COUNTY OF SACRAMENTO

DEPARTMENT OF FINANCE - AUDITOR-CONTROLLER DIVISION – INTERNAL AUDIT UNIT

INTERNAL AUDIT REPORT

457(b) AND 401(a) DEFERRED COMPENSATION PLANS PERFORMANCE AUDIT DEPARTMENT OF PERSONNEL SERVICES

SACRAMENTO COUNTY

Audit Committee Submittal Date: 01/16/2024

SUMMARY

Background

The County of Sacramento (County) Department of Personnel Services (DPS) requested the Department of Finance to perform a performance audit of the County 457(b) and 401(a) Plans (Benefit Plans) for compliance with Internal Revenue Service (IRS) regulations, California Government Code Section 53212 and 53215 *et seq*., the Benefit Plans' Documents, and Recordkeeping and Related Services Agreement (Agreement) between the County and Fidelity Workplace Services LLC, a Delaware Limited Liability Company for the period of July 1, 2020 to June 30, 2021.

Audit Objective

To verify whether the Benefit Plans were in compliance with IRS regulations, California Government Code Section 53212 and 53215 *et seq.*, the Benefit Plans' Documents, and the Agreement managed by DPS.

Summary

Based on our procedures performed, we noted several noncompliance and internal control issues related to 401(a) employer matching contribution, recordkeeping fees, and annual reporting requirement.

Department of Finance
Chad Rinde
Director

County of Sacramento

Divisions
Auditor-Controller
Consolidated Utilities Billing & Services
Investments
Revenue Recovery
Tax Collection & Licensing
Treasury

November 6, 2023

Sylvester Fadal
Director of Personnel Services
Department of Personnel Services
700 H Street, Ste. 4650
Sacramento, CA 95814

Dear Mr. Fadal:

We have audited County of Sacramento (County) Department of Personnel Services (DPS)' management and oversight of 457(b) and 401(a) Benefit Plans (Benefit Plans) for the period July 1, 2020 to June 30, 2021.

Our audit was conducted to verify compliance at DPS over Internal Revenue Service regulations, California Government Code Section 53212 and 53215 *et seq.*, the Benefit Plans' Documents, and Recordkeeping and Related Services Agreement (Agreement) between the County and Fidelity Workplace Services LLC, a Delaware Limited Liability Company (Fidelity) for the period July 1, 2020 to June 30, 2021, and ensure DPS has adequate internal controls to manage and oversee the Benefit Plans.

DPS' management is responsible for the design, implementation, and maintenance of effective internal controls to ensure compliance with applicable laws and regulations, the Benefit Plans' Documents, and the Agreement.

The scope of our audit included DPS' management and oversight of the Benefit Plans in accordance with applicable laws and regulations, Benefit Plans' Documents, and the Agreement for the period July 1, 2020 to June 30, 2021.

The audit methodology utilized to conduct this performance audit included:

Regulatory and Contractual Requirements

- Reviewed laws and regulations, Benefit Plans' documents, and the Agreement related to the Benefit Plans.

Based on our procedures performed, it appears that DPS did not comply with County 401(a) Plan Document regarding certain employer matching contributions for first year employees. In addition, it appears that DPS did not comply with 457(b) Plan Document's annual reporting requirement. See Findings #1 and #3 at ATT 1 – *Current Findings and Recommendations.*

Internal Control Review

- Interviewed key staff/management involved in the Benefit Plans to gain an understanding of the County's responsibilities as it relates to the Benefit Plans.

- Reviewed DPS's written internal control policies and procedures related to the Benefit Plans and tested key control activities.

- Reviewed DPS's procedures regarding the secure, accurate and timely transmission of relevant participant data, such as payroll data establishing eligibility, to determine whether all eligible covered employees have been properly included, whether accurate participant data was supplied to Fidelity, Record Keeper, and whether Fidelity utilized the data in a timely manner.

Based on our review, it appear that DPS did not have written policies and procedures related to the process of reconciliation of the trust account activities and balances, periodic analysis of appropriateness of recordkeeping fees charged to participants of the Benefit Plans, and the process of setting the fees based on the analysis as described in Finding #2 of ATT 1 – *Current Findings and Recommendations.*

Testing

- Tested 64 457(b) regular participants, 10 457(b) Roth participants, 10 457(b) Part-time, Seasonal and Temporary (PST) participants, and 15 401(a) Plan participants' contributions to verify:

    a. Fund transfers from employer were timely, secure, and posted promptly by Fidelity.

    b. Amounts received were properly recorded by Fidelity and disclosed in the participant's financial statement on record.

    c. Employer and employees contribution payments were in accordance with Benefit Plans' provisions and transactions were properly recorded in the proper accounts, amounts and periods.

- Tested 35 457(b) Plan participants' timing of initial contributions and contribution changes to verify that initial contributions did not take place in the same calendar month the participants entered into agreements to defer compensations and that the initial contributions were made on the date indicated by the participants.

- Tested 25 participants' purchases of Sacramento County Employees' Retirement System (SCERS) service credits using 457(b) rollovers to verify that the payments were in accordance with SCERS and 457(b) Plan Documents and processed timely.

- Tested 10 participants eligible for the 401(a) employer matching contribution to verify that contributions were in accordance with 401(a) Plan Document.

- Reviewed participant election process (e.g., elected deferral rates) to verify that the appropriate payroll deductions occurred as elected by participants.

Based on our procedures performed, we did not note any exception except for 401(a) employer matching fund contrubtion for three eligible employees in the first year. It appears that DPS did not comply with County 401(a) Plan Document regarding 401(a) employer matching fund contribution as described in Finding #1 of ATT 1 – *Current Findings and Recommendations*.

Other

- Followed up on status of prior year audit findings and recommendations. See ATT 2 – *Current Status of Prior Recommendations.*

We conducted this performance audit in accordance with *Generally Accepted Government Auditing Standards (GAGAS)* issued by the Comptroller General of the United States except for paragraph 3.56 regarding our independence as described in the below paragraph. 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 objective. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objective.

As required by various statutes within the California Government Code, County Auditor-Controllers or Directors of Finance are mandated to perform certain accounting, auditing, and financial reporting functions. These activities, in themselves, necessarily impair *GAGAS'* independence standards. Specifically, auditors should not audit their own work or provide non-audit services in situations where the amounts or services involved are significant/material to the subject matter of the audit.

Although the Director of Finance is statutorily obligated to maintain the accounts of departments, districts or funds that are held in County Treasury, the staff that has the responsibility to perform audits within the Auditor-Controller Division has no other responsibility of the accounts and records being audited including the approval or posting of financial transactions, which would therefore enable the reader of this report to rely on the information contained herein.

Sylvester Fadal, Director of Personnel Services
Department of Personnel Services
November 6, 2023

Based on our audit, DPS complied with applicable laws and regulations, the Benefit Plans' Documents, and the Agreement for the period of July 1, 2020 to June 30, 2021 except for noncompliance and internal control deficiencies noted in ATT 1 – *Current Findings and Recommendations* and ATT 2 – *Current Status of Prior Findings and Recommendations.*

DPS's management responses to the findings identified during our engagement are described in ATT 1 – *Current Findings and Recommendations*. We did not perform procedures to validate DPS's management responses to the findings and, accordingly, we do not express an opinion on the responses to the findings.

This report is intended solely for the information and use of Sacramento County Board of Supervisors, Sacramento County Executives, Sacramento County Audit Committee, and DPS' management, and should not be used for any other purpose. It is not intended to be, and should not be, used by anyone other than these specified parties. However, this report is a matter of public record and its distribution is not limited.

Sincerely,

CHAD RINDE
DIRECTOR OF FINANCE

By: Hong Lun (Andy) Yu, CPA
Chief of Audits

Attachments:
ATT 1 – *Current Findings and Recommendations*
ATT 2 – *Current Status of Prior Recommendations*

County of Sacramento
Department of Personnel Services
457(b) and 401(a) Deferred Compensation Plans
Performance Audit
Current Findings and Recommendations
For the Period July 1, 2020 through June 30, 2021

1. 401(a) Employer Matching Contribution

Condition

During our sample testing of employer matching contributions to the 401(a) Plan for eligible employees, we noted three out of 10 of the sample selections do not appear to comply with the 401(a) Plan Document regarding the employer matching requirements.

Department of Personnel Services (DPS)' Employee Benefits staff (Benefit staff) stated that it was DPS' practice that matching contribution was made only to the employee where year-to-date (YTD) total 457(b) contribution amount was at least 1% of YTD salary. The Benefit staff also stated that DPS' new management discovered this issue after they were hired in the department, changed the practice to remove ambiguity between the practice and plan documents, and now allow the matching contribution as soon as the employee meets or exceeds the 457(b) contribution of 1% of each payroll period salary.

As the individual YTD 457(b) contribution amount of the three employees identified above was less than 1% of the individual YTD salary, matching contribution was not made available to the three employees in the first year when they became eligible to receive the matching contribution.

Criteria

Per County of Sacramento 401(a) Plan Document, Section 3.02(a), *".....in order to be eligible for a County Matching Contribution, a Participant must: (i) On any day of the payroll period for which County Matching Contributions are made, be a current Employee or Elected Official and member of a group or occupy a position listed in Appendix A of this Plan; and (ii) Have deferred Compensation under the Eligible 457(b) Plan as required in Section 3.02(b)."*

Per Section 3.02(b)(ii), *"For each Plan Year beginning on and after January 1, 2008, the Participant must have deferred under the Eligible 457(b) Plan in each applicable payroll period at least one percent (1%) of his or her Compensation earned during that payroll period"* and per Section 3.02(b)(iii)(B), *"If a Participant who is an Employee or Elected Official but not currently receiving a County Matching Contribution under this Plan elects during a Plan Year to increase his or her deferrals of Compensation under the Eligible 457(b) Plan to at least one percent (1%) of Compensation, such election* *shall be taken into account for purposes for eligibility to receive a County Matching Contribution under this Plan during the remainder of such Plan Year."*

Effect
Prior to the change made by the new management, due to differences between DPS' practice of administering 401(a) and the 401(a) Plan Document, those employees who became eligible for the matching contribution during the plan year but whose 457(b) contribution was less than 1% of their YTD salary, may not have received the matching contribution.

Recommendation
We recommend DPS review the 401(a) Plan Document and adjust its practice of administering 401(a) or update the Plan Document and its practice accordingly. We also recommend DPS assess the impact of not complying to the Plan documents as it relates to the employer contributions.

DPS Management's Response
Agree. DPS will consult with Counsel to determine an appropriate response to the identified discrepancy between its practice and the plan document related to employee contributions. As noted in the audit report, DPS interpreted and has been applying the same standard for matching contributions since the inception of the 401 (a) plan until April 1, 2023, when the plan was amended to clarify the criteria for matching contributions and the DPS practice revised accordingly. Additionally, DPS has reviewed the plan document and amended it effective April 1, 2023, which was approved by the Board of Supervisors (Board) on March 28, 2023. As a result, DPS believes this finding has been resolved.

2. Recordkeeping Fees

Condition
Fidelity Workplace Services LLC, a Delaware Limited Liability Company (Fidelity) maintains recordkeeping fees charged to participants of 457(b) and 401(a) Deferred Compensation Benefit Plans (Benefit Plans) in the accounts under its custody (Fidelity Accounts). The portion of the fee included Sacramento County's revenue for administering Benefit Plans.

County of Sacramento
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457(b) and 401(a) Deferred Compensation Plans
Performance Audit
Current Findings and Recommendations
For the Period July 1, 2020 through June 30, 2021

During our audit procedures, we noted that DPS did not have written policies and procedures related to the reconciliation process of the Fidelity Accounts' financial activities and balances, periodic analysis of the appropriateness of recordkeeping fees charged to participants of the Benefit Plans, and the process of setting the fees based on the analysis.

Criteria
Written policies and procedures related to the reconciliation process of the Fidelity Accounts' financial activities and balances should be maintained in order to account for the Fidelity Accounts' financial activities and balances consistently and accurately. In addition, written policies and procedures related to periodic analysis of appropriateness of recordkeeping fees charged to participants of the Benefit Plans, and the process of setting the fees based on the analysis should be maintained. The written policies and procedures will assist DPS to re-evaluate the fee structures in a standardized manner and to maintain appropriate funds level that would cover expenses for the Benefit Plans' operation without under or over charging participants.

Effect
Not maintaining policies and procedures related to the reconciliation process of the Fidelity Accounts' financial activities and balances, periodic analysis of appropriateness of recordkeeping fees charged to participants of the Benefit Plans, and the process of setting the fees based on the analysis limits transparency and increases the risk of over or under collection of the fees from Benefit Plan participants.

Recommendation
We recommend DPS:

- Establish written policies and procedures related to the reconciliation process of the Fidelity Accounts' financial activities and balances in order to account for the Fidelity Accounts' financial activities and balances consistently and accurately.
- Establish written policies and procedures related to periodic analysis of appropriateness of recordkeeping fees charged to participants of the Benefit Plans, and the process of setting the fees based on the analysis. The written policies and procedures will assist DPS to re-evaluate the fee structures in a standardized manner and to maintain appropriate trust funds level that would cover expenses for the Benefit Plans' operation without under or over charging participants.

DPS Management's Response
Partially Agree. The recordkeeping fees charged to the participants, the Third-Party Plan Administrator (currently Fidelity) fees are part of the Request for Proposal (RFP) process and negotiated during the contracting process. The RFP is a competitive process used to ensure public sector entities are receiving the most responsive, responsible, and competitive price or value for the services being procured. Additionally, along with the last contract extension, a new lowered fee was negotiated with Fidelity for the 2023 and 2024 plan years.

Additionally, DPS monitors the fee structures and trust fund levels to ensure an appropriate fund level is maintained to support the required expenses. This is in part achieved through the working committee, including Department of Finance (DOF) staff, who review the fees participants pay and ongoing plan administration costs. As a result of this monitoring process, the Advisory Committee approved a fee holiday for plan participants during fiscal year 2022-23 where no fees were assessed and a new fee structure for participants was established effective July 1, 2023, which we expect will align with administrative and recordkeeping costs.

The fee accounts are reconciled quarterly, and plan expenses are reviewed. However, we agree that the reconciliation and fee determination beyond the contracting processes would be best served by a written procedure with specific criteria for assessing the fees in a standardized manner giving a rubric for decision-making for the committees and ensure sufficient funding for plan expenses.

3. Annual Reporting Requirement

Condition
According to the County of Sacramento 457(b) Deferred Compensation Plan Document [457(b) Plan Document], Section 9.2(c), DPS is subject to annual reporting requirement to the Board. However, DPS did not prepare and submit the Annual Report to the Board.

Subsequent to the commencement of our audit, DPS completed an Annual Report for the Benefit Plan Years 2016 through 2022. However, the Annual Report did not include the required elements as discribed in the Plan Document. Total amount of general fund expenditures for County administrative operations, and a description and the amount of any expenditure reimbursement or revenue credited to general fund administration of the Plan by the Plan assets was not reported.

Criteria

Per 457(b) Plan Document, Section 9.2(c), *"The Plan Administrator shall annually report to the Board regarding the earnings or losses experienced on investment accounts, the number of Participants in the Plan, deferral amounts, withdrawal amounts, transfers and listing of investment providers and other outside service providers. The annual report shall also include a description of administrative charges to Participants for third party administration, the total amount of general fund expenditures for County administrative operations and a description and the amount of any expenditure reimbursement or revenue credited to general fund administration of the Plan."*

Effect

DPS did not comply with the 457(b) Plan Document.

Recommendation

We recommend DPS ensure the submission of the Annual Report on Benefit Plans to the Board timely. We also recommend DPS ensure to report the required elements which includes total amount of general fund expenditures for County administrative operations, and a description and the amount of any expenditure reimbursement or revenue credited to general fund administration of the Plan by the Plan assets.

DPS Management's Response

Agree. DPS agrees with the finding that the annual report was not filed with the Board in a timely manner. This was remedied on January 24, 2023, when the Deferred Compensation Annual Report for Years 2016-2022 was filed with the Board. The 2022-23 annual report was filed timely with the Board on October 24, 2023. This report will continue to be filed in a timely manner going forward.

DPS believed they were following the requirements of the plan document and ensured all required sections were included. Our understanding is that no general fund monies are used to pay for plan expenses. In view of DOF's explanation that the general fund account for deferred compensation operating budget is reimbursed by the plan fees and this budget is part of the general fund, and thus should be reported, the annual deferred compensation operating budget can be added to the Board annual report going forward so these reimbursed charges are also provided to the Board.

County of Sacramento
Department of Personnel Services
457(b) and 401(a) Plans Performance Audit
Current Status of Prior Recommendations
For the Period July 1, 2020 through June 30, 2021

CURRENT STATUS OF PRIOR RECOMMENDATIONS (REPORT DATE SEPTEMBER 28, 2021 FOR THE PERIOD JULY 1, 2019 THROUGH JUNE 30, 2020)

1. **Outdated Employee Enrollment Procedure**

Prior Recommendation
We recommended Department of Personnel Services (DPS) update the provision regarding enrollment forms in the 457(b) Plan Document to reflect current policies and procedures. We also suggested assigning a personnel in charge to make sure that the Plan restatement along with the assessment of current policies and procedures would be completed during the year.

Current Status
It appears the recommendation have been implemented.

2. **Service Credit Purchase Rollover**

Prior Recommendation
We recommended DPS management ensure all necessary forms are properly signed and dated prior to processing of fund rollover and distribution. We also recommended DPS management establish and implement a written procedure requiring staff to investigate any outstanding checks issued to Sacramento County Employees' Retirement System for purchase of service credit over normal deposit processing time.

Current Status
It appears the recommendation has been implemented.

3. **Revenue Allowances and Recordkeeping Fees**

Prior Recommendation
We recommended DPS deposit revenue allowances and fees collected from participants to the Treasury and pay any fees related to the Benefit Plan out of the Treasury account. We also recommended DPS establish and implement internal control procedures to properly account for revenue allowances and recordkeeping fees in Sacramento County Accounting System .

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Current Status

It appears the recommendation was partially implemented. See Finding #2 of ATT 1 – *Current Findings and Recommendations.*