

# COMPLIANCE AUDIT

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## Upper Gwynedd Township Police Pension Plan Montgomery County, Pennsylvania For the Period January 1, 2015 to December 31, 2018

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January 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  
Upper Gwynedd Township  
Montgomery County  
North Wales, PA 19454

We have conducted a compliance audit of the Upper Gwynedd 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 the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our finding and conclusions based on our audit objective. We believe that the evidence obtained provides a reasonable basis for our finding and conclusions based on our audit objective.

The objective of the audit was 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 objective identified above. 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 2015, 2016 and 2017 due to the fact that employee contributions were appropriately waived by the municipality. In addition, we determined whether employee contributions for the year 2018 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 lone 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 benefits due to the retired individual and comparing these amounts to supporting documentation evidencing amounts determined and actually paid to the recipient. We also determined whether retirement benefits calculated for the one plan member 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 benefits due to the retired individual 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 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.

Upper Gwynedd 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 Upper Gwynedd 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 objective, 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 objective.

The results of our procedures indicated that, in all significant respects, the Upper Gwynedd 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 – Incorrect Data On Certification Form AG 385 Resulting In An Overpayment Of State Aid

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 Upper Gwynedd 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.

December 11, 2019



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 Upper Gwynedd 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 600 - Police Pension Fund Act, Act of May 29, 1956 (P.L. 1804, No. 600), as amended, 53 P.S. § 767 et seq.

The Upper Gwynedd Township Police Pension Plan is a single-employer defined benefit pension plan locally controlled by the provisions of Ordinance No. 2005-15, 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 September 1, 1966. Active members are required to contribute 5 percent of compensation to the plan; however, member contributions were eliminated for the years 2015, 2016 and 2017 and reduced to 1 percent for the year 2018. As of December 31, 2018, the plan had 20 active members, 2 terminated members eligible for vested benefits in the future, and 15 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 50 and 25 years of service.
Early Retirement	None
Vesting	100% vesting available after 12 years of service.

### Retirement Benefit:

Monthly benefit equals 50% of final 36 months average salary, plus a service increment of \$100 per month for 26 or more 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:

A monthly benefit equal to 60% of the member's salary at the time the disability was incurred, offset by Social Security disability benefits received for the same injury.

UPPER GWYNEDD TOWNSHIP POLICE PENSION PLAN  
FINDING AND RECOMMENDATION

**Finding – Incorrect Data On Certification Form AG 385 Resulting In An Overpayment Of State Aid**

Condition: The township certified an ineligible police officer (2 units) and overstated payroll by \$118,362, \$120,559 and \$130,198, respectively, on the Certification Form AG 385 filed in 2017, 2018 and 2019, respectively. The ineligible member retired effective February 9, 2016, and entered the township’s Deferred Retirement Option Program (DROP). The data contained on these certification forms is based on prior calendar year information.

Criteria: Pursuant to Act 205, at Section 402(e)(2), in order to be eligible for certification, an employee must have been employed on a full-time basis for at least six consecutive months and must have been participating in a pension plan during the certification year.

Furthermore, Act 205 at Section 402(e)(2) states, in part:

For the purpose of computing and reporting the applicable number of units, a DROP participant shall not be reported to the Auditor General as an active employee.

Cause: Plan officials were unaware that DROP participants and their compensation are not eligible for certification and failed to establish adequate internal control procedures to ensure the accuracy of the data certified.

Effect: The data submitted on these certification forms is used, in part, to calculate the state aid due to the municipality for distribution to its pension plans. Because the township’s state aid allocations were based on unit value, the incorrect certification of pension data affected the township’s state aid allocations, as identified below:

<u>Year</u>	<u>Units Overstated</u>	<u>Unit Value</u>	<u>State Aid Overpayment</u>
2017	2	\$ 4,588	\$ 9,176
2018	2	4,684	9,368
2019	2	5,120	<u>10,240</u>
Total Overpayment of State Aid			<u><u>\$ 28,784</u></u>

Furthermore, the township’s future state aid allocations may be withheld until the finding recommendation is complied with.

UPPER GWYNEDD TOWNSHIP POLICE PENSION PLAN  
FINDING AND RECOMMENDATION

**Finding – (Continued)**

In addition, the township used the overpayments of state aid to pay the minimum municipal obligations (MMOs) due to the police pension plan; therefore, if the reimbursement to the Commonwealth is made from the pension plan, the plan's MMOs will not be fully paid.

Recommendation: We recommend that the total excess state aid, in the amount of \$28,784, plus interest, be returned to the Commonwealth. A check in this amount, with interest compounded annually from date of receipt to date of repayment, at a rate earned by the pension plan, should be made payable to: Commonwealth of Pennsylvania and mailed to: Department of the Auditor General, Municipal Pension & Fire Relief Programs Unit, 321 Finance Building, Harrisburg, PA 17120. A copy of the interest calculation must be submitted along with the check.

We also recommend that in the future, plan officials establish adequate internal control procedures, such as having at least two people review the data certified, to ensure compliance with the instructions that accompany Certification Form AG 385 to assist them in accurately reporting the required pension data.

In addition, if the reimbursement to the Commonwealth is made from police pension plan funds, we recommend that any resulting MMO deficiencies be paid to the pension plan with interest, at a rate earned by the pension plan.

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

Auditor's Conclusion: Due to the potential withhold of state aid, the township's compliance with the finding recommendation will be monitored subsequent to the release of the audit report and through our next audit of the plan.

UPPER GWYNEDD TOWNSHIP POLICE PENSION PLAN  
POTENTIAL WITHHOLD OF STATE AID

The finding contained in this audit report cites an overpayment of state aid to the township in the amount of \$28,784, plus interest. A condition of this nature may lead to a total withholding of state aid in the future unless that finding is corrected. A check in this amount with interest, at a rate earned by the pension plan, should be made payable to: Commonwealth of Pennsylvania, and mailed to: Department of the Auditor General, Municipal Pension & Fire Relief Programs Unit, 321 Finance Building, Harrisburg, PA 17120.

UPPER GWYNEDD 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	\$ 292,665	\$ 334,046	\$ 282,430	\$ 313,994	\$ 323,171
Interest	796,330	820,482	862,768	916,312	992,538
Differences between expected and actual experience	-	(286,531)	86,978	-	-
Changes of assumptions	-	-	-	348,276	417,537
Benefit payments, including refunds of member contributions	(498,822)	(498,822)	(498,822)	(498,823)	(498,820)
Net Change in Total Pension Liability	590,173	369,175	733,354	1,079,759	1,234,426
Total Pension Liability – Beginning	11,332,893	11,923,066	12,292,241	13,025,595	14,105,354
Total Pension Liability – Ending (a)	<u>\$ 11,923,066</u>	<u>\$ 12,292,241</u>	<u>\$ 13,025,595</u>	<u>\$ 14,105,354</u>	<u>\$ 15,339,780</u>
Plan Fiduciary Net Position					
Contributions – employer	\$ 489,783	\$ 767,778	\$ 724,632	\$ 737,046	\$ 758,957
Contributions – employee	-	-	-	-	24,104
Net investment income	561,678	102,556	702,217	1,820,133	(652,183)
Benefit payments, including refunds of member contributions	(498,822)	(498,822)	(498,822)	(498,823)	(498,820)
Administrative expense	(65,350)	(89,121)	(65,902)	(71,441)	(75,638)
Net Change in Plan Fiduciary Net Position	487,289	282,391	862,125	1,986,915	(443,580)
Plan Fiduciary Net Position – Beginning	10,129,923	10,617,212	10,899,603	11,761,728	13,748,643
Plan Fiduciary Net Position – Ending (b)	<u>\$ 10,617,212</u>	<u>\$ 10,899,603</u>	<u>\$ 11,761,728</u>	<u>\$ 13,748,643</u>	<u>\$ 13,305,063</u>
Net Pension Liability – Ending (a-b)	<u>\$ 1,305,854</u>	<u>\$ 1,392,638</u>	<u>\$ 1,263,867</u>	<u>\$ 356,711</u>	<u>\$ 2,034,717</u>
Plan Fiduciary Net Position as a Percentage of the Total Pension Liability	89.05%	88.67%	90.30%	97.48%	86.74%
Estimated Covered Employee Payroll	\$ 2,054,865	\$ 2,011,419	\$ 2,132,118	\$ 2,180,743	\$ 2,339,825
Net Pension Liability as a Percentage of Covered Employee Payroll	63.55%	69.24%	59.28%	16.36%	63.55%

UPPER GWYNEDD 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, 2014, 2015, 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 – 12/31/14	\$ 2,862,808	\$ 1,305,854	\$ 11,970
Net Pension Liability – 12/31/15	\$ 3,021,315	\$ 1,392,638	\$ 42,511
Net Pension Liability – 12/31/16	\$ 2,961,806	\$ 1,263,867	\$ (145,492)
Net Pension Liability – 12/31/17	\$ 2,236,687	\$ 356,711	\$ (1,189,336)
Net Pension Liability – 12/31/18	\$ 4,073,754	\$ 2,034,717	\$ 357,237

UPPER GWYNEDD 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>
2014	\$ 489,783	\$ 489,783	\$ -	\$ 2,054,865	23.84%
2015	767,778	767,778	-	2,011,419	38.17%
2016	724,632	724,632	-	2,132,118	33.99%
2017	737,046	737,046	-	2,180,743	33.80%
2018	758,957	758,957	-	2,339,825	32.44%

SCHEDULE OF INVESTMENT RETURNS

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

2018	(5.21%)
2017	14.81%
2016	6.37%
2015	0.96%
2014	5.53%

UPPER GWYNEDD 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 Accrued Liability (AAL) - Entry Age (b)	Unfunded (Assets in Excess of) Actuarial Accrued Liability (b) - (a)	Funded Ratio (a)/(b)
01-01-13	\$ 8,534,384	\$ 11,044,002	\$ 2,509,618	77.3%
01-01-15	10,245,926	11,636,535	1,390,609	88.0%
01-01-17	12,108,413	13,351,087	1,242,674	90.7%

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 five-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.

UPPER GWYNEDD 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.

UPPER GWYNEDD 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	4 years
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	4.5%

UPPER GWYNEDD TOWNSHIP POLICE PENSION PLAN  
REPORT DISTRIBUTION LIST

This report was initially distributed to the following:

**The Honorable Tom W. Wolf**  
Governor  
Commonwealth of Pennsylvania

**Mr. Kenneth E. Kroberger**  
President, Board of Township Commissioners

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**Ms. Liz McNaney**  
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**Mr. David J. Brill**  
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