

LIMITED PROCEDURES ENGAGEMENT

West Caln Township Police Pension Plan Chester County, Pennsylvania For the Period January 1, 2012 to December 31, 2015

September 2016



Commonwealth of Pennsylvania
Department of the Auditor General

Eugene A. DePasquale • Auditor General



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EUGENE A. DePASQUALE
AUDITOR GENERAL

Board of Township Supervisors
West Caln Township
Chester County
Wagontown, PA 19376

We conducted a Limited Procedures Engagement (LPE) of the West Caln Township Police Pension Plan for the period January 1, 2012 to December 31, 2015 to determine its compliance with applicable state laws, regulations, contracts, administrative procedures, and local ordinances and policies. We also evaluated compliance with some requirements subsequent to that period when possible. The LPE was conducted pursuant to authority derived from Section 402(j) of the Municipal Pension Plan Funding Standard and Recovery Act (P.L. 1005, No. 205, as amended, 53 P.S. § 895.101 et seq.) but was not conducted in accordance with *Government Auditing Standards* issued by the Comptroller General of the United States. 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. We believe that the evidence obtained provides a reasonable basis to support our LPE results.

Our LPE was limited to determining the following:

- Whether municipal officials took appropriate corrective action to address the findings contained in our prior audit report, by inquiring of plan officials and evaluating supporting documentation provided by officials evidencing that the suggested corrective action has been appropriately taken.
- Whether state aid was properly determined and deposited in accordance with Act 205 requirements by verifying the annual deposit date of state aid and determining whether deposits were made within 30 days of receipt for all years within the engagement period.
- Whether annual employer contributions were calculated and deposited in accordance with the plan's governing document and applicable laws and regulations by examining the municipality's calculation of the plan's annual financial requirements and minimum municipal obligation (MMO) and comparing these calculated amounts to amounts actually budgeted and deposited into the pension plan as evidenced by supporting documentation.

- Whether the January 1, 2011, January 1, 2013 and January 1, 2015 actuarial valuation reports were prepared and submitted to the Public Employee Retirement Commission (PERC) by March 31, 2012, 2014 and 2016, respectively, in accordance with Act 205 and whether 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 by comparing selected information to supporting source documentation.

Based on the results of our procedures performed during our LPE, nothing came to our attention indicating that the West Caln Township Police Pension Plan was not being 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 subsequent to this letter:

- Finding No. 1 – Noncompliance With Prior Audit Recommendation – Incorrect Data On Certification Form AG 385 Resulting In A Net Underpayment Of State Aid
- Finding No. 2 – Noncompliance With Prior Audit Recommendation – Failure To Properly Determine And Fully Pay The Minimum Municipal Obligation Of The Plan

The findings contained in this LPE results letter repeat conditions that were cited in our previous audit report that have not been corrected by township officials. We are concerned by the township's failure to correct those previously reported audit findings and strongly encourage timely implementation of the recommendations noted in this letter.

Our determination to perform a LPE for this engagement period does not preclude the Department from conducting an audit in accordance with *Government Auditing Standards* of the pension plan in subsequent periods. The township should continue to maintain documentation related to this 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 letter were discussed with officials of West Caln Township and, where appropriate, their responses have been included in this letter.

September 12, 2016


EUGENE A. DEPASQUALE
Auditor General

CONTENTS

| | <u>Page</u> |
|---|-------------|
| Status of Prior Findings | 1 |
| Findings and Recommendations: | |
| Finding No. 1 – Noncompliance With Prior Audit Recommendation – Incorrect Data On Certification Form AG 385 Resulting In A Net Underpayment Of State Aid..... | 2 |
| Finding No. 2 – Noncompliance With Prior Audit Recommendations - Failure To Properly Determine And Fully Pay The Minimum Municipal Obligation Of The Plan | 3 |
| Potential Withhold of State Aid | 6 |
| Supplementary Information | 7 |
| Distribution List | 13 |

WEST CALN TOWNSHIP POLICE PENSION PLAN
STATUS OF PRIOR FINDINGS

Noncompliance With Prior Audit Recommendations

West Caln Township has not complied with the prior audit recommendations concerning the following as further discussed in the Findings and Recommendations section of this letter:

- Incorrect Data On Certification Form AG 385 Resulting In A Net Underpayment Of State Aid
- Failure To Properly Determine and Fully Pay The Minimum Municipal Obligation Of The Plan

WEST CALN TOWNSHIP POLICE PENSION PLAN
FINDINGS AND RECOMMENDATIONS

Finding No. 1 - Noncompliance With Prior Audit Recommendation - Incorrect Data On Certification Form AG 385 Resulting In A Net Underpayment Of State Aid

Condition: As disclosed in the prior audit report, the township certified 2 ineligible police officers and certified 2 ineligible non-uniformed employees on the Certification Form AG 385 filed in 2009. In addition, the township certified 2 ineligible police officers and certified 1 ineligible non-uniformed employee on the Certification Form AG 385 filed in 2010. The township also failed to certify 2 eligible police officers on the Certification Form AG 385 filed in 2011. Furthermore, the township certified 1 ineligible non-uniformed employee on the Certification Form AG 385 filed in 2012. The effect on the township's state aid allocations was a net underpayment of state aid in the amount of \$10,126.

During the current engagement period, although the township properly certified 2 eligible police officers and their corresponding payroll of \$148,527 on the Certification Form AG 385 filed in 2013, the township incorrectly indicated the plan was established on January 4, 2010, not the actual plan establishment date of November 1, 2007. Therefore, since the plan establishment date on the form indicated the plan was established subsequent to January 1, 2010, the township did not receive an allocation of state aid for the police pension plan.

Criteria: Section 402(d) of Act 205 states that pension plans established subsequent to December 18, 1984, must be maintained for at least three plan years before becoming eligible for state aid. Furthermore, Section 102 of Act 205 defines a plan year as "a calendar year commencing on January 1 and ending on December 31."

Cause: Plan officials entered an incorrect plan establishment date on the 2013 Certification Form AG 385 rather than the actual establishment date of November 1, 2007; therefore, based on the certification error, the township was deemed ineligible to receive state aid for the police pension plan in 2013.

In addition, plan officials failed to establish adequate internal control procedures to ensure the accuracy of the data certified.

WEST CALN TOWNSHIP POLICE PENSION PLAN
FINDINGS AND RECOMMENDATIONS

Finding No. 1 - (Continued)

Effect: The data submitted on this certification form is used, in part, to calculate the state aid due to the municipality for distribution to its pension plans.

The effect on the township’s 2013 state aid allocation is illustrated below:

| <u>State Aid Allocation</u> | <u>State Aid Entitlement</u> | <u>State Aid Overpayment (Underpayment)</u> |
|---------------------------------|----------------------------------|---|
| \$ 18,625 | \$ 46,612 | \$ (27,987) |

Although the township will be reimbursed for the underpayment of state aid due to the township’s certification error, the full amount of the state aid allocation due was not available to be deposited timely and therefore was not available to pay operating expenses or for investment.

Recommendation: We again recommend that plan officials establish adequate internal control procedures to ensure compliance with the instructions that accompany Certification Form AG 385 to assist them in accurately reporting the required pension data.

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

Auditor’s Conclusion: Compliance will be evaluated during our next engagement.

Finding No. 2 - Failure To Properly Determine And Fully Pay The Minimum Municipal Obligation Of The Plan

Condition: As disclosed in the prior audit report, plan officials did not properly determine the minimum municipal obligation (MMO) of the police pension plan for the years 2011 and 2012, as required by Act 205. In addition, the township did not fully pay the MMOs due for the years 2011 and 2012. The MMOs determined by the municipality understated payroll by \$29,709 for the year 2011 and \$21,027 for the year 2012. Based upon an estimate prepared by this Department, the municipality had unpaid MMO balances of \$6,194 for the year 2011 and \$4,384 for the year 2012.

WEST CALN TOWNSHIP POLICE PENSION PLAN
FINDINGS AND RECOMMENDATIONS

Finding No. 2 - (Continued)

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:

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 at a rate equal to the interest assumption used for the actuarial valuation report or the discount rate applicable to treasury bills issued by the Department of Treasury of the United States with a six-month maturity as of the last business day in December of the plan year in which the obligation was due, whichever is greater, expressed as a monthly rate and compounded monthly.

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

WEST CALN TOWNSHIP POLICE PENSION PLAN
FINDINGS AND RECOMMENDATIONS

Finding No. 2 - (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 2011 and 2012 MMOs by the December 31, 2011 and December 31, 2012 deadlines, the municipality must add the unpaid MMO balances to the current year's MMO and include interest, as required by Act 205.

Furthermore, the township's future state aid allocations may be withheld until the finding recommendation is complied with.

Recommendation: We again recommend that the municipality revise the 2011 and 2012 MMO determinations and fully pay the MMOs due for the years 2011 and 2012 in accordance with Act 205 requirements.

Furthermore, we again recommend that plan officials establish adequate internal control procedures to ensure that future MMOs are properly determined and fully paid in accordance with Act 205 requirements.

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

Auditor's Conclusion: Compliance will be evaluated subsequent to the release of this report and during our next engagement.

WEST CALN TOWNSHIP POLICE PENSION PLAN
POTENTIAL WITHHOLD OF STATE AID

A condition of a repeat finding such as that reported by Finding No. 2 contained in this letter 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 & Liquor Control Audits, 314 Finance Building, Harrisburg, PA 17120.

WEST CALN TOWNSHIP POLICE PENSION PLAN
SUPPLEMENTARY INFORMATION
(UNAUDITED)

The supplementary information contained on Pages 7 and 8 reflect the implementation of GASB Statement No. 67, *Financial Reporting for Pension Plans*. The objective of this statement is to improve financial reporting by state and local governmental pension plans.

SCHEDULE OF CHANGES IN THE NET PENSION
LIABILITY AND RELATED RATIOS
FOR THE YEAR ENDED DECEMBER 31, 2014

| | |
|--|--------------------------|
| Total Pension Liability | |
| Service cost | \$ 30,878 |
| Interest | 14,457 |
| Difference between expected and actual experience | <u>(16,827)</u> |
| Net Change in Total Pension Liability | 28,508 |
| Total Pension Liability - Beginning | <u>231,984</u> |
| Total Pension Liability - Ending (a) | <u><u>\$ 260,492</u></u> |
| | |
| Plan Fiduciary Net Position | |
| Contributions - employer | \$ 30,801 |
| Net investment income | 10,253 |
| Administrative expense | <u>(481)</u> |
| Net Change in Plan Fiduciary Net Position | 40,573 |
| Plan Fiduciary Net Position - Beginning | <u>185,950</u> |
| Plan Fiduciary Net Position - Ending (b) | <u><u>\$ 226,523</u></u> |
| | |
| Net Pension Liability - Ending (a-b) | <u><u>\$ 33,969</u></u> |
| | |
| Plan Fiduciary Net Position as a Percentage of the Total Pension Liability | 86.96% |
| | |
| Estimated Covered Employee Payroll | \$ 161,639 |
| | |
| Net Pension Liability as a Percentage of Covered Employee Payroll | 21.02% |

WEST CALN TOWNSHIP POLICE PENSION PLAN
 SUPPLEMENTARY INFORMATION
 (UNAUDITED)

Sensitivity of the Net Pension Liability to Changes in the Discount Rate

The following presents the net pension liability of the township, calculated using the discount rate of 5.5%, as well as what the township's net pension liability would be if it were calculated using a discount rate that is 1 percentage-point lower or 1 percentage-point higher than the current rate:

| | 1% Decrease (4.5%) | Current Discount Rate (5.5%) | 1% Increase (6.5%) |
|-----------------------|-----------------------|------------------------------------|-----------------------|
| Net Pension Liability | \$ 76,007 | \$ 33,969 | \$ (802) |

WEST CALN TOWNSHIP 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, 2011, is as follows:

| | (1) | (2) | (3) | (4) |
|--------------------------------|--|--|--|----------------------------|
| 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) |
| 01-01-11 | \$ 76,086 | \$ 114,491 | \$ 38,405 | 66.5% |
| 01-01-13 | 149,156 | 190,257 | 41,101 | 78.4% |
| 01-01-15 | 228,905 | 260,492 | 31,587 | 87.9% |

WEST CALN TOWNSHIP 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.

WEST CALN TOWNSHIP POLICE PENSION PLAN
 SUPPLEMENTARY INFORMATION
 (UNAUDITED)

SCHEDULE OF CONTRIBUTIONS FROM EMPLOYER
 AND OTHER CONTRIBUTING ENTITIES

| Year Ended December 31 | Annual Required Contribution | Percentage Contributed |
|------------------------|------------------------------|------------------------|
| 2010 | \$ 32,596 | 100.0% |
| 2011 | 36,235 | 82.9% * |
| 2012 | 34,425 | 87.3% * |
| 2013 | 29,598 | 100.0% |
| 2014 | 30,801 | 100.0% |
| 2015 | 36,145 | 100.0% |

* See Finding No. 2 contained in the Findings and Recommendations section of this report.

WEST CALN TOWNSHIP POLICE PENSION PLAN
SUPPLEMENTARY INFORMATION
NOTES TO SUPPLEMENTARY SCHEDULES
(UNAUDITED)

The information presented in the 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, 2015 |
| Actuarial cost method | Entry age normal |
| Amortization method | Level dollar |
| Remaining amortization period | 11 years |
| Asset valuation method | Fair value |
| Actuarial assumptions: | |
| Investment rate of return | 5.5%, net of expenses |
| Projected salary increases | Age-related scale for merit/seniority (e.g. age 30 – 6.4%; age 40 – 5.0%; age 50 - 4.1%; age 60 – 3.7%) |
| Cost-of-living adjustments | 3.0%, where applicable |

WEST CALN TOWNSHIP POLICE PENSION PLAN
DISTRIBUTION LIST

This letter was initially distributed to the following:

The Honorable Tom W. Wolf
Governor
Commonwealth of Pennsylvania

Mr. Paul E. Pfitzenmeyer
Chairman, Board of Township Supervisors

Mr. Donald W. Martz
Vice-Chairman, Board of Township Supervisors

Mr. Allen Martin
Township Supervisor

Mr. Thomas Siedenbuehl
Township Manager

Ms. Kristine M. Cline
Pennsylvania Municipal Retirement System

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