

# COMPLIANCE AUDIT

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## Frackville Borough Police Pension Plan Schuylkill County, Pennsylvania For the Period January 1, 2015 to December 31, 2016

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April 2018



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  
Frackville Borough  
Schuylkill County  
Frackville, PA 17931

We have conducted a compliance audit of the Frackville Borough Police Pension Plan for the period January 1, 2015 to December 31, 2016. 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 finding and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our finding 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. To determine if municipal officials took appropriate corrective action to address the findings 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 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 benefit due to the retired individual and comparing these amounts to supporting documentation evidencing amounts determined and actually paid to the recipient. We also determined whether retirement benefits calculated for the plan member who elected to vest during the current audit period, represent payments to all (and only) those entitled to receive them and were properly determined in accordance with the plan's governing document, applicable laws and regulations by recalculating the amount of the pension benefit due to the retired individual and comparing these amounts to supporting documentation evidencing amounts determined.
- We determined whether the January 1, 2013 and January 1, 2015 actuarial valuation reports were prepared and submitted to the former Public Employee Retirement Commission (PERC) by March 31, 2014 and 2016, respectively, in accordance with Act 205 and whether selected information provided on these reports are 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.

Borough officials are responsible for establishing and maintaining effective internal controls to provide reasonable assurance that the Frackville 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 Frackville 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 – Inconsistent And Unauthorized Pension Benefits
- Finding No. 2 – Noncompliance With Prior Audit Recommendation – Untimely Deposit Of State Aid

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

As previously noted, one of the objectives of our audit of the Frackville 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 53.1% as of January 1, 2015, which is the most recent data available. Based on this information, and the funded status of the borough's non-uniformed pension plan, 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 Frackville 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

March 30, 2018

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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 Frackville 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 600 - Police Pension Fund Act, Act of May 29, 1956 (P.L. 1804, No. 600), as amended, 53 P.S. § 767 et seq.

The Frackville Borough Police Pension Plan is a single-employer defined benefit pension plan locally controlled by the provisions of Ordinance No. 76-1, 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 April 7, 1964. Active members are required to contribute 3 and 4.5 percent of base salary, in 2015 and 2016, respectively, to the plan. As of December 31, 2016, the plan had 4 active members, 2 terminated members eligible for vested benefits in the future, and 9 retirees receiving pension benefits from the plan.

## **BACKGROUND – (Continued)**

As of December 31, 2016, selected plan benefit provisions are as follows:

### Eligibility Requirements:

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

### Retirement Benefit:

Benefit equals 50% of final 36 months average salary, plus a service increment of \$100 per month for participants who retire with 26 or more 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 75% of the member's salary at the time the disability was incurred, offset by Social Security disability benefits received for the same injury.

FRACKVILLE BOROUGH POLICE PENSION PLAN  
STATUS OF PRIOR FINDINGS

Noncompliance With Prior Audit Recommendations

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

- Inconsistent And Unauthorized Pension Benefits
- Untimely Deposit Of State Aid



FRACKVILLE BOROUGH POLICE PENSION PLAN  
FINDING AND RECOMMENDATION

**Finding No. 1 – Noncompliance With Prior Audit Recommendation – Inconsistent And Unauthorized Pension Benefits**

Condition: As disclosed in the prior audit report, although Borough officials adopted Ordinance No. 1-11 to bring the police pension plan’s benefit structure into compliance with Act 600, the collective bargaining agreement between the borough and members of its police department (CBA) continues to contain benefit provisions that conflict with the governing document and are not in accordance with Act 600, as noted below:

<u>Benefit Provision</u>	<u>Governing Document</u>	<u>Collective Bargaining Agreement</u>	<u>Act 600 (as amended)</u>
Service-related disability benefit	50% of the member’s salary at the time the disability was incurred, reduced by Social Security disability benefits received for the same injury.	75% of highest monthly compensation.	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, reduced by the amount of Social Security disability benefits received for the same injury.
Normal retirement age	A member who has served in the police force for an aggregate total of at least 25 years and has attained the age of 55 years.	Upon completion of 25 years of service (20 years of service when allowed by Act 600) in the municipal police force and attainment of the age of fifty (50) years old.	Each ordinance or resolution establishing a police pension fund shall prescribe a minimum period of total service in the aggregate of twenty-five years in the same borough, town, township or regional police department and shall fix the age of the members of the force at fifty-five years, or, if an actuarial study of the cost shows that such reduction in age is feasible, may fix the age of the members of the force at fifty years.

FRACKVILLE BOROUGH POLICE PENSION PLAN  
FINDING AND RECOMMENDATION

**Finding No. 1 – (Continued)**

<u>Benefit Provision</u>	<u>Governing Document</u>	<u>Collective Bargaining Agreement</u>	<u>Act 600 (as amended)</u>
Survivor's Benefit	A lifetime survivor's benefit must be provided to the surviving spouse (or if no spouse survives or if he or she subsequently dies, the child or children under 18 years of age or if attending college, under or attaining the age of 23) of no less than 50% of the pension the member was receiving or would have been entitled to receive had he been retired at the time of death.	50% of the pension that the member was receiving or would have been receiving had he been eligible and retired at the time of his death, payable to the surviving spouse until death or remarriage. Upon the death or remarriage of the surviving spouse, or if there is no surviving spouse, the benefit is payable to the surviving child or children until age 18.	A lifetime survivor's benefit must be provided to the surviving spouse (or if no spouse survives or if he or she subsequently dies, the child or children under 18 years of age or if attending college, under or attaining the age of 23) of no less than 50% of the pension the member was receiving or would have been entitled to receive had he been retired at the time of death. ("Attending college" shall mean the eligible children are registered at an accredited institution of higher learning and are carrying a minimum course load of 7 credit hours per semester.)
Killed in service	Not provided. (Repealed pursuant to Act 51 of 2009.)	A pension calculated at 100% of the member's highest monthly compensation.	Not authorized. (Repealed by Act 51 of 2009.)

In addition, the plan's January 1, 2013 and January 1, 2015 actuarial valuation reports submitted to the Public Employee Retirement Commission reported the benefit provisions included in the collective bargaining agreement.

Criteria: The plan's governing document and the collective bargaining agreement should contain consistent benefit provisions to ensure the sound administration of retirement benefits.

FRACKVILLE BOROUGH POLICE PENSION PLAN  
FINDING AND RECOMMENDATION

**Finding No. 1 – (Continued)**

Cause: Plan officials again failed to establish adequate internal control procedures to ensure the plan’s governing document and the collective bargaining agreement contained consistent benefit provisions that are in compliance with Act 600 and compliance with our prior audit recommendation.

Effect: Inconsistent plan documents could result in inconsistent or improper benefit calculations and incorrect benefit payments from the pension plan.

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 for its pension plans 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 municipal officials take appropriate action to ensure the plan’s governing document and the collective bargaining agreement contain consistent benefit provisions that are in compliance with Act 600 at their earliest opportunity to do so.

Management’s Response: Municipal officials agreed with the finding without exception. Municipal officials stated that the current CBA does not expire until December 31, 2018; however, they will work with their solicitor to ensure that the plan’s governing document and the collective bargaining agreement contain consistent benefit provisions that are in compliance with Act 600.

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.

FRACKVILLE BOROUGH POLICE PENSION PLAN  
FINDING AND RECOMMENDATION

**Finding No. 2 – Noncompliance With Prior Audit Recommendation – Untimely Deposit Of State Aid**

Condition: As disclosed in the two prior audit reports, the municipality failed to pay the interest due to the plan for the late deposits of its 2007, 2008, 2009, 2013 and 2014 state aid allocations as required by Act 205. As of our fieldwork date, the borough has not deposited interest due the plan from the late deposits.

Criteria: Section 402(g) of Act 205 states, in part:

. . . the total amount of the general municipal pension system State aid received by the municipality shall, within 30 days of receipt by the treasurer of the municipality, be deposited in the pension funds or the alternate funding mechanisms applicable to the respective pension plans.

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

Effect: Although the state aid was eventually deposited into the pension plan, the interest earned beyond the 30 day grace period was not deposited into the pension plan. When state aid is not deposited into a pension plan account in a timely manner, the funds are not available to fund benefits, pay operating expenses or for investment and the risk of misapplication is increased.

Recommendation: We again recommend that the municipality deposit the interest due to the pension plan for the untimely deposit of the state aid allocations. A copy of the interest calculation must be maintained by the borough for examination during our next audit period of the plan.

Management's Response: Municipal officials agreed with the finding without exception. Municipal officials intend to contact their actuary to calculate the interest owed on the late deposits of their 2007, 2008, 2009, 2013 and 2014 state aid allocations which amounted to \$54,509, \$44,609, \$43,792, \$46,612 and \$45,084, respectively, and will deposit the interest into the police pension plan.

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.

FRACKVILLE 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, 2011, 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)
01-01-11	\$ 1,275,899	\$ 2,178,248	\$ 902,349	58.6%
01-01-13	1,199,905	2,212,644	1,012,739	54.2%
01-01-15	1,350,577	2,542,032	1,191,455	53.1%

Note: The market values of the plan's assets at 01-01-11, 01-01-13, and 01-01-15 have been adjusted to reflect the smoothing of gains and/or losses over a 5-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.

FRACKVILLE 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.

FRACKVILLE 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
2011	\$ 123,972	100.0%
2012	126,063	100.0%
2013	162,438	101.1%
2014	156,189	100.3%
2015	165,699	100.0%
2016	172,009	100.0%

FRACKVILLE 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, 2015
Actuarial cost method	Entry age normal
Amortization method	Level dollar
Remaining amortization period	11 years
Asset valuation method	Fair value, 5-year smoothing
Actuarial assumptions:	
Investment rate of return	7.0%
Projected salary increases	5.0%
Cost-of-living adjustments	4.0% per year postretirement



FRACKVILLE BOROUGH POLICE PENSION PLAN  
REPORT DISTRIBUTION LIST

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