

MINUTES OF THE AUDIT & COMPLIANCE COMMITTEE MEETING
October 30, 2018

Members Present:

David Morris, Vice Chairperson
Loren Iglarsh, SERS Retiree

Members Absent:

Shaun Dawson, SERS Trustee

Others in attendance:

Tim Blair, Executive Secretary
Casey Evans, Chief Internal Auditor (CIA)

The SERS Audit and Compliance Committee convened on Tuesday, October 30, 2018 at 9:00 a.m. in the System's Springfield office. The meeting was called to order at 9:00 a.m. with a quorum being established to conduct business.

Seeing that there were no members of the public present for comment, the Committee moved on to the review and approval of the July 24, 2018 Committee meeting minutes. With there being no revisions to the meeting minutes, Retiree Iglarsh moved to approve the minutes as presented and Vice Chairperson Morris seconded the motion. The meeting minutes were approved.

Vice Chairperson Morris turned the meeting over to Chief Internal Auditor (CIA) Evans to discuss internal audit reports and other activities. CIA Evans directed the Committee to the FY2018 Year End Audit Report and explained that this is a statutorily mandated report required by the Fiscal Control and Internal Auditing Act that essentially highlight the internal audit work performed during the previous fiscal year. Several of the audits were discussed in detail with background being given on various audit findings, risks, and internal controls examined in these audits.

The Committee discussed the FY2019 retirement eligibility audits. It was explained that while the auditors routinely test benefits and substantiate retirement eligibility, they had not performed this type of testing on a much larger scale. During this project, the auditors used retirement data to design formulas to look for members who based on their age and service credit at time of retirement did not appear to be eligible for a retirement benefit. It was explained that by using the data, the auditors judgmentally sampled 83 member accounts and found no issues. Several false positives were found in the auditor's analysis which was attributed to two distinct benefit scenarios.

First, several members in the sample chose to retire with a reduced retirement benefit. CIA Evans explained that under Section 107 of Article 14 of the Pension Code, members that have between 25 and 30 years of service and are between the age of 55 and 60 may choose to retire early with a reduction of their retirement benefit. This reduction is one-half of one percent for each month the member is under the age of 60.

In addition, members may also retire early from non-occupational disability when the member has met the maximum period of disability and is still disabled. To be eligible, the member must have 15 years or more of service and be at least age 55 or the member must be over age 50 and have 20 years of service credit. Members can also retire from occupational disability when disability benefits cease due to reaching the maximum period of disability and the member is found to still be disabled from performing their job duties.

The Committee discussed the tier determination audit that was recently completed. Similar to the retirement eligibility project, the auditors obtained member data and developed formulas to search for members that may be incorrectly coded with the wrong retirement tier. This was performed by comparing the membership date and the tier indicator to develop potential mismatches which could be indicative of a tier determination error. Once a population was obtained and the formulas were applied, the auditors then judgmentally sampled member accounts to determine if any tier determination issues existed.

In review of over 300 member accounts in which membership dates did not correspond with the retirement tier indicator, no errors were found. CIA Evans explained that this analysis also yielded several false positives in which the member appeared to be a Tier 2 member but in fact was a Tier 1 member. Several of these false positives were attributed to a lack of a reciprocal membership date. In these cases, the retirement system knew the member had participated in a reciprocal fund but did not have their earliest membership date from that participating fund. If the auditors had this information, the formulas utilized could have been revised to take this into account and possibly avoid the false positives.

Further, the auditors found several members that appeared to be a Tier 2 member based upon their membership date, however they were found to be a Tier 1 member that had separated from the State, received a contribution refund, and subsequently re-entered State service. It was explained that if a Tier 1 member receives a termination refund and then re-enters service after the Tier 2 implementation date, he or she would retain their Tier 1 status regardless of the repayment of the refund.

The Committee discussed recent and on-going disability investigations. CIA Evans explained that the updating of the semi-annual disability form in 2016 has been a great improvement as it allows for the retirement system to monitor whether disability recipients are currently self-employed or working and may not be eligible for benefits. One issue that the retirement system has been encountering as of late is members falsifying or omitting their employment information in an effort to maintain benefits. It was explained that along with the disability medical report, the disability certification is a key eligibility document that the retirement

system utilizes to determine if members should continue to receive disability benefits. CIA Evans stated that when members falsify or materially omit information on these forms, this could be considered a fraudulent act in an attempt to receive monies that otherwise may not have been paid. CIA Evans noted that by administrative rule, members on disability may earn \$2,490 per calendar quarter to remain eligible for benefits.

Recently the retirement system staff has found, typically through the receipt of tips, members receiving disability benefits that are currently self-employed and have not disclosed their employment activity on their disability certification forms. These members will be discussed during the Executive Committee for disposition on how to proceed in the investigation or possible suspension of benefits. In addition, CIA Evans noted one case was forwarded to the State Police for further investigation of a forged medical report. The committee discussed at length current disability cases, internal procedures, and schemes encountered.

CIA Evans stated that the external audit began in early June and the RSM auditors are expected to wrap-up their on-site work in late November. A more detailed report will be given to the Committee in January for the financial audit and later in April for the compliance examination once the results of the audit are available.

The Committee moved on to discuss old and new business. CIA Evans stated that Ms. Cabey-Kaufmann, Internal Auditor 1, had separated from the retirement system to take a promotional opportunity at the Illinois Department of Transportation effective October 1, 2018. It was noted that the vacancy would be filled in the near future and that the position had already been posted on the State's employment website. Several candidates have already applied for this position. The group discussed the number of internal auditors within the peer public pension systems. CIA Evans stated that both the Teacher's Retirement System and State Universities Retirement System has three internal auditors. It was noted that both funds are larger than SERS and are more complex in the fact that these peer systems manage investments internally, so their internal auditors are responsible for performing a number of investment audits. Two full-time audit staff appears to be sufficient for the SERS internal auditors to accomplish their statutory and risk-based audits each fiscal year.

CIA Evans then directed the Committee to the tentative calendar year 2019 Audit and Compliance Committee Meeting Schedule. It was noted that the meetings would continue to be on the morning of each quarterly board meeting at 9:00 a.m. In calendar year 2019, the committee will meet on January 15th, April 30th, June 25th, and October 29th.

Retiree Iglarsh moved to adjourn the meeting with the motion seconded by Chairman Morris. The meeting was adjourned at 9:55 a.m. ahead of the Board of Trustees quarterly meeting. The next scheduled meeting for the Audit and Compliance Committee will be Tuesday, January 15, 2019 at 9:00 a.m.