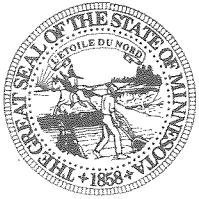


**TEACHERS RETIREMENT ASSOCIATION
FINANCIAL AND COMPLIANCE AUDIT
FOR THE YEAR ENDED JUNE 30, 1988**

MARCH 1989



STATE OF MINNESOTA

OFFICE OF THE LEGISLATIVE AUDITOR

VETERANS SERVICE BUILDING, ST. PAUL, MN 55155 • 612/296-4708

JAMES R. NOBLES, LEGISLATIVE AUDITOR

Senator Randolph W. Peterson, Vice-Chairman
Legislative Audit Commission

Members of the Legislative Audit Commission

and

Mr. Elton Erdahl, Executive Director
Teachers Retirement Association

Audit Scope

We have completed a financial and compliance audit of the Teachers Retirement Association for the year ended June 30, 1988. Our audit was made in accordance with generally accepted auditing standards and the standards for financial and compliance audits contained in the U.S. General Accounting Office Government Auditing Standards, and accordingly, included such audit procedures as we considered necessary in the circumstances. Our audit field work was completed on December 2, 1988.

The objectives of the audit were to:

- express an opinion on the financial statements of the Teachers Retirement Association (TRA) including the College Supplemental Retirement Fund for the year ended June 30, 1988;
- study and evaluate major TRA internal control systems, including a review of annuity payments and other withdrawals, receipts, contributions, payroll, and administrative disbursements; and
- verify that financial transactions were made in accordance with applicable laws, regulations, and policies, including Minnesota Statute Chapters 354 and 356, and other finance-related laws and regulations.

Management Responsibilities

The management of TRA is responsible for establishing and maintaining a system of internal control. In fulfilling this responsibility, estimates and judgments by management are required to assess the expected benefits and related costs of control procedures. The objectives of a system are to provide management with reasonable, but not absolute, assurance that assets are safeguarded against loss from unauthorized use or disposition, and that transactions are executed in accordance with management's authorization and recorded properly.

Senator Randolph W. Peterson, Vice-Chairman
Members of the Legislative Audit Commission
Mr. Elton Erdahl, Executive Director
Teachers Retirement Association
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Because of inherent limitations in any system of internal accounting control, errors or irregularities may occur and not be detected. Also, projection of any evaluation of the system to future periods is subject to the risk that procedures may become inadequate because of changes in conditions, or that the degree of compliance with the procedures may deteriorate.

The management of TRA is also responsible for the agency's compliance with laws and regulations. In connection with our audit, we selected and tested transactions and records from the programs administered by TRA. The purpose of our testing of transactions was to obtain reasonable assurance that TRA had, in all material respects, administered their programs in compliance with applicable laws and regulations.

Conclusions

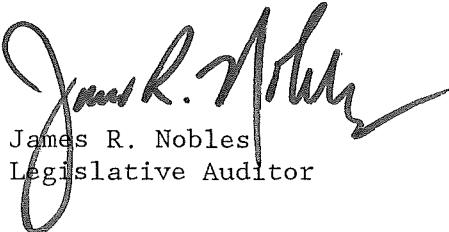
We have issued an unqualified opinion on the TRA financial statements for the year ended June 30, 1988. Our audit opinion, dated December 2, 1988, is included within the 1988 TRA Comprehensive Annual Report.

In our opinion, except for the issues raised in Section II, finding 2, the TRA's system of internal accounting control in effect on June 30, 1988, taken as a whole, was sufficient to provide management with reasonable, but not absolute assurance that assets are safeguarded against loss from unauthorized use or disposition, and that transactions are executed in accordance with management's authorization and recorded properly.

In our opinion, except for the issues raised in Section II, finding 1, for the year ended June 30, 1988, TRA administered its programs in compliance, in all material respects, with applicable finance-related and regulations.

The recommendations included in this audit report are presented to assist the Teachers Retirement Association in resolving the audit findings and in improving accounting procedures and controls. We will be monitoring and reviewing the association's on resolving these findings.

We would like to thank the Teachers Retirement Association staff for the cooperation extended to us during this audit.



James R. Nobles
Legislative Auditor



John Asmussen, CPA
Deputy Legislative Auditor

March 2, 1989

TEACHERS RETIREMENT ASSOCIATION

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AUDIT PARTICIPATION

The following members of the Office of the Legislative Auditor participated in this audit:

John Asmussen, CPA	Deputy Legislative Auditor
Tom Donahue	Audit Manager
Colleen Berg Skillings	Auditor-in-Charge
John Wicklund, CPA	Audit Staff

EXIT CONFERENCE

The findings and recommendations included in this report were discussed with the following staff of the Teachers Retirement Association on January 5, 1988:

Elton Erdahl	Executive Director
Gary Austin	Assistant Executive Director
John Gardner	Assistant Executive Director
Frank Merry	Accounting Director

TEACHERS RETIREMENT ASSOCIATION

I. INTRODUCTION

The Teachers Retirement Association (TRA) was established on July 1, 1931 by the Minnesota State Legislature. It is governed by a board of trustees which manages the Teachers Retirement Fund and the College Supplemental Fund in a fiduciary capacity. The board consists of eight trustees: three ex-officio trustees (the commissioners of Education, Finance, and Commerce); four members elected by the members of the fund; and a retiree elected by the retirees of the fund. The board elects an executive director to serve at its pleasure and to manage the association.

All teachers employed in Minnesota's public elementary and secondary schools, state universities, community colleges and all other educational institutions maintained by the state (except those teachers employed by the cities of Minneapolis, St. Paul, and Duluth and by the University of Minnesota) are required to be TRA members.

Pension costs of the Teachers Retirement Fund are funded from member and employer contributions collected by TRA. Each coordinated or basic member contributes 4.5 percent or 8.5 percent of their salary, respectively. Basic members are not covered by social security. All new members of the fund are automatically considered coordinated members and are covered by social security. Employers, in addition to matching their employee's contribution, must pay 4.48 percent of the members salary for the purpose of amortizing the unfunded liability of the fund. During fiscal year ended June 30, 1988, TRA revenues from member and employer contributions was approximately \$222.6 million. Annuity benefit payments for the same time period were approximately \$148.1 million.

The College Supplemental Retirement Fund was established in 1967 to cover unclassified employees of the State University Board and the Community College Board. Members of the fund contribute 5 percent of their wages between \$6,000 and \$15,000 to a maximum annual contribution of \$450. The employer matches the members contribution to the fund. Total contributions and contribution refunds for fiscal year 1988 were \$2.75 million and \$2.31 million, respectively.

TEACHERS RETIREMENT ASSOCIATION

II. CURRENT FINDINGS AND RECOMMENDATIONS

1. The Teachers Retirement Association (TRA) has not complied with the financial reporting requirements specified in Minn. Stat. Section 356.20.

Minn. Stat. Section 356.20, Subd. 1 provides that TRA shall annually prepare and file a financial report following the close of each fiscal year. Subdivision 3 further provides that "a signed copy of the report shall be delivered to the executive director of the legislative commission on pensions and retirement . . . not later than six months after the close of each fiscal year or one month following the completion and delivery to the retirement fund of the actuarial valuation report . . . whichever is later."

TRA's fifty-sixth annual report for fiscal year ended June 30, 1987 was issued in August 1988, almost eight months after the actuarial valuation report was received. A copy of the annual report was not filed with either the executive director of the legislative commission on pensions and retirements or the legislative reference library.

TRA staff attributed the delay to developing the investment section of the report. In future reports, this section will no longer be developed. Instead, a reference to the State Board of Investment will be made for those readers wanting a listing of TRA investments.

RECOMMENDATION

- TRA should issue its annual financial report within six months after the fiscal year end or one month after receiving its actuarial valuation report, whichever is later.

2. TRA is not following specific procedures enumerated within the bargaining unit contract concerning management overtime.

Generally, managers and supervisors are not compensated for overtime. Bargaining agreements recognize that managers and supervisors, because of the nature of their duties, may work in excess of the normal work day and/or payroll period. Such agreements generally provide the manager or supervisor with the flexibility to adjust their work schedule in subsequent days or payroll periods. The agreements however do not provide for overtime payment or guarantee hour-for-hour time off for extra hours worked.

According to the agreement, managers may be compensated for overtime hours worked if they have been assigned to a special project that is in addition to their normal duties or workload and the manager receives advance approval from the appointing authority. The appointing authority also

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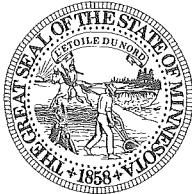
decides if overtime is to be paid in cash or time off. The agreement provides overtime may be accrued as compensatory time off to a maximum of 40 hours.

TRA made overtime payments and accrued compensatory time off for two EDP managers during fiscal years 1987 and 1988. No evidence indicated that the two managers were working on special projects or had received prior approval of the appointing authority. One manager recorded 496 hours of overtime in fiscal year 1987 and 122 hours in fiscal year 1988. Of the 496 hours, 447 hours were paid in cash totaling \$9,525. The remaining hours, as well as the overtime hours worked in fiscal year 1988, were taken as compensatory time off. Another supervisor recorded 62 hours and 401 hours of overtime for fiscal years 1987 and 1988, respectively. Seven hours of overtime in 1987 and 290 hours in 1988, totaling \$5,808 was paid in cash with the remaining hours taken as compensatory time off.

TRA indicated that two major projects required considerable development time and effort during this period. The projects were performed at the direct request of the executive director but were not formalized in writing before the work started. It is TRA's firm conviction that these projects would have qualified as special projects under the terms and definitions of the bargaining agreement had they been properly documented and approved in writing in advance.

RECOMMENDATION

- TRA should not recognize manager hours worked in excess of a normal work day as overtime unless a special project has been assigned and approved in advance by the appointing authority. If a special project is assigned to a manager, TRA should follow the provisions for overtime as specified in the appropriate bargaining agreement.



STATE OF MINNESOTA
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March 2, 1989

Mr. James Nobles, Legislative Auditor
Office of the Legislative Auditor
Veterans Service Building
St. Paul, MN 55155

Dear Mr. Nobles:

This is in reference to the draft of your management letter for the audit of the Teachers Retirement Association for the fiscal year ended June 30, 1988.

In response to the first finding and recommendation, we wish to state that your finding is correct and that we did encounter unusual delays in the preparation of our June 30, 1987 annual report. We are handling our investment reporting in a simpler format for the current report and although we are making some new improvements to other sections of the report we expect to have it issued no later than March 24, 1989. Mr. Gary Austin, Assistant Executive Director for Finance and Systems, is responsible for the preparation of this report.

As far as providing annual report information to our individual members is concerned, it should be noted that a two page comprehensive Synopsis of the Annual Report for June 30, 1987 was included in our February, 1988 Newsletter which was mailed directly to the home address of each of our approximately 61,000 active members. The same procedure has been followed for our June 30, 1988 report.

In regard to the second finding and recommendation, it is important to emphasize that all overtime worked by the two EDP supervisors was performed at the direct request of the Executive Director and the Assistant Executive Director for Finance and Systems. It was obviously a misunderstanding on our part that verbal requests for the work to be performed and our signed approval of time sheets would be inadequate to authorize payment for the overtime worked. After notification of the lack of proper procedure in this regard, we have carefully studied the requirements of the employment agreements in effect and will not approve any overtime in the future that has not been properly authorized in advance.

It was not until November, 1985 that TRA acquired its first computer. Since that time, we have been building a computer staff and developing a number of new application procedures which were required to be implemented within a fixed period of time. It is our conviction that these new applications which required overtime to be worked for their

James Nobles

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March 2, 1989

timely completion could well have qualified as special projects had they been properly documented and approved in writing in advance. Two major projects in particular required a great deal of development time and effort. The first was a special project to develop and establish the computer capability needed to implement an Electronic Fund Transfer system for the direct deposit of annuitants' benefit checks and the second required a complete new computer application to implement substantial changes to the College Supplemental Retirement Plan needed as a result of new legislation enacted by the 1987 Legislature. During the past two years, we have also had several untimely personnel changes which added to the need for overtime to be worked. In recent months, we have added new members to our computer staff which should aid immeasurably as we move forward with our computer applications.

Mr. Gary Austin, Assistant Executive Director for Finance and Systems, is responsible for supervision of the EDP staff and will assure that any overtime required to be worked in the future will be properly authorized.

Except for the two findings referred to above, we are pleased that the rest of our audit was found to be satisfactory. We are also appreciative of the courtesy and professional attitude extended to us by members of your staff.

If further information is needed regarding any of these items, please let us know.

Sincerely,


Elton Erdahl
Executive Director

EE:jr