information	4
Report Distribution List	8

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 Nesquehoning 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 Nesquehoning Borough Police Pension Plan is a single-employer defined benefit pension plan locally controlled by the provisions of Ordinance No. 2-1976, 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. As of December 31, 2012, the plan had 4 active members, no terminated members eligible for vested benefits in the future and 4 retirees receiving pension benefits.

NESQUEHONING BOROUGH POLICE PENSION PLAN
STATUS OF PRIOR FINDINGS

Compliance With Prior Audit Recommendation

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

- Incorrect Data On Certification Form AG 385 Resulting In An Overpayment Of State Aid

The borough reimbursed \$14,190 to the Commonwealth for the overpayment of state aid received.

Noncompliance With Prior Audit Recommendation

Nesquehoning Borough has not complied with the prior audit recommendation concerning the following as further discussed in the Finding and Recommendation section of this report:

- Improper Disposition Of Insurance Policy

NESQUEHONING BOROUGH POLICE PENSION PLAN
FINDING AND RECOMMENDATION

Finding - Noncompliance With Prior Audit Recommendation – Improper Disposition Of Insurance Policy

Condition: As disclosed in the prior audit report, the municipality did not cash surrender and deposit the proceeds of an insurance policy into the pension plan that was maintained to fund pension benefits for a retired member. The plan member retired on January 1, 2001, and began receiving a retirement benefit \$2,590 per month in accordance with the plan's governing document. The insurance policy matured on June 7, 2008, and the retired member began receiving an additional pension benefit of approximately \$168 per month, instead of the proceeds being properly deposited into the pension plan to fund future benefit payments to the retiree.

Criteria: The municipality should have cash surrendered the insurance policy maintained for the retired member of the plan and deposited the proceeds into the pension plan to help fund the retiree's future monthly pension benefits.

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

Effect: The retiree is receiving excess pension benefits of \$168 per month.

Recommendation: In light of the plan's funded status that was previously referred to in this audit report, we again recommend that the municipality reduce the retiree's monthly pension benefit by \$168 per month at their earliest opportunity to do so to ensure that the retiree is only receiving the benefit that he is entitled to in accordance with the plan's governing document.

Management Response: Plan officials discussed the matter with the borough's solicitor. The borough solicitor was aware of the situation, but thought that the matter had been resolved. Plan officials further indicated that an additional response will be provided upon receipt of the audit report.

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.

NESQUEHONING 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	\$ 552,565	\$ 1,164,535	\$ 611,970	47.4%	\$ 178,110	343.6%
01-01-09	577,061	1,223,011	645,950	47.2%	227,066	284.5%
01-01-11	708,757	1,256,735	547,978	56.4%	260,389	210.5%

Note: The market value of the plan's assets at 01-01-07, 01-01-09 and 01-01-11, has been adjusted to reflect the smoothing of gains and/or losses over a 5-year averaging period. In no event is the actuarial value of assets allowed to be greater than 120% or less than 80% of market value. 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.

NESQUEHONING 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.

NESQUEHONING 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	\$ 103,253	100.0%
2008	124,087	100.0%
2009	127,931	100.0%
2010	130,460	101.9%
2011	145,295	100.0%
2012	141,980	100.0%

NESQUEHONING 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
Remaining amortization period	7 years
Asset valuation method	5-year smoothing, subject to 80%-120% of the market value of assets.
Actuarial assumptions:	
Investment rate of return	8.0%
Projected salary increases	5.0%

NESQUEHONING BOROUGH POLICE PENSION PLAN
REPORT DISTRIBUTION LIST

This report was initially distributed to the following:

The Honorable Tom Corbett
Governor
Commonwealth of Pennsylvania

Nesquehoning Borough Police Pension Plan
Carbon County
114 West Catawissa Street
Nesquehoning, PA 18240

The Honorable K. Tony Walck	Mayor
Mr. Frank Jacobs	Council President
Ms. RoniSue Ahner	Chief Administrative Officer

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.