



A Report on

The Audit of the Teacher Retirement System's Fiscal Year 2015 Financial Statements

John Keel, CPA

December 1, 2015

Members of the Legislative Audit Committee:

In our audit report dated November 18, 2015, we concluded that the Teacher Retirement System's (System) basic financial statements for fiscal year 2015 were materially correct and presented in accordance with accounting principles generally accepted in the United States of America. The System published our audit report as part of its basic financial statements, which it posted on its Web site at http://trs.texas.gov/global.jsp?page_id=/global/publications_all.

We also issued a report on internal control over financial reporting and on compliance and other matters as required by auditing standards (that report, including responses from management, is presented in the attachment to this letter). In that report, auditors determined that the System should strengthen controls over plan member census data to help ensure that data is complete and accurate.

Our procedures were not intended to provide an opinion on internal control over financial reporting or to provide an opinion on compliance with laws and regulations. Accordingly, we do not express an opinion on the effectiveness of the System's internal control over financial reporting or on compliance with laws and regulations.

Subsequent to the issuance date of the System's fiscal year 2015 financial statements, the System formed a private limited company, which will be wholly owned by the System, in the United Kingdom for the purpose of opening a London investment office that was expected to be operational in November 2015.

Testing of Plan Member Census Data

Auditors conducted census data testing for fiscal year 2015 (see text box for the key data elements tested) as part of this audit. The completeness and accuracy of that data is important because the System's actuary uses that data to calculate the System's pension liability.

Auditors implemented a risk-based approach for selecting employers (including school districts, charter schools, education service centers, and higher education institutions) for fiscal year 2015 census data testing as required by American Institute of Certified Public Accountants (AICPA) guidance. That resulted in auditors selecting 89 employers for which census data was tested. (A list of the employers selected for testing is presented in the attachment to this letter.) Testing included reviewing documentation to verify that the census data that the employers submitted to the System was accurate.

Census Data Tested

Census data is key demographic data that affects the actuarial estimate of the pension liability amount that the System presents in the notes to its financial statements.

Auditors identified and tested the following key data elements for the System's census data:

- Name.
- Date of birth.
- Years of service.
- Eligible compensation.
- Gender.
- Employment Status.

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Based on the testing performed, auditors determined that the underlying census data was materially complete and accurate to support the System's plan's financial statement amounts. That was reflected as part of our unmodified audit opinion on the System's financial statements for fiscal year 2015. For fiscal year 2014, auditors tested the System's census data using the same methodology described above and concluded that the data was materially complete and accurate. The System intends to post the results of the census data testing for fiscal year 2014 on its Web site at <http://trs.texas.gov>.

Additionally, auditors will be issuing an opinion later this fiscal year on the System's fiscal year 2015 pension liability allocation schedules. Those schedules provide employers with the information they need to record their share of the pension liability in their financial statements, in accordance with AICPA requirements. Auditors previously issued an opinion on the System's pension liability allocation schedules for fiscal year 2014. The System published our audit report, along with the schedules, on its Web site at http://www.trs.state.tx.us/employers.jsp?submenu=gasb&page_id=/reporting/gasb_67_68.

Other Issues

Auditors communicated certain issues that were not material or significant to the audit objectives in writing to the System's management.

As required by auditing standards, we will also communicate to the System's board of trustees certain matters related to the conduct of a financial statement audit.

We appreciate the System's cooperation during this audit. If you have any questions, please contact Angelica Ramirez, Audit Manager, or me at (512) 936-9500.

Sincerely,

Lisa R. Collier, CPA, CIDA
First Assistant State Auditor

Attachment

cc: The Honorable Greg Abbott, Governor
Members of the Teacher Retirement System Board of Trustees
Mr. R. David Kelly, Chairman
Ms. Nanette Sissney, Vice Chair
Mr. Todd Barth
Ms. T. Karen Charleston
Mr. Joe Colonna
Mr. David Corpus
Mr. Christopher Moss
Ms. Anita Smith Palmer
Ms. Dolores Ramirez
Mr. Brian Guthrie, Executive Director, Teacher Retirement System



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Attachment

Section 1

List of Employers Selected for Census Data Testing

Table 1 lists the 89 employers for which auditors tested the accuracy of census data to determine whether that data was materially complete and accurate to support the Teacher Retirement System’s plan’s financial statement amounts.¹

Table 1

List of Employers Selected for Census Data Testing for Fiscal Year 2015
<ul style="list-style-type: none">▪ Abilene Independent School District▪ Alamo Community College District▪ Alief Independent School District▪ Allen Independent School District▪ Alvin Independent School District▪ Amarillo College▪ Angelo State University▪ Angleton Independent School District▪ Arlington Independent School District▪ Atlanta Independent School District▪ Barbers Hill Independent School District▪ Beaumont Independent School District▪ Ben Bolt-Palito Blanco Independent School District▪ Brazosport College▪ Bryan Independent School District▪ Burnet Consolidated Independent School District▪ Canyon Independent School District▪ Chapel Hill Independent School District▪ Clint Independent School District▪ Coahoma Independent School District▪ College of the Mainland▪ Coppell Independent School District▪ Copperas Cove Independent School District▪ Corsicana Independent School District▪ Dallas Independent School District▪ Dickinson Independent School District▪ Dilley Independent School District▪ Donna Independent School District▪ Dumas Independent School District▪ Eagle Pass Independent School District▪ Eanes Independent School District

¹ Auditors followed the American Institute of Certified Public Accountants’ sampling guide methodology and selected a representative population of employees from each employer selected for testing.

**List of Employers Selected for Census Data Testing
for Fiscal Year 2015**

- El Paso Community College
- Ennis Independent School District
- Fort Worth Independent School District
- Galveston College
- Galveston Independent School District
- Grand Prairie Independent School District
- Grapevine Colleyville Independent School District
- Harlingen Consolidated Independent School District
- Henderson Independent School District
- Hidalgo Independent School District
- Houston Independent School District
- IDEA Public Schools
- Kennedale Independent School District
- Kerrville Independent School District
- Laredo Community College
- Laredo Independent School District
- Longview Independent School District
- Los Fresnos Consolidated Independent School District
- Lubbock Independent School District
- Lufkin Independent School District
- Marshall Independent School District
- McAllen Independent School District
- Mercedes Independent School District
- Midland College
- Midland Independent School District
- Midlothian Independent School District
- Nacogdoches Independent School District
- Navarro College
- Needville Independent School District
- Northside Independent School District
- Odessa College
- Paradise Independent School District
- Plainview Independent School District
- Reagan County Independent School District
- Region 7 Education Service Center
- Robstown Independent School District
- Roma Independent School District
- San Antonio Independent School District
- San Benito Consolidated Independent School District
- Sharyland Independent School District
- South Plains College
- South Texas College
- Spearman Independent School District
- Spring Branch Independent School District
- Spring Independent School District
- Stephen F. Austin State University
- Texarkana College

**List of Employers Selected for Census Data Testing
for Fiscal Year 2015**

- Texarkana Independent School District
- The University of Texas at Austin
- The University of Texas M.D. Anderson Cancer Center
- The University of Texas Medical Branch at Galveston
- The University of Texas Southwestern Medical Center
- Uvalde Consolidated Independent School District
- Victoria College
- Weatherford College
- Weslaco Independent School District
- Wichita Falls Independent School District
- Wylie Independent School District

Report on Internal Control Over Financial Reporting and on Compliance and Other Matters as Required by Auditing Standards



Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with Government Auditing Standards

Independent Auditor's Report

Teacher Retirement System Board of Trustees

Mr. R. David Kelly, Chairman
Ms. Nanette Sissney, Vice Chair
Mr. Todd Barth
Ms. T. Karen Charleston
Mr. Joe Colonna
Mr. David Corpus
Mr. Christopher Moss
Ms. Anita Smith Palmer
Ms. Dolores Ramirez

We have audited, in accordance with the 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 the United States, the financial statements of the major enterprise fund and the aggregate remaining funds information, consisting of the fiduciary funds and the non-major enterprise fund of the Teacher Retirement System (System) as of and for the year ended August 31, 2015, and the related notes to the financial statements, which collectively comprise the System's basic financial statements and have issued our report thereon dated November 18, 2015.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered the System's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the System's internal control. Accordingly, we do not express an opinion on the effectiveness of the System'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, or 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 entity's financial statements will not be prevented, or detected and corrected on a timely basis. 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.

SAO Report No. 16-304

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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 or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. We did identify certain deficiencies in internal control described in the accompanying schedule of findings and responses that we consider to be a significant deficiency.

Summary of Findings and Responses
Finding Number
2015-1

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the System's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement 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*.

Auditors communicated certain issues that were not material or significant to the audit objectives in writing to the System's management.

The System's Response to Findings

The System's response to the finding identified in our audit is described in the accompanying schedule of findings and responses. The System's response was not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on it.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control over financial reporting or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control over financial reporting and compliance. Accordingly, this communication is not suitable for any other purpose.

Lisa R. Collier, CPA, CIDA
First Assistant State Auditor

November 18, 2015

Schedule of Findings and Responses

Section 1

The System Should Strengthen Controls to Help Ensure the Completeness and Accuracy of the Active Employee Census Data That Employers Submit

Reference No. 2015-1

Type of finding: Significant Deficiency

The Teacher Retirement System (System) should strengthen controls over active employee census data to help ensure that data is complete and accurate (see text box for additional information). More than 1,300 school districts, colleges, and universities submit active employee census data regarding the active members who participate in the System's pension plan. The completeness and accuracy of that data is important because the System uses that data to calculate member pension benefits and the pension liability amount that the System presents in its financial statements. Auditors previously reported this finding during the audit of the System's fiscal year 2014 financial statements.¹

Active Employee Census Data

Active employee census data is key demographic data that affects the actuarial estimate of the pension liability amount that the System presents in its financial statements.

Key data elements include:

- Gender.
- Date of birth.
- Salary.
- Years of service.

Source: American Institute of Certified Public Accountants February 2014 white paper entitled *Single-Employer and Cost-Sharing Multiple-Employer Plans: Issues Associated with Testing Census Data in an Audit of Financial Statements*.

The System's controls over active employee census data are not sufficient to properly identify data that is incomplete or inaccurate. The absence of effective management processes and controls represents a deficiency in internal control over financial reporting, as noted in the guidance that the American Institute of Certified Public Accountants (AICPA) issued in a February 2014 white paper.²

Auditors tested census data at 89 school districts, colleges, and universities. The majority of that data was accurate, and auditors identified no systematic issues. However, strengthening controls at the System would:

- Help to ensure that data is complete and accurate.
- Help to ensure that school districts, colleges, and universities are fully and accurately reporting that data.

¹ See *A Report on the Audit of the Teacher Retirement System's Fiscal Year 2014 Financial Statements* (State Auditor's Office Report No. 15-010, November 2014).

² The AICPA's white paper is entitled *Single-Employer and Cost-Sharing Multiple-Employer Plans: Issues Associated with Testing Census Data in an Audit of Financial Statements*.

- Improve the quality of the data that the System provides to its actuary to calculate the pension liability amount presented in the System's financial statements.

Examples of ways in which the System could strengthen controls over active employee census data include:

- Performing periodic site visits at employers to verify active employee census data.
- Providing employers with training or guidance on capturing active employee census data.
- Requiring school districts to periodically test the active employee census data and to certify the completeness and accuracy of that data when they submit that data to the System.

Recommendation

The System should develop and implement a process to strengthen controls over active employee census data.

Management's Response

TRS is undertaking a modernization effort of its pension administration system that will, among other things, help strengthen controls over active employee census data to ensure its accuracy and completeness through additional data elements and stronger validations. The new pension administration system is expected to go live in FY 2017. TRS Staff is currently beginning the User Acceptance Testing for Phase 1A Employer Certification. Beginning late February 2016 TRS will begin Employer Training on the new Pension Line of Business. Those sessions will be conducted throughout the state at the Region Service Centers in addition to TRS Headquarters. Once the training is complete we will begin the Employer Certification where the Reporting Entities will submit their reports using the new employer portal for the Pension Line of Business System through a test environment.

TRS Reporting Entity Coaches conducted their FY 2016 fall workshops for employer reporting officials at the twenty Education Service Centers. This training consisted of reviewing the reporting requirements and any new legislative or rule changes. The Coaches have also provided additional follow up training as requested by attendees at the sessions.

TRS staff is also heavily involved in the Data Management Project that is identifying missing employee census data. The data conditioning portion of that project is working through the missing data elements and using various methods to identify and locate the missing data by using Lexis Nexis software and our actuaries' software to identify information on members based on tax identification numbers. The TRS staff is then correcting or adding the missing information to the employee data file.

TRS Internal Audit staff will continue testing employer census data and controls in FY 2016 pertaining to the census data reporting process for active members. TRS is auditing the following elements of the data: gender; dates of birth; dates of hire or years of service; eligible compensation; and termination or retirement dates. TRS internal auditors are also testing eligibility and compensation for accuracy, completeness, and compliance with TRS Laws & Rules. Employer self-audit tools are available on the TRS website. These tools provide specific how-to instructions and guidelines for conducting a self-audit of the data and contributions of various reports submitted to TRS.

All processes described above are being implemented and are ongoing processes with the exception of the new pension line of business which will be implemented for active membership September 2016 with the full implementation of the pension line of business scheduled for May 2018.