January 28, 2009

Members of the Legislative Audit Committee:

In our audit report dated December 19, 2008, we concluded that the Office of the Fire Fighters’ Pension Commissioner’s (Office) basic financial statements for fiscal year 2008 were materially correct and presented in accordance with accounting principles generally accepted in the United States of America.

We also issued a report on internal control over financial reporting and on compliance and other matters as required by auditing standards. Our procedures were not intended to provide an opinion on internal control over financial reporting or to provide an opinion on other laws and regulations. Our procedures did not identify any instances of noncompliance that materially affected the financial statements.

As required by professional auditing standards, we will also communicate the results of the audit and certain matters related to the conduct of a financial statement audit to the Audit Committee of the Texas Emergency Services Retirement System’s (System) Board of Trustees.

Actuarial Funding Status

Conducting our audit of the Office’s financial statements enabled us to obtain information on the actuarial funding status of the System’s pension plan. The actuarial valuation was as of August 31, 2008.

The primary change that occurred in the System since the prior biennial actuarial valuation as of August 31, 2006, was the State’s appropriation of $8,800,000 to the System in September 2007. This contribution was significantly more than the maximum state contribution expected in accordance with Texas Government Code, Section 865.015, governing the System (“...the state’s contribution may not exceed one-third of the total of all contributions by governing bodies in a particular year”). The amounts originally requested for the biennium from September 1, 2007, through August 31, 2009, were $794,905 for the first fiscal year and $838,149 for the second fiscal year. Primarily as a result of the $8,800,000 appropriation, the actuarial valuation indicated that the System has:

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1 For additional information about the System’s actuarial funding status and subsequent events, see Texas Emergency Services Retirement Actuarial Valuation as of August 31, 2008 by Rudd and Wisdom, Inc. at http://www.ffpc.state.tx.us/tesrs/publications/2008%20final%20val%20report.pdf.

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- An adequate contribution arrangement with the expected contributions from the governing body of each participating department.

- Approximately $425,000 each year from state appropriations to help pay for the System’s administrative expenses, but without any future maximum annual contributions from the State.

Subsequent Events

Since the August 31, 2008, actuarial valuation date, the national and global economies have worsened, and the domestic and international equity markets have dropped significantly. In the two months between the valuation date and October 31, 2008, the market value of the System’s net assets dropped from $56 million to $44 million. Markets dropped further in November 2008, and there are uncertainties about how and when the national and global economies will recover.

The System has an adequate contribution arrangement with the expected contributions from the governing body of each participating department, assuming that the State will continue to appropriate (1) the maximum annual contribution as needed in accordance with the state law governing the System and (2) approximately $425,000 each year to pay for a portion of the System’s administrative expenses. Without these expected appropriations from the State, the System would have an inadequate contribution arrangement because of the significant decrease in the System’s assets in the two months immediately following the August 31, 2008, valuation date. Table 1 lists additional information related to the System’s actuarial valuations.

Table 1

<table>
<thead>
<tr>
<th>Selected Information from Actuarial Valuations of the Texas Emergency Services Retirement System</th>
<th>As of August 31, 2006</th>
<th>As of August 31, 2008</th>
</tr>
</thead>
<tbody>
<tr>
<td>Information Related to Unfunded Actuarial Accrued Liability</td>
<td>$58,082,828</td>
<td>$64,227,341</td>
</tr>
<tr>
<td>Actuarial Accrued Liability</td>
<td>$42,268,305</td>
<td>$60,987,157</td>
</tr>
<tr>
<td>Actuarial Value of Assets (excludes unrecognized investment gains and losses)</td>
<td>$15,814,523</td>
<td>$3,240,184</td>
</tr>
<tr>
<td>Unfunded Actuarial Accrued Liability (UAAL)</td>
<td>$8,853,211</td>
<td>$0</td>
</tr>
<tr>
<td>Present Value of Maximum State Contributions</td>
<td>$8,143,105</td>
<td>$3,682,061</td>
</tr>
<tr>
<td>Adjusted UAAL</td>
<td>$8,143,105</td>
<td>$3,682,061</td>
</tr>
</tbody>
</table>

Information Related to Projected Contributions

| Required Annual Contributions to Fund Normal Costs | $1,856,675 | $1,887,720 |
| Expected Annual Contributions | $2,553,216 | $2,692,680 |
| Annual Amount Available to Amortize the Adjusted UAAL | $696,541 | $804,960 |
| Years to Amortize the Adjusted UAAL | 30 | 6 |

Implementation of Prior Year Recommendations

The Office has fully implemented recommendations included in *A Report on the Audit of the Office of the Fire Fighters’ Pension Commissioner’s Fiscal Year 2007 Financial Statements* (State Auditor’s Office Report No. 08-019, January 2008). Table 2 lists the implementation status of each prior year recommendation.

Table 2

<table>
<thead>
<tr>
<th>Recommendation</th>
<th>Status</th>
</tr>
</thead>
<tbody>
<tr>
<td>The Office should ensure that all reconciliations are performed and documented within a reasonable amount of time after the end of each month.</td>
<td>Implemented. The System’s Board of Trustees approved accounting policies and procedures in May 2008 that require the Office to complete monthly reconciliations and that each reconciliation be completed before the end of the following month. Auditors selected and reviewed a reconciliation and confirmed that it was performed within the required time frame.</td>
</tr>
<tr>
<td>The Office should ensure that transactions are recorded in the accounting systems on a timely basis and are posted to the month in which they occur.</td>
<td>Implemented. As a result of completing monthly reconciliations, transactions are being posted to the month in which they occur.</td>
</tr>
<tr>
<td>The Office should ensure that management-level reviews of all reconciliations are performed and documented.</td>
<td>Implemented. During review of a selected monthly reconciliation, auditors determined that a management-level review was performed and documented on a timely basis.</td>
</tr>
</tbody>
</table>

If you have any questions, please contact Lisa Collier, Assistant State Auditor, or me at (512) 936-9500.

Sincerely,

John Keel, CPA
State Auditor

cc: Members of the Texas Emergency Services Retirement System Board of Trustees
    Mr. Frank Torres, Chairman
    Mr. Kyle A. Donaldson
    Ms. Gracie G. Flores
    Mr. Patrick Hull
    Mr. Dan Key
    Mr. Rex W. Klesel
    Mr. Ron Larson
    Mr. Maxie L. Patterson
    Mr. Don Shipman
    Ms. Lisa Ivie Miller, Commissioner, Office of the Fire Fighters’ Pension Commissioner