

EAST PENN TOWNSHIP NONUNIFORMED PENSION PLAN

CARBON COUNTY

COMPLIANCE AUDIT REPORT

FOR THE PERIOD

JANUARY 1, 2006, TO DECEMBER 31, 2008



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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 East Penn Township Nonuniformed Pension Plan 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.

The East Penn Township Nonuniformed Pension Plan is a single-employer defined benefit pension plan locally controlled by the provisions of Resolution No. 99-3.



Board of Township Supervisors
East Penn Township
Carbon County
Lehighon, PA 18235

We have conducted a compliance audit of the East Penn Township Nonuniformed Pension Plan for the period January 1, 2006, to December 31, 2008. The audit was conducted pursuant to authority derived from Section 402(j) of Act 205 and in accordance with *Government Auditing Standards* applicable to performance audits 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.

Township officials are responsible for establishing and maintaining an internal control structure to provide reasonable assurance that the East Penn Township Nonuniformed Pension Plan is administered in compliance with applicable state laws, regulations, contracts, administrative procedures, and local ordinances and policies. To assist us in planning and performing our audit, we obtained an understanding of the township's internal control structure as it relates to the township's compliance with those requirements. Additionally, we tested transactions, assessed official actions, performed analytical procedures and interviewed selected officials to the extent necessary to satisfy the audit objectives.

The results of our tests indicated that, in all significant respects, the East Penn Township Nonuniformed 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 –
Improper Receipt Of State Aid
- Finding No. 2 – Incorrect Data On Certification Form AG 385 Resulting In
An Underpayment Of State Aid
- Finding No. 3 – Failure To Properly Determine And Fully Pay The Minimum
Municipal Obligation Of The Plan

We also noted a matter that has been included in the following observation further discussed later in this report:

Observation – Failure To Prepare Financial Statements

The accompanying supplementary information is presented for purposes of additional analysis. We did not audit the information and, accordingly, express no form of assurance on it.

The contents of this report were discussed with officials of East Penn Township and, where appropriate, their responses have been included in the report.

April 9, 2009

JACK WAGNER
Auditor General

EAST PENN TOWNSHIP NONUNIFORMED PENSION PLAN
STATUS OF PRIOR FINDINGS

Compliance With Prior Audit Recommendation

East Penn Township has complied with the prior audit recommendation concerning the following:

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

The township reimbursed \$1,355 to the Commonwealth for the overpayment of state aid.

Partial Compliance With Prior Audit Recommendation

- Improper Receipt Of State Aid

The township returned the improper state aid allocations received for the years 2003 and 2004, totaling \$9,128, to the Commonwealth; however, applicable interest was not included in the reimbursement.

Status Of Prior Audit Recommendation

- Failure To Prepare Financial Statements

The status of the prior audit recommendation is addressed in the Observation discussed later in this report.

EAST PENN TOWNSHIP NONUNIFORMED PENSION PLAN
FINDINGS AND RECOMMENDATIONS

Finding No. 1 – Partial Compliance With Prior Audit Recommendation – Improper Receipt Of
State Aid

Condition: As disclosed in our prior audit report, the township improperly received state aid for the years 2003 and 2004, totaling \$9,128 prior to funding the police pension plan for three plan years. Since the improper state aid allocations were deposited into the nonuniformed pension plan, the prior audit report contained a finding recommendation that the improper state aid allocations be returned to the Commonwealth, with interest compounded annually from the date of receipt to the date of repayment, at a rate earned by the pension plan.

During the audit period, the township returned \$9,128 to the Commonwealth; however, the township failed to pay any interest on the reimbursement.

Criteria: The case of Peyton v. Margiotti, 398 Pa. 86, (1959), states that a person has the right to collect interest of money which is unlawfully withheld from him. When interest is not expressly provided for... it is due... from the date of withholding. Id. at 94.

Cause: Township officials failed to establish adequate internal control procedures to ensure full compliance with the prior audit recommendation.

Effect: The pension plan retained the interest earned on the state aid overpayment.

Recommendation: We again recommend that the interest due on the state aid overpayments received in 2003 and 2004, compounded annually from date of receipt to date of repayment, at a rate earned by the pension plan, be reimbursed to the Commonwealth. A check should be made payable to: Commonwealth of Pennsylvania and mailed to: Department of the Auditor General, Municipal Pension & Fire Relief Programs Unit, 1205 Pittsburgh State Office Building, 300 Liberty Avenue, Pittsburgh, PA 15222. A copy of the interest calculation must be submitted along with evidence of payment.

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

Finding No. 2 – Incorrect Data On Certification Form AG 385 Resulting In An Underpayment
Of State Aid

Condition: The township understated the police payroll by \$364, and failed to certify 1 eligible nonuniformed employee and understated payroll by \$23,041 in 2007 on Certification Form AG 385. In addition, the township failed to certify 1 eligible police officer and understated payroll by \$38,879, and failed to certify 2 eligible nonuniformed employees and understated payroll by \$47,388 in 2008 on Certification Form AG 385.

EAST PENN TOWNSHIP NONUNIFORMED PENSION PLAN
FINDINGS AND RECOMMENDATIONS

Finding No. 2 – (Continued)

Criteria: Pursuant to Act 205, at Section 402(e)(2), an employee who has been employed on a full-time basis for at least six consecutive months and has been participating in a pension plan during the certification year is eligible for certification.

In addition, pursuant to the instructions that accompany Certification Form AG 385, the total payroll eligible to be certified should be Internal Revenue Service Form W-2 earnings pertaining to full-time positions.

Cause: Plan officials were unaware of the applicable Act 205 guidelines for the certification of eligible employees. In addition, plan officials failed to establish adequate internal control procedures to ensure the accuracy of the data certified.

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. Since the township’s state aid allocations were based on pension costs, the effect of the incorrect certification of pension data on the township’s state aid allocations is identified below:

<u>Year</u>	<u>Type Of Plan</u>	<u>Normal Cost</u>	<u>Payroll Understated</u>	<u>State Aid Underpayment</u>
2007	Police	15.50%	\$ 364	\$ 56
	Nonuniformed	11.09%	\$ 23,041	<u>2,555</u>
				<u>2,611</u>
2008	Police	12.61%	\$ 38,879	4,903
	Nonuniformed	14.30%	\$ 47,388	<u>6,776</u>
				<u>11,679</u>
Total Underpayment of State Aid				<u>\$ 14,290</u>

Although the township will be reimbursed for the underpayment of state aid due to the township’s certification errors, the full amount of the 2007 and 2008 state aid allocations were not available to be deposited timely and therefore were not available to pay operating expenses or for investment.

EAST PENN TOWNSHIP NONUNIFORMED PENSION PLAN
FINDINGS AND RECOMMENDATIONS

Finding No. 2 – (Continued)

Recommendation: We recommend that, in the future, plan officials comply with the instructions that accompany Certification Form AG 385 to assist them in accurately reporting the required pension plan data.

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

Finding No. 3 – Failure To Properly Determine And Fully Pay The Minimum Municipal Obligation Of The Plan

Condition: Plan officials did not properly determine or fully pay the minimum municipal obligation (MMO) of the nonuniformed pension plan for the year 2008, as required by Act 205. The MMO determined by the municipality understated payroll by \$18,862. Based upon an estimate prepared by this department, the municipality had an unpaid 2008 MMO balance of \$2,301.

Criteria: With regard to the MMO, Section 302(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.

With regard to the payroll estimate used in the preparation of the MMO, the Pennsylvania Code, Title 16, Section 204.1(c)(1) states, in part:

The payroll used in determining the minimum municipal obligation of a pension plan under section 302(c) of the act shall be based on the payroll to be reported on the Internal Revenue Service Form W-2 and shall be calculated as the total payroll for active members of the plan as of the date of the determination, plus the payroll for the same active members of the plan projected to the year's end using the payroll rates in effect as of the date of the determination.

Section 302(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.

EAST PENN TOWNSHIP NONUNIFORMED PENSION PLAN
FINDINGS AND RECOMMENDATIONS

Finding No. 3 – (Continued)

Furthermore, Section 302(e) of Act 205 states, in part:

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. . . .

Cause: Plan officials failed to include the payroll of all active members of the pension plan in the MMO calculation.

Effect: The proper determination of the plan's MMO ensures plan officials can properly allocate the necessary resources to the pension plan for the upcoming year. The failure to fully 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 fully pay the 2008 MMO by the December 31, 2008, deadline, the municipality must add the 2008 MMO balance to the current year's MMO and include interest, as required by Act 205.

Recommendation: We recommend that the municipality pay the MMO due to the nonuniformed pension plan for the year 2008, with interest, in accordance with Section 302(e) of Act 205. 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, in the future, plan officials properly determine the amount of payroll to be used in the MMO calculation and pay the full MMO due to the plan.

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

EAST PENN TOWNSHIP NONUNIFORMED 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, except for distressed pension plans, for which annual reporting was required through January 1, 2003. The historical information, beginning as of January 1, 2003, is as follows:

	(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)]
01-01-03	\$ 36,484	\$ 71,368	\$ 34,884	51.1%	\$ 75,477	46.2%
01-01-05	66,071	94,535	28,464	69.9%	105,700	26.9%
01-01-07	97,125	45,317	(51,808)	214.3%	53,799	(96.3%)

EAST PENN TOWNSHIP NONUNIFORMED 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.

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.

EAST PENN TOWNSHIP NONUNIFORMED PENSION PLAN
SUPPLEMENTARY INFORMATION
(UNAUDITED)

SCHEDULE OF CONTRIBUTIONS FROM EMPLOYER
AND OTHER CONTRIBUTING ENTITIES

Year Ended December 31	Annual Required Contribution	Percentage Contributed
2003	\$ 11,775	100.0%
2004	12,830	100.0%
2005	15,558	112.5%
2006	11,903	100.0%
2007	12,587	100.0%
2008	10,095	77.2%

EAST PENN TOWNSHIP NONUNIFORMED PENSION PLAN
 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:

Actuarial valuation date	January 1, 2007
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	6.0%
Projected salary increases	4.5%
Includes inflation at	Not disclosed
Cost-of-living adjustments	None assumed

EAST PENN TOWNSHIP NONUNIFORMED PENSION PLAN
OBSERVATION

Observation – Failure To Prepare Financial Statements

Plan officials have not prepared financial statements or required notes to the financial statements for the nonuniformed pension plan for the years ended December 31, 2006, 2007 and 2008.

Financial reporting assists in fulfilling a municipality's duty to be publicly accountable and should enable users to assess accountability. Guidance for the form and content of annual financial statements and notes to the financial statements can be found in Governmental Accounting Standards Board Statements No. 25 (GASB 25), as amended by No. 50 (GASB 50), and No. 3 (GASB 3), as amended by No. 40 (GASB 40).

Plan officials should consider establishing and implementing procedures to ensure the preparation of annual financial statements, which include note disclosures required by GASB 25, as amended by GASB 50, and GASB 3, as amended by GASB 40, in accordance with accounting principles generally accepted in the United States of America.

EAST PENN TOWNSHIP NONUNIFORMED PENSION PLAN
REPORT DISTRIBUTION LIST

This report was initially distributed to the following:

The Honorable Edward G. Rendell
Governor
Commonwealth of Pennsylvania

East Penn Township Nonuniformed Pension Plan
Carbon County
167 Municipal Road
Lehigh, PA 18235

Mr. Gary P. Kuehner Chairman, Board of Township Supervisors

Mr. Nathan A. Scherer Treasurer

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.