

CITY OF BETHLEHEM AGGREGATE PENSION FUND

NORTHAMPTON COUNTY

COMPLIANCE AUDIT REPORT

FOR THE PERIOD

JANUARY 1, 2010, TO DECEMBER 31, 2011



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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.

Pension plan aid is provided from a 2 percent foreign casualty insurance premium tax, a portion of the foreign 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 City of Bethlehem Aggregate Pension Fund is also governed by implementing regulations adopted by the 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 147 - Special Ad Hoc Municipal Police and Firefighter Postretirement Adjustment Act, Act of December 14, 1988 (P.L. 1192, No. 147), as amended, 53 P.S. § 896.101 et seq.

- Act 399 - Optional Third Class City Charter Law, Act of July 15, 1957 (P.L. 901, No. 399), as amended, 53 P.S. § 41101 et seq.

The City of Bethlehem Aggregate Pension Fund serves as a common investment and administrative agent for the city's police, officers' and employees' and paid firemen's pension plans. The plans are single-employer defined benefit pension plans locally controlled by the provisions of the City's Codified Ordinances, at Articles 153, 155 and 151, respectively. The plans are also affected by the provisions of collective bargaining agreements between the city and its police officers, nonuniformed employees hired on or prior to August 1, 1978, and firefighters.



The Honorable Mayor and City Council
City of Bethlehem
Northampton County
Bethlehem, PA 18018

We have conducted a compliance audit of the City of Bethlehem Aggregate Pension Fund for the period January 1, 2010, to December 31, 2011. 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. Our methodology addressed determinations about the following:

- Whether state aid was properly determined and deposited in accordance with Act 205 requirements.
- Whether employer contributions are determined and deposited in accordance with the plan's governing document and applicable laws and regulations.
- Whether employee contributions are required and, if so, are determined, deducted and deposited into the pension plan and are in accordance with the plan provisions and applicable laws and regulations.

- Whether benefit payments, if any, represent payments to all (and only) those entitled to receive them and are properly determined in accordance with applicable laws and regulations.
- Whether obligations for plan benefits are accurately determined in accordance with plan provisions and based on complete and accurate participant data; and whether actuarial valuation reports are prepared and submitted to the Public Employee Retirement Commission (PERC) in accordance with state law and 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.
- Whether the special ad hoc postretirement adjustment granted to eligible pensioners is in accordance with applicable laws and regulations and whether the ad hoc reimbursement received by the municipality was treated in accordance with applicable laws and regulations.
- Whether benefit payments have only been made to living recipients, based on the Social Security numbers found in the pension records for retirees and beneficiaries.
- Whether the pension plan is in compliance with state regulations for distressed municipalities.
- Whether the terms and methodologies of the issuance of bonds by the municipality, and any restrictions, are in compliance with plan provisions and state regulations.
- Whether Deferred Retirement Option Plan (DROP) participants' benefit payments are properly determined in accordance with the provisions of the DROP and any other applicable laws and regulations.

The City of Bethlehem contracted with an independent certified public accounting firm for annual audits of its basic financial statements which are available at the city's offices. Those financial statements were not audited by us and, accordingly, we express no opinion or other form of assurance on them.

City officials are responsible for establishing and maintaining effective internal controls to provide reasonable assurance that the City of Bethlehem Aggregate Pension Fund 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 city's internal controls as they relate to the city'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, 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 tests indicated that, in all significant respects, the City of Bethlehem Aggregate Pension Fund 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:

Firemen's Pension Plan

Finding No. 1 – Restated Plan Document Not Adopted By Ordinance

Police Pension Plan

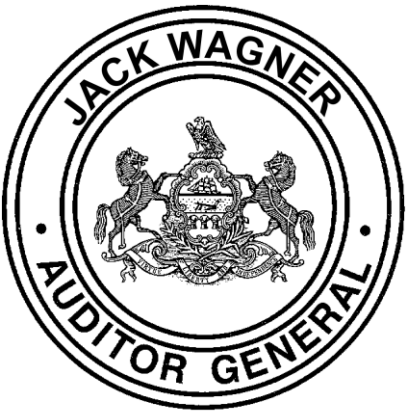
Finding No. 2 – Restated Plan Document Not Adopted By Ordinance

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 the City of Bethlehem and, where appropriate, their responses have been included in the report.

October 31, 2012

JACK WAGNER
Auditor General



CITY OF BETHLEHEM AGGREGATE PENSION FUND
STATUS OF PRIOR FINDINGS

Compliance With Prior Audit Recommendations

The City of Bethlehem has complied with the prior audit recommendations concerning the following:

Firemen's Pension Plan

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

During the current audit period, the city reimbursed \$6,474 to the Commonwealth for the overpayment of state aid received in 2009;

- Incorrect Data Supplied To Actuary For Actuarial Valuation Report Preparation

The city executed a restated pension plan document on March 26, 2009, which included the non-service related disability benefit provision reported by the plan's actuary; however, this restated plan document was not adopted by ordinance as further discussed in the Findings and Recommendations section of this report;

- Inconsistent Pension Benefit

The city executed a restated pension plan document on March 26, 2009, which included the deferred retirement option plan (DROP) benefit reported by the plan's actuary; however, this restated plan document was not adopted by ordinance as further discussed in the Findings and Recommendations section of this report; and

Police Pension Plan

- Incorrect Data Supplied To Actuary For Actuarial Valuation Report Preparation

The city executed a restated pension plan document on March 26, 2009, which included the service increment benefit reported by the plan's actuary; however, this restated plan document was not adopted by ordinance as further discussed in the Findings and Recommendations section of this report.

CITY OF BETHLEHEM AGGREGATE PENSION FUND
FINDINGS AND RECOMMENDATIONS

Firemen's Pension Plan

Finding No. 1 – Restated Plan Document Not Adopted By Ordinance

Condition: The City of Bethlehem Firemen's Pension Plan is currently controlled by the provisions of the City's Codified Ordinance at Article 151. The terms, provisions and conditions of the firemen's pension plan were amended and restated in a separately executed plan document effective March 26, 2009; however, the City's Codified Ordinance at Article 151 has not been amended to reflect the provisions of the updated plan document.

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

Furthermore, in Wynne v. Lower Merion Township, 181 Pa. Superior Ct., 524, the Pennsylvania Superior Court held that an ordinance may be amended only by another ordinance and not by a resolution.

Cause: Plan officials were unaware that the city should formally adopt the provisions of the amended and restated plan document through a properly executed ordinance.

Effect: The failure to properly adopt the plan document 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 amended and restated plan document through a properly executed ordinance.

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

Police Pension Plan

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

Condition: The City of Bethlehem Police Pension Plan is currently controlled by the provisions of the City's Codified Ordinance at Article 153. The terms, provisions and conditions of the police pension plan were amended and restated in a separately executed plan document effective March 26, 2009, however, the City's Codified Ordinance at Article 153 has not been amended to reflect the provisions of the updated plan document.

CITY OF BETHLEHEM AGGREGATE PENSION FUND
FINDINGS AND RECOMMENDATIONS

Police Pension Plan – (Continued)

Finding No. 2 – (Continued)

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

Furthermore, in Wynne v. Lower Merion Township, 181 Pa. Superior Ct., 524, the Pennsylvania Superior Court held that an ordinance may be amended only by another ordinance and not by a resolution.

Cause: Plan officials were unaware that the city should formally adopt the provisions of the amended and restated plan document through a properly executed ordinance.

Effect: The failure to properly adopt the plan document 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 amended and restated plan document through a properly executed ordinance.

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

CITY OF BETHLEHEM AGGREGATE PENSION FUND
 SUPPLEMENTARY INFORMATION
 (UNAUDITED)

SCHEDULES 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, 2007, is as follows:

POLICE PENSION PLAN

	(1)	(2)	(3)	(4)	(5)	(6)
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)	Covered Payroll (c)	Unfunded (Assets in Excess of) Actuarial Accrued Liability as a % of Payroll [(b-a)/(c)]
01-01-07	\$ 64,234,097	\$ 67,122,710	\$ 2,888,613	95.7%	\$ 8,603,708	33.6%
01-01-09	64,399,190	74,423,894	10,024,704	86.5%	10,058,301	99.7%
01-01-11	63,718,342	83,930,276	20,211,934	75.9%	11,565,225	174.8%

Note: The market value of the plan's assets at 01-01-09 has 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 130 percent and a minimum of 70 percent of the fair market value of assets. The market value of the plan's assets at 01-01-11 has 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. These methods 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.

CITY OF BETHLEHEM AGGREGATE PENSION FUND
 SUPPLEMENTARY INFORMATION
 (UNAUDITED)

SCHEDULES OF FUNDING PROGRESS – (Continued)

FIREMEN’S PENSION PLAN

	(1)	(2)	(3)	(4)	(5)	(6)
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)	Covered Payroll (c)	Unfunded (Assets in Excess of) Actuarial Accrued Liability as a % of Payroll [(b-a)/(c)]
01-01-07	\$ 48,461,160	\$ 49,968,614	\$ 1,507,454	97.0%	\$ 5,994,014	25.1%
01-01-09	48,780,258	55,305,397	6,525,139	88.2%	6,544,422	99.7%
01-01-11	48,626,861	62,441,284	13,814,423	77.9%	7,317,502	188.8%

Note: The market value of the plan’s assets at 01-01-09 has 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 130 percent and a minimum of 70 percent of the fair market value of assets. The market value of the plan’s assets at 01-01-11 has 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. These methods will lower contributions in years of less than expected returns and increase contributions in years of greater 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.

CITY OF BETHLEHEM AGGREGATE PENSION FUND
 SUPPLEMENTARY INFORMATION
 (UNAUDITED)

SCHEDULES OF FUNDING PROGRESS – (Continued)

OFFICERS’ AND EMPLOYEES’ PENSION PLAN

	(1)	(2)	(3)	(4)	(5)	(6)
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)	Covered Payroll (c)	Unfunded (Assets in Excess of) Actuarial Accrued Liability as a % of Payroll [(b-a)/(c)]
01-01-07	\$ 9,001,028	\$ 10,177,845	\$ 1,176,817	88.4%	\$ 321,240	366.3%
01-01-09	7,943,203	8,984,437	1,041,234	88.4%	240,846	432.3%
01-01-11	7,120,687	8,530,589	1,409,902	83.5%	120,237	1,172.6%

Note: The market value of the plan’s assets at 01-01-09 has 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 130 percent and a minimum of 70 percent of the fair market value of assets. The market value of the plan’s assets at 01-01-11 has 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. These methods will lower contributions in years of less than expected returns and increase contributions in years of greater 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.

CITY OF BETHLEHEM AGGREGATE PENSION FUND
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.

Trends in unfunded (assets in excess of) actuarial accrued liability and annual covered payroll are both affected by inflation. Expressing the unfunded (assets in excess of) actuarial accrued liability as a percentage of annual covered payroll (Column 6) approximately adjusts for the effects of inflation and aids analysis of the plan's progress made in accumulating sufficient assets to pay benefits when due. Generally, where there is an unfunded actuarial accrued liability, the smaller this percentage, the stronger the plan. However, when assets are in excess of the actuarial accrued liability, the higher the bracketed percentage, the stronger the plan.

CITY OF BETHLEHEM AGGREGATE PENSION FUND
SUPPLEMENTARY INFORMATION
(UNAUDITED)

SCHEDULES OF CONTRIBUTIONS FROM EMPLOYER
AND OTHER CONTRIBUTING ENTITIES

POLICE PENSION PLAN

Year Ended December 31	Annual Required Contribution	Percentage Contributed
2006	\$ 1,571,524	100.0%
2007	1,692,287	100.0%
2008	1,713,031	100.0%
2009	1,847,708	100.0%
2010	1,921,109	100.0%
2011	2,534,484	100.0%

CITY OF BETHLEHEM AGGREGATE PENSION FUND
SUPPLEMENTARY INFORMATION
(UNAUDITED)

SCHEDULES OF CONTRIBUTIONS FROM EMPLOYER
AND OTHER CONTRIBUTING ENTITIES

FIREMEN'S PENSION PLAN

Year Ended December 31	Annual Required Contribution	Percentage Contributed
2006	\$ 986,961	100.0%
2007	1,044,942	100.0%
2008	1,018,719	100.0%
2009	1,174,242	100.0%
2010	1,136,780	100.0%
2011	1,672,843	100.0%

CITY OF BETHLEHEM AGGREGATE PENSION FUND
SUPPLEMENTARY INFORMATION
(UNAUDITED)

SCHEDULES OF CONTRIBUTIONS FROM EMPLOYER
AND OTHER CONTRIBUTING ENTITIES

OFFICERS' AND EMPLOYEES' PENSION PLAN

Year Ended December 31	Annual Required Contribution	Percentage Contributed
2006	\$ 381,266	100.0%
2007	381,269	100.0%
2008	379,382	100.0%
2009	622,663	100.0%
2010	467,762	100.0%
2011	455,998	100.0%

CITY OF BETHLEHEM AGGREGATE PENSION FUND
SUPPLEMENTARY INFORMATION
NOTES TO SUPPLEMENTARY SCHEDULES
(UNAUDITED)

The information presented in the required supplementary schedules was determined as part of the actuarial valuation at the date indicated. Additional information as of the latest actuarial valuation date follows:

POLICE PENSION PLAN

Actuarial valuation date	January 1, 2011
Actuarial cost method	Entry age normal
Amortization method	Level dollar
Remaining amortization period	18 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	7.5%
Projected salary increases	5.0%
Includes inflation at	Not disclosed
Cost-of-living adjustments	None assumed

CITY OF BETHLEHEM AGGREGATE PENSION FUND
SUPPLEMENTARY INFORMATION
NOTES TO SUPPLEMENTARY SCHEDULES
(UNAUDITED)

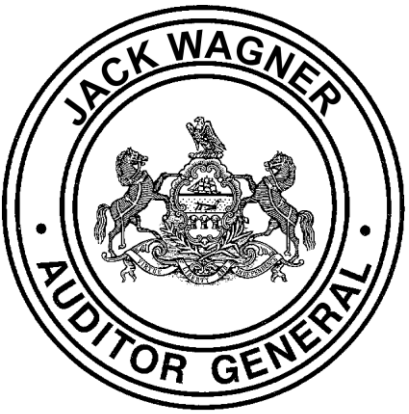
FIREMEN'S PENSION PLAN

Actuarial valuation date	January 1, 2011
Actuarial cost method	Entry age normal
Amortization method	Level dollar
Remaining amortization period	18 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	7.5%
Projected salary increases	4.5%
Includes inflation at	Not disclosed
Cost-of-living adjustments	None assumed

CITY OF BETHLEHEM AGGREGATE PENSION FUND
SUPPLEMENTARY INFORMATION
NOTES TO SUPPLEMENTARY SCHEDULES
(UNAUDITED)

OFFICERS' AND EMPLOYEES' PENSION PLAN

Actuarial valuation date	January 1, 2011
Actuarial cost method	Entry age normal
Amortization method	Level dollar
Remaining amortization period	2 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	7.5%
Projected salary increases	4.5%
Includes inflation at	Not disclosed
Cost-of-living adjustments	None assumed



CITY OF BETHLEHEM AGGREGATE PENSION FUND
REPORT DISTRIBUTION LIST

This report was initially distributed to the following:

The Honorable Tom Corbett
Governor
Commonwealth of Pennsylvania

City of Bethlehem Aggregate Pension Fund
Northampton County
10 East Church Street
Bethlehem, PA 18018

The Honorable John B. Callahan	Mayor
Mr. Eric R. Evans	City Council President
Mr. Dennis W. Reichard	City Business Administrator
Ms. Cynthia H. Biedenkopf	City Clerk

This report is a matter of public record. Copies of this report may be obtained from the Pennsylvania Department of the Auditor General, Office of Communications, Room 318 Finance Building, Harrisburg, PA 17120. If you have any questions regarding this report or any other matter, you may contact the Department of the Auditor General by accessing our website at www.auditorgen.state.pa.us.