

COMPLIANCE AUDIT

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

January 2024



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
Freeport Borough
Armstrong County
Freeport, PA 16229

We have conducted a compliance audit of the Freeport 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 findings 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 findings 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 also tested individual employee contributions for all three active employees employed during the audit period amounting to \$9,288, \$4,588, \$4,721, \$4,851, and \$4,968, for the years 2018, 2019, 2020, 2021, and 2022, respectively, made during the audit period.
- We determined whether retirement benefits calculated for the plan member who retired during the current audit period represents 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 monthly pension benefits due to the retired individual and comparing these amounts to supporting documentation evidencing amounts determined and actually paid to the recipient.
- 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 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.

The Freeport 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 Freeport 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.

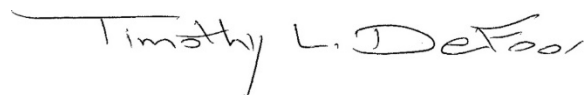
The results of our procedures indicated that, in all significant respects, the Freeport Borough Non-Uniformed Pension Plan was administered in compliance with applicable state laws, regulations, contracts, administrative procedures, and local ordinances and policies, except as noted in the following 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 – Noncompliance With Prior Recommendation – Failure To Implement Professional Services Contract Provisions Of Act 205

Finding No. 2 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 correct this previously reported finding and strongly encourage timely implementation of the recommendation 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 Freeport 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
December 28, 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 two 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 Freeport 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 Freeport Borough Non-Uniformed Pension Plan is a single-employer cash balance pension plan locally controlled by the provisions of Ordinance No. 409, effective July 1, 2020, and a separately executed plan agreement with the plan custodian adopted pursuant to Act 15. Prior to July 1, 2020, the plan was locally controlled by the provisions of Ordinance No. 369 and an agreement with the plan custodian also adopted pursuant to Act 15. The plan is also affected by the provisions of collective bargaining agreements between the borough and its non-uniformed employees. The plan was established January 1, 1987. Active members are required to contribute five percent of compensation to the plan. The municipality is required to contribute five percent of compensation. As of December 31, 2022, the plan had two active members, one terminated member eligible for vested benefits in the future, and one retiree receiving pension benefits.

FREEPORT BOROUGH NON-UNIFORMED PENSION PLAN
STATUS OF PRIOR FINDINGS

Compliance With Prior Recommendation

Freeport Borough has complied with the prior recommendation concerning the following:

- Failure To Deposit The Full Amount Of State Aid Into An Eligible Pension Plan

On October 15, 2018, the borough deposited \$466 of state aid into the borough's police pension plan.

Partial Compliance With Prior Recommendation

Freeport 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 \$8,476 to the Commonwealth for the excess state aid received during 2015 and 2017; however, plan officials again failed to reconcile the borough's state aid allocation with the plan's annual pension costs, as further discussed in the Findings and Recommendations section of this report.

Noncompliance With Prior Recommendation

Freeport Borough has not complied with the prior recommendation concerning the following as further discussed in the Findings and Recommendations section of this report:

- Failure To Implement Professional Services Contract Provisions Of Act 205

FREEPORT 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 Findings section of this report, the borough partially complied with the prior recommendation by returning the excess state aid received during the years 2015 and 2017. However, a similar condition occurred during the current audit period. Municipal officials again failed to reconcile the annual state aid allocation with the plan’s annual pension costs for the year years 2018 and 2019, as illustrated below:

	<u>2018</u>	<u>2019</u>
State aid allocation	\$ 7,694	\$ 7,119
Actual municipal pension costs	(6,956)	(4,588)
Excess state aid	\$ 738	\$ 2,531

The excess state aid remained in the general fund as of completion of our audit procedures.

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: The borough again failed to implement consistent procedures to annually reconcile the borough’s state aid allocation received and allocated to the pension plan with the plan’s annual pension costs. *(It was noted during conduct of the engagement that the borough did not calculate pension costs based on total compensation as defined by the plan’s governing document (i.e., W-2 amounts excluding bonuses, incentives, longevity, and etc.), but correctly certified total W-2 compensation in accordance with the instructions accompanying the annual AG 385 certification forms which may have contributed to the excesses noted in the Condition above).*

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 years 2018 and 2019 must be returned to the Commonwealth for redistribution.

FREEPORT BOROUGH NON-UNIFORMED PENSION PLAN
FINDINGS AND RECOMMENDATIONS

Finding No. 1 – (Continued)

Furthermore, the borough’s future state aid allocations may be withheld until the finding recommendation is complied with.

Recommendation: We recommend that the municipality return the \$3,269 of excess state aid received in the years 2018 and 2019 to the Commonwealth. (*Auditor’s Note: Prior to the return of excess state aid, the borough should consult with its solicitor and plan administrator and determine whether contributions made to members’ accounts during 2018 and 2019 were made in accordance with contributory requirements established in the plan’s governing document and make any necessary adjustments, if warranted, prior to returning the excess state aid.*) 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, 321 Finance Building, Harrisburg, PA 17120. A copy of the interest calculation must be submitted along with evidence of payment.

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: Due to the potential withhold of state aid, 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 plan.

Finding No. 2 – Noncompliance With Prior Recommendation – Failure To Implement Professional Services Contract Provisions Of Act 205

Condition: As disclosed in the prior report, municipal officials have not adopted the mandatory provisions regarding professional services contracts under Act 205.

Criteria: Section 701-A of Act 205, as amended by Act 44 of 2009, 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.

FREEPORT BOROUGH 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.

Cause: Plan officials again failed to implement procedures to ensure compliance with provisions of Act 205 as previously recommended.

Effect: The failure to implement and follow the provisions stipulated in Act 205 regarding the procurement of professional investment and advisory services for the borough's pension plan could result in a lack of transparency over actions taken by plan officials relative to the awarding of contracts for investment and advisory services contract for the borough's pension plan.

FREEPORT BOROUGH NON-UNIFORMED PENSION PLAN
FINDINGS AND RECOMMENDATIONS

Finding No. 2 – (Continued)

Recommendation: We again recommend that municipal officials obtain a comprehensive understanding of Act 205 and develop and implement procedures for the procurement of professional services for the borough's pension plan to ensure compliance with provisions stipulated in Act 205.

Management's Response: Municipal officials agreed with the finding without exception and again, indicated they would implement a resolution that adopts the Act 44 procedures at their earliest opportunity.

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

FREEPORT BOROUGH NON-UNIFORMED PENSION PLAN
POTENTIAL WITHHOLD OF STATE AID

Finding No. 1 contained in this audit report cites an overpayment of state aid to the borough in the amount of \$3,269, plus interest. A condition of a repeat finding 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.

FREEPORT 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	\$ 9,019	\$ 9,019	\$ -	\$ 178,378	5.06%
2015	8,091	7,998	93	159,808	5.00%
2016	7,681	7,681	-	151,627	5.07%
2017	7,599	1,796	5,803	149,970	1.20%
2018	6,957	3,571	3,386	137,539	2.60%
2019	4,668	6,717	(2,049)	91,754	7.32%
2020	4,801	4,801	-	94,424	5.08%
2021	4,930	4,931	(1)	97,013	5.08%
2022	4,968	4,968	-	***	***

* 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 SRC and the actual Contributions in Relation to the SRC were provided by the custodian. Deviation between these amounts may be due to contributions to or transfers from the municipal reserve account.

In 2017, the borough met the plan's \$7,599 funding requirement through the deposit of \$512 in state aid and allocation of \$7,087 in terminated employee forfeitures.

In 2018 and 2019, the net deficiency was a timing difference due to the deposit of 2018 contributions during 2019.

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

FREEPORT 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 Zachary Gent
Mayor

Mr. Clint Warnick
Council President

Mr. Zachary Filous
Borough Manager

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.