

**MACUNGIE BOROUGH POLICE PENSION PLAN**

**LEHIGH COUNTY**

**COMPLIANCE AUDIT REPORT**

**FOR THE PERIOD**

**JANUARY 1, 2007, TO DECEMBER 31, 2009**





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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 Macungie Borough Police 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 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. § 761 et seq.

The Macungie Borough Police Pension Plan is a single-employer defined benefit pension plan locally controlled by the provisions of Ordinance No. 392, 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 Honorable Mayor and Borough Council  
Macungie Borough  
Lehigh County  
Macungie, PA 18062

We have conducted a compliance audit of the Macungie Borough Police Pension Plan for the period January 1, 2007, to December 31, 2009. 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 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.

Borough officials are responsible for establishing and maintaining effective internal controls to provide reasonable assurance that the Macungie Borough Police 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 borough's internal controls as they relate to the borough'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 the extent necessary to satisfy the audit objectives.

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

Finding – Noncompliance With Prior Audit Recommendation – Inconsistent  
And Unauthorized Pension Benefits

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 Macungie Borough and, where appropriate, their responses have been included in the report.

August 9, 2010

JACK WAGNER  
Auditor General

MACUNGIE BOROUGH POLICE PENSION PLAN  
STATUS OF PRIOR FINDING

Noncompliance With Prior Audit Recommendation

Macungie Borough has not complied with the prior audit recommendation concerning the following as further discussed in the Finding and Recommendation section of this report:

· Inconsistent Pension Benefits

The plan's joinder agreement and the collective bargaining agreement between the borough and its police officers continue to contain inconsistent cost-of-living adjustment provisions. In addition, during the current audit period, it was noted that the service-related disability benefit provision contained in the joinder agreement is not consistent with the collective bargaining agreement and the joinder agreement provides for an unauthorized probationary period for membership eligibility as disclosed in the finding and recommendation contained in this audit report.

MACUNGIE BOROUGH POLICE PENSION PLAN  
FINDING AND RECOMMENDATION

Finding – Noncompliance With Prior Audit Recommendation – Inconsistent And Unauthorized Pension Benefits

Condition: As disclosed in the prior audit report, the plan’s joinder agreement and the collective bargaining agreement between the borough and its police officers continue to contain inconsistent cost-of-living adjustment provisions. In addition, during the current audit period, it was noted that the service-related disability benefit provision contained in the joinder agreement is not consistent with the collective bargaining agreement and the joinder agreement provides for an unauthorized probationary period for membership eligibility, as illustrated below:

<u>Benefit Provision</u>	<u>Joinder Agreement</u>	<u>Collective Bargaining Agreement</u>	<u>Act 600</u>
Cost-of-living adjustments	This plan shall not provide for an annual cost-of-living increase as set forth in section 4.07 of Chapter II of the Master Plan and Trust.	So long as the pension plan has a surplus of at least \$500,000, retirees shall be entitled to an annual cost-of-living adjustment, within the limits provided by Act 600.	The ordinance or resolution establishing the police pension fund may provide for a cost of living increase for members of the police force receiving retirement benefits.
Probationary period for membership eligibility	An employee shall be eligible to become a participant in the plan upon completion of a probationary period of six (6) months.	None provided	None provided
Service-related disability benefit	The amount of the benefit shall be equal to 50% of final monthly average salary. In no event may the benefit be less than fifty (50%) of the member’s salary at the time the disability was incurred with no offset by Social Security disability benefits.	None provided	The benefit must be in conformity with a uniform scale and fixed by the plan’s governing document at no less than 50% of the member’s salary at the time the disability was incurred, reduced by the amount of Social Security disability benefits received for the same injury.

MACUNGIE BOROUGH POLICE PENSION PLAN  
FINDING AND RECOMMENDATION

Finding – (Continued)

Criteria: The plan’s governing document and the collective bargaining agreement should contain consistent benefit provisions that are in compliance with Act 600 to ensure the sound administration of retirement benefits.

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

Effect: Inconsistent plan documents and unauthorized benefit provisions could result in inconsistent or improper benefit calculations and incorrect benefit payments from the pension plan.

Recommendation: We again recommend that municipal officials ensure the plan’s governing document and the collective bargaining agreement contain consistent benefit provisions that are in compliance with Act 600 at its earliest opportunity to do so.

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

MACUNGIE 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, 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)
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)]
01-01-05	\$ 539,442	\$ 485,436	\$ (54,006)	111.1%	\$ 171,936	(31.4%)
01-01-07	587,095	539,649	(47,446)	108.8%	238,490	(19.9%)
01-01-09	587,193	614,031	26,838	95.6%	265,719	10.1%

Note: The market values of the plan's assets at 01-01-05, 01-01-07 and 01-01-09, have been adjusted to reflect the smoothing of gains and/or losses over a 4-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.

MACUNGIE 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.

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.

MACUNGIE 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
2004	\$ 18,430	100.0%
2005	23,980	100.0%
2006	28,303	100.0%
2007	27,362	100.0%
2008	38,383	100.0%
2009	40,995	100.0%



MACUNGIE BOROUGH POLICE 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	Fair value, 4-year smoothing
Actuarial assumptions:	
Investment rate of return	7.5%
Projected salary increases	5.0%



MACUNGIE BOROUGH POLICE PENSION PLAN  
REPORT DISTRIBUTION LIST

This report was initially distributed to the following:

The Honorable Edward G. Rendell  
Governor  
Commonwealth of Pennsylvania

Macungie Borough Police Pension Plan  
Lehigh County  
21 Locust Street  
Macungie, PA 18062

The Honorable Rickie Hoffman	Mayor
Mr. Guy Ramsey	Council President
Ms. Chris L. Boehm	Borough 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](http://www.auditorgen.state.pa.us).