CITY OF SHAMOKIN POLICE PENSION PLAN

NORTHUMBERLAND COUNTY

COMPLIANCE AUDIT REPORT

FOR THE PERIOD

JANUARY 1, 2009, TO DECEMBER 31, 2010

CITY OF SHAMOKIN POLICE PENSION PLAN

NORTHUMBERLAND COUNTY

COMPLIANCE AUDIT REPORT

FOR THE PERIOD

JANUARY 1, 2009, TO DECEMBER 31, 2010

CONTENTS

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 Shamokin 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 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 Shamokin Police Pension Plan is a single-employer defined benefit pension plan locally controlled by the provisions of Chapter 20 of the city code, adopted by Ordinance No. 02-01, as amended, pursuant to Act 317. The plan is also affected by the provisions of collective bargaining agreements between the city and its police officers.

JACK WAGNER

AUDITOR GENERAL

The Honorable Mayor and City Council
City of Shamokin
Northumberland County
Shamokin, PA 17872

We have conducted a compliance audit of the City of Shamokin Police Pension Plan 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 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. The City of Shamokin 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 Shamokin 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 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 Shamokin 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 – Inconsistent And Unauthorized Pension Benefits

Finding No. 2 – Noncompliance With Prior Audit Recommendation – Pension Benefits Not Authorized By The Third Class City Code

Finding No. 3 – Failure To Appoint A Chief Administrative Officer

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 Shamokin and, where appropriate, their responses have been included in the report.

September 29, 2011

JACK WAGNER
Auditor General

CITY OF SHAMOKIN POLICE PENSION PLAN
STATUS OF PRIOR FINDINGS

Compliance With Prior Audit Recommendation

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

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

  During the current audit period, plan officials complied with the instructions that accompany Certification Form AG 385 and accurately reported the required pension data.

Noncompliance With Prior Audit Recommendations

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

- Inconsistent And Unauthorized Pension Benefits

- Pension Benefit Not Authorized By The Third Class City Code

CITY OF SHAMOKIN POLICE PENSION PLAN
FINDINGS AND RECOMMENDATIONS

Finding No. 1 – Noncompliance With Prior Audit Recommendation – Inconsistent And Unauthorized Pension Benefits

Condition: As disclosed in the prior audit report, the pension plan's governing document, Chapter 20 of the city code, adopted by Ordinance No. 02-01, as amended, contains benefit provisions that conflict with the collective bargaining agreement (CBA) between the police officers and the city. In addition, the governing document and the CBA contain benefit provisions that are not authorized by the Third Class City Code, as follows:

Benefit Provision	Governing Document	Collective Bargaining Agreement	Third Class City Code
Compulsory retirement age	Compulsory retirement of all police officers will be required at 70 years of age.	Not provided	Not authorized
Pension benefit	50% of average monthly salary at the time of retirement, or at the time of vesting of his retirement, or 50% of the average annual salary received during any 5 years of service preceding retirement, whichever is higher.	50% of annual pay at the time of retirement, or at the time of vesting his retirement, or 50% of average pay over the highest 5 year period, whichever is higher, plus an additional 3% annuity per year for every year over 20 years, to maximum of 5 years, or 15%.	Up to 50% of the higher of the rate of monthly pay at the date of termination or the highest average annual salary during any 5 years of service.

Criteria: The pension plan's benefit provisions contained in the governing document and the collective bargaining agreement should be consistent and in compliance with the provisions of the Third Class City Code.

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

Finding No. 1 – (Continued)

Effect: During the prior audit period, the city determined a pension benefit for a police officer who retired on December 31, 2005, with 27 years of service, based on 71 percent of final monthly compensation, which is in excess of the Third Class City Code and the collective bargaining agreement provisions. As of the date of this audit report, the retiree, who died on May 23, 2008, and his surviving spouse have received excess benefits of $1,321 per month, which totaled approximately $91,134 from the date of retirement through the date of this audit report. Furthermore, during the prior audit period, the city determined a pension benefit for a police officer who retired on August 11, 2008, with 25 years of credited service, based on 65 percent of final monthly compensation, which is in excess of the Third Class City Code. As of the date of this audit report, the retiree is receiving excess benefits of $820 per month, which totaled approximately $30,352 from the date of retirement through the date of this audit report.

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 for its pension plans 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.

Recommendation: We again recommend that municipal officials take appropriate action to ensure the plan's benefit provisions contained in the plan's governing document and the CBA are consistent and in compliance with the Third Class City Code at their earliest opportunity to do so.

To the extent that the city is not in compliance with the Third Class City Code and/or is contractually obligated to pay benefits to existing retirees in excess of those authorized by the Third Class City Code, 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 excess benefits on the plan's future state aid allocations and submit this information to the Department.

Management's Response: The City of Shamokin is reviewing the audit finding with the plan consultant. Once this review is completed, we will comply with your audit request.

Auditor's Conclusion: Compliance will be evaluated during our next audit of the plan.

Finding No. 2 – Noncompliance With Prior Audit Recommendation – Pension Benefits Not Authorized By The Third Class City Code

Condition: As disclosed in the prior audit report, city officials provided a pension benefit in excess of the Third Class City Code. City officials included accumulated unused compensatory time, sick leave, vacation and personal leave that was not earned during the pension computation period in the determination of the highest average annual salary used to calculate monthly pension benefits for a police officer who retired on December 31, 2005. In addition, during the prior and current audit periods, city officials improperly included accumulated unused compensatory time, sick leave, vacation and personal leave that were not earned during the pension computation period in the monthly pension benefit determinations for 2 police officers who retired on August 11, 2008, and April 3, 2009, respectively.

Criteria: Ordinance No. 02-01, Section 11A, states:

> A member who retires after twenty (20) years service shall receive a retirement allowance of fifty percent (50%) of his average monthly salary at the time of his retirement, or at the time of vesting his retirement, or fifty percent (50%) of the average annual salary received during any five (5) years of service preceding retirement, which ever is higher.

Section 4303(a) of the Third Class City Code states, in part:

> The basis of the apportionment of the pension shall be determined by the rate of the monthly pay of the member at the date of injury, death, honorable discharge, vesting under section 4302.1 or retirement, or the highest average annual salary which the member received during any five years of service preceding injury, death, honorable discharge, vesting under section 4302.1 or retirement, whichever is the higher, and except as to service increments provided for in subsection (b) of this section, shall not in any case exceed in any year one-half the annual pay of such member computed at such monthly or average annual rate, whichever is the higher.

Furthermore, Section 4309 of the Third Class City Code states:

> As used in this subdivision, the term “salary” is defined as the fixed amount of compensation paid at regular, periodic intervals by the city to the member and from which pension contributions have been deducted.

Finding No. 2 – (Continued)

The department has concluded that lump-sum payments at retirement are not encompassed by "salary" or "rate of the monthly pay" as used in Section 4303(a) of the Third Class City Code, unless the payments were earned during the pension computation period.

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

Effect: The plan is paying benefits to 3 retirees in excess of those authorized by the Third Class City Code and the plan's governing document. The retirees are receiving total excess benefits of $1,533 per month, which have totaled approximately $66,399 from the dates of their respective retirements through the date of this audit report.

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 for its pension plans 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.

Recommendation: We again recommend that pension benefits be determined in accordance with the provisions of the Third Class City Code. To the extent that the city is not in compliance with the Third Class City Code and/or is contractually obligated to pay benefits to existing retirees in excess of those authorized by the Third Class City Code, 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 excess benefits on the plan's future state aid allocations and submit this information to the department.

Management's Response: The City of Shamokin is reviewing the audit finding with the plan consultant. Once this review is completed, we will comply with your audit request.

Auditor's Conclusion: Compliance will be evaluated during our next audit of the plan.

Finding No. 3 – Failure To Appoint A Chief Administrative Officer

Condition: Municipal officials did not appoint a chief administrative officer (CAO) for the pension plan by ordinance, resolution or by a motion recorded in the minutes of a council meeting.

Criteria: Section 102 of Act 205 defines the CAO as "The person who has primary responsibility for the execution of the administrative affairs of the municipality in the case of the municipality, or of the pension plan in the case of the pension plan, or the designee of that person."

Municipal officials may appoint two CAOs - one for the pension plan and one for the municipality or appoint one person to fill both positions. Act 205 identifies specific duties for each position, as follows:

CAO of the Municipality

- Supervise and direct the preparation of actuarial reports (Section 201(d));
- Certify and file actuarial valuation reports with the Public Employee Retirement Commission (Section 201(b)); and
- Make actuarial report information available to plan members (Section 201(e)).

CAO of the Pension Plan

- Annually, determine and submit to the governing body of the municipality the financial requirements of the pension plan and minimum municipal obligation (Section 302(b), Section 302(c), Section 303(b), Section 303(c) and Section 304); and
- Provide the governing body of the municipality with a cost estimate of the effect of any proposed benefit plan modification (Section 305(a)).

Cause: Plan officials were unaware of the need to appoint a CAO for the pension plan in accordance with Act 205 provisions.

Effect: The failure to formally appoint a CAO could result in important filing deadlines being overlooked, state aid being adversely affected or delayed and investment opportunities being lost.

Finding No. 3 – (Continued)

Recommendation: Because of the significance of the CAO's responsibilities to the municipality and pension plan, we recommend that the CAO be formally appointed by ordinance, resolution or motion recorded in the minutes of a council meeting. Such ordinance, resolution or motion should detail the CAO's responsibilities and be filed with other plan documents.

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

CITY OF SHAMOKIN 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. 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	$ 4,846,472	$ 6,007,300	$ 1,160,828	80.7%	$ 576,500	201.4%
01-01-07	6,264,587	6,175,523	(89,064)	101.4%	642,372	(13.9%)
01-01-09	5,642,451	6,572,732	930,281	85.8%	698,195	133.2%

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 at 130 percent of market value. 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 SHAMOKIN 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.

CITY OF SHAMOKIN POLICE PENSION PLAN
SUPPLEMENTARY INFORMATION
(UNAUDITED)

SCHEDULE OF CONTRIBUTIONS FROM EMPLOYER
AND OTHER CONTRIBUTING ENTITIES

Year Ended December 31	Annual Required Contribution	Percentage Contributed
2005	$ 146,705	100.0%
2006	144,250	100.0%
2007	51,828	100.0%
2008	56,248	100.0%
2009	61,767	100.0%
2010	57,553	100.0%

CITY OF SHAMOKIN 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	18 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 130% of the market value of assets.
Actuarial assumptions:	
Investment rate of return	8.0%
Projected salary increases	5.0%

JACK WAGNER

AUDITOR GENERAL

CITY OF SHAMOKIN POLICE PENSION PLAN
REPORT DISTRIBUTION LIST

This report was initially distributed to the following:

The Honorable Tom Corbett
Governor
Commonwealth of Pennsylvania

City of Shamokin Police Pension Plan
Northumberland County
47 East Lincoln Street
Shamokin, PA 17872

The Honorable George S. Rozinskie, Jr.	Mayor
Mr. Stephen D. Bartos	City Clerk
Ms. Brenda L. Scandle	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.