

**MOUNT CARMEL BOROUGH POLICE PENSION PLAN**

**NORTHUMBERLAND COUNTY**

**COMPLIANCE AUDIT REPORT**

**FOR THE PERIOD**

**JANUARY 1, 2003, TO DECEMBER 31, 2006**





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## BACKGROUND

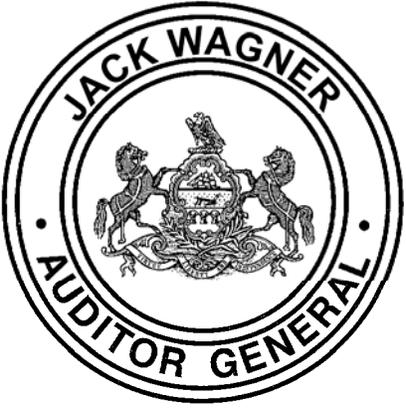
On December 18, 1984, the Pennsylvania Legislature adopted the Municipal Pension Plan Funding Standard and Recovery Act (P.L. 1005, No. 205, 53 P.S. §895.101, et seq.). The act established mandatory actuarial reporting and funding requirements and a uniform basis for the distribution of state aid to 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 Mount Carmel 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 147 - Special Ad Hoc Municipal Police and Firefighter Postretirement Adjustment Act, Act of 1988, (P.L. 1192, No. 147), as amended, 53 P.S. § 896.101, et seq.
- Act 600 - Police Pension Fund Act, Act of May 29, 1956, (P.L. (1955) 1804, No. 600), as amended, 53 P.S. § 767, et seq.

The Mount Carmel Borough Police Pension Plan is a single-employer defined benefit pension plan locally controlled by the provisions of Ordinance No. 4-81, 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  
Mount Carmel Borough  
Northumberland County  
Mount Carmel, PA 17851

We have conducted a compliance audit of the Mount Carmel Borough Police Pension Plan for the period January 1, 2003, to December 31, 2006. The audit was conducted pursuant to authority derived from Section 402(j) of Act 205 of 1984 and in accordance with *Government Auditing Standards*, issued by the Comptroller General of the United States.

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 Department of the Auditor General (Department) is mandated by state statute to calculate state aid provided to municipal pension funds and to audit municipal pension funds having received such aid. State aid is calculated by an administrative unit that is not involved in the audit process. The Department's Comptroller Office then pre-audits the calculation and submits requests to the Commonwealth's Treasury Department for the disbursement of state aid to the municipality. The Department has implemented procedures to ensure that Department audit personnel are not directly involved in the calculation and disbursement processes. The Department's mandatory responsibilities are being disclosed in accordance with *Government Auditing Standards*.

Borough officials are responsible for establishing and maintaining an internal control structure to provide reasonable assurance that the Mount Carmel Borough Police Pension Plan is administered in compliance with applicable state laws, regulations, contracts, administrative procedures, and local ordinances and policies. To assist us in planning and performing our audit, we obtained an understanding of the borough's internal control structure as it relates to the borough's compliance with those requirements. 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 Mount Carmel 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 findings and observation further discussed later in this report:

- Finding No. 1 – Partial Compliance With Prior Audit Recommendation – Failure To Properly Determine And Pay The Minimum Municipal Obligations Of The Plan
- Finding No. 2 – Noncompliance With Prior Audit Recommendation – Pension Plan Not In Compliance With Act 600 Provisions
- Finding No. 3 – Pension Benefits Not Authorized By Act 600
- Finding No. 4 – Incorrect Data Supplied To Actuary For Actuarial Valuation Report Preparation
- Observation – Failure To Prepare Financial Statements

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

April 24, 2007

JACK WAGNER  
Auditor General

MOUNT CARMEL BOROUGH POLICE PENSION PLAN  
STATUS OF PRIOR FINDINGS

Partial Compliance With Prior Audit Recommendation

- Failure To Properly Determine And Pay The Minimum Municipal Obligation Of The Plan

On October 1, 2004, the borough paid the minimum municipal obligation (MMO) due to the police pension plan for the year 2002, with interest. However, as of the date of this report, the borough has not paid the MMOs for the years 2000 and 2001, as further discussed in Finding No. 1 contained in the Findings and Recommendations section of this report.

Status Of Prior Audit Recommendation

- Failure To Prepare Financial Statements

The status of the prior audit recommendation is addressed in the Observation included in the Comments section of this report.

Noncompliance With Prior Audit Recommendation

Mount Carmel Borough has not complied with the prior audit recommendation concerning the following as further discussed in the Findings and Recommendations section of this report:

- Pension Plan Not In Compliance With Act 600 Provisions

MOUNT CARMEL BOROUGH POLICE PENSION PLAN  
FINDINGS AND RECOMMENDATIONS

Finding No. 1 – Partial Compliance With Prior Audit Recommendation – Failure To Properly Determine And Pay The Minimum Municipal Obligations Of The Plan

Condition: As disclosed in our prior audit report, plan officials did not properly determine or pay the minimum municipal obligations (MMOs) of the police pension plan for the years 2000, 2001 and 2002, as required by Act 205. On October 1, 2004, the borough paid the MMO due to the police pension plan for the year 2002, with interest. However, as of the date of this report, the 2000 and 2001 MMOs remain unpaid.

The revised MMOs determined by the municipality improperly indicated that the actuarial value of assets exceeded the present value of future benefits and, therefore, that no MMO was due to the plan for the years 2000 and 2001. However, based upon data contained in the plan's actuarial valuation report that was submitted to the Public Employee Retirement Commission (PERC), the municipality had unpaid MMOs of \$12,257 and \$12,877 for the years 2000 and 2001, respectively.

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. 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. (Emphasis added)

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, 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 did not comply with the Act 205 requirements because they did not believe MMOs were due to the plan for the years 2000 and 2001.

MOUNT CARMEL BOROUGH POLICE PENSION PLAN  
FINDINGS AND RECOMMENDATIONS

Finding No. 1 – (Continued)

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 2000 and 2001 MMOs by the respective December 31, deadlines, the municipality must add the 2000 and 2001 MMOs to the current year's MMO and include interest, as required by Act 205.

Recommendation: We again recommend that the municipality pay the MMOs due to the police pension plan for the years 2000 and 2001, 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.

Furthermore, we recommend that, in the future, plan officials properly determine and pay the MMO in accordance with Act 205 requirements.

Management's Response: Borough officials stated that they did not pay the 2000 and 2001 MMOs because the plan's actuary advised them in December of 2003 that he had revised the plan's actuarial valuation report dated January 1, 1999, and the plan's corresponding 2000 and 2001 MMOs. The actuary reported that the revised MMOs showed no amount due to the plan for those years. Municipal officials now agree with the finding and will review the situation with the plan's actuary.

Auditor's Conclusion: Because the revised actuarial valuation report was not submitted to and accepted by PERC, it cannot be used to revise the plan's 2000 and 2001 MMOs. Therefore, the finding remains as stated above.

Finding No. 2 – Noncompliance With Prior Audit Recommendation – Pension Plan Not In Compliance With Act 600 Provisions

Condition: The pension plan's governing document, Ordinance No. 4-81, as amended, contains benefit provisions that conflict with the collective bargaining agreement between the police officers and the borough and are not authorized by Act 600.

**MOUNT CARMEL BOROUGH POLICE PENSION PLAN  
FINDINGS AND RECOMMENDATIONS**

Finding No. 2 – (Continued)

Also, on April 17, 2002, Act 600 was amended by Act No. 30, which made significant changes to the statutorily prescribed benefit structure of police pension plans subject to Act 600. Municipal officials have not amended the police pension plan’s benefit structure to adopt all of the changes mandated by Act 30. The specific inconsistencies are as follows:

Benefit Provision	Governing Document	Collective Bargaining Agreement	Act 600 (as amended)
Service-related disability	Borough council shall promulgate regulations that shall provide for benefits to members who are permanently disabled while in service to the Borough.	The benefit shall be 50% of the employees’ last 36 months reduced by such payments received by Worker’s Compensation and any disability insurance that exists or may be purchased by the borough in the future.	The benefit shall be in conformity with a uniform scale and fixed by the plan’s governing document, but at least 50% of the member’s salary at the time of disability, provided that if the member receives Social Security disability benefits for the same injury, his disability benefit is reduced by the amount of the Social Security benefit.
Nonservice-related disability	None provided	The benefit shall be 50% of the employees’ last 36 months reduced by such payments received by Worker’s Compensation and any disability insurance that exists or may be purchased by the borough in the future.	Not authorized
Killed in service benefit	Borough council shall promulgate regulations that shall provide for benefits to members who are killed while in service to the Borough.	The benefit shall be provided to a surviving spouse or children up to age 18, or 23 years of age if attending college, calculated at 100% of the last 36 months average monthly salary.	Pensions for the families of members killed in service shall be calculated at 100% of the member’s salary at the time of death.

**MOUNT CARMEL BOROUGH POLICE PENSION PLAN  
FINDINGS AND RECOMMENDATIONS**

Finding No. 2 – (Continued)

<u>Benefit Provision</u>	<u>Governing Document</u>	<u>Collective Bargaining Agreement</u>	<u>Act 600 (as amended)</u>
Survivors benefits	The widow of a member of the police force, and which member retired on pension having met the age and service requirements, during course of her lifetime or so long as she does not remarry, shall be entitled to receive a pension at the rate of 50 percent of pension the member was receiving.	A widow's benefit shall be provided to a surviving spouse or children up to age 18, or 23 years of age if attending college. The amount of said pension shall be one-half (1/2) of the pension the employee was receiving or would have been entitled to receive had he been retired when he died.	A lifetime survivor's benefit shall be provided to the surviving spouse or if no spouse survives or if he or she subsequently dies, the child or children under 18 years of age or if attending college, under or attaining the age of 23. (Attending college shall mean the eligible children are registered at an accredited institution of higher learning and are carrying a minimum course load of seven credit hours per semester.)
Early retirement	None provided	A member of the police force with 20 or more years of service who terminates employment prior to superannuation retirement date may retire and receive the actuarial equivalent of a partial superannuation retirement benefit.	A member of the police force with 20 or more years of service who terminates employment prior to superannuation retirement date may retire and receive the actuarial equivalent of a partial superannuation retirement benefit.

Criteria: A governing document which contains clearly defined and updated benefit provisions is a prerequisite for the consistent, sound administration of retirement benefits. Furthermore, the police pension plan's benefit structure should be in compliance with Act 600, as amended.

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

Effect: Inconsistent plan documents could result in inconsistent or improper benefit calculations and incorrect benefit payments from the pension plan. Also, maintaining a benefit structure which is not in compliance with Act 600 could result in plan members or their beneficiaries receiving incorrect benefit amounts or being denied benefits to which they are statutorily entitled.

Recommendation: We again recommend that municipal officials, after consulting with their solicitor, take whatever action is necessary to bring the police pension plan's benefit structure into compliance with Act 600, as amended, at their earliest opportunity to do so.

MOUNT CARMEL BOROUGH POLICE PENSION PLAN  
FINDINGS AND RECOMMENDATIONS

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

MOUNT CARMEL BOROUGH POLICE PENSION PLAN  
FINDINGS AND RECOMMENDATIONS

Finding No. 3 – Pension Benefit Not Authorized By Act 600

Condition: Plan officials provided pension benefits in excess of those authorized by Act 600. Plan officials included accumulated unused compensatory time that was not earned during the pension computation period in the determination of the final average salary used to calculate monthly pension benefits for a police officer who retired during the audit period.

Criteria: Section 5(c) of Act 600 states, in part:

Monthly pension or retirement benefits other than length of service increments shall be computed at one-half the monthly average salary of such member during not more than the last sixty nor less than the last thirty-six months of employment.

Although Act 600 does not define “salary,” the department has concluded, based on a line of court opinions, that the term does not encompass lump-sum payments for leave that was not earned during the pension computation period.

Cause: Municipal officials were unaware that Act 600 does not authorize the inclusion of lump-sum payments for accumulated unused compensatory time earned outside the pension computation period in pension calculations.

Effect: The retiree is receiving excess benefits of \$282 per month, which totaled approximately \$5,076 from the date of retirement until the date of this 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 borough received state aid based on unit value during the current audit period, it did not receive allocations attributable to the excess pension benefits provided. However, in the future, 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 recommend that the borough determine pension benefits in accordance with Act 600. To the extent that the borough has already obligated itself to pay benefits to the existing retiree in excess of those authorized by Act 600, 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, the unauthorized portion of 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: Municipal officials agreed with the finding without exception.

MOUNT CARMEL BOROUGH POLICE PENSION PLAN  
FINDINGS AND RECOMMENDATIONS

Finding No. 4 – Incorrect Data Supplied To Actuary For Actuarial Valuation Report Preparation

Condition: Actuarial valuation report forms PC-201C, with valuation dates of January 1, 2003, and January 1, 2005, 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 municipality supplied the following incorrect information to the plan's actuary:

The demographic data for members terminated with vesting benefits improperly included a member who did not complete the required 12 years of service.

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 discrepancy in the data submitted to the plan's actuary occurred because plan officials did not verify the eligibility for vesting benefits for the terminated member.

Effect: Although the borough did not receive an incorrect allocation of state aid during the audit period, since a 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 could result in the borough receiving an incorrect allocation of state aid in the future.

Recommendation: 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.

MOUNT CARMEL POLICE PENSION PLAN  
POTENTIAL WITHHOLD OF STATE AID

A condition of a repeat finding such as that reported by Finding No. 1 contained in this audit report may lead to a total withholding of state aid in the future unless the finding is corrected. However, such action will not be considered if sufficient written documentation is provided to verify compliance with this department's recommendation. Such documentation should be submitted to: Department of the Auditor General, Bureau of Municipal Pension Audits, 406 Finance Building, Harrisburg, PA 17120.

MOUNT CARMEL 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, 2001, 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)]
01-01-01	\$ 2,191,709	\$ 1,689,970	\$ (501,739)	129.7%	\$ 309,550	(162.1%)
01-01-03	2,007,917	2,102,065	94,148	95.5%	325,539	28.9%
01-01-05	2,222,557	2,578,337	355,780	86.2%	456,676	77.9%

MOUNT CARMEL 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.

MOUNT CARMEL 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
2001	None	N/A
2002	\$ 22,574	100.0%
2003	31,090	114.2%
2004	31,172	100.0%
2005	90,789	100.0%
2006	120,580	100.0%

MOUNT CARMEL 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, 2005
Actuarial cost method	Entry age normal
Amortization method	Level dollar
Remaining amortization period	17 years
Asset valuation method	Fair value
Actuarial assumptions:	
Investment rate of return	7.0%
Projected salary increases	5.0%

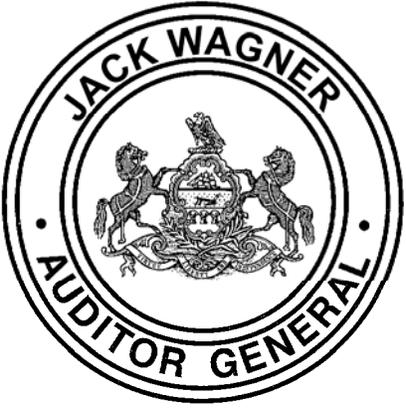
MOUNT CARMEL BOROUGH POLICE PENSION PLAN  
COMMENTS

Observation – Failure To Prepare Financial Statements

Plan officials have not prepared financial statements or required notes to the financial statements for the police pension plan for the years ended December 31, 2006, 2005, 2004 and 2003.

Financial reporting assists in fulfilling a municipality's duty to be publicly accountable and should enable users to assess accountability. Guidance for the form and content of annual financial statements and note to the financial statements can be found in Governmental Accounting Standards Board Statements No. 25 (GASB 25) and No. 3 (GASB 3), as amended by No. 40 (GASB 40).

Plan officials should consider establishing and implementing procedures to ensure the preparation of annual financial statements, which include note disclosures required by GASB 25 and GASB 3, as amended by GASB 40, in accordance with accounting principles generally accepted in the United States of America.



MOUNT CARMEL BOROUGH POLICE PENSION PLAN  
REPORT DISTRIBUTION LIST

This report was initially distributed to the following:

The Honorable Edward G. Rendell  
Governor  
Commonwealth of Pennsylvania

Mount Carmel Borough Police Pension Plan  
Northumberland County  
137 West Fourth Street  
Mount Carmel, PA 17851

The Honorable J. Kevin Jones	Mayor
Mr. Carl J. Froutz, III	Council President
Mr. Joseph K. Bass	Borough Manager

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](http://www.auditorgen.state.pa.us).