



Commonwealth of Massachusetts
Office of the State Auditor
Suzanne M. Bump

Making government work better

Official Audit Report – Issued April 29, 2015

Massachusetts Teachers' Retirement System

For the period July 1, 2011 through June 30, 2013





Commonwealth of Massachusetts
Office of the State Auditor
Suzanne M. Bump

Making government work better

April 29, 2015

Ms. Erika M. Glaster, Executive Director
Massachusetts Teachers' Retirement System
One Charles Park, Second Floor
Cambridge, MA 02142-1206

Dear Ms. Glaster:

I am pleased to provide this performance audit of the Massachusetts Teachers' Retirement System. This report details the audit objectives, scope, methodology, findings, and recommendations for the audit period, July 1, 2011 through June 30, 2013. My audit staff discussed the contents of this report with management of the agency, whose comments are reflected in this report.

I would also like to express my appreciation to the Massachusetts Teachers' Retirement System for the cooperation and assistance provided to my staff during the audit.

Sincerely,

A handwritten signature in blue ink, appearing to read "SMB", written in a cursive style.

Suzanne M. Bump
Auditor of the Commonwealth

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LIST OF ABBREVIATIONS

BVF	Biennial Verification Form
CMR	Code of Massachusetts Regulations
HRD	Human Resources Division
IRS	Internal Revenue Service
IT	information technology
MMARS	Massachusetts Management Accounting and Reporting System
MTRS	Massachusetts Teachers' Retirement System
OSC	Office of the State Comptroller
OSD	Operational Services Division
OST	Office of the State Treasurer
PERAC	Public Employee Retirement Administration Commission
PRIM	Pension Reserves Investment Management Board
SSTA	Self-Service Time and Attendance

EXECUTIVE SUMMARY

The Massachusetts Teachers' Retirement System (MTRS), the Commonwealth's largest contributory retirement system, provides retirement, disability, and survivor benefits to public-school teachers and administrators and their families.

In this performance audit, we reviewed and assessed selected financial and management activities of MTRS to evaluate its ability to perform and administer its functions and responsibilities efficiently, effectively, and in compliance with laws and regulations.

Below is a summary of our findings and recommendations, with links to each page listed.

Finding 1 Page 11	When employees leave MTRS, their user access to the agency's benefit-administration system (MyTRS) is not promptly deactivated. Insufficient controls over user access could place sensitive and confidential information—member data in particular—at risk of unauthorized access, modification, misuse, and/or loss.
Recommendations Page 12	<ol style="list-style-type: none">1. MTRS should develop formal written policies and procedures requiring that (1) the Human Resources Unit notify the Information Technology Services Unit of any changes in employee status that warrant a change or deactivation of access privileges to MyTRS and (2) periodic (e.g., quarterly) reviews of user access rights be performed to ensure that specific employees' access privileges are appropriate and up to date.2. MTRS should perform an immediate review of the status of all active MyTRS users and deactivate access privileges for individuals who no longer require, and/or are not authorized to have, access to this system.
Finding 2a Page 15	Records for accounts payable and receivable to and from retiree estates are not accurately maintained. On MTRS's reported financial statements for fiscal year 2013, the balance for accounts payable was overstated by a net of \$43,396 and the balance for accounts receivable was understated by \$116,980. Without accurate financial records, MTRS may not be collecting or otherwise resolving all funds due the Commonwealth and paying all funds owed to surviving beneficiaries.
Finding 2b Page 17	MTRS's published list of unclaimed funds owed to deceased members' surviving beneficiaries is not current, accurate, and complete. Therefore, surviving beneficiaries may not know MTRS has unclaimed funds on account for them, and there is no assurance that this list is an effective tool to communicate and resolve instances of funds owed to the public.
Recommendation Page 17	MTRS should implement supervisory oversight controls to ensure that individual balances on the aging lists for accounts payable and receivable are accurate and complete; that the total of the individual balances agrees with MTRS's financial-statement balances; and that the Unclaimed Funds List is accurately maintained. MTRS should update its documented policies and procedures to include these supervisory oversight controls.

Post-Audit Action

Since the completion of our audit, MTRS senior management has presented and recommended to its board revised policies regarding overpayments and an annual write-off of accounts receivable that are at least three years old. In addition, management recommended writing off accounts receivable outstanding as of June 30, 2011. At the November 21, 2014 board meeting, the board approved the aforementioned policy revisions and recommended to the Office of the State Comptroller the write-off of \$1,063,412.59 in accounts receivable for the period 1988 through 2011.

OVERVIEW OF AUDITED ENTITY

According to its website, the Massachusetts Teachers' Retirement System (MTRS) was established on July 1, 1914 and "is the largest of the Commonwealth's 104 contributory retirement systems"; it is a defined benefit plan that provides "retirement, disability and survivor benefits to Massachusetts teachers, administrators and their families." Chapter 32 of the Massachusetts General Laws establishes the benefits, contribution requirements, and accounting structure for the system. Teachers and administrators in Massachusetts public schools (except those in the City of Boston¹) or educational collaboratives are eligible for membership.

All members are required to enroll with MTRS and make mandatory contributions through payroll deductions. Members contribute a percentage of their earnings based on when they joined the public retirement system:

Date Joined	Contribution Rate
Before January 1, 1975	5%
January 1, 1975 through December 31, 1978	7%
January 1, 1979 through December 31, 1983	7% + 2% on earnings over \$30K
January 1, 1984 through June 30, 1996	8% + 2% on earnings over \$30K
July 1, 1996 through June 30, 2001	9% + 2% on earnings over \$30K
July 1, 2001 through April 1, 2012	11%
April 2, 2012 or later	11% (reduced by 3% after 30 years of service)

In accordance with Chapter 15, Section 16, of the General Laws, MTRS is administered by a seven-member, unpaid board made up of the following members:

- Commissioner of Education or his/her designee, Chairperson
- Massachusetts State Treasurer or his/her designee
- Massachusetts State Auditor or his/her designee
- Governor's designee (who must be a retired teacher)
- two members elected by the active and retired members of the system

1. Teachers employed by the City of Boston are members of the Boston Retirement System.

- one member elected by the board members

Each member serves a four-year term, except the Commissioner, the State Treasurer, and the State Auditor, who serve as long as they are in office. According to MTRS's website,

The board, which meets at least once a month,

- *votes on every disability retirement allowance,*
- *investigates all claims for accidental and ordinary disabilities,*
- *establishes the rules and regulations of the agency, and*
- *oversees the dissemination of services and information to its membership of more than 88,000 active educators and 59,000 retirees and survivors.*

MTRS maintains staff in Boston and Springfield to administer and implement the policies of the board. As of June 30, 2013, there were 88 full-time and 11 part-time employees serving more than 86,000 active members, 24,000 inactive members (resigned members who leave their money in the system), and 59,000 retirees and survivors.²

MTRS and other public employee retirement systems are overseen and regulated by the Public Employee Retirement Administration Commission (PERAC) in accordance with Chapter 7 of the General Laws. PERAC promulgated 840 Code of Massachusetts Regulations 1.00 (Protection of Interests of Retirement System Members and Their Beneficiaries), which governs the administrative procedures, financial operations, recordkeeping, and reports that public employee retirement systems must follow. As part of its oversight under these requirements, PERAC performs periodic field examinations and desk reviews of records of all retirement systems at least once every three years. PERAC also provides training as well as legal and technical assistance. MTRS (and the state employees' retirement system) must file fiscal year-end financial statements for each year on or before December 31 of the following year. These annual reports contain the financial condition of each retirement system as well as statistical information regarding membership, findings of audits, the most recent actuarial valuation, the system's investment portfolio, and other pertinent information that PERAC deems appropriate.

The Pension Reserves Investment Management Board (PRIM) manages and invests MTRS member contributions, and the funds are held in a trust fund known as the Pension Reserves Investment Trust.

2. For membership numbers during our audit period, see the appendix of this report.

Retirement benefits that members will eventually receive are made up of two parts: an annuity and a pension. The annuity portion consists of contributions deducted during the course of employment; the pension portion is the difference between the total retirement allowance specified by law and the amount of members' contributions and related investment earnings.

MTRS operations are funded by the income that is earned on the retirement investments managed by PRIM. PRIM provides funding to MTRS based on an expenditure budget approved by the MTRS board and filed for review with the Senate and House Ways and Means Committees. On request from MTRS, PRIM transfers six allotments of cash per year (one-sixth of the budget every two months) to the State Treasurer's cash account for expenditure by MTRS (see the appendix of this report for MTRS general disbursement data).

AUDIT OBJECTIVES, SCOPE, AND METHODOLOGY

In accordance with Chapter 11, Section 12, of the Massachusetts General Laws, the Office of the State Auditor has conducted a performance audit of certain activities of the Massachusetts Teachers' Retirement System (MTRS) for the period July 1, 2011 through June 30, 2013. In our examination of unclaimed funds, we also reviewed information outside this audit period.

We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

Below is a list of our audit objectives, indicating each question we intended our audit to answer; the conclusion we reached regarding each objective; and, if applicable, where each objective is discussed in the audit findings.

Objective	Conclusion
1. Was MTRS able to perform and administer its functions and responsibilities efficiently, effectively, and in compliance with applicable laws, regulations, and policies in the following areas?	
a. Pension-benefit activities, including pension-benefit calculations, terminations of retirement benefits, and refunds of contributions to members that terminated employment	Yes
b. payment of administrative expenditures	Yes
c. board governance, including compliance with open-meeting laws and board-member requirements	Yes
d. issues identified in our prior audit report (No. 2004-0163-3A) that relate to our current audit objectives	Partially; see Findings 2a and 2b

In addition, in the course of our audit work, we found issues with MTRS's management of user accounts for its benefit-administration system (Finding [1](#)).

In order to achieve our objectives, we performed the following audit procedures:

- We reviewed our prior audit report, dated March 30, 2007, and various MTRS internal documents, including its current internal control plan, organizational chart, financial statements, personnel policy and procedure manual, board minutes, and various documents supporting retirement applications.
- To follow up on the findings from our prior audit that were related to our current audit objectives, we reviewed MTRS's policies and procedures regarding the recording of accounts payable and receivable related to payments made on behalf of beneficiaries, representing over- or underpayments that resulted from timing differences between cessation of payments and actual benefit termination periods. We reviewed MTRS's lists of individual accounts-payable and accounts-receivable balances as well as its financial statements. Because accounts-receivable and accounts-payable lists are cumulative, we conducted our review as of June 30, 2013, the end of our audit period.
- We assessed MTRS's controls regarding the oversight of pension benefit activities. Specifically, we performed the following procedures:
 - We reviewed MTRS policies and procedures for pension benefit calculations, as well as applicable criteria including 840 Code of Massachusetts Regulations (CMR) 9.00 and Chapter 32, Section 5, of the General Laws. We interviewed Benefit Administration Unit management personnel to obtain an understanding of MTRS's process for calculating pension benefits. We tested 124 benefit calculations (comprising a non-statistical random sample of 47 retirees who chose MTRS's Option A,³ 30 retirees who chose Option B,⁴ and 47 retirees who chose Option C⁵) from a population of 5,604 benefit payments in MTRS's benefit-administration system (MyTRS). We reviewed supporting documentation such as retirement applications, birth certificates, marriage certificates, creditable-service worksheets, and salary-average worksheets to determine whether benefit payments were accurately calculated.
 - We reviewed MTRS policies and procedures for termination of retirement benefits, as well as applicable criteria such as 840 CMR 15.00. We interviewed managers of MTRS's Benefit Administration and Finance Units to obtain an understanding of MTRS's process for detecting and resolving instances where benefits should be terminated (in particular, benefit recipients' deaths). To determine whether benefits were being paid to deceased recipients, we obtained a list of all benefit payments made to retirees for the month of February 2014 from MyTRS and ran a match against the Social Security Administration's Death Master File, which contains the Social Security numbers of deceased individuals. We also reviewed bank-account records and supporting records for the MTRS bank account used to deposit benefit checks not sent to

3. Members receive their full retirement benefit in monthly payments as long as they live. All benefit payments cease upon their death and no benefits are provided for their survivors.

4. Members receive a lifetime benefit that is approximately 1% to 5% less per month than that of Option A. The annuity portion (member contributions) of their benefits is reduced to allow for a potential benefit for their beneficiaries. Upon a member's death, his or her surviving beneficiaries are paid the unexpended balance of the accumulated total contributions.

5. Members receive a lifetime benefit that is approximately 7% to 15% less per month than that of Option A. Upon a member's death, his or her designated beneficiary is paid a monthly benefit for the remainder of his or her lifetime.

recipients because they did not file completed Biennial Verification Forms (BVF).⁶ Specifically, we performed the following procedures:

- We reviewed the only verification process conducted by MTRS during our audit period (the process commenced in January 2013). From the MTRS Retiree Services Unit file used during our audit period to track the receipt of completed BVFs, we tested all 11 instances where a benefit recipient did not file a completed BVF in 2013. We reviewed MTRS's records of all escrow account activity and escrow bank account statements to determine whether checks held were accurately recorded and deposited.
- We tested a judgmental sample of 6 out of 23 checks issued by the MTRS Finance Unit during our audit period to assess escrow account activity. We reviewed supporting documentation such as completed BVFs, bank statements, and canceled checks to determine that checks were payable to the benefit recipient for the correct amount. We also reviewed all bank statements and reconciliations from our audit period to determine whether all checks cashed were recorded and whether all bank reconciliations were completed in accordance with MTRS policy.
- We reviewed the escrow activity files to determine whether the total of individual benefit recipients' balances agreed with the reconciled balance in the bank account as well as the financial statements as of June 30, 2013.
- We reviewed MTRS policies and procedures for refunding contributions to members who terminated employment, as well as the related criterion Internal Revenue Service (IRS) Publication 15-A, Section 8.⁷ We interviewed Compliance and Financial Reporting Unit management to obtain an understanding of MTRS's process for recording refund applications and issuing refund checks. We tested a judgmental sample of 20 individual refund payments from a population of 97 refunds processed in MyTRS during a two-week period within our audit period. We reviewed refund applications to determine whether federal income taxes were withheld in accordance with IRS regulations.
- We conducted an analysis of administrative expenditures paid in fiscal years 2012 and 2013 to determine expense categories for audit review and selected the three expense categories (Salaries, IT Professionals, and Leases) whose expenses made up the highest percentages of MTRS's discretionary expenses paid; these three categories represented 83% of total discretionary expenses. We assessed MTRS's controls over payment of these administrative expenses. Specifically, we performed the following procedures:
 - We reviewed MTRS policies and procedures for recording and approving employee attendance and approving the payroll expenditure, as well as applicable criteria such as the state Human

6. The Public Employee Retirement Administration Commission regulation 840 CMR 15.01 requires that each retirement board perform, at least once every two years, a verification of all retirees and beneficiaries who receive a monthly benefit. To this end, MTRS requires that each benefit recipient file a BVF, which is a notarized affidavit that includes a statement certifying that the recipient is currently living. The BVF is mailed in January, and if no BVF is filed within six months, future benefit checks are sent to MTRS, not the recipient. Checks are held for six months, unless the recipient files a completed BVF. If no BVF is filed, the checks are deposited in an escrow bank account maintained by MTRS, and future benefit checks are stopped. If a BVF is subsequently filed, a check is issued from the escrow account to the benefit recipient.

7. Refunds of member contributions are subject to 20% federal withholding tax unless directly rolled over into another qualified retirement plan.

Resources Division (HRD) Executive Department Time and Attendance Policy and the Office of the State Comptroller (OSC) Payroll Expenditure Approval Policy. We interviewed managers of MTRS's Human Resources and Finance Units to obtain an understanding of MTRS's process for recording and approving employee attendance. MTRS started using HRD's Self-Service Time and Attendance (SSTA) system in July 2012. We randomly selected 3 of 13 biweekly payrolls processed from January 2013 through June 2013 and tested all employees who appeared on the 281 SSTA attendance reports for the 3 payrolls to determine whether attendance had been approved in SSTA. In addition, we tested a non-statistical random sample of 45 employees out of the population of 281 to determine whether the attendance recorded in the SSTA reports agreed with the attendance recorded on supporting attendance logs.

- We reviewed MTRS policies and procedures for the procurement of information-technology (IT) professionals' contracts, as well as applicable criteria such as 801 CMR 21.00, the Operational Services Division's (OSD's) How to Do a Competitive Procurement policy, and requirements stipulated in OSD's Request for Response for vendors applying for a statewide contract to supply IT professional services. We interviewed managers of MTRS's Information Technology Services and Finance Units to obtain an understanding of the agency's process for conducting a competitive procurement, executing a statewide contract agreement, and approving and recording invoices for payment. We conducted an analysis of payments made to vendors in fiscal years 2012 and 2013 to determine vendors for audit review and selected two vendors that received 81% of the total payments. They were contracted to design, develop, and implement a new, Web-based pension-administration system. We reviewed contract procurement files to determine whether the procurement was conducted in accordance with state regulations. We also tested a judgmental sample of 10 payments from a population of 83 payments recorded in the Massachusetts Management Accounting and Reporting System (MMARS) for the two vendors selected. We reviewed paid invoices to determine whether payments were approved and accurately paid.
- We interviewed Finance Unit managers to obtain an understanding of MTRS's process for executing a lease for office space and paying monthly rent. MTRS has leased office space at two locations: Cambridge and Springfield. We tested a judgmental sample of 4 rent payments from a population of 48 rent payments recorded in MMARS. We reviewed executed lease agreements to determine whether leases were properly executed and whether rent payments agreed with the payments stipulated in the lease agreements.
- To assess the reliability of the MyTRS system, we reviewed existing information, tested selected system controls, and interviewed knowledgeable IT staff members about the data. Based on the analysis conducted, we determined that the data were sufficiently reliable for the purposes of this report.
- To assess the reliability of MMARS, which is maintained by OSC, we reviewed selected process and system controls and interviewed knowledgeable agency officials about the data. Process controls are an organization's policies and procedures that could affect the accuracy and completeness of data. System controls are the underlying structures and programming of computer systems that could affect the accuracy and completeness of data. Based on the analysis conducted, we determined that the data were sufficiently reliable for the purposes of this report.

- We assessed MTRS's controls regarding board governance. Specifically, we reviewed MTRS's board-governance policies and procedures and applicable criteria including Chapter 30A, Sections 18–25, of the General Laws (the Open Meeting Law); Chapter 268A, Section 27, of the General Laws (the Conflict of Interest Law for State Employees); and 940 CMR 29 (the Attorney General's regulations that interpret and enforce the Open Meeting Law). We interviewed MTRS's executive staff to obtain an understanding of its processes for conducting monthly board meetings and obtaining required documents from board members. We tested a random, non-statistical sample of four months during our audit period. We reviewed board meeting agendas and minutes (both open and executive sessions) to determine whether notice of meetings was publicly posted before they occurred and whether minutes were properly completed and approved. We also conducted a review to determine whether there were meeting minutes documented for all months during our audit period. We reviewed board member files to determine whether all required documents were received from board members.

DETAILED AUDIT FINDINGS WITH AUDITEE'S RESPONSE

1. When employees choose to leave the agency, their user accounts are not promptly deactivated.

Of the 12 Massachusetts Teachers' Retirement System (MTRS) employees who left the agency during our audit period, 6 still had access to MTRS's benefit-administration system, MyTRS, when we performed our testing. We did find that MTRS had documented certain information-technology (IT) policies and procedures; assigned responsibility for system access security controls over MyTRS; and instituted appropriate controls for user account activation, password composition, and frequency of password changes. However, increased monitoring over user accounts is required to evaluate user account access and identify accounts that should be deactivated to ensure that only authorized individuals have access to MyTRS. Although our audit found no evidence that the system had been improperly accessed by terminated users, not acting in a timely manner to deactivate user access privileges that are no longer required could place sensitive and confidential information—member data in particular—at risk of unauthorized access, modification, misuse, and/or loss.

MyTRS consists of separate application modules used to manage information related to members, retirees, staff, and employers. Accordingly, the applications contain confidential and sensitive data. Information provided by MTRS IT senior management indicates that all 12 employees had some level of ability to update information in MyTRS.

Authoritative Guidance

MassIT (formerly the Commonwealth of Massachusetts' Information Technology Division) has an Enterprise Staff Information Technology Security Policy that describes what all the Commonwealth's Executive Department secretariats, agencies, and organizations must do to address data-security considerations involving their staff. According to Section 3 of this policy (Termination or Change of Employment or Contract Engagement),

In instances where any Commonwealth staff is voluntarily or involuntarily terminated from employment or is on an extended leave of absence, it is the respective agency's responsibility to immediately implement steps to terminate access and privileges as appropriate. Further, it is each agency's responsibility to ensure they implement and maintain documented procedures to review all access and privileges to data, IT Resources, networks, and facilities and implement appropriate procedures and to ensure the return of all equipment and devices.

Further, MassIT has Enterprise Access Control Security Standards supporting the aforementioned policy. Section 2.4 (Review of User Access Rights) contains the following language:

User's access rights must be reviewed at regular intervals through a formal process that requires:

- *Regular review of users' access rights, after any change to access rights as a result of a change in employment status or duties, and more frequent reviews for special privileged access rights. . . .*
- *Privilege allocations must be checked at regular intervals to ensure that unauthorized privileges have not been obtained.*

All Executive Department agencies are required to comply with this policy and supporting standard.

Reasons for Lack of Timely Deactivation of User Access Rights

Although MTRS had a general access-control requirement (a documented System Security Plan for MyTRS, which requires timely notification regarding all terminations, transfers, changes of responsibility, or leaves of absence of MTRS employees who have access to MyTRS), there were no documented policies or procedures in place requiring MTRS's Human Resources Unit to notify its Information Technology Services Unit when an employee leaves the organization so that the latter unit can remove the employee's access rights in MyTRS.

Effective communication controls help ensure that information is shared among operating units and support personnel.

In addition, we found no evidence that MTRS was periodically performing a reconciliation of the active-account list to a list of authorized employees to ensure that specific employees' access privileges were still appropriate (no more than what each employee needs to perform his or her duties). MTRS IT senior management told us that users' access rights are only reviewed if there has been a change in job responsibility.

Recommendations

1. MTRS should develop formal written policies and procedures requiring that (1) the Human Resources Unit notify the Information Technology Services Unit of any changes in employee status that warrant a change or deactivation of access privileges to MyTRS and (2) periodic (e.g., quarterly) reviews of user access rights be performed to ensure that specific employees' access privileges are appropriate and up to date.

2. MTRS should perform an immediate review of the status of all active MyTRS users and deactivate access privileges for individuals who no longer require, and/or are not authorized to have, access to this system.

Auditee's Response

As noted in the draft report, the auditors found that of the twelve staff who had left the agency during the audit period, six still had active log-in credentials to MyTRS, our benefits administration system. While we agree that this is an issue that requires remediation, and as detailed below, we have taken immediate corrective steps, I want to clarify the limits of access that those six employees retained. The security features of the MyTRS application are such that it cannot be accessed from outside the agency by employees. Staff can only access the application from a computer within our internal agency network, and only after signing into the agency network. The six employees who left MTRS and whose MyTRS access had not been deactivated did not have access to MTRS's network. Their network accounts were properly disabled at their date of departure. Thus, since they could not access the network, they could not access the MyTRS application even if they happened to be onsite.

Corrective actions taken:

The MTRS has established formal written policies and procedures as recommended. . . . The written policy includes a quarterly review (self-audit) of the status of all MTRS users' access to our building, network and MyTRS system.

Auditor's Reply

MTRS is responsible for having controls in place to ensure that it fully complies with MassIT policies and standards, including immediately terminating all access privileges of employees whose status no longer requires it, e.g., those who leave the agency. MTRS's response indicates that its written policies and procedures and periodic reviews of active user accounts will strengthen the security of the MyTRS application.

2. Prior audit results partially resolved—Accounts payable and receivable to and from retiree estates were not recorded in MTRS's financial records.

Our prior audit (No. 2004-0163-3A) noted that certain pension-benefit-related balances were not reflected in the formal accounting records, but rather were tracked informally outside MTRS's accounting system. Furthermore, these balances were not included on MTRS's financial statements filed annually with the Public Employee Retirement Administration Commission (PERAC). We recommended that MTRS take the following actions:

1. Incorporate these retirement-related accounts into its accounting system and include their balances on its financial statements reported to PERAC.

2. Prepare an aging list of all the accounts payable and remit to the Abandoned Property Division of the Office of the State Treasurer (OST) all accounts that were over three years old.
3. Prepare an aging list of all of the accounts receivable and refer all past-due accounts to the Attorney General for collection.

During our current audit, we determined that these accounts were included in MTRS's accounting system and the financial statements reported to PERAC; aging lists⁸ of individual accounts-receivable and accounts-payable balances were prepared; and MTRS maintained an Unclaimed Funds List of open accounts-payable balances. After our audit period, in June 2014, MTRS began referring unpaid accounts-receivable balances to a collection agency.

However, the aging lists were not accurately maintained, resulting in inaccurate financial statements reported to PERAC. In addition, the Unclaimed Funds List was not accurate, complete, and up to date. Without accurate aging lists, MTRS may not be collecting or otherwise resolving all funds due the Commonwealth and paying all funds owed to surviving beneficiaries. Also, without an accurate and current Unclaimed Funds List on MTRS's website, surviving beneficiaries may not be aware that MTRS has unclaimed funds on account for them. Thus there is no assurance that this list is an effective tool to communicate and resolve instances of funds owed to the public.

The specific issues we found, and the authoritative guidance applicable to all these issues, are discussed below.

Authoritative Guidance

Chapter 32, Section 20(5)(h), of the Massachusetts General Laws states,

Each board shall annually, on or before May first, file in the office of the public employee retirement administration commission the financial statement of the system. . . . The state board of retirement and the teachers' retirement board shall each file such report annually, on or before December 31, in the office of the public employee retirement administration commission which shall show the financial condition of their respective retirement system as of June 30 of the prior fiscal year.

Although MTRS has taken steps to implement our prior audit recommendations, our follow-up audit showed inaccurate recordkeeping with regard to estate accounts payable and receivable.

8. Lists of all individual balances and the length of time the amounts have been outstanding.

In addition, Chapter 32, Section 21(1)(a), of the General Laws states,

The commission shall require each board to keep in convenient form such data as is required for the purpose of valuing the assets [and] determining the liabilities of the system.

To fulfill these purposes, MTRS must ensure that the financial records used to produce these records are accurate.

a. Records for accounts payable and receivable are not accurate.

Accounts Payable

The balance for accounts payable on the June 30, 2013 financial statements was overstated by a net of \$43,396. Specifically,

- Twenty-eight individual balances, totaling \$65,633, on the accounts-payable aging list were inaccurately recorded. These balances should have been recorded as accounts receivable on the accounts-receivable aging list. As a result, the total accounts-payable balance was overstated by \$65,633.
- Ninety-seven individual balances, totaling \$10,069, on the accounts-payable aging list were inaccurately recorded as negative balances instead of positive balances. As a result, the total accounts-payable balance was understated by \$20,138.
- Eleven individual balances, totaling \$2,099, on the accounts-receivable aging list were inaccurately recorded as negative balances. These balances should have been recorded as positive balances on the accounts-payable aging list. As a result, the total accounts-payable balance was understated by \$2,099.

Accounts Receivable

The balance for accounts receivable on the June 30, 2013 financial statements was understated by \$116,980. Specifically,

- The total accounts-receivable balance of \$1,236,630 on the financial statements did not agree with the accounts-receivable aging list's total of \$1,285,878 that we were given. MTRS could not explain why there was an understatement of \$49,248 on the financial statements.
- Twenty-eight individual balances, totaling \$65,633, on the accounts-payable aging list were inaccurately recorded. These balances should have been recorded as accounts receivable on the accounts-receivable aging list. As a result, the total accounts-receivable balance was understated by \$65,633.
- Eleven individual balances, totaling \$2,099, on the accounts-receivable aging list were inaccurately recorded as negative balances. These balances should have been recorded as

positive balances on the accounts-payable aging list. As a result, the total accounts-receivable balance was understated by \$2,099.

Payable Balances

MTRS processes its pension payrolls at the end of the month for the current month. Thus, if a member dies during the month and MTRS receives notification before processing that month's payroll, the agency can cancel benefits effective on the date of death. In this case, the member's beneficiary or estate is not sent a check for that full month; rather, a pro rata check for days the member was alive during the month is owed to the beneficiary or member's estate, creating an accounts-payable balance. MTRS notifies the beneficiary of the funds owed and requests a completed claim form and a copy of a death certificate. If it cannot contact the beneficiary even after several attempts, MTRS closes the case and the balance remains outstanding and due. To help process these cases, MTRS enters these balances on an Unclaimed Funds List on its website, showing the names of former members with unclaimed funds, in the hope that their survivors and/or estates will contact the agency to claim any funds that are due.

Receivable Balances

If MTRS does not receive notification of a member's death promptly, the agency may not learn of the member's death until the member has already received a check for the full month in which the death occurred. The amount paid for the days after the member's death is therefore an overpayment, resulting in an account receivable due the Commonwealth. Since fiscal year 2014, MTRS's practice has been to send an initial billing and up to four subsequent dunning notices (demands for payment) to the administrator of the benefit recipient's estate or another contact person for the recipient. The billing and dunning notices include the amount of the debt owed and instructions on how to pay it. Since implementing these procedures, MTRS has also been contacting the Office of the State Comptroller (OSC) after sending any final notice so that OSC can initiate a state intercept⁹ and referral to a collection agency.

Reasons for Inaccurate Recordkeeping

MTRS's financial staff relied on the accuracy and completeness of the aging lists for accounts payable and receivable when preparing MTRS's financial statements. However, there was

9. Under Chapter 7A, Section 3, of the General Laws, the State Comptroller can intercept funds owed to an individual or company and apply them to funds owed to the Commonwealth.

inadequate supervisory oversight to ensure that the detailed aging lists were accurate, complete, and up to date.

b. The Unclaimed Funds List is not accurate and current.

MTRS's published list of unclaimed funds is not current, accurate, and complete. We compared the aging list of individual accounts-payable balances as of June 30, 2013 to the Unclaimed Funds List on the MTRS website as of July 8, 2014 and found the following:

- Out of 1,217 names on the accounts-payable aging list (whose individual balances totaled \$418,154), 528 were not on the Unclaimed Funds List. The majority of the missing names were relatively current: 501 names, whose balances totaled \$387,560, were from fiscal years 2011–2013.
- Out of the 733 names on the Unclaimed Funds List, 40 were not recorded on the accounts-payable aging list.

Practices for Unclaimed Funds

Although OST publishes a list of unclaimed property, it does not include MTRS's Unclaimed Funds List because of space limitations. After our previous audit, OST did agree to include a reference to MTRS's Unclaimed Funds List on its own published list, though it does not include the full list.

Reason for Inaccurate and Outdated Unclaimed Funds List

MTRS does not have supervisory oversight to ensure that the Unclaimed Funds List is accurate, complete, and up to date.

Recommendation

MTRS should implement supervisory oversight controls to ensure that individual balances on the aging lists for accounts payable and receivable are accurate and complete; that the total of the individual balances agrees with MTRS's financial-statement balances; and that the Unclaimed Funds List is accurately maintained. MTRS should update its documented policies and procedures to include these supervisory oversight controls.

Auditee's Response

With regard to the inaccurate estate accounts payable and receivable records, MTRS responded,

The MTRS disburses over \$180 million per month or \$2.2 billion in benefits each year. On average the system processes over 1,200 benefit recipient deaths per year in accordance with the benefit option selected, triggering a review of approximately \$2.7 million in benefit payments.

As noted, the MTRS has made progress on the recording and aging of our accounts receivable and payable from retiree estates. The records provided to [the State Auditor's Office, or SAO] supporting the accounts payable and receivable did not match the financial statements as there was additional activity posted in the detailed records after the date the financial statements were published. The tracking spreadsheet shared with the SAO was a working document, to which updates were made as payments were received or disbursed. A copy of the tracking spreadsheet was not preserved as of the period close for the annual financial report for PERAC, which led to the variances described in the audit report. We do agree that some of the entries were mislabeled and they have been corrected.

Corrective actions taken:

In the future the MTRS will preserve a copy of the detailed report of accounts payable/receivable as of the close of the annual financial statements. In addition, our new management information system (MyTRS) tracks the account balance receivable or payable at the member account level ensuring an exact reconciliation process going forward. Finally, to improve management oversight, the Director of Retiree Services, Director of Finance and the Compliance Officer will meet quarterly to review the estate accounts payable and receivable activity.

With regard to the inaccurate and outdated Unclaimed Funds list, MTRS stated,

While the MTRS has had a three-step procedure in place to locate and notify named beneficiaries and estates of accounts payable due to a benefit recipient's death, we agree that improvements were needed to our procedures for adding new estate accounts payable to our Unclaimed Funds list when beneficiaries and estates do not respond in a timely manner.

Corrective actions taken:

In accordance with our updated procedures, estate accounts payable are added to the Unclaimed Funds list immediately following the three-step notification process, which is generally completed within 90 days after a reported death. In addition, the Director of Retiree Services will perform quarterly audits to ensure compliance with this procedure.

Auditor's Reply

Based on its response, MTRS is taking appropriate measures to address concerns we identified.

Post-Audit Action

Chapter 447 of the Acts of 2012 (An Act Relative to the Filing of Statements of Financial Condition by Public Employee Retirement Systems) gave MTRS the authority to write off any outstanding pension payments payable or receivable that it could not resolve after three years. In November 2014, MTRS senior management recommended to its board a revised policy providing for an annual write-off of accounts receivable that are at least three years old. Management also recommended a write-off of all outstanding accounts receivable as of June 30, 2011. At the November 21, 2014 board meeting, the board approved the aforementioned policy revisions and recommended to OSC the write-off of \$1,063,412.59 in accounts receivable for the period 1988 through 2011.

APPENDIX

Massachusetts Teachers' Retirement System Information

Membership Information

	Fiscal Year 2012	Fiscal Year 2013
Active Members	85,854	86,647
Inactive Members	20,109	24,771
Retired Members, Beneficiaries, and Survivors	57,777	59,409
Total Members	<u>163,740</u>	<u>170,827</u>

General Disbursement Financial Information¹⁰

	Calendar Year 2011	Calendar Year 2012	Fiscal Year 2013
Pensions Paid (regular pension payments)	\$1,647,559,978	\$1,731,941,224	\$1,769,381,570
Annuities Paid	\$393,981,869	\$421,369,011	\$434,152,064
Expense Fund (including management fees and general and administrative expenses)	\$135,732,294	\$178,009,752	\$157,726,587

10. Disclosures of disbursements represent information reported in the Massachusetts Teachers' Retirement System Annual Statement of Financial Condition filed with Public Employee Retirement Administration Commission for fiscal year 2013 and are intended solely for informational purposes. As of June 30, 2013, the Massachusetts Teachers' Retirement System had assets totaling approximately \$22.7 billion.