

# COMPLIANCE AUDIT

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## Southern Regional Police Pension Plan Lancaster County, Pennsylvania For the Period January 1, 2011 to December 31, 2013

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March 2015



Commonwealth of Pennsylvania  
Department of the Auditor General

Eugene A. DePasquale • Auditor General



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**EUGENE A. DePASQUALE  
AUDITOR GENERAL**

Regional Police Commission  
Southern Regional Police Department  
Lancaster County  
Conestoga, PA 17516

We have conducted a compliance audit of the Southern Regional Police Pension Plan for the period January 1, 2011 to December 31, 2013. We also evaluated compliance with some requirements for the 2014 year 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 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.

The Southern Regional Police Commission contracted with an independent certified public accounting firm for annual audits of its basic financial statements which are available at the commission's offices. Those financial statements were not audited by us and, accordingly, we express no opinion or other form of assurance on them.

Commission officials are responsible for establishing and maintaining effective internal controls to provide reasonable assurance that the Southern 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, 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.

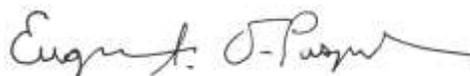
The results of our tests indicated that, in all significant respects, the Southern Regional Police Pension Plan was administered in compliance with applicable state laws, regulations, contracts, administrative procedures, and local ordinances and policies, except as noted in the following finding further discussed later in this report:

Finding – 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 or conclude on it and, accordingly, express no form of assurance on it.

The contents of this report were discussed with officials of the Southern Regional Police Commission and, where appropriate, their responses have been included in the report. We would like to thank commission officials for the cooperation extended to us during the conduct of the audit.

February 18, 2015

A handwritten signature in black ink, appearing to read "Eugene A. DePasquale". The signature is fluid and cursive, with a long horizontal stroke extending to the right.

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 Southern Regional 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.

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 Southern Regional Police Pension Plan is a single-employer defined benefit pension plan locally controlled by the provisions of Resolution No. 02-14, effective September 1, 2014, adopted pursuant to Act 15. Prior to September 1, 2014, the plan was a single-employer defined benefit pension plan controlled by the provisions of Resolution No. 02-2009, as amended, adopted pursuant to Act 600. The plan is also affected by the provisions of collective bargaining agreements between the regional and its police officers. The plan was established June 7, 1974. Active members are required to contribute 5 percent of compensation to the plan; however, member contributions were reduced to 1.3 percent of compensation to the plan in the years 2011, 2012, and 2013. As of December 31, 2013, the plan had 8 active members, 2 terminated members eligible for vested benefits in the future, and 1 retiree receiving pension benefits from the plan. On September 29, 2014, the pension plan's assets were transferred to the Pennsylvania Municipal Retirement System (PMRS).

## **BACKGROUND – (Continued)**

As of December 31, 2013, 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 compensation, plus \$25 per month for each year of service in excess of 25 (\$100 maximum).

### Survivor Benefit:

Before Retirement Eligibility	Refund of member contributions plus interest.
After Retirement Eligibility	A monthly benefit equal to 50% of the participant's vested accrued pension.

### Service Related Disability Benefit:

Benefit equals 50% of the member's salary at the time the disability was incurred, offset by Social Security disability benefits received for the same injury.

SOUTHERN REGIONAL POLICE PENSION PLAN  
STATUS OF PRIOR FINDINGS

Compliance With Prior Audit Recommendations

The Southern Regional Police Commission has complied with the prior audit recommendations concerning the following:

- Failure To Fully Pay The Minimum Municipal Obligation Of The Plan

During the current audit period, plan officials deposited the remaining 2010 minimum municipal obligation (MMO) balance, plus interest, into the pension plan; however, plan officials failed to properly determine and fully pay the 2014 MMO as noted in the Finding contained in this report; and

- Improper Vested Pension Benefit Calculation

Plan officials had the plan's consultant recalculate the vested pension benefit to exclude the unused sick pay in accordance with the plan's governing document.

SOUTHERN REGIONAL 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 or fully pay the minimum municipal obligation (MMO) of the police pension plan for the year 2014, as required by Act 205. The MMO determined by the commission understated the normal cost percentage by 1.3 percent. Based upon an estimate prepared by this department, the police pension plan had an unpaid 2014 MMO balance of \$6,206.

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.

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 that the MMO was properly determined in accordance with Act 205 requirements.

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.

SOUTHERN REGIONAL POLICE PENSION PLAN  
FINDING AND RECOMMENDATION

**Finding - (Continued)**

Due to the commission's failure to fully pay the 2014 MMO by the December 31, 2014, deadline, the commission must add the 2014 MMO balance to the current year's MMO and include interest as required by Act 205.

Recommendation: We recommend that the commission pay the MMO due to the police pension plan for the year 2014, with interest, in accordance with Section 302(e) of Act 205. A copy of the interest calculation must be maintained 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 fully paid in accordance with Act 205 requirements.

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

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

SOUTHERN 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, 2009, 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)]
01-01-09	\$ 1,231,626	\$ 931,644	\$ (299,982)	132.2%	\$ 482,397	(62.2%)
01-01-11	1,428,444	1,301,792	(126,652)	109.7%	517,217	(24.5%)
01-01-13	1,619,230	1,358,066	(261,164)	119.2%	488,547	(53.5%)

Note: The market values of the plan's assets at 01-01-09, 01-01-11, and 01-01-13, have been adjusted to reflect the smoothing of gains and/or losses over a 5-year averaging period which will be limited to a maximum of 120 percent and a minimum of 80 percent of the fair 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.

SOUTHERN 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.

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. When assets are in excess of the actuarial accrued liability, the higher the bracketed percentage, the stronger the plan.

SOUTHERN 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
2008	\$ 58,252	100.0%
2009	60,346	101.6%
2010	76,108	100.0%
2011	83,995	100.2%
2012	82,252	100.0%
2013	83,282	100.0%

SOUTHERN REGIONAL 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, 2013
Actuarial cost method	Entry age normal
Amortization method	N/A
Remaining amortization period	N/A
Asset valuation method	5-year smoothing - 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	Related to the Consumer Price Index (up to 3% in such year) with an overall benefit limit of 130% of the normal retirement benefit.

SOUTHERN REGIONAL POLICE PENSION PLAN  
REPORT DISTRIBUTION LIST

This report was initially distributed to the following:

The Honorable Tom W. Wolf  
Governor  
Commonwealth of Pennsylvania

Southern Regional Police Pension Plan  
Lancaster County  
P.O. Box 254  
Conestoga, PA 17516

Mr. Craig Eshleman	Chairman, Regional Police Commission
Mr. John Fiorill	Chief Administrative Officer
Ms. Kristine M. Cline	Pennsylvania Municipal Retirement System

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