



STATE OF WISCONSIN
Legislative Audit Bureau
NONPARTISAN • INDEPENDENT • ACCURATE

Report 23-12
August 2023

State Retiree Health Insurance Reporting for the State of Wisconsin

June 30, 2022



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Legislative Audit Bureau

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Response

From the Department of Administration

Opinions Published Separately

The schedules and our opinions on them are available on the Department of Administration's website.



STATE OF WISCONSIN

Legislative Audit Bureau

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State Auditor

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August 31, 2023

Senator Eric Wimberger and
Representative Robert Wittke, Co-chairpersons
Joint Legislative Audit Committee
State Capitol
Madison, Wisconsin 53702

Dear Senator Wimberger and Representative Wittke:

As requested by the Department of Administration (DOA), we have completed an audit of the Schedule of Employer Allocations of the State Retiree Health Insurance program, the Schedule of OPEB Amounts by Participating Employer of the State Retiree Health Insurance program, and the related notes to these schedules as of and for the year ended June 30, 2022. These schedules and our unmodified opinions on them may be found on DOA's website. These schedules will be used by DOA and other employers that are part of the State's financial reporting entity, but that prepare separately issued financial statements.

The State Retiree Health Insurance program, which is one of the other postemployment benefits (OPEB) plans offered by the State of Wisconsin to eligible retirees, is administered by the Department of Employee Trust Funds (ETF). OPEB refers to the benefits, other than pensions, that a state or local government employee may receive after they have left employment, generally upon retirement. An OPEB plan may include medical, prescription drug, dental, vision, and other health-related benefits, whether provided separately or through a pension plan. An OPEB plan may also include death benefits, life insurance, and long-term care coverage, when provided separately from a pension plan.

Under the State Retiree Health Insurance program, the State offers retirees who are not yet eligible for Medicare the option to participate in the State's Group Health Insurance program. Although the State does not directly pay any portion of the premium for retirees who choose to participate in the program, the State does pay higher premiums for its active employees than it otherwise would if retirees were excluded. Therefore, the State implicitly subsidizes the premiums paid by participating retirees by offering these individuals access to health insurance coverage at a lower rate than they might otherwise pay based upon their age. This, in turn, creates an OPEB liability the State must recognize for purposes of financial reporting.

DOA reported a total OPEB liability of \$717.2 million as of June 30, 2022, for the State Retiree Health Insurance program. This liability will be reported in the State's financial statements, which will be included in the State of Wisconsin's Annual Comprehensive Financial Report (ACFR) for the year ended June 30, 2023. This is an increase of \$4.3 million from the \$712.9 million liability as of June 30, 2021, which was reported in the State's ACFR for the year ended June 30, 2022. This increase is primarily related to normal program operations and changes in health care cost trend rates and the discount rate assumptions.

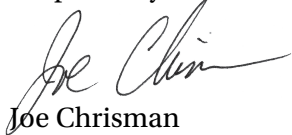
As part of this audit, we retained an actuary to conduct an independent review of the State Retiree Health Insurance program's actuarial calculations and actuarial valuation report. In general, the actuarial audit concluded that the actuarial valuation report of the program was prepared in compliance with

Governmental Accounting Standards Board (GASB) standards and the valuation was performed in accordance with the Actuarial Standards of Practice promulgated by the Actuarial Standards Board (ASB). The actuarial audit identified four errors related to the application of certain rates and assumptions in the actuarial valuation, which included three that had been identified in the prior year actuarial audit but had not yet been addressed. The actuarial audit also included six recommendations for improvement, all of which were identified in the prior year actuarial audit. Not all recommendations were expected to be addressed this year. DOA's consulting actuary agreed with the results and revised the actuarial valuation to address the three prior year errors. Since DOA did not identify that its consulting actuary had not addressed the prior year errors, we recommend that DOA ensure its consulting actuary addresses the remaining errors and recommendations identified in the actuarial audit.

The Independent Auditor's Report on Internal Control over Financial Reporting and on Compliance and Other Matters, which is required by *Government Auditing Standards*, begins on page 11.

We appreciate the courtesy and cooperation extended to us by DOA and ETF staff during our audit. A response from DOA follows our report.

Respectfully submitted,



Joe Chrisman
State Auditor

JC/BG/ag

State Retiree Health Insurance Program

Under s. 40.51, Wis. Stats., the State Retiree Health Insurance program provides postemployment health insurance coverage to all eligible retired employees of the State of Wisconsin. Through the program, the State offers certain retirees who are not yet eligible for Medicare benefits the option to continue participating in the State's Group Health Insurance program and to pay for coverage at the premium rate set for active state employees. Although the State does not directly pay any portion of the premium for retirees who choose to participate in the program, the State does pay higher premiums for its active employees than it otherwise would if retirees were excluded. Therefore, the State implicitly subsidizes the premiums paid by participating retirees by offering these individuals access to health insurance coverage at a lower rate than they might otherwise pay based upon their age. This subsidy, in turn, creates an other postemployment benefits (OPEB) liability, which the State must recognize and report under Governmental Accounting Standards Board (GASB) standards.

Calculating the Total OPEB Liability

The State Retiree Health Insurance program is considered a non-trusted OPEB plan.

Under GASB standards, the State Retiree Health Insurance program is considered a non-trusted OPEB plan because the program does not accumulate assets dedicated to providing benefits to plan members. With the oversight of the Group Insurance Board, the Department of Employee Trust Funds (ETF) has administrative responsibilities for the program, including collecting premiums and paying the providers. However, because it is a non-trusted OPEB plan, ETF is not responsible for calculating the total OPEB liability. Instead, the Department of Administration (DOA), which is the entity responsible for preparing the financial statements of the State of Wisconsin on the basis of generally

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accepted accounting principles (GAAP), is responsible for ensuring that the employer reporting requirements of the standards are being met, including the calculation of the total OPEB liability.

The total OPEB liability is the sum of amounts needed to pay for the OPEB benefits earned by each participant as of the date of the actuarial valuation. A liability exists because the State has committed to providing the benefit at some point in the future. The calculation of the total OPEB liability is complex and includes various actuarial assumptions and calculations, such as:

- a projection of future benefit payments for active and retired participants and their beneficiaries based upon the current terms of the plan;
- a discount of those payments to their present value, which is the amount of funds currently needed to provide the projected payments in the future; and
- an allocation of the present value of benefit payments over past, present, and future periods of employee service.

Assumptions Used to Calculate the Total OPEB Liability

As of June 30, 2022, the total OPEB liability for the State Retiree Health Insurance program was \$717.2 million.

Three important assumptions used in the calculation of the total OPEB liability include the discount rate, health care cost trend rates, and participation rates. In determining the total OPEB liability for the program, the consulting actuary for the State Retiree Health Insurance program used these and other assumptions to perform an actuarial valuation as of January 1, 2021. This valuation was adjusted for changes such as interest earned, contributions paid, and benefits paid through June 30, 2022. Based on this valuation and the adjustments, the total OPEB liability for the program as of June 30, 2022, was \$717.2 million, which was an increase of \$4.3 million from the \$712.9 million total OPEB liability calculated as of June 30, 2021. This increase is primarily related to normal program operations and changes in health care cost trend rates and the discount rate assumptions. Because the program is funded on a “pay-as-you-go” basis, premiums are established and collected based on the current needs of the program, and assets are not accumulated to pay future benefits.

Discount Rate

The discount rate is the interest rate used to calculate the present value of projected benefit payments and is used to calculate the total OPEB liability for the State Retiree Health Insurance program. For a non-trusted OPEB plan, GASB standards require the discount rate

to be the 20-year, tax-exempt general obligation municipal bond index rate (with an average rating of AA/Aa or higher), which was 3.54 percent as of June 30, 2022, using the Bond Buyer 20-year General Obligation Municipal Bond Index.

A change in the discount rate can have a significant effect on the amount of the total OPEB liability.

The discount rate is a critical factor in calculating the total OPEB liability and can have a significant effect on the amount of the total OPEB liability. A one percentage point increase in the discount rate for the program reduces the total OPEB liability to \$667.1 million (at 4.54 percent), and a one percentage point decrease in the discount rate increases the liability to \$770.8 million (at 2.54 percent).

Health Care Cost Trend Rates

The health care cost trend rates measure the rate of change in per capita health costs over time and are calculated for significant portions of costs, such as medical, prescription drug, and dental. For the State Retiree Health Insurance program, the consulting actuary develops the assumption using their internal guidelines, including various data sources and actual premium equivalent rates.

Changes in the health care cost trend rates can have a significant effect on the amount of the total OPEB liability.

These trend rates can have a significant effect on the amount of the total OPEB liability. A one percentage point increase in each health care cost trend rate increases the total OPEB liability to \$813.7 million, and a one percentage point decrease in each health care cost trend rate decreases the total OPEB liability to \$635.9 million.

Participation Rates

The assumptions for the participation rates measure how many retirees are expected to continue health insurance coverage after retirement as well as when retirees may discontinue coverage. Several factors can affect participation rates, including the cost of insurance on the open market, age at retirement, and eligibility for subsidized health care on public health care exchanges. Participation rates are also affected by the option for retired state employees to use accumulated sick leave balances to pay health insurance premiums under the State's Accumulated Sick Leave Conversion Credit or Supplemental Health Insurance Conversion Credit programs, which are separate programs funded by employer contributions and administered by ETF.

Because assumptions for the participation rates have a significant effect on the calculation of the total OPEB liability, and because changes to program participation may occur, it is important to ensure that the assumptions are supported by actual experience. The consulting actuary performed a participation rate experience study in May 2022.

Actuarial Audit

As part of this audit, we retained an actuary to conduct an independent review of the State Retiree Health Insurance program's actuarial calculations and actuarial valuation report. In general, the actuarial audit concluded that the actuarial valuation report of the program was prepared in compliance with GASB standards and the valuation was performed in accordance with the Actuarial Standards of Practice promulgated by the Actuarial Standards Board (ASB).

The actuarial audit identified four errors related to the application of certain rates and assumptions in the actuarial valuation, three of which had been identified in the prior year actuarial audit but had not been addressed. In response to the current year actuarial audit, DOA's consulting actuary subsequently revised the actuarial valuation to address the three prior year errors. These corrections reduced the total OPEB liability by \$1.2 million. Further, the consulting actuary stated that they would consider the remaining error in a future valuation.

The actuarial audit also identified six recommendations for improvement, all of which were identified in the prior year actuarial audit. Not all recommendations were expected to be addressed this year. The consulting actuary agreed with the results of the actuarial audit and stated that they would consider two of the recommendations in a future valuation and four of the recommendations as part of the next participation rate experience study, which is anticipated to be completed in late 2024 or early 2025.

The actuarial audit identified the same errors in the actuarial valuation as the prior year actuarial audit.

DOA staff stated that they had discussed the prior year actuarial audit findings with its consulting actuary in August 2022 and, at that time, the consulting actuary stated they had a plan to address them. Since the actuarial audit continued to identify the same errors in the actuarial valuation as the prior year, DOA should improve its procedures for working with its consulting actuary and ensure the remaining actuarial audit errors and recommendations are addressed.

Recommendation

We recommend the Department of Administration ensure that its consulting actuary for the State Retiree Health Insurance program addresses the remaining errors and recommendations identified in the actuarial audit in the next valuation or participation rate experience study.

Employer Reporting

We provided unmodified opinions on the employer schedules that report the OPEB liability and related amounts.

The total OPEB liability of \$717.2 million as of June 30, 2022, for the State Retiree Health Insurance program, as well as other collective amounts presented on the employer schedules, will be presented in the State's financial statements in the State of Wisconsin's Annual Comprehensive Financial Report (ACFR) for the year ended June 30, 2023. In addition, some state agencies, such as the University of Wisconsin (UW) System, and various authorities, including the UW Hospitals and Clinics Authority, that are reported in the State's ACFR also separately issue GAAP-based financial statements. To assist each of these agencies and authorities in determining its proportionate share of the total OPEB liability, DOA prepared employer schedules that include these amounts. We audited and provided unmodified opinions on these schedules, which are published on DOA's website. In addition, the Independent Auditor's Report on Internal Control over Financial Reporting and on Compliance and Other Matters, which is required by *Government Auditing Standards*, begins on page 11.

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Auditor's Report





Independent Auditor's Report on Internal Control over Financial Reporting and on Compliance and Other Matters

Senator Eric Wimberger and
Representative Robert Wittke, Co-chairpersons
Joint Legislative Audit Committee

Ms. Kathy Blumenfeld, Secretary
Department of Administration

We have audited the Schedule of Employer Allocations of the State Retiree Health Insurance program as of and for the year ended June 30, 2022, and the related notes. We have also audited the totals for the columns titled Ending Total OPEB Liability, Total Deferred Outflows of Resources, Total Deferred Inflows of Resources, and Total Employer OPEB Expense included in the Schedule of OPEB Amounts by Participating Employer of the State Retiree Health Insurance program as of and for the year ended June 30, 2022, and the related notes. We have issued our report thereon dated August 28, 2023. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, which is issued by the Comptroller General of the United States. The schedules and related auditor's opinions have been included in the *State of Wisconsin Retiree Health Insurance Plan 2023 GASB 75 Employer Schedules* report, as prepared by the State of Wisconsin Department of Administration (DOA).

Report on Internal Control over Financial Reporting

Management is responsible for establishing and maintaining effective internal control over financial reporting (internal control). In planning and performing our audit of the State Retiree Health Insurance program schedules, we considered DOA's internal control as a basis for designing audit procedures that are appropriate in the circumstances for the purpose of expressing our opinions on the schedules, but not for the purpose of expressing an opinion on the effectiveness of DOA's internal control. Accordingly, we do not express an opinion on the effectiveness of DOA's internal control.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent misstatements, or to detect and correct misstatements on a timely basis. A *material weakness* is a deficiency or a combination of deficiencies in internal control such that there is a reasonable possibility that a material misstatement of the schedules will not be prevented, or that a material misstatement will not be detected and corrected on a timely basis. A *significant deficiency* is a deficiency or a combination of deficiencies in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any

deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses or significant deficiencies may exist that have not been identified.

Report on Compliance and Other Matters

As part of obtaining reasonable assurance about whether the State Retiree Health Insurance program schedules are free from material misstatement, we performed tests of compliance with certain provisions of laws, regulations, and contracts, noncompliance with which could have a direct and material effect on the schedules. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

Purpose of This Report

This report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be used when considering DOA's internal control and compliance. The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the result of that testing, and not to provide an opinion on the effectiveness of DOA's internal control or on compliance. Accordingly, this report is not suitable for any other purpose.

LEGISLATIVE AUDIT BUREAU



August 28, 2023

Response



STATE OF WISCONSIN
DEPARTMENT OF ADMINISTRATION

Tony Evers, Governor
Kathy Blumenfeld, Secretary

August 28, 2023

Mr. Joe Chrisman, State Auditor
Legislative Audit Bureau
22 East Mifflin Street, Suite 500
Madison, Wisconsin 53703

Dear Mr. Chrisman,

Thank you for the opportunity to respond to the 2023 audit report for the Schedule of Employer Allocations of the State Retiree Health Insurance Program. The Department of Administration (DOA) understands our responsibility for ensuring the actuarial valuation is materially accurate each year. During the current year DOA worked with our consulting actuary to correct material findings. DOA will also work with our consulting actuary on future valuations to ensure changes related to the remaining findings or recommendations are addressed.

DocuSigned by:

A handwritten signature in black ink that reads "Kathy Blumenfeld".

Kathy Blumenfeld, Secretary
Department of Administration