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Janice Mueller
State Auditor

October 20, 2006

Senator Carol Roessler and
Representative Suzanne Jeskewitz, Co-chairpersons
Joint Legislative Audit Committee
State Capitol
Madison, Wisconsin 53702

Dear Senator Roessler and Representative Jeskewitz:

We completed an annual financial audit of the Department of Employee Trust Funds in November 2005, as requested by the Department and to fulfill our audit requirements under s. 13.94(1)(dd), Wis. Stats. The audit covered the period of January 1, 2004 through December 31, 2004. The 2004 financial statements and our unqualified opinion on them are included in the Department's recently issued financial report, which provides information on the financial position and activity of various benefit programs available to public employees.

Most of the Department's programs reported positive financial results in 2004. The largest program administered by the Department is the Wisconsin Retirement System, which reported net assets of \$67.9 billion at the end 2004 and provided benefits totaling \$2.9 billion during 2004. Positive investment returns contributed to the net increase in retirement assets of \$5.8 billion. At the end of 2004, the Wisconsin Retirement System was 99.4 percent funded based on actuarial measures that compare the actuary's valuation of assets to the estimated value of the benefit obligations for services already rendered by present and future retirees.

Another major program administered by the Department is the group health insurance program for participating state and local government employees and retirees. In an effort to control increasing costs and premiums in the program, the State implemented several new program features in 2004, including a three-tier premium contribution structure for active State employees and a single pharmacy benefit manager to provide pharmacy benefits services to all plan participants. The program reported a net increase in assets during the year of \$48.9 million and a net asset balance of \$78.0 million at December 31, 2004.

The final program we highlight is the Duty Disability program, which offers special disability insurance for state and local participants in the Wisconsin Retirement System who are in protective occupations. Benefits are payable for duty-related injuries and diseases that are likely to be permanent and that cause the employees to retire, accept reduced pay or a light-duty assignment, or that impair the employee's promotional opportunities. The program is funded through contributions from employers and investment earnings. Since its initial years, the program has had an accounting deficit, which the Department has been attempting to reduce over a period of several years. Net income of \$30.1 million

Senator Carol Roessler and
Representative Suzanne Jeskewitz, Co-chairpersons
Page 2
October 20, 2006

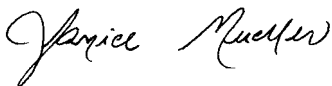
in 2004 decreased the deficit balance by 15.8 percent to \$159.6 million at December 31, 2004. The Department currently plans to eliminate the deficit by 2018.

In 2005, we reported that the Department experienced difficulties and delays in implementing a new benefit payment system and terminated contracts for the development of the new system in 2004. In February 2005, the Department contracted with a new firm for the project. The Department did not meet its initial goal of implementation in January 2006 and currently anticipates implementing the new system by early 2007.

Finally, accompanying this letter is a management letter we provided to the Department. As required by *Government Auditing Standards*, we include an auditor's report on internal control and compliance with the management letter. We identified a reportable condition under these standards related to the lack of cash reconciliations on a program level and we noted other issues related to the calculation of sick leave conversion credits and the adequacy of computer access controls for the new pharmacy benefit program.

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

Respectfully submitted,



Janice Mueller
State Auditor

JM/DA/bm

Enclosures

cc: Senator Robert Cowles
Senator Scott Fitzgerald
Senator Mark Miller
Senator Julie Lassa

Representative Samantha Kerkman
Representative Dean Kaufert
Representative David Travis
Representative David Cullen