

COMPLIANCE AUDIT

Westtown-East Goshen Regional Police Pension Plan Chester County, Pennsylvania For the Period January 1, 2014 to December 31, 2016

October 2017



Commonwealth of Pennsylvania
Department of the Auditor General

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AUDITOR GENERAL

Board of Commissioners
Westtown-East Goshen Regional Police Commission
Chester County
West Chester, PA 19382

We have conducted a compliance audit of the Westtown-East Goshen Regional Police Pension Plan for the period January 1, 2014 to December 31, 2016. We also evaluated compliance with some requirements subsequent to that period when possible. 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 finding and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our finding 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 finding 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. To determine if commission officials took appropriate corrective action to address the finding contained in our prior audit report, we inquired of plan officials and evaluated supporting documentation provided by officials evidencing that the suggested corrective action has been appropriately taken. To determine whether the pension plan was administered in compliance with applicable state laws, regulations, contracts, administrative procedures, and local ordinances and policies, our methodology included the following:

- We determined 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 period under audit.

- We determined whether annual employer contributions were calculated and deposited in accordance with the plan's governing document and applicable laws and regulations by examining the commission'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.
- We determined whether annual employee contributions were calculated, deducted, and deposited into the pension plan in accordance with the plan's governing document and applicable laws and regulations by testing members' contributions on an annual basis using the rates obtained from the plan's governing document in effect for all years within the period under audit and examining documents evidencing the deposit of these employee contributions into the pension plan.
- We determined whether retirement benefits calculated for all 3 of the plan members who retired during the current audit period represent payments to all (and only) those entitled to receive them and were properly determined and disbursed in accordance with the plan's governing document, applicable laws and regulations by recalculating the amount of the monthly pension benefit due to the retired individuals and comparing these amounts to supporting documentation evidencing amounts determined and actually paid to the recipients. We also determined whether retirement benefits calculated for the plan member who elected to vest during the current audit period represent payments to all (and only) those entitled to receive them and were properly determined in accordance with the plan's governing document, applicable laws and regulations by recalculating the amount of the pension benefit due and comparing these amounts to supporting documentation evidencing amounts determined.
- We determined whether the January 1, 2013 and January 1, 2015 actuarial valuation reports were prepared and submitted to the former Public Employee Retirement Commission (PERC) by March 31, 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.
- We determined whether transfers were properly authorized, timely, and appropriately recorded by plan officials by examining supporting documentation for all of the transfers made during the audit period and through the completion of our fieldwork procedures.
- We determined whether provisions of the Deferred Retirement Option Plan (DROP) were in accordance with the provisions of Act 205 by examining provisions stated in the plan's governing documents.

Commission officials are responsible for establishing and maintaining effective internal controls to provide reasonable assurance that the Westtown-East Goshen Regional 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 commission’s internal controls as they relate to the commission’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 and as previously described, 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 procedures indicated that, in all significant respects, the Westtown-East Goshen Regional 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 – Noncompliance With Prior Audit Recommendation - Pension Benefit
Provision Not In Compliance With Act 600

The finding contained in this audit report repeats a condition that was cited in our previous audit report that has not been corrected by commission officials. We are concerned by the commission’s failure to correct this previously reported audit finding and strongly encourage timely implementation of the recommendation noted in this audit report.

As previously noted, the objective of our audit of the Westtown-East Goshen Regional Police Pension Plan was to determine compliance with applicable state laws, regulations, contracts, administrative procedures, and local ordinances and policies. Act 205 was amended on September 18, 2009, through the adoption of Act 44 of 2009. Among several provisions relating to municipal pension plans, the act provides for the implementation of a distress recovery program. Three levels of distress have been established:

<u>Level</u>	<u>Indication</u>	<u>Funding Criteria</u>
I	Minimal distress	70-89%
II	Moderate distress	50-69%
III	Severe distress	Less than 50%

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. However, **we are extremely concerned about the funded status of the plan contained in the schedule of funding progress included in this report which indicates the plan's funded ratio is 66.9% as of January 1, 2015**, which is the most recent data available. Based on this information, the commission is currently in Level II moderate distress status. We encourage commission officials to monitor the funding of the police pension plan to ensure its long-term financial stability.

The contents of this report were discussed with officials of Westtown-East Goshen Regional Police Commission and, where appropriate, their responses have been included in the report.

October 16, 2017



EUGENE A. DEPASQUALE
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.

Annual state aid allocations are provided from a 2 percent foreign (out-of-state) casualty insurance premium tax, a portion of the foreign (out-of-state) 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 Westtown-East Goshen Regional Police Pension Plan is also governed by implementing regulations adopted by the former 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. § 767 et seq.

The Westtown-East Goshen Regional Police Pension Plan is a single-employer defined benefit pension plan locally controlled by the provisions of Resolution No. 2013-03, adopted pursuant to Act 600. The plan is also affected by the provisions of collective bargaining agreements between the commission and its police officers. The plan was established January 1, 1983. Active members are required to contribute 5 percent of compensation to the plan. As of December 31, 2016, the plan had 26 active members, 2 terminated members eligible for vested benefits in the future, and 24 retirees receiving pension benefits from the plan.

BACKGROUND – (Continued)

As of December 31, 2016, selected plan benefit provisions are as follows:

Eligibility Requirements:

Normal Retirement	Age 50 and 25 years of service.
Early Retirement	Eligible with 20 years of service.
Vesting	A member is 100% vested after 12 years of service.

Retirement Benefit:

Benefit equals 50% of final 36 months average monthly salary. For officers hired on or after 10/10/12, the final 36 month's salary shall be computed on base salary. Service increment is \$100 per month for compensation of 26th year of service.

Survivor Benefit:

Before Retirement Eligibility	Refund of member contributions plus interest.
After Retirement Eligibility	A monthly benefit equal to 50% of the pension the member was receiving or was entitled to receive on the day of the member's death.

Service Related Disability Benefit:

If hired prior to 10/10/12, 50% of average compensation over the last 36 months of employment. If hired on or after 10/10/12, 50% of base salary.

WESTTOWN-EAST GOSHEN REGIONAL POLICE PENSION PLAN
STATUS OF PRIOR FINDING

Noncompliance With Prior Audit Recommendation

Westtown-East Goshen Regional Police Commission has not complied with the prior audit recommendation concerning the following as further discussed in the Finding and Recommendation section of this report:

- Pension Benefit Provision Not In Compliance With Act 600

WESTTOWN-EAST GOSHEN REGIONAL POLICE PENSION PLAN
FINDING AND RECOMMENDATION

**Finding – Noncompliance With Prior Audit Recommendation – Pension Benefit Provision
Not In Compliance With Act 600**

Condition: As disclosed in the prior audit report, the commission amended the pension plan by adopting Resolution No. 2013-03, which contains a service-related disability provision that does not comply with Act 600, as illustrated below:

Benefit Provision	Governing Document	Act 600 (as amended)
Service-related disability	If hired prior to 10/10/12, 50% of average 36 month compensation calculated at the time the disability commenced. If hired on or after 10/10/12, 50% of base salary.	In the case of the payment of pensions for permanent injuries incurred in service, the amount and commencement of the payments shall be fixed by regulations of the governing body of the borough, town, township or regional police department and shall be calculated at a rate no less than fifty per centum of the member’s salary at the time the disability was incurred, provided that any member who receives benefits for the same injuries under the Social Security Act (49 Stat. 620, 42 U.S.C. § 301 et. seq.) <u>shall have his disability benefits offset or reduced by the amount of such benefits.</u> All such pensions as shall be allowed to those who are retired by reason of disabilities shall be in conformity with a uniform scale. (Emphasis added.)

Criteria: The pension plan’s governing document should contain a service-related disability benefit provision that provides for a Social Security offset to be in compliance with Act 600, as amended.

Cause: The amended service-related disability benefit provision was pursuant to an arbitration award. The commission was not able to address this issue during the current audit period due to the collective bargaining agreement not having been negotiated yet. The current contract will expire on December 31, 2018.

Effect: 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.

WESTTOWN-EAST GOSHEN REGIONAL POLICE PENSION PLAN
FINDING AND RECOMMENDATION

Finding – (Continued)

Recommendation: We again recommend that commission officials, after consulting with their solicitor, take whatever action is necessary to bring the plan's service-related disability benefit provision into compliance with Act 600, as amended, at their earliest opportunity to do so.

Management's Response: The commission acknowledges that as a result of the 2013-2018 collective bargaining agreement, the governing document's service-related disability benefit provision was amended to be consistent with the collective bargaining agreement. Upon future contract negotiations, the commission will attempt through the negotiation process to amend this benefit provision to be in compliance with Act 600.

Auditor's Conclusion: Compliance will be evaluated during our next audit of the plan.

WESTTOWN-EAST GOSHEN REGIONAL POLICE PENSION PLAN
SUPPLEMENTARY INFORMATION
(UNAUDITED)

The supplementary information contained on Pages 6 and 7 reflects 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 YEARS ENDED DECEMBER 31, 2014, 2015 AND 2016

	<u>2014</u>	<u>2015</u>	<u>2016</u>
Total Pension Liability			
Service cost	\$ 326,652	\$ 308,581	\$ 324,010
Interest	1,098,662	1,193,157	1,246,735
Difference between expected and actual experience	-	284,941	-
Changes of assumptions	-	284,564	-
Benefit payments, including refunds of member contributions	<u>(792,507)</u>	<u>(798,627)</u>	<u>(896,251)</u>
Net Change in Total Pension Liability	632,807	1,272,616	674,494
Total Pension Liability - Beginning	<u>13,802,881</u>	<u>14,435,688</u>	<u>15,708,304</u>
Total Pension Liability - Ending (a)	<u>\$14,435,688</u>	<u>\$15,708,304</u>	<u>\$16,382,798</u>
Plan Fiduciary Net Position			
Contributions - employer	\$ 681,705	\$ 675,538	\$ 847,860
Contributions – state aid	201,379	180,358	218,732
Contribution - member	116,872	122,351	120,952
Net investment income	514,089	(136,251)	759,777
Benefit payments, including refunds of member contributions	<u>(792,507)</u>	<u>(798,627)</u>	<u>(896,251)</u>
Administrative expense	<u>(3,325)</u>	<u>(7,815)</u>	<u>(4,633)</u>
Net Change in Plan Fiduciary Net Position	718,213	35,554	1,046,437
Plan Fiduciary Net Position - Beginning	<u>8,819,166</u>	<u>9,537,379</u>	<u>9,572,933</u>
Plan Fiduciary Net Position - Ending (b)	<u>\$ 9,537,379</u>	<u>\$ 9,572,933</u>	<u>\$10,619,370</u>
Net Pension Liability - Ending (a-b)	<u>\$ 4,898,309</u>	<u>\$ 6,135,371</u>	<u>\$ 5,763,428</u>
Plan Fiduciary Net Position as a Percentage of the Total Pension Liability	66.1%	60.9%	64.8%
Estimated Covered Employee Payroll	\$ 2,599,736	\$ 2,280,620	\$ 2,278,638
Net Pension Liability as a Percentage of Covered Employee Payroll	188.4%	269.0%	252.9%

WESTTOWN-EAST GOSHEN REGIONAL 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 commission as of December 31, 2014, 2015, and 2016 calculated using the discount rate of 8.0%, as well as what the commission'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 (7.0%)	Current Discount Rate (8.0%)	1% Increase (9.0%)
Net Pension Liability – 12/31/14	\$ 6,588,752	\$ 4,898,309	\$ 3,470,967
Net Pension Liability – 12/31/15	\$ 7,960,719	\$ 6,135,371	\$ 4,595,777
Net Pension Liability – 12/31/16	\$ 7,647,293	\$ 5,763,428	\$ 4,171,455

SCHEDULE OF INVESTMENT RETURNS

Annual Money-Weighted Rate of Return, Net of Investment Expense:

2016	7.94%
2015	(1.42%)
2014	6.02%

WESTTOWN-EAST GOSHEN REGIONAL 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	\$ 6,590,448	\$ 10,922,714	\$ 4,332,266	60.3%
01-01-13	8,331,357	13,156,713	4,825,356	63.3%
01-01-15	10,165,770	15,201,039	5,035,269	66.9%

Note: The market values of the plan's assets at 01-01-11 and 01-01-13 have been adjusted to reflect the smoothing of gains and/or losses subject to a ceiling of 130 percent of the market value of assets. The market value of the plan's assets at 01-01-15 has been adjusted to reflect the smoothing of gains and/or losses subject to a ceiling of 120 percent of the 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.

WESTTOWN-EAST GOSHEN REGIONAL 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.

WESTTOWN-EAST GOSHEN REGIONAL POLICE PENSION PLAN
SUPPLEMENTARY INFORMATION
(UNAUDITED)

SCHEDULE OF CONTRIBUTIONS FROM EMPLOYER
AND OTHER CONTRIBUTING ENTITIES

Year Ended December 31	Annual Required Contribution	Percentage Contributed
2011	\$ 525,754	140.1%
2012	626,131	126.4%
2013	613,501	127.0%
2014	653,008	135.2%
2015	767,907	111.5%
2016	829,801	128.5%

WESTTOWN-EAST GOSHEN REGIONAL 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	12 years
Asset valuation method	Smoothing method described in Section 210 of Act 205, as amended, subject to a ceiling of 120% of the market value of assets.
Actuarial assumptions:	
Investment rate of return	8.0%
Projected salary increases	5.0%
Cost-of-living adjustments	None assumed

WESTTOWN-EAST GOSHEN REGIONAL POLICE PENSION PLAN
REPORT DISTRIBUTION LIST

This report was initially distributed to the following:

The Honorable Tom W. Wolf
Governor
Commonwealth of Pennsylvania

Mr. Charles Proctor
Chairman, Board of Commissioners

Mr. Thomas Haws
Vice-Chairman, Board of Commissioners

Mr. Rick Smith
East Goshen Township Manager

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Mr. Jonathan C. Stafford
Pension Plan Administrator

Chief Brenda M. Bernot
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Ms. Kathy Brill
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