New Jersey State Legislature
Office of Legislative Services
Office of the State Auditor

Department of the Treasury
Division of Pensions and Benefits
Selected Pension Services

July 1, 2009 to February 24, 2012

Stephen M. Eells
State Auditor

New Jersey State Legislature

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The Honorable Stephen M. Sweeney
President of the Senate

The Honorable Sheila Y. Oliver
Speaker of the General Assembly

Mr. Albert Porroni
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Enclosed is our report on the audit of the Department of the Treasury, Division of Pensions and Benefits, Selected Pension Services for the period of July 1, 2009 to February 24, 2012. If you would like a personal briefing, please call me at (609) 847-3470.

Stephen M. Eells

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State Auditor
May 22, 2012

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Scope

We have completed an audit of the Department of the Treasury, Division of Pensions and Benefits, Selected Pension Services for the period July 1, 2009 to February 24, 2012. Our audit included financial activities accounted for in the various pension systems. The scope of our audit included the following areas.

- Pension benefit calculations
- Unpaid loans at retirement
- Post-retirement employment
- Payments made to deceased retirees
- Information technology security access

Expenditures of the pension trust funds during fiscal year 2011 were $7.6 billion. The primary responsibilities of the division are the administrative functions of the pension trust funds except for the investment of assets which is handled by the Division of Investments. The pension funds' financial statements are audited annually by an independent accounting firm.

Objectives

The objectives of our audit were to determine the accuracy of the pension benefit calculations and the adequacy of security measures in place to protect personal and confidential information maintained by the division. We also tested for resolution of the significant conditions noted in our prior report. These included the collection of outstanding pension loans, the prevention and collection of overpayments made to deceased retirees, and the monitoring of post-retirement employment.

This audit was conducted pursuant to the State Auditor's responsibilities as set forth in Article VII, Section I, Paragraph 6 of the State Constitution and Title 52 of the New Jersey Statutes.

Methodology

Our audit was conducted in accordance with *Government Auditing Standards*, issued by the Comptroller General of the United States.

In preparation for our testing, we studied legislation, the administrative code, circular letters promulgated by the Department of the Treasury, and policies of the division. Provisions we considered significant were documented and compliance with those requirements was verified by interview, observation, and through our testing of financial transactions. We also interviewed division personnel to obtain an understanding of the programs and the internal controls.

Statistical and nonstatistical sampling approaches were used. Our samples of financial transactions were designed to provide conclusions about the validity of transactions, as well as internal control and compliance attributes. Sample populations were sorted and transactions were randomly and judgmentally selected for testing.

To ascertain the status of significant findings included in our prior report dated April 6, 2004, we identified corrective action taken by the division and walked through the system and performed testing to determine if the corrective action was effective.

Conclusions

We found that pension benefit calculations were accurate and controls over security of personal and confidential information were adequate. We also found the division has complied with our prior audit recommendations pertaining to multiple employer pension calculations and post-retirement employment. However, although we found the division has complied with the prevention aspect of overpayments made to deceased retirees, it still needs to improve its collection efforts. In addition, the division has not resolved the issue regarding unpaid loans at retirement. These issues have been updated in our current report.

During our audit, we also observed how pension reform legislation allows retirees to exceed the monetary limitations for mandatory re-enrollment. We recommended the division closely monitor this situation and determine whether legislative changes may be warranted.

Unpaid Loans

The division should improve the identification and collection of outstanding loans.

Prior to retirement, members of Public Employees' Retirement System, Teachers' Pension and Annuity Fund, Police and Firemen's Retirement System, and State Police Retirement System that have at least three years of service in the applicable pension fund may borrow up to 50 percent of their employee pension contributions. Members who retire with an outstanding loan balance have the option of paying the loan in full prior to receiving any pension benefits or continuing their monthly loan payment schedule into retirement. If a retiree dies before the loan balance is repaid, the division obtains the remaining balance from the retiree's group life insurance proceeds or other benefit payable.

The division has access to the Employer Pensions and Benefits Information Connection (EPIC), which can be utilized to identify outstanding loans of retired employees. The division moves the existing loan balance from EPIC to the Retired Loan Sub-ledger (RLS) to enable the continued collection of the loans. Our analysis of EPIC data revealed 4,919 members who retired from July 1, 2009 to January 1, 2012 had outstanding loan balances totaling $19.8 million. Our random sample of 258 retirees revealed 14 loan balances were not accurately transferred to the RLS or errors occurred in balances resulting in $67,000 in loans not being collected. Statistically projecting this error rate to the population, we estimate that at least $1.3 million in loans are not being collected.

Recommendation

We recommend the division take appropriate collection actions for the 14 loans and investigate the remaining population to ensure all outstanding retiree loan balances are collected.

Retiree Deaths

The division should improve the collection of overpayments made to retirees after their death.

Usually, a family member or survivor notifies the division when a retiree of a pension system dies. The division also reviews reports generated by the New Jersey Bureau of Vital Statistics and an outside vendor that match pension payment files against death files. When a match occurs, the division suspends payment to the retiree.

We performed our own match and identified 445 deceased individuals receiving pension payments as of September 2009. We investigated 45 retirees. We found one individual, who died in November 2006, received pension benefits until June 2011. The improper pension payments totaled $84,500. The division identified the remaining 44 retirees through their process but not until $545,000 was paid after the retirees' deaths. As of July 2011, $241,000 had been recouped. However, only $23,000 of the remaining $304,000 has been part of a collection effort. The remaining $281,000 is outstanding because of a lack of communication between the individual who performs the death matches and the individuals who attempt to recover such overpayments. As of June 2011, the division did not have an account receivable set up to track the overpayments made to deceased individuals.

Recommendation

We recommend the division continue to review the death matches reported from vital statistics records and from the contracted vendor. We also recommend the division establish an account receivable for the payments to deceased individuals and improve communication between its employees to enhance collection efforts on overpayments.

Observation

Post-Retirement Employment

The division should continue to monitor the effect recent pension enrollment legislation has on rehiring of retirees.

In accordance with state statutes, retirees from Public Employees' Retirement System (PERS) and Teachers' Pension and Annuity Fund (TPAF) are permitted to work for private industry, the federal government, or a government agency in another state without affecting their retirement benefits. A PERS or TPAF retiree can also be hired in a position covered by a different New Jersey state-administered retirement system and continue to receive their retirement allowance from their respective retirement system, but may not enroll in the new pension system. Our analysis of calendar year 2010 identified over 6,000 individuals receiving a pension and earning wages from public employment. Based on our limited review, many of these retirees are working in a position covered by another pension system, an acceptable post-retirement practice. For example, teachers who retire from TPAF may work as a substitute teacher, which is a position covered by PERS. Prior to May 2010, however, a PERS retiree was required to re-enroll in PERS if they started employment in a PERS-covered position and earned in excess of $15,000. Pension reform legislation effective May 2010 stated enrollment in PERS would also be limited to employees based on a minimum number of hours worked (32 local, 35 state). Similarly, prior to May 2010, a TPAF retiree was required to re-enroll in TPAF if they started employment in a TPAF-covered position regardless of earnings. The pension reform legislation for TPAF also added a minimum of 32 hours (both state and local) provision for enrollment.

The "minimum number of hours worked" requirement was found to be beneficial in the enrollment process. However, its implementation may result in an unintended consequence in the re-enrollment process. By working less than the minimum number of hours, the pension reform legislation allows retirees to exceed the monetary limitations for mandatory re-enrollment. The retiree can return to a similar or the same position on a part-time basis while still receiving their pension allowance. This condition may encourage and lead to earlier retirements and increase pension payments over the retirees' lives. It may be too early to recognize a significant effect from this re-enrollment change. However, management has expressed concern that employing entities may take advantage of the current legislation by rehiring a retiree at less than full-time and that this practice may have a detrimental financial impact on the pension systems. The division should monitor this situation closely and determine whether stronger legislation for retiree re-enrollments should be sought.

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May 16, 2012

Mr. John J. Termyna
Assistant State Auditor
New Jersey State Legislature
Office of Legislative Services
125 South Warren Street
Trenton, NJ 08625-0067

Dear Mr. Termyna:

Enclosed are our comments in response to the audit report of the Department of the Treasury, Division of Pensions and Benefits, Selected Pension Services.

If you have any questions, please contact me at 292-3674.

Sincerely,

John D. Megariotis
Deputy Director

c. Florence J. Sheppard

Unpaid Loans

The audit revealed 14 members did not have their outstanding pension loan obligation at the time of their retirement deducted from their monthly retirement allowance. The 14 identified have been corrected and monthly deductions from their retirement allowances have been scheduled to recover the outstanding balances.

Division staff has reviewed the procedure to identify members who have outstanding loan balances at the time of retirement to ensure all members are identified and monthly deductions are scheduled from their retirement allowance. Specifically, an enhancement to either the Retirement Tracking System (RTS) or the Loan System will be implemented to identify members with outstanding loan balances before a member is placed on the monthly payroll. Until the system enhancement is implemented a manual process will be followed to ensure all outstanding loan balances at retirement are identified and scheduled for repayment.

Retiree Deaths

Division staff will continue to review death matches identified via our contracted service and from information obtained from Vital Statistics. Additionally, the Division has begun the process to recoup all the overpayments identified in the audit.

The audit revealed a breakdown in communication between the unit that performs the death matches and the unit that pays claims which resulted in some overpayments not being scheduled for repayment. Modifications to our procedures have been implemented to address this issue.

The Audit also recommended the Division establish an accounts receivable system to assist in the recovery of outstanding overpayments. We will work with our technology staff to develop an automated system for this effort.

Post-Retirement Employment

The pension reform that changed the eligibility requirement for enrollment from minimum salary to hours worked has resulted in unintended consequences that have made it easier for a retiree to return to work and continue to receive a pension. As a result, we have determined that corrective legislation is required to clarify the rules governing post-retirement employment.