

COMPLIANCE AUDIT

Lynn Township Non-Uniformed Employees' Pension Plan Lehigh County, Pennsylvania For the Period January 1, 2013 to December 31, 2016

June 2017



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
Lynn Township
Lehigh County
New Tripoli, PA 18066

We have conducted a compliance audit of the Lynn Township Non-Uniformed Employees' Pension Plan for the period January 1, 2013 to December 31, 2016. 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 findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

The objectives of the audit were:

1. To determine if municipal officials took appropriate corrective action to address the findings contained in our prior audit report; and
2. To determine if the pension plan was administered in compliance with applicable state laws, regulations, contracts, administrative procedures, and local ordinances and policies.

Our audit was limited to the areas related to the objectives identified above. To determine if municipal officials took appropriate corrective action to address the findings 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. State aid allocations that were deposited into the defined contribution plan for the years ended December 31, 2013 to December 31, 2016, are presented on the Summary of Deposited State Aid and Employer Contributions.

- 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. Employer contributions that were deposited into the defined contribution plan for the years ended December 31, 2013 to December 31, 2016, are presented on the Summary of Deposited State Aid and Employer Contributions.
- We determined that there were no employee contributions required by the plan's governing document and applicable laws and regulations for the years covered by our audit period.
- We determined whether retirement benefits calculated for all 7 of the plan members who elected to vest during the current audit period represent payments to all (and only) those 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 and comparing these amounts to supporting documentation evidencing amounts determined.
- We determined whether retirement benefits calculated for the one plan member who terminated employment and elected a lump-sum form of pension benefit 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 comparing the distributed amounts to supporting documentation evidencing amounts determined and actually paid to the recipient.
- We determined whether the January 1, 2011, January 1, 2013 and January 1, 2015 actuarial valuation reports were prepared and submitted to the former Public Employee Retirement Commission (PERC) by March 31, 2012, 2014 and 2016, 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 transfers were properly authorized, timely, and appropriately recorded by plan officials by examining supporting documentation for one of the transfers made during the audit period and through the completion of our fieldwork procedures.

Township officials are responsible for establishing and maintaining effective internal controls to provide reasonable assurance that the Lynn Township Non-Uniformed Employees' 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

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 Lynn Township Non-Uniformed Employees' Pension Plan was administered in compliance with applicable state laws, regulations, contracts, administrative procedures, and local ordinances and policies, except as noted in the following findings further discussed later in this report:

- Finding No. 1 – Partial Compliance With Prior Audit Recommendation – Failure To Pay The Minimum Municipal Obligation Of The Plan
- Finding No. 2 – Restated Plan Document Not Adopted By Ordinance Or Resolution
- Finding No. 3 – 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 Lynn 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.

June 21, 2017



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 Lynn Township Non-Uniformed Employees' 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.

The Lynn Township Non-Uniformed Employees' Pension Plan has a single-employer defined benefit pension plan component locally controlled by the provisions of Resolution No. 2003-11. On June 9, 2011, the township adopted Resolution No. 2011-15 to freeze the defined benefit plan and provide a defined contribution plan for the township's non-uniformed employees. The municipality is required to contribute 6 percent of each members' compensation to the defined contribution plan. The defined contribution component was established July 1, 2011. Active members are not required to contribute to the plan. As of December 31, 2016, the plan had 6 active members, 15 terminated members eligible for vested benefits in the future, 5 retirees receiving pension benefits from the plan and 1 retiree receiving benefits funded through an annuity purchased with plan assets.

BACKGROUND – (Continued)

As of December 31, 2016, selected defined benefit plan benefit provisions are as follows:

Eligibility Requirements:

Normal Retirement	Age 65
Early Retirement	Age 60 with 6 years of service.
Vesting	Vesting schedule is 20% per year of service to 100%.

Retirement Benefit:

Benefit equals \$35 per month multiplied by years of benefit service.

Survivor Benefit:

Before Retirement Eligibility	Benefit equals 100% of the vested benefit payable at Normal Retirement Date.
After Retirement Eligibility	Subject to the provisions of the form of payment elected by the participant.

LYNN TOWNSHIP NON-UNIFORMED EMPLOYEES' PENSION PLAN
STATUS OF PRIOR FINDINGS

Compliance With Prior Audit Recommendation

Lynn Township has complied with the prior audit recommendation concerning the following:

- Unauthorized Deposit Of State Aid

During the current audit period, the township opened an eligible defined contribution plan and transferred \$37,838 from the ineligible Section 457 plan to the eligible defined contribution plan. In addition, the township paid the outstanding 2012 defined benefit minimum municipal obligation (MMO) on September 17, 2013.

Partial Compliance With Prior Audit Recommendation

Lynn Township has partially complied with the prior audit recommendation concerning the following:

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

During the current audit period, the township paid the outstanding 2012 MMO due to the defined benefit pension plan; however, the township failed to pay a portion of the 2014 MMO, along with the entire 2015 and 2016 MMO's to the defined contribution pension plan, as further discussed in the Findings and Recommendations section of this report.

LYNN TOWNSHIP NON-UNIFORMED EMPLOYEES' PENSION PLAN
FINDINGS AND RECOMMENDATIONS

**Finding No. 1 – Partial Compliance With Prior Audit Recommendation – Failure To Pay
The Minimum Municipal Obligation Of The Plan**

Condition: During the current audit period, the township paid the outstanding 2012 MMO due to the defined benefit plan; however, the township did not pay a portion of the 2014 MMO, or the entire 2015 and 2016 MMOs due to the defined contribution pension plan.

Criteria: With regard to the MMO, Section 303(c) of Act 205 states, in part:

Annually, the chief administrative officer of the pension plan shall determine the minimum obligation of the municipality with respect to the pension plan for the following plan year.

Section 303(d) of Act 205 states, in part:

The minimum obligation of the municipality shall be payable to the pension plan from the revenue of the municipality.

Furthermore, Section 303(e) of Act 205 states:

Any amount of the minimum obligation of the municipality which remains unpaid as of December 31 of the year in which the minimum obligation is due shall be added to the minimum obligation of the municipality for the following year, with interest from January 1 of the year in which the minimum obligation was first due until the date the payment is paid at a rate equal to the interest assumption used for the actuarial valuation report or the discount rate applicable to treasury bills issued by the Department of Treasury of the United States with a six-month maturity as of the last business day in December of the plan year in which the obligation was due, whichever is greater, expressed as a monthly rate and compounded monthly.

Cause: Plan officials deposited the defined contribution minimum municipal obligation to the defined benefit plan account.

Effect: The failure to pay the MMO could result in the plan not having adequate resources to meet current and future benefit obligations to its members.

Due to the municipality's failure to pay the outstanding MMOs due to the defined contribution plan, the municipality must add the remaining 2014 MMO balance, along with the 2015 and 2016 MMO's to the current year's MMO and include interest, as required by Act 205.

LYNN TOWNSHIP NON-UNIFORMED EMPLOYEES' PENSION PLAN
FINDINGS AND RECOMMENDATIONS

Finding No. 1 – (Continued)

Recommendation: We recommend that the municipality pay the MMO due to the defined contribution pension plan for the years 2014, 2015 and 2016, with interest, in accordance with Section 303(e) of Act 205. Municipal officials should consult with the township's solicitor to determine if the required contributions can be made through a transfer of funds from the defined benefit plan. A copy of the interest calculation must be maintained by the township for examination during our next audit of the plan.

Furthermore, we recommend that municipal officials establish adequate internal control procedures to ensure future MMOs are paid timely in accordance with Act 205 requirements.

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.

Finding No. 2 – Restated Plan Document Not Adopted By Ordinance Or Resolution

Condition: The defined contribution plan is currently controlled by the provisions of Resolution 2011-15. The terms, provisions and conditions of the defined contribution pension plan were restated in a separately executed plan document with Northwest Retirement Services effective April 1, 2016. However, Resolution No. 2011-15 has not been amended to reflect the provisions of the updated plan agreement.

Criteria: Sound internal control procedures dictate that benefit provisions should be consistent within the plan documents to avoid the payment of improper or inconsistent benefits for plan members and their beneficiaries.

Cause: Municipal officials failed to adopt adequate internal control procedures to ensure compliance with the prior audit verbal observation.

Effect: The failure to properly adopt the plan agreement could result in improper or inconsistent benefit payments to plan members and their beneficiaries.

Recommendation: We recommend that municipal officials take appropriate action to formally adopt the restated plan document through a properly executed ordinance or resolution.

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.

LYNN TOWNSHIP NON-UNIFORMED EMPLOYEES' PENSION PLAN
FINDINGS AND RECOMMENDATIONS

Finding No. 3 – Failure To Deposit The Full Amount Of State Aid Into The Pension Plan

Condition: The township did not deposit the full amount of its 2013 state aid allocation into the defined benefit pension plan. The township received its 2013 state aid allocation in the amount of \$27,191 on September 25, 2013; however only \$26,494 was deposited into the defined benefit 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 be deposited in the pension funds or the alternate funding mechanisms applicable to the respective pension plans.

Cause: Municipal officials failed to establish adequate internal control procedures to ensure the full amount of the 2013 state aid allocation was deposited timely.

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 the municipality deposit the township's remaining 2013 state aid allocation of \$697, plus interest earned during the period beyond the 30 day grace period allowed by Act 205, compounded annually into the defined benefit pension plan account. A copy of the interest calculation must be maintained by the township for examination during our next audit of the plan.

We also recommend that plan officials establish adequate internal control procedures to ensure that future state aid allocations are deposited timely in accordance with Act 205 requirements.

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.

LYNN TOWNSHIP NON-UNIFORMED EMPLOYEES' PENSION PLAN
 SUPPLEMENTARY INFORMATION
 DEFINED BENEFIT PLAN
 (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, 2011, 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)
01-01-11	\$ 347,165	\$ 446,683	\$ 99,518	77.7%
01-01-13	373,770	453,047	79,277	82.5%
01-01-15	415,228	472,973	57,745	87.8%

Note: The market value of the plan's assets at 01-01-13 has been adjusted to reflect the smoothing of gains and/or losses. 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.

LYNN TOWNSHIP NON-UNIFORMED EMPLOYEES' PENSION PLAN
SUPPLEMENTARY INFORMATION
DEFINED BENEFIT PLAN
(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.

LYNN TOWNSHIP NON-UNIFORMED EMPLOYEES' PENSION PLAN
 SUPPLEMENTARY INFORMATION
 DEFINED BENEFIT PLAN
 (UNAUDITED)

SCHEDULE OF CONTRIBUTIONS FROM EMPLOYER
 AND OTHER CONTRIBUTING ENTITIES

Year Ended December 31	Annual Required Contribution	Percentage Contributed
2011	\$ 27,293	100.0%
2012	14,485	100.0%
2013	14,485	100.0%
2014	14,485	102.3%
2015	12,219	100.0%
2016	12,219	100.0%

LYNN TOWNSHIP NON-UNIFORMED EMPLOYEES' PENSION PLAN
SUPPLEMENTARY INFORMATION
NOTES TO SUPPLEMENTARY SCHEDULES
DEFINED BENEFIT PLAN
(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, 2015
Actuarial cost method	Entry age normal
Amortization method	Level dollar
Remaining amortization period	10 years
Asset valuation method	Fair value
Actuarial assumptions:	
Investment rate of return	6.0%
Projected salary increases	None

LYNN TOWNSHIP NON-UNIFORMED EMPLOYEES' PENSION PLAN
SUMMARY OF DEPOSITED STATE AID AND EMPLOYER CONTRIBUTIONS
DEFINED CONTRIBUTION PLAN

Year Ended December 31	State Aid	Employer Contributions
2013	\$ 12,009	\$ None
2014	11,017	4,358
2015	11,306	4,724
2016	14,029	1,394

The employer contribution for 2014 and the total contributions allocated to the defined contribution plan were erroneously deposited into the defined benefit account, see Finding No. 1.

LYNN TOWNSHIP NON-UNIFORMED EMPLOYEES' PENSION PLAN
REPORT DISTRIBUTION LIST

This report was initially distributed to the following:

The Honorable Tom W. Wolf
Governor
Commonwealth of Pennsylvania

Mr. Justin N. Smith
Chairman, Board of Township Supervisors

Mr. Steve I. Feinour
Vice Chairman, Board of Township Supervisors

Mr. Brian C. Dietrich
Township Supervisor

Ms. Tammy M. White
Chief Administrative Officer

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