

COMPLIANCE AUDIT

Auburn Township Non-Uniformed Pension Plan Susquehanna County, Pennsylvania For the Period January 1, 2016 to December 31, 2019

September 2020



Commonwealth of Pennsylvania
Department of the Auditor General

Eugene A. DePasquale • Auditor General



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**EUGENE A. DePASQUALE
AUDITOR GENERAL**

Board of Township Supervisors
Auburn Township
Susquehanna County
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We have conducted a compliance audit of the Auburn Township Non-Uniformed Pension Plan for the period January 1, 2016 to December 31, 2019. 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 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. State aid allocations that were deposited into the pension plan for the years ended December 31, 2014 to December 31, 2019, are presented on the Summary of Deposited State Aid and Employer Contributions.

- 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 years ended December 31, 2014 to December 31, 2019, 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 whether retirement benefits calculated for plan members 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, 2015, January 1, 2017, and January 1, 2019 actuarial valuation reports were prepared and submitted by March 31, 2016, 2018, and 2020, 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.
- We determined whether the terms of all of the plan's allocated insurance contracts, 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.
- We determined whether transfers were properly authorized, timely, and appropriately recorded by plan officials by examining supporting documentation for all of the transfers made during the audit period and through the completion of our fieldwork procedures.

The township has elected to purchase allocated insurance contracts to fund the pension benefits for plan members. Under an allocated funding arrangement, the insurer receives and retains consideration in exchange for a legally enforceable obligation to pay future benefits. In accordance with Statement No. 67 of the Governmental Accounting Standards Board, as amended, allocated insurance contracts are excluded from the pension plan's assets. Consequently, the plan has no reportable assets for the years of 2016 and 2017. These allocated contracts were cash surrendered in 2018 and deposited into a traditional Roth IRA account for each individual, which is not an eligible funding mechanism as further discussed later, in Finding No.1 of this report.

Township officials are responsible for establishing and maintaining effective internal controls to provide reasonable assurance that the Auburn Township 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 objective.

The results of our procedures indicated that, in all significant respects, the Auburn Township 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 – Unauthorized Funding Mechanism

Finding No. 2 – Awarding Of Professional Services Contract Inconsistent With Provisions Of Act 205

The contents of this report were discussed with officials of Auburn 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 14, 2020



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.

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 Auburn Township 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 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 Auburn Township Non-Uniformed Pension Plan is a single-employer defined contribution pension plan locally controlled by the provisions of Resolution dated February 1, 1993. The plan was established June 1, 1975. Active members are not required to contribute to the plan. The municipality is required to contribute \$4,000 per individual. As of December 31, 2019, the plan had four active members.

AUBURN TOWNSHIP NON-UNIFORMED PENSION PLAN
FINDINGS AND RECOMMENDATIONS

Finding No. 1 – Unauthorized Funding Mechanism

Condition: During the current audit period, the municipality improperly funded individual retirement accounts (IRAs) to provide benefits at retirement to members of the non-uniformed pension plan, beginning in year 2018. These types of investments are not eligible for funding provided through the state aid program.

Criteria: Section 102 of Act 205 defines a pension plan as follows:

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.

Section 201.2 of Part IV of Title 16 of the Pennsylvania Code further elaborates on the definition included in Act 205, stating:

The term does not include a plan, program, or arrangement that is funded solely by municipal employee earnings or compensation reported as municipal employee earnings or compensation to the Internal Revenue Service on the Form W-2 Wage and Tax Statement or established under sections 8.1-8.3 of the act of March 30, 1811 (P.L. 145 Sm.L.228) (72 P.S. 4521.1-4521.3) or Section 408 of the Internal Revenue Code (26 U.S.C.A. 408).

Consequently, the former Public Employee Retirement Commission (PERC) has determined that Individual Retirement Accounts (IRAs) and IRS Section 457 Deferred Compensation plans are not eligible to participate in the state aid program.

Cause: Municipal officials were not aware that IRAs were not eligible funding vehicles for pension plans participating in the state aid program.

Effect: Since the funding mechanism does not meet the definition of a pension plan as prescribed above, it is not eligible for participation in the state aid program. In addition, since the individual employees rather than the municipality own these types of contracts, the municipality cannot ensure the integrity of these pension assets and the related benefits funded through state aid allocations from surrender by members prior to reaching retirement. Furthermore, the township's future state aid allocations may be withheld until the finding recommendation is complied with.

AUBURN TOWNSHIP NON-UNIFORMED PENSION PLAN
FINDINGS AND RECOMMENDATIONS

Finding No. 1 – (Continued)

Recommendation: We recommend that municipal officials either transfer plan assets to an eligible funding mechanism or return all state aid allocated to the individual IRAs during the years 2018 and 2019, in the total amount of \$24,172, to the Commonwealth. In the latter case, 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. A copy of the interest calculation must be submitted along with the check. Further, municipal officials should exclude members belonging to the ineligible plan from future Certification Forms AG 385 submitted to the department.

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 audit report and through our next audit of the pension plan.

Finding No. 2 – Awarding Of Professional Services Contract Inconsistent With Provisions Of Act 205

Condition: In 2018, the township changed custodians and entered into an agreement with a provider for custodial services for the pension plan; however, there was no evidence provided to support that the contracting for these professional services was conducted and awarded in accordance with provisions of Act 205.

Criteria: Section 701-A of Act 205, as amended by Act 44, defines a “Professional Services Contract”, as follows:

“Professional services contract.” A contract to which the municipal pension system is a party that is:

- (1) for the purchase or provision of professional services, including investment services, legal services, real estate services and other consulting services; and
- (2) not subject to a requirement that the lowest bid be accepted.

AUBURN TOWNSHIP NON-UNIFORMED PENSION PLAN
FINDINGS AND RECOMMENDATIONS

Finding No. 2 – (Continued)

In addition, Section 702-A (a) of Act 205 states, in part:

Each municipal pension system ... shall develop procedures to select the most qualified person to enter into a professional services contract. The procedures shall ensure that the availability of a professional services contract is advertised to potential participants in a timely and efficient manner. Procedures shall include applications and disclosure forms to be used to submit a proposal for review and to receive the award of a professional services contract.

Additionally, Section 702-A (c), (e), (f) and (h) state, in part:

Review. Procedures to select the most qualified person shall include a review of the person's qualifications, experience and expertise and the compensation to be charged.

Conflict of interest. The municipal pension system shall adopt policies relating to potential conflicts of interest in the review of a proposal or the negotiation of a contract.

Public information. Following the award of a professional services contract, all applications and disclosure forms shall be public except for proprietary information or other information protected by law.

Notice and summary. The relevant factors that resulted in the award of the professional services contract must be summarized in a written statement to be included in or attached to the documents awarding the contract. Within ten days of the award of the professional services contract, the original application, a summary of the basis for the award and all required disclosure forms must be transmitted to all unsuccessful applications and posted on the municipal pension system's Internet website, if an Internet website is maintained, at least seven days prior to the execution of the professional services contract.

Section 703-A (c) states in part:

Upon advertisement for a professional services contract by the municipal pension system, the contractor may not cause or agree to allow a third party to communicate with officials or employees of the municipal pension system except for requests for technical clarification.

AUBURN TOWNSHIP NON-UNIFORMED PENSION PLAN
FINDINGS AND RECOMMENDATIONS

Finding No. 2 – (Continued)

Furthermore, Resolution No. 2012-15, adopted by the borough to adhere to Act 44 of 2009, which amended Act 205, contains similar provisions as aforementioned above.

Cause: Plan officials failed to establish adequate internal controls procedures to evidence compliance with provisions of Resolution No. 2012-15 and Act 205 relative to professional services contracts for its pension plans.

Effect: The township's failure to comply in all respects with the provisions stipulated in Act 205, as adopted in Resolution No. 2012-15 for the procurement of professional investment and advisory services for the borough's pension plan, denotes a general lack of overall transparency of the actions taken by plan officials relative to the contracting for investment and advisory services for the borough's pension plan.

Recommendation: We recommend that municipal officials obtain a comprehensive understanding of Act 205 provisions, as adopted in Resolution 2012-15, for the procurement of professional services and develop and implement formal written procedures to ensure compliance with these provisions which should include the maintaining of appropriate and sufficient supporting documentation evidencing every phase of the process to ensure the transparency of the actions taken by plan officials relative to the awarding of any future professional services contracts for its pension plan.

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

Auditor's Conclusion: Compliance with the finding recommendation will be evaluated during our next audit of the plan.

AUBURN TOWNSHIP NON-UNIFORMED PENSION PLAN
POTENTIAL WITHHOLD OF STATE AID

Finding No. 1 contained in this audit report cites a potential overpayment of state aid to the township in the amount of \$24,172, plus interest, due to an unauthorized funding mechanism. 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.

AUBURN TOWNSHIP NON-UNIFORMED PENSION PLAN
SUMMARY OF DEPOSITED STATE AID AND EMPLOYER CONTRIBUTIONS

Year Ended December 31	State Aid	Employer Contributions
2014	\$ 7,500	None
2015	7,307	\$ 193
2016	7,975	2,025
2017	9,925	6,075
2018	11,049	4,951
2019	13,123	2,877

AUBURN TOWNSHIP NON-UNIFORMED PENSION PLAN
REPORT DISTRIBUTION LIST

This report was initially distributed to the following:

The Honorable Tom W. Wolf
Governor
Commonwealth of Pennsylvania

Mr. Berton Hollister
Chairman, Board of Township Supervisors

Mr. Daniel Trivett
Supervisor

Ms. Emily Cleveland
Secretary

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.