

COMPLIANCE AUDIT

Freedom Borough Non-Uniformed Pension Plan Beaver County, Pennsylvania For the Period January 1, 2018 to December 31, 2022

July 2023



Commonwealth of Pennsylvania
Department of the Auditor General

Timothy L. DeFoor • Auditor General



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**TIMOTHY L. DEFOOR
AUDITOR GENERAL**

The Honorable Mayor and Borough Council
Freedom Borough
Beaver County
Freedom, PA 15042

We have conducted a compliance audit of the Freedom Borough Non-Uniformed Pension Plan for the period January 1, 2018 to December 31, 2022. We also evaluated compliance with some requirements subsequent to that period when possible. The audit was conducted pursuant to authority derived from the Municipal Pension Plan Funding Standard and Recovery Act (Act 205 of 1984, as amended, 53 P.S. § 895.402(j)), which requires the Auditor General, as deemed necessary, to audit every municipality which receives general municipal pension system state aid and every municipal pension plan and fund in which general municipal pension system state aid is deposited. The audit was not conducted, nor was it required to be, in accordance with Government Auditing Standards issued by the Comptroller General of the United States. We planned and performed the 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 finding contained in our prior 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. To determine if municipal officials took appropriate corrective action to address the finding contained in our prior report, we inquired of plan officials and evaluated supporting documentation provided by officials evidencing that the suggested corrective action has been appropriately taken. 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 whether annual employee contributions were calculated, deducted, and deposited into the pension plan in accordance with the plan's governing document and applicable laws and regulations by testing total members' contributions on an annual basis using the rates obtained from the plan's governing document in effect for all years within the period under audit and examining documents evidencing the deposit of these employee contributions into the pension plan.
- We determined whether retirement benefits calculated for plan members who retired and who separated employment and received a lump-sum distribution during the current audit period, and through the completion of our fieldwork procedures, 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 pension benefits due to the retired individuals and comparing these amounts to supporting documentation evidencing amounts determined and actually paid to the recipients.
- We determined whether the January 1, 2019 and January 1, 2021 actuarial valuation reports were prepared and submitted by March 31, 2020 and 2022, respectively, in accordance with Act 205 and whether selected information provided on this report 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.

The Freedom Borough Non-Uniformed Pension Plan participates in the Pennsylvania Municipal Retirement System (PMRS), which is an agent multiple-employer public employee retirement system that acts as a common investment and administrative agent for participating municipal pension plans. PMRS issues a separate Annual Comprehensive Financial Report, copies of which are available from the PMRS accounting office. PMRS's financial statements were not audited by us and, accordingly, we express no opinion or other form of assurance on them.

Borough officials are responsible for establishing and maintaining effective internal controls to provide reasonable assurance that the Freedom Borough Non-Uniformed Pension Plan is administered in compliance with applicable state laws, regulations, contracts, administrative procedures, and local ordinances and policies. As previously described, we tested transactions, interviewed selected officials, and performed procedures to the extent necessary 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 objectives.

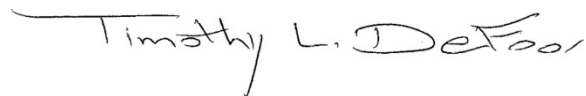
The results of our procedures indicated that, in all significant respects, the Freedom Borough Non-Uniformed Pension Plan was administered in compliance with applicable state laws, regulations, contracts, administrative procedures, and local ordinances and policies, except as noted in the following findings further discussed later in this report:

- Finding No. 1 – Partial Compliance With Prior Recommendation – Receipt Of State Aid In Excess Of Entitlement
- Finding No. 2 – Inadequate Accounting/Reporting Over Activity Of The Pension Plan
- Finding No. 3 – Ordinance Improperly Amended By Resolution

Finding No. 1 contained in this audit report repeats a condition that was cited in our previous report that has not been corrected by borough officials. We are concerned by the borough's failure to fully correct this previously reported finding and strongly encourage timely implementation of the recommendations noted in this audit report.

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 Freedom 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.



Timothy L. DeFoor
Auditor General
July 12, 2023

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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.

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 Freedom Borough Non-Uniformed Pension Plan is also governed by implementing regulations 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 15 - Pennsylvania Municipal Retirement Law, Act of February 1, 1974
(P.L. 34, No. 15), as amended, 53 P.S. § 881.101 et seq.

The Freedom Borough Non-Uniformed Pension Plan is a single-employer cash balance pension plan locally controlled by the provisions of Resolution No. 10142020 (see *Finding No. 3*), and a separately executed adoption agreement with the plan custodian, adopted pursuant to Act 15. Prior to September 1, 2020, the plan was controlled by the provisions of Ordinance No. 518, and an agreement with the plan's custodian, adopted pursuant to Act 15. The plan was established October 11, 2000. Active members are not required to contribute to the plan; however, they may optionally contribute up to 10 percent of compensation to the plan. Prior to April 11, 2018, the municipality was required to contribute 10 percent of compensation per active member. Effective April 11, 2018, the municipality is required to contribute 15 percent of compensation to the plan. As of December 31, 2022, the plan had three active members and four retirees receiving pension benefits from the plan.

FREEDOM BOROUGH NON-UNIFORMED PENSION PLAN
STATUS OF PRIOR FINDING

Partial Compliance With Prior Recommendation

Freedom Borough has partially complied with the prior recommendation concerning the following:

· Receipt Of State Aid In Excess Of Entitlement

During the current audit period, the borough reimbursed \$481 to the Commonwealth for excess state aid received in 2017; however, plan officials again failed to reconcile the borough's state aid allocation with the plan's annual pension costs for the year 2020 and reimburse any excess state aid received to the Commonwealth as further discussed in Finding No. 1 in the Findings and Recommendations section of this report.

FREEDOM BOROUGH NON-UNIFORMED PENSION PLAN
FINDINGS AND RECOMMENDATIONS

Finding No. 1 – Partial Compliance With Prior Recommendation – Receipt Of State Aid In Excess Of Entitlement

Condition: As disclosed in the Status of Prior Finding section of this report, the borough partially complied with the prior recommendation by reimbursing the excess state aid received in 2017 to the Commonwealth, however, plan officials again failed to reconcile the borough’s state aid allocation with the plan’s annual pension costs for the year 2020 and failed to reimburse the excess state aid received to the Commonwealth, as illustrated below:

State aid allocation	\$ 14,772
Actual municipal pension costs	<u>(12,025)</u>
Excess state aid	<u>\$ 2,747</u>

In addition, as of the date of our audit fieldwork completion, the excess state aid remains in the borough’s general fund and has not been deposited into the pension plan according to municipal records.

Criteria: Section 402(f)(2) of Act 205 states:

No municipality shall be entitled to receive an allocation of general municipal pension system State aid in an amount which exceeds the aggregate actual financial requirements of any municipal pension plans for police officers, paid firefighters or employees other than police officers or paid firefighters maintained by the municipality, less the amount of any aggregate annual member or employee contributions during the next succeeding plan year, as reported in the most recent complete actuarial report filed with the commission.

Cause: Plan officials again failed to establish adequate internal control procedures to reconcile the borough’s annual state aid allocation with the plan’s actual pension costs.

Effect: It is this department’s opinion that because the entire proceeds of the insurance premium tax on foreign casualty insurance companies are distributed annually to each eligible recipient municipality, it is inappropriate to use state aid in one year to offset pension costs in other years. Consequently, the overpayment of state aid in the year 2020 must be returned to the Commonwealth for redistribution.

FREEDOM BOROUGH NON-UNIFORMED PENSION PLAN
FINDINGS AND RECOMMENDATIONS

Finding No. 1 – (Continued)

Recommendation: We recommend that the municipality return the \$2,747 from the borough's general fund to the Commonwealth for the excess state aid received in the year 2020. A check in this amount, with interest compounded annually from date of receipt to date of repayment, at a rate earned by the plan, should be made payable to: Commonwealth of Pennsylvania and mailed to: Department of the Auditor General, Municipal Pension & Liquor Control Audits, 314 Finance Building, Harrisburg, PA 17120. A copy of the interest calculation must be submitted along with the check.

Furthermore, we again recommend that, in the future, plan officials reconcile the borough's annual state aid allocation with the plan's annual pension costs and reimburse any excess state aid received to the Commonwealth.

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

Auditor's Conclusion: The borough's compliance with the finding recommendation will be monitored subsequent to the release of the audit report and through our next audit of the pension plan.

Finding No. 2 – Inadequate Accounting/Reporting Over Activity Of The Pension Plan

Condition: The municipality's accounting/reporting system did not provide effective control over the transactional activity of the pension plan during the year 2022. Municipal officials were unable to furnish annual financial statements or custodial account statements summarizing the financial activity of its pension plan.

Criteria: An adequate system of accounting and record keeping is a prerequisite for sound administration of pension plans. In addition, assets held in a custodial account for the purpose of plan management are to be governed by the terms and provisions of the account contract, provided that the terms and provisions of the contract are within the parameters of all prevailing pension legislation. Although the municipality may contract with a trustee to administer the financial management of the plan, the fiduciary responsibility for the plan remains with the municipality.

Cause: Municipal officials did not maintain a separate detailed accounting of pension plan transactions which, among other things, helps assure the production of proper financial statements to effectively monitor the annual activity of the pension plan. Additionally, municipal officials indicated that the plan's custodian failed to provide copies of the custodial account transaction statements summarizing activity of the pension plan account for the year 2022.

FREEDOM BOROUGH NON-UNIFORMED PENSION PLAN
FINDINGS AND RECOMMENDATIONS

Finding No. 2 – (Continued)

Effect: Although we were able to obtain alternate documentation from the municipality to evidence the propriety of individual transactions tested during performance of the audit, the failure to maintain annual financial and/or account transaction statements prohibits municipal officials from effectively monitoring the plan’s financial operations and could lead to undetected errors or improprieties in account transactions.

Recommendation: We recommend that municipal officials establish and maintain a financial accounting and reporting system that allows the municipality to effectively monitor the plan’s financial operations, even in the absence of statements from the plan custodian. Municipal officials should refer to the Auditor General’s Bulletin No. 2-88 entitled “Preparation, Maintenance and Auditability of Financial Records,” for further guidance in establishing adequate accounting and record-keeping procedures. In addition, we recommend that municipal officials contact the plan custodian and obtain annual financial statements of the custodial account for its pension plan for the year 2022 to ensure the accuracy and propriety of the transaction activity.

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

Auditor’s Conclusion: It was noted that the plan custodian went through a substantial upgrade to the plan administration software and implemented a new accounting system. The modernization process, along with the COVID-19 pandemic, resulted in unforeseen delays in the year-end reporting process for financial statements and GASB 68 reports. The custodian expects 2022 financial reports to be distributed before the end of 2023. Compliance with the finding recommendation will be evaluated during our next audit of the plan.

Finding No. 3 – Ordinance Improperly Amended By Resolution

Condition: The Freedom Borough Non-Uniformed Pension Plan was established effective October 11, 2020 via Ordinance No. 518. During the current audit period, Ordinance No. 518 was restated in its entirety by Resolution No. 10142020, dated October 11, 2020, effective September 1, 2020, which adopted a revised plan agreement with the plan custodian with the same effective date. Plan provisions adopted by ordinance must be amended by ordinance, not by a resolution.

Criteria: In Wynne v. Lower Merion Township, 181 Pa. Superior Ct., 524, the Pennsylvania Superior Court held that an ordinance may be amended only by another ordinance and not by a resolution.

FREEDOM BOROUGH NON-UNIFORMED PENSION PLAN
FINDINGS AND RECOMMENDATIONS

Finding No. 3 – (Continued)

Cause: In September 2020, the plan custodian provided an updated Cash Balance Plan Adoption Agreement along with a document for the borough to formally adopt the amendment. Although the document was drafted as an ordinance, at its October 5, 2020 Monthly Workshop Meeting, the borough moved to adopt it as a resolution, which was officially executed at its October 14, 2020 borough council meeting. Municipal officials were not aware that a resolution cannot amend an ordinance.

Effect: The failure to properly adopt the restated plan document could result in inconsistent or improper benefit calculations and incorrect benefit payments from the pension plan.

Recommendation: We recommend that the borough amend the plan’s governing document with a properly executed ordinance.

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

Auditor’s Conclusion: Compliance will be evaluated during our next audit of the plan.

FREEDOM BOROUGH NON-UNIFORMED PENSION PLAN
 SUPPLEMENTARY INFORMATION
 (UNAUDITED)

SCHEDULE OF CONTRIBUTIONS

Year Ended December 31	Statutorily Required Contribution (SRC)*	Contributions in Relation to the SRC*	Contribution Deficiency (Excess)**	Covered- Employee Payroll***	Contributions as a Percentage of Covered- Employee Payroll
2014	\$ 9,743	\$ 9,778	\$ (35)	\$ 96,628	10.12%
2015	10,039	10,063	(24)	99,591	10.10%
2016	10,117	10,117	-	100,373	10.08%
2017	9,554	9,574	(20)	94,733	10.11%
2018	14,900	8,962	5,938	109,651	8.17%
2019	17,011	23,046	(6,035)	112,609	20.47%
2020	12,030	12,031	(1)	79,537	15.13%
2021	18,302	18,303	(1)	121,350	15.08%
2022	19,909	19,909	-		

* The Statutorily Required Contribution (SRC) is a contribution amount based upon the payroll and the contribution rate as outlined under the terms of the cash balance pension plan.

** The Statutorily Required Contribution and the actual Contribution were provided by PMRS. Deviation between these amounts may be due to contributions to or transfers from the municipal reserve account.

In 2018, PMRS credited the plan with \$6,035 in advance employer and employee contribution credit which was satisfied in 2019 plus administrative expenses.

*** Due to the timing of this audit, covered-employee payroll for 2022 was not provided in this schedule.

FREEDOM BOROUGH NON-UNIFORMED PENSION PLAN
REPORT DISTRIBUTION LIST

This report was initially distributed to the following:

The Honorable Joshua D. Shapiro
Governor
Commonwealth of Pennsylvania

The Honorable Nadine Padezanin
Mayor

Mr. John Kaercher
Council President

Mr. Eric Climo
Council Vice-President

Ms. Sharon Miller
Chief Administrative Officer

Mr. Richard Cardamone, CPA, CGMA
Pennsylvania Municipal Retirement System

This report is a matter of public record and is available online at www.PaAuditor.gov. Media questions about the report can be directed to the Pennsylvania Department of the Auditor General, Office of Communications, 229 Finance Building, Harrisburg, PA 17120; via email to: news@PaAuditor.gov.