

COMPLIANCE AUDIT

East Pennsboro Township Police Pension Plan Cumberland County, Pennsylvania For the Period January 1, 2015 to December 31, 2018

December 2019



Commonwealth of Pennsylvania
Department of the Auditor General

Eugene A. DePasquale • Auditor General



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**EUGENE A. DePASQUALE
AUDITOR GENERAL**

Board of Township Commissioners
East Pennsboro Township
Cumberland County
Enola, PA 17025

We have conducted a compliance audit of the East Pennsboro Township Police Pension Plan for the period January 1, 2015 to December 31, 2018. We also evaluated compliance with some requirements subsequent to that period when possible. 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. To determine whether the pension plan was administered in compliance with applicable state laws, regulations, contracts, administrative procedures, and local ordinances and policies, our methodology included the following:

- We determined whether state aid was properly determined and deposited in accordance with Act 205 requirements by verifying the annual deposit date of state aid and determining whether deposits were made within 30 days of receipt for all years within the period under audit.
- We determined whether annual employer contributions were calculated and deposited in accordance with the plan's governing document and applicable laws and regulations by examining the municipality's calculation of the plan's annual financial requirements and minimum municipal obligation (MMO) and comparing these calculated amounts to amounts actually budgeted and deposited into the pension plan as evidenced by supporting documentation.

- We determined whether annual employee contributions were calculated, deducted, and deposited into the pension plan in accordance with the plan's governing document and applicable laws and regulations by testing total members' contributions on an annual basis using the rates obtained from the plan's governing document in effect for all years within the period under audit and examining documents evidencing the deposit of these employee contributions into the pension plan.
- We determined whether retirement benefits calculated for all 3 of the plan members who retired during the current audit period represent payments to all (and only) those entitled to receive them and were properly determined and disbursed in accordance with the plan's governing document, applicable laws and regulations by recalculating the amount of the monthly pension benefits due to the retired individuals and comparing these amounts to supporting documentation evidencing amounts determined and actually paid to the recipients.
- We determined whether the January 1, 2015 and January 1, 2017 actuarial valuation reports were prepared and submitted by March 31, 2016 and 2018, respectively, in accordance with Act 205 and whether 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 by comparing selected information to supporting source documentation.
- We determined whether the terms of the contractual agreement with the Pennsylvania Municipal Retirement System were in accordance with the plan's governing document, if separately stated, and applicable laws and regulations by comparing the terms of the contractual agreement with the plan's governing document, if separately stated, and applicable laws and regulations.
- We determined whether provisions of the Deferred Retirement Option Plan (DROP) were in accordance with the provisions of Act 205 by examining provisions stated in the plan's governing documents.

The East Pennsboro Township Police Pension Plan participates in the Pennsylvania Municipal Retirement System (PMRS), which is an agent multiple-employer public employee retirement system that acts as a common investment and administrative agent for participating municipal pension plans. PMRS issues a separate Comprehensive Annual Financial Report, copies of which are available from the PMRS accounting office. PMRS's 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 East Pennsboro 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 and as previously described, 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 procedures indicated that, in all significant respects, the East Pennsboro 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 – Incorrect Data On Certification Form AG 385 Resulting In An Overpayment Of State Aid

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 East Pennsboro Township and, where appropriate, their responses have been included in the report. We would like to thank township officials for the cooperation extended to us during the conduct of the audit.

December 5, 2019



EUGENE A. DEPASQUALE
Auditor General

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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.

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 East Pennsboro Township Police Pension Plan is also governed by implementing regulations adopted by the former 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 15 - Pennsylvania Municipal Retirement Law, Act of February 1, 1974
(P.L. 34, No. 15), as amended, 53 P.S. § 881.101 et seq.

The East Pennsboro Township Police Pension Plan is a single-employer defined benefit pension plan locally controlled by the provisions of Ordinance No. 787-15, adopted pursuant to Act 15. The plan is also affected by the provisions of collective bargaining agreements between the township and its police officers. The plan was established June 1, 1979. Active members are required to contribute 8 percent of their compensation to the plan; however, member contributions were waived in 2015, reduced to 1 percent for 2016, 1.25 percent for 2017, 1.50 percent for 2018 and are currently reduced to 1.75 percent for 2019. As of December 31, 2018, the plan had 20 active members, 1 terminated member eligible for vested benefits in the future, and 19 retirees receiving benefits funded through annuities purchased with plan assets.

BACKGROUND – (Continued)

As of December 31, 2018, selected plan benefit provisions are as follows:

Eligibility Requirements:

Normal Retirement	Available at age 50 with 12 years of credited service.
Early Retirement	A voluntary early retirement available after 20 years of service. An involuntary early retirement is available after 8 years of service.
Vesting	100% vesting available after 12 years of service.

Retirement Benefit:

Benefit equals 2.0% times credited service times Final Average Salary (FAS), but in no event is the basic benefit greater than 50% of FAS. FAS based on final 3 years annualized salary. There is no Social Security offset. A service increment for credited service in excess of 25 years provided. Maximum service increment \$250 per month.

Survivor Benefit:

If eligible to retire or if retired at time of death, spouse receives 50% of member's benefit.

Disability Benefit:

Service Related	A 50% disability benefit is provided to a member who is unable to perform gainful employment regardless of age or service, offset by available Workers' Compensation benefits.
Non-service Related	A 30% disability benefit is provided to a member who has at least 10 years of service and who is able to perform gainful employment.

EAST PENNSBORO TOWNSHIP POLICE PENSION PLAN
FINDING AND RECOMMENDATION

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

Condition: The township certified 2 ineligible police officers (4 units) and overstated payroll by \$187,319 on the Certification Form AG 385 filed in 2016. The ineligible members retired effective April 11, 2015, and entered the township's Deferred Retirement Option Program (DROP). In addition, the township certified an ineligible police officer (2 units) and overstated payroll by \$90,388 and an ineligible non-uniformed employee (1 unit) and overstated payroll by \$5,596 on the Certification Form AG 385 filed in 2018. The ineligible police officer retired June 23, 2017 and entered the township's DROP. Similarly, subsequent to the current audit period, the township certified an ineligible police officer (2 units) and overstated payroll by \$50,113 and failed to certify an eligible non-uniformed employee (1 unit) and understated payroll by \$33,257 on the Certification Form AG 385 filed in 2019. The ineligible police officer retired on April 11, 2015, and entered the township's DROP. The data contained on these certification forms is based on prior calendar year information.

Criteria: Pursuant to Act 205, at Section 402(e)(2), in order to be eligible for certification, an employee must have been employed on a full-time basis for at least six consecutive months and must have been participating in a pension plan during the certification year.

Furthermore, Act 205 at Section 402(e)(2) states, in part:

For the purpose of computing and reporting the applicable number of units, a DROP participant shall not be reported to the Auditor General as an active employee.

Cause: Plan officials were unaware that DROP participants along with their applicable compensation are not eligible for certification purposes and failed to establish adequate internal control procedures to ensure the accuracy of the data certified.

Effect: The data submitted on the certification form is used, in part, to calculate the state aid due to the municipality for distribution to its pension plans. Because the township's state aid allocations were based on unit value, the incorrect certification of pension data affected the township's state aid allocation, as identified below:

EAST PENNSBORO TOWNSHIP POLICE PENSION PLAN
FINDING AND RECOMMENDATION

Finding – (Continued)

<u>Year</u>	<u>Type Of Plan</u>	<u>Units Overstated (Understated)</u>	<u>Unit Value</u>	<u>State Aid Overpayment</u>
2016	Police	4	\$ 4,375	\$ 17,500
2018	Police	2	4,684	\$ 9,368
	Non-Uniformed	1	4,684	4,684
			Total	<u>\$ 14,052</u>
2019	Police	2	5,120	\$ 10,240
	Non-Uniformed	(1)	5,120	(5,120)
			Total	<u>\$ 5,120</u>
Total Overpayment of State Aid				<u>\$ 36,672</u>

Furthermore, the township’s future state aid allocations may be withheld until the finding recommendation is complied with.

Recommendation: We recommend that the total excess state aid, in the amount of \$36,672, be returned to the Commonwealth. A check in this amount, with interest compounded annually from date of receipt to date of repayment, at a rate earned by the pension plan, should be made payable to: Commonwealth of Pennsylvania and mailed to: Department of the Auditor General, Municipal Pension & Fire Relief Programs Unit, 321 Finance Building, Harrisburg, PA 17120. A copy of the interest calculation must be submitted along with the check.

We also recommend that in the future, plan officials establish adequate internal control procedures, such as having at least two people review the data certified, to ensure compliance with the instructions that accompany Certification Form AG 385 to assist them in accurately reporting the required pension data.

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

Auditor’s Conclusion: Due to the potential withhold of state aid, the township’s compliance with the finding recommendation will be monitored subsequent to the release of the audit report and through our next audit of the plan.

EAST PENNSBORO TOWNSHIP POLICE PENSION PLAN
POTENTIAL WITHHOLD OF STATE AID

The finding contained in this audit report cites an overpayment of state aid to the township in the amount of \$36,672, plus interest. A condition of this nature may lead to a total withholding of state aid in the future unless that finding is corrected. A check in this amount with interest, at a rate earned by the pension plan, should be made payable to: Commonwealth of Pennsylvania, and mailed to: Department of the Auditor General, Municipal Pension & Fire Relief Programs Unit, 321 Finance Building, Harrisburg, PA 17120.

EAST PENNSBORO TOWNSHIP POLICE PENSION PLAN
SUPPLEMENTARY INFORMATION
(UNAUDITED)

The supplementary information contained on Pages 6 through 8 reflects the implementation of GASB Statement No. 67, *Financial Reporting for Pension Plans*. The objective of this statement is to improve financial reporting by state and local governmental pension plans.

SCHEDULE OF CHANGES IN THE NET PENSION LIABILITY AND RELATED RATIOS
FOR THE YEARS ENDED DECEMBER 31, 2014, 2015, 2016, AND 2017

	<u>2014</u>	<u>2015</u>	<u>2016</u>	<u>2017</u>
Total Pension Liability				
Service cost	\$ 351,201	\$ 394,388	\$ 301,340	\$ 372,921
Interest	641,978	683,419	704,066	724,878
Difference between expected and actual experience	203,613	-	(29,267)	-
Changes of assumptions	-	(141,482)	421,130	-
Benefit payments, including refunds of member contributions	<u>(497,849)</u>	<u>(474,876)</u>	<u>(460,704)</u>	<u>(464,776)</u>
Net Change in Total Pension Liability	698,943	461,449	936,565	633,023
Total Pension Liability – Beginning	11,566,728	12,265,671	12,727,120	13,663,685
Total Pension Liability – Ending (a)	<u>\$ 12,265,671</u>	<u>\$ 12,727,120</u>	<u>\$ 13,663,685</u>	<u>\$ 14,296,708</u>
Plan Fiduciary Net Position				
Contributions – employer	\$ 295,658	\$ 354,949	\$ 391,466	\$ 368,447
Contributions – PMRS assessment	-	-	-	760
Contributions – employee	-	-	16,385	24,523
PMRS investment income	623,476	617,356	650,812	653,466
Market value investment income	(176,893)	(856,439)	366,294	1,437,538
Benefit payments, including refunds of member contributions	(497,849)	(474,876)	(460,704)	(464,776)
PMRS administrative expense	(800)	(780)	(780)	(760)
Additional administrative expense	<u>(23,910)</u>	<u>(25,736)</u>	<u>(31,884)</u>	<u>(30,052)</u>
Net Change in Plan Fiduciary Net Position	219,682	(385,526)	931,589	1,989,146
Plan Fiduciary Net Position – Beginning	11,422,510	11,642,192	11,256,666	12,188,255
Plan Fiduciary Net Position – Ending (b)	<u>\$ 11,642,192</u>	<u>\$ 11,256,666</u>	<u>\$ 12,188,255</u>	<u>\$ 14,177,401</u>
Net Pension Liability – Ending (a-b)	<u>\$ 623,479</u>	<u>\$ 1,470,454</u>	<u>\$ 1,475,430</u>	<u>\$ 119,307</u>
Plan Fiduciary Net Position as a Percentage of the Total Pension Liability	94.92%	88.45%	89.20%	99.17%
Estimated Covered Employee Payroll	\$ 1,582,807	\$ 1,764,999	\$ 1,638,473	\$ 1,885,085
Net Pension Liability as a Percentage of Covered Employee Payroll	39.39%	83.31%	90.05%	6.33%

EAST PENNSBORO TOWNSHIP POLICE PENSION PLAN
 SUPPLEMENTARY INFORMATION
 (UNAUDITED)

Sensitivity Of The Net Pension Liability To Changes In The Discount Rate

The following presents the net pension liability of the township as of December 31, 2014 and 2015, calculated using the discount rate of 5.50%, as well as what the township's net pension liability would be if it were calculated using a discount rate that is 1 percentage-point lower or 1 percentage-point higher than the current rate:

	<u>1% Decrease (4.50%)</u>	<u>Current Discount Rate (5.50%)</u>	<u>1% Increase (6.50%)</u>
Net Pension Liability – 12/31/14	\$ 2,291,876	\$ 623,479	\$ (763,520)
Net Pension Liability – 12/31/15	\$ 3,210,828	\$ 1,470,454	\$ 28,915

In addition, the following presents the net pension liability of the township as of December 31, 2016 and 2017, calculated using the discount rate of 5.25%, as well as what the township's net pension liability would be if it were calculated using a discount rate that is 1 percentage-point lower or 1 percentage-point higher than the current rate:

	<u>1% Decrease (4.25%)</u>	<u>Current Discount Rate (5.25%)</u>	<u>1% Increase (6.25%)</u>
Net Pension Liability – 12/31/16	\$ 3,381,291	\$ 1,475,430	\$ (95,690)
Net Pension Liability – 12/31/17	\$ 2,113,464	\$ 119,307	\$ (1,524,601)

EAST PENNSBORO TOWNSHIP POLICE PENSION PLAN
 SUPPLEMENTARY INFORMATION
 (UNAUDITED)

SCHEDULE OF CONTRIBUTIONS

Year Ended December 31	Actuarially Determined Contribution	Actual Contributions	Contribution Deficiency (Excess)	Covered- Employee Payroll *	Contributions as a Percentage of Covered- Employee Payroll
2014	\$ 288,596	\$ 295,658	\$ (7,062)	\$1,582,807	18.68%
2015	354,949	354,949	-	1,764,999	20.11%
2016	367,945	391,466	(23,521)	1,638,473	23.89%
2017	391,466	369,207	22,259	1,885,085	19.59%
2018	415,619	415,619	-		

Note: 2017 Actual Contributions above are shown net of excess contributions (\$23,521) from 2016 which were refunded to the township during 2017 and a \$1,262 miscellaneous deposit into the Municipal Reserve Account. As such, there was no funding deficiency during 2017 as required by Act 205.

* Due to the timing of this audit, covered-employee payroll for 2018 was not provided in this schedule.

EAST PENNSBORO 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, 2013, is as follows:

	(1)	(2)	(3)	(4)
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)
01-01-13	\$ 10,989,981	\$ 10,801,796	\$ (188,185)	101.7%
01-01-15	11,930,576	12,265,671	335,095	97.3%
01-01-17	13,165,256	13,663,685	498,429	96.4%

EAST PENNSBORO 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.

EAST PENNSBORO TOWNSHIP POLICE PENSION PLAN
 SUPPLEMENTARY INFORMATION
 NOTES TO SUPPLEMENTARY SCHEDULES
 (UNAUDITED)

The information presented in the 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, 2017
Actuarial cost method	Entry age normal
Amortization method	Level dollar
Remaining amortization period	12 years
Asset valuation method	The Actuarial Value of Assets equals the plan's member, municipal, DROP (if applicable) reserve accounts plus the retiree actuarial liability. This asset smoothing is based on the unique legislative structure of PMRS and the administrative rules adopted by the PMRS Board in conjunction with Pennsylvania Municipal Retirement Law, all of which are subject to comply with the Actuarial Standards of Practice No. 44, Selection and Use of Asset Valuation Methods when defining the actuarial Value of Assets.

Actuarial assumptions:

Investment rate of return	5.25%, compounded annually, net of investment and administration expenses.
Projected salary increases	Total rate (including inflation) (e.g. age 25 – 7.05%; age 35 – 4.55%; age 45 – 3.97%; age 55 – 3.44%; age 65 – 2.80%).
Cost-of-living adjustments	2.8% per year, subject to plan limitations.

EAST PENNSBORO TOWNSHIP POLICE PENSION PLAN
REPORT DISTRIBUTION LIST

This report was initially distributed to the following:

The Honorable Tom W. Wolf
Governor
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