

# COMPLIANCE AUDIT

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## Caln Township Police Pension Plan Chester County, Pennsylvania For the Period January 1, 2015 to December 31, 2018

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March 2020



Commonwealth of Pennsylvania  
Department of the Auditor General

Eugene A. DePasquale • Auditor General



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EUGENE A. DePASQUALE  
AUDITOR GENERAL

Board of Township Commissioners  
Caln Township  
Chester County  
Thorndale, PA 19372

We have conducted a compliance audit of the Caln Township Police Pension Plan for the period January 1, 2015 to December 31, 2018. 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 findings 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 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 total 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 the plan member 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 individual and comparing this amount to supporting documentation evidencing the amount determined and actually paid to the recipient. We also determined whether retirement benefits calculated for all three of the plan members 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 to retired individuals and comparing these amounts to supporting documentation evidencing amounts determined.
- We determined whether the January 1, 2015 and January 1, 2017 actuarial valuation reports were prepared and submitted by March 31, 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 all annual special ad hoc postretirement reimbursements received by the municipality were authorized and appropriately deposited in accordance with Act 147 by tracing information to supporting documentation maintained by plan officials.
- 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.

Caln 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 Caln 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 Caln 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 - Partial Compliance With Prior Audit Recommendation -  
Unauthorized Pension Benefit Provision

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

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 67.5% as of January 1, 2017**, which is the most recent data available. We encourage township 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 Caln 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.

February 27, 2020



EUGENE A. DEPASQUALE  
Auditor General

# CONTENTS

	<u>Page</u>
Background.....	1
Status Of Prior Finding.....	3
Finding And Recommendation:	
Finding - Partial Compliance With Prior Audit Recommendation - Unauthorized Pension Benefit Provision.....	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 Caln 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 including, but not limited to, the following:

- Act 147 - Special Ad Hoc Municipal Police and Firefighter Postretirement Adjustment Act, Act of December 14, 1988 (P.L. 1192, No. 147), as amended, 53 P.S. § 896.101 et seq.
- 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 Caln Township Police Pension Plan is a single-employer defined benefit pension plan locally controlled by the provisions of Ordinance No. 2008-13, 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 May 29, 1956. Active members are required to contribute 5 percent of compensation to the plan. As of December 31, 2018, the plan had 16 active members, 3 terminated members eligible for vested benefits in the future, and 11 retirees receiving pension benefits from the plan.

## **BACKGROUND – (Continued)**

As of December 31, 2018, selected plan benefit provisions are as follows:

### Eligibility Requirements:

Normal Retirement	Age 52 and 25 years of service. If hired after 1/1/2014, age 54 and 25 years of service.
Early Retirement	None
Vesting	100% after 12 years of service.

### Retirement Benefit:

Benefit equals 50% of final 36 months average salary, plus a service increment of \$100 for service in excess of 26 years.

### 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 50% of the member's final monthly average salary at the time the disability, offset by Workers Compensation and Social Security disability benefits received for the same injury.

CALN TOWNSHIP POLICE PENSION PLAN  
STATUS OF PRIOR FINDING

Partial Compliance With Prior Audit Recommendation

Caln Township has partially complied with the prior audit recommendation concerning the following:

· Unauthorized Pension Benefit Provision

Plan officials ratified a new collective bargaining agreement for the period January 1, 2018 to December 31, 2022 that contains a service related disability provision that is in compliance with Act 600. However, the plan's governing document still contains a service related disability provision that is not in compliance with Act 600, as further discussed in the Finding and Recommendation section of this report.



CALN TOWNSHIP POLICE PENSION PLAN  
FINDING AND RECOMMENDATION

**Finding - Partial Compliance With Prior Audit Recommendation - Unauthorized Pension Benefit Provision**

Condition: As disclosed in the prior audit report, the pension plan’s governing document and collective bargaining agreement (CBA) contained a service-related disability benefit provision that was not in accordance with Act 600. During the current audit period, plan officials ratified a new collective bargaining agreement for the period January 1, 2018 to December 31, 2022 that contained a service related disability benefit in accordance with Act 600. However, the service related disability benefit in the governing document is still not in accordance with Act 600, as noted below:

<u>Benefit Provision</u>	<u>Governing Document</u>	<u>Act 600</u>
Service-related disability benefit	A participant who retires due to a Total and Permanent Disability, ...shall be eligible for a disability retirement benefit equal to fifty percent (50%) of the member’s Final Average Monthly Salary at the time of the disability was incurred (excluding overtime), less any Workers Compensation benefits receivable. A participant who receives benefits for the same injuries under social security disability shall have the Participant’s disability benefits offset or reduced by the amount of such benefits.	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 <u>at the time the disability was incurred</u> , reduced by the amount of social security disability benefits received for the same injury. [Emphasis added.]

Criteria: The plan’s governing document and the collective bargaining agreement should contain consistent benefit provisions that are in compliance with Act 600.

Cause: Municipal officials failed to ensure full compliance with this department’s prior audit recommendation.

Effect: Inconsistent plan documents could result in inconsistent or improper benefit calculations and incorrect benefit payments from the pension plan. In addition, 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.

CALN TOWNSHIP POLICE PENSION PLAN  
FINDING AND RECOMMENDATION

**Finding - (Continued)**

Recommendation: We again recommend that municipal officials, after consulting with their solicitor, ensure that the plan's governing document and the collective bargaining agreement contain consistent benefit provisions that are in compliance with Act 600 at their earliest opportunity to do so.

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.

CALN 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, 2016, 2017, AND 2018

	<u>2014</u>	<u>2015</u>	<u>2016</u>	<u>2017</u>	<u>2018</u>
Total Pension Liability					
Service cost	\$ 247,523	\$ 302,114	\$ 317,220	\$ 373,430	\$ 392,102
Interest	583,268	629,617	674,711	724,257	781,750
Change of benefit terms	-	202,140	-	-	-
Difference between expected and actual experience	-	(104,991)	-	(227,179)	-
Changes of assumptions	-	523,605	-	191,565	-
Benefit payments, including refunds of member contributions	(285,345)	(291,435)	(314,207)	(294,919)	(295,136)
Net Change in Total Pension Liability	<u>545,446</u>	<u>1,261,050</u>	<u>677,724</u>	<u>767,154</u>	<u>878,716</u>
Total Pension Liability - Beginning	7,669,465	8,214,911	9,475,961	10,153,685	10,920,839
Total Pension Liability - Ending (a)	<u>\$ 8,214,911</u>	<u>\$ 9,475,961</u>	<u>\$ 10,153,685</u>	<u>\$ 10,920,839</u>	<u>\$ 11,799,555</u>
Plan Fiduciary Net Position					
Contributions - employer	\$ 468,734	\$ 539,937	\$ 546,388	\$ 721,776	\$ 670,139
Contributions - member	87,217	91,959	93,087	94,030	86,622
Net investment income	267,591	50,021	526,989	971,352	(180,915)
Benefit payments, including refunds of member contributions	(285,345)	(291,435)	(314,207)	(294,919)	(295,136)
Administrative expense	(12,675)	(42,856)	(48,337)	(56,401)	(70,950)
Net Change in Plan Fiduciary Net Position	<u>525,522</u>	<u>347,626</u>	<u>803,920</u>	<u>1,435,838</u>	<u>209,760</u>
Plan Fiduciary Net Position - Beginning	5,044,325	5,569,847	5,917,473	6,721,393	8,157,231
Plan Fiduciary Net Position - Ending (b)	<u>\$ 5,569,847</u>	<u>\$ 5,917,473</u>	<u>\$ 6,721,393</u>	<u>\$ 8,157,231</u>	<u>\$ 8,366,991</u>
Net Pension Liability - Ending (a-b)	<u>\$ 2,645,064</u>	<u>\$ 3,558,488</u>	<u>\$ 3,432,292</u>	<u>\$ 2,763,608</u>	<u>\$ 3,432,564</u>
Plan Fiduciary Net Position as a Percentage of the Total Pension Liability	67.80%	62.45%	66.20%	74.69%	70.91%
Estimated Covered Employee Payroll	\$ 1,714,193	\$ 1,806,387	\$ 1,932,398	\$ 1,571,340	\$ 1,747,000
Net Pension Liability as a Percentage of Covered Employee Payroll	154.30%	196.99%	177.62%	175.88%	196.48%

CALN 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, calculated using the discount rate of 5.5%, 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 (4.5%)	Current Discount Rate (5.5%)	1% Increase (6.5%)
Net Pension Liability - 12/31/15	\$ 4,852,872	\$ 3,558,488	\$ 2,480,786

In addition, the following presents the net pension liability of the township as of December 31, 2016, 2017, and 2018, calculated using the discount rate of 7.0%, 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 (6.0%)	Current Discount Rate (7.0%)	1% Increase (8.0%)
Net Pension Liability - 12/31/16	\$ 4,794,133	\$ 3,432,292	\$ 2,296,575
Net Pension Liability - 12/31/17	\$ 4,251,500	\$ 2,763,608	\$ 1,529,572
Net Pension Liability - 12/31/18	\$ 5,002,164	\$ 3,432,564	\$ 2,129,494

CALN TOWNSHIP POLICE PENSION PLAN  
 SUPPLEMENTARY INFORMATION  
 (UNAUDITED)

SCHEDULE OF CONTRIBUTIONS

Year Ended December 31	Actuarially Determined Contribution	Actual Contributions	Contribution Deficiency (Excess)	Covered- Employee Payroll	Contributions as a Percentage of Covered- Employee Payroll
2014	\$ 468,734	\$ 468,734	\$ -	\$1,714,193	27.34%
2015	539,937	539,937	-	1,806,387	29.89%
2016	546,388	546,388	-	1,932,398	28.28%
2017	721,776	721,776	-	1,571,340	45.93%
2018	670,139	670,139	-	1,747,000	38.36%

SCHEDULE OF INVESTMENT RETURNS

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

2018	(2.22%)
2017	14.46%
2016	8.95%
2015	0.91%
2014	5.99%

CALN 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:

	(1)	(2)	(3)	(4)
Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Liability (AAL) - Entry Age (b)	Unfunded (Assets in Excess of) Actuarial Liability (b) - (a)	Funded Ratio (a)/(b)
01-01-13	\$ 4,371,581	\$ 7,152,025	\$ 2,780,444	61.1%
01-01-15	5,478,678	8,835,665	3,356,987	62.0%
01-01-17	6,825,168	10,118,071	3,292,903	67.5%

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 four-year averaging period, which will be limited to a maximum of 120 percent and a minimum of 80 percent of 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.

CALN 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.

CALN 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	9 years
Asset valuation method	4-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	For participants who retire after April 1, 2010, effective on each anniversary of retirement, a retiree will receive an increase in the monthly benefit equal to the percentage change in the Consumer Price Index (CPI-W). The total of all increases may not exceed 8% of final monthly salary or 30% of the retiree’s original monthly benefit.

\* Includes inflation at 3.0%



CALN TOWNSHIP POLICE PENSION PLAN  
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This report was initially distributed to the following:

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