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Alexander Bustamante
SENIOR VICE PRESIDENT
CHIEF COMPLIANCE AND AUDIT OFFICER

December 17, 2019

ACTING VICE PRESIDENT LLOYD

RE: Final Report Project No. P19A009: Retirement Savings Program Administrative Fees

Attached is a copy of the final report for: Audit Services Project No. P19A009 Retirement Savings Program Administrative Fees. With the issuance of this final report, please destroy any previous draft versions. We very much appreciate the assistance provided to us by you and members of your staff during our review. If you should have any questions please feel free to contact me at 510-987-9646 (email: matthew.hicks@ucop.edu).

A handwritten signature in black ink, appearing to read "Matt Hicks".

Matt Hicks
Systemwide Deputy Audit Officer

Attachment

cc: Senior Vice President Bustamante
Executive Vice President Nava
Executive Director Baptista
Executive Director Schlimgen
Director Reicher
Director Swanson
Systemwide Associate Audit Director Cataldo
Systemwide Principal Auditor Sinutko

UNIVERSITY OF CALIFORNIA
ETHICS, COMPLIANCE AND AUDIT SERVICES
OFFICE OF THE PRESIDENT
INTERNAL AUDIT SERVICES

RETIREMENT SAVINGS PROGRAM ADMINISTRATIVE FEES
Audit Project No. P19A009
November 2019

Work Performed by:

Derek Sinutko, Systemwide Principal Auditor

Work Reviewed by:

Peter Cataldo, Systemwide Associate Audit Director

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Executive Summary

Introduction and Background

As part of the University of California Office of the President (UCOP) 2018 – 2019 fiscal year internal audit plan, Internal Audit performed an audit of the policies, procedures, and internal controls pertaining to the Retirement Savings Program's (RSP) administrative fees.

In recent years, litigation has placed a spotlight on the administrative fees that employers charge participants for employer-sponsored retirement savings plans. Consequently, the University of California (UC) hired Mercer to review its RSP with a focus on administrative fees and governance. After restructuring the program, the Retirement Savings Program Advisory Committee (RSPAC) selected Fidelity as the recordkeeper and State Street as the holder of the assets in trust, which are managed by the UC Office of the Chief Investment Officer (OCIO).

In addition, State Street holds the funds that the RSP collects for its per-participant administrative service fee in the Plan Expense Account and invests them in the State Street Institutional Liquid Reserve Fund. The RSP then uses these funds to pay its administrative expenses as specified in the *Administrative Fee Processing Guidelines for the UC Retirement Savings Program (Processing Guidelines)*. Accordingly, UCOP pays these expenses from internal UC Fund 69705 and the State Street Plan Expense Account, and reconciles the accounts monthly per the *Processing Guidelines* so that the RSPAC can monitor the program's budgetary condition.

In addition to the RSP, the University's primary retirement benefit is nearly unique in offering a choice between defined benefit and defined contribution plans. This choice component adds complexity to the overall benefit administration, which includes the voluntary RSP, and as a result only a few recordkeepers can provide the necessary services.

Objectives and Scope

The primary objectives of the audit were to verify that properly trained staff, documented procedures, and effective internal controls are in place to ensure that:

- The administrative budget includes only eligible compensation expenses, which consist of salaries and benefits for internal staff that provide services to the RSP.
- Only eligible expenses are paid from the trusts or custodial account.
- Only authorized staff can approve expenses paid from Fund 69705.
- Monthly reconciliations of administrative fee income with the Plan Expense Account and Fund 69705 are performed to promptly detect potential deficits or significant surpluses.

The scope of the audit consisted of a review of the Retirement Savings Program's current practices and a sample of direct non-compensation expenses from October 2017 through April 2018.

Audit Procedures

1. Obtained and reviewed background documentation on UC and regulatory requirements:
 - a) *Administrative Fee Policy Guidelines for the UC Retirement Savings Program (Policy Guidelines)*
 - b) *Administrative Fee Processing Guidelines for the UC Retirement Savings Program*
 - c) *Mercer Fiduciary Duties and Governance* training (presentation by consultant at Retirement Savings Program Advisory Committee meeting, February 2018)
2. For all departments performing RSP administration, identified the process that management uses to determine the proportions of employees' time spent working on the program and their basis for these determinations.
3. Judgmentally selected 16 approved non-compensation expenses for Fund 69705 and tested each expense for compliance with the Retirement Savings Program's *Policy Guidelines* and *Processing Guidelines*, and noted any exceptions. Specifically, reviewed each expense for the following:
 - a) Eligibility of expenses charged to the fund
 - b) Any vendor expenses paid from the fund, which are not permitted
 - c) Authorized expense approvers
4. Reviewed reconciliations of administrative fee income with the Plan Expense Account and Fund 69705 to determine whether reconciliations have been completed and reviewed monthly.
5. Based on the information gathered in Steps 1-4, evaluated sufficiency of existing controls and identified potential opportunities to improve compliance with best practices and Retirement Savings Program Advisory Committee policy objectives as indicated in the *Policy Guidelines*.

Conclusion

Our review of Retirement Savings Program administrative fees identified a number of internal control areas in which improvement is necessary to comply fully with the *Processing Guidelines* and thereby ensure only eligible and reasonable expenses are paid. We noted that not all RSP units document the employee effort determinations that underlie the RSP's annual budget, nor track and document employee time, which is the basis for those determinations. Improvements are also required to ensure management performs account reconciliations timely and thoroughly,

only grants necessary employees signature authority, and appropriately trains employees. We further noted that the RSP has not fully defined eligible expenses nor implemented a process to apportion expenses that relate to multiple funds besides RSP. Accordingly, we have developed recommendations for improvement as detailed in the following section.

Opportunities for Improvement and Action Plans

A. Time Tracking and Effort Determination

1. Employee Time Not Tracked

Departments that charge salaries and benefits expenses to the Retirement Savings Program (RSP) do not routinely track employee hours worked as specified by the *Policy Guidelines*. The *Policy Guidelines* specify that “staff who spend their time on the administration, investment oversight and management of the Plans will track 100% of their hours in a time-keeping system and document the services provided to the Plans if any time is charged to the trusts or custodial account.” In addition to fulfilling this policy expectation, documented records of employee time would provide a basis for the employee effort determinations that underlie development of the Retirement Savings Program’s annual budget for direct program administrative expenses. Given that the program is currently without such documentation and compensation expenses constitute most of its direct expenses, management lacks a substantive defense should concerns be raised regarding its spending of participant funds.

Tracking time on a monthly basis would be a reasonable requirement given that UCOP financial policy requires “a monthly sampling and review of individual financial transactions by a supervisor to ensure transactions are appropriately approved, accurately recorded, and supported by proper documentation.”

Action Plan:

The Retirement Savings Program Director will (a) request that the Plan Administrator determine a procedure to track and document employee hours worked on behalf of the Retirement Savings Program, (b) implement the timekeeping procedure, (c) revise the Administrative Fee Processing Guidelines accordingly, and (d) communicate the new procedures and revised guidelines to the Retirement Savings Program Advisory Committee.

Target Date: April 1, 2020

2. No Documented Basis for Employee Effort Determinations

We noted that all units except the Retirement Administration Service Center (RASC) lack a systematic, documented basis for the annual staff effort determinations upon which the compensation expenses for the RSP administrative budget are based. Since RASC’s customer relationship management system records the program for each inquiry that it receives, RASC has a documented basis for its effort determinations. Additionally, none

of the RSP units document the underlying determinations that demonstrate how management arrived at the specific effort percentage for each employee that it includes in the program's budget. Along with documented employee time, documentation of employee effort determinations would support a substantive response to concerns that interested parties could raise regarding management's spending of participant funds.

Action Plans:

1. The Retirement Savings Program Director will instruct business units to (a) use documented employee time to determine staff effort for the Retirement Savings Program budget and (b) document those effort determinations for employees whose salaries and benefits expenses they charge in whole or in part to the RSP. Their approach will apply the guidance contained in the appendices of the Administrative Fee Policy Guidelines and the principles for allowable plan-related tasks presented in the "Fee Budgeting and Allocation Methodology" chapter (4) of the Administrative Fee Processing Guidelines.

Target Date: July 1, 2020

2. The Executive Director of Retirement Programs & Services will arrange training for management of all units that perform Retirement Savings Program-related functions (BPS Administration, Vendor Relations Management, Benefits Information Systems, Retirement Policy, RASC Customer Service, RASC Operations, RASC Calculations, and Benefit Plan Accounting) to ensure that they have accurate knowledge of eligible employee effort, and will document the content and completion of their training.

Target Date: April 1, 2020

3. No Control to Ensure Fund Adjustments following Staff Effort Changes

Management occasionally implements staff effort changes that necessitate adjusting the percentage of an employee's compensation attributable to the Retirement Savings Program, yet has not implemented a procedure to ensure that it adjusts the percentage of compensation paid from Fund 69705. If management reduces or increases the amount of time that one or more employees perform related work, it should also change the allocation of funds for those employees' salaries and benefits accordingly. Such fund allocation changes are important to ensure that the compensation amounts charged to Fund 69705 accurately reflect those employees' compensation attributable to the RSP.

Action Plan:

The Retirement Savings Program Director will semi-annually verify that, for any changes in Retirement Savings Program-related employee effort, management has timely and correctly adjusted the percentage of affected employees' salaries and benefits charged to Fund 69705. In addition, the Retirement Savings Program Director will revise the Administrative Fee Processing Guidelines accordingly and obtain Plan Administrator approval of these revisions. If management identifies any delayed or incorrect fund

adjustments, the Retirement Savings Program Director will request that Benefit Plan Accounting correct the associated charges.

Target Date: February 1, 2020

B. Improvements Related to Training and Procedures

1. Procedures Not Documented

The *Policy Guidelines* and *Processing Guidelines* both indicate the importance of documenting processes and procedures. However, we noted that the *Processing Guidelines* do not document all of the procedures that constitute the Retirement Savings Program's operations. Specifically, four of five units that have RSP-related procedures have not documented them (Benefits Information Systems has documented procedures and RASC does not have RSP-specific tasks, which are performed by Fidelity). Documented procedures help to facilitate new employee training, promote operational consistency, and ensure business continuity in the event of a wave of critical staff turnover. Further, these documented procedures can serve as one part of a substantive demonstration that management has exercised care in its oversight of plan administration.

Action Plan:

The Executive Director of Benefits Programs & Strategy, the Executive Director of Retirement Programs & Services, and the Director of Benefit Plan Accounting will each document all Retirement Savings Program-related procedures for their respective departments that perform RSP-related tasks (BPS Administration, Vendor Relations Management, Retirement Policy, and Benefit Plan Accounting).

Documentation of these procedures should include, but not be limited to, the following:

- *For BPS Administration, development of the RSP budget and staff allocations, both at the unit and overall budget coordinator levels.*
- *For Benefit Plan Accounting, performance of monthly budget reconciliations of Fund 69705 and review of underlying expenses charged to that fund.*

Target Date: April 1, 2020

2. RSP-related Training Is Not Documented

Most units that perform RSP-related tasks lack documentation of training content and employee training completion. Similar to the above discussion regarding procedural documentation, documentation of training can serve as another part of a substantive demonstration that management has exercised care in its oversight of plan administration.

Action Plan:

The Executive Director of Benefits Programs & Strategy, the Executive Director of Retirement Programs & Services, and the Director of Benefit Plan Accounting will each implement a policy requirement to document Retirement Savings Program-related training content and employee training completion.

Target Date: February 1, 2020

C. Review of Expenses Charged to Fund 69705

1. Potentially Ineligible or Partially Eligible Expenses (undetermined)

We identified several examples of expenses charged to Fund 69705 that presented eligibility concerns, including food for meetings, office supplies, copying services, and travel. Further clarification of eligible expenses is warranted to ensure compliance with the *Policy Guidelines*.

Meal expenses: We noted that the *Policy Guidelines* do not provide explicit guidance regarding meal expenses. Although the guidelines, as noted in Appendix B, promote a review of the expenses to ensure they are necessary for the establishment or operation of the plan and primarily for the benefit of plan participants and beneficiaries, they do not specifically address whether meal expenses meet this test. In addition, we identified one set of catering invoices that was incorrectly charged to Fund 69705 as it was not related to an RSP event but rather for a different program's event.

Expenses that may benefit other programs: Office supplies, copying services, and travel expenses also provide potential cause for concern. Goods and services that are used exclusively for plan-related activities may be eligible for reimbursement, but those that are only partially attributable to the RSP should be charged proportionally.

Accordingly, the *Policy Guidelines* specify in Appendix B that “the accounting department must keep a contemporaneous list of supplies requisitioned for such services. The cost of supplies must then be apportioned among the plans involved. If it can't accurately be determined for which plan a particular item is used, then the cost of all supplies for the reporting period...will be allocated to the plans on the basis of total time spent by employees providing services to each plan.” We noted several expenses for goods and services that appear to fit this category, but which management charged 100% to the RSP without explanation.

In addition, management has not documented invoice reviews, which presents the risk that it has not thoroughly reviewed expenses. As part of this review process, legal counsel should be consulted regarding any nonstandard or unusual charges to affirm that they are eligible.

Action Plans:

1. *The Executive Director of Retirement Programs & Services will arrange for eligible expense training to be provided to all invoice reviewers and expense approvers to ensure that they have accurate knowledge of eligible expenses for the Retirement Savings Program, and will document the content and completion of their training.*

Target Date: April 1, 2020

2. *The Executive Directors of Benefits Programs & Strategy and Retirement Programs & Services will request that the Plan Administrator determine if and when meal expenses are appropriate to be charged to the RSP. Specifics should include (a) whether meal expenses for meetings during which participants work through a lunch period are an appropriate use of participant funds, and if so, (b) which meetings qualify and (c) an expense apportionment methodology for any qualifying meetings that include business unrelated to the Retirement Savings Program. In addition, the Executive Director of Retirement Programs & Services will update the Administrative Fee Policy Guidelines accordingly and obtain Plan Administrator approval of these revisions.*

Target Date: April 1, 2020

3. *Benefit Plan Accounting will reverse the food expenses for the 2019 UC Retiree Health Benefits Design Kickoff Meeting held in January 2018 that management charged to Fund 69705 (\$570.17).*

Target Date: Completed during review. No further action required.

4. *The Retirement Savings Program Director will develop a control to ensure that UCOP only charges Fund 69705 for the portion of direct non-compensation expenses, including travel, that management can attribute to the Retirement Savings Program.*

Target Date: April 1, 2020

5. *The Retirement Savings Program Director will develop and implement an invoice review and approval form for all non-compensation (both direct and vendor) expenses that incorporates the questions from the Expense Eligibility Checklist (Administrative Fee Policy Guidelines Appendix A-1), corresponding options for reviewers to check, including legal counsel review as necessary, and places for reviewers and applicable approvers to sign.*

Target Date: Completed during review. No further action required.

2. Vendor Expenses Charged to Incorrect Account

We identified two expenses for professional services from external vendors that were charged to Fund 69705, which is inconsistent with the *Processing Guidelines*' requirement that invoices for vendor expenses be paid through State Street's vendor payment system. That system deducts the payment from the Plan Expense Account that State Street

maintains on behalf of the RSP, and acts as a control over the payment of vendor expenses because it will only pay vendors that the University has specifically approved.

The *Processing Guidelines* state that “no vendor expenses should be paid directly from 69705,” and require that “if non-UC staff expenses are charged directly to 69705 the expenses should be reversed and a corrected invoice should be requested from the vendor and BPA should process the payment from the Plan Expense Account.”

During our review, we learned that these particular vendor expenses were internal cost transfers that management charged to Fund 69705 because the vendors provided a single invoice that UCOP paid and then recovered through fund transfers. Further, one of these internal cost transfers is a recurring expense for audit services that management budgets to be recovered on a regular basis from Fund 69705, and the other is for financial services that the vendor invoiced before it began separately invoicing the RSP. Although these internal cost transfers were technically inconsistent with the *Processing Guidelines*, under the circumstances it was reasonable to process them in this manner.

Action Plan:

The Executive Director of Retirement Programs & Services will request that the Plan Administrator revise the Administrative Fee Processing Guidelines to reflect an exception for internal cost transfers for audit services to its requirement that management provide invoices for vendor expenses to Benefit Plan Accounting for payment through State Street’s vendor payment system. In addition, this executive director will communicate this change to the Retirement Savings Program Advisory Committee.

Target Date: April 1, 2020

3. Excessive Number of Expense Approvers

According to the Business Resource Center (BRC), an employee with delegated signature authority is the single control point for ensuring that the BRC only charges eligible expenses to Fund 69705. Management should limit this authority to the extent practical to those who are sufficiently familiar with RSP operations and expense eligibility requirements. We noted that the current number of 17 individuals with expense authority for Fund 69705 was excessive.

Action Plan:

The Executive Directors of Benefits Programs & Strategy and Retirement Programs & Services will reduce the current list of authorized approvers and provide the Business Resource Center with the revised list of authorized approvers for Fund 69705.

Target Date: January 2, 2020

4. Monthly Budget Reconciliations Do Not Include Expense Reviews and Lack Controls

Although Benefit Plan Accounting is performing monthly reconciliations of budgeted to actual expenses for Fund 69705, it is not reviewing each item charged to the fund to ensure that it is an eligible expense. Given that internal cost transfers, such as printing and facility charges, can occur without approval by a delegated signature authority, RSP management should ensure that monthly reconciliations include a review of all charges to Fund 69705. Without a regular review of all expenses charged to the fund, management may never discover and correct erroneous and ineligible charges.

In addition, Benefit Plan Accounting management does not have a control in place to ensure that these monthly budget reconciliations and expense reviews are performed timely and approved by a member of management other than the person who performed the original work.

Action Plans:

- 1. As part of its monthly budget reconciliation, Benefit Plan Accounting will perform a documented review of all expenses charged to Fund 69705 to ensure that they are eligible. Benefit Plan Accounting will work with the Business Resource Center to ensure that Benefit Plan Accounting has sufficient access to the financial records system to perform these expense reviews.*

Target Date: April 1, 2020

- 2. Benefit Plan Accounting will develop, document, and implement a control to ensure that budget reconciliations of Fund 69705 and its expense reviews are (1) performed monthly and (2) approved by a member of management other than the person who performed the original work.*

Target Date: April 1, 2020