

Teachers Retirement Association

Financial Audit

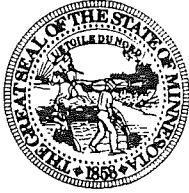
For the Fiscal Year Ended June 30, 1996

January 1997

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Financial Audit Division
Office of the Legislative Auditor
State of Minnesota

97-4



STATE OF MINNESOTA

OFFICE OF THE LEGISLATIVE AUDITOR

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Teachers Retirement Association

Mr. Gary Austin, Executive Director
Teachers Retirement Association

We have audited the financial statements of the Teachers Retirement Association (TRA) for the fiscal year ended June 30, 1996, as further explained in Chapter 1. The work conducted at TRA is part of our Statewide Audit of the state of Minnesota's financial statements for the fiscal year ended June 30, 1996. TRA's Comprehensive Annual Financial Report for the year ended June 30, 1996, includes our unqualified audit opinion, thereon dated November 20, 1996. The following Summary highlights the audit objectives and conclusions.

We conducted our audit in accordance with generally accepted auditing standards and *Government Auditing Standards*, as issued by the Comptroller General of the United States. Those standards require that we obtain an understanding of management controls relevant to the audit. The standards also require that we design the audit to provide reasonable assurance that the Teachers Retirement Association complied with provisions of laws, regulations, contracts, and grants that are significant to the audit. Management of the Teachers Retirement Association is responsible for establishing and maintaining the internal control structure and complying with applicable laws, regulations, contracts, and grants.

This report is intended for the information of the Legislative Audit Commission and the management of the Teachers Retirement Association. This restriction is not intended to limit the distribution of this report, which was released as a public document on January 17, 1997.

James R. Nobles
Legislative Auditor

John Asmussen, CPA
Deputy Legislative Auditor

End of Fieldwork: November 20, 1996

Report Signed On: January 10, 1997

SUMMARY

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Teachers Retirement Association

Financial Audit

Fiscal Year Ended June 30, 1996

Public Release Date: January 17, 1997

No. 97-4

Agency Background

The Teachers Retirement Association (TRA) is the administrator of a multi-employer, cost sharing Teachers Retirement Fund. Its function is to provide a secure and dependable source of retirement income for its members or beneficiaries as a result of retirement, disability, or death. TRA's assets as of June 30, 1996, were approximately \$9.4 billion.

Audit Objectives and Scope

The primary objective of our audit was to render an opinion on the Teachers Retirement Association's financial statements. These statements are included in both TRA's and the state of Minnesota's Comprehensive Annual Financial Reports for fiscal year 1996. This objective included whether TRA's financial statements present fairly its financial position and results of operations in conformity with generally accepted accounting principles.

As part of our work, we are required to gain an understanding of the internal control structure and ascertain whether the TRA complied with laws and regulations that may have a material effect on its financial statements. During our audit, we gained an understanding of the contributions, annuities, refunds, payroll control cycles, and the financial statement preparation cycle.

Conclusions

The TRA's Comprehensive Annual Financial Report for the year ended June 30, 1996, includes our unqualified audit opinion thereon, dated November 20, 1996. The TRA financial statements are also included in the state of Minnesota's Comprehensive Annual Financial Report for the year ended June 30, 1996, which includes our audit opinion dated December 2, 1996. TRA designed and implemented management controls for material financial activities, and for the items tested, complied with material legal provisions.

Teachers Retirement Association

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Audit Participation

The following members of the Office of the Legislative Auditor prepared this report:

John Asmussen, CPA	Deputy Legislative Auditor
Tom Donahue, CPA	Audit Manager
Sonya Hill, CPA	Auditor-in-Charge
Laura Peterson	Auditor

Exit Conference

We discussed the results of the audit at an exit conference with the following staff of the Teachers Retirement Association on January 10, 1997:

Gary Austin	Executive Director
John Wicklund	Assistant Executive Director
John Gardner	Assistant Executive Director
Judith Strobel	Assistant Executive Director

Teachers Retirement Association

Chapter 1. Introduction

The Minnesota Legislature established the Teachers Retirement Association (TRA) on July 1, 1931. TRA serves as the administrator of a multi-employer, cost sharing Teachers Retirement Fund. TRA's mission is to provide a secure and dependable source of retirement income for its members. It administers two types of plans: Basic (without Social Security coverage) and Coordinated (with Social Security coverage) in accordance with Minn. Stat. Chapters 354 and 356. An eight member board of trustees is responsible for the management of the Teachers Retirement Fund. The board appointed Gary Austin as the Executive Director of TRA to manage day to day operations.

TRA members include teachers employed in Minnesota's public elementary and secondary schools, state universities, community colleges, and all other state educational institutions, with the exception of teachers employed by the cities of Minneapolis, St. Paul, Duluth, and the University of Minnesota or any state university or college teacher who has chosen coverage under a defined contribution plan administered by the Minnesota State Colleges and Universities System (MnSCU).

TRA's assets on June 30, 1996, totaled \$9,407,071,770. Table 1-1 shows TRA's balance sheet as of June 30, 1996.

Table 1-1
Balance Sheet
June 30, 1996

<u>Assets:</u>	
Cash	\$ 1,793,407
Accounts Receivable	40,480,050
Accrued Investment Income	212,555
Investments	5,138,663,559
Equity in Post Retirement Fund	4,225,515,000
Fixed Assets	<u>407,199</u>
Total Assets	<u>\$9,407,071,770</u>
<u>Liabilities:</u>	
Accounts Payable	\$ 3,545,400
Due to the Post Retirement Fund	17,493,297
Accrued Compensated Absences	<u>286,784</u>
Total Liabilities	<u>\$ 21,325,481</u>
Net Assets	<u>\$9,385,746,289</u>

Source: 1996 audited TRA Statement of Revenues, Expenses, and Changes in Fund Balance.

Teachers Retirement Association

During our audit, we gained an understanding of the cash and investments, contributions, benefits, refunds, investment income, and payroll control cycles. The State Board of Investment performs a significant portion of the controls over TRA investments. We reviewed the controls over state investments as part of our annual audit of the State Board of Investment.

The primary objective of our audit was to render an opinion on TRA's financial statements. These statements are included in both TRA's and the state of Minnesota's Comprehensive Annual Financial Reports for fiscal year 1996. This objective included whether TRA's financial statements present fairly its financial position and results of operations in conformity with generally accepted accounting principles. As part of our work, we are required to gain an understanding of the internal control structure and ascertain whether TRA complied with laws and regulations that may have a material effect on its financial statements.

To address our audit objectives, we interviewed key TRA employees, reviewed applicable policies and procedures, reviewed TRA's preparation of the financial statements through its general ledger, tested representative samples of financial transactions, and performed analytical procedures, as appropriate. We relied on the annual actuarial valuation performed by the Legislative Commission on Pension and Retirement's actuary. The purpose of the actuarial valuation is to determine the financial status of TRA's defined benefit plan. As of June 30, 1996, TRA's actuarial liability was \$10,366,168,000. With net assets of \$9,385,746,289, TRA is approximately 90.5 percent funded.

The TRA's Comprehensive Annual Financial Report for the year ended June 30, 1996, includes our unqualified audit opinion thereon, dated November 20, 1996. The TRA financial statements are also included in the state of Minnesota's Comprehensive Annual Financial Report for the year ended June 30, 1996, which includes our audit opinion dated December 2, 1996.

Chapter 2. Contributions

Chapter Conclusions

TRA fairly presented contribution revenue on its fiscal year 1996 financial statements. TRA designed and implemented management controls to provide reasonable assurance that contributions were adequately safeguarded, and that transactions were properly recorded in the accounting records and financial statements. TRA complied with material financial legal provisions for contributions tested.

Local school district teachers and other TRA eligible members pay a percentage of their annual salary into the Teachers Retirement Fund. Employers also pay a percentage of their employees' salaries into the fund as well. These contributions are used to pay benefits to members upon their retirement. Minn. Stat. Section 354.42 specifies the employee and employer contribution rates to be used for basic and coordinated members as a percentage of salaries paid. Basic members, those without Social Security coverage, contribute 10.5 percent of their annual salary to the fund. Coordinated members, those with Social Security coverage, contribute 6.5 percent of their annual salary to the fund. Contributions from members totaled approximately \$148 million during fiscal year 1996.

The employers of TRA eligible members contribute 8.5 percent of total salaries for basic members and 4.5 percent of total salaries for coordinated members. In addition, Minn. Stat. Section 354.43, subdivision 5, requires an additional employer contribution of 3.64 percent of the member's salary. The purpose of this additional contribution is to amortize the unfunded liability of the fund and to meet the full funding date of June 30, 2020.

Audit Objectives and Methodology

We focused on the following objectives during our review of contributions:

- Did TRA fairly present employee and employer contributions on its fiscal year 1996 financial statements?
- Did TRA design and implement management controls to provide reasonable assurance that contributions were adequately safeguarded, and that transactions were authorized and properly recorded in the accounting records and financial statements? Our objective in reviewing management controls over contributions was not to provide an opinion on the effectiveness of the controls.
- Did TRA comply with material financial legal provisions in administering contributions?

The methodology used to audit contributions included interviewing TRA staff, observing the processing and recording of incoming contributions, reviewing Minn. Stat. Sections 354.42 and 354.43, and performing detailed tests of employer and employee transactions.

Teachers Retirement Association

Conclusions

TRA fairly presented contribution revenue on its fiscal year 1996 financial statements. TRA designed and implemented management controls to provide reasonable assurance that contributions were adequately safeguarded, and that transactions were properly recorded in the accounting records and financial statements. TRA complied with material financial legal provisions for contributions tested.

Chapter 3. Annuities

Chapter Conclusions

TRA fairly presented annuity benefits on its fiscal year 1996 financial statements. TRA designed and implemented management controls to provide reasonable assurance that assets for annuity benefits were adequately safeguarded, and that annuity payments were authorized and properly recorded in the accounting records and financial statements. TRA also complied with applicable legal requirements in calculating annuity benefits for the items tested.

TRA's largest expense is annuity benefits as noted on Table 1-1. During fiscal year 1996, TRA paid over \$378 million in benefits. Annuities comprised 96 percent of all TRA expenses. Minn. Stat. Chapter 354 identifies three primary factors that determines a members benefit: the member's age, the average of the member's highest five successive annual salaries, and an accumulated percentage factor based on the members total years of service credit. Members choose from six different retirement plans. Each plan offers different payment options to members and their beneficiaries.

Annuitants receive an annual increase in their benefits based on the Consumer Price Index and the activities of the Minnesota Post Retirement Investment Fund. On January 1, 1996, TRA annuitants with an effective retirement date prior to July 1, 1994, received a 6.395 percent cost of living adjustment. Members retiring after July 1, 1994, but before June 2, 1995, received a prorated adjustment.

Audit Objectives and Methodology

We focused on the following objectives during our review of annuities:

- Did TRA fairly present annuity benefits on its fiscal year 1996 financial statements?
- Did TRA design and implement management controls over annuity payments that provided reasonable assurance that assets for annuity benefits were adequately safeguarded, and that annuity payments were authorized and properly recorded in the accounting records and financial statements? Our objective in reviewing management controls over annuity payments was not to provide an opinion on the effectiveness of the controls.
- Did TRA calculate and disburse annuity benefits in accordance with applicable laws and regulations?

To answer these questions, we interviewed TRA employees to gain an understanding of the annuity process, recalculated benefits based on applicable statutes, reviewed member files and actuarial tables, and analyzed the increases and prorated cost of living increases paid to annuitants.

Teachers Retirement Association

Conclusions

TRA fairly presented annuity benefits on its fiscal year 1996 financial statements. TRA designed and implemented management controls to provide reasonable assurance that assets for annuity benefits were adequately safeguarded, and that annuity payments were authorized and properly recorded in the accounting records and financial statements. TRA also complied with applicable legal requirements in calculating annuity benefits for the items tested.

Chapter 4. Refunds

Chapter Conclusions

TRA fairly presented refunds on its financial statements. TRA designed and placed in operation management controls to provide reasonable assurance that assets for refund payments were adequately safeguarded, and that refund transactions were authorized and properly recorded in the accounting records and financial statements. TRA also complied with applicable legal requirements in calculating member refunds for those transactions tested.

TRA members who stop teaching have the option of taking a refund of their contributions upon submitting an application to TRA. The application for a refund may be submitted anytime after 30 days from the termination of service. TRA pays interest on the member's accumulated contributions at the rate of 5 percent compounded annually if the person terminated service before May 16, 1989. If the person terminated service on or after May 16, 1989, the accumulated contributions receive interest at 6 percent compounded annually. TRA issued approximately \$5 million in refunds during fiscal year 1996.

There are two types of refund calculations. If the refund is one due to a death, interest is paid to the date of death. For a regular refund, interest is computed on fiscal year end balances to the first day of the month that the refund is issued. The member has several refund options. For example, the member can request that the entire amount be directly rolled over or transferred to a specific institution, or sent directly to the individual less any applicable taxes, or a combination of the two.

Audit Objectives and Methodology

We focused on the following objectives during our review of refunds:

- Did TRA fairly present refunds on its fiscal year 1996 financial statements?
- Did TRA design and implement management controls to provide reasonable assurance that assets to pay refunds were adequately safeguarded, and that refund transactions were authorized and properly recorded in the accounting records and financial statements?
Our objective in reviewing management controls over refunds was not to provide an opinion on the effectiveness of the controls.
- Did TRA pay refunds in accordance with applicable legal requirements?

The methodology used to audit refunds included interviewing TRA staff regarding their processing and recording of member refunds. We also performed detailed tests of refund transactions.

Teachers Retirement Association

Conclusions

TRA fairly presented refunds on its financial statements. TRA designed and placed in operation management controls to provide reasonable assurance that assets for refund payments were adequately safeguarded, and that refund transactions were authorized and properly recorded in the accounting records and financial statements. TRA also complied with applicable legal requirements in calculating member refunds for those transactions tested.

Chapter 5. Payroll

Chapter Conclusions

TRA's control structure over payroll during the audit period was adequate to prevent or detect material errors or irregularities. TRA time sheets were adequately documented and approved, including the proper accrual and recording of leave accruals. In addition, TRA paid its staff using the appropriate pay rates.

The Teachers Retirement Association's largest administrative expenditure during fiscal year 1996 was payroll. TRA's payroll expenditures totaled approximately \$2 million during fiscal year 1996. TRA has 55 employees and consists of three divisions: legal services, member records and retirement services, and accounting and information services. Each division is under the direction of an assistant executive director.

TRA accounted for payroll on the state payroll personnel system (PPS) until December 1995. At that time, TRA began accounting for its payroll on the new Statewide Employee Management System (SEMA4).

Audit Objectives and Methodology

We focused on the following objectives during our review of payroll:

- Was TRA's control structure over payroll during the audit period adequate to prevent or detect material errors or irregularities?
- Were TRA employee time sheets adequately documented and approved, including the use of employee leave balances?
- Did TRA use the appropriate pay rates in calculating payments to staff?

The methodology we used to audit payroll included making inquiries of TRA staff to gain an understanding of TRA's payroll process. We reviewed the bargaining agreements affecting TRA. We performed analytical reviews of payroll disbursements and tested payroll transactions through to SEMA4, the states new payroll/personnel system.

Conclusions

Based on our review of payroll, we concluded that TRA's control structure over payroll during the audit period was adequate to prevent or detect material errors or irregularities. TRA's employee time sheets were adequately documented and approved, including the proper accrual and recording of leave accruals. In addition, TRA paid its staff using the appropriate pay rates.