

COMPLIANCE AUDIT

Shenandoah Borough Police Pension Plan Schuylkill County, Pennsylvania For the Period January 1, 2015 to December 31, 2018

November 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
Shenandoah Borough
Schuylkill County
Shenandoah, PA 17976

We have conducted a compliance audit of the Shenandoah Borough Police Pension Plan for the period January 1, 2015 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 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. To determine if municipal officials took appropriate corrective action to address the finding contained in our prior audit report, we inquired of plan officials and evaluated supporting documentation provided by officials evidencing that the suggested corrective action has been appropriately taken. 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 benefits 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, 2015 and January 1, 2017 actuarial valuation reports were prepared and submitted by March 31, 2016 and 2018, respectively, in accordance with Act 205 and whether 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 by comparing selected information to supporting source documentation.
- We determined whether all annual special ad hoc postretirement reimbursements received by the municipality were authorized and appropriately deposited in accordance with Act 147 by tracing information to supporting documentation maintained by plan officials.
- We determined whether transfers were properly authorized, timely, and appropriately recorded by plan officials by examining supporting documentation for the transfers made during the audit period.

Borough officials are responsible for establishing and maintaining effective internal controls to provide reasonable assurance that the Shenandoah 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 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 objectives.

The results of our procedures indicated that, in all significant respects, the Shenandoah 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 – Partial Compliance With Prior Recommendation - Failure To Timely Pay
The Minimum Municipal Obligation Of The Plan

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 Shenandoah 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.

October 31, 2019



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 Shenandoah 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 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. § 767 et seq.

The Shenandoah Borough Police Pension Plan is a single-employer defined benefit pension plan locally controlled by the provisions of an Ordinance dated May 4, 1970, 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 15, 1958. Active members are required to contribute 5 percent of compensation to the plan. As of December 31, 2018, the plan had 5 active members, 3 terminated members eligible for vested benefits in the future, and 9 retirees receiving pension benefits.

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.
Early Retirement	None
Vesting	100% vesting available after 12 years of service.

Retirement Benefit:

Benefit equals 50% of final 36 months average compensation, plus a service increment of \$100 per month after 26 years of service.

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.

SHENANDOAH BOROUGH POLICE PENSION PLAN
STATUS OF PRIOR FINDINGS

Partial Compliance With Prior Audit Recommendation

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

- Failure To Fully Pay The Minimum Municipal Obligation (MMO) Of The Plan

The borough paid the outstanding balances due to the plan for the years 2013 and 2014 plus interest. However, a similar condition occurred during the current audit period as disclosed in the finding contained in this report.

Status Of Prior Audit Recommendations

As disclosed in the two prior audit reports, the police pension plan was paying cost-of-living adjustments to retired plan members in excess of the 30 percent threshold provided by Act 600. Subsequent to the current audit period, municipal officials took appropriate action to limit cost of living increases to future retirees in accordance with Act 600 through the collective bargaining process. However, four existing retirees continue to receive excess cost-of-living adjustments, which amounted to \$38,780 during our current audit period and up to the date of this report. Since the borough received state aid based on unit value during the audit period, it did not receive state aid attributable to the excess cost-of-living adjustments. The Department will continue to monitor the effect of the excess benefits being paid to existing retirees on the borough's future state aid allocations.

SHENANDOAH BOROUGH POLICE PENSION PLAN
FINDING AND RECOMMENDATION

**Finding – Partial Compliance With Prior Audit Recommendation - Failure To Timely Pay
The Minimum Municipal Obligation (MMO) Of The Plan**

Condition: As disclosed in the Status of Prior Finding section of this report, the borough partially complied with the prior recommendation by depositing the outstanding MMO balances due to the plan for the years 2013 and 2014, which included interest. However, a similar condition occurred during the current audit period. Plan officials failed to timely pay the entire 2015, 2016 and 2017 MMOs by their respective December 31 deadlines, as required by Act 205. The borough had an unpaid 2015 MMO of \$40,045 at December 31, 2015, an unpaid 2016 MMO of \$52,652 at December 31, 2016, and an unpaid 2017 MMO of \$56,524 at December 31, 2017. Although the borough ultimately paid the outstanding 2015 MMO balance on October 24, 2016, the outstanding 2016 MMO balance through payments made during 2017 and the outstanding 2017 MMO balance through payments made during 2018, the borough failed to include interest on these late MMO payments in accordance with Act 205.

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. Payment of the minimum obligation of the municipality shall be made by the municipality prior to December 31.

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.

SHENANDOAH BOROUGH POLICE PENSION PLAN
FINDING AND RECOMMENDATION

Finding – (Continued)

Cause: The borough did not have sufficient financial resources necessary to timely fund the MMOs of its pension plan along with the required interest in accordance with Act 205 and to ensure compliance with this department’s prior audit recommendation.

Effect: Due to the municipality’s failure to pay the 2015, 2016 and 2017 MMOs by their respective December 31 deadlines, the borough incurred interest penalties under Act 205 that would not have otherwise been required had the MMOs been timely paid. Since the interest has not yet been paid, the plan has not been adequately compensated for the municipality’s failure to deposit the MMOs timely in accordance with Act 205 requirements.

Recommendation: We recommend that the municipality calculate and pay the interest due to the police pension plan for the untimely payments of the 2015, 2016 and 2017 MMOs 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.

We also again recommend that plan officials implement internal control procedures to ensure that future MMOs are paid by their respective deadlines, or that payments made after such deadlines include appropriate interest in accordance with Act 205 requirements.

Management’s Response: Municipal officials disagreed with the recommendation and indicated that they feel that the payment made on December 30, 2016 in the amount of \$15,000 was enough to cover the interest for the late payments of the MMOs.

Auditor’s Conclusion: Based on the documentation provided, it was noted that the payment made on December 30, 2016 in the amount of \$15,000 was enough to pay the outstanding MMO amounts due for the plan years 2013 and 2014 and the applicable interest owed to the plan due to the late payment as previously recommended in the prior audit finding. Therefore, the finding remains as stated. Compliance will be evaluated during our next audit of the plan.

SHENANDOAH 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	\$ 1,553,867	\$ 2,236,153	\$ 682,236	69.5%
01-01-15	1,647,400	2,332,095	684,695	70.6%
01-01-17	1,714,310	2,113,041	398,731	81.1%

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.

SHENANDOAH 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.

SHENANDOAH 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
2013	\$ 116,024	100.0%
2014	94,674	100.0%
2015	94,541	100.0%
2016	95,725	100.0%
2017	135,637	100.0%
2018	149,261	100.0%

SHENANDOAH 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
Remaining amortization period	6 years
Asset valuation method	Fair value, 4-year smoothing
Actuarial assumptions:	
Investment rate of return	8.0%
Projected salary increases	5.0%
Cost-of-living adjustments	3.0%

SHENANDOAH BOROUGH POLICE PENSION PLAN
REPORT DISTRIBUTION LIST

This report was initially distributed to the following:

The Honorable Tom W. Wolf
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Commonwealth of Pennsylvania

The Honorable Andrew Szczyglak
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Mr. Leo Pietkiewicz
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