



Internal Audit Report

Employee Benefit Plans Audit

457 Deferred Compensation Plan and 401(a) Plans

January 1, 2012 through December 31, 2012

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Transmittal Letter

Audit Committee
Port of Seattle
Seattle, Washington

We have completed an audit of the Employee Retirement Benefit Plans.

We reviewed information relating to the 457 Deferred Compensation Plan and the three 401(a) Plans for represented and non-represented employees for 2012.

We conducted this performance audit in accordance with generally accepted government auditing standards. 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 audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

We extend our appreciation to the management and staff of Human Resources for their assistance and cooperation during the audit.



Joyce Kirangi, CPA, CGMA
Director, Internal Audit

Executive Summary

Audit Scope and Objective The purpose of the audit was to determine whether management has implemented adequate controls to ensure:

1. The Plans comply with IRS requirements, such as:
 - Contributions do not exceed annual contribution limits.
 - Loans and unforeseen emergency withdrawals have been administered in accordance with Plan regulations.
 - Required distributions have been made to eligible individuals.
 - Employer contributions have been made in accordance with the applicable Plan documents.
2. The Port's fiduciary responsibilities have been adequately met, such as:
 - Sufficient information is provided so employees can make informed investment decisions.
 - A variety of investment choices are available with different risk and reward characteristics.
 - Expenses are reasonable.
 - Deposits are processed by the record keeper on a timely basis.

We reviewed information for the period January 1, 2012, through December 31, 2012.

Background For eligible employees, the Port offers the following retirement benefits:

- 457 Deferred Compensation Plan.
- 401(a) Plan - The plan is a money-purchase plan with employer-only contributions.
- Washington State Public Employee Retirement System (PERS) Plans.
- Union pension benefits provided under collective bargaining agreement.

The state and union plans were outside the scope of this audit.

A third party is the record keeper for the Plans and receives contributions, disburses payments, and passively directs investment into selected funds as chosen by participants. The Port has delegated authority to Port employee committees for administration:

- Administrative Committee for managing the Plans.
- Investment Committee for selecting appropriate investments for participants.

Audit Result Summary Management has implemented adequate controls to provide reasonable assurance that the Plans comply with IRS requirements and that the Port's fiduciary responsibilities are met.

Background

For eligible employees, the Port offers several retirement benefits: a tax-deferred compensation plan, retirement savings plans, and a contribution to the Washington state-run pension systems (“PERS”).

- 457 Deferred Compensation Plan:

This plan, which began in the 1970s, is a voluntary tax-deferred savings plan, similar to a 401(k) plan. This plan is subject to the applicable IRS rules and regulations. All contributions are from employees only – there is no employer contribution. Contributions are tax deductible, that is, contributions are before income taxes are calculated. Benefits are taxed upon receipt. The IRS sets contribution limits annually, with additional “catch-up” limits for those participants age 50+ and those who are within three years of retirement.

- 401(a) Plan:

This plan is a money-purchase plan with employer-only contributions. The IRS also regulates these plans. Port contributions vary from non-represented to Police and Firefighters:

- Non-represented employees participating in the 457 Plan:
 - The Port provides an initial dollar-for-dollar match up to \$1,000 per year. The dollar limit increases with length of service up to a maximum of \$2,200 per year.
- For Police and Firefighters – separate plans:
 - The Port contributes 6.2% of gross earnings up to a maximum of \$110,100 of earnings, in lieu of contributing to Social Security. The Port also contributed \$1.15 per hour worked for Firefighters.
- Washington State Public Employee Retirement System (PERS) Plan (other plans available depending on position).
 - PERS plans 1 and 2 are defined benefits plans. PERS Plan 3 is a defined benefit plan with a member-funded defined contribution component.
- Union pension benefits provided under collective bargaining agreements:
 - The benefits vary by plans offered.

The state and union plans described previously and the executive 401(a) plan were outside the scope of this audit.

The following outlines the key characteristics of these Plans

Characteristics of the Port's 457 and 401 (a) plans			
<i>As of December 31, 2012. Dollars in millions*</i>			
Characteristics In 2012	457 Plan	401(a) Plan	
		Non-Represented	Police/Fire (separate plans)
Assets*	\$106	\$13	\$18
2012 Contributions*	\$6.7	\$0.9	\$1.1
Participants (includes retirees)	1,545	1,147	219
Contributions from	Employee	Port	Port
Voluntary	Yes	Yes ¹	No
Tax-deductible	Yes	No	No
Loans Allowed	Yes	No	No
Normal Limit	\$17,000	\$1,000 - \$2,200	\$6,826
Contribution rate	Variable	By years of service	6.2% ²
Age 50+ Catch-up limit	\$5,500	N/A	N/A
Normal Retirement	\$34,000	N/A	N/A
Age Catch-up Limit		N/A	N/A
Investment management	Employee	Employee	Employee

Data Source: IRS; Plan documents; ICMA-RC reports
Data Note:¹ Employee must contribute to the 457 plan.
² An additional \$1.15 per hour for Firefighters.

There is a variety of internal parties involved in the administration and management of these plans:

- Committees:
 - Administrative Committee: Port employees with delegated authority from the CEO to administer the plans, such as choosing the record keeper and trustee.
 - Investment Committee: Port employees delegated to make all decisions related to investments. The Committee selects a variety of investment options with varying risk and reward characteristics for participants to select for investment. The investment choices range from expected low-risk/low-return such as money market funds to expected higher risk/higher return such as emerging markets. The portfolio also includes a number of asset allocation funds which automatically reallocate funds by asset category based on expected age at retirement.
- Corporate Departments:
 - Human Resources: responsible for the retirement benefit plans, such as processing Salary Reduction Agreements and retirement forms, and is the key contact with the record keeper.
 - Payroll: responsible for the appropriate deductions for employee and employer contributions and reporting the details of contributions to the record keeper.
 - Treasury: responsible for transferring the appropriate funds to the record keeper.
- Plan Participants:
 - Employees who participate in the plans manage their contributions by selecting the appropriate investment funds directly with the record keeper from a portfolio selected by the Investment Committee. A participant may also select the self-directed brokerage option that is available. The plan has no control over investment decisions made by the participants.

There are also external parties administering these plans:

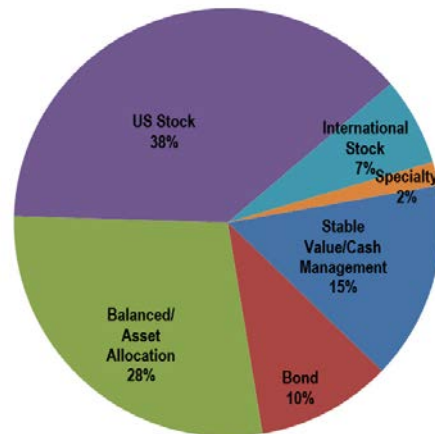
- Record keeper
 - Since March 2012, ICMA-RC (International City/County Management Association – Retirement Corporation) receives contributions, disburses payments, and passively directs investment into selected funds as chosen by participants. Their fee is \$60 per participant per year, which currently is paid out of revenue sharing from the fund companies. All fees and expenses are paid from the Plans. The Record Keeper also provides a variety of financial planning education and advice to participants, from seminars to detailed financial plans prepared by Certified Financial Planners.
- Trustee
 - The Trustee provides oversight of the process for ICMA-RC’s handling of plan contributions, investments and disbursements. Wilmington Trust Retirement and Institutional Services Company is the current trustee. The trustee is independent from the record keeper and does not sell investment funds.
- Investment consultant
 - The consultant provides investment advice and performance analysis to the Investment Committee. The consultant does not sell investment funds.

The figures below provide a detailed breakout of the Asset Allocation for the 457 Plan as at December 31, 2012:

Value and Distribution of Asset Allocations in the Port of Seattle’s 457 Plan

As of December 31, 2012

Asset Category	Balance
Stable Value/Cash Management	\$15,820,573
Bond	10,805,602
Balanced/Asset Allocation	29,709,019
US Stock	40,541,635
International Stock	7,012,584
Specialty	1,891,769
Total Asset Value	\$105,781,181



Data Source: ICMA-RC

Participants in the 457 plan may obtain an interest-bearing loan against their contributions, to a maximum of \$50,000 and loans must be repaid within five years, except for purchasing a residence. For 2012, 131 participants took \$1.6 million in new loans.

Highlights and Accomplishments

During the course of the audit, we observed the following highlights:

- The roles and responsibilities of the Administrative and Investment Committees for each Plan were documented and formalized by approval by the CEO in September 2012 by the *Administration Policy and Procedures for Employee Benefits Plan*.
- In 2012, the Plans changed to a new record keeper, trustee, and investment consultant respectively to reduce Plan expenses and provide fresh insights.
- The change of record keeper allows participants to view all their retirement plans, including the PERS 3 pension plan, and to manage their 457 and 401(a) accounts on-line, such as allocating investments and requesting loans. ICMA-RC has robust reporting capabilities available both to participants and to the plan administrators.

Audit Scope and Methodology

We reviewed information for the period January 1, through December 31, 2012. We utilized a risk-based audit approach from planning to testing. We gathered information through research, interviews, observations, analytical reviews, and obtain a complete understanding of the 457 plan and the 401(a) plans. We assessed significant risks and identified controls to mitigate those risks. We evaluated whether the controls were functioning as intended.

We applied additional detailed audit procedures to areas with the highest likelihood of significant negative impact as follows:

1. To determine whether management has implemented adequate controls to ensure compliance with IRS requirements:
 - We tested a risk-based sample of 38 of 457 plan participants that possibly exceeded the maximum annual contribution; we reviewed their Salary Reduction Agreement forms and ICMA-RC records.
 - We tested a risk-based sample of ten participants with loans for adequate documentation and repayments per the plan and IRS regulations.
 - We tested that all 2012 loans met the IRS regulations regarding maximum size, repayment period, and reasonable interest rate.
 - We tested the only two emergency withdrawals selected from ICMA-RC records for proper documentation.
 - We analyzed data to for any required distributions for participants who attained age 70½ in 2012.
 - We tested all employer contributions related to gross earnings to the Police and Firefighters 401(a) plans for proper and timely employer contributions.
 - We tested three months of employer contributions for hours worked for the Firefighters 401(a) plan for proper employer contributions
 - We tested a risk-based sample of 119 participants in the 401(a) plan for non-represented employees for proper and timely employer contributions.

2. To determine whether management has implemented adequate controls to ensure the Port's fiduciary responsibilities have been adequately met:
- We reviewed two quarterly plan performance reports for compliance with the Investment Policy.
 - We reviewed the 2011 costs for the previous record keeper and trustee compared to 2012 costs.
 - We reviewed the most recent revenue and cost analysis.
 - We tested random samples of deposits for timely processing.
 - We reviewed the reconciliation of the participant records from Great-West transfer to ICMA-RC.
 - We reviewed reports available from ICMA-RC for investment choices, performance evaluations, and plan administration.
 - We reviewed the Title I requirements of Employee Retirement Income Security Act (ERISA) for applicability to the plans.
 - We reviewed the Service Organization Control 1 Type II reports for ICMA-RC and Wilmington Trust for applicable controls and test results.
 - We conducted an on-site visit to ICMA-RC to evaluate controls.

Conclusion

Management has implemented adequate controls to provide reasonable assurance that the plans comply with IRS requirements and that the Port's fiduciary responsibilities are met.