

CITY OF CARBONDALE AGGREGATE PENSION FUND

LACKAWANNA COUNTY

COMPLIANCE AUDIT REPORT

FOR THE PERIOD

JANUARY 1, 2009, TO DECEMBER 31, 2010



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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.

Pension plan aid is provided from a 2 percent foreign casualty insurance premium tax, a portion of the foreign 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 City of Carbondale Aggregate Pension Fund 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 177 - General Local Government Code, Act of December 19, 1996 (P.L. 1178, No. 177), as amended, 53 Pa.C.S. § 101 et seq.
- Act 317 - The Third Class City Code, Act of June 23, 1931 (P.L. 932, No. 317), as amended, 53 P.S. § 35101 et seq.

The City of Carbondale Aggregate Pension Fund retains the assets and acts as a common investment and administrative agent for the city's police and firemen's pension plans. The police and firemen's pension plans are single-employer defined benefit pension plans locally controlled by the provisions of Chapter 27 of the city's code of ordinances, adopted pursuant to Act 317. The plans are also affected by the provisions of collective bargaining agreements between the city and its police officers and firefighters.



The Honorable Mayor and City Council
City of Carbondale
Lackawanna County
Carbondale, PA 18407

We have conducted a compliance audit of the City of Carbondale Aggregate Pension Fund for the period January 1, 2009, to December 31, 2010. The audit was conducted pursuant to authority derived from Section 402(j) of Act 205 and in accordance with *Government Auditing Standards* applicable to performance audits 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 fund 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. The City of Carbondale contracted with an independent certified public accounting firm for annual audits of its basic financial statements which are available at the city's offices. Those financial statements were not audited by us and, accordingly, we express no opinion or other form of assurance on them.

City officials are responsible for establishing and maintaining effective internal controls to provide reasonable assurance that the City of Carbondale Aggregate Pension Fund 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 city's internal controls as they relate to the city'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 the extent necessary to satisfy the audit objectives.

The results of our tests indicated that, in all significant respects, the City of Carbondale Aggregate Pension Fund 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 – Provision Of Benefits In Excess Of The Third Class City Code

Finding No. 2 – Failure To Pay The Minimum Municipal Obligation Of The Plans

The accompanying supplementary information is presented for purposes of additional analysis. We did not audit the information and, accordingly, express no form of assurance on it.

The contents of this report were discussed with officials of the City of Carbondale and, where appropriate, their responses have been included in the report.

January 31, 2012

JACK WAGNER
Auditor General

CITY OF CARBONDALE AGGREGATE PENSION FUND
STATUS OF PRIOR FINDINGS

Compliance With Prior Audit Recommendation

The City of Carbondale has complied with the prior audit recommendation concerning the following:

- Incorrect Data On Certification Form AG 64 Resulting In An Excess Reimbursement Of Special 2002 Ad Hoc Postretirement Adjustment

The city reimbursed \$3,752 to the Commonwealth for the excess reimbursement received.

Noncompliance With Prior Audit Recommendation

The City of Carbondale has not complied with the prior audit recommendation concerning the following as further discussed in the Findings and Recommendations section of this report:

- Provision Of Benefits In Excess Of The Third Class City Code

CITY OF CARBONDALE AGGREGATE PENSION FUND
FINDINGS AND RECOMMENDATIONS

Finding No. 1 – Noncompliance With Prior Audit Recommendation – Provision Of Benefits In Excess Of The Third Class City Code

Condition: As disclosed in the prior audit report, the city adopted a home rule charter pursuant to the Home Rule Charter and Optional Plans Law, 53 Pa. C.S. § 2901 *et seq.* (previously 53 P.S. § 1-101 *et seq.*). Our audit determined that the city has provided benefits to its firefighters in excess of the restrictions found in the Third Class City Code, as follows:

<u>Benefit</u>	<u>Governing Document/Collective Bargaining Agreement</u>	<u>Third Class City Code</u>
Cost-of-living allowances	Firemen who retire on or after January 1, 1993, shall receive an increase of 2.5% on the third anniversary of retirement and each year thereafter.	Increases shall be in conformity with a uniform scale with the total benefit limited to 50% of the current salary of the firemen of the highest pay grade.

Criteria: On January 24, 2001, the Commonwealth Court of Pennsylvania issued its opinion in *Municipality of Monroeville v. Monroeville Police Department Wage Policy Committee*. Therein, the court held that Section 2962(c)(5) of the Home Rule Charter and Optional Plans Law, 53 Pa. C.S. § 2962(c)(5), “clearly precludes home rule municipalities from providing pension benefits different from those prescribed in general law including Act 600.” The court’s holding was in accord with the position taken by this Department since at least January 1995.

Cause: Plan officials were unable to amend the cost-of-living provision through the collective bargaining process.

Effect: 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 city 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.

CITY OF CARBONDALE AGGREGATE PENSION FUND
FINDINGS AND RECOMMENDATIONS

Finding No. 1 – (Continued)

Recommendation: We again recommend that the city restrict pension benefits to those authorized by the Third Class City Code for all employees who began full-time employment on or after January 24, 2001 (the date *Monroeville* was issued) upon the renewal, extension, or renegotiation of the collective bargaining agreement. To the extent that the city is not in compliance with the Third Class City Code and/or is contractually obligated to provide benefits in excess of those authorized by the Third Class City Code to employees who began employment on or after January 24, 2001, 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 unauthorized benefits on the plan's future state aid allocations and submit this information to the Department.

Management's Response: Municipal officials agreed with the finding without exception. According to city officials, the cost-of-living increases are required by the current collective bargaining agreement for the period January 1, 2010, to December 31, 2015, between the city and its firefighters. In order to stay in compliance with this agreement, the city deems it necessary to pay these increases even though they are not in compliance with the Third Class City Code.

Auditor's Conclusion: The Department is aware that the provision of cost-of-living adjustments is subject to the collective bargaining process. The city's commitment to provide excess cost-of-living increases to its firefighters who were hired on or after January 24, 2001, will continue to be monitored during future audits.

Finding No. 2 – Failure To Pay The Minimum Municipal Obligation Of The Plans

Condition: The city did not pay the minimum municipal obligation (MMO) that was due to the police and firemen's pension plans for the year 2011 as required by Act 205. The city has unpaid 2011 MMO balances of \$201,598 and \$73,128 for the police and firemen's pension plans, respectively.

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.

CITY OF CARBONDALE AGGREGATE PENSION FUND
FINDINGS AND RECOMMENDATIONS

Finding No. 2 – (Continued)

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.

Furthermore, Section 302(e) of Act 205 states, in part:

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. . . .

Cause: Plan officials failed to establish adequate internal control procedures to ensure the plans' MMOs were paid in accordance with Act 205 requirements.

Effect: The failure to pay the MMOs could result in the plans not having adequate resources to meet current and future benefit obligations to its members.

Due to the municipality's failure to pay the 2011 MMOs by the December 31, 2011, deadline, the municipality must add the 2011 MMOs to the current year's MMOs and include interest, as required by Act 205.

Recommendation: We recommend that the city pay the MMOs due to the police and firemen's pension plans for the year 2011, with interest, in accordance with Section 302(e) of Act 205. A copy of the interest calculations must be maintained by the city for examination during our next audit of the fund.

Furthermore, we recommend that plan officials establish adequate internal control procedures to ensure that future MMOs are paid in accordance with Act 205 requirements.

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

CITY OF CARBONDALE AGGREGATE PENSION FUND
 SUPPLEMENTARY INFORMATION
 (UNAUDITED)

SCHEDULES 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, 2005, is as follows:

POLICE PENSION PLAN

	(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 Liability (b) - (a)	Funded Ratio (a)/(b)	Covered Payroll (c)	Unfunded (Assets in Excess of) Actuarial Liability as a % of Payroll [(b-a)/(c)]
01-01-05	\$ 763,788	\$ 4,173,093	\$ 3,409,305	18.3%	\$ 608,327	560.4%
01-01-07	4,528,414	4,514,707	(13,707)	100.3%	718,859	(1.9%)
01-01-09	4,205,322	4,757,201	551,879	88.4%	788,442	70.0%

The increased asset balance as of January 1, 2007, reflects the deposit of bond proceeds in December of 2006.

The market value of the plan's assets at 01-01-09 has 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.

CITY OF CARBONDALE AGGREGATE PENSION FUND
 SUPPLEMENTARY INFORMATION
 (UNAUDITED)

SCHEDULES OF FUNDING PROGRESS – (Continued)

FIREMEN’S PENSION PLAN

	(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)]
01-01-05	\$ 1,609,143	\$ 2,190,579	\$ 581,436	73.5%	\$ 383,537	151.6%
01-01-07	2,385,509	2,378,288	(7,221)	100.3%	385,191	(1.9%)
01-01-09	2,440,459	2,694,105	253,646	90.6%	472,764	53.7%

The increased asset balance as of January 1, 2007, reflects the deposit of bond proceeds in December of 2006.

The market value of the plan’s assets at 01-01-09 has 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.

CITY OF CARBONDALE AGGREGATE PENSION FUND
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. However, when assets are in excess of the actuarial accrued liability, the higher the bracketed percentage, the stronger the plan.

CITY OF CARBONDALE AGGREGATE PENSION FUND
SUPPLEMENTARY INFORMATION
(UNAUDITED)

SCHEDULE OF CONTRIBUTIONS FROM EMPLOYER
AND OTHER CONTRIBUTING ENTITIES

POLICE PENSION PLAN

Year Ended December 31	Annual Required Contribution	Percentage Contributed
2005	\$ 253,513	100.0%
2006	259,918	100.0%
2007	99,304	100.0%
2008	99,542	100.0%
2009	100,099	100.0%
2010	102,623	100.0%

CITY OF CARBONDALE AGGREGATE PENSION FUND
SUPPLEMENTARY INFORMATION
(UNAUDITED)

SCHEDULE OF CONTRIBUTIONS FROM EMPLOYER
AND OTHER CONTRIBUTING ENTITIES

FIREMEN'S PENSION PLAN

Year Ended December 31	Annual Required Contribution	Percentage Contributed
2005	\$ 152,056	100.0%
2006	151,456	100.0%
2007	55,885	100.0%
2008	57,506	100.0%
2009	61,152	100.0%
2010	63,466	100.0%

CITY OF CARBONDALE AGGREGATE PENSION FUND
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:

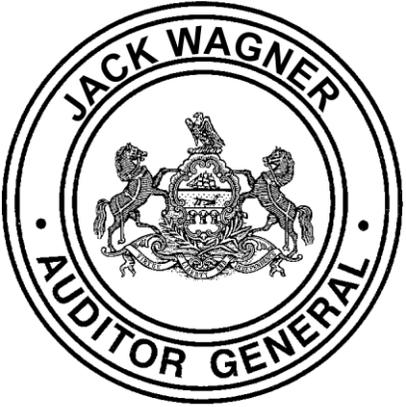
POLICE PENSION PLAN

Actuarial valuation date	January 1, 2009
Actuarial cost method	Entry age normal
Amortization method	Level dollar
Remaining amortization period	9 years
Asset valuation method	Fair value, 5-year smoothing
Actuarial assumptions:	
Investment rate of return	8.0%
Projected salary increases	5.0%
Includes inflation at	Not disclosed
Cost-of-living adjustments	1.0% per year postretirement

CITY OF CARBONDALE AGGREGATE PENSION FUND
SUPPLEMENTARY INFORMATION
NOTES TO SUPPLEMENTARY SCHEDULES
(UNAUDITED)

FIREMEN'S PENSION PLAN

Actuarial valuation date	January 1, 2009
Actuarial cost method	Entry age normal
Amortization method	Level dollar
Remaining amortization period	12 years
Asset valuation method	Fair value, 5-year smoothing
Actuarial assumptions:	
Investment rate of return	8.0%
Projected salary increases	5.0%
Includes inflation at	Not disclosed
Cost-of-living adjustments	2.5% per year postretirement



CITY OF CARBONDALE AGGREGATE PENSION FUND
REPORT DISTRIBUTION LIST

This report was initially distributed to the following:

The Honorable Tom Corbett
Governor
Commonwealth of Pennsylvania

City of Carbondale Aggregate Pension Fund
Lackawanna County
1 North Main Street
Carbondale, PA 18407

The Honorable Justin Taylor	Mayor
Ms. Kathleen M. Conner	Council President
Mr. Thomas Rainey, CPA	Finance Director
Ms. Michele Bannon	City Clerk

This report is a matter of public record. Copies of this report may be obtained from the Pennsylvania Department of the Auditor General, Office of Communications, Room 318 Finance Building, Harrisburg, PA 17120. If you have any questions regarding this report or any other matter, you may contact the Department of the Auditor General by accessing our website at www.auditorgen.state.pa.us.