



# Legislative Post Audit Performance Audit Report Highlights

## Kansas Public Employees Retirement System: Evaluating Controls to Detect and Prevent Fraud and Abuse

### Report Highlights

September 2015 • R-15-011

#### **Summary of Legislator Concerns**

*Legislators have expressed concerns that some individuals might be circumventing KPERS current controls in order to continue earning years of service credit or earning credit for employer contributions while not working for a KPERS-covered employer.*

#### **Background Information**

*KPERS is a \$16 billion public pension system for 1,500 public employers and covers about 295,000 state and local public employees.*

*KPERS provides pension benefits for retired members as well as disability and death benefits.*

*KPERS currently has about 100 FTE staff who work in the following five divisions; administrative, benefits and members services, fiscal services, information technology, and investments. KPERS also contracts for actuarial and investment services.*

#### **QUESTION 1: Does the Kansas Public Employees Retirement System Have Sufficient Controls to Detect and Prevent Fraud and Abuse?**

- Because of the volume of applications, contributions and benefit payments handled on a regular basis, public pension plans are at risk for fraud and abuse. For example, there is risk of making inaccurate benefit payments and not collecting enough in contributions. These risks can be exploited and result in fraud and abuse.
- These risks can be mitigated by implementing the following controls:
  - Requiring proof of identity helps verify members' identities.
  - Regular monitoring helps ensure that benefits are calculated correctly and that information used to calculate benefits is accurate.
  - Segregating duties helps ensure that one employee cannot both enroll and approve benefits and also ensures that sensitive information is safeguarded from internal and external threats.
- KPERS had many, but not all, controls to help prevent and detect fraud abuse.
  - Recent financial audits confirmed that KPERS requires proof of identity when processing benefits.
  - We confirmed KPERS monitors benefit processing through supervisory reviews.
  - We confirmed KPERS segregates duties between staff who collect contributions and staff who distribute benefits.
  - However, we also found evidence of inadequate controls in three areas as detailed in the following sections.
- Since late 2013, KPERS had not conducted field audits to verify the accuracy of employer-reported information.
  - KPERS uses field audits as a control to help ensure retirement contributions are accurate.
  - However, KPERS temporarily suspended its field audit function for 20 months beginning in 2013 because of turnover and the need to implement other projects.
  - During the time when the field audits were suspended, KPERS was at increased risk of not collecting all the contributions it should.
  - Pay-period reporting and new government accounting standards provide KPERS with additional controls, but are not a substitute for field audits.

- KPERS could strengthen its efforts to identify recipients of disability benefits who are not eligible for those benefits.
  - KPERS relies on a third-party contractor to monitor the ongoing eligibility of KPERS disability recipients.
  - We identified at least 16 KPERS disability recipients who earned substantial income while also receiving disability benefits.
  - Information from the Kansas Department of Revenue (KDOR) and the Kansas Department of Labor (KDOL) could help KPERS identify disability recipients who earned substantial income while also receiving disability benefits.
  - KDOR and KDOL officials told us they foresee few if any problems in sharing income-related data with KPERS in the future.
  
- We found seven teachers who were incorrectly awarded KPERS service credits while working for education associations.
  - The seven teachers were no longer teaching in their district and were officers in their education association.
  - In reporting payroll information to KPERS, each school district continued to show the teachers as working for the school district.
  - Because education associations are not KPERS-covered employers, the seven former teachers should not have been awarded KPERS service credits while working for them.
  - It is likely that service credits have been incorrectly awarded this way for many years and KPERS plans to investigate and correct any errors.

### Other Findings

- When calculating members' retirement benefits, KPERS handled final average salary calculations appropriately.
  - Current state law includes provisions intended to limit the impact of accumulated leave and late-in-career salary increases on members' retirement benefits.
  - Our test work showed that benefit inflation rarely happens, but when it did KPERS made the required adjustments.
    - Significant increases in final average salaries used to calculate members' monthly retirement benefits have been rare—5% of retirees in the past two years had significant salary increases and those instances are allowed by law.
    - For the 61 retirees included in our sample, KPERS appropriately identified increases in their final average salaries and then made the necessary adjustments.
  
- Legislation considered during the 2015 Legislative Session would have substantially limited the opportunity for retirees to include unused leave when calculating retirement benefits.
  - Currently, two KPERS retirement plans call for unused leave to be included when calculating retirement benefits.
    - For members of the KPERS 1 retirement plan who were hired on or before July 1, 1993, KPERS must consider unused leave when calculating retirement benefits.
    - For members of the Kansas Police and Firefighters (KP&F) retirement system who were hired on or before July 1, 1993, KPERS must include unused leave when calculating retirement benefits.

*KPERs retirements benefits are funded through member contributions, employer contributions, and investment earnings.*

*As of May 2015, the total assets for the system were about \$16.8 billion.*

*As of December 2014, KPERS had an unfunded liability of about \$9.5 billion that is projected to be eliminated by 2033. Unfunded liability occurs when the value of benefits earned by public employees is greater than the value of the plan's assets.*

- Although rare, the monthly retirement benefit for some retirees was substantially increased when large amounts of unused leave were included in their final salary calculation, as provided for by state law.
  - In reaction to such instances, the 2015 Legislature considered two bills which would have limited employees' ability to include unused leave when calculating retirement benefits.
- Restricting or eliminating the inclusion of unused leave could reduce KPERS' unfunded liability up to \$80 million, but the actual impact likely will be far less.
    - KPERS' actuaries estimated eliminating the inclusion of unused leave in the benefits calculation would save the plan up to \$80 million.
    - We estimated that setting a 240-hour limit on the amount of unused leave that can be included would save the plan up to \$62 million.
    - Neither estimate is likely to be fully realized because many members would retire before either policy change took effect.

## SUMMARY OF RECOMMENDATIONS

### Question 1 Recommendations:

- We recommended that KPERS should follow through with its plan to reinstitute field audits.
- We recommended that KPERS work to establish inter-agency data-sharing agreements with the Kansas Department of Revenue and the Kansas Department of Labor to identify KPERS members receiving disability benefits but who are no longer eligible.
- We recommended that KPERS incorporate a check of members' service records into its field audit function, correct any inaccuracies and, for the seven teachers we identified, that KPERS make any corrections to records and contributions as required by law.

## AGENCY RESPONSE

- KPERS officials agreed to implement our recommendations and had no comments in their formal response that required us to change the report.

### Legislative Division of Post Audit

800 SW Jackson Street  
Suite 1200  
Topeka, Kansas 66612-2212  
Telephone (785) 296-3792  
Fax: (785) 296-4482  
Website:  
<http://www.kslpa.org/>

Scott Frank  
Legislative Post Auditor

For more information on this  
audit report, please contact

**Laurel Murdie**

(785) 296-3792

Laurel.Murdie@lpa.ks.gov

### HOW DO I REQUEST AN AUDIT?

By law, individual legislators, legislative committees, or the Governor may request an audit, but any audit work conducted by the division must be directed by the Legislative Post Audit Committee. Any legislator who would like to request an audit should contact the division directly at (785) 296-3792.