California Public Employees' Retirement System
Office of Audit Services
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October 31, 2012

Employer Code: 1815
CalPERS ID: 7403108474
Job Number: P11-016

Health Plan of San Joaquin
Victoria Hazen, Vice President
Human Resources and Customer Service
7751 South Manthey Road
French Camp, CA 95231

Dear Ms. Hazen:

Enclosed is our final report on the results of the public agency review completed for the Health Plan of San Joaquin. Your agency's written response, included as an appendix to the report, indicates disagreement with Findings 1 and 2, and agreement with Finding 3. Based on the information contained in your agency's response pertaining to these findings, our recommendations remain as stated in the report. However, after review of your agency's written response, we expanded Findings 1 and 2 to further clarify the issues. In accordance with our resolution policy, we have referred the issues identified in the report to the appropriate division at CalPERS. Please work with this division to address the recommendations specified in our report. It was our pleasure to work with your agency and we appreciate the time and assistance of you and your staff during this review.

Sincerely,

Original Signed by Margaret Junker
MARGARET JUNKER, Chief
Office of Audit Services

Enclosure

cc: Risk and Audit Committee Members, CalPERS
Peter Mixon, General Counsel, CalPERS
Karen DeFrank, Chief, CASD, CalPERS
Anthony Suine, Chief, BNSD, CalPERS
Paul Antigua, Chief Financial Officer, Health Plan of San Joaquin

Office of Audit Services

Public Agency Review

Health Plan of San Joaquin

Employer Code: 1815
Job Number: P11-016

October 2012

HEALTH PLAN OF SAN JOAQUIN

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HEALTH PLAN OF SAN JOAQUIN

RESULTS IN BRIEF

The Office of Audit Services (OAS) reviewed the Health Plan of San Joaquin's (Plan) enrolled individuals, member compensation, required retirement information and other documentation for individuals included in test samples. This review did not include a determination as to whether the Plan is a "public agency" (as that term is used in the California Public Employees' Retirement Law), and OAS therefore expresses no opinion or finding with respect to whether the Plan is a public agency or whether its employees are employed by a public agency.

A detail of the findings is noted in the Results section beginning on page three of this report. Specifically, the following findings were noted during the review:

- Non-reportable compensation was reported to CalPERS.
- Payrates reported to CalPERS failed to qualify as compensation earnable under the Public Employees' Retirement Law (PERL).
- Temporary/part-time employees were not enrolled into CalPERS membership when membership eligibility requirements were met.

PLAN BACKGROUND

The Plan is a publicly sponsored, not-for-profit, managed care health plan designed by and for the people of San Joaquin County. The Plan is governed by the San Joaquin County Health Commissioners whose members are appointed by the County Board of Supervisors. The Employee Handbook outlines all Plan employees' salaries and benefits and states the terms of employment agreed upon between the Plan and its employees.

The Plan contracted with CalPERS effective January 28, 2002, to provide retirement benefits for local miscellaneous employees. The Plan's current contract amendment identifies the length of the final compensation period as three years for all coverage groups.

All contracting public agencies, including the Plan, are responsible for the following:

- Determining CalPERS membership eligibility for its employees.
- Enrolling employees into CalPERS upon meeting membership eligibility criteria.
- Enrolling employees in the appropriate membership category.
- Establishing the payrates for its employees.
- Approving and adopting all compensation through its governing body in accordance with requirements of applicable public meeting laws.

- Publishing all employees' payrates in a publicly available pay schedule.
- Identifying and reporting compensation during the period it was earned.
- Ensuring special compensation is properly identified and reported.
- Reporting payroll accurately.
- Notifying CalPERS when employees meet Internal Revenue Code annual compensation limits.
- Ensuring the employment of retired annuitants is lawful and reinstating retired annuitants that work more than 960 hours in a fiscal year.

SCOPE

As part of the Board approved plan for fiscal year 2011/2012, the OAS reviewed the Plan's payroll reporting and member enrollment processes as these processes relate to the Plan's retirement contract with CalPERS. The review period was limited to the examination of sampled records and processes from July 1, 2008, to June 30, 2011. The on-site fieldwork for this review was conducted from January 23, 2012, through January 27, 2012. The review objectives and a summary of the procedures performed are listed in Appendix B.

HEALTH PLAN OF SAN JOAQUIN

OFFICE OF AUDIT SERVICES REVIEW RESULTS

Finding 1: The Plan erroneously reported non-reportable compensation to CalPERS.

Recommendations:

The Plan should discontinue reporting bilingual pay and cafeteria supplemental compensation to CalPERS. The Plan should ensure that only compensation earnable, as defined under the PERL and corresponding regulations, is reported to CalPERS.

OAS recommends CASD deny all non-reportable compensation incorrectly reported to CalPERS. CASD should make the necessary adjustments to members' accounts pursuant to Government Code Section 20160.

Conditions:

Bilingual pay

The Plan paid and reported bilingual pay to eligible employees during the review period. OAS found the Plan incorrectly reported the bilingual pay as special compensation. Bilingual pay was not contained in a written labor policy or agreement approved by the Plan's Health Commissioners; therefore, bilingual pay should not have been reported to CalPERS. Special compensation shall be limited to that which is received by a member pursuant to a labor policy or agreement per Government Code Section 20636(c)(2), which became effective in 1993. Section 571(a) of the California Code of Regulations, effective July 5, 1994, exclusively identifies and defines special compensation items that must be reported to CalPERS if they are contained in a written labor policy or agreement.

Cafeteria supplemental compensation

The Plan reported non-reportable compensation for nine sampled employees. Specifically, the Plan paid and reported cafeteria supplemental pay in the employees' base payrate and regular earnings. Cafeteria supplemental pay is not compensation earnable as defined in Government Code Section 20636 and the California Code of Regulations Section 571. Only compensation earnable, as defined under Government Code Section 20636 and corresponding regulations is reportable to CalPERS and considered when calculating retirement benefits.

Specifically, compensation earnable for retirement purposes is defined as a member's payrate and special compensation. Payrate is defined as the normal rate of pay or base pay of the member paid in cash to similarly situated members of the same group or class of employment for services rendered on a full-time basis during normal working hours, pursuant to publicly available pay schedules. Cafeteria supplemental pay does not meet the definition of payrate because the pay is not part of the normal monthly rate of pay or base pay paid to similarly situated members of the same group or class of employment. It also does not appear to have been paid for services but instead as a cafeteria supplemental pay to help pay for health and welfare benefits. Further, Government Code Section 20636(c), and Section 571(a) of the California Code of Regulations exclusively identify and define the reportable items of special compensation. Cafeteria supplemental pay does not meet the definition of special compensation given it is not included among those pay types specified in Section 20636(c) or in Regulation Section 571(a). Therefore, cafeteria supplemental pay, and any other named compensation item given in lieu of a health and welfare benefits does not meet the definition of compensation earnable and should not have been reported to CalPERS.

Criteria:

Government Code: § 20160, § 20636(a), § 20636(b), § 20636(c)(2), § 20636(c)(6)
California Code of Regulations: § 571(a), § 571(b)

Finding 2: The Plan reported a payrate that was not listed on a publicly available pay schedule.

Recommendation:

The Plan should ensure that all employees' payrates are listed on a publicly available pay schedule that has been duly approved and adopted by its governing body in accordance with requirements applicable public meeting laws.

The Plan should also work with the CalPERS CASD to ensure that all pay schedules are public records and identify the position title for every employee position.

Condition:

OAS reviewed the reported payrates for the Plan's Chief Executive Officer (CEO) during the entire review period July 1, 2008, to June 30, 2011, to determine whether the payrates were properly authorized and reported in accordance with publicly available pay schedules. OAS requested the CEO's employment agreements and any other documentation showing that pay increases reported were properly approved and available for public scrutiny. However, the Plan did not provide any document showing pay increases reported to CalPERS were publicly approved or listed on a publicly available pay schedule. Copies of personnel action forms provided showed the pay increases reported to CalPERS were only signed by the Commission's Chairman. The CEO pay reported increased a total of 23.1 percent from July 2008, to July 2010, as shown in the table below.

Pay period reported increase	Hourly Payrate	Monthly Payrate	Yearly Salary	Percentage increase
07/08-3	$114.36	$19,822.40	$237,868.80	-
10/08-3	$121.06	$20,983.73	$251,804.80	5.9%
07/09-3	$127.64	$22,124.27	$265,491.20	5.4%
02/10-3	$132.29	$22,930.27	$275,163.20	3.6%
07/10-3	$140.76	$24,398.40	$292,780.80	6.4%

Subsequent to the on-site field review, the Plan stated that the CEO's salary had never been made public. OAS determined the records establishing and documenting the CEO's pay increases were not available for public scrutiny per Government Code Section 20636(d) and California Code of Regulations Section 570.5.

OAS also reviewed and compared the payrates reported during the review period for the CEO and two other Plan management employees, to determine whether payrate increases reported were also available to other similarly situated Plan employees. OAS found that during the review period of July 2008, to July 2010, the Plan reported payrate increases totaling 23.1 percent for the CEO, while the payrate increases reported for the Medical Director totaled seven percent and 17.1 percent for the Chief of Finance.

The Plan should consider the CEO's payrate increases within the context of Government Code Section 20636(e)(2) which states, "Increases in compensation earnable granted to an employee who is not in a group or class shall be limited during the final compensation period applicable to the employees, as well as the two years immediately preceding the final compensation period, to the average increase in compensation earnable during the same period reported by the employer for all employees who are in the same membership classification, except as may otherwise be determined pursuant to regulations adopted by the board that establish reasonable standards for granting exceptions."

The Plan may request an exception for the average payrate increase for its CEO. This requests needs to be sent to and reviewed by the Customer Account Services Division, per section 572 of the California Code of Regulations. If an exception is not granted by CalPERS, and the CEO retirees within the next one to three years, then increases in his compensation earnable may be reduced per Government Code Section 20636(e)(2).

Criteria:

Government Code: § 20049, § 20160(a), § 20222.5(a), § 20222.5(b), § 20636(a), § 20636(b)(1), § 20636(d), § 20636(e)(2)

California Code of Regulations: § 570.5, § 572

HEALTH PLAN OF SAN JOAQUIN

Finding 3: The Plan did not enroll employees hired through temporary employment agencies when membership eligibility requirements were met.

Recommendation:

The Plan should monitor the hours worked by temporary/part-time employees hired through temporary employment agencies to ensure employees are enrolled, earnings are reported, and contributions are submitted to CalPERS when the 1,000-hour membership eligibility requirement is met.

OAS recommends CASD work with the Plan to assess the impact of this membership eligibility issue, and determine what adjustments, if any, are needed. CASD should also make the necessary adjustments to members' accounts pursuant to Government Code Section 20160.

Condition:

OAS examined the number of hours worked in fiscal years 2008/09, 2009/10 and 2010/11 for a sample of 12 temporary/part-time employees hired through several temporary employment agencies to determine whether the employees met membership eligibility, and if so, were enrolled timely into CalPERS membership. OAS found the following:

- Eight temporary/part-time employees met CalPERS membership eligibility requirements by working more than 1,000 hours in a fiscal year; however, the employees were not enrolled into membership.
- Two temporary/part-time employees met CalPERS membership eligibility requirements by working more than 1,000 hours in a fiscal year; however, the employees were not enrolled on a timely basis. One employee reached 1,000 hours worked as of June 6, 2010; however, the employee was not enrolled into CalPERS membership until July 18, 2011. The other employee reached 1,000 hours of work as of January 24, 2010; however, the employee was not enrolled into CalPERS membership until August 16, 2010.

Criteria:

Government Code: § 20160, § 20305(a)(3)(B)

CONCLUSION

OAS limited this review to the areas specified in the scope section of this report and in the objectives as outlined in Appendix B. OAS limited the test of transactions to employee samples selected from the Plan's payroll records. Sample testing procedures provide reasonable, but not absolute, assurance that these transactions complied with the California Government Code except as noted.

Since OAS did not review whether the Plan is a "public agency" (as that term is used in the California Public Employees' Retirement Law), this report expresses no opinion or finding with respect to whether the Plan is a public agency or whether its employees are employed by a public agency.

The findings and conclusions outlined in this report are based on information made available or otherwise obtained at the time this report was prepared. This report does not constitute a final determination in regard to the findings noted within the report. The appropriate CalPERS divisions will notify the Plan of the final determinations on the report findings and provide appeal rights, if applicable, at that time. All appeals must be made to the appropriate CalPERS division by filing a written appeal with CalPERS, in Sacramento, within thirty days of the date of the mailing of the determination letter, in accordance with Government Code Section 20134 and Sections 555-555.4, Title 2, California Code of Regulations.

Respectfully submitted,

Original Signed by Margaret Junker
MARGARET JUNKER, CPA, CIA, CIDA
Chief, Office of Audit Services

Date: October 2012
Staff: Michael Dutil, CIA, Senior Manager
Alan Feblowitz, CFE, Manager
Jose Martinez
Richard Parsons, CFE, CIA

APPENDIX A

BACKGROUND

BACKGROUND

California Public Employees' Retirement System

The California Public Employees' Retirement System (CalPERS) provides a variety of programs serving members employed by more than 2,500 local public agencies as well as state agencies and state universities. The agencies contract with CalPERS for retirement benefits, with CalPERS providing actuarial services necessary for the agencies to fund their benefit structure. In addition, CalPERS provides services which facilitate the retirement process.

CalPERS Customer Account Services Division (CASD) manages contract coverage for public agencies and receives, processes, and posts payroll information. In addition, CASD provides services for eligible members who apply for service or disability retirement. In addition, CASD provides eligibility and enrollment services to the members and employers that participate in the CalPERS Health Benefits Program, including state agencies, public agencies, and school districts. CalPERS Benefit Services Division (BNSD) sets up retirees' accounts, processes applications, calculates retirement allowances, prepares monthly retirement benefit payment rolls, and makes adjustments to retirement benefits.

Retirement allowances are computed using three factors: years of service, age at retirement and final compensation. Final compensation is defined as the highest average annual compensation earnable by a member during the last one or three consecutive years of employment, unless the member elects a different period with a higher average. State and school members use the one-year period. Local public agency members' final compensation period is three years unless the agency contracts with CalPERS for a one-year period.

The employer's knowledge of the laws relating to membership and payroll reporting facilitates the employer in providing CalPERS with appropriate employee information. Appropriately enrolling eligible employees and correctly reporting payroll information is necessary to accurately compute a member's retirement allowance.

APPENDIX B

OBJECTIVES

HEALTH PLAN OF SAN JOAQUIN

OBJECTIVES

The objectives of this review were limited to the determination of:

- Whether the Plan complied with applicable sections of the California Government Code (Sections 20000 et seq.) and Title 2 of the California Code of Regulations.
- Whether prescribed reporting and enrollment procedures as they relate to the Plan's retirement contract with CalPERS were followed.

This review covers the period of July 1, 2008, through June 30, 2011.

SUMMARY

To accomplish the review objectives, OAS interviewed key staff members to obtain an understanding of the Plan's personnel and payroll procedures, reviewed documents, and performed the following procedures. This review did not include a determination as to whether the Plan is a "public agency", and expresses no opinion or finding with respect to whether the Plan is a public agency or whether its employees are employed by a public agency.

- ✓ Reviewed:
  - o Provisions of the Contract and contract amendments between the Plan and CalPERS
  - o Correspondence files maintained at CalPERS
  - o Plan Health Commission minutes and resolutions
  - o Plan Employee Handbook
  - o Plan salary, wage and benefit agreements including applicable resolutions
  - o Plan personnel records and employee hours worked records
  - o Plan payroll information including Summary Reports and CalPERS listings
  - o Other documents used to specify payrate, special compensation and benefits for all employees
  - o Plan resolutions as necessary
  - o Various other documents as necessary

- ✓ Reviewed Plan payroll records and compared the records to data reported to CalPERS to determine whether the Plan correctly reported compensation.

HEALTH PLAN OF SAN JOAQUIN

- ✓ Reviewed payrates reported to CalPERS and reconciled the payrates to Plan public salary records to determine whether base payrates reported were accurate, pursuant to publicly available pay schedules that identify the position title, payrate and time base for each position, and duly approved by the Plan's governing body in accordance with requirements of applicable public meeting laws.
- ✓ Reviewed CalPERS listing reports to determine whether the payroll reporting elements were reported correctly.
- ✓ Reviewed the Plan's enrollment practices for temporary and part-time employees to determine whether individuals met CalPERS membership requirements.
- ✓ Reviewed the Plan's enrollment practices for retired annuitants to determine if retirees were lawfully employed and reinstated when 960 hours were worked in a fiscal year.
- ✓ Reviewed the Plan's independent contractors to determine whether the individuals were either eligible or correctly excluded from CalPERS membership.
- ✓ Reviewed the Plan's affiliated entities to determine if the Plan shared employees with an affiliated entity and if the employees were CalPERS members and whether their earnings were reported by the Plan or by the affiliated entity.
- ✓ Reviewed the Plan's calculation and reporting of unused sick leave balances, if contracted to provide for additional service credits for unused sick.

APPENDIX C

PLAN'S WRITTEN RESPONSE

Note: The Plan provided attachments to the response which were intentionally omitted from this appendix.

August 16, 2012

Margaret Junker, Chief
Office of Audit Services
California Public Employees' Retirement System
P.O. Box 942701
Sacramento, CA 94229-2701

Dear Ms. Junker:

We are responding on behalf of Health Plan of San Joaquin ("HPSJ") to the draft Public Agency Review dated June, 2012. We appreciate being granted an extension to August 20, 2012, and the time Richard Parsons and Alan Feblowitz took to meet with us to provide clarification of the findings.

Health Plan of San Joaquin will make every effort to work with CalPERS to resolve the issues detailed in the findings in a manner that is in the best interests of our organization, our employees and CalPERS.

Finding #1: The Plan erroneously reported non-reportable compensation to CalPERS.

<u>Part One: Plan incorrectly reported the bilingual pay as special compensation.</u>
HPSJ does not concur with this finding.

The finding indicates that HPSJ's bilingual pay was not contained in a written labor policy or agreement approved by the Plan's Health Commissioners, a requirement of CCR 570.5.

However, CCR 570.5 was not in effect until August, 2011, which is subsequent to the audit review period - HPSJ can't comply with a requirement that wasn't articulated at the time. It is our opinion that Government Code section 20636 is the regulation that applies, and it requires that special compensation schedules are available for public scrutiny. HPSJ complies with this requirement – pay schedules are available to the public upon request. This pay was approved by the CEO in June of 2008.

Going forward, however, HPSJ will work with CASD to ensure that our bilingual pay schedules comply with this requirement.

Part Two: "Cafeteria" pay is not compensation earnable
HPSJ does not concur with this finding.

While the label of "cafeteria benefit" may be misleading, this pay is additional base pay, is included in a monthly rate of pay of each employee and is paid in cash.

It is our opinion that this meets the definition of "compensation earnable." This pay was approved by the San Joaquin County Health Commission, and is specifically defined as a "base salary increase." (See Exhibit A)

HPSJ acknowledges that this pay does not meet the criteria for a publicly available pay schedule, and will work with CASD to meet this requirement.

Finding #2: The Plan did not list employees' pay rates in a publicly available pay schedule.

Part One – OAS was unable to match any of the pay rates reported to the amounts listed in the publicly available pay schedules.

HPSJ does not concur with this finding.

The finding indicates that OAS could not match any of the pay rates reported to the amounts listed in the publicly available pay schedules, a requirement of 570.5.

As mentioned above, CCR 570.5 was not in effect until August, 2011, which is subsequent to the audit review period - HPSJ can't comply with a requirement (570.5) that wasn't articulated at the time. It is our opinion that Government Code section 20636 is the regulation that applies, and it defines a publicly available pay schedule as one that is available for public scrutiny. HPSJ complies with this requirement. HPSJ also complies with the requirement that that pay rate schedules be approved and adopted by the employer's governing body – the San Joaquin County Health Commission approves HPSJ's pay schedules. (See Exhibit B).

The requirement that salary ranges have discrete steps has the effect of dictating the manner in which HPSJ administers its salary program. HPSJ competes with other health plans for scarce employee resources. We must have the ability to set pay rates without regard to rigid, predetermined pay increase amounts, such as step rates.

In addition, HPSJ competes with non-public organizations for business and employees. These organizations are not required to nor do most of them choose to publish pay rates, either in the form of salary schedules or salary ranges for specific jobs, because it puts them at a competitive disadvantage. This requirement puts HPSJ at a competitive disadvantage, as well.

HPSJ does not disagree that we should have a structured method for determining pay rates. HPSJ does utilize a thorough, documented methodology to determine the pay rates for each position, and individual employee salaries, as outlined below.

Salary Policy
HPSJ's salary policy was approved by the San Joaquin County Health Commission. (See Exhibit B.)

Salary Structure (pay schedule)
As mentioned above, HPSJ's pay schedules are approved by the San Joaquin County Health Commission each year. (See Exhibit B.)

Pay Rates for Individual Jobs
A fundamental aspect of HPSJ's salary program is the analysis of external equity.

HPSJ engages Mercer to conduct an annual analysis of its pay program, which includes an evaluation of external equity for selected benchmark jobs**, to ensure that HPSJ's salaries are reasonable and competitive. This is called the market rate.

Jobs are then placed into the salary structure based on this market rate. The salary structure is constructed by Mercer and is based on best practices – that is, range spread (minimum to maximum) and midpoint progression (the differences in midpoints from one salary grade to another).

After the jobs are placed into the salary structure based on external equity, members of HPSJ's Executive Team evaluate internal equity (the value of jobs relative to one another) and make adjustments to salary grade assignments as appropriate.

** The salary structure consists of multiple salary grades, divided into quartiles.*
***Benchmark jobs are those HPSJ jobs that can be matched to jobs in salary surveys*

Merit increases for Individual Employees
HPSJ utilizes salary increase guidelines to determine appropriate merit increases. These guidelines indicate the range of merit increases for which employees are eligible, given their performance and the placement (by quartile) of their salary in the salary range. (See Exhibit C.) The increase amounts are thoroughly vetted during four levels of review.

The CEO's salary is determined by the Executive Compensation Committee Health Commission. The approval is done in closed session under Public Employee Performance Evaluation – Government Code Section 54957. (See Exhibit D.) Subsequent to that meeting the Board Chairman notifies the Vice President of Human Resources of the increase amount, which is then signed off by the Board Chair, the Vice President of Human Resources and the CFO. While the merit increase amount is not specified in the minutes of the Health Commission meetings, it is fully vetted by the Health Commission.

We believe these policies and methodologies provide the necessary structure to ensure that salaries are administered in a reasonable and competitive manner.

Despite these differences of opinion, HPSJ will with CASD to develop a mutually agreeable process.

Finding #3: The Plan did not enroll employees hired through temporary employment agencies when membership eligibility requirements were met.

HPSJ acknowledges that it did not comply with the requirements of 20303(a)(3)(B). However, we maintain that this is not a reasonable requirement given our business environment and associated financial challenges.

HPSJ's business environment is complex and constantly changing - we cannot always predict staffing needs and require a flexible workforce in order to respond. Utilizing temporary workers, including long-term, gives us the ability to adjust the workforce as needed. Some of these temporaries are here for as little as two weeks and as much as two years.

While we understand the regulations, your requirement that we enroll these workers in CalPERS when they meet the 1,000 hour threshold has the effect of dictating our hiring practices.

Despite these differences of opinion, HPSJ will with CASD to develop a mutually agreeable process.

On behalf of Health Plan of San Joaquin, we want to thank you, Richard and Alan for your assistance during this process. Please call either of us if you have questions about our response.

Sincerely,

John Hackworth
Chief Executive Officer

Paul A. Antigua
Chief Financial Officer

cc: Victoria Hazen, Vice President of Human Resources