

FISCAL AUDIT

DEPARTMENT OF PERSONNEL & CIVIL SERVICE COMMISSION

**VOLUNTARY EMPLOYEE BENEFICIARY ASSOCIATION TRUST FUNDS
(Workers' Compensation and Health & Welfare Benefits)**

Report by the
Office of City Controller

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May, 2015

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MICHAEL E. LAMB

CITY CONTROLLER

First Floor City-County Building • 414 Grant Street • Pittsburgh, Pennsylvania 15219

May 14, 2015

To the Honorables: Mayor William Peduto and
Members of Pittsburgh City Council:

The Office of the City Controller is pleased to present this Fiscal Review of the **Voluntary Employee Beneficiary Association Trust Funds (Workers' Compensation and Health & Welfare Benefits)** conducted pursuant to the Controller's powers under Section 404(b) of the Pittsburgh Home Rule Charter.

EXECUTIVE SUMMARY

The Voluntary Employee Beneficiary Association (VEBA) Trust Funds were established to account for monies reserved for the payments of workers' compensation obligations and health and welfare insurance premiums. The Workers' Compensation Medical Trust Fund was established in 1989 via resolution #823 for the payment of the City's workers' compensation medical expenses. The Health and Welfare Employee Beneficiary Association Trust Fund was established in 1996 via resolution #207 for payment of employee health insurance premiums.

We performed procedures to determine whether policies, procedures and internal controls over the payment of the City's VEBA trust funds obligations are adequate, and identified a need for improved controls over invoice payment processing and the monitoring of budgeted expense line items. Specifically, our procedures revealed the need for improved segregation of duties over the payment process. Invoice approvals, payment authorization as well as the execution of actual wire payments transfers were all performed by the Department of Personnel without any independent check during the period of our review, January 1 2012 to December 31 2013. Although the responsibility for executing the wire payments was transferred to the Treasurer early 2014, the Director of Personnel is still authorized to perform this function. Detail of our observations and recommendations are explained further in the Result section of this report.

We appreciate the cooperation of those involved with the administration of the fund.

Sincerely,

Michael E. Lamb
City Controller

INTRODUCTION

This fiscal review of the Voluntary Employee Beneficiary Association Trust Funds (VEBATF) was conducted pursuant to the Controller's powers under Section 404(b) of the Pittsburgh Home Rule Charter.

SCOPE AND METHODOLOGY

Our procedures were conducted pursuant to Article IV, Section 404(b) of the City of Pittsburgh Home Rule Charter and covered the period January 1, 2012 through December 31, 2013.

Our review examines whether payments made from the trust funds are properly supported and internal controls over the payment procedures are adequate and performed efficiently. Our procedures consisted primarily of inquiries and examination of relevant records. These procedures were neither designed nor intended to be a detailed audit of the VEBA funds. Specifically we:

- Interviewed personnel involved with the funds to gain an understanding of the funds' operations, processes and related internal controls.
- Reviewed procedures relating to the operation of the trust funds including the disbursement process.
- Reviewed relevant laws and regulations.
- Examined supporting documentation related to expenses charged to the funds.
- Summarized expenses paid from the funds during the period of our review.

BACKGROUND

The Voluntary Employee Beneficiary Association (VEBA) Trust Funds were established to account for monies reserved for the payments of workers' compensation obligations and health and welfare premiums. The Workers' Compensation Medical Trust Fund was established in 1989 via resolution #823 for the payment of the City's workers' compensation expenses. The Health and Welfare Employee Beneficiary Association Trust Fund was established in 1996 via resolution #207 to ensure timely payment of monthly premiums for health and welfare benefits. Both funds are funded via transfers from the City's General Fund.

Invoices for all VEBA related expenses are received monthly, reviewed and approved for payment by the Director of Personnel Department. Prior to February of 2014, wires for the payment of approved invoices were also executed by the Personnel Director.

Workers' Compensation Program

The City opted for self-insurance to meet and comply with its workers' compensation obligations with services provided under a "Managed Care" program provided by a third party administrator. The City contracted with the University Of Pittsburgh Medical Center (UPMC) Benefits Management Services Inc. to act as its "Third Party Administrator" (TPA) and administer its workers' compensation program. Under this program, the TPA provides a customized comprehensive program designed to provide a complete management services package that includes Claims Administration and Nurse Case Management Services.

Claims for work related injuries are initiated when an employee reports an injury to their department head and completes the appropriate work injury forms available online. The Personnel department contacts the TPA to initiate and process the claim. All submitted claims are reviewed and processed by TPA Case workers and the decisions on whether claims are accepted or rejected are made within 21 days and communicated to the employee. Accepted claims are eligible for workers' compensation benefits and employees whose claims are denied may appeal the decision. Benefits paid includes medical coverage for treatment of injuries, death benefits, disability compensation, indemnity (loss of wages) payments and other worker's compensation related expenses. All legal and settlement (when both sides agree to a onetime payment) expenses related to each case are paid after all the appeal or settlement process is completed. The costs of legal services to represent the City on appealed cases are also paid from the fund.

The fund is also used to pay for insurance brokerage fees and the premiums for excess workers' compensation insurance the City carries as required by Counsel Resolution #339.

A total of \$43,324,118* was transferred during the audit period January 1, 2012 to December 31, 2013 into the VEBA Workers' Compensation account to pay for related expenses.

A total of \$41,258,640* in actual expenses was paid during the same period as detailed on table I below:

Table I – Workers’ Compensation Trust Fund Expenditures For the Period January 1, 2012 to December 31, 2013			
Expense	2012	2013	Grand Total
Indemnity	\$ 11,938,729	\$ 12,047,039	\$ 23,985,768
Medical	5,048,952	4,451,228	9,500,180
Legal**	2,229,719	2,185,779	4,415,498
Settlements	1,969,274	1,387,920	3,357,194
Total	\$ 21,186,674	\$ 20,071,966	\$ 41,258,640*

*: Difference between the two amounts is attributed to timing issues

** : Includes TPA contract payments, excess insurance premiums and brokerage fees

Health & Welfare Benefits

The Health and Welfare Employee Beneficiary Association Trust Fund was established in 1996 via resolution #207 for the payment of employee health insurance premiums and other provisions under the City’s Health and Welfare Benefit Plan. The fund accounted for in a separate bank (trust) account is subject to both Commonwealth of Pennsylvania and Federal regulations and funded via transfers from the general fund (employer contributions and employee withholdings).

A total of \$96,567,406^ was transferred from the General Fund to the Health & Welfare Benefits trust fund account; \$46,918,471 in 2012 and \$49,648,935 in 2013 during the audit period January 1, 2012 to December 31, 2013. A total of \$89,967,367^ in actual expenses was paid for the same period as detailed below:

Table III – Health & Welfare Benefits Trust Fund Expenditures For the Period January 1, 2012 to December 31, 2013			
Expense	2012	2013	Grand Total
Health Insurance	\$ 32,588,444	\$ 28,677,521	\$ 61,265,965
Retiree health Insurance	14,901,623	13,778,215	28,679,838
Bank Fees	9,664	11,900	21,564
Total	\$ 47,499,731	\$ 42,467,636	\$ 89,967,367^

^Difference between the two amounts is attributed to timing issues

RESULT

Finding #1: Lack of Written Policies and Procedures

There are no formal policies and procedures governing the VEBA trust funds. Written policies and procedures define responsibilities as well as explain processes involved in accomplishing tasks involved in the collection and deposit of funds. To ensure adequate monitoring and management of the fund, detailed documentation of operating procedures that incorporate appropriate level of internal controls provide a foundation for an effective internal control structure. Without written policies and procedures, roles and responsibilities may not be clearly defined thereby making it difficult to establish and/or enforce accountability.

Recommendation

Develop detailed policies and procedures that include the duties and responsibilities involved with the collection and deposit of all rick receipt types. The policy and procedures should include authorization and documentation requirements for issuing any refund from the fund, deposit policy, record retention etc.

Finding #2: Inadequate Segregation of Duties over Payment Process

Duties and responsibilities over the VEBA expenses payment procedures were not adequately segregated during the period January 1, 2012 to December 31, 2013. The functions of authorizing invoice payments and executing wire transfers from the VEBA accounts were both performed by the Personnel Director. Although this practice was improved by transferring the function of executing the wire transfers to the Treasurer around February 2014, the Director is currently authorized to execute the wire transfers. In general, sound internal controls dictate key duties and responsibilities are segregated to reduce the risk of error or fraud and ensure fiscal integrity and transparency. The functions of approving the payment of invoices should be separated from executing wire transfers to pay the invoices.

Recommendation

- Eliminate the Personnel Director (including any Personnel staff) from the list of those approved to execute wire transfers from the VEBA accounts.
- Ensure back up for executing wire transfers from the VEBA accounts comes from the Treasurer's Office and not the Personnel Department.

Finding #3: Need for Independent Review

The Personnel Department does not have procedures in place to allow for independent verification of the VEBA payments function by the Controller's Office; invoices are approved by

the Personnel Department and the wire payments are executed by the Treasurer. The current practice of sending documentation to the Controller's Office after payments of the expenses to be recorded on the City's accounting system does not provide for an independent verification of the process prior to payments to ensure proper checks and balances. Involving the Controller's office to perform independent review prior to making payments will enhance fiscal monitoring and ensure sound internal controls within the City's functions and operations.

Recommendation

Implement procedures to allow for an independent verification of relevant documentation by the Controller's office prior to the Treasurer executing the wire payments. This could be achieved by notifying the Controller's Office when invoices are approved for payment by the Personnel Director prior to the Treasurer executing the wire payments. The Controller's Office will then notify the Treasurer to execute the wire payments. Implementing this recommendation will also help with the issue on segregation of duties identified above (finding #2).

Finding #4: Need for Improved Monitoring of Budgeted Expenses

There are no formal procedures for monitoring budgeted line items against invoices received for payment. Invoice amounts are not compared against established budgets to ensure amounts are within the amounts budgeted for that expenditure line item. As a result invoices maybe paid that are over the amounts specified per the budget line item. Reviewing budget amounts for each expense line item allows for the investigation of any variances between budgeted and actual amounts for each expense category. This also ensures budgeted line items are utilized as appropriate planning tool to provide control over overspending.

Recommendation

Establish a formal policy and procedure to implement a review of invoice amounts to budget before payments are made for each expense category to ensure the availability of funds. This will ensure that expenses for that particular category are within the established budget and also allow for proper monitoring of budget variances and allow for the timely development of corrective action when necessary.



CITY OF PITTSBURGH

Department of Personnel & Civil Service Commission

William Peduto, Mayor

Todd Siegel, Director

Michael E. Lamb
City Controller
City of Pittsburgh
Office of the City Controller
414 Grant Street
Pittsburgh, PA 15219

May 8, 2015

Response to the City of Pittsburgh Voluntary Employee Beneficiary Association Trust Funds (VEBA)
(Workers' Compensation and Health and Welfare Benefits)

The Department of Personnel and Civil Service is in receipt of your audit report. We appreciate your input and efforts in gathering the information presented in the audit. We recognize and acknowledge that there is always room for improvement in any program. As we move forward with our response, we are pleased to note that the audit did not find the VEBAs lacking in requirements necessary to meet State and Federal regulations. In addition, we are pleased to see that your audit has found a balance of funding and distribution in both of the VEBA accounts.

The following document addresses the findings and recommendations of the audit and presents action plans where appropriate. Our goal is to provide the workers of the City of Pittsburgh with a seamless benefits experience so they can concentrate on their work and home life.

Again, we appreciate your input and are confident the action plans outlined in our response will contribute to the continued success of our programs.

Sincerely,

Todd Siegel
Director

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PITTSBURGH
A MOST LIVABLE CITY

**DEPARTMENT OF PERSONNEL AND
CIVIL SERVICE COMMISSION**

RESPONSE TO THE CONTROLLER'S DRAFT FISCAL AUDIT

**VOLUNTARY AND EMPLOYEE BENEFICIARY ASSOCIATION TRUST FUNDS
(Workers' Compensation and Health & Welfare Benefits)(VEBA)**

May 2015

Recommendation No. 1:

Develop detailed policies and procedures that include the duties and responsibilities involved with the collection and deposit of all rink receipt types. The policy and procedures should include authorization and documentation requirements for issuing any refund from the fund, deposit policy, record retention etc.

Response to Recommendation No. 1:

Upon review of your draft audit, Personnel immediately implemented documentation of policies and procedures in relation to the VEBA accounts. While much of the procedures are governed by the City of Pittsburgh cash management policy, we will prepare thorough documentation of the policies and procedures for the VEBA accounts that are in conjunction with Citywide policies.

Recommendation No. 2:

Eliminate the Personnel Director (including any Personnel staff) from the list of those approved to execute wire transfers from the VEBA accounts.

Ensure back up for executing wire transfers from the VEBA accounts comes from the Treasurer's Office and not the Personnel Department.

Response to Recommendation No. 2:

We are pleased to note that prior to the release of this draft audit, Personnel did remove all Personnel employees from the approval process for the wire transfers from the VEBA accounts. Currently, as you recommend above, the Treasurer is the approval party and another employee from the Treasurer's office is her back up.

Recommendation No. 3:

Implement procedures to allow for an independent verification of relevant documentation by the Controller's Office prior to the Treasurer executing the wire payments. This could be achieved by notifying the Controller's Office when invoices are approved for payment by the Personnel Director prior to the Treasurer executing the wire payments. The Controller's Office will then notify the Treasurer to execute the wire payments. Implementing this recommendation will also help with the issue on segregation of duties identified above (finding #2).

Response to Recommendation No. 3:

While the segregation of duties as noted (Response to Recommendation No. 2) were addressed prior to the receipt of this draft fiscal audit, Personnel will further review our processes and determine the best way to implement this recommendation.

Recommendation No. 4

Establish a formal policy and procedure to implement a review of invoice amounts to budget before payments are made for each expense category to ensure the availability of funds. This will ensure that expenses for that particular category are within the established budget and also allow for proper monitoring of budget variances and allow for the timely development of corrective action when necessary.

Response to Recommendation No. 4:

Some of the procedures in place may not have been thoroughly defined during the audit interview. In regard to payments from the Health and Welfare VEBA, the benefits are divided into retiree and active and a request is sent to transfer the exact funds from the appropriate General Fund account. After the transfer has been approved and completed, the funds are disbursed from the VEBA. This ensures the appropriate budget checks are run and expenditures are properly recorded in the General Fund accounts. The Workers' Compensation VEBA does present a bigger challenge as the City is required by the State to transfer \$6M monthly into the VEBA account in order to maintain the City's self-insured status. Proof of this transfer is sent monthly to the State. Another condition to maintain our self-insured status is that all payments related to workers' compensation be paid out of the VEBA. All of the individual account information is still available by account number, but needs to be accessed through the VEBA fund, not the General Fund. Personnel is willing to explore specific recommendations that are administratively feasible while still meeting the requirements of the state.

Conclusion:

In conclusion, we are again pleased with the results of the fiscal audit and will take steps to explore the two recommendations that have not already been implemented.