



**Alameda County Employees' Retirement Association
BOARD OF RETIREMENT**

**AUDIT COMMITTEE/BOARD MEETING
NOTICE and AGENDA**

ACERA MISSION:

To provide ACERA members and employers with flexible, cost-effective, participant-oriented benefits through prudent investment management and superior member services.

Thursday, February 20, 2020
1:00 p.m.

LOCATION	COMMITTEE MEMBERS	
ACERA C.G. "BUD" QUIST BOARD ROOM 475 14TH STREET, 10TH FLOOR OAKLAND, CALIFORNIA 94612-1900 MAIN LINE: 510.628.3000 FAX: 510.268.9574	TARRELL GAMBLE, CHAIR	APPOINTED
	HENRY LEVY, VICE-CHAIR	EX-OFFICIO
	DALE AMARAL	ELECTED SAFETY
	OPHELIA BASGAL	APPOINTED
	KEITH CARSON	APPOINTED

Should a quorum of the Board attend this meeting, this meeting shall be deemed a joint meeting of the Board and Committee.

The order of agenda items is subject to change without notice. Board and Committee agendas and minutes are available online at www.acera.org.

Note regarding public comments: Public comments are limited to four (4) minutes per person in total.

Note regarding accommodations: The Board of Retirement will provide reasonable accommodations for persons with special needs of accessibility who plan to attend Board meetings. Please contact ACERA at (510) 628-3000 to arrange for accommodation.

AUDIT COMMITTEE/BOARD MEETING

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Call to Order: 1:00 p.m.

Public Comment:

Action Items: Matters for Discussion and Possible Motion by the Committee

External Audit:

- 1. Presentation, discussion, and possible motion to approve the external audit scope of work and timeline of services for the Financial Statements ended December 31, 2019, performed by Williams Adley & Co. LLP.**

- Audrey Elbert, Partner
- Kenneth Yu, Senior Manager
Williams, Adley & Company-CA, LLP
- Margo Allen

Recommendation:

The Audit Committee recommends to the Board of Retirement that the Board approve the external audit scope of work and timeline of services for the Financial Statements ended December 31, 2019, to be performed by Williams Adley & Co. LLP, .

Information Items: These items are not presented for Committee action but consist of status updates and cyclical reports

External Audit

- 1. 2020 Audit Committee Work Plan (Proposed)** - Margo Allen

Internal Audit

- 1. Review Completed Audits** - Harsh Jadhav
- 2. Review of Annual Risk Assessment** - Harsh Jadhav
- 3. Presentation of the 2020 Internal Audit Plan (Proposed)** - Harsh Jadhav
- 4. Enterprise Risk Management Presentation** - Margo Allen

Trustee Comment:

AUDIT COMMITTEE/BOARD MEETING

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Future Discussion Items

External Audit

1. Presentation and discussion of the GASB Statement No. 67 Valuation and addendums as of December 31, 2019 (Segal)
2. Presentation and discussion of the GASB Statement No. 74 Valuation and addendums as of December 31, 2019 (Segal)

Internal Audit


1. Progress report on the Internal Audit Plan
2. Review complete audits

Establishment of Next Meeting Date

April 16, 2020, at 1:00 pm



MEMORANDUM TO THE AUDIT COMMITTEE

DATE: February 20, 2020
TO: Members of the Audit Committee
FROM: Margo Allen, Fiscal Services Officer
SUBJECT: **Proposed 2020 Audit Committee Work Plan** 

The proposed 2020 Audit Committee Work Plan is attached for your consideration and review. The main action and topical discussion items for 2020 are listed below for quick reference:

- February 20 committee meeting: Williams, Adley & Co. will present the external audit scope of work and timeline;
- April 16 committee meeting: Presentation and discussion of the Government Accounting Standards Board (GASB) Statement No. 67 and No. 74 Valuations and addendums as of December 31, 2019 (Segal);
- May 21 committee meeting:
 - External auditor's report and presentation of the December 31, 2019 audited financial statements; and,
 - Recommend adoption of the GASB Statement No. 67 and No. 74 Valuations and addendums as of December 31, 2019;
- June 18 committee meeting:
 - Adoption of the audited Schedules of Employer Allocations and Schedules of Pension and OPEB Amounts by Employer; and
 - Presentation of the GASB Statement No. 68 and No. 75 Valuations and Employer Schedules as of December 31, 2019; and
- Throughout the year, ACERA's Chief Internal Auditor will review the progress on the internal audit plan, present new internal audit initiatives, and review completed audits.

As the need arises, agenda items may be changed or added to the work plan during the year. Your comments on the proposed 2020 work plan are welcomed.



ALAMEDA COUNTY EMPLOYEES' RETIREMENT ASSOCIATION

Audit and Communications Plan for the Year Ended
December 31, 2019



Confidence Earned

Agenda

- ▶ Engagement Team
- ▶ Auditor Responsibilities
- ▶ Management Responsibilities
- ▶ Audit Committee Responsibilities
- ▶ Our Risk-Based Approach
- ▶ Areas of Significant Risk
- ▶ Areas of Audit Emphasis
- ▶ Timeline
- ▶ New GASB Reporting Standards

Engagement Team

- ▶ Audrey F. Elbert, CPA, Engagement Partner
 - ▶ Has overall responsibility for the engagement, including service levels and adherence to timelines. Responsible for the engagement, including the content of reports and compliance with firm and professional standards.
- ▶ Kenneth Yu, CPA, Senior Manager
 - ▶ Primarily responsible for the achievement of engagement objectives and quality control of the audit procedures performed and the reports issued.
- ▶ Robert Griffin, CPA, Technical Review Partner
 - ▶ Primary responsibility is to provide an independent view of the engagement team's judgments related to auditing and technical accounting matters. He will also provide consultation on technical issues and serve as a liaison to GASB, AICPA, and other authoritative sources.

Auditor Responsibilities

- ▶ Our responsibility under U.S. Generally Accepted Auditing Standards and *Government Auditing Standards* is to express opinions about whether the financial statements prepared by management with your oversight are fairly presented, in all material respects, in conformity with U.S. GAAP. Provide an in-relation to opinion on the other supplementary information.
- ▶ Issue report on internal controls and compliance (no opinion) based on results of tests of compliance with certain provisions of laws, regulations, contracts and grants
- ▶ Perform an audit of the GASB 68 & GASB 75 schedules in accordance with GAAS.
- ▶ Express opinions on whether the GASB 68 & GASB 75 schedules are fairly presented in conformity with U.S. GAAP.
- ▶ Communicate significant matters related to the audits.

Management Responsibilities

- ▶ Prepare and present financial statements and supplementary information in conformity with U.S GAAP.
- ▶ Establish and maintain effective internal controls.
- ▶ Implement systems designed to achieve compliance with applicable laws, regulations, and contracts.
- ▶ Select and apply appropriate accounting principles.
- ▶ Comply with applicable laws and regulations and the provisions of contracts.
- ▶ Design and implement programs and controls to prevent and detect fraud, and inform us about all known or suspected fraud.
- ▶ Provide written representations.

Audit Committee Responsibilities

- ▶ Meet periodically with the auditors to discuss audit progress and findings.
- ▶ Resolve conflicts between auditors and management, if necessary.
- ▶ Review auditor's findings and recommendations and evaluate management's response.

Our Risk-Based Approach

- ▶ Audit planning is a continuous process. We use our most experienced team members to perform risk assessment procedures.
- ▶ External and internal risks are identified based on interviews, review of documentation (minutes, policies and procedures, IAD reports, etc.), results of internal control walkthroughs and testing, and institutional knowledge.
- ▶ We consider the effects of current risk factors on ACERA and emphasis is also placed on those areas requiring subjective judgment by management.
- ▶ Our approach to the internal control environment is to update our understanding of key controls annually, and perform testing on a rotational basis over a three year cycle.
- ▶ Our audit procedures emphasize testing areas with the highest risk of material misstatement, i.e., those accounts or transactions where we believe there is the greatest risk of material misstatement to the financial statements, whether due to error or fraud.
- ▶ Our reporting objective focuses on the fairness of presentation of the financial statements and schedules and the clarity and accuracy of related disclosures.

Areas of Significant Risk

Additions (Revenue)	Management Override of Controls	Investments
<p><u>Risks</u></p> <ul style="list-style-type: none"> ▪ Contributions are misstated. ▪ Investment income, including appreciation, is misstated. 	<p><u>Risks</u></p> <ul style="list-style-type: none"> ▪ Financial statements could be materially misstated. ▪ Misappropriation of assets. 	<p><u>Risks</u></p> <ul style="list-style-type: none"> ▪ Over-statement of account balances. ▪ Valuations not reported using proper methodology. ▪ Transactions reported in incorrect period. ▪ Assets not held in ACERA's name.
<p><u>Audit Response</u></p> <ul style="list-style-type: none"> ▪ Confirm with employers the amount of contributions and related receivables. ▪ Confirm investment valuation and perform analytical procedures. 	<p><u>Audit Response</u></p> <ul style="list-style-type: none"> ▪ Evaluate and update our understanding of controls over the financial reporting process. ▪ Select a sample of transactions and test to see if controls are operating effectively. 	<p><u>Audit Response</u></p> <ul style="list-style-type: none"> ▪ Independent confirmation and reconciliation testing. ▪ Review of third party valuations and market quotes.

Other Areas of Audit Emphasis

- ▶ In addition to significant risks identified previously, we have identified areas below as areas of focus during the audit due to materiality of the balance and/or complexity/judgment involved in the accounting.
 - ▶ Participant data and actuarial information
 - ▶ Benefit payments
 - ▶ Reserves
 - ▶ Cash activity
 - ▶ Presentation and disclosure of the financial statements
 - ▶ Accounting and reporting for actuarially determined estimates

Timeline

- ▶ Planning and client assistance - January / February 2020
- ▶ Fieldwork - Mid February - April 2020
- ▶ Presentation of Audit Results to Audit Committee - May 2020
- ▶ Reporting Deadlines
 - ▶ State Controller's Report - June 30, 2020
 - ▶ CAFR to GFOA - June 30, 2020
- ▶ Management Letter Comments - June 2020
- ▶ GASB 68 & 75 reports - June 2020

New GASB Reporting Standards

New pronouncements for 2019


- ▶ **Statement No. 91 - *Conduit Debt Obligations***
 - ▶ This does not effect ACERA.



MEMORANDUM TO THE AUDIT COMMITTEE

DATE: February 20, 2020

TO: Members of the Audit Committee

FROM: Margo Allen, Fiscal Services Officer 

SUBJECT: **Williams, Adley & Co., 2019 Financial Statement External Audit**

The Fiscal Services Department has reviewed the 2020 external audit scope of work and timeline of services to be performed by Williams, Adley, & Co. ACERA is prepared to commence with its annual financial statement audit for year ended December 31, 2019. The allotted time frame of the audit field work is approximately 60 days, ending April 18, 2020.

Throughout the audit period, bi-weekly status meetings with the Fiscal Services Department will be conducted. Likewise, status meetings with Senior Managers will also be scheduled on an as needed basis. The Fiscal Services Officer will oversee the audit process and is responsible for ensuring the completeness and accuracy of all financial information provided to Williams, Adley, & Co.

Recommendation

Staff recommends that the Audit Committee recommend to the Board of Retirement that the Board approve the 2019 Financial Statement External Audit Scope of Work and Timeline of Services to be performed by Williams, Adley & Co. LLP



2020 Audit Committee Work Plan (Proposed)

Action Items	Information Items	Staff Items
<p>Feb 20 – 1:00 PM (3rd Thurs, same day as Board Meeting)</p>	<p><i>External Audit</i></p> <ul style="list-style-type: none"> • Presentation, discussion, and possible motion to approve the external audit scope of work and timeline of services for the Financial Statements ended December 31, 2019, performed by the external audit firm 	<p><i>External Audit</i></p> <ul style="list-style-type: none"> • Audit Committee Work Plan (Proposed) • <i>Internal Audit</i> • Review of Annual Risk Assessment • Presentation of the 2020 <i>Internal Audit</i> • Review completed audits • Enterprise Risk Management Presentation
<p>Apr 16 – 1:00 PM (3rd Thurs, same day as Board Meeting)</p>	<p><i>External Audit</i></p> <ul style="list-style-type: none"> • None. <p><i>Internal Audit</i></p> <ul style="list-style-type: none"> • None 	<p><i>External Audit</i></p> <ul style="list-style-type: none"> • Presentation and discussion of the GASB Statement No. 67 Valuation and addendums as of December 31, 2019 (Segal) • Presentation and discussion of the GASB Statement No. 74 Valuation and addendums as of December 31, 2019 (Segal) <p><i>Internal Audit</i></p> <ul style="list-style-type: none"> • Progress report on the Internal Audit Plan • Review complete audits

Note: This work plan is subject to change without prior notice. Periodic rearrangements of agenda items will be made to the work plan to provide a reasonable length of time for each meeting.



2020 Audit Committee Work Plan (Proposed)

	Action Items	Information Items	Staff Items
<p>May 21 – 1:00 PM (3rd Thurs, same day as Board Meeting)</p>	<p><i>External Audit</i></p> <ul style="list-style-type: none"> • Discussion and possible motion to recommend approval of the December 31, 2019 Audited Financial Statements and Independent Auditor’s Report • Discussion and possible motion to recommend adoption of the Government Accounting Standards Board (GASB) Statement No. 67 Actuarial Valuation and addendum as of December 31, 2019 • Discussion and possible motion to recommend adoption of the Government Accounting Standards Board (GASB) Statement No. 74 Actuarial Valuation and addendum as of December 31, 2019 <p><i>Internal Audit</i></p> <ul style="list-style-type: none"> • None 	<p><i>External Audit</i></p> <p><i>Internal Audit</i></p> <ul style="list-style-type: none"> • Progress Report on the Internal Audit Plan • Review completed audits • ERM Risk Universe Presentation 	

Note: This work plan is subject to change without prior notice. Periodic rearrangements of agenda items will be made to the work plan to provide a reasonable length of time for each meeting.



2020 Audit Committee Work Plan (Proposed)

Action Items	Information Items	Staff Items
<p>Jun 17 – 1:00 PM (3rd Thurs, same day as Board Meeting)</p>	<p><i>External Audit</i></p> <ul style="list-style-type: none"> • Discussion and possible motion to adopt the audited Schedules of Employer Allocations and Schedules of Pension Amounts by Employer with Related Notes, <i>based on the Addendum to GASB Statement No. 67 Valuation as of December 31, 2019</i> • Discussion and possible motion to adopt the audited Schedules of Employer Allocations and Schedules of OPEB Amounts by Employer with Related Notes, <i>based on the Addendum to GASB Statement No. 74 Valuation as of December 31, 2019</i> <p><i>Internal Audit</i></p> <ul style="list-style-type: none"> • None 	<p><i>External Audit</i></p> <ul style="list-style-type: none"> • Presentation of the 2019 Auditor’s Observations and Recommendations (if any) • Recommendation to receive and file the Observations and Recommendations from WACO (if any) • Presentation and discussion of the GASB Statement No. 68 Valuation and Employer Schedules as of December 31, 2019 • Presentation and discussion of the GASB Statement No. 75 Valuation and Employer Schedules as of December 31, 2019 <p><i>Internal Audit</i></p> <ul style="list-style-type: none"> • Progress Report on the Internal Audit Plan • Review completed audits
<p>Oct 15 - 1:00 PM (3rd Thurs, same day as Board Meeting)</p>	<p><i>External Audit</i></p> <ul style="list-style-type: none"> • None <p><i>Internal Audit</i></p> <ul style="list-style-type: none"> • None 	<p><i>External Audit</i></p> <p><i>Internal Audit</i></p> <ul style="list-style-type: none"> • Progress Report on the Internal Audit Plan • Review completed audits • ERM Presentation

Note: This work plan is subject to change without prior notice. Periodic rearrangements of agenda items will be made to the work plan to provide a reasonable length of time for each meeting.



MEMORANDUM TO THE AUDIT COMMITTEE

DATE: February 20, 2019

TO: Members of the Audit Committee

FROM: Harsh Jadhav, Chief of Internal Audit

SUBJECT: 2020 Internal Audit Program

Executive Summary

The Audit Committee Meeting in February 2020 will feature the proposed 2020 Internal Audit Program, discussion regarding the updated risk assessment process, and a presentation of the completed Superior Courts Employer Audit.

The annual risk assessment is complete. The Internal Audit Department has reassessed the internal controls and risks identified by management to determine how changes in business processes, laws, and regulations, pension practices, or the organizational structure have affected the risk ranking for 2020. Based on the results of the risk assessment, the Internal Audit Department has planned to conduct four internal audits, two policy audits, complete the Alameda Health System (AHS), and Superior Courts Employer Audits, implement three special projects, and continue to provide staff training on fraud.

Key objectives for this year will be to work with management and the trustees to review the benefits of implementing an agency-wide enterprise risk management process to understand and address entity-level risk. Evaluating entity-level risks is a crucial driver to ensure that the strategic objectives of an organization are attained. In addition, we are exploring the opportunity to develop an Internal Audit Internship Program. Internship programs are an effective method to introduce talented business students to career opportunities in a government setting. Finally, the Internal Audit Department will be working closely with PRISM to conduct a Cybersecurity and Data Security Self-Assessment. Performing a self-assessment of the incident response procedures, security management process, IT infrastructure, and cybersecurity training allows the agency to uncover gaps, potential weaknesses, and threats that could undermine the security of sensitive information (i.e., member records, medical data, and bank account information).

The Internal Audit Department completed the last year of the participating employer audit cycle. We are pleased to report that we have completed the Alameda Health System Employer Audit, which was the last employer audit in the first audit cycle. We are waiting for the new Chief Counsel to arrive to discuss the audit results and ensure we interpreted the PEPRAs accurately. The next step will be to review the results with the employer and close the audit out.

Proposed 2020 Audit Plan

Internal Audit Program (2020)	Service Line	Assigned	Status	Q1	Q2	Q3	Q4
Retiree Payroll Deduction Policy Audit	Policy Audit	Lyndon	Started				
Felony Forfeiture Policy Audit	Policy Audit	Caxton	Started				
Member Identity Theft Audit	Internal Audit	Lyndon	Not Started				
Cash Management (Positive Pay) Audit	Internal Audit	Caxton	Not Started				
Final Year Salary Calculation Audit	Internal Audit	Lyndon/Caxton	Not Started				
Cybersecurity Incident Response Review	Internal Audit	Harsh	Not Started				
Employer Audit Testing/Report - Alameda Health System	Employer Audit	Caxton	In Progress				
Employer Audit Testing/Report - Superior Courts	Employer Audit	Caxton	Complete				
2020 Annual Internal Audit Risk Assessment	Administration	Harsh	Complete				
2021 Annual Internal Audit Risk Assessment	Administration	Harsh	Not Started				
Fraud Hotline Management	Administration	Lyndon	In Progress				
Fraud Training	Administration	Lyndon/Caxton	Not Started				
Enterprise Risk Assessment	Special Project	Margo/Harsh	Started				
Cybersecurity and Data Security Self-Assessment	Special Project	Vijay/Harsh	Not Started				
Internal Audit Internship Program	Special Project	Vicki/Harsh	Not Started				

Proposed 2019 Internal Audit Program

Policy Audits

Audit - Retiree Payroll Deduction Policy

The purpose of this audit is to review compliance with the ACERA Retiree Payroll Deduction Policy. This policy provides guidance in the administration of pension benefits by listing approved benefit deductions and prohibiting the assignment of benefits for any purpose other than those authorized by statute.

Audit - Felony Forfeiture Policy

The purpose of the audit is to review compliance with the ACERA Felony Forfeiture Policy. This policy provides guidance on how participating employers handle felony forfeitures of retirement benefits. The Public Employees' Pension Reform Act of 2013 ("PEPRA") added two forfeiture statutes applicable to all public employees convicted of felonies on or after January 1, 2013. The audit also examines participating employer compliance by selecting a sample of employers to determine if the employer implemented procedures to report felony forfeitures to ACERA.

Internal Audits

Audit – Prevent Member Identity Theft

The purpose of this audit is to examine how to strengthen internal fraud controls to prevent third parties from making unauthorized changes to member accounts and banking information. The examination will review the business process and explore technology solutions to enhance identity management controls.

Audit – Cash Management (Positive Pay)

The purpose of the audit is to identify internal control weaknesses and recommend strategies to improve cash management. The Positive Pay process is a bank control that systematically compares checks presented for payment to the issued-check files to detect serial numbers and dollar amounts that don't match. This audit will review the payee validation process to ensure ACERA has implemented the necessary internal controls to safeguard against fraud.

Audit – Final Pensionable Salary Calculation

The purpose of the audit is to sample retired members to verify if the final pensionable salary calculation was accurate. The amount of final pensionable salary depends on member type and membership tier and is a function of the highest salary earned over the qualifying period (i.e., highest salary earned over 36 months for Tier II General Members).

Audit – Cybersecurity Incident Response Review

The purpose of this audit is to test ACERA's organization-wide cybersecurity incident response plan. ACERA has implemented the CIS control framework, which includes basic, foundational, and organizational controls that collectively form a defense-in-depth set of best practices that mitigate the most common attacks against systems and networks. This audit would examine whether the incident response plans in place would allow the business to recover critical functions within an acceptable time frame adequately.

Employer Audits

Audit – PEPRA Employer Audit of Alameda Health System

The employer audit of the Alameda Health System will assess the participating employer's compliance with state laws, rules, regulations and administrative policies regarding the enrollment of members, reporting of member data, and the reporting and remittance of employer contributions in accordance with the Public Employees' Pension Reform Act of 2013.

Audit – PEPRA Employer Audit of Superior Courts of California

The employer audit of Superior Courts of California will assess the participating employer's compliance with state laws, rules, regulations and administrative policies regarding the enrollment of members, reporting of member data, and the reporting and remittance of employer contributions in accordance with the Public Employees' Pension Reform Act of 2013.

Special Projects

Special Project - Enterprise Risk Assessment

The objective of this special project will be for the Internal Audit Department to support the business with technical guidance on risk and internal controls as the leadership roles out the enterprise risk assessment process to the organization.

Special Project - Cybersecurity and Data Security Self-Assessment

The objective of this special project will be to work with the PRISM Department to determine if adequate firewall, access controls, employee training, and processes for incident response, business recovery, and threat analysis are in place to ensure sensitive organizational data and member data are protected and secure.

Special Project - Internal Audit Internship Program

The objective of this special project will be to establish an internship program. An internship program would allow the department to hire a student to work on audits during the summer. We expect that the student will gain valuable audit experience through their application of audit knowledge learned in the classroom. In addition, we hope to increase the awareness of challenging opportunities and a career path in local government.

Summary

The Proposed 2020 Audit Program includes four internal audits, two employer audits, two policy audits, and three special projects. Similar to the previous year, the proposed audits cover a cross-section of departments and risks. Last year, we successfully completed our sixth year of employer audits and several challenging internal and compliance audits. I want to acknowledge my staff for doing excellent work in 2019. I have full confidence that 2020 will be no different, and the Internal Audit Staff will continue to a great job partnering with management, servicing the Board of Retirement, and protecting our members.



**Alameda County Employees' Retirement Association
Internal Audit Department**



Internal Audit Department 2020 Internal Audit Plan

February 20, 2020

Agenda

1. Results of the Superior Courts
Employer Audit
2. Annual Risk Assessment Process
3. Proposed Internal Audit Plan – 2020

SUPERIOR COURT OF CALIFORNIA EMPLOYER AUDIT



Audit Objective and Scope of Work

Eligibility

- 1) Determined if the Superior Court of California was submitting enrollment forms for employees eligible to be covered under ACERA's defined benefit plan.
- 2) Determined if ineligible employees were being reported as eligible to participate in ACERA's defined benefit plan.

Eligible Compensation

- 1) Determined if the Superior Court of California was reporting the correct pensionable compensation to ACERA.
- 2) Scanned for unusual items included in the payroll reports/transmittal files to ACERA.
- 3) Determined if pensionable pay codes were applied correctly in the employer's payroll system.
- 4) Determined if the employer complied with the PEPRA's pensionable compensation limits for new employees hired after January 1, 2013.
- 5) Determined if the employer complied with the pensionable compensation limits specified in Section 401(a)(17) of Title 26 of the United States Code.

Conclusion

We found the Superior Court's payroll data, payroll process, and other reporting requirements were in compliance with PEPRA and/or the CERL as added, impacted or amended by PEPRA. Please note that we limited this review to the areas specified in the scope section of this report.

We would like to recognize the Superior Court's leadership team (**Glenys Rogers and Melanie Lewis**) and their staff for their excellent cooperation throughout this audit process.

Annual Internal Audit Risk Assessment Process

1. Reviewed the strategic objectives of each department and current and potential risks the departments were concerned about. Risks covered benefits, fiscal operations, investments, legal, IT, actuarial and human resources.
2. Discussed potential control weaknesses, new business processes introduced in the current year, staffing changes, and new legislative mandates which may impact the current business.
3. Reviewed potential cybersecurity risks related to privacy and data security.
4. Considered risks for fraud and compliance issues.
5. We summarized the key risks from each department to help prioritize our audit effort and develop the Internal Audit Plan for 2020.

Identified Internal Audit Risks

- Employee Turnover and Training
- Entity-Level Risk Management
- Policy Compliance

- Project Risk – PAS, ONBASE
- Cybersecurity
- Social Engineering Attacks

Operations

Technology

Benefits

Investments

- Member Identity
- Theft
- Overpayments (i.e., death, retirement, etc.)

- Cash Management
- Economic Risk

Proposed 2020 Internal Audit Plan

Internal Audit Program (2020)	Service Line	Assigned	Status	Q1	Q2	Q3	Q4
Retiree Payroll Deduction Policy Audit	Policy Audit	Lyndon	Started				
Felony Forfeiture Policy Audit	Policy Audit	Caxton	Started				
Member Identity Theft Audit	Internal Audit	Lyndon	Not Started				
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Cybersecurity Incident Response Review	Internal Audit	Harsh	Not Started				
Employer Audit Testing/Report - Alameda Health System	Employer Audit	Caxton	In Progress				
Employer Audit Testing/Report - Superior Courts	Employer Audit	Caxton	Complete				
2020 Annual Internal Audit Risk Assessment	Administration	Harsh	Complete				
2021 Annual Internal Audit Risk Assessment	Administration	Harsh	Not Started				
Fraud Hotline Management	Administration	Lyndon	In Progress				
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Enterprise Risk Assessment	Special Project	Margo/Harsh	Started				
Cybersecurity and Data Security Self-Assessment	Special Project	Vijay/Harsh	Not Started				
Internal Audit Internship Program	Special Project	Vicki/Harsh	Not Started				

What's missing.....is
Enterprise Risk
Management (ERM).





MEMORANDUM TO THE AUDIT COMMITTEE

DATE: February 20, 2020

TO: Members of the Audit Committee

FROM: Harsh Jadhav, Chief of Internal Audit

SUBJECT: Results of the Superior Courts Employer PEPRA Audit

Executive Summary

Pursuant to Government Code Sections 31542.5, 31543, 7522.40 – 7522.74, the Board of Retirement (“Board”) may audit the participating employer to determine the correctness of contributions, retirement benefits, reportable compensation, enrollment and reinstatement in the retirement system, post-retirement employment, and certain reported felony convictions. This audit is to determine if the employer’s payroll data and payroll processes comply with applicable Public Employees’ Pension Reform Act (PEPRA) and the County Employee Retirement Law of 1937 (CERL) as added, impacted or amended by PEPRA.

Audit Objective

The objective of this compliance audit was to determine if the employer’s payroll data, payroll process, and other reporting requirements comply with PEPRA and the CERL as added, impacted, or amended by PEPRA. To accomplish the audit objective, a review of applicable PEPRA legislation, applicable ACERA Policy, and the CERL as added, impacted, or amended by PEPRA was conducted. In addition, the participating employer’s documents and procedures were examined, and key personnel from the employing agencies were interviewed to gain an understanding of the employer’s business process and practices.

Audit Scope

With the Board of Retirement’s approval, the Internal Audit Department engaged with the participating employer to perform a limited scope audit related to compliance with PEPRA and ACERA polices. After reviewing the employer’s completed risk assessment matrix and after interviewing the employer’s management team, we were able to understand the control environment and identify the highest risk areas and subsequently used this information to determine the scope for the audit.

We primarily audited the employer’s payroll and enrollment data ranging from January 1, 2017, to June 30, 2018. In addition, a sample of compensation records for dates prior to January 1, 2017, was selected to test compliance with PEPRA Section 7522.32, which requires retirement benefits to be determined using the highest average annual pensionable compensation earned by the member during a period of at least 36 consecutive months.

We reviewed the Superior Court of California's payroll reporting for both full-time and part-time employees, job classification codes, and the pay rate schedules. In addition, we sampled individual payroll records against ACERA's Pension Gold Database (PG) records to identify variances in reported pensionable pay.

We performed audit testing of key controls in the following identified risk areas:

Eligibility:

- 1) Determined if the Superior Court of California was submitting enrollment forms for employees eligible to be covered under ACERA's defined benefit plan.
- 2) Determined if ineligible employees were being reported as eligible to participate in ACERA's defined benefit plan.

Eligible Compensation:

- 1) Determined if the Superior Court of California was reporting the correct pensionable compensation to ACERA.
- 2) Scanned for unusual items included in the payroll reports/transmittal files to ACERA.
- 3) Determined if pensionable pay codes were applied correctly in the employer's payroll system.
- 4) Determined if the employer complied with the PEPRA's pensionable compensation limits for new employees hired after January 1, 2013.
- 5) Determined if the employer complied with the pensionable compensation limits specified in Section 401(a)(17) of Title 26 of the United States Code

Conclusion

In conclusion, we found the employer's payroll data, payroll process, and other reporting requirements were effective, and in compliance with PEPRA and the CERL as added, impacted, or amended by PEPRA. Please note that we limited this review to the areas specified in the scope section of this report. We want to thank the Superior Court of California's management team and staff for their cooperation throughout the audit process.

Based on our audit results, we made the following key recommendation to strengthen the employer's internal controls and make the business process, as it relates to meeting the PEPRA requirements, more effective:

1. We recommend that the employer strengthen the bi-weekly review process on vacation sell activities.

Any findings, recommendations, and conclusions outlined in the audit report were based on information made available or otherwise obtained at the time this report was prepared.



Alameda County Employees' Retirement Association
Internal Audit Department

The Superior Court of California the County of Alameda

**AUDIT TO VERIFY COMPLIANCE WITH THE PUBLIC EMPLOYEES'
PENSION REFORM ACT (PEPRA) AND ACERA POLICY**



**REPORT PREPARED FOR:
ACERA BOARD OF RETIREMENT**

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CONTROL SUMMARY

KEY CONTROLS

#	Control	Risk Level	Effectiveness
1	ACERA Membership Eligibility and Enrollment: This control is used to validate whether the participating employer properly enrolls eligible employees into ACERA's pension plan and whether new employees submit the required membership enrollment forms to ACERA.	High	Effective
2	Eligible Compensation: This control is used to verify if the employer is reporting the correct pensionable compensation to ACERA, and if the employer complies with PEPRA's pensionable compensation limits for new employees hired after January 1, 2013. It will also provide reasonable assurance that the employer complies with the pensionable compensation limits specified in Section 401(a) (17) of Title 26 of the United States Code.	High	Effective

RISK LEVEL

High-Risk Controls:

Controls associated with critical processes within an organization. Typically they are related to overall monitoring controls or valued in key or numerous processes. They can be controls that had significant findings in previous years. A high-risk control failing could result in a material weakness. Material weakness includes material misstatements in the financial statements, significant process errors and misuse of ACERA resources.

Medium-Risk Controls:

Controls associated with important processes within an organization, where a deficiency in the control could cause financial loss or breakdown in process, but in most cases, do not lead to a critical systemic failure. Typically, these controls had minimal or no findings in previous years, but are integral to the process and necessary to test on a regular basis. A medium-risk control failing could result in a significant deficiency, and in some instances, a material weakness. Significant deficiencies can include staff competency, lack of consistent business process and poor utilization of ACERA resources.

Low-Risk Controls:

Controls associated with process optimization and non-critical processes. Typically they represent controls that did not have findings in the previous year's testing and have not changed in how they operate or in the personnel performing the controls. Low-risk controls are inherent in the current control environment but are unlikely to cause a material misstatement, unless there is a failure of several low-risk controls within the same process.

CONTROL EFFECTIVENESS

Effective:

The control is fully operating as designed.

Partially Effective:

The control is operating as designed with the modification necessary due to a change in business process, change in personnel, inadequate documentation, the control has not been fully implemented, or the control requires additional enhancements to be effective. Often new controls will fall in this category.

Improvement Opportunity:

The control is only marginally effective and should be redesigned or implemented. Typically these controls require review due to an ineffective design, which will prevent the control from detecting control risk.

Ineffective:

The control is not operating as designed and could lead to a significant risk to the organization, if not remediated.

Remediated/In Remediation:

The control was previously ineffective, partially effective, or an improvement opportunity. A remediation plan is in place to correct the deficiency. Note that reliance can be placed on the remediated control, once retested by internal audit, which typically occurs in the following audit cycle.

EXECUTIVE SUMMARY

Pursuant to Government Code Sections 31542.5, 31543, 7522.40 – 7522.74, the Board of Retirement (“Board”) may audit the participating employer to determine the correctness of contributions, retirement benefits, reportable compensation, enrollment and reinstatement in the retirement system, post-retirement employment, and certain reported felony convictions. This audit is to determine if the employer’s payroll data and payroll processes comply with applicable Public Employees’ Pension Reform Act (PEPRA) and the County Employee Retirement Law of 1937 (CERL) as added, impacted or amended by PEPRA. On October 18, 2018, the Board approved the proposed audit plan for the employer audit of the Superior Court of California for the County of Alameda (Court) for the year 2019.

AUDIT OBJECTIVE

The objective of this compliance audit is to determine if the employer’s payroll data, payroll process, and other reporting requirements comply with PEPRA and the CERL as added, impacted, or amended by PEPRA. To accomplish the audit objective, a review of applicable PEPRA legislation, applicable ACERA Policy, and the CERL as added, impacted, or amended by PEPRA was conducted. In addition, the participating employer’s documents and procedures were examined, and key personnel from the employing agencies were interviewed to gain an understanding of the employer’s business process and practices.

SCOPE AND STRATEGY

With the Board of Retirement’s approval, the Internal Audit Department engaged with the participating employer to perform a limited scope audit related to compliance with PEPRA and ACERA polices. After reviewing the employer’s completed risk assessment matrix and after interviewing the employer’s management team, we were able to understand the control environment and identify the highest risk areas and subsequently used this information to determine the scope for the audit.

We primarily audited the employer’s payroll and enrollment data ranging from January 1, 2017, to June 30, 2018. In addition, a sample of compensation records for dates prior to January 1, 2017 were selected to test compliance with PEPRA Section 7522.32, which requires retirement benefits to be determined using the highest average annual pensionable compensation earned by the member during a period of at least 36 consecutive months.

We reviewed the Superior Court of California’s payroll reporting for both full-time and part-time employees, job classification codes, and the pay rate schedules. In addition, we sampled individual payroll records against ACERA’s Pension Gold Database (PG) records to identify variances in reported pensionable pay.

We performed audit testing of key controls in the following identified risk areas:

Eligibility

- 1) Determined if the Superior Court of California was submitting enrollment forms for employees eligible to be covered under ACERA's defined benefit plan.
- 2) Determined if ineligible employees were being reported as eligible to participate in ACERA's defined benefit plan.

Eligible Compensation

- 1) Determined if the Superior Court of California was reporting the correct pensionable compensation to ACERA.
- 2) Scanned for unusual items included in the payroll reports/transmittal files to ACERA.
- 3) Determined if pensionable pay codes were applied correctly in the employer's payroll system.
- 4) Determined if the employer complied with the PEPRA's pensionable compensation limits for new employees hired after January 1, 2013.
- 5) Determined if the employer complied with the pensionable compensation limits specified in Section 401(a)(17) of Title 26 of the United States Code.

AUDIT LIMITATIONS

The PEPRA regulations are mostly untested, which made the interpretation of certain statutes difficult. To mitigate this ambiguity, we solicited the assistance of ACERA's Legal and Benefits Departments to provide guidance on the intent and application of specific legislation. In addition, due to certain resource constraints, the employer audits were limited in scope to focus on the highest risk areas, which may not represent a comprehensive review of all high-risk areas.

Further, to be efficient in the audit testing, we sampled records, which we believed represented the population. Whenever a sampling approach is used, a sampling risk arises from the possibility that the conclusions that the auditor draws from testing the sample may be different from the conclusions that they would draw if the entire population had been tested. Finally please note that the primary purpose of this audit was not intended to detect payroll fraud, non-compliance with federal or state statutes or other compliance issues outside the scope of this audit. Sometimes during the course of an audit, new information is uncovered or a new risk is identified, which could change our audit strategy, including potentially expanding the audit scope.

INSTITUTE OF INTERNAL AUDITORS (IIA) AUDIT GUIDANCE AND STANDARDS

Internal auditing is conducted in diverse legal and cultural environments; within organizations that vary in purpose, size, complexity, and structure; and by persons within or outside the organization. While differences may affect the practice of internal auditing in each environment, conformance with The IIA's *International Standards for the Professional Practice of Internal Auditing (Standards)* is essential in meeting the responsibilities of internal auditors and the internal audit activity. If internal auditors or the internal audit activity is prohibited by law or regulation from conformance with certain parts of the *Standards*, conformance with all other parts of the *Standards* and appropriate disclosures are needed.

If the *Standards* are used in conjunction with standards issued by other authoritative bodies, internal audit communications may also cite the use of other standards, as appropriate. In such a case, if inconsistencies exist between the *Standards* and other standards, internal auditors and the internal audit activity must conform to the *Standards* and may conform with the other standards if they are more restrictive.

The purpose of the *Standards* is to:

- (1) Delineate basic principles that represent the practice of internal auditing.
- (2) Provide a framework for performing and promoting a broad range of value-added internal auditing.
- (3) Establish the basis for the evaluation of internal audit performance.
- (4) Foster improved organizational processes and operations.

The *Standards* are principles-focused, mandatory requirements consisting of:

- (1) Statements of basic requirements for the professional practice of internal auditing and for evaluating the effectiveness of performance, which are internationally applicable at organizational and individual levels.
- (2) Interpretations, which clarify terms or concepts within the Statements. The Standards employ terms that are specific. Specifically, the Standards use the word "must" to specify an unconditional requirement and the word "should" where conformance is expected unless, when applying professional judgment, circumstances justify deviation. It is necessary to consider the Statements and their Interpretations as well as the specific meanings from the Glossary to understand and apply the Standards correctly.
- (3) The structure of the *Standards* is divided between Attribute and Performance Standards. Attribute Standards address the attributes of organizations and individuals performing internal auditing. The Performance Standards describe the nature of internal auditing and provide quality criteria against which the performance of these services can be measured. The Attribute and Performance Standards are also provided to apply to all internal audit services.

Assurance services involve the internal auditor's objective assessment of evidence to provide an independent opinion or conclusions regarding an entity, operation, function, process, system, or other subject matter. The nature and scope of the assurance engagement are determined by the internal auditor. There are generally three parties involved in assurance services:

- (1) The person or group directly involved with the entity, operation, function, process, system, or other subject-matter - the process owner
- (2) The person or group making the assessment - the internal auditor
- (3) The person or group using the assessment - the user.

Consulting services are advisory in nature, and are generally performed at the specific request of an engagement client. The nature and scope of the consulting engagement are subject to agreement with the engagement client. Consulting services generally involve two parties:

- (1) The person or group offering the advice - the internal auditor
- (2) The person or group seeking and receiving the advice - the engagement client.

Consulting services are advisory in nature, and are generally performed at the specific request of an engagement client. The nature and scope of the consulting engagement are subject to

agreement with the engagement client. Finally, the Internal Audit Department personnel are not trained or qualified to offer recommendations on legal, actuarial, or investment matters. Any questions on these issues should be directed to the appropriate ACERA Department or qualified consultant. Hence, no part of the Internal Audit Report should be construed as legal, actuarial, or investment advice.

CONTROLS TESTED

CONTROL 1 – ACERA MEMBERSHIP ELIGIBILITY AND ENROLLMENT

Risk Level - High

Audit Results – Effective

Control:

The participating employer is required to enroll employees who are eligible to receive retirement benefits from ACERA, and also submit a new member's payroll record and retirement contribution to ACERA in a timely manner. This control is used to validate whether the participating employer properly enrolls eligible employees into ACERA's pension plan and whether new employees submit the required membership enrollment forms to ACERA.

Risk:

The risk that the participating employer may not correctly enroll eligible employees into ACERA's pension plan or incorrectly enroll non-eligible employees. Moreover, PEPRA sections 7522.02 and 7522.04 require employees hired on or after January 1, 2013, to be enrolled in a new tier plan unless the employee meets an exception stated in PEPRA.

TEST 1: EMPLOYEES HIRED FOR A RETIREMENT BENEFITS-ELIGIBLE POSITION WERE PROPERLY ENROLLED INTO ACERA'S PENSION PLAN

We examined the original payroll registers from the employer, which included the population of all employees for a specific pay period, regardless of employment type (full-time or part-time) or whether the employee was eligible for retirement benefits.

We then sampled if the Superior Court of California correctly enrolled and reported employees who have a job classification eligible for retirement benefits in the transmittal files submitted to ACERA.

Test Results:



No exceptions noted.

TEST 2: CONFIRM NEW EMPLOYEES HIRED IN THE YEAR 2013 WERE BEING ENROLLED IN THE NEW TIER IV PLAN AND NEW MEMBER ENROLLMENT QUESTIONNAIRES WERE RECEIVED BY ACERA

Employees hired on and after January 1, 2013, should be enrolled in the new Tier IV retirement plan in accordance with PEPRA Section 7522.10. We sampled new employees hired between the year 2013 and year 2018 for testing to verify the retirement plan tier for which they were enrolled. We also confirmed if the Member Enrollment Questionnaire was received by ACERA.

Our testing confirmed that the sample of new employees who were hired by the Superior Court of California after January 1, 2013, confirmed employees selected in the sample were properly enrolled in the new Tier IV plan. We also confirmed that for the employees selected in our sample, the Member Enrollment Questionnaire forms were received by ACERA and stored in ACERA's Electronic Data Management System (EDMS).

Test Results:



No exceptions noted.

CONTROL 2 - ELIGIBLE PENSIONABLE COMPENSATION

Risk Level - High

Audit Results – Partially Effective

Control:

This control examines the accuracy of the employer's reporting of pensionable wages to ACERA, including observing the PEPRA compensation limits and the IRS code Section 401(a)(17) compensation limit. It included an examination of the employer's original payroll registers, ACERA PG records, and the employer's data in their payroll system.

Risk:

The risk that certain pay items reported to ACERA as pensionable compensation are "Non-Pensionable Compensation." There is also a risk that employer may report inaccurate pensionable wages to ACERA.

A risk also exists that the employer can be out of compliance if their employees receive pensionable compensation, which exceeds the compensation limits described in PEPRA Section 7522.10 for employees hired on or after January 1, 2013.

In addition to the new PEPRA compensation limits, PEPRA Section 7522.42 reiterates the existing pensionable compensation limit for all members hired on or after July 1, 1996, as prescribed under the IRS Code Section 401(a)(17) of Title 26 of the United States Code.

TEST 1: VERIFY THAT THE EMPLOYER REPORTED PENSIONABLE PAY CODES CORRECTLY TO ACERA

We sampled payroll data to examine if the employer reported pensionable compensation correctly by comparing the employer's original payroll registers to the PG records. In addition, we selected a sample of pay records with pensionable pay codes used in the employer's payroll system to verify these pay codes were approved by the ACERA Board of Retirement.

Test Results:



No exceptions noted.

TEST 2: VERIFY PENSIONABLE COMPENSATION REPORTED IN THE ORIGINAL PAYROLL REGISTER MATCHES THE RECORDS IN PENSION GOLD

We selected a sample of the Superior Court of California members with pensionable compensation reported in the Court payroll registers and compared them to the records in Pension Gold. This test was to confirm if the employer payroll system had correctly transmitted data into the transmittal files submitted to ACERA. We confirmed the pensionable compensation amount in the employer's payroll system matched what was recorded in PG.

Test Results:



No exceptions noted.

TEST 3: REVIEW PEPRA PENSIONABLE COMPENSATION LIMITS FOR NEW TIER MEMBERS HIRED ON OR AFTER JANUARY 1, 2013

PEPRA Section 7522.10 (a), (c), and (d)(1) defined the pensionable compensation limits that could be used to calculate retirement benefits for new members hired on or after January 1, 2013. We tested samples of Court employees hired in year 2013 and 2017 to determine if their annual compensation complied with the PEPRA compensation limit (2017 limit was \$118,775).

Test Results:



No exceptions noted.

TEST 4: REVIEW IRS 401(A)(17) PENSIONABLE COMPENSATION LIMITS FOR EMPLOYEES HIRED ON OR AFTER JULY 1, 1996

PEPRA Section 7522.04 and 7522.42 (a) states participating employers are governed by Section 401 (a) of Title 26 of the United States Code, and compensation taken into account under the plan for any year shall not exceed the amount permitted under Section 401(a)(17).

We selected a sample of 2017 pay records from the Court's highly compensated employees and tested if their annual pensionable compensation was under the limit (the limit was \$270,000 for year 2017). We found there were no records reached the limit.

Test Results:



No exceptions noted.

TEST 5: REVIEW PENSIONABLE SALARY INCREASES FOR UNUSUAL ITEMS

We sampled several Court members' accounts to review their pensionable compensation records in PG, scanning for any unusual pay items or unusual payroll activities in their accounts.

We also selected some payroll samples to examine if there was an unusual salary increase within recent years.

Test Results:



No exceptions noted.

TEST 6: REVIEW VACATION SELL ACCORDING TO DIFFERENT BARGAINING UNIT'S MEMORANDUM OF UNDERSTANDING (MOU)

We selected samples to test the vacation sell transactions in the years 2015, 2016, and 2017. The purpose of this test was to identify if the vacation sell transactions complied with the employees' bargaining unit's MOU. We verified whether employees were selling vacations according to the rules prescribed in the employee's bargaining unit MOU. We also checked with employer about their internal procedures on the vacation sell transactions.

Test Results:



Partially Effective

We sampled vacation sell transactions, and we found that the majority of vacation accruals and vacation sell were completed according to the rules prescribed in the employee’s bargaining unit MOU.

We had one finding where the vacation sell did not meet the rules stated in MOU. We discussed our findings with the employer and determined that the internal controls and the procedures were incomplete.

Recommendations	Business Owner
1. We recommend that the Superior Court of California’s management team should develop a special payroll report to monitor their employees’ accumulative annual vacation sell and hours total based on the rules stated in the MOU for all different bargaining units. We also recommend for the employer to consider establishing a new process to have payroll staff review the new vacation sell reports to ensure the vacation sell is allowed by MOU as part of the bi-weekly payroll closing procedure.	<ul style="list-style-type: none">• The Superior Court of California
2. We recommend that ACERA Benefits Department work with the employer to strengthen the current review process on vacation sell and employees’ contributions so that any deviations in vacation sell activities can be identified and communicated promptly to the employer. The Benefits Department should consider implementing a long-term solution in Pension Gold (PG) to enable PG to send an alert when the member’s vacation sell activities exceed their MOU limits.	<ul style="list-style-type: none">• ACERA Benefits Department

CONCLUSION

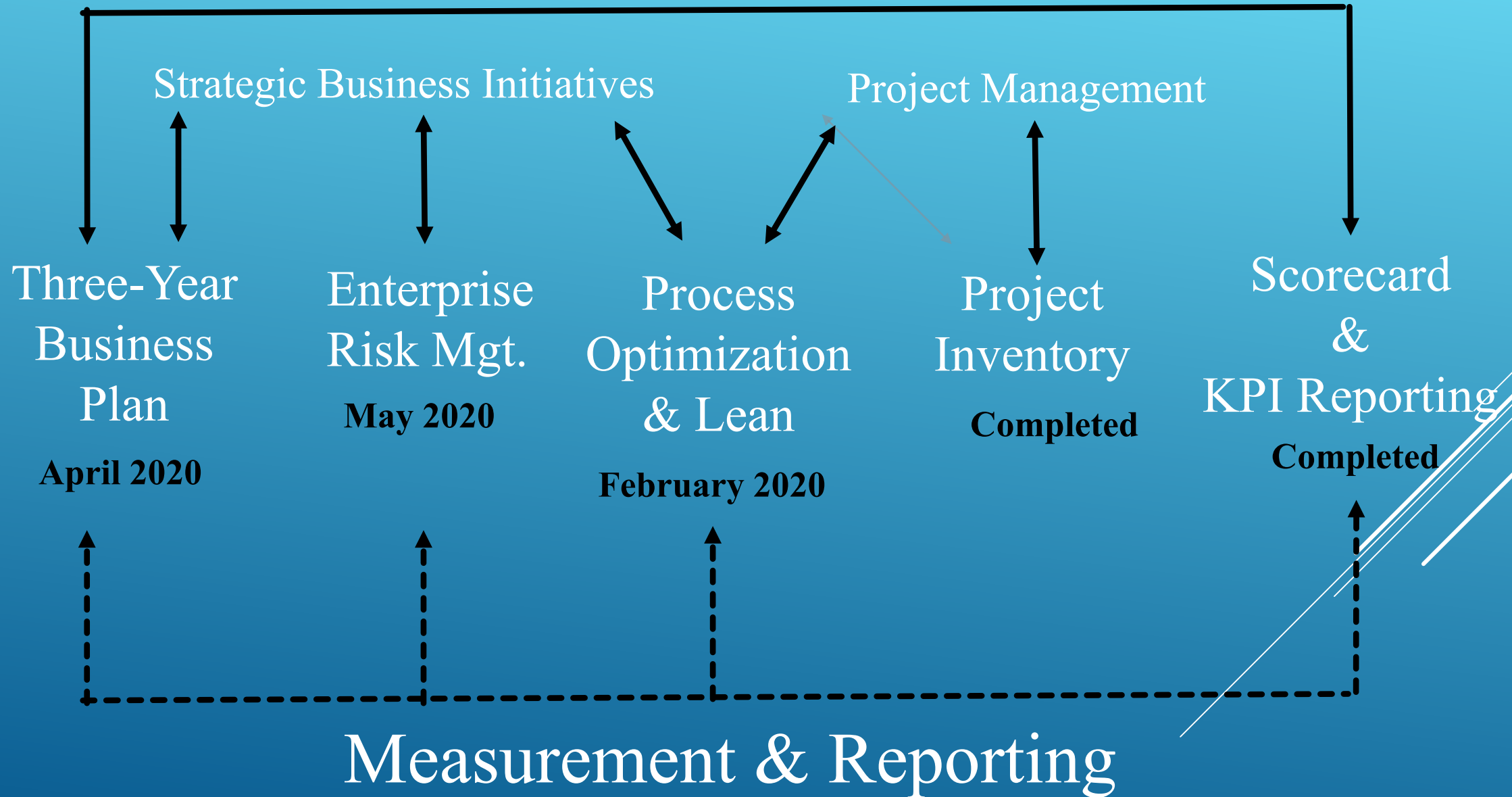
In conclusion, we found the employer’s payroll data, payroll process, and other reporting requirements were effective, and in compliance with PEPRA and the CERL as added, impacted, or amended by PEPRA. Please note that we limited this review to the areas specified in the scope section of this report. We want to thank the Superior Court of California’s management team and staff for their cooperation throughout the audit process.

Based on our audit results, we made the following key recommendation to strengthen their internal controls and make the business process, as it relates to meeting the PEPRA requirements, more effective:


1. We recommend that the employer strengthen the bi-weekly review process on vacation sell activities.

Any findings, recommendations, and conclusions outlined in this report were based on information made available or otherwise obtained at the time this report was prepared. If the employer disagrees with findings in this report, they have the right to appeal. All appeals must be made to ACERA Internal Audit Department in writing following the timeline stated in the Audit of Employer Compensation and Retirement Information Policy.

Performance Excellence



ENTERPRISE RISK MANAGEMENT...ERM

- Overview of Enterprise Risk Management
 - Summary of ERM activities
 - How to apply ERM
 - Key Success Factors for ERM / Starting ERM
 - Q&A
- 
- A decorative graphic consisting of several parallel white lines of varying thicknesses, slanted diagonally from the bottom right towards the top right, located in the lower right quadrant of the slide.

TWO MOST COMMON MYTHS ABOUT ERM

Myth #1:

ERM is a process only handled by the chief financial officer or finance.

Fact #1:

The ERM risk universe consists of strategic, financial, operational, and compliance risks. All members of senior management are needed to participate in the ERM process to have adequate knowledge and experience with the various risk strategies required. ERM does not lie within finance alone.

TWO MOST COMMON MYTHS ABOUT ERM

Myth #2:

ERM is a periodic event that requires updates only quarterly, semi-annually or annually.

Fact #2:

ERM is a process just like any other process within the organization (payroll, inventory, revenue, accounts payable, etc.). The ERM process for each company are at different stages of maturity. Your risk profile is continuously changing and your ERM process to adapt with your risk profile.

WHAT IS ENTERPRISE RISK MANAGEMENT (ERM)?

The Committee of Sponsoring Organization (COSO) defined ERM:



Enterprise risk management is a **process**, affected by an entity's board of directors, management and other personnel, applied in **strategy setting** and across the enterprise, designed to **identify potential events** that may affect the entity, and **Manage risk** to be within its **risk appetite**, to **provide reasonable assurance** regarding the achievement of entity objectives.

Evolution of Risk Management

1960s

1970s

1980s

1990s

2000s

2010s

2020s

Today's Focus

Insurable Risk

Risks based on historical loss experience and for which insurance policies can be purchased:

- Property/Casualty
- Errors & omissions
- Liability
- Workman's compensation
- Fire/Flood

Quantifiable Risk

Financial instruments emerged and shifted focus to quantifiable risk and other management tools:

- Earnings at risk
- Value at risk
- Historical predictors
- Monte Carlo simulations

Enterprise Risk

Risks are classified as:

- Strategic
- Finance/Reporting
- Operational
- Compliance

Management uses a top-down approach to identify, measure, and mitigate risks

ERM – Internal Environment

An organization must ensure that the risk management environment occurs on an enterprise-wide approach vs. a silo approach. Monitoring controls are established at the entity level for a entity-wide view of risk taking to account for risk objectives from each process.



ERM INFRASTRUCTURE FRAMEWORK

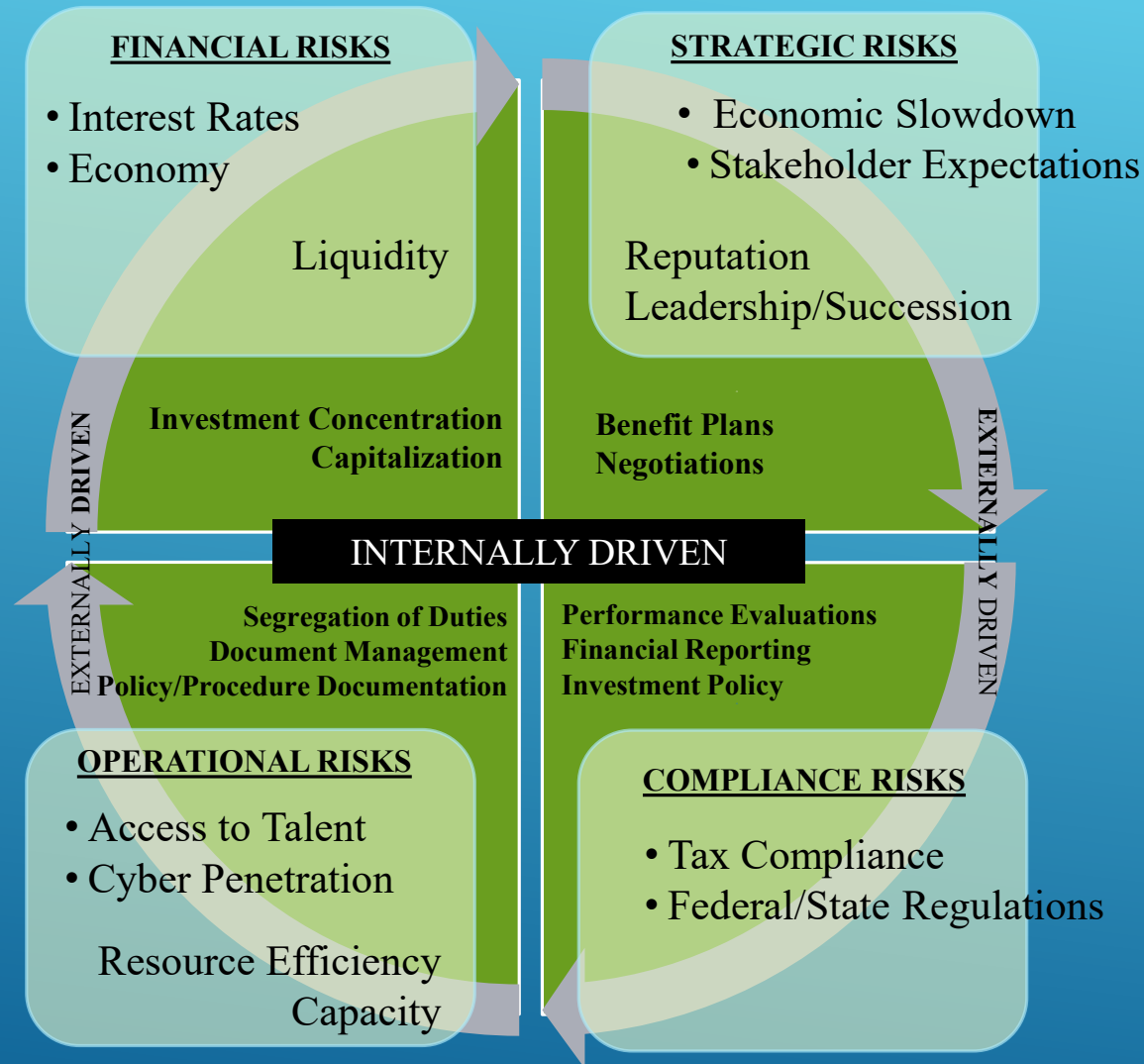
ERM INFRASTRUCTURE	RESPONSIBILITIES
--------------------	------------------

Board of Trustees	Approve ERM Charter, Assign Authority, Board Oversight
Management Team of Fund	Program sponsorship, establish tone at the top, delegate authority, report to Board
ERM Committee	Program Coordination, establish Policy & Procedures, create monitoring controls, assignment of risk owners, establish reporting protocols

INFORMATION FLOW

FINANCIAL/ REPORTING RISK OWNERS	STRATEGIC RISK OWNERS	OPERATIONAL RISK OWNERS	COMPLIANCE RISK OWNERS	Risk Owners: Identify risks applicable to each function of the organization and assume monitoring responsibility	1st Line of Defense
SENIOR LEADERS & DEPT. HEADS,	SENIOR LEADERS & DEPT. HEADS,	SENIOR LEADERS & DEPT. HEADS,	SENIOR LEADERS & DEPT. HEADS,	Control Owners: Perform monitoring of each risk and report back to Risk Owners and/ or ERM Committee	

ERM – RISK UNIVERSE - SAMPLE



Risk Universe

The risk universe is unique and evolving:

- Inherent risks change more frequently than with operating businesses
- Velocity of change is a more significant factor.
- Complexities of pension funds and investment risk, increase the need for coordinated risk management.

ERM – OBJECTIVE DEFINITIONS

Risk:

The possibility of an event occurring that may have either a positive or negative impact on the achievement of objectives.

Inherent Risk:

The impact and likelihood of a risk event occurring BEFORE consideration of mitigating controls or circumstances.

Mitigating
Activities:

The internal controls or safeguards in place to decrease the chance of a risk event from occurring.

Residual Risk:

The impact and likelihood of a risk event occurring AFTER consideration of a risk event occurring.

INHERENT RISK

IMPACT & LIKELIHOOD RANKING CRITERIA

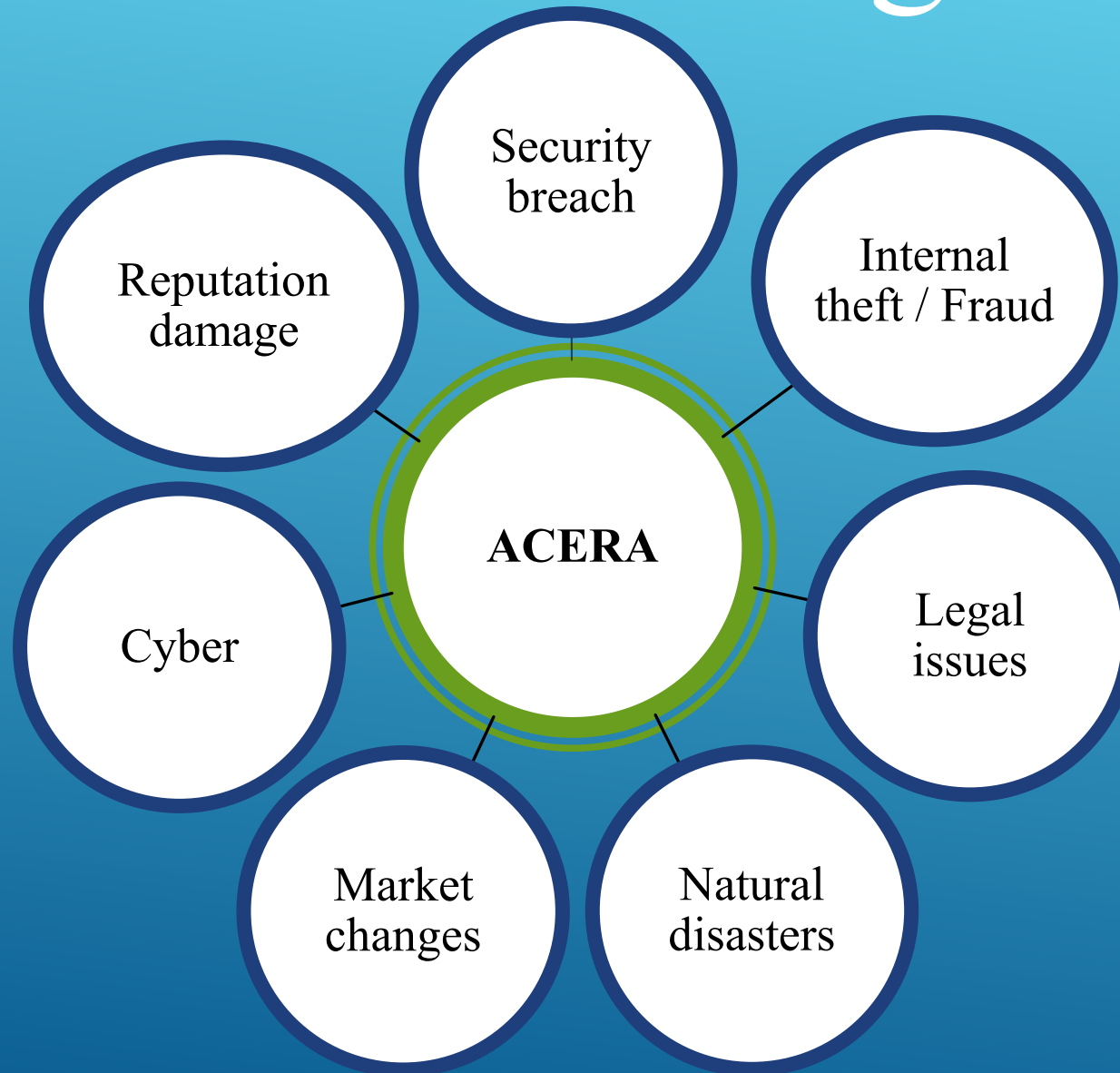
IMPACT RANKING	5 (high)	4	3	2	1 (low)
Financial – Loss of Market Value and/or Loss of Funded Ratio and/or Increased Expenses					
	>\$3 Billion	\$3 Billion – \$2 Billion	\$2 Billion - \$500 Million	\$500 Million - \$200K	<\$50K
Or Strategic:					
	Catastrophic Impact to Strategic Plan	Major Impact to Multiple Strategic Objectives	Major Impact to 2 Strategic Objectives	Major Impact to 1 Strategic Objective	Minimal Impact to 1 Strategic Objective
Or Operational :					
Building or IT System Shutdown	>3 Days	24 – 72 hours	12 – 24 hours	4 – 12 hours	< 4 hours
Reputation and Stakeholder Confidence	Catastrophic	Serious	Moderate	Limited	Minimal
Ability to Provide Retirement Benefits	Inability to deliver member services	Serious impact to deliver member services	Moderate impact to deliver member services	Limited impact to deliver member services	Minimal impact to deliver member services
Or Regulatory:					
Federal, State, & Local Govt./ EPA/ OSHA/ HIPAA, etc.	Large-scale Material breach of regulation	Material breach but cannot be rectified	Material breach which can be rectified	Minimal breach which cannot be rectified	Minimal breach which can be readily rectified
Likelihood Criteria - Inherent Risk					
Likelihood Ranking	5 (high)	4	3	2	1 (low)
Probability of an event occurring in a given year:					
	>50%	20 – 50%	10 – 20%	5 – 10%	<5%
or Event Occurrence (on average):					
	Once a year or more	1 in 3 years	1 in 5 years	1 in 7 years	1 in 10 years

KEY RISK INDICATORS (KRI'S)

Types of Data Sources Example

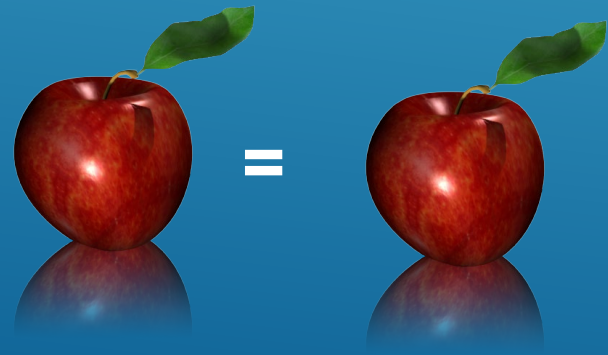
Data Source	KRI Dashboards
Public Available Information	Risk Owner Monitoring:
Economic Slowdown Risk	<ul style="list-style-type: none"> • Unemployment rates • Interest rates • Consumer spending/ CPI • Commodity prices
Internal System Information	Risk Owner Monitoring:
Cybersecurity Risk	<ul style="list-style-type: none"> • Firewall system report • Penetration attack volumes • 24/7 monitoring diagnostics
Internal Manual Information	Risk Owner Monitoring:
Physical Security Risk	<ul style="list-style-type: none"> • Property inspection routine • Security Alarms • Video Surveillance • News events (weather reports, protesters, etc.)

ERM – Risk Thinking



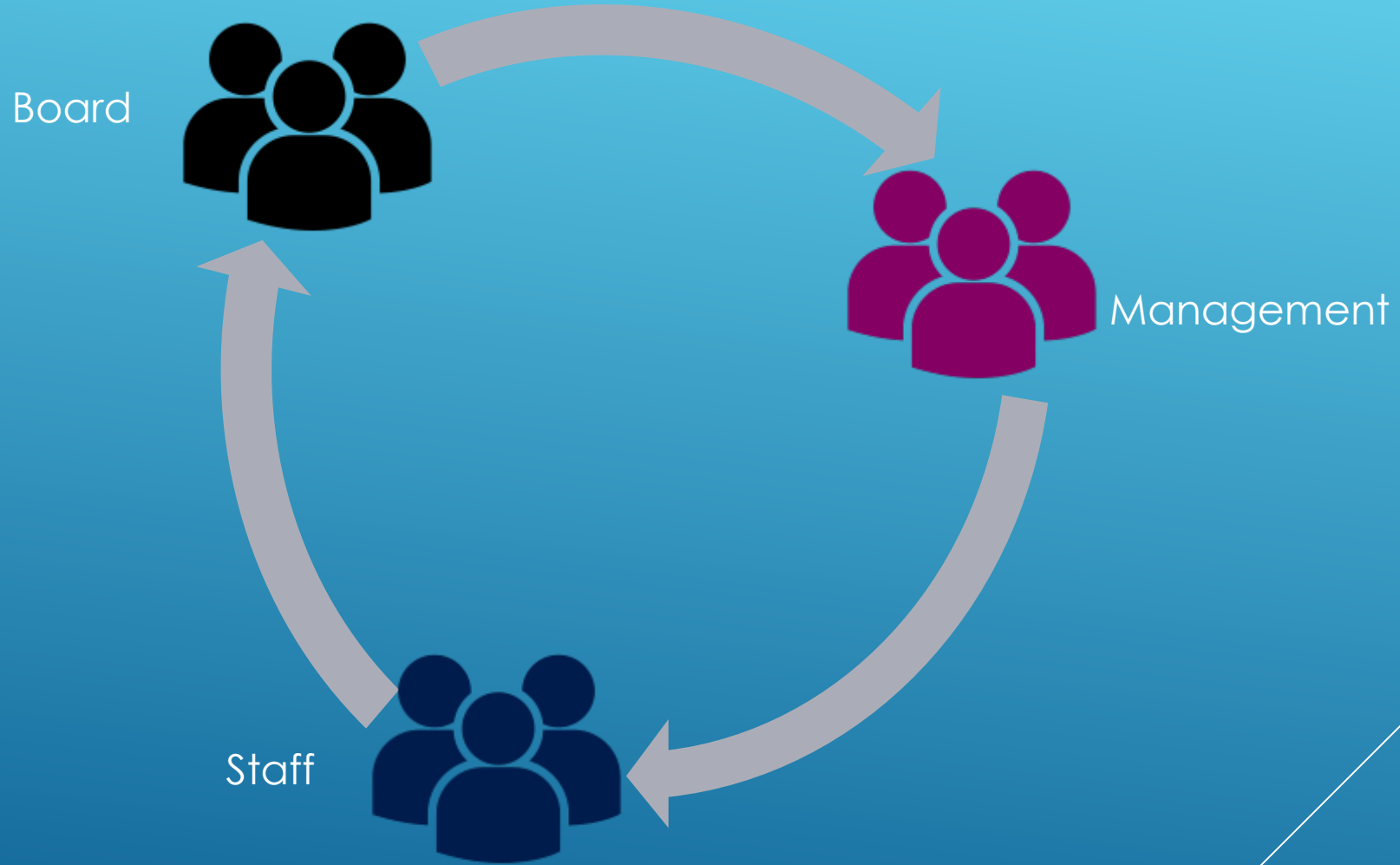
Risk Thinking – Common Language

- Define terminology
- Define reporting tools



COMMONALITY ACROSS THE ORGANIZATION WILL NOT ONLY YIELD BENEFITS FOR INTERNAL CONTROLS AND ACCOUNTING BUT ACROSS OPERATIONS

Risk Thinking - Communication



CRITICAL SUCCESS FACTORS

Value propositions from a mature ERM process:

Ownership

Risk owners are assigned and understand their responsibility for management, oversight and assurance.

Assurance

- Stakeholders are assured that risk is being managed within the organization's risk tolerance and receive information regarding the quality and type of control in place.
- Critical risks facing the organization have been identified, managed and reported on a level and frequency that support the organization's risk tolerance.

Oversight & Responsibility

Management has clear view of their risk universe utilizing dashboards showing monitoring controls and residual risk with an actionable playbook ready to execute.

THANK YOU

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