

**Report 15-12
August 2015**

Wisconsin Retirement System Reporting for Participating Employers Calendar Year 2014

STATE OF WISCONSIN



Legislative Audit Bureau ■

Wisconsin Retirement System Reporting for Participating Employers Calendar Year 2014

Joint Legislative Audit Committee Members

Senate Members:

Robert Cowles, Co-chairperson
Mary Lazich
Alberta Darling
Kathleen Vinehout
Janet Bewley

Assembly Members:

Samantha Kerkman, Co-chairperson
John Macco
John Nygren
Melissa Sargent
Terese Berceau

LEGISLATIVE AUDIT BUREAU

State Auditor

Joe Chrisman

Special Assistant

Anne Sappenfield

**Financial Audit
Director**

Carolyn Stittleburg

Supervisor

Lisa Kasel

Legislative Auditors

Jeffrey Beckett

Kevin Cords

Mark Fignar

Garrett Gardner

Jake Gasser

Kendra Glander

Josh Petersen

Mike Rateike

Amelia Slaney

Aaron Stoltenberg

Stephanie Yost

**Publications and
Design Coordinator**

Susan Skowronski

The Bureau is a nonpartisan legislative service agency responsible for conducting financial and program evaluation audits of state agencies. The Bureau's purpose is to provide assurance to the Legislature that financial transactions and management decisions are made effectively, efficiently, and in compliance with state law and that state agencies carry out the policies of the Legislature and the Governor. Audit Bureau reports typically contain reviews of financial transactions, analyses of agency performance or public policy issues, conclusions regarding the causes of problems found, and recommendations for improvement.

Reports are submitted to the Joint Legislative Audit Committee and made available to other committees of the Legislature and to the public. The Audit Committee may arrange public hearings on the issues identified in a report and may introduce legislation in response to the audit recommendations. However, the findings, conclusions, and recommendations in the report are those of the Legislative Audit Bureau.

The Bureau accepts confidential tips about fraud, waste, and mismanagement in any Wisconsin state agency or program through its hotline at 1-877-FRAUD-17.

For more information, visit www.legis.wisconsin.gov/lab

Joint Legislative Audit Committee Members

Senate Members:

Robert Cowles, Co-chairperson

Mary Lazich

Alberta Darling

Kathleen Vinehout

Janet Bewley

Assembly Members:

Samantha Kerkman, Co-chairperson

John Macco

John Nygren

Melissa Sargent

Terese Berceau



CONTENTS

Letter of Transmittal	1
Introduction	3
New Pension Standards and Employer Reporting	4
Census Data	6
Auditor's Report	9

OPINIONS PUBLISHED SEPARATELY

The employer schedules and our opinions on them are available on the Department of Employee Trust Fund's website



STATE OF WISCONSIN

Legislative Audit Bureau

22 East Mifflin Street, Suite 500 ■ Madison, WI 53703 ■ (608) 266-2818 ■ Hotline: 1-877-FRAUD-17 ■ www.legis.wisconsin.gov/lab

Celebrating
50 Years of
Service

1966-2016

Joe Chrisman
State Auditor

August 18, 2015

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

Dear Senator Cowles and Representative Kerkman:

As requested by the Department of Employee Trust Funds (ETF), we have completed an audit of the Schedule of Employer Allocations of the Wisconsin Retirement System (WRS), the Schedule of Pension Amounts by Employer of the WRS, and the related notes to these schedules as of December 31, 2014. These schedules, and our unmodified opinions on them, may be found on ETF's website.

The Governmental Accounting Standards Board (GASB) has issued new pension accounting standards, which ETF adopted for its 2014 WRS financial statements. We audited those financial statements and related notes and provided our unmodified opinion on them in report 15-11, which we also published today. Because the \$92.2 billion fiduciary net position of the WRS, which represents resources available to pay pension benefits, was greater than the total pension liability of \$89.7 billion, ETF calculated a net pension asset for the WRS of \$2.5 billion, as of December 31, 2014.

Under the new pension accounting standards, each of the almost 1,500 participating employers in the WRS is required to report its proportionate share of this net pension asset on its financial statements if prepared in accordance with generally accepted accounting principles (GAAP). The proportionate share of the net pension asset for all State of Wisconsin agencies was \$686.9 million, or 27.9 percent of the total net pension asset. Of this amount, \$330.2 million related to the University of Wisconsin System. The net pension asset for the state agencies will be reported in the State's Comprehensive Annual Financial Report for the year ended June 30, 2015.

The Independent Auditor's Report on Internal Control over Financial Reporting and on Compliance and Other Matters, which is required by *Government Auditing Standards*, is on page 11. We did not identify any control or compliance concerns that were required to be reported under these standards.

Respectfully submitted,

A handwritten signature in black ink, appearing to read 'Joe Chrisman'.

Joe Chrisman
State Auditor

JC/CS/ss

Introduction ■

The Wisconsin Retirement System is a cost-sharing, multiple-employer, defined-benefit pension plan.

Created in January 1982, the WRS is a cost-sharing, multiple-employer, defined-benefit pension plan that provides post-retirement financial benefits to participating employees, as well as disability and death benefits to participants and their beneficiaries.

Approximately 604,000 individuals participated in the WRS on December 31, 2014, including:

- 257,300 (42.6 percent) active participants who were making contributions;
- 185,600 (30.7 percent) retired participants who were receiving WRS benefits; and
- 161,100 (26.7 percent) inactive participants, such as former employees, who were not yet receiving benefits and were not required to make contributions.

ETF and SWIB work together to manage the Wisconsin Retirement System.

The WRS is the ninth-largest public pension plan in the United States. As of December 31, 2014, the WRS had a fiduciary net position of \$92.2 billion, which represents resources available to pay pension benefits. ETF is responsible for managing the operations of the WRS that interact with employers and participants, including collecting contributions from and paying retirement benefits to WRS participants, and the State of Wisconsin Investment Board (SWIB) is responsible for managing WRS

investments. ETF and SWIB work closely together to ensure the solvency and long-term future of the WRS.

In report 15-11, we provided an unmodified opinion on the WRS financial statements and related notes for the year ended December 31, 2014.

In this report, we summarize the results of our audit of the Schedule of Employer Allocations and the Schedule of Pension Amounts by Employer as of December 31, 2014. We have also completed an audit of the financial statements and related notes of the WRS as of December 31, 2014, as required by statutes. The financial statements and our unmodified opinion on them are included in report 15-11. In that report, we describe a significant deficiency in internal control related to ETF's financial reporting process.

New Pension Standards and Employer Reporting

In 2012, the Governmental Accounting Standards Board (GASB) issued new accounting standards for public pension plans and participating employers. Specifically:

- GASB Statement Number 67, *Financial Reporting for Pension Plans—an amendment of GASB Statement No. 25*; and
- GASB Statement Number 68, *Accounting and Financial Reporting for Pensions—an amendment of GASB Statement No. 27*.

Under the new pension accounting standards, ETF calculated a net pension asset of \$2.5 billion for the WRS as of December 31, 2014.

These new standards establish accounting and financial reporting requirements for measuring the pension liability, as well as requirements for both the notes to the WRS financial statements and the GAAP-based financial statements of the almost 1,500 employers that participate in the plan. In preparing the 2014 financial statements and notes of the WRS, ETF implemented the new pension accounting standards, which required the calculation of the total pension liability for the WRS. As of December 31, 2014, ETF reported a fiduciary net position of \$92.2 billion for the WRS. In addition, ETF calculated and disclosed in the notes to the WRS financial statements, a total pension liability of \$89.7 billion, and a net pension asset of \$2.5 billion as of December 31, 2014. For additional information on ETF's implementation of the new pension accounting standards, see report 15-11.

In addition, the new pension accounting standards require public pension plans to calculate pension expense, as well as amounts that are considered deferred, for the plan. Pension expense is the net increase or decrease in the net pension liability or asset, with certain adjustments. For example, the benefits earned during the year by participants of the WRS will increase the net pension liability and

would be included in the calculation of pension expense. However, certain changes in the net pension liability are initially reported as a deferred outflow or deferred inflow of resources, which are then amortized into pension expense. Differences between actual investment earnings and the investment assumptions are amortized over a five-year period and changes in experience, such as salary increases being lower than expected, are amortized over the average remaining service life of the participants, which was approximately five years for 2014. Reporting of pension expense under the new pension accounting standards more closely aligns the pension expense with the periods during which the pension benefits are earned by the employees.

Each WRS participating employer was allocated its proportionate share of the net pension asset.

Under the new pension accounting standards, each employer participating in the WRS is required to report its proportionate share of the net pension asset, as well as pension expense, deferred outflows of resources, and deferred inflows of resources, on its own GAAP-based financial statements. To assist WRS employers in meeting the requirements for reporting these amounts, ETF prepared the Schedule of Employer Allocations and the Schedule of Pension Amounts by Employer for the year ended December 31, 2014.

We provided an unmodified opinion on the WRS employer schedules prepared under the new pension accounting standards.

We reviewed ETF's preparation of the schedules, considered ETF's internal controls over the preparation of the schedules, and completed testing of the underlying amounts to ensure the accuracy of the allocation in the Schedule of Employer Allocations and of the total amounts reported for all entities, referred to as specified column totals for the columns titled Beginning Net Pension Liability (Asset), Ending Net Pension Liability (Asset), Total Deferred Outflows of Resources, Total Deferred Inflows of Resources, and Total Employer Pension Expense (Income) included in the Schedule of Pension Amounts by Employer. In addition to providing an unmodified opinion on the schedules and related notes for the year ended December 31, 2014, we have issued our Independent Auditor's Report on Internal Control over Financial Reporting and on Compliance and Other Matters, which is on page 11. Our unmodified opinions on the schedules are included on ETF's website at <http://etf.wi.gov/>.

As shown in Table 1, the ten largest WRS participating employers were allocated a total of \$1.0 billion, or 40.9 percent of the \$2.5 billion net pension asset. The proportionate share of the net pension asset for State of Wisconsin agencies was \$686.9 million, of which \$330.2 million related to the University of Wisconsin (UW) System. The net pension asset for the state agencies will be included in the State's GAAP-based financial statements, which will be published in the State's Comprehensive Annual Financial Report for the year ended June 30, 2015.

Table 1

Net Pension Asset by Employer^{1, 2}
December 31, 2014

Participating Employers	Proportionate Share	Net Pension Asset
State Agencies, excluding the UW System	14.5%	\$ 356,706,794
UW System	13.4	330,166,674
University Hospitals and Clinics	3.1	76,075,835
Milwaukee Teachers Retirement System	2.7	67,124,330
City of Madison	1.6	38,965,978
Madison Metropolitan School District	1.5	37,330,073
Dane County	1.1	27,677,075
Kenosha Unified School District	1.0	24,739,006
Green Bay Area Public Schools	1.0	23,569,378
Racine Unified School District	1.0	23,529,492
Subtotal	40.9	1,005,884,635
Total for Other Participating Employers	59.1	1,450,388,949
Total	100.0%	\$2,456,273,584

¹ For complete information on the net pension asset of each employer in the WRS, the Schedule of Pension Amounts by Employer of the Wisconsin Retirement System is available on ETF's website at <http://etf.wi.gov/>.

² For complete information on the calculation of the net pension asset, see report 15-11.

The employer's proportionate share of the net pension asset is not available to the employer to meet other outstanding obligations. Because the WRS is an irrevocable trust, all funds remain in the trust and can only be used to fund pension benefits.

Census Data

Census data, including participant birthdate, gender, and earnings, are important to the actuarial calculation of the total pension liability for the WRS. ETF is responsible for the design, implementation, and maintenance of internal control over financial reporting for the WRS, including ensuring the accuracy of participant census data in ETF's systems. According to recent guidance provided by the American Institute of Certified Public Accountants, a complete system of internal control related to the total pension liability calculation

should include processes to document the risk of error related to the significant census data elements for plan participants and, for active participants, include procedures to verify the completeness and accuracy of the information with underlying payroll records of the participating employers.

As part of our audits of the WRS financial statements and the employer schedules, we assessed ETF's procedures to ensure the accuracy and completeness of census data from employers. In addition, for a selection of WRS employers, we tested key census data elements, including employee birthdate, gender, and earnings by comparing ETF records to participating employer records. Overall we found the key census data on ETF's systems to be in agreement with employer records.

We note that ETF has generally relied on WRS employers to ensure the accuracy of the census data. ETF provides training and resources to assist employers in understanding the reporting requirements, and it conducts review and analyses to ensure the reasonableness of employee-related information. In addition, ETF implemented a pilot program during 2014 to review employer policies and procedures for reporting WRS eligible earnings and for completing annual reporting and reconciliation procedures. ETF's Office of Internal Audit also plans to conduct audit work on employer census data beginning in fall 2015.

■ ■ ■ ■

Auditor's Report ■



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
Mr. Robert J. Conlin, Secretary

We have audited the Schedule of Employer Allocations of the Wisconsin Retirement System as of and for the year ended December 31, 2014, and the related notes. We have also audited the total for all entities, referred to as specified column totals for the columns titled Beginning Net Pension Liability (Asset), Ending Net Pension Liability (Asset), Total Deferred Outflows of Resources, Total Deferred Inflows of Resources, and Total Employer Pension Expense (Income) included in the Schedule of Pension Amounts by Employer of the Wisconsin Retirement System as of and for the year ended December 31, 2014, and the related notes. We have issued our report on these schedules thereon dated August 13, 2015. 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.

Internal Control over Financial Reporting

Management of the Department of Employee Trust Funds is responsible for establishing and maintaining effective internal control over financial reporting (internal control). In planning and performing our audit of the Wisconsin Retirement System schedules, 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 schedules, 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 schedules will not be prevented, or that a material misstatement will not be detected and corrected on a timely basis.

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. 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.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Wisconsin Retirement System schedules 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 schedule 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 have also audited, 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 United States, the financial statements and related notes of the Wisconsin Retirement System as of and for the year ended December 31, 2014. We expressed an unmodified opinion, dated August 13, 2015, on those financial statements. In addition, we issued an Independent Auditor's Report on Internal Control over Financial Reporting and on Compliance and Other Matters, dated August 13, 2015, and included in report 15-11, related to the audit of the financial statements and reported a significant deficiency in internal control over financial reporting. As included in that report, 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.

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



Joe Chrisman
State Auditor

August 13, 2015