

NORTH FRANKLIN TOWNSHIP POLICE PENSION PLAN

WASHINGTON COUNTY

COMPLIANCE AUDIT REPORT

FOR THE PERIOD

JANUARY 1, 2006, TO DECEMBER 31, 2008



NORTH FRANKLIN TOWNSHIP POLICE PENSION PLAN

WASHINGTON COUNTY

COMPLIANCE AUDIT REPORT

FOR THE PERIOD

JANUARY 1, 2006, TO DECEMBER 31, 2008

CONTENTS

	<u>Page</u>
Background.....	1
Letter from the Auditor General	3
Status of Prior Findings	5
Findings and Recommendations:	
Finding No. 1 – Noncompliance With Prior Audit Recommendation – Pension Benefit Not Authorized By Act 600 And The Plan’s Governing Document	6
Finding No. 2 – Failure To Pay Cost-of-Living Adjustments To Eligible Retirees	7
Supplementary Information	9
Report Distribution List	13

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 North Franklin 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. 1804, No. 600), as amended, 53 P.S. § 761 et seq.

The North Franklin Township Police Pension Plan is a single-employer defined benefit pension plan locally controlled by the provisions of Ordinance No. 15-2000, 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
North Franklin Township
Washington County
Washington, PA 15301

We have conducted a compliance audit of the North Franklin Township Police Pension Plan for the period January 1, 2006, to December 31, 2008. The audit was conducted pursuant to authority derived from Section 402(j) of Act 205 and in accordance with *Government Auditing Standards* applicable to performance audits 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. North Franklin 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.

Township officials are responsible for establishing and maintaining an internal control structure to provide reasonable assurance that the North Franklin 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 North Franklin 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 – Pension Benefit Not Authorized By Act 600 And The Plan’s Governing Document

Finding No. 2 – Failure To Pay Cost-of-Living Adjustments To Eligible Retirees

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

June 8, 2009

JACK WAGNER
Auditor General

NORTH FRANKLIN TOWNSHIP POLICE PENSION PLAN
STATUS OF PRIOR FINDINGS

Compliance With Prior Audit Recommendation

North Franklin 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 \$6,688 to the Commonwealth for the overpayment of state aid.

Status Of Prior Audit Recommendation

- Incorrect Pension Calculations

Excess benefits are still being paid to existing retirees. However, since the municipality received state aid based on unit value during the audit period, it did not receive state aid attributable to the excess benefits provided. The department will continue to monitor the impact of the excess benefits being paid to the existing retirees on the plan's future state aid allocations during future audits of the plan.

Noncompliance With Prior Audit Recommendation

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

- Pension Benefit Not Authorized By Act 600 And The Plan's Governing Document

NORTH FRANKLIN TOWNSHIP POLICE PENSION PLAN
FINDINGS AND RECOMMENDATIONS

Finding No. 1 – Noncompliance With Prior Audit Recommendation – Pension Benefit Not Authorized By Act 600 And The Plan’s Governing Document

Condition: As disclosed in the prior audit report, plan officials provided a pension benefit not authorized by Act 600 and the plan’s governing document. Plan officials included payment for accumulated sick leave that was not earned during the pension computation period in the determination of final average salary used to calculate monthly pension benefits for a police officer who retired on September 25, 2004.

Criteria: 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 payments for leave that was not earned during the pension computation period. Furthermore, Article I at Section 1.19 of the pension plan’s governing document, Ordinance No. 15-2000, states, in part:

“Final Average Monthly Salary” shall mean the average monthly salary earned by the Participant and paid by the Employer during the final thirty-six (36) months immediately preceding termination of employment. Salary shall include the Employee’s Compensation to which the Employee is entitled for the rendering of services in Employment but shall exclude for this purpose any single sum or extraordinary payment made which are not directly attributable to active Employment during the averaging period including but not limited to payment for accumulated sick leave, payment of a longevity bonus, or payment of a back pay damage award...

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

Effect: The plan is paying pension benefits to a retiree in excess of those authorized by Act 600 and the plan’s governing document. The retiree is receiving excess benefits of \$38 per month, which totaled approximately \$2,189 from the date of retirement through the date of this audit report. In addition, the retiree has received annual cost-of-living adjustments based on the excess pension benefit determination resulting in overpayments of \$916 through the date of this audit report.

NORTH FRANKLIN TOWNSHIP POLICE PENSION PLAN
FINDINGS AND RECOMMENDATIONS

Finding No. 1 – (Continued)

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.

Recommendation: We again recommend that the improper pension benefit be recalculated and adjusted prospectively. In addition, any excess benefit payments made from the plan will be deemed ineligible for funding with state aid. Accordingly, the pension plan's actuary may be required to determine the impact, if any, on the excess benefit payments on the plan's future state aid allocations and submit this information to the department.

We further recommend that future pension benefits be calculated and paid in accordance with the applicable provisions contained in the plan's governing document in effect at the time of a plan member's retirement.

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

Finding No. 2 – Failure To Pay Cost-of-Living Adjustments To Eligible Retirees

Condition: In 2008, the township did not authorize and pay the cost-of-living adjustments (COLAs) due to 2 eligible retirees in accordance with the plan's governing document and the collective bargaining agreement. In addition, the township did not authorize payment of the 2006 and 2007 COLAs until February and May of 2008, respectively.

Criteria: Section 5(g) of Act 600 states in part:

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.

NORTH FRANKLIN TOWNSHIP POLICE PENSION PLAN
FINDINGS AND RECOMMENDATIONS

Finding No. 2 – (Continued)

Section 4.06 of Ordinance No. 15-2000, states, in part:

Each Participant who shall retire and receive a retirement benefit under this Article IV shall be entitled to receive a cost of living adjustment to the amount of benefit payable to such Participant effective as of each annual anniversary date of the original commencement of the Participant's retirement benefit payments hereunder.

In addition, Section 4(F) of Article XVIII of the collective bargaining agreement (CBA) effective January 1, 2005, to December 31, 2008, states, in part:

All officers retiring after January 1, 2000, shall be entitled to a cost-of-living adjustment to their pension.

Cause: Municipal officials failed to establish adequate internal control procedures to ensure COLAs were determined and paid in accordance with the plan's governing document and the collective bargaining agreement.

Effect: The retirees did not receive the COLAs that they were entitled to.

Recommendation: We recommend that the township calculate and pay the COLAs due to the 2 retirees, with applicable interest.

We also recommend that plan officials establish adequate internal control procedures to ensure that future COLAs are paid timely and in accordance with Act 600 provisions.

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

NORTH FRANKLIN 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, 2003, 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)]
01-01-03	\$ 1,254,067	\$ 1,667,854	\$ 413,787	75.2%	\$ 366,179	113.0%
01-01-05	1,467,920	1,918,389	450,469	76.5%	236,706	190.3%
01-01-07	1,747,175	2,132,106	384,931	81.9%	327,122	117.7%

Note: The market values of the plan's assets at 01-01-03, 01-01-05 and 01-01-07, have been adjusted to reflect the smoothing of gains and/or losses over a 4-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.

NORTH FRANKLIN 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.

NORTH FRANKLIN 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
2003	\$ 81,866	100.0%
2004	94,024	100.0%
2005	92,131	100.0%
2006	83,899	100.0%
2007	95,337	100.0%
2008	102,411	100.0%

NORTH FRANKLIN 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, 2007
Actuarial cost method	Entry age normal
Amortization method	Level dollar, closed
Remaining amortization period	12 years
Asset valuation method	Market value, 4-year smoothing
Actuarial assumptions:	
Investment rate of return	7.5%
Projected salary increases *	5.0%
* Includes inflation at	3.0%

NORTH FRANKLIN TOWNSHIP POLICE PENSION PLAN
REPORT DISTRIBUTION LIST

This report was initially distributed to the following:

The Honorable Edward G. Rendell
Governor
Commonwealth of Pennsylvania

North Franklin Township Police Pension Plan
Washington County
620 Franklin Farms Road
Washington, PA 15301

Mr. Donald Hazlett	Chairman, Board of Township Supervisors
Mr. Dennis Dydiw	Township Supervisor
Ms. Jacqueline Kotchman	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.