

AUDIT REPORT

Oregon Public Employees Retirement System: Benefit Calculation Audit



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Summary

PURPOSE

The purpose of our audit was to determine whether the Oregon Public Employees Retirement System (PERS) accurately calculated retirement benefits in compliance with laws and regulations, and whether adequate controls over benefit calculations were in place. We reviewed a sample of 200 benefit calculations for members who retired or had adjustments made to their retirement calculations during calendar year 2001.

RESULTS IN BRIEF

We found that PERS did not always accurately calculate retirement benefits and could improve its controls over retirement benefit calculations.

Of the 200 calculations reviewed, 30 (15 percent) had errors that financially impacted the member or the employer, or both.

- Errors in payments to members totaled \$15,826. Of this amount, \$5,307 represents overpayments to members and \$10,519 represents underpayments to members.
- Errors in reserve accounts totaled \$58,469.

Although these errors were not material to PERS, they may be significant to an individual member.

RECOMMENDATION

We recommend that PERS accurately calculate benefits and ensure that adequate controls over benefit calculations are in place.

AGENCY RESPONSE

PERS generally agrees with the recommendations.

Introduction

The Public Employees Retirement System (PERS) was established in 1946 to provide service and disability retirement income and death benefits to Oregon public employees. Membership includes employees of the state, school districts, and local governments. As of December 31, 2001, 211,141 current and former employees were entitled to benefits but not yet receiving them, and 85,136 retirees and beneficiaries were receiving benefits. During fiscal year 2001, PERS paid over \$1.5 billion in benefits to retirees.

Upon retirement or disability, members receive benefits based on a number of factors. These factors include, but are not limited to, age, years of service, final average salary, account balance, type of service (police and fire, legislator, or general service) and option of survivorship.

As required by Oregon Revised Statute 238.300, PERS uses three methods to calculate retirement benefits: Full Formula, Formula Plus Annuity, and Money Match. The statute requires PERS to use the method that produces the highest benefit.

PERS uses the Retirement Information Management System (RIMS) to calculate most benefits. RIMS, however, is not programmed to compute many of the more complex calculations, resulting in PERS staff performing manual calculations and system work-arounds. For instance, all divorce and about one-third of disability benefits are calculated manually. In addition, complex regular retirement benefits, such as members who worked for multiple PERS covered employers (e.g., state, school districts, cities), often cannot be processed by RIMS.

PERS relies on retirement counselors to accurately perform

manual calculations and enter data into RIMS without error. In addition, PERS relies on an independent review process in which manual calculations are reviewed by another counselor for accuracy.

Upon retirement, PERS transfers each member's account balance and amounts from one or more Employer Reserve accounts to the Benefits Reserve. The Benefits Reserve contains the funds set aside to pay future retirement benefits. Amounts transferred are calculated based on information provided by PERS' actuary.

Background

Each year, the Secretary of State Audits Division conducts an audit to determine if PERS' financial statements are presented fairly in accordance with generally accepted accounting principles. In 2001, the Audits Division issued an unqualified or "clean" opinion on PERS' financial statements.

During our testing for the fiscal year 2000 and 2001 audits, we noted several benefit calculation errors. While these errors were not considered material to PERS' financial statements, we did find them significant enough to warrant management's attention and issued letters to the management of PERS detailing the nature of these errors.

During the fiscal year 2001 audit, PERS provided to us a list of instances where RIMS does not correctly calculate retirement benefits. PERS staff is aware of these instances and should calculate these benefits manually.

Based on our prior audit work, the list provided by PERS, and concerns expressed by PERS' management, we determined that an expanded audit of benefit calculations should be performed to determine the causes and the impacts of incorrect calculations.

Audit Results

Benefit Calculations Not Always Accurate

We reviewed a sample of benefit calculations for 200 retired members and alternate payees. The selected retired members and alternate payees all retired in calendar year 2001 or received a benefit calculation adjustment in 2001 for an earlier retirement. Our sample included 58 system calculations and 142 manual calculations.

We found that PERS did not always accurately calculate retirement benefits and could improve its controls over retirement benefit calculations. Specifically, we found that 60 of the 200 benefit calculations reviewed (30 percent) had at least one error. We identified errors in both system and manual calculations. Half of the calculation errors resulted in financial impacts. As of May 2002, these errors resulted in the following:

- PERS owed 13 members a total of \$10,519.
- Twelve members owed PERS a total of \$5,307.
- Reserve errors totaled \$58,469.

Errors impacted both monthly payments and lump sum payments. As we identified errors, we discussed the errors with PERS' staff members, who made the necessary corrections. The dollar amounts of errors listed above were from the time the calculation error was made until it was corrected by PERS.

Extrapolating our sample results to the entire population of members who retired or had retirement adjustments during 2001, we estimate that the benefits members received through May 2002 are in error by approximately \$171,000. Of this amount, we estimate that \$73,000 was overpaid to members and \$98,000 was underpaid to members. We also estimate that the Benefits Reserve owes Employer Reserve accounts a net amount of \$99,000.

We placed causes of the errors into three categories:

- Retirement counselor errors,
- Data entry errors, and
- Programming errors and inconsistencies.

In addition to the errors noted above, we found instances of documentation missing from PERS' archived files. In these cases, we were unable to verify whether the information PERS used to calculate the retirement benefits was correct.

Retirement Counselor Errors

In 47 of the 200 benefit calculations reviewed (24 percent), retirement counselors made one or more errors in computing benefits. In four of these errors, retirement counselors did not review all of the

documentation pertinent to the calculation.

Of these 47 errors, 22 had a financial impact resulting in errors made to members totaling \$15,664 and reserve errors totaling \$58,077. The remaining 25 errors were non-financial errors, such as calculating a benefit using the incorrect amount of sick leave remaining in an employee's account at the retirement date. This does not have a financial impact to members who retire under the Money Match option.

PERS' primary control to detect errors made in manual calculations is a review process in which a second employee reviews the retirement counselor's computations to verify their accuracy. This review process, however, did not effectively identify these errors.

One factor that could contribute to this situation is that PERS tends to emphasize speed rather than accuracy. State statute requires PERS to mail a retired member's first monthly benefit payment within 92 days of the retirement date. We found that PERS management emphasizes completing benefit calculations quickly so that members can receive their benefit payments as soon as possible after their retirement date. PERS management has set a goal of mailing the first monthly benefit payment within 45 days of a member's retirement date. PERS, however, has not established goals related to benefit calculation accuracy.

Data Entry Errors

We found that nine of the 200 benefit calculations reviewed (five percent) had data entry errors. In these instances, retirement counselors incorrectly entered data into the system. These errors were not caught during review and resulted in \$162 of incorrect payments to members and incorrect reserve transfers of \$137.

Programming Errors and Inconsistencies

PERS uses RIMS and other personal computer programs to calculate retirements. Four of the 200 benefit calculations reviewed (two percent) had errors resulting from programming errors or inconsistencies. Two of the errors caused a financial impact, resulting in the Employer Reserve owing the Benefits Reserve \$255.

The programming errors were as follows:

- In one benefit calculation, RIMS incorrectly included a variable adjustment even though the member had transferred out of the variable option two years prior to the calculation.
- In two benefit calculations, a program used to calculate benefits for ex-spouses of members was calculating the amount of Employer Reserve transferred to the Benefits Reserve in a manner inconsistent with methods used by all other PERS programs.
- In another benefit calculation, a program calculated the age of a member inconsistent with the methods used by all other PERS programs.

Missing Documentation

In 10 of the 200 benefit calculations we reviewed (five percent), one or more documents supporting the calculations were missing from PERS' documentation archives. For these 10 calculations, documents were not available to support 17 elements (e.g., salary, age and retirement date) used in the calculations. Because we were unable to verify the information used in these calculations, we could not conclude on the accuracy of these calculations and did not consider them to be errors. Without documentation, PERS cannot provide evidence that it complied with laws and regulations.

Recommendations

We recommend that PERS:

- Correct the errors identified during our audit by paying members the amounts due, collecting from members the amounts owed, and transferring the appropriate amounts between Employer and Benefit Reserves.
- Emphasize accuracy over speed in calculating benefits and develop goals for accuracy.
- Ensure proper review of all benefit calculation elements, including the payment setup and reserve transfers.
- Create a process to ensure that staff receive and review all documents pertinent to a benefit calculation. Staff also should ensure that all documents are properly archived.
- Ensure consistency between all programs in calculating Employer Reserves and ages. Programs with programming errors and inconsistencies should be modified to prevent inaccuracies in future calculations. Review benefit calculations for all members that may have been affected by these programming errors and inconsistencies and make corrections as deemed necessary.

Agency's Response:

PERS agrees with the audit's findings and recommendations. Staff has corrected all member benefit and employer reserve errors identified by the audit, and ensured that all missing documents were filmed and filed in the members' records. To address benefit calculation accuracy, PERS management is pursuing an "accuracy initiative," the remediation and replacement of RIMS, and the development of an electronic document management system. Some plans are underway, while others require funding that has been either requested in the 2003-05 biennial budget package, or which

the agency plans to submit to the Joint Legislative Committee on Information Management and Technology and Emergency Board periodically.

PERS is requesting funding to address accuracy issues under a plan named the "accuracy initiative." PERS intends to use funding to hire additional staff that will focus on more intensive review of manual calculations and the comparison of data entered into RIMS to source documents. Current staffing is stretched to the point that errors are not always identified. PERS agrees that benefit calculation accuracy performance measures are important and is planning to establish such measures.

In addition, PERS is pursuing funding for a new information technology (IT) platform to replace RIMS and a host of associated manual processes. The new system will include automatic data edits, detailed audit tracking, and strengthened benefit calculation controls. Automated electronic processes will replace the manual aspects of benefit calculations, which account for a disproportionate share of errors. PERS is completing RIMS remediation work packages, as staffing and funding allows, to fix current problems and extend the life of RIMS until a modern, effective IT infrastructure can be implemented. PERS anticipates a series of RIMS work packages to be launched over the next several years assuming the approval of necessary resources.

Finally, PERS is beginning the first phase of a project to develop and maintain an electronic document management system that includes the storage and retrieval of documents, on-line document viewing, workflow management, and calculation process activity reports. This system will increase efficiencies and control over PERS processes.

PERS would like to commend the audit team on its professionalism

and cooperative approach throughout the audit. The Audits Division's willingness to expand the benefit calculation audit sample from 100 to 200, and increase the number of samples from transactions believed to be high risk, is greatly appreciated. The Audits Division's cooperation provided PERS with additional information about the accuracy of the benefit calculations, the sources of errors, and potential management responses.

Objectives, Scope and Methodology

Our objectives were to determine whether PERS:

- Accurately calculated retirement benefits;
- Was in compliance with laws and regulations that relate to benefit calculations; and
- Had controls in place over benefit calculations.

Approximately 4,000 members and alternate payees retire each year. Alternate payees include the spouses of members who were

awarded a PERS retirement benefit as a part of a divorce decree.

We reviewed the benefit calculations for a sample of 200 retired members and alternate payees. These retired members and alternate payees retired in calendar year 2001 or received a benefit calculation adjustment in 2001 for an earlier retirement. We relied on RIMS for salaries and account balances. We used PERS' source documentation, obtained from employers and members, to verify other elements of the benefit calculations.

Our sample of 200 retirees was selected using a non-statistical sampling method. We selected 142 manually calculated retirements and 58 system-calculated retirements. Many retiree benefit calculations must be manually calculated because RIMS is not programmed to process them. Because we perceived increased risk associated with manually calculated retirements as compared to the system-processed retirements, our sample included more manual calculations. Some calculations contained both manual and system calculated factors. Retirement calculations with any

manual transaction codes were considered manual retirees.

As part of our sample selection, we also considered the number of PERS covered employers a member worked for, and the various retirement benefit types, such as general service, judges, disabilities, police and fire units, and alternate payees. Twenty of the 200 retirements were selected solely because the member had worked for four or more PERS covered employers.

We tested calculations for accuracy, compliance with laws and regulations and the application of established PERS' controls. For example, we tested whether retirement applications were signed, the calculation used correct service time amounts, and the calculations were reviewed by appropriate staff. We tested all sample retirements for the same elements.

We conducted this audit according to generally accepted government auditing standards. We conducted our audit between January and May of 2002. We limited our audit to the areas specified above.

This report, which is a public record, is intended to promote the best possible management of public resources. Copies may be obtained by mail at Oregon Audits Division, Public Service Building, Salem, Oregon 97310, by phone at 503-986-2255 and 800-336-8218 (hotline), or internet at Audits.Hotline@state.or.us and <http://www.sos.state.or.us/audits/auditthp.htm>

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The courtesies and cooperation extended by the officials and staff of the Oregon Public Employees Retirement System were commendable and much appreciated.

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