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Correspondence Memorandum

Date: March 4, 2016
To: Audit Committee Members
From: Yikchau Sze, Director
Office of Internal Audit
Subject: Wisconsin Retirement System (WRS) Employer Reporting Audit

This report is for Audit Committee review and discussion. No action is required.

Attached is the WRS Employer Reporting audit report. The results of this audit have been submitted and discussed with the Office of the Secretary, Department of Employee Trust Funds (ETF).

This audit was conducted in accordance with the biennial Audit Plan for 2015-2017.

The primary focus of the audit is on whether or not employers are reporting complete and correct information to ETF for the employees whom the employers identified as WRS eligible. Based on the audit performed, the Office of Internal Audit concluded with reasonable assurance that the census data elements¹ reported by WRS employers for their eligible employees are free from material misstatement.

Although there were no significant findings, the Office of Internal Audit identified process improvement opportunities that the Division of Retirement Services and the Division of Trust Finance could implement to mitigate risks.

This audit was conducted by Mary Statz, Auditor–Advanced, who will be available at the Audit Committee meeting to answer any questions.

Attachment: WRS Employer Reporting audit report

¹ Including date of birth; date of hire; eligible compensation; class of employee (WRS category); gender; complete name and Social Security Number

Reviewed and approved by Robert J. Conlin, Secretary

Electronically Signed: 3/11/2016

Board	Mtg Date	Item #
AUD	3.24.16	5A

Office of Internal Audit

WRS Employer Reporting



March 4, 2016

Objective:

The audit objectives are to assist in identifying gaps in Wisconsin Retirement System (WRS) employer compliance in submitting complete and accurate information for eligible members (identified as eligible by the employer) as well as earnings and service reporting and to provide advice on risk mitigation and process improvements.

Scope:

The audit scope is 2014 active state and local employer reporting including the following elements¹ that impact a WRS benefit calculation: date of birth; date of hire or years of service; eligible compensation; class of employee (WRS category); and gender. Additional elements included in this audit were complete name and Social Security Number (SSN).

The primary risks associated with employer reporting are that employers will

- Exclude eligible employees
- Include ineligible employees
- Report incomplete or incorrect employee information

The Office of Internal Audit's (OIA) primary focus of the audit was on whether or not employers are reporting complete and correct employee information.

Background:

Program: The WRS is a public pension plan with multiple employers. WRS benefits and other plan provisions are established in Wis. Stat. Chapter 40. The Department of Employee Trust Funds (ETF), under the direction of the Employee Trust Funds Board, administers the WRS. The WRS is open to all Wisconsin public employers and is funded through employee and employer contributions and investment earnings. ETF's consulting actuary reviews the contribution percentages annually and makes recommendations to the Employee Trust Funds Board when change is needed. Participation is mandatory for school districts with respect to teachers, some municipalities with respect to police and firefighters (based on population), and all counties with the exception of Milwaukee County. There were 1,482 participating employers at the end of 2014. ETF's Divisions and Offices as well as ETF's consulting actuaries rely on employers providing accurate and complete information.

¹ This list includes all significant elements of census data for active, inactive, and retired employees as noted in *Single-Employer and Cost-Sharing Multiple-Employer Plans: Issues Associated with Testing Census Data in an Audit of Financial Statements*, American Institute of Certified Public Accountants, SLGEP (State and Local Government Expert Panel) Pension Whitepaper Series, February 2014

Any employee of a participating employer who is expected to work at least 1,200 hours per year (880 hours for teachers and school district educational support employees) must be covered by the WRS. Employment categories include

- General, Teachers and Educational Support Personnel
- Executive, Elected and Judges
- Protective with Social Security
- Protective without Social Security

WRS membership includes active employees, inactive participants, retirees, and beneficiaries currently receiving benefits such as disability annuitants and death benefit annuitants. At the end of 2014 there were 603,983 WRS participants including 257,255 active employees, 185,605 annuitants, and 161,123 inactive employees with deferred benefits payable.²

WRS transactions processed by ETF's Employer Services Section currently focus on three data elements for participant verification: last name, date of birth, and SSN. Chapter six of the WRS Administration Manual states that "Social Security Numbers (SSN) are used by ETF as the major identifier for participant records ... Date of birth is crucial in computing benefits and is used by ETF as the second identifier (in addition to the SSN) ..."

Employer Reporting: Employers submit monthly and periodic (also known as supplemental) reports by WRS category to ETF via the Online Network for Employers (ONE) system. The ONE system automatically calculates the contribution by category (employee and employer) when the employer completes the report. Employers have the contribution payment sent via ACH³.

Employers submit an Annual Report to ETF by January 31st which includes employees who are active, on leave of absence, on a temporary layoff, and terminated employees not previously reported during the year. The Annual Reconciliation process balances the monthly and periodic reports by category and reconciles to the employee level. ETF makes several online reports available to assist employers with annual reconciliation.

The Division of Trust Finance (DTF) creates journal entries based on the contributions reported by employers in the ONE system which feeds into the Wisconsin Employee Benefit System (WEBS). The journal entries are manually keyed into the STAR⁴ System.

² State of Wisconsin Department of Employee Trust Funds 2014 Comprehensive Annual Financial Report

³ having executed an Automated Clearing House Direct Withdrawal Authorization, ET-1734, with ETF

⁴ STAR is an acronym for "State Transforming Agency Resources," the Department of Administration's initiative to consolidate information technology systems

Benefit Calculations: How do significant elements of census data impact a WRS benefit calculation?

- Identification of the participant is verified by using SSN and date of birth
- Age is calculated by using the date of birth and impacts age reduction factors (used in annuity calculations when the participant is under the normal retirement age) and is also used to determine the minimum and normal retirement ages
- Class of employee or WRS category is used to determine the minimum and normal retirement ages
- Date of hire is used to calculate years of creditable service and to identify Wisconsin Statutes applicable to the years of service
- Eligible compensation or earnings are used to calculate the final average earnings
- Gender is used in actuarial tables to calculate the WRS contribution rates

Employer Compliance Review Program: The purpose of the Division of Retirement Services' (DRS) Compliance Review Program is to promote and document compliance with laws and regulations applicable to administration of the WRS. Compliance reviews are designed to ensure compliance pertaining to basic census data and to validate the broad range of employer reporting responsibilities including eligibility and enrollment. DRS is scheduling employers for compliance reviews on a rotating basis.

Roles and Responsibilities:

Employee Trust Funds Board

- Has general oversight of ETF
- Oversees administration of the benefit programs, including the WRS

ETF

- Administers, with the Employee Trust Funds Board, the WRS including oversight of the consulting actuary
- Collects and accounts for all monies due the trust funds including employee and employer WRS contributions
- Calculates and disburses all benefit payments from the trust funds
- Establishes the controls, systems, and procedures to ensure appropriate administration and security of the trust
- Staffs the Employer Communication Center/Employer Services Section
- Staffs the Online Network for Employers (ONE) related to enrollments, changes, contributions, and reporting including annual reconciliation
- Authors the WRS administration manual for employers
- Creates and updates informational material including forms

- Provides information to and answers inquiries from employees and employers
- Provides employer training

Employers

- Name an agent to assist in WRS administration
- Evaluate and determine WRS eligibility
- Enroll eligible employees in the WRS thus creating a participant account at ETF
- Inform employees and distribute materials
- Report service and earnings to ETF monthly (by WRS category) and reconcile annually (by employee)
- Deduct employee WRS contributions from payroll and remit to ETF
- Remit the employer WRS contribution to ETF

Conclusion:

OIA attained an understanding of the processes and controls used by ETF management to support the completeness and accuracy of census data reported by employers and subsequently used by ETF staff in benefit calculations and provided to the actuaries. OIA did not discover any material findings in the test sample related to the census data submitted by employers for WRS eligible employees. Therefore, OIA concluded the following as it relates to employer identified WRS eligible employees

- Likelihood of misstatement is minimal
- Impact of any potential misstatement of census data impacting financial reporting is minimal

Refer to the chart on page seven for sample error rates.

OIA suggests the following recommendations to improve processes and mitigate risk.

Recommendations and Management Response:

Recommendations for DRS

1. Expand the Employer Compliance Review Program to include
 - a. Hours
 - b. Payroll screen shots
 - c. Verification of completeness of WRS reporting by testing sample ineligible employees on an employer's payroll
2. Follow-up with employers who routinely report and/or pay late and provide education and/or training

3. Educate employers on sending confidential and personally identifiable information securely (32 employer responses were not sent securely; 3% of test population)
4. Collect WRS earnings and hours at the employee level more frequently than on an annual basis.

OIA understands that the Benefit Administration System (BAS) Rollout 2 (scheduled for 1/1/2018) will require employers to submit all payroll information on WRS eligible and non-eligible participants by payroll cycle. Rollout 2 will also alert ETF to monthly variances based on a threshold established by ETF as well as match key demographic data with external databases.

Management Response from DRS

1. DRS supports the recommendation to verify employee hours worked during DRS' employer compliance review. However, doing so will either require additional resources or we will need to reallocate resources. DRS only has two employees working on the employer compliance review and both have other duties, such as testing for the Benefit Administration System (BAS) and updating the employer manuals. Verifying hours is an important factor used to determine creditable service and benefits. Therefore, to implement this recommendation, DRS intends to scale back the 2015-2019 strategic initiative to expand the number of employers that would be reviewed on an annual basis. Instead of expanding the number of employers reviewed each year, DRS will broaden its review to include a sampling to verify employee hours. In addition, DRS will include more samples of payroll screen shots for applicable employers.

Responsible staff: Jeff Miller
Completion time: second quarter 2016

DRS agrees with the recommendation to review employer reports to determine employee eligibility for the WRS. This will be addressed by the BAS implementation, in particular Rollout 2. ETF will ask employers to submit data for all their employees, not just WRS eligible employees. Prior to the implementation of BAS Rollout 2, DRS will add a requirement to the Employer Compliance Review Program that employers submit a sample of ineligible employees for review by ETF staff.

Responsible staff: Jeff Miller
Completion time: second quarter 2016

2. DRS does take into account the employers that make continual reporting errors and struggle with timeliness when determining what employers to review as part of the employer compliance program. However, we try to balance the review of employers who

are frequently late with our intent to keep some of the selection of employers random. DRS agrees with the recommendation to provide more training and education to employers that frequently make errors. The DRS Employer Services Section case managers will follow-up with the employers identified by this audit, the monthly remittance report tracking sheet and staff. The follow-up will serve as an opportunity to educate the employer(s) and answer any questions they have.

Responsible staff: Kathy Wienkes
Completion time: 5/1/2016

3. DRS will work with the Office of Policy, Privacy and Compliance to communicate privacy risks and tips to employers.

Responsible staff: Matt Stohr
Completion time: Next 2016 Employer Bulletin

4. The BAS will require employers to submit payroll data on a monthly basis. Under current ETF policy, employers are required to submit a file with employee data annually.

Responsible staff: Matt Stohr
Completion time: 1/1/2018

Recommendation for DTF

Charge interest when employers do not report earnings and contributions timely. At present interest is charged for not submitting a monthly remittance report. An employer can submit a monthly report with or without reporting earnings and with or without paying associated contributions without any interest charged.

OIA understands that BAS Rollout 2 will eliminate this scenario as employers will be submitting payroll information every payroll cycle and providing a Work Report with earnings and contributions specific to each employee for each payroll cycle.

Management Response from DTF

The existing policy on charging interest dates back to the 1980's when the WEBS Employer Remittance System was designed and developed. At that time contributions were paid by a check accompanying the monthly report. It was unusual for a monthly report not to include a check, and normally for the correct amount. In that environment it made sense to simplify system design by freezing interest assessments at the time a report was received.

With the more sophisticated systems available today, it now makes sense to assess interest on all amounts due from the due date until paid. The BAS system is being designed to assess interest on any amounts due, including late reports, partial payments and missing reports. This will ensure the trust is fully compensated for payments not received timely.

Our analysis shows that the foregone interest on underpayments is negligible and has no measureable financial impact on the retirement system. Given the imminence of BAS, and the difficulty of reprogramming the existing employer reporting system, it is not feasible to implement the recommendation at this time. The recommendation will be fully incorporated in the BAS when implemented in 2018.

Responsible staff: Laura Vang
Completion time: 1/1/2018

The remainder of the report provides more detailed information about the audit procedures and testing results.

Employees active in 2014 were divided into four pools for testing:

- University of Wisconsin (excluding Protective)
- School Districts
- Protective
- All Other (state and local excluding Protective)

Test samples were randomly selected using a confidence level of 95% coupled with a 5% margin of error for each sample population with ACL data analytics software.

		NOTED EXCEPTIONS					
		Earnings		Name		Other	
Sample Pool	Sample/ Population	Variance	Sample error rate	Variance	Sample error rate	Variance	Sample error rate
UW	380/32,357	10 (all reported)	2.6%	7 (all resolved)	1.8%	1 date of birth (resolved)	
School Districts	383/111,482	9 (8 reported)	2.3%	8 (5 resolved)	2.1%	1 gender (resolved)	
Protectives	378/23,249	8 (all reported)	2.1%	4 (all resolved)	1.1%	none	
All Other	383/122,211	2 (1 reported)	0.5%	5 (all resolved)	1.3%	none	
TOTAL	1,524/289,299	29 (27 reported)	1.9% with 93% due to timing	24 (21 resolved)	1.57%	2	0.1%

School Districts

Unreported Earnings: waiting for one school district to respond regarding a \$620 variance which represents 1.8% of 2014 earnings for that employee per the employer

Unresolved Name: one school district acknowledges the payroll system should reflect the legal name; two are no longer active employees with the 2014 school district employer

All Other

Unreported Earnings: one employer has not responded regarding a \$1,713.42 variance which represents 3.8% of 2014 earnings for that employee per the employer

Earnings variances observed as late reported earnings included contract settlements and position/category changes. Employer approval delays led to the 2014 earnings being reported late. Name variances reflect employees who changed their name and the change was not reported to ETF. Please note that there are name variances not included in the chart above such as suffixes, middle names/initials, and first names (Steve versus Steven). The Wisconsin Employee Benefit System (WEBS) does not have field space for suffixes or middle initials. BAS will accommodate these fields.

Other variances included the following:

- The WRS Enrollment form (ET-2316) was submitted twice for an employee with female checked on one form and male checked on the other
- One employer made a keying error when entering an employee's date of birth
- One employer entered an employee's name incorrectly in the ONE system

OIA found variances with date of hire. There are valid reasons for the current WRS employer's payroll system to not have the original WRS eligibility date including:

- Current employer was not the first WRS employer (for example, a state employee who has worked for multiple agencies)
- Initial position with the current employer was not WRS eligible (for example, a Limited Term Employee)
- Employer's payroll system may capture a hire date when a contract was signed, but WRS earnings do not begin until a future date (for example, a teacher signs a contract in June and school does not begin until September)
- Employee received a separation benefit

Any questions regarding the WRS eligibility date/date of hire are addressed when a benefit is being calculated.

Employer payroll systems do not all capture the WRS category, gender, complete SSN, or allow for a name suffix. A few employers were in the midst of a system conversion and had limited access to 2014 data and were not able to provide all requested information in screen shot format.

One employer refused to provide the requested information from the payroll system.

The audit was conducted on site with the employer's payroll staff for Madison based employers including the University of Wisconsin. Employers outside of Madison were asked to securely submit payroll screen shots with the requested census data elements.

Although hours of service were not specifically requested from employers as part of this audit, many employers provided it. Therefore, hours of service for 20 school district employees were reviewed and no variances were found. Hours of service for 20 protectives were also reviewed. Variances were observed and the sample size was expanded to 50 with three variances found. One employer did not include holiday hours for protective employees. Once discovered, the employer corrected the 2014 hours for 23 employees totaling 1,692 more hours with an overall average increase of 73.5 hours per employee. The other employer with hour variances for two employees did not respond to requests for additional information.