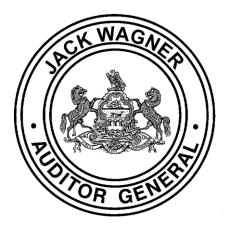
## LOWER NAZARETH TOWNSHIP NONUNIFORMED PENSION PLAN

#### NORTHAMPTON COUNTY

## **COMPLIANCE AUDIT REPORT**

#### FOR THE PERIOD

#### **JANUARY 1, 2008, TO DECEMBER 31, 2010**



## LOWER NAZARETH TOWNSHIP NONUNIFORMED PENSION PLAN

## NORTHAMPTON COUNTY

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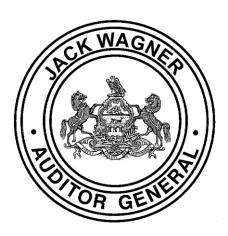
#### BACKGROUND

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 <u>et seq</u>.). 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 Lower Nazareth 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 Lower Nazareth Township Nonuniformed Pension Plan is a single-employer defined benefit pension plan locally controlled by the provisions of Resolution No. TR-9-88, as amended.



Board of Township Supervisors Lower Nazareth Township Northampton County Bethlehem, PA 18020

We have conducted a compliance audit of the Lower Nazareth Township Nonuniformed Pension Plan for the period January 1, 2008, to December 31, 2010. 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 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. Lower Nazareth Township contracted with an independent certified public accounting firm for audits of its basic financial statements for the years ended December 31, 2008 and 2009, and an audit 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, for the year ended December 31, 2010, 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 Lower Nazareth Township Nonuniformed 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 objective, 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 the extent necessary to satisfy the audit objective.

The results of our tests indicated that, in all significant respects, the Lower Nazareth 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 finding further discussed later in this report:

# Finding – Incorrect Data On Certification Form AG 385 Resulting In An Overpayment Of State Aid

As previously noted, the objective of our audit of the Lower Nazareth Township Nonuniformed Pension Plan was to determine compliance with applicable state laws, contracts, administrative procedures, and local ordinances and policies. During the current audit period, Act 205 was amended on September 18, 2009, through the adoption of Act 44 of 2009. Among several provisions relating to municipal pension plans, the bill provides for the implementation of a distress recovery program. Three levels of distress have been established:

Level	Indication	Funding Criteria
Ι	Minimal distress	70-89%
Π	Moderate distress	50-69%
III	Severe distress	Less than 50%

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. However, we are extremely concerned about the funded status of the plan contained in the schedule of funding progress included in this report which indicates the plan's funded ratio is 67.6% as of January 1, 2009, which is the most recent date available. Based on this information, the Public Employee Retirement Commission issued a notification that the township is currently in Level II moderate distress status. We encourage township officials to monitor the funding of the nonuniformed pension plan to ensure its long-term financial stability.

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

June 9, 2011

JACK WAGNER Auditor General

#### LOWER NAZARETH TOWNSHIP NONUNIFORMED PENSION PLAN FINDING AND RECOMMENDATION

#### <u>Finding – Incorrect Data On Certification Form AG 385 Resulting In An Overpayment Of State</u> <u>Aid</u>

<u>Condition</u>: The township certified an ineligible employee and overstated payroll by \$7,086 in 2009 on Certification Form AG 385.

<u>Criteria</u>: 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.

<u>Cause</u>: Plan officials failed to establish adequate internal control procedures to ensure the accuracy of the data certified.

<u>Effect</u>: 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 Lower Nazareth Township participates in a regional police pension plan, the township's state aid allocation for its nonuniformed 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 2009 was \$38,341; however, based on the corrected information, the township was entitled to an allocation of \$35,484, therefore, the township received a \$2,857 overpayment of state aid.

<u>Recommendation</u>: We recommend that the overpayment of state aid, in the amount of \$2,857, 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, 11 Stanwix Street, Suite 1450, Pittsburgh, PA 15222. A copy of the interest calculation must be submitted along with the check.

We also recommend that plan officials establish adequate internal control procedures to ensure compliance with the instructions that accompany Certification Form AG 385 to assist them in accurately reporting the required pension data.

#### LOWER NAZARETH TOWNSHIP NONUNIFORMED PENSION PLAN FINDING AND RECOMMENDATION

#### Finding – (Continued)

<u>Management's Response</u>: Municipal officials agreed with the finding without exception. Subsequent to the current audit period, the township reimbursed \$3,227 to the Commonwealth for the overpayment of state aid.

<u>Auditor's Conclusion</u>: Based on the management response, municipal officials have partially complied with the finding recommendation. Full compliance will be evaluated during our next audit of the plan.

#### LOWER NAZARETH 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, 2005, is as follows:

	(1)	(2)	(3)	(4)	(5)	(6)
						Unfunded
			Unfunded			(Assets in
		Actuarial	(Assets in			Excess of)
		Accrued	Excess of)			Actuarial
	Actuarial	Liability	Actuarial			Accrued
Actuarial	Value of	(AAL) -	Accrued	Funded	Covered	Liability as a %
Valuation	Assets	Entry Age	Liability	Ratio	Payroll	of Payroll
Date	(a)	(b)	(b) - (a)	(a)/(b)	(c)	[(b-a)/(c)]
01-01-05	\$ 246,371	\$ 255,948	\$ 9,577	96.3%	\$ 457,682	2.1%
01-01-07	446,717	356,464	(90,253)	125.3%	548,833	(16.4%)
01-01-09	653,914	966,614	312,700	67.6%	550,058	56.8%

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 subject to a corridor between 80 and 120 percent of the fair market value of assets. 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.

#### LOWER NAZARETH 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.

## LOWER NAZARETH 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
2005	\$ 48,515	154.6%
2006	34,758	225.8%
2007	39,303	222.8%
2008	29,075	333.0%
2009	27,351	365.6%
2010	96,189	114.4%

#### LOWER NAZARETH 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, 2009
Actuarial cost method	Entry age normal
Amortization method	Level dollar
Remaining amortization period	20 years
Asset valuation method	5-year smoothing method subject to a corridor between 80-120% of the 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

#### LOWER NAZARETH TOWNSHIP NONUNIFORMED PENSION PLAN REPORT DISTRIBUTION LIST

This report was initially distributed to the following:

#### The Honorable Tom Corbett Governor Commonwealth of Pennsylvania

#### Lower Nazareth Township Nonuniformed Pension Plan Northampton County 306 Butztown Road Bethlehem, PA 18020

Mr. Eric E. Nagle	Chairman, Board of T	ownship Supervisors

Mr. Timm A. Tenges Township Manager

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.