



ERNEST A. ALMONTE, CPA, CFE  
Auditor General

State of Rhode Island and Providence Plantations

GENERAL ASSEMBLY

Office of the Auditor General

1145 Main Street  
Pawtucket, Rhode Island 02860-4807

OFFICE  
(401) 222-2435  
FAX  
(401) 222-2111

March 3, 2000

JOINT COMMITTEE ON LEGISLATIVE SERVICES:

SPEAKER John B. Harwood, Chairman

Senator Paul S. Kelly

Senator Dennis L. Algiere

Representative Gerard M. Martineau

Representative Robert A. Watson

We have completed our audit of the financial statements of the State of Rhode Island and Providence Plantations Employees' Retirement System for the fiscal year ended June 30, 1999 in accordance with Rhode Island General Laws, Chapters 22-13 and 35-7.

Our report is contained herein as outlined in the Table of Contents.

Sincerely,

Ernest A. Almonte, CPA, CFE  
Auditor General

**STATE OF RHODE ISLAND AND PROVIDENCE PLANTATIONS  
EMPLOYEES' RETIREMENT SYSTEM  
FOR THE FISCAL YEAR ENDED JUNE 30, 1999**

**TABLE OF CONTENTS**

	<b><u>PAGE</u></b>
<b>I. <u>INDEPENDENT AUDITOR'S REPORT</u></b> .....	1
<b>II. <u>FINANCIAL STATEMENTS</u></b>	
Statements of Plan Net Assets .....	3
Statements of Changes in Plan Net Assets .....	4
Notes to Financial Statements.....	5
<b>III. <u>REQUIRED SUPPLEMENTARY INFORMATION</u></b>	
Schedules of Funding Progress .....	18
Schedules of Contributions From the Employers and Other Contributing Entity .....	19
Notes to Required Supplementary Information .....	20
Year 2000 Disclosure.....	22
<b>IV. <u>INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE AND ON INTERNAL CONTROL OVER FINANCIAL REPORTING BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH <i>GOVERNMENT AUDITING STANDARDS</i></u></b> .....	23



State of Rhode Island and Providence Plantations

GENERAL ASSEMBLY

Office of the Auditor General

1145 Main Street  
Pawtucket, Rhode Island 02860-4807

OFFICE  
(401) 222-2435  
FAX  
(401) 222-2111

## **INDEPENDENT AUDITOR'S REPORT**

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

We have audited the accompanying statements of plan net assets of the State of Rhode Island and Providence Plantations Employees' Retirement System (the System) as of June 30, 1999 and the related statements of changes in plan net assets for the year then ended. These financial statements are the responsibility of the System's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with generally accepted auditing standards and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

As discussed in Note 1(a), the financial statements referred to above present only the plan net assets and changes in plan net assets of the Pension Trust Funds of the State of Rhode Island and Providence Plantations (the State) and are not intended to present fairly the financial position and results of operation of the State, in conformity with generally accepted accounting principles.

In our opinion, the financial statements referred to above present fairly, in all material respects, the net assets of the plans within the System as of June 30, 1999, and the changes in plan net assets for the year then ended in conformity with generally accepted accounting principles.

In accordance with *Government Auditing Standards*, we have also issued a report dated February 1, 2000 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.

Joint Committee on Legislative Services

Page 2

The Schedules of Funding Progress, the Schedules of Contributions from the Employers and Other Contributing Entity, and the Year 2000 Disclosure on pages 18, 19, and 22 are not a required part of the basic financial statements but are supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consist principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However, we did not audit the information and express no opinion on it. With respect to the Year 2000 Disclosure, we do not provide assurance that the System's Year 2000 remediation efforts will be successful in whole or in part, or that parties with which the System does business will become Year 2000 compliant.



Ernest A. Almonte, CPA, CFE  
Auditor General

February 1, 2000



**EMPLOYEES' RETIREMENT SYSTEM OF RHODE ISLAND**  
**Statements of Plan Net Assets**  
**June 30, 1999**

	<u>ERS</u>	<u>MERS</u>	<u>SPRBT</u>	<u>JRBT</u>	<i>Total (Memorandum Only)</i>
<b>Assets</b>					
Cash (Note 3)	\$ -	\$ -	\$ 124,303	\$ 15,114	\$ 239,417
Receivables					
Member contributions	8,158,219	1,374,811	-	-	9,533,030
Employer contributions	7,680,212	978,554	-	-	8,658,766
Due from state for teachers	6,514,467	-	-	-	6,514,467
Miscellaneous	<u>88,209</u>	<u>7,457</u>	<u>708</u>	<u>858</u>	<u>97,232</u>
Total receivables	<u>22,441,107</u>	<u>2,360,822</u>	<u>708</u>	<u>858</u>	<u>24,803,495</u>
Investments, at fair value (Note 3)					
Equity in Short-Term Investment Fund	193,022	1,023	-	-	194,045
Equity in Pooled Trust	5,683,181,388	831,579,819	8,508,644	5,512,752	6,528,782,603
Plan specific investments	<u>27,786,464</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>27,786,464</u>
Total investments	<u>5,711,160,874</u>	<u>831,580,842</u>	<u>8,508,644</u>	<u>5,512,752</u>	<u>6,556,763,112</u>
Total assets	5,733,601,981	833,941,664	8,633,655	5,628,724	6,581,806,024
<b>Liabilities</b>					
Cash overdraft (Note 3)	6,785,725	1,192,980	-	-	7,978,705
Accounts and vouchers payable	3,613,809	528,079	5,403	3,501	4,150,792
Payable to certain individuals (Note 5)	<u>653,985</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>653,985</u>
Total liabilities	<u>11,053,519</u>	<u>1,721,059</u>	<u>5,403</u>	<u>3,501</u>	<u>12,783,482</u>
<b>Net assets held in trust for pension benefits (A schedule of funding progress for each plan is presented on page 18.)</b>					
	<u>\$ 5,722,548,462</u>	<u>\$ 832,220,605</u>	<u>\$ 8,628,252</u>	<u>\$ 5,625,223</u>	<u>\$ 6,569,022,542</u>

See notes to financial statements.

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

## **Statements of Changes In Plan Net Assets Fiscal Year ended June 30, 1999**

	<u>ERS</u>	<u>MERS</u>	<u>SPRBT</u>	<u>JRBT</u>	<u>Total (Memorandum Only)</u>
<b>Additions</b>					
Contributions					
Member contributions	\$ 106,124,233	\$ 13,228,854	\$ 481,640	\$ 275,348	\$ 120,110,075
Employer contributions	92,286,944	6,608,642	631,386	737,414	100,264,386
State contributions for teachers	30,202,943	-	-	-	30,202,943
Interest on service credits purchased	1,284,052	195,335	-	-	1,479,387
Service credit transfer payments	<u>371,685</u>	<u>130,425</u>	<u>-</u>	<u>-</u>	<u>502,110</u>
Total contributions	<u>230,269,857</u>	<u>20,163,256</u>	<u>1,113,026</u>	<u>1,012,762</u>	<u>252,558,901</u>
Investment income					
Net appreciation in fair value of investments	376,448,359	55,000,236	578,364	378,385	432,405,344
Interest	114,889,899	16,511,164	156,614	98,961	131,656,638
Dividends	41,937,237	6,132,868	58,909	37,244	48,166,258
Other investment income	<u>14,061,666</u>	<u>2,056,627</u>	<u>19,871</u>	<u>12,594</u>	<u>16,150,758</u>
	547,337,161	79,700,895	813,758	527,184	628,378,998
Less investment expense	<u>18,633,202</u>	<u>2,724,058</u>	<u>27,888</u>	<u>17,281</u>	<u>21,402,429</u>
Net investment income	<u>528,703,959</u>	<u>76,976,837</u>	<u>785,870</u>	<u>509,903</u>	<u>606,976,569</u>
Total additions	<u>758,973,816</u>	<u>97,140,093</u>	<u>1,898,896</u>	<u>1,522,665</u>	<u>859,535,470</u>
<b>Deductions</b>					
Benefits					
Retirement benefits	230,830,638	25,033,839	-	-	255,864,477
Cost of living adjustment	54,134,439	2,029,134	-	-	56,163,573
SRA Plus (option)	14,341,411	1,034,693	-	-	15,376,104
Supplemental benefits	852,299	-	-	-	852,299
Death benefits post-retirement	2,582,004	509,189	-	-	3,091,193
Death benefits pre-retirement	<u>295,380</u>	<u>82,400</u>	<u>-</u>	<u>-</u>	<u>377,780</u>
Total benefits	303,036,171	28,689,255	-	-	331,725,426
Refund of contributions	5,485,162	1,689,037	-	-	7,174,199
Administrative expense	2,177,894	319,021	270	234	2,497,419
Service credit transfer payments	<u>130,425</u>	<u>371,685</u>	<u>-</u>	<u>-</u>	<u>502,110</u>
Total deductions	<u>310,829,652</u>	<u>31,068,998</u>	<u>270</u>	<u>234</u>	<u>341,899,154</u>
<b>Net increase</b>	448,144,164	66,071,095	1,898,626	1,522,431	517,636,316
<b>Net assets held in trust for pension benefits</b>					
Beginning of year	<u>5,274,404,298</u>	<u>766,149,510</u>	<u>6,729,626</u>	<u>4,102,792</u>	<u>6,051,386,226</u>
End of year	<u>\$ 5,722,548,462</u>	<u>\$ 832,220,605</u>	<u>\$ 8,628,252</u>	<u>\$ 5,625,223</u>	<u>\$ 6,569,022,542</u>

See notes to financial statements.

## *Notes to Financial Statements*

### **1. Plan Descriptions**

#### **(a). General**

The Employees' Retirement System of Rhode Island (the "System") acts as a common investment and administrative agent for pension benefits to be provided for four defined benefit retirement plans as listed below:

<u>Plan Name</u>	<u>Type of Plan</u>
Employees' Retirement System ( <i>ERS</i> )	Cost-sharing multiple-employer defined benefit plan
Municipal Employees' Retirement System ( <i>MERS</i> )	Agent multiple-employer defined benefit plan
State Police Retirement Benefits Trust ( <i>SPRBT</i> )	Single-employer defined benefit plan
Judicial Retirement Benefits Trust ( <i>JRBT</i> )	Single-employer defined benefit plan

Although the assets of the plans are commingled for investment purposes, each plan's assets are accounted for separately and may be used only for the payment of benefits to the members of that plan, in accordance with the terms of that plan.

The System's financial statements are included as Pension Trust Funds within the Trust and Agency Funds in the Comprehensive Annual Financial Report of the State of Rhode Island and Providence Plantations.

The System is administered by the State of Rhode Island Retirement Board which consists of 15 members: the general treasurer; the director of administration or his or her designee; the budget officer or his or her designee; the fiscal advisor to the house finance committee or his or her designee; the president of the league of cities and towns or his or her designee; two (2) active State employee members of the retirement system or officials from state employee unions to be elected by active State employees; two (2) active teacher members of the retirement system or officials from a teachers union to be elected by active teachers; one active municipal employee member of the retirement system or an official from a municipal employees union to be elected by active municipal employees; one retired member of the retirement system to be elected by retired members of the System; the chairperson of the house finance committee or his or her designee; the chairperson of the senate finance committee or his or her designee; and two (2) public representatives, one of whom shall be a C.L.U. competent in the area of pension benefits, shall be appointed by the governor and whose term shall be for four (4) years, or until their successors are appointed.

The System's purpose is to provide retirement benefits to state employees, public school teachers, general municipal employees, public safety employees, state police officers and judges.

**EMPLOYEES' RETIREMENT SYSTEM OF RHODE ISLAND**  
**Notes to Financial Statements**

A summary of membership in the plans as of the June 30, 1998 actuarial valuation is listed below:

	<i>Retirees and beneficiaries</i>	<i>Terminated plan members entitled to but not yet receiving benefits</i>	<i>Active Vested</i>	<i>Active Non- vested</i>	<i>Total by Plan</i>
<b><u>ERS</u></b>					
State Employees	9,033	1,759	8,523	4,582	23,897
Teachers	5,775	1,243	7,219	5,664	19,901
<b><u>MERS</u></b>					
General Employees	3,033	786	2,416	3,369	9,604
Public Safety	224	34	390	541	1,189
<b><u>SPRBT</u></b>					
	-	-	-	130	130
<b><u>JRBT</u></b>					
	-	-	-	29	29
<i>Total by type</i>	18,065	3,822	18,548	14,315	54,750

**(b). Membership and Benefit Provisions**

(1) Employees' Retirement System (ERS)

The ERS was established under section two of chapter 2334 of the Rhode Island Public Laws of 1936 and placed under the management of the Retirement Board for the purpose of providing retirement allowances for employees of the State of Rhode Island under the provisions of chapters 8 to 10, inclusive, of title 36, and public school teachers under the provisions of chapters 15 to 17, inclusive, of title 16 of the Rhode Island General Laws.

**EMPLOYEES' RETIREMENT SYSTEM OF RHODE ISLAND**  
**Notes to Financial Statements**

The plan covers most State employees other than certain personnel at the State colleges and university (principally faculty and administrative personnel). Elected officials may become members on an optional basis. Membership in the plan is compulsory for teachers, including superintendents, principals, school nurses, and certain other school officials in the public schools in the cities and towns. Rhode Island Airport Corporation (RIAC) employees hired before July 1, 1993 are also covered and have the same benefits as State employees. Rhode Island Economic Development Corporation (RIEDC) employees who were (1) active contributing members and employees of the Department of Economic Development of the State of Rhode Island before October 31, 1995, and (2) elected to continue membership in the plan are also covered and have the same benefits as State employees.

The plan provides unreduced benefits of 1.7% of earnings for each of the first ten years of service; 1.9% for each of the next ten years; 3.0% per year for each of the next fourteen years; and 2% for the 35th year. Joint and survivor options are available as well as the Service Retirement Allowance (SRA) Plus option that provides for the payment of a larger benefit before the attainment of age sixty-two (62) and a reduced amount thereafter. The reduced amount is equal to the benefit before age sixty-two (62), including cost-of-living increases, minus the member's estimated social security benefit payable at age sixty-two (62). The maximum benefit is 80% of final average earnings after 35 years of service. Such benefits are available to members at least age 60 with 10 years of service, or after 28 years at any age. A different benefit formula applies to State correctional officers who may retire at age 50 if they have 20 years of service. Benefits for all employees are based on the average of the highest three consecutive years' earnings, exclusive of overtime.

On the third January after retirement, a cost-of-living increase of 3% (compounded annually) is provided independent of actual changes in the consumer price index. The plan also provides non-service-connected disability benefits after five years of service; service-connected disability pensions with no minimum service requirement; vested benefits after ten years of service; survivor's benefits for service-connected death; and certain lump sum death benefits.

The plan also provides benefits to legislators elected to office prior to January 1, 1995, of \$600 for every year served up to a maximum of \$12,000. Such benefits are available to legislators 55 and over with at least 8 years of service or, at any age with 20 or more years of service.

The plan provides a survivor benefit to public school teachers via a "Teachers Survivor Benefits Fund" in lieu of Social Security. Not all school districts participate in the plan. The cost of the benefits provided by the plan are two percent (2%) of the member's annual salary up to but not exceeding an annual salary of \$9,600; one-half (1/2) of the cost is contributed by the member by deductions from his or her salary, and the other half (1/2) is contributed and paid by the respective city, town, or school district by which the member is

**EMPLOYEES' RETIREMENT SYSTEM OF RHODE ISLAND**  
**Notes to Financial Statements**

employed. These contributions are in addition to the contributions required for regular pension benefits.

Spouse, parents, family and children benefits are payable following the decease of a member. A spouse shall be entitled to benefits upon attaining the age of sixty (60) years. Children's benefits are payable to the child, including a stepchild or adopted child of a deceased member if the child is unmarried and under the age of eighteen (18) years or twenty-three (23) years and a full time student, and was dependent upon the member at the time of the member's death. Family benefits are provided if at the time of the member's death the surviving spouse has in his or her care a child of the deceased member entitled to child benefits. Parents benefits are payable to the parent or parents of a deceased member if the member did not leave a widow, widower, or child who could ever qualify for monthly benefits on the member's wages and the parent.

The Teachers Survivor Benefits Fund provides benefits based on the highest salary at the time of retirement of the teacher. Benefits are payable in accordance with the following table:

<u>Highest Annual Salary</u>	<u>Spousal Monthly Minimum Benefit</u>
\$17,000 or less	\$600
\$17,001 to \$25,000	\$700
\$25,001 to \$33,000	\$800
\$33,001 to \$40,000	\$900
\$40,001 and over	\$1,000

Benefits payable to children and families are equal to the spousal benefit multiplied by the percentage below:

Parent and 1 Child	Parent and 2 Children	Parent and more than 2 Children	One Child Alone	Two Children Alone	Three or more Children Alone
150%	175%	175%	75%	150%	175%

**EMPLOYEES' RETIREMENT SYSTEM OF RHODE ISLAND**  
**Notes to Financial Statements**

(2) Municipal Employees' Retirement System (MERS)

The MERS was established under section one of chapter 2784 of the Rhode Island Public Laws of 1951 and placed under the management of the Retirement Board for the purpose of providing retirement allowances to employees of municipalities, housing authorities, water and sewer districts, and municipal police and fire persons that have elected to participate.

The plan generally provides retirement benefits equal to 2% of a member's final average salary multiplied by the number of years of total service up to a maximum of 75%. Joint and survivor options are available as well as the Service Retirement Allowance (SRA) Plus option that provides for the payment of a larger benefit before the attainment of age sixty-two (62) and a reduced amount thereafter. The reduced amount is equal to the benefit before age sixty-two (62), including cost-of-living increases, minus the member's estimated social security benefit payable at age sixty-two (62). Such benefits are available to members at least age 58 with 10 years of service or after 30 years of service at any age. Police and fire personnel may retire at age 55 if they have 10 years of service or after 25 years of service at any age. An optional cost-of-living provision may be elected for police and fire personnel and general employees. An option may be elected to provide a 20 year service pension with a benefit equal to 2.5% for each year of service up to a maximum of 75% for police and fire personnel. Benefits are based on the average of the highest three consecutive years' earnings, exclusive of overtime.

The plan also provides non-service-connected disability benefits after 5 years of service; service-connected disability pensions with no minimum service requirement; vested benefits after 10 years of service; survivor's benefits; and certain lump sum death benefits. A summary of participating employers is listed below:

Municipalities, housing authorities, water and sewer districts.	62
Municipal police and fire departments.	<u>44</u>
Total participating units as of June 30, 1999	106

(3) State Police Retirement Benefits Trust (SPRBT)

The State Police Retirement Benefits Trust was established under Rhode Island General Laws 42-28-22.1 and was placed under the management of the Retirement Board for the purpose of providing retirement allowances to State Police.

The plan covers all State Police and Superintendents hired after July 1, 1987.

The plan generally provides retirement benefits equal to 50% of final salary after 20 years of service, plus 3.0% of final salary times service in excess of 20 years through 25 years to a maximum of 65% of final salary. Such benefits are available to members after 20 years of service regardless of age. The Superintendent of the State Police will receive 50% of his/her final salary and may retire after attainment of age 60 and 10 years of service. A cost-of-

living adjustment of \$1,500 per annum beginning on January 1st of the year in which a member attains his/her third anniversary of retirement is provided to all members.

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

### ***Notes to Financial Statements***

Benefits are based on the final base salary earned at retirement including longevity increment, holiday pay, clothing allowance and up to 400 overtime hours.

The plan also provides nonservice-connected disability benefits after 10 years of service and service-connected disability pensions with no minimum service requirement.

#### **(4) Judicial Retirement Benefits Trust (JRBT)**

The Judicial Retirement Benefits Trust was established under Rhode Island General Laws 8-3-16; 8-8-10.1; 28-30-18.1; 31-43-11.1; and was placed under the management of the Retirement Board for the purpose of providing retirement allowances to Justices of the Supreme, Superior, Family, District, Workers Compensation and Administrative Adjudication courts.

The plan covers all Judges appointed after December 31, 1989.

The plan generally provides retirement benefits equal to 75% of the final salary at the time of retirement after 20 years of service, or 10 years of service and attainment of age 65. Judges retiring after 20 years of service after age 65 or 15 years of service after age 70 will receive full retirement benefits which is the final salary at time of retirement. On the third January after the date of retirement, a cost-of-living increase amounting to 3% not compounded is provided to Supreme, Superior, Family and District Court Judges, independent of actual changes in the consumer price index. Administrative Adjudication and Workers' Compensation Court Judges, on the third January after the date of retirement, receive a cost-of-living increase amounting to 3% compounded annually.

## **2. Summary of Significant Accounting Policies**

These financial statements were prepared in accordance with generally accepted accounting principles as prescribed by the Governmental Accounting Standards Board (GASB). The Governmental Accounting Standards Board (GASB) has the responsibility for establishing generally accepted accounting principles for defined benefit pension plans established by governmental entities. In accordance with GASB Statement No. 20, in the absence of specific guidance from a GASB pronouncement, pronouncements of the Financial Accounting Standards Board (FASB) issued on or before November 30, 1989 have been followed.

**EMPLOYEES' RETIREMENT SYSTEM OF RHODE ISLAND**  
*Notes to Financial Statements*

**Basis of Accounting** - The financial statements of the System are prepared on the accrual basis of accounting. Under this method revenues are recorded when earned and expenses are recorded when incurred. Plan member contributions are recognized in the period in which the contributions are due. Employer contributions to each plan are recognized when due and the employer has made a formal commitment to provide the contributions. Benefits and refunds are recognized when due and payable in accordance with the terms of each plan. Dividend income is recorded on the ex-dividend date. Investment transactions are recorded on a trade date basis.

**Method Used to Value Investments** - Investments are recorded in the financial statements at fair value. Fair value is the amount that a plan can reasonably expect to receive for an investment in a current sale between a willing buyer and a willing seller - that is, other than a forced liquidation sale. The fair value of fixed income and domestic and international stocks are generally based on published market prices and quotations from national security exchanges and securities pricing services. Real estate is primarily valued on appraisals by independent appraisers or as adjusted by the general partner. Other securities and investments that are not traded on a national security exchange are valued by the respective fund manager.

**Cash and Cash Equivalents** - Cash represents cash held in trust in a financial institution. Cash equivalents are highly liquid investments with a maturity of three months or less at the time of purchase.

**Foreign Currency Exchange Contracts** - The System may enter into foreign currency exchange contracts to minimize the short-term impact of foreign currency fluctuations on the asset and liability positions of foreign investments. The gains or losses on these contracts are included in income in the period in which the exchange rates change. Gains and losses on contracts which hedge specific foreign currency denominated commitments are deferred and recognized in the period in which the transaction is completed.

**Mortgage-Backed Securities** - The System invests in various mortgage-backed securities, such as collateralized mortgage obligations, interest-only strips, and principal-only strips. They are reported in aggregate as U.S. Government and Agency Securities in the disclosure of custodial credit risk (See Note 3 on Investments). The System may invest in interest-only (IO) and principal-only strips (PO) in part to hedge against a rise in interest rates. Interest-only strips are based on cash flows from interest payments on underlying mortgages. Therefore, they are sensitive to pre-

payments by mortgagees, which may result from a decline in interest rates. Principal-only strips receive principal cash flows from the underlying

**EMPLOYEES' RETIREMENT SYSTEM OF RHODE ISLAND**  
*Notes to Financial Statements*

mortgages. In periods of rising interest rates, homeowners tend to make fewer mortgage prepayments. The System held no interest-only strips and principal-only strips at June 30, 1999.

**Memorandum Only - Total Columns** - Total columns on the financial statements are captioned "memorandum only" to indicate that they are presented only to facilitate financial analysis. Data in these columns are not comparable to a consolidation. Interfund eliminations have not been made in the aggregation of this data.

### 3. Cash Deposits and Investments

#### (a). Cash Deposits and Cash Equivalents

At June 30, 1999, the carrying amounts of the plans' cash deposits, including cash overdrafts, are listed below:

	<u>ERS</u>	<u>MERS</u>	<u>SPRBT</u>	<u>JRBT</u>
<i>Book balance</i>	\$ (6,785,725)	\$ (1,192,980)	\$ 124,303	\$ 115,114
<i>Bank balance</i>	\$ 447,967	\$ 86,377	\$ 124,240	\$ 115,817

The bank balances represent the plans' deposits in short-term trust accounts that are covered by federal depository insurance.

In accordance with Rhode Island General Laws, Chapter 35-10.1, depository institutions holding deposits of the State, its agencies or governmental subdivisions of the State, shall at a minimum, insure or pledge eligible collateral equal to one hundred percent of time deposits with maturities greater than sixty days. Any of these institutions that do not meet minimum capital standards prescribed by federal regulators shall insure or pledge eligible collateral equal to one hundred percent of deposits, regardless of maturity. None of the System's deposits was required to be collateralized at June 30, 1999.

**EMPLOYEES' RETIREMENT SYSTEM OF RHODE ISLAND**  
*Notes to Financial Statements*

**(b). Investments**

The State Investment Commission oversees all investments made by the State of Rhode Island, including those made for the System. Investment managers engaged by the Commission, at their discretion and in accordance with the investment objectives and guidelines for the System, make certain investments. The General Treasurer makes certain short-term investments on a daily basis. Rhode Island General Laws, Section 35-10-11 (b)(3) requires that all investments shall be made in securities as would be acquired by prudent persons of discretion and intelligence who are seeking a reasonable income and the preservation of capital.

On July 1, 1992, the State Investment Commission pooled the assets of the ERS with the assets of the MERS for investment purposes only, and assigned units to the plans based on their respective share of market value. On September 29, 1994 and November 1, 1995, the assets of the SPRBT and the JRBT, respectively, were added to the pool for investment purposes only. The custodian bank (State Street Bank) holds most assets of the System in two pooled trusts, Short-term Investment Trust and Pooled Trust. Each plan holds units in the trusts. The number of units held by each plan is a function of each plans' respective contributions to or withdrawals from the trust.

Certain investments are not pooled and are held by only one plan (Plan specific investments). As of June 30, 1999, the ERS held investments in bonds issued by the R.I. Housing and Mortgage Finance Corporation having a fair value of \$4,050,373 and the R.I. Industrial Facilities Corporation having a fair value of \$23,000,000. These entities are included as discretely presented proprietary component units in the State of Rhode Island Comprehensive Annual Financial Report.

The System's investments (at fair value) are categorized in the following table to give an indication of the level of risk assumed by the entity at June 30, 1999:

**Category 1** includes insured or registered, or securities held by the System or its agent in the System's name.

**Category 2** includes uninsured and unregistered, with securities held by the counterparty's trust department or agent in the System's name.

**Category 3** includes uninsured and unregistered, with securities held by the counterparty, or by its trust department or agent but not in the System's name.

**EMPLOYEES' RETIREMENT SYSTEM OF RHODE ISLAND**  
**Notes to Financial Statements**

	<i>Short-term Investment Fund</i>	<i>Pooled Trust</i>	<i>Plan Specific</i>
<i>Investments - Category 1</i>			
U.S. Government and Agency Securities	\$ -	\$ 1,187,638,500	\$ -
Commercial Paper		116,907,109	
Corporate Bonds and Notes		653,673,861	27,050,373
Foreign Bonds		33,185,542	
Equity Securities		3,141,819,132	
Foreign Equity Securities		687,354,952	
International Unit Investment Trust		252,535,913	
Subtotal	-	6,073,115,009	27,050,373
<i>Investments not categorized</i>			
Emerging Markets Mutual Fund		21,997,724	
Real Estate and Venture Capital Limited Partnerships		233,108,675	
Money Market Mutual Funds	192,960	314,833,384	
Subtotal	192,960	569,939,783	-
Total	\$ 192,960	\$ 6,643,054,792	\$ 27,050,373
<i>Reconciliation to investments on Statements of Plan</i>			
<i>Net Assets</i>			
Total above	192,960	6,643,054,792	27,050,373
Net investment payable and receivable	1,085	(126,187,759)	736,091
Foreign Cash *		9,719,535	
Domestic Cash *	-	2,196,035	-
Investments on Statements of Plan Net Assets	\$ 194,045	\$ 6,528,782,603	\$ 27,786,464

\*Deposits at the System's custodian bank, which consist of uncollateralized deposits in foreign banks, are not covered by United States federal depository insurance. The deposits in domestic banks are covered by federal depository insurance.

**(c). Forward Foreign Currency Contracts**

The System may enter into forward foreign currency contracts. These contracts involve risk in excess of the amount reflected in the System's Statements of Plan Net Assets. The face or contract amount in U.S. dollars reflects the total exposure the System has in that particular currency contract. By policy, no more than 50% of actively managed Foreign Equity

securities (at fair value) may be hedged into the base currency (US Dollars). The U.S. dollar value of forward foreign currency contracts is determined using forward currency exchange rates supplied by a quotation service. Losses may arise due to changes in the value of the foreign currency or if the counterparty does not perform under the contract.

***EMPLOYEES' RETIREMENT SYSTEM OF RHODE ISLAND***  
***Notes to Financial Statements***

#### **4. Contributions and Reserves**

Contribution requirements for plan members and employers are established pursuant to Rhode Island General Laws. Employers are required to contribute at an actuarially determined rate. Plan member contributions are fixed by statute.

##### **(a). Funding Policy**

###### ERS, SPRBT and JRBT

The funding policy, as set forth in Rhode Island General Laws, Section 36-10-2 provides for actuarially determined periodic contributions to the plans. The Employer's contributions to the plans include (1) normal cost and (2) a payment required to amortize the unfunded frozen actuarial liability of the plans. The ERS' liability is amortized, as of June 30, 1985, over thirty (30) years in multiples of two hundred and fifteen thousandths of one percent (.215%) starting with one multiple in the fiscal year beginning July 1, 1986, and increasing by one multiple in each successive year until the fiscal year ending June 30, 1989; and amortize the remaining unfunded liability of the system as of June 30, 1988, over twenty-seven (27) years beginning in the fiscal year beginning July 1, 1989, calculated such that each year's total unfunded liability payment increases at the assumed rate of inflation over the prior year's total payment. The unfunded liabilities of the SPRBT and JRBT plans are amortized over a 30-year period beginning July 1, 1992. Any subsequent changes to the unfunded liability due to changes to benefits or actuarial assumptions are amortized over a new 30-year period or over the remaining initial amortization period depending on how large the total change to the unfunded liability for each fiscal year is relative to the existing unfunded liability. The normal cost is determined using the frozen entry age cost method.

###### MERS

The funding policy, as set forth in Rhode Island General Laws, Section 45-21-42 provides for actuarially determined periodic contributions to the plans. Each employer's contribution to the plans includes normal cost and a payment, where applicable, to amortize the unfunded actuarial liability. The normal cost is determined using the entry age normal cost method. In 1989, the rules regarding the amortizing of the unfunded liability were changed. The new rules provided that the unfunded liability in 1988 will be amortized over the remainder of a 25-year period which commenced on the date the unit joined the plan. Subsequent divergences from the actuarial assumptions are funded over the projected future salaries of active members.

**EMPLOYEES' RETIREMENT SYSTEM OF RHODE ISLAND**  
**Notes to Financial Statements**

Administrative Expenses

Administrative costs of the System are financed through investment earnings up to a maximum of 1.5% as reported in the audited financial statements for the next preceding fiscal year.

**(b). Contributions**

The table below displays the contribution rates for the year ending June 30, 1999:

<b>Plan</b>	<b>Employee</b>	<b>Employer</b>
<b>ERS</b>		
State Employees	8.75%	9.85%
Teachers <i>Municipal funded</i>	9.50%	6.62% (5.63% for towns not participating in the 1990 early retirement incentive)
<i>State funded</i>		4.90% (4.24% for towns not participating in the 1990 early retirement incentive)
<b>MERS</b>		
General Employees	6.00% (additional 1% with a cost-of-living adjustment)	62 Municipalities, housing authorities, water and sewer districts contributed various actuarially determined rates.
Public Safety	7.00% (additional 1% with a cost-of-living adjustment and /or 1% with a 20 year service plan)	44 Municipal police and fire departments contributed various actuarially determined rates.
<b>SPRBT</b>	8.75%	11.43%
<b>JRBT</b>	8.75%	23.36%

**5. Payable To Certain Individuals**

The ERS was involved in federal litigation by certain individuals who were contesting the constitutionality of Section 36-9.1-2, which repealed Section 36-9-33 of the General Laws thereby depriving those individuals of the right to participate in the plan. Pursuant to the statute, the plan was required by January 1, 1995, to return to the employees and employers their contribution with interest at the rate of 8% for the applicable time periods during which the contributions were held by the plan. By agreement between the parties, the plan held employee and employer contributions pending outcome of the litigation or further agreement between the parties. On March 24, 1999, a judgment was entered whereby Section 36-9-33 was found constitutional as it applied to the plaintiffs by the United States First Circuit Court of Appeals. The U.S. Supreme Court affirmed the First Circuit decision by denying a petition for a writ of certiorari on October 12, 1999. The judgment ordered additional payment of interest on contributions to September 1, 1998. As

***EMPLOYEES' RETIREMENT SYSTEM OF RHODE ISLAND***  
***Notes to Financial Statements***

of June 30, 1999 certain individuals have received payments decreasing the payable from \$1,123,087 to \$653,985.

**EMPLOYEES' RETIREMENT SYSTEM OF RHODE ISLAND**  
**Required Supplementary Information**  
**Schedules Of Funding Progress**

Actuarial Valuation Date	Actuarial Value of Assets (AVA) (a)	Unfunded Frozen Actuarial Liability (UFAL) (b)	Frozen Actuarial Liability (c) = (a + b)	Funded Ratio (a / c)	Covered Payroll (d)	UFAL as a Percentage of Covered Payroll (b / d)
<b>ERS (State Employees)</b>						
06/30/1998	\$ 2,075,619,300	\$ 500,662,800	\$ 2,576,282,100	80.6%	\$ 477,319,600	104.9%
06/30/1997	1,810,447,600	502,116,100	2,312,563,700	78.3%	443,709,300	113.2%
06/30/1996	1,529,403,200	444,814,700	1,974,217,900	77.5%	452,608,500	98.3%
06/30/1995	1,345,530,000	442,370,600	1,787,900,600	75.3%	440,574,000	100.4%
06/30/1994	1,234,373,500	438,794,100	1,673,167,600	73.8%	454,687,000	96.5%
06/30/1993	1,151,128,700	434,225,700	1,585,354,400	72.6%	444,572,000	97.7%
<b>ERS (Teachers)</b>						
06/30/1998	\$ 3,045,858,900	\$ 953,864,000	\$ 3,999,722,800	76.2%	\$ 636,246,600	149.9%
06/30/1997	2,626,621,500	953,031,000	3,579,652,500	73.4%	604,076,600	157.8%
06/30/1996	2,181,535,900	767,893,900	2,949,429,800	74.0%	556,114,500	138.1%
06/30/1995	1,824,102,300	762,202,100	2,586,304,400	70.5%	507,125,000	150.3%
06/30/1994	1,642,292,300	754,727,900	2,397,020,200	68.5%	485,325,000	155.5%
06/30/1993	1,492,915,800	745,698,400	2,238,614,200	66.7%	473,295,000	157.6%
<b>SPRBT</b>						
06/30/1998	\$ 6,756,900	\$ 581,300	\$ 7,338,200	92.1%	\$ 7,211,900	8.1%
06/30/1997	4,861,600	574,300	5,435,900	89.4%	5,371,000	10.7%
06/30/1996	3,115,500	560,200	3,675,700	84.8%	4,948,800	11.3%
06/30/1995	1,858,800	545,700	2,404,500	77.3%	4,751,100	11.5%
06/30/1994	926,300	530,800	1,457,100	63.6%	3,060,300	17.3%
<b>JRBT</b>						
06/30/1998	\$ 4,120,000	\$ 928,800	\$ 5,048,900	81.6%	\$ 3,040,000	30.6%
06/30/1997	2,607,482	900,845	3,508,327	74.3%	2,815,218	32.0%
06/30/1996	1,345,100	40,800	1,385,900	97.1%	2,596,900	1.6%
06/30/1995	801,300	39,700	841,000	95.3%	2,398,400	1.7%
06/30/1994	462,800	38,500	501,300	92.3%	1,521,700	2.5%
<hr/>						
<b>MERS</b>						
Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) - Entry Age - (b)	Unfunded AAL (UAAL) (b - a)	Funded Ratio (a / b)	Covered Payroll (c)	UAAL as a Percentage of Covered Payroll ((b - a) / c)
06/30/1998	\$ 737,745,574	\$ 572,905,862	\$ (164,839,712)	128.8%	\$ 181,260,006	(90.9)%
06/30/1997	667,632,428	502,247,591	(165,384,837)	132.9%	167,527,881	(98.7)%
06/30/1996	564,388,311	465,004,064	(99,384,247)	121.4%	153,750,203	(64.6)%
06/30/1995	485,074,227	416,731,907	(68,342,320)	116.4%	151,125,008	(45.2)%
06/30/1994	445,340,947	369,782,138	(75,558,809)	120.4%	133,213,341	(56.7)%

See notes to required supplementary information

**EMPLOYEES' RETIREMENT SYSTEM OF RHODE ISLAND**  
**Required Supplementary Information**  
**Schedules Of Contributions From The Employers**  
**And Other Contributing Entity**

<b>ERS</b>							
Fiscal	<u>State Employees</u>			<u>Teachers (State)</u>		<u>Teachers (Employers)</u>	
Year Ended	Annual Required	Percentage	Annual Required	Percentage	Annual Required	Percentage	
<u>June 30</u>	<u>Contribution</u>	<u>Contributed</u>	<u>Contribution</u>	<u>Contributed</u>	<u>Contribution</u>	<u>Contributed</u>	
1999	\$ 48,526,064	100%	\$ 30,202,943	100%	\$ 42,373,952	100%	
1998	51,310,092	100%	35,005,382	100%	52,040,574	100%	
1997	45,403,827	100%	34,871,679	100%	48,945,845	100%	
1996	42,949,692	100%	30,779,586	100%	47,238,332	100%	
1995	52,569,291	66%	36,922,896	81%	50,217,729	100%	
1994	47,586,243	100%	32,746,070	100%	47,098,906	100%	

---

<b>MERS</b>		
Fiscal	Annual Required	Percentage
Year Ended	<u>Contribution</u>	<u>Contributed</u>
<u>June 30</u>		
1999	\$ 6,608,642	100%
1998	5,139,666	100%
1997	8,734,795	100%
1996	4,600,276	100%
1995	4,481,460	100%
1994	4,694,650	100%

---

<b>SPRBT</b>		
Fiscal	Annual Required	Percentage
Year Ended	<u>Contribution</u>	<u>Contributed</u>
<u>June 30</u>		
1999	\$ 631,386	100%
1998	602,630	100%
1997	453,621	100%
1996	717,874	100%
1995	606,150	100%

---

<b>JRBT</b>		
Fiscal	Annual Required	Percentage
Year Ended	<u>Contribution</u>	<u>Contributed</u>
<u>June 30</u>		
1999	\$ 737,414	100%
1998	744,054	100%
1997	618,513	100%
1996	260,299	100%
1995	155,840	100%

*See notes to required supplementary information*

**EMPLOYEES' RETIREMENT SYSTEM OF RHODE ISLAND**  
**Notes to Required Supplementary Information**  
**Fiscal Year Ended June 30, 1999**

## **1. Schedules Of Funding Progress**

Effective with the June 30, 1998 valuation, the actuarial value of assets was developed using a four-year moving average technique for ERS, SPRBT and JRBT. The MERS actuarial value of assets was developed using a three-year smoothing of the market value of assets.

Effective with the June 30, 1997 valuation, certain actuarial assumptions were changed due to an experience study. Specifically, the actuarial value of assets for ERS, MERS, SPRBT and JRBT was reset to equal the fair market value of assets at June 30, 1997. The investment rate of return was increased from 8.00% to 8.25%. Projected salary increases were changed from a fixed percentage to a sliding scale based on age and service. The inflation assumption was increased to 3.5% from 3.0%.

Effective with the June 30, 1996 valuation, the actuarial value of assets for ERS and MERS was reset to equal the market value of assets at June 30, 1996.

In 1993 the Retirement Board elected to compute future fiscal year costs one extra year in advance to assist the fiscal budget process. Therefore employer costs for fiscal year ending June 30, 2001 is based on the valuation results and data as of June 30, 1998.

The MERS funded ratio is a composite of all units in the plan. The System performs a separate valuation for each unit.

Historical trend information has been presented for all years, for which it is available.

## **2. Schedules Of Employer Contributions**

In the fiscal year ended June 30, 1994, the contributions to MERS reflect a reduction mainly due to a mark-to-market of the assets and change to the salary growth assumption from a graduated scale to a fixed 4.5% annually.

The MERS contributions for the fiscal year ended June 30, 1997 include a \$3,843,955 transfer from a new unit joining the plan.

In the fiscal year ended June 30, 1995, ERS contributed less than 100% of the required contribution. This is the result of fiscal year 1991 supplemental budget legislation; whereby, the State of Rhode Island (the State) withdrew \$20,788,812 from ERS. The Internal Revenue Service (IRS) determined that this action was in violation of Section 401(a) of the Internal Revenue Code (the Code). On February

**EMPLOYEES' RETIREMENT SYSTEM OF RHODE ISLAND**  
**Notes to Required Supplementary Information**  
**Fiscal Year Ended June 30, 1999**

4, 1994, the District Director of the IRS approved an agreement between the State and the IRS whereby the State agreed to repay to the ERS by no later than December 31, 1994, \$20,788,812 plus accrued interest at eight percent (8%) compounded monthly retroactive to March 1, 1991. As of December 31, 1994, the State repaid the amount withdrawn plus interest by designating current year contributions as payment of the obligation.

The SPRBT and JRBT made contributions prior to 1995 but such contributions were not based on actuarial valuations.

The information presented in the required supplementary schedules was determined as part of the actuarial valuations at the dates indicated. Additional information as of the latest actuarial valuation follows.

### 3. Actuarial Assumptions and Methods

	ERS		MERS	SPRBT	JRBT
	<i>State Employees</i>	<i>Teachers</i>			
Valuation Date	6/30/98	6/30/98	6/30/98	6/30/98	6/30/98
Actuarial Cost Method	Frozen Entry Age	Frozen Entry Age	Entry Age Normal	Frozen Entry Age	Frozen Entry Age
Amortization Method	Level Percent of Payroll – Closed	Level Percent of Payroll – Closed	<i>Initial base:</i> Level dollar – Closed <i>All subsequent changes:</i> Level Percent of Payroll – Open	Level Percent of Payroll – Closed	Level Percent of Payroll – Closed
Equivalent Single Remaining Amortization Period	17 years	18 years	Various	24 years	29 years
Asset Valuation Method	4 Year Moving Average	4 Year Moving Average	3 Year Smoothing of Market Value	4 Year Moving Average	4 Year Moving Average
Actuarial Assumptions					
Investment Rate of Return	8.25%	8.25%	8.25%	8.25%	8.25%
Projected Salary Increases	4.75% to 8.75%	4.25% to 13.25%	<i>General Employees</i> 4.75% to 10.75%  <i>Police &amp; Fire Employees</i> 5.00% to 15.00%	5.00% to 15.00%	5.50%
Inflation	3.50%	3.50%	3.50%	3.50%	3.50%
Cost of Living Adjustments	3.0% compounded	3.0% compounded	3.0% Non-compounded	\$1,500 per annum	3.0% <i>(see Note 1(b)(4))</i>

**EMPLOYEES' RETIREMENT SYSTEM OF RHODE ISLAND**  
**Required Supplementary Information**  
**Year 2000 Disclosure**

The Year 2000 issue is the result of shortcomings in many electronic data processing systems and other electronic equipment that may adversely effect the Employees Retirement System of Rhode Island's (ERSRI) operations as early as fiscal year 1999.

ERSRI completed an inventory of its computer systems and determined that certain software and personal computers required upgrading to be Year 2000 compliant. ERSRI assessed these systems and purchased new Year 2000 compliant versions of the software and new personal computers where necessary.

ERSRI, through the Treasury, uses external organizations (banks and trust custodians) to make certain payments and invest assets. The external organizations are responsible for any required remediation to these systems. Any costs associated with remediation and testing of these systems will be borne by the external organizations. At June 30, 1999, the System's master custodian reported that its Year 2000 readiness project was in the validation/testing phase, with completion of the project estimated for September 1999. The General Treasurer of the State of Rhode Island has established a task force comprised of private sector information professionals and treasury managers to evaluate the progress of the external organizations' efforts.

ERSRI utilizes the statewide accounting system and two specific accounting systems (retirement contributions and pension payroll) that are critical to conducting its operations. The State's Department of Administration maintains these systems and is also responsible for any required remediation. At June 30, 1999 these systems were in the validation/testing stage.

Because of the unprecedented nature of the Year 2000 issue, its effect and the success of related remediation efforts will not be determinable until the year 2000 and thereafter. Management cannot assure that ERSRI will be Year 2000 ready, that the ERSRI's remediation efforts will be successful in whole or in part, or that the parties with whom the ERSRI does business will be Year 2000 ready.



State of Rhode Island and Providence Plantations

GENERAL ASSEMBLY

Office of the Auditor General

1145 Main Street  
Pawtucket, Rhode Island 02860-4807

OFFICE  
(401) 222-2435  
FAX  
(401) 222-2111

**INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE AND  
ON INTERNAL CONTROL OVER FINANCIAL REPORTING  
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:

We have audited the statements of plan net assets of the State of Rhode Island and Providence Plantations Employees' Retirement System (the System) as of June 30, 1999 and the related statements of changes in plan net assets for the year then ended, and have issued our report thereon dated February 1, 2000. We conducted our audit in accordance with generally accepted auditing standards and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

**Compliance**

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 that are required to be reported under *Government Auditing Standards*. However, we noted certain immaterial instances of noncompliance that we will report to the management of the System in a separate communication.

**Internal Control Over Financial Reporting**

In planning and performing our audit, we considered the System's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control over

financial reporting. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be material weaknesses. A material weakness is a condition in which the design or

Joint Committee on Legislative Services  
Page 2

operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over financial reporting and its operation that we consider to be material weaknesses. However, we noted other matters involving the internal control over financial reporting that we will report to the management of the System in a separate communication.

This report is intended solely for the information and use of the members of the Retirement Board, management, and the Joint Committee on Legislative Services, 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.



Ernest A. Almonte, CPA, CFE  
Auditor General

February 1, 2000