

COMPLIANCE AUDIT

Washington Township Police Pension Plan Northampton County, Pennsylvania For the Period January 1, 2014 to December 31, 2017

November 2018



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 Supervisors
Washington Township
Northampton County
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We have conducted a compliance audit of the Washington Township 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 the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our conclusions based on our audit objective. We believe that the evidence obtained provides a reasonable basis for our 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 the plan member who retired during the current audit period represents 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 these amounts to supporting documentation evidencing amounts determined and actually paid to the recipient.
- 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 plan's unallocated insurance contract, including ownership and any restrictions, were in compliance with plan provisions, investment policies, and state regulations by comparing the terms of the contract with the plan's provisions, investment policies, and state regulations.

Washington 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 effective internal controls to provide reasonable assurance that the Washington 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 Washington Township Police Pension Plan was administered in compliance with applicable state laws, regulations, contracts, administrative procedures, and local ordinances and policies.

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. However, we are extremely concerned about the funded status of the plan contained in the schedule of funding progress included in this report which indicates a decline of assets available to satisfy the long-term liabilities of the plan. The plan's funded ratio went from 74.2% as of January 1, 2013, to a ratio of 57.2% as of January 1, 2017, which is the most recent data available. Based on this information, the former Public Employee Retirement Commission issued a notification that the township is currently in Level II moderate distress status. We encourage township officials to monitor the funding of the police pension plan to ensure its long-term financial stability.

The contents of this report were discussed with officials of Washington 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.

October 18, 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 Washington 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 600 - Police Pension Fund Act, Act of May 29, 1956 (P.L. 1804, No. 600), as amended, 53 P.S. § 767 et seq.

The Washington Township Police Pension Plan is a single-employer defined benefit pension plan locally controlled by the provisions of Ordinance No. 248, 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. The plan was established December 30, 1968. Active members are required to contribute 5 percent of compensation to the plan. As of December 31, 2017, the plan had 5 active members, no terminated members eligible for vested benefits in the future, and 4 retirees receiving pension benefits from the plan.

BACKGROUND – (Continued)

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

Eligibility Requirements:

Normal Retirement	Age 50 and 25 years of service for participants hired on or after 7/27/98. Age 50 and 20 years of service for participants hired before 7/27/98.
Early Retirement	None
Vesting	Member is 100% vested after 12 years of service.

Retirement Benefit:

Benefit equals 50% of final 60 months average salary for employees hired on or after 7/27/98.

Benefit equals 75% of final 60 months average salary for employees hired before 7/27/98.

Survivor Benefit:

Before Retirement Eligibility Refund of member contributions plus interest.

After Retirement Eligibility A monthly benefit equal to 50% of the pension the member was receiving or was entitled to receive on the day of the member's death.

Service Related Disability Benefit:

Benefit equals 50% of the member's salary at the time the disability was incurred, offset by Social Security disability benefits received for the same injury.

WASHINGTON TOWNSHIP POLICE PENSION PLAN
SUPPLEMENTARY INFORMATION
(UNAUDITED)

The supplementary information contained on Pages 3 through 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 AND 2015

	<u>2014</u>	<u>2015</u>
Total Pension Liability		
Service cost	\$ 47,633	\$ 51,889
Interest	94,702	121,779
Difference between expected and actual experience	-	266,719
Changes of assumptions	-	66,782
Benefit payments, including refunds of member contributions	<u>(71,717)</u>	<u>(113,326)</u>
Net Change in Total Pension Liability	70,618	393,843
Total Pension Liability – Beginning	<u>1,172,003</u>	<u>1,242,621</u>
Total Pension Liability - Ending (a)	<u><u>\$ 1,242,621</u></u>	<u><u>\$ 1,636,464</u></u>
 Plan Fiduciary Net Position		
Contributions – employer	\$ 28,284	\$ 30,099
Contributions – member	14,292	16,814
Contributions – State Aid	41,425	39,907
Net investment income	37,376	(18,837)
Benefit payments, including refunds of member contributions	<u>(71,717)</u>	<u>(113,326)</u>
Administrative expenses	<u>(5,000)</u>	<u>(6,250)</u>
Net Change in Plan Fiduciary Net Position	44,660	(51,593)
Plan Fiduciary Net Position – Beginning	<u>893,224</u>	<u>937,884</u>
Plan Fiduciary Net Position - Ending (b)	<u><u>\$ 937,884</u></u>	<u><u>\$ 886,291</u></u>
 Net Pension Liability - Ending (a-b)	<u><u>\$ 304,737</u></u>	<u><u>\$ 750,173</u></u>
 Plan Fiduciary Net Position as a Percentage of the Total Pension Liability	75.5%	54.2%
 Estimated Covered Employee Payroll	\$ 303,158	\$ 299,850
 Net Pension Liability as a Percentage of Covered Employee Payroll	100.5%	250.2%

WASHINGTON TOWNSHIP POLICE PENSION PLAN
SUPPLEMENTARY INFORMATION
(UNAUDITED)

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

	<u>2016</u>	<u>2017</u>
Total Pension Liability		
Service cost	\$ 54,483	\$ 45,399
Interest	126,335	131,852
Difference between expected and actual experience	-	30,312
Changes of assumptions	-	47,510
Benefit payments, including refunds of member contributions	<u>(121,648)</u>	<u>(121,648)</u>
Net Change in Total Pension Liability	59,170	133,425
Total Pension Liability – Beginning	<u>1,636,464</u>	<u>1,695,634</u>
Total Pension Liability - Ending (a)	<u>\$ 1,695,634</u>	<u>\$ 1,829,059</u>
 Plan Fiduciary Net Position		
Contributions – employer	\$ 77,289	\$ 67,616
Contributions – member	16,963	16,902
Contributions – State Aid	36,221	48,062
Net investment income	33,684	108,464
Benefit payments, including refunds of member contributions	<u>(121,648)</u>	<u>(121,648)</u>
Administrative expenses	<u>(6,250)</u>	<u>(6,250)</u>
Net Change in Plan Fiduciary Net Position	36,259	113,146
Plan Fiduciary Net Position – Beginning	<u>886,291</u>	<u>922,550</u>
Plan Fiduciary Net Position - Ending (b)	<u>\$ 922,550</u>	<u>\$ 1,035,696</u>
 Net Pension Liability - Ending (a-b)	<u>\$ 773,084</u>	<u>\$ 793,363</u>
 Plan Fiduciary Net Position as a Percentage of the Total Pension Liability	54.4%	56.6%
 Estimated Covered Employee Payroll	\$ 324,296	\$ 343,748
 Net Pension Liability as a Percentage of Covered Employee Payroll	238.4%	230.8%

WASHINGTON 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, 2017, calculated using the discount rate of 7.50%, 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:

	1% Decrease (6.50%)	Current Discount Rate (7.50%)	1% Increase (8.50%)
Net Pension Liability- 12/31/17	\$ 990,123	\$ 793,363	\$ 625,465

In addition, the following presents the net pension liability of the township as of December 31, 2015 and 2016, calculated using the discount rate of 7.75%, 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:

	1% Decrease (6.75%)	Current Discount Rate (7.75%)	1% Increase (8.75%)
Net Pension Liability - 12/31/15	\$ 930,178	\$ 750,173	\$ 597,013
Net Pension Liability - 12/31/16	\$ 962,055	\$ 773,084	\$ 612,058

WASHINGTON 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
2008	\$ 25,184	\$ 25,184	\$ -	\$ 197,497	12.8%
2009	31,879	31,879	-	239,604	13.3%
2010	44,144	45,182	(1,038)	252,577	17.9%
2011	44,502	48,132	(3,630)	281,214	17.1%
2012	54,148	54,148	-	301,741	17.9%
2013	53,100	53,100	-	291,665	18.2%
2014	69,709	69,709	-	303,158	23.0%
2015	70,006	70,006	-	299,850	23.3%
2016	113,510	113,510	-	324,296	35.0%
2017	115,678	115,678	-	343,748	33.7%

SCHEDULE OF INVESTMENT RETURNS

Annual Money-Weighted Rate of Return, Net of Investment Expense:

2017	12.36%
2016	4.06%
2015	(2.07%)
2014	4.34%

WASHINGTON 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	\$ 807,551	\$ 1,089,017	\$ 281,466	74.2%
01-01-15	959,572	1,576,122	616,550	60.9%
01-01-17	1,014,362	1,773,456	759,094	57.2%

Note: The market values of the plan’s assets at 01-01-13, 01-01-15, and 01-01-17 have been adjusted to reflect the smoothing of gains and/or losses over a 5-year averaging period which will be 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.

The Actuarial Accrued Liability as of 01-01-17 increased as a result of changes in actuarial assumptions. The value of the interest rate decreased from 7.75% from 01-01-13 to 7.5% as of 01-01-17. There were also changes in mortality assumptions, and a decrease in the normal cost percentage of compensation. In addition during the audit period, there was a plan member who retired in 2017. As a result of these changes, the plan experienced an actuarial loss.

WASHINGTON 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.

WASHINGTON 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	13 years
Asset valuation method	5-year smoothing - the actuarial value of assets will be limited to a maximum of 120% and a minimum of 80% of the fair market value of assets.
Actuarial assumptions:	
Investment rate of return	7.50%
Projected salary increases	5.00%

WASHINGTON TOWNSHIP POLICE PENSION PLAN
REPORT DISTRIBUTION LIST

This report was initially distributed to the following:

The Honorable Tom W. Wolf
Governor
Commonwealth of Pennsylvania

Mr. Robert Smith
Chairman, Board of Township Supervisors

Mr. David Hess
Vice-Chairman, Board of Township Supervisors

Ms. Stacy Diehl
Township Supervisor

Ms. Gail Putvinski
Chief Administrative Officer

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