

COMPLIANCE AUDIT

Freedom Borough Non-Uniformed Pension Plan Beaver County, Pennsylvania For the Period January 1, 2011 to December 31, 2013

October 2014



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**

**EUGENE A. DePASQUALE
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, 2011 to December 31, 2013. 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. Our methodology addressed determinations about the following:

- Whether state aid was properly determined and deposited in accordance with Act 205 requirements. State aid allocations that were deposited into the pension plan for the years ended December 31, 2008 to December 31, 2013, are presented on the Summary of Deposited State Aid and Employer Contributions.
- Whether employer contributions are determined and deposited in accordance with the plan's governing document and applicable laws and regulations. Employer contributions that were deposited into the pension plan for the years ended December 31, 2008 to December 31, 2013, are presented on the Summary of Deposited State Aid and Employer Contributions.
- Whether employee contributions are required and, if so, are determined, deducted, and deposited into the pension plan and are in accordance with the plan provisions and applicable laws and regulations.

- Whether benefit payments, if any, represent payments to all (and only) those entitled to receive them and are properly determined in accordance with applicable laws and regulations.
- Whether obligations for plan benefits are accurately determined in accordance with plan provisions and based on complete and accurate participant data; and whether actuarial valuation reports are prepared and submitted to the Public Employee Retirement Commission (PERC) in accordance with state law and 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.
- Whether the terms of the contractual agreement with the Pennsylvania Municipal Retirement System are in accordance with the plan's governing document, if separately stated, and applicable laws and regulations.

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 Comprehensive Annual 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. 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, 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.

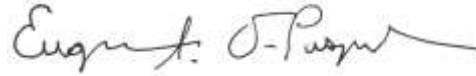
The results of our tests indicated that, in all significant respects, the Freedom Borough Non-Uniformed Pension Plan was administered in compliance with applicable state laws, regulations, contracts, administrative procedures, and local ordinances and policies, except as noted in the following findings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

Finding No. 1 – Receipt Of State Aid In Excess Of Entitlement

Finding No. 2 – Incorrect Data On Certification Form AG 385 Resulting In An Underpayment Of State Aid

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.

October 20, 2014

A handwritten signature in black ink, appearing to read "Eugene A. DePasquale". The signature is fluid and cursive, with a long horizontal stroke at the end.

EUGENE A. DEPASQUALE
Auditor General

CONTENTS

| | <u>Page</u> |
|---|-------------|
| Background..... | 1 |
| Findings and Recommendations: | |
| Finding No. 1 – Receipt Of State Aid In Excess Of Entitlement..... | 2 |
| Finding No. 2 – Incorrect Data On Certification Form AG 385 Resulting In An Underpayment Of State Aid..... | 3 |
| Summary of Deposited State Aid and Employer Contributions..... | 5 |
| Report Distribution List | 6 |

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 Freedom Borough Non-Uniformed 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 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 Ordinance No. 518, as amended, adopted pursuant to Act 15. The plan was established October 11, 2000. Active members are not required to contribute to the plan. The municipality is required to contribute 10 percent of each member's compensation. As of December 31, 2013, the plan had 3 active members, no terminated members eligible for vested benefits in the future, and 1 retiree receiving pension benefits.

FREEDOM BOROUGH NON-UNIFORMED PENSION PLAN
FINDINGS AND RECOMMENDATIONS

Finding No. 1 – Receipt Of State Aid In Excess Of Entitlement

Condition: The borough received state aid in excess of the non-uniformed pension plan’s annual pension costs in the year 2011, as illustrated below:

| | |
|--------------------------------|----------------|
| State aid allocation | \$ 8,806 |
| Actual municipal pension costs | <u>(7,817)</u> |
| Excess state aid | <u>\$ 989</u> |

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 failed to reconcile the borough’s allocation of state aid to the plan’s annual pension costs.

Effect: It is this Department’s opinion that since 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 received in one year to offset pension costs in other years. Consequently, the overpayment of state aid received in the year 2011, in the total amount of \$989, must be returned to the Commonwealth for redistribution.

Recommendation: We recommend that the municipality return the \$989 overpayment of state aid received in the year 2011 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 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 evidence of payment.

FREEDOM BOROUGH NON-UNIFORMED PENSION PLAN
FINDINGS AND RECOMMENDATIONS

Finding No. 1 – (Continued)

Furthermore, we 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: 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 – Incorrect Data On Certification Form AG 385 Resulting In An Underpayment Of State Aid

Condition: The borough understated payroll by \$1,468 on the Certification Form AG 385 filed in 2013. The data contained on this certification form is based on prior calendar year information.

Criteria: Pursuant to the instructions that accompany Certification Form AG 385, the total payroll eligible to be certified should be Internal Revenue Service Form W-2 earnings pertaining to full-time positions.

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 plan. Because the borough’s state aid allocation was based on pension costs, the borough received an underpayment of state aid of \$147 as identified below:

| <u>Year</u> | <u>Normal Cost</u> | <u>Payroll Understated</u> | <u>State Aid Underpayment</u> |
|-------------|--------------------|----------------------------|-------------------------------|
| 2013 | 10.0% | \$ 1,468 | \$ 147 |

Although the borough will be reimbursed for the underpayment of state aid due to the borough’s certification error, the full amount of the 2013 state aid allocation was not available to be deposited timely and therefore resulted in the borough having to make additional municipal contributions in order to meet the plan’s funding obligation.

FREEDOM BOROUGH NON-UNIFORMED PENSION PLAN
FINDINGS AND RECOMMENDATIONS

Finding No. 2 – (Continued)

Recommendation: We 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.

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

Auditors Response: Compliance will be subject to verification through our next audit of the plan.

FREEDOM BOROUGH NON-UNIFORMED PENSION PLAN
SUMMARY OF DEPOSITED STATE AID AND EMPLOYER CONTRIBUTIONS

| Year Ended December 31 | State Aid | Employer Contributions |
|------------------------|-----------|------------------------|
| 2008 | \$ 8,603 | None |
| 2009 | 8,529 | \$ 47 |
| 2010 | 8,516 | 388 |
| 2011 | 8,806 | None |
| 2012 | 7,150 | 1,247 |
| 2013 | 8,190 | 1,166 |

FREEDOM BOROUGH NON-UNIFORMED PENSION PLAN
REPORT DISTRIBUTION LIST

This report was initially distributed to the following:

The Honorable Tom Corbett
Governor
Commonwealth of Pennsylvania

Freedom Borough Non-Uniformed Pension Plan
Beaver County
901 3rd Avenue
Freedom, PA 15042

| | |
|------------------------------------|--|
| The Honorable Arthur D. Evans, Jr. | Mayor |
| Mr. John V. Kaercher | Council President |
| Ms. Karen L. M. Willison | Borough Secretary |
| Ms. Kristine M. Cline | Pennsylvania Municipal Retirement System |

This report is a matter of public record and is available online at www.auditorgen.state.pa.us. Media questions about the report can be directed to the Pennsylvania Department of the Auditor General, Office of Communications, 231 Finance Building, Harrisburg, PA 17120; via email to: news@auditorgen.state.pa.us.