

MILLERSVILLE BOROUGH POLICE PENSION PLAN

LANCASTER COUNTY

COMPLIANCE AUDIT REPORT

FOR THE PERIOD

JANUARY 1, 2007, TO DECEMBER 31, 2008



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CONTENTS

	<u>Page</u>
Background.....	1
Letter from the Auditor General	3
Status of Prior Finding	5
Finding and Recommendation:	
Finding – Failure To Properly Determine And Fully Pay The Minimum Municipal Obligation Of The Plan	6
Supplementary Information	10
Report Distribution List	15

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 Millersville 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 600 - Police Pension Fund Act, Act of May 29, 1956 (P.L. 1804, No. 600), as amended, 53 P.S. § 761 et seq.

The Millersville Borough Police Pension Plan is a single-employer defined benefit pension plan locally controlled by the provisions of Ordinance No. 1998-4, as amended, adopted pursuant to Act 600. The plan is also affected by the provisions of collective bargaining agreements between the borough and its police officers.



The Honorable Mayor and Borough Council
Millersville Borough
Lancaster County
Millersville, PA 17551

We have conducted a compliance audit of the Millersville Borough Police Pension Plan for the period January 1, 2007, 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 finding 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. Millersville Borough contracted with an independent certified public accounting firm for annual audits of its basic financial statements which are available at the borough's offices. Those financial statements were not audited by us and, accordingly, we express no opinion or other form of assurance on them.

Borough officials are responsible for establishing and maintaining effective internal controls to provide reasonable assurance that the Millersville 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 Millersville 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 – Failure To Properly Determine And Fully Pay The Minimum
Municipal Obligation Of The Plan

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

November 13, 2009

JACK WAGNER
Auditor General

MILLERSVILLE BOROUGH POLICE PENSION PLAN
STATUS OF PRIOR FINDING

Compliance With Prior Audit Recommendation

Millersville Borough has complied with the prior audit recommendation concerning the following:

- Failure To Eliminate Member Contributions In Accordance With Act 600 And The Plan's Governing Document

Borough officials eliminated member contributions pursuant to Act 600 provisions and the plan's governing document. Borough officials also amended the plan's governing document to include a member contribution provision in accordance with Act 600.

MILLERSVILLE BOROUGH POLICE PENSION PLAN
FINDING AND RECOMMENDATION

Finding – Failure To Properly Determine And Fully Pay The Minimum Municipal Obligation Of
The Plan

Condition: Plan officials did not properly determine or fully pay the minimum municipal obligation (MMO) of the police pension plan for the year 2008, as required by Act 205. The MMO determined by the municipality was not based on data contained in the January 1, 2005, actuarial valuation report, which was the most recent actuarial valuation report certified by the Public Employee Retirement Commission (PERC) at the time the MMO was determined. Based upon an estimate prepared by this department, the municipality had an unpaid MMO balance of \$14,982 for the year 2008.

Criteria: With regard to the MMO, Section 302(b) of Act 205 states, in part:

(1) Annually, the chief administrative officer of the pension plan shall determine the financial requirements of the pension plan for the following plan year. The financial requirements of the pension plan for the following plan year shall be based on the most recent actuarial valuation report of the pension plan prepared pursuant to Chapter 2.

Section 302(c) of Act 205 states:

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. The minimum obligation of the municipality with respect to the pension plan shall be equal to the financial requirements of the pension plan reduced by the following amounts:

(1) The amount of any member contributions anticipated as receivable for the following year.

(2) If the actuarial value of the assets of the pension plan exceed the actuarial accrued liability of the pension plan, an amount equal to one-tenth of the amount by which the actuarial value exceeds the actuarial accrued liability.

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.

MILLERSVILLE BOROUGH POLICE PENSION PLAN
FINDING AND RECOMMENDATION

Finding – (Continued)

Furthermore, Section 302(e) of Act 205 states, in part:

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. . . .

Cause: Plan officials failed to establish adequate internal control procedures to ensure compliance with Act 205 requirements.

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 fully 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 fully pay the 2008 MMO by the December 31, 2008, deadline, the municipality must add the 2008 MMO balance to the current year's MMO and include interest, as required by Act 205.

Recommendation: We recommend that the municipality pay the MMO due to the police pension plan for the year 2008, with interest, in accordance with Section 302(e) of Act 205. A copy of the interest calculation must be maintained by the borough for examination during our next audit of the plan.

Management's Response: The Borough of Millersville is not under any financial constraints in meeting any debt obligations; in fact we have had and continue to have a healthy operating fund balance and thus we have no reason to intentionally understate the obligation amount in question. Standard Insurance Company has provided actuarial services to the Borough for the past 5 years. They have maintained an open channel of communication with the Public Employee Retirement Commission and the Auditor General's Office in regards to pension issues. The plan's actuary recalls specifically addressing this issue back when the circumstance arose. Obviously, the communication was not clear at the time and unfortunately we find ourselves trying to defend a position based primarily on those communications made over a year ago.

MILLERSVILLE BOROUGH POLICE PENSION PLAN
FINDING AND RECOMMENDATION

Finding – (Continued)

We understand that it is our responsibility as Plan Administrator to meet the letter of the law as you've referenced but we would ask for consideration in allowing the actuarial report used for the MMO computation under the circumstances as mentioned above and the opinion stated below. We have discussed the funding obligation shortage at length with Standard and we understand in the long term the net effect of the understatement would be accounted for when the next actuarial report is finalized. A representative of the Department indicated that our 2010 MMO could be revised to reflect the added payment thereby reducing the 2010 MMO amount due since we switched to a 5-year smoothing method of MMO calculating. That would almost produce a zero net effect, if possible.

It appears that this finding has to do with verbiage in the PA State Code Section 302 in regards to what actuarial report to use when and which MMO to use when there's a difference using the two actuarial reports. If information obtained after the audit year determined that our municipality could not meet the obligations so stated, it may make sense to make the changes as noted, especially if the net affect wasn't marginal. That isn't our case. Also please recognize that a number of local audit reports have been generated over the past couple of years that tie into the MMO figures as recommended by the actuarial valuation reports and promulgated by Borough Council in September of any given year. Changing previously reported information would complicate future financial analysis as well. Additionally, our annual General, Sewer and Solid Waste Fund budgets would have to be revised to reflect an adverse decision. Since the actuarial studies themselves are merely estimates of fund soundness, we don't believe that the *estimated* variance noted substantially affects the financial integrity of the pension fund when recognizing the next valuation report and subsequent MMO determinations.

The Borough would ask the Auditor General's Office accept the actuarial report that was used for the initial determination of the 2008 minimum municipal contribution.

We would appreciate your immediate attention to this as we would like to minimize any interest charges.

MILLERSVILLE BOROUGH POLICE PENSION PLAN
FINDING AND RECOMMENDATION

Finding – (Continued)

Auditor’s Conclusion: The Department of the Auditor General accepts that Millersville Borough had no reason or motivation to intentionally determine their 2008 MMO payment due to the police pension plan incorrectly. However, as stated in the Management Response, it is the Borough’s responsibility to comply with applicable laws and regulations. The regulation issued by the Public Employee Retirement Commission that was previously cited clearly states that if the data contained in the actuarial valuation report subsequently filed with the Commission differ from the extracted data previously certified and used to determine the minimum municipal obligation, the data resulting in the higher minimum municipal obligation will be applied in determining compliance with the actuarial funding standard. Therefore, the funding adjustment that is reported in the certified actuarial valuation report must be used to determine compliance with the funding standard, otherwise the statutory and regulatory provisions concerning MMO determinations would be rendered moot.

As to the municipality’s argument that the effect of not fully paying the 2008 MMO can be reflected in future actuarial valuation reports; as previously cited, Act 205 at Section 302(e) states that 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. (Emphasis added)

Therefore, based on the Criteria previously cited and the conclusions outlined above, the finding and recommendation remain as stated.

MILLERSVILLE 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	\$ 2,184,077	\$ 1,959,668	\$ (224,409)	111.5%	\$ 693,586	(32.4%)
01-01-05	2,903,557	2,211,675	(691,882)	131.3%	744,443	(92.9%)
01-01-07	3,281,647	2,719,272	(562,375)	120.7%	787,122	(71.4%)

MILLERSVILLE 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.

MILLERSVILLE BOROUGH POLICE PENSION PLAN
SUPPLEMENTARY INFORMATION
(UNAUDITED)

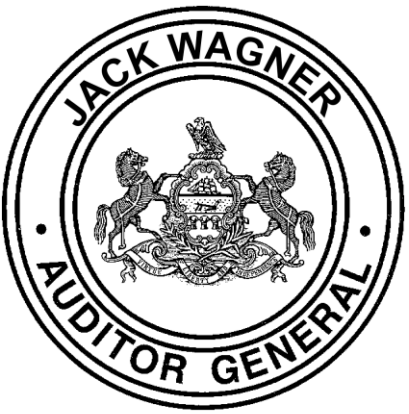
SCHEDULE OF CONTRIBUTIONS FROM EMPLOYER
AND OTHER CONTRIBUTING ENTITIES

Year Ended December 31	Annual Required Contribution	Percentage Contributed
2003	\$ 19,766	100.0%
2004	82,835	100.0%
2005	78,763	100.0%
2006	16,497	100.0%
2007	21,544	100.0%
2008	52,973	15.2%

MILLERSVILLE 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 *	7.75%
Projected salary increases *	4.75%
* Includes inflation at	Not disclosed
Cost-of-living adjustments	In no case shall the adjustment be more than 3%. The COLA will be limited to a maximum of 30%, and the COLA will not result in a monthly retirement benefit that exceeds 75% of the participant's basic monthly earnings as determined on his retirement date.



MILLERSVILLE BOROUGH POLICE PENSION PLAN
REPORT DISTRIBUTION LIST

This report was initially distributed to the following:

The Honorable Tom Corbett
Governor
Commonwealth of Pennsylvania

Millersville Borough Police Pension Plan
Lancaster County
100 Municipal Drive
Millersville, PA 17551

The Honorable Richard Moriarty	Mayor
Mr. Scott Bailey	Council President
Mr. Edward Arnold	Borough Manager
Ms. Jessie Ebersole	Administrative Assistant
Mr. James P. McAneny	Public Employee Retirement Commission

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.