

COMPLIANCE AUDIT

South Londonderry Township Police Pension Plan Lebanon County, Pennsylvania For the Period January 1, 2014 to December 31, 2016

March 2018



Commonwealth of Pennsylvania
Department of the Auditor General

Eugene A. DePasquale • Auditor General



**Commonwealth of Pennsylvania
Department of the Auditor General
Harrisburg, PA 17120-0018**
Facebook: Pennsylvania Auditor General
Twitter: @PAAuditorGen
www.PaAuditor.gov

EUGENE A. DEPASQUALE
AUDITOR GENERAL

Board of Township Supervisors
South Londonderry Township
Lebanon County
Palmyra, PA 17078

We have conducted a compliance audit of the South Londonderry Township 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 municipal 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 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.
- We determined that there were no employee contributions required for the years covered by our audit period due to the fact that employee contributions were appropriately waived by the municipality.
- We determined that there were no benefit calculations prepared for the years covered by our audit period
- We determined whether the January 1, 2013, January 1, 2015 and January 1, 2017 actuarial valuation reports were prepared and submitted to the former Public Employee Retirement Commission (PERC) by March 31, 2014, 2016 and 2018, 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 the terms of the plan's unallocated insurance contract, including ownership and any restrictions, were in compliance with plan provisions, investment policies, and state regulations by comparing the terms of the contract with the plan's provisions, investment policies, and state regulations.

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

Township officials are responsible for establishing and maintaining effective internal controls to provide reasonable assurance that the South Londonderry Township 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 township's internal controls as they relate to the township'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 South Londonderry Township 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 – Pension Provision Not In Compliance With Act 600

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 South Londonderry Township and, where appropriate, their responses have been included in the report. We would like to thank township officials for the cooperation extended to us during the conduct of the audit.



March 6, 2018

EUGENE A. DEPASQUALE
Auditor General

CONTENTS

	<u>Page</u>
Background	1
Status of Prior Finding	3
Finding and Recommendation:	
Finding – Pension Provision Not In Compliance With Act 600	4
Supplementary Information	6
Report Distribution List	12

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 South Londonderry Township 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:

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 South Londonderry Township Police Pension Plan is a single-employer defined benefit pension plan locally controlled by the provisions of Ordinance 191, as amended, adopted pursuant to Act 600. The plan is also affected by the provisions of collective bargaining agreements between the township and its police officers. The plan was established January 1, 1982. Active members are required to contribute 5 percent of compensation to the plan, however, member contributions were eliminated during the audit period. As of December 31, 2016, the plan had 7 active members, no terminated members eligible for vested benefits in the future, and 2 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	None
Vesting	Member is 100% vested after 12 years of service

Retirement Benefit:

Benefit equals 50% of final 36 months average salary, plus a service increment of \$100 per month after 25 years 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:

Benefit equals 75% of the member's monthly salary at the time the disability was incurred, offset by Social Security disability benefits received for the same injury, and any disability benefit payable, as funded by the plan.

SOUTH LONDONDERRY TOWNSHIP POLICE PENSION PLAN
STATUS OF PRIOR FINDING

Compliance With Prior Audit Recommendation:

South Londonderry Township has complied with the prior audit recommendation concerning the following:

- **Incorrect Pension Benefit Calculation**

Municipal officials adjusted the retiree's pension benefit as recommended and paid the retiree the amount of the increase retroactive to his retirement date.

SOUTH LONDONDERRY TOWNSHIP POLICE PENSION PLAN
FINDING AND RECOMMENDATION

Finding – Pension Provision Not In Compliance With Act 600

Condition: The pension plan's collective bargaining agreement between the police officers and the township, entered into on November 6, 2016 for the period January 1 2017 to December 31, 2019, contains a service/transfer of service credit provision that is not in compliance with Act 600, as follows:

Benefit Provision	Collective Bargaining Agreement	Act 600 (as amended)
Service Credit and Transfer of Service Credit	Article #21 (B).10 states: Officers shall be permitted to "buy back" previous years of State or Municipal Police service to count toward retirement, at an amount to be determined during the next pension actuarial study.	Section 4 of Act 600 enumerates transfers of service credits for police pension plans, including intervening and non-intervening Military Service; entering into an inter-municipal agreement for a regional police department, disbanding a police department and entering into an inter-municipal agreement with another municipality for the provision of police services, and/or subsequently re-establishes a police force and re-employs one or more police officers. <i>(As indicated above, Act 600 does not provide for the transfer of service credit from previous years of State or Municipal Police service within the enumerated conditions in Section 4 of Act 600.)</i>

Criteria: A governing document which contains clearly defined and updated benefit provisions is a prerequisite for the consistent, sound administration of retirement benefits. In addition, the police pension plan's benefit structure should be in compliance with Act 600, as amended. Moreover, provisions of the collective bargaining agreement should be consistent with the governing document and should be in compliance with Act 600 as amended.

Cause: Municipal officials were unaware that the collective bargaining agreement was not in compliance with Act 600.

Effect: Re-negotiated terms of a collective bargaining agreement could result in necessary amendments or restatement of existing plan documents. Inconsistent plan documents could result in inconsistent or improper benefit calculations and incorrect benefit payments from the pension plan.

**SOUTH LONDONDERRY TOWNSHIP POLICE PENSION PLAN
FINDING AND RECOMMENDATION**

Finding – (Continued)

Recommendation: We recommend that municipal officials, after consulting with their solicitor, take whatever action is necessary to adopt revisions to the collective bargaining agreement so that benefits are in compliance with Act 600, as amended, as soon as deemed appropriate, but not later than the expiration of the current collective bargaining agreement on December 31, 2019.

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

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

SOUTH LONDONDERRY TOWNSHIP POLICE PENSION PLAN
SUPPLEMENTARY INFORMATION
(UNAUDITED)

The supplementary information contained on Pages 6 through 8 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	\$ 82,764	\$ 100,263	\$ 105,276
Interest	172,100	145,712	159,321
Difference between expected and actual experience	-	(528,074)	-
Changes of assumptions*	-	59,858	-
Benefit payments, including refunds of member contributions	(75,100)	(75,390)	(75,390)
Net Change in Total Pension Liability	<u>179,764</u>	<u>(297,631)</u>	<u>189,207</u>
Total Pension Liability – Beginning	<u>2,106,036</u>	<u>2,285,800</u>	<u>1,988,169</u>
Total Pension Liability – Ending (a)	<u><u>\$ 2,285,800</u></u>	<u><u>\$ 1,988,169</u></u>	<u><u>\$ 2,177,376</u></u>
Plan Fiduciary Net Position			
Contributions – employer	\$ 104,203	\$ 62,190	\$ 6,806
Contribution – state aid	58,435	105,863	122,490
Net investment income	80,477	(19,833)	95,918
Benefit payments, including refunds of member contributions	(75,100)	(75,390)	(75,390)
Administrative expense	(5,375)	(6,475)	(5,600)
Net Change in Plan Fiduciary Net Position	<u>162,640</u>	<u>66,355</u>	<u>144,224</u>
Plan Fiduciary Net Position – Beginning	<u>1,587,558</u>	<u>1,750,198</u>	<u>1,816,553</u>
Plan Fiduciary Net Position – Ending (b)	<u><u>\$ 1,750,198</u></u>	<u><u>\$ 1,816,553</u></u>	<u><u>\$ 1,960,777</u></u>
Net Pension Liability – Ending (a-b)	<u><u>\$ 535,602</u></u>	<u><u>\$ 171,616</u></u>	<u><u>\$ 216,599</u></u>
Plan Fiduciary Net Position as a Percentage of the Total Pension Liability	76.6%	91.4%	90.1%
Estimated Covered Employee Payroll	\$ 512,529	\$ 543,122	\$ 570,159
Net Pension Liability as a Percentage of Covered Employee Payroll	104.5%	31.6%	38.0%

Note to schedule - Assumption Changes* – In 2015, the interest rate assumption was lowered from 8% to 7.75% per annum.

**SOUTH LONDONDERRY 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 as of December 31, 2015 and 2016, calculated using the discount rate of 7.75%, 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 (6.75%)	Current Discount Rate (7.75%)	1% Increase (8.75%)
Net Pension Liability - 12/31/15	\$ 470,132	\$ 171,616	\$ (74,954)
Net Pension Liability - 12/31/16	\$ 544,414	\$ 216,599	\$ (54,565)

Additionally, the following presents the net pension liability of the township as of December 31, 2014, calculated using the discount rate of 8%, 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 (7.0%)	Current Discount Rate (8.0%)	1% Increase (9.0%)
Net Pension Liability	\$ 853,573	\$ 535,602	\$ 271,782

**SOUTH LONDONDERRY TOWNSHIP POLICE PENSION PLAN
SUPPLEMENTARY INFORMATION
(UNAUDITED)**

SCHEDULE OF CONTRIBUTIONS

<u>Year Ended December 31</u>	<u>Actuarially Determined Contribution</u>	<u>Actual Contributions</u>	<u>Contribution Deficiency (Excess)</u>	<u>Covered-Employee Payroll</u>	<u>Contributions as a Percentage of Covered-Employee Payroll</u>
2007	\$ 65,583	\$ 65,583	\$ -	\$ 265,052	24.7%
2008	60,352	60,352	-	334,481	18.0%
2009	58,244	58,244	-	324,256	18.0%
2010	88,222	88,222	-	340,430	25.9%
2011	82,538	82,538	-	368,221	22.4%
2012	104,163	104,163	-	421,586	24.7%
2013	127,253	127,253	-	443,142	28.7%
2014	162,638	162,638	-	512,529	31.7%
2015	168,053	168,053	-	543,122	30.9%
2016	129,296	129,296	-	570,159	22.7%

SCHEDULE OF INVESTMENT RETURNS

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

2016	5.36%
2015	-1.13%
2014	5.12%

**SOUTH LONDONDERRY 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, 2013, is as follows:

Actuarial Valuation Date	(1) Actuarial Value of Assets (a)	(2) Actuarial Accrued Liability (AAL) - Entry Age (b)	(3) Unfunded (Assets in Excess of) Actuarial Accrued Liability (b) - (a)	(4) Funded Ratio (a)/(b)
01-01-13	\$ 1,341,899	\$ 1,962,602	\$ 620,703	68.4%
01-01-15	1,734,537	1,817 584	83,047	95.4%
01-01-17	2,095,733	2,144,309	48,576	97.7%

Note: The market values of the plan's assets at 01-01-13, 01-01-15, and 01-01-17 have been adjusted to reflect the smoothing of gains and/or losses over a 5-year averaging period subject to a corridor between 80 to 120 percent of the 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.

**SOUTH LONDONDERRY 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.

SOUTH LONDONDERRY 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, 2017
Actuarial cost method	Entry age normal
Amortization method	Level dollar
Remaining amortization period	3 years
Asset valuation method	5-year smoothing subject to a corridor between 80-120 percent of the market value of assets.

Actuarial assumptions:

Investment rate of return	7.75%
Projected salary increases	5%
Cost-of-living adjustments	3%

SOUTH LONDONDERRY TOWNSHIP POLICE PENSION PLAN
REPORT DISTRIBUTION LIST

This report was initially distributed to the following:

The Honorable Tom W. Wolf
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