City of Lancaster
Police Pension Fund

Financial Statements and Required Supplementary Information

Years Ended December 31, 2018 and 2017 with
Independent Auditor's Report

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CITY OF LANCASTER
POLICE PENSION FUND

YEARS ENDED DECEMBER 31, 2018 AND 2017

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Independent Auditor's Report

To the Honorable
Danene Sorace, Mayor and
Members of the Police Pension Fund
City of Lancaster, Pennsylvania

We have audited the accompanying financial statements of the Police Pension Fund of the City of Lancaster as of and for the years ended December 31, 2018 and 2017, and the related notes to the financial statements, as listed in the table of contents.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Police Pension Fund of the City of Lancaster as of December 31, 2018 and 2017, and the changes in financial position thereof for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matters

Required Supplementary Information

Management has omitted the Management's Discussion and Analysis that accounting principles generally accepted in the United States of America require to be presented to supplement the basic financial statements. Such missing information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. Our opinion on the basic financial statements is not affected by this missing information.

Accounting principles generally accepted in the United States of America require that the historical pension plan information on pages 12 through 15 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audits of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Emphasis of Matter

As discussed in Note 1, the financial statements present only the Police Pension Fund and do not purport to, and do not, present fairly the financial position of the City of Lancaster, as of December 31, 2018 and 2017, the changes in its financial position, or, where applicable, its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America. Our opinion is not modified with respect to this matter.

Maher Duessel

Harrisburg, Pennsylvania
August 9, 2019

CITY OF LANCASTER
POLICE PENSION FUND

STATEMENTS OF PLAN NET POSITION

DECEMBER 31, 2018 AND 2017

	2018	2017
Assets		
Investments (at fair value):		
Money market funds	$ 2,814,338	$ 5,120,495
U.S. government obligations	6,835,765	7,313,393
U.S. government agency obligations	32,549	52,559
Corporate bonds	14,981,908	12,019,061
Common stock	39,190,400	45,684,581
Exchange-traded funds	1,493,777	894,882
Accrued interest	241,778	209,629
Total Assets	65,590,515	71,294,600
Net Position		
Restricted for pension benefits	$ 65,590,515	$ 71,294,600

The accompanying notes are an integral part of these financial statements.

CITY OF LANCASTER
POLICE PENSION FUND

STATEMENTS OF CHANGES IN PLAN NET POSITION

YEARS ENDED DECEMBER 31, 2018 AND 2017

	2018	2017
Additions:		
Contributions:		
Employees	$ 617,420	$ 621,225
Employer	3,104,156	2,996,610
Total contributions	3,721,576	3,617,835
Investment income (loss):		
Net appreciation (depreciation) in fair value of investments	(5,331,414)	6,058,474
Interest and dividends	1,824,955	1,791,412
	(3,506,459)	7,849,886
Less: investment expenses	(293,700)	(302,683)
Net investment income (loss)	(3,800,159)	7,547,203
Total additions	(78,583)	11,165,038
Deductions:		
Benefits	5,594,950	5,264,907
Administrative expenses	30,552	4,170
Total deductions	5,625,502	5,269,077
Change in Plan Net Position	(5,704,085)	5,895,961
Net Position:		
Beginning of year	71,294,600	65,398,639
End of year	$ 65,590,515	$ 71,294,600

The accompanying notes are an integral part of these financial statements.

1. Summary of Significant Accounting Policies

General

The Police Pension Fund (Fund) is a single-employer public employee retirement system established and administered by the City of Lancaster, Pennsylvania (City), to provide pension benefits for employees of its Bureau of Police. The Fund is considered part of the City's financial reporting entity and is included in the City's financial reports as a pension trust fund. The accompanying financial statements do not include any other funds of the City and, therefore, do not present fairly the financial position and the changes in financial position of the City in conformity with accounting principles generally accepted in the United States of America.

Basis of Accounting

These financial statements are prepared using the accrual basis of accounting. Police Pension Plan (Plan) member contributions are recognized as revenues in the period in which the contributions are due. Employer contributions are recognized when due and the employer has a formal commitment to provide the contributions. Benefits and refunds are recognized when due and payable in accordance with the terms of the Plan.

Investments

Investments are carried at fair value. The City categorizes its fair value measurements within the fair value hierarchy established by accounting principles generally accepted in the United States of America. The hierarchy is based on the valuation inputs used to measure the fair value of the asset. Level 1 inputs are quoted prices in active markets for identical assets. Level 2 inputs are significant other observable inputs. Level 3 inputs are significant unobservable inputs.

Purchases and sales of securities are recorded on a trade-date basis. Interest income is recorded on the accrual basis. Dividends are recorded on the ex-dividend date.

Net appreciation (depreciation) in fair value of investments includes both realized and unrealized gains and losses.

Use of Estimates

The process of preparing financial statements in conformity with accounting principles generally accepted in the United States of America requires the use of estimates and assumptions regarding certain amounts and disclosures. Accordingly, actual results may differ from estimated amounts.

2. Plan Description and Contribution Information

Plan Participants

Membership of the Plan consisted of the following at December 31, 2018 and 2017:

	2018	2017
Inactive plan members or beneficiaries currently receiving benefits	188	177
Inactive plan members entitled to but not yet receiving benefits	1	1
Active plan members	138	139
	327	317

Plan Description and Administration

The Plan is a single-employer defined benefit pension plan that covers all full-time members of the City's Bureau of Police. The Plan provides retirement, disability, and death benefits to Plan members and their beneficiaries. Plan provisions are established and may be amended through the collective bargaining process. The Plan is governed by the City of Lancaster Police Pension Board (Board) which consists of the Mayor, the City Treasurer, the City Controller, three active police officers to be duly elected by a majority of all active police officers for three-year overlapping terms, and one retired police officer on the pension list to be duly elected by a majority of the retired police officers on the pension list for a two-year term.

Normal Retirement

A participant is eligible for normal retirement after completion of 25 years of service. Retirement is mandatory upon the attainment of age 60. The normal retirement pension is payable monthly during the participant's lifetime, with payments continuing after the participants' death to the surviving spouse, or to dependent children under the age of 18 equal to 100% (75% if hired before January 1, 2003) of the initial amount payable to the participant.

The amount of monthly pension is equal to 50% (pro-rated for service less than 25 years if age 60 mandatory retirement) of the final month's salary plus longevity, plus a service increment of 2.5% of the benefit multiplied by years of service in excess of 20, but not more than $500 additional if hired before January 1, 2011, or $100 if hired on or after January 1, 2011.

Disability Retirement

In the event of occupational disability, the pension is paid regardless of years of service. In the event of non-occupational disability, the pension is prorated for service less than 25 years. Both occupational and non-occupational pensions are based on 50% of actual salary, plus longevity.

Survivor Benefit

A spouse's pension is payable in the event an active member dies after completing five years of service, or in the event an active member dies in the line of duty, regardless of service. The pension of the spouse of an active member killed in the line of duty is equal to 100% of the pension the member would have received had he/she been retired.

The pension of the spouse of a deceased (not in the line of duty) active member is equal to 2.5% of the pension the member would have received had he/she been retired, multiplied by the number of years of service up to 20 years. If a member with at least 20 years of service is deceased not in the line of duty, the spouse shall receive a pension equal to 100% of the monthly pension the member would have received had he/she been retired.

Contributions

Plan members hired on or before January 1, 2011 are required to contribute 5% of lieutenant's pay (or actual pay, if higher) and longevity, plus $5 per month for the service increment. Plan members hired on or after January 1, 2011 contribute 5% of base pay and longevity, plus $1 per month for the service increment. The City is required to make actuarially determined periodic contributions at rates that, for individual employees, increase over time so that sufficient assets will be available to pay benefits when due.

The annual required contribution is determined annually during the budgeting process. The results of actuarial valuations are used in budgeting for future years.

The City made contributions to the Plan of $3,104,156 and $2,996,610 for the years ended December 31, 2018 and 2017, respectively.

Administrative Expenses

Administration costs are financed through investment income.

Net Pension Liability

The components of the net pension liability at December 31, 2018 and 2017 were as follows:

	2018	2017
Total pension liability	$ 97,611,944	$ 93,986,872
Plan fiduciary net position	(65,590,515)	(71,294,600)
Net pension liability	$ 32,021,429	$ 22,692,272
Plan fiduciary net position as a percentage of the total pension liability	67.20%	75.86%

The net pension liability was measured as of December 31, 2018 and 2017 and was determined by rolling forward the liabilities from the January 1, 2017 actuarial valuation. No significant events or changes occurred between the valuation date and the fiscal year-ends.

Actuarial Assumptions – The January 1, 2017 actuarial valuation used the entry age normal actuarial cost method and the IRS 2017 Static Combined Table for Small Plans mortality table. The actuarial assumptions include: a) 8.00% investment rate of return, b) a projected salary increase of 5.00%, c) 3.00% inflation rate, d) level dollar closed amortization method, and e) 11-year remaining amortization period. These assumptions were applied to all periods included in the measurement of total pension liability.

Investment Policy – The Plan's policy in regard to the allocation of invested assets is established and may be amended by the Board. The Board seeks to optimize the total return of the Plan's portfolio through a policy of balanced investments, structured to achieve the maximum returns possible, as measured on the total portfolio, consistent with a policy that emphasizes the prudent management of risk.

Long-Term Expected Rate of Return – The long-term expected rate of return on Plan investments was determined using a building-block method in which best-estimate ranges of expected future real rates of return are developed for each major asset class. These ranges are combined to produce the long-term expected rate of return by weighting the expected future real rates of return by the target asset allocation percentage and by adding expected inflation. The target allocation and best estimates of arithmetic real rates of return for each major asset class as of December 31, 2018 and 2017 are summarized in the following table:

Asset Class	Target Allocation	Long-Term Expected Real Rate of Return
Domestic equity	66.0%	5.5%-7.5%
Fixed income	30.0%	1.0%-3.0%
Cash	4.0%	0.0%-1.0%
	100.0%	

Rate of Return – The money-weighted rate of return expresses investment performance, net of investment expense, adjusted for the changing amounts actually invested. For the years ended December 31, 2018 and 2017, the annual money-weighted rate of return on Plan investments, net of investment expense, were -5.47% and 12.04%, respectively.

Discount Rate – The discount rate used to measure the total pension liability as of December 31, 2018 and 2017 was 8.00%. The Plan’s fiduciary net position is projected to be available to make all projected future benefit payments of current active and inactive employees. Therefore, the long-term expected rate of return on pension plan investments was applied to all periods of projected benefit payments to determine the total pension liability.

Sensitivity of the Net Pension Liability to Changes in the Discount Rate – The following presents the net pension liability of the Plan calculated using the discount rate described above, as well as what the Plan's net pension liability would be if it were calculated using a discount rate that is one-percentage-point lower or higher than the current rates:

December 31, 2018:

1% Decrease (7.00%)	Current Discount Rate (8.00%)	1% Increase (9.00%)
$ 43,815,482	$ 32,021,429	$ 22,143,389

December 31, 2017:

1% Decrease (7.00%)	Current Discount Rate (8.00%)	1% Increase (9.00%)
$ 34,109,814	$ 22,692,272	$ 13,140,392

3. Deposits and Investments

The deposit and investment policy of the Fund is administered by the trustees and the Board. The Fund adheres to state statutes, the Third Class City Code, and prudent business practice.

Investments consist of the following as of December 31:

	2018		
	Level 1	Level 2	Total
Money market funds	$ 2,814,338	$ -	$ 2,814,338
U.S. government obligations	6,835,765	-	6,835,765
U.S. government agency obligations	32,549	-	32,549
Corporate bonds:			
Domestic	-	9,573,959	9,573,959
Foreign	-	5,407,949	5,407,949
Common stock:			
Materials	256,290	-	256,290
Energy	3,521,358	-	3,521,358
Information technology	8,091,875	-	8,091,875
Consumer discretionary	1,958,514	-	1,958,514
Consumer staples	6,505,922	-	6,505,922
Industrials	2,979,165	-	2,979,165
Financials	5,124,075	-	5,124,075
Healthcare	4,904,113	-	4,904,113
Utilities	2,715,026	-	2,715,026
Communication services	3,134,062	-	3,134,062
Exchange-traded funds:			
Equity	1,493,777	-	1,493,777
Total investments	$ 50,366,829	$ 14,981,908	$ 65,348,737

	2017		
	Level 1	Level 2	Total
Money market funds	$ 5,120,495	$ -	$ 5,120,495
U.S. government obligations	7,313,393	-	7,313,393
U.S. government agency obligations	52,559	-	52,559
Corporate bonds:			
Domestic	-	7,778,129	7,778,129
Foreign	-	4,240,932	4,240,932
Common stock:			
Energy	4,456,039	-	4,456,039
Information technology	9,000,844	-	9,000,844
Consumer discretionary	3,494,275	-	3,494,275
Consumer staples	7,167,489	-	7,167,489
Industrials	2,689,038	-	2,689,038
Financials	4,804,881	-	4,804,881
Healthcare	6,425,282	-	6,425,282
Utilities	3,094,998	-	3,094,998
Telecom service	4,551,735	-	4,551,735
Exchange-traded funds:			
Equity	894,882	-	894,882
Total investments	$ 59,065,910	$ 12,019,061	$ 71,084,971

Corporate bonds are valued utilizing several points for price calculation, including quantity, bid/ask spread, historical comparisons, pricing models, and matrices. The valuation techniques used reflect market participants' assumptions and maximize the use of relevant observable inputs including quoted prices for similar assets, the issuer, credit rating, coupon rate, time left until maturity, and special redemption features. Due to the valuation process used, corporate bonds are within Level 2 of the fair value hierarchy.

Custodial Credit Risk. Custodial credit risk is the risk that the financial institution or the counterparty to an investment transaction will fail and the government will not recover the value of the investment or collateral securities that are in possession of an outside party. The Fund does not have an investment policy for custodial credit risk. All of the Fund's investments are uninsured, registered investments for which the securities are held by the broker or dealer, or by its trust department or agent, in the Fund's name.

Concentration of Credit Risk. The Fund places no limit on the amount the Fund may invest in any one issuer. At December 31, 2018, none of the Fund's investments were more than five percent of the Fund's total asset value.

Credit Risk. The Fund does not have a formal policy that would limit its investment choices with regard to credit risk. The Fund's money market funds and fixed income investments had the following level of exposure to credit risk as of December 31, 2018:

	Fair Value	Rating
Money market funds	$ 2,814,338	Unrated
U.S. government agency obligations	32,549	Unrated
Corporate bonds	1,837,677	AAA
Corporate bonds	1,399,166	AA
Corporate bonds	4,283,151	AA-
Corporate bonds	3,403,395	A+
Corporate bonds	856,793	A
Corporate bonds	3,201,726	A-

Interest Rate Risk. The Fund does not have a formal policy that limits investment maturities as a means of managing its exposure to fair value losses arising from increasing interest rates. The average maturity of the Fund's money market funds at December 31, 2018 was less than one year. The average maturities for the Fund's fixed income investments as of December 31, 2018 were as follows:

		Investment Maturity		
	Fair Value	2019	2020-2024	2025-2029
U.S. government obligations	$ 6,835,765	$ 4,503,049	$ 2,332,716	$ -
U.S. government agency obligations	32,549	-	1,423	31,126
Corporate bonds	14,981,908	-	11,940,969	3,040,939
	$ 21,850,222	$ 4,503,049	$ 14,275,108	$ 3,072,065

REQUIRED SUPPLEMENTARY INFORMATION

CITY OF LANCASTER
POLICE PENSION FUND

SCHEDULE OF CHANGES IN PLAN NET PENSION LIABILITY AND RELATED RATIOS

	2018*	2017*	2016*	2015*	2014*
Total Pension Liability:					
Service cost	$ 1,782,287	$ 1,697,416	$ 1,811,305	$ 1,725,052	$ 1,755,477
Interest	7,437,735	7,156,987	6,673,575	6,375,804	6,117,633
Changes for experience	-	1,124,608	-	(613,024)	-
Changes of assumptions	-	1,556,000	-	-	-
Benefit payments, including refunds	(5,594,950)	(5,264,907)	(4,752,979)	(4,176,983)	(3,828,043)
Net Changes in Total Pension Liability	3,625,072	6,270,104	3,731,901	3,310,849	4,045,067
Total Pension Liability - Beginning	93,986,872	87,716,768	83,984,867	80,674,018	76,628,951
Total Pension Liability - Ending (a)	$ 97,611,944	$ 93,986,872	$ 87,716,768	$ 83,984,867	$ 80,674,018
Plan Fiduciary Net Position:					
Contributions - employer	$ 3,104,156	$ 2,996,610	$ 2,814,350	$ 2,748,596	$ 2,439,350
Contributions - employees	617,420	621,225	699,760	636,599	723,981
Net investment income (loss)	(3,800,159)	7,547,203	4,172,859	809,462	5,207,899
Benefit payments, including refunds	(5,594,950)	(5,264,907)	(4,752,979)	(4,176,983)	(3,828,043)
Administrative expenses	(30,552)	(4,170)	(26,100)	(11,344)	(4,540)
Net Change in Plan Fiduciary Net Position	(5,704,085)	5,895,961	2,907,890	6,330	4,538,647
Plan Fiduciary Net Position - Beginning	71,294,600	65,398,639	62,490,749	62,484,419	57,945,772
Plan Fiduciary Net Position - Ending (b)	$ 65,590,515	$ 71,294,600	$ 65,398,639	$ 62,490,749	$ 62,484,419
Net Pension Liability - Ending (a-b)	$ 32,021,429	$ 22,692,272	$ 22,318,129	$ 21,494,118	$ 18,189,599
Plan Fiduciary Net Position as a Percentage of the Total Pension Liability	67.20%	75.86%	74.56%	74.41%	77.45%
Covered Payroll	$ 11,716,931	$ 11,562,299	$ 10,995,284	$ 10,972,837	$ 10,707,385
Net Pension Liability as a Percentage of Covered Payroll	273.29%	196.26%	202.98%	195.88%	169.88%

* This schedule is intended to illustrate information for 10 years. However, until a full 10-year trend is compiled, the City is presenting information for those years only for which information is available.

See accompanying note to required supplementary information - pension plan.

CITY OF LANCASTER
POLICE PENSION FUND

SCHEDULE OF CITY CONTRIBUTIONS AND INVESTMENT RETURNS

Schedule of City Contributions	2018*	2017*	2016*	2015*	2014*	2013	2012	2011	2010	2009
Actuarially determined contribution under Act 205	$ 3,104,156	$ 2,996,610	$ 2,814,350	$ 2,748,596	$ 2,439,350	$ 2,427,282	$ 1,718,841	$ 1,732,970	$ 1,618,199	$ 1,565,272
Contributions in relation to the actuarially determined contribution	3,104,156	2,996,610	2,814,350	2,748,596	2,439,350	2,427,282	1,718,841	1,732,970	2,588,199 (1)	1,565,272
Contribution deficiency (excess)	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ (970,000)	$ -
Covered payroll	$ 11,716,931	$ 11,562,299	$ 10,995,284	$ 10,972,837	$ 10,707,385					
Contributions as a percentage of covered payroll	26.49%	25.92%	25.60%	25.05%	22.78%					

(1) Includes contribution under the City's retirement incentive program.

Investment Returns	2018*	2017*	2016*	2015*	2014*
Annual money-weighted rate of return, net of investment expense	-5.47%	12.04%	7.10%	1.22%	9.29%

* This schedule is intended to illustrate information for 10 years. However, until a full 10-year trend is compiled, the City is presenting information for those years only for which information is available.

See accompanying note to required supplementary information - pension plan.

1. Actuarial Methods and Assumptions

The information presented in the required supplementary information was determined as part of the actuarial valuations at the dates indicated. Methods and assumptions used to determine contribution rates required under Act 205 are as follows:

Contribution Year	12/31/2018	12/31/2017
Actuarial valuation date	1/1/2015	1/1/2015
Actuarial cost method	Entry age normal	Entry age normal
Amortization method	Level dollar closed	Level dollar closed
Remaining amortization period	12 years	12 years
Asset valuation method	Smoothed value with a corridor of 80% to 120% of market value	Smoothed value with a corridor of 80% to 120% of market value
Actuarial assumptions:		
Investment rate of return	8.0%	8.0%
Projected salary increases	5.0%	5.0%
Underlying inflation rate	3.0%	3.0%
Mortality table	RP2000 mortality table	RP2000 mortality table

<u>Changes in Actuarial Assumptions</u>

In the January 1, 2017 actuarial valuation, the mortality table was changed to the IRS 2017 Static Combined Table for Small Plans from the RP2000 Mortality Table and the remaining amortization period was updated from 12 years to 11 years.

In the January 1, 2015 actuarial valuation, the remaining amortization period was updated from 13 years to 12 years.

In the January 1, 2013 actuarial valuation, the asset valuation method was updated from smoothed value with a corridor of 70% to 130% of market value to smoothed value with a corridor of 80% to 120% of market value. The remaining amortization method was also updated from 15 years to 13 years.