

COMPLIANCE AUDIT

West Chester Borough Non-Uniformed Defined Contribution Pension Plan Chester County, Pennsylvania For the Period January 1, 2019 to December 31, 2022

May 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
West Chester Borough
Chester County
West Chester, PA 19380

We have conducted a compliance audit of the West Chester Borough Non-Uniformed Defined Contribution Pension Plan for the period January 1, 2019 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. Employer contributions that were deposited into the pension plan for the years ended December 31, 2017 to December 31, 2022, are presented on the Summary of Deposited State Aid and Employer Contributions.
- 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 separated employment and received a lump-sum distribution during the current audit period, and through the completion of our fieldwork 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 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, January 1, 2019, and January 1, 2021 actuarial valuation reports were prepared and submitted by March 31, 2018, 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.

Borough officials are responsible for establishing and maintaining effective internal controls to provide reasonable assurance that the West Chester Borough Non-Uniformed Defined Contribution 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 West Chester Borough Non-Uniformed Defined Contribution 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:

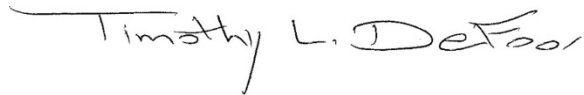
Finding No. 1 – Noncompliance With Prior Recommendation – Incorrect Data On Certification Form AG 385 Resulting In An Underpayment Of State Aid

Finding No. 2 – Noncompliance With Prior Recommendation – Improper Loan Provision Contained In The Plan’s Adoption Agreement

Finding No. 3 – Failure To Properly Fund Member Accounts

Finding Nos. 1 and 2 contained in this audit report repeat conditions that were cited in our previous report that have not been corrected by borough officials. We are concerned by the borough’s failure to correct those previously reported findings and strongly encourage timely implementation of the recommendations noted in this audit report.

The contents of this report were discussed with officials of West Chester 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
April 4, 2024

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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 West Chester Borough Non-Uniformed Defined Contribution 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.

The West Chester Borough Non-Uniformed Defined Contribution Pension Plan is a single-employer defined contribution pension plan locally controlled by the provisions of Ordinance No. 12-2013 and a separately executed plan agreement with the plan's custodian. The plan is also affected by the provisions of collective bargaining agreements between the borough and its non-uniformed employees. The plan was established October 16, 2013 for non-uniformed employees hired on or after January 1, 2013. Active members are not required to contribute to the plan. The municipality is required to contribute 5 percent of compensation to the plan. As of December 31, 2022, the plan had 28 active members and 44 terminated members eligible for vested benefits in the future.

WEST CHESTER BOROUGH NON-UNIFORMED DEFINED CONTRIBUTION
PENSION PLAN
STATUS OF PRIOR FINDINGS

Noncompliance With Prior Recommendations

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

- Incorrect Data On Certification Form AG 385 Resulting In A Net Underpayment Of State Aid
- Improper Loan Provision Contained In The Plan's Adoption Agreement

WEST CHESTER BOROUGH NON-UNIFORMED DEFINED CONTRIBUTION
PENSION PLAN
FINDINGS AND RECOMMENDATIONS

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

Condition: Our prior audit report disclosed that the borough reported incorrect data on the Certification Forms AG 385 filed in 2016, 2018, and 2019, resulting in a net underpayment of state aid in the amount of \$23,293. This amount was subsequently allocated to the borough in October 2019.

During and subsequent to the current audit period, the borough again failed to comply with the instructions that accompanied Certification Form AG 385 to assist them in accurately reporting the required pension data. The borough failed to certify two eligible non-uniformed employees (2 units) and understated payroll by \$75,646 on the Certification Form AG 385 filed in 2020. The borough also failed to certify an eligible police officer (2 units) and two eligible non-uniformed employees (2 units) and understated payroll by \$127,876 and \$80,260, respectively, on the Certification Form AG 385 filed in 2021. In addition, the borough failed to certify an eligible police officer (2 units) and four eligible non-uniformed employees (4 units) and understated payroll by \$145,586 and \$162,878, respectively, on the Certification Form AG 385 filed in 2023. The data contained on these certification forms 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.

Cause: The borough again failed to establish adequate internal control procedures, such as having another individual review the data certified, to ensure the accuracy of the reported data prior to submission and to ensure compliance with the prior audit 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 plans. Because the borough's state aid allocations were based on unit value, the borough received an underpayment of state aid in the amount of \$64,004 as identified below:

WEST CHESTER BOROUGH NON-UNIFORMED DEFINED CONTRIBUTION
PENSION PLAN
FINDINGS AND RECOMMENDATIONS

Finding No. 1 – (Continued)

| <u>Year</u> | <u>Type of Plan</u> | <u>Units Understated</u> | <u>Unit Value</u> | <u>State Aid Underpayment</u> |
|-------------|------------------------------------|------------------------------|---------------------------------|-----------------------------------|
| 2020 | Non-Uniformed Defined Contribution | 2 | \$ 4,924 | \$ 9,848 |
| 2021 | Police | 2 | \$ 4,797 | \$ 9,594 |
| | Non-Uniformed Defined Contribution | 2 | \$ 4,797 | 9,594 |
| | | | 2021 Subtotal | \$ 19,188 |
| 2023 | Police | 2 | \$ 5,828 | \$ 11,656 |
| | Non-Uniformed Defined Contribution | 4 | \$ 5,828 | 23,312 |
| | | | 2023 Subtotal | \$ 34,968 |
| | | | Total Underpayment of State Aid | \$ 64,004 |

Although the additional state aid will be allocated to the borough, the full amount of the 2020, 2021, and 2023 state aid allocations was not available to be deposited timely and therefore was not available to pay operating expenses or for investment.

Recommendation: We again recommend that 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.

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.

WEST CHESTER BOROUGH NON-UNIFORMED DEFINED CONTRIBUTION
PENSION PLAN
FINDINGS AND RECOMMENDATIONS

**Finding No. 2 – Noncompliance With Prior Recommendation – Improper Loan Provision
Contained In The Plan’s Adoption Agreement**

Condition: As previously disclosed in our two prior audit reports, Section Q of the pension plan’s adoption agreement, which was approved on June 26, 2013, improperly contains a provision that allows for loans to active plan members. In 2023, a loan was made to an active member of the plan.

Criteria: Section 102 of Act 205 contains the following definitions:

“Pension plan or system.” 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.

“Defined contribution pension plan.” A type of pension benefit plan which provides for a fixed contribution rate or amount and which provides for periodic benefit payments calculable at retirement dependent on the accumulated contributions, investment income, experience gains and losses credited to the member and the expected mortality of the member.

Therefore, Act 205 funding (state aid) is intended to provide retirement benefit payments, not for loans to be made to active plan members.

Cause: Plan officials again failed to adopt adequate internal control procedures to ensure compliance with this department’s prior audit recommendations.

Effect: The unauthorized loan provision violates the intent of Act 205, which is to only provide distributions to plan members upon their retirement or termination of employment with the municipality.

Recommendation: We again recommend that municipal officials take appropriate action to eliminate the unauthorized loan provision from the plan’s governing document and to limit future distributions to benefits authorized by Act 205.

WEST CHESTER BOROUGH NON-UNIFORMED DEFINED CONTRIBUTION
PENSION PLAN
FINDINGS AND RECOMMENDATIONS

Finding No. 2 – (Continued)

Management’s Response: The borough provided the following response:

We acknowledge that the plan document has a loan provision (Section 13 of the plan doc) referenced by Appendix B-1 of the adoption agreement updated and signed May 27, 2022. We have consulted with legal counsel and the plan actuary and affirm this finding. We are working with our plan provider, [firm name omitted], to issue a restatement of the plan that removes the plan loan provisions. We are also preparing an ordinance to affirm and restate the changes to the defined contribution plan. This should be completed by June or July of 2024.

Additionally, we are looking into resolving the loan that was issued to a plan participant in 2023 so that the plan comes into compliance.

Auditor’s Conclusion: Compliance will be evaluated during our next audit of the plan.

Finding No. 3 – Failure To Properly Fund Member Accounts

Condition: The borough failed to properly fund members’ accounts in the years 2019, 2020, 2021, and 2022, as illustrated below:

| <u>Employee Hire Date</u> | <u>2019 Required Contributions</u> | <u>2019 Actual Contributions</u> | <u>Contributions Due</u> |
|-------------------------------|--|--------------------------------------|------------------------------|
| 01/01/2018 (1) | \$ 1,753 | \$ 607 | \$ 1,146 |
| 01/01/2018 (2) | 2,029 | 703 | 1,326 |
| | | Total | <u>\$ 2,472</u> |

WEST CHESTER BOROUGH NON-UNIFORMED DEFINED CONTRIBUTION
PENSION PLAN
FINDINGS AND RECOMMENDATIONS

Finding No. 3 – (Continued)

| <u>Employee Hire Date</u> | <u>2020 Required Contributions</u> | <u>2020 Actual Contributions</u> | <u>Contributions Due (In Excess)</u> |
|-------------------------------|--|--------------------------------------|--|
| 01/01/2018 (1) | \$ 1,875 | \$ - | \$ 1,875 |
| 01/01/2018 (2) | 2,138 | - | 2,138 |
| 01/08/2018 | 4,660 | 4,838 | (178) |
| | | Total | <u>\$ 3,835</u> |

| <u>Employee Hire Date</u> | <u>2021 Required Contributions</u> | <u>2021 Actual Contributions</u> | <u>Contributions Due (In Excess)</u> |
|-------------------------------|--|--------------------------------------|--|
| 01/01/2018 (1) | \$ 1,859 | \$ 2,462 | \$ (603) |
| 01/01/2018 (2) | 2,038 | 2,159 | (121) |
| 10/15/2020 | 1,431 | 372 | 1,059 |
| | | Total | <u>\$ 335</u> |

| <u>Employee Hire Date</u> | <u>2022 Required Contributions</u> | <u>2022 Actual Contributions</u> | <u>Contributions Due (In Excess)</u> |
|-------------------------------|--|--------------------------------------|--|
| 01/01/2018 (1) | \$ 1,887 | \$ - | \$ 1,887 |
| 01/01/2018 (2) | 2,153 | - | 2,153 |
| 05/10/2021 | 72 | 87 | (15) |
| 05/31/2022 | 1,056 | 373 | 683 |
| 08/08/2020 | 644 | 138 | 506 |
| | | Total | <u>\$ 5,214</u> |

Criteria: The plan agreement, adopted by Ordinance No. 12-2013, contains the following employer contributions provision:

A discretionary amount to be allocated to each Participant’s Account in the same proportion that each such Participant’s Compensation for the Plan Year bears to the total Compensation of all Participants for such Plan year.

WEST CHESTER BOROUGH NON-UNIFORMED DEFINED CONTRIBUTION
PENSION PLAN
FINDINGS AND RECOMMENDATIONS

Finding No. 3 – (Continued)

In conjunction with that provision, the collective bargaining agreement set the contribution rate at five percent of employee pay. During the current audit period, the borough correctly contributed at this rate with the exceptions noted above.

Cause: Plan officials failed to establish adequate internal control procedures to ensure eligible plan members' accounts were properly funded in accordance with the provisions contained in the plan documents.

Effect: The failure to properly fund members' accounts has resulted in certain plan members receiving benefits in excess of those to which they are entitled, and other members being denied benefits to which they are entitled in accordance with the plan documents.

Furthermore, due to the failure to properly fund the accounts of several members, the borough must now pay interest on the delinquent contributions.

Recommendation: We recommend that the borough review members' accounts and make the adjustments deemed necessary to ensure they are funded in accordance with the provisions contained in the plan documents.

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

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.

WEST CHESTER BOROUGH NON-UNIFORMED DEFINED CONTRIBUTION
PENSION PLAN
SUMMARY OF DEPOSITED STATE AID AND EMPLOYER CONTRIBUTIONS

| Year Ended December 31 | State Aid | Employer Contributions |
|------------------------|-----------|------------------------|
| 2017 | None | \$ 74,889 |
| 2018 | None | 80,824 |
| 2019 | None | 94,061 |
| 2020 | None | 79,488 |
| 2021 | None | 94,089 |
| 2022 | None | 92,494 |

WEST CHESTER BOROUGH NON-UNIFORMED DEFINED CONTRIBUTION
PENSION PLAN
REPORT DISTRIBUTION LIST

This report was initially distributed to the following:

The Honorable Joshua D. Shapiro
Governor
Commonwealth of Pennsylvania

The Honorable Lillian DeBaptiste
Mayor

Mr. Patrick McCoy
Council President

Mr. Sean Metrick
Borough Manager

Ms. Barbara Lioni
Finance Director

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