



STATE OF WISCONSIN

Legislative Audit Bureau

22 East Mifflin Street, Suite 500
Madison, Wisconsin 53703
(608) 266-2818
Fax (608) 267-0410

www.legis.wisconsin.gov/lab

Toll-free hotline: 1-877-FRAUD-17

Joe Chrisman
State Auditor

December 17, 2014

Senator Robert Cowles and
Representative Samantha Kerkman, Co-chairpersons
Joint Legislative Audit Committee
State Capitol
Madison, Wisconsin 53702

Dear Senator Cowles and Representative Kerkman:

We have completed our 2013 financial audit of the Department of Employee Trust Funds, as required by s. 13.94(1)(dd), Wis. Stats., and as requested by the Department. The Department's financial statements present the financial position and activity of various benefit programs available to state and local public employees, including the Wisconsin Retirement System (WRS) and health and life insurance programs for active and retired employees of the State and participating local governments. The statements, and our unmodified opinions on them, are included in the Department's 2013 Comprehensive Annual Financial Report, which can be found on its website.

The largest program administered by the Department is the WRS, which reported a net position of \$89.9 billion as of December 31, 2013, an increase of \$8.9 billion over the prior year. During 2013, the WRS provided benefits totaling \$4.2 billion, collected contributions of \$1.8 billion, and had positive investment returns of \$11.3 billion. As of December 31, 2013, the WRS was 105.3 percent funded based on the fair value of its assets and 99.9 percent funded based on standard actuarial measures, which smooth investment returns over a five-year period.

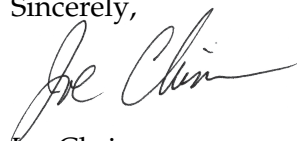
Enclosed is the Independent Auditor's Report on Internal Control over Financial Reporting and on Compliance and Other Matters, as required by *Government Auditing Standards*. As noted in that report, we identified a deficiency in internal control related to the preparation of the financial statements that we are required to report under these standards. We recommend the Department develop and implement procedures to improve the oversight of its financial reporting process.

Before our next audit, which will review the financial position and activity as of December 31, 2014, the Department will implement Governmental Accounting Standards Board (GASB) Statement Number 67 and GASB Statement Number 68. For financial reporting purposes, the Department will be required to follow the requirements of the GASB standards in calculating the total pension liability of the WRS and will be required to use fair value of investment assets in determining the net pension liability or net pension asset. Further, each WRS participating

Senator Robert Cowles and
Representative Samantha Kerkman, Co-chairpersons
Page 2
December 17, 2014

employer will be required to report its share of the net pension liability or net pension asset in its financial statements. The Department will provide information for each participating employer to calculate its proportionate share of the liability or asset.

Sincerely,



Joe Chrisman
State Auditor

JC/CS/ss

Enclosure

cc: Senator Mary Lazich
Senator Alberta Darling
Senator Kathleen Vinehout
Senator John Lehman

Representative Howard Marklein
Representative John Nygren
Representative Jon Richards
Representative Melissa Sargent

Robert Conlin, Secretary
Department of Employee Trust Funds



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Joe Chrisman
State Auditor

December 17, 2014

Mr. Robert J. Conlin, Secretary
Department of Employee Trust Funds
801 West Badger Road
Madison, Wisconsin 53707

Dear Mr. Conlin:

We have completed the financial audit of the State of Wisconsin Department of Employee Trust Funds as of and for the year ended December 31, 2013. In our opinion, the financial statements of each fiduciary fund and of each proprietary fund administered by the Department present fairly, in all material respects, its financial position as of December 31, 2013. The financial statements and related opinion are included in the Department's 2013 Comprehensive Annual Financial Report.

As required by *Government Auditing Standards*, we are furnishing you with the Independent Auditor's Report on Internal Control over Financial Reporting and on Compliance and Other Matters. The report includes a deficiency in internal control over financial reporting that we are required to report under these standards.

We appreciate the courtesy and cooperation extended to us by the Department's staff during the audit.

Sincerely,

Joe Chrisman
State Auditor

JC/CS/ss

Enclosure



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State Auditor

Independent Auditor's Report on Internal Control over Financial Reporting and on Compliance and Other Matters

Senator Robert Cowles and
Representative Samantha Kerkman, Co-Chairpersons
Joint Legislative Audit Committee

Members of the Employee Trust Funds Board and
Mr. Robert J. Conlin, Secretary
Department of Employee Trust Funds

We have audited the financial statements and related notes of each fiduciary fund and each proprietary fund, administered by the State of Wisconsin Department of Employee Trust Funds as of and for the year ended December 31, 2013, and have issued our report thereon dated December 16, 2014. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, which is issued by the Comptroller General of the United States. The financial statements and related auditor's report have been included in the Department's 2013 Comprehensive Annual Financial Report.

Internal Control over Financial Reporting

Management of the Department is responsible for establishing and maintaining effective internal control over financial reporting (internal control). In planning and performing our audit of the financial statements, we considered the Department's internal control to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Department's internal control. Accordingly, we do not express an opinion on the effectiveness of the Department's internal control.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent misstatements, or to detect and correct misstatements on a timely basis. *A material weakness* is a deficiency or a combination of deficiencies in internal control such that there is a reasonable possibility that a material misstatement of the Department's financial statements will not be prevented, or that a material misstatement will not be detected and corrected on a timely basis. *A significant deficiency* is a deficiency or a combination of deficiencies in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified. We did identify a deficiency in internal control, described in the following paragraph, that we consider to be a significant deficiency.

During the audit of the Department's 2013 financial statements, we identified an error in the financial statements for the Health Insurance, State Retiree Health Insurance, and Local Retiree Health Insurance funds that we believe should have been detected by the Department's financial reporting review process. In the Department's financial statements, activity related to administering the health insurance program is reported in these three separate funds, each covering the financial activity for a specific coverage group including active state and local employees, state retirees, and local retirees. Prior to the end of the calendar year, the Department paid \$109.0 million for January 2014 premiums to Health Maintenance Organization (HMO) providers providing health insurance coverage to state and local employees, and state and local retirees. Because the payment was made prior to the end of calendar year 2013, but related to January 2014 coverage, a prepaid expense was reported by the Department. However, the Department only reported the prepaid expense in the Health Insurance Fund and did not allocate a portion of the prepaid expense to the State Retiree Health Insurance and Local Retiree Health Insurance funds. As a result, prepaid expense was overstated by \$11.1 million in the Health Insurance Fund, understated by \$9.8 million in the State Retiree Health Insurance Fund and understated by \$1.3 million in the Local Retiree Health Insurance Fund. In addition, we identified other errors in the cash flow statement for the Health Insurance Fund related to the prepayment to the HMOs.

Although the Department corrected the errors in the financial statements, we recommend the Department develop and implement procedures to improve the oversight of its financial reporting process.

Department of Employee Trust Fund Response: The Department appreciates the diligence of the auditors in identifying an error in the financial statements for the Health Insurance, State Retiree Health Insurance, and Local Retiree Health Insurance funds. The Department sets a high standard for the accuracy of the financial statements, and acknowledges this error should have been detected. The Department will put in place appropriate procedures to ensure the proper allocation of these expenses in the future.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Department's financial statements are free from material misstatement, we performed tests of compliance with certain provisions of laws, regulations, and contracts, noncompliance with which could have a direct and material effect on the determination 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 or other matters that are required to be reported under *Government Auditing Standards*.

Department of Employee Trust Fund's Response to Findings

The Department's written response to the findings identified in our audit is described above. The Department's response was not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on it.

Purpose of This Report

This report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be used when considering the Department's internal control and compliance. The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the result of that testing, and not to provide an opinion on the effectiveness of the Department's internal control or on compliance. Accordingly, this report is not suitable for any other purpose.

LEGISLATIVE AUDIT BUREAU

A handwritten signature in black ink, appearing to read "Joe Chrisman". The signature is fluid and cursive, with a long horizontal stroke extending to the right.

Joe Chrisman
State Auditor

December 16, 2014