Audit Department

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Angela M. Darragh, CPA, CFE, CISA, Director

August 14, 2015

Mr. Don Burnette
Clark County Manager
500 South Grand Central Parkway, 6th Floor
Las Vegas, Nevada 89106

Dear Mr. Burnette:

We recently completed an audit of the Retirement Health Account. The audit was added to the audit plan at the request of the Comptroller. The last day of fieldwork was April 27, 2015. The objective of this audit is to determine whether:

- Plan transactions consisting of employee contributions, reimbursement of health premiums, and interest allocations are in accordance with Plan provisions and are correct and properly recorded.
- Plan balances agree with amounts held with the Mass Mutual and with the Clark County financial records.
- Internal controls exist to address the completeness and accuracy of the Plan balance.

We found that plan transactions consisting of employee contributions, reimbursement of health premiums, and interest allocations are in accordance with Plan provisions. However, transactions are not always correct and properly recorded. Our audit identified eight plan participants who were not fully credited for their payroll contributions in July 2008. We identified one participant who was given credit for another participant's contribution match. We also found a systemic minor miscalculation in how interest is allocated to plan participants. Overall, plan balances agreed with amounts held with the Mass Mutual and with the Clark County financial records. However, we believe internal controls could be improved by implementing an independent review of the Plan ledgers.

A draft report was provided to Comptroller for comment, and her response is included.

We appreciate the cooperation and assistance provided by the staff of the Comptroller's Office.

Sincerely,

Angela M Darragh

Angela M. Darragh, CPA
Audit Director

AUDIT DEPARTMENT

Audit Report

Clark County
Retirement Health Account

August 2015

Angela M. Darragh, CPA, CISA, CFE
Audit Director

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BACKGROUND

On June 1, 1993 the Board of County Commissioners approved the Excess Deferred Compensation Plan, later known as the Retirement Health Account Plan (Plan). The Plan provides a benefit to participating County employees by providing a means of deferring current income in order to set aside future funding to pay for health insurance costs upon retirement. Employees generally became eligible to participate in the Plan at the age of 54 or upon completing 14 years of service with the County.

The plan was amended several times to comply with regulatory mandates set forth by the Internal Revenue Service (IRS). In 2007, the County closed the program to new participants due to an adverse opinion by the IRS. At that time, participants were allowed to continue payroll contributions on an elective, post-tax basis.

Contributions come from employees, with the County providing a 100 percent contribution match up to $480 annually for a maximum of five years.

Withdrawals from the Plan occur only when an employee retires under the Public Employees' Retirement System of Nevada (PERS). Withdrawals may only be used to pay for the cost of health insurance premiums. Retirees are reimbursed from their individual accounts for their out-of-pocket health insurance premiums.

The Plan includes provisions for forfeitures of funds. If an employee terminates prior to retirement, death, or disability, the employee's contributions are forfeited. The forfeited funds become part of the pooled amounts to be used for future obligations of the Plan. The Plan holds the majority of funds in the Clark County general investment pool. The funds held in the investment pool earn interest that is proportionately allocated every month based on the amount invested to total pooled investments. A smaller portion of the total plan contributions are held with Massachusetts Mutual Life Insurance Company (Mass Mutual) in an interest earning account. Interest earnings are allocated to each participant based on their share of the Plan's total average monthly balance.

An authorized designated employee of the County administers the Plan. The Plan Administrator is responsible for recording all plan transactions and correspondences. The Plan Administrator maintains a yearly ledger detailing each participant's Plan balance. The Plan ledgers detail each participant's contributions, interest earnings and withdrawals; it is the primary record for participant transactions.

As of year-end 2014 there are 202 active participants with an average balance of $8,413 along with $9,816 in forfeited funds. In 2014, the Plan paid out $275,553 in reimbursement claims while total employee contributions were $21,622. The total plan balance as of year-end 2014 is $1,709,249, of which $89,592 is held with Mass Mutual, while the remaining balance is held in the County's general investment pool. Total interest income for 2014 was $17,861.

This audit was requested by the Clark County Comptroller due to a newly designated Plan Administrator. Reviewing plans and programs is important when changing administrators, as this provides a means of financial transparency and accountability should erroneous or unwarranted transactions be discovered. A periodic audit is also required under Article IV, Section 4.06 of the Plan agreement.

OBJECTIVES, SCOPE, AND METHODOLOGY

The objective of this audit is to determine whether:

- Plan transactions consisting of employee contributions, reimbursement of health premiums, and interest allocations are in accordance with Plan provisions and are correct and properly recorded.
- Plan balances agree with amounts held with the Mass Mutual and with the Clark County financial records.
- Internal controls exist to address the completeness and accuracy of the Plan balance.

To accomplish our objectives, we conducted a preliminary survey that included reviewing the Plan documents, correspondences, interviewing the Plan Administrator and observing the Plan administration. Based on the risks noted during our preliminary survey, we developed an audit program. The following detailed testing procedures were performed:

- We reviewed all (100%) payroll records related to employee Plan contributions between 2008 and 2014 to ensure amounts were correct and appropriately recorded by the Plan Administrator.
- We reviewed all (100%) payroll records related to employee contribution matches between 2008 and 2014 to ensure amounts were correct and appropriately recorded by the Plan Administrator.
- We reviewed all (100%) accounts payable records related to paid reimbursement claims between 2008 and 2014 to ensure amounts were correct and appropriately recorded by the Plan Administrator.

- We statistically sampled 71 out of 3,233 (2.20%) paid reimbursement claims between 2008 and 2014 to ensure amounts were correct and appropriately recorded by the Plan Administrator and paid claims were in accordance with Plan provisions.
- We reviewed all (100%) balance forfeitures between 2008 and 2014 to ensure the forfeiture was in accordance with Plan Provisions and appropriately recorded by the Plan Administrator.
- We statistically sampled the employment status of 63 out of 345 (18.26%) active and inactive Plan participants between 2008 and 2014 to determine if their balance should be forfeited in accordance with Plan provisions.
- We reviewed all (100%) monthly investment statements between 2008 and 2014 and agreed the total interest earnings with what was recorded by the Plan Administrator.
- We re-computed the monthly interest allocation of all (100%) plan participants between 2008 and 2014 to determine if the amounts agreed with the figures recorded by the Plan Administrator.
- We re-computed all (100%) active participant balances as of year-end 2014 to determine if the balance was in agreement with what was recorded by the Plan Administrator.
- We compared the year-end 2014 plan balance as per the Plan Administrator with what is recorded in SAP, the County's financial enterprise system.

Our audit scope included transactions processed between January 1, 2008 and December 31, 2014. Our last day of field work was April 27, 2015.

We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

RESULTS IN BRIEF

Plan transactions consisting of employee contributions, reimbursement of health premiums, and interest allocations are in accordance with Plan provisions. However, transactions are not always correct and properly recorded. Our audit identified eight plan participants who were not fully credited for their payroll contributions in July 2008. We identified one participant who was given credit for another participant's contribution match. We also found a systemic minor miscalculation in how interest is allocated to plan participants.

Plan balances agreed with amounts held with the Mass Mutual and with the Clark County financial records. However, we believe internal controls could be improved by implementing an independent review of the Plan ledgers.

Each finding includes a ranking of risk based on the risk assessment that takes into consideration the circumstances of the current condition including compensating controls and the potential impact on reputation and customer confidence, safety and health, finances, productivity, and the possibility of fines or legal penalties.

DETAILED RESULTS

Independent Periodic Review of Plan Ledgers Will Reduce the Risk of Fraudulent Acts and Significant Errors (MEDIUM)

During our audit, we found that the ledgers maintained by the Plan Administrator do not get reviewed. The Administrator performs the recording, reconciling, initiation of payments, and monitoring of all processes for the Plan.

The recording of employee contributions, claim reimbursement, forfeitures, and interest allocations into the Plan ledger is mainly a manual process performed by one person. Manual processes are susceptible to human error. The lack of segregation of duties combined with a manual process could allow fraudulent acts and significant errors to go undetected. Mitigating controls, such as a review process by a person independent of the Plan administration, can reduce this risk by deterring and detecting intentional or unintentional errors.

Recommendation

1. Implement a periodic review of the plan ledgers by an individual independent of the retirement health account administration process. The review should be sufficient to ensure that account

balances are accurate.

Payroll Contributions Not Accurately Recorded Lead to a Few Account Balance Errors (LOW)

During our testing we found 8 out of 92 contributing employees, or 8.70%, that did not get fully credited for a payroll cycle contribution in July 2008. This was a result of payroll reports being generated shortly before a cost of living adjustment raised employee salaries. The impact was isolated to those employees who elected to have a percentage of their wages withheld for Plan contributions, as opposed to a set dollar amount. The net impact was an allocation shortage of $320, with the majority belonging to one employee, who was under-allocated $269. The Plan Administrator identified the discrepancy while reconciling the fund balance, but attributed the discrepancy to an unrelated accounting error that occurred around the same timeframe. Because of this, the discrepancies were never rectified.

In 2011, we found one employee who was given credit for another employee's County contribution match of $480. The employees have adjacent names in the Plan ledger. An oversight during data entry caused the error. The error was caught during the reconciliation process and partially fixed in one section of the ledger. However, when carrying forward the participant balance, a reference was made to the section of the ledger with the incorrect data, causing the mistake to be carried forward year to year.

Failing to record payroll contributions leads to discrepancies in a participant's Plan balance. All contributions must be recorded and credited to each participant's account in accordance with Article IV, Section 4.03 the Plan agreement which states *"For convenience, and to facilitate an orderly administration of the Plan, individual participation accounts for all participants will be maintained by the County or Administrator showing the Participant's name with all applicable debit and credit balances. The Participant's deferred account shall be credited each pay period with the amount determine from the preceding pay period, if any."*

Recommendation

1. Adjust the balance of each participant who did not receive full credit for their payroll contribution in July 2008. If the participant is no longer active in the plan, issue a check.
2. Adjust the balances accordingly for the two participants who

were over/under credited for the contribution match in 2011.

Error in Interest Allocation Formula Causes Small Errors in Account Balances (LOW)

During our testing, we found an error in the interest allocation formula used in the Plan Administrator's ledgers. The intent of the formula was to allocate a participant's share of interest earnings based on their average monthly balance. However, the actual formula used did not calculate the average balance, and allocated interest based on the ending account balance. The miscalculation resulted in each Plan participant being over or under credited on their interest earnings. The formula has been in place since 2004.

We believe the financial impact on each participant is immaterial. Between 2008 and 2014 the average difference in interest allocation per participant, based on what was calculated and what should have been calculated, was approximately $0.10. In reviewing former participants who exhausted their account balances between 2008 and 2014 and were no longer active in the plan, we noted that the average discrepancy in interest allocation was approximately $0.55. The highest overpayment of interest was approximately $16 while the highest underpayment was approximately $17.

An accurate participant balance is required under Article IV, Section 4.02 of the Plan agreement which states *"A separate account, the Participation Account, shall be maintained for each Participant. Each participation account shall reflect the monies contributed by the County to the Trust and all consequences of the investment."* Inaccurate calculations and formulas compromise the integrity of a participant's balance.

Recommendation

1. Fix the interest allocation formula so that it is based on the average monthly balance.
2. Correct the balances for active participants.

JESSICA L. COLVIN
Comptroller

MEMORANDUM Office of the County Comptroller

To: Angela Darragh, Audit Director

From: Jessica Colvin, Comptroller

Subject: Retirement Health Account Audit

Date: 7/31/2015

This memo serves as the response to the Retirement Health Account Audit findings and recommendations.

Audit Finding #1: Independent periodic review of plan ledgers was not performed.

Management Response: The comptroller's office recently implemented internal controls that address this finding. Beginning in May 2015, an individual independent of the retirement health account administration process reviews the plan ledgers on a monthly basis.

Audit Finding #2: Payroll contributions not accurately recorded leading to a few account balance errors.

Management Response: The participant account balances will be corrected for the identified errors. If a participant is no longer active in the plan, a check will be issued. Additionally, the recent implementation of an independent review of ledger activity should prevent similar errors in the future.

Audit Finding #3: Error in interest allocation formula caused small errors in account balances.

Management Response: The formula will be adjusted to allocate interest based on the average monthly balance. The balances for active participants will be corrected.