WEST CHESTER BOROUGH NONUNIFORMED PENSION PLAN

CHESTER COUNTY

COMPLIANCE AUDIT REPORT

FOR THE PERIOD

JANUARY 1, 2010, TO DECEMBER 31, 2011

COMMONWEALTH OF PENNSYLVANIA

EUGENE A. DEPASQUALE - AUDITOR GENERAL

DEPARTMENT OF THE AUDITOR GENERAL

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CONTENTS

Page

Background 1

Letter from the Auditor General 2

Status of Prior Findings 5

Finding and Recommendation:

Finding – Noncompliance With Prior Audit Recommendation – Failure To Maintain Vested Pension Benefit Calculations 6

Supplementary Information 7

Report Distribution List 11

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.

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 West Chester Borough Nonuniformed 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 177 - General Local Government Code, Act of December 19, 1996 (P.L. 1158, No. 177), as amended, 53 Pa.C.S. § 101 et seq.

The West Chester Borough Nonuniformed Pension Plan is a single-employer defined benefit pension plan locally controlled by the provisions of Ordinance No. 7-2001, as amended. The plan is also affected by the provisions of collective bargaining agreements between the borough and its nonuniformed employees.

Commonwealth of Pennsylvania
Department of the Auditor General
Harrisburg, PA 17120-0018
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EUGENE A. DEPASQUALE
AUDITOR GENERAL

The Honorable Mayor and Borough Council
West Chester Borough
Chester County
West Chester, PA 19380

We have conducted a compliance audit of the West Chester Borough Nonuniformed Pension Plan for the period January 1, 2010, to December 31, 2011. 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 contracts, including ownership and any restrictions, are in compliance with plan provisions, investment policies and state regulations.

- Whether benefit payments have only been made to living recipients, based on the Social Security numbers found in the pension records for retirees and beneficiaries.

West Chester Borough contracted with an independent certified public accounting firm for annual audits of its basic 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.

Borough officials are responsible for establishing and maintaining effective internal controls to provide reasonable assurance that the West Chester Borough Nonuniformed 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 borough's internal controls as they relate to the borough'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 West Chester Borough Nonuniformed 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 – Failure To Maintain Vested Pension Benefit Calculations

As previously noted, one of the objectives of our audit of the West Chester Borough Nonuniformed 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:

Level	Indication	Funding Criteria
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 61.1% as of January 1, 2011**, which is the most recent date available. Based on this information, the Public Employee Retirement Commission issued a notification that the borough is currently in Level II moderate distress status. We encourage borough officials to monitor the funding of the nonuniformed pension plan to ensure its long-term financial stability.

The contents of this report were discussed with officials of West Chester Borough and, where appropriate, their responses have been included in the report.

April 24, 2013

EUGENE A. DEPASQUALE
Auditor General

WEST CHESTER BOROUGH NONUNIFORMED PENSION PLAN
STATUS OF PRIOR FINDINGS

Compliance With Prior Audit Recommendation

West Chester Borough has complied with the prior audit recommendation concerning the following:

- Incorrect Data On Certification Form AG 385 Resulting In An Underpayment Of State Aid

  During the current audit period, municipal officials established adequate internal control procedures to ensure compliance with the instructions that accompany Certification Form AG 385 and accurately reported the required pension data.

Noncompliance With Prior Audit Recommendation

West Chester Borough has not complied with the prior audit recommendation concerning the following as further discussed in the Finding and Recommendation section of this report:

- Failure To Maintain Vested Pension Benefit Calculations

WEST CHESTER BOROUGH NONUNIFORMED PENSION PLAN
FINDING AND RECOMMENDATION

Finding – Noncompliance With Prior Audit Recommendation – Failure To Maintain Vested Pension Benefit Calculations

Condition: As disclosed in the prior audit report, the borough failed to maintain vested pension benefit calculations for 9 plan members who terminated employment with the borough between July 1, 1991, and June 29, 1996. None of these former plan members was eligible to begin receiving a vested pension benefit during the current audit period. In addition, it appears that one of the former plan members who terminated employment on February 1, 1993, did not have the 5 years of service required for a vested benefit.

Criteria: The municipality should maintain adequate supporting documentation to substantiate the accuracy of all pension benefit determinations.

Cause: Plan officials have not been successful in obtaining the vested pension benefit calculations from the prior plan consultant.

Effect: The failure of plan officials to maintain vested pension benefit calculations could result in inconsistent or improper benefit calculations and incorrect benefit payments from the pension plan.

Recommendation: We again recommend that plan officials obtain adequate supporting documentation to verify the accuracy of the vested pension benefits to be paid from the pension plan.

Furthermore, we recommend that plan officials determine whether the former plan member who terminated employment on February 1, 1993, is entitled to a vested pension benefit pursuant to the provisions contained in the plan's governing document. If it is determined that the former member is not eligible to receive a benefit, plan officials should take appropriate action to ensure that an unauthorized pension benefit is not paid to the former plan member.

We also recommend that plan officials establish adequate internal control procedures to ensure that all pension benefit calculations are properly determined and maintained by the borough.

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

WEST CHESTER BOROUGH NONUNIFORMED 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, 2007, 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)]
01-01-07	$ 6,167,628	$ 9,548,941	$ 3,381,313	64.6%	$ 4,001,322	84.5%
01-01-09	7,341,860	11,165,972	3,824,112	65.8%	4,460,818	85.7%
01-01-11	8,255,452	13,501,829	5,246,377	61.1%	4,732,212	110.9%

Note: The market values of the plan's assets at 01-01-07, 01-01-09 and 01-01-11, 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.

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.

WEST CHESTER BOROUGH NONUNIFORMED PENSION PLAN
SUPPLEMENTARY INFORMATION
(UNAUDITED)

SCHEDULE OF CONTRIBUTIONS FROM EMPLOYER
AND OTHER CONTRIBUTING ENTITIES

Year Ended December 31	Annual Required Contribution	Percentage Contributed
2006	$ 622,102	100.0%
2007	612,157	100.0%
2008	587,635	100.0%
2009	603,341	100.0%
2010	611,367	100.0%
2011	563,126	100.0%

WEST CHESTER BOROUGH NONUNIFORMED 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, 2011
Actuarial cost method	Entry age normal
Amortization method	Level dollar
Remaining amortization period	13 years
Asset valuation method	Fair value, 4-year smoothing
Actuarial assumptions:	
Investment rate of return *	7.5%
Projected salary increases *	5.0%
* Includes inflation at	Not disclosed
Cost-of-living adjustments	None assumed

WEST CHESTER BOROUGH NONUNIFORMED PENSION PLAN
REPORT DISTRIBUTION LIST

This report was initially distributed to the following:

The Honorable Tom Corbett
Governor
Commonwealth of Pennsylvania

West Chester Borough Nonuniformed Pension Plan
Chester County
401 East Gay Street
West Chester, PA 19380

The Honorable Carolyn T. Comitta	Mayor
Ms. Holly V. Brown	Council President
Mr. Ernest B. McNeely	Borough Manager

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