

# COMPLIANCE AUDIT

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## Southern Regional Police Pension Plan Lancaster County, Pennsylvania For the Period January 1, 2014 to December 31, 2017

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November 2018



Commonwealth of Pennsylvania  
Department of the Auditor General

Eugene A. DePasquale • Auditor General



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EUGENE A. DePASQUALE  
AUDITOR GENERAL

Pequea Township Board of Supervisors  
Southern Regional Police Department  
Lancaster County  
Willow Street, PA 17584

We have conducted a compliance audit of the Southern Regional Police Pension Plan for the period January 1, 2014 to December 31, 2017. 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 our audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our finding and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our finding 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 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. To determine if municipal officials took appropriate corrective action to address the finding contained in our prior audit report, we inquired of plan officials and evaluated supporting documentation provided by officials evidencing that the suggested corrective action has been appropriately taken. 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 the plan member 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 benefit due to the retired individual and comparing this amount to supporting documentation evidencing the amount determined and actually paid to the recipient. We also determined whether retirement benefits calculated for the plan member who elected to vest during the current audit period represent payments to one entitled to receive them and were properly determined in accordance with the plan's governing document, applicable laws and regulations by recalculating the amount of the pension benefit due to the terminated-vested individual and comparing this amounts to supporting documentation evidencing the amount determined.
- We determined whether the January 1, 2013, January 1, 2015, and January 1, 2017 actuarial valuation reports were prepared and submitted by March 31, 2014, 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.

The Southern Regional 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.

Regional officials are responsible for establishing and maintaining effective internal controls to provide reasonable assurance that the Southern Regional 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 regional officials' internal controls as they relate to the regional officials' compliance with those requirements and that we considered to be significant within the context of our audit objectives, 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 objectives.

The results of our procedures indicated that, in all significant respects, the Southern Regional 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 – Failure To Deposit The Full Amount Of State Aid Into The Pension Plan

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 Southern Regional Police Department and, where appropriate, their responses have been included in the report. We would like to thank regional officials for the cooperation extended to us during the conduct of the audit.

October 17, 2018



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 Southern Regional 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.

Act 600 - Police Pension Fund Act, Act of May 29, 1956 (P.L. 1804, No. 600), as amended, 53 P.S. § 767 et seq.

The Southern Regional Police Pension Plan is a single-employer defined benefit pension plan locally controlled by the provisions of Ordinance No. 205-2017, effective January 1, 2018, adopted pursuant to Act 15. Prior to January 1, 2018, the plan was a single-employer defined benefit pension plan controlled by the provisions of Resolution No. 02-14, effective September 1, 2014, adopted pursuant to Act 15. Prior to September 1, 2014, the plan was a single-employer defined benefit pension plan controlled by the provisions of Resolution No. 02-2009, as amended, adopted pursuant to Act 600. The plan is also affected by the provisions of collective bargaining agreements between the regional and its police officers. The plan was established June 7, 1974. Active members are required to contribute 1.3 percent of their compensation to the plan. As of December 31, 2017, the plan had 7 active members, 2 terminated member eligible for vested benefits in the future, and 3 retirees receiving pension benefits.

Pursuant to Ordinance No. 205-2017, the Southern Regional Police Commission was dissolved effective December 31, 2017 and assets of the commission were transferred to Pequea Township. The Southern Regional Police Department continues under the oversight and direction of Pequea Township, and the township assumed responsibility for the regional police pension plan effective January 1, 2018.

## **BACKGROUND – (Continued)**

As of December 31, 2017, selected plan benefit provisions are as follows:

### Eligibility Requirements:

Normal Retirement	Age 50 and 12 years of service.
Early Retirement	Voluntary after 20 years of credited service; involuntary after 8 years of credited service.
Vesting	A member is 100% vested after 12 years of service.

### Retirement Benefit:

2% times Final Average Salary (FAS) times credited service, maximum 50% of FAS. FAS based upon last 3 years annualized salary. There is no Social Security offset. A service increment for credited service in excess of 25 years provided. Maximum benefit \$100 per month.

### Survivor Benefit:

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

### Service Related Disability Benefit:

A 50% disability benefit is provided to a member who is unable to perform gainful employment regardless of age or service. Offset by Social Security disability benefits.

SOUTHERN REGIONAL POLICE PENSION PLAN  
STATUS OF PRIOR FINDING

Compliance With Prior Audit Recommendation

The Southern Regional Police Commission complied with the prior audit recommendation concerning the following:

- Failure To Properly Determine And Fully Pay The Minimum Municipal Obligation Of The Plan

During the current audit period, the regional commission paid the MMO due to the police pension plan for the year 2014, with interest, in accordance with Section 302(e) of Act 205.



SOUTHERN REGIONAL POLICE PENSION PLAN  
FINDING AND RECOMMENDATION

**Finding – Failure To Deposit The Full Amount Of State Aid Into The Pension Plan**

Condition: Plan officials did not deposit the full amount of the regional’s 2016 state aid allocation into the pension plan. The regional received its 2016 state aid allocation in the amount of \$69,994 on September 23, 2016, but, as of the date of this report, only state aid totaling \$68,150 was deposited into the pension plan.

Criteria: Section 402(g) of Act 205 states, in part:

. . . the total amount of the general municipal pension system State aid received by the municipality shall, within 30 days of receipt by the treasurer of the municipality, be deposited in the pension fund or the alternate funding mechanism applicable to the pension plan.

Cause: The full amount of the 2016 state aid was not deposited into the pension plan because internal control procedures were not in effect to ensure the deposit of the full amount of state aid.

Effect: When state aid is not deposited into a pension plan account, the funds are not available to pay operating expenses or for investment and the risk of misapplication is increased.

Recommendation: We recommend that plan officials deposit the regional’s remaining state aid allocation of \$1,844, plus interest earned during the period beyond the 30 day grace period allowed by Act 205, compounded annually, into the pension plan. A copy of the interest calculation must be maintained by the plan officials for examination during our next audit of the plan.

We also recommend that plan officials develop and implement procedures to ensure that future state aid is deposited into an eligible pension plan within 30 days of receipt by the municipal treasurer.

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

Auditor’s Conclusion: Compliance will be evaluated during our next audit of the plan.

SOUTHERN REGIONAL POLICE PENSION PLAN  
SUPPLEMENTARY INFORMATION  
(UNAUDITED)

The supplementary information contained on Pages 5 and 6 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, AND 2016

	<u>2014</u>	<u>2015</u>	<u>2016</u>
Total Pension Liability			
Service cost	\$ 27,081	\$ 99,616	\$ 76,937
Interest	28,678	116,320	123,229
Difference between expected and actual experience	-	-	160,509
Changes of assumptions	-	(32,512)	91,573
Transfers	1,980,187	-	-
Benefit payments, including refunds of member contributions	<u>(5,844)</u>	<u>(30,019)</u>	<u>(40,370)</u>
Net Change in Total Pension Liability	2,030,102	153,405	411,878
Total Pension Liability - Beginning	<u>-</u>	<u>2,030,102</u>	<u>2,183,507</u>
Total Pension Liability - Ending (a)	<u>\$ 2,030,102</u>	<u>\$ 2,183,507</u>	<u>\$ 2,595,385</u>
Plan Fiduciary Net Position			
Contributions – employer*	\$ 61,025	\$ 81,759	\$ 68,130
Contributions – PMRS assessment	-	-	20
Contributions – employee	2,432	6,206	5,615
PMRS investment income	34,982	117,490	130,324
Market value investment income	(72,206)	(124,109)	95,895
Transfers	2,081,603	-	-
Benefit payments, including refunds of member contributions	(5,844)	(30,019)	(40,370)
PMRS administrative expense	(220)	(220)	(220)
Additional administrative expense	<u>(1,342)</u>	<u>(4,898)</u>	<u>(6,385)</u>
Net Change in Plan Fiduciary Net Position	2,100,430	46,209	253,009
Plan Fiduciary Net Position - Beginning	<u>-</u>	<u>2,100,430</u>	<u>2,146,639</u>
Plan Fiduciary Net Position - Ending (b)	<u>\$ 2,100,430</u>	<u>\$ 2,146,639</u>	<u>\$ 2,399,648</u>
Net Pension Liability - Ending (a-b)	<u>\$ (70,328)</u>	<u>\$ 36,868</u>	<u>\$ 195,737</u>
Plan Fiduciary Net Position as a Percentage of the Total Pension Liability	103.46%	98.31%	92.46%
Estimated Covered Employee Payroll	\$ 527,623	\$ 485,209	\$ 431,948
Net Pension Liability as a Percentage of Covered Employee Payroll	(13.33%)	7.60%	45.31%

\* 2014 employer contributions include \$220 administrative expenses and \$621 allocated insurance premiums. 2015 employer contributions include \$7,985 deposited for the 2014 MMO including interest and \$507 in member contributions.

SOUTHERN REGIONAL 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 regional as of December 31, 2014 and 2015, calculated using the discount rate of 5.50%, as well as what the regional'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	\$ 257,053	\$ (70,328)	\$ (338,552)
Net Pension Liability - 12/31/15	\$ 391,251	\$ 36,868	\$ (252,354)

The following presents the net pension liability of the regional as of December 31, 2016, calculated using the discount rate of 5.25%, as well as what the regional'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 - 12/31/17	\$ 613,246	\$ 195,737	\$ (144,482)

SOUTHERN REGIONAL 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	\$ 1,619,230	\$ 1,358,066	\$ (261,164)	119.2%
01-01-15	2,136,326	2,030,102	(106,224)	105.2%
01-01-17	2,561,016	2,595,385	34,369	98.7%

Note: The market value of the plan's assets at 01-01-13 was adjusted to reflect the smoothing of gains and/or losses over a 5-year averaging period limited to a maximum of 120 percent and a minimum of 80 percent of the fair market value of assets. 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.

SOUTHERN REGIONAL 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.

SOUTHERN REGIONAL POLICE PENSION PLAN  
SUPPLEMENTARY INFORMATION  
(UNAUDITED)

SCHEDULE OF CONTRIBUTIONS FROM EMPLOYER  
AND OTHER CONTRIBUTING ENTITIES

Year Ended December 31	Annual Required Contribution	Percentage Contributed
2012	\$ 82,252	100.0%
2013	83,282	100.0%
2014	66,390	100.0%
2015	73,267	100.0%
2016	68,130	100.0%
2017	98,314	100.0%

SOUTHERN REGIONAL 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	13 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
Salary scale	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

SOUTHERN REGIONAL POLICE PENSION PLAN  
REPORT DISTRIBUTION LIST

This report was initially distributed to the following:

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