

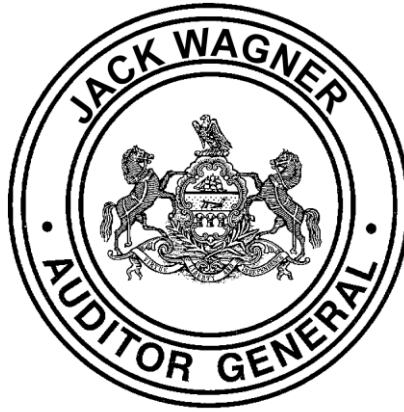
MCKEAN TOWNSHIP NONUNIFORMED PENSION PLAN

ERIE COUNTY

COMPLIANCE AUDIT REPORT

FOR THE PERIOD

JANUARY 1, 2007, TO DECEMBER 31, 2009



MCKEAN TOWNSHIP NONUNIFORMED PENSION PLAN

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CONTENTS

	<u>Page</u>
Background	1
Letter from the Auditor General	3
Findings and Recommendations:	
Finding No. 1 – Underpayment Of Pension Benefits	5
Finding No. 2 – Incorrect Data On Certification Form AG 385 Resulting In An Underpayment Of State Aid.....	6
Supplementary Information	7
Report Distribution List	11

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.

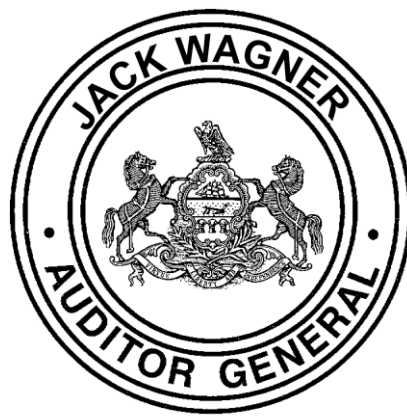
Pension plan aid is provided from a 2 percent foreign casualty insurance premium tax, a portion of the foreign fire insurance tax designated for paid firefighters and any investment income earned on the collection of these taxes. Generally, municipal pension plans established prior to December 18, 1984, 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 McKean Township 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 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 McKean Township Nonuniformed Pension Plan is a single-employer defined benefit pension plan locally controlled by the provisions of Resolution No. 1161 of 2007, as amended, effective August 1, 2007.

Prior to the adoption of Resolution No. 1161 of 2007, the pension plan was a single-employer defined contribution pension plan locally controlled by the provisions of Resolution No. 914, as amended.



Board of Township Supervisors
McKean Township
Erie County
McKean, PA 16426

We have conducted a compliance audit of the McKean Township 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 findings and conclusions based on our audit objective. We believe that the evidence obtained provides a reasonable basis for our findings 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.

Township officials are responsible for establishing and maintaining effective internal controls to provide reasonable assurance that the McKean Township 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 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 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 McKean Township 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 findings further discussed later in this report:

Finding No. 1 – Underpayment Of Pension Benefits

Finding No. 2 – Incorrect Data On Certification Form AG 385 Resulting In
An Underpayment Of State Aid

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

April 8, 2010

JACK WAGNER
Auditor General

MCKEAN TOWNSHIP NONUNIFORMED PENSION PLAN
FINDINGS AND RECOMMENDATIONS

Finding No. 1 – Underpayment Of Pension Benefits

Condition: The McKean Township Nonuniformed Pension Plan was a defined contribution pension plan until the passage of Resolution No. 1161 of 2007, which adopted a defined benefit pension plan effective August 1, 2007. A new plan custodial agreement was entered into effective October 4, 2007, and on November 1, 2007, all of the individual member's account balances were transferred to the new custodian.

The newly created defined benefit adoption agreement enacted by Resolution No. 1161 of 2007, provided that pension benefits under the new plan shall be no less than the individual account balances transferred on November 1, 2007.

A member of the pension plan retired on January 1, 2009, and subsequently died on December 21, 2009. The retiree received pension benefits from the defined benefit plan totaling \$1,905; however, the retiree had an account balance of \$9,869 transferred on November 1, 2007.

Criteria: Page AG-5 of the plan's adoption agreement states:

Monthly Benefit Formula: ...the benefit to be paid will not be less than the amount transferred from the individual accounts of each member.

Cause: Township officials failed to establish adequate internal control procedures to ensure that the benefits due to the retiree were distributed to the retiree's estate.

Effect: The estate of the deceased retiree was underpaid retirement benefits totaling \$7,964.

Recommendation: We recommend that the township, with the assistance of its solicitor, take appropriate action to ensure that the retiree's estate receives a \$7,964 distribution from the pension plan.

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

MCKEAN TOWNSHIP NONUNIFORMED PENSION PLAN
FINDINGS AND RECOMMENDATIONS

Finding No. 2 – Incorrect Data On Certification Form AG 385 Resulting In An Underpayment Of State Aid

Condition: The township understated payroll by \$11,828 in 2008 on Certification Form AG 385.

Criteria: Pursuant to the instructions that accompany Certification Form AG 385, the total payroll eligible to be certified should be Internal Revenue Service Form W-2 earnings pertaining to full-time positions.

Cause: Plan officials failed to establish adequate internal control procedures to ensure the accuracy of the data certified.

Effect: The data submitted on this certification form is used, in part, to calculate the state aid due to the township for distribution to its pension plan. Because the township's state aid allocation was based on pension costs, the township received an underpayment of state aid as identified below:

<u>Normal Cost</u>	<u>Payroll Understated</u>	<u>State Aid Underpayment</u>
7.2%	\$ 11,828	\$ 852

Although the township will be reimbursed for the underpayment of state aid due to the township's certification error, the full amount of the 2008 state aid allocation was not available to be deposited timely and therefore was not available to pay operating expenses or for investment.

Recommendation: We recommend that, in the future, plan officials establish adequate internal control procedures 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.

MCKEAN TOWNSHIP 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, 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	\$ 324,361	\$ 462,354	\$ 137,993	70.2%	\$ 279,459	49.4%

Generally accepted accounting principles require the above data to be presented as of the plan's actuarial valuation dates for the past six consecutive fiscal years. Since six years of data were not yet available, this requirement will be implemented prospectively.

MCKEAN TOWNSHIP 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.

MCKEAN TOWNSHIP NONUNIFORMED PENSION PLAN
SUPPLEMENTARY INFORMATION
(UNAUDITED)

SCHEDULE OF CONTRIBUTIONS FROM EMPLOYER
AND OTHER CONTRIBUTING ENTITIES

Year Ended December 31	Annual Required Contribution	Percentage Contributed
2007	\$ 26,466	100.0%
2008	26,466	100.0%
2009	26,466	100.0%

Generally accepted accounting principles require the above data to be presented for the past six consecutive fiscal years. Since six years of data were not yet available, this requirement will be implemented prospectively.

MCKEAN TOWNSHIP 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	12 years
Asset valuation method	Market value
Actuarial assumptions:	
Investment rate of return *	7.0%
Projected salary increases *	4.0%
* Includes inflation at	Not disclosed
Cost-of-living adjustments	None assumed

MCKEAN TOWNSHIP NONUNIFORMED PENSION PLAN
REPORT DISTRIBUTION LIST

This report was initially distributed to the following:

The Honorable Edward G. Rendell
Governor
Commonwealth of Pennsylvania

McKean Township Nonuniformed Pension Plan
Erie County
P.O. Box 62
McKean, PA 16426

Ms. Janice T. Dennis Chairperson, Board of Township Supervisors

Mr. Edward L. Hess Vice-Chairman, Board of Township Supervisors

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.