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Joint Legislative Committee on Performance Evaluation and Expenditure Review (PEER)

Report to
the Mississippi Legislature

A Review of the Administration of the Public Employees' Retirement System

The Public Employees' Retirement System's (PERS's) administrative expenses have risen during the last five fiscal years because of staffing increases to manage increased membership. However, PERS's salary cost per member is comparable to that of other states' retirement systems. Since 2000, PERS has spent $1.56 million on capital improvement projects approved by the Legislature, including renovation of the PERS Building and purchase and renovation of a separate building.

Concerning accuracy of contribution collections, PERS has the fiduciary responsibility to employ reasonable means to ensure that information on members from public employer agencies is correct. While PERS has implemented certain controls, it has not complied with statutory requirements to collect members' Social Security information, which was intended to assure record accuracy. Also, while PERS must rely on the public employer agencies to submit correct employee information, PERS has not established a formal audit process for verifying employee records.

Regarding PERS's implementation of laws and regulations for selected employee groups, PEER found that PERS has complied with a Supreme Court ruling regarding the inclusion of travel expenses as compensation for Supreme Court justices and Court of Appeals judges. PERS has instituted a repayment schedule with a group of retirees that was overpaid $1.7 million, but the entire amount will never be repaid due to the ages and income levels of the retirees. Also, PEER found that PERS does not have a surety bond in place, as required by statute, for the executive director, nor does it have any type of public official or surety bond for the members of the board of trustees.

Regarding investment performance, PERS's investment program has performed consistent with market conditions over the past ten years while utilizing prudent policies and procedures in pursuing the program's objectives.

December 17, 2002

PEER: The Mississippi Legislature's Oversight Agency

The Mississippi Legislature created the Joint Legislative Committee on Performance Evaluation and Expenditure Review (PEER Committee) by statute in 1973. A standing joint committee, the PEER Committee is composed of five members of the House of Representatives appointed by the Speaker and five members of the Senate appointed by the Lieutenant Governor. Appointments are made for four-year terms with one Senator and one Representative appointed from each of the U. S. Congressional Districts. Committee officers are elected by the membership with officers alternating annually between the two houses. All Committee actions by statute require a majority vote of three Representatives and three Senators voting in the affirmative.

Mississippi's constitution gives the Legislature broad power to conduct examinations and investigations. PEER is authorized by law to review any public entity, including contractors supported in whole or in part by public funds, and to address any issues that may require legislative action. PEER has statutory access to all state and local records and has subpoena power to compel testimony or the production of documents.

PEER provides a variety of services to the Legislature, including program evaluations, economy and efficiency reviews, financial audits, limited scope evaluations, fiscal notes, special investigations, briefings to individual legislators, testimony, and other governmental research and assistance. The Committee identifies inefficiency or ineffectiveness or a failure to accomplish legislative objectives, and makes recommendations for redefinition, redirection, redistribution and/or restructuring of Mississippi government. As directed by and subject to the prior approval of the PEER Committee, the Committee's professional staff executes audit and evaluation projects obtaining information and developing options for consideration by the Committee. The PEER Committee releases reports to the Legislature, Governor, Lieutenant Governor, and the agency examined.

The Committee assigns top priority to written requests from individual legislators and legislative committees. The Committee also considers PEER staff proposals and written requests from state officials and others.

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The Mississippi Legislature

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December 17, 2002

Honorable Ronnie Musgrove, Governor
Honorable Amy Tuck, Lieutenant Governor
Honorable Tim Ford, Speaker of the House
Members of the Mississippi State Legislature

On December 17, 2002, the PEER Committee authorized release of the report entitled **A Review of the Administration of the Public Employees' Retirement System.**

Senator William Canon, Chairman

This report does not recommend increased funding or additional staff.

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List of Exhibits

A Review of the Administration of the Public Employees' Retirement System

Executive Summary

The PEER Committee conducted a management and expenditure review of the Mississippi Public Employees' Retirement System. PEER sought to determine:

- whether PERS's expenses for administering the state's retirement programs, including administration of recently approved capital improvement projects, are excessive;
- whether PERS ensures the accuracy of contribution collections;
- PERS's implementation of laws and regulations for selected employee groups; and,
- investment performance for the last ten years and whether management fees are economical.

Assessment of Administrative Expenses

PERS's administrative expenses have risen during the last five fiscal years because of staffing increases to manage increased membership. PERS's salary cost per member is comparable to that of other states' retirement systems.

Over the last five fiscal years, PERS's administrative expenses have risen 28%, primarily due to an increase in the number of positions and other routine expenses. The State Personnel Board approved the reorganization of PERS, which divided the Membership Services division into three divisions: Special Programs, Membership Services, and Wage and Contribution. According to PERS, these twenty-seven additional positions were needed to address expanded services and increases in retirees and new members.

In comparing the retirement system's administrative costs to those of other states' systems, PEER chose the salary cost per member measure. This measure provides the most consistent recurring expense information on all retirement systems and provides a comparable measure of resources used to support administration of the retirement systems.

PERS's FY 2001 salary cost per member was $22.12, while comparable states' salary cost per member ranged from $16.05 to $69.11. PERS's salary cost per member increased 24.63% from FY 1997 to FY 2002; when adjusted for inflation at 1996 dollars, the salary cost per member increase over that six-year period was 14.40%. While this is a large increase, it is due to an increase in PERS staff. The increase in staff is due to the reorganization of PERS and the preparation of PERS to handle the increase of services, retirees, and members over the next few years.

Administration of Capital Improvement Projects

Since 2000, PERS has spent $1.56 million on capital improvement projects approved by the Legislature, including renovation of the PERS Building and purchase and renovation of a separate building.

In 2001, the Legislature appropriated $12.46 million for PERS to renovate its building at 429 Mississippi Street to add workspace, a boardroom, upgraded heating and cooling systems, and other improvements. As of September 2002, PERS had expended $270,132 on architectural fees and $210,436 on other building expenses.

PERS completed the purchase and renovation of a building at 301 North President Street in August 2002 at a cost of $1.08 million. PERS purchased this building for additional expansion space. However, PERS was required to have a long-term lease with a state agency or the Legislature. Therefore, the first tenant, the Office of the Secretary of State, moved in during September 2002 with a five-year lease, which will prohibit PERS from occupying the space for at least that amount of time.

Although the Bureau of Building approved PERS's architectural contract and reviewed its renovation plans as required by state law, PERS did not use the bureau as its construction manager. Also, the Department of Finance and Administration (DFA) approved PERS's building expenditures through the state accounting system, but in order to meet all requirements of the appropriation bill, DFA will have to add information to the Mississippi Comprehensive Annual Financial Report to show all expenditures.

Assessment of Administration of Contribution Collections

PERS has the fiduciary responsibility to employ reasonable means to ensure that information on members from public employer agencies is correct. While PERS has implemented certain controls, PERS has not complied with statutory requirements to collect members' Social Security information, which was intended to assure record accuracy. Also, while PERS must rely on the public employer agencies to submit correct information on employees, PERS has not established a formal audit process for verifying employee records.

PERS has not collected Social Security information on PERS members as required by statute. PERS requires all public employers to use its computer collection program, but PERS is not taking all steps necessary to ensure accuracy of the data collected.

PERS has also accepted contributions in the Public Employees' and Municipal Retirement systems that were later ruled ineligible. PERS does not have an audit process for employer records, which could have detected the reporting errors.

Implementation of Laws and Regulations for Selected Employee Groups and Related Issues

As noted on page vii, in addition to reviewing administrative issues and investment performance at PERS, PEER reviewed PERS's implementation of laws and regulations for selected employee groups.

The first issue was whether PERS has complied with a Supreme Court ruling regarding the inclusion of travel expenses as compensation for Supreme Court justices and Court of Appeals judges. PEER found that PERS has complied with *PERS v. Hawkins,* 781 So. 2d 899 (Miss. 2001).

The second issue PEER addressed was PERS's overpayment of $1.7 million to twenty-three retirees from 1987 to 2001. Due to a clerical error, PERS did not adjust twenty-three accounts to comply with a benefit option selection, thus resulting in the overpayment of $1.7 million to these retirees. PERS has instituted a repayment schedule with the retirees, but the entire amount will never be repaid due to the ages and income levels of the retirees.

During the course of reviewing the second issue, PEER found that PERS does not have a surety bond in place, as required by statute, for the executive director, nor does it have any type of public official or surety bond for the members of the Board of Trustees. This is necessary to protect the trust against the possible misspending of funds.

Investment Performance

The Public Employees' Retirement System's investment program has performed consistent with market conditions over the past ten years while utilizing prudent policies and procedures in pursuing the program's objectives.

The Public Employees' Retirement System's investments have increased from a net assessed value of over $6.8 billion in 1993 to approximately $14.2 billion in 2002. During this ten-year period, the annualized rate of return for PERS investments was 8.6%.

PERS's process for selecting investment managers enables it to negotiate reasonable investment manager fees and the system's use of the Commission Recapture Program has enabled it to benefit from investment managers' use of selected brokerage firms without inhibiting the performance of investment managers.

Recommendations

1. Should the Legislature wish the Bureau of Building to oversee the PERS renovation projects, it should include language in the PERS FY 2004 appropriation bill to require the bureau to assist in the renovation projects through construction program management, which includes independent oversight of the professional and construction teams, as well as monitoring and adherence to the job schedule and the review of change orders.

2. In accordance with requirements in the PERS appropriation bills, the Department of Finance and Administration should ensure that the Mississippi Comprehensive Annual Financial Report includes expenses for the renovation of the two PERS buildings and that all expenditures for the renovation projects continue to receive its review and approval.

3. PERS should study its contribution collection system to develop accuracy controls in order to meet its fiduciary responsibility to assure accurate reporting. The areas that should be studied include

annual verification of Social Security information as required by MISS. CODE ANN. Section 25-11-123 (f) (1972); methods to correct monthly reporting errors from public employers; periodic random audits of data collected; and automated system controls within GENESIS for checking of overreported wages.

If PERS does not believe that it is practicable to gather the Social Security information or if other sources of comparable data are more accurate and appropriate, PERS should develop an alternative and recommend that this section be repealed.

4. PERS should comply with the provision in MISS. CODE ANN. Section 25-11-121 (1972) that requires that the executive director acquire a surety bond.

5. PERS should review its decision with respect to the purchase of bond coverage for its board members. In light of the fact that board members are in a position to certify expenditures in error, PERS should consider whether it would be advisable to procure fiduciary insurance or public official bond for the members of the PERS board.

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A Review of the Administration of the Public Employees' Retirement System

Introduction

Authority

Pursuant to the authority granted by MISS. CODE ANN. Section 5-3-57 et seq. (1972), the PEER Committee conducted a management and expenditure review of the Mississippi Public Employees' Retirement System (PERS).

Scope and Purpose

This review sought to determine:

- whether PERS's expenses for administering the state's retirement programs, including administration of recently approved capital improvement projects, are excessive;
- whether PERS ensures the accuracy of contribution collections;
- PERS's implementation of laws and regulations for selected employee groups; and,
- investment performance for the last ten years and whether management fees are economical.

Method

PEER reviewed state laws, regulations, and Attorney General's opinions related to PERS, as well as PERS's annual reports and agency handbooks. PEER reviewed other states' retirement systems' annual reports concerning administrative expense and membership information and obtained investment information from other states' retirement systems. PEER observed PERS staff as they processed monthly contribution collections and processed retirees' applications for benefits. PEER interviewed PERS staff, other state retirement systems' staff, and Department of Finance and Administration staff.

Background

Mississippi Public Employees' Retirement System

State law designates the PERS board as custodian of the funds of the retirement system.

The Legislature established the Mississippi Public Employees' Retirement System in 1952. The system is "under the management of the board of trustees for the purpose of providing retirement allowances and other benefits. . .for officers and employees in that state service and their beneficiaries." The board of trustees has the responsibility for the general administration and the proper operation of the Public Employees' Retirement System. According to MISS. CODE ANN. Section 25-11-15 (6) (1972), "the board shall establish rules and regulations for the administration of the system." The board appoints an executive director and employs staff required to "transact the business of the system." This staff is staff of the Public Employees' Retirement System (PERS) and administers five retirement systems, including PERS, the Highway Patrol system, the Municipal Retirement System, the Supplemental Legislative Retirement System, and the Optional Retirement Plan for college professors and administrators.

According to MISS. CODE ANN. Section 25-11-121 (8) (1972), "the board of trustees shall be the custodian of the funds of the system." Also according to MISS. CODE ANN. Section 25-11-121 (12) (1972):

> *The board, the executive secretary and employees shall discharge their duties with respect to the investments of the system solely for the interest of the system with the care, skill, prudence and diligence under the circumstances then prevailing that a prudent person acting in a like capacity and familiar with such matters would use in the conduct of an enterprise of a like character and with like aims, including diversifying the investments of the system so as to minimize the risk of large losses, unless under the circumstances it is clearly prudent not to do so.*

This point was reiterated by an Attorney General's opinion to Frank Ready, the Executive Director of PERS, May 25, 2001 (Docket 01-4457), which stated that the "Board of Trustees has a fiduciary responsibility to protect and preserve the trust funds."

Retirement Systems Administered by the Board of Trustees

The Board of Trustees and its staff administer five retirement programs for public employers in Mississippi.

Public Employees' Retirement System (PERS)

PERS covers employees of state agencies, state universities, public school districts, and community and junior colleges, as well as some other public entities.

The PERS retirement system is a defined benefit plan for members and their families, which allows the retiree at the time of retirement to select a retirement benefit. The fund is financed by member contribution rate of 7.25% and an employer contribution rate of 9.75%. A member qualifies for retirement after twenty-five years of credited service regardless of age, or with at least four years of membership service credit at the age of sixty.

According to MISS. CODE ANN. Section 25-11-105 (1972), the following are included in membership of the Public Employees' Retirement System:

> *All persons who shall become employees in the state service after January 31, 1953, and whose wages are subject to payroll taxes and are lawfully reported on IRS Form W-2, except those specifically excluded, or as to whom election is provided in Articles 1 and 3, shall become members of the retirement system as a condition of their employment.*

Therefore by law this retirement system covers all employees of state agencies, state universities, public school districts, and community and junior colleges. PERS has entered into separate agreements with many public agencies to cover their employees with a retirement benefit. This includes counties, local governmental entities, juristic entities, local hospitals, and local libraries.

Mississippi Highway Safety Patrol Retirement System (MHSPRS)

MHSPRS allows higher contribution rates by the state and provides benefits sooner than the PERS system because of the dangerous nature of highway patrol officers' employment.

The MHSPRS system, created in 1958, provides benefits for highway patrol officers. Due to the dangerous nature of their employment, the state created a system that allows higher contribution rates by the state and provides benefits sooner than the PERS system. The MHSPRS system's contribution rate for members is 6.5% of annual earnings and the employer contribution rate is 26.16% of annual earnings. A member may retire after twenty years of service at the age of forty-five or after twenty-five years of service at any age. A member may also retire at the age of fifty-five with at least five years of credited service. MISS. CODE ANN. Section 25-13-3 (1972) established the membership of the system to include all officers of the Mississippi Highway Safety Patrol *who have completed a course of instruction in an authorized highway patrol training school on general law enforcement* and who are sworn officers of the Highway Patrol.

Municipal Retirement System (MRS)

MRS serves some Mississippi cities and fire and police departments.

The Mississippi Legislature created the MRS in 1948 as a city employee retirement fund for two municipalities and seventeen fire and police departments. The fire and police systems closed to new members in 1976, with the municipal funds closing membership in 1987. Since 1987, any municipality can become a member of the PERS retirement system through agreement. The Board of Trustees of PERS is responsible for the general administration of MRS. The members of this system finance the system by paying between 7% and 10% of their salaries as employee contributions, while each municipality levies between .49 mills and 9.19 mills of assessed valuations as employer contributions. A member may retire after twenty years of service regardless of age.

Supplemental Legislative Retirement Plan (SLRP)

SLRP provides benefits for legislators and the President of the Senate.

In 1989, the Mississippi Legislature created the SLRP to provide supplemental allowance for members of the state Legislature, the President of the Senate (Lieutenant Governor), and their beneficiaries. The SLRP employee contribution rate is 3% of all remuneration up to $125,000, except mileage allowance, and the state legislative agency pays a contribution rate of 6.33% to finance SLRP. The benefit provisions are the same as the PERS system.

Optional Retirement Plan (ORP)

ORP, created as a recruitment tool for the institutions of higher learning, provides benefits based solely on the amount of contributions to the member's account and its earnings.

The Legislature created the Optional Retirement Plan in 1990 as a recruitment tool for the institutions of higher learning (IHL). This plan provides a separate account for each member, and benefits based solely on the amount of contributions to the member's account and its earnings. Plan participants direct the investment of the funds through three investment vendors. Members of ORP contribute 7.25% of annual earnings up to $125,000, each employer contributes 9.75%, of which 7.25% is deposited to the member account, which becomes the property of the member. The additional 2.5% is contributed to PERS to reduce the actuarially accrued liability. All new teachers and members of administrative faculties of IHL are eligible for membership in ORP. Benefits payable to plan participants are not obligations of the State of Mississippi. These benefits are the liability of the investment vendors and are governed solely by the terms of the annuity contract.

Public Employer Membership

As of October 2002, eight hundred fifty-six public employers were within the Mississippi Public Employees' Retirement System. These employers include state agencies, local governments, schools, and universities (see Exhibit 1, below).

As of FY 2002, the five retirement systems PERS administers covered 208,853 members, including 56,705 retirees and beneficiaries and 152,148 active members.

Exhibit 1: Public Employer Membership of Retirement System

Public Employees' Retirement System	
State Agencies	115
State Universities *	9
Public Schools	150
Community/Junior Colleges	15
Counties	82
Municipalities	219
Hospitals	14
Libraries	46
Other Political Subdivisions (including juristic)	181
Mississippi Highway Safety Patrol Retirement System	
Highway Patrol	1
Bureau of Narcotics	1
Municipal Retirement System	
Municipalities	2
Police and Fire Departments	17
Supplemental Legislative Retirement System	4
Total	**856**

* This is for the nine university administrative entities and includes the University of Mississippi Medical Center. All nine entities participate in the Optional Retirement Plan for college professors and administrators.

SOURCE: PERS.

Automation of the Retirement System

In order to automate management of the components of its retirement system, PERS developed GENESIS. PERS uses GENESIS to collect wage and contribution data and create benefit payments for retirees. GENESIS's specific roles include:

- storing enrollment and demographics information;
- processing mail and imaging documents;
- reporting wage and contribution data;
- processing refunds;
- maintaining a general ledger;
- generating benefit estimates;
- processing retirement applications;
- processing payroll for retirees; and,
- processing taxes for retirees.

Assessment of Administrative Expenses

PERS's administrative expenses have risen during the last five fiscal years because of staffing increases to manage increased membership. PERS's salary cost per member is comparable to that of other states' retirement systems.

Salary cost per member provides the most consistent recurring expense information on retirement systems and provides a comparable measure of resources used to support administration of retirement systems.

Administrative expenses are expenses used for the management of the retirement systems and include routine expenses such as salaries, printing costs, and computer systems. In order to assess PERS's administrative expenses, PEER examined trends in administrative expenses by major object of expenditure, identifying underlying causes of fluctuations, and reasons for increases. PEER adjusted expenditures to account for the contractual costs of implementation of the GENESIS system and building costs. PEER then compared administrative salary cost per member with that of similar states.

The salary cost per member measure provides the most consistent recurring expense information on all retirement systems and provides a comparable measure of resources used to support administration of the retirement systems.

PERS's Administrative Expenses

Over the last five fiscal years, PERS's administrative expenses have risen 28%, primarily due to an increase in the number of positions and other routine expenses.

Over the last five fiscal years, PERS has had an increase in administrative expenses (see Exhibit 2, page 8). One main reason is the increase of twenty-seven positions. The increase in positions has caused an increase in salary expenses, as well as expenses for capital outlay-equipment, including computer equipment and modular units for the staff positions.

Other routine expenses have caused the administrative cost of PERS to rise. For example, postage (Contractual Services) and printing costs (Commodities) have risen significantly over the last five years. Between 2001 and 2002, postage costs increased over $200,000, while printing costs increased in 2000 by $45,000 and in 2001 by $30,000. In 1999, there was an increase in travel costs due to an increase in in-state travel for expanded pre-retirement seminar services; there was also a large increase in equipment costs due to the purchase of a vehicle for in-state travel and computer and office equipment. In 2000 and 2001, equipment costs increased in order to purchase computers and office equipment for the new positions and the purchase of replacement computer equipment.

Exhibit 2: PERS's Administrative Expenses, FY 1998-2002

	FY 1998	FY 1999	FY 2000	FY 2001	FY 2002	5 Year Percent Increase/ Decrease
Personnel Services- Salaries	$4,203,756.45	$ 3,977,274.87	$4,491,483.22	$4,621,046.25	$5,279,584.16	26%
Personnel Services -Travel	54,669.63	74,502.02	73,637.28	72,766.67	62,447.82	14%
Contractual Services	1,747,244.24	1,754,092.30	1,937,520.81	2,141,923.91	2,466,707.09	41%
Commodities	211,570.25	242,313.49	288,280.44	357,610.57	222,821.23	5%
Capital Outlay-Other	9,100.00	-	-	-	-	-100%
Capital Outlay - Equipment	20,462.19	72,349.89	143,663.33	136,436.82	19,445.99	-5%
Subsidies, Loans and Grants*	64,481.00	54,924.00	51,740.00	43,780.00	36,616.00	-43%
	$6,311,283.76	$ 6,175,456.57	$6,986,325.08	$7,373,564.22	$8,087,622.29	28%

* Subsidies, Loans, and Grants are a separate appropriation for the Bea Barnard Teacher Retirement Funds, which will decrease as the number of retirees/beneficiaries decreases.

SOURCE: MERLIN.net, Mississippi Department of Finance and Administration budget information. Building renovation and GENESIS development costs are not included.

PERS's Reorganization

The State Personnel Board approved the reorganization of PERS, which divided the Membership Services division into three divisions: Special Programs, Membership Services, and Wage and Contribution.

PERS reorganized due to implementation of GENESIS and the pre-retirement education program, as well as growth in the number of members eligible for retirement.

In March 2001, the Executive Director of PERS requested of the State Personnel Board a reorganization of PERS's executive-level management. The reason for this reorganization is due to the "enhancements that have occurred to the System, which include the implementation of the new automated system, GENESIS and the Pre-Retirement Educational Program," as well as growth in the number of members eligible for retirement. According to a study by PERS in 2001:

> *Since 1990, the number of active members has grown 1.6% annually while the number of member agencies increased 1.5% per year. During this same period the number of service retirees/beneficiaries have grown 5% per year and the number of disability retirees have increased 7% annually with a combined average annual increase in retiree payroll of 11.3%.*

According to PERS, in 2001, there were 56,000 retirees and at this time, there were approximately 37,500 members eligible to retire in the next five years. Therefore, if all employees eligible to retire did so, there would be a large growth in this category in the next five years, thus increasing claims processing and retirement counseling services. At the time of request, PERS was experiencing backlogs in many areas due to the volume of requests coming into the Information Center.

Staffing Increases

PERS has increased its staffing by twenty-seven positions in the last five fiscal years. These positions are in four different departments, including Administrative Services, Membership Services, Wage and Contribution, and Special Programs.

Over the past six years, retirees have increased over 17%, while active members have increased 3%.

In FY 1999 through FY 2002, the Legislature appropriated funds for an increase of twenty-seven positions at PERS. For FY 2002, PERS was funded at 98% of total funds necessary to fund all authorized positions fully. In FY 2002, PERS stated that the increases are "directly related to management's attempt to meet the increasing demands placed on the System by retirees and members. The demographic effects of the aging 'baby boomer' generation continues to increase the volume of work in servicing members planning to retire as well as the increasing numbers in retirement." Retirees have increased over 17%, while active members have increased 3% over the past six years (see Exhibit 3, page 10, for the numbers of retirees and active members). According to information provided by PERS, additional positions have been added in Administrative Services, Membership Services, Wage and Contribution, and Special Programs.

Administrative Services

Administrative Services has added six positions in order to move from a mainframe environment to an integrated network environment with GENESIS.

In the last five fiscal years, Administrative Services has added six positions in order to move from a mainframe environment to an integrated network environment with GENESIS. PERS has developed many internet-based activities. This includes benefit estimate calculators, eventual submission of wage and contribution data over the web, as well as individual account access via the web. While PERS had an on-site contractor for the development and implementation of GENESIS, in 2000 PERS took over full responsibility for the system. This includes any programming changes as well as technical assistance for the staff. The administrative staff is also responsible for the support and integration of fifteen other software applications in addition to the GENESIS system.

Exhibit 3: Mississippi's Salary Cost Per Member, FY 1997-2002

	FY 1997	FY 1998	FY 1999	FY 2000	FY 2001	FY 2002	6-Year Percent Increase
Retirees/Beneficiaries	48,186	49,918	51,616	53,964	56,592	56,705	
Annual Percent Change		3.59%	3.40%	4.55%	4.87%	0.20%	17.68%
Active members	146,802	146,390	149,644	152,783	152,068	152,148	
Annual Percent Change		-0.28%	2.22%	2.10%	-0.47%	0.05%	3.64%
Total	194,988	196,308	201,260	206,747	208,660	208,853	
Annual Percent Change		0.68%	2.52%	2.73%	0.93%	0.09%	7.11%
Salaries, wages, and fringe benefits	$ 3,981,000	$ 4,062,000	$ 4,134,000	$ 4,522,000	$ 4,616,000	$ 5,316,000	33.53%
Actual Salary Cost per member	**$ 20.42**	**$ 20.69**	**$ 20.54**	**$ 21.87**	**$ 22.12**	**$ 25.45**	24.63%
Deflated Salaries (1996 dollars)	$ 3,941,584	$ 3,959,064	$ 3,978,826	$ 4,278,146	$ 4,266,174	$ 4,828,338	22.50%
Deflated Salary Cost per member (1996 dollars)	**$ 20.21**	**$ 20.17**	**$ 19.77**	**$ 20.69**	**$ 20.45**	**$ 23.12**	14.40%

SOURCE: State Retirement Comprehensive Annual Financial Reports. Mississippi PERS Comprehensive Annual Financial Report (CAFR) salary amounts are different from state budget information listed in previous exhibits. PEER used CAFR information because of its comparability to information from other states.

Membership Services

The largest increase in staffing, 17 positions, has been within the Membership Services division, which is due to increased services offered.

The largest increase in positions has been within the Membership Services division, which is due to increased services offered. Since the reorganization, PERS added seventeen staff positions to the Membership Services division. The Information Call Center was developed in 1997, using existing benefit analyst positions. PERS has since added six analysts to the Call Center. According to PERS, member feedback from 1996 and 1997 of difficulty receiving account information, led to the development of the Call Center. A Call Center analyst can provide an Estimate of Benefits, Balance Letters, and Benefit Verification Letters over the phone. Calls to the call center have increased, as have total number of answered calls. For example, in FY 1999, total calls attempted were over 400,000; this number continued to grow to over 700,000 calls in FY 2001. However, since the addition of trained staff, and better service delivery, the number of calls has decreased in FY 2002.

PERS is also offering more pre-retirement education opportunities to members and has added one position in this area. Since FY 2001, three new types of sessions, PERS on the

Move; Half-Day Mid-Career Sessions; and Focus Sessions have been added. This has increased the number of opportunities to counsel retirees on their options for retirement.

PERS has added two quality assurance analysts and eight other positions in the Retiree Payroll and Benefits staff. The quality assurance employees verify the accuracy of the data entered into the system with regard to payroll and benefit information. The number of retirees moved to payroll has increased. From FY 1998 to FY 2002, the number of retirees processed to payroll has risen for a net increase of retirees added to payroll from 1,200 to 2,600. According to PERS, the payroll process was taking over twelve months; this process with more staff is now taking three months. The number of pre-retirement estimates provided to members has increased from 6,000 in FY 1998 to 10,000 in FY 2002. There has been an increase in the recalculation of retirement benefits due to the legislative increase of the retirement formula. As of July 1, 2002, the retirement formula increased from 1.875% to 2%. The implementation of this increase was phased in and began in 1999. All retirees on payroll were notified of the increase and their benefits recalculated. PERS has also begun to provide in the annual member statements benefit calculations for members who are within four years of retirement.

Wage and Contribution

There has been an addition of two staff members to the Wage and Contribution Division. PERS created this division through the reorganization of 2001. PERS originally staffed the division with employees who had previously worked in the Membership Services division. The number of retiree and active members has increased (as noted in Exhibit 3, page 10), as well as the number of public employers increasing from 837 to 856.

Special Programs

PERS added two staff members to Wage and Contribution and two to Special Programs.

PERS has added two staff positions to the Special Programs division. PERS created this division in the reorganization to house the disability retirement program, and other special programs including the Municipal Retirement, Highway Patrol, and Optional Retirement systems as well as the PERS Retiree Insurance Plan and the Deferred Compensation plan. PERS experienced an increase in the number of disability retirees from 3,100 in FY 1998 to 4,000 in FY 2002, requiring additional review time. According to information provided by PERS, with the increase in positions, disability claims processing has decreased from 106 days to 86 days.

Trends in Administrative Salary Costs

From FY 1997 to FY 2002, PERS's salary cost per member increased 24.63% due to an unusually large FY 2002 increase. The FY 2001 salary cost per member was $22.12, while comparable states' salary cost per member range from $16.05 to $69.11.

Mississippi's Salary Cost Per Retirement System Member

PERS's salary cost per member increased 24.63% from FY 1997 to FY 2002; when adjusted for inflation at 1996 dollars, the salary cost per member increase over that six-year period was 14.40%. While this is a large increase, it is due to an increase in PERS staff. The increase in staff is due to the reorganization of PERS and the preparation of PERS to handle the increase of services, retirees, and members over the next few years.

From FY 1997 to FY 2002, PERS had a 7.11% increase in members. Salaries and wages increased 33.53% over the same period.

From FY 1997 to FY 2002, PERS's salary cost per member rose due to an increase in members and salary expenditures. There has been an increase in retirees/beneficiaries of 17.68%, and active members, 3.64%, for an overall increase of members of 7.11% (see Exhibit 3, page 10). Salary and wage expenditures have increased 33.53% while total staff has increased by 27 positions, or 23.68%, to accommodate an increase in the number of retirees and services. When adjusted for inflation at 1996 dollars, the salary cost per member has increased 14.40%.

The salary cost per member has increased from 8.35% for the five-year period to 24.63% for the six-year period. This large increase is due to the increase of salary expenditures from 15.95% (five-year period) to 33.53% (six-year period). This represents a large increase in the percentages due to a large increase in the salary and wage expenditures in FY 2002. This increase can be attributed to PERS's reorganization (see discussion on page 8) and preparations for an increase in retirees and members and services provided to these members. PEER divided the total number of members by the salary cost to determine the salary cost per member.

Comparison of Salary Costs with Those of Other State Retirement Systems

With regard to salary cost per member of retirement systems, Mississippi is in the lower end of the range of comparable states with similar numbers of members.

PEER selected salary cost per retirement system member as the comparison factor instead of "administrative expense" because salary cost per retirement system member is a recurring category that all states use in their financial statements. Many states include different factors in "administrative expense." For example, some states include outside investment manager fees in administrative expense, while Mississippi accounts for this separately.

PEER compared Mississippi's system to other systems with dedicated staff, similar composition (state, local and teacher members), and similar number of members.

In selecting retirement systems for comparison, PEER chose systems with similar composition and numbers of members. Mississippi's FY 2001 membership of retirees, beneficiaries, and active members was 208,660. Mississippi's retirement system includes state, local, and teacher representatives as members of the system. PEER compared Mississippi's system to other systems with dedicated staff, similar composition (state, local and teacher members), and similar number of members. PEER collected descriptive information from seven other systems, which ranged in membership from approximately 124,000 to 268,000 in FY 2001.

PEER used the *State of Wisconsin Retirement Research Committee Staff Report No. 83,* "2000 Comparative Study of Major Public Employee Retirement Systems" to obtain information on the other states' retirement systems. See Exhibit 4, page 14, for the comparison.

Exhibit 4: Other States' Salary Cost Per Member, FY 2000 and FY 2001

FY 2000

State	Total Members	Salaries and Wages	Cost per member
Utah *	123,886	$ 8,272,000	$ 66.77
Colorado	217,253	14,359,000	66.09
Oregon	240,100	10,276,192	42.80
Maryland	260,359	9,194,000	35.31
Arizona	241,962	5,876,560	24.29
Mississippi	**206,747**	**4,522,000**	**21.87**
Kansas	202,822	3,656,038	18.03
Iowa	221,293	3,079,546	13.92

FY 2001

State	Total Members	Salaries and Wages	Cost per member
Utah *	124,519	$ 8,606,000	$ 69.11
Colorado	227,693	15,644,000	68.71
Oregon	247,146	10,923,014	44.20
Maryland	268,785	10,926,000	40.65
Arizona	252,321	6,559,788	26.00
Mississippi	**208,660**	**4,616,000**	**22.12**
Kansas	205,895	3,788,052	18.40
Iowa	223,313	3,583,467	16.05

* Utah's salaries are as of December 31, 2000 and 2001.
The total membership includes retirees, beneficiaries, and active employee members. PEER did not include inactive employee members in this calculation.

SOURCE: State Retirement Comprehensive Annual Financial Reports. Mississippi PERS Comprehensive Annual Financial Report (CAFR) salary amounts are different from state budget information listed in previous exhibits. PEER used CAFR information because of its comparability to information from other states.

Administration of Capital Improvement Projects

Since 2000, PERS has spent $1.56 million on capital improvement projects approved by the Legislature, including renovation of the PERS Building and purchase and renovation of a separate building.

According to the project justification provided by PERS, the "program needs of the organization necessitate" the renovation and addition of infrastructure to serve the "growing client base." In 2000, PERS received a legislative appropriation for the purchase of the 301 North President building.

According to the Executive Director this building was to be used for the future expansion of PERS staff with the addition of the Retiree Insurance Program; however, the Legislature required in the appropriation bill a long-term lease for the building from a state agency or the Legislature. PERS has entered into a five-year lease with the Office of the Secretary of State, which will prevent PERS from occupying the space for at least five years if there is an expansion of staff. In 2001, PERS received legislative approval for the renovation of the 301 North President building and the agency's main building at 429 Mississippi Street.

PERS's Capital Improvement Projects

Renovation of the PERS Building

In 2001, the Legislature appropriated $12.46 million for PERS to renovate the building at 429 Mississippi Street to add workspace, a boardroom, upgraded heating and cooling systems, and other improvements.

Beginning in June 1999, PERS's Board of Trustees began discussing the issue of limited staff space within the PERS Building located at 429 Mississippi Street. The Executive Director of PERS suggested to the board the acquisition of the MCI WorldCom Building located on Amite Street, but the MCI WorldCom building was not listed for sale.

In January 2000, the Executive Director discussed with the Board of Trustees Building Committee the proposed remodeling of the PERS Building, which would include a board room, additional office work space, training room, redesigned lobby area, additional parking, upgraded heating and cooling systems, and other renovations, adding over 20,000 square feet. At the same meeting, the committee also discussed issues related to the purchase of a building for investment property (see following section).

The Building Committee proposed passage of two bills: a bill allowing the remodeling of PERS Building, constructing a wing to the existing building, and constructing a parking garage; and a bill allowing the purchase and remodeling of the 301 North President Street contingent upon the Legislature or state agency leasing the building from PERS.

In the 2000 legislative session, the PERS FY 2001 appropriation bill passed with funds for the purchase and renovation of the 301 North President Street building and $371,000 for architectural fees for the planning of future construction and or renovations.

In the 2001 legislative session, the PERS FY 2002 appropriation bill passed with a total project cost listed at $12,831,650 for the renovation of the PERS building. The bill included $12,460,650 for the "expenses of construction and renovation, including furnishings, as well as moving and relocation costs" of the PERS Building located on Mississippi Street. The following was also included:

> *The expenditure of funds appropriated under this section shall be subject to the approval of the Department of Finance and Administration, and the Department of Finance and Administration shall submit an annual report regarding such expenditures to the Legislative Budget Office, the House Public Buildings, Grounds and Lands Committee and the Senate Public Property Committee.*

As of September 2002, PERS had expended $270,132 on architectural fees and $210,436 on other building expenses for the PERS Building at 429 Mississippi Street. The architectural fees were appropriated separately.

Construction bids were due for the renovation project in December 2002.

The Legislature reappropriated $12,634,639 for the reauthorization of expenditure of funds to defray the construction and renovation of the PERS Building in the 2002 legislative session (PERS's FY 2003 appropriation bill). The FY 2003 appropriation bill also included the previous language for the approval of funds by the Department of Finance and Administration.

As of September 2002, PERS had expended $270,132 on architectural fees and $210,436 on other building expenses for the PERS Building at 429 Mississippi Street. The architectural fees were appropriated separately in the FY 2001 appropriation bill. Construction bids were due for the renovation project in December 2002. (Exhibit 5, page 17, shows a summary of renovation costs of the PERS building.)

Exhibit 5: Summary of Renovation Costs of PERS Building, as of September 2002

Building Surveys	$17,060
Relocation Expenses *	193,377
Total	**$210,437**
Architecture Fees (appropriated separately)	270,132
Total Cost as of September 2002	$480,569

* Relocation expenses include wiring for computers and telephones, as well as rent and other moving expenses.

SOURCE: PEER analysis of PERS's construction documentation.

Acquisition and Renovation of Additional Property

PERS completed the purchase and renovation of the 301 North President Street location in August 2002 at a cost of $1.08 million. The first tenant, the Office of the Secretary of State, moved in during September 2002.

As noted above, in January 2000, the Executive Director discussed with the Board of Trustees Building Committee the issues related to the purchase of a building at 301 North President Street. At that time, the estimated cost of purchasing and renovating the building was approximately $902,000. According to the PERS Executive Director, the building was purchased for projected expansion of PERS staff with the addition of the PERS Retiree Insurance Program.

In response to instructions in the appropriation bill, PERS entered into a five-year lease with the Office of the Secretary of State for the North President Street building. This lease will prohibit PERS from occupying the space for at least five years.

In the 2000 legislative session, the Legislature appropriated $371,000 to PERS for architecture fees for any future renovations and $950,000 (total project cost) for the purchase and renovation of the 301 North President Street building. However, the funds could only be expended if PERS could "secure a long-term lease for the building from either the State Legislature or an agency of state government." Therefore, PERS entered into a five-year lease with the Office of the Secretary of State, which will prohibit PERS from occupying the space for at least five years should it expand.

In the 2001 legislative session, the PERS FY 2002 appropriation bill included $468,000 (of the total project cost) for expenses of the renovation of the building located at 301 North President Street. The following was also included:

> *The expenditure of funds appropriated under this section shall be subject to the approval of the*

Department of Finance and Administration, and the Department of Finance and Administration shall submit an annual report regarding such expenditures to the Legislative Budget Office, the House Public Buildings, Grounds and Lands Committee and the Senate Public Property Committee.

The total cost of acquisition, construction, and renovation of the 301 North President Street building was $1,050,006. Architectural fees for the project totaled $32,885, appropriated separately.

PERS purchased the building in 2000 for $486,500. In June 2001, the Building Committee determined that PERS should proceed with collecting bids for its renovation. PERS collected eight bids from construction companies in August 2001 for the remodeling and renovation of the building. McMillan-Pitts Construction was the low bidder at the contract price of $457,750. McMillan-Pitts Construction proceeded with renovation in October 2001, with project completion scheduled for April 2002. Demolition of walls and construction began and continued through January 2002. At that time, the contractor discovered black mold, which led to the project being shut down until a separate contractor completed mold abatement. The mold abatement added $101,000 to the building renovation. The Department of Finance and Administration approved additional funds of $110,000 for the mold abatement in January 2002. The Legislature appropriated these funds in the PERS FY 2003 appropriation bill. The total legislative appropriation for the project was $1.06 million, with additional funds appropriated for architecture fees.

The contractor completed construction in August 2002, with the Secretary of State's Office moving in as the first tenant in September 2002. The total cost of acquisition, construction, and renovation of the 301 North President Street building was $1,050,006. Architectural fees for the project totaled $32,885, appropriated separately in the FY 2001 appropriation bill. (Exhibit 6, below, shows a summary of costs of the PERS property at 301 North President Street.)

Exhibit 6: 301 North President Street Building Cost, as of September 2002

Purchase Cost*	$485,500
Contractor Fees	457,750
Asbestos Inspection/Geotech Services	4,972
Mold Abatement	101,784
Total	**$ 1,050,006**
Architecture Fees (appropriated separately)	32,885
Total Cost as of September 2002	**$1,082,891**

* PERS received a $1,000 credit for fixtures removed from the building by the seller.

SOURCE: PEER analysis of PERS construction documentation.

Compliance with Legislative Requirements for Construction Oversight

Although the Bureau of Building approved PERS's architectural contract and reviewed its renovation plans as required by state law, PERS did not use the bureau as its construction manager. Also, the Department of Finance and Administration (DFA) approved PERS's building expenditures through the state accounting system, but in order to meet all requirements of the appropriation bill, DFA will have to add information to the Mississippi Comprehensive Annual Financial Report to show all expenditures for the PERS buildings.

The Bureau of Building approved PERS's architectural contract and reviewed its renovation plans as required by state law, but PERS did not use the bureau as its construction manager.

PERS submitted the architecture contract for approval to the Department of Finance and Administration's Bureau of Building (BOB), as required by MISS. CODE ANN. Section 31-11-3 (7):

> *The department shall review and preapprove all architectural and engineering services contracts entered into by any state entity regardless of the source of funding…*

BOB approved the architecture contract in August 2000. PERS submitted the renovation plans of both buildings to BOB as well, but it provided no formal feedback to PERS.

DFA contends that the department complied with the language of the appropriation bill because DFA approved all expenditures through the issuance of warrants in the state accounting system. (See language of appropriation bill, page 17.) Also, according to DFA the submission of the annual report required by the appropriation bill will be completed upon the release of the Mississippi Comprehensive Annual Financial Report (CAFR) for FY 2002. Currently, the CAFR lists the total amounts for all state building projects. This includes the project authorization amount, expended to date amount, and the outstanding commitment amount. Each agency is listed separately for projects over $10 million. However, PERS buildings are not state property; therefore, the CAFR will have to list the PERS buildings as non-state-owned buildings.

The Bureau of Building is the state's construction manager; however, PERS did not use the bureau as construction manager for its renovation projects.

The Department of Finance and Administration's Bureau of Building is responsible for administration, management, and decision making for public building projects constructed with funds appropriated by the Legislature. If a state entity's construction project is funded with self-generated funds or if the funds have been placed under the direct control of the entity constructing the project, the Bureau of Building provides construction program management services at no charge if the entity requests assistance.

The Bureau of Building has knowledge of the construction field and typically serves as the construction program manager for all significant construction projects for the state and could have served at no cost to PERS.

The bureau serves as the construction program management agent for state entities, representing the interests of the entity and exercising independent oversight of the construction team. When the Bureau of Building performs the construction program management function, the bureau exercises oversight of architects, engineers, or construction contractors. The bureau has authority to compel adherence to contract specifications and schedules, applying sanctions to firms or individuals within the constructor team that do not fulfill their responsibilities. BOB oversees all construction projects with general funds and may be given the authority to oversee projects unless prohibited by the constitution (e.g., Institutions of Higher Learning projects paid from self-generated funds are exempted from BOB oversight).

The funds used by PERS for the renovation projects are pension trust funds. The Legislature provided these appropriated funds to PERS, not BOB, for the renovation of the two buildings. PERS did not request construction management services from the bureau.

The legislation did not specify that BOB serve as the construction manager. PERS used its architecture firm as the construction project manager. However, BOB has the knowledge of the construction field and typically serves as the construction manager for all significant construction projects for the state and could have served at no cost to PERS.

Assessment of Administration of Contribution Collection

PERS has the fiduciary responsibility to employ reasonable means to assure that information on members from public employer agencies is correct. While PERS has implemented certain controls, PERS has not complied with statutory requirements to collect members' Social Security information, which was intended to assure record accuracy. Also, while PERS must rely on the public employer agencies to submit correct information on employees, PERS has not established a formal audit process for verifying employee records.

PERS could work with public employer agencies to develop self-audit and audit procedures, which are currently being used in other states.

According to MISS. CODE ANN. Section 25-11-121 (8) (1972), "the board of trustees shall be the custodian of the funds of the system." However, PERS must accept and rely on employee information provided by public employers. While PERS has some accuracy checks in place that check monthly information as the public employer submits the information, an audit step of this information is absent. This audit step would add a level of assurance that the information adheres to requirements in statutes and regulations. PERS could work with the various public employer agencies to develop self-audit and audit procedures, which are currently being used in other states. (See discussion page 28.)

PERS's Contribution Collection Process

PERS's Lack of Compliance with Statutory Requirements

PERS has not complied with statutory requirements to collect Social Security reports, which could be used to verify employee records and help assure accuracy of information.

MISS. CODE ANN. Section 25-11-123 (f) (1972) states:

> *Once each year, under procedures established by the system, each employer* ***shall*** *submit to the Public Employees' Retirement System a copy of their report to Social Security of all employees' earnings.*

PERS requested the addition of the section in 1994 because of investigations that had shown some agencies not reporting all eligible employees. According to PERS, the purpose of the section was to require submission of certain information and find a more efficient way to compare the number of individuals who were reported to PERS to the number of individuals with

Social Security forms. This legislation was added before the GENESIS project was started. In its proposed GENESIS implementation plan, PERS acknowledged that the comparison of the two sources had merit; however, actual implementation of the automated task was not incorporated into the system.

While still required by statute, as of January 2001, PERS no longer requires employers to submit Social Security information, because PERS believes that there is limited value in the information due to variance in timing and items reported.

PERS believes that there is limited value in reporting the Social Security information due to variance in timing and items reported.

Based on existing documentation, PERS intended to use this Social Security information (W-2 reported wages) to determine discrepancies between actual wages reported to the federal government and wages reported to PERS. This information also could be used to identify where corrections should be made to service credit and issues if wages were reported under the wrong Social Security number.

PERS's Collection of Contributions

Public employers deduct contributions through a PERS-developed computer program.

The public employer is responsible for reporting accurate information to PERS regarding the correct earned compensation and contribution. However, the PERS Board of Trustees has the fiduciary responsibility to maintain the integrity of the funds within the PERS system.

According to MISS. CODE ANN. Section 25-11-123 (e) (1972), "The employer shall cause to be deducted on each and every payroll. . .the contributions payable by the member." MISS. CODE ANN. Section 25-11-123 (f) (1972) states that "the board shall provide by rules for the methods of collection of contributions of employers and members." Therefore, the employer has the primary responsibility of proper contribution collection as outlined by PERS regulations.

According to the PERS Agency Handbook, "the correct employee contributions must be collected by the agency." The handbook also states:

> *The Public Employees' Retirement System is responsible for maintaining complete and accurate wage and contribution records for all individuals covered under the retirement program. The individual's wage and contribution record contains all of his earnings in covered employment as reported by the respective employer. To determine eligibility and the proper amount of any benefits payable, all records maintained by PERS must be complete and correct.*

Therefore, it is the responsibility of the agency to report accurate information to PERS regarding the correct earned compensation and contribution information. However, the PERS Board of Trustees has the fiduciary responsibility to maintain the integrity of the funds within the PERS system. For example, if contributions are credited to the wrong account, an individual may be overpaid or underpaid at the time of retirement. While a retiree's record is reviewed at the time of retirement, it is important to assure the accuracy of the records for the employee during the employee's time of employment.

Required Uniform Formats

PERS requires uniform formats for data submitted by agencies through the computer program.

According to PERS Reporting Instructions:

> *PERS uses social security numbers and employee names as keys for tracking employee wages, contributions, and services credit. It is imperative that social security numbers and employee names be uniquely recorded for each employee reported. Since these records are maintained electronically incorrect social security numbers and or employee names will result in erroneous posting of accounts. It is the reporting agency's responsibility to report a correct social security number and name for each employee.*

PERS developed the Wages and Contribution Edit Program in 1994, with agency regulation requiring use in 1996.

PERS developed the Wages and Contribution Edit Program (Edit Program) in 1994, with agency regulation requiring use in 1996. The Edit Program allows member agencies to modify payroll data to create the current month's wages and contribution report or to import data from their payroll for the contribution report. The information required includes Social Security number of each payee; payee name, which includes last name, first name, middle initial; reporting wages for each employee; employee and employer contribution; and, salary amounts and number of months of that salary.

The Edit Program processes the employee and employer contribution rates and verifies the calculation of employee and employer contribution amounts from the data entered by the agency. The Edit Program validates fields for data within acceptable ranges, and checks for other common report errors, which may cause the data to be rejected. Once edit checks and calculation verification have passed, the Edit Program prints a Form 8 (Wage and Contribution report listing total contributions to PERS), creates a backup copy of the information for the agency, and copies the file to a disk for submission to PERS. PERS Regulation 14 requires that member employee and employer retirement contributions and disks are due on the fifth working day of each month. PERS authorizes employers to transfer funds electronically.

As of October 2002, seven local government agencies reported their wage and contribution information on paper because they are small agencies with no computers. Seven hundred forty-one agencies use the Edit Program software to save wage and contribution data to disk for PERS. The remaining 108 are state agencies. The state's Department of Finance and Administration's Statewide Payroll and Human Resources System (SPAHRS) completes these agencies' payroll. Therefore, DFA complies with the Edit Program specifications and reports wage and contribution data through SPAHRS for state employees.

PERS's Efforts to Check Submitted Data for Accuracy

PERS spends a large amount of its monthly posting time correcting name records and posting suspended records.

Once the agency has sent the wage and contribution report on disk and the Form 8, PERS must enter the data into the GENESIS computer system. All employee members have a file in the GENESIS system, generated by the original Form 1. Form 1 is the enrollment and demographic form that all members must have on file with PERS that includes beneficiaries.

The types of errors PERS encounters from public employer agencies include incorrect contribution information, employee name errors, Social Security number errors, and wage information errors.

PERS staff manually load seven hundred forty-one disks monthly into the computer system. After the data is entered into the system, PERS staff must then "accept" the data. In this acceptance process, PERS staff checks the contribution data that was loaded into the system and insures the data on the disk matches the Form 8, within a $5 tolerance. After PERS's staff accepts the contribution data, GENESIS runs a batch process, which creates error reports showing contribution and employee information problems. As of September 2002, PERS was completing the error reporting of the August contribution information. Two hundred sixteen employer agencies had error reports. The types of errors include incorrect contribution information, employee name errors, Social Security number errors, and wage information errors.

PERS must correct all errors before GENESIS will accept the records. The error correcting process takes two employees between twelve and fifteen days, or 192 to 240 hours per month.

Problems with Contribution Reporting and Non-Verification of Data

PERS has accepted contributions in the Public Employees' and Municipal Retirement Systems that were later ruled ineligible. PERS does not have an audit process for employer records, which could have detected the reporting errors.

PERS does not review service time, reported contributions, or average compensation until the time of retirement or when an employee requests a retirement estimate or other type of membership inquiry. PERS has accepted contributions for overtime pay that are not eligible for inclusion as compensation. This has occurred in the Public Employees' Retirement System and the Municipal Retirement System. PERS detected and has since corrected the overcollection by the two retirement systems.

PERS's Collection of Ineligible Compensation

Definition of Compensation within the Public Employees' Retirement System

According to MISS. CODE ANN. Section 25-11-103 (k) (1972), earned compensation is the full amount earned by an employee within that pay period, up to $150,000. However, MISS. CODE ANN. Section 25-3-39 (2) (1972) prohibits state employees from receiving compensation, including overtime, which exceeds that of their agency directors.

MISS. CODE ANN. Section 25-11-103 (k) (1972) defines earned compensation for Public Employees' Retirement System members as:

> *. . .the full amount earned by an employee for a given pay period including any maintenance furnished up to a maximum of One Hundred Fifty Thousand Dollars ($150,000.00) per year, and proportionately for less than one (1) year of service.*

MISS. CODE ANN. Section 25-3-33 (1972) sets the salaries of appointive state and district officials and employees for sixty-nine agencies and commissions. According to MISS. CODE ANN. Section 25-3-39 (2), the employees for these agencies cannot make more than the agency director's salary, which is statutorily set, through either regular compensation or overtime.

Currently, the PERS GENESIS system and DFA's SPAHRS system are programmed to cap compensation at the statutory limit of $150,000. However, no program check exists for exceeding the statutory cap of executive directors. According to DFA's Office of Fiscal Management, DFA cannot limit wages paid to an individual who makes more than the agency head.

PERS regulations for employers state the following:

> *The Public Employees' Retirement System is responsible for maintaining complete and accurate wage and contribution records for all individuals covered under the retirement program. The individual's wage and contribution record contains all of his earnings in covered employment as reported by the respective employer.*

State Agency Reporting of Ineligible Compensation

A state agency reported overtime compensation in 2001 and 2002 that exceeded the statutory cap of the executive director.

In 2001 and 2002, the Mississippi Bureau of Narcotics reported contributions on salary to which employees were not entitled. According to MISS. CODE ANN. Section 25-3-33 (1972), the Bureau of Narcotics agency director's salary is $60,000. The bureau paid salary, which included overtime for employees, that exceeded the agency director's salary cap.

PERS became aware of the over-reporting of compensation when contacted by two employees who were planning to retire. The Bureau of Narcotics allowed overtime for two employees in excess of the $60,000 salary cap, for three years before retirement, and reported overtime for another employee who was a sworn officer of the Highway Patrol and therefore was capped at that agency director's salary of $80,000.

PERS, as fiduciary, is ultimately responsible for ensuring that proper amounts are collected from members to ensure the proper amounts will be paid at the time of retirement. This is reinforced by MISS. CODE ANN. Section 25-11-121 (8) (1972), which states the Board of Trustees is the "custodian of the funds of the system."

PERS requested an Attorney General's opinion regarding the limitation of reportable compensation. The Attorney General released an opinion in July 2002 (Attorney General's Opinion 02-0224) that stated the employee cannot be paid in excess of the executive head and stated "responsibility for enforcing the provisions of Section 25-3-39 (2) lies first with the agency." The Attorney General released another opinion in September 2002 that stated Highway Patrol officers assigned to MBN salaries are capped at the agency director limit of the Commissioner of Public Safety, $80,000.

PEER does not dispute the Attorney General's opinion that each agency is responsible for sending the correct salary and contribution information to PERS. However, PERS, as fiduciary, is ultimately responsible for ensuring that proper amounts are collected from members to ensure the proper amounts will be paid at the time of retirement. This is reinforced by MISS. CODE ANN. Section 25-11-121 (8) (1972), which states the Board of Trustees is the "custodian of the funds of the system."

According to the July 2002 Attorney General's opinion, PERS is not required to pay retirement benefits based on salary that "exceeds that permitted by Section 25-3-39 (2)." PERS does have the responsibility based on MISS. CODE ANN. Section 25-11-131 (1972) to correct the error that has occurred. Therefore, MBN received a credit adjustment of $15,513 in order to repay the employee and employer contributions that were over-reported in 2001 and 2002 for one MBN agent and the patrol officer assigned to MBN. The other MBN employee withdrew his employee contributions in March 2002.

Municipal Retirement System's Collection of Ineligible Compensation

Definition of Compensation within the Municipal Retirement System

According to MISS. CODE ANN. Section 21-29-321 (1972), only regularly scheduled overtime for the last six months of employment can be included in employee compensation.

According to MISS. CODE ANN. Section 21-29-321 (1972):

> *For purposes of determining the "average monthly base salary and longevity pay" as provided in Sections 21-29-101 et seq., the wages to be considered shall be the average base salary and longevity pay which was received in consecutive pay periods immediately preceding retirement. This amount shall be the average of six (6) pay periods if the employee was paid monthly, or the equivalent if the pay periods are bi-weekly, semi-monthly or weekly. In addition, wages* ***may include holiday pay and regularly scheduled overtime pay earned for services performed during the last six (6) months of employment, as certified by the employer****. (PEER emphasis added)*

Therefore, an employee who has worked regularly scheduled overtime may include this compensation for retirement determination. However, if an employee has worked any other overtime, it may not be included within compensation for determining retirement benefits.

Municipal Employer Reporting of Ineligible Compensation

The City of Jackson reported overtime and lump sum leave pay, allowing higher retirement benefits than due for sixteen employees from 1996 to 2002.

PERS has overpaid benefits of $85,845 to these sixteen retirees. PERS requested repayment from the City of Jackson in November 2002.

PERS became aware of the overtime payments after an inquiry from a retiring officer, who requested an estimate of benefits. At this time, PERS conducted an audit of the City of Jackson's wage and contribution information, and found that non-regularly scheduled overtime payments and lump-sum leave payments were reported. According to the audit, in 1996 the City of Jackson began reporting all overtime payments and unused leave payments in the final average compensation. PERS found sixteen cases affected by the over reporting of compensation. Therefore, PERS has overpaid benefits of $85,845 to these sixteen retirees.

PERS requested repayment of the funds from the City of Jackson in November 2002. PERS also adjusted the retirement benefits of the sixteen retirees to reflect the correct benefit.

PERS is the fiduciary of the trust funds and is ultimately responsible for ensuring that proper amounts are collected from members to ensure proper amounts will be paid at the time of retirement. This is reinforced by MISS. CODE ANN. Section 25-11-121 (8) (1972), which states that the Board of Trustees is the "custodian of the funds of the system."

Method of Assuring Accuracy of Public Employer Data

While PERS has some control measures in place to check the accuracy of the data provided, it does not perform an audit of employer information. Currently, the Washington and Oregon retirement systems have audit programs that work with public employers in order to assure the accuracy of the data reported.

Currently, PERS has no method to assure that public employers follow all regulations and statutory provisions regarding compensation.

Monthly, PERS receives contribution collection information. At this time, records are checked against information within the GENESIS system. (See discussion, page 24.) While methods exist for correcting some errors, there are no methods to assure that the public employer is following all regulations and statutory provisions regarding compensation. Because of this, some compensation has been overreported within the Public Employees' and the Municipal Retirement systems. These errors might have been detected if an audit program had been in place as in other states.

Washington State Department of Retirement Systems

The Washington Department of Retirement Systems' Employer Audit Unit verifies employee compensation and assures that the employer follows applicable statutes and regulations.

Washington developed an Employer Audit Unit within the Department of Retirement Systems in the 1980s. Over twelve hundred employer agencies use the Washington state retirement system. The unit averages one hundred audits a year. The purposes for the audits are to verify:

- all employers who are being reported to the department are eligible to participate;
- all employees that should be participating in the system are being reported;
- compensation reported is in compliance with state law and regulations that relate to the system; and,
- recent retirees are receiving their benefit based upon correct average final compensation/final average salary.

This process also allows agencies to make corrections within the contribution information. Audits are conducted on the previous year information for all employees. The audit also checks employees who have retired and the years used for their average final compensation. The unit also provides a self-audit for all agencies to check their compensation records and make sure they are sending in the correct information and make any corrections necessary. This information is not sent to the department. This self-audit allows the agency to verify the same information as a unit audit and assists the employers in identifying any training needed.

Oregon Public Employees' Retirement System

The Oregon Employer Compliance Review Program works with public employers to assure that reported contributions comply with Oregon statutes and administrative rules.

Oregon developed the Employer Compliance Review Program in 2000. The program was developed to "promote teamwork between [Oregon] PERS and public employers in the areas of reporting and training needs" and to help employers report contributions and information according to Oregon statutes and rules. Over eight hundred agencies use the Oregon PERS. The Oregon PERS's first year of full on-site audits was in 2002, with fifteen agency audits.

Oregon has three types of reviews:

- A self-assessment is a questionnaire mailed to employers to complete and return to Oregon PERS. Oregon PERS evaluates the results and the employers receive a summary and suggestions, if any, for improving compliance or training needs.
- A compliance interview is a scheduled visit at the employer's worksite. The interview covers such topics as employer forms, contributions, subject salary, remittance advices, and annual reporting. The employer and a review team member discuss the questions and answers. The employer receives a summary of the discussion and suggestions regarding training or improving reporting.
- An on-site compliance review is an in-depth, scheduled review of employer records. PERS examines a sample of records such as payroll, W-2s, 1099s, and independent contracts that affect Oregon PERS reporting. The employer receives a summary of findings and required remedies.

Implementation of Laws and Regulations for Selected Employee Groups and Related Issues

As noted on page 1, in addition to reviewing administrative issues and investment performance at PERS, PEER reviewed PERS's implementation of laws and regulations for selected employee groups.

The first issue was whether PERS has complied with *PERS v. Hawkins*, infra, a Supreme Court ruling regarding the inclusion of travel expenses as compensation for Supreme Court justices and Court of Appeals judges. As discussed in the first section of this chapter, PERS has complied with the ruling.

The second issue PEER addressed was PERS's overpayment of $1.7 million to twenty-three retirees from 1987 to 2001. As discussed on page 34, PERS has instituted a repayment schedule with the retirees, but the entire amount will never be repaid due to the ages and income levels of the retirees.

During the course of reviewing the second issue, PEER found that PERS does not have a surety bond in place, as required by statute, for the executive director, nor does it have any type of public official or surety bond for the members of the Board of Trustees. This is necessary to protect the trust against the possible misspending of funds.

Compliance with *PERS v. Hawkins*

PERS has complied with PERS v. Hawkins, 781 So. 2d 899 (Miss. 2001), which required that travel reimbursements be included in the judges' compensation for purposes of computing retirement benefits for Supreme Court justices and Court of Appeals judges.

The Supreme Court began withholding retirement contributions on travel expenses in 1993 for three Supreme Court justices as allowed by the Department of Finance and Administration. PERS did not accept these contributions until 2001, after the former Chief Justice of the Supreme Court Armis Hawkins filed suit against PERS.

According to Supreme Court information, in 1993 three Supreme Court justices elected to have Social Security and retirement withheld from travel expense earnings as allowed by the Department of Finance and Administration's directive regarding taxable income. In December 1993, the justices made a payment for travel incurred from December 1992 through December 1993. The Supreme Court contacted PERS to seek clarification as to whether travel expenses could be included in earned compensation for the justices. PERS acknowledged the Attorney General's opinion to Robert L. Crook dated April 10, 1984, which allows for reimbursement of travel expenses to justices. PERS responded to the Supreme Court request by stating: "We do not find any provision in the PERS statutes which would permit the Retirement System to consider reimbursement for travel expenses to be reported and considered by the System for salary retirement purposes."

However, the Supreme Court withheld the employee and employer contribution of travel expenses for 1993 through 1995 and reported the contributions to PERS, as it believed was allowed by the 1984 Attorney General's opinion. PERS did not realize it was accepting the contributions until 1995, when Chief Justice Hawkins made a benefit inquiry at the time of retirement. The Supreme Court asked for a reevaluation of PERS's decision to not include travel expenses for retirement purposes. In 1997, PERS returned employee and employer contributions to the Supreme Court for the three justices.

Chief Justice Hawkins retired in 1995 and notified PERS that he was claiming retirement benefits based on the travel reimbursements. However, PERS had decided to not include travel expenses in earned compensation. Justice Hawkins filed suit in the Supreme Court against PERS in 1997 in order to have travel expenses included as earned compensation, require PERS to accept contributions, and to require PERS to include travel expense reimbursements as earned compensation.

The Supreme Court justices recused themselves from the decision, and pursuant to the Mississippi Constitution, a panel of special justices was appointed. This panel rendered a decision in 2001: "The amounts paid to Hawkins for reimbursement of meals, lodging, utilities, and mileage are included in the definition of 'earned compensation' for retirement purposes and shall be reported and considered for retirement purposes." The PERS Board of Trustees decided that the ruling applied to Supreme Court justices and Court of Appeals judges.

The Supreme Court paid the employer contribution for eleven retired and active Supreme Court justices and eight retired and active Court of Appeals judges in August 2002. All retired justices and judges have paid their employee contribution. PERS has requested that the Supreme Court collect the employee contributions for seven active justices and judges. PERS and the Supreme Court have requested the justices and judges to pay their part; however, as of October 2002, the seven judges and justices had not.

Overpayment of Retirement Benefits

Due to a clerical error, PERS did not adjust twenty-three accounts to comply with a benefit option selection, thus resulting in the overpayment of $1.7 million to these retirees.

PERS staff did not properly code twenty-three retirement accounts as selecting a benefit option that would have adjusted the retiree benefits at the age of 62.

PERS staff determined that benefits were overpaid to twenty-three retirees who retired during 1986 and 1987. Overpayment began in 1987 and continued through 2001, resulting in an overpayment of $1.7 million. Due to an error made in the PERS database by PERS staff not properly coding the accounts, the retirees' accounts did not reflect the selection of Option 4-C, the Social Security Leveling Option. Under Option 4-C, benefits received by the retiree from PERS should decrease once the retiree reaches age 62.

The correct coding information was not in the PERS computer system; therefore, the computer programs in place to identify Option 4-C retirees reaching age 62 did not select these improperly coded accounts for benefit reduction at the appropriate time. This error resulted in PERS's failure to reduce benefits of these retirees/beneficiaries once they reached age 62.

According to MISS. CODE ANN. 25-11-131 (1972):

> *Should any change or error in the records result in any member or beneficiary receiving from the retirement system more or less than he would have been entitled to receive had the records been correct, the board of trustees shall correct such error upon detection, regardless of the length of time between the reporting error or the time payment started and the time the board became aware of the error, and, as far as practicable, adjust the payment in such a manner that the actuarial equivalent of the benefit to which such member or beneficiary was correctly entitled shall be paid. This responsibility is, and has been, the duty of the board since the creation of the retirement system.*

At its June 19, 2001, meeting, the PERS Board of Trustees approved the following recovery plan for collecting the overpayments:

> *The overpayment will be recovered beginning September 1, 2001, after ample notice had been provided to each retiree, at the rate calculated*

based on 25% of the corrected monthly benefit and COLA as of July 1, 2001. At such time as the overpayment has been received, benefits will be restored to the corrected post age-62 amount and COLA. Such recovery will be made only until the monthly benefit is no longer payable due to death of the member/beneficiary or the expiration of the benefit based on the option selected. Affected individuals receiving the COLA in a lump sum will be allowed to elect to receive it on a monthly basis regardless of when the election is received.

The average age of the retirees in this group is seventy-one and full recovery of funds will not likely be realized during the lifetime of the retirees.

By recovering the Option 4-C benefit overpayments at the rate of 25% of the corrected benefit amount including the cost-of-living adjustment, the average length of repayment is 20.7 years, with full recovery requiring 39 years. The average age of the retirees is seventy-one and therefore, full recovery will not likely be realized during the lifetime of the retirees. Since voting to recover the overpayments at the rate of 25%, the PERS Claims Committee has heard appeals from two individual retirees who both requested a smaller, unspecified recovery amount due to financial hardships. The Board of Trustees reduced the rate of repayment to 1% in August 2001, to become effective in October 2001.

Lack of Bond Coverage as a Remedy of Overpayment of Benefits

PERS does not have any type of surety bond in place, which could have been used to repay overpaid retirement funds. PERS does not comply with MISS. CODE ANN. Section 25-11-121 (1972), which requires the executive director to give surety bond.

The MISSISSIPPI CODE does not require any type of bond or insurance of the PERS Board of Trustees. While the PERS Board of Trustees is covered under the Mississippi Tort Claims Board, the previous example of the Option 4-C overpayment would not be covered by tort claims.

PERS only retains a bond covering criminal misconduct. Such coverage would not be broad enough to cover misspending of funds that might be certified in error.

In order to protect the trust against the possible misspending of funds, as has occurred with the overpayment of retirement funds (see previous discussion, page 33), the Legislature required in MISS. CODE ANN. Section 25-11-121 (8) (1972) that the executive director of the Public Employees' Retirement System have a surety bond. Specifically, this section provides:

> *The board of trustees shall be the custodian of the funds of the system.* ***All expense vouchers and retirement allowance payrolls shall be certified by the executive secretary who shall furnish the board a surety bond*** *in a company authorized to do business in Mississippi in such an amount as shall be required by the board, the premium to be paid by the board from the expense account.* (PEER emphasis added)

In reviewing records of the retirement system, PEER determined that the agency only retains a bond covering criminal misconduct. Such coverage would not be broad enough to cover misspending of funds that might be certified in error by the executive director, and approved by the board as discussed in the previous example.

While PERS falls under the scope of the Tort Claims Act, some acts of PERS employees could result in loss to the trust fund that would not constitute negligent acts under the Tort Claims Act.

The executive director has asserted that the current bond is sufficient because the agency staff and board members are employees for purposes of the Mississippi Tort Claims Act (MISS. CODE ANN. Section 11-46-1 et seq. [1972]). The Tort Claims Act includes a partial waiver of the state's immunity for the tortious conduct of agencies committed by employees or officers acting in the course and scope of their employment. In tort claims, plaintiffs generally seek damages for injuries, death, or loss of property proximately caused by defendants. The PERS board staff cites research it prepared that asserts that the board and its staff are personally immune from actions brought under the provisions of Section 11-46-1 et seq. (1972) and that the state tort claims fund would insure the agency from tort actions brought against the Public Employees' Retirement System for damages. While the agency falls under the scope of the Tort Claims Act including all caps for negligent torts, some acts of employees of the agency could result in loss to the trust fund that would not constitute negligent acts under the Tort Claims Act.

PEER does not question that the agency is protected under the provisions of the Tort Claims Act for civil actions brought against the agency for damages to persons or property. PEER would note that it is customary to have bond coverage for key employees to insure the faithful performance of their duties. This includes the correct and accurate certification of records that, as a matter of law must be certified in order to pay individuals or firms, or to make transfers of money. When officers or employees err in such certifications, the action brought against them is not a tort action under Section 11-46-1 et seq., but an action by the State Auditor to recover misspent funds under Section 7-7-211(g). This provision states:

> *(g) To make written demand, when necessary, for the recovery of any amounts representing public funds improperly withheld, misappropriated and/or otherwise illegally*

expended by an officer, employee or administrative body of any state, county or other public office, and/or for the recovery of the value of any public property disposed of in an unlawful manner by a public officer, employee or administrative body, such demands to be made (i) upon the person or persons liable for such amounts and upon the surety on official bond thereof. . . .

This section is in no way abrogated by the Tort Claims Act.

Investment Performance

The Public Employees' Retirement System's investment program has performed consistent with market conditions over the past ten years while utilizing prudent policies and procedures in pursuing the program's objectives.

The investment philosophy of the Public Employees' Retirement System and its Board of Trustees is to ensure the prudent investment of the PERS's assets and the financial security of PERS members. The primary objective of the investment program is to provide adequate funding of current and future pension benefits. Through its asset allocation plan, PERS seeks to minimize the exposure risk of the investment portfolio.

Asset Value and Allocation

The Public Employees' Retirement System's investments have increased from a net assessed value of over $6.8 billion in 1993 to approximately $14.2 billion in 2002.

Return on Investments

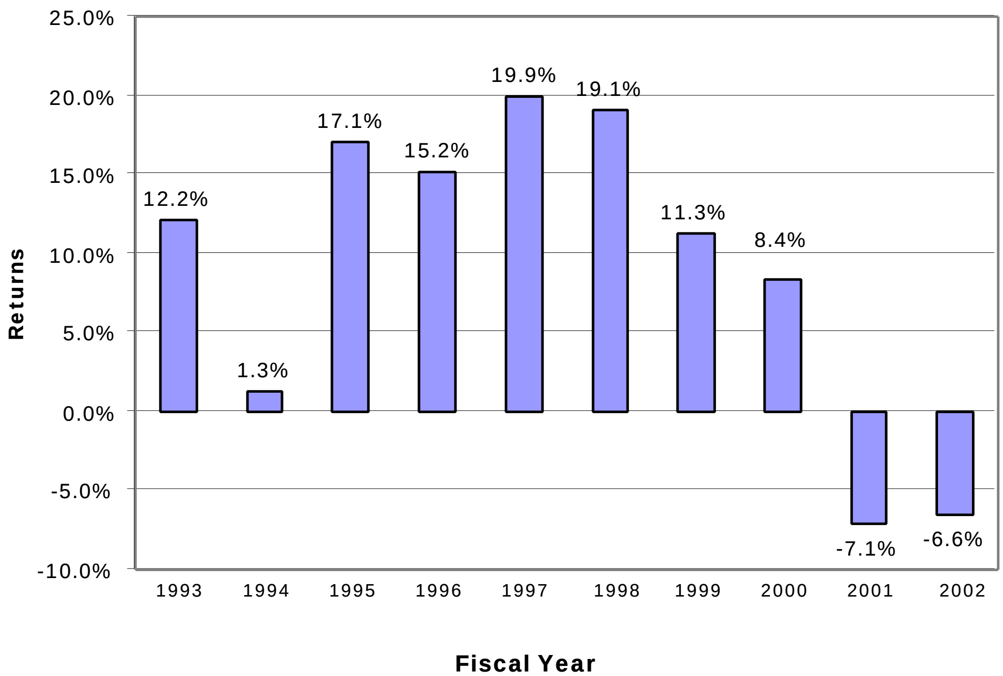
PERS's investment performance during fiscal years 2001 and 2002 has been consistent with the performance of leading market indicators.

The unusually high rates of return that occurred in the equity markets during most of the nineties were replaced by negative returns over the past two years. In light of market conditions, PERS's investment performance during fiscal years 2001 and 2002 has been consistent with the performance of leading market indicators. For example, during 2001, the Standard & Poor's 500 Stock Price Index experienced a 14.8% decline and the NASDAQ (National Association of Securities Dealers Automated Quotations) suffered a 45.4% loss.

Annualized Rate of Return: To express a rate of return for a period greater than one year or less than one year in terms of twelve months.

PERS's investments showed strong returns throughout the 1990s, outperforming the plan's minimum expected 4.25% rate of return, with the exception of 1994. (See Exhibit 7, page 38.) From 1993 until 2002, the annualized rate of return for PERS investments was 8.6%.

Exhibit 7: Return on PERS Investments, FY 1993-2002

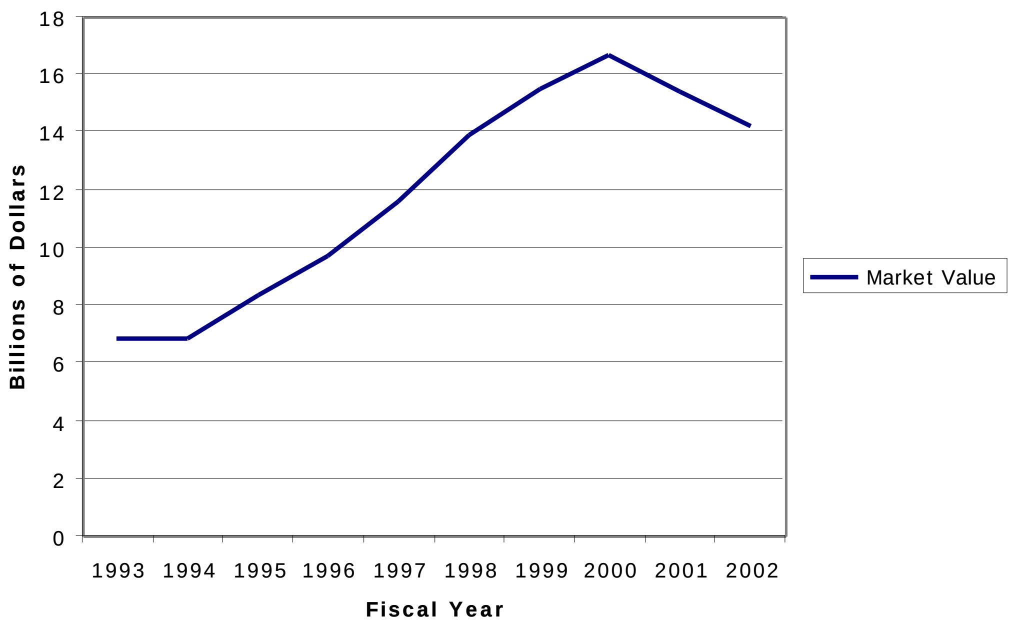


SOURCE: Public Employees' Retirement System's FY 2002 Presentation to the Legislative Budget Committee and the FY 2002 PERS CAFR .

The net asset value of the system has followed the same trend over the past ten years. The net asset value is determined by subtracting the fair value of securities lending investments and the interest and sales of securities lending from the market value of all investment securities, including those on loan.

Performing well throughout the nineties, the value of PERS investments grew from over $6.8 billion in 1993 to a peak of $16.7 billion in 2000. Due to the market volatility characteristic of the last two years, the value of the plan portfolio decreased during both 2001 and 2002 to the current market value of $14.2 billion, as of June 30, 2002. (See Exhibit 8, page 39.)

Exhibit 8: Net Asset Values of PERS Investments, FY 1993-2002



SOURCE: Public Employees' Retirement System Investment Division

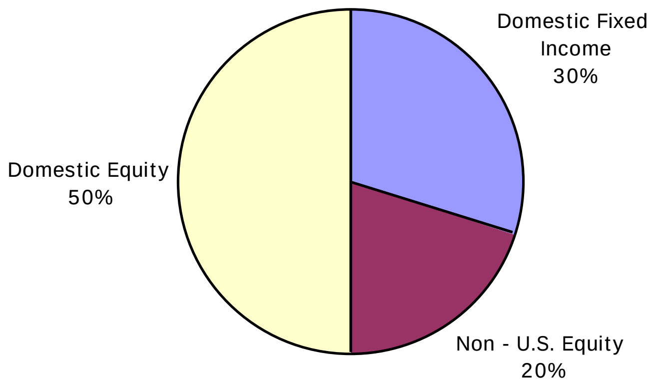
Asset Allocation

MISS . CODE ANN. Section 25-11-121 (1) (1972) specifies the types of investments in which PERS is authorized to invest. With respect to statutory guidelines, the Board of Trustees adopts the PERS investment policy, which determines the asset allocation plan (how PERS investments are distributed among different asset classes). PERS performs asset allocation studies every four to five years. The Board of Trustees adopted the current long-term asset allocation plan in Fiscal Year 2000.

PERS's asset allocation is based on projected future liabilities and statutory investment restrictions.

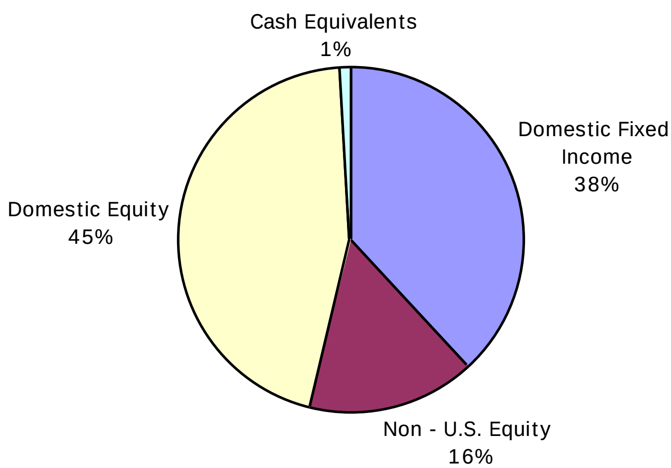
In order to provide adequate funding of current and future pension benefits, the asset allocation is based on projected future liabilities and statutory investment restrictions. The current PERS asset allocation plan targets 50% of funds invested in domestic equity, 30% of system investments in domestic fixed income, and 20% of funds invested in non-U.S. equity. (See Exhibit 9, page 40.) The fund's actual asset allocation as of June 30, 2002, is 45% domestic equity investments, 38% domestic fixed income investments, 16% non-U.S. equity, and 1% cash equivalents. (See Exhibit 10, page 41.)

Exhibit 9: Long-Term Target Asset Allocation as Adopted by PERS Board of Trustees



SOURCE: PERS 2002 Comprehensive Annual Financial Report

Exhibit 10: Actual Asset Allocation, FY 2002



SOURCE: PERS 2002 Comprehensive Annual Financial Report

Fees for Investment Advisors/Managers

PERS's process for selecting investment managers enables it to negotiate reasonable investment manager fees.

Selection of Investment Advisors

PERS's process for selection of investment managers is comparable with the practices of other states.

The PERS Board of Trustees hires investment managers to make decisions about how funds are invested in order to achieve the objectives of the system. The board sets screening criteria used when PERS adds a new investment manager. Based on these criteria, PERS submits a request to its investment management consultant Callan Associates to perform a screening process that will produce a list of twelve to fifteen potential management firms. With Callan, PERS staff reviews the firms presented to evaluate each potential firm. Callan and PERS Staff analyze each firm and mutually select three candidates to submit to the Board of Trustees. The three selected candidates are invited to make a presentation to the board, which makes the final selection of a new management firm.

PERS's process for selection of investment managers is comparable with the practices of other states. Most surrounding states utilize an investment management consultant, such as Callan Associates, whether in conjunction with a formal request for proposal process or through a screening process performed exclusively by the consultant. Arkansas, Louisiana, and Tennessee use an external consultant to recommend and evaluate possible management firms, following a process similar to the one utilized by PERS. Arkansas and Tennessee both use Callan Associates as their investment management consultant. The Georgia retirement system staff conducts research and evaluations and makes recommendations to the system's governing committee for final selection without the use of an external consulting firm. In Florida, staff performs initial research independently and makes selections before conferring with Callan Associates for additional input and narrowing the group to firms selected for interviews, when staff makes the final selection of new investment management firms.

Use of Callan Associates as an Investment Management Consultant

Through a formal request for proposals process in 1996, the PERS Board of Trustees hired Callan Associates as investment management consultant. PERS employs Callan to calculate the total investment return of the system, as well as the performance of each investment management firm employed by the Board of Trustees to invest the system's assets. Callan also provides a manager search service to recommend potential investment management firms.

In an effort to provide objective information and reduce the potential for conflicts of interest, Callan Associates reports that it observes the following procedures and practices:

- *Code of Ethical Responsibility*--Callan emphasizes the quality of information it provides, the degree of professionalism, honesty and integrity in the collection, processing and dissemination of information.

- *Full Disclosure*--Callan provides full disclosure of all business activities and relationships to its membership. Every year, or on request, Callan furnishes clients with a complete list of all investment managers who do business with their Institutional Consulting Group and who are members of the Callan Investments Institute. All new clients receive this information at the onset. Additionally, in manager search candidate reports prepared for clients, Callan indicates whether any manager search candidate included in the report does any business with Callan.

- *Oversight Committees*--In services where the potential for conflict of interest is high, such as the manager search process, Callan attempts to eliminate bias through a formal, internal oversight system. Callan's Manager Search Committee, composed of thirteen senior consultants, verifies the accuracy, completeness, and objectivity of data gathering, due diligence, and evaluation used during the manager screening process.

- *Separation of Profit Centers*--Callan groups that serve investment managers --the Institutional Consulting Group (ICG) and the Callan Investments Institute (CII)--operate as separate profit centers within the firm, maintaining their own staffs, as well as their own profit and loss accounting systems. Callan does not involve personnel from these groups in any manager search activity or fund sponsor consulting.

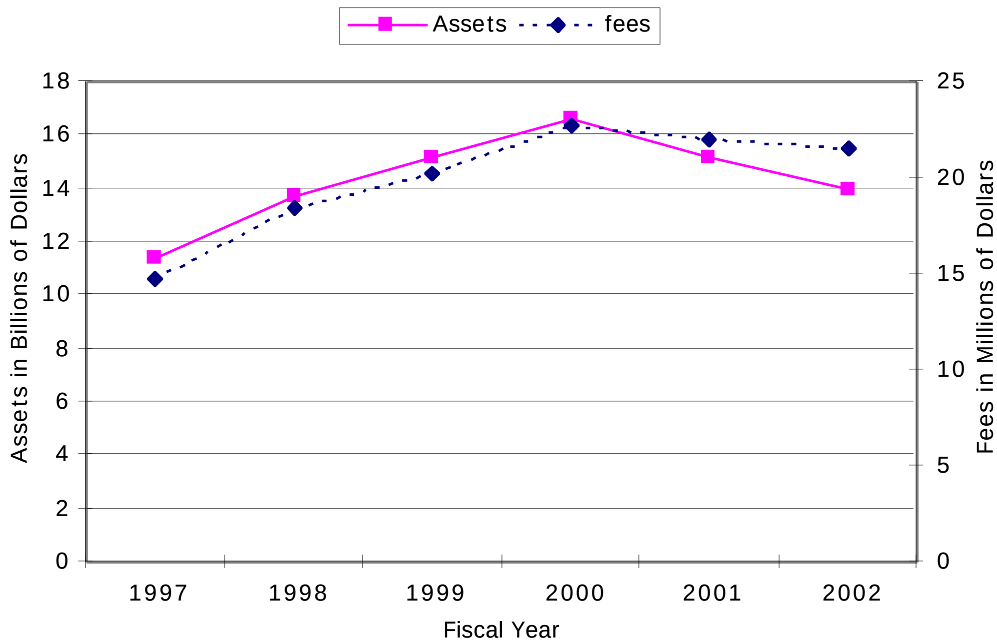
Management Fees and Funding for PERS Investment Managers

Because management fees are computed based on the value of assets, management fees have fluctuated at a rate comparable to that of the assets under management.

While an investment management consultant such as Callan Associates provides information and performs a variety of services such as assisting with investment manager searches, investment managers are responsible for making investment decisions regarding how funds are to be invested. One component of the investment manager search screening criteria is that the management firm must be willing to negotiate management fees if selected by the board, which is the practice of surrounding states. Upon selection by the board, management firms typically present a fee schedule from which PERS most often negotiates down. As part of the negotiation, PERS utilizes information on average management fees. Management funding agreements negotiated by PERS are a set fee schedule.

Fees for management firms are determined by the entire assets of the accounts under the management of the investment advisor. (See Exhibit 11, page 44.) Therefore, because management fees are computed based on the value of the assets, management fees have fluctuated at a rate comparable to that of the assets under management.

Exhibit 11: Comparison of System Assets and Annual Investment Management Fees



SOURCE: PERS Comprehensive Annual Financial Report, 1997 - 2002

PERS has been successful in negotiating reasonable investment management fees. During the investment manager search process, PERS reviews the management fee schedules submitted by potential management firms. Once the board has made its final selection, PERS staff has a broad knowledge of typical fee schedules offered by management firms and uses this information in negotiating management fees. In addition, Callan Associates is aware of PERS's fee sensitivity and takes that factor into consideration when screening management firms for potential candidates during the search process. Firms that require a high fee schedule are usually eliminated from the candidate pool before any recommendations are made to PERS.

Since FY 1997, less than 0.2% of funds from the retirement system have been used to pay investment manager fees.

As a result of the selection and fee negotiation process, PERS is paying reasonable management fees to its portfolio managers. According to survey data compiled by a financial research firm, Greenwich Associates, compared to other state retirement plans participating in the survey, management fees paid by PERS are consistently lower than those of other plans. Since Fiscal Year 1997, less than 0.2% of funds from the retirement system have been used to pay investment manager fees. (See Exhibit 12, page 45.)

Exhibit 12: Annual Management Fees as Percentage of Managed Fund Assets

Fiscal Year	Annual Management Fees	Percent of Fund Assets
1997	$14,802,703	0.130%
1998	$18,431,277	0.135%
1999	$20,216,062	0.133%
2000	$22,681,345	0.137%
2001	$22,029,124	0.145%
2002	$21,495,764	0.153%

SOURCE: Analysis of PERS Comprehensive Annual Financial Report, 1997 - 2002

Funding of Investment Management Accounts

When a new investment manager is added, PERS determines how much to invest with the firm based on several factors. These factors include the size of the firm and the management class. For example, index funds tend to be larger management accounts and small capitalization managers tend to manage smaller accounts for the system. Based on the asset class, domestic equity, non-U.S. equity, or domestic fixed income, PERS prefers that its accounts be no more than 25% of a firm's assets in a particular class. Over time, the length of PERS's relationship with the firm impacts the size of investment with a particular firm. Most of PERS's large accounts are accounts that have been in place approximately twenty years.

Selection of Brokerage Firms

PERS's use of the Commission Recapture Program has enabled PERS to benefit from investment managers' use of selected brokerage firms without inhibiting the performance of investment managers.

Management firms are hired to decide what funds are invested where in keeping with direction from PERS; management firms then use brokerage firms to make transactions for the accounts, matching up buyers and sellers. Once a management firm is selected, PERS does not play a direct role in the selection of brokerage firms.

However, in the 1980s, PERS developed a Commission Recapture Program in an effort to recapture a percentage of brokerage commissions. Expanding the program in 1997, PERS performed an analysis of the trading habits of its external managers to determine which brokers were being used most frequently without any influence or requirements from PERS. This analysis produced a subset of firms that investment managers were most likely to utilize if they were included in a recapture program. PERS sought relationships with those more heavily used brokers either directly or indirectly through commission recapture firms. In return for directing trades to certain brokers, a portion of the commissions generated on those trades is returned to the plan.

For example, the brokerage firm agrees to rebate one cent of a three-cent commission on each trade back to PERS. Unlike arrangements where "rebated" funds are used to pay expenses "off the books" of a plan, commission recapture dollars are accounted for and put directly back into the PERS investment fund. PERS does not have an established schedule for evaluating firms for possible inclusion in the program; however, it does periodically review and renegotiate recapture rates with existing providers. PERS informs all of its investment managers of the Commission Recapture Program, but does not require that managers use brokerage firms participating in the program.

Additionally, PERS does not have any influence on the amount invested by each brokerage firm, the management of brokerage accounts, or the determination of brokerage commissions. PERS has limited oversight of brokerage transactions in that it receives periodic updates by which it monitors transactions. PERS uses this information to monitor for anomalies in brokerage commissions. Most surrounding states use a similar approach regarding brokerage firms. Typically, investment officers in surrounding states do not direct or influence the selection of brokerage firms and only periodically monitor broker transactions.

Since expanding the Commission Recapture Program in 1997, PERS has reported $7,100,000 in income from the program.

PERS's use of the Commission Recapture Program has not inhibited the performance of investment managers because the program does not require that investment managers use the brokerage firms included in the program. By including brokers most commonly used by existing manager accounts and not placing requirements on the managers regarding the use of specific brokerage firms, PERS benefits from the use of brokerage firms in the program by the investment managers. Since expanding the program in 1997, PERS has reported to its membership in the Comprehensive Annual Financial Report the income derived from the Commission Recapture Program. This income has totaled $7,100,000 during fiscal years 1997 through 2002. (See Exhibit 13, page 47.)

Exhibit 13: Commission Recapture Income, FY 1997–2002

Year	Income
1997	$371,000
1998	874,000
1999	471,000
2000	1,275,000
2001	1,191,000
2002	2,918,000
Total	**$7,100,000**

SOURCE: PERS Comprehensive Annual Financial Reports, Fiscal Years 1997–2002.

Recommendations

Capital Improvement Projects

1. Should the Legislature wish the Bureau of Building to oversee the PERS renovation projects, it should include language in the PERS FY 2004 appropriation bill to require the bureau to assist in the renovation projects through construction program management, which includes independent oversight of the professional and construction teams, as well as monitoring and adherence to the job schedule and the review of change orders.

2. In accordance with requirements in the PERS appropriation bills, the Department of Finance and Administration should ensure that the Mississippi Comprehensive Annual Financial Report includes expenses for the renovation of the two PERS buildings and that all expenditures for the renovation projects continue to receive its review and approval.

Contribution Collection

3. PERS should study its contribution collection system to develop accuracy controls in order to meet its fiduciary responsibility to assure accurate reporting. The areas that should be studied include annual verification of Social Security information as required by MISS. CODE ANN. Section 25-11-123 (f) (1972); methods to correct monthly reporting errors from public employers; periodic random audits of data collected; and automated system controls within GENESIS for checking of over-reported wages.

   If PERS does not believe that it is practicable to gather the Social Security information or if other sources of comparable data are more accurate and appropriate, PERS should develop an alternative and recommend that this section be repealed.

Bond

4. PERS should comply with the provision in MISS. CODE ANN. Section 25-11-121 (1972) that requires that the executive director acquire a surety bond.

5. PERS should review its decision with respect to the purchase of bond coverage for its board members. In light of the fact that board members are in a position to certify expenditures in error, PERS should consider whether it would be advisable to procure fiduciary insurance or public official bond for the members of the PERS board.

PERS
PUBLIC EMPLOYEES' RETIREMENT SYSTEM OF MISSISSIPPI
PROVIDING SECURITY FOR YOUR FUTURE
PUBLIC EMPLOYEES' RETIREMENT SYSTEM BUILDING
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JACKSON, MISSISSIPPI
39201-1005
(601) 359-3589
1-800-444-PERS
FRANK READY
Executive Director

December 16, 2002

Dr. Max Arinder, Executive Director
Performance Evaluation Expenditure Review Committee
501 N. West Street
3rd Floor, Woolfolk Building
Jackson, MS 39201

Dear Dr. Arinder and Members of the Committee:

The PEER Committee has concluded its five-month review of the PERS' administration of the retirement system and has presented its findings and recommendations. PERS is pleased to have the opportunity to respond to this generally positive report.

Much of the PEER report was devoted to the Wage and Contribution reporting processes. Our comments to the findings on this process will be found in the response to PEERS' third recommendation.

RESPONSES TO RECOMMENDATIONS

1. **Should the Legislature wish the Bureau of Building to oversee the PERS renovation projects, it should include language in the PERS FY 2004 appropriation bill to require the bureau to assist in the renovation projects through construction program management, which includes independent oversight of the professional and construction teams, as well as monitoring and adherence to the job schedule and the review of change orders.**

   While PERS has no objection with receiving assistance with the projects from the BOB and welcomes constructive criticism that will enhance the project, the ultimate responsibility for the success of the project rests with PERS, and as such, PERS is reluctant to relinquish the responsibility of project management to the BOB. PERS executive staff, in conjunction with the architectural firm, have managed the capital improvement projects in the best interest of PERS. While PERS executive staff may not have specific architectural or construction project management experience, the staff does have project management experience and has been very diligent in managing projects in the best interests of PERS.

2. **In accordance with requirements in the PERS appropriations bills, the Department of Finance and Administration should ensure that the Mississippi Comprehensive Annual Financial Report includes expenses for the renovation of the two PERS buildings and that all expenditures for the renovation projects continue to receive its review and approval.**

   Whether DFA segregates and reports the costs associated with PERS capital projects in the State's CAFR is a matter for discussion between DFA and their auditors. All costs associated with all PERS capital projects are expended in accordance with all applicable statutes, as well as, purchasing rules and regulations. Costs for PERS capital projects are reported annually in its CAFR. As a matter of record, all costs associated with PERS capital projects, as well as the administration of PERS, are reported in the State's CAFR.

3. **PERS should study its contribution collection system to develop accuracy controls in order to meet its fiduciary responsibility to assure accurate reporting. The areas that should be studied include annual verification of Social Security information as required by Miss. Code Ann. Section 25-11-123(f); methods to correct monthly reporting errors from public employers; periodic random audits of data collected; and automated system controls within Genesis for checking of overreported wages.**

   If PERS does not believe that it is practicable to gather the Social Security information or if other sources of comparable data are more accurate and appropriate, PERS should develop an alternative and recommend this section be repealed.

   PEER has recognized that PERS has implemented certain controls in meeting its fiduciary responsibility to employ reasonable means to ensure that information on members reported from the employing agency is correct. PEER also recognized that PERS accepted contributions in the form of non-regularly scheduled overtime for certain municipal fund members which although CERTIFIED BY THE EMPLOYER were later ruled ineligible. Likewise, PEER also commented in the report on a situation in which PERS refused to accept contributions on amounts paid to a member which it felt was not lawful compensation based on the law. The amounts paid were later determined by a court of law to be reportable compensation and contributions due on those amounts. Under each of these situations, PERS took appropriate steps to correct the member's record once a final determination was made. It is questionable whether the first of these situations, i.e., the reporting of non-regularly scheduled overtime, could have been detected by any normal audit procedure, and it is certain that the second situation could not have been prevented by any such audit process as it was related to an interpretation of the law.

The Public Employees' Retirement System is a very complex plan covering all types of governmental employees and all types of payroll systems. Overlaying that complexity is the fact that there are some 27 different types of retirement systems each with separate rules and benefit structures. In addition, there are some employers, such as the City of Jackson, that have employees in the same job position reported to different retirement systems with different reporting requirements. To add to this complexity, the employer must make judgement calls as to whether an individual is in a covered position as positions of less than half-time, as well as sporadic or intermittent employment are not covered. Likewise, the employer may in some cases have to make determinations as to whether payments are regular periodic compensation and not litigation fees, bond fees or other similar extraordinary non-recurring payments which should not be reported to PERS.

These are but a few of the ways that a reporting error might occur even in good faith. Add to that, the various state laws which prohibit amounts which might be paid as bonuses, unlawful donations, or amounts in excess of what is supposed to be a statutory salary cap (but which are actually paid), and you will see that reporting of wages to PERS is not the precise science that lends itself to standardized edits or approaches. Because of the variations in the way compensation is set and paid, PERS must rely on the integrity of the information certified to it by the employer unless it clearly finds a pattern of wrongdoing or error that it is obligated to question and later correct if appropriate.

PEER noted in its Report the amount of effort PERS staff spends in correcting information so that it can be posted to the member's account. The vast majority of the corrections PERS makes each month in the posting of wages and contributions are detected by the Edits already in place and relate to the manner in which the individual's name is shown on the report where there has been a name change which has not been reported to PERS or where a new employee is reported but the Agency has not previously filed a Form 1 on the new employee. Very little of PERS's efforts in posting the reports are the result of correcting wage information as PERS does not have the necessary information at that time to know that wages being reported are incorrect. One of the edits already in place verifies that correct contributions are being remitted on the reported wages.

PERS agrees that it should continue its efforts to educate payroll officers on the proper reporting of retirement earnings. As PEER is aware, individual agency representatives certify the accuracy of the reporting information when it is submitted. Even with this assurance, PERS takes its role in providing reporting directions seriously and as a result conducts regular training programs, has provided a dedicated Employer Hotline for direct employer access to staff in the Wage and Contribution Department, and enhanced the Employer Updates in which we highlight various reporting problems and rulings of the Attorney General which affect earnings and contributions reportable to PERS. PERS is in the process of introducing Internet Reporting of Wage and Contribution Information and will use this opportunity to review reporting criteria and guidelines.

In assessing the responsibility for proper reporting, we believe that PEER is under-emphasizing the direct responsibility of the individual agency itself as well as other control agencies such as the State Personnel Board, the State Department of Audit and the Department of Finance and Administration for ensuring that certain federal and state laws are not violated in the payment of income to an employee. Attorney General Opinion dated July 26, 2002, recognizes that the responsibility for enforcing the provisions that provide that state employees can not be paid in excess of the salary/compensation of the Executive Director lies first with the Agency. Responsibility also lies with the State Personnel Board, State Auditor and the Department of Finance and Administration.

The Attorney General has also recognized that PERS has the duty to inquire regarding contributions it believes are outside those permitted by law. Further, if that inquiry results in a determination that contribution have been received for a salary that exceed that permitted by law, then PERS must proceed accordingly and make any necessary corrections.

It must be acknowledged that PERS does not in fact control, and cannot prevent, how much a state agency actually pays an employee where such payment conflicts with either agency policy or state law; likewise it can not control other situations where payments are made in excess of the amount specified in a particular contract or amounts in excess of allowable unused leave payments at termination or retirement. PERS can only attempt to identify these situations, particularly where they are used to inflate retirement benefits, and take steps to correct them when they are found.

PERS does not now nor has it ever had the internal staff to provide a full scale payroll audit of each participating employer prior to the monthly report and contribution due date. With 856 employers covering 155,000 employees, such a task would be impossible. Thus, PERS must accept what is certified to it as accurate by the Employer until such time as information indicates otherwise.

PERS can and will review its resources with regard to auditing compliance of employers in reporting members and compensation after the submission of records. To do so however, PERS will need additional staff dedicated to auditing employer compliance with reporting laws and the travel budget to allow such staff to move throughout the state. In addition, PERS feels that its efforts in this regard would be enhanced if:

1) DFA as the party responsible for actual payroll responsibilities for state employees were to program its payroll system to prevent the payment of amounts in violation of state law; and
2) The Legislature were to provide meaningful penalties for chronic or intentional violation of PERS reporting requirements.

Finally, PERS will review current efforts to assist participating employers with reporting and will review what role, if any, the collection of Social Security information can play in enhancing accurate reporting by Employers.

4. **PERS should comply with the provision in MISS. CODE. ANN. Section 25-11-121 that requires that the executive director acquire a surety bond.**

PERS is in the process of securing a surety bond for the executive director in accordance with the provision in MISS. CODE ANN. Section 25-11-121.

After speaking with the Office of the State Auditor, it is PERS understanding that the Auditor's office has never made a demand for the recovery of public funds misspent as a result of a clerical error. Generally, action under MISS. CODE ANN. Section 7-7-211(g) is reserved for intentional acts or acts of wrongdoing. PERS is unsure as to what, if any, action might be taken by the State Auditor to collect on an official bond in situations that result from a clear clerical error. Thus, PERS is not sure that such coverage would have provided or will provide the protection to the trust fund that PEER suggests. However, PERS will investigate whether other coverage is available which would reimburse the fund in the event of a loss resulting from such clerical error.

5. **PERS should review its decision with respect to the purchase of bond coverage for its board members. In light of the fact that board members are in a position to certify expenditures in error, PERS should consider whether it would be advisable to procure fiduciary insurance or public official bond for the members of the PERS board.**

PERS is currently researching the protection that would be afforded the trust fund, as well as board members, with the purchase of fiduciary insurance. PERS will review its decision with respect to the purchase of bond coverage for its board members and consider whether it would be advisable to procure fiduciary insurance or public official bond for the members of the PERS board.

Should you have any additional questions, please contact my office.

Sincerely,

Frank Ready

Frank Ready
Executive Director

STATE OF MISSISSIPPI
DAVID RONALD MUSGROVE, GOVERNOR

DEPARTMENT OF FINANCE AND ADMINISTRATION

GARY ANDERSON
EXECUTIVE DIRECTOR

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PEER
COMMITTEE

December 10, 2002

Honorable William Canon, Chairman
Joint Committee on Performance Evaluation and Expenditure Review
Post Office Box 1204
Jackson, Mississippi 39215-1204

Via Hand Mail

Dear Chairman Canon:

I have reviewed the draft **Review of the Administration of the Public Employees' Retirement System** prepared by the PEER Committee and offer the following response from the Department of Finance and Administration.

The report states:

> **"Although the Bureau of Building approved PERS's architectural contract and reviewed its renovation plans as required by state law, PERS did not use the bureau as its construction manager."**

DFA responds:

> **In accordance with Section 31-11-3(7), the Department of Finance and Administration, acting through the Bureau of Building, Grounds and Real Property Management, is responsible for the review and preapproval of architectural or engineering service contracts entered into by any state agency, institution, commission, board or authority. In this capacity, DFA has reviewed and preapproved the professional service contract agreement between PERS and Cooke, Douglass, Farr, Lemons Architects.**

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December 10, 2002
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The report states:

> **"Also, DFA approved PERS's building expenditures through the state accounting system, but in order to meet all requirements of the appropriation bill, DFA will have to add information to the Mississippi Comprehensive Annual Financial Report to show all expenditures."**

DFA responds:

> **The Mississippi Comprehensive Annual Financial Report includes PERS's expenditures for the renovation projects undertaken. PERS's independent audit of its operations is incorporated in the CAFR. The Notes to the Financial Statements of the Mississippi CAFR direct the reader to PERS's Comprehensive Annual Financial Report, which details this information.**

The Department of Finance and Administration appreciates the opportunity to provide this information to the PEER Committee in response to the referenced report. I trust this fully addresses your concerns.

Sincerely,

Gary Anderson

Gary Anderson

PEER Committee Staff

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