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STATE OF RHODE ISLAND  
**EMPLOYEES' RETIREMENT SYSTEM**

Independent Auditor's Report on Internal Control Over Financial Reporting  
and on Compliance and Other Matters Based on an Audit of Financial  
Statements Performed In Accordance With *Government Auditing Standards*

Schedule of Findings and Responses

FISCAL YEAR ENDED JUNE 30, 2010

Dennis E. Hoyle, CPA  
Acting Auditor General

Office of the Auditor General  
General Assembly - State of Rhode Island

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STATE of RHODE ISLAND and PROVIDENCE PLANTATIONS  
GENERAL ASSEMBLY

OFFICE of the AUDITOR GENERAL

- ◆ INTEGRITY
- ◆ RELIABILITY
- ◆ INDEPENDENCE
- ◆ ACCOUNTABILITY

March 11, 2011

JOINT COMMITTEE ON LEGISLATIVE SERVICES:

SPEAKER Gordon D. Fox, Chairman

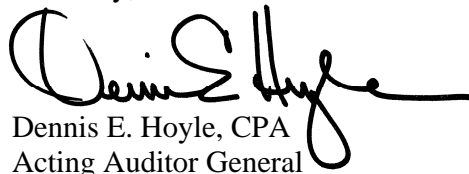
Senator M. Theresa Paiva-Weed  
Senator Dennis L. Algieri  
Representative Nicholas A. Mattiello  
Representative Robert A. Watson

We have audited the financial statements of the Employees' Retirement System of the State of Rhode Island (the "System") for the year ended June 30, 2010 and have issued our report thereon dated December 20, 2010. The System's financial statements and our independent auditor's report thereon are included in a separate audit report entitled *STATE OF RHODE ISLAND EMPLOYEES' RETIREMENT SYSTEM - FISCAL YEAR ENDED JUNE 30, 2010*.

In accordance with *Government Auditing Standards*, we have also prepared a report, dated December 20, 2010 and included herein, on our consideration of the System's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations and contracts.

We noted certain matters involving internal controls, and other operational matters that are presented for your consideration. These comments and recommendations are intended to enhance internal control or result in other operational efficiencies.

Sincerely,



Dennis E. Hoyle, CPA  
Acting Auditor General

**EMPLOYEES' RETIREMENT SYSTEM OF THE STATE OF RHODE ISLAND**

FISCAL YEAR ENDED JUNE 30, 2010

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- ◆ INTEGRITY
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**INDEPENDENT AUDITOR'S REPORT ON INTERNAL CONTROL OVER  
FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS  
BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED  
IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS**

JOINT COMMITTEE ON LEGISLATIVE SERVICES, GENERAL ASSEMBLY  
STATE OF RHODE ISLAND AND PROVIDENCE PLANTATIONS:

RETIREMENT BOARD OF THE EMPLOYEES' RETIREMENT SYSTEM OF THE  
STATE OF RHODE ISLAND:

We have audited the statements of fiduciary net assets of the Employees' Retirement System of the State of Rhode Island (the System) as of June 30, 2010 and the related statements of changes in fiduciary net assets for the year then ended, and have issued our report thereon dated December 20, 2010. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the System's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the System's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the System's internal control over financial reporting.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses and therefore, there can be no assurance that all deficiencies, significant deficiencies, or material weaknesses have been identified. However, as described in the accompanying Schedule of Findings and Responses, we identified a deficiency in internal control over financial reporting that we consider to be a material weakness.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the System's financial statements will not be prevented, or detected and corrected on a timely basis. We consider the deficiency described in the accompanying Schedule of Findings and Responses under Finding 2010-1 to be a material weakness.

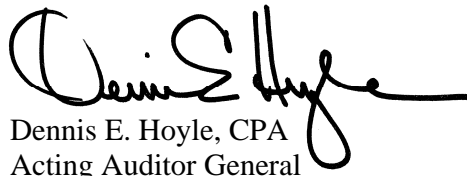
Compliance and Other Matters

As part of obtaining reasonable assurance about whether the System's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, and contracts, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

We did, however, note certain other matters that we reported to management of the System in the accompanying Schedule of Findings and Responses.

The System's responses to the findings identified in our audit are included in the accompanying Schedule of Findings and Responses. We did not audit the System's responses and, accordingly, we express no opinion on it.

This report is intended solely for the information and use of the members of the Retirement Board, the State Investment Commission, System management, the Joint Committee on Legislative Services, and the House Committee on Finance, General Assembly, State of Rhode Island and Providence Plantations and is not intended to be and should not be used by anyone other than these specified parties.



Dennis E. Hoyle, CPA  
Acting Auditor General

December 20, 2010



**EMPLOYEES' RETIREMENT SYSTEM  
OF THE  
STATE OF RHODE ISLAND**

**SCHEDULE OF FINDINGS AND RESPONSES**

**FINDING 2010-1**

**IMPROVE CONTROLS OVER THE RELIABILITY OF CONTRIBUTIONS RECEIVABLE FOR FINANCIAL STATEMENT PURPOSES**

Contributions from both employees and employers are recognized as revenue (additions) based on employer payroll activity – contributions are considered receivable when wages are paid to the employee. For financial reporting purposes, contributions receivable at June 30 are derived from (1) the ANCHOR wage and contribution system based on actual contributions data submitted, without cash remittance to the system prior to the end of the fiscal year, and (2) an analysis performed to calculate contributions receivable based upon actual contribution data received after the end of the fiscal year relating to payroll periods prior to the end of the fiscal year.

The year-end analysis of contributions receivable can be improved to provide a higher level of assurance that the contributions receivable balances are accurately recorded. Our audit procedures in prior years found several instances where one or more of the contributions receivable balances were misstated.

Our 2010 audit found another instance where one of the receivable balances (and related revenue balance) was misstated – both were understated by \$6.5 million. Specifically, the System typically performs an analysis at year-end to calculate employee and employer contributions accruals for the teacher units within the ERS fund. The 2010 analysis resulted in an appropriate accrual related to the employer portion of this receivable. ERSRI did not, however, accrue the receivable due from the employee share (because of an oversight).

The System should adopt certain control procedures that would help to prevent or detect misstatements in the contributions receivable balances. This should include a written policy describing standard close-out procedures. This policy should require specific analytical procedures that would aid in determining whether or not the receivables balances are complete in all material respects (in fact, this is how we discovered that the balance was understated by \$6.5 million in 2010).

**RECOMMENDATION**

2010-1            Implement control procedures over the manual processes used to calculate contributions receivable at fiscal year end for financial reporting purposes.

**Auditee Views:**

*The System has over 190 participating member units that submit wage and contribution data into the ANCHOR system on various payroll frequencies. The process for analyzing contributions receivable is reviewed by the accounting department. However, given the various pension reforms enacted during the 2010 session, additional off-line efforts were required to be immediately implemented to comply with the enacted budget articles. The limited resources of the accounting department dedicated a significant amount of time to these additional year-end efforts and inadvertently omitted the referenced transaction.*

*Currently, ERSRI is seeking to procure a new accounting system in addition to an updated line-of-business system in which it will develop enhanced capability for computing, recording, and tracking accounts receivable.*

**SCHEDULE OF FINDINGS AND RESPONSES**  
***Material Weakness In Internal Control Over Financial Reporting***

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*In the interim, ERSRI will develop additional procedures to improve financial reporting of contributions receivable.*



**Management Comment 2010-1**

**MEMBER DATA FILE COMPLETENESS**

The System's ANCHOR computer system contains detailed information for each member which includes:

- basic information such as social security number, gender, date of birth,
- service credits earned and earnings, and
- designated beneficiaries and other member options.

ANCHOR system data is derived from a membership application typically completed upon hiring and the periodic reporting of contribution and wage data. Data is extracted from the ANCHOR system and provided to the System's actuary each year to perform an actuarial valuation of each plan's liabilities. The accuracy and completeness of member information is critical to the integrity of the actuarial valuation.

We found the integrity of the System's membership data is impacted by (1) the failure of some members to submit a membership application upon hiring and (2) data conversion issues continuing from the implementation of the ANCHOR computer system in 2001. Each of these issues is discussed more fully below.

**Incomplete Data Due to Failure to Submit Membership Application**

During our prior and current audits, we found a significant number of member records were incomplete because date of birth and gender were missing. As of June 30, 2009, the most recent actuarial valuation completed at the time of our audit, missing data elements (gender and date of birth) were observed consistent with the prior audit results although efforts were underway to address this issue.

Missing data impacts the results of the actuarial valuation because the actuary must make assumptions for certain member characteristics which differ from actual data. Previously, the actuary assumed all members unknown as to gender were males and then used the average age of the entire population when date of birth was unknown. More recently, the actuary revised his assumptions for missing data and now assumes 25% are male and the remainder are female in the case of teachers and 50% male, 50% female for other members.

ERSRI management informed us that these unknown data elements are caused by members who fail to submit a membership application upon hiring. Applications are mailed to new employees and the employee is responsible for returning the completed application.

ERSRI has been taking steps to obtain the missing data elements from employers. Additionally, ERSRI has modified its ANCHOR accounting system to suspend contribution and service credit data from employers when key data elements are missing from the ERSRI member database. Employers will be prompted to provide the missing data thereby allowing posting of the contribution and service credit data to ERSRI's ANCHOR system.

While the steps taken and planned by ERSRI to address the missing member data elements should be effective in addressing that specific problem, we believe ERSRI should still consider revising its current policy which requires each new member to independently submit a membership application. We believe there are multiple advantages to requiring employers to submit membership applications on behalf of new hires. These advantages are summarized below:

- ➔ ERSRI's member database would be complete immediately as new members begin to make contributions – the aforementioned ANCHOR system enhancement only suspends posting of contribution data when date of birth and gender information are missing.
- ➔ Eligibility for membership in the System's plans would be determined at the time of hiring. In a prior audit, we found 18 state employees who were not contributing to the ERS plan but were required by statute to participate. We believe completion of a membership application (or a determination of ineligibility) by both the employee and employer at the time of hire would strengthen controls over this process and provide documentation of those determined to be both eligible and ineligible for participation.
- ➔ Members who have not submitted membership applications fail to designate a beneficiary for their contributions and death benefit.

#### RECOMMENDATIONS

- MC 2010-1a    Modify the membership application process to require participating employers to submit member applications upon hiring a new employee. Consider alternate on-line membership application options.
- MC 2010-1b    Complete the process of obtaining critical member data directly from employers when necessary.

#### **Data Conversion Issues at the Implementation of ANCHOR**

Other ANCHOR data integrity issues emanate from the original conversion of data to the new system in 2001. The original system design and implementation envisioned a "data cleansing" to validate each member's file information thereby ensuring the integrity of the system data upon conversion. Although the data cleansing process was planned, it was never performed. Consequently, there are instances of erroneous data within the ANCHOR system which generally involve service credits earned. As a result, when data is extracted for the annual actuarial valuation, the data must be reviewed to search for obvious inconsistent data. Further, the actuary performs certain data validation steps to isolate potentially inconsistent or invalid data. Data for members joining after the implementation of the ANCHOR system is unaffected. Ultimately, member data is validated when an active member retires and applies to begin receiving benefits. At that time, service credits and salary information are validated as part of the pension benefit calculation. However, from a data validation perspective, this process will take many years.

ERSRI should reassess the need to have a one-time "data cleansing" to ensure the validity and integrity of ANCHOR system data.

RECOMMENDATION

MC 2010-1c Reassess the need to perform a one-time data cleansing to ensure the validity of member information stored in ANCHOR.

Auditee Views:

*MC 2010-1a / 2010-1b - ERSRI's current practice for receiving member applications is based on the initial receipt of member contributions by the employer. As mentioned, ERSRI's system enhancements of the data file received from employers now include sex code and date of birth as well as other required components of information that would be provided on a hardcopy membership application. The request for remaining components are subsequently mailed directly to the member for (as a result of the information generated by the received data file) validation and completion by the member. In addition, beneficiary forms are provided as well to allow members to collect various details of selected beneficiaries that must be provided to ERSRI. Additionally, ERSRI has contacted employers with lists of members to collect required information from members.*

*ERSRI's experience suggests there is limited, if any, correlation between determining membership eligibility and the delivery of membership applications. Such determinations of employment status (i.e., part-time, seasonal, full-time etc.) are made prior to the official offer and acceptance of employment, membership applications are not the determinate. Additionally, completion of the application does not always ensure receipt of contributions. Experience has proven applications are received but due to a myriad of budgetary issues, positions may no longer have anticipated funding and thus no FTE is created.*

*ERSRI will strengthen its vigilance in securing completed applications and beneficiary information from members and employers. Additionally, ERSRI will review and consider the programmatic and procedural costs associated with providing and on-line application process.*

*MC 2010-1c - Reference is made to the original data conversion to the ANCHOR system in 2001. The matter being referenced relates to member service credit. It should be noted that prior to the development of the ANCHOR system, member service credit was not a data element in the legacy system and was manually calculated using various other data elements. Therefore, the issue is not one of "data" conversion. During development, algorithms were performed to calculate service credits from data available in the legacy systems. In tests of the applicable algorithms, calculation of service credit produced a 95% accuracy level.*

*Since the implementation of ANCHOR, technically trained staff has been working to validate accounts beyond an as-needed basis. However, efforts were somewhat compromised with the enactment of pension and healthcare reforms in recent years.*

*ERSRI is and will continue to increase its efforts to validate accounts and will evaluate additional resources to perform data validations.*

**Management Comment 2010-2**

**INVESTMENT RELATED ACCOUNTING MATTERS**

**Fair Value of Alternative Investments**

Generally accepted accounting principles (GAAP) require that the System's investments be reported at fair value. The fair value determination process is more challenging for alternative investments since they are not exchange traded and generally involve more subjective valuation characteristics. The System has developed a process which begins with audited fair values reported for each alternative investment as of December 31 and then adjusts such values for cash inflows and outflows for the period January 1 to June 30. Other significant events or factors occurring during this six-month period are also considered for their impact on these estimated fair values.

The System can improve documentation of its consideration of these significant events or factors in completing its estimated fair values for alternative investments. Spreadsheets detailing the estimated fair values of each alternative investment indicated no significant factors for consideration in the fair value process, although later consideration during the audit resulted in adjustment to the initial fair values.

**Derivative Type Investment Disclosures**

GAAP require comprehensive disclosures of the System's use and exposure to derivative type investments. Newly effective accounting principles (GASB Statement No. 53 – *Accounting and Financial Reporting for Derivative Instruments*) required modification of the derivative note disclosures included in the System's fiscal 2010 financial statements.

The System's investment custodian provided significantly enhanced information about derivative instruments during the fiscal year and at year-end to meet these required disclosures. ERSRI and General Treasurer staff should enhance their understanding of the accounting and disclosure requirements of GASB Statement No. 53 to ensure draft financial statements made available for audit fully meet these GAAP requirements.

**RECOMMENDATIONS**

- MC 2010-2a Improve documentation of the consideration of significant events or other factors impacting the System's determination of estimated fair values for alternative investments.
- MC 2010-2b Enhance staff understanding of the accounting and disclosure requirements of GASB Statement No. 53 – *Accounting and Financial Reporting for Derivative Instruments*.

**Auditee Views:**

*MC 2010-2a - Staff generally agrees with the auditor recommendation. There is room to improve the documentation of significant events that impact estimated fair values of alternatives.*

*In light of the events that unfolded in calendar year 2008 into 2009; staff made a proactive effort to be more involved in the reporting of outliers. These efforts go beyond accounting. It is difficult to standardize a methodology around unknown events; however, we will attempt to be more systematic in disclosing our approach.*

*MC 2010-2b - Staff generally agrees with the recommendation to enhance our understanding of the newly effective principle, GASB No. 53.*

*The consultant (Russell Investments) and the custodian bank (State Street) have helped us to build a robust system to address this principle; however, there is room for improvement. As of this report there is no set industry standard. As we see a pension accepted methodology develop, we will do our best to expedite our understanding of such practices.*

**Management Comment 2010-3**

**CONSIDER ELECTRONIC REMITTANCE OF CONTRIBUTIONS TO THE SYSTEM**

Member contribution data is uploaded to the ANCHOR computer system electronically; however, municipal employer units remit their contributions to the system by mailing a check to the System. The System should require electronic remittance of employer contributions to speed their availability thereby limiting the need to liquidate investments to meet the monthly pension benefit payroll. The impact on employer units should be minimal since most are already remitting federal and state withholding taxes and FICA contributions electronically as required by federal and state law and the cost to effect an electronic ACH payment is less than the cost to process a check. A change to the General Laws may be required to mandate electronic remittance of contributions for member units.

Additionally, the System should seek amendment to the General Laws, which currently requires that contributions to the System be remitted by the 15<sup>th</sup> of the month following the month in which the payroll was paid. Requiring remittance of contributions electronically within five business days of the payroll date would speed the availability of contributions to the system and is generally consistent with the remittance requirements for federal, state and FICA taxes paid by employers.

Accelerating the timing of contributions remitted to the System is important to minimize the amount of investments that need to be liquidated each month to meet the ERS plan's pension benefit payroll.

**RECOMMENDATIONS**

MC 2010-3a    Require member units to remit contributions to the System electronically rather than by check.

MC 2010-3b    Seek amendment to the General Laws to require remittance of contributions by employers within five business days of the payroll date.

Auditee Views:

*ERSRI has considered this approach in the past. Currently, ERSRI has over 190 different employers that post and make payments to ERSRI on a payroll frequency basis. ERSRI will again examine employer coordination, programmatic and legislative efforts involved and make appropriate determinations.*

*Also, the larger issue of liquidating investments each month to meet pension benefit payroll has limited if any relation to the timing of receipt of contributions. Other actuarial / funding issues are determinate of that issue.*

<b>Management Comment 2010-4</b>
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**WRITTEN POLICIES FOR VARIOUS PENSION ADMINISTRATION ISSUES**

Administration of the System is largely governed by specific statutes regarding membership, required contributions, actuarial matters, and benefit provisions. However, in certain instances, statutes are not specific to all situations and therefore various issues require judgment, interpretation of various statutes individually or collectively, consultation with the System's actuary, or decision by the ERSRI board. Oftentimes, precedent and past practices are used to guide various administrative decisions.

We believe ERSRI should undertake a process to collect and codify these presently informal policies and formalize their adoption and acceptance by the ERSRI Board.

**RECOMMENDATION**

MC 2010-4     Collect and codify various informal policies used in the administration of the System.

Auditee Views:

*ERSRI regularly publishes regulations that are approved and promulgated by the Board. ERSRI has updated regulations and members handbooks to support current business needs and is currently undertaking steps to promulgate regulations related to the 26 service credit purchase types. ERSRI is and has been in an ongoing effort to codify rules. ERSRI prioritizes the delivery of rules given the order of magnitude of an affected procedure or issue. With the required efforts involved in development and frequency of certain matters, it may be impractical to codify certain procedures at the present time.*

**Management Comment 2010-5**

**COMPLETE DEVELOPMENT OF AN ACCOUNTING MANUAL**

The System has been developing an accounting manual to formalize its accounting policies and procedures and to structure its annual closing and financial statement preparation process. While progress has been made, the manual is not complete and requires additional development to serve as a resource for the System's accounting staff.

**RECOMMENDATION**

MC 2010-5    Complete the ERSRI accounting manual.

**Auditee Views:**

*ERSRI, under the direction from an outside accounting firm, has begun the process to establish and complete an accounting manual. It is the intention of the System to complete this manual during fiscal year 2011 or early 2012.*

**Management Comment 2010-6**

**INFORMATION TECHNOLOGY GOVERNANCE AND STRATEGIC PLAN**

The System can enhance oversight of its IT systems through development of an Information Technology Governance and Strategic Plan. Although most IT responsibilities have been outsourced, such a plan could ensure that security, operational documentation, program change controls, user access rights, and equipment issues have been adequately addressed and continually monitored. For example, the plan could outline required monitoring of the consultant's reports on system changes and user access rights – and ensure that the functioning/processing performed by the consultant complies with contract provisions.

A comprehensive Information Technology Governance and Strategic Plan would also be useful as the System contemplates procurement of an upgrade or replacement for its ANCHOR and general ledger applications and is defining responsibilities to be performed by a contractor.

**RECOMMENDATION**

MC 2010-6    Develop and implement an IT Governance and Strategic Plan.

**Auditee Views:**

*ERSRI's senior management meets regularly with the IT consultants to ensure issues indicated above are being addressed. In addition, the service level agreement with the IT consultant addresses specific responsibilities of the vendor and the items mentioned in the finding.*

*Due to ERSRI's anticipated ANCHOR system upgrade, it has been addressing such issues with its IT Systems Consultant and will translate such plans into the updated system.*

**Management Comment 2010-7**

**CONSIDER EXPANDING IN-HOUSE INFORMATION TECHNOLOGY RESOURCES**

ERSRI's computer system was developed by a contract vendor and continues to be supported by the same vendor. The vendor is contracted to operate the on-site data center and essentially is responsible for all operations of ERSRI's IT systems.

While it would be impractical for ERSRI to assume these responsibilities with existing or additional employees, ERSRI should consider adding an additional in-house IT staff person to oversee the responsibilities of the contractor, be responsible for security administration, and build institutional knowledge of the system to potentially reduce reliance on the contractor in the future. This individual could provide the needed "in-house" guidance, assistance and oversight regarding the current and future technical issues facing ERSRI's expanding IT systems.

Additional IT staff may also be warranted as ERSRI procures a significant upgrade to its system necessitated by software used in the ANCHOR system that will no longer be supported by the software vendor. The upgrade will likely be a significant project in terms of time and funding and will require project management resources. Without adding IT resources, project management would fall to existing staff, and likely negatively impact performance of their current duties or also need to be outsourced.

**RECOMMENDATION**

MC 2010-7     Consider adding information staff member to oversee the system responsibilities performed by the contracted IT vendor and to provide the needed "in-house" guidance, assistance and oversight regarding the current and future technical issues facing ERSRI's expanding IT systems.

**Auditee Views:**

*ERSRI must contend with budgetary constraints when seeking additional human resources. Given the anticipated upgrade to the ANCHOR system, ERSRI will consider necessary IT staffing accordingly.*



**Management Comment 2010-8**

**CONTROL OVER CHANGES TO CRITICAL DATA WITHIN THE ANCHOR SYSTEM -  
LOGGING OF AUDITABLE DATA ELEMENTS**

The ANCHOR system lacks the functionality to track and log changes made to selected/specific critical data elements. Currently, the ANCHOR system does not maintain a true “audit log” that captures and reports upon all changes made to critical data fields or events. ANCHOR maintains “history” tables; however, there is no automated method to extract and report upon any changes made to critical individual data elements or application system events.

It is critical that management know if any changes (authorized and unauthorized) to retirement contribution or benefit data and/or the application system that have been made as it could have a direct impact on future benefits payments paid to members.

ERSRI management considered acquiring a third-party audit software to report on data elements that have been changed. A number of vendors offer packages that are designed to selectively capture and report upon user selected “auditable” data elements. The “audit package” is designed as an add-on application that works in conjunction with the ANCHOR system and therefore requires no additional programming be performed within the user application. This feature should also be incorporated within any future modification to the current system or replacement system and would be another area where the addition of an IT staff member would be instrumental in selection of a package and review of output from the package.

**RECOMMENDATION**

MC 2010-8     Enhance control over changes to critical data elements by acquiring third-party audit software that can accomplish the task of reporting on data elements that have been changed.

**Auditee Views:**

*ERSRI has made this a requirement in its ANCHOR system upgrade and will seek to determine the selected vendors’ choice of the third-party software suggested by the OAG. IT will then attempt to procure this software for use in the current ANCHOR system and determine the feasibility.*

**Management Comment 2010-9**

**MONITORING OF CONSULTANT CHANGE MANAGEMENT PROCESS**

ERSRI does not have documented change management procedures to monitor changes made to the ANCHOR application system. We noted that ERSRI does not have sufficient documentation of changes made to the system. Although ERSRI management does track their initiated change requests they do not receive or review on a periodic basis any change reports or logs to verify that only approved/authorized changes have been made to the system. In addition, ERSRI relies on the

documentation contained within their vendors change management system to evidence changes that were made to the ANCHOR application system.

Additionally, we found that the vendor system did not document expected results prior to testing system changes. Without expected results there is no information to compare the results of testing in order to ensure the change is operating as intended.

ERSRI management must have a clear understanding and proper documentation of what change(s) are made to the ANCHOR system and that those changes properly address management's concerns and work as intended. This is critically important as a significant number of statutory benefit changes are programmed into the ANCHOR system. Additionally, management should monitor on a periodic basis that only authorized changes are being made to the system and not rely solely on the vendor to review and control changes.

**RECOMMENDATION**

MC 2010-9 Enhance oversight of the program change management function as performed by the System's contracted IT vendor. Receive and review change logs and determine if they are authorized and in accordance with documented management directives.

**Auditee Views:**

*ERSRI meets with senior members of the IT Outsource Team on a regular basis to discuss/review changes which may be required to the ANCHOR system. Expected results are discussed, then coded and deployed to the test environment to be tested by applicable ERSRI staff. Upon successful confirmation from staff on the results of testing, the IT Outsource team communicates the items to be deployed to production and awaits approval from management. The System maintains Change Control Request documentation when implementing major programmatic changes such as the legislative changes required by recently enacted pension reforms.*

*ERSRI will examine additional change management procedures.*

<b>Management Comment 2010-10</b>
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**SECURITY AWARENESS TRAINING**

ERSRI did not conduct any security awareness training for its staff within the fiscal year. Awareness training is important to periodically reinforce the System's policies regarding security, management's intolerance of security breaches, and to educate staff about external threats to system security. A formal security awareness training program should be implemented.

**RECOMMENDATION**

MC 2010-10 Implement an ongoing periodic security awareness training program.

Auditee Views:

*The System has performed security awareness training with all employees. The System will continue to consult with its outside IT System auditors to determine any additional training sessions. Additionally, ERSRI receives IT security communication from DOIT which is forwarded to the systems IT outsource consultant and communicated to staff where applicable.*

**Management Comment 2010-11**

**ACCELERATE THE TIMELINESS OF THE SYSTEM'S ANNUAL REPORT**

The System prepares an annual report as required by Section 36-8-8 of the General Laws. The System's annual report includes the audited financial statements of the System and our Independent Auditor's Report thereon. The annual report, which includes other information on the System, largely actuarial information, is generally not available until nearly a year after the audited financial statements are publicly available. We believe it would be beneficial to have the System's annual report available shortly after completion of the annual audit.

**RECOMMENDATION**

MC 2010-11 Complete the System's annual report shortly after completion of the annual audit.

Auditee Views:

*At the conclusion of the fiscal year audit conducted by the Office of the Auditor General (OAG), approved actuarial valuations are only available from the prior fiscal year, which are referenced in the notes to financial statements. With the efforts and timing involved in completion and approval of the annual actuarial valuation, the timing of the financial audit and corresponding fiscal year valuation are not synchronized. ERSRI's annual report contains the corresponding financial statements and actuarial information thus; there is a lag in production of the report. It should be noted that this lag is accounted for in RIGL §36-8-8 and ERSRI has been in compliance with the law.*

**Management Comments Communicated Confidentially**

As permitted by General Law section 22-13-10, *Audit of Information Security Systems*, we have communicated two findings confidentially that relate to security over ERSRI's computer systems.