

**Office of the Auditor General**  
Report on Internal Control Over Financial Reporting

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**Michigan State Employees' Retirement System**  
Schedule of Employer Allocations and Schedules of Pension and  
Other Postemployment Benefit Amounts by Employer

Fiscal Year Ended September 30, 2019

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The auditor general shall conduct post audits of financial transactions and accounts of the state and of all branches, departments, offices, boards, commissions, agencies, authorities and institutions of the state established by this constitution or by law, and performance post audits thereof.

The auditor general may make investigations pertinent to the conduct of audits.

*Article IV, Section 53 of the Michigan Constitution*

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Office of the Auditor General

## Report Summary

*Report on Internal Control Over Financial Reporting  
Michigan State Employees' Retirement System  
- Schedule of Employer Allocations and Schedules of Pension and Other Postemployment Benefit Amounts by Employer  
Fiscal Year Ended September 30, 2019*

**Report Number:**  
**071-0165-20**

**Released:**  
**November 2020**

Generally accepted auditing standards require that an auditor report to management and those charged with governance any significant deficiencies or material weaknesses coming to the attention of the auditor during the completion of a financial audit. We are issuing this report in conjunction with our independent auditor's report dated September 29, 2020 on the Michigan State Employees' Retirement System's schedule of employer allocations and schedules of pension and other postemployment benefit amounts by employer for the fiscal year ended September 30, 2019.

<b>Findings Related to Internal Control Over Financial Reporting</b>	<b>Material Weakness</b>	<b>Significant Deficiency</b>	<b>Agency Preliminary Response</b>
Lack of internal control resulted in an improper allocation of net pension and other postemployment benefit liabilities between employers that was not detected and corrected by Financial Services, Department of Technology, Management, and Budget, prior to audit ( <u>Finding #1</u> ).		X	Agrees

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Lansing, Michigan 48913

**Doug A. Ringler, CPA, CIA**  
Auditor General

**Laura J. Hirst, CPA**  
Deputy Auditor General





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**Doug A. Ringler, CPA, CIA**  
Auditor General

November 24, 2020

Colonel John J. Wojcik, Chair  
State of Michigan Retirement Board  
Stevens T. Mason Building  
and  
Mr. Brom Stibitz, Director  
Department of Technology, Management, and Budget  
Elliott-Larsen Building  
and  
Mr. Anthony J. Estell, Director  
Office of Retirement Services  
Stevens T. Mason Building  
Lansing, Michigan

Dear Colonel Wojcik, Mr. Stibitz, and Mr. Estell:

This is our report on internal control over financial reporting of the Michigan State Employees' Retirement System Schedule of Employer Allocations and Schedules of Pension and Other Postemployment Benefit Amounts by Employer for the fiscal year ended September 30, 2019.

Your agency provided the preliminary response to the recommendation at the end of our fieldwork. The *Michigan Compiled Laws* and administrative procedures require an audited agency to develop a plan to comply with the recommendations and to submit it to the State Budget Office upon completion of an audit. Within 30 days of receipt, the Office of Internal Audit Services, State Budget Office, is required to review the plan and either accept the plan as final or contact the agency to take additional steps to finalize the plan.

We appreciate the courtesy and cooperation extended to us during this audit.

Sincerely,

A handwritten signature in black ink that reads "Doug Ringler". The signature is written in a cursive, slightly slanted style.

Doug Ringler  
Auditor General



## TABLE OF CONTENTS

### **MICHIGAN STATE EMPLOYEES' RETIREMENT SYSTEM Schedule of Employer Allocations and Schedules of Pension and Other Postemployment Benefit Amounts by Employer**

	<u>Page</u>
Report Summary	1
Report Letter	3
Independent Auditor's Report on Internal Control Over Financial Reporting	8
Fiscal Year 2019 Findings, Recommendations, and Agency Preliminary Responses	
1. Improvement in internal control needed to ensure proper allocation of net pension and OPEB liabilities.	12
Fiscal Year 2018 Report on Internal Control Over Financial Reporting Follow-Up	16
Glossary of Abbreviations and Terms	17





# INDEPENDENT AUDITOR'S REPORT ON INTERNAL CONTROL



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**Doug A. Ringler, CPA, CIA**  
Auditor General

## Independent Auditor's Report on Internal Control Over Financial Reporting

Colonel John J. Wojcik, Chair  
State of Michigan Retirement Board  
Stevens T. Mason Building  
and  
Mr. Brom Stibitz, Director  
Department of Technology, Management, and Budget  
Elliott-Larsen Building  
and  
Mr. Anthony J. Estell, Director  
Office of Retirement Services  
Stevens T. Mason Building  
Lansing, Michigan

Dear Colonel Wojcik, Mr. Stibitz, and Mr. Estell:

We planned and performed our audit of the Michigan State Employees' Retirement System's schedule of employer allocations and the specified column totals of the schedules of pension and other postemployment benefit amounts by employer as of and for the fiscal year ended September 30, 2019 and the related notes in accordance with auditing standards generally accepted in the United States of America. We considered the System's internal control over financial reporting (internal control) as a basis for designing audit procedures that are appropriate in the circumstances for the purpose of expressing our opinions on the schedule of employer allocations and on the specified column totals of the schedules of pension and other postemployment benefit amounts by employer, 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 schedules 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.

Our consideration of internal control was for the limited purpose described in the first paragraph 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 have not been 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 a deficiency in internal control, as described in Finding #1, that we consider to be a significant deficiency.

The System's preliminary response to the finding identified in our audit is included in the body of our report. The System's response was not subjected to the auditing procedures applied in the audit of the schedule of employer allocations and the specified column totals of the schedules of pension and other postemployment benefit amounts by employer and, accordingly, we express no opinion on it.

This communication is intended solely for the information and use of the State of Michigan Retirement Board, the Department of Technology, Management, and Budget, and the Office of Retirement Services and is not intended to be, and should not be, used by anyone other than these specified parties.

Sincerely,



Doug Ringler  
Auditor General  
September 29, 2020



FISCAL YEAR 2019  
FINDINGS, RECOMMENDATIONS,  
AND AGENCY PRELIMINARY RESPONSES

## **FINDING #1**

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### **Improvement in internal control needed to ensure proper allocation of net pension and OPEB liabilities.**

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Financial Services (FS), Department of Technology, Management, and Budget (DTMB), did not have sufficient internal control\* to ensure the proper allocation of the Michigan State Employees' Retirement System's (MSERS's) net pension and other postemployment benefit (OPEB) liabilities on the schedules of pension and OPEB amounts by employer for the fiscal year ended September 30, 2019. Although FS corrected the misstatements we identified prior to issuing the schedules, without implementing sufficient control improvements, risk exists that other misstatements could occur and not be detected in a timely manner.

Section 18.1485 of the *Michigan Compiled Laws* states that each department shall establish and maintain an internal accounting and administrative control system using generally accepted accounting principles\*. These controls should include a system of authorization and recordkeeping procedures to control assets, liabilities, revenues, and expenditures; a system of practices to be followed in the performance of duties; qualified personnel that maintain a level of competence; and internal control techniques that are effective and efficient. Each principal department head shall document the system and ensure that the system functions as intended.

In addition, Governmental Accounting Standards Board\* (GASB) Statement No. 68, *Accounting and Financial Reporting for Pensions*, and GASB Statement No. 75, *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions*, require employers participating in a cost-sharing pension plan to recognize in their financial statements the proportionate share of the collective net pension and OPEB liabilities, deferred inflows and outflows of resources, and pension and OPEB expenses. The proportionate share of the net pension and OPEB liabilities is determined based on each employer's required employer contributions.

FS calculates the employer's required pension and OPEB contributions using employee wage data confirmed with each reportable employer. FS sends instructions to each employer on how to determine employee wage data and relevant payroll adjustments. The actuaries then calculate net pension and OPEB liabilities amounts based on the required contribution.

\* See glossary at end of report for definition.

Our audit disclosed the following misstatements, which FS corrected prior to the issuance of the schedules:

- a. FS did not properly classify employee wages and required pension and OPEB contributions between employers, which impacted pension and OPEB liabilities:

<u>Employer</u>	<u>Overstatement (Understatement) of September 30, 2019 Net Pension Liability</u>	<u>Percent Impact of Error on Each Employer Net Pension Liability</u>	<u>Overstatement (Understatement) of September 30, 2019 Net OPEB Liability</u>	<u>Percent Impact of Error on Each Employer Net OPEB Liability</u>
State of Michigan	\$ 2,011,948	0.0%	\$ 3,752,187	0.1%
Liquor Purchase Revolving Fund	\$ 532,977	3.8%	\$ 615,537	3.9%
Office Services Revolving Fund	\$(1,082,714)	(8.2%)	\$(1,296,096)	(8.5%)
Motor Transport Fund	\$ 257,513	5.1%	\$ 276,249	4.7%
Attorney Discipline System	\$ (411,437)	(61.9%)	See part b.	
Risk Management Fund	\$ (86,990)	(16.4%)	\$ (107,989)	(16.3%)
Michigan State Housing Development Authority	\$ (431,596)	(1.0%)	\$ (527,911)	(1.1%)
Michigan Strategic Fund	\$ 365,584	5.2%	\$ 455,709	5.6%
Michigan Economic Development Corporation	\$ (664,741)	(5.6%)	\$ (823,660)	(5.9%)
Mackinac Island State Park Commission	\$ (53,473)	(2.1%)	\$ (65,918)	(2.1%)
State Land Bank	\$ (428,306)	(30.5%)	\$ (531,954)	(30.5%)
State Bar of Michigan	\$ 14,448	3.8%	See part b.	

When determining the wages and contributions by employers, we noted that, although FS provided instructions to employers which included the consideration of accounting adjustments, this did not prevent the above misstatements.

- b. For two employers, FS did not properly calculate the employers' OPEB contributions based on the required method of actual fiscal year 2019 OPEB claims incurred on behalf of retirees:

Employer	Overstatement (Understatement) of September 30, 2019 Net OPEB Liability	Percent Impact of Error on Each Employer Net OPEB Liability
Attorney Discipline System	\$ (293,038)	(37.4%)
State Bar of Michigan	\$ (1,497,726)	(1,789.2%)

FS inadvertently did not use the required method, and its departure from this method was not detected during the supervisory review.

In our report on internal control over financial reporting for the fiscal year ended September 30, 2018, we reported this same significant deficiency\* that also resulted in misstatements. DTMB indicated that it agreed with the recommendation and developed and provided instructions to employers to help ensure the accuracy of reporting.

**RECOMMENDATION**

We again recommend that FS implement sufficient internal control to ensure the proper allocation of MSERS's net pension and OPEB liabilities on the schedules of pension and OPEB amounts by employer.

**AGENCY  
PRELIMINARY  
RESPONSE**

DTMB provided us with the following response:

*DTMB agrees with the recommendation. DTMB Financial Services, with assistance from the Office of Financial Management, will continue to expand its efforts with the employers to establish more effective controls for all responsible parties to collectively ensure that proper wage and contribution information is provided to the actuary. Instructions and tools will be enhanced to provide employers with more detailed steps to properly validate their wage and contribution information for accuracy and completeness.*

\* See glossary at end of report for definition.



FISCAL YEAR 2018  
REPORT ON INTERNAL CONTROL  
OVER FINANCIAL REPORTING  
FOLLOW-UP

Following is the status of the reported finding from the fiscal year 2018 Michigan State Employees' Retirement System schedule of employer allocations and schedules of pension and other postemployment benefit amounts by employer report on internal control over financial reporting (071-0165-19):

Prior Audit Finding Number	Topic Area	Current Status	Current Finding Number
1	Improvement in internal control needed to ensure proper allocation of net pension and OPEB liabilities.	Repeated*	1

\* See glossary at end of report for definition.

## **GLOSSARY OF ABBREVIATIONS AND TERMS**

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deficiency in internal control over financial reporting	The design or operation of a control that 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.
DTMB	Department of Technology, Management, and Budget.
financial audit	An audit that is designed to provide reasonable assurance about whether the financial schedules of an audited entity are presented fairly, in all material respects, in accordance with the applicable financial reporting framework.
FS	Financial Services.
generally accepted accounting principles (GAAP)	A technical accounting term that encompasses the conventions, rules, guidelines, and procedures necessary to define accepted accounting practice at a particular time; also cited as "accounting principles generally accepted in the United States of America."
Governmental Accounting Standards Board (GASB)	An arm of the Financial Accounting Foundation established to promulgate standards of financial accounting and reporting with respect to activities and transactions of state and local governmental entities.
internal control	A process, effected by those charged with governance, management, and other personnel, designed to provide reasonable assurance about the achievement of the entity's objectives with regard to the reliability of financial reporting, effectiveness and efficiency of operations, and compliance with applicable laws and regulations.
material misstatement	A misstatement in the financial schedules that causes the schedules to not present fairly the financial position or the changes in financial position, and, where applicable, cash flows thereof, in accordance with the applicable financial reporting framework.
material weakness in internal control over financial reporting	A deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the financial schedules will not be prevented, or detected and corrected, on a timely basis.
MSERS	Michigan State Employees' Retirement System.

OPEB other postemployment benefits.

repeated The same problem was noted in the current audit, and the wording of the current recommendation remains essentially the same as the prior audit recommendation.

significant deficiency in internal control over financial reporting 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.









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