

COMPLIANCE AUDIT

Covington Township Non-Uniformed Pension Plan Clearfield County, Pennsylvania For the Period January 1, 2019 to December 31, 2023

May 2024



Commonwealth of Pennsylvania
Department of the Auditor General

Timothy L. DeFoor • Auditor General



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**TIMOTHY L. DEFOOR
AUDITOR GENERAL**

Board of Township Supervisors
Covington Township
Clearfield County
Frenchville, PA 16836

We have conducted a compliance audit of the Covington Township Non-Uniformed Pension Plan for the period January 1, 2019 to December 31, 2023. 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. State aid allocations that were deposited into the pension plan for the years ended December 31, 2018 to December 31, 2023, are presented on the Summary of Deposited State Aid and Employer Contributions.

- 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, 2018 to December 31, 2023, 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 that there were no benefit calculations prepared for the years covered by our audit period.
- 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 this report 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.
- We determined whether the terms of the plan's allocated insurance contract, including ownership and any restrictions, were in compliance with plan provisions, investment policies, and state regulations by comparing the terms of the contract with the plan's provisions, investment policies, and state regulations.
- We determined whether transfers were properly authorized, timely, and appropriately recorded by plan officials by examining supporting documentation of the transfer made during the audit period.

The township had elected to purchase allocated insurance contracts to fund the pension benefits for a plan member for the years 2019, 2020, 2021 and 2022. 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. 67 of the Governmental Accounting Standards Board, allocated insurance contracts are excluded from the pension plan's assets. Consequently, the plan has no reportable assets for the years 2019, 2020, 2021 and 2022.

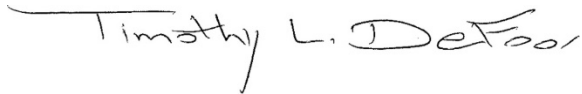
Township officials are responsible for establishing and maintaining effective internal controls to provide reasonable assurance that the Covington Township Non-Uniformed Pension Plan is administered in compliance with applicable state laws, regulations, contracts, administrative procedures, and local 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 Covington 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 Members' Accounts

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

A handwritten signature in black ink that reads "Timothy L. DeFoor". The signature is written in a cursive style with a long horizontal line extending to the left of the first letter.

Timothy L. DeFoor
Auditor General
May 2, 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 Covington 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 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 Covington Township Non-Uniformed Pension Plan is a single-employer discretionary pension plan locally controlled by the provisions of Resolution No. 2024-2, effective March 5, 2024, and a separately executed plan agreement. Prior to March 5, 2024, the plan was controlled by Resolution No. 2022-4, effective December 19, 2022, and Resolution No. 95-1, effective January 1, 1995. The plan was established January 1, 1995. Active members are not required to contribute to the plan. The municipality maintains a pension plan with no defined contributions and variable pension, or retirement benefits provided, usually through discretionary purchases of insurance or annuity contracts. As of December 31, 2023, the plan had two active members.

COVINGTON 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 year 2023, as illustrated below:

Actual municipal pension costs	\$ 2,081
State aid allocated	<u>(4,265)</u>
Excess state aid received	<u>\$ 2,184</u>

Criteria: Sections 6-2(a), (b) of the plan’s separately executed plan agreement with the custodian, adopted pursuant to Resolution No 2022-4, indicates the following:

- (a) Discretionary Contribution, The Employer will determine in its sole discretion how much, if any, it will make as an Employer Contribution.
- (b) Fixed contribution. Fixed dollar, \$1,000 for each Participant.

Section 402(f)(2) of Act 205 states:

No municipality shall be entitled to receive an allocation of general municipal pension system State aid in an amount which exceeds the aggregate actual financial requirements of any municipal pension plans for police officers, paid firefighters or employees other than police officers or paid firefighters maintained by the municipality, less the amount of any aggregate annual member or employee contributions during the next succeeding plan year, as reported in the most recent complete actuarial report filed with the commission.

Cause: The township recently changed plan custodians and adopted a new plan document, effective January 1, 2023, identifying the two contribution provisions noted in the Cause above. Municipal officials were not aware of the fixed dollar provision at the time of the contribution.

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 2023, must be returned to the Commonwealth for redistribution.

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

COVINGTON TOWNSHIP NON-UNIFORMED PENSION PLAN
FINDINGS AND RECOMMENDATIONS

Finding No. 1 – (Continued)

Recommendation: We recommend that the municipality return the \$2,184 of excess state aid received in the year 2023, 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.

Furthermore, 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. On March 5, 2024, the township adopted Resolution No. 2024-2 changing the adoption agreement to reflect changes in the contribution rate to a sole discretionary plan with no fixed defined contribution amount or percentage and removing the fixed contribution option previously enacted.

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 – Failure To Properly Fund Members’ Accounts

Condition: The township allocated contributions to the accounts of two members in excess of the plan’s governing document during 2023, as illustrated below:

<u>Employee Hire Date</u>	<u>Actual Contributions</u>	<u>Required Contributions</u>	<u>Contributions In Excess</u>
3/29/2010	\$ 4,265	\$ 1,000	\$ 3,265
1/24/2022	4,500	1,000	3,500
		Total	<u>\$ 6,765</u>

Criteria: Section 6-2 (a), (b)(2) of the separately executed plan adoption agreement enacted by Resolution No. 2022-4, effective January 1, 2023, states:

Discretionary contribution. The employer will determine in its sole discretion how much, if any, it will make as an employer contribution; and

Fixed contribution: Fixed dollar amount of \$1,000 for each participant.

COVINGTON TOWNSHIP NON-UNIFORMED PENSION PLAN
FINDINGS AND RECOMMENDATIONS

Finding No. 2 – (Continued)

Cause: As previously disclosed in Finding No. 1, municipal officials were not aware of the fixed dollar provision (*\$1,000 per participant*) contained in the newly enacted plan adoption agreement and the township lacked adequate internal control procedures to ensure that participant accounts were funded in accordance with revised plan provisions during 2023.

Effect: The failure to properly allocate contributions to the members' accounts resulted in plan members receiving benefits in excess of those to which they are entitled under the plan document.

Recommendation: We recommend that the township review the applicable members' accounts and make the adjustments deemed necessary to ensure that they are funded in accordance with the provisions contained in the plan's governing document.

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. On March 5, 2024, the township adopted Resolution No. 2024-2 changing the adoption agreement to reflect changes in the contribution rate to a sole discretionary plan with no fixed defined contribution amount or percentage and removing the fixed contribution option previously enacted.

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

COVINGTON 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 \$2,184, plus interest. A condition of this nature may lead to a total withholding of state aid in the future unless that finding is corrected. A check in this amount with interest, at a rate earned by the pension plan, should be made payable to: Commonwealth of Pennsylvania, and mailed to: Department of the Auditor General, Municipal Pension & Fire Relief Programs Unit, 321 Finance Building, Harrisburg, PA 17120.

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

Year Ended December 31	State Aid	Employer Contributions
2018	\$ 3,453	\$ 1,000
2019	3,555	1,000
2020	3,729	1,000
2021	3,683	1,000
2022	3,438	4,500
2023	4,265	4,500

COVINGTON 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. Valentine Bolognese, Sr.
Chairman, Board of Township Supervisors

Ms. Laurie Hess
Secretary

This report is a matter of public record and is available online at www.PaAuditor.gov. Media questions about the report can be directed to the Pennsylvania Department of the Auditor General, Office of Communications, 229 Finance Building, Harrisburg, PA 17120; via email to: news@PaAuditor.gov.