Follow-Up Review of Review of Broward County Employee Benefits Internal Service Fund

Office of the County Auditor

Robert Melton, CPA, CIA, CFE, CIG
County Auditor

Review Conducted by:
Jed Shank, CPA, CIA, Audit Manager
Sahil Grover, CPA, CIA, Staff Auditor

Report No. 19-23
September 30, 2019
September 30, 2019.

Honorable Mayor and Board of County Commissioners,

We have conducted a follow-up review of our Review of Broward County Employee Benefits Internal Service Fund. The objective of our review was to determine the implementation status of our previous recommendations.

All three of the previous recommendations were implemented. We commend management on implementing all recommendations.

We conducted this review in accordance with Generally Accepted Government Auditing Standards. Those standards require that we plan and perform the review to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our review objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our review objectives.

We appreciate the cooperation and assistance provided by the Finance and Administrative Services Department and Office of Management and Budget throughout our review process.

Respectfully submitted,

Bob Melton
County Auditor

cc: Bertha Henry, County Administrator
    Andrew Meyers, County Attorney
    Monica Cepero, Deputy County Administrator
    George Tablack, Chief Financial Officer
    Kevin Kelleher, Deputy Chief Financial Officer
    David Kahn, Director, Human Resources
    Norman Foster, Director, Office of Management and Budget
    Kristin Carpenter, Director, Accounting Division
# TABLE OF CONTENTS

**INTRODUCTION**

- Scope and Methodology .............................................................................................................................. 1
- Overall Conclusion ........................................................................................................................................ 1
- Background .................................................................................................................................................. 2

**OPPORTUNITIES FOR IMPROVEMENT**

- The Fund Balance Should be Reduced and Charges to County Agencies and Employees Should be Based on Actual Costs ......................................................................................................................... 4

**APPENDICES**

- Appendix A - Discussion of Revenues and Expenditures Impact on Fund Balance ................................. 8
- Appendix B – Management’s Response to Audit (Dated May 8, 2019) ...................................................... 9
- Appendix C - Update to Management’s Response to Audit (Dated October 1, 2018) ............................ 17
- Appendix D – Management Update to Follow-up to Audit Report (Dated September 9, 2019) ........ 19
INTRODUCTION

Scope and Methodology

The Office of the County Auditor conducts audits of Broward County’s entities, programs, activities, and contractors to provide the Board of County Commissioners, Broward County’s residents, County management, and other stakeholders unbiased, timely, and relevant information for use in promoting government accountability and stewardship and improving government operations.

We conducted a follow-up review of the Review of the Broward County Employee Benefits Internal Service Fund (Fund). The purpose of our follow-up was to determine the status of previous recommendations for improvement.

The objectives of the original review were:

1. To Determine whether the Fund balance and related allocation of costs were reasonable and appropriate, and

2. To determine opportunities for improvement.

We conducted this review in accordance with Generally Accepted Government Auditing Standards. Those standards require that we plan and perform the review to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our review objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our review objectives.

Our follow-up review included such tests of records and other auditing procedures, as we considered necessary in the circumstances. The review period was May 10, 2018 through September 9, 2019.

Overall Conclusion

All three of our previous recommendations were implemented. We commend management on implementing our recommendations.
Background

The County offers an array of employee benefit programs including Group Health (including pharmacy), Dental, and Vision. Employees can choose various coverage options ranging from opt out (no coverage) to family coverage. The County pays the majority of group health insurance costs for its employees (employer portion) and employees pay a premium (employee portion), which varies based on the type(s) of group health insurance the employee chooses.

Group health insurance costs are charged as expenses to the agencies, and monies are transferred from the agencies as revenue to the Fund. The employee portion of health premiums are also transferred into the fund via payroll deductions. Actual expenditures are paid from the Fund. Therefore, the fund should function on a cost reimbursement basis.

Budgeting Group Health Insurance Costs

OMB forecasts group health insurance costs on an annual basis. These costs include health insurance and pharmacy claims costs, third party administrator fees for claims processing, funding for employee Health Reimbursement/Savings Accounts, and opt out payments for those waiving coverage. The costs also include the costs of the Employee Benefits Administration and the Employee Assistance Program Sections of the Human Resources Division.

OMB also forecasts the revenues from employee payroll deductions for premiums, interest income and surcharges. The total estimated revenue less the estimated cost is the net cost for group health insurance that OMB estimates the County must contribute to the Employee Benefits Internal Service Fund (Fund).

The net cost for group health insurance is divided by the total number of County employees resulting in the estimated cost per position of health insurance for the next fiscal year. This estimated cost per position is then multiplied by each agency budgeted position to determine health insurance costs budgeted for each agency.
Accounting for Group Health Insurance Costs

When an agency is charged for health insurance, the funding moves from the agency’s budget into the Fund. The Fund in turn recognizes the transfers from the agency as revenue. The employee portion of health premiums are also transferred into the fund via payroll deductions. Actual health insurance expenses are paid out of the Fund. Figure 1 illustrates the flow of funds for Group Health Insurance.

Figure 1 – Funding of Group Health Insurance Costs
This section reports follow-up on actions taken by management on the Findings in our previous review. The issues and recommendations herein are those of the original review, followed by the current status of the recommendations.

**The Fund Balance Should be Reduced and Charges to County Agencies and Employees Should be Based on Actual Costs.**

An excess of $6.6 to $12.6 million has accumulated in the Employee Benefits Internal Service Fund as of September 30, 2017. The actual cash balance of the fund was $31.6 million which, along with other assets and accrued liabilities, resulted in a fund balance of $22.6 million as of September 30, 2017. Generally, governmental accounting literature specifies that internal service funds should operate on a break-even basis. However, in the operation of a self-insurance fund, we believe it is reasonable and prudent to also maintain a level of reserves. Accordingly, Figure 2 presents the elements comprising the fund balance of $22.6 million and two options for establishing appropriate reserves. This results in a $6.6 to $12.6 million excess balance as follows:

Figure 2 – Benefits Internal Service Fund Excess Fund Balance

<table>
<thead>
<tr>
<th>Benefits Internal Service Fund Excess Fund Balance As of September 30, 2017 (Unaudited)</th>
<th>Current</th>
<th>Option 1</th>
<th>Option 2</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cash</td>
<td>$31,605,313</td>
<td>$31,605,313</td>
<td>$31,605,313</td>
</tr>
<tr>
<td>Other Assets</td>
<td>3,285,925</td>
<td>3,285,925</td>
<td>3,285,925</td>
</tr>
<tr>
<td>Accounts Payable</td>
<td>(1,723,101)</td>
<td>(1,723,101)</td>
<td>(1,723,101)</td>
</tr>
<tr>
<td>Accrued Liabilities</td>
<td>(6,292,231)</td>
<td>(6,292,231)</td>
<td>(6,292,231)</td>
</tr>
<tr>
<td>Claim Reserve</td>
<td>(4,265,000)</td>
<td>(4,265,000)</td>
<td>(4,265,000)</td>
</tr>
<tr>
<td>Fund Balance</td>
<td><strong>22,610,906</strong></td>
<td><strong>22,610,906</strong></td>
<td><strong>22,610,906</strong></td>
</tr>
<tr>
<td>Catastrophic Loss Reserve</td>
<td>(10,000,000)</td>
<td>(10,000,000)</td>
<td></td>
</tr>
<tr>
<td>Rate Stabilization Reserve</td>
<td></td>
<td>(6,000,000)</td>
<td></td>
</tr>
<tr>
<td>Excess Fund Balance</td>
<td><strong>$22,610,906</strong></td>
<td><strong>$12,610,906</strong></td>
<td><strong>$6,610,906</strong></td>
</tr>
</tbody>
</table>

Source: Auditor compilation from PeopleSoft accounting system

Figure 2 presents two options for establishing appropriate reserves to address the fund balance. To calculate recommended reserves, we considered the nature of expenses of the fund and the potential need for stabilization in the event of a spike in claims. The potential for huge spikes is minimized using stop-loss insurance.
**Option 1** considers a conservative reserve policy to be 60 days of anticipated claims which is $10.0 million (based on estimated annual claims of $60 million). While not statutorily required, this reserve appears to be consistent with the guidelines established by the State of Florida Office of Insurance Regulation (FOIR). The County is required to annually submit Form OIR-B2-574, titled “General Information and Surplus Statements for Self-Funded Health Benefit Plans” to the FOIR. The form states “If the plan’s surplus is less than sixty days of anticipated claims, other questions may be asked of the plan as the office sees fit.” Accordingly, Option 1 applies a $10.0 million reserve shown in Figure 2 as a *Catastrophic Loss Reserve*. This results in an excess fund balance of $12.6 million as of September 30, 2017.

**Option 2** is a more conservative reserve policy. This option includes the *Catastrophic Loss Reserve* established in Option 1 and further considers the need for stabilization of annual charges to employees and County agencies. Option 2 applies an additional reserve of 10% of annual claims which is $6.0 million (based on estimated annual claims of $60 million) and is shown in Figure 2 as a *Rate Stabilization Reserve* in addition to the *Catastrophic Loss Reserve*. This results in an excess fund balance of $6.6 million as of September 30, 2017.

The remaining excess balance of $6.6 to $12.6 million has occurred because the fund is not functioning on a cost reimbursement basis. Since fiscal year end 2010, County funds, agencies, and employees have been overcharged by amounts in excess of the actual costs incurred by the fund. Costs incurred represent payments out of the fund for actual group health costs.

Overcharges to County agencies and employees reduce the amount of available funds to provide programs and services to Broward County citizens. In addition, overcharges of costs to grant, enterprise, and other funds may require the County to refund the excess amounts. Certain grant, enterprise, and other funds are governed by strict financial regulatory requirements which may require Broward County to refund such overcharges. For example, charges to grant funds are typically reimbursed by the grantor but those charges should be based on actual expenditures. In addition, inaccurately charging costs to the various County agencies reduces funding available to County agencies to deliver programs and services to the citizens of Broward County.

As shown in Figure 3, the fund balance has grown from $5.8 million as of September 30, 2011 to $22.6 million as of September 30, 2017.
Figure 3 – Benefits Internal Service Fund – Fund Balance

Source: Auditor compilation from Advantage and PeopleSoft accounting systems
* The County became self-insured effective January 1, 2015.

Appendix A further describes the transactions within the Fund that impact the fund balance. As described in the background, group health insurance costs are charged to agencies and monies are transferred from the agencies to the employee benefits internal service fund (Fund). Actual expenditures are paid from the Fund. Therefore, the Fund should function on a cost reimbursement basis.

The Governmental Accounting Standards Board Statement No. 34 states “Internal Service Funds are used to report any activity that provides goods or services to other funds, departments, or agencies of the primary government and its component units, or to other governments, on a cost reimbursement basis.”

A potential cause of overcharges to County agencies and accumulation of excessive fund balance within the employee benefits internal service fund is OMB’s practice not to include the ending fund balance from the prior year as revenue in the calculation of per position cost charged to the agencies for the following year. Including the prior fund balance will reallocate an appropriate portion of surplus revenues from the prior year back to group health insurance costs in the next fiscal year resulting in the reduction of charges to agencies and maintenance of appropriate reserve levels. For example, as described in the background, OMB forecasts group health insurance costs and offsetting revenue to calculate the per position cost charged to the agencies. The ending fund balance from the prior year should be included as a revenue and desired ending fund balance for the following year should be included as an expense.
Another potential cause of overcharges to County agencies and accumulation of excessive fund balance within the employee benefits internal service fund is that charges to County agencies are not adequately applied based on actual positions and are reliant upon direction from OMB. The Accounting Division charges group health insurance costs to agencies via quarterly journal entries based on the budgeted amount developed by OMB for each budgeted FTE. While utilizing the budgeted amount is appropriate, charges should be applied to actual filled positions. Further, the Accounting Division relies upon direction from OMB in determining how much to charge the agencies in the fourth quarter of each year. The charges should be applied independent of OMB.

Management has also advised of the significant changes that have occurred over the past three years which may have contributed to the excess fund balance. Starting in fiscal year 2015, the County switched to a self-insured group health insurance model. This resulted in greater uncertainties and changes in costs structure as has changes in employee health plans (e.g., more employees enrolled in high deductible health plans). Management believes these are significant contributors to the $22.6 million as of September 30, 2017.

Sound financial management practices require that revenues be established at a level that approximates actual costs along with the maintenance of a reasonable reserve. We do not consider an excess balance of $6.6 to $12.6 million to be reasonable or necessary. Consequently, action should be taken to reduce the fund balance to a reasonable level.

**We recommend** management:

A) Establish a policy requiring reserves be maintained in an amount to be reasonable. These reserves should be maintained at a target level, with any excesses or shortfalls being taken into account during the annual premium-setting process.

B) Refund $6.6 to $12.6 million to the employees and agencies that paid the excess charges, including grant and enterprise funds, or as an alternative, establish planned reductions over time to reduce the fund balance to an appropriate level.

C) Charge group health care costs to agencies based on actual filled positions.

**Status:**

A) **Implemented.** Management established a reserve policy to hold an amount equal to three months of claims cost.

B) **Implemented.** Management established planned reductions over time to reduce the fund balance to an appropriate level. The fund balance dropped from $22.6 million as of September 30, 2017 to $17.6 million as of September 30, 2018. Based on data as of June 30, 2019, Management forecasts the fund balance as of September 30, 2019 to be between $15.8 and $17.7 million.

C) **Implemented.** Agencies are charged a portion of group health care costs each pay period based on the actual filled positions that pay period.
Appendix A - Discussion of Revenues and Expenditures Impact on Fund Balance.

Figure 4 shows the employee benefits internal service fund revenues and expenditures that impact the fund balances, including the annual surplus (deficit) charged to the County agencies as compared to the actual amounts required for payment of actual group health insurance costs. For fiscal years 2011 through 2017, the net surplus exceeded $14.2 million. These surpluses have resulted in the accumulated fund balance of $22.6 million within the Fund as of September 30, 2017.

Figure 4 – Benefits Internal Service Fund
Statement of Revenues, Expenses and Changes in Net Position (Fund Balance)

| Fiscal Years Ended September 30, 2011 through 2017 (Unaudited) (In Thousands) |
|---|---|---|---|---|---|---|---|
| Employer Portion | 47,911 | 48,532 | 49,676 | 48,814 | 55,497 | 50,823 | 58,890 |
| Employee Portion (a) | 3,972 | 4,034 | 4,152 | 5,260 | 6,374 | - | - |
| COBRA/Retire Contribution (a) | 521 | 570 | 574 | 681 | 1,419 | - | - |
| Total Group Health Insurance Revenues | 52,404 | 53,136 | 54,402 | 54,755 | 63,289 | 50,823 | 58,890 |
| Group Health Insurance Premium | 34,466 | 33,548 | 33,856 | 35,978 | 29,742 | 25,369 | 25,771 |
| Prescription Plan Costs | 11,016 | 10,632 | 11,462 | 14,608 | 17,041 | 11,534 | 9,169 |
| HRA/HSA COST | 4,710 | 2,508 | 4,583 | 4,714 | 5,162 | 12,157 | 9,297 |
| Administrator Fees-TPA/Broker Services | - | - | - | - | 3,059 | 3,028 | 4,499 |
| Benefits Administration Costs | 1,397 | 1,321 | 1,479 | 1,558 | 1,741 | 1,933 | 1,858 |
| Self Insurance Liability Accrual | - | - | - | - | 2,763 | 1,104 | 398 |
| Total Group Health Insurance Costs | 51,590 | 48,009 | 51,380 | 56,858 | 59,507 | 55,124 | 50,992 |
| Group Health Insurance Surplus (Shortfall) | 814 | 5,127 | 3,022 | (2,104) | 3,782 | (4,301) | 7,898 |
| Other Pass Through Surplus (Shortfall) | 1,103 | 812 | 895 | (59) | 713 | 694 | 371 |
| Change in Net Position | 1,917 | 5,939 | 3,917 | (2,162) | 4,495 | (3,607) | 8,269 |
| Beginning Net Position | 3,843 | 5,760 | 11,699 | 15,616 | 13,454 | 17,949 | 14,342 |
| Ending Net Position (Fund Balance) | 5,760 | 11,699 | 15,616 | 13,454 | 17,949 | 14,342 | 22,611 |

Source: Auditor compilation from Advantage and PeopleSoft accounting system
(a) Effective fiscal year 2016, the employee portion was applied to and netted against the Group Health Insurance Premium cost. Accordingly, in fiscal year 2016 and 2017 the group health insurance premium reflects the total cost, net of employee contribution.
Appendix B – Management’s Response to Audit (Dated May 8, 2018)

MEMORANDUM

TO: Robert Melton, CPA, CIA, CFE, CIG  
    County Auditor

FROM: Bertha Henry  
    County Administrator

DATE: May 8, 2018

RE: Management’s Response to Audit Report Regarding Review of the Broward County Employee Benefits Internal Service Fund

Management has reviewed the County Auditor’s Report regarding the Employee Benefits Internal Service Fund (Fund). While Management concurs that a policy should be developed describing reserve levels for the self-insured health and pharmacy plans, the uncertain and changing nature of the health care market, the County’s rationale for responding to that uncertainty by moving to a self-insurance model, and the County’s experience with the first few years of self-insurance, means that a number of factors have to be assessed in developing a prudent reserve level.

Health Care Costs from a National Perspective

Health plan costs (medical and pharmacy) are a major concern of U.S. employers due to the high cost to provide health care to employees and the dramatic increases in average health plan costs over the past decade. In fact, average health care costs have increased about 55% from 2007 to 2017.¹

Many factors have contributed to these increases, including:
- Federal and state benefit mandates, including the Affordable Care Act of 2010
- Aging population
- Advances in medical technology and prescription medications
- Direct-to-consumer advertising and increased consumer demand
- Unhealthy lifestyles

Regardless of the reasons behind the increases, most employers are not able to absorb increases of that magnitude over the long term, particularly in the recent economy. The magnitude and volatility of health plan costs are a national issue and have an impact on Broward County as well.

Impact on Broward County and Its Response

Like the rest of the country, Broward County was impacted by the volatility in the health care market. The County was faced with multiple years of double-digit increases with a recent high increase of 29% in 2011. To mitigate recurring large increases, the County implemented various strategies to address cost increases (including going from three providers to a sole provider in 2008, made significant plan design changes, eliminated high-costing plans such as PPO’s, and rebid two years in a row when necessary. These constant and drastic changes every year were very unsettling to employees.

To address this instability, Management’s goal for the medical and pharmacy plans over the past five to six years has been to:

- Provide affordable quality healthcare
- Improve health of our workforce
- Provide overall long-term stability to benefit plan and cost

A major part of this stabilization strategy was for the County to consider self-insuring medical as a funding option.

What is a self-insured plan and why self-insure?

With a self-insured (or self-funded) plan, the employer bears the risk of all costs incurred under the plan for claims and administration. Conversely, under a fully-insured funding model, the employer pays a premium to the insurance company to cover claims and administration costs, and the insurance company bears the full responsibility for paying all incurred claims and retains any premiums that exceed the claims.

There are many reasons why self-insuring a health plan (medical and pharmacy) is attractive to a group of the County’s size:

- Not subject to many federal insurance laws;
- Exempted from state premium taxes on claims costs;
- Exempted from state regulations (i.e. insuring dependent to age 30)
- Cash flow advantage of paying claims as incurred versus a flat rate;
- Exempted from several Affordable Care Act requirements.

The County’s Decision to Self-Insure

As the County’s pharmacy plan had been self-insured since 2001 and was running smoothly, the Board had expressed an interest in moving from a fully-insured medical program to a self-insured medical program for many years. Due to the volatility and high increases in health care, as well as concerns over the accuracy of claims utilization data, our Benefits Consultant cautioned that the change to self-insurance needed careful timing and planning for the transition. The Consultant and Management worked together to come up with a four- to five-year strategy to mitigate high increases, stabilize the health plans and build reserves to move toward self-insuring.
Since the County switched to a self-insurance model in 2015, staff has strived to maintain a $14-$15 million reserve due to the additional risk and potential volatility of the health care market, in addition to the newness of the program and available data (i.e., only two years of claims history when the FY18 budget was developed). Figure 3 of the Auditor’s report demonstrates the success of Management’s strategy to stabilize the benefit plan and costs to the County and employee while maintaining an adequate reserve level:

![Fund Balance Chart]

**Setting Reserves**

A major part of self-insuring is ensuring that there are a sufficient amount of reserves to cover the various contingencies that face a self-insured plan. According to an industry white paper from the Self-Insurance Institute of America, Inc. (SIIA), a national association dedicated to protecting and promoting the business interests of organizations involved in self-insurance, “the maintenance of appropriate reserves is critical to the financial health of a self-funded health care plan.”

The white paper further explains the following four types of reserves that may apply to a self-insured plan:

- **Incurred but Not Reported (IBNR) Claims Reserve** – establish sufficient funds to pay claims that are incurred during the coverage period but have not yet been reported to the claims administrator.
- **Administrative Reserve** – funds established to cover administrative expenses for the run-out of claims should the self-funded plan become insured or terminate.
- **Risk Factor Reserve** – funds established to cover the amount the employer is responsible for before aggregate stop-loss insurance is triggered. For the County, that amount is 20% meaning that the County is responsible for the first 120% of costs before the aggregate stop-loss coverage would cover.
- **Rate Stabilization Reserve** – funds established to offset the costs so they do not need to drastically change from year to year.

According to the SIIA, these four reserves are generally 25% to 35% of total annual plan costs.

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State Regulations

There are many different rules and regulations that govern accounting functions and benefit plans, such as actuarial soundness and reserves.

Florida Statutes allows local government to self-insure for its health plan subject to the approval based on actuarial soundness by the Florida Office of Insurance Regulation (FLOIR). FLOIR requires an annual filing for self-insured plans, which includes: an actuarial memorandum; annual rate certification; annual report and operating projections for the current year plus the next two years for self-funded health benefit plans, along with supporting documentation.

According to FLOIR, Rule 690-140.053, Florida Administrative Code, establishes a minimum surplus standard of 60 days of anticipated claims, also referred to as the “safe harbor guidelines”. If a self-funded health plan made an annual filing which does not satisfy the 60-day surplus requirement, the FLOIR would need to make a determination of whether the plan was actuarially sound. The failure to hold at least 60 days of claims reserves would call into question whether claims reserves were adequate and whether the plan was sufficiently funded to respond to adverse loss development. If the FLOIR determines that the reserves are not in accordance with sound actuarial principles, the plan could be determined to be deficient; at which point, the FLOIR may withdraw approval. Without approval, a self-funded health plan may not operate in Florida.

County’s Process

Under a self-insured plan, the County pays the actual health and pharmacy claims costs plus an administrative fee to a third party administrator to manage the plan and adjudicate claims. The plan is required to develop actuarial sound plan equivalent rates, by plan and tier, each year, which include the cost of claims and third party administrator fees. The County’s Consultant prepares combined health and pharmacy plan equivalent rates each year. The plan equivalent rates do not include Benefits Administration staff or Employee Assistance staff expenses.

The Consultant also works with Staff and the Office of Management and Budget (OMB) to project the overall level of costs for the upcoming fiscal year. As this process is completed very early in the calendar year for the upcoming fiscal year, the Consultant provides published industry projections to assist OMB with forecasting upcoming fiscal year rates by plan and tier of coverage.

OMB’s Role

The Office of Management and Budget (OMB) routinely forecasts revenues and expenses throughout the year to ensure that current year expenses remain within the budgeted amounts, to assist with projecting expenses for the upcoming new fiscal year, and to estimate the amount of fund balance remaining at the end of the fiscal year in order to include the amount in the new year’s Adopted Budget.

3 Florida Statutes, Section 112.08.
As shown in the Adopted Budget (see relevant page attached), the estimated FY17 year-end fund balance is included in the FY18 Adopted Budget, and is included in every Adopted Budget. In the Employee Benefits Fund, the fund balance is generally appropriated to a reserve for the following purposes:

- To ensure funding is available in the event that there are spikes in health and pharmacy claims,
- To cover the County’s share of claims that must be paid before the stop-gap policy coverage begins, and
- To ensure that there are sufficient funds to pay all claims should the County determine that it is advantageous to return to purchasing health insurance

Reserving funds for the above purposes is in accordance with the Section 20.10 of the Administrative Code, which provides the fund balance policy.

The audited financial statements indicate that the actual fund balance remaining at the end of FY17 was $22.6 million, which is $7.4 million more than the amount estimated during the budget development process. There are many variables that impact the fund balance, but the primary reason is that the County received more in prescription rebates than the prior fiscal year due to the implementation of a new pharmacy agreement on January 1, 2017 and outstanding rebates from 2016 as part of the transition to a new pharmacy benefit manager. Some of these additional rebates were received after FY17 ended. Staff is working on estimating a more accurate rebate estimate based on the new agreement to use in developing the FY19 budget.

**Internal Services Funds**

As described in the audit report, employee benefits are largely paid from an “Internal Service Fund”, which is supported with charges to agency budgets. From a budget standpoint, using Internal Service Funds for programs, such as Fleet Services, Risk Management and Employee Benefits, enables agency budgets to better reflect the full cost of providing a particular service. The Government Finance Officers Association (GFOA) gives a short summary of this approach:

“Internal services are those responsibilities a government provides to support its own internal operations. Common examples of internal services include information technology, payroll, motor pool, budgeting, legal, accounting, and human resources. Certain management objectives are served by creating a system to assign prices for the use of these internal services, which are then assessed to the departments that use the services. However, there is a cost to develop and maintain internal pricing systems. Governments must weigh the benefits of an internal services costing system against the cost and complexity of system design choices.”

The County currently budgets for all employee benefit programs in the Employee Benefits Internal Service Fund. In addition to health care and pharmacy premiums, the salaries of Employee Benefits staff that works with employees and administers the employee benefit program, as well as the Employee Assistance Program, are all included in the Internal Service Fund. These costs are allocated to each agency based on a blended rate per budgeted position.
May 8, 2018
Robert Melton, County Auditor
Management Response to Audit of Employee Benefits Internal Service Fund

Page 6 of 7

Follow-up Review of Review of Broward County Employee Benefits Internal Service Fund

Management’s Responses to the Recommendations

Based on the foregoing background and taking into consideration the newness of our self-insured program, the volatility of the health care market, and maintaining a prudent reserve level, below are Management’s responses to the Auditor’s recommendations:

Recommendation A:

Management concurs with the recommendation to establish a policy creating a reserve amount for the employee benefit self-insurance fund.

Since the County switched to a self-insurance model, staff has strived to maintain a $14-$15 million reserve to cover the additional risk, volatility of the health care industry, and limited data due to the recent establishment of the program. Staff agrees that it would be prudent to formalize our current reserve policy, which equates to approximately three months of program costs. Maintaining three months of program costs will take into account the other potential contingencies (not just IBNR) and is consistent with the amount estimated by SIIA of 25% to 35% of the total annual program costs. More importantly, three months of program costs will pass the FLOIR’s 60-day surplus requirement. It is also noted that the amount of three months reserve is comparable to Option 2 suggested in the Auditor’s Report.

Management would not recommend Option 1 as that reserve policy of 60 days of anticipated claims is the threshold amount required by FLOIR and any use of this reserve that brought the reserve level below the 60-day surplus requirement would call into question by FLOIR whether claims reserves were adequate and whether the plan was sufficiently funded to respond to adverse loss development. If the plan is determined to have deficient funding, FLOIR may withdraw approval and without approval, the County’s self-funded health plan would not be able to operate in Florida. FLOIR approval is statutorily required. Additionally, funding reserves at the FLOIR 60-day surplus requirement does not allow for the County to absorb any fluctuations in claims and may subject employees to drastic rate increases to maintain the FLOIR 60-day surplus requirement.

Recommendation B:

Management concurs with the recommendation to address the additional funding over three months ($15 million), which was contributed by all funds including the General Fund and self-supporting funds. As provided in the Auditor’s report, the County is establishing planned reductions over time to reduce the reserves to an appropriate level without comprising the County’s ability to meet the FLOIR’s 60-day surplus requirement or address claim fluctuations without drastic increases.

There are many options for addressing the additional funding over $15 million. Despite FY’19 forecasted increases in health care and pharmacy costs as well as costs to administer, at this point in the budget development process, staff has not adjusted the amount budgeted to agencies for the FY’19 Core Budget, which will reduce the health care reserve if cost increases do occur as projected. In addition, staff plans to review the performance of the plan mid-year to determine if other adjustments are necessary.
May 8, 2018
Robert Melton, County Auditor
Management Response to Audit of Employee Benefit Internal Services Fund

Page 7 of 7

**Recommendation C:**

Management concurs with the recommendation to charge the cost for employee benefits to agencies based on actual filled positions.

Management is developing a process to charge each agency in a manner that would factor in vacancies. To avoid any issues with transitioning mid-year, the implementation of this new process is anticipated to begin with the new FY19 budget year. Additionally, when the Human Capital Management (HCM) component of the ERP system is fully functioning, Management will reevaluate this methodology.

**Conclusion**

Management appreciates the opportunity to respond to the Auditor’s Report in order to highlight that the County’s proactive strategies to achieving multi-year stability in funding of County employee health care costs has been successful. Management agrees that it is timely to review the level of reserves now that a few years’ experience is available and to formally establish a reserve level policy.

If there are any additions, deletions/omissions, or other changes or modifications to Management's response, please provide us the opportunity to review prior to issuance. Should you have any questions, please do not hesitate to contact me.

**Attachment:** Fiscal Year 2018 Adopted Operating Budget; Human Resources – Employee Benefits Fund

c: Mayor and Broward County Commissioners
   Monica Cepero, Deputy County Administrator
   Andrew Meyers, County Attorney
   George Tablack, CPA, Chief Financial Officer
   Kevin Kelleher, Deputy Chief Financial Officer
   Norman Foster, Director, Office of Management and Budget
   Marci Gelman, Assistant Director, Office of Management and Budget
   David Mackenzie, Senior Budget Management Analyst, Office of Management and Budget
   Mary McDonald, Acting Director, Human Resources Division
   Lisa Morrison, Employee Benefits Manager, Human Resources Division
   Susan Friend, Director, Accounting Division
### SECTION SUMMARY

<table>
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<tr>
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<th>FY16 Actual</th>
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<th>FY18 Budget</th>
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<tr>
<td>Employee Assistance Program</td>
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<td>Employee Benefit Services</td>
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<td>Employee Benefits Administration</td>
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<td>Reserve</td>
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<td>$14,936,602</td>
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<td>$53,966,883</td>
<td>$70,975,450</td>
<td>$74,996,460</td>
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### REVENUES

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<th>FY16 Actual</th>
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<tr>
<td>Miscellaneous Revenue</td>
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<td>Charges For Services</td>
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<td>Less 5%</td>
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<td>Interest Earnings</td>
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### APPROPRIATIONS

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<td>Personal Services</td>
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<td>Operating Expenses</td>
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<td>Capital Outlay</td>
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Follow-up Review of Review of Broward County Employee Benefits Internal Service Fund

Appendix C- Update to Management’s Response to Audit (Dated October 1, 2018)

TO: Robert Melton, CPA, CIA, CFE, CIG
County Auditor

FROM: Kevin Kelleher, Deputy Chief Financial Officer
Finance and Administrative Services Department

DATE: October 1, 2018

RE: Update to Management’s Response to Audit Report Regarding Review of the Broward County Employee Benefits Internal Service Fund

This is an update to Management’s Response to the County Auditor’s Report regarding the Employee Benefits Internal Service Fund (Fund) dated May 8, 2018. Due to the ongoing nature of some of the actions to be taken and delays due to system restraints on others, the following are status updates on Management’s responses to the Auditor’s recommendations:

Recommendation A: Establish a policy requiring reserves be maintained in an amount to be reasonable. The reserves should be maintained at a target level, with any excesses or shortfalls being taken into account during the annual premium-setting process.

COMPLETED. Management has documented its current reserve policy of three months of program costs (anticipated claims, health savings account funding, and administration costs).

Recommendation B: Refund $6.6 to $12.6 million to the employees and agencies that paid the excess charges, including grant and enterprise funds, or as an alternative, established planned reductions over time to reduce the fund balance to an appropriate level.

COMPLETED IN PART AND ON-GOING. As indicated in the original Management Response, Management has opted to maintain or adjust benefit costs to agencies over time to reduce the reserve fund. Specifically, despite FY19 forecasted increases in health care and pharmacy costs as well as costs to administer, staff has not adjusted the amount budgeted to agencies for FY19, which will reduce the health care reserve if costs increases do occur as projected. In addition, staff plans to review the performance of the
plan in October to determine if other adjustments are necessary to further manage the reserve balance to an appropriate level.

**Recommendation C: Charge group health care costs to agencies based on actual filled positions.**

**IN PROCESS.** Management has developed a process to charge each agency in a manner that would factor in vacancies. Due to system complications that could impact individual employee enrollment information, staff anticipates implementing the new process in January 2019 with the new benefit plan year (calendar) rather than with the FY19 budget year as previously reported.

Should you have any questions, please do not hesitate to contact me.

c: Bertha Henry, County Administrator
   Monica Cepero, Deputy County Administrator
   Andrew Meyers, County Attorney
   George Tablack, CPA, Chief Financial Officer
   Norman Foster, Director, Office of Management and Budget
   David Mackenzie, Senior Budget Management Analyst, Office of Management and Budget
   David Kahn, Director, Human Resources Division
   Lisa Morrison, Employee Benefits Manager, Human Resources Division
   Susan Friend, Director, Accounting Division
The following is Management’s update as a follow-up to the recommendations in the County Auditor’s Report regarding the Employee Benefits Internal Service Fund (Fund) dated May 8, 2018:

**Recommendation A:** Establish a policy requiring reserves be maintained in an amount to be reasonable. The reserves should be maintained at a target level, with any excesses or shortfalls being taken into account during the annual premium-setting process.

**COMPLETED.** Management has documented its current reserve policy of three months of program costs (anticipated claims, health savings account funding, and administration costs), approximately $15 million.

**Recommendation B:** Refund $6.6 to $12.6 million to the employees and agencies that paid the excess charges, including grant and enterprise funds, or as an alternative, established planned reductions over time to reduce the fund balance to an appropriate level.

**COMPLETED IN PART AND ON-GOING.** As indicated in the original Management Response, Management has opted to maintain or adjust benefit costs to agencies over time to reduce the reserve fund. To further reduce the fund balance in the Employee Benefits Fund during FY19, Management opted to maintain the FY18 amount budgeted for benefit costs to agencies in FY19, despite anticipated increases in health care and pharmacy expenses. Year-end financial reporting indicated that the actual fund balance remaining at the end of FY18 was $17.6 million, and the current fund balance forecast for year-end, FY19, ranges between $15.8 million and $17.7 million. Management is committed to the objective of reducing the fund balance to an appropriate level and
continues to monitor activity within the fund. Staff plans to review the performance of the 
plan in October, 2019, to determine if other adjustments are necessary to further 
manage the fund balance to an appropriate level.

**Recommendation C: Charge group health care costs to agencies based on actual 
filled positions.**

**COMPLETED.** Effective with payroll check dated 1/4/19, Group Health Care costs are 
allocated based on actual enrollments processed biweekly to the general ledger. A 
charge of $477.00 is processed to the agencies expense account 510540, under their 
respective funds and department IDs. The revenue to the Benefit Fund goes into 
50025-35653000-421810. The amount to be charged will be reviewed each October to 
determine if any adjustments are necessary to ensure that the appropriate amount is 
being charged.

Should you have any questions, please do not hesitate to contact me.

c: Bertha Henry, County Administrator  
Monica Cepero, Deputy County Administrator  
Andrew Meyers, County Attorney  
George Tablack, Chief Financial Officer  
Norman Foster, Director, Office of Management and Budget  
David Mackenzie, Senior Budget Management Analyst, Office of Management and 
Budget  
David Kahn, Director, Human Resources Division  
Lisa Morrison, Employee Benefits Manager, Human Resources Division  
Kristin Carpenter, Director, Accounting Division