

# 1. Meeting of the ERS Board of Trustees' Audit Committee

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August 29, 2018



# Public Agenda Item # 1.1

## *Call Meeting of the ERS Board of Trustees' Audit Committee to Order*



August 29, 2018

## Public Agenda Item # 2.1

*Review and Approval of the Minutes to the May 23, 2018  
ERS Audit Committee Meeting (**Action**)*

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August 29, 2018

Questions?  
Action Item



# Public Agenda Item # 3.1

## *Review of Internal Audit Reports*



August 29, 2018

Tony Chavez, Director of Internal Audit

# Status of Audit Recommendations



Tony Chavez, Director of Internal Audit

Beth Gilbert, Internal Auditor

# Status of Audit Recommendations



## **Status Levels**

- Implemented
- Partially Implemented
- No Action Taken
- Management Acceptance

## **Methodology**

- Process owner self-assessment and information-sharing
- Internal Audit review and evaluation

# Summary



Audit Engagement	MAP Owner	MAPs Partially Implemented
Revenue Processing	Director of Finance	1
HealthSelect Denial	Assistant Director of Group Benefits	2



Questions?



## Public Agenda Item # 3.2

*Review of Audit Administrative Items:  
Internal Audit Assessment and Proposed FY19 Audit Plan (Action)*



August 29, 2018

Tony Chavez, Director of Internal Audit

# Risk Assessment and Proposed FY19 Audit Plan



Tony Chavez, Director of Internal Audit  
Beth Gilbert, Internal Auditor

# Risk Assessment and Proposed FY19 Audit Plan

**A risk-based audit  
plan must be  
established.**

(Gov. Code Chapter 2102)

**Identify risks**



**Measure risks**



**Prioritize risks**



**Select and develop proposed  
audit plan**

# Key Takeaways

- Total number of engagements reduced
- Number of contingent audits increased
- “Strategic” risk criteria weight increased in the investment universe to reflect asset allocation changes
- “Governance” risk criteria weight increased in the information technology universe based on results of audit observations

# Key Takeaways



In addition to overall risk rating of individual audit units, the following factors had a significant influence:

- industry trends,
- engagements suggested by leading practices,
- division management input,
- legislative interest and
- time since last review.

# Carried Over from FY18 Audit Plan



Function	Engagement
Group Benefits	HealthSelect Contract Administration
Investments	Investment Management Fees Real Assets - Infrastructure

# Proposed FY19 Internal Audit Plan



OPERATIONS	GROUP BENEFITS	INFORMATION SYSTEMS	INVESTMENTS
<ul style="list-style-type: none"><li>• Client Reconciliation</li><li>• Financial Opinion</li><li>• Incentive Compensation</li><li>• Temporary Workers Contract Management</li></ul>	<ul style="list-style-type: none"><li>• HealthSelect Financial Management</li></ul>	<ul style="list-style-type: none"><li>• Data Loss Prevention</li><li>• IT Governance</li></ul>	<ul style="list-style-type: none"><li>• Private Equity</li><li>• Profit Sharing</li></ul>



Questions?  
**Action Item**



## Public Agenda Item # 3.3

*Review of Internal Audit Administrative Items:  
Annual Internal Audit Independence Assessment*



August 29, 2018

Tony Chavez, Director of Internal Audit

# Audit Independence



Tony Chavez, Director of Internal Audit  
Beth Gilbert, Internal Auditor

# Background



- ERS Audit Charter states the Internal Audit director will report annually to the Board.
- 2016 peer review recommended formally documenting independence assessment.
- Audit standards: *Internal Auditor's International Professional Practices Framework (IPPF)* and *Government Auditing Standards Generally Accepted Auditing Standards (GAGAS)*
- Independence assessed by individual, organization and non-audit services performed.

# Assessing Independence



GAGAS conceptual framework for independence:

- A. Identify threats to independence.
- B. Evaluate the significance of the threats identified, both individually and in the aggregate.
- C. Apply safeguards as necessary to eliminate the threats or reduce them to an acceptable level.

# Independence Assessment



- Auditor Independence (Individual) – Staff free from impairments to independence
- Organizational Independence – Audit function is free from interference
- Non-Audit Services – Safeguards are in place to prevent non-audit services from impacting independence

Questions?



# Public Agenda Item # 4.1

## *Review of the Investment Compliance*



August 29, 2018

Tony Chavez, Director of Internal Audit  
Aaron Ismail, Investment Compliance Officer



# ERS Compliance Program Overview



## *Mission and Scope*

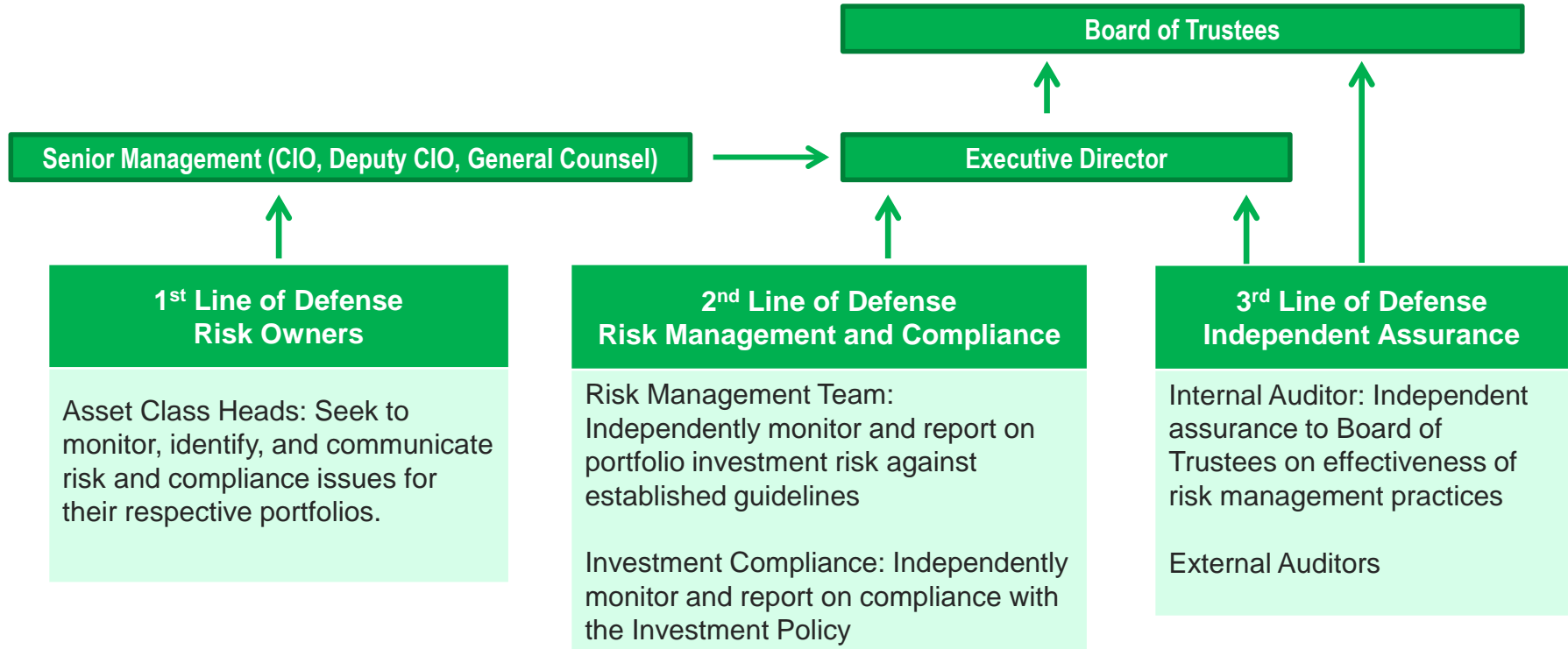
The ERS Investment Compliance Office's mission is to define and oversee a compliance program that:

- Prevents, detects and addresses issues of non-compliance.
- Helps ERS meet its fiduciary, regulatory and contractual obligations.
- Align policies and procedures with high ethical conduct.
- Effectively educates, trains and communicates the program to the organization and Board.

# ERS Compliance Program Overview



## Three Lines of Defense Model for Risk Governance



# ERS Compliance Program Overview



## *Implementation of an Effective Compliance Program*

- Emphasize the independence of the investment compliance function.
- Create a “Culture of Compliance”, including the Board and senior management, across groups and control functions.
- Develop procedures to effectively monitor, test and report compliance risks.
- Maintain a goal of being proactive, not reactive in addressing compliance issues.

# Engagement with the Board

## *Proposed Reporting and Communication*



- Compliance reports provided to the Board on a quarterly basis.
- Annual Compliance presentation to the Board starting March 2019, including:
  - Annual Compliance Review and Report
  - Discussion of compliance risks and material issues
  - Outline of compliance program roadmap for next period
- As necessary, periodic presentations on material compliance issues during the Board Audit Committee meeting.

# Quarterly Investment Compliance Report



The compliance report has been reformatted, but still includes reviews of personal trading, securities lending, portfolio compliance, and proxy voting.

Additional updates in the report may include:

- Internal Investment Committee approvals during the Period.
- Status of investments in prohibited countries (review or divestment).
- Other elements of the ERS compliance program as it evolves.

# Compliance Program Roadmap



## *Accomplishments*

- Fully transitioned ongoing compliance monitoring from Internal Audit to Investment Compliance.
- Reviewed and commented on current policies and procedures in connection with the Investment Policy Update (ongoing).
- Set up the My Compliance Office “MCO” system to automate personal trading information and streamline review processes.
- Collaborated with legal and investment operations to implement new procedures related to investments in prohibited countries.

# Compliance Program Roadmap

## *Near Term Goals*



- Develop a comprehensive Annual Compliance Report for the Board and Executive Director.
- Create a pro forma checklist for Alternative Investments in ACIC meetings.
- Work with the Investment Policy steering committee to ensure compliance issues are addressed.
- Evaluate the use of MCO to capture all employee compliance reporting.

# Compliance Program Roadmap



## *Long Term Goals*

- Consolidate current ERS Compliance and Ethics Policies and Procedures.
- Continue to develop compliance monitoring and testing frameworks across ERS.
- Become a primary resource for compliance related issues.
- Participate in periodic training for ERS staff and Board.
- Develop the ERS compliance “risk matrix.”



Questions?



# Public Agenda Item # 5.1

## *Executive Session –*

*In accordance with Section 551.089, Texas Government Code, the Audit Committee of the Board of Trustees, a committee of the whole of the Board will meet in executive session to discuss: (1) security assessments or deployments relating to information resources technology; (2) network security information as described by Section 2059.055(b); or (3) the deployment, or specific occasions for implementation, of security personnel, critical infrastructure, or security devices. Thereafter, the Board may consider appropriate action in open session.*



August 29, 2018

## Public Agenda Item # 6.1

### *Adjournment of the ERS Board of Trustees' Audit Committee Meeting*



August 29, 2018

## Public Agenda Item # 6.2

*Recess of the Board of Trustees -*

*Following a temporary recess, the Board of Trustees will reconvene with the Investment Advisory Committee to take up the following joint Board of Trustees and Investment Advisory Committee agenda items.*



August 29, 2018