

COMPLIANCE AUDIT

Fountain Hill Borough Non-Uniformed Cash Balance Pension Plan

Lehigh County, Pennsylvania
For the Period
June 1, 2018 to December 31, 2021

November 2022



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
Fountain Hill Borough
Lehigh County
Fountain Hill, PA 18015

We have conducted a compliance audit of the Fountain Hill Borough Non-Uniformed Cash Balance Pension Plan for the period June 1, 2018 to December 31, 2021. 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.

- 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, 2018 to December 31, 2021, are presented on the Summary of Deposited State Aid and Employer Contributions.
- 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 also tested individual employee contributions made during the audit period for the lone active employee employed during the year 2018, amounting to \$95, all three active employees employed during the year 2019, amounting to \$1,336, all four active employees employed during the year 2020, amounting to \$2,784, and all five active employees employed during the year 2021, amounting to \$5,104.
- We determined that there were no benefit calculations prepared for the years covered by our audit period.
- We determined whether the January 1, 2019 actuarial valuation report was prepared and submitted by March 31, 2020, 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 Fountain Hill Borough Non-Uniformed Cash Balance 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 Fountain Hill Borough Non-Uniformed Cash Balance 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.

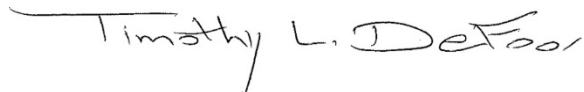
The results of our procedures indicated that, in all significant respects, the Fountain Hill Borough Non-Uniformed Cash Balance Pension Plan was administered in compliance with applicable state laws, regulations, contracts, administrative procedures, and local ordinances and policies, except as noted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

Finding No. 1 – Municipal Contributions Made In Excess Of Contributions Required To Fund The Plan

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

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 Fountain Hill 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
November 4, 2022

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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 Fountain Hill Borough Non-Uniformed Cash Balance 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 Fountain Hill Borough Non-Uniformed Cash Balance Pension Plan is a single-employer cash balance pension plan locally controlled by the provisions of Ordinance No. 842, and a separately executed plan agreement with the plan custodian, effective June 1, 2018, adopted pursuant to Act 15 for non-uniformed employees hired on or after June 1, 2018. The plan is also affected by the provisions of collective bargaining agreements between the borough and its non-uniformed employees. The plan was established June 1, 2018. Active members are required to contribute 3.5 percent of compensation to the plan. The municipality is required to contribute five (5.0) percent of compensation per member. As of December 31, 2021, the plan had two active members.

FOUNTAIN HILL BOROUGH NON-UNIFORMED CASH BALANCE PENSION PLAN
FINDINGS AND RECOMMENDATIONS

Finding No. 1 – Municipal Contributions Made In Excess Of Contributions Required To Fund The Plan

Condition: The borough made contributions to the non-uniformed cash balance pension plan in excess of contributions required to fund the pension plan, as illustrated below:

	<u>2020</u>	<u>2021</u>	<u>Total</u>
Actual municipal pension costs	\$ 4,037	\$ 7,345	\$ 11,382
State aid allocated	-	-	-
Municipal contributions required to fund plan	\$ 4,037	\$ 7,345	\$ 11,382
Actual municipal contributions made	\$ 6,094	\$ 10,530	\$ 16,624
Municipal contributions required to fund plan	(4,037)	(7,345)	(11,382)
Excess municipal contributions	\$ 2,057	\$ 3,185	\$ 5,242

Criteria: Section 3.01 of the PMRS Adoption Agreement effective June 1, 2018 states, in part:

Municipal Contributions Required in an amount equal to five percent (5.00%) of each member's compensation per calendar quarter.

Cause: Due to recent turnover in personnel responsible for the administration of the plan, current plan officials did not have a thorough understanding of the contributions required to fund the plan. In addition, the borough lacked adequate internal control procedures to ensure that municipal contributions were limited to those authorized by the plan's governing document.

Effect: As a result of the borough making contributions to the non-uniformed pension plan in excess of contributions required to fund the pension plan, an unallocated reserve fund was generated, and these funds could have been better utilized for other general municipal governmental purposes.

FOUNTAIN HILL BOROUGH NON-UNIFORMED CASH BALANCE PENSION PLAN
FINDINGS AND RECOMMENDATIONS

Finding No. 1 – (Continued)

It is the opinion of this department that the borough's failure to withdraw excess municipal contributions made in prior years does not preclude the borough from withdrawing the municipal contributions maintained in the unallocated reserve fund at this time.

Recommendation: We recommend that the borough liquidate the unallocated reserve fund maintained by the non-uniformed cash balance pension plan by transferring the assets to the borough's general fund or offset future municipal contributions until the unallocated reserve fund is depleted.

We also recommend that, in the future, plan officials reconcile the amount of contributions made to the pension plan with the pension plan's annual defined contribution pension costs.

Management's Response: Municipal officials agreed with the finding without exception. Furthermore, Borough officials have reached out to PMRS to resolve excess contribution amounts.

Auditor's Conclusion: Based on the management response, it appears municipal officials intend to comply with the finding recommendation. Compliance will be evaluated during the next audit of the plan.

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

Condition: The borough's accounting/reporting system did not provide effective control over the transactional activity of the pension plan during the year 2021. 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 2021.

FOUNTAIN HILL BOROUGH NON-UNIFORMED CASH BALANCE 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 2021 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 recently 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. In addition, the custodian has taken active measures to resolve these issues and expects 2021 financial reports to be distributed before the end of 2022. Compliance with the finding recommendation will be evaluated during our next audit of the plan.

FOUNTAIN HILL BOROUGH NON-UNIFORMED CASH BALANCE PENSION PLAN
SUMMARY OF DEPOSITED STATE AID AND EMPLOYER CONTRIBUTIONS

Year Ended December 31	State Aid	Employer Contributions
2018	None	\$ 156
2019	None	1,966
2020	None	6,094*
2021	None	10,530*

** It was noted that the borough made contributions in excess of contributions required to fund the plan during 2020 and 2021 (refer to Finding No. 1 of this report).*

FOUNTAIN HILL BOROUGH NON-UNIFORMED CASH BALANCE PENSION PLAN
REPORT DISTRIBUTION LIST

This report was initially distributed to the following:

The Honorable Tom W. Wolf
Governor
Commonwealth of Pennsylvania

The Honorable Michael Johnson
Mayor

Mr. Norman E. Blatt Jr.
Council President

Mr. Eric C. Gratz
Chief Administrative Officer

Ms. Cordula Voges
Finance Director

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

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