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*Auditing for a Better Oregon*

December 16, 2005

Paul Cleary, Executive Director  
Oregon Public Employees Retirement System  
11410 SW 68<sup>th</sup> Parkway  
Tigard, Oregon 97223

The Board of Trustees  
Oregon Public Employees Retirement System Board  
11410 SW 68<sup>th</sup> Parkway  
Tigard, Oregon 97223

Dear Mr. Cleary and the Board:

We have completed our financial statement audit of the Oregon Public Employees Retirement System (PERS) for the year ended June 30, 2005. Based on our audit, we identified conditions needing corrective action. Our findings and recommendations are presented in the enclosed Audit Findings and Recommendations Summary accompanying this letter.

We identified a reportable condition related to internal control. Professional auditing standards define reportable conditions as matters relating to significant deficiencies in the design or operation of internal control over financial reporting that, in our judgment, could adversely affect PERS' ability to initiate, record, process, and report financial data consistent with the assertions of management in the financial statements. The reportable condition was included within the Report on Compliance and Internal Control in the PERS 2005 Comprehensive Annual Financial Report.

The reportable condition, along with your response, will be included in our Statewide Single Audit Report. Including your response with responses from other state agencies satisfies the federal requirement that management prepare a Corrective Action Plan (CAP) covering all reported audit findings. Satisfying the federal requirement in this manner, however, can only be accomplished if the response to the reportable finding includes the information specified by the federal requirement, and only if the response is received in time to be included in the audit report. The following information is required for the response:

1. Your agreement or disagreement with the finding. If you do not agree with the audit finding or believe corrective action is not required, include in your response an explanation and specific reasons for your position.

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2. The corrective action planned.
3. The anticipated completion date.
4. The name(s) of the contact person(s) responsible for corrective action.

For the reportable condition, please submit your written response, containing all the required information, by January 20, 2006.

The other conditions are issues of lesser significance that we wanted to communicate to agency management. These conditions do not require a Corrective Action Plan. We will follow up on PERS' progress in addressing these issues during the next fiscal year audit.

Should you have any questions, please contact Amy Palacios or me at (503) 986-2255.

Sincerely,  
OREGON AUDITS DIVISION

Nancy L. Young, CPA, CISA, CFE  
Audit Manager

NLY:bk

cc: James Dalton, Audit Committee Chair  
David Tyler, Administrator, Chief Financial Officer  
Lindsay A. Ball, Director, Department of Administrative Services

# **Audit Findings and Recommendations Summary**

## **Oregon Public Employees Retirement System**

### **State Fiscal Year 2005**

#### **REPORTABLE CONDITION**

##### Inadequate Control Over Personal Member Information

PERS did not adequately protect some personal member information (including names, addresses, birth dates, and social security numbers) when it used production data from the live pension system in test and development regions. PERS staff, as well as contractors and vendors, had access to confidential data not required to perform their job duties. On at least one occasion, confidential production data was placed on PERS' personal computers that were taken to the contractor's place of business where PERS no longer had control over their security and use. Furthermore, while PERS staff stated that it would be difficult to create test data that would cover all retirement scenarios, PERS did not scrub the production data to remove specific identification of PERS members.

In addition, PERS did not protect some member's medical information. PERS staff, who did not require access to perform their job duties, were given access to view confidential medical information through the archival imaging system. Though aware that access to the confidential information was not limited, PERS was not proactive to identify and remove those confidential records.

A lack of security increases the risk that personal member information could be used for inappropriate or malicious purposes.

**We recommend** that PERS:

1. Discontinue the use of production data for test and development purposes and document in formal policy.
2. Create test data to use in test and development regions.
3. Actively identify and remove all confidential medical information that has been posted to the archival imaging system.
4. Review and modify archival procedures to ensure that confidential medical information is not made available to persons not needing access.

#### **OTHER CONDITIONS**

##### Prior Year Reportable Condition – Reconciling Items Not Cleared in a Timely Manner

During the 2004 opinion audit we found that PERS was not promptly clearing reconciling items from three clearing accounts. The total unreconciled balance of these accounts exceeded \$285 million as of June 30, 2004. As of June 30, 2005, the total unreconciled balance exceeded \$250 million, of which 68 percent was more than one year old.

Items are placed in the clearing accounts when there is a disagreement between amounts reported in the Membership and Benefit Reserve Subsystems of the Retirement Information Management System (RIMS). Each item remains in the clearing accounts until PERS staff can review and resolve the discrepancies. Uncorrected reconciling items may result in the over or under payment of refunds or benefits. Failure to correct reconciling items promptly may increase the magnitude of errors.

This prior year reportable condition is partially resolved and the status of PERS corrective action will be included in the 2005 Statewide Single Audit Report.

**We recommend** PERS management continue to focus attention toward the correction of the RIMS clearing account reconciling items.

#### Account Reconciliations Not Timely

We found that cash account reconciliations are not always prepared or reviewed timely and reconciling items are not always cleared timely. PERS' policy is to prepare reconciliations within thirty days after closing the general ledger, and review within fifteen days of preparation. Untimely preparation or review of reconciliations and untimely clearing of reconciling items increases the likelihood that items could become permanent differences, or fail to be appropriately adjusted on the financial statements. Reconciliations are an important control that help ensure accurate and complete financial reporting.

**We recommend** PERS management ensure that all reconciliations are prepared and reviewed timely and that reconciling items are addressed and cleared in a timely manner.

#### Weak Controls Over Check Stock

During our review, we found PERS does not maintain a control log of blank check stock and does not perform periodic physical inventories.

The Oregon State Treasury Cash Management Manual states that all agencies are to maintain physical controls over blank check stock. At a minimum, these controls must include periodic physical inventories of blank check stock reconciled to the control log by someone lacking access and responsibility for check stock and check issuance.

The absence of a periodic physical inventory of blank check stock increases the risk that misappropriation could go undetected and uncorrected for an extended period of time.

**We recommend** PERS management maintain an inventory log of check stock and ensure that a periodic physical inventory of blank check stock is performed by an employee not associated with check stock handling and the check issuance process.

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#### Out-of-date Policies

PERS has not maintained an up-to-date RIMS security manual or current policies and procedures.

The RIMS Security Manual has not been reviewed since November 2000 and contains out-of-date information. Furthermore, twelve of seventeen information technology policies and one disabilities related policy reviewed by auditors have not been reviewed or updated since 2001.

PERS policy and best practices indicate that policies should be kept up-to-date by reviewing them at least annually and making revisions as determined necessary.

**We recommend** PERS management ensure all policies and procedures are reviewed and updated annually as required by policy, including the RIMS Security Manual.