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# REPORT DIGEST

## STATE UNIVERSITIES RETIREMENT SYSTEM

### COMPLIANCE AUDIT

For the Year Ended:  
June 30, 1996

#### Summary of Findings:

Total this audit	7
Total last audit	7
Repeated from last audit	2

Release Date:



State of Illinois  
Office of the Auditor General

**WILLIAM G. HOLLAND**  
AUDITOR GENERAL

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### SYNOPSIS

- ◆ The State Universities Retirement System (SURS) had inadequate controls over the processing of membership information in their computer system. Staff with access to the membership data had unlimited access privileges to all processing functions within the membership system.
- ◆ SURS did not comply with certain statutory requirements involving contractual services.
- ◆ SURS did not comply with certain provisions of the Fiscal Control and Internal Auditing Act.

{Financial Information and Activity Measures are summarized on the reverse page.}

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**STATE UNIVERSITIES RETIREMENT SYSTEM**  
**INFORMATION FROM FINANCIAL AND COMPLIANCE AUDITS**  
**Two Years Ended June 30, 1996**

FINANCIAL OPERATIONS	FY 1996	FY 1995
Revenues		
Contributions		
Participants .....	\$197,005,577	\$185,899,240
Federal, trust funds, other .....	23,291,855	25,673,483
State of Illinois.....	123,911,000	102,236,700
Other.....	164,781	205,975
Total Contributions .....	<u>\$344,373,213</u>	<u>\$314,015,398</u>
Net investment income.....	258,391,559	238,505,555
Gain on sale of investments .....	219,362,905	55,335,589
Total Revenues .....	<u>\$822,027,677</u>	<u>\$607,856,542</u>
Expenses		
Total benefits .....	\$379,496,338	\$343,602,018
Other expenses.....	33,840,008	36,996,478
Total Expenses.....	<u>\$413,336,346</u>	<u>\$380,598,496</u>
Revenues in excess of Expenses .....	<u>\$408,691,331</u>	<u>\$227,258,046</u>
INVESTMENT PORTFOLIO ANALYSIS (Book Value)	JUNE 30, 1996	JUNE 30, 1995
Total common stock.....	\$2,309,445,281	\$2,166,149,758
Preferred stock .....	54,439,650	54,729,351
Total fixed income securities .....	1,821,532,375	1,913,409,908
Short-term investments .....	553,381,815	151,084,100
Real estate investments .....	315,104,597	363,921,902
Total Investments at Book Value .....	<u>\$5,053,903,718</u>	<u>\$4,649,295,019</u>
Total Investments at Market Value .....	<u>\$6,930,828,396</u>	<u>\$5,926,095,729</u>
ADMINISTRATIVE EXPENSES	FY 1996	FY 1995
Personal services.....	\$2,696,845	\$2,802,754
Other professional services .....	1,549,450	1,431,881
Depreciation.....	1,214,190	1,103,668
Postage, freight, and expenses.....	265,598	261,615
Equipment repair and rental.....	270,908	257,195
Printing and copying services.....	243,495	245,598
Building operations expenses.....	254,566	215,332
Other expenses.....	486,189	533,283
	<u>\$6,981,241</u>	<u>\$6,851,326</u>
SELECTED ACCOUNT BALANCES	JUNE 30, 1996	JUNE 30, 1995
Contributions receivable .....	\$15,334,375	\$13,760,020
Prepaid expenses.....	37,704	12,741
Accrued investment income receivable.....	22,912,070	19,668,509
Investments, at cost.....	5,053,903,718	4,649,295,019
Property and equipment .....	14,490,228	12,956,664
Total Assets .....	<u>\$5,106,678,095</u>	<u>\$4,695,692,953</u>
Total Liabilities.....	\$ 23,786,964	\$ 21,493,152
Fund balance (reserved):		
Participant contributions .....	2,761,947,622	2,533,361,319
Benefits from employee and employer contributions.....	7,393,091,377	6,846,037,094
Unfunded accrued actuarial liability.....	(5,072,147,868)	(4,705,198,612)
Total Fund Balance.....	<u>\$5,082,891,131</u>	<u>\$4,674,199,801</u>
Total Liabilities and Fund Balance .....	<u>\$5,106,678,095</u>	<u>\$4,695,692,953</u>
SUPPLEMENTARY INFORMATION	FY 1996	FY 1995
Total investment administrative expenses .....	\$11,849,905	\$11,524,349
Return on investments.....	18.3%	16.5%
Average number of employees.....	71	74
Number of active members .....	76,088	73,527
Number of inactive members .....	34,446	27,399
Number of retirement benefit recipients.....	19,538	18,585
Number of survivors benefit recipients .....	4,540	4,363
Number of disabilities benefit recipients.....	926	932

**EXECUTIVE DIRECTOR(S)**

During Audit Period: Dr. Robert Mandeville Interim Executive Director (7/1/95 - 12/18/95), James M. Hacking (12/19/95 - 6/30/96)  
 Currently: James M. Hacking, Executive Director

## **INTRODUCTION**

This digest covers our State compliance audit of the System for the year ended June 30, 1996. A financial audit covering the year ending June 30, 1996 was issued at a earlier date.

## **FINDINGS, CONCLUSIO RECOMMENDATIONS**

### **INADEQUATE SECURITY CONTROLS OVER MEMBERSHIP DATA**

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#### **Unlimited Access Privileges**

SURS had inadequate security controls over the processing of membership information in their computer system. Staff with access to the membership data had unlimited access privileges to all processing functions within the membership system. In addition, security access controls did not appropriately limit access within the membership system nor provide for an appropriate segregation of duties.

All membership system menus and update features were available to any user. Access to specific system functions should be granted based upon job responsibilities. Further, audit trails within the system should provide a history of all changes made to a record and provide a means to determine what action has been taken on membership records and who performed that action. (Finding 4, page 14)

We recommended implementing access controls within the membership system to limit users' access to the level needed to perform their job. In addition, SURS should enhance the membership system to: 1) provide a transaction history within the existing audit trail, and 2) modify password security so the password can be entered without displaying the password on the screen.

SURS officials concurred with our recommendations and stated they would implement all of the recommendations.

### **CONTRACTUAL SERVICES**

The State Universities Retirement System did not comply

with certain statutory requirements involving contractual services. **This finding has been repeated from the prior audit.**

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**No written contract**

In our testing we noted one contractual service arrangement did not have a written contract. The Illinois Purchasing Act (30 ILCS 505/9.01) states that "Whenever any State agency contracts for services involving professional or artistic skill and involving an expenditure of more than \$5,000 for the same type of service at the same location during any fiscal year, which contract is exempt from competitive procurement procedures .... a copy of the contract, which must be reduced to writing, shall be filed with the Comptroller. All copies of contracts filed pursuant to this Section are public records...."

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**Payments made prior to written contract execution**

Also, 2 of 19 contracts reviewed were approved between 24 and 25 days, respectively, after the start date of the contract. Payments totaling \$36,737 for services performed under these two contracts were made prior to the execution of the contracts. (Finding 5, pages 16 - 17)

We recommended that SURS use good business practice and comply with State law and related rules and regulations pertaining to the writing, filing, and executing contracts.

SURS officials concurred with this recommendation and stated they have centralized the contracting function with the Office of the Deputy Director of Finance, which should improve compliance. Further, SURS Internal audit staff has expanded its reviews of administrative expense payments in order to detect contractual violations and to increase staff awareness of contractual regulations. (For previous agency response, see Digest Footnote 1.)

**INTERNAL AUDIT**

The System was not in compliance with certain provisions of the Fiscal Control and Internal Auditing Act (FCIAA). **This finding has been repeated from our FY 95 audit and first appeared in the FY 94 audit.**

FCIAA (30 ILCS 10/2003) requires that the internal audit program include audits of major systems of internal accounting and administrative control and be conducted on a periodic basis so that all major systems are reviewed at least

once every two years.

Our review of the internal audit work for the year ended June 30, 1996 disclosed that the internal audit department did not complete reviews of all the major systems as required by State law. The internal audit department was comprised of one internal auditor employed on a full time basis and one internal auditor on a part-time basis during fiscal year 1996.

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**Need to review all major systems every two years**

We recommended that the System establish and follow a program of internal auditing that includes a review of all major systems of internal accounting and administrative controls at least once every two years as required by State law. (Finding 6, page 18)

System officials concurred with this recommendation and stated that a new full time auditor position will increase audit coverage and they expect the goal of auditing every major system every two years will be achieved in the future. (For previous agency responses, see Digest Footnote 2.)

**OTHER FINDINGS**

The remaining findings are less significant and the System's response indicates it is addressing the conditions. We will review the System's progress in implementing our recommendations in our next audit.

Mr. Steve Hayward, Internal Auditor at the System provided responses to our recommendations. All responses were received in December, 1996.

**FUTURE REPORTING REQUIREMENTS**

In November 1994, the Governmental Accounting Standards Board (GASB) issued Statement No. 25, "Financial Reporting for Defined Benefit Pension Plans and Note Disclosures for Defined Contribution Plans". This Statement requires that plan assets be reported at fair value, rather than at cost. In addition, this Statement establishes a new financial reporting framework that will result in significant changes to the financial statements as well as the required supplementary information. The requirements of this Statement are effective for periods beginning after June 15, 1996, with earlier implementation encouraged. If comparative financial statements are presented, restatement

of the prior year financial statements is required.

The System will adopt this Statement beginning with the fiscal year ending June 30, 1997. One effect of this Statement will be to increase the net assets by the difference between fair value and cost of the net assets on the date of adoption. The Statement, however, allows for different valuation methods of assets related to some function of market value (i.e. smoothing of market values over time or current market values) for determining funded status and the annual required contribution. If the System had implemented Statement No. 25 at June 30, 1996 and used the current market value method, the net assets available for benefits would have been \$6,958,012,000 resulting in a funding ratio of 68.5%.

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**Funding ratio at 68.5% using  
current market value**

At present, investments are valued at cost or book value as specified by State law (40 ILCS 5/15.167). Thus, implementation of Statement No. 25 will require a change to existing State law to comply with generally accepted accounting principles. Net assets available for benefits at cost at June 30, 1996 were \$5,082,891,132 resulting in a funding ratio of 50.1%.

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**Funding ratio at 50.1% with  
investments valued at cost**

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WILLIAM G. HOLLAND, Auditor General

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**SPECIAL ASSISTANT AUDITORS**

KPMG Peat Marwick, LLP were our special assistant auditors for this audit.

**DIGEST FOOTNOTES**

**#1 CONTRACTUAL SERVICES - Previous Agency Response**

1995: Although SURS believes that a number of items in this Finding do not apply to SURS or came into existence after the execution of the contracts examined, SURS will comply with the rules and regulations governing contracts, contract content and advance payment for services.

**#2 INTERNAL AUDIT - Previous Agency Responses**

- 1995: Prior to fiscal year 1995, SURS established a plan to audit all major systems every two years and had every intention of following the plan. SURS hired a part time audit associate to ensure that the plan was followed. However, because of circumstances cited in the finding, SURS was unable to complete all of the planned audits. SURS will continue to work toward the goal of auditing every major system every two years.
- 1994: The SURS internal auditor operationally reports to the Associate Executive Director. However, for purposes of the FCIAA he has a direct reporting relationship to the Executive Director concerning the outcomes of all his internal audits.

During the year the executive staff reviewed and classified with the Internal Auditor all of the major systems of internal accounting and administrative controls so that they could be reviewed at least once every two years as required by State law. In addition, the System hired an audit intern to assist the Internal Auditor with the reviews.

