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Acting State Auditor
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Constitutional Mandate

The Office of the Auditor, pursuant to Article VII, Section 10 of the Hawai'i State Constitution, is required to conduct post-audits of the transactions, accounts, program and performance of departments, offices and agencies of the State and its political subdivisions, and to certify to the accuracy of all financial statements issued by the respective accounting officers.

Financial Audit of the Hawai'i Employer-Union Health Benefits Trust Fund

Financial Statements, Fiscal Year Ended June 30, 2013

The primary purpose of the audit was to form an opinion on the fairness of the presentation of the financial statements for the Hawai'i Employer-Union Health Benefits Trust Fund as of and for the fiscal year ended June 30, 2013. The audit was conducted by PKF Pacific Hawai'i LLP (PKF).

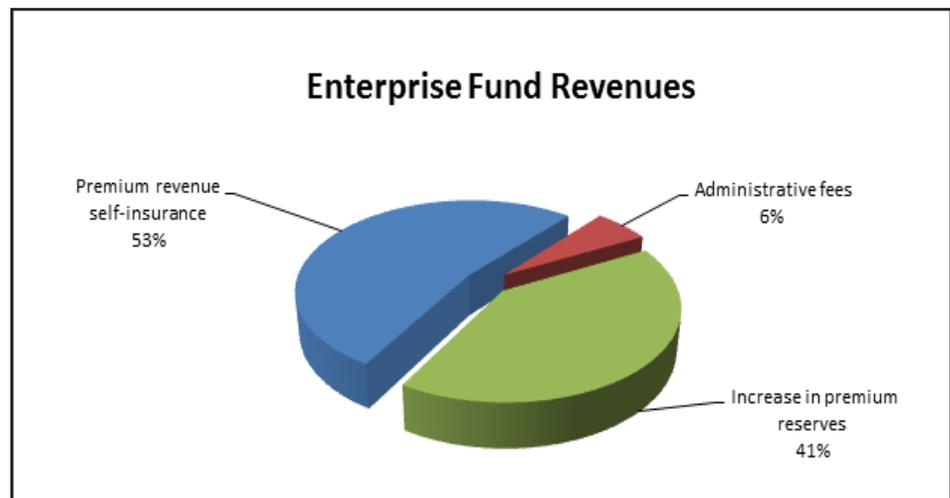
About the Trust Fund

The Hawai'i Employer-Union Health Benefits Trust Fund (EUTF or "Trust Fund") is a state agency that provides eligible State of Hawai'i and county (Honolulu, Hawai'i, Kaua'i, and Maui) employees and retirees and their eligible dependents with health and life insurance benefits at a cost affordable to both the public employers and participants. The EUTF is administered by a Board of Trustees, which is composed of ten trustees appointed by the Governor. The Trust Fund currently provides medical, prescription drug, dental, vision, chiropractic, dual-coverage medical and prescription and group life insurance benefits.

Financial Highlights

The EUTF uses an enterprise fund to account for the revenues, expenses, net position, assets and liabilities for active employee health benefits. For retiree beneficiaries, the EUTF accounts for assets and liabilities associated with other post-retirement benefits (OPEB) in an agency fund. In addition, on June 30, 2013, the EUTF began using an OPEB Trust Fund to account for contributions received from the State and county government employers to pre-fund retiree health benefits, as well as the assets and net position arising from the pre-funding contributions and related investment income.

Enterprise Fund: For the fiscal year ended June 30, 2013, operating revenues totaled \$96.4 million and operating expenses totaled \$53.4 million, resulting in a net operating income of \$43 million.





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Auditors' Opinion

Financial Statements: **Unmodified opinion** +

Issues of Concern

Material Weaknesses

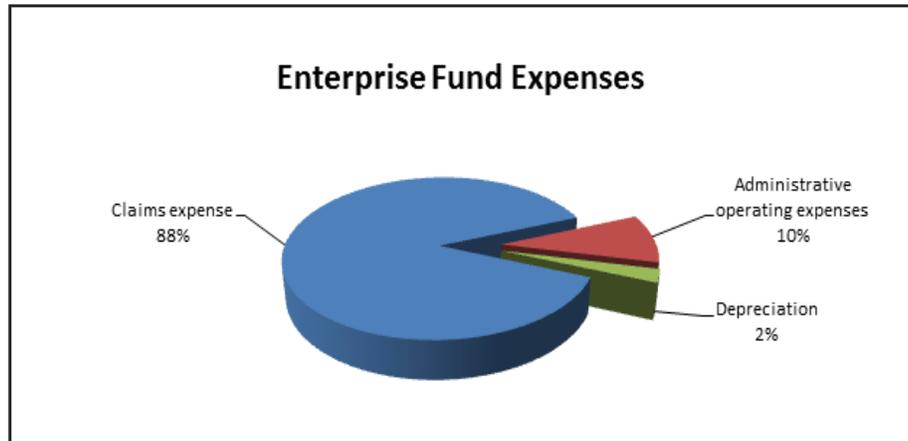
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Significant Deficiencies

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Enterprise Fund operating expenses included \$46.8 million related to claims. The fund also reported \$5.2 million for administrative operating expenses and \$1.4 million for depreciation.



As of June 30, 2013, Enterprise Fund assets totaled \$93.6 million and liabilities \$42.2 million, leaving a net position balance of \$51.4 million.

Agency Fund: As of June 30, 2013, the EUTF's Agency Fund held \$185.6 million in assets, which included \$127.4 million in cash and investments. Other Agency Fund assets included \$50 million in receivables and \$8 million in deposits with insurance carriers. Agency Fund liabilities also totaled \$185.6 million, of which \$159.3 million was held on behalf of employers for retiree benefits.

OPEB Trust Fund: Effective June 30, 2013, \$314.8 million in employer pre-funding contributions and related net investment earnings were transferred from the Agency Fund into the OPEB Trust Fund. Accordingly, cash and investment assets reported for the OPEB Trust Fund totaled \$314.8 million at June 30, 2013.

Auditors' Opinion

The EUTF received an unmodified opinion that the financial statements were presented fairly, in all material respects, in accordance with generally accepted accounting principles.

Findings

PKF identified two material weaknesses and one significant deficiency in internal controls, as follows:

Material Weaknesses

- Reconciliations of insurance rebates receivable accounts did not timely identify a material difference between quarterly rebate estimates and actual rebates, resulting in a \$2.4 million understatement of the receivable balance. (This understatement error has been corrected in the audited financial statements.) The EUTF should implement procedures to reconcile rebates receivable upon receipt and adjust the accounts for any differences between estimated and actual amounts received.
- The EUTF engages an external benefit plan consultant to assist in determining accruals for benefit claims payable, which includes estimates for "incurred but not reported" (IBNR) claims. As a result of audit procedures performed, PKF auditors noted a material error in IBNR accruals, which resulted in a \$2.5 million overstatement of benefit claims payable. (This overstatement error has been corrected in the audited financial statements.) The EUTF should implement procedures to more closely review the IBNR reports prepared by the consultant.

Significant Deficiency

- As noted in prior audits, the EUTF does not have a formal risk assessment or monitoring process and does not have current policies and procedures documented.

For the complete report and financial statements visit our website at:
http://files.hawaii.gov/auditor/Reports/2013_Audit/EUTF2013.pdf