

INTERNAL AUDIT REPORT

2015-10

Police and Fire Retiree Medical Trust
Five-Year Review

Employee Relations Department

December 10, 2015

MUNICIPALITY OF ANCHORAGE
Internal Audit Department
632 W 6th Avenue, Suite 600
P.O. Box 196650
Anchorage, Alaska 99519-6650
www.muni.org/departments/internal_audit



INTERNAL AUDIT DEPARTMENT
Michael Chadwick, CICA
Acting Director
Phone: (907) 343-4438
Fax: (907) 343-4370
E-Mail: chadwickmb@muni.org



Municipality of Anchorage

Ethan Berkowitz, Mayor

Internal Audit Department

December 10, 2015

Honorable Mayor and Members of the Assembly:

I am pleased to present for your review **Internal Audit Report 2015-10, Police and Fire Retiree Medical Trust Five-Year Review, Employee Relations Department**. A brief summary of the report is presented below.

In accordance with the 2015 Audit Plan, we have completed an audit of the Police and Fire Retiree Medical Trust. The objective of this audit was to perform the fourth five-year (January 1, 2010, through December 31, 2014) review of the operation of the Retiree Medical Funding Program for Police Officers and Firefighters as required by Anchorage Municipal Code 3.87.070.A. Specifically, we reviewed the operation of the Retiree Medical Funding Program for Police Officers and Firefighters to determine whether it was being operated in compliance with Anchorage Municipal Code 3.87, including the accuracy of monthly trust contributions and participant transactions.

Based on our review, the Retiree Medical Funding Program for Police Officers and Firefighters was operated in compliance with Anchorage Municipal Code 3.87. Trust contributions were properly adjusted annually for the Medical Consumer Price Index. Moreover, we found that members' individual health reimbursement agreement accounts were properly credited with the correct monthly contribution amount matching the members' class. However, our review found that the calculations of the 2014 and 2015 monthly surplus distribution amounts for the "deferred vested" members were not correct.

There was one finding in connection with this audit. Management was responsive to the audit finding and recommendation.

Michael Chadwick, CICA
Acting Director, Internal Audit



Municipality of Anchorage

Ethan Berkowitz, Mayor

Internal Audit Department

December 10, 2015

Internal Audit Report 2015-10
Police and Fire Retiree Medical Trust Five-Year Review
Employee Relations Department

Introduction. Anchorage Municipal Code (AMC) Chapter 3.87, *Retiree Medical Funding Program for Police Officers and Firefighters*, establishes the Retiree Medical Funding Program for Police Officers and Firefighters (Program). The Program's purpose "...is to provide those retirees receiving retirement benefits under the police and fire retirement system and who qualify as members of the program with a health reimbursement agreement (HRA) to cover the eligible medical expenses of the members, their spouses and eligible dependents." In 2009 AMC 3.87.050, *Eligibility for active municipal police or fire health insurance plan*, was amended to provide a monthly discount from the stated premium to all members purchasing municipal health insurance. The Program is staffed by one trust program staff administrator (administrator) and one part-time contractor. As of October 2015 there were 382 Program participants who received into their HRA accounts a monthly trust contribution ranging from \$589.50 to \$849.65 for a total of \$2,787,722 for the first ten months of 2015.

- **Municipal Contributions:** Program contributions are made solely by the Municipality. The Municipality's responsibilities under this funding program are limited to the following:
 - An initial prefunding contribution of \$2 million.
 - Monthly contribution for the benefit of each member of \$490 starting January 1, 1995, adjusted annually based on a set percentage of the national Medical Consumer Price Index (MCPI).
 - An amount equal to 50 percent of the Medicare Part A Premium that the member is required to pay for part A coverage if, upon reaching the age of Medicare eligibility, a

member is not eligible to participate in Medicare without paying the Medicare Part A Premium.

- A balloon payment in 2006 of \$9.8 million.
 - Funding for an administrator to administer the Program.
 - Office space necessary to house the administrator, according to Assembly Memorandum 1298-94.
- **Health Reimbursement Arrangement:** The Program reimburses members and, as applicable, surviving spouses and dependents for medical expenses eligible under Section 213 of the Internal Revenue Code including eligible health insurance costs and long-term care premiums. According to AMC 3.87.060.J, *Eligible expense reimbursements*, “The program will not reimburse an expense incurred before the date . . . an employee first becomes enrolled in the HRA. The maximum dollar amount reimbursable shall not exceed the balance in the member’s account.”
 - **Surplus Distribution:** According to the Program’s Policy and Procedure Manual (Manual), “In 1995, the Trust received a \$2 million contribution from the Municipality. These funds are for expenses incurred in the Trust administration and to offset members’ increasing medical expense. This initial contribution has grown by investment returns since the inception of the Trust. The accumulated assets are more than necessary to pay the projected administrative expenses. These excess assets are referred to as ‘surplus’.

“A surplus analysis will be performed annually by the staff at the end of the third quarter and presented to the board for review. It is the board’s discretion whether to distribute the surplus after reviewing the analysis each year. A distribution WILL NOT occur in any year that an analysis does not indicate a surplus. Distribution may resume whenever a surplus is present.”

The Program distributed a monthly surplus payment to participants in 2013, 2014, and 2015. In 2015, the surplus paid each month to each participant ranged from \$65.45 to \$94.79.

- **Monthly Premium Discount:** In 2009 AMC 3.87.050 was amended to provide a monthly discount to all members purchasing municipal health insurance. For 2015 the discount was \$788.33. In addition, benefits provided to a surviving spouse and dependents were extended.
- **Prefunding Program:** Anchorage Municipal Code 3.88, *Prefunding of Police and Fire Retiree Medical Program*, was "...established for the purpose of managing the funding necessary to meet the obligations of the municipality for the police and fire retiree medical funding program . . . and making contributions to the retiree medical funding program trust on the behalf of eligible members...". The objective of the investment program is to accumulate Municipal assets "...through a 34-year prefunding program of regular annual deposits by the municipality and accumulated interest earnings so that the municipal obligation is fully funded, requiring no further deposits." An annual municipal deposit to the investment program was established and has been adjusted as necessary to ensure full funding at the end of the year 2028. The amount was based on the results of actuarial valuations and recommendations of the investment board. The prefunding included a balloon payment by the Municipality of \$9.8 million in 2006 paid for with proceeds from the Retirement Certificates of Participation Debt Service Fund. An actuarial valuation of the Municipality's obligation to the funding program and the funding status of the investment program is completed, at a minimum, every three years. Although the prefunding program was not part of this audit, the information was included to help the reader understand Program funding.
- **Assembly Review:** Anchorage Municipal Code 3.87.070.A, *Assembly review*, states that "Every five years from January 1, 1995, the assembly will review the operation of the program including the amount of the initial monthly contribution established in Section 3.87.060 to be made by the municipality."
- **Internal Audit Review:** Anchorage Municipal Code 3.87.070.B, *Internal audit review*, requires that "The Internal Auditor will perform an audit of the trust at least once every two years. The scope of the audit may include, but is not limited to, evaluating trust administrative

costs, and reviewing enrollment and payment records for members purchasing health insurance through the Municipality.” The objectives of an Internal Audit review under AMC 3.87.070.B were not performed during this audit since they were reviewed in 2014 and will be reviewed again in 2016.

Objective and Scope. The objective of this audit was to perform the fourth five-year (January 1, 2010, through December 31, 2014) review of the operation of the Program as required by AMC 3.87.070.A. Specifically, we reviewed the operation of the Program to determine whether it was being operated in compliance with AMC 3.87, including the accuracy of monthly trust contributions and participant transactions.

The audit was conducted in accordance with generally accepted government auditing standards, except for the requirement of an external quality control review, and accordingly, included tests of accounting records and such other auditing procedures as we considered necessary in the circumstances. The audit was performed during the period of September through October 2015. The audit was performed to satisfy AMC requirements for periodic independent reviews.

Overall Evaluation. Based on our review, the Program was operated in compliance with AMC 3.87. Trust contributions were properly adjusted annually for the MCPI. Moreover, we found that members’ individual HRA accounts were properly credited with the correct monthly contribution amount matching the members’ class. However, our review found that the calculations of the 2014 and 2015 monthly surplus distribution amounts for the “deferred vested” members were not correct.

FINDINGS AND RECOMMENDATIONS

1. Incorrect Monthly Surplus Distribution Amounts.

- a. Finding.** The monthly surplus distribution amounts to some members were not always paid correctly. Specifically, in 2014 the Program overpaid “deferred vested”

members and in 2015 the Program underpaid “deferred vested” members. The distribution percentage was calculated incorrectly due to an error when data was manually transferred between computer systems. While these overpayments and underpayments were not significant, they were not consistent with the Manual regarding the surplus fund distribution. The Manual states that “Each retired member will receive the same monthly percentage distribution...”.

- b. **Recommendation.** The administrator should evaluate whether the account balances should be adjusted for the minor errors found in 2014 and 2015.

- c. **Management Comments.** Management concurred and stated, “The administrator has evaluated the overpayments and underpayments and is currently in the process of making the corrections. The administrator plans to finalize the corrections prior to the end of 2015. In addition, the Surplus Funds Analysis Report has been modified to include information showing the annual percentage distribution.”

- d. **Evaluation of Management Comments.** Management comments were responsive to the audit finding and recommendation.

Discussion With Responsible Officials. The results of this audit were discussed with appropriate Municipal officials on November 16, 2015.

Audit Staff:
Scott Lee