

PENBROOK BOROUGH POLICE PENSION PLAN

DAUPHIN COUNTY

COMPLIANCE AUDIT REPORT

FOR THE PERIOD

JANUARY 1, 2008, TO DECEMBER 31, 2009



PENBROOK BOROUGH POLICE PENSION PLAN

DAUPHIN COUNTY

COMPLIANCE AUDIT REPORT

FOR THE PERIOD

JANUARY 1, 2008, TO DECEMBER 31, 2009

CONTENTS

	<u>Page</u>
Background.....	1
Letter from the Auditor General	3
Finding and Recommendation:	
Finding – Failure To Properly Determine And Fully Pay The Minimum Municipal Obligation Of The Plan	5
Supplementary Information	7
Report Distribution List	11

ABBREVIATION

PMRS - Pennsylvania Municipal Retirement System

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 Penbrook 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 15 - Pennsylvania Municipal Retirement Law, Act of February 1, 1974
(P.L. 34, No. 15), as amended, 53 P.S. § 881.101 et seq.

The Penbrook Borough Police Pension Plan is a single-employer defined benefit pension plan locally controlled by the provisions of an ordinance dated March 5, 1979, adopted pursuant to Act 15. 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
Penbrook Borough
Dauphin County
Harrisburg, PA 17103

We have conducted a compliance audit of the Penbrook Borough Police Pension Plan for the period January 1, 2008, 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 finding and conclusions based on our audit objective. We believe that the evidence obtained provides a reasonable basis for our finding 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 the objective identified above. The Penbrook Borough Police Pension Plan participates in the Pennsylvania Municipal Retirement System (PMRS), which is an agent multiple-employer public employee retirement system that acts as a common investment and administrative agent for participating municipal pension plans. PMRS issues a separate Comprehensive Annual Financial Report, copies of which are available from the PMRS accounting office. PMRS's 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 Penbrook 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 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 Penbrook 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 Penbrook Borough and, where appropriate, their responses have been included in the report.

December 27, 2010

JACK WAGNER
Auditor General

PENBROOK 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 and fully pay the minimum municipal obligation (MMO) of the police pension plan for the years 2009 and 2010, as required by Act 205. The MMOs determined by the municipality understated payroll by \$74,836 and \$84,415 in 2009 and 2010, respectively. Based upon an estimate prepared by this department, the municipality had unpaid MMO balances of \$16,973 and \$19,146 for the years 2009 and 2010, 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.

With regard to the payroll estimate used in the preparation of the MMO, the Pennsylvania Code, Title 16, Section 204.1(c)(1) states, in part:

The payroll used in determining the minimum municipal obligation of a pension plan under section 302(c) of the act shall be based on the payroll to be reported on the Internal Revenue Service Form W-2 and shall be calculated as the total payroll for active members of the plan as of the date of the determination, plus the payroll for the same active members of the plan projected to the year's end using the payroll rates in effect as of the date of the determination.

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 failed to establish adequate internal control procedures to ensure the MMOs were properly determined and fully paid as required by Act 205.

PENBROOK BOROUGH POLICE PENSION PLAN
FINDING AND RECOMMENDATION

Finding – (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 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 2009 and 2010 MMOs by the December 31, 2009 and 2010 deadlines, the municipality must add the outstanding MMO balances to the current year’s MMO and include interest, as required by Act 205.

Recommendation: We recommend that the municipality pay the outstanding MMOs due to the police pension plan for the years 2009 and 2010, plus 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 establish adequate internal control procedures to ensure the MMO is properly determined and paid in accordance with Act 205 requirements.

Management’s Response: Municipal officials disagreed with the finding and recommendation. The borough manager indicated that the plan has been reviewed by PMRS on several occasions since he became borough manager and they have not found it to be underfunded in any way. In addition, subsequent to the preparation of the 2009 and 2010 MMOs, the borough incurred additional costs for the police department due to the hiring of an additional full-time police officer and extending the amount of overtime worked and these factors were beyond the borough’s control. Additionally, the borough feels that while there may have errors in the payroll estimates, they did not deliberately underfund the plan and that absent the ability to show such intent, the finding should be rescinded.

Auditor’s Conclusion: As previously stated, our audit objective is to determine if the pension plan was administered in compliance with applicable state laws, regulations, contracts, administrative procedures, and local ordinances and policies. As indicated in the Management Response, a municipality is required to estimate the total payroll to be used in the determination of the plan’s MMO. The audit finding is not intended to give the impression municipal officials deliberately intended to underfund the plan. However, the fact remains that the payroll estimates used in the 2009 and 2010 MMO determinations were materially understated. Therefore, based on the condition and criteria previously cited, the finding and recommendation remain as stated.

PENBROOK 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, 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	\$ 2,499,529	\$ 2,088,135	\$ (411,394)	119.7%	\$ 331,348	(124.2%)
01-01-07	2,744,343	2,472,546	(271,797)	111.0%	379,587	(71.6%)
01-01-09	3,206,760	2,944,388	(262,372)	108.9%	470,039	(55.8%)

PENBROOK 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.

PENBROOK 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
2004	None	N/A
2005	None	N/A
2006	None	N/A
2007	\$ 36,969	100.0%
2008	42,073	120.7%
2009	62,166	72.7%

PENBROOK 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, 2009
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	6.0%, net of expenses
Projected salary increases *	4.5%
* Includes inflation at	3.0%
Cost-of-living adjustments	3.0%, where applicable

PENBROOK BOROUGH POLICE PENSION PLAN
REPORT DISTRIBUTION LIST

This report was initially distributed to the following:

The Honorable Tom Corbett
Governor
Commonwealth of Pennsylvania

Penbrook Borough Police Pension Plan
Dauphin County
150 South 28th Street
Penbrook, PA 17103

The Honorable Kenneth J. Cramer	Mayor
Mr. Kevin Rampert	Council President
Mr. James Armbruster	Borough Manager
Ms. Ronda White	Treasurer
Ms. Kristine Cline	Pennsylvania Municipal Retirement System

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.