

PALO ALTO BOROUGH POLICE PENSION PLAN

SCHUYLKILL COUNTY

COMPLIANCE AUDIT REPORT

FOR THE PERIOD

JANUARY 1, 2006, TO DECEMBER 31, 2008



PALO ALTO BOROUGH POLICE PENSION PLAN

SCHUYLKILL COUNTY

COMPLIANCE AUDIT REPORT

FOR THE PERIOD

JANUARY 1, 2006, TO DECEMBER 31, 2008

CONTENTS

	<u>Page</u>
Background	1
Letter from the Auditor General	3
Status of Prior Findings	5
Finding and Recommendation:	
Finding – Noncompliance With Prior Audit Recommendation – Improper Survivors’ Benefit.....	6
Supplementary Information	8
Observation.....	12
Report Distribution List	13

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 Palo Alto 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 581 - The Borough Code, Act of February 1, 1966 (P.L. 1656, No. 581), Article XI(f), Police Pension Fund in Boroughs Having a Police Force of Less Than Three Members, as amended, 53 P.S. § 46131 et seq.

The Palo Alto Borough Police Pension Plan is a single-employer defined benefit pension plan locally controlled by the provisions of Ordinance No. 114-77, as amended.



The Honorable Mayor and Borough Council
Palo Alto Borough
Schuylkill County
Palo Alto, PA 17901

We have conducted a compliance audit of the Palo Alto Borough Police Pension Plan for the period January 1, 2006, to December 31, 2008. 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 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.

Borough officials are responsible for establishing and maintaining effective internal controls to provide reasonable assurance that the Palo Alto 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 Palo Alto 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 – Noncompliance With Prior Audit Recommendation – Improper
Survivors' Benefit

We also noted a matter that has been included in the following observation further discussed later in this report:

Observation – Failure To Prepare Financial Statements

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

February 18, 2010

JACK WAGNER
Auditor General

PALO ALTO BOROUGH POLICE PENSION PLAN
STATUS OF PRIOR FINDINGS

Status Of Prior Audit Recommendation

· Failure To Prepare Financial Statements

The status of the prior audit recommendation is addressed in the Observation discussed later in this report.

Noncompliance With Prior Audit Recommendation

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

· Improper Survivors' Benefit

PALO ALTO BOROUGH POLICE PENSION PLAN
FINDING AND RECOMMENDATION

Finding – Noncompliance With Prior Audit Recommendation – Improper Survivors’ Benefit

Condition: As disclosed in the prior audit report, the pension plan’s governing document grants a survivors’ benefit which is not authorized by Act 581. Section 505(c) of Article 5 of the borough’s codified ordinances states:

The widow of a member of the police force, or a member who retires on pension who dies, or if no widow survives, or if she survives and subsequently dies or remarries, then the child or children under the age of eighteen (18) years of such member or a member who retires on pension who dies on or after the effective date of this ordinance shall, during her lifetime or so long as she does not remarry, in the case of a widow, or until reaching the age of eighteen (18) years, in the case of a child or children, be entitled to receive a pension calculated at the rate of fifty percent (50%) of the pension the member was receiving or would have been receiving had he been retired at the time of his death.

Criteria: Section 1131 of Act 581 states, in part:

All pension funds established under the provisions of this section shall be under the direction of the borough council, or such committee as it may designate, and shall be applied under such regulations as the council may by ordinance prescribe for the benefit of such members of the police force as shall receive honorable discharge therefrom by reason of age or disability and the families of such as may be injured or killed in the service. Any allowances made to those who are retired by reason of disability or age shall be in conformity with a uniform scale. (Emphasis added)

Consequently, Act 581 only authorizes the payment of survivor benefits to families of police officers who are disabled or killed in service.

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

PALO ALTO BOROUGH POLICE PENSION PLAN
FINDING AND RECOMMENDATION

Finding – (Continued)

Effect: Providing unauthorized pension benefits increases the plan’s pension costs and reduces the amount of funds available for investment purposes or the payment of authorized benefits or administrative expenses. Since the borough did not receive state aid allocations during the audit period, it did not receive any excess state aid allocations attributable to the unauthorized benefits provided. However, the provision of unauthorized pension benefits may result in the receipt of excess state aid in the future and could increase the municipal contributions necessary to fund the plan in accordance with Act 205 funding standards.

Recommendation: We again recommend that the borough eliminate the unauthorized survivor benefit provisions at its earliest opportunity to do so. Should the borough fail to eliminate the unauthorized benefit provisions, the cost of the improper 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, 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.

PALO ALTO 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, 2003, 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)]
01-01-03	\$ 158,090	\$ 15,471	\$ (142,619)	1,021.8%	\$ 30,270	(471.2%)
01-01-05	170,892	24,426	(146,466)	699.6%	27,558	(531.5%)
01-01-07	186,618	65,141	(121,477)	286.5%	28,936	(419.8%)

PALO ALTO 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.

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.

PALO ALTO 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
2003	None	N/A
2004	None	N/A
2005	None	N/A
2006	None	N/A
2007	None	N/A
2008	None	N/A

PALO ALTO 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, 2007
Actuarial cost method	Entry age normal
Amortization method	N/A
Remaining amortization period	N/A
Asset valuation method	Fair value
Actuarial assumptions:	
Investment rate of return	5.0%
Projected salary increases	3.0%

PALO ALTO BOROUGH POLICE PENSION PLAN
OBSERVATION

Observation – Failure To Prepare Financial Statements

Plan officials have not prepared financial statements or required notes to the financial statements for the police pension plan for the years ended December 31, 2006, 2007 and 2008.

Financial reporting assists in fulfilling a municipality's duty to be publicly accountable and should enable users to assess accountability. Guidance for the form and content of annual financial statements and notes to the financial statements can be found in Governmental Accounting Standards Board Statements No. 25 (GASB 25), as amended by No. 50 (GASB 50), and No. 3 (GASB 3), as amended by No. 40 (GASB 40).

Plan officials should consider establishing and implementing procedures to ensure the preparation of annual financial statements, which include note disclosures required by GASB 25, as amended by GASB 50, and GASB 3, as amended by GASB 40, in accordance with accounting principles generally accepted in the United States of America.

PALO ALTO BOROUGH POLICE PENSION PLAN
REPORT DISTRIBUTION LIST

This report was initially distributed to the following:

The Honorable Edward G. Rendell
Governor
Commonwealth of Pennsylvania

Palo Alto Borough Police Pension Plan
Schuylkill County
142 East Bacon Street
Palo Alto, PA 17901

The Honorable Thomas W. Beveridge	Mayor
Mr. John A. Deatrich, Jr.	Council President
Ms. Sharon Uscilowicz	Secretary

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.