

CALN TOWNSHIP POLICE PENSION PLAN

CHESTER COUNTY

COMPLIANCE AUDIT REPORT

FOR THE PERIOD

JANUARY 1, 2009, TO DECEMBER 31, 2011



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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.

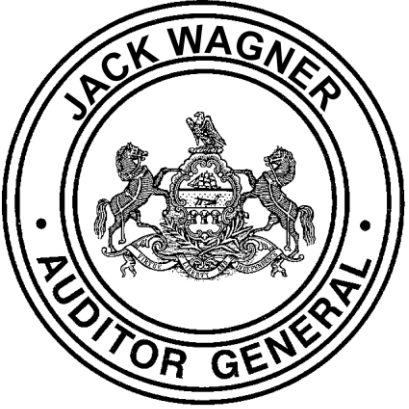
Pension plan aid is provided from a 2 percent foreign casualty insurance premium tax, a portion of the foreign fire insurance tax designated for paid firefighters and any investment income earned on the collection of these taxes. Generally, municipal pension plans established prior to December 18, 1984, 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 Caln Township 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 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. § 761 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.



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, 2009, 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 findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings 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 special ad hoc postretirement adjustment granted to eligible pensioners is in accordance with applicable laws and regulations and whether the ad hoc reimbursement received by the municipality was treated in accordance with applicable laws and 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.
- Whether Deferred Retirement Option Plan (DROP) participants' benefit payments are properly determined in accordance with the provisions of the DROP and any other applicable laws and regulations.

Caln Township contracted with an independent certified public accounting firm for annual audits of the Caln Township Police Pension Plan's 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, 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 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 findings further discussed later in this report:

Finding No. 1 – Noncompliance With Prior Audit Recommendation - Failure To Provide A Survivor Benefit In Accordance With Act 600 Provisions

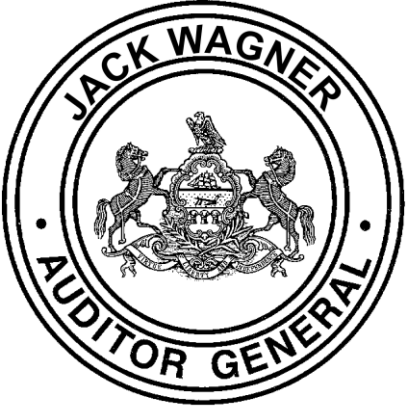
Finding No. 2 – Noncompliance With Prior Audit Recommendation - Inconsistent And Unauthorized Pension Benefit Provisions

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 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 65.0% as of January 1, 2011, which is the most recent date 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.

October 9, 2012

JACK WAGNER
Auditor General



CALN TOWNSHIP POLICE PENSION PLAN
STATUS OF PRIOR FINDINGS

Compliance With Prior Audit Recommendation

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

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

The township reimbursed \$9,918 to the Commonwealth for the overpayment of state aid.

Noncompliance With Prior Audit Recommendations

Caln Township has not complied with the prior audit recommendations concerning the following as further discussed in the Findings and Recommendations section of this report:

- Failure To Provide A Survivor Benefit In Accordance With Act 600 Provisions
- Inconsistent And Unauthorized Pension Benefit Provisions

CALN TOWNSHIP POLICE PENSION PLAN
FINDINGS AND RECOMMENDATIONS

Finding No. 1 - Noncompliance With Prior Audit Recommendation - Failure To Provide A Survivor Benefit In Accordance With Act 600 Provisions

Condition: As disclosed in the prior audit report, township officials failed to determine a benefit for a surviving spouse of a police officer who died on May 5, 2008. The police officer had 19 years of service and was 49 years old at the time of death.

Criteria: Act 600 at Section 1(a)(4), states:

The surviving spouse of a member of the police force or a member who retires on pension who dies or if no spouse survives or if he or she survives and subsequently dies, then the child or children under the age of eighteen years or, if attending college, under or attaining the age of twenty-three years, of a member of the police force or a member who retires on pension who dies shall during her lifetime in the case of a surviving spouse or until reaching the age of eighteen years or if attending college, under or attaining the age of twenty-three years, in the case of a child or children, be entitled to receive a pension calculated at no less than fifty per centum of the pension the member was receiving or would have been receiving had he been retired at the time of his death.

Furthermore, Section 5(h)(ii) of Act 600 states, in part:

...should a police officer, before completing superannuation retirement age and service requirements but after having completed twelve years of total service, for any reason cease to be employed as a full-time police officer by the municipality or regional police department in whose pension fund he has been a member, he shall be entitled to vest his retirement benefits...

In addition, Act 600 at Section 1(a)(5), states, in part:

The surviving spouse of a member of the police force who dies before his pension has vested . . . shall be entitled to receive repayment of all money which the member invested in the pension fund plus interest or other increases in value of the member's investment in the pension fund, unless the member has designated another beneficiary for this purpose.

Cause: Plan officials, along with the township solicitor, are not convinced that either the plan's governing document or Act 600 requires a vested benefit for a surviving spouse of a member who dies and fails to reach his superannuation date or formally elects to vest under the plan.

CALN TOWNSHIP POLICE PENSION PLAN
FINDINGS AND RECOMMENDATIONS

Finding No. 1 – (Continued)

Effect: The police officer’s surviving spouse will not receive the pension benefits due pursuant to Act 600 provisions.

Recommendation: We again recommend that plan officials determine a monthly vested pension benefit for the surviving spouse of the deceased police officer and pay the pension benefit beginning on what would have been the deceased officer’s superannuation retirement date.

Management’s Response: With regard to the finding regarding the surviving spouse of an unretired officer who dies prior to reaching normal retirement, the Township believes that the finding is inappropriate and the interpretation relied upon by the Department is unsupported by the plain language of Act 600. As set forth in the finding, if a member of a police force ceases to be a member after rendering twelve or more years of service, he or she may vest his pension. The statute further provides that, if an officer dies before his pension has vested, a return of contributions is warranted.

Based upon the above, the Township believes that its pension plan document and the collective bargaining agreement are in compliance with Act 600 and, therefore, its actions were appropriate. Act 600 expressly sets forth the procedure under which an officer must vest his pension. Specifically, Section 5 of Act 600 expressly requires an officer to submit an application evidencing his intent to vest. Clearly, the General Assembly, in enacting Act 600, recognized that it put in place a mechanism in order to vest an individual’s pension benefit. Had they intended for some sort of posthumous vesting through the Act 30 amendments, they would have expressly set such provisions in the amendments. In the absence of such language, it is the Township’s position that it is not obligated under Act 600 to allow the widow of an officer to vest his pension after the fact. To the contrary, in compliance with Act 600, the Township has offered to refund the contributions made by the officer. In light of the fact that the Township’s plan document and collective bargaining agreement comply with the provisions of Act 600 on this issue, the Township respectfully submits that no audit finding should be issued.

Auditor’s Conclusion: The Pennsylvania legislature passed Act 30 of 2002 on April 17, 2002, which amended Act 600 in several respects. Among the changes was a provision specifying that the “surviving spouse of a member of the police force who dies before his pension has vested . . . shall be entitled to receive repayment of all money which the member invested in the pension fund plus interest. . . .” (Emphasis added). The Department of the Auditor General has concluded therefore that the surviving spouse of a police officer who dies after his pension has vested is entitled to receive benefits determined in accordance with Sections 1 and 5(h) of Act 600. These benefits are payable beginning on what would have been the deceased officer’s superannuation retirement date. In addition, it is our understanding that the township does not have any procedures in place for active police officers to affirmatively elect to vest their pension benefits; therefore, the finding and recommendation remain as stated.

CALN TOWNSHIP POLICE PENSION PLAN
FINDINGS AND RECOMMENDATIONS

Finding No. 2 – Noncompliance With Prior Audit Recommendation – Inconsistent And Unauthorized Pension Benefit Provisions

Condition: As disclosed in the prior audit report, the pension plan’s collective bargaining agreement (CBA) contains a service-related disability benefit that is not in compliance with Act 600 and is not consistent with the plan’s governing document. In addition, the plan’s governing document contains a cost-of-living adjustment (COLA) provision that conflicts with the CBA and neither provision is in accordance with Act 600 as noted below:

<u>Benefit Provision</u>	<u>Governing Document</u>	<u>Collective Bargaining Agreement</u>	<u>Act 600 (as amended)</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 the disability was incurred provided that any 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.	Any police officer who suffers a permanent service-related disability shall receive a monthly service-related disability benefit of fifty (50%) percent of the police officer’s final average salary (excluding overtime) over the last thirty-six (36) months of employment prior to the date of disability less any Workers Compensation benefit receivable. Any police officer who receives benefits for the same injuries under the Social Security Act shall have his 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 at the time the disability was incurred, reduced by the amount of Social Security disability benefits received for the same injury.

CALN TOWNSHIP POLICE PENSION PLAN
FINDINGS AND RECOMMENDATIONS

Finding No. 2 – (Continued)

<u>Benefit Provision</u>	<u>Governing Document</u>	<u>Collective Bargaining Agreement</u>	<u>Act 600 (as amended)</u>
Cost of Living Adjustment (COLA)	All Participants who retire after April 1, 2010, shall receive a cost of living adjustment increase equal to the Consumer Price Index to their benefits each year with a maximum multi-year COLA not to exceed 8%.	Effective April 1, 2010, an annual COLA of no more than 8% of the officer’s final average salary.	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.

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

CALN TOWNSHIP POLICE PENSION PLAN
FINDINGS AND RECOMMENDATIONS

Finding No. 2 – (Continued)

Cause: Plan officials failed to establish adequate internal control procedures to ensure compliance with the 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.

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, as amended, at their earliest opportunity to do so.

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

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, 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	\$ 3,270,915	\$ 4,763,270	\$ 1,492,355	68.7%	\$ 1,376,859	108.4%
01-01-09	3,720,199	5,088,535	1,368,336	73.1%	1,348,680	101.5%
01-01-11	4,064,598	6,253,446	2,188,848	65.0%	1,413,192	154.9%

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 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.

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.

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.

CALN TOWNSHIP POLICE PENSION PLAN
 SUPPLEMENTARY INFORMATION
 (UNAUDITED)

SCHEDULE OF CONTRIBUTIONS FROM EMPLOYER
 AND OTHER CONTRIBUTING ENTITIES

Year Ended December 31	Annual Required Contribution	Percentage Contributed
2006	\$ 214,056	107.4%
2007	263,699	100.0%
2008	264,702	100.0%
2009	287,151	100.0%
2010	305,301	100.1%
2011	343,071	100.0%

CALN TOWNSHIP 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, 2011
Actuarial cost method	Entry age normal
Amortization method	Level dollar
Remaining amortization period	12 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 *	7.5%
Projected salary increases *	5.0%
* Includes inflation at	3.0%
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 CPI-W. The total of all increases may not exceed 8% of final monthly average salary or 30% of the retiree's original monthly benefit.

CALN TOWNSHIP POLICE PENSION PLAN
REPORT DISTRIBUTION LIST

This report was initially distributed to the following:

The Honorable Tom Corbett
Governor
Commonwealth of Pennsylvania

Caln Township Police Pension Plan
Chester County
253 Municipal Drive
Thorndale, PA 19372

Mr. Vincent Rose President, Board of Township Commissioners

Mr. Gregory E. Prowant Township 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.