

LIMITED PROCEDURES ENGAGEMENT

Southampton Township Non-Uniformed Pension Plan Cumberland County, Pennsylvania For the Period January 1, 2014 to December 31, 2017

October 2018



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
Southampton Township
Cumberland County
Shippensburg, PA 17257

We conducted a Limited Procedures Engagement (LPE) of the Southampton Township Non-Uniformed Pension Plan for the period January 1, 2014 to December 31, 2017 to determine its compliance with applicable state laws, regulations, contracts, administrative procedures, and local ordinances and policies. We also evaluated compliance with some requirements subsequent to that period when possible. The LPE was conducted pursuant to authority derived from Section 402(j) of the Municipal Pension Plan Funding Standard and Recovery Act (P.L. 1005, No. 205, as amended, 53 P.S. § 895.101 et seq.) but was not conducted in accordance with *Government Auditing Standards* issued by the Comptroller General of the United States. 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. We believe that the evidence obtained provides a reasonable basis to support our LPE results.

Our LPE was limited to determining the following:

- 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 engagement period. State aid allocations that were deposited into the pension plan for the years ended December 31, 2012 to December 31, 2017, are presented on the Summary of Deposited State Aid and Employer Contributions.
- 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, 2012 to December 31, 2017, are presented on the Summary of Deposited State Aid and Employer Contributions.

- Whether annual employee contributions were required during the engagement period and, if so, were calculated, deducted, and deposited into the pension plan in accordance with the plan's governing document and applicable laws and regulations by testing total members' contributions on an annual basis using the rates obtained from the plan's governing document in effect for all years within the engagement period and examining documents evidencing the deposit of these employee contributions into the pension plan.
- Whether retirement benefits calculated for plan members who retired during the engagement 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 benefit due to retired individuals and comparing these amounts to supporting documentation evidencing amounts determined and actually paid to recipients.
- Whether the January 1, 2013, January 1, 2015, and January 1, 2017 actuarial valuation reports were prepared and submitted by March 31, 2014, 2016, and 2018, 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.
- Whether refunds made to plan members were authorized in accordance with plan provisions and applicable laws and regulations.

Based on the results of our procedures performed during our LPE, nothing came to our attention indicating that the Southampton Township Non-Uniformed Pension Plan was not being 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 – Incorrect Data On Certification Form AG 385 Resulting In An Overpayment Of State Aid

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

Our determination to perform a LPE for this engagement period does not preclude the Department from conducting an audit in accordance with *Government Auditing Standards* of the pension plan in subsequent periods. The township should continue to maintain documentation related to this pension plan.

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 this report. We would like to thank township officials for the cooperation extended to us during the conduct of this LPE.

September 25, 2018

A handwritten signature in black ink, appearing to read "Eugene A. DePasquale". The signature is fluid and cursive, with a long horizontal stroke extending to the right.

EUGENE A. DEPASQUALE
Auditor General

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SOUTHAMPTON TOWNSHIP NON-UNIFORMED PENSION PLAN
FINDINGS AND RECOMMENDATIONS

Finding No. 1 – Incorrect Data On Certification Form AG 385 Resulting In An Overpayment Of State Aid

Condition: The township overstated payroll by \$7,939 on the Certification Form AG 385 filed in 2015. The township also certified 1 ineligible non-uniformed employee (1 unit) and overstated payroll by \$47,652 on the Certification Form AG 385 filed in 2016. The data contained on these certification forms is based on prior calendar year information.

Criteria: Pursuant to Act 205, at Section 402(e)(2), in order to be eligible for certification, an employee must have been employed on a full-time basis for at least six consecutive months and must have been participating in a pension plan during the certification year.

Cause: Plan officials failed to establish adequate internal control procedures to ensure the accuracy of the data certified.

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>
2015	10.0%	\$ 7,939	\$ 794
2016	10.0%	\$ 47,652	<u>\$ 4,765</u>
Total Overpayment of State Aid			<u><u>\$ 5,559</u></u>

In addition, the township used portions of the overpayments of state aid to pay the minimum municipal obligations (MMOs) due to the pension plan; therefore, if the full reimbursement to the Commonwealth is made from the pension plan, the plan’s MMOs will not be fully paid.

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

SOUTHAMPTON TOWNSHIP NON-UNIFORMED PENSION PLAN
FINDINGS AND RECOMMENDATIONS

Finding No 1 – (Continued)

Recommendation: We recommend that the total overpayment of state aid, in the amount of \$5,559, 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. It should be noted that based on the schedule which appears in Finding No. 2 of this report, the township did not utilize excess state aid amounting to \$3,800 (\$794 in 2015 and \$3,006 in 2016) to fund the pension plan's 2015 and 2016 MMOs and may be returned from the pension plan. However, the remaining excess state aid received by the township amounting to \$1,759 (\$5,559 less \$3,800) was used by the township to fund the 2016 MMO and must be returned from the general fund.

We also 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: Due to the potential withhold of state aid, the township's compliance will be monitored subsequent to the release of the report and through our next engagement.

SOUTHAMPTON TOWNSHIP NON-UNIFORMED PENSION PLAN
FINDINGS AND RECOMMENDATIONS

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

Condition: The township received state aid in excess of the pension plan’s pension costs and also made municipal contributions in excess of those required to fund the plan, as illustrated below:

	<u>2014</u>	<u>2015</u>	<u>2016</u>
Actual municipal pension costs	\$ 27,611	\$ 24,301	\$ 24,225
Employee forfeitures available	-	(3,887)	-
Adjusted actual municipal pension costs	\$ 27,611	\$ 20,414	\$ 24,225
State aid allocated	(28,209)	(27,331)	(27,231)
Excess state aid received	<u>\$ 598</u>	<u>\$ 6,917</u>	<u>\$ 3,006</u>
Overpayment of State aid (<i>see Finding No. 1</i>)	-	(794)	(4,765)
Additional excess state aid received	<u>\$ 598</u>	<u>\$ 6,123</u>	<u>\$ -</u>
Actual municipal contributions made	\$ 280	\$ -	\$ -
Municipal contributions required to fund plan	-	-	-
Excess municipal contributions	<u>\$ 280</u>	<u>\$ -</u>	<u>\$ -</u>

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.

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.

SOUTHAMPTON TOWNSHIP NON-UNIFORMED PENSION PLAN
FINDINGS AND RECOMMENDATIONS

Finding No. 2 – (Continued)

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.

Cause: Plan officials failed to reconcile the amount of state aid allocated and employee forfeitures available to reduce municipal contributions in accordance with provisions contained in the plan’s governing document 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 overpayments of state aid in the years 2014 and 2015 must be returned to the Commonwealth for redistribution.

In addition, as a result of the township receiving excess state aid and making contributions to the pension plan in excess of contributions required to fund the pension plan, the unallocated current reserve fund in the amount of \$20,957 at January 1, 2014 increased to a reserve fund in the amount of \$37,662 at December 31, 2017, as illustrated by the following:

	<u>2014</u>	<u>2015</u>	<u>2016</u>	<u>2017</u>	<u>Total</u>
Unallocated reserve fund at January 1	\$ 20,957	\$ 22,905	\$ 31,175	\$ 35,854	\$ 20,957
Excess state aid	598	6,917	3,006	-	10,521
Excess municipal Contributions	280	-	-	-	280
Interest earned on reserve funds	<u>1,070</u>	<u>1,353</u>	<u>1,673</u>	<u>1,808</u>	<u>5,904</u>
Unallocated reserve fund at December 31	<u>\$ 22,905</u>	<u>\$ 31,175</u>	<u>\$ 35,854</u>	<u>\$ 37,662</u>	<u>\$ 37,662</u>

SOUTHAMPTON TOWNSHIP NON-UNIFORMED PENSION PLAN
FINDINGS AND RECOMMENDATIONS

Finding No 2 – (Continued)

The current reserve fund maintained by the pension plan increased because no reduction of municipal contributions occurred to reconcile the amount of state aid and employee forfeitures available to reduce municipal contributions with the plan's defined contribution pension costs. It is appropriate to use state aid to reimburse a municipality for contributions made to the pension plan to fund the pension costs in that same fiscal year, as long as annual pension costs for that pension plan are equal to or greater than the state aid allocated to that pension plan.

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 municipal reserve account at this time.

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

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 \$6,721 of excess state aid received in the years 2014 and 2015 to the Commonwealth from the pension plan. A check in this additional 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.

We also recommend that the township liquidate the unallocated reserve fund maintained by the pension plan by transferring the assets, which represent non-state 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 plan officials establish adequate internal control procedures to reconcile the annual state aid allocation, along with any available employee forfeitures and municipal contributions made to the pension plan, with the plan's annual pension costs and reimburse any excess state aid received to the Commonwealth including consulting with PMRS if employee forfeitures become available to determine if additional municipal contributions are required to meet the plan's funding requirements.

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

Auditor's Conclusion: Due to the potential withhold of state aid, the township's compliance will be monitored subsequent to the release of the report and through our next engagement.

SOUTHAMPTON TOWNSHIP NON-UNIFORMED PENSION PLAN
POTENTIAL WITHHOLD OF STATE AID

The findings contained in this report cite overpayments of state aid to the township in the total amount of \$12,280, plus interest. Conditions of this nature may lead to a total withholding of state aid in the future unless those findings are 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.

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

The supplementary information contained on Pages 7 and 8 reflects the implementation of GASB Statement No. 67, *Financial Reporting for Pension Plans*. The objective of this statement is to improve financial reporting by state and local governmental pension plans.

SCHEDULE OF CHANGES IN THE NET PENSION
LIABILITY AND RELATED RATIOS
FOR THE YEARS ENDED DECEMBER 31, 2014, 2015, AND 2016

	<u>2014</u>	<u>2015</u>	<u>2016</u>
Total Pension Liability			
Service cost	\$ 34,881	\$ 31,674	\$ 31,119
Interest	39,488	40,149	42,928
Difference between expected and actual experience	(243)	(2,338)	1,823
Changes of assumptions	-	2,620	6,514
Benefit payments, including refunds of member contributions	(16,265)	(24,271)	(22,999)
Net Change in Total Pension Liability	<u>57,861</u>	<u>47,834</u>	<u>59,385</u>
Total Pension Liability – Beginning	<u>674,507</u>	<u>732,368</u>	<u>780,202</u>
Total Pension Liability – Ending (a)	<u><u>\$ 732,368</u></u>	<u><u>\$ 780,202</u></u>	<u><u>\$ 839,587</u></u>
Plan Fiduciary Net Position			
Contributions – employer	\$ 28,489	\$ 27,031	\$ 26,951
Contributions – PMRS assessment	-	300	280
Contributions – member	7,549	7,673	7,173
PMRS investment income	40,361	41,165	44,124
Market value investment income	(4,864)	(43,352)	20,945
Benefit payments, including refunds of member contributions	(16,265)	(24,271)	(22,999)
PMRS administrative expense	(280)	(300)	(280)
Additional administrative expense	(1,548)	(1,716)	(2,162)
Net Change in Plan Fiduciary Net Position	<u>53,442</u>	<u>6,530</u>	<u>74,032</u>
Plan Fiduciary Net Position – Beginning	<u>685,047</u>	<u>738,489</u>	<u>745,019</u>
Plan Fiduciary Net Position – Ending (b)	<u><u>\$ 738,489</u></u>	<u><u>\$ 745,019</u></u>	<u><u>\$ 819,051</u></u>
Net Pension Liability - Ending (a-b)	<u><u>\$ (6,121)</u></u>	<u><u>\$ 35,183</u></u>	<u><u>\$ 20,536</u></u>
Plan Fiduciary Net Position as a Percentage of the Total Pension Liability	100.84%	95.49%	97.55%
Estimated Covered Employee Payroll	\$ 216,529	\$ 240,006	\$ 239,454
Net Pension Liability as a Percentage of Covered Employee Payroll	(2.83%)	14.66%	8.58%

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

Sensitivity of the Net Pension Liability to Changes in the Discount Rate

The following presents the net pension liability of the township as of December 31, 2014 and 2015, calculated using the discount rate of 5.50%, as well as what the township's net pension liability would be if it were calculated using a discount rate that is 1 percentage-point lower or 1 percentage-point higher than the current rate:

	<u>1% Decrease (4.50%)</u>	<u>Current Discount Rate (5.50%)</u>	<u>1% Increase (6.50%)</u>
Net Pension Liability - 12/31/14	\$ 111,391	\$ (6,121)	\$ (119,178)
Net Pension Liability - 12/31/15	\$ 162,209	\$ 35,183	\$ (87,546)

In addition, the following presents the net pension liability of the township as of December 31, 2016, calculated using the discount rate of 5.25%, as well as what the township's net pension liability would be if it were calculated using a discount rate that is 1 percentage-point lower or 1 percentage-point higher than the current rate:

	<u>1% Decrease (4.25%)</u>	<u>Current Discount Rate (5.25%)</u>	<u>1% Increase (6.25%)</u>
Net Pension Liability - 12/31/16	\$ 159,161	\$ 20,536	\$ (113,855)

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

Year Ended December 31	State Aid	Employer Contributions
2012	\$ 21,457	\$ 7,603
2013	28,820	47
2014	28,209	280
2015	27,331	None
2016	27,231	None
2017	23,945	1,355

Note: In 2015, the township met the plan's \$24,301 funding requirement through the deposit of \$27,331 in state aid and \$3,887 in terminated employee forfeitures.

SOUTHAMPTON 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. Charles O'Donnell
Vice-Chairman, Board of Township Supervisors

Mr. Scott Mack
Township Supervisor

Ms. Charity Rosenberry, CPA
Pennsylvania Municipal Retirement System

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