

LOWER HEIDELBERG TOWNSHIP POLICE PENSION PLAN

BERKS COUNTY

COMPLIANCE AUDIT REPORT

FOR THE PERIOD

JANUARY 1, 2004, TO DECEMBER 31, 2006



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BACKGROUND

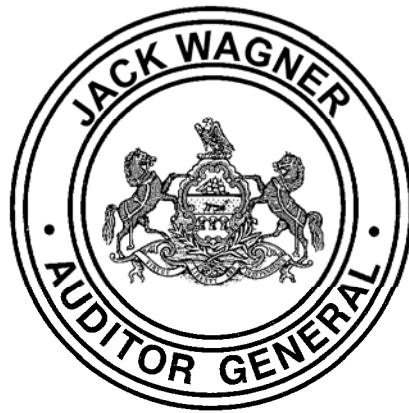
On December 18, 1984, the Pennsylvania Legislature adopted the Municipal Pension Plan Funding Standard and Recovery Act (P.L. 1005, No. 205, 53 P.S. §895.101, et seq.). The act established mandatory actuarial reporting and funding requirements and a uniform basis for the distribution of state aid to 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 Lower Heidelberg 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 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 Lower Heidelberg Township Police Pension Plan is a single-employer defined benefit pension plan locally controlled by the provisions of Ordinance No. 159, 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
Lower Heidelberg Township
Berks County
Sinking Spring, PA 19608

We have conducted a compliance audit of the Lower Heidelberg 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 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.

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 Lower Heidelberg 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 Lower Heidelberg 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 Properly Determine And Fully Pay The Minimum
Municipal Obligation Of The Plan

Finding No. 2 – Inconsistent Pension Benefits

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

July 19, 2007

JACK WAGNER
Auditor General

LOWER HEIDELBERG TOWNSHIP POLICE PENSION PLAN
STATUS OF PRIOR FINDINGS

Compliance With Prior Audit Recommendations

Lower Heidelberg Township has complied with the prior audit recommendations concerning the following:

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

The township reimbursed \$6,926 to the Commonwealth for the overpayment of state aid; and

- Failure To Prepare Financial Statements

The township has established and implemented procedures to ensure the preparation of annual financial statements in accordance with accounting principles generally accepted in the United States of America.

Rescission Of Prior Audit Recommendation

The following prior audit recommendation has been rescinded:

- Incorrect Data Supplied To Actuary For Actuarial Valuation Preparation

The township provided adequate documentation which supported the data contained in the January 1, 2003, actuarial valuation report.

LOWER HEIDELBERG TOWNSHIP POLICE PENSION PLAN
FINDINGS AND RECOMMENDATIONS

Finding No. 1 – Failure To Properly Determine And Fully Pay The Minimum Municipal
Obligation Of The Plan

Condition: Plan officials did not properly determine or fully pay the minimum municipal obligation (MMO) of the police pension plan for the year 2005, as required by Act 205. The MMO determined by the municipality understated payroll by \$48,310. Based upon an estimate prepared by this department, the municipality had an unpaid 2005 MMO balance of \$7,923.

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.

With regard to the payroll estimate used in the preparation of the MMO, the Pennsylvania Code, Title 16, Section 204.1(c)(1) states, in part:

The payroll used in determining the minimum municipal obligation of a pension plan under section 302(c) of the act shall be based on the payroll to be reported on the Internal Revenue Service Form W-2 and shall be calculated as the total payroll for active members of the plan as of the date of the determination, plus the payroll for the same active members of the plan projected to the year's end using the payroll rates in effect as of the date of the determination.

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. . . .

LOWER HEIDELBERG TOWNSHIP POLICE PENSION PLAN FINDINGS AND RECOMMENDATIONS

Finding No. 1 – (Continued)

Cause: The township did not comply with the Act 205 requirements because plan officials failed to include the estimated fourth quarter payroll in their determination of the MMO.

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 2005 MMO by the December 31, 2005, deadline, the municipality must add the 2005 MMO balance to the current year's MMO and include interest, as required by Act 205.

Recommendation: We recommend that the municipality pay the MMO due to the police pension plan for the year 2005, 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 that municipal officials develop and implement adequate internal control procedures to ensure that future MMO determinations are in accordance with Act 205 requirements.

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

Finding No. 2 – Inconsistent Pension Benefits

Condition: The pension plan's governing document, Ordinance No. 159, as amended, contains a benefit provision that conflicts with the collective bargaining agreement between the police officers and the township, as follows:

<u>Benefit Provision</u>	<u>Governing Document</u>	<u>Collective Bargaining Agreement</u>
Service-Related Disability Benefit	50% of the current monthly compensation at the date of disability.	75% of compensation of the member at the date of disability.

LOWER HEIDELBERG TOWNSHIP POLICE PENSION PLAN
FINDINGS AND RECOMMENDATIONS

Finding No. 2 – (Continued)

Criteria: A governing document which contains clearly defined and updated benefit provisions is a prerequisite for the consistent, sound administration of retirement benefits.

Cause: Municipal officials failed to update the plan's governing document to reflect the service-related disability benefit provision contained in the current bargaining agreement.

Effect: Inconsistent plan documents could result in inconsistent or improper benefit calculations and incorrect benefit payments from the pension plan.

Recommendation: We recommend that municipal officials amend the plan's governing document, as necessary, to reflect all benefit obligations of the pension plan and eliminate inconsistencies among the various plan documents.

Management's Response: Municipal officials agreed with the finding without exception and indicated that the plan's governing document will be amended to coincide with the current collective bargaining agreement.

Auditor's Conclusion: Based on the management response, it appears municipal officials intend to comply with the finding recommendation. This compliance will be evaluated during our next audit of the plan.

LOWER HEIDELBERG 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	\$ 460,439	\$ 393,620	\$ (66,819)	117.0%	\$ 252,814	(26.4%)
01-01-03	447,168	441,077	(6,091)	101.4%	274,158	(2.2%)
01-01-05	638,178	532,897	(105,281)	119.8%	304,071	(34.6%)

LOWER HEIDELBERG 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.

LOWER HEIDELBERG 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	\$ 25,518	116.3%
2002	26,511	134.9%
2003	35,759	100.0%
2004	38,677	100.0%
2005	34,448	100.0%
2006	37,272	100.0%

LOWER HEIDELBERG 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	Market value
Actuarial assumptions:	
Investment rate of return *	7.5%
Projected salary increases *	5.0%
* Includes inflation at	Not disclosed
Cost-of-living adjustments	1% for every 3% increase in Consumer Price Index with a maximum total increase of 30% or 75% of pension computation salary

LOWER HEIDELBERG TOWNSHIP POLICE PENSION PLAN
REPORT DISTRIBUTION LIST

This report was initially distributed to the following:

The Honorable Edward G. Rendell
Governor
Commonwealth of Pennsylvania

Lower Heidelberg Township Police Pension Plan
Berks County
720 Brownsville Road
Sinking Spring, PA 19608

Mr. R. David Seip	Chairman, Board of Township Supervisors
Ms. Sharon Leffler	Secretary/Treasurer

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.