



DARBY TOWNSHIP POLICE PENSION PLAN

DELAWARE COUNTY

COMPLIANCE AUDIT REPORT

FOR THE PERIOD

JANUARY 1, 2010, TO DECEMBER 31, 2012

COMMONWEALTH OF PENNSYLVANIA

EUGENE A. DEPASQUALE - AUDITOR GENERAL

DEPARTMENT OF THE AUDITOR GENERAL



Commonwealth of Pennsylvania
Department of the Auditor General
Harrisburg, PA 17120-0018
Facebook: Pennsylvania Auditor General
Twitter: @PAAuditorGen

EUGENE A. DePASQUALE
AUDITOR GENERAL

Board of Township Commissioners
Darby Township
Delaware County
Glenolden, PA 19036

We have conducted a compliance audit of the Darby Township Police Pension Plan for the period January 1, 2010, to December 31, 2012. 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. 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 contract, including ownership and any restrictions, are in compliance with plan provisions, investment policies and state regulations.
- 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 disability/killed-in-service insurance premiums are proper and in accordance with plan provisions and applicable laws, regulations, and policies.
- Whether transfers were properly authorized, accurate, timely and properly recorded.

Township officials are responsible for establishing and maintaining effective internal controls to provide reasonable assurance that the Darby 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, 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 tests indicated that, in all significant respects, the Darby 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 - Pension Benefits Inconsistent And Not Authorized By Act 600

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 Darby Township and, where appropriate, their responses have been included in the report.

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

May 2, 2013

CONTENTS

| | <u>Page</u> |
|---|-------------|
| Background | 1 |
| Finding and Recommendation: | |
| Finding – Pension Benefits Inconsistent And Not Authorized By Act 600 | 2 |
| 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.

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 Darby 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 Darby Township Police Pension Plan is a single-employer defined benefit pension plan locally controlled by the provisions of Ordinance No. 671, 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.

DARBY TOWNSHIP POLICE PENSION PLAN
FINDING AND RECOMMENDATION

Finding – Pension Benefits Inconsistent And Not Authorized By Act 600

Condition: The pension plan’s governing document and the collective bargaining agreement (CBA) between the police officers and the township contain provisions that are inconsistent with each other and in certain instances not in compliance with Act 600.

The methodology contained in the plan’s governing document provides for the determination of pension benefits in excess of what is authorized by Act 600.

Section 1.06 of Ordinance No. 671 states, in part:

Compensation shall be based on W-2 earnings in which all forms of earnings are derived from the terms and conditions of the employee’s employment.

The CBA provides for severance pay to retiring police officers in a sum equal to 80 days at the officer’s annual base salary. The township has interpreted this provision to authorize the inclusion of lump-sum severance payments in the calculations of pension benefits. Consequently, plan officials included lump-sum severance payments in the determination of final average salary used to calculate monthly pension benefits for 2 police officers who retired during the current audit period.

Section 5(c) of Act 600 states, in part:

Monthly pension or retirement benefits other than length of service increments shall be computed at one-half the monthly average salary of such member during not more than the last sixty nor less than the last thirty-six months of employment.

Although Act 600 does not define “salary,” the department has concluded, based on a line of court opinions, that the term does not encompass lump-sum severance payments.

In addition, the plan’s governing document and the CBA both provide for a normal retirement benefit at age 50 and 25 years of service or age 60 with 20 years of service.

Section 3 of Act 600 states, in part:

Each ordinance or resolution establishing a police pension fund shall prescribe a minimum period of total service in the aggregate of twenty-five years in the same borough, town, township or regional police department and shall fix the age of the members of the force at fifty-five years, or, if an actuarial study of the cost shows that such reduction in age is feasible, may fix the age of the members of the force at fifty years, after which they may retire from active duty....

DARBY TOWNSHIP POLICE PENSION PLAN
FINDING AND RECOMMENDATION

Finding – (Continued)

Consequently, Act 600 does not provide for a normal retirement benefit at age 60 with 20 years of service.

Furthermore, while the service increment provisions in the plan’s governing document, prior to, and effective January 1, 2012, were in compliance with Act 600, the service increment provision contained in the CBA remains inconsistent with the plan’s governing document and is not in compliance 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 increments | <p>Governing document effective 1/1/12: Additional benefit of \$100 per month for each year of completed service in excess of 25 up to a maximum of \$500 per month.</p> <p>Governing document in effect prior to 1/1/12: Each member who has completed 26 years of service shall receive an additional monthly pension benefit equal to a maximum of \$100 per month.</p> | Additional benefit of \$100 per month for each year of completed service in excess of 25. | \$100 per month for each completed year of service in excess of 25 years up to a maximum of \$500 per month after 5 completed years of service in excess of 25 years. |

In addition, the pension plan’s governing document contains a survivor’s benefit provision that is in compliance with Act 600; however, the survivor’s benefit provision contained in the CBA is inconsistent with the plan’s governing document and is not in compliance with Act 600. The provision in the CBA discontinues benefits upon remarriage of the surviving spouse and only provides benefits to children under the age of 18.

DARBY TOWNSHIP POLICE PENSION PLAN
FINDING AND RECOMMENDATION

Finding – (Continued)

Section 1(a)(4) of Act 600 states:

The surviving spouse of a member of the police force or a former member of the police force who, prior to April 18, 2002, retired on pension and dies subsequent to retirement or who, after April 16, 2002, retires on pension and dies subsequent to retirement, 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.

The service-related disability benefit provision in the CBA also is not in compliance with Act 600 and is inconsistent with the plan’s governing document 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 | 75% of salary at the time of disability was incurred, offset by any Social Security benefits received for the same injury. | 75% of 12 month wages preceding retirement with no Social Security offset. | 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. |

DARBY TOWNSHIP POLICE PENSION PLAN
FINDING AND RECOMMENDATION

Finding – (Continued)

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

Cause: Plan officials believed that their methodology for calculating pension benefits was authorized by Act 600. In addition, the municipality has been unable to resolve the inconsistencies between the plan's governing document and the CBA through the collective bargaining agreement process.

Effect: Inconsistent plan documents resulted in excess service increments being granted to two police officers who retired in 2011 and were subject to the provisions of the plan's governing document in effect prior to January 1, 2012. One retiree is receiving service increments of \$200 per month, which exceed the plan's governing document then in effect by \$100 per month. Combined with the inclusion of lump-sum severance payments in the calculation of this member's pension benefit, this retiree is receiving total excess pension benefits of \$396 per month. The second retiree is receiving service increments of \$1,400 per month, which exceed the plan's governing document then in effect by \$1,300 per month and is also in excess of Act 600 provisions. Combined with the inclusion of lump-sum severance payments in the calculation of this member's pension benefit, this retiree is receiving total excess pension benefits of \$1,761 per month. It should be noted that the pension benefits granted to the second retiree were upheld through the arbitration process.

The excess benefits have totaled approximately \$56,878 from the dates of the members' retirements through the date of the completion of our audit fieldwork procedures.

Providing unauthorized pension benefits increases the plan's pension costs and reduces the amount of funds available for investment purposes or for the payment of authorized benefits or administrative expenses. Since the township received state aid based on unit value during the current audit period, it did not receive allocations attributable to the excess pension benefits provided. However, the increased costs to the pension plan as a result of the excess pension benefits could result in the receipt of excess state aid in the future and increase the municipal contributions necessary to fund the plan in accordance with Act 205 funding standards.

DARBY TOWNSHIP POLICE PENSION PLAN
FINDING AND RECOMMENDATION

Finding – (Continued)

Recommendation: We recommend that municipal officials take appropriate action to ensure the plan's governing document and the CBA contain consistent benefit provisions that are in compliance with Act 600, as amended, at its earliest opportunity to do so. To the extent that the township is not in compliance with Act 600 and/or is contractually obligated to pay benefits to existing retirees in excess of those authorized by Act 600, the excess benefits must be reflected in the Act 205 actuarial valuation reports for the plan and funded in accordance with Act 205 funding standards. Furthermore, such benefits will be deemed ineligible for funding with state pension aid. In such case, the plan's actuary may be required to determine the impact, if any, of the excess benefits on the township's future state aid allocations and submit this information to the Department. If it is determined the excess benefits had an impact on the township's future state aid allocations after the submission of this information, the plan's actuary would then be required to contact the Department to verify the overpayment of state aid received. Plan officials would then be required to reimburse the overpayment to the Commonwealth.

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

DARBY 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 | \$ 3,838,564 | \$ 4,902,329 | \$ 1,063,765 | 78.3% | \$ 928,968 | 114.5% |
| 01-01-09 | 4,046,211 | 5,715,331 | 1,669,120 | 70.8% | 909,381 | 183.5% |
| 01-01-11 | 4,817,906 | 6,213,931 | 1,396,025 | 77.5% | 1,135,101 | 123.0% |

Note: The market value of the plan's assets at 01-01-07 has been adjusted to reflect the smoothing of gains and/or losses over a 4-year averaging period. The market values of the plan's assets at 1-1-09 and 1-1-11 have been adjusted to reflect the smoothing of gains and/or losses at 130% of market value. These methods 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.

DARBY 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. When assets are in excess of the actuarial accrued liability, the higher the bracketed percentage, the stronger the plan.

DARBY 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 |
|------------------------|------------------------------|------------------------|
| 2007 | \$ 206,590 | 100.0% |
| 2008 | 238,183 | 100.0% |
| 2009 | 242,957 | 100.0% |
| 2010 | 252,260 | 102.2% |
| 2011 | 276,229 | 100.0% |
| 2012 | 280,243 | 100.0% |

DARBY 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 | 7 years |
| Asset valuation method | Plan assets are valued using the method described in Section 210 of Act 205, as amended, subject to a ceiling of 130% of the market value of assets. |
| Actuarial assumptions: | |
| Investment rate of return * | 8.0% |
| Projected salary increases * | 5.0% |
| Cost-of-living adjustments | 3.0% per annum |

* Inflation rate not disclosed

DARBY TOWNSHIP POLICE PENSION PLAN
REPORT DISTRIBUTION LIST

This report was initially distributed to the following:

The Honorable Tom Corbett
Governor
Commonwealth of Pennsylvania

Darby Township Police Pension Plan
Delaware County
21 Bartram Avenue
Glenolden, PA 19036

Mr. Lawrence Patterson President, Board of Township Commissioners

Mr. John B. Ryan, Jr. Township Manager

This report is a matter of public record and is available online at www.auditorgen.state.pa.us.
Media questions about the report can be directed to the Pennsylvania Department of the Auditor
General, Office of Communications, 231 Finance Building, Harrisburg, PA 17120; via email to:
news@auditorgen.state.pa.us.