

STATE OF NEW YORK INSURANCE DEPARTMENT
REPORT ON EXAMINATION
OF THE
NEW YORK CITY
POLICE SUPERIOR OFFICERS' VARIABLE SUPPLEMENTS FUND
AS OF
JUNE 30, 1999

DATE OF REPORT:

MARCH 16, 2001

EXAMINER:

EUGENE THUMMEL

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STATE OF NEW YORK
INSURANCE DEPARTMENT
25 BEAVER STREET
NEW YORK, NEW YORK 10004

March 16, 2001

Honorable Gregory V. Serio
Superintendent of Insurance
Albany, New York 12257

Sir:

In accordance with instructions contained in Appointment No. 21625, dated October 4, 2000 and annexed hereto, an examination has been made into the condition and affairs of the Police Superior Officers' Variable Supplements Fund, hereinafter referred to as "the Fund," at its home office located at located at 1 Police Plaza, New York, New York 10038.

Wherever "Department" appears in this report, it refers to the State of New York Insurance Department.

The report indicating the results of this examination is respectfully submitted.

1. EXECUTIVE SUMMARY

The Fund was established effective July 1, 1970 and provides supplemental benefits to police officers who retired from service on or after October 1, 1968. Benefits became guaranteed to eligible members of the police force in 1993 with the adoption of Chapter 479 of the laws of 1993, which amended Title 13, Chapter 2 of the New York City Administrative Code (“Administrative Code”).

The examiner’s review of a sample of transactions did not reveal any differences, which materially affected the Fund’s financial condition as presented in its financial statements contained in the June 30, 1999, filed annual statement. (See item 5 of this report)

The board of trustees did not approve the actuarial assumptions as required by Section 13-270(e) of the Administrative Code. (See item 4 of this report)

The examiner recommends that, upon the adoption of updated Rules and Regulations by the New York City Police Department, Subchapter Two Pension Fund (“Police Pension Fund”), the Fund incorporate all changes that have been instituted since 1940. (See item 8 of this report)

2. SCOPE OF EXAMINATION

The prior examination was conducted as of June 30, 1997. This examination covers the period from July 1, 1997 through June 30, 1999. As necessary, the examiner reviewed transactions occurring subsequent to June 30, 1999 but prior to the date of this report (i.e., the completion date of the examination).

The examination comprised a verification of assets and liabilities as of June 30, 1999 to determine whether the Fund's 1999 filed annual statement fairly presents its financial condition. The examiner reviewed the Fund's income and disbursements necessary to accomplish such verification and utilized such other examination procedures, as deemed appropriate, in the review or audit of the following matters:

- Fund history
- Administration
- Accounts and records
- Member benefits
- Financial statements

The examiner reviewed the corrective actions taken by the Fund with respect to violations, recommendations and/or comments contained in the prior report on examination. The results of the examiner's review are contained in item 10 of this report.

This report on examination is confined to financial statements and comments on those matters which involve departure from laws, regulations or rules, or which require explanation or description.

3. DESCRIPTION OF FUND

A. History

The Fund was established effective July 1, 1970 by amendment to the Administrative Code, which added a new Article 4 to Title B of Chapter 18. The Police Officers' Variable Supplements Fund was established the same date as the Fund by the addition of a new Article 3 and is covered under a separate report on examination. Article 3 and 4 were combined and recodified as Title 13, Chapter 2, and Subchapter 3 of the Administrative Code.

The Fund receives monies from the Police Pension Fund pursuant to the provisions of Section 13-232.3 of Subchapter 2 of the Administrative Code, which are referred to as transferable earnings ("SKIM"), in addition to monies received from any other source pursuant to law.

The Fund is administered independently by a board of trustees and has the powers and privileges of a corporation. Members of the board are trustees of the monies and have the power to invest the same in accordance with the limitations and restrictions imposed on savings banks and the Administrative Code. The Comptroller of the City of New York ("Comptroller") is the custodian of the assets and also provides certain administrative services to the Fund.

Basic pension benefits are provided to police officers through their membership in the Police Pension Fund. The Fund provides supplemental benefits to police superior officers who are service retirees of the New York City Police Department on or after October 1, 1968 with 20 years or more of service. Receipt of benefits does not constitute membership in a pension or retirement system and benefits paid to recipients do not constitute pension or retirement benefits.

Under Section 13-287 of the Administrative Code, the Fund is subject to the supervision of the Department, which may examine its affairs with the same powers and jurisdiction as are applicable to a life insurance company under Article 3 of the New York Insurance Law.

B. Growth

The assets of the Fund increased by 25.6% during the examination period. The total retirees receiving benefits increased from 7,758 as of June 30, 1997 to 8,016 as of June 30, 1999.

4. ADMINISTRATION

Management of the Fund is vested in its board of trustees. Section 13-280 of the Administrative Code states that the board shall consist of a representative of the Mayor, the Comptroller, the Commissioner of Finance and four representatives of the police superior officers.

The members of the board of trustees and their principal business affiliation as of June 30, 1999 were as follows:

<u>Members</u>	<u>Affiliation</u>
Laurence Levy	Representative of the Mayor of the City of New York
Jane Levine	Representative of the Comptroller of the City of New York
Seth A. Cohen	Representative of the Commissioner of Finance
John F. Driscoll	President, Captain's Endowment Association
Anthony Garvey	President, Lieutenant's Benevolent Association
Thomas J. Scotto	President, Detective's Endowment Association
Joseph J. Toal	President, Sergeant's Benevolent Association

Faith Miller replaced Seth A. Cohen on July 1, 2000. On September 8, 2000, Faith Miller was replaced by Susan Rockford. Bernard Pound replaced Joseph J. Toal on December 17, 1999.

The examiner's review of the minutes of the meetings of the board of trustees and its committees indicated that meetings were well attended and that each trustee attended a majority of meetings.

Section 13-280(b) of the Administrative Code provides that the board of trustees of the Fund consists of seven members. The Fund annual statements for 1998 and 1999 each showed an eighth member of the board of trustees, the Fund treasurer, Alan G. Hevesi. It is recommended that the annual statement show as board members only the actual board members or their designated representative. A similar recommendation appeared in the previous report on examination.

Section 13-270(e) of the Administrative Code states, in part:

“The actuarial assumptions used by the actuary in making such annual valuation of liabilities including assumptions as to interest rate, mortality of pension fund beneficiaries and number of police officers in service . . . shall be adopted by the board on the recommendation of the actuary”.

A review of the minutes of the board indicated that the actuarial assumptions for the years 1998 and 1999 were not approved by the board. The examiner recommends that the Fund adhere to Section 13-270(e) of the Administrative Code by having the board approve the actuarial assumptions and reflecting such in the board meeting minutes. This recommendation appeared in the previous report on examination.

5. FINANCIAL STATEMENTS

The following statements show the comparative statement of income and disbursements for the period since the prior examination and the assets and liabilities as of June 30, 1998 and June 30, 1999.

A. STATEMENT OF INCOME AND DISBURSEMENTSFiscal Year Ending June 30,

	<u>1998</u>	<u>1999</u>
Ledger assets at end of previous year	\$ <u>860,605,813</u>	\$ <u>879,514,096</u>
<u>Income</u>		
Interest on collateral loans	\$ 473,926	\$ 0
Gross interest on bonds less accrued interest	22,332,121	21,104,283
Gross dividends	9,919,767	9,802,798
Gross interest on STIF	702,941	1,318,602
Gross interest on commercial paper	11,976	104,649
Investment income	296,871	27,646
Security lending	51,623	287,359
Gross profit on sale of bonds	6,450,047	4,941,262
Gross profit on sale of stocks	33,736,771	56,869,571
Gross increase by adjustment on book value of bonds	<u>524,411</u>	<u>260,982</u>
Total income	\$ <u>74,500,454</u>	\$ <u>94,717,152</u>
<u>Disbursements</u>		
Benefit payments	\$ 48,363,773	\$ 51,636,622
Investment expense	19,237	1,530
Foreign tax withheld on foreign investment	827	983
Federal withholding tax	1,500	0
Gross loss on sale or maturity of bonds	687,047	2,394,730
Gross loss on sale or maturity of stocks	5,036,159	21,261,103
Decrease by adjustment in book value of bonds	<u>961,790</u>	<u>1,224,307</u>
Total disbursements	\$ <u>55,592,171</u>	\$ <u>76,519,275</u>
Net increase	\$ <u>18,908,283</u>	\$ <u>18,197,877</u>
Ledger assets at end of current year	\$ <u>879,514,096</u>	\$ <u>897,711,973</u>

B. STATEMENT OF ASSETS AND LIABILITIES

	<u>June 30, 1997</u>	<u>June 30, 1999</u>	<u>Increase (Decrease)</u>
<u>Assets</u>			
<u>Ledger assets</u>			
Cash on deposit	\$ 551,876	\$ 137,287	\$ (414,589)
Commercial paper	1,113,925	12,539,656	11,425,731
Bonds	330,427,591	334,285,932	3,858,341
Stocks	419,348,727	397,497,438	(21,851,289)
International investments	101,200,000	135,424,739	34,224,739
Short term funds	12,501,991	16,157,409	3,655,418
Treasury bills	2,920,000	3,800,000	880,000
Receivable for investment securities sold	20,816,182	24,840,104	4,023,922
Payment for investment securities purchased	<u>(28,274,479)</u>	<u>(26,970,592)</u>	<u>1,303,887</u>
Total ledger assets	<u>\$ 860,605,81</u>	<u>\$ 897,711,973</u>	<u>\$ 37,106,160</u>
<u>Non-ledger assets</u>			
Interest due and accrued on commercial paper	\$ 1,249	\$ 240,305	\$ 239,056
Interest due and accrued on bonds	3,927,282	3,930,682	3,400
Dividends due and accrued	693,329	706,220	12,891
Market value of stocks over book value	<u>215,393,832</u>	<u>454,797,500</u>	<u>239,403,668</u>
Total non-ledger assets	<u>\$ 220,015,692</u>	<u>\$ 459,674,707</u>	<u>\$239,659,015</u>
Total admitted assets	<u>\$1,080,621,404</u>	<u>\$1,357,386,680</u>	<u>\$276,765,276</u>
<u>Liabilities</u>			
Present value of benefits payable on account of beneficiaries now drawing allowances	\$ 633,986,308	\$ 732,416,394	\$ 98,430,086
Present value of benefits provided by employer for members now in active service	<u>391,742,683</u>	<u>551,066,459</u>	<u>159,323,776</u>
Total liabilities	<u>\$1,025,728,991</u>	<u>\$1,283,484,853</u>	<u>\$257,755,862</u>
Excess of admitted assets over liabilities	<u>\$ 54,892,413</u>	<u>\$ 73,901,827</u>	<u>\$ 19,009,414</u>
Total	<u>\$1,080,621,404</u>	<u>\$1,357,386,680</u>	<u>\$276,765,276</u>

6. TRANSFERS FROM THE NEW YORK CITY POLICE DEPARTMENT,
SUBCHAPTER TWO PENSION FUND

The Police Pension Fund provides the necessary funding for the Fund. Section 13-232.3 of the Administrative Code states, among other things, how the amounts transferred into the Fund shall be computed.

The Administrative Code provides that the Police Pension Fund transfer to the Fund (and the Police Officers' Variable Supplements Fund) an amount equal to certain excess earnings on equity investments, referred to as transferable earnings or "SKIM", which exceed what the earnings might have been had such funds been hypothetically invested in fixed income securities, less any cumulative earnings deficiencies. If earnings on equity investments were below those of the hypothetical fixed income securities no SKIM would be available.

During the period under examination, no SKIM was transferred from the Police Pension Fund to the Fund.

7. MEMBER BENEFITS

Benefits are paid to retired eligible officers based on Section 13-281(b)(1) of the Administrative Code. Benefits are offset by a portion of the Cost of Living Allowance (“COLA”) supplement to the police superior officer’s pension until the retiree reaches age 62 or calendar year 2007, whichever is later.

Prior to July 21, 1993, supplemental benefits paid to Fund members had to be declared by the board of trustees on an annual basis. As a result of labor negotiations, Chapter 479 of the Laws of 1993 (effective July 21, 1993) was enacted and provided for defined schedules of supplemental benefit payments, which are guaranteed by the City of New York (“the City”). As a result, if the assets of the Fund could not support the supplemental benefit payments, then the City would be required by law to fund the difference.

For police officers who were hired prior to July 1, 1988 and who retire on or after July 1, 1997 from service (with a credit of 20 or more years), the following table reflects the guaranteed benefits payable per beneficiary:

<u>Calendar Year</u>	<u>Annual Supplement</u>	<u>Calendar Year</u>	<u>Annual Supplement</u>
1997	\$7,000	2003	\$10,000
1998	\$7,500	2004	\$10,500
1999	\$8,000	2005	\$11,000
2000	\$8,500	2006	\$11,500
2001	\$9,000	2007 and each	\$12,000
2002	\$9,500	calendar year thereafter	

For officers hired on or after July 1, 1988, the annual benefit would start at \$2,500 (prorated from the date of retirement) and increase in \$500 increments each calendar year until reaching the \$12,000 maximum. Benefits are paid once a year on or about December 15th.

The examiner reviewed a random sample of benefit payments to retirees and beneficiaries to determine whether the member or beneficiary was treated fairly and in accordance with the rules governing the Fund. The examiner also reviewed the various controls

involved, checked the accuracy of the computations and traced accounting data to the books of account. Based upon the random sample reviewed, no significant findings were noted.

8. RULES AND REGULATIONS

The previous report on examination recommended that the Fund develop and maintain updated Rules and Regulations and have these available for the next examination. The Fund utilizes the same Rules and Regulations as the Police Pension Fund. The Administrative Code was re-codified in 1985. The Rules and Regulations used by the Fund are based on the Administrative Code as reenacted in 1940, and therefore, make reference to provisions of the Administrative Code which are obsolete and no longer applicable. The Police Pension Fund has stated that it will begin the process of rewriting its Rules and Regulations and submit them to the New York City Law Department for review. The revised Rules and Regulations will also be applicable to the Police Officers' Variable Supplements Fund. Upon the adoption of updated Rules and Regulations by the Police Pension Fund, the examiner recommends that the Fund adopt the same updated Rules and Regulations as the Police Pension Fund, incorporating all changes that have been instituted since 1940.

9. CUSTODIAL AFFIDAVIT

Citibank is the custodian of securities for the Fund. At the beginning of the examination, a request to confirm the Fund's securities was sent to the bank. The examiners did not receive a proper confirmation from Citibank. The Comptroller provided the examiners with an electronic inventory of securities held by Citibank on CD-ROM and Citibank separately confirmed that the CD-ROM we received from the Comptroller did in fact contain the inventory of securities held for the Fund. A proper confirmation should require the custodian to provide an inventory of all securities held by them, as well as, a notarized affidavit.

The examiner recommends that the Fund facilitate the Department in obtaining proper confirmations from its custodian.

10. PRIOR REPORT SUMMARY AND CONCLUSIONS

Following are the violations, recommendations and comments contained in the prior report on examination and the subsequent actions taken by the Fund in response to each citation:

<u>Item</u>	<u>Description</u>
A	<p>The examiner recommends that the Fund demonstrate compliance with Section 13-280(e) of the Administrative Code and show approval of the actuarial assumptions annually in the board meeting minutes.</p> <p>The Fund failed to take corrective action in response to this recommendation. (See item 4 of this report)</p>
B	<p>The examiner recommends that the Fund's filed annual statement show as board members only the actual board members or their designated representative.</p> <p>The Fund failed to take corrective action in response to this recommendation. (See item 4 of this report)</p>
C	<p>The examiner recommends that the minutes of the meetings of the board of trustees indicate who the attendees are at the meeting and whom they represent. The examiner further recommends that the Fund retain the document authorizing the representative to act on behalf of the board member.</p> <p>The minutes of the meetings of the board of trustees indicated who the attendees were and whom they represented for each of the years under examination. The Fund retained the document authorizing the representative to act on behalf of the board member for each of the years under examination.</p>
D	<p>The Fund violated Section 136.4 of Department Regulation No. 85 when it failed to maintain documentation supporting the amounts reported in its 1997 filed annual statement.</p> <p>A review of the Fund's workpapers revealed that the Fund maintains supporting documentation for amounts reported in its filed annual statements.</p>

<u>Item</u>	<u>Description</u>
E	<p>The Fund reported a liability, “Unallocated loss,” of \$1,683,485, which represented an adjustment to the bond asset. The examiner recommends that the Fund report bonds at book value, net of any adjustments on the asset page of the annual statement.</p> <p>The Fund is reporting bonds at book value, net of any adjustments, on the asset page of the annual statement.</p>
F	<p>The examiner recommends that the Fund properly identify in its annual statement income from the source that generates it.</p> <p>A review of the Fund’s workpapers revealed that the Fund identified income from the sources that generated it during each of the two years under examination.</p>
G	<p>The examiner recommends that the Fund develop and maintain Rules and Regulations.</p> <p>The Fund utilizes the same Rules and Regulations as the Police Pension Fund. The Police Pension Fund has not updated its Rules and Regulations to incorporate all the changes that have been instituted since 1940. The Police Pension Fund has stated that in response to the examiner’s recommendation, it will rewrite the Rules and Regulations and submit them to the New York City Law Department for review.</p>

11. SUMMARY AND CONCLUSIONS

Following are the recommendations contained in this report:

<u>Item</u>	<u>Description</u>	<u>Page No(s).</u>
A	The examiner recommends that the annual statement show as board members only the board members or their designated representative. This is a repeat recommendation from the prior report on examination.	5
B	The examiner recommends that the Fund adhere to Section 13-270(e) of the Administrative Code by approving the actuarial assumptions and reflecting it in the board meeting minutes. This is a repeat recommendation from the prior report on examination.	6
C	The examiner recommends that upon the adoption of updated Rules and Regulations by the Police Pension Fund, the Fund incorporate all changes that have been instituted since 1940. This is a repeat recommendation from the prior report on examination.	11
D	The examiner recommends that the Fund facilitate the Department in obtaining proper confirmations from its custodian.	11

APPOINTMENT NO. 21625

STATE OF NEW YORK
INSURANCE DEPARTMENT

I, NEIL D. LEVIN, Superintendent of Insurance of the State of New York,
pursuant to the provisions of the Insurance Law, do hereby appoint:

EUGENE THUMMEL

as a proper person to examine into the affairs of the
POLICE SUPERIOR OFFICERS' VARIABLE SUPPLEMENTS FUND
and to make a report to me in writing of the condition of the said
FUND

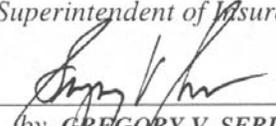
with such other information as he shall deem requisite.

In Witness Whereof, I have hereunto subscribed by name
and affixed the official Seal of the Department
at the City of New York

this 4th day of October, 2000



NEIL D. LEVIN
Superintendent of Insurance


by GREGORY V. SERIO
First Deputy Superintendent