

COMPLIANCE AUDIT

Southampton Township Non-Uniformed Pension Plan Cumberland County, Pennsylvania For the Period January 1, 2018 to December 31, 2021

February 2023



Commonwealth of Pennsylvania
Department of the Auditor General

Timothy L. DeFoor • Auditor General



**Commonwealth of Pennsylvania
Department of the Auditor General
Harrisburg, PA 17120-0018
Facebook: Pennsylvania Auditor General
Twitter: @PAAuditorGen
www.PaAuditor.gov**

**TIMOTHY L. DEFOOR
AUDITOR GENERAL**

Board of Township Supervisors
Southampton Township
Cumberland County
Shippensburg, PA 17257

We have conducted a compliance audit of the Southampton Township Non-Uniformed Pension Plan for the period January 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 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 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, 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, 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 Southampton 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 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.

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

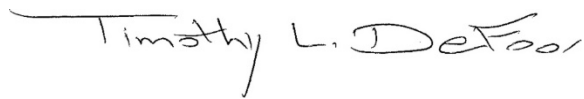
The results of our procedures indicated that, in all significant respects, the Southampton Township Non-Uniformed Pension Plan was administered in compliance with applicable state laws, regulations, contracts, administrative procedures, and local ordinances and policies, except as noted in the following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

- Finding No. 1 – Partial Compliance With Prior Recommendation – Incorrect Data On Certification Form AG 385 Resulting In An Overpayment Of State Aid
- Finding No. 2 – Partial Compliance With Prior Recommendation – Receipt Of State Aid In Excess Of Entitlement And Municipal Contributions Made In Excess Of Contributions Required To Fund The Plan
- Finding No. 3 – Failure To Implement Mandatory Act 44 Procedures For The Procurement Of Professional Services

Finding No. 1 and Finding No. 2, contained in this audit report repeat conditions that were cited in our previous report that have not been corrected by township officials. We are concerned by the township's failure to correct these previously reported findings 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 Southampton 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.



Timothy L. DeFoor
Auditor General
January 26, 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 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 Southampton 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.
- 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 Southampton Township Non-Uniformed Pension Plan is a single-employer cash balance pension plan locally controlled by the provisions of Ordinance No. 2020-2, effective January 1, 2020, and a separately executed plan agreement with the plan custodian, adopted pursuant to Act 15. Prior to January 1, 2020, the plan was locally controlled by the provisions of Ordinance No. 98-02 and an agreement, also adopted pursuant to Act 15. The plan was established January 1, 1992. 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, 2021, the plan had eight active members, three terminated members eligible for vested benefits in the future, and nine retirees receiving pension benefits.

SOUTHAMPTON TOWNSHIP NON-UNIFORMED PENSION PLAN
STATUS OF PRIOR FINDINGS

Partial Compliance With Prior Recommendations

Southampton Township has partially complied with the prior recommendations concerning the following:

- Incorrect Data On Certification Form AG 385 Resulting In An Overpayment Of State Aid

During the current audit period, the township reimbursed the overpayment of state aid for 2015 and 2016, with interest, to the Commonwealth; however, plan officials again failed to comply with the instructions that accompany Certification Form AG 385 to assist them in accurately reporting the required pension data as further discussed in the Findings and Recommendations section of this report; and

- Receipt Of State Aid In Excess Of Entitlement And Municipal Contributions Made In Excess Of Contributions Required To Fund The Plan

During the current audit period, the township returned the excess state aid for 2014 and 2015, with interest, to the Commonwealth, however, plan officials again failed to reconcile the amount of state aid allocated to the pension plan with the pension plan's pension cost amounts and/or liquidate the unallocated reserve funds, as further discussed in the Findings and Recommendations section of this report.

SOUTHAMPTON TOWNSHIP NON-UNIFORMED PENSION PLAN
FINDINGS AND RECOMMENDATIONS

Finding No. 1 – Partial Compliance With Prior Recommendation – Incorrect Data On Certification Form AG 385 Resulting In An Overpayment Of State Aid

Condition: As disclosed in the Status of Prior Findings section of this report, the township partially complied with the prior audit recommendation by reimbursing the Commonwealth for the overpayment of state aid received during 2015 and 2016; however, plan officials again failed to comply with the instructions that accompany Certification Form AG 385 to assist them in accurately reporting the required pension data in the years 2018, 2019, 2020, 2021 and 2022. The township overstated payroll by \$1,875, \$1,875, \$2,500, \$2,500, and \$2,500 on the Certification Form AG 385s filed in 2018, 2019, 2020, 2021 and 2022, respectively, by including supervisor meeting pay. The data contained on these certification forms 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 again failed to implement adequate internal control procedures, such as having another individual review the data certified, to ensure the accuracy of the reported data and compliance with the prior recommendation.

Effect: The data submitted on these certification forms is used, in part, to calculate the state aid due to the municipality for distribution to its pension plan. Because the township’s state aid allocations were based on pension costs, the incorrect certification of pension data affected the township’s state aid allocations, as identified below:

<u>Year</u>	<u>Normal Cost</u>	<u>Payroll Overstated</u>	<u>State Aid Overpayment</u>
2018	10.00%	\$ 1,875	\$ 188
2019	10.00%	1,875	188
2020	10.00%	2,500	250
2021	10.00%	2,500	250
2022	10.00%	2,500	<u>250</u>
Total Overpayment Of State Aid			<u><u>\$ 1,126</u></u>

SOUTHAMPTON TOWNSHIP NON-UNIFORMED PENSION PLAN
FINDINGS AND RECOMMENDATIONS

Finding No. 1 – (Continued)

In addition, the township used the 2018-2020 and 2022 overpayments of state aid to pay the minimum municipal obligations (MMOs) due to the non-uniformed pension plan; therefore, if the reimbursement to the Commonwealth is made from the pension plan, the plan's MMOs will not be fully paid. For 2021, the excess state aid remained in the general fund (*refer to Finding No. 2*).

Recommendation: We recommend that the total excess state aid, in the amount of \$1,126, plus interest, be returned 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 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.

We also recommend that in the future, plan officials establish adequate internal control procedures, such as having at least two 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.

In addition, if the reimbursement to the Commonwealth is made from pension plan funds, we recommend that any resulting MMO deficiencies be paid to the pension plan with interest, at a rate earned by the pension plan.

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.

SOUTHAMPTON TOWNSHIP NON-UNIFORMED PENSION PLAN
FINDINGS AND RECOMMENDATIONS

Finding No. 2 – Partial Compliance With Prior Recommendation – Receipt Of State Aid In Excess Of Entitlement And Municipal Contributions Made In Excess Of Contributions Required To Fund The Plan

Condition: As disclosed in the Status of Prior Findings section of this report, the township partially complied with the prior recommendation by returning the excess state aid for 2014 and 2015, with interest, to the Commonwealth. However, a similar condition occurred during the current audit period. The township again failed to reconcile the amount of state aid received and allocated to the pension plan with the pension plan’s defined contribution pension costs for full-time plan members during the year 2021, as illustrated below:

State aid allocation		\$ 38,205
Actual municipal pension costs		<u>(37,857)</u>
Overpayment of State Aid (<i>see Finding No. 1</i>)		<u>(250)</u>
Excess state aid		<u><u>\$ 98</u></u>

In addition, it was also previously recommended that the township liquidate the unallocated reserve fund (\$37,662 as of December 31, 2017) maintained by the pension plan by transferring the assets representing nonstate aid funds, to the township’s general fund. Although, the township did not deposit additional contributions in excess of contributions required to fund the pension plan during the current audit period, the township again failed to liquidate the funds in the unallocated reserve fund as recommended in the prior audit, and there remains an unallocated municipal reserve fund balance amounting to \$35,427 as of December 31, 2021.

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 (full-time) 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.

SOUTHAMPTON TOWNSHIP NON-UNIFORMED PENSION PLAN
FINDINGS AND RECOMMENDATIONS

Finding No. 2 – (Continued)

In addition, Section 12 of the plan agreement states:

The Township will contribute quarterly ten percent (10%) of each member's compensation to the System.

Furthermore, Section 13 of the plan agreement states:

In the event a member's service with the Township is terminated for any reason whatsoever before the funds set aside for such member are vested or if the member elects not to receive a benefit, then the amount of such funds which have not been contributed by the member and which are not vested shall be credited against the next contribution due from the Township for the remaining or future members of this Plan.

Since state aid allocated to a pension plan must be expended on pension costs, it is the opinion of this department that where municipal contributions and state aid are both deposited into a pension plan, the state aid is expended first to fund pension costs.

Cause: The township again failed to establish consistent internal control procedures to annually reconcile the township's state aid allocation with the plan's actual defined contribution pension costs for plan members. Also, the township indicated that since no funds were owed to the plan, the township decided to leave the excess in the unallocated reserve account to cover any future shortfalls of funds.

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 year 2021 must be returned to the Commonwealth for redistribution.

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 at this time. Additionally, maintaining excess municipal funds in an unallocated account within the pension plan is not an appropriate use of general taxpayer money that could have been used for other general municipal government purposes.

SOUTHAMPTON TOWNSHIP NON-UNIFORMED PENSION PLAN
FINDINGS AND RECOMMENDATIONS

Finding No. 2 – (Continued)

Recommendation: We recommend that, in addition to the return of excess state aid resulting from Finding No.1 contained in this report, the municipality return an additional \$98 of excess state aid received during 2021 to the Commonwealth. A check in this amount, *along with the amount disclosed in Finding No. 1*, 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

We also again recommend that the township liquidate the unallocated reserve fund maintained by the non-uniformed pension plan by transferring the assets which represent nonstate aid funds, to the township’s general fund. In addition, any interest income earned on assets held in the reserve fund to the date of transfer should also be transferred to the general fund.

Furthermore, we again recommend that, in the future, plan officials implement consistent procedures to reconcile the township’s annual state aid allocation and municipal contributions made to the pension plan 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. 3 – Failure To Implement Mandatory Act 44 Procedures For The Procurement Of Professional Services

Condition: As disclosed as a verbal observation during the prior engagement, municipal officials failed to adopt the mandatory provisions of Act 205 regarding professional services contracts.

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.

SOUTHAMPTON TOWNSHIP NON-UNIFORMED PENSION PLAN
FINDINGS AND RECOMMENDATIONS

Finding No. 3 – (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 failed to establish adequate internal controls procedures to ensure compliance with provisions of Act 205 as previously recommended.

Effect: The township's failure to comply in all respects with the previous recommendation and the provisions stipulated in Act 205 regarding the procurement of professional investment and advisory services for the township's pension plan could result in a general lack of overall transparency of the actions taken by plan officials relative to the awarding of the investment and advisory services contract for the township's pension plan.

SOUTHAMPTON TOWNSHIP NON-UNIFORMED PENSION PLAN
FINDINGS AND RECOMMENDATIONS

Finding No. 3 – (Continued)

Recommendation: We recommend that municipal officials obtain a comprehensive understanding of Act 205 provisions for the procurement of professional services and develop and implement formal written procedures to ensure compliance with these provisions which include maintaining appropriate and sufficient supporting documentation evidencing every phase of the process in the awarding of future professional services contracts for the pension plan, including authorizations/approvals of township officials in the official minutes of formal board meetings and the required notifications and disclosure responsibilities to ensure the transparency of the actions taken by plan officials relative to the awarding of such professional services contracts.

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

Auditor's Conclusion: Compliance will be evaluated during our next engagement of the plan.

SOUTHAMPTON TOWNSHIP 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	\$ 27,612	\$ 28,489	\$ (877)	\$ 216,529	13.16%
2015	24,301	27,331	(3,030)	240,006	11.39%
2016	24,226	27,231	(3,005)	239,454	11.37%
2017	25,280	25,300	(20)	249,996	10.12%
2018	26,918	20,754	6,164	266,181	7.80%
2019	33,738	33,738	-	334,856	10.08%
2020	38,585	38,585	-	382,054	10.10%
2021	37,857	37,857	-		

* 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 Contribution were provided by the custodian. Deviation between these amounts may be due to contributions to or transfers from the municipal reserve account.

*** Due to the timing of this audit, covered-employee payroll for 2021 was not provided in this schedule.

SOUTHAMPTON TOWNSHIP NON-UNIFORMED PENSION PLAN
REPORT DISTRIBUTION LIST

This report was initially distributed to the following:

The Honorable Joshua D. Shapiro
Governor
Commonwealth of Pennsylvania

Mr. Talon Landreth
Chairman, Board of Township Supervisors

Mr. Scott Mack
Township Manager

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

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