

COMPLIANCE AUDIT

New Milford Township Non-Uniformed Pension Plan Susquehanna County, Pennsylvania For the Period January 1, 2011 to December 31, 2013

March 2015



Commonwealth of Pennsylvania
Department of the Auditor General

Eugene A. DePasquale • Auditor General



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EUGENE A. DePASQUALE
AUDITOR GENERAL

Board of Township Supervisors
New Milford Township
Susquehanna County
New Milford, PA 18834

We have conducted a compliance audit of the New Milford Township Non-Uniformed Pension Plan for the period January 1, 2011 to December 31, 2013. We also evaluated compliance with some requirements for the 2014 year 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 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. To determine if municipal officials took appropriate corrective action to address the findings contained in our prior audit report, we inquired of plan officials and evaluated supporting documentation provided by officials evidencing that the suggested corrective action has been appropriately taken. 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 that there were no employee contributions required by the plan's governing document and applicable laws and regulations for the years covered by our audit period.
- We determined that there were no benefit calculations prepared for the years covered by our audit period.
- We determined whether the January 1, 2011 and January 1, 2013 actuarial valuation reports were prepared and submitted to the Public Employee Retirement Commission (PERC) by March 31, 2012 and 2014, 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 the terms of the plan's unallocated insurance contract, including ownership and any restrictions, were in compliance with plan provisions, investment policies, and state regulations by comparing the terms of the contract with the plan's provisions, investment policies, and state regulations.

Township officials are responsible for establishing and maintaining effective internal controls to provide reasonable assurance that the New Milford Township Non-Uniformed 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 township's internal controls as they relate to the township'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 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 objectives.

The results of our procedures indicated that, in all significant respects, the New Milford Township Non-Uniformed 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 – Partial Compliance With Prior Audit Recommendation – Incorrect Data On Certification Form AG 385 Resulting In An Underpayment Of State Aid
- Finding No. 2 – Failure To Properly Determine And Pay The Minimum Municipal Obligation Of The Plan
- Finding No. 3 – Failure To Deposit State Aid Into The Pension Plan
- Finding No. 4 – Failure To Implement Mandatory Act 44 Distressed Provisions

Finding No. 1 contained in this audit report repeats a condition that was cited in our previous audit report that has not been corrected by township officials. We are concerned by the township’s failure to correct this previously reported audit finding and strongly encourage timely implementation of the recommendation noted in this audit report.

As previously noted, one of the objectives of our audit of the New Milford Township Non-Uniformed Pension Plan was to determine compliance with applicable state laws, regulations, contracts, administrative procedures, and local ordinances and policies. Act 205 was amended on September 18, 2009, through the adoption of Act 44 of 2009. Among several provisions relating to municipal pension plans, the act provides for the implementation of a distress recovery program. Three levels of distress have been established:

<u>Level</u>	<u>Indication</u>	<u>Funding Criteria</u>
I	Minimal distress	70-89%
II	Moderate distress	50-69%
III	Severe distress	Less than 50%

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. However, we are extremely concerned about the funded status of the plan contained in the schedule of funding progress included in this report which indicates **the plan’s funded ratio is 41.1% as of January 1, 2013**, which is the most recent date available. Based on this information, the Public Employee Retirement Commission issued a notification that the township is currently in Level III severe distress status. We encourage township officials to monitor the funding of the non-uniformed pension plan to ensure its long-term financial stability.

The contents of this report were discussed with officials of New Milford Township and, where appropriate, their responses have been included in the report. We would like to thank township officials for the cooperation extended to us during the conduct of the audit.



EUGENE A. DEPASQUALE
Auditor General

March 5, 2015

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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.

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 New Milford Township Non-Uniformed 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 69 - The Second Class Township Code, Act of May 1, 1933 (P.L. 103, No. 69), as reenacted and amended, 53 P.S. § 65101 et seq.

The New Milford Township Non-Uniformed Pension Plan is a single-employer defined benefit pension plan locally controlled by the provisions of a resolution dated March 14, 2001, as amended. The plan was established January 1, 2001. Active members are not required to contribute to the plan. As of December 31, 2013, the plan had 3 active members, no terminated members eligible for vested benefits in the future, and 2 retirees receiving pension benefits from the plan.

BACKGROUND – (Continued)

As of December 31, 2013, selected plan benefit provisions are as follows:

Eligibility Requirements:

Normal Retirement Age 65 and 5 years of service

Early Retirement None

Vesting 100% after 5 years of service

Retirement Benefit:

1.5% of the average final 36 months of compensation times years of service.

Survivor Benefit:

50% of vested benefit at time of death payable immediately for life or until remarriage. If survived by minor children and no spouse, benefit is paid in equal share to minor children to age 18.

Service Related Disability Benefit:

None

NEW MILFORD TOWNSHIP NON-UNIFORMED PENSION PLAN
STATUS OF PRIOR FINDINGS

Compliance With Prior Audit Recommendation

New Milford Township has complied with the prior audit recommendation concerning the following:

- Failure To Appoint A Chief Administrative Officer

The township formally appointed a chief administrative officer of the plan by motion recorded in the minutes of the township supervisors meeting.

Partial Compliance With Prior Audit Recommendation

New Milford Township has partially complied with the prior audit recommendations concerning the following:

- Incorrect Data On Certification Form AG 385 Resulting In An Overpayment Of State Aid

During the current audit period, the township reimbursed \$3,235 to the Commonwealth for the overpayment of state aid received in 2010; however, plan officials failed to comply with the instructions that accompany Certification Form AG 385 to assist them in accurately reporting the required pension data in the year 2013, as further discussed in Finding No. 1 of this report.

NEW MILFORD TOWNSHIP NON-UNIFORMED PENSION PLAN
FINDINGS AND RECOMMENDATIONS

Finding No. 1 – Partial Compliance With Prior Audit Recommendation – Incorrect Data On Certification Form AG 385 Resulting In An Underpayment Of State Aid

Condition: As disclosed in the Status of Prior Findings section of this report, the township partially complied with our prior audit recommendation by reimbursing \$3,235 to the Commonwealth for the overpayment of state aid received in 2010; however, plan officials again failed to comply with the instructions that accompany Certification Form AG 385 to assist them in accurately reporting the required pension data submitted in 2013. The township failed to certify 3 eligible non-uniformed employees and understated payroll by \$108,697 on the Certification Form AG 385 filed in 2013. The data contained on this certification form is based on prior calendar year information.

Criteria: Pursuant to Act 205, at Section 402(e)(2), an employee who has been employed on a full-time basis for at least six consecutive months and has been participating in a pension plan during the certification year is eligible for certification.

Cause: Plan officials failed to establish adequate internal control procedures to ensure the accuracy of the data certified and to ensure full compliance with the prior audit recommendation.

Effect: The data submitted on this certification form is used, in part, to calculate the state aid due to the municipality for distribution to its pension plan. Because the township’s state aid allocation was based on adjusted unit value, the township received an underpayment of state aid of \$11,186 as identified below:

<u>Units Understated</u>	<u>Unit Value</u>	<u>State Aid Underpayment</u>
3	\$ 3,729	\$ 11,187

Although the township will be reimbursed for the underpayment of state aid due to the township’s certification error, the full amount of the 2013 state aid allocation was not available to be deposited timely and therefore was not available to pay operating expenses or for investment.

NEW MILFORD TOWNSHIP NON-UNIFORMED PENSION PLAN
FINDINGS AND RECOMMENDATIONS

Finding No. 1 – (Continued)

Recommendation: We again recommend that, in the future, plan officials establish adequate internal control procedures, such as having at least 2 people review the data certified, to ensure compliance with the instructions that accompany Certification Form AG 385 to assist them in accurately reporting the required pension data.

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

Auditor's Conclusion: We are concerned by the relief association's failure to correct this previously reported audit finding and strongly encourage timely implementation of the recommendation noted in this audit report.

Finding No. 2 – Failure To Properly Determine And Pay The Minimum Municipal Obligation Of The Plan

Condition: Plan officials did not pay the minimum municipal obligation (MMO) that was due to the non-uniformed pension plan for the year 2013 amounting to \$29,608, as required by Act 205. In addition, subsequent to our audit period, plan officials did not properly determine and pay the minimum municipal obligation (MMO) of the non-uniformed pension plan for the year 2014, as required by Act 205, due to understating payroll by \$30,203. Based upon an estimate prepared by this department, the municipality had a total outstanding MMO balance due the non-uniformed pension plan totaling \$70,252 for the years 2013 and 2014.

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.

With regard to the payroll estimate used in the preparation of the MMO, the Pennsylvania Code, Title 16, Section 204.1(c)(1) states, in part:

The payroll used in determining the minimum municipal obligation of a pension plan under section 302(c) of the act shall be based on the payroll to be reported on the Internal Revenue Service Form W-2 and shall be calculated as the total payroll for active members of the plan as of the date of the determination, plus the payroll for the same active members of the plan projected to the year's end using the payroll rates in effect as of the date of the determination.

NEW MILFORD TOWNSHIP NON-UNIFORMED PENSION PLAN
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:

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 at a rate equal to the interest assumption used for the actuarial valuation report or the discount rate applicable to treasury bills issued by the Department of Treasury of the United States with a six-month maturity as of the last business day in December of the plan year in which the obligation was due, whichever is greater, expressed as a monthly rate and compounded monthly.

Cause: Plan officials did not comply with the Act 205 requirements due to a lack adequate internal control procedures to ensure the MMO was deposited timely.

Effect: The proper determination of the plan’s MMO ensures plan officials can properly allocate the necessary resources to the pension plan for the upcoming year. The failure to 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 pay the entire 2013 and 2014 MMOs by the December 31, deadlines, the municipality must add the outstanding 2013 and 2014 MMOs to the current year’s MMO and include interest, as required by Act 205.

Furthermore, the township’s future state aid allocations may be withheld until the finding recommendation is complied with.

Recommendation: We recommend that the municipality pay the outstanding MMO balance due to the non-uniformed pension plan for the years 2013 and 2014, with interest, in accordance with Section 302(e) of Act 205. A copy of the interest calculation must be maintained by the township for examination during our next audit of the plan.

Furthermore, we recommend that, in the future, plan officials pay the full MMO due the plan.

NEW MILFORD TOWNSHIP NON-UNIFORMED PENSION PLAN
FINDINGS AND RECOMMENDATIONS

Finding No. 2 – (Continued)

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

Auditor's Conclusion: Due to the potential withhold of state aid, the township's compliance with the finding recommendation will be monitored subsequent to the release of the audit report and through our next audit of the relief association.

Finding No. 3 – Failure To Deposit State Aid Into The Pension Plan

Condition: Subsequent to our audit period, the municipality did not deposit its 2014 state aid allocation into the pension plan. The municipality received its 2014 state aid allocation in the amount of \$11,271 on September 25, 2014; however, as of the date of this report, none of the 2014 state aid allocation was deposited into the pension plan.

Criteria: Section 402(g) of Act 205 states, in part:

. . . the total amount of the general municipal pension system State aid received by the municipality shall, within 30 days of receipt by the treasurer of the municipality, be deposited in the pension fund or the alternate funding mechanism applicable to the pension plan.

Cause: The 2014 state aid was not deposited into the pension plan because internal control procedures were not in effect to ensure the deposit of state aid.

Effect: When state aid is not deposited into a pension plan account, the funds are not available to pay operating expenses or for investment and the risk of misapplication is increased. Furthermore, the township's future state aid allocations may be withheld until the finding recommendation is complied with.

Recommendation: We recommend that the municipality deposit the township's state aid allocation of \$11,271, plus interest earned during the period beyond the 30 day grace period allowed by Act 205, compounded annually into the pension plan. A copy of the interest calculation must be maintained by the township for examination during our next audit of the plan.

We also recommend that plan officials develop and implement procedures to ensure that future state aid is deposited into the non-uniformed pension plan within 30 days of receipt by the municipal treasurer.

NEW MILFORD TOWNSHIP NON-UNIFORMED PENSION PLAN
FINDINGS AND RECOMMENDATIONS

Finding No. 3 – (Continued)

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

Auditor’s Conclusion: Due to the potential withhold of state aid, the township’s compliance with the finding recommendation will be monitored subsequent to the release of the audit report and through our next audit of the relief association.

Finding No. 4 – Failure To Implement Act 44 Mandatory Distressed Provisions

Condition: Act 205 was amended on September 18, 2009, through the adoption of Act 44 of 2009. Among several provisions relating to municipal pension plans, the act provides for the implementation of a distress recovery program. Three levels of distress have been established:

<u>Level</u>	<u>Indication</u>	<u>Funding Criteria</u>
I	Minimal distress	70-89%
II	Moderate distress	50-69%
III	Severe distress	Less than 50%

Based on the plan’s funded ratio of 41.1% as of January 1, 2013, the Public Employee Retirement Commission (PERC) issued a notification in 2014 that the township was in Level III severe distress status. Based on the plan’s funded ratio of 37.7% as of January 1, 2011, PERC issued a notification in 2012 that the township is currently in Level III severe distress status.

Included with the determination notices, PERC sent the municipality the Act 205 Recovery Program Election Form outlining the mandatory remedies that must be implemented and the voluntary remedies that the municipality could elect to implement. This form was required to be signed by the plan’s Chief Administrative Officer and returned to PERC.

The municipality never returned the election forms to PERC, therefore the township did not comply with the plan for administrative improvement and establishment of a revised benefit plan for newly hired municipal employees.

NEW MILFORD TOWNSHIP NON-UNIFORMED PENSION PLAN
FINDINGS AND RECOMMENDATIONS

Finding No. 4 – (Continued)

Criteria: Act 205, amended by Act 44, at Section 606(b), states:

Recovery program level III.

- (b) Mandatory remedies. Any municipality to which level III of the recovery program applies shall utilize the following remedies:
- (1) The aggregation of trust funds pursuant to section 607(b).
 - (2) The establishment of a revised benefit plan for newly hired municipal employees pursuant to section 607(e).
 - (3) The preparation, submission, and implementation of a plan for improvement of the administration of the pension plan or plans pursuant to section 607(i).

Cause: Municipal officials failed to establish adequate internal control procedures to ensure that the mandatory distress remedies have been implemented.

Effect: The municipality is not in compliance with the Act 44 mandatory distress remedy provisions applicable to Level III which are designed to improve the funding status and administrative efficiency of its pension plans.

Recommendation: We recommend that municipal officials contact PERC for guidance in the implementation of the mandatory distress remedies applicable to Level III pursuant to Act 44 of 2009.

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.

NEW MILFORD TOWNSHIP NON-UNIFORMED PENSION PLAN
POTENTIAL WITHHOLD OF STATE AID

Conditions such as those reported by Finding No. 2 and Finding No. 3 contained in this audit report may lead to a total withholding of state aid in the future unless those findings are corrected. However, such action will not be considered if sufficient written documentation is provided to verify compliance with this department's recommendations. Such documentation should be submitted to: Department of the Auditor General, Bureau of Municipal Pension & Liquor Control Audits, 316-D Finance Building, Harrisburg, PA 17120.

NEW MILFORD TOWNSHIP NON-UNIFORMED 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, 2009, 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)]
01-01-09	\$ 57,001	\$ 160,133	\$ 103,132	35.6%	\$ 96,831	106.5%
01-01-11	80,963	214,620	133,657	37.6%	97,231	137.5%
01-01-13	121,045	294,492	173,447	41.1%	108,697	159.6%

NEW MILFORD TOWNSHIP NON-UNIFORMED 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. When assets are in excess of the actuarial accrued liability, the higher the bracketed percentage, the stronger the plan.

NEW MILFORD TOWNSHIP NON-UNIFORMED PENSION PLAN
 SUPPLEMENTARY INFORMATION
 (UNAUDITED)

SCHEDULE OF CONTRIBUTIONS FROM EMPLOYER
 AND OTHER CONTRIBUTING ENTITIES

Year Ended December 31	Annual Required Contribution	Percentage Contributed
2008	\$ 10,883	100.0%
2009	10,297	100.0%
2010	22,422	100.0%
2011	18,669	100.0%
2012	27,972	100.0%
2013	29,608	*0.0%

** refer to Finding No. 2 contained in this report*

NEW MILFORD TOWNSHIP NON-UNIFORMED 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, 2013
Actuarial cost method	Entry age normal
Amortization method	Level dollar
Remaining amortization period	9 years
Asset valuation method	Fair value
Actuarial assumptions:	
Investment rate of return	4.5%
Projected salary increases	3.5%

NEW MILFORD TOWNSHIP NON-UNIFORMED PENSION PLAN
REPORT DISTRIBUTION LIST

This report was initially distributed to the following:

The Honorable Tom W. Wolf
Governor
Commonwealth of Pennsylvania

New Milford Township Non-Uniformed Pension Plan
Susquehanna County
19730 State Route 11
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Mr. Donald Shibley Chairman, Board of Township Supervisors
Ms. Julene Graham Chief Administrative Officer

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