HAMBURG BOROUGH POLICE PENSION PLAN

BERKS COUNTY

COMPLIANCE AUDIT REPORT

FOR THE PERIOD

JANUARY 1, 2008, TO DECEMBER 31, 2009

HAMBURG BOROUGH POLICE PENSION PLAN

BERKS COUNTY

COMPLIANCE AUDIT REPORT

FOR THE PERIOD

JANUARY 1, 2008, TO DECEMBER 31, 2009

CONTENTS

Page

Background 1

Letter from the Auditor General 3

Status of Prior Findings 5

Findings and Recommendations:

Finding No. 1 – Noncompliance With Prior Audit Recommendation – Failure To Update The Plan's Governing Ordinance 6

Finding No. 2 – Noncompliance With Prior Audit Recommendation – Improper Reduction Of Members' Contributions 7

Finding No. 3 – Noncompliance With Prior Audit Recommendation – Pension Benefits Not In Compliance With Act 600 Provisions 7

Finding No. 4 – Failure To Fully Pay The Minimum Municipal Obligation Of The Plan 9

Supplementary Information 11

Report Distribution List 15

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 Hamburg 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 600 - Police Pension Fund Act, Act of May 29, 1956, (P.L. (1955) 1804, No. 600), as amended, 53 P.S. § 767, et seq.

The Hamburg Borough Police Pension Plan is a single-employer defined benefit pension plan locally controlled by the provisions of Ordinance No. 314, 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.

JACK WAGNER

AUDITOR GENERAL

The Honorable Mayor and Borough Council
Hamburg Borough
Berks County
Hamburg, PA 19526

We have conducted a compliance audit of the Hamburg Borough Police Pension Plan for the period January 1, 2008, to December 31, 2009. 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 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. Hamburg 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 Hamburg 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 the extent necessary to satisfy the audit objectives.

The results of our tests indicated that, in all significant respects, the Hamburg 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 – Failure To Update The Plan's Governing Ordinance
Finding No. 2	–	Noncompliance With Prior Audit Recommendation – Improper Reduction Of Members' Contributions
Finding No. 3	–	Noncompliance With Prior Audit Recommendation – Pension Benefits Not In Compliance With Act 600 Provisions
Finding No. 4	–	Failure To Fully 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 and, accordingly, express no form of assurance on it.

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

March 23, 2011

JACK WAGNER
Auditor General

HAMBURG BOROUGH POLICE PENSION PLAN
STATUS OF PRIOR FINDINGS

Compliance With Prior Audit Recommendation

Hamburg 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 $6,457 to the Commonwealth for the overpayment of state aid.

Noncompliance With Prior Audit Recommendations

Hamburg Borough has not complied with the prior audit recommendations concerning the following as further discussed in the Findings and Recommendations section of this report:

- Failure To Update The Plan's Governing Ordinance
- Improper Reduction Of Members' Contributions
- Pension Benefits Not In Compliance With Act 600 Provisions

HAMBURG BOROUGH POLICE PENSION PLAN
FINDINGS AND RECOMMENDATIONS

Finding No. 1 – Noncompliance With Prior Audit Recommendation – Failure To Update The Plan's Governing Ordinance

Condition: As disclosed in the prior audit report, the borough has not updated the governing ordinance of the police pension plan to reflect changes that resulted from the discontinuation of the previous agreement with the prior plan administrator. Numerous plan benefits and eligibility requirements had been established through a separate joinder and trust agreement with the Pennsylvania State Association of Boroughs (PSAB), including vesting eligibility, survivor benefits and disability requirements. However, the relationship between the two parties no longer exists and Act 600 has been amended since that previous agreement was effective (See Finding No. 3).

In addition, the collective bargaining agreement covering the years 2006 through 2010 between the borough and its police officers includes the implementation of a Deferred Retirement Option Program (DROP). In this agreement, the borough was required to adopt a DROP through an ordinance on or before March 31, 2007. The parties subsequently agreed to extend the time period for the ordinance adoption to January 15, 2008; however, as of the date of this report, no formal action has been taken with regards to formally adopting the DROP.

Criteria: Act 600 mandates that pension plan benefits be established through an ordinance or resolution. Since the governing document of the plan is an ordinance, any amendments to the plan must be made through a properly executed ordinance.

Cause: Borough officials have arranged for an updated ordinance to be prepared by their solicitor; however, the amended ordinance has yet to be completed and adopted by borough council.

Effect: The absence of updated, formalized pension plan benefit provisions may result in inadequate members' contributions, the payment of unauthorized benefits and/or inconsistent benefit calculations.

Recommendation: We again recommend that borough officials consult with their solicitor and amend the police pension plan's governing ordinance to include all current benefit provisions.

Furthermore, the borough should implement adequate internal control procedures to ensure that all future benefit changes be incorporated into the plan's governing document in a timely manner.

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

Finding No. 2 – Noncompliance With Prior Audit Recommendation – Improper Reduction Of Members' Contributions

Condition: As disclosed in the prior audit report, the governing body of the municipality failed to adopt an annual ordinance or resolution to reduce members' contributions in accordance with Act 600 requirements.

Criteria: Section 6(c) of Act 600 states, in part:

> The governing body of the borough, town, township or regional police department may, on an annual basis, by ordinance or resolution, reduce or eliminate payments into the fund by members.

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

Effect: Municipal officials failed to ensure members' contributions were properly reduced in accordance with Act 600 provisions.

Recommendation: We again recommend that the borough either reduce members' contributions in accordance with Act 600, or reinstate the collection of members' contributions in accordance with the rate approved by the borough.

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

Finding No. 3 – Noncompliance With Prior Audit Recommendation – Pension Benefits Not In Compliance With Act 600 Provisions

Condition: As disclosed in the prior audit report, the pension plan's governing document, Ordinance No. 314, as amended, contains benefit provisions that are not in compliance with Act 600.

Furthermore, as previously disclosed, Act 600 was amended by Act 30 on April 17, 2002, and made significant changes to the statutorily prescribed benefit structure of police pension plans subject to Act 600. However, municipal officials have not amended the police pension plan's benefit structure to adopt all of the changes mandated by Act 30.

Finding No. 3 – (Continued)

The specific inconsistencies are noted below:

Benefit Provision	Governing Document	Act 600 (as amended)
Survivor's benefit	None disclosed	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.)
Pre-vesting death benefit	None disclosed	The surviving spouse of a member of the police force who dies before his pension has vested or if no spouse survives or if he or she survives and subsequently dies, the child or children under the age of eighteen years, or, if attending college, under or attaining the age of twenty-three years, of the member of the police force shall be entitled to receive repayment of all money which the member invested in the pension fund plus interest or other increases in value of the member's investment in the pension fund, unless the member has designated another beneficiary for this purpose.
Service-related disability benefit	None disclosed	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.

Finding No. 3 – (Continued)

Criteria: A governing document which contains clearly defined and updated benefit provisions is a prerequisite for the consistent, sound administration of retirement benefits. In addition, the police pension plan's benefit structure should be in compliance with Act 600, as amended.

Cause: Borough officials have arranged for an updated ordinance to be prepared by their solicitor; however, the amended ordinance has yet to be completed and adopted by borough council.

Effect: Maintaining a benefit structure which is not in compliance with Act 600 could result in plan members or their beneficiaries receiving incorrect benefit amounts or being denied benefits to which they are statutorily entitled.

Recommendation: We again recommend that municipal officials, after consulting with their solicitor, take whatever action is necessary to bring the police pension plan's benefit structure into compliance with Act 600, as amended.

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

Finding No. 4 – Failure To Fully Pay The Minimum Municipal Obligation Of The Plan

Condition: The municipality did not fully pay the minimum municipal obligation (MMO) that was due to the police pension plan for the year 2008, as required by Act 205. The municipality had a 2008 unpaid MMO balance of $1,209.

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.

Finding No. 4 – (Continued)

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 MMO was fully paid in accordance with Act 205 requirements.

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

Due to the municipality's failure to fully pay the 2008 MMO by the December 31, 2008, deadline, the municipality must add the 2008 MMO balance to the current year's MMO and include interest, as required by Act 205.

Recommendation: We recommend that the municipality pay the outstanding MMO due to the police pension plan for the year 2008, with interest, 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 of the plan.

Furthermore, we recommend that plan officials establish adequate internal control procedures to ensure the MMO is fully paid in accordance with Act 205 requirements.

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

HAMBURG 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, except for distressed pension plans, for which annual reporting was required through January 1, 2003. The historical information, beginning as of January 1, 2005, 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)]
01-01-05	$ 1,440,252	$ 1,575,117	$ 134,865	91.4%	$ 373,714	36.1%
01-01-07	1,636,775	1,710,123	73,348	95.7%	271,213	27.0%
01-01-09	1,567,314	1,795,964	228,650	87.3%	328,503	69.6%

Note: The market values of the plan's assets at 01-01-05 and 01-01-07 have been adjusted to reflect the smoothing of gains and/or losses over a 5-year averaging period. The market value of the plan's assets at 01-01-09 has been adjusted to reflect the smoothing of gains and/or losses at 120% of market value. These methods 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.

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.

HAMBURG 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
2004	$ 23,789	132.5%
2005	31,732	103.9%
2006	53,062	100.0%
2007	52,256	100.0%
2008	41,020	97.1%
2009	46,330	100.0%

HAMBURG 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, 2009
Actuarial cost method	Entry age normal
Amortization method	Level dollar
Remaining amortization period	9 years
Asset valuation method	Plan assets are valued using the method described in Section 210 of Act 205, as amended, subject to a ceiling of 120% of the market value of assets.
Actuarial assumptions:	
Investment rate of return *	8.0%
Projected salary increases *	5.0%
* Includes inflation at	Not disclosed
Cost-of-living adjustments	None assumed

HAMBURG BOROUGH POLICE PENSION PLAN
REPORT DISTRIBUTION LIST

This report was initially distributed to the following:

The Honorable Tom Corbett
Governor
Commonwealth of Pennsylvania

Hamburg Borough Police Pension Plan
Berks County
61 North Third Street
Hamburg, PA 19526

The Honorable Roy C. Del Rosario	Mayor
Ms. Martha Bertolet	Council President
Ms. Lynda Albright	Borough Manager

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.