Public Employees Retirement Association Financial Audit

For the Fiscal Year Ended June 30, 1998

January 1999

Financial Audit Division
Office of the Legislative Auditor
State of Minnesota

99-2

Centennial Office Building, Saint Paul, MN 55155 ● 651/296-4708

SUMMARY

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Public Employees Retirement Association

Financial Audit
For the Fiscal Year Ended June 30, 1998

Public Release Date: January 15, 1999 No. 99-2

Agency Background

The Public Employees Retirement Association (PERA) administers pension funds that serve approximately 220,000 county, school, and local public employees, their survivors and dependents. Approximately 2,000 separate Minnesota government units participate in the retirement funds administered by PERA. These units include counties, cities, townships, and school districts.

The association administers three defined benefit funds. These funds provide retirement annuities and survivor and disability benefits to members. PERA also administers a defined contribution plan. The PERA Board of Trustees is responsible for administering these funds in accordance with state statutes. The board has a fiduciary obligation to PERA's members, the employers, and to the state. PERA assets at June 30, 1998, totaled approximately $13.3 billion for all of its retirement plans.

Audit Objectives and Scope

The primary objective of our audit was to render an opinion on PERA's financial statements. These financial statements are included in both PERA's and in the state of Minnesota's Comprehensive Annual Financial Report for fiscal year 1998. Our objective included determining whether PERA's financial statements presented fairly its financial position and results of operations in conformity with generally accepted accounting principles.

As part of our work, we gained an understanding of the internal control structure and ascertained whether PERA 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, Police and Fire Consolidation Fund mergers, and the financial statement preparation cycles.

Conclusions

PERA's Comprehensive Annual Financial Report for the year ended June 30, 1998, includes our qualified audit opinion dated December 1, 1998. PERA’s financial statements were fairly presented; however, we qualified our report because sufficient audit evidence did not exist to verify PERA’s disclosures with respect to the year 2000. We do not provide assurance that PERA is or will be year 2000 ready, that its year 2000 remediation efforts will be successful in whole or in part, or that parties with which PERA does business will be year 2000 ready. PERA designed internal controls to provide reasonable assurance that it properly administered its material financial activities, except that management needs to ensure that contributions to the Defined Contribution Plan are made in accordance with statutory specifications. PERA complied with material financial legal provisions for the items tested, except for the contributions to the Defined Contribution Plan.

Public Employees Retirement Association

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Audit Participation

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

Claudia Gudvangen, CPA	Deputy Legislative Auditor
Jim Riebe, CPA	Audit Manager
Sonya Johnson, CPA	Auditor-in-Charge
Lori Kloos, CPA	Auditor
Jason Stauffenecker	Auditor
Mike Willis	Auditor

Exit Conference

We discussed the results of the audit at an exit conference with the following PERA staff on January 5, 1999:

Mary Most Vanek	Executive Director
Dave DeJonge	Manager of Finance
Gary Hovland	Senior Accounting Supervisor

Senator Deanna Wiener, Chair
Legislative Audit Commission

Members of the Legislative Audit Commission

Members of the Public Employees Retirement Association

Mary Most Vanek, Executive Director
Public Employees Retirement Association

We have audited the financial statements of the Public Employees Retirement Association (PERA) as of and for the fiscal year ended June 30, 1998, as further explained in Chapter 1. The work conducted in the department was part of our Statewide Audit of the State of Minnesota's fiscal year 1998 financial statements. We qualified our audit opinion, dated December 1, 1998, on PERA's Comprehensive Annual Financial Report for the year ended June 30, 1998. The financial statements were fairly presented. Our report was qualified, however, because of uncertainties about the potentially adverse affect the year 2000 computer issue may have on PERA's operations. Information technology experts believe that many computer applications in private businesses and government may fail as a result of data integrity problems and erroneous calculations beyond December 31, 1999. Sufficient audit evidence did not exist to verify PERA's disclosures with respect to the year 2000 issue. Because of the unprecedented nature of the year 2000 issue, its effects and the success of related remediation efforts will not be fully determinable until the year 2000 and thereafter. The following Summary highlights the audit objectives and conclusions. We discuss these issues more fully in the individual chapters of this report.

We conducted our audit in accordance with generally accepted auditing standards and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we obtain an understanding of internal controls over financial reporting to plan the audit and to determine the nature, timing, and extent of audit tests to be performed. The standards also require that we design the audit to provide reasonable assurance of detecting noncompliance with provisions of laws, regulations, contracts, and grants that have a direct and material effect on the financial statements. The management of PERA is responsible for establishing and maintaining the internal control structure and complying with applicable laws, regulations, contracts, and grants.

As part of obtaining reasonable assurance about whether PERA's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grants, noncompliance with which could have a direct and material effect on the determinations of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance that are required to be reported under *Government Auditing Standards*

In planning and performing our audit, we considered PERA's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control over financial reporting. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be material weaknesses. A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce, to a relatively low level, the risk that misstatements in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over financial reporting and its operation that we consider to be material weaknesses. However, we noted another matter involving internal control over contributions that is presented in Chapter 2.

This report is intended for the information of the Legislative Audit Commission and the management of SBI. However, this report, which was released as a public document on January 15, 1998, is a matter of public record, and its distribution is not limited.

James R. Nobles	Claudia J. Gudvangen, CPA
Legislative Auditor	Deputy Legislative Auditor

End of Fieldwork: December 1, 1998

Report Signed On: January 12, 1999

Chapter 1. Background

The Public Employees Retirement Association (PERA) administers pension funds that serve approximately 220,000 county, school, and local public employees, their survivors and dependents. More than 2,000 separate Minnesota government units participate in the retirement funds administered by PERA. These units include counties, cities, townships, and school districts.

The association administers the following defined benefit funds. These funds provide retirement annuities and survivor and disability benefits to members.

Basic Plan — Participants in this plan are public employees hired prior to January 1, 1968, who did not elect to be covered by social security benefits. This plan is closed to new members.

Coordinated Plan — Members in this plan include public employees other than police officers and firefighters. Coordinated members are covered by social security benefits.

Police and Fire Fund: Originally established for police officers and firefighters not covered by a local relief association, the fund now covers all police officers and firefighters hired since 1980.

Police and Fire Consolidated Fund — Legislation passed in 1987 allows local police and salaried firefighters' relief associations to consolidate retirement programs with PERA. The law requires the local relief associations to transfer all assets to PERA as of the effective date of each merger. Two mergers took place during the fiscal year ending June 30, 1998. As of June 30, 1998, 43 local relief associations had consolidated with PERA.

PERA also administers a defined contribution plan. This plan is a tax-deferred retirement savings program for elected public officials and public ambulance service personnel.

Agency Management

The PERA Board of Trustees is responsible for administering the retirement funds in accordance with state statutes. The board has a fiduciary obligation to PERA's members, the employers, and to the state. The board consists of ten members and the State Auditor. The Governor appoints five of the members who serve four-year terms. These members represent cities, counties, school boards, retired annuitants, and the general public. The PERA active membership elects the remaining five trustees. One of these trustees must be a member of the Police and Fire Fund, and one member must be a former member of PERA or a member who receives a disability benefit.

Public Employees Retirement System

The board appoints the executive director of PERA. Mary Most Vanek has been the executive director since January 1997. With the approval of the board, the director develops the annual administrative budget, determines staffing requirements, contracts for actuarial and other services, and directs the day-to-day operations of the association. The executive director also is a member of the State Investment Advisory Council. The council advises the State Board of Investment on the management and investment of pension funds and other assets.

Financial Information

During the year ended June 30, 1998, PERA reclassified the Public Employees Defined Contribution Plan (PEDCP) from an agency fund to a pension trust fund. This resulted in PERA presenting a Statement of Changes in Plan Net Assets in fiscal year 1998.

For the three defined benefit pension funds administered by PERA, as well as the defined contribution plan, Table 1-1 shows plan net assets at June 30, 1998, and Table 1-2 shows the changes in plan net assets during fiscal year 1998.

Table 1-1
Statement of Plan Net Assets (in thousands)
as of June 30, 1998

	Public Employees Retirement Fund	Police and Fire Fund	Police and Fire Consolidation Fund	Defined Contribution Plan
Assets:				
Cash	$ 656	$ 206	$ 12	$ 3
Accounts Receivable	1,221	139	4,697	0
Investments	4,109,953	1,939,636	478,880	12,276
Equity in Minnesota Post Retirement Investment Fund	5,239,332	778,461	764,431	
Securities Lending Collateral	916,571	258,807	122,448	1,115
Fixed Assets (Net)	537	0	0	0
Total Assets	$10,268,270	$2,977,249	$1,370,468	$,13,394
Total Liabilities	$ 933,303	$ 262,952	$ 129,070	$ 1,172
Net Assets Held in Trust	$ 9,334,967	$2,714,297	$1,241,398	$ 12,222

Note: Assets are reported at fair value.

Source: Condensed information from PERA's Comprehensive Annual Financial Report for the year ended June 30, 1998.

Table 1-2
Statement of Changes in Plan Net Assets (in thousands)
for the Year Ended June 30, 1998

	Public Employees Retirement Fund	Police and Fire Fund	Police and Fire Consolidation Fund	Defined Contribution Plan
Additions:				
Member Contribution	$ 140,386	$ 28,552	$ 3,733	$ 691
Employer Contribution	151,499	42,786	13,229	812
Net Investment Income	1,578,237	490,584	230,268	2045
Net Income from Securities Lending Activity	3,313	941	442	3
Other Additions	1,382	193	24,222	0
Total Additions	$1,874,817	$ 563,056	$ 271,894	$ 3,551
Deductions:				
Benefits Paid	$ 412,745	$ 56,034	$ 61,106	$ 0
Refunds of Contributions	16,922	1,182	296	520
Other	8,377	654	626	57
Total Operating Expenses	$ 438,044	$ 57,870	$ 62,028	$ 577
Net Increase	$1,436,773	$ 505,186	$ 209,866	$ 2,974
Net Assets Held in Trust, July 1, 1997	7,898,194	2,209,111	1,031,532	0
Adjustment for classification change	0	0	0	9,248
Net Assets Held in Trust, June 30, 1998	$9,334,967	$2,714,297	$1,241,398	$12,222

Source: Condensed information from PERA's Comprehensive Annual Financial Report for the year ended June 30, 1998.

Table 1-3 below highlights the funding ratios of the three defined benefit funds at June 30, 1998, as reported by the consulting actuary for the Legislative Commission on Pensions and Retirement. The purpose of an actuarial valuation is to test how the retirement system is achieving its fundamental financing objectives and to determine the actuarial status of PERA's defined benefit funds.

Table 1-3
Defined Benefit Funds
Funding Ratios
June 30, 1998

Retirement Fund Name	Funding Date	Funding Ratio
Public Employees	2020	87.08%
Police and Fire	2020	134.22%
Police and Fire Consolidated	2010	104.13%

Source: Condensed information from the actuarial section of PERA's Comprehensive Annual Financial Report for the year ended June 30, 1998. This funding ratio, based on the entry age normal actuarial cost method, is the ratio of assets to actuarial accrued liabilities. According to statute, assets for this computation are valued at cost plus one-third of the difference between cost and market values.

Audit Scope, Objectives, and Conclusions

The primary objective of our audit was to render an opinion on PERA's financial statements. Our objective included determining whether PERA's financial statements presented fairly its financial position and results of operations in conformity with generally accepted accounting principles. As part of our work we gained an understanding of the internal control structure and ascertained whether PERA complied with laws and regulations that have a material effect on its financial statements.

Our audit focused on contributions, annuities, defined contribution plan refunds, and Police and Fire Consolidation Fund mergers. We also reviewed investments and investment activity as reported on the financial statements. The State Board of Investment (SBI) performs a significant portion of the controls over PERA investments. We review the controls over state investments as part of our annual audit of SBI.

To address our audit objectives, we interviewed key department employees, reviewed applicable policies and procedures, and reviewed PERA's process for preparing its financial statements. We tested representative samples of financial transactions and performed analytical procedures as we considered appropriate. We also relied on the annual actuarial valuation performed by the Legislative Commission on Pension and Retirement's actuary.

PERA's Comprehensive Annual Financial Report for the year ended June 30, 1998, includes our qualified audit opinion dated December 1, 1998. PERA’s financial statements were fairly presented; however, we qualified our report because sufficient audit evidence did not exist to verify PERA’s disclosures with respect to the year 2000 computer issue. PERA’s financial statements are also included in the State of Minnesota's Comprehensive Annual Financial Report for the year ended June 30, 1998, which includes our audit opinion dated December 1, 1998.

Chapter 2. Contributions

Chapter Conclusions

PERA's financial statements fairly presented employee and employer contributions. Generally, PERA designed internal controls to provide reasonable assurance that contributions were adequately safeguarded and that transactions were authorized and properly reported in the accounting records and financial statements, except that PERA did not design controls to ensure that members of the Defined Contribution Plan contributed at the required statutory rate. Except for Defined Contribution Plan contributions that were not made at the required statutory rate, PERA complied with material financial legal provisions for contributions tested.

PERA collects and processes contributions from participating counties, cities, townships, school districts, and other public agencies. Employee and employer contribution rates are set in statute. Employers also make additional contributions to cover unfunded liabilities. Similarly, Minn. Stat. Section 353A.09, Subd. 5(b), requires cities whose relief associations have consolidated with PERA to make an additional municipal contribution to amortize the unfunded liability of the relief association at the time of consolidation. During fiscal year 1998 the contribution rates increased for the Public Employees Retirement Fund. Table 2-1 shows contribution rates.

Table 2-1Retirement Plan Contribution Rates
Fiscal Year 1998

	Employee Contributions		**Employer Contributions**		**Additional Employer Contributions**	
	7/1/97-12/31/97	1/1/98 – 6/30/98*	7/1/97-12/31/97	1/1/98 – 6/30/98*	7/1/97-12/31/97	1/1/98 – 6/30/98*
<u>Retirement Plan</u>						
Public Employees Retirement Fund:						
Basic Plan	8.23%	8.75%	8.23%	8.75%	2.50%	2.68%
Coordinated Plan	4.23%	4.75%	4.23%	4.75%	0.25%	0.43%
Public Employees			11.40%		0.00%	0.00%
Police and Fire Fund	7.60%	7.6%		11.40%		
Police and Fire Consolidation Fund	7.60%	7.6%	11.40%	11.40%	**(1)**	**(1)**
Defined Contribution Plan	5%	5%	5%	5%	0.00%	0.00%

* Contributions rate changes took effect the first full pay period after 1/1/98 **(1)** Additional lump sum municipal contribution as required by MS 353A.09.

Source: Minnesota Statutes 353.27, 353.65, and 353A.09.

Public Employees Retirement System

Audit Objectives and Methodology

The primary objectives of our audit were to answer the following questions:

- Were employee and employer contributions presented fairly in PERA's financial statements?

- Did PERA design and implement management controls to provide reasonable assurance that contributions were adequately safeguarded and that transactions were authorized and properly reported in the accounting records and financial statements?

- Did PERA comply with material financial legal provisions in administering contributions?

To answer these questions, we gained an understanding of the management controls over contributions by interviewing PERA staff, reviewing policies and procedures, and determining if the controls were implemented. We recalculated employee and employer contributions and additional employer contributions as specified in statute for a sample of transactions. We also performed analytical procedures on contribution amounts.

Conclusions

Contributions were fairly presented in PERA's financial statements. PERA also designed and implemented internal controls to provide reasonable assurance that contributions were adequately safeguarded. Contribution transactions were authorized and properly posted to the appropriate units and member accounts and recorded in the proper funds, except PERA did not ensure that members of the Defined Contribution Plan contributed at the required statutory rate. We discuss that issue in Finding 1. We concluded that except for employee and employer contributions to the Defined Contribution Plan, PERA complied with material financial legal provisions for the contributions tested.

1. PERA did not have adequate controls to ensure that the Defined Contribution Plan contributions were made at the specified statutory amounts.

PERA did not monitor employee and employer contributions to the Defined Contribution Plan (DCP) to ensure that the contributions were made at the amount specified in statute. Minn. Stat. Section 353D.03 Subd. 1 requires that eligible elected local government officials who participate in the public employees Defined Contribution Plan shall contribute an amount equal to five percent of their salaries. The governmental unit is required to contribute a matching amount to the plan. PERA has responsibility to administer the plan in accordance with Minn. Stat. Chapter 353 D.

During our audit of contributions to the Defined Contribution Plan, we identified 100 out of a total of 39,000 contribution transactions to the plan where participants had contributed either more or less than the required five percent of gross salary. Contribution percentages for these 100 transactions ranged from 50 percent to one percent of the gross salary as compared to the five percent statutory rate. We performed detailed tests on 22 of these 100 transactions. Of the 22 transactions tested, 20 were either above or below the required five percent of gross salary.

Public Employees Retirement System

The local unit of government had identified and corrected the other two exceptions. Including both employee and employer contributions, we projected fiscal year 1998 underpayments of approximately $400 and overpayments of about $1,200. Similar errors may have occurred in prior years. Errors in employee and employer contributions result not only in noncompliance with the statutory contribution provisions, but also impact the amount of retirement benefits the participants will receive in the future.

Recommendations

- *PERA should implement procedures to ensure that contributions to the defined contribution plan are made at the statutory amounts and to resolve instances where incorrect amounts are contributed.*

- *PERA should analyze prior years contributions that were not made at the required rate and determine if it is cost beneficial to resolve those differences.*

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Chapter 3. Annuities and Defined Contribution Refunds

Chapter Conclusions

PERA's financial statements fairly presented annuity benefit and defined contribution plan payments. PERA designed internal controls to provide reasonable assurance that annuity benefits and defined contribution plan refunds were authorized and properly reported in the accounting records and financial statements. We concluded that, for the items tested, PERA complied with applicable legal requirements in calculating annuity benefits and defined contribution plan refunds.

PERA provides retirement and disability benefits to members and survivor benefits upon the death of eligible members. Retirement benefits are based on a member's highest average salary for any five successive years of allowable service, age, and years of credit at termination. Table 1-2 shows annuities paid during fiscal year 1998. PERA also administers a defined contribution plan, which is a deferred compensation plan for specific elected local government officials, emergency medical service personnel and physicians.

A retiring member receives the higher of a step-rate benefit accrual formula or a level accrual formula. Normal retirement age for Public Employees Retirement Fund (PERF) members is age 65 if the member was employed prior to July 1, 1989. For a person who became a public employee after June 30, 1989, normal retirement age is the higher of age 65 or retirement age as defined in United State Code, Title 42, Section 416(l), as amended. If the member had reached normal retirement age, the level accrual formula increased from 2.5 percent to 2.7 percent for each year of service for basic members and increased from 1.5 percent to 1.7 percent for each year of service for coordinated members for those members who retired on or after July 1, 1997.

Public Employees Police and Fire Fund (PEPFF) members who have attained the age of 55 and received credit for not less than three years of service qualify for the normal retirement annuity upon separation from public service. Effective July 1, 1997, PEPFF members receive 3.0 percent for each year of service, an increase from 2.65 percent in prior years.

Members of the Police and Fire Consolidated Fund (PFCF) have the option to choose benefits identical to those of the PEPFF or the local relief association of which they were members at the time of consolidation. Certain benefit qualifications apply depending on the effective date of the consolidation.

Members of the various defined benefit funds may select from several different types of retirement annuities. The normal annuity is a lifetime annuity that ceases upon the death of the retiree. Another type of annuity is the joint and survivor annuity that provides payments to a designated joint annuitant upon the member’s death. For all defined benefit plans, a reduced retirement annuity is available to eligible members seeking early retirement.

At the time of retirement, actuarially determined reserves required to pay the cost of the member's annuity are transferred from the member's retirement fund to the Minnesota Post Retirement Investment Fund (MPRIF). Table 1-1 shows each retirement fund's equity in the MPRIF. Annuitants receive an annual increase in their benefits based on an inflation adjustment and the investment performance of the MPRIF. The benefit increase on January 1, 1998, was 10.09 percent, which is an increase from the January 1, 1997, benefit increase of 8.04%. Either a full or partial increase is granted depending on the member's retirement date.

In addition to the defined benefit plans, PERA administers a defined contribution plan (DCP). This plan is a tax-deferred retirement savings program for elected public officials and public ambulance service personnel. Participants determine how employee and employer contributions are to be invested through the purchase of shares in the Minnesota Supplemental Investment Fund administered by the State Board of Investment. Total contributions plus investment performance determine the ultimate benefit to the member. The benefit is paid as a lump sum upon withdrawal. As stated in Minn. Stat. Section 353D.03, elected public officials contribute five percent of their salary and their employers contribute an identical amount. Since DCP is a qualified tax-deferred program, withdrawals are subject to taxation. If funds are withdrawn before reaching age 59½, and not rolled into another qualified plan, withdrawals are subject to an additional ten percent tax surcharge. For the year ended June 30, 1998, approximately $520,000 was refunded to DCP members.

Audit Objectives and Methodology

The primary objectives of our audit of annuity benefits and defined contribution refunds were to answer the following questions:

- Were annuity benefits and defined contribution refunds fairly presented in PERA's financial statements?
- Did PERA design internal controls to provided reasonable assurance that annuity benefits and defined contribution refund transactions were authorized and properly reported in the accounting records and financial statements?
- Were annuities and defined contribution refunds paid in accordance with applicable legal requirements?

To answer these questions, we interviewed key department personnel to gain an understanding of the controls over annuity and defined contribution refund calculations. We also reviewed applicable policies, procedures, and legal provisions. In addition, we tested a representative sample of annuity payments and defined contribution refunds.

Conclusions

Annuity benefits and defined contribution refunds were fairly presented in PERA's financial statements. PERA designed internal controls to provide reasonable assurance that annuity benefit and defined contribution refund transactions were authorized and properly recorded in the appropriate employer and member accounts and funds, and in the financial statements. For the items tested, PERA complied with applicable legal requirements in calculating annuity benefits and defined contribution refunds.

Chapter 4. Police and Fire Consolidation Fund Mergers

Chapter Conclusions

PERA fairly presented Police and Fire Consolidation Fund financial activity in the financial statements. PERA also designed and implemented internal controls to provide reasonable assurance that assets were adequately safeguarded, and that merger transactions were authorized and properly recorded in the accounting records and financial statements. In addition, for the merger transactions tested, PERA complied with material financial legal provisions.

In accordance with Minn. Stat. Section 353A, local police or fire relief associations can merge with the Police and Fire Consolidated Fund administered by PERA. At the time of consolidation, the local relief association transfers all assets to the consolidation fund. These assets are recorded at market value as of the date of consolidation. Upon consolidation, PERA takes responsibility for administering the association's benefit plan, but bears no responsibility for financing it. The cities continue to retain sole responsibility for financing the benefits paid to former members of the local relief association.

Minn. Stat. Section 353A.09, Subd. 5, requires municipalities to make an additional municipal contribution to the consolidation account. The additional payments are required in order to amortize, by the year 2010, the unfunded actuarial accrued liabilities of the merged relief associations (determined at the date of consolidation). Additional employer contributions are also required to amortize subsequent actuarial losses over 15 years. Approximately $7.9 million of additional municipal contributions were made to the consolidation account in fiscal year 1998.

Prior to 1987, 50 local relief associations administered independent pension plans for their employees. From December 1987 to June 30, 1998, 43 police and fire associations had consolidated with PERA. Two consolidation mergers took place during fiscal year 1998, with assets totaling approximately $22.6 million being added to the Police and Fire Consolidation Fund.

Audit Objectives and Methodology

The primary objectives of our audit were to answer the following questions:

- Did PERA fairly present local relief association merger activities in the financial statements?

- Did PERA design internal controls to provide reasonable assurance that assets were adequately safeguarded, and that merger transactions were authorized and properly recorded in the accounting records and financial statements?

- Were actuarial calculations completed prior to the local relief association consolidations, and were the assets transferred to PERA after consolidation?

To satisfy our audit objectives, we reviewed the procedures PERA followed to complete consolidation fund mergers. We determined that actuarial calculations were done prior to the consolidation for each local relief association. We verified assets transferred to the state during the consolidation process and traced the individual and total amount of assets to the financial statements.

Conclusions

We found that PERA fairly presented Police and Fire Consolidation Fund activity in the financial statements. PERA also designed and implemented internal controls to provide reasonable assurance that assets were adequately safeguarded, and that merger transactions were authorized and properly recorded in the accounting records and financial statements. In addition, for the merger transactions tested, PERA complied with material financial legal provisions.

Status of Prior Audit Issues
As of December 9, 1998

Most Recent Audits

Legislative Audit Report 98-4, February 1998, covered the fiscal year ended June 30, 1997. The primary objective of our audit was to render an opinion on PERA's financial statements. Our objective included determining whether PERA's financial statements presented fairly its financial position, results of operations, and changes in cash flows in conformity with generally accepted accounting principles. We issued an unqualified opinion on the PERA financial statements. We did not develop any written audit findings or recommendations to report to PERA management.

State of Minnesota Audit Follow-Up Process

The Department of Finance, on behalf of the Governor, maintains a quarterly process for following up issues cited in financial audit reports issued by the Legislative Auditor. The process consists of an exchange of written correspondence that documents the status of audit findings. The follow-up process continues until Finance is satisfied that the issues have been resolved. It covers entities headed by gubernatorial appointees, including most state agencies, boards, commissions, and Minnesota state colleges and universities. It is not applied to audits of the University of Minnesota, any quasi-state organizations, such as the Metropolitan agencies or the State Agricultural Society, the state constitutional officers, or the judicial branch.

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January 7, 1999

Mr. James Nobles
Office of the Legislative Auditor
1st Floor South, Centennial Building
658 Cedar Street
St. Paul, MN 55155

Dear Mr. Nobles:

While conducting the fiscal year 1998 financial audit on the Public Employees Retirement Association, it was discovered that out of 39,000 contribution transactions in our Defined Contribution Plan, employers made mathematical errors in approximately 100 of those transactions resulting in an average of $8.00 in excess contributions for each of those 100 members. We have put the following controls in place to ensure inaccurate amounts are not contributed in the future.

We are in the process of completing a new computer system that will be used to collect and maintain all contribution transactions. We have already built a control into that system that makes sure the correct amount is contributed based on the salary provided. Any incorrect contribution amounts will be kicked out daily to an investigator who will resolve the problem with the employer. That system will be activated in July 1999.

In the meantime, we have stepped up our efforts to follow through on incorrect contribution amounts. An edit report, printed daily, lists inaccurate contribution amounts based on the given salary amounts. Our cashiers check that report and, if necessary, contact employers to fix the problems.

We have requested a file of all the contribution transactions added to the Defined Contribution Plan for the past 3 years to determine if this has been an underlying problem. The data we have examined so far lead us to believe that a vast majority of the mistakes are a result of math errors by payroll personnel. We have not detected an employer who seems to make these mistakes on a regular or consistent basis. We will continue to evaluate the data and determine if it is cost beneficial to resolve past differences.

If you have questions, please feel free to contact me at (651) 297-3573.

Sincerely,

Dave DeJonge

Dave DeJonge
Finance Manager