

COMPLIANCE AUDIT

Upper Macungie Township Non-Uniformed Employees' Pension Plan

Lehigh County, Pennsylvania
For the Period
January 1, 2016 to December 31, 2018

October 2019



Commonwealth of Pennsylvania
Department of the Auditor General

Eugene A. DePasquale • Auditor General



Commonwealth of Pennsylvania
Department of the Auditor General
Harrisburg, PA 17120-0018
Facebook: Pennsylvania Auditor General
Twitter: @PAAuditorGen
www.PaAuditor.gov

EUGENE A. DePASQUALE
AUDITOR GENERAL

Board of Township Supervisors
Upper Macungie Township
Lehigh County
Breinigsville, PA 18031

We have conducted a compliance audit of the Upper Macungie Township Non-Uniformed Employees' Pension Plan for the period January 1, 2016 to December 31, 2018. We also evaluated compliance with some requirements subsequent to that period when possible. 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 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 by the plan's governing document and applicable laws and regulations for the years covered by our audit period
- We determined whether retirement benefits calculated for all three of the plan members who retired 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 benefit due to retired individuals and comparing these amounts to supporting documentation evidencing amounts determined and actually paid to recipients. We also determined whether retirement benefits calculated for both of the plan members who elected to vest during the current audit period, represent payments to all (and only) those entitled to receive them and were properly determined in accordance with the plan's governing document, applicable laws and regulations by recalculating the amount of the pension benefit due to retired individuals and comparing these amounts to supporting documentation evidencing amounts determined.
- We determined whether the January 1, 2015 and January 1, 2017 actuarial valuation reports were prepared and submitted by March 31, 2016 and 2018, 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.

Upper Macungie Township contracted with an independent certified public accounting firm for annual audits of its basic financial statements, 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 Upper Macungie Township Non-Uniformed Employees' 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 and as previously described, 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 objective.

The results of our procedures indicated that, in all significant respects, the Upper Macungie Township Non-Uniformed Employees' 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 – Incorrect Data On Certification Form AG 385 Resulting In A Net Overpayment Of State Aid

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 Upper Macungie Township and, where appropriate, their responses have been included in the report. We would like to thank township officials for the cooperation extended to us during the conduct of the audit.

September 24, 2019



EUGENE A. DEPASQUALE
Auditor General

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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.

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 Upper Macungie Township Non-Uniformed Employees' Pension Plan is also governed by implementing regulations adopted by the former 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 69 - The Second Class Township Code, Act of May 1, 1933 (P.L. 103, No. 69), as reenacted and amended, 53 P.S. § 65101 et seq.

The Upper Macungie Township Non-Uniformed Employees' Pension Plan is a single-employer defined benefit pension plan locally controlled by the provisions of Ordinance No. 2009 – 1. The plan was established April 1, 1982. Active members are not required to contribute to the plan. As of December 31, 2018, the plan had 43 active members, 6 terminated members eligible for vested benefits in the future, and 28 retirees receiving pension benefits from the plan.

BACKGROUND – (Continued)

As of December 31, 2018, selected plan benefit provisions are as follows:

Eligibility Requirements:

Normal Retirement Age 65

Early Retirement Age 55 and 10 years of service.

Vesting 20% vesting available after 1 year of service, increasing 20% each year to 100% after 5 years of service.

Retirement Benefit:

Monthly benefit equals 2% of average monthly pay based on highest 3 consecutive plan years of employment multiplied by years of service up to 30 years, with 120 months guaranteed. For members hired prior to 1-1-2002, minimum benefit is 55% of average monthly pay.

Survivor Benefit:

Before Retirement Eligibility Actuarial equivalent of the pension accrued to date.

Disability Benefit:

After 6 months of service – actuarial equivalent of accrued benefit.

UPPER MACUNGIE TOWNSHIP NON-UNIFORMED EMPLOYEES' PENSION PLAN
FINDING AND RECOMMENDATION

Finding – Incorrect Data On Certification Form AG 385 Resulting In A Net Overpayment Of State Aid

Condition: The township certified 2 ineligible police officers (4 units) and certified 3 ineligible non-uniformed employees (3 units) on the Certification Form AG 385 filed in 2017. In addition, the township certified an ineligible non-uniformed employee (1 unit) on the Certification Form AG 385 filed in 2018. Furthermore, subsequent to the current engagement period, the township certified 2 ineligible police officers (4 units) and failed to certify an eligible non-uniformed employee (1 unit) on the Certification Form AG 385 filed in 2019. 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. Moreover, the various plan documents associated with the township's individual pension plans provide participation eligibility criteria that is more stringent than that prescribed by Act 205. For participation in the police pension plan, the collective bargaining agreement between the township and its police officer's also requires completion of a one-year probationary period prior to participation in the plan. And, for non-uniformed plan participation, there is an additional plan entry date requirement (*January 1 nearest the date on which the individual participant satisfies both the age and service requirements*) stipulated in the governing document prior to participation in the pension plan.

Cause: 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. Because the township's state aid allocations were based on unit value, the incorrect certification of pension data affected the township's state aid allocations for the years 2017 and 2018, as identified below:

Year	Type Of Plan	Units Overstated (Understated)	Unit Value	State Aid Overpayment (Underpayment)
2017	Police	4	\$ 4,588	\$ 18,352
	Non-Uniformed	3	\$ 4,588	13,764
				\$ 32,116
2018	Non-Uniformed	1	\$ 4,684	\$ 4,684
Net Overpayment of State Aid 2017-2018				\$ 36,800

UPPER MACUNGIE TOWNSHIP NON-UNIFORMED EMPLOYEES' PENSION PLAN
FINDING AND RECOMMENDATION

Finding – (Continued)

Subsequent to the current period, since the township's state aid allocation was also based on unit value, the incorrect certification of pension data affected the township's state aid allocation for 2019, as follows:

Year	Type Of Plan	Units Overstated (Understated)	Unit Value	State Aid Overpayment (Underpayment)
2019	Police	4	\$ 5,121	\$ 20,484
	Non-Uniformed	(1)	\$ 5,121	<u>(5,121)</u>
				<u>\$ 15,363</u>

In addition, the township used the overpayments of state aid to pay the minimum municipal obligations (MMOs) due to its pension plans; therefore, if the reimbursement to the Commonwealth is made from the pension plans, the plans' MMOs will not be fully paid.

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

Recommendation: We recommend that the net overpayment of state aid, in the amount of \$52,163 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 its pension plan funds, we recommend that any resulting MMO deficiencies be paid to the pension plans with interest, at a rate earned by the pension plans.

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

Auditor's Conclusion: Due to the potential withhold of state aid, the township's compliance with the finding recommendation will be monitored subsequent to the release of the report and through our next plan engagement.

UPPER MACUNGIE TOWNSHIP NON-UNIFORMED EMPLOYEES' PENSION PLAN
POTENTIAL WITHHOLD OF STATE AID

The finding contained in this audit report cites an overpayment of state aid to the township in the amount of \$52,163, 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.

UPPER MACUNGIE TOWNSHIP NON-UNIFORMED EMPLOYEES' PENSION PLAN
SUPPLEMENTARY INFORMATION
(UNAUDITED)

The supplementary information contained on Pages 6 through 9 reflects the implementation of GASB Statement No. 67, *Financial Reporting for Pension Plans*. The objective of this statement is to improve financial reporting by state and local governmental pension plans.

SCHEDULE OF CHANGES IN THE NET PENSION
LIABILITY AND RELATED RATIOS
OFOR THE YEARS ENDED DECEMBER 31, 2014, 2015, AND 2016

	<u>2014</u>	<u>2015</u>	<u>2016</u>
Total Pension Liability			
Service cost	\$ 246,293	\$ 196,069	\$ 205,872
Interest	468,884	468,561	490,504
Difference between expected and actual experience	-	(365,122)	-
Benefit payments, including refunds of member contributions	<u>(251,980)</u>	<u>(356,284)</u>	<u>(407,434)</u>
Net Change in Total Pension Liability	463,197	(56,776)	288,942
Total Pension Liability – Beginning	<u>6,131,480</u>	<u>6,594,677</u>	<u>6,537,901</u>
Total Pension Liability – Ending (a)	<u><u>\$ 6,594,677</u></u>	<u><u>\$ 6,537,901</u></u>	<u><u>\$ 6,826,843</u></u>
Plan Fiduciary Net Position			
Contributions – employer	\$ 382,494	\$ 380,731	\$ 295,561
Net investment income (loss)	331,039	(37,799)	303,205
Benefit payments, including refunds of member contributions	<u>(251,980)</u>	<u>(356,284)</u>	<u>(407,434)</u>
Net Change in Plan Fiduciary Net Position	461,553	(13,352)	191,332
Plan Fiduciary Net Position – Beginning	<u>5,487,212</u>	<u>5,948,765</u>	<u>5,935,413</u>
Plan Fiduciary Net Position – Ending (b)	<u><u>\$ 5,948,765</u></u>	<u><u>\$ 5,935,413</u></u>	<u><u>\$ 6,126,745</u></u>
Net Pension Liability – Ending (a-b)	<u><u>\$ 645,912</u></u>	<u><u>\$ 602,488</u></u>	<u><u>\$ 700,098</u></u>
Plan Fiduciary Net Position as a Percentage of the Total Pension Liability	90.21%	90.78%	89.74%
Estimated Covered Employee Payroll	\$ 1,811,476	\$ 1,973,790	\$ 2,154,016
Net Pension Liability as a Percentage of Covered Employee Payroll	35.66%	30.52%	32.50%

UPPER MACUNGIE TOWNSHIP NON-UNIFORMED EMPLOYEES' PENSION PLAN
SUPPLEMENTARY INFORMATION
(UNAUDITED)

SCHEDULE OF CHANGES IN THE NET PENSION
LIABILITY AND RELATED RATIOS
FOR THE YEARS ENDED DECEMBER 31, 2017 AND 2018

	<u>2017</u>	<u>2018</u>
Total Pension Liability		
Service cost	\$ 247,322	\$ 259,688
Interest	538,719	564,932
Difference between expected and actual experience	332,740	-
Benefit payments, including refunds of member contributions	<u>(447,981)</u>	<u>(449,814)</u>
Net Change in Total Pension Liability	670,800	374,806
Total Pension Liability – Beginning	<u>6,826,843</u>	<u>7,497,643</u>
Total Pension Liability – Ending (a)	<u>\$ 7,497,643</u>	<u>\$ 7,872,449</u>
Plan Fiduciary Net Position		
Contributions – employer	\$ 315,529	\$ 334,212
Net investment income (loss)	749,554	(391,941)
Benefit payments, including refunds of member contributions	<u>(447,981)</u>	<u>(449,814)</u>
Net Change in Plan Fiduciary Net Position	617,102	(507,543)
Plan Fiduciary Net Position – Beginning	<u>6,126,745</u>	<u>6,743,847</u>
Plan Fiduciary Net Position – Ending (b)	<u>\$ 6,743,847</u>	<u>\$ 6,236,304</u>
Net Pension Liability – Ending (a-b)	<u>\$ 753,796</u>	<u>\$ 1,636,145</u>
Plan Fiduciary Net Position as a Percentage of the Total Pension Liability	89.95%	79.22%
Estimated Covered Employee Payroll	\$ 2,412,665	\$ 2,447,739
Net Pension Liability as a Percentage of Covered Employee Payroll	31.24%	66.84%

UPPER MACUNGIE TOWNSHIP NON-UNIFORMED EMPLOYEES' PENSION PLAN
 SUPPLEMENTARY INFORMATION
 (UNAUDITED)

Sensitivity Of The Net Pension Liability To Changes In The Discount Rate

The following presents the net pension liability of the township as of December 31, 2015, 2016, 2017 and 2018, calculated using the discount rate of 7.5%, as well as what the township's net pension liability would be if it were calculated using a discount rate that is 1 percentage-point lower or 1 percentage-point higher than the current rate:

	1% Decrease (6.5%)	Current Discount Rate (7.5%)	1% Increase (8.5%)
Net Pension Liability – 12/31/15	\$ 1,355,779	\$ 602,488	\$ (43,221)
Net Pension Liability – 12/31/16	\$ 1,489,073	\$ 700,098	\$ 23,131
Net Pension Liability – 12/31/17	\$ 1,611,381	\$ 753,796	\$ 16,943
Net Pension Liability – 12/31/18	\$ 2,538,299	\$ 1,636,145	\$ 860,157

SCHEDULE OF CONTRIBUTIONS

Year Ended December 31	Actuarially Determined Contribution	Actual Contributions	Contribution Deficiency (Excess)	Covered- Employee Payroll	Contributions as a Percentage of Covered- Employee Payroll
2014	\$ 382,494	\$ 382,494	\$ -	\$1,811,476	21.12%
2015	380,731	380,731	-	1,973,790	19.29%
2016	295,561	295,561	-	2,154,016	13.72%
2017	315,529	315,529	-	2,412,665	13.08%
2018	334,212	334,212	-	2,447,739	13.65%

UPPER MACUNGIE TOWNSHIP NON-UNIFORMED EMPLOYEES' PENSION PLAN
SUPPLEMENTARY INFORMATION
(UNAUDITED)

SCHEDULE OF INVESTMENT RETURNS

Annual Money-Weighted Rate of Return, Net of Investment Expense:

2018	(5.45%)
2017	11.51%
2016	5.38%
2015	(0.13%)
2014	6.79%

UPPER MACUNGIE TOWNSHIP NON-UNIFORMED EMPLOYEES' 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, 2013, 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)
01-01-13	\$ 4,584,148	\$ 5,674,079	\$ 1,089,931	80.8%
01-01-15	5,948,765	6,229,555	280,790	95.5%
01-01-17	6,126,745	7,159,583	1,032,838	85.6%

UPPER MACUNGIE TOWNSHIP NON-UNIFORMED EMPLOYEES' 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.

UPPER MACUNGIE TOWNSHIP NON-UNIFORMED EMPLOYEES' 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, 2017
Actuarial cost method	Entry age normal
Amortization method	Level dollar
Remaining amortization period	12 years
Asset valuation method	Fair value
Actuarial assumptions:	
Investment rate of return	7.5%
Projected salary increases	5.0%

UPPER MACUNGIE TOWNSHIP NON-UNIFORMED EMPLOYEES' PENSION PLAN
REPORT DISTRIBUTION LIST

This report was initially distributed to the following:

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