

# COMPLIANCE AUDIT

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## Rush Township Non-Uniformed Pension Plan Centre County, Pennsylvania For the Period January 1, 2011 to December 31, 2013

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October 2014



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  
Rush Township  
Centre County  
Philipsburg, PA 16866

We have conducted a compliance audit of the Rush Township Non-Uniformed Pension Plan for the period January 1, 2011 to December 31, 2013. The audit was conducted pursuant to authority derived from Section 402(j) of Act 205 and in accordance with the standards applicable to performance audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States. Those standards require that we plan and perform our 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 audit 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. Our methodology addressed determinations about the following:

- Whether state aid was properly determined and deposited in accordance with Act 205 requirements. State aid allocations that were deposited into the pension plan for the years ended December 31, 2008 to December 31, 2013, are presented on the Summary of Deposited State Aid and Employer Contributions.
- Whether employer contributions are determined and deposited in accordance with the plan's governing document and applicable laws and regulations. Employer contributions that were deposited into the pension plan for the years ended December 31, 2008 to December 31, 2013, are presented on the Summary of Deposited State Aid and Employer Contributions.

- Whether employee contributions are required and, if so, are determined, deducted, and deposited into the pension plan and are in accordance with the plan provisions and applicable laws and regulations.
- Whether benefit payments, if any, represent payments to all (and only) those entitled to receive them and are properly determined in accordance with applicable laws and regulations.
- Whether obligations for plan benefits are accurately determined in accordance with plan provisions and based on complete and accurate participant data; and whether actuarial valuation reports are prepared and submitted to the Public Employee Retirement Commission (PERC) in accordance with state law and 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.
- Whether the terms of the allocated insurance contract, including ownership and any restrictions, are in compliance with plan provisions, investment policies, and state regulations.

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. 25 of the Governmental Accounting Standards Board, allocated insurance contracts are excluded from the pension plan's assets. Consequently, the plan has no reportable assets.

Township officials are responsible for establishing and maintaining effective internal controls to provide reasonable assurance that the Rush Township Non-Uniformed Pension Plan is administered in compliance with applicable state laws, regulations, contracts, administrative procedures, and local ordinances and policies. In conducting our audit, we obtained an understanding of the township's internal controls as they relate to the township's compliance with those requirements and that we considered to be significant within the context of our audit objectives, and assessed whether those significant controls were properly designed and implemented. Additionally, we tested transactions, assessed official actions, performed analytical procedures, and interviewed selected officials 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 tests indicated that, in all significant respects, the Rush 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 Audit Recommendation -  
Receipt Of State Aid In Excess Of Entitlement

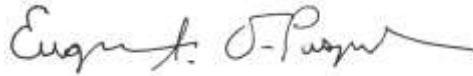
Finding No. 2 – Unauthorized Funding Mechanism

Finding No. 3 – Failure To Deposit The Full Amount Of State Aid Into The  
Pension Plan

Finding No. 4 – Failure To Properly Fund Members' Accounts

The contents of this report were discussed with officials of Rush 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.

August 21, 2014



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. Section 402(j) of Act 205 specifically requires the Auditor General, as deemed necessary, to make an audit of every municipality which receives general municipal pension system state aid and of every municipal pension plan and fund in which general municipal pension system state aid is deposited.

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 Rush Township Non-Uniformed Pension Plan is also governed by implementing regulations adopted by the Public Employee Retirement Commission published at Title 16, Part IV of the Pennsylvania Code and applicable provisions of various other state statutes.

The Rush Township Non-Uniformed Pension Plan is a single-employer defined contribution pension plan locally controlled by the provisions of a resolution dated July 8, 1999. The plan was established January 1, 1979. Active members choose their own dollar amount to contribute to the plan and the township matches the contribution of each employee. As of December 31, 2013, the plan had 2 active members, no terminated members eligible for vested benefits in the future, and no retirees receiving pension benefits.

RUSH TOWNSHIP NON-UNIFORMED PENSION PLAN  
STATUS OF PRIOR FINDINGS

Partial Compliance With Prior Audit Recommendations

Rush Township has partially complied with the prior audit recommendations concerning the following:

- Receipt Of State Aid In Excess Of Entitlement

Township officials returned \$394 of excess state aid received in 2009 and 2010 to the Commonwealth; however, plan officials failed to reconcile the amount of state aid allocated to the pension plan with the plan's actual defined contribution pension costs in 2012 and 2013, as further discussed in the Findings and Recommendations section of this report.

- Improper Ownership Of Allocated Insurance Contract

Municipal officials determined that ownership of the allocated insurance contract cannot be changed from the plan member to the pension plan or municipality without penalty to the plan member, and the township ceased making contributions to this account in 2012. The municipality then improperly purchased, and deposited state aid into, an individual retirement account (IRA) to provide benefits to the plan member at retirement, as further discussed in the Findings and Recommendations section of this report.

RUSH TOWNSHIP NON-UNIFORMED PENSION PLAN  
FINDINGS AND RECOMMENDATIONS

**Finding No. 1 – Partial Compliance With Prior Audit Recommendation - Receipt Of State Aid In Excess Of Entitlement**

Condition: As disclosed in the prior audit report, the township received state aid in excess of the non-uniformed pension plan’s defined contribution pension costs in the years 2009 and 2010. During the current audit period, municipal officials returned \$394 to the Commonwealth for the excess state aid received; however, plan officials failed to reconcile the township’s annual state aid allocation with the plan’s defined contribution pension costs in the years 2012 and 2013, as illustrated below:

	<u>2012</u>	<u>2013</u>
State aid allocation	\$ 3,964	\$ 3,915
Actual municipal pension costs	(3,120)	(3,640)
Excess state aid	\$ 844	\$ 275

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 state aid allocation with the plan’s actual defined contribution pension costs and ensure full compliance with the prior audit recommendation.

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 received in one year to offset pension costs in other years. Consequently, the overpayments of state aid received in the years 2012 and 2013, in the total amount of \$1,119, must be returned to the Commonwealth for redistribution.



RUSH TOWNSHIP NON-UNIFORMED PENSION PLAN  
FINDINGS AND RECOMMENDATIONS

**Finding No. 1 – (Continued)**

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

Recommendation: We recommend that the municipality return the \$1,119 of excess state aid received in the years 2012 and 2013 to the Commonwealth from the township's general fund. 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, 320 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 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 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 plan.

**Finding No. 2 – Unauthorized Funding Mechanism**

Condition: Our prior audit report included a finding that the township is funding an allocated insurance contract that improperly designates an individual plan member as the owner of the contract. During the current audit period, municipal officials determined that ownership of this contract cannot be changed from the plan member to the pension plan or municipality without penalty to the plan member, and the township ceased making contributions to this account in 2012. The municipality then improperly purchased, and deposited state aid into, an individual retirement account (IRA) to provide benefits to the plan member at retirement. This account also designates the individual plan member as the owner of the account.

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.

RUSH TOWNSHIP NON-UNIFORMED PENSION PLAN  
FINDINGS AND RECOMMENDATIONS

**Finding No. 2 – (Continued)**

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 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 an IRA was not an eligible funding vehicle for pension plans participating in the state aid program.

Effect: Since the IRA 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.

Regarding the allocated insurance contract, continued improper ownership of this annuity contract could result in premature withdrawals or other improper dispositions of the funds. Improper distribution from the insurance contract could result in the township having to reimburse the Commonwealth for any improper distribution to the plan member.

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

Recommendation: We recommend that municipal officials either transfer plan assets from the IRA to an eligible funding mechanism or return all state aid allocated to the unauthorized funding mechanism for the years 2012 and 2013, in the amount of \$5,200, 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, 320 Finance Building, Harrisburg, PA 17120. A copy of the interest calculation must be submitted along with the check.

RUSH TOWNSHIP NON-UNIFORMED PENSION PLAN  
FINDINGS AND RECOMMENDATIONS

**Finding No. 2 – (Continued)**

Regarding the allocated insurance contract, since the municipality has determined that ownership of this contract cannot be changed from the plan member to the pension plan or municipality without penalty to the plan member, we again recommend that the municipality implement adequate internal control procedures to ensure that the proceeds from the allocated insurance contract are not surrendered to the plan member prior to eligibility to receive benefits from the pension plan.

Management 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 plan.

**Finding No. 3 – Failure To Deposit The Full Amount Of State Aid Into The Pension Plan**

Condition: The municipality did not deposit the full amount of its 2013 state aid allocation into the pension plan. The municipality received its 2013 state aid allocation in the amount of \$3,915; however, only \$2,600 was deposited into the pension plan. As reported in Finding No. 1, \$275 of the township’s 2013 state aid allocation must be returned to the Commonwealth, leaving a balance of \$1,040 that must be deposited into the pension plan, specifically into the account of the member whose account was underfunded, as described in Finding No. 4.

Criteria: Section 402(g) of Act 205 states, in part:

. . . the total amount of the general municipal pension system State aid received by the municipality shall, within 30 days of receipt by the treasurer of the municipality, be deposited in the pension fund or the alternate funding mechanism applicable to the pension plan.

Cause: The full amount of the 2013 state aid was not deposited into the pension plan because internal control procedures were not in effect to ensure the deposit of the full amount of state aid.

Effect: When state aid is not deposited into a pension plan account, the funds are not available to pay operating expenses or for investment and the risk of misapplication is increased.

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

RUSH TOWNSHIP NON-UNIFORMED PENSION PLAN  
FINDINGS AND RECOMMENDATIONS

**Finding No. 3 – (Continued)**

Recommendation: We recommend that the municipality deposit the township's remaining state aid allocation of \$1,040, plus interest earned during the period beyond the 30 day grace period allowed by Act 205, compounded annually, into the account of the member whose account was underfunded, as described in Finding No. 4. A copy of the interest calculation must be maintained by the township for examination during our next audit of the plan.

We also recommend that plan officials develop and implement procedures to ensure that future state aid is deposited into the non-uniformed pension plan within 30 days of receipt by the municipal treasurer.

Management 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 plan.

**Finding No. 4 – Failure To Properly Fund Members' Accounts**

Condition: The township underfunded the account of one member in 2013 by \$1,040, and overfunded the account of another member in 2012 by \$200.

Criteria: The plan's governing resolution, dated July 8, 1999, states the township will equally match the contributions of the employee.

Cause: Plan officials failed to establish adequate internal control procedures to ensure that eligible plan members' accounts were properly funded in accordance with the provisions contained in the plan's governing document. In addition, the township failed to fully deposit its 2013 state aid allocation into the pension plan (See Finding No. 3).

Effect: The failure to properly fund the members' accounts could result in plan members being denied benefits to which they are entitled or granted benefits to which they were not entitled to in accordance with the plan's governing document.

Recommendation: We recommend that the township review the applicable members' accounts and make the adjustments deemed necessary (see Finding No. 3) to ensure they are funded in accordance with the provisions contained in the plan's governing document.

RUSH TOWNSHIP NON-UNIFORMED PENSION PLAN  
FINDINGS AND RECOMMENDATIONS

**Finding No. 4 – (Continued)**

We also recommend that 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.

RUSH TOWNSHIP 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 township in the amount of \$1,119. 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, 320 Finance Building, Harrisburg, PA 17120.

In addition, conditions such as those reported by Finding Nos. 2 and 3 contained in this audit report may lead to a total withholding of state aid in the future unless those findings are corrected. However, such action will not be considered if sufficient written documentation is provided to verify compliance with this Department's recommendations. Such documentation should be submitted to: Department of the Auditor General, Bureau of Municipal Pension & VFRA Audits, 316-D Finance Building, Harrisburg, PA 17120.

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

Year Ended December 31	State Aid	Employer Contributions
2008	\$ 525	\$ 2,645
2009	3,170	None
2010	2,870	None
2011	2,739	81
2012	3,120	200
2013	2,600	None

RUSH TOWNSHIP NON-UNIFORMED PENSION PLAN  
REPORT DISTRIBUTION LIST

This report was initially distributed to the following:

The Honorable Tom Corbett  
Governor  
Commonwealth of Pennsylvania

Rush Township Non-Uniformed Pension Plan  
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150 North Richard Street  
P.O. Box 152  
Philipsburg, PA 16866

Mr. John A. Shannon      Chairman, Board of Township Supervisors

Ms. Joan Cowher          Secretary

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