

COMPLIANCE AUDIT

West Chester Borough Non-Uniformed Defined Contribution Pension Plan Chester County, Pennsylvania For the Period January 1, 2014 to December 31, 2014

December 2015



Commonwealth of Pennsylvania
Department of the Auditor General
Eugene A. DePasquale • Auditor General



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EUGENE A. DePASQUALE
AUDITOR GENERAL

The Honorable Mayor and Borough Council
West Chester Borough
Chester County
West Chester, PA 19380

We have conducted a compliance audit of the West Chester Borough Non-Uniformed Defined Contribution Pension Plan for the period January 1, 2014 to December 31, 2014. 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 findings and conclusions based on our audit objective. We believe that the evidence obtained provides a reasonable basis for our findings 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. Employer contributions that were deposited into the pension plan for the year ended December 31, 2014, are presented on the Summary of Deposited State Aid and Employer Contributions.

- × 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 that there were no benefit calculations prepared for the years covered by our audit period.
- × We determined whether the terms of the plan's 1 unallocated insurance contract, including ownership and any restrictions, were in compliance with plan provisions, investment policies, and state regulations by comparing the terms of the contract with the plan's provisions, investment policies, and state regulations.

Borough officials are responsible for establishing and maintaining effective internal controls to provide reasonable assurance that the West Chester Borough Non-Uniformed Defined Contribution 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 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 West Chester Borough Non-Uniformed Defined Contribution 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 – Incorrect Data On Certification Form AG 385 Resulting In An Overpayment Of State Aid

Finding No. 2 – Improper Loan Provision Contained In The Plan's Adoption Agreement

The contents of this report were discussed with officials of West Chester Borough and, where appropriate, their responses have been included in the report. We would like to thank borough officials for the cooperation extended to us during the conduct of the audit.

December 1, 2015



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 West Chester Borough Non-Uniformed Defined Contribution 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 West Chester Borough Non-Uniformed Defined Contribution Pension Plan is a single-employer defined contribution pension plan locally controlled by the provisions of Ordinance No. 12-2013. The plan is also affected by the provisions of collective bargaining agreements between the borough and its non-uniformed employees. The plan was established October 16, 2013 for non-uniformed employees hired on or after January 1, 2013. Active members are not required to contribute to the plan. The municipality is required to contribute 5 percent of compensation. As of December 31, 2014, the plan had 17 active members, no terminated members eligible for vested benefits in the future, and no retirees receiving pension benefits.

WEST CHESTER BOROUGH NON-UNIFORMED DEFINED CONTRIBUTION
PENSION PLAN
FINDINGS AND RECOMMENDATIONS

**Finding No. 1 - Incorrect Data On Certification Form AG 385 Resulting In An Overpayment
Of State Aid**

Condition: The borough certified 1 ineligible non-uniformed employee (1 unit) and overstated payroll by \$36,122 on the Certification Form AG 385 filed in 2015. The data contained on this certification form 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.

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

Effect: 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 plans. Because the borough’s state aid allocation was based on unit value, the incorrect certification of pension data affected the borough’s state aid allocation, as identified below:

<u>Year</u>	<u>Units Overstated</u>	<u>Unit Value</u>	<u>State Aid Overpayment</u>
2015	1	\$3,921	\$ 3,921

In addition, the borough used the overpayment of state aid to pay the minimum municipal obligation (MMO) due to the plan; therefore, if the reimbursement to the Commonwealth is made from the pension plan, the plan’s MMO will not be fully paid.

Recommendation: We recommend that the overpayment of state aid, in the amount of \$3,921, be returned to the Commonwealth from the borough’s general fund. 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, 320 Finance Building, Harrisburg, PA 17120. A copy of the interest calculation must be submitted along with the check.

WEST CHESTER BOROUGH NON-UNIFORMED DEFINED CONTRIBUTION
PENSION PLAN
FINDINGS AND RECOMMENDATIONS

Finding No. 1 - (Continued)

We also recommend that in the future, plan officials establish adequate internal control procedures, such as having at least 2 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 plan funds, we recommend that any resulting MMO deficiency be paid to the pension plan with interest, at a rate earned by the pension plan.

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

Auditor's Conclusion: Compliance will be monitored subsequent to the release of the audit report and through our next audit of the pension plan.

WEST CHESTER BOROUGH NON-UNIFORMED DEFINED CONTRIBUTION
PENSION PLAN
FINDINGS AND RECOMMENDATIONS

Finding No. 2 – Improper Loan Provision Contained In The Plan’s Adoption Agreement

Condition: Section Q of the pension plan’s adoption agreement, which was approved on June 26, 2013, improperly contains a provision that allows for loans to active plan members.

Criteria: Section 102 of Act 205 contains the following definitions:

“Pension plan or system.” The various aspects of the relationship between a municipality and its employees with respect to the retirement coverage provided by a municipality to the employees.

“Defined contribution pension plan.” A type of pension benefit plan which provides for a fixed contribution rate or amount and which provides for periodic benefit payments calculable at retirement dependent on the accumulated contributions, investment income, experience gains and losses credited to the member and the expected mortality of the member.

Therefore, Act 205 funding (state aid) is intended to provide retirement benefit payments, not for loans to be made to active plan members.

Cause: Plan officials were unaware that plan documents should not contain loan provisions.

Effect: The unauthorized loan provision violates the intent of Act 205 to only provide distributions to plan members upon their retirement or termination of employment with the municipality.

Recommendation: We recommend that municipal officials take appropriate action to eliminate the unauthorized loan provision from the plan’s governing document and to limit future distributions to those benefits authorized under Act 205.

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

Auditor Conclusion: Compliance with the finding recommendation will be monitored during our next audit of the pension plan.

WEST CHESTER BOROUGH NON-UNIFORMED DEFINED CONTRIBUTION
PENSION PLAN
SUMMARY OF DEPOSITED STATE AID AND EMPLOYER CONTRIBUTIONS

Year Ended December 31	State Aid	Employer Contributions
2014	None	\$ 29,535

WEST CHESTER BOROUGH NON-UNIFORMED DEFINED CONTRIBUTION
PENSION PLAN
REPORT DISTRIBUTION LIST

This report was initially distributed to the following:

The Honorable Tom W. Wolf
Governor
Commonwealth of Pennsylvania

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401 East Gay Street
West Chester, PA 19380

The Honorable Carolyn T. Comitta	Mayor
Mr. Jordan C. Norley	Council President
Mr. Michael A. Cotter	Borough Manager

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