

COMPLIANCE AUDIT

North Catasauqua Borough Police Pension Plan Northampton County, Pennsylvania For the Period January 1, 2018 to December 31, 2021

December 2022



Commonwealth of Pennsylvania
Department of the Auditor General

Timothy L. DeFoor • Auditor General



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**TIMOTHY L. DEFOOR
AUDITOR GENERAL**

The Honorable Mayor and Borough Council
North Catasauqua Borough
Northampton County
North Catasauqua, PA 18032

We have conducted a compliance audit of the North Catasauqua Borough Police Pension Plan for the period January 1, 2018 to December 31, 2021. We also evaluated compliance with some requirements subsequent to that period when possible. The audit was conducted pursuant to authority derived from the Municipal Pension Plan Funding Standard and Recovery Act (Act 205 of 1984, as amended, 53 P.S. § 895.402(j)), which requires the Auditor General, as deemed necessary, to audit every municipality which receives general municipal pension system state aid and every municipal pension plan and fund in which general municipal pension system state aid is deposited. The audit was not conducted, nor was it required to be, in accordance with Government Auditing Standards issued by the Comptroller General of the United States. We planned and performed the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our finding and conclusions based on our audit objective. We believe that the evidence obtained provides a reasonable basis for our finding and 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 that there were no employee contributions required for the years covered by our audit period due to the fact that employee contributions were appropriately waived by the municipality.
- We determined whether retirement benefits calculated for plan members who retired and 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 and disbursed in accordance with the plan's governing document, applicable laws, and regulations by recalculating the amount of the monthly pension benefits due to the retired individuals and comparing these amounts to supporting documentation evidencing amounts determined and actually paid or payable to the recipients.
- We determined whether the January 1, 2017, January 1, 2019, and January 1, 2021 actuarial valuation reports were prepared and submitted by March 31, 2018, 2020, and 2022, 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.
- We determined whether the terms of the plan's allocated 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.

North Catasauqua Borough contracted with an independent certified public accounting firm for annual audits of its financial statements prepared in conformity with the accounting practices prescribed or permitted by the Department of Community and Economic Development of the Commonwealth of Pennsylvania, which are available at the borough's offices. Those financial statements were not audited by us and, accordingly, we express no opinion or other form of assurance on them.

The borough has also elected to purchase allocated insurance contracts to fund a portion of the benefits provided by the pension plan at retirement. Under an allocated funding arrangement, the insurer receives and retains consideration in exchange for a legally enforceable obligation to pay future benefits. In accordance with Statement No. 67 of the Governmental Accounting Standards Board, allocated insurance contracts are excluded from the pension plan's assets.

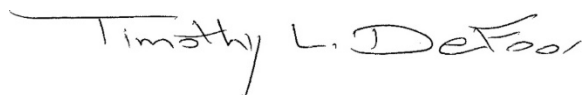
Borough officials are responsible for establishing and maintaining effective internal controls to provide reasonable assurance that the North Catasauqua Borough Police Pension Plan is administered in compliance with applicable state laws, regulations, contracts, administrative procedures, and local ordinances and policies. As previously described, we tested transactions, interviewed selected officials, and performed procedures to the extent necessary 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 North Catasauqua Borough 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 findings further discussed later in this report:

- Finding No. 1 – Incorrect Data On Certification Form AG 385 Resulting In An Overpayment Of State Aid
- Finding No. 2 – Failure To Implement Mandatory Act 44 Procedures For The Procurement Of Professional Services

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 North Catasauqua Borough and, where appropriate, their responses have been included in the report. We would like to thank borough officials for the cooperation extended to us during the conduct of the audit.



Timothy L. DeFoor
Auditor General
November 4, 2022

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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.

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 North Catasauqua Borough Police Pension Plan is also governed by implementing regulations 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 North Catasauqua Borough Police Pension Plan is a single-employer defined benefit pension plan locally controlled by the provisions of Ordinance No. 374, as amended, adopted pursuant to Act 600. The plan is also affected by the provisions of collective bargaining agreements between the borough and its police officers. The plan was established December 11, 1978. Active members are required to contribute five (5.0) percent of compensation to the plan; however, member contributions were waived during the audit period. As of December 31, 2021, the plan had five active members, one terminated member eligible for vested benefits in the future, and three retirees receiving pension benefits.

NORTH CATASAUQUA BOROUGH POLICE PENSION PLAN
FINDINGS AND RECOMMENDATIONS

Finding No. 1 – Incorrect Data On Certification Form AG 385 Resulting In An Overpayment Of State Aid

Condition: The borough certified an ineligible police officer (2 units) and overstated payroll by \$51,920 and \$43,886 on the Certification Forms AG 385 filed in 2020 and 2021. 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 failed to establish adequate internal control procedures, such as having another individual review the data certified, to ensure the accuracy of the required pension data.

Effect: The data submitted on these certification forms is used, in part, to calculate the state aid due to the municipality for distribution to its pension plans. Because the borough’s state aid allocations were based on unit value, the incorrect certification of pension data affected the borough’s state aid allocations, as identified below:

<u>Year</u>	<u>Units Overstated</u>	<u>Unit Value</u>	<u>State Aid Overpayment</u>
2020	2	\$ 4,924	\$ 9,848
2021	2	4,797	<u>9,594</u>
Total Overpayment of State Aid			<u>\$ 19,442</u>

In addition, the borough used the overpayments of state aid to pay the minimum municipal obligations (MMOs) due to the police pension plan; therefore, if the reimbursement to the Commonwealth is made from the pension plan, the plan’s MMOs will not be fully paid.

Furthermore, the borough’s future state aid allocations may be withheld until the finding recommendation is complied with.

NORTH CATASAUQUA BOROUGH POLICE PENSION PLAN
FINDINGS AND RECOMMENDATIONS

Finding No. 1 – (Continued)

Recommendation: We recommend that the total excess state aid, in the amount of \$19,442, 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 recommend that in the future, plan officials establish adequate internal control procedures, such as having at least two 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.

In addition, if the reimbursement to the Commonwealth is made from police pension plan funds, we recommend that any resulting MMO deficiencies be paid to the pension plan with interest, at a rate earned by the pension plan.

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 – Failure To Implement Mandatory Act 44 Procedures For The Procurement Of Professional Services

Condition: As disclosed to the borough during the prior engagement, municipal officials failed to adopt the mandatory provisions of Act 205 regarding professional services contracts.

Criteria: Section 701-A of Act 205, as amended by Act 44 of 2009, defines a “Professional Services Contract”, as follows:

“Professional services contract.” A contract to which the municipal pension system is a party that is:

- (1) for the purchase or provision of professional services, including investment services, legal services, real estate services and other consulting services; and
- (2) not subject to a requirement that the lowest bid be accepted.

NORTH CATASAUQUA BOROUGH POLICE PENSION PLAN
FINDINGS AND RECOMMENDATIONS

Finding No. 2 – (Continued)

In addition, Section 702-A (a) of Act 205 states in part:

Each municipal pension system ... shall develop procedures to select the most qualified person to enter into a professional services contract. The procedures shall ensure that the availability of a professional services contract is advertised to potential participants in a timely and efficient manner. Procedures shall include applications and disclosure forms to be used to submit a proposal for review and to receive the award of a professional services contract.

Additionally, Section 702-A (c), (e), (f) and (h) state, in part:

Review. Procedures to select the most qualified person shall include a review of the person's qualifications, experience and expertise and the compensation to be charged.

Conflict of interest. The municipal pension system shall adopt policies relating to potential conflicts of interest in the review of a proposal or the negotiation of a contract.

Public information. Following the award of a professional services contract, all applications and disclosure forms shall be public except for proprietary information or other information protected by law.

Notice and summary. The relevant factors that resulted in the award of the professional services contract must be summarized in a written statement to be included in or attached to the documents awarding the contract. Within ten days of the award of the professional services contract, the original application, a summary of the basis for the award and all required disclosure forms must be transmitted to all unsuccessful applications and posted on the municipal pension system's Internet website, if an Internet website is maintained, at least seven days prior to the execution of the professional services contract.

Cause: Plan officials failed to establish adequate internal controls procedures to ensure compliance with provisions of Act 205 as previously recommended.

NORTH CATASAUQUA BOROUGH POLICE PENSION PLAN
FINDINGS AND RECOMMENDATIONS

Finding No. 2 – (Continued)

Effect: The borough's failure to comply in all respects with the previous recommendation and the provisions stipulated in Act 205 regarding the procurement of professional investment and advisory services for the borough's pension plan could result in a general lack of overall transparency of the actions taken by plan officials relative to the awarding of the investment and advisory services contract for the borough's pension plan.

Recommendation: We recommend that municipal officials obtain a comprehensive understanding of Act 205 provisions for the procurement of professional services and develop and implement formal written procedures to ensure compliance with these provisions which includes maintaining appropriate and sufficient supporting documentation evidencing every phase of the process in the awarding of future professional services contracts for the pension plan, including authorizations/approvals of borough officials in the official minutes of formal board meetings and the required notifications and disclosure responsibilities to ensure the transparency of the actions taken by plan officials relative to the awarding of such professional services contracts.

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

Auditor's Conclusion: Compliance will be evaluated during our next engagement of the plan.

NORTH CATASAUQUA BOROUGH POLICE PENSION PLAN
POTENTIAL WITHHOLD OF STATE AID

Finding No. 1 contained in this audit report cites an overpayment of state aid to the borough in the amount of \$19,442, plus interest. A condition of this nature may lead to a total withholding of state aid in the future unless that finding is corrected. A check in this amount with interest, 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.

NORTH CATASAUQUA BOROUGH 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, 2015, 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)
01-01-17	\$ 1,511,812	\$ 1,398,778	\$ (113,034)	108.1%
01-01-19	1,613,574	1,509,168	(104,406)	107.1%
01-01-21	1,650,754	1,516,342	(134,412)	108.9%

The amounts in the above table (*for 01-01-2017 and 01-01-2019 valuations*) have been adjusted, as appropriate, for an insurance contract maintained preretirement to fund a portion of the benefits provided by the pension plan at retirement. This insurance contract was surrendered, and the proceeds were deposited into the pension plan on October 1, 2019.

NORTH CATASAUQUA BOROUGH 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.

NORTH CATASAUQUA BOROUGH POLICE PENSION PLAN
SUPPLEMENTARY INFORMATION
(UNAUDITED)

SCHEDULE OF CONTRIBUTIONS FROM EMPLOYER
AND OTHER CONTRIBUTING ENTITIES

Year Ended December 31	Annual Required Contribution	Percentage Contributed
2016	\$ 17,930	100.0%
2017	21,936	100.0%
2018	22,468	117.2%
2019	24,848	100.0%
2020	46,367	100.0%
2021	49,871	100.0%

NORTH CATASAUQUA BOROUGH 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, 2021
Actuarial cost method	Entry age normal
Amortization method	N/A
Remaining amortization period	N/A
Asset valuation method	Fair value
Actuarial assumptions:	
Investment rate of return	6.00%
Projected salary increases	5.00%

NORTH CATASAUQUA BOROUGH POLICE PENSION PLAN
REPORT DISTRIBUTION LIST

This report was initially distributed to the following:

The Honorable Tom W. Wolf
Governor
Commonwealth of Pennsylvania

The Honorable William J. Molchany, Jr.
Mayor

Mr. Peter Paone
Council President

Ms. Michelle Hazzard
Chief Administrative Officer

Ms. Annette Englert
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