

Internal Audit Department

O R A N G E C O U N T Y
6th Largest County in the USA

FINAL CLOSE-OUT **FIRST FOLLOW-UP AUDIT:**

COUNTY OF ORANGE RETIREE MEDICAL PLAN – ANNUAL REQUIRED COUNTY CONTRIBUTIONS

AS OF MARCH 31, 2015

Our First Follow-Up Audit found that CEO has fully implemented the four (4) recommendations from our original audit report dated September 11, 2014.

During the original audit period, the County contributed \$37,275,730 to the Retiree Medical Plan and has transferred \$46,663,719, including contributions made by some employees and other public entity participants, to the Trust within the Orange County Employees Retirement System (OCERS).

AUDIT NO: 1316-F1
(REFERENCE 1417)
ORIGINAL AUDIT NO. 1316

REPORT DATE: MAY 21, 2015

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Senior Audit Manager: Alan Marcum, CPA, CIA
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RISK BASED AUDITING

GAO & IIA Peer Review Compliant – 2001, 2004, 2007, 2010, 2013



American Institute of Certified Public Accountants Award to Dr. Peter Hughes as 2010 Outstanding CPA of the Year for Local Government

GRC (Government, Risk & Compliance) Group 2010 Award to IAD as MVP in Risk Management



2009 Association of Certified Fraud Examiners' Hubbard Award to Dr. Peter Hughes for the Most Outstanding Article of the Year – Ethics Pays



2008 Association of Local Government Auditors' Bronze Website Award



2005 Institute of Internal Auditors' Award to IAD for Recognition of Commitment to Professional Excellence, Quality, and Outreach



ORANGE COUNTY BOARD OF SUPERVISORS'
Internal Audit Department

GAO & IIA Peer Review Compliant - 2001, 2004, 2007, 2010, 2013

Providing Facts and Perspectives Countywide

RISK BASED AUDITING

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OC Fraud Hotline (714) 834-3608



Transmittal Letter



Audit No. 1316-F1 May 21, 2015

TO: Frank Kim
County Executive Officer

FROM: Dr. Peter Hughes, CPA, Director
Internal Audit Department

SUBJECT: **First and Final Close-Out Follow-Up Audit:**
County of Orange Retiree Medical Plan –
Annual Required County Contributions,
Original Audit No. 1316, Issued
September 11, 2014

We have completed a First Follow-Up Audit of County of Orange Retiree Medical Plan – Annual Required County Contributions. Our audit was limited to reviewing, as of March 31, 2015, actions taken to implement the **four (4) recommendations** from our original audit report dated September 11, 2014. We conducted this First Follow-Up Examination in accordance with the *FY 14-15 Audit Plan and Risk Assessment* approved by the Audit Oversight Committee.

The results of our First Follow-Up Audit are discussed in the **OC Internal Auditor's Report** following this transmittal letter. Our First Follow-Up Audit found that **CEO implemented ALL four (4) recommendations** from the original audit report. Because satisfactory corrective action has been taken for the four (4) recommendations, **this report represents the final close-out of the original audit.**

Each month I submit an **Audit Status Report** to the Board of Supervisors (BOS) where I detail any material and significant audit findings released in reports during the prior month and the implementation status of audit recommendations as disclosed by our Follow-Up Audits. Accordingly, the results of this audit will be included in a future status report to the BOS.

Other recipients of this report are listed on the **OC Internal Auditor's Report** on page 4.

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County of Orange Retiree Medical Plan -
Annual Required County Contributions
Audit No. 1316-F1*

As of March 31, 2015

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Audit No. 1316-F1

May 21, 2015

TO: Frank Kim
County Executive Officer

FROM: Dr. Peter Hughes, CPA, Director
Internal Audit Department

SUBJECT: First and Final Close-Out Follow-Up Audit: County of Orange Retiree Medical Plan - Annual Required County Contributions, Original Audit No. 1316, Issued September 11, 2014

Scope of Review

We have completed a First Follow-Up Audit of the County of Orange Retiree Medical Plan – Annual Required County Contributions. Our audit was limited to reviewing actions taken, as of March 31, 2015, to implement the **four (4) recommendations** from our original audit report dated September 11, 2014.

Background

Retiree Medical Plan Overview

Effective August 1, 1993, the County of Orange adopted the County of Orange Retiree Medical Plan (Plan) to assist career employees in maintaining health insurance coverage following their retirement from County service.

The County is responsible for administration of the Plan, including level and amount of benefits available to participants, determining participant eligibility, determining health plans qualified to be offered, establishing and administering claims procedures, appointing a Plan Administrator, and all other rights and obligations under the Plan.

Retiree Medical Plan Trust (Trust)

The County funds the Plan through a trust account. Effective July 2, 2007, the County established County of Orange Retiree Medical Trust (an Internal Revenue Code Section 115 trust and 401(h) account) to provide a source of funds to assist the County in meeting its liabilities under the Plan. This Trust is irrevocable and its assets shall be used exclusively for providing medical benefits for eligible retirees and related costs of investment and administration.

The Orange County Employees Retirement System (OCERS) maintains and administers 401(h) Trust Account (Trust) as per the Participation Agreement with the County. OCERS has fiduciary responsibility for investing the assets of the Trust and making monthly benefit payments from this Trust.

The County maintains and administers Section 115 Trust Account. Also, Fund 17A, a fiduciary fund account, is established in the County accounting system to record transactions pertaining to the Trust.



Retiree Medical Plan Trust Contributions

The County makes full Annual Required Contributions (ARC) to the Plan through payroll deductions. Due to subsequent labor negotiations, the Plan has been restructured. Some employees make employee contributions to the Plan to offset the County's Annual Required Contributions.

The contributions (employer's, employee's and other public entities) are automatically processed in the County-wide Accounting and Personnel System (known as CAPS+) and are posted in Fund 17A each time payroll is processed. The amounts are included in the County Treasurer's Investment Pool (Investment Pool) for investment until the CEO Public Finance Division electronically transmits the amount to a third party bank to deposit into the Trust account within OCERS.

Annual Required Contribution (ARC) Rates

Governmental Accounting Standard Board (GASB) Statement No. 45 requires the County to have an actuarial valuation at least biennially. The purpose of the actuarial valuation is to determine the projected Plan benefit obligations and calculate the ARC and the corresponding contribution rates (known as ARC rates) for each rate group. The County contracted with a firm to provide actuary services.

Results

Our First Follow-Up Audit found that **CEO implemented ALL four (4) recommendations** from our original audit report. **As such, this report represents the final close-out of the original audit.** Based on our First Follow-Up Audit, the following is the implementation status of the four (4) original recommendations:

Finding No. 1 – The Revised Annual Required Contribution (ARC) Rates Were Not Submitted to the Board of Supervisors (BOS) for Approval (Control Finding)

Recommendation No. 1: We recommend that the CEO establish a policy to ensure the Annual Retiree Contribution rates (actuarial and/or revised) are submitted to the Board of Supervisors for approval.

Current Status: Implemented. CEO revised Administrative Procedural Manual (Manual) Section 4.1 to ensure the Annual Required Contribution (ARC) rates are submitted to the Board of Supervisors (BOS). The Manual requires the CEO provide a memo, which summarizes the ARC rate changes to the BOS, and the actuarial valuation report when the actuarial valuation report becomes available. In addition, it requires that a description of the ARC rate changes be included in the Quarterly Budget Adjustment Report (QBAR) report to the BOS.

The ARC rates for 2014/15 were implemented in October 2014. We reviewed documents and verified that the CEO prepared a memo to notify the BOS of the new rates and they were also included in the FY 2014-15 First QBAR for the BOS consideration. As such, we determined that the CEO has implemented our recommendation.



Finding No. 2 – Review of ARC Rates Update in County Accounting and Payroll System Was Not Being Performed as Required (Control Finding)

Recommendation No. 2: We recommend that the CEO establish controls to ensure that a review of the Annual Required Contribution (ARC) rates update in the County Accounting and Payroll System (CAPS+) is performed as required by the CEO Administrative Procedural Manual, Administration of the Retiree Medical Trust, Section 4.1.

Current Status: Implemented. The Administrative Procedural Manual Section 4.1 states that *“Each time the ARC is changed in the payroll system, it is necessary to verify that the correct percentages were entered into the payroll system. This shall be accomplished by taking a random sample of at least three employees from each labor group and utilizing the Human Resources portion of the County Accounting and Payroll System to verify that each sample reflects the correct ARC percentage of payroll under the “RMBR” pay code. The verification of the ARC percentages shall be documented in writing and reviewed by either the County Chief Financial Officer, Public Finance Director or their designee”.*

The FY 2014-15 ARC rates were implemented in October 2014. We reviewed documents and confirmed that Auditor-Controller/Payroll selected three samples from each labor group to verify that correct percentages were inputted into the system. Also, the Public Finance Director designee has reviewed and documented the review in writing as required by the Manual. As such, we determined that the CEO has implemented our recommendation.

Finding No. 3 – Annual Required Contributions Were Not Being Transferred to 401(h) Trust Account Regularly (Control Finding)

Recommendation No. 3: We recommend that the CEO ensure that ARC transfers are made regularly and timely to the 401(h) trust (Trust) account at OCERS.

Current Status: Implemented. The Administrative Procedural Manual (Manual) Section 2.1 states that *“Every two to four payroll cycles if possible and provided there are sufficient funds in Fund 17A, the Public Finance analyst administering the Trust will electronically transfer funds from Fund 17A to OCERS for deposit into the IRC 401(h) Trust held at OCERS”.*

During the audit period from September 2014 through March 2015, there were four (4) transfers. We found that trust fund transfers were made as required by the Manual. As such, we determined that the CEO has implemented our recommendation.



Finding No. 4 – Reconciliations and Recording of Trust Account Activities Were Not Done Monthly as Required (Control Finding)

Recommendation No. 4: We recommend that the CEO ensure that reconciliations and recording of the trust account activities are done monthly as required by the CEO Administrative Procedural Manual.

Current Status: Implemented. The Administrative Procedural Manual (Manual) Section 2.2, has been revised. It states that *“Once the OCERS statements are received, the activity reflected on the statements must be reconciled to the County’s accounting records. The reconciliations shall be performed monthly. At least quarterly, a journal voucher shall be prepared in order to record the Trust activity in Fund 17A”*. The revision of the Manual has adequately addressed our recommendation.

We reviewed documents and found that reconciliations were done on a monthly basis and two Journal Vouchers (JV) were prepared from September 2014 through March 2015. Since trust activities are being reconciled and recorded in CAPS+ as required by the Manual, we determined that the CEO has implemented our recommendation.

Distribution Pursuant to Audit Oversight Committee Procedure No. 1:

Members, Board of Supervisors
Members, Audit Oversight Committee
Mark Denny, Chief Operating Officer
Michelle Aguirre, Director, CEO/County Budget Office
Suzanne Luster, Director, CEO/Public Finance
Louis McClure, Administrative Manager, CEO/Public Finance
Anil Kukreja, Manager, CEO/County Budget Office
Jaime Martinez, Administrative Manager, CEO/County Budget Office
Foreperson, Grand Jury
Robin Stieler, Interim Clerk of the Board of Supervisors
Macias Gini & O’Connell LLP, County External Auditor