

# COMPLIANCE AUDIT

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## Valley Township Police Pension Plan Chester County, Pennsylvania For the Period January 1, 2016 to December 31, 2019

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April 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 Supervisors  
Valley Township  
Chester County  
Coatesville, PA 19320

We have conducted a compliance audit of the Valley Township Police Pension Plan for the period January 1, 2016 to December 31, 2019. 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 covered by our audit period due to the fact that employee contributions were appropriately waived by the municipality.
- We determined whether retirement benefits calculated for the plan member who retired during the current audit period represent payments to one 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 recipients.
- We determined whether the January 1, 2015, January 1, 2017, and January 1, 2019 actuarial valuation reports were prepared and submitted by March 31, 2016, 2018, and 2020, 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.

Township officials are responsible for establishing and maintaining effective internal controls to provide reasonable assurance that the Valley 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 Valley 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 Underpayment 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 Valley 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 18, 2020

A handwritten signature in black ink, appearing to read "Eugene A. DePasquale". The signature is fluid and cursive, with a long horizontal stroke extending to the right.

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 Valley 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 Valley Township Police Pension Plan is a single-employer defined benefit pension plan locally controlled by the provisions of Ordinance No. 2016-03, 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, 1977. 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, 2019, the plan had 6 active members, no terminated members eligible for vested benefits in the future, and 1 retiree receiving pension benefits from the plan.

## **BACKGROUND – (Continued)**

As of December 31, 2019, selected plan benefit provisions are as follows:

### Eligibility Requirements:

Normal Retirement	Age 55 and 25 years of service.
Early Retirement	None
Vesting	A member is 100% vested after 12 years of service.

### Retirement Benefit:

Benefit equals 50% of final 36 months average salary, plus \$100 per month for each year of service in excess of 25 years, maximum \$500 per month.

### Survivor Benefit:

Before Retirement Eligibility	Refund of member contributions equal to the participant's contribution account.
After Retirement Eligibility	A monthly benefit equal to 50% of the participant's vested accrued pension.

### Service Related Disability Benefit:

Benefit equals 50% of the member's salary at the time the disability was incurred, offset by Social Security disability benefits and any disability insurance benefit payable, which is funded by the plan, payable until normal retirement, death, or recovery, and a deferred annuity payable at the normal retirement date.

VALLEY TOWNSHIP POLICE PENSION PLAN  
FINDING AND RECOMMENDATION

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

Condition: The township failed to certify 1 eligible police officer and understated payroll by \$57,721 on the Certification Form AG 385 filed in 2018. In addition, the township failed to certify 1 eligible non-uniformed employee and understated payroll by \$42,891 on the Certification Form AG 385 filed in 2019. The data contained on these certification forms is based on prior calendar year information.

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

Cause: The township’s failure to include the eligible employees was attributed to clerical oversights.

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 pension costs, the township received an underpayment of state aid of \$14,154, as identified below:

<u>Year</u>	<u>Type of Plan</u>	<u>Normal Cost</u>	<u>Payroll Understated</u>	<u>State Aid Underpayment</u>
2018	Police	15.50669%	\$ 57,721	\$ 8,951
2019	Non-Uniformed	12.13000%	\$ 42,891	\$ 5,203
Total Underpayment of State Aid				<u>\$ 14,154</u>

Although the additional state aid will be allocated to the township, the full amount of the 2018 and 2019 state aid allocations was not available to be deposited timely and therefore was not available to pay operating expenses or for investment.

Recommendation: We 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.



VALLEY TOWNSHIP POLICE PENSION PLAN  
FINDING AND RECOMMENDATION

**Finding - (Continued)**

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.

VALLEY TOWNSHIP POLICE PENSION PLAN  
SUPPLEMENTARY INFORMATION  
(UNAUDITED)

The supplementary information contained on Pages 5 through 7 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	\$ 44,331	\$ 46,033	\$ 48,335	\$ 57,195	\$ 60,055
Interest	56,988	62,901	71,244	78,860	87,970
Difference between expected and actual experience	-	(36,469)	-	(28,816)	-
Changes of assumptions	-	12,300	-	1,922	-
Benefit payments, including refunds of member contributions	-	-	-	-	(34,899)
Net Change in Total Pension Liability	<u>101,319</u>	<u>84,765</u>	<u>119,579</u>	<u>109,161</u>	<u>113,126</u>
Total Pension Liability - Beginning	<u>715,503</u>	<u>816,822</u>	<u>901,587</u>	<u>1,021,166</u>	<u>1,130,327</u>
Total Pension Liability - Ending (a)	<u><u>\$ 816,822</u></u>	<u><u>\$ 901,587</u></u>	<u><u>\$ 1,021,166</u></u>	<u><u>\$ 1,130,327</u></u>	<u><u>\$ 1,243,453</u></u>
Plan Fiduciary Net Position					
Contributions - State Aid	\$ 24,572	\$ 28,529	\$ 23,198	\$ 31,685	\$ 40,331
Net investment income	46,371	(21,193)	60,324	173,994	(94,026)
Benefit payments, including refunds of member contributions	-	-	-	-	(34,899)
Administrative expense	(5,375)	(5,750)	(6,375)	(6,250)	(5,875)
Net Change in Plan Fiduciary Net Position	<u>65,568</u>	<u>1,586</u>	<u>77,147</u>	<u>199,429</u>	<u>(94,469)</u>
Plan Fiduciary Net Position - Beginning	<u>1,035,084</u>	<u>1,100,652</u>	<u>1,102,238</u>	<u>1,179,385</u>	<u>1,378,814</u>
Plan Fiduciary Net Position - Ending (b)	<u><u>\$ 1,100,652</u></u>	<u><u>\$ 1,102,238</u></u>	<u><u>\$ 1,179,385</u></u>	<u><u>\$ 1,378,814</u></u>	<u><u>\$ 1,284,345</u></u>
Net Pension Liability - Ending (a-b)	<u><u>\$ (283,830)</u></u>	<u><u>\$ (200,651)</u></u>	<u><u>\$ (158,219)</u></u>	<u><u>\$ (248,487)</u></u>	<u><u>\$ (40,892)</u></u>
Plan Fiduciary Net Position as a Percentage of the Total Pension Liability	134.7%	122.3%	115.5%	122.0%	103.3%
Estimated Covered Employee Payroll	\$ 319,693	\$ 348,872	\$ 327,835	\$ 389,152	\$ 432,637
Net Pension Liability as a Percentage of Covered Employee Payroll	(88.8%)	(57.5%)	(48.3%)	(63.9%)	(9.5%)

VALLEY 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 7.5%, 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 (6.5%)	Current Discount Rate (7.5%)	1% Increase (8.5%)
Net Pension Liability - 12/31/14	\$ (158,323)	\$ (283,830)	\$ (388,742)
Net Pension Liability - 12/31/15	\$ (63,156)	\$ (200,651)	\$ (315,234)
Net Pension Liability - 12/31/16	\$ (7,045)	\$ (158,219)	\$ (284,284)
Net Pension Liability - 12/31/17	\$ (84,403)	\$ (248,487)	\$ (385,217)
Net Pension Liability - 12/31/18	\$ 139,780	\$ (40,892)	\$ (191,451)

VALLEY 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
2010	\$ 14,771	\$ 18,124	\$ (3,353)	\$ 242,523	7.5%
2011	18,124	18,124	-	264,057	6.9%
2012	6,788	6,788	-	288,638	2.4%
2013	8,521	8,521	-	290,110	2.9%
2014	24,572	24,572	-	303,015	8.1%
2015	28,529	28,529	-	319,693	8.9%
2016	23,198	23,198	-	327,835	7.1%
2017	31,685	31,685	-	389,152	8.1%
2018	40,331	40,331	-	432,637	9.3%
2019	31,209	31,209	-	*	

\* Due to the timing of this audit, covered-employee payroll for 2019 was not provided in this schedule.

SCHEDULE OF INVESTMENT RETURNS

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

2018	(6.90%)
2017	14.82%
2016	5.51%
2015	(1.92%)
2014	4.50%

VALLEY 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, 2015, 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)
01-01-15	\$ 1,073,138	\$ 792,653	\$ (280,485)	135.4%
01-01-17	1,255,835	994,272	(261,563)	126.3%
01-01-19	1,421,638	1,301,906	(119,732)	109.2%

Note: The market values of the plan’s assets at 01-01-15, 01-01-17, and 01-01-19 have been adjusted to reflect the smoothing of gains and/or losses subject to a corridor between 80 to 120 percent of the market value of assets over a five-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.

VALLEY 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.

VALLEY 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, 2019
Actuarial cost method	Entry age normal
Amortization method	Not applicable
Remaining amortization period	None
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	7.5%
Projected salary increases	5.0%

VALLEY TOWNSHIP POLICE PENSION PLAN  
REPORT DISTRIBUTION LIST

This report was initially distributed to the following:

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Township Manager

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