



**OLD FORGE BOROUGH POLICE
PENSION PLAN**

LACKAWANNA COUNTY

COMPLIANCE AUDIT REPORT

FOR THE PERIOD

JANUARY 1, 2009, TO DECEMBER 31, 2011

COMMONWEALTH OF PENNSYLVANIA

EUGENE A. DEPASQUALE - AUDITOR GENERAL

DEPARTMENT OF THE AUDITOR GENERAL



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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.

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 Old Forge 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 Old Forge Borough Police Pension Plan is a single-employer defined benefit pension plan locally controlled by the provisions of Ordinance No. 96-14, 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.



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EUGENE A. DePASQUALE
AUDITOR GENERAL

The Honorable Mayor and Borough Council
Old Forge Borough
Lackawanna County
Old Forge, PA 18518

We have conducted a compliance audit of the Old Forge Borough Police Pension Plan for the period January 1, 2009, to December 31, 2011. 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. Our methodology addressed determinations about the following:

- Whether state aid was properly determined and deposited in accordance with Act 205 requirements.
- Whether employer contributions are determined and deposited in accordance with the plan's governing document and applicable laws and regulations.
- Whether employee contributions are required and, if so, are determined, deducted and deposited into the pension plan and are in accordance with the plan provisions and applicable laws and regulations.

- Whether benefit payments, if any, represent payments to all (and only) those entitled to receive them and are properly determined in accordance with applicable laws and regulations.
- Whether obligations for plan benefits are accurately determined in accordance with plan provisions and based on complete and accurate participant data; and whether actuarial valuation reports are prepared and submitted to the Public Employee Retirement Commission (PERC) in accordance with state law and 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.
- Whether the terms of the unallocated insurance contract, including ownership and any restrictions, are in compliance with plan provisions, investment policies and state regulations.
- Whether benefit payments have only been made to living recipients, based on the Social Security numbers found in the pension records for retirees and beneficiaries.
- Whether Deferred Retirement Option Plan (DROP) participants' benefit payments are properly determined in accordance with the provisions of the DROP and any other applicable laws and regulations.

Old Forge 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 Old Forge 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 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 tests indicated that, in all significant respects, the Old Forge 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 further discussed later in this report:

Finding No. 1 – Noncompliance With Prior Audit Recommendation –
Improper Pension Benefit Modification

Finding No. 2 – Failure To Deposit The Full Amount Of State Aid Into The
Pension Plan

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.

The contents of this report were discussed with officials of Old Forge Borough and, where appropriate, their responses have been included in the report.



EUGENE A. DEPASQUALE
Auditor General

April 9, 2013

OLD FORGE BOROUGH POLICE PENSION PLAN
STATUS OF PRIOR FINDINGS

Compliance With Prior Audit Recommendation

Old Forge Borough has complied with the prior audit recommendation concerning the following:

- Improper Disposition Of The Proceeds Of A Cash Surrendered Insurance Policy

The borough deposited the proceeds of the cash surrendered insurance policy, less legal fees, into the pension plan.

Noncompliance With Prior Audit Recommendation

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

- Improper Pension Benefit Modification

OLD FORGE BOROUGH POLICE PENSION PLAN
FINDINGS AND RECOMMENDATIONS

Finding No. 1 – Noncompliance With Prior Audit Recommendation – Improper Pension Benefit Modification

Condition: As first disclosed in our prior audit report for the years ended December 31, 1999 and 1998, and repeated in each subsequent audit report, on April 18, 2000, Old Forge Borough enacted Ordinance No. 4 of 2000, which established disability benefits “at the rate of 70 percent of the police officer’s average monthly salary” where the previous rate had been 50 percent. On the same date, the borough enacted Resolution No. 6 of 2000, which made the increased rate applicable to an existing retiree, retroactive to April 1, 1997.

Criteria: Act 600 mandates service-related disability benefits and, at Section 5(e), authorizes the governing body of the municipality to fix the amount and commencement of payments by regulation. Therefore, the increase in the disability benefit contained in Ordinance No. 4 of 2000 is authorized under Act 600 and unobjectionable, provided that the increased benefit is applied prospectively, i.e., only to those police officers who retire on service-related disability after the effective date of the ordinance.

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

Effect: The referenced retiree’s original monthly benefit was \$1,291, calculated at 50 percent of average monthly salary, was subsequently retroactively increased to \$1,936, calculated at 70 percent of average monthly salary, inclusive of cost-of-living adjustments.

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 did not receive state aid for this pension plan in 2009 and received state aid based on unit value in 2010 and 2012, it did not receive allocations in those years attributable to the unauthorized pension benefits provided. However, since the borough received state aid based on pension costs in 2011, the provision of the unauthorized pension benefits may have resulted in the receipt of excess state aid in 2011 and could increase the municipal contributions necessary to fund the plan in accordance with Act 205 funding standards.

OLD FORGE BOROUGH POLICE PENSION PLAN
FINDINGS AND RECOMMENDATIONS

Finding No. 1 – (Continued)

Recommendation: We again recommend that municipal officials adjust the referenced retiree's pension benefit to be in accordance with the ordinance that was in effect at the time of his retirement.

If municipal officials determine that the borough remains obligated to continue paying the unauthorized pension benefit to the retiree, 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, municipal officials should consult with the plan's actuary to determine if Supplemental Actuarial Information Form AG-MP-1 should be prepared. If it is determined the excess benefits had an impact on the borough's state aid allocation received in 2011, the form should be submitted to the Department. Furthermore, after the submission of the form, the plan's actuary should contact the Department to verify the overpayment of state aid received and plan officials should then reimburse the overpayment to the Commonwealth.

Management's Response: Municipal officials were notified that a written response to this finding would be required; however, no such response has been provided.

Auditor's Conclusion: The Department will continue to monitor the borough's compliance with this audit finding subsequent to the release of the audit report.

Finding No. 2 – Failure To Deposit The Full Amount Of State Aid Into The Pension Plan

Condition: The municipality did not deposit the full amount of its 2010 and 2011 state aid allocations into the pension plan. The municipality received its 2010 and 2011 state aid allocations in the amounts of \$54,992 and \$79,264, on September 26, 2010, and April 26, 2012, respectively; however, only state aid totaling \$101,152 was deposited into an eligible pension plan. Since the finding contained in the nonuniformed pension plan audit report recommends the borough reimbursed an overpayment of their 2010 state aid allocation to the Commonwealth in the amount of \$6,470, and the municipality has met its funding obligations to its nonuniformed defined contribution plans for the years 2010 and 2011, the remaining balance of the undeposited state aid allocations must be deposited into the police pension plan.

OLD FORGE BOROUGH POLICE PENSION PLAN
FINDINGS AND RECOMMENDATIONS

Finding No. 2 – (Continued)

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 funds or the alternate funding mechanisms applicable to the respective pension plans.

Cause: The borough failed to establish adequate internal control procedures to ensure that the full amount of the 2010 and 2011 state aid allocations were deposited in accordance with Act 205 provisions.

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.

Recommendation: We recommend that the municipality deposit the balance of the undeposited 2010 and 2011 state aid allocations, plus interest, into the police pension plan after the reimbursement is made to the Commonwealth pursuant to the finding contained in the nonuniformed pension plan audit report. A copy of the interest calculation must be maintained by the borough for examination during our next audit of the plan.

We also recommend that plan officials develop and implement adequate internal control procedures to ensure that future state aid allocations are fully deposited into an eligible pension plan in accordance with Act 205 requirements.

Management's Response: Municipal officials indicated that they would provide a written response to this finding within 10 days; however, no such response has been provided.

Auditor's Conclusion: The Department will continue to monitor the borough's compliance with this audit finding subsequent to the release of the audit report.

OLD FORGE BOROUGH 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 that 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, 402-D Finance Building, Harrisburg, PA 17120.

OLD FORGE 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. The historical information, beginning as of January 1, 2007, 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)]
01-01-07	\$ 2,278,580	\$ 1,900,090	\$ (378,490)	119.9%	\$ 158,699	(238.5%)
01-01-09	2,211,294	2,105,286	(106,008)	105.0%	198,111	(53.5%)
01-01-11	2,176,459	2,189,391	12,932	99.4%	245,771	5.3%

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 which will be limited to a maximum of 130 percent and a minimum of 70 percent of the fair market value of assets. The market value of the plan's assets at 01-01-11 has been adjusted to reflect the smoothing of gains and/or losses which will be limited to a maximum of 120 percent and a minimum of 80 percent of the fair market value of assets. These methods 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.

OLD FORGE 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.

OLD FORGE 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
2006	None	N/A
2007	None	N/A
2008	None	N/A
2009	None	N/A
2010	None	N/A
2011	\$ 42,906	100.0%

OLD FORGE 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, 2011
Actuarial cost method	Entry age normal
Amortization method	Level dollar
Remaining amortization period	20 years
Asset valuation method	The actuarial value of assets will be limited to a maximum of 120% and a minimum of 80% of the fair market value of assets.
Actuarial assumptions:	
Investment rate of return	7.0%
Projected salary increases	5.0%
Cost-of-living adjustments	4.0% per year postretirement

OLD FORGE BOROUGH POLICE PENSION PLAN
REPORT DISTRIBUTION LIST

This report was initially distributed to the following:

The Honorable Tom Corbett
Governor
Commonwealth of Pennsylvania

Old Forge Borough Police Pension Plan
Lackawanna County
310 South Main Street
Old Forge, PA 18518

The Honorable Michele Petrini Avvisato	Mayor
Mr. Brian Rinaldi	Council President
Ms. MaryLynn Bartoletti	Borough Manager

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