



**STATE OF WISCONSIN**

**Legislative Audit Bureau**

22 E. Mifflin St., Ste. 500  
Madison, Wisconsin 53703  
(608) 266-2818  
Fax (608) 267-0410  
Leg.Audit.Info@legis.state.wi.us

Janice Mueller  
State Auditor

October 20, 2006

Mr. Eric Stanchfield, Secretary  
Department of Employee Trust Funds  
801 West Badger Road  
Madison, Wisconsin 53702

Dear Mr. Stanchfield:

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, 2004. We have issued an unqualified auditor's report, dated November 30, 2005, on the fair presentation of the Department's financial statements. The financial statements and related opinion are included in the Department's Comprehensive Annual Financial Report.

As required by *Government Auditing Standards*, we also are furnishing you with the auditor's report on internal control over financial reporting, compliance with laws and regulations, and other matters. We identified a reportable condition under these standards related to the lack of cash reconciliations on a program level. We also identified issues related to the calculation of accumulated sick leave credits and the adequacy of computer access controls for the new pharmacy benefit program.

The Department's responses and corrective action plans to implement recommended improvements are included in the text so that readers may see your intended resolution of the matters discussed. In future audits, the Audit Bureau will determine the extent to which the issues in this letter have been resolved.

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

Sincerely,

Janice Mueller  
State Auditor

JM/DA/bm

Enclosures





STATE OF WISCONSIN

## Legislative Audit Bureau

22 E. Mifflin St., Ste. 500  
Madison, Wisconsin 53703  
(608) 266-2818  
Fax (608) 267-0410  
Leg.Audit.Info@legis.state.wi.us

Janice Mueller  
State Auditor

### **INDEPENDENT AUDITOR'S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS**

We have audited the financial statements of the State of Wisconsin Department of Employee Trust Funds as of and for the year ended December 31, 2004, and have issued our report thereon dated November 30, 2005. 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*, issued by the Comptroller General of the United States.

#### **Internal Control over Financial Reporting**

In planning and performing our audit, we considered the Department'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 an opinion on the internal control over financial reporting. However, we noted a certain matter involving the internal control over financial reporting and its operation that we consider to be a reportable condition. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over financial reporting that, in our judgment, could adversely affect the State's ability to record, process, summarize, and report financial data consistent with the assertions of management in the financial statements. The reportable condition is the lack of cash reconciliations on a program level, which is the level on which the Department reports and on which we opine on the Department's financial information. Further discussion of this concern and the Department's response to a corresponding recommendation are included in the accompanying narrative.

A material weakness is a reportable 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 caused by error or fraud 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. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. However, we do not believe that the reportable condition described above is a material weakness.

## Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Department's financial statements are free of material misstatement, we performed tests of its 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*.

We further noted certain additional matters pertaining to the calculation of accumulated sick leave conversion credits and the adequacy of computer access controls for the new pharmacy benefit program that are discussed in the accompanying narrative.

This independent auditor's report is intended solely for the information and use of the Department's management and the Wisconsin Legislature. This independent auditor's report, upon submission to the Joint Legislative Audit Committee, is a matter of public record and its distribution is not limited. However, because we do not express an opinion on internal control over financial reporting or on compliance, this report is not intended to be used by anyone other than these specified parties.

LEGISLATIVE AUDIT BUREAU

November 30, 2005

by



Diann Allsen  
Audit Director

## **DEPARTMENT OF EMPLOYEE TRUST FUNDS**

The Department of Employee Trust Funds is responsible for administering the Wisconsin Retirement System and several other programs that provide retirement, disability, health, and other benefits to participants who are current and retired employees of state and local government employers.

As part of our annual financial audits, we review and consider the Department's internal controls for the purpose of determining the audit work necessary to express an opinion on its financial statements. During our audit of the Department's 2004 financial statements, we noted internal control issues related to cash reconciliations, accumulated sick leave conversion credits, and computer access for the new pharmacy benefit program.

### **Reconciliations of Cash**

The Department uses WiSMART, the State's accounting system, to process financial transactions and Helmsman, a financial reporting software package, to create financial statements for its programs. Section 16.41, Wis. Stats., requires all agencies to keep their accounts and other financial records in the form as prescribed by the Department of Administration (DOA) under s. 16.40, Wis. Stats. DOA implemented and established WiSMART as the State's official accounting system. As a state agency, the Department is responsible for ensuring its information on WiSMART is complete and accurate. An important step in ensuring the accuracy of the financial information on WiSMART is to reconcile it to the Department's internal financial records and systems. Further, regular reconciliations between the systems better ensures that information reported by the Department in its financial report is complete and accurate.

The Department has taken some steps to reconcile information on Helmsman to that reported on WiSMART. However, as we have communicated for several years, it has not been able to fully reconcile its cash balances. While the Department has made some attempts to reconcile cash balances at the fund level, varying amounts of unreconciled differences exist at the end of each year. Further, it has made only limited attempts to reconcile cash balances on a program level, which is the level on which it reports and on which we opine on the financial information in its annual financial report.

For the last several years we have reported the unexplained variances between the sets of records to the Department. For example, at the end of 2004, the Department reported:

- a cash balance for Fund 262, the Public Employee Trust Fund, that was \$1.0 million greater than that reported by DOA's Cash Management Operations Section, which reconciles its records to WiSMART; and
- a cash balance for Fund 747, the Core Retirement Investment Trust Fund, that was \$2.0 million greater than that reported by the Investment Board, which invests the funds in the Core Fund and reconciles its records to WiSMART.

On an overall fund level, the unreconciled amounts represent a very small percentage of the cash balances—0.9 percent for Fund 262 and 0.2 percent for Fund 747.

However, the unreconciled differences on a program level can be significantly greater. For example, the Department reported a cash balance for the Life Insurance Program that was 123.2 percent less than that reported on WiSMART. In the case of Fund 747, reconciling cash balances on a program level can be more difficult because of the volume and complexity of the cash transactions in this fund. Consequently, such reconciliations may require more detailed analyses of cash-related transactions. The Department attempted such reconciliations of the Fund 747 programs for 2001, but was unable to fully reconcile the variances. It has not attempted to repeat these reconciliations for subsequent years.

Based on our review of how the reconciliations are completed at the program level, we believe two issues are contributing to the difficulty in fully reconciling the cash balances. First, cash apparently was not properly allocated at the program level when WiSMART was first implemented in fiscal year 1993-94. To address this situation, the State Controller's Office (SCO) determined the adjustments it believed to be necessary to allocate cash balances among programs and has been using these adjustments in preparing the State's financial report for several years. The Department considered these adjustments as reconciling items when it completed the reconciliations at the program level, but it is not confident that the adjustments were for the correct amounts. Instead, it believes the balances on Helmsman are correct, but it has not taken steps to work with SCO to correct the balances on WiSMART.

Second, we believe the Department has not identified all reconciling items that need to be considered in the reconciliation process. For instance, we identified several reconciling items that the Department had not identified for the Commuter Benefits Program in its first year of operation.

While, to date, we have accepted the cash balances reported by the Department in its financial reports as materially correct, larger unreconciled variances could affect our ability to issue unqualified auditor's opinions in the future. Further, as a state agency, the Department has a responsibility to ensure the accuracy of its information on the State's official accounting system and records. Consequently, it should take steps to ensure that reliable and accurate reconciliations of the cash balances at the program level are performed and the State's official accounting system reflects the proper cash balances of its programs. While the State's official accounting system is currently WiSMART, the State is in the process of replacing it with a new system, the Integrated Business Information System. Thus, the Department should target the completion of its reconciliations by the time the new system is implemented.

**Recommendation**

*We recommend the Department of Employee Trust Funds develop a plan to fully reconcile the cash balances for each program by the time the State's new Integrated Business Information System is implemented and take steps to correct any inaccuracies identified in the beginning cash balances on the State's official accounting system or Helmsman through the reconciliation process.*

Department Response and Corrective Action Plan: Reconciliations of cash balances between the Department's internal accounting records and the actual investment balances maintained by the Investment Board and DOA's Cash Management Operations Section are an integral part of the annual financial statement preparation. These reconciliations can only be performed at the fund level, because investment balances are maintained at the fund level. As noted, these reconciliations have consistently demonstrated that the Department's cash balances are materially correct based on investment balances. While immaterial variances do exist, we believe it is best not to delay presentation of materially correct financial statements in order to resolve variances that do not affect the usefulness of the financial statements.

Historically, the Department maintained a full accounting system and prepared generally accepted accounting principles (GAAP) financial statements that were regularly audited and opined on by the Legislative Audit Bureau. With the implementation of WiSMART, SCO made an attempt to establish assets and reserves at the program level. In the case of the Department's programs, it did so without taking advantage of the audited statements and account balances that already existed. As a result, SCO created account balances in WiSMART that were inconsistent with the Department's records.

The Department agrees that it would be desirable for the State's central accounting system to have the most accurate possible balances for the Department's programs. Ultimately, it may not be possible to fully reconcile that system to the Department's given the amount of time that has passed since it was implemented and its beginning balances were established. However, it would be possible to adjust those balances for consistency with the Department's balances. If that step was taken, regular reconciliations would be possible in the future.

The Department has already contacted SCO and they have agreed to commence work on reconciliation of cash balances between the systems. The Department agrees that completing such a reconciliation prior to the implementation of a new central accounting system would be ideal.

### **Determination of Accumulated Sick Leave Conversion Credits**

The Department of Employee Trust Funds administers the Accumulated Sick Leave Conversion Credit program and the Supplemental Health Insurance Conversion Credit program. Both programs provide credits to eligible participants that may be used to pay for health insurance premiums after retirement. Eligible participants or their beneficiaries may also use these credits at the time of layoff or death.

The total credits granted through the Accumulated Sick Leave Conversion Credit program is a product of the participant's balance of sick leave hours and highest base hourly pay rate while employed with the State. The supplemental program provides additional matching credits for eligible state participants who have at least 15 years of continuous state service. The supplemental program also includes a provision allowing the restoration of up to 500 hours of sick leave upon retirement for eligible participants who used sick leave hours for a single injury or illness during the three years preceding retirement.

State agencies submit an Accumulated Leave Certification form to the Department to enroll eligible participants in both programs. This form provides the participant's base salary rate, accumulated sick leave hours, years of continuous State service, and calculation of the credits to be awarded. Agencies are responsible for ensuring the accuracy of the information on the forms.

During our past several audits, we have found errors in the calculation of sick leave credits. In a review of 20 calculations during our 2003 audit, we identified four instances in which errors were made. The errors ranged from a \$394 understatement to a \$5,787 overstatement of the credit. During our 2004 audit, we found only one error in a selection of 20 calculations. However, the error was significantly larger—an employee was granted an excess credit of \$18,206. The errors occurred because of human errors in determining the number of creditable years of service, the rate of pay, and the sick leave balance. Four of the five errors occurred for employees at the University of Wisconsin (UW) campuses.

Overall, the errors did not have a material effect on the financial statements. However, such errors could cause the Department to pay health insurance premiums in excess of credits actually earned or to prematurely cease to pay health insurance premiums for a participant with understated credits. In addition, actuarially determined contribution rates and liability amounts for the sick leave conversion and supplemental programs could ultimately be affected, depending on the size and volume of errors that actually exist.

While the Department is responsible for obtaining and processing the Accumulated Leave Certification forms as completed by the agencies, it does not have all the necessary information to ensure that the forms are correctly completed. The state agencies typically maintain the personnel files, which are the primary source for completing these forms. Further, the Office of State Employment Relations (OSER) historically has been the resource for questions regarding the completion of these forms. Therefore, the Department would likely need to work with OSER to improve the accuracy of the calculations performed by state agencies.

Additional information and reminders for these calculations could be provided in employer bulletins or at monthly payroll meetings. Training could also be provided to individual payroll staff as needed, such as for agencies that complete these calculations infrequently or have experienced changes in payroll staff. Further, the Department and OSER may want to focus informational and training efforts to the UW campuses where most of the errors noted in our testing occurred.

**Recommendation**

*We recommend the Department of Employee Trust Funds work with the Office of State Employment Relations to establish a plan for promoting the accurate completion of the Accumulated Sick Leave Certification forms.*

Department Response and Corrective Action Plan: The Department issued an Employer Bulletin in October 2004 to provide additional information to state agencies on the calculation of sick leave conversion credits. The Accumulated Sick Leave Certification form was revised to more accurately reflect the changes resulting from 2003 Wisconsin Act 33 and to facilitate accurate



calculations. The Department recently updated the State Health Insurance Manual for employers, which includes an increased emphasis on certification of program requirements and accurate calculations.

The Department is also developing a set of talking points and materials for state agency employers, which it plans to present at a state payroll council meeting in January 2007. The Department will also make this offering available to the UW central payroll office since four of the five errors cited in 2003 and 2004 occurred for employees at UW campuses. In addition, the Department has been working with the OSER contact for administration of the supplemental program to discuss the nature and volume of questions referred there from employers on calculating the value on the Accumulated Sick Leave Certification form and any follow-up necessitated by those employer questions.

### **Pharmacy Benefit Program**

Beginning January 1, 2004, pharmacy benefits were separated from all of the health insurance benefit options offered to state and local government employees and a separate pharmacy benefit program was created. Navitus Health Solutions, LLC was selected as the pharmacy benefit manager for the new program. Navitus contracts with SXC Health Solutions, Inc., which operates the system through which pharmacy claims are processed. Most claims are electronically submitted and entered into the system, although some paper claims need to be manually entered.

Access to the pharmacy claims system needs to be properly controlled to ensure that only valid claims can be entered into the system. However, during our 2004 audit, we noted a concern with the access provided to Navitus employees. Various Navitus employees require access to the pharmacy claims system in order to add eligibility information or to process the manual claims. Although Navitus has assigned different staff responsibility for these functions, staff who have access can perform both functions on the system. With such access, an employee potentially could establish a false eligible participant, process manual claims for that participant, and receive inappropriate claims payments. Navitus management noted that it was already aware of this issue and had begun considering options for appropriately limiting employee access.

\*\*\*\*