

POTTSTOWN BOROUGH POLICE PENSION PLAN

MONTGOMERY COUNTY

COMPLIANCE AUDIT REPORT

FOR THE PERIOD

JANUARY 1, 2009, TO DECEMBER 31, 2010



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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 Pottstown 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 December 14, 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. 1804, No. 600), as amended, 53 P.S. § 761 et seq.

The Pottstown Borough Police Pension Plan is a single-employer defined benefit pension plan locally controlled by the provisions of Ordinance No. 1679, 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
Pottstown Borough
Montgomery County
Pottstown, PA 19464

We have conducted a compliance audit of the Pottstown Borough Police Pension Plan for the period January 1, 2009, to December 31, 2010. 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 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. Pottstown 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 Pottstown 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 Pottstown 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 –
Restated Plan Document Not Adopted By Ordinance

Finding No. 2 – Noncompliance With Prior Audit Recommendation –
Pension Benefits In Excess Of Act 600

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

October 14, 2011

JACK WAGNER
Auditor General

POTTSTOWN BOROUGH POLICE PENSION PLAN
STATUS OF PRIOR FINDINGS

Compliance With Prior Audit Recommendations

Pottstown Borough has complied with the prior audit recommendations concerning the following:

- Incorrect Data On Certification Form AG 385 Resulting In A Net Overpayment Of State Aid

The borough reimbursed \$8,698 to the Commonwealth for the overpayment of state aid.

- Incorrect Data Supplied To Actuary For Actuarial Valuation Report Preparation

The borough submitted a revised January 1, 2007, actuarial valuation report to the Public Employee Retirement Commission. In addition, the January 1, 2009, actuarial valuation report contained the correct data.

Noncompliance With Prior Audit Recommendations

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

- Restated Plan Document Not Adopted By Ordinance
- Pension Benefits In Excess Of Act 600

POTTSTOWN BOROUGH POLICE PENSION PLAN
FINDINGS AND RECOMMENDATIONS

Finding No. 1 – Noncompliance With Prior Audit Recommendation – Restated Plan Document
Not Adopted By Ordinance

Condition: As disclosed in the prior audit report, the terms, provisions and conditions of the police pension plan were restated in a separately executed plan agreement with the Pottstown Police Pension/Investment Board effective September 13, 2006. However, the restated plan agreement has not been formally adopted by an ordinance that would properly amend the plan's existing governing ordinance.

Criteria: Act 600 at Section 1(a)(1) states, in part:

Each borough, town and township of this Commonwealth maintaining a police force of three or more full-time members and each regional police department shall, and all other boroughs, towns or townships may, establish, by ordinance or resolution, a police pension fund. . . .

Furthermore, in Wynne v. Lower Merion Township, 181 Pa. Superior Ct., 524, the Pennsylvania Superior Court held that an ordinance may be amended only by another ordinance and not by a resolution.

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

Effect: The failure to properly adopt the plan agreement could result in improper or inconsistent benefit payments to plan members and their beneficiaries.

Recommendation: We again recommend that municipal officials take appropriate action to formally adopt the restated plan document through a properly executed ordinance.

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

Finding No. 2 – Noncompliance With Prior Audit Recommendation – Pension Benefits In
Excess Of Act 600

Condition: As disclosed in the prior audit report, the restated plan document and collective bargaining agreement between the police officers and the borough grant cost of living adjustments (COLAs) for survivors which are not authorized by Act 600.

POTTSTOWN BOROUGH POLICE PENSION PLAN
FINDINGS AND RECOMMENDATIONS

Finding No. 2 – (Continued)

Criteria: Section 5(g) (1) of Act 600 states, in part:

The ordinance or resolution establishing the police pension fund may provide for a cost of living increase for members of the police force receiving retirement benefits. (Emphasis added)

Therefore, Act 600 does not provide for COLAs for surviving spouses.

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

Effect: The pension plan is paying pension benefits to 5 survivors in excess of those authorized by Act 600. Providing unauthorized pension benefits increases the plan's pension costs and reduces the amounts of funds available for investment purposes or for the payment of authorized benefits or administrative expenses. Although the borough did not receive any excess state aid during the audit period attributable to the excess benefits provided, the payment of excess benefits resulted in the borough receiving excess state aid totaling \$8,190 in 2006 and 2007.

Recommendation: We recommend the borough reimburse the \$8,190 of excess state aid received for the years 2006 and 2007 to the Commonwealth. A check in this amount, with interest compounded annually from the date of receipt to date of repayment, at a rate earned by the plan, should be made payable to: Commonwealth of Pennsylvania and mailed to: Department of the Auditor General, Municipal Pension & Fire Relief Programs Unit, 11 Stanwix Street, Suite 1450, Pittsburgh, PA 15222. A copy of the interest calculation must be submitted along with the check.

In addition, we again recommend that the borough comply with Act 600 upon the renewal, extension, or renegotiation of the collective bargaining agreement. To the extent that the borough is not in compliance with Act 600 and/or is contractually obligated to pay benefits to existing beneficiaries 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, 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 borough's future state aid allocations and submit this information to the department.

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

POTTSTOWN 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	\$14,621,541	\$13,379,494	\$ (1,242,047)	109.3%	\$ 2,551,835	(48.7%)
01-01-07	15,677,645	15,243,030	(434,615)	102.9%	3,028,575	(14.4%)
01-01-09	14,912,717	17,606,635	2,693,918	84.7%	3,461,228	77.8%

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 subject to a corridor between 70 to 130 percent of the market value of assets. This method 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.

POTTSTOWN 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.

POTTSTOWN BOROUGH POLICE PENSION PLAN
 SUPPLEMENTARY INFORMATION
 (UNAUDITED)

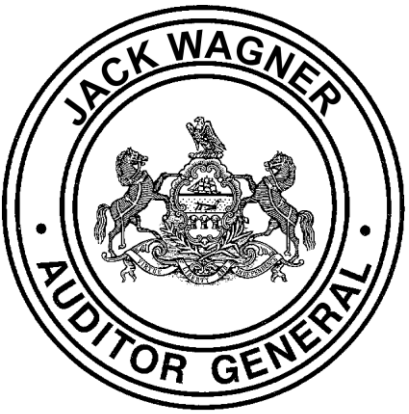
SCHEDULE OF CONTRIBUTIONS FROM EMPLOYER
 AND OTHER CONTRIBUTING ENTITIES

Year Ended December 31	Annual Required Contribution	Percentage Contributed
2005	None	N/A
2006	\$ 219,514	101.2%
2007	241,969	108.3%
2008	289,598	100.0%
2009	298,187	132.8%
2010	288,444	207.7%

POTTSTOWN 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	Level dollar
Remaining amortization period	17 years
Asset valuation method	Plan assets are valued using the method described in Section 210 of Act 205, as amended, subject to a corridor between 70-130% of the market value of assets.
Actuarial assumptions:	
Investment rate of return *	7.0%
Projected salary increases *	4.0%
* Includes inflation at	Not disclosed
Cost-of-living adjustments	Based on Philadelphia CPI - For those retired after 1/1/95 to 8/10/97, a maximum of 7.5% of final average compensation; for those retired on or after 8/11/97, a maximum of 15% of final average compensation.



POTTSTOWN BOROUGH POLICE PENSION PLAN
REPORT DISTRIBUTION LIST

This report was initially distributed to the following:

The Honorable Tom Corbett
Governor
Commonwealth of Pennsylvania

Pottstown Borough Police Pension Plan
Montgomery County
100 North High Street
Pottstown, PA 19464

The Honorable Bonnie Heath	Mayor
Mr. Stephen M. Toroney	Council President
Mr. Jason M. Bobst	Borough Manager
Ms. Janice Lee	Finance Director
Mr. Charles McClincy	Chairman, Police Pension Board

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.