

# COMPLIANCE AUDIT

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## Prospect Borough Non-Uniformed Pension Plan Butler County, Pennsylvania For the Period January 1, 2016 to December 31, 2019

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January 2021



Commonwealth of Pennsylvania  
Department of the Auditor General

Eugene A. DePasquale • Auditor General



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**EUGENE A. DePASQUALE  
AUDITOR GENERAL**

The Honorable Mayor and Borough Council  
Prospect Borough  
Butler County  
Prospect, PA 16052

We have conducted a compliance audit of the Prospect Borough Non-Uniformed Pension Plan for the period January 1, 2016 to December 31, 2019. 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.

- 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 the lone plan member 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 individual and comparing these amounts to supporting documentation evidencing amounts determined and actually paid to the recipient.
- We determined whether the January 1, 2015, January 1, 2017, and January 1, 2019 actuarial valuation reports were prepared and submitted by March 31, 2016, 2018, and 2020, 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 Prospect Borough 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 Comprehensive Annual 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.

Borough officials are responsible for establishing and maintaining effective internal controls to provide reasonable assurance that the Prospect Borough 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 Prospect Borough 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 – 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
- Finding No. 3 – Failure To Maintain An Adequate Record-Keeping System To Effectively Monitor Activity Of The 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 Prospect 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.

December 16, 2020



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.

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 Prospect Borough 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.

The Prospect Borough Non-Uniformed Pension Plan is a single-employer cash balance pension plan locally controlled by the provisions of Ordinance No. 2013-2, and a separately executed plan agreement with the Pennsylvania Municipal Retirement System (PMRS), adopted pursuant to Act 15. The plan was established July 1, 2013. Active members are not required to contribute to the plan. The municipality is required to contribute \$625 per member per quarter. As of December 31, 2019, the plan had 2 active members and 1 retiree receiving pension benefits.

PROSPECT BOROUGH 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 borough certified an ineligible non-uniformed employee (1 unit) and overstated payroll by \$39,164 and \$16,873, respectively, on the Certification Form AG 385s filed in 2016 and 2019. The borough also incorrectly certified that the plan was established on or before December 31, 1984, rather than the plan's effective date, July 1, 2013, on the Certification Form AG 385 submitted during 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.

In addition, the instructions accompanying Certification Form AG 385 require a municipality to report the date the plan was established for all plans established after December 31, 1984. In addition, pursuant to Section 402(e)(2) of Act 205, if a plan is established after December 31, 1984, the plan is required to be maintained by the municipality for at least three plan years prior to becoming eligible for state aid.

Moreover, the instructions that accompanied Certification Form AG 385 for 2016 indicated the following:

**3b. PENSION PLAN ESTABLISHED**

If the pension plan was established after December 31, 1984, you must write in the date the plan was established. Each plan must have been established on or before 1/1/13 to be eligible for state aid.

Cause: Plan officials inadvertently selected the option that the plan was established on or before December 31, 1984, on the AG 385 form submitted during 2016. In addition, plan officials were unaware that an employee hired during 2018 did not become a plan member until January 1, 2019, and therefore, was not eligible to be certified. Additionally, the borough lacked adequate procedures, such as having another individual 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.

PROSPECT BOROUGH NON-UNIFORMED PENSION PLAN  
FINDINGS AND RECOMMENDATIONS

**Finding No. 1 – (Continued)**

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 borough’s state aid allocations were based on pension costs, the incorrect certification of pension data affected the borough’s state aid allocations, as identified below:

<u>Year</u>	<u>Normal Cost</u>	<u>Payroll Overstated</u>	<u>State Aid Overpayment</u>
2016	N/A	N/A	\$ 2,322
2019	.0770%	\$ 16,873	1,299
<b>Total Overpayment of State Aid</b>			<b>\$ 3,621</b>

*N/A – Since the plan was not established until 7/1/2013, the borough did not maintain the plan for at least 3 years and therefore, was not entitled to an allocation of state aid during 2016.*

In addition, the borough used the overpayments of state aid to fund 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.

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

Recommendation: We recommend that the excess state aid, in the amount of \$3,621, 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 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.

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

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



PROSPECT BOROUGH NON-UNIFORMED PENSION PLAN  
FINDINGS AND RECOMMENDATIONS

**Finding No. 1 – (Continued)**

Auditor Conclusion: Due to the potential withhold of state aid, the borough’s compliance with the finding recommendation will be monitored subsequent to the release of the audit report and through our next audit of the pension plan.

**Finding No. 2 – Receipt Of State Aid In Excess Of Entitlement**

Condition: The borough received state aid in excess of the non-uniformed pension plan’s pension costs in the year 2018, as illustrated below, which remains in the borough’s general fund as of the date of this report:

State aid allocation	\$ 4,986
Actual municipal pension costs	<u>(2,540)</u>
Excess state aid	<u>\$ 2,446</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.

Cause: Plan officials failed to establish adequate internal control procedures to annually reconcile the borough’s state aid allocation with the plan’s actual 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 overpayment of state aid in the year 2018 must be returned to the Commonwealth for redistribution.

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

PROSPECT BOROUGH NON-UNIFORMED PENSION PLAN  
FINDINGS AND RECOMMENDATIONS

**Finding No. 2 – (Continued)**

Recommendation: We recommend that the municipality return the \$2,446 of excess state aid received in the year 2018 to the Commonwealth from the 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, 321 Finance Building, Harrisburg, PA 17120. A copy of the interest calculation must be submitted along with evidence of payment.

Furthermore, we recommend that, in the future, plan officials reconcile the borough's annual state aid allocation with the plan's annual pension costs and reimburse any excess state aid received to the Commonwealth.

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

Auditor Conclusion: Due to the potential withhold of state aid, the borough's compliance with the finding recommendation will be monitored subsequent to the release of the audit report and through our next audit of the pension plan.

**Finding No. 3 – Failure To Maintain An Adequate Record-Keeping System To Effectively Monitor Activity Of The Pension Plan**

Condition: The borough's record-keeping system did not provide effective control over the transactional activity of the non-uniformed pension plan during 2019. Municipal officials were unable to furnish annual financial statements or custodial account transaction statements for the non-uniformed pension plan. These annual financial and account statements have historically been provided by the plan's custodian, PMRS. However, as of the date of this report, annual financial and accounting statements summarizing the pension account activity have not been provided for the year 2019.

Criteria: An adequate system of accounting and record keeping is a prerequisite for sound administration of pension plans. In addition, assets held in a custodial account for the purpose of plan management are to be governed by the terms and provisions of the account contract, provided that the terms and provisions of the contract are within the parameters of all prevailing pension legislation. Although the municipality may contract with a trustee to administer the financial management of the plan, the fiduciary responsibility for the plan remains with the municipality.

PROSPECT BOROUGH NON-UNIFORMED PENSION PLAN  
FINDINGS AND RECOMMENDATIONS

**Finding No. 3 – (Continued)**

Cause: Municipal officials indicated that the plan’s custodian, PMRS, failed to provide copies of the custodial account transaction statements summarizing activity of the pension plan account for the year 2019. In addition, municipal officials did not maintain a separate detailed accounting of pension plan transactions which, among other things, helps assure the production of proper financial statements to effectively monitor the annual activity of the pension plan.

Effect: Although we were able to obtain alternate documentation from the municipality to evidence the propriety of the individual transactions tested during performance of the audit for the year 2019, the failure to maintain annual financial and/or account transaction statements prohibits municipal officials from effectively monitoring the plan’s financial operations. Additionally, inadequate monitoring of the pension plan account could lead to undetected errors or improprieties in account transactions as well as deficiencies in authorizing and implementing pension plan policies and procedures.

Recommendation: We recommend that municipal officials contact the plan custodian and obtain annual financial statements of the custodial account of the non-uniformed pension plan for the year 2019 to ensure the accuracy and propriety of the transaction activity. In addition, we recommend that municipal officials establish and maintain a financial record-keeping system that allows the municipality to effectively monitor the plan’s financial operations, even in the absence of statements from the plan custodian. Municipal officials should refer to the Auditor General’s Bulletin No. 2-88 entitled “Preparation, Maintenance and Auditability of Financial Records,” for further guidance in establishing adequate accounting and record-keeping procedures.

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

Auditor Conclusion: PMRS has indicated that they are in the process of preparing 2019 Year-End Financial Activity Reports and Annual Member Statements for all municipalities. PMRS has also indicated that they recently went through a substantial upgrade to the plan administration software and implemented a new accounting system. This transition in addition to disruptions in normal government operation due to COVID-19 has resulted in a three to four month delay in the 2019 year-end reporting process. Compliance with the finding recommendation will be evaluated during our next audit of the plan.

PROSPECT BOROUGH NON-UNIFORMED PENSION PLAN  
POTENTIAL WITHHOLD OF STATE AID

Findings No. 1 and No. 2 contained in this audit report cite a total overpayment of state aid to the borough in the amount of \$6,067, 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.

PROSPECT BOROUGH NON-UNIFORMED PENSION PLAN  
 SUPPLEMENTARY INFORMATION  
 (UNAUDITED)

SCHEDULE OF CONTRIBUTIONS (CASH BASIS)

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	\$ 2,520	\$ 2,520	\$ -	\$ 42,165	6.0%
2015	2,520	2,520	-	39,164	6.4%
2016	4,395	4,415	(20)	58,357	7.6%
2017	5,040	5,040	-	63,189	8.0%
2018	2,540	1,924	616	39,746	4.8%
2019	5,040	4,623	(417)		

\* The Statutorily Required Contribution (SRC) is a contribution amount based upon the payroll and the contribution rate as outline under the terms of the cash balance pension plan.

\*\* The SRC and the actual Contributions (*in relation to SRC*) were provided by PMRS. Deviation between these amounts may be due to contributions to or transfers from the Municipal account.

\*\*\* Due to the timing of this audit, covered-employee payroll for 2019 was not provided in this schedule.

PROSPECT BOROUGH NON-UNIFORMED PENSION PLAN  
REPORT DISTRIBUTION LIST

This report was initially distributed to the following:

**The Honorable Tom W. Wolf**  
Governor  
Commonwealth of Pennsylvania

**The Honorable James Butler**  
Mayor

**Mr. Bill Katz**  
Council President

**Ms. Debra Perry**  
Secretary

**Ms. Charity Rosenberry, CPA**  
Pennsylvania Municipal Retirement System

This report is a matter of public record and is available online at [www.PaAuditor.gov](http://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](mailto:news@PaAuditor.gov).