

**EASTTOWN TOWNSHIP POLICE PENSION PLAN**

**CHESTER COUNTY**

**COMPLIANCE AUDIT REPORT**

**FOR THE PERIOD**

**JANUARY 1, 2004, TO DECEMBER 31, 2006**





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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, 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 Easttown 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 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. (1955) 1804, No. 600), as amended, 53 P.S. § 767, et seq.

The Easttown Township Police Pension Plan is a single-employer defined benefit pension plan locally controlled by the provisions of Ordinance No. 121, 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 Supervisors  
Easttown Township  
Chester County  
Devon, PA 19333

We have conducted a compliance audit of the Easttown Township Police Pension Plan for the period January 1, 2004, to December 31, 2006. The audit was conducted pursuant to authority derived from Section 402(j) of Act 205 of 1984 and in accordance with *Government Auditing Standards*, issued by the Comptroller General of the United States.

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. Easttown 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.

The Department of the Auditor General (Department) is mandated by state statute to calculate state aid provided to municipal pension funds and to audit municipal pension funds having received such aid. State aid is calculated by an administrative unit that is not involved in the audit process. The Department's Comptroller Office then pre-audits the calculation and submits requests to the Commonwealth's Treasury Department for the disbursement of state aid to the municipality. The Department has implemented procedures to ensure that Department audit personnel are not directly involved in the calculation and disbursement processes. The Department's mandatory responsibilities are being disclosed in accordance with *Government Auditing Standards*.

Township officials are responsible for establishing and maintaining an internal control structure to provide reasonable assurance that the Easttown Township Police Pension Plan is administered in compliance with applicable state laws, regulations, contracts, administrative procedures, and local ordinances and policies. To assist us in planning and performing our audit, we obtained an understanding of the township's internal control structure as it relates to the township's compliance with those requirements. Additionally, we tested transactions, assessed official actions, performed analytical procedures and interviewed selected officials to the extent necessary to satisfy the audit objectives.

The results of our tests indicated that, in all significant respects, the Easttown 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 - Failure To Adopt Benefit Provisions Mandated By Act 30

Finding No. 2 - Failure To Fully Pay The Minimum Municipal Obligation Of The Plan

The accompanying supplementary information is presented for purposes of additional analysis. We did not audit the information and, accordingly, express no form of assurance on it.

The contents of this report were discussed with officials of Easttown Township and, where appropriate, their responses have been included in the report.

June 1, 2007

JACK WAGNER  
Auditor General

EASTTOWN TOWNSHIP POLICE PENSION PLAN  
STATUS OF PRIOR FINDING

Status Of Prior Audit Recommendation

· Failure To Prepare Adequate Financial Statements

During the audit period, the township prepared financial statements in accordance with accounting principles generally accepted in the United States of America.

EASTTOWN TOWNSHIP POLICE PENSION PLAN  
FINDINGS AND RECOMMENDATIONS

Finding No. 1 – Failure To Adopt Benefit Provisions Mandated By Act 30

Condition: On April 17, 2002, Act 600 was amended by Act 30, which made significant changes to the statutorily prescribed benefit structure of police pension plans subject to Act 600. Municipal officials have not amended the police pension plan’s benefit structure to adopt all of the changes mandated by Act 30. The specific inconsistencies are as follows:

<u>Benefit Provision</u>	<u>Governing Document</u>	<u>Act 600 (as amended)</u>
Survivor’s benefit	Same as Act 600 with a 50% survivor’s pension. However, the benefit stops upon remarriage and there is no provision for children under age 23 attending college to receive the benefit. There is also no definition for “attending college”.	A lifetime survivor’s benefit must be provided to the surviving spouse (or if no spouse survives or if he or she subsequently dies, the child or children under 18 years of age or if attending college, under or attaining the age of 23) of no less than 50% of the pension the member was receiving or would have been entitled to receive had he been retired at the time of death. (“Attending college” shall mean the eligible children are registered at an accredited institution of higher learning and are carrying a minimum course load of 7 credit hours per semester.)
Service-related disability benefit	70% of monthly average salary as of onset of disability until normal retirement date and then 50% of monthly average salary thereafter, reduced by workers’ compensation or any other program of disability benefits financed in whole or in part by the township.	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.

EASTTOWN TOWNSHIP POLICE PENSION PLAN  
FINDINGS AND RECOMMENDATIONS

Finding No. 1 – (Continued)

<u>Benefit Provision</u>	<u>Governing Document</u>	<u>Act 600 (as amended)</u>
Pre-vesting death benefit	Not provided	The surviving spouse of a member of the police force who dies before his pension has vested or if no spouse survives or if he or she survives and subsequently dies, the child or children under the age of eighteen years, or, if attending college, under or attaining the age of twenty-three years, of the member of the police force 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.

Criteria: The police pension plan's benefit structure should be in compliance with Act 600, as amended.

Cause: Municipal officials failed to establish adequate internal control procedures to ensure the plan's governing document was in compliance with Act 600, as amended.

Effect: 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 recommend that municipal officials, after consulting with their solicitor, take whatever action is necessary to bring the police pension plan's benefit structure into compliance with Act 600, as amended, at their earliest opportunity to do so.

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

EASTTOWN TOWNSHIP POLICE PENSION PLAN  
FINDINGS AND RECOMMENDATIONS

Finding No. 2 – Failure To Fully Pay The Minimum Municipal Obligation Of The Plan

Condition: The municipality did not fully pay the minimum municipal obligation (MMO) that was due to the police pension plan for the year 2006, as required by Act 205. Based upon an estimate prepared by this department, the municipality had an unpaid MMO balance of \$3,275.

Criteria: With regard to the MMO, Section 302(c) of Act 205 states, in part:

Annually, the chief administrative officer of the pension plan shall determine the minimum obligation of the municipality with respect to the pension plan for the following plan year.

Section 302(d) of Act 205 states, in part:

The minimum obligation of the municipality shall be payable to the pension plan from the revenue of the municipality.

Furthermore, Section 302(e) of Act 205 states, in part:

Any amount of the minimum obligation of the municipality which remains unpaid as of December 31 of the year in which the minimum obligation is due shall be added to the minimum obligation of the municipality for the following year, with interest from January 1 of the year in which the minimum obligation was first due until the date the payment is paid. . . .

Cause: Plan officials failed to establish adequate internal control procedures to ensure the MMO was fully paid in accordance with Act 205 requirements.

Effect: The proper determination of the plan's MMO ensures plan officials can properly allocate the necessary resources to the pension plan for the upcoming year. The failure to fully pay the MMO could result in the plan not having adequate resources to meet current and future benefit obligations to its members.

Due to the municipality's failure to fully pay the 2006 MMO by the December 31, 2006, deadline, the municipality must add the 2006 MMO balance to the current year's MMO and include interest, as required by Act 205.

EASTTOWN TOWNSHIP POLICE PENSION PLAN  
FINDINGS AND RECOMMENDATIONS

Finding No. 2 – (Continued)

Recommendation: We recommend that the municipality pay the MMO due to the police pension plan for the year 2006, with interest, in accordance with Section 302(e) of Act 205. A copy of the interest calculation must be maintained by the township for examination during our next audit of the plan.

Furthermore, we recommend the township develop adequate internal control procedures to ensure the plan's MMO is paid in accordance with Act 205 requirements.

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

EASTTOWN 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, except for distressed pension plans, for which annual reporting was required through January 1, 2003. The historical information, beginning as of January 1, 2001, 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)]
01-01-01	\$ 5,431,455	\$ 4,388,636	\$ (1,042,819)	123.8%	\$ 890,778	(117.1%)
01-01-03	4,688,210	5,147,544	459,334	91.1%	973,632	47.2%
01-01-05	5,045,505	5,804,761	759,256	86.9%	1,108,996	68.5%

Note: The market values of the plan's assets at 01-01-03 and 01-01-05 have been adjusted to reflect the smoothing of gains and/or losses over a 2-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.



EASTTOWN 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.

EASTTOWN TOWNSHIP POLICE PENSION PLAN  
 SUPPLEMENTARY INFORMATION  
 (UNAUDITED)

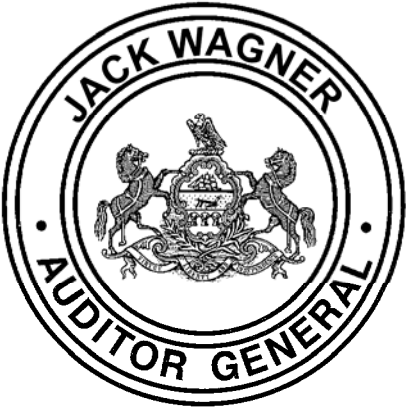
SCHEDULE OF CONTRIBUTIONS FROM EMPLOYER  
 AND OTHER CONTRIBUTING ENTITIES

Year Ended December 31	Annual Required Contribution	Percentage Contributed
2001	None	N/A
2002	\$ 74,948	100.0%
2003	77,209	100.0%
2004	168,420	100.0%
2005	178,748	100.0%
2006	208,976	98.4%

EASTTOWN 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, 2005
Actuarial cost method	Entry age normal
Amortization method	N/A
Remaining amortization period	N/A
Asset valuation method	Fair value, 2-year smoothing
Actuarial assumptions:	
Investment rate of return *	7.5%
Projected salary increases *	5.0%
* Includes inflation at	3.0%
Cost-of-living adjustments	Reflects the cost-of-living change in the preceding year based on one-half of the increase in the CPI-U Consumer Price Index of the U.S. Department of Labor.



EASTTOWN TOWNSHIP POLICE PENSION PLAN  
REPORT DISTRIBUTION LIST

This report was initially distributed to the following:

The Honorable Edward G. Rendell  
Governor  
Commonwealth of Pennsylvania

Easttown Township Police Pension Plan  
Chester County  
P.O. Box 79  
Devon, PA 19333

Mr. William F. Connor      Chairman, Board of Township Supervisors

Mr. Gene Williams      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](http://www.auditorgen.state.pa.us).