

# COMPLIANCE AUDIT

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## Hanover Township Non-Uniformed Pension Plan Northampton County, Pennsylvania For the Period January 1, 2015 to December 31, 2016

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February 2018



Commonwealth of Pennsylvania  
Department of the Auditor General

Eugene A. DePasquale • Auditor General



Commonwealth of Pennsylvania  
Department of the Auditor General  
Harrisburg, PA 17120-0018  
Facebook: Pennsylvania Auditor General  
Twitter: @PAAuditorGen  
www.PaAuditor.gov

EUGENE A. DePASQUALE  
AUDITOR GENERAL

Board of Township Supervisors  
Hanover Township  
Northampton County  
Bethlehem, PA 18017

We have conducted a compliance audit of the Hanover Township Non-Uniformed Pension Plan for the period January 1, 2015 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 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 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 the plan member 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 to retired individuals and comparing these amounts to supporting documentation evidencing amounts determined.
- We determined whether the January 1, 2013 , January 1, 2015, and January 1, 2017, actuarial valuation reports were prepared and submitted to the former Public Employee Retirement Commission (PERC) 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.

Hanover 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 Hanover Township Non-Uniformed 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 Hanover Township Non-Uniformed 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 – Partial Compliance With Prior Audit Recommendation – Incorrect Data On Certification Form AG 385 Resulting In A Net 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 Hanover 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.

February 5, 2018



EUGENE A. DEPASQUALE  
Auditor General

## CONTENTS

	<u>Page</u>
Background.....	1
Status of Prior Finding.....	3
Finding and Recommendation:	
Finding – Partial Compliance With Prior Audit Recommendation – Incorrect Data On Certification Form AG 385 Resulting In A Net Overpayment Of State Aid.....	4
Supplementary Information .....	6
Report Distribution List .....	11

## **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 Hanover Township Non-Uniformed 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 Hanover Township Non-Uniformed Pension Plan is a single-employer defined benefit pension plan locally controlled by the provisions of Resolution No. 96-20, as amended. The plan was established October 26, 1970. Active members are not required to contribute to the plan. As of December 31, 2016, the plan had 12 active members, 2 terminated members eligible for vested benefits in the future, and 9 retirees receiving pension benefits from the plan.

## **BACKGROUND – (Continued)**

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

### Eligibility Requirements:

Normal Retirement	Age 62 and 7 years of service
Early Retirement	Age 55 and 10 years of service
Vesting	Member is 100% vested after 10 years of service

### Retirement Benefit:

Benefit equals 3.0% of compensation for each year of credited service through December 31, 2000 plus 2.25% of compensation for each year of credited service after December 31, 2000. Compensation is averaged over 3 highest consecutive of the 5-year period immediately preceding retirement. Minimum benefit is \$30 per month. Maximum benefit for employees hired after August 1, 2001 is 75% of average monthly compensation.

### Survivor Benefit:

Before Retirement Eligibility	Present value of member's accrued benefit or a qualified 50% survivor benefit.
After Retirement Eligibility	Subject to the provisions of the form of payment elected by the participant.

### Disability Benefit:

Actuarial equivalent of the normal retirement benefit earned to the date of disability.

HANOVER TOWNSHIP NON-UNIFORMED PENSION PLAN  
STATUS OF PRIOR FINDING

Partial Compliance With Prior Audit Recommendation

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

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

During the current audit period, the township reimbursed \$11,982 to the Commonwealth for the overpayment of state aid in 2014; however, plan officials again failed to comply with the instructions that accompany Certification Form AG 385 to assist them in accurately reporting the required pension data in the years 2015 and 2016 as further discussed in the Finding and Recommendation section of this report.

HANOVER TOWNSHIP NON-UNIFORMED PENSION PLAN  
FINDING AND RECOMMENDATION

**Finding – Partial Compliance With Prior Audit Recommendation – Incorrect Data On Certification Form AG 385 Resulting In A Net Overpayment Of State Aid**

Condition: As disclosed in the Status of Prior Finding section of this report, the township partially complied with our prior audit recommendation by reimbursing the Commonwealth for the overpayment of state aid in 2014; however, a similar condition occurred during the current audit period. Plan officials again failed to comply with the instructions that accompanied Certification Form AG 385 to assist them in accurately reporting the required pension data in the years 2015 and 2016. The township certified 2 ineligible non-uniformed employees (2 units) and overstated payroll by \$46,268 on the Certification Form AG 385 filed in 2015. In addition, the township failed to certify 1 eligible non-uniformed employees (1 unit) and understated payroll by \$54,022 on the Certification Form AG 385 filed in 2016. 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.

Cause: Plan officials again failed to establish adequate internal control procedures to ensure the accuracy of the data certified and ensure compliance with this department's prior audit recommendation.

Effect: The data submitted on this certification form is used, in part, to calculate the state aid due to the municipality for distribution to its pension plan. Because Hanover Township participates in a regional police pension plan, the township's state aid allocation for its non-uniformed pension plan is separately calculated by the Department of the Auditor General Comptroller's Office using an alternate method, taking into account the municipality's pension costs and unit value as well as the municipality's percentage of the regional police pension plan's pension costs and unit value. The township's state aid allocation for 2015 was \$90,179, which was based on the plans' unit values. Based on the corrected information, the township was entitled to an allocation of \$82,341, based on the plans' adjusted pension costs. Therefore, the township received a \$7,838 overpayment of state aid in 2015. Additionally, the township's state aid allocation for 2016 was \$96,242, which was based on the plans' unit values. Based on the corrected information, the township was entitled to an allocation of \$100,625, based on the plans' adjusted pension costs. Therefore, the township received a \$4,383 underpayment payment of state aid in 2016. The total net effect resulted in a \$3,455 overpayment of state aid.

HANOVER TOWNSHIP NON-UNIFORMED PENSION PLAN  
FINDING AND RECOMMENDATION

**Finding – (Continued)**

Recommendation: We recommend that the net overpayment of state aid, in the amount of \$3,455, plus interest, 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 again recommend that in the future, plan officials establish adequate internal control procedures, such as having at least 2 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: We are concerned that the municipality has not fully complied with the prior audit recommendation and encourage compliance at the earliest opportunity to do so. Compliance will be evaluated during our next audit of the plan.

HANOVER TOWNSHIP NON-UNIFORMED PENSION PLAN  
 SUPPLEMENTARY INFORMATION  
 (UNAUDITED)

The supplementary information contained on Pages 6 and 7 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 YEAR ENDED DECEMBER 31, 2015

	<u>2015</u>
Total Pension Liability	
Service cost	\$ 169,211
Interest	619,136
Benefit payments, including refunds of member contributions	(327,251)
Net Change in Total Pension Liability	461,096
Total Pension Liability – Beginning	8,249,559
Total Pension Liability - Ending (a)	\$ 8,710,655
Plan Fiduciary Net Position	
Contributions – employer	\$ 361,911
Contribution – state aid	90,179
Net investment income	(26,828)
Benefit payments, including refunds of member contributions	(327,251)
Net Change in Plan Fiduciary Net Position	98,011
Plan Fiduciary Net Position – Beginning	7,064,823
Plan Fiduciary Net Position - Ending (b)	\$ 7,162,834
Net Pension Liability - Ending (a-b)	\$ 1,547,821
Plan Fiduciary Net Position as a Percentage of the Total Pension Liability	82.2%
Estimated Covered Employee Payroll	\$ 817,520
Net Pension Liability as a Percentage of Covered Employee Payroll	189.3%

HANOVER TOWNSHIP NON-UNIFORMED 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, 2015, calculated using the discount rate of 7.5%, 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 (6.5%)	Current Discount Rate (7.5%)	1% Increase (8.5%)
Net Pension Liability	\$ 2,656,041	\$ 1,547,821	\$ 613,288

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
2006	\$ 225,535	\$ 302,748	\$ (77,213)	\$ 813,428	37.2%
2007	247,936	321,683	(73,747)	990,970	32.5%
2008	329,188	399,287	(70,099)	972,166	41.1%
2009	330,304	411,632	(81,328)	977,776	42.1%
2010	371,166	468,199	(97,033)	925,212	50.6%
2011	372,083	550,942	(178,859)	930,094	59.2%
2012	402,318	495,279	(92,961)	949,440	52.2%
2013	396,668	510,981	(114,313)	921,701	55.4%
2014	369,164	497,802	(128,638)	904,873	55.0%
2015	336,288	452,090	(115,802)	817,520	55.3%
2016	323,358	419,600	(96,242)	*	*

\* Due to the timing of this audit, covered-employee payroll for 2016 was not provided in this schedule.

HANOVER TOWNSHIP NON-UNIFORMED 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	\$ 6,084,725	\$ 7,312,291	\$ 1,227,566	83.2%
01-01-15	7,385,183	8,249,559	864,376	89.5%
01-01-17	8,233,167	8,732,576	499,409	94.3%

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. 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.

HANOVER TOWNSHIP NON-UNIFORMED 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.

HANOVER TOWNSHIP NON-UNIFORMED 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	5 years
Asset valuation method	Fair value, 5-year smoothing
Actuarial assumptions:	
Investment rate of return	7.5%
Projected salary increases	5.0%
Cost-of-living adjustments	3.0%

HANOVER TOWNSHIP NON-UNIFORMED PENSION PLAN  
REPORT DISTRIBUTION LIST

This report was initially distributed to the following:

**The Honorable Tom W. Wolf**  
Governor  
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**Mr. John N. Diacogiannis**  
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**Mr. Stephen R. Salvesen**  
Township Supervisor

**Mr. John J. Finnigan, Jr.**  
Township Manager

**Ms. Beth A. Bucko**  
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