

**SWARTHMORE BOROUGH POLICE PENSION PLAN**

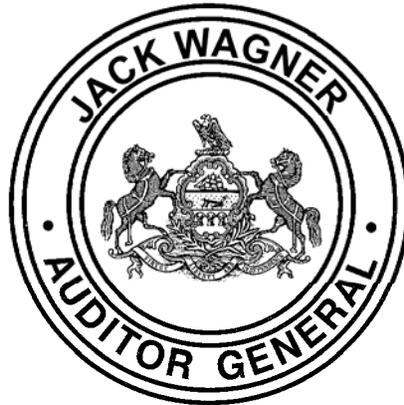
**DELAWARE COUNTY**

**COMPLIANCE AUDIT REPORT**

**FOR THE PERIOD**

**JANUARY 1, 2005, TO DECEMBER 31, 2006**





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**DELAWARE COUNTY**

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## BACKGROUND

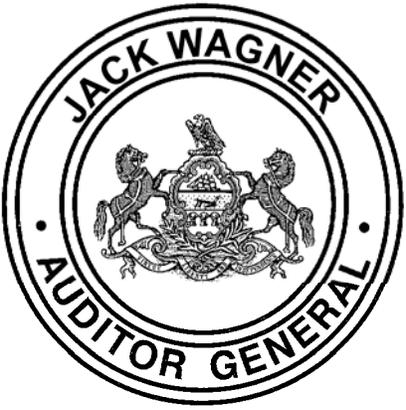
On December 18, 1984, the Pennsylvania Legislature adopted the Municipal Pension Plan Funding Standard and Recovery Act (P.L. 1005, No. 205, 53 P.S. §895.101, et seq.). The act established mandatory actuarial reporting and funding requirements and a uniform basis for the distribution of state aid to 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 Swarthmore 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 600 - Police Pension Fund Act, Act of May 29, 1956 (P.L. 1804, No. 600), as amended, 53 P.S. § 761 et seq.

The Swarthmore Borough Police Pension Plan is a single-employer defined benefit pension plan locally controlled by the provisions of Ordinance No. 825, 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  
Swarthmore Borough  
Delaware County  
Swarthmore, PA 19081

We have conducted a compliance audit of the Swarthmore Borough Police Pension Plan for the period January 1, 2005, to December 31, 2006. The audit was conducted pursuant to authority derived from Section 402(j) of Act 205 of 1984 and in accordance with *Government Auditing Standards*, issued by the Comptroller General of the United States.

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. Swarthmore Borough contracted with an independent certified public accounting firm for annual audits of the Swarthmore Borough Police Pension Plan's 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.

The Department of the Auditor General (Department) is mandated by state statute to calculate state aid provided to municipal pension funds and to audit municipal pension funds having received such aid. State aid is calculated by an administrative unit that is not involved in the audit process. The Department's Comptroller Office then pre-audits the calculation and submits requests to the Commonwealth's Treasury Department for the disbursement of state aid to the municipality. The Department has implemented procedures to ensure that Department audit personnel are not directly involved in the calculation and disbursement processes. The Department's mandatory responsibilities are being disclosed in accordance with *Government Auditing Standards*.

Borough officials are responsible for establishing and maintaining an internal control structure to provide reasonable assurance that the Swarthmore Borough Police Pension Plan is administered in compliance with applicable state laws, regulations, contracts, administrative procedures, and local ordinances and policies. To assist us in planning and performing our audit, we obtained an understanding of the borough's internal control structure as it relates to the borough's compliance with those requirements. 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 Swarthmore 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 - Partial Compliance With Prior Audit Recommendation - Failure To Adopt Benefit Provisions Mandated By Act 30
- Finding No. 2 - Noncompliance With Prior Audit Recommendation – Pension Benefit Not Authorized By Act 600
- Finding No. 3 - Unauthorized Cost Of Living Adjustment

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

September 21, 2007

JACK WAGNER  
Auditor General

SWARTHMORE BOROUGH POLICE PENSION PLAN  
STATUS OF PRIOR FINDINGS

Compliance With Prior Audit Recommendation

Swarthmore Borough has complied with the prior audit recommendation concerning the following:

- Plan's Governing Document Fails To Contain An Intervening Military Service Provision

The borough adopted Ordinance No. 1003, which contains a provision for intervening military service credit, in accordance with Act 600.

Partial Compliance With Prior Audit Recommendation

Swarthmore Borough has partially complied with the prior audit recommendation concerning the following:

- Failure To Adopt Benefit Provisions Mandated By Act 30

The borough adopted Ordinance No. 1003 to bring the police pension plan's benefit structure into compliance with Act 600, as amended by Act 30. However, the killed in service benefit and the service-related disability benefit remain unaddressed, as noted in Finding No. 1 discussed later in this report.

Noncompliance With Prior Audit Recommendation

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

- Pension Benefit Not Authorized By Act 600

SWARTHMORE BOROUGH POLICE PENSION PLAN  
FINDINGS AND RECOMMENDATIONS

Finding No. 1 – Partial Compliance With Prior Audit Recommendation – Failure To Adopt  
Benefit Provisions Mandated By Act 30

Condition: As disclosed in the status of prior findings section of this report, municipal officials partially complied with the prior audit recommendation by adopting Ordinance No. 1003. However, two benefit provisions were not addressed and are not in compliance with Act 600, as amended by Act 30. The specific inconsistencies are as follows:

<u>Benefit Provision</u>	<u>Governing Document</u>	<u>Act 600 (as amended)</u>
Killed in service benefit	100% of the officer’s total W-2 earnings in the twelve month period immediately preceding the officer’s death or the highest twelve calendar month W-2 received by that officer during his service with the Borough, whichever is higher.	Pensions for the families of members killed in service shall be calculated at 100% of the member’s salary at the time of death.
Service-related disability benefit	Police officer shall receive a pension computed at 75% of the officer’s annual salary for the thirty-six (36) month period prior to the date on which the officer is declared unable to return to active duty. This benefit will be paid only to those persons who qualify for and receive disability benefits from Social Security Administration, and the benefits paid from the Police Pension Fund will be reduced by one-half of the benefits paid by Social Security.	The benefit must be in conformity with a uniform scale and fixed by the plan’s governing document at no less than 50% of the member’s salary at the time the disability was incurred, reduced by the amount of Social Security disability benefits received for the same injury.

SWARTHMORE BOROUGH POLICE PENSION PLAN  
FINDINGS AND RECOMMENDATIONS

Finding No. 1 – (Continued)

Criteria: The police pension plan’s benefit structure should be in compliance with Act 600, as amended, by Act 30.

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

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.

Recommendation: We again recommend that municipal officials, after consulting with their solicitor, take whatever action is necessary to bring the police pension plan’s benefit structure into compliance with Act 600, as amended, at their earliest opportunity to do so.

Management’s Response: Management stated that the benefits are contractually negotiated and would be difficult to change. Management also stated that the definition of salary contained in the service-related disability provision of Act 600 was too vague for interpretation.

Auditor’s Conclusion: Based on the provisions of Act 600 previously cited, the finding remains as stated.

Finding No. 2 – Noncompliance With Prior Audit Recommendation – Pension Benefit Not Authorized By Act 600

Condition: As disclosed in our prior audit report, the pension plan’s governing document and the collective bargaining agreements (CBAs) between the police officers and the borough each grant a benefit that is not authorized by Act 600. Chapter 282 of the Codified Ordinances of the Borough of Swarthmore defines average monthly compensation for the calculation of pension benefits as follows:

The monthly compensation of a participant means all salary, wages and fees, including all overtime pay, bonuses, and severance payments, but specifically excludes amounts contributed by the employer to any public or private employee pension, insurance or welfare benefits plan (including this plan as herein set forth or as subsequently amended) or to any profit-sharing plan, or any other form of non-recurring compensation.

SWARTHMORE BOROUGH POLICE PENSION PLAN  
FINDINGS AND RECOMMENDATIONS

Finding No. 2 – (Continued)

Furthermore, the 2001–2004, 2005-2006 and the 2007-2010 CBAs all provide the following with respect to sick leave accruals:

One hundred forty-four [144] hours of sick leave per year with a maximum accumulation of 1200 hours.

The CBAs further provide:

Officers who retire on or after January 1, 2001, shall receive severance pay calculated as half of unused sick time.

Pension benefits will be computed at 50 percent of the officer’s annual salary based on W-2 forms averaged over the 36 month period prior to the officer’s date of retirement.

W-2 wages shall be called gross pay.

Therefore, in accordance with the CBAs, a retiring police officer may receive a lump-sum severance payment for unused sick leave up to a maximum of 600 hours, which is above the total amount of sick leave earned during the pension computation period.

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

Monthly pension or retirement benefits other than length of service increments shall be computed at one-half the monthly average salary of such member during not more than the last sixty nor less than the last thirty-six months of employment.

Although Act 600 does not define “salary,” the department has concluded, based on a line of court opinions, that the term does not encompass lump-sum payments for leave that was not earned during the pension computation period.

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

SWARTHMORE BOROUGH POLICE PENSION PLAN  
FINDINGS AND RECOMMENDATIONS

Finding No. 2 – (Continued)

Providing unauthorized pension benefits could increase the plan’s pension costs and reduce the amount of funds available for investment purposes or for the payment of authorized benefits or administrative expenses. The provision of unauthorized pension benefits may also result in the receipt of excess state aid in the future, and could increase the municipal contributions necessary to fund the plan in accordance with Act 205 funding standards.

Recommendation: We again recommend that the borough eliminate all benefits not authorized by Act 600 at its earliest opportunity to do so. To the extent that the borough has obligated itself 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, the excess 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 plan’s state aid allocations received during the audit period and submit this information to the Department.

Management’s Response: Municipal officials stated that the borough was under contractual obligation to provide these benefits.

Auditor’s Conclusion: Based on the provision of Act 600 previously cited, the finding remains as stated.

Finding No. 3 – Unauthorized Cost Of Living Adjustment

Condition: The borough granted an unauthorized cost of living adjustment to the surviving spouse of a former officer who died in 2006.

Criteria: Act 600 at Section 5(g)(1) states:

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. The cost of living increase shall not exceed the percentage increase in the Consumer Price Index from the year in which the police member last worked, shall not cause the total police pension benefits to exceed seventy-five per centum of the salary for computing retirement benefits and shall not cause the total cost of living increase to exceed thirty per centum. No cost of living increase shall be granted which would impair the actuarial soundness of the pension fund. (Emphasis added)

SWARTHMORE BOROUGH POLICE PENSION PLAN  
FINDINGS AND RECOMMENDATIONS

Finding No. 3 – (Continued)

Cause: The borough was not aware that Act 600 limited cost of living adjustments to only retired members of the police force. Furthermore, the plan's governing document, allows for cost of living adjustments to eligible participants of the pension plan.

Effect: The borough has been paying unauthorized benefits from the pension plan.

Providing unauthorized pension benefits could increase the plan's pension costs and reduce the amount of funds available for investment purposes or for the payment of authorized benefits or administrative expenses. The provision of unauthorized pension benefits may also result in the receipt of excess state aid in the future, and could increase the municipal contributions necessary to fund the plan in accordance with Act 205 funding standards.

Recommendation: We recommend that the borough eliminate all benefits not authorized by Act 600 at its earliest opportunity to do so. To the extent that the borough has obligated itself 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, the excess 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 plan's state aid allocations received during the audit period and submit this information to the Department.

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

SWARTHMORE 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, 2001, 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)]
01-01-01	\$ 3,656,581	\$ 2,594,511	\$ (1,062,070)	140.9%	\$ 508,822	(208.7%)
01-01-03	3,229,092	2,796,645	(432,447)	115.5%	532,168	(81.3%)
01-01-05	3,354,417	3,409,672	55,255	98.4%	573,187	9.6%

Note: The market values of the plan's assets at 01-01-03 and 01-01-05 have been adjusted to reflect the smoothing of gains and/or losses over a 4-year averaging period. 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.

SWARTHMORE 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.

SWARTHMORE 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
2001	None	N/A
2002	None	N/A
2003	\$ 5,649	100.0%
2004	39,600	100.0%
2005	39,855	100.0%
2006	92,267	100.0%

SWARTHMORE 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, 2005
Actuarial cost method	Entry age normal
Amortization method	Level dollar
Remaining amortization period	15 years
Asset valuation method	Fair value, 4-year smoothing
Actuarial assumptions:	
Investment rate of return *	8.0%
Projected salary increases *	5.0%
* Includes inflation at	Not disclosed
Cost-of-living adjustments	Discretionary, limited to a maximum of 30%.

SWARTHMORE BOROUGH POLICE PENSION PLAN  
REPORT DISTRIBUTION LIST

This report was initially distributed to the following:

The Honorable Edward G. Rendell  
Governor  
Commonwealth of Pennsylvania

Swarthmore Borough Police Pension Plan  
Delaware County  
121 Park Avenue  
Swarthmore, PA 19081

The Honorable Elric C. Gerner	Mayor
Ms. Peg Hebner-Christensen	Council President
Ms. Jane C. Billings	Borough Manager

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](http://www.auditorgen.state.pa.us).