



NEBRASKA AUDITOR OF PUBLIC ACCOUNTS

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December 18, 2014

Phyllis Chambers, Director
Nebraska Public Employees Retirement Systems
1526 K Street, Suite 400
Lincoln, Nebraska 68509-4816

Dear Mrs. Chambers:

We have audited the basic financial statements of the State of Nebraska (State) as of and for the year ended June 30, 2014, in accordance with auditing standards generally accepted in the United States of America and standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, and have issued our report thereon dated December 16, 2014. In planning and performing our audit, we considered the State's internal control over financial reporting (internal control) as a basis for designing audit procedures for the purpose of expressing our opinions on the basic financial statements of the State, but not for the purpose of expressing an opinion on the effectiveness of the State's internal control. Accordingly, we do not express an opinion on the effectiveness of the State's internal control.

In connection with our audit described above, we noted certain internal control or compliance matters related to the activities of the Nebraska Public Employees Retirement Systems – Deferred Compensation Plan (Agency) or other operational matters that are presented below for your consideration. The comment and recommendation, which has been discussed with the appropriate members of the Agency's management, is intended to improve internal control or result in other operating efficiencies.

Our consideration of internal control included a review of prior year comments and recommendations, where applicable. To the extent the situations that prompted the recommendations in the prior year still exist, they have been incorporated in the comment presented for the current year. All other prior year comments and recommendations (if applicable) have been satisfactorily resolved.

Our consideration of internal control was for the limited purpose described in the first paragraph and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and, therefore, material weaknesses or significant deficiencies may exist that were not identified.

Draft copies of this letter were furnished to the Agency to provide management with an opportunity to review and to respond to the comment and recommendation contained herein. All formal responses received have been incorporated into this letter. Responses have been objectively evaluated and recognized, as appropriate, in the letter. Responses that indicate corrective action has been taken were not verified at this time, but will be verified in the next audit.

The following is our comment and recommendation for the year ended June 30, 2014.

Service Organization Control Report

A good internal control plan requires an agency utilizing a service organization to obtain a Service Organization Control (SOC) report.

As defined in AICPA U.S. Auditing Standards, AU-C 402.08, a service organization is “an organization or segment of an organization that provides services to user entities that are relevant to those user entities' internal control over financial reporting.” Furthermore, AU-C 402.A3 goes on to state:

A user entity may use a service organization, such as one that processes transactions and maintains the related accountability for the user entity or records transactions and processes related data. Service organizations that provide such services include, for example, bank trust departments that invest and service assets for employee benefit plans or for others

A SOC report offers an independent assessment of the controls for the service organization providing services to the entity and reports information on controls the entity should have to complement the service organization's controls. The entity should review the SOC report to ensure the service organization's controls are operating effectively.

The Agency utilized Massachusetts Mutual Life Insurance Company (MassMutual) as the record keeper to process participant transactions during the year. MassMutual was also the custodian of the Deferred Compensation Plan (Plan) investment assets, effective June 20, 2014. Previous to this date, Hartford Life Insurance Company (Hartford) was the custodian of the plan assets. The custodian invests and services the assets of the plan.

The Agency did not obtain a SOC report for the recordkeeping functions performed by MassMutual until after inquiry by the Auditor of Public Accounts. Furthermore, Hartford did not have a SOC report for the custodial function for the calendar year 2013 reporting period; thus, the Agency was not able to obtain a SOC report from Hartford for the custodial services it provided for the members. As of June 30, 2014, \$39,627,323 was invested with MassMutual for the Plan.

Without obtaining and reviewing the SOC reports, there is an increased risk the service organization could have control weaknesses of which the Agency would be unaware, which could increase the risk of loss or misappropriation of member assets held by the Plan.

We recommend the Agency work with its service organizations to ensure all SOC reports are received. We further recommend the Agency review the reports to ensure its service organization's controls are operating effectively.

Agency Response: NPERS will implement procedures to ensure that SOC reports for our service organizations are received and reviewed in a timely manner.

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Our audit procedures are designed primarily on a test basis and, therefore, may not bring to light all weaknesses in policies or procedures that may exist. Our objective is, however, to use our knowledge of the Agency and its interaction with other State agencies and administrative departments gained during our work to make comments and suggestions that we hope will be useful to the Agency.

This communication is intended solely for the information and use of the Agency, the Governor and State Legislature, others within the Agency, Federal awarding agencies, pass-through entities, and management of the State of Nebraska and is not intended to be, and should not be, used by anyone other than the specified parties. However, this communication is a matter of public record, and its distribution is not limited.



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