

PORT ALLEGANY BOROUGH NONUNIFORMED PENSION PLAN

MCKEAN COUNTY

COMPLIANCE AUDIT REPORT

FOR THE PERIOD

JANUARY 1, 2007, TO DECEMBER 31, 2009



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ABBREVIATION

PERC - Public Employee Retirement Commission

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 Port Allegany Borough Nonuniformed 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.

The Port Allegany Borough Nonuniformed Pension Plan is a single-employer defined benefit pension plan locally controlled by the provisions of Resolution No. 89-24, as amended. The plan is also affected by the provisions of collective bargaining agreements between the borough and its nonuniformed employees.



The Honorable Mayor and Borough Council
Port Allegany Borough
McKean County
Port Allegany, PA 16743

We have conducted a compliance audit of the Port Allegany Borough Nonuniformed Pension Plan for the period January 1, 2007, 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 the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our finding and conclusions based on our audit objective. We believe that the evidence obtained provides a reasonable basis for our finding 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 this objective.

Borough officials are responsible for establishing and maintaining effective internal controls to provide reasonable assurance that the Port Allegany Borough Nonuniformed 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, we tested transactions, assessed official actions, performed analytical procedures and interviewed selected officials to the extent necessary to satisfy the audit objective.

The results of our tests indicated that, in all significant respects, the Port Allegany Borough Nonuniformed 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 – Incorrect Data Supplied To Actuary For Actuarial Valuation Report Preparation

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

August 3, 2010

JACK WAGNER
Auditor General

PORT ALLEGANY BOROUGH NONUNIFORMED PENSION PLAN
FINDING AND RECOMMENDATION

Finding – Incorrect Data Supplied To Actuary For Actuarial Valuation Report Preparation

Condition: Actuarial valuation report form PC-203C, with a valuation date of January 1, 2009, submitted to the Public Employee Retirement Commission (PERC), contained incorrect information. The information was based on data supplied by the municipality to the plan's actuary.

The current collective bargaining agreement between the borough and its nonuniformed employees, dated January 1, 2009, and effective January 1, 2009, to December 31, 2011, provides for an increase in the retirement benefit formula from 1.425% to 1.525% and amends the early retirement benefit eligibility requirements from age 60 to age 55 or 30 years of service. These changes are not reflected in the summary of plan benefit provisions contained in the actuarial valuation report.

Criteria: Section 201(d) of Act 205 states:

Responsibility for preparation and filing of reports and investigations. The actuarial valuation report or experience investigation required pursuant to subsection (a) shall be prepared under the supervision and at the discretion of the chief administrative officer of the municipality, who shall be responsible for the filing of the document. The actuarial valuation report or experience investigation shall be signed by the chief administrative officer, indicating that to the extent of the understanding and knowledge of the officer, the report or investigation represents a true and accurate portrayal of the actuarial, financial and demographic condition of the pension plan of the municipality.

Cause: The discrepancies in the data submitted to the plan's actuary occurred because plan officials did not amend the plan's governing document until July 5, 2010, to reflect the changes contained in the collective bargaining agreement.

Effect: Because the municipality's state aid allocation is determined, in part, by the information contained in the actuarial valuation report, the submission of incorrect data to the actuary may have resulted in the municipality receiving an incorrect allocation of state aid.

In addition, the information contained in the actuarial valuation report is used to determine the municipality's minimum municipal obligation (MMO); therefore, the incorrect data may have resulted in an erroneous MMO calculation.

PORT ALLEGANY BOROUGH NONUNIFORMED PENSION PLAN
FINDING AND RECOMMENDATION

Finding – (Continued)

Recommendation: We recommend that plan officials contact PERC to determine if a revised actuarial valuation report may be filed. If a revised report is prepared and accepted by PERC, a copy should be submitted to: Department of the Auditor General, Bureau of Municipal Pension Audits, 406 Finance Building, Harrisburg, PA 17120.

We also recommend that if a revised actuarial valuation report is prepared and accepted by PERC, the chief administrative officer of the pension plan recalculate the MMO and make any necessary deposit to the plan, with interest in accordance with Section 302(e) of Act 205.

Finally, we recommend that, in the future, plan officials review and verify all information submitted to and received from the plan's actuary so that future actuarial valuation reports properly reflect the status of the pension plan.

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

PORT ALLEGANY BOROUGH NONUNIFORMED 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 | \$ 880,344 | \$ 953,259 | \$ 72,915 | 92.4% | \$ 382,719 | 19.1% |
| 01-01-07 | 974,313 | 1,073,589 | 99,276 | 90.8% | 390,477 | 25.4% |
| 01-01-09 | 998,361 | 1,227,849 | 229,488 | 81.3% | 448,770 | 51.1% |

Note: 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 4-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.

PORT ALLEGANY BOROUGH NONUNIFORMED 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.

PORT ALLEGANY BOROUGH NONUNIFORMED PENSION PLAN
SUPPLEMENTARY INFORMATION
(UNAUDITED)

SCHEDULE OF CONTRIBUTIONS FROM EMPLOYER
AND OTHER CONTRIBUTING ENTITIES

| Year Ended December 31 | Annual Required Contribution | Percentage Contributed |
|------------------------|------------------------------|------------------------|
| 2004 | \$ 28,071 | 127.0% |
| 2005 | 34,731 | 109.7% |
| 2006 | 37,180 | 109.1% |
| 2007 | 34,158 | 109.1% |
| 2008 | 35,326 | 114.1% |
| 2009 | 37,779 | 113.1% |

PORT ALLEGANY BOROUGH NONUNIFORMED 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 | 8 years |
| Asset valuation method | Fair value, 4-year smoothing |
| Actuarial assumptions: | |
| Investment rate of return * | 8.0% |
| Projected salary increases * | 5.0% |
| * Includes inflation at | Not disclosed |
| Cost-of-living adjustments | None assumed |

PORT ALLEGANY BOROUGH NONUNIFORMED PENSION PLAN
REPORT DISTRIBUTION LIST

This report was initially distributed to the following:

The Honorable Edward G. Rendell
Governor
Commonwealth of Pennsylvania

Port Allegany Borough Nonuniformed Pension Plan
McKean County
45 West Maple Street
Port Allegany, PA 16743

| | |
|--------------------------------|---------------------|
| The Honorable Donald G. Carley | Mayor |
| Ms. Judith Taylor | Council President |
| Mr. Richard Kallenborn | Borough Manager |
| Ms. Susan Carter Roboski | Secretary/Treasurer |

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.