

COMPLIANCE AUDIT

Midland Borough Police Pension Plan Beaver County, Pennsylvania For the Period January 1, 2014 to December 31, 2017

November 2018



Commonwealth of Pennsylvania
Department of the Auditor General

Eugene A. DePasquale • Auditor General



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

EUGENE A. DePASQUALE
AUDITOR GENERAL

The Honorable Mayor and Borough Council
Midland Borough
Beaver County
Midland, PA 15059

We have conducted a compliance audit of the Midland Borough Police Pension Plan for the period January 1, 2014 to December 31, 2017. 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 the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objective. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objective.

The objective of the audit was 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 objective identified above. 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 2 plan members 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 retired individuals and comparing these amounts to supporting documentation evidencing amounts determined and actually paid to recipients.
- We determined whether the January 1, 2013, January 1, 2015, and January 1, 2017 actuarial valuation reports were prepared and submitted by March 31, 2014, 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 refunds made to plan members were authorized in accordance with plan provisions and applicable laws and regulations by testing both of the refunds disbursed to plan members during the current audit period.

Midland Borough contracted with an independent certified public accounting firm for annual audits of its basic financial statements for the years ended 2014, 2015, and 2016 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 Midland 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 objective, 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 objective.

The results of our procedures indicated that, in all significant respects, the Midland 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 – Failure To Timely File Certification Form AG 385 Resulting In An Untimely Receipt Of State Aid
- Finding No. 2 – Failure To Deposit Member Contributions
- Finding No. 3 – Failure To Maintain An Adequate Record-Keeping System

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

November 8, 2018



EUGENE A. DEPASQUALE
Auditor General

CONTENTS

	<u>Page</u>
Background.....	1
Findings and Recommendations:	
Finding No. 1 – Failure To Timely File Certification Form AG 385 Resulting In An Untimely Receipt Of State Aid.....	3
Finding No. 2 – Failure To Deposit Member Contributions.....	3
Finding No. 3 – Failure To Maintain An Adequate Record-Keeping System.....	4
Supplementary Information	6
Report Distribution List	12

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 Midland 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 Midland Borough Police Pension Plan is a single-employer defined benefit pension plan locally controlled by the provisions of Ordinance No. 683, as amended, adopted pursuant to Act 600, as amended. The plan is also affected by the provisions of collective bargaining agreements between the borough and its police officers. The plan was established December 18, 1957. Active members are required to contribute 7 percent of monthly wages to the plan. As of December 31, 2017 the plan had 2 active members, no terminated members eligible for vested benefits in the future, and 8 retirees receiving pension benefits from the plan.

BACKGROUND – (Continued)

As of December 31, 2017, selected plan benefit provisions are as follows:

Eligibility Requirements:

Normal Retirement Age 50 and 25 years of service.

Early Retirement None

Vesting None

Retirement Benefit:

Benefit equals 50% of final 36 months average earnings.

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:

The greater of 75% of the member's average monthly compensation during the last 60 months, or 50% of the member's salary at the time the disability was incurred, offset by Social Security disability benefits received for the same injury.

MIDLAND BOROUGH POLICE PENSION PLAN
FINDINGS AND RECOMMENDATIONS

Finding No. 1 – Failure To Timely File Certification Form AG 385 Resulting In An Untimely Receipt Of State Aid

Condition: The borough failed to timely file the Certification Form AG 385 in 2017 for the police and non-uniformed pension plans by the March 31, 2017 deadline. Although the borough did eventually certify accurate information for the plans, the form was not submitted to the Department of the Auditor General until March 22, 2018 and the borough did not receive its 2017 state aid allocation until April of 2018.

Criteria: The general instructions that accompany Certification Form AG 385 disclose that municipalities must complete and return the Certification Form AG 385 to the Department of the Auditor General by March 31st of the given year.

Cause: Plan officials failed to establish adequate internal control procedures to ensure the timely submission of the certification form.

Effect: The data submitted on this form is used, in part, to calculate the state aid due to the municipality for distribution to its pension plans. Although the borough received its 2017 allocation of state aid in April of 2018, the state aid was not available to be deposited timely and therefore was not available to pay operating expenses or for investment.

Recommendation: We recommend that in the future, plan officials establish adequate internal control procedures to ensure compliance with the instructions that accompany Certification Form AG 385 to assist them in timely reporting the required pension data.

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

Auditor's Conclusion: Compliance will be evaluated during our next audit of the plan.

Finding No. 2 – Failure To Deposit Member Contributions

Condition: Municipal officials failed to deposit member contributions into the pension plan for the year 2017. In addition, we were not able to determine from municipal records whether member contributions were actually deducted from employee earnings.

Criteria: The plan's governing document, Resolution No. 9149, at Section 9.06(a) states:

A Participant shall be required to make personal contributions to the Plan commencing on the date he initially becomes a Participant in an amount equal to not less than five percent (5) nor more than eight percent (8%) of his monthly wages such percentage to be established by the Council at the beginning of each Plan Year.

MIDLAND BOROUGH POLICE PENSION PLAN
FINDINGS AND RECOMMENDATIONS

Finding No. 2 – (Continued)

Cause: Plan officials failed to establish adequate internal control procedures to ensure that member contributions were deducted and deposited into the pension plan.

Effect: Insufficient member contributions could result in the plan not having adequate resources to meet current and future benefit obligations to its members.

Recommendation: We recommend that the delinquent member contributions be deposited into the pension plan.

Management's Response: Municipal officials agreed with the finding without exception and stated that member contributions of 7 percent for 2017 will be funded to Huntingdon Bank Pension Plan for three full-time police officer with interest.

Auditor's Conclusion: The borough's full compliance with the finding recommendation will be evaluated during our next audit of the plan.

Finding No. 3 – Failure To Maintain An Adequate Record-Keeping System

Condition: The pension plan's record-keeping system did not establish adequate accounting procedures to allow plan officials to effectively monitor the pension plan's financial operations. Additionally, many of the records requested in February 2018 for the audit were not provided until September 2018, if at all. The deficiencies are as follows:

- A journal was not maintained to record financial transactions of the pension plan;
- Ledgers were not utilized to record receipts and disbursements;
- A chart of accounts was not maintained;
- Custodial account statements were not provided upon request;
- Documentation of active members' annual payroll amounts and member contribution deductions reported to the plan's custodian were not maintained;
- A minute book and/or ordinances pertaining to pension plan were not provided upon request;

MIDLAND BOROUGH POLICE PENSION PLAN
FINDINGS AND RECOMMENDATIONS

Finding No. 3 – (Continued)

- Pension benefit calculations and lump-sum distribution letters for terminated members were not maintained;
- Financial statements for all years of the audit period were not provided upon request; and
- Copies of actuarial valuation reports were not maintained.

In addition, plan officials have not prepared management guidelines which describe the duties and responsibilities of municipal and plan officials in the operation of the police pension plan.

Criteria: An adequate system of accounting and record keeping is a prerequisite for sound administration of pension plans. In addition, management guidelines are necessary to ensure an acceptable transition of duties in the event of changes in management personnel. Without such measures, the risk exists that important filing deadlines may be overlooked, fundamental plan obligations to active or retired members may not be correctly fulfilled, state aid may be adversely affected and/or delayed and investment opportunities may be lost.

Cause: Plan officials were unaware of their various record-keeping responsibilities and experienced turnover in personnel during the audit period.

Effect: Although we were able to obtain copies from a third-party source in order to complete our audit procedures, the failure of plan officials to maintain adequate records prohibits municipal officials from effectively monitoring the plan's financial operations.

Recommendation: We recommend that plan officials establish and maintain a financial record-keeping system that allows plan officials to effectively monitor the plan's financial operations. In addition, the borough should consider preparing a written operations manual which describes, in detail, the duties of municipal and plan officials responsible for the operation of the pension plan. This manual should be kept on file with other important plan documents. Plan officials should refer to the Auditor General's Bulletin No. 2-88 entitled "Preparation, Maintenance and Auditability of Financial Records" for further guidance in establishing adequate accounting procedures.

Management's Response: Municipal officials agreed with the finding without exception and stated that procedures will be written and utilized to ensure an adequate record-keeping system.

Auditor's Conclusion: Compliance will be evaluated during our next audit of the plan.

MIDLAND BOROUGH POLICE PENSION PLAN
SUPPLEMENTARY INFORMATION
(UNAUDITED)

The supplementary information contained on Pages 6 and 7 reflects the implementation of GASB Statement No. 67, *Financial Reporting for Pension Plans*. The objective of this statement is to improve financial reporting by state and local governmental pension plans.

SCHEDULE OF CHANGES IN THE NET PENSION
LIABILITY AND RELATED RATIOS
FOR THE YEAR ENDED DECEMBER 31, 2015

Total Pension Liability	
Service cost	\$ 68,827
Interest	146,045
Difference between expected and actual experience	(194,290)
Benefit payments, including refunds of member contributions	(189,431)
Net Change in Total Pension Liability	(168,849)
Total Pension Liability – Beginning	2,315,734
Total Pension Liability – Ending (a)	\$ 2,146,885
Plan Fiduciary Net Position	
Contributions – employer	\$ 113,490
Contributions – member	24,147
Net investment income	(9,845)
Benefit payments, including refunds of member contributions	(189,431)
Administrative expense	(13,902)
Net Change in Plan Fiduciary Net Position	(75,541)
Plan Fiduciary Net Position – Beginning	1,830,601
Plan Fiduciary Net Position – Ending (b)	\$ 1,755,060
Net Pension Liability – Ending (a-b)	\$ 391,825
Plan Fiduciary Net Position as a Percentage of the Total Pension Liability	81.75%
Estimated Covered Employee Payroll	\$ 310,713
Net Pension Liability as a Percentage of Covered Employee Payroll	126.11%

MIDLAND BOROUGH POLICE PENSION PLAN
 SUPPLEMENTARY INFORMATION
 (UNAUDITED)

Sensitivity of the Net Pension Liability to Changes in the Discount Rate

The following presents the net pension liability of the borough as of December 31, 2015, calculated using the discount rate of 6.40%, as well as what the borough's net pension liability would be if it were calculated using a discount rate that is 1 percentage-point lower or 1 percentage-point higher than the current rate:

	1% Decrease (5.40%)	Current Discount Rate (6.40%)	1% Increase (7.40%)
Net Pension Liability	\$ 638,966	\$ 391,825	\$ 185,392

Note: The discount rate of 6.40% was used in the preparation of the borough's December 31, 2015 GASB 67 report. This rate differs from the 7.0% reported in Notes to Supplementary Schedules on page 11 of this report.

MIDLAND 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	\$ 1,473,050	\$ 2,028,716	\$ 555,666	72.6%
01-01-15	1,727,923	2,171,871	443,948	79.6%
01-01-17	1,843,634	2,164,374	320,740	85.2%

MIDLAND 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.

MIDLAND 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
2012	\$ 63,768	100.0%
2013	67,346	100.0%
2014	112,674	100.0%
2015	113,490	100.0%
2016	107,836	100.0%
2017	103,056	100.0%

MIDLAND 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	9 years
Asset valuation method	Market value, 4-year smoothing
Actuarial assumptions:	
Investment rate of return	7.0%
Projected salary increases *	5.0%

* Includes inflation at 2.5%

MIDLAND BOROUGH POLICE PENSION PLAN
REPORT DISTRIBUTION LIST

This report was initially distributed to the following:

The Honorable Tom W. Wolf
Governor
Commonwealth of Pennsylvania

The Honorable Angela M. Adkins
Mayor

Mr. Peter Quinn, Esq.
Interim Council President

Mr. Albert Troiani, Jr.
Interim Council Vice-President

Ms. Connie Drozdjibob
Councilwoman

Ms. Jeanne Hupp
Councilwoman

Mr. Norman Kraus, Jr.
Borough Manager

Ms. Mary Lou Turbish
Treasurer

This report is a matter of public record and is available online at www.PaAuditor.gov. Media questions about the report can be directed to the Pennsylvania Department of the Auditor General, Office of Communications, 229 Finance Building, Harrisburg, PA 17120; via email to: news@PaAuditor.gov.