

COMPLIANCE AUDIT

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

November 2020



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
www.PaAuditor.gov**

**EUGENE A. DePASQUALE
AUDITOR GENERAL**

Board of Township Supervisors
Smithfield Township
Monroe County
East Stroudsburg, PA 18301

We have conducted a compliance audit of the Smithfield 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.

- 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 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 retired during the current audit period, and through the completion of our field work 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 monthly 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, 2017 and January 1, 2019 actuarial valuation reports were prepared and submitted by March 31, 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.

The Smithfield Township 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.

Township officials are responsible for establishing and maintaining effective internal controls to provide reasonable assurance that the Smithfield 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 Smithfield 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 – Receipt Of State Aid In Excess Of Entitlement
- Finding No. 2 – Failure To Properly Fund Member Accounts
- Finding No. 3 – Incorrect Data On Certification Form AG 385 Resulting In An Underpayment Of State Aid
- Finding No. 4 – Failure To Maintain An Adequate Record-Keeping System To Effectively Monitor Activity Of The Pension Plan

The contents of this report were discussed with officials of Smithfield 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 30, 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 Smithfield 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 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 Smithfield Township Non-Uniformed Pension Plan is a single-employer cash balance pension plan locally controlled by the provisions of Ordinance No. 213, and a separately executed plan agreement, adopted pursuant to Act 15. The plan is also affected by the provisions of collective bargaining agreements between the township and its non-uniformed employees. The plan was established June 26, 1984. Active members are not required to contribute to the plan, but may optionally contribute up to, but not to exceed, 20 percent of compensation. The municipality is required to contribute \$3,000 per member for 2016, \$3,313 per member for 2017, \$3,500 per member for 2018 and \$3,771 per member for 2019. As of December 31, 2019, the plan had 7 active members, 1 terminated member eligible for vested benefits in the future, and 3 retirees receiving pension benefits.

SMITHFIELD TOWNSHIP NON-UNIFORMED PENSION PLAN
FINDINGS AND RECOMMENDATIONS

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

Condition: The township received state aid in excess of the non-uniformed pension plan’s defined contribution pension costs in the years 2017 and 2018, as illustrated below:

	<u>2017</u>	<u>2018</u>
State aid allocation	\$ 26,475	\$ 25,468
Actual municipal pension costs	<u>(25,593)</u>	<u>(23,992)</u>
Excess state aid*	<u>\$ 882</u>	<u>\$ 1,476</u>

** State aid overpayments totaling \$2,198 remained in the township’s general fund as of the date of this report.*

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 establish adequate internal control procedures to reconcile the township’s annual state aid allocation with the plan’s actual defined contribution 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 years 2017 and 2018 must be returned to the Commonwealth for redistribution.

Recommendation: We recommend that the municipality return the \$2,358 of excess state aid received in the years 2017 and 2018 to the Commonwealth. 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.

SMITHFIELD TOWNSHIP NON-UNIFORMED PENSION PLAN
FINDINGS AND RECOMMENDATIONS

Finding No. 1 – (Continued)

Furthermore, we recommend that, in the future, plan officials reconcile the township’s annual state aid allocation with the plan’s annual defined contribution 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 will be evaluated during our next audit of the plan.

Finding No. 2 – Failure To Properly Fund Member Accounts

Condition: The borough did not properly fund the accounts of members during 2016 and 2017, in accordance with the plan document as illustrated below:

<u>2016 Employees</u>	<u>Required Contributions</u>	<u>Actual Contributions</u>	<u>Contributions Due/(Excess)</u>
1	\$ 1,030	\$ 1,500	\$ (470)
2	1,141	1,500	(359)
		Total	<u>\$ (829)</u>
<u>2017 Employees</u>	<u>Required Contributions</u>	<u>Actual Contributions</u>	<u>Contributions Due/(Excess)</u>
1	\$ 1,430	\$ 1,500	\$ (70)
2	972	1,500	(528)
3	3,313	2,250	1,063
		Total	<u>\$ 465</u>

In addition, it was also noted that although the township contributed \$25,593 towards participants’ pension costs during 2017 (*refer to Finding No. 1*), the township only actually allocated \$23,250 to individual members’ accounts according to custodial statements resulting in a shortage to 6 additional members’ accounts amounting to \$1,878 (\$2,343 (\$25,593-\$23,250) less the \$465 overall shortage from above table or \$313 per member for the 6 additional members) for 2017.

SMITHFIELD TOWNSHIP NON-UNIFORMED PENSION PLAN
FINDINGS AND RECOMMENDATIONS

Finding No. 2 – (Continued)

Criteria: Section 9.1 of the separately executed plan agreement adopted by Ordinance No. 213, states in part:

- (a) The Municipality shall contribute three hundred seventy-five dollars (\$375) to each Member's Accounts per quarter in accordance with the Board's policy regarding the treatment of member contributions.
- (b) For Members who so not earn Credited Service for the full quarter, the Municipality shall contribute an amount equal to a proportion of the Member's actual Credited Service earned during the quarter.
- (c) The Municipality may annually elect to contribute at a higher amount in future years by adopting a resolution and filing a copy of it with the Board.

For 2016, the township elected to increase annual required contributions to \$3,000 per plan member by adopting Resolution 378 of 2015 and further increased contributions to \$3,313 for plan members during 2017 through Resolution 406 of 2018.

Cause: Plan officials were unaware of the provision in the plan document that required contributions to members be prorated to certain members based on service credit earned during 2016 and 2017. In addition, the township lacked adequate procedures to ensure that members' accounts are accurately funded in accordance with the plan's governing document.

Effect: The failure to properly fund the members' accounts could result in plan members being denied benefits to which they are entitled in accordance with the plan's governing document. In addition, due to the township's failure to properly fund the accounts of several members, the township must now include interest on the delinquent contributions.

Furthermore, due to the township's failure to properly fund members' accounts, an unallocated reserve fund in the amount of \$826 at January 1, 2016 increased to a reserve fund in the amount of \$4,938 at December 31, 2018 (*2019 statements were unavailable as described in Finding No. 4*), as illustrated by the following:

SMITHFIELD TOWNSHIP NON-UNIFORMED PENSION PLAN
FINDINGS AND RECOMMENDATIONS

Finding No. 2 – (Continued)

	<u>2016</u>	<u>2017</u>	<u>2018</u>
Unallocated reserve fund at January 1	\$ 826	\$ 808	\$ 3,936
Excess municipal contributions	828	-	-
Excess state aid <i>(deposited, but unallocated see Finding 1)</i>	-	160	-
Unallocated state aid due to members' accounts	-	2,343	-
Allocated reserves to members	(1,485)	(28)	(476)
Interest earned on reserve funds	819	833	1,678
Transfers for admin expense	<u>(180)</u>	<u>(180)</u>	<u>(200)</u>
Unallocated reserve fund at December 31	<u>\$ 808</u>	<u>\$ 3,936</u>	<u>\$ 4,938</u>

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

Recommendation: We recommend that the township review the applicable members' accounts and make the adjustments deemed necessary to ensure they are properly funded and/or allocations correctly made (2017) in accordance with the provisions contained in the plan's governing document.

We also recommend that in the future, plan officials implement adequate internal control procedures to ensure that the members' accounts are properly funded in accordance with the provisions contained in the plan's governing document.

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.

SMITHFIELD TOWNSHIP NON-UNIFORMED PENSION PLAN
FINDINGS AND RECOMMENDATIONS

Finding No. 3 – Incorrect Data On Certification Form AG 385 Resulting In An Underpayment Of State Aid

Condition: The township failed to certify an eligible non-uniformed employee (1 unit) and understated payroll by \$30,769 on the Certification Form AG 385 filed in 2019. Plan officials failed to include an employee, who terminated employment during August 2018, but met the qualifications under Act 205 and the instructions accompanying Form AG 385 for certification purposes. The data contained on this certification form is based on prior calendar year information.

Criteria: Pursuant to Act 205, at Section 402(e)(2), an employee who has been employed on a full-time basis for at least six consecutive months and has been participating in a pension plan during the certification year is eligible for certification. Additionally, the instructions accompanying Certification Form AG 385 prescribes the following criteria for certification purposes:

Each Non-Uniformed Employee MUST meet each of these conditions anytime between January 1st and December 31st of the *prior calendar year*:

- a. Be an active, full-time non-uniformed employee employed by the municipality.
- b. Be employed for any six (6) consecutive months during the *prior calendar year*.
- c. Work not less than 35 hours per week.
- d. Be a member of a non-uniformed employee pension plan and meet all of its requirements.

Cause: Plan officials failed to establish adequate internal control procedures, such as having another individual review the accuracy of the data certified, to assist in accurately reporting the required pension data prior to submission.

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 plans. Because the township’s state aid allocation was based on pension costs, the township received an underpayment of state aid as identified below:

<u>Year</u>	<u>Type Of Plan</u>	<u>Normal Cost</u>	<u>Payroll Understated</u>	<u>State Aid Underpayment</u>
2019	Non-Uniformed	7.5%	\$ 30,769	\$ 2,308

It should be noted however, that since only \$2,085 in general fund contributions was needed to cover the plan’s pension costs for 2019, the township’s entitlement for additional state aid will be limited to \$2,085 towards its eligible pension costs.

SMITHFIELD TOWNSHIP NON-UNIFORMED PENSION PLAN
FINDINGS AND RECOMMENDATIONS

Finding No. 3 – (Continued)

Although the township will be reimbursed for the underpayment of state aid due to the township's certification error, the full amount of the 2019 state aid allocation was not available to be deposited timely and therefore resulted in the township having to make additional municipal contributions in order to meet the plan's funding obligation.

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.

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

Finding No. 4 – Failure To Maintain An Adequate Record-Keeping System To Effectively Monitor Activity Of The Pension Plan

Condition: The township's record-keeping system did not provide effective control over the transactional activity of the non-uniformed pension plan during 2019. Municipal officials were unable to furnish annual financial statements or custodial account transaction statements for the non-uniformed pension plan. These annual financial and account statements have historically been provided by the plan's custodian, PMRS. However, as of the date of this report, annual financial and accounting statements summarizing the pension account activity have not been provided for the year 2019.

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 indicated that the plan's custodian, PMRS, failed to provide copies of the custodial account transaction statements summarizing activity of the pension plan account for the year 2019. In addition, 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.

SMITHFIELD TOWNSHIP NON-UNIFORMED PENSION PLAN
FINDINGS AND RECOMMENDATIONS

Finding No. 4 – (Continued)

Effect: Although we were able to obtain alternate documentation from the municipality to evidence the propriety of the individual transactions tested during performance of the audit for the year 2019, the failure to maintain annual financial and/or account transaction statements prohibits municipal officials from effectively monitoring the plan’s financial operations. Additionally, inadequate monitoring of the pension plan account could lead to undetected errors or improprieties in account transactions as well as deficiencies in authorizing and implementing pension plan policies and procedures.

Recommendation: We recommend that municipal officials contact the plan custodian and obtain annual financial statements of the custodial account of the non-uniformed pension plan for the year 2019 to ensure the accuracy and propriety of the transaction activity. In addition, we recommend that municipal officials establish and maintain a financial record-keeping 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.

Management’s Response: Management agreed with the finding.

Auditor’s Conclusion: PMRS has indicated that they are in the process of preparing 2019 Year-End Financial Activity Reports and Annual Member Statements for all municipalities. PMRS has also indicated that they recently went through a substantial upgrade to the plan administration software and implemented a new accounting system. This transition in addition to disruptions in normal government operation due to COVID-19 has resulted in a three to four month delay in the 2019 year-end reporting process. Compliance with the finding recommendation will be evaluated during our next audit of the plan.

SMITHFIELD TOWNSHIP NON-UNIFORMED PENSION PLAN
 SUPPLEMENTARY INFORMATION
 (UNAUDITED)

SCHEDULE OF CONTRIBUTIONS

Year Ended December 31	Statutorily Determined Contribution (SRC)*	Contributions in Relation to the SRC*	Contribution Deficiency (Excess)**	Covered- Employee Payroll	Contributions as a Percentage of Covered- Employee Payroll
2014	\$ 10,889	\$ 10,889	\$ -	\$ 300,786	3.62%
2015	24,160	24,002	158	325,306	7.38%
2016	24,160	23,343	817	318,217	7.34%
2017	23,410	25,725	(2,315)	359,483	7.16%
2018	24,191	23,534	657	380,661	6.18%
2019	29,957	28,151	1,806	***	

* The Statutorily Required Contribution 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. Deviations between these amounts may be due to or transfers from the municipal reserve account.

*** Due to the timing of this audit, covered-employee payroll for 2019 was not provided in this schedule.

SMITHFIELD 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. Brian Barrett
Chairman, Board of Township Supervisors

Ms. Terri Timko
Assistant Secretary

Ms. Charity Rosenberry, CPA
Pennsylvania Municipal Retirement System

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