



Commonwealth of Massachusetts

Management Letter

June 30, 2016



KPMG LLP
Two Financial Center
60 South Street
Boston, MA 02111

March 31, 2017

The Comptroller's Advisory Board
Commonwealth of Massachusetts
Boston, Massachusetts

Advisory Board Members:

We have audited the basic financial statements of the Commonwealth of Massachusetts (the Commonwealth) as of and for the year ended June 30, 2016, and have issued our report thereon dated January 6, 2017. In planning and performing our audit of the basic financial statements of the Commonwealth, in accordance with auditing standards generally accepted in the United States of America, we considered the Commonwealth's internal control over financial reporting (internal control) as a basis for designing our auditing procedures for the purpose of expressing our opinions on the basic financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Commonwealth's internal control. Accordingly, we do not express an opinion on the effectiveness of the Commonwealth's internal control.

During our audit, we noted certain matters involving internal control and other operational matters that are presented for your consideration. These comments and recommendations, all of which have been discussed with the appropriate members of management, are intended to improve internal control or result in other operating efficiencies and are summarized on the attached schedule of observations.

The Commonwealth's written responses to our comments and recommendations have not been subjected to the auditing procedures applied in the audit of the basic financial statements and, accordingly, we express no opinion on them.

In addition, we identified certain deficiencies in internal control that we consider to be a material weakness and others that we consider to be significant deficiencies, and in accordance with *Government Auditing Standards* communicated them in writing to the Commonwealth in a separate report dated January 6, 2017.

Our audit procedures are designed primarily to enable us to form opinions on the basic financial statements, and therefore may not bring to light all weaknesses in policies or procedures that may exist. We aim, however, to use our knowledge of the Commonwealth's organization gained during our work to make comments and suggestions that we hope will be useful to you.

We would be pleased to discuss these comments and recommendations with you at any time.

This communication is intended solely for the information and use of management of the Commonwealth, and is not intended to be and should not be used by anyone other than these specified parties.

Very truly yours,

KPMG LLP

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Schedule of Observations

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MLC 2016-01

Comptroller's Office (CTR) - HR/CMS User Access Review

Repeat observation: No

Observation

In 2016, KPMG identified exceptions with the User Access Review process for HR/CMS. In the User Access Review, users with more than the default access (by default the majority of the Commonwealth employees obtain access to HR/CMS for time and expense entry) are reviewed by each of the 150+ departments. For 4 of the 15 departments sampled for the user access review, KPMG determined that the user access review was not completed timely (within 30 days of the due date). Additionally, it was noted that 8 users from 3 departments were identified in the department reviews whose access should be removed. However, the access for these 8 users was still active approximately 4 months after the reviews. Access for these users was revoked after identification by KPMG.

Furthermore, when testing samples for new hires, KPMG determined that for 2 of the selected samples of new access, there was no documentation or evidence of approval for the access granted. Upon further analysis with the Comptroller's office, it was determined that this access was granted due to a technical glitch in November 2015. Due to moving off of Daylight Savings Time (DST), a job that runs daily and revokes excessive access after business hours and restores that access prior to the start of business hours did not complete appropriately. As part of the procedures performed by the Massachusetts Office of Information Technology (MassIT) to re-run the job and re-assign all access rights, inadvertent access was granted to HR/CMS. About 70 users were granted a total of about 250 inappropriate access roles due to this glitch.

In December of 2015, all agencies performed a user access review. As part of that user access review, management did not identify that this inappropriate access had been granted to the 70 users discussed above. As such, KPMG concluded that the December user access review was not performed adequately, as it did not identify a group of users with inappropriate access.

A user access review is a detective control that can identify users that have inappropriate access and whose accounts may have been used to perform unauthorized activity. Without a user access review, the risk increases that there are users with inappropriate access to the system who could perform unauthorized transactions.

Recommendation

Management should consider to:

- Reinforce the importance of the user access review with all people performing the review.
- Strengthen the user access review by identifying which reviewer is responsible for which user and by getting positive confirmation from the reviewers that they have completed the review.
- If deviations are identified, ensure access is changed accordingly for all identified deviations and that the reviewers obtain a new access list to confirm the deviations are resolved.

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- Perform an additional review of the additional users and the additional access since the previous review was performed. That way, reviewers are enabled to identify the key changes since the prior review.

Management's Corrective Actions

User Access Review – Current Process:

- **Security Review Due** notification sent out 2 weeks prior to deadline via email and eUpdate.
- DAB bureau director reaches out to all non-respondents (5) business days after the **Security Review Due** deadline.
- Deputy Comptroller reaches out to all non-respondents (21) business days after the **Security Review Due** deadline.
- All departments responded to the last User Access Review request of 6/30/2016.

User Access Review – New Steps:

- CTR is developing a quality assurance report among 3 systems' security tables (MMARS, HR/CMS, and Intempo) to identify and resolve security inconsistencies. *Begun 8/3/2016.*
- CTR will begin its own desk reviews of departments' back-up documentation of their user access reviews. *To begin October 2016.*
- Additional V&V step for code migrations: CTR/ITD to review security profiles for changes pre- and post- implementations of security role updates. *First security profile V&V will be on 9/22/2016.*
- MassIT has enabled audit records to track any changes to PeopleSoft's OPERDEFN table, which contains each user's roles/permissions and email address. *9/22/2016*

To Avoid Conflict with Switch to DST:

- MassIT has made a scheduling change so the Restore Security job runs at 5 a.m., in order to avoid any conflict with the switch to and from Daylight Savings Time. *9/22/2016*

Responsible Officials

Chris Guido, Deputy Comptroller, Comptroller of the Commonwealth's Office
Kathy Sheppard, Deputy Comptroller, Comptroller of the Commonwealth's Office
HR/CMS Product Support Team, Massachusetts Office of Information Technology

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MLC 2016-02

Department of Revenue (DOR) – Child Support Enforcement Program

Repeat Observation: No

Observation

Subject to federal grant award terms, the Department of Revenue (DOR) manages the Child Support Enforcement (CSE) program. The federal grant award terms include provisions for eligible or allowable costs and the reimbursement of such costs. The CSE's eligible costs include certain Trial Court disbursements related to the CSE program. In December of each year, the Trial Court submits its prior fiscal year eligible CSE costs to DOR. DOR typically begins requesting reimbursement of such eligible costs from the federal government the following February. For example, DOR won't begin requesting reimbursement of eligible fiscal 2016 Trial Court CSE expenditures totaling approximately \$8.6 million until February 2017.

Recommendation

Given that the CSE program is permitted to draw federal funds for all eligible costs on a weekly basis (as noted in the Commonwealth's most recent Treasury-State Cash Management Improvement Act or CMIA agreement) and that federal guidelines allow for a reconciliation between actual allowable expenditures and actual weekly draws (i.e. estimated costs), we recommend that CSE implement procedures to minimize the time it takes to accumulate data from the Trial Court and to ultimately seek reimbursement from the federal government for these allowable costs.

Management's Corrective Action

While DOR does not challenge the base fact that the Trial Court draw was not requested within the normally expected draw timeline, we do want to clarify the circumstances that exist so that reasonable assumptions on the timeliness of this particular draw can be made.

- 1) The data received from the Trial Court is the sole responsibility of the Trial Court to compile and deliver to DOR.
- 2) Even with the timely receipt and processing of Trial Court data, the physical drawing of the Trial Court allocation is not advisable prior to the determination of adequate Grant Authorization and disbursement availability for the quarter ending 12/31 of the particular year.
- 3) A reasonable expectation for drawing the Trial Court draw would be following the calculation and submission of the Federal Financial FFR-425 and Expenditure 396-A reports 30 days following the close of the quarter.
- 4) If the above information is acceptable then the (actual) delay seen in the FY2015 Trial Court draw referred to above should be the difference between an anticipated first week of February submission and the actual submission of February 26th which was related to events that will not be reoccurring.

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As further illustration, the FY2016 Trial Court draw was processed on February 2, 2017 and, because of authorization limitations, \$2,307,993 of the allowable draw was not drawn and is currently being held pending a future adjustment award. If the full amount of the draw had been processed sooner, the Department would have run the risk of overdrawing its Federal account at the end of the corresponding quarter. Moving forward, the Department will continue balancing draw timeliness within the constraints of available authorization limitations.

Responsible Officials

Bryan Kingsbury, Director of Finance and Reporting, DOR
Daniel Mcgrory, Director of Finance, CSE

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MLC 2016-03

Executive Office of Labor and Workforce Development (EOLWD) – Allowance for Uncollectible Receivables

Repeat Observation: Yes, 2015-06

Observation

During our audit, we reviewed EOLWD's allowance methodology and related documentation to support its estimate of uncollectible receivables and noted the following:

- The analysis is not performed at the employer-type level.
- The methodology does not factor in the likelihood of collections of a particular assessment year decreases over time.
- Approximately 83% of the gross employer accounts receivable balance has been outstanding greater than 22 months.
- The overpayments allowance calculation methodology did not change from the prior year and is not based upon an aging analysis.

Recommendation

We recommend that EOLWD annually update its methodology based upon a look back of its actual collection experience. The methodology should properly reflect receivable type, including various employer types, and incorporate an accounts receivable aging analysis. The look back period should be established by management and should include sufficient history to accurately estimate the net realizable value of its receivables at year-end.

Management's Corrective Action Plan

EOLWD is the process of updating the allowance methodology that will reflect receivable type and the details recommended by the auditors.

Responsible Officials

Male Kamyra, Deputy Chief Financial Officer, EOLWD

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MLC 2016-04

Executive Office of Health and Human Services (EOHHS) - Unpaid Claims

Repeat Observation: No

Observation

For fiscal year-end financial reporting purposes, the Commonwealth records a liability for Medicaid and several capitated benefits incurred but not yet paid, referred to as the Unpaid Claim Liability (UCL). During our audit, we noted the following:

- Management's initial UCL estimate was revised after errors in the tabulation of the capitation paid loss data were discovered.
- For cash flow purposes, the Commonwealth often times adjusts the disbursement pattern for certain of its Medicaid and capitated benefit payments. Management's initial UCL failed to properly reflect the disbursement pattern in its models, thereby resulting in an inaccurate initial UCL.

Recommendation

We recommend that additional management review controls should be put in place over the accuracy of both the inputs and methodology of the UCL estimate.

Management's Corrective Action Plan

In response to the observations highlighted above, by July 2017, EOHHS will implement the following management controls:

1. EOHHS will develop procedures related to annual review of Managed Care Entities (MCE) program unpaid claims liabilities that include documentation.
2. EOHHS will generate annual lag triangles for all Managed Care programs to ensure that no undue variation is present and investigate noteworthy variation.
3. EOHHS will develop capitation lag models for all MassHealth Managed Care program programs that align with historical disbursement patterns.

Responsible Officials

Mohamed Sesay, MassHealth Director of Finance

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MLC 2016-05

Group Insurance Commission (GIC) – Service Organization Controls Report

Repeat Observation: Yes, 2015-09

Observation

The Group Insurance Commission (GIC) utilizes five insurance companies providing health plan administrative services. GIC relies on insurance companies for claim receipt and entry, claim adjudication, and claim payment and customer funding. The insurance companies' controls are reviewed annually by a third-party which provides a service organization control (SOC) report detailing the status of controls and whether they are operating effectively. For one insurance company, no SOC report was provided covering fiscal year 2016.

Recommendation

We recommend that the GIC require all its health plan administrators provide appropriate confirmation, in the form of a SOC report and bridge letter, if applicable, regarding the status of its control environment for the full fiscal year.

Management's Corrective Action Plan

The GIC requires that all of its health care vendors provide a service organization control (SOC) report detailing the status of controls and whether they are operating effectively. Our current contract with Beacon Health requires that the Statement on Standards for Attestation Engagements (SSAE) No. 16 report must be received by the Commission annually, no later than three months from the report's end date, October 1, 20xx. The report must cover a twelve month period starting July 1, 20xx. The report must include a summary of all noted weaknesses of control objectives, control activities and related processes. Additionally, the vendor must submit a corrective action plan, including the date on which the plan anticipates the weaknesses being corrected. Quarterly updates shall be submitted until there is resolution satisfactory to the Commission. The Commission may assess an annual penalty of up to \$50,000 if an acceptable SSAE (now SOC 1) report is not received by October 1 of the applicable year, and Beacon will be assessed that penalty next month for the FY2016 report that was due in FY2017.

In January 2017, Beacon notified GIC that it was suspending its SOC-1 Type II testing/report to remediate control observations noted by its independent auditors.

Beacon has committed to providing the GIC with 2017 SOC1 Type II report in FY2018, which they intend to deliver to the GIC by December 31, 2017.

Responsible Official

Catherine Moore, Acting Director of Financial Management, GIC

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MLC 2016-06

Massachusetts State Employees' Retirement System (MSERS) – Census Data

Repeat Observation: Yes, 2015-13

Observation

The Massachusetts State Retirement Board (MSRB) is responsible for maintaining member census information for all active employees who contribute to and participate in the Massachusetts State Employees' Retirement System (MSERS). Significant elements of census data include: date of birth, date of hire or years of service, eligible compensation, and gender, among other elements. Effective management of the census data for active employees includes procedures to verify the underlying payroll records of the participating employers to determine that the information provided is complete and accurate, as the census information is also utilized by the Public Employee Retirement Administration Commission (PERAC) to calculate a projected pension liability, a significant accounting estimate that is part of the financial reporting process.

During the fiscal 2016 audit, we selected over 250 active members accounts for census data testing. The accounts were selected not only from the Commonwealth, but also two state universities, one community college, and one of its component units for detail testing, which also included comparing such information to the census file used by PERAC.

The results of our testwork indicated the following data quality issues:

- Under its current Legacy computer system, on an annual basis, an active member census file is run by the MSRB to compile census information for PERAC. Based on our discussions with the MSRB, due to the size of the database, this file is run in a series of queries over a multi-week period over the active or "live" MSERS database.
- One of the data elements utilized by the PERAC as part of the calculation for total pension liability is creditable service. The MSRB derives creditable service based on date(s) and amounts(s) of member contributions. Additionally, based on the timing of when the MSRB queries the active system, a member who is queried during the first week the query is run will have fewer contributions than a member who is queried during the later periods the query is run. This methodology results in varying creditable service for members with the same service history, as of a fixed point in time.
- Approximately 11% of the samples selected for testing had one month of additional creditable service during calendar year 2015 than expected. Approximately 11% of the samples selected for testing had one month less of creditable service during calendar year 2015 than expected. This incremental month of service was not related to items such as leave of absence, buy back, part-time schedule, or similar scenarios.

Recommendation

We recommend that MSRB freeze the active member database prior to producing the census file. In addition, we recommend that the MSRB assess the impact of the additional month more or less of service given to certain members on the total pension liability.

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We also continue to recommend that the MSRB consider including a payroll audit function, either as an internal or outsourced resource, as part of its overall internal control strategy. A payroll audit function should include a risk based approach to determine which participating employers' payroll records require greater oversight and review.

Management's Corrective Action Plan

The MSRB went live with its new computer system software, MARIS, in January 2017. In the years leading up to the activation of MARIS, a critical component of the project has been data conversion. The MSRB and its vendors expended considerable effort and resources to review, update, and cleanse all data being converted from the Legacy system. This data includes current and historical information associated with active, retired, and inactive members of the MSERS.

The MSRB will assess the benefits of dedicating resources toward a payroll audit function after it has had an opportunity to determine whether the revised reporting of payroll and related expanded data, now available to it, has improved the quality of census information. Also, assessments as to whether "freezing the active member database" would still be necessary, would occur after the MSRB has had a reasonable period of time from data conversion.

Similarly, it is unclear, under MARIS, whether the MSRB will utilize the same process, or require an extended period of time, to compile the census data as it has previously required for audit purposes as under its Legacy system.

Responsible Official

Nicola Favorito, Executive Director, MSRB

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MLC 2016-07

Massachusetts State Employees' Retirement System (MSERS) - ORP assets in transfer

Department of Higher Education, Retirement Plans Group (DHE) – ORP assets in transfer

Repeat Observation: No

Observation

Chapter 176 of the Acts of 2011, *An Act Providing for Pension Reform and Benefit Modernization* made a number of changes to M.G.L. Chapter 32 pension law. One of the changes concerns the Optional Retirement Plan (ORP), a defined contribution plan for higher education employees. The law provided a one-time opportunity for ORP members (and former ORP members) to transfer to the Massachusetts State Employees' Retirement System (MSERS). From January 1, 2016, according to the MSERS actuarial valuation report, an estimated 1,600 members made or were expected to make this one-time election to transfer out of the ORP and into the MSERS.

As a condition of transferring into the MSERS, members were also required to transfer their accumulated existing ORP assets, with certain exceptions, to the MSERS. As of June 30, 2016, the Commonwealth estimated that there were approximately \$118M of accumulated balances due to the MSERS for ORP members who had elected to join the MSERS.

After initially failing to record any of the outstanding ORP assets in transfer, the MSERS, in consultation with the Department of Higher Education (DHE), did develop a list of outstanding assets in transfer at year-end. However, the outstanding assets in transfer detail was not completely accurate, as we noted differences between the amount recorded and the amount ultimately settled or received for 10 out of 10 sample selections.

Recommendation

We recommend that the MSERS regularly update and maintain its listing of ORP assets in transfer and continue to work with DHE to ensure the accuracy of the ORP assets transfer data.

Management's Corrective Action

The transfer process under Section 60 of Chapter 176 of the Acts of 2011 required the development by DHE of a shared data base for use by DHE and the MSRB, as the MSRB would not have employment or service information for the affected ORP participants. The DHE obtains participant payroll information from all the eligible campuses where the participants have worked.

Once information has been entered and updated in the database, the MSRB staff must calculate the cost of establishing creditable service with the MSERS and the amount owed by each participant. An initial payment statement is generated and forwarded to the DHE, which then issues it to the transferring participant. After a participant confirms they are transferring from the ORP, the DHE arranges to have all applicable employee contributions forwarded from the applicable investment manager.

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Once the cost associated with the employee contributions has been determined and an initial transfer of funds has been received, if an outstanding balance remains, a further statement or “balance letter” is generated and sent to the participant. Once the balance has been satisfied, a “payment in full” letter is issued to the participant.

Under the MSERS plan rules, no member may retire with an account that is not in balance, or may access their funds for a refund or rollover should they separate from service prior to retiring.

Reviewing the ten accounts that are mentioned above, eight are ORP participants whose transfers are incomplete. These participants have remaining funds in a TIAA Traditional account and are locked and not accessible at present. TIAA has informed both DHE and the MSRB that these funds may not be distributed except as under account rules. The MSERS and DHE are working on the logistics of transferring these funds during the course of the participant’s employment.

The remaining two accounts are waiting on an initial transfer of funds from DHE.

MARIS, the MSERS’ new operational software, has the flexibility to track transferring ORP participants and any funds owed to the MSERS.

Responsible Official

Nicola Favorito, Executive Director, MSRB

Commonwealth of Massachusetts

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MLC 2016-08

Massachusetts Teachers' Retirement System (MTRS) – Census Data

Repeat Observation: Yes, 2015-12

Observation

The Massachusetts Teachers' Retirement Board (MTRB) is responsible for maintaining member census information for all active employees who contribute to and participate in the Massachusetts Teachers' Retirement System (MTRS). Significant elements of census data include: date of birth, date of hire or years of service, eligible compensation, and gender, among other elements. Effective management of the census data for active employees include procedures to verify the underlying payroll records of the participating employers to determine that the information provided is complete and accurate, as this census information is also utilized by the Public Employees Retirement Administration Commission (PERAC) to calculate a projected pension liability, a significant accounting estimate that is part of the financial reporting process.

During the fiscal 2016 audit, we selected over 700 active members for census data testing. The members were selected from 34 participating employers (from a population of over 400 participating employers).

The results of our testwork indicated several errors in various census elements, including:

- 3 date of birth errors
- 14 gender errors
- 15 pensionable wage errors
 - 7 actives where wages were not annualized for members returning to service
 - 8 new hires where wages were not properly annualized (e.g. annualizing one-time items such as coaching or other one time stipends)
- 17 other census errors
 - 7 members with incorrect status (active or inactive)
 - 10 members with incorrect creditable service

Recommendation

While MTRB continues to make significant improvement in its census data collection and reporting process, census data errors continue to occur, albeit with decreasing frequency. We recommend that MTRB identify root causes for its pensionable wage and service credit errors and refine its system of internal controls, including its IT controls, to eliminate those root causes. Certain root causes may require a collaborative effort on the part of the MTRB and PERAC to resolve, especially for new hires and for members who work part-time.

We also recommend that MTRB be more diligent when inputting or updating members' date of birth, as such errors are a result of human error and/or a lack of proper review of such activity.

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We also continue to recommend that MTRB consider including a payroll audit function, either as an internal or outsourced resource, as part of its overall internal control strategy. A payroll audit function should include a risk based approach to determine which participating employers' payroll records require greater oversight and review.

Management's Corrective Action Plan

The quality of the census data information from our 422 employers continues to improve. The pension management system's data validations implemented to detect and eliminate financial data discrepancies are applied before each monthly retirement deduction report is released into the system. MTRS service representatives are also in frequent contact with the payroll officers at the school districts to ensure that the demographic and financial data is accurate.

In addition, the MTRS provides an annual statement to members detailing their pension account balance and their demographic data, including: date of birth, gender, and marital status. Each year, members are asked to validate the information provided on their annual statement and report any updates and/or discrepancies. MTRS staff then enter corrections as needed. Also, MTRS is in the process of providing on-line access to all members to enable them to view and validate their pension accounts. Currently, nearly 35,000 active and inactive members have access to their information online. Further, as an example of a control for census data accuracy, members are required to provide their birth certificate with their retirement application. Applications are not processed without proof of the member's date of birth.

In regard to pensionable wage errors, we continue to work with PERAC staff to root out the errors for newly hired members and members who had returned from inactive to active status. As noted previously, the wage errors in the census data file are created when PERAC annualizes the reported earnings. Last year, the MTRS provided PERAC with a separate file that listed the annual salary of newly hired MTRS members and will do so again this year with the hope that that data is included in the final census data file.

In regard to the creditable service errors, previous year audits triggered corrections to the logic that populates a field called the "adjusted employment date," which substantially reduced the number of creditable service anomalies in 2016. All but one of the anomalies detected this year were situational and expected under the methodology used by PERAC to estimate creditable service for our members. The remaining creditable service issue, which is member specific, is being researched and will be resolved.

In addition, as the result of an ongoing project to convert our historical contribution data, the MTRS currently has validated service credit for 58% of our active and inactive members, including 71% of active and inactive members hired on or after January of 2000. We continue to annually increase the number of members with validated service credit so that ultimately, the PERAC actuary will not be required to estimate our member's service credit.

The MTRS continues to discuss implementing a payroll audit function.

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Responsible Officials

Erika Glaster, Executive Director, MTRS

Sean Neilon, Assistant Executive Director, MTRS

Marybeth Shaughnessy-Newell, Compliance and Financial Reporting Officer, MTRS

Robert George, Director of Employer Services, MTRS

David Percoco, Assistant Director of Employer Services, MTRS