

ORANGE COUNTY EMPLOYEES RETIREMENT SYSTEM

BOARD OF RETIREMENT  
2223 WELLINGTON AVENUE, SUITE 100  
SANTA ANA, CA 92701

AUDIT COMMITTEE MEETING  
February 28, 2017  
1:00 p.m.

AGENDA

This agenda contains a brief general description of each item to be considered. Except as otherwise provided by law, no action shall be taken on any item not appearing in the following agenda.

A. [AUDIT COMMITTEE ORIENTATION](#)

*Presentation by David James, Director of Internal Audit*

**Recommendation:** Receive and file the *Audit Committee Orientation*.

B. [CONSIDERATION OF INTERNAL AUDIT CHARTER AND AUDIT COMMITTEE CHARTER](#)

*Presentation by David James, Director of Internal Audit*

**Recommendation:** Take appropriate action.

C. [REVIEW OF THE CHIEF INVESTMENT OFFICER \(CIO\) POSITION](#)

*Presentation by David James, Director of Internal Audit*

**Recommendation:** Receive and file the report *Review of the CIO Position*.

D. [RFP FOR AN ACTUARIAL FIRM TO PERFORM AN AUDIT OF OCERS' CONSULTING ACTUARY](#)

*Presentation by David James, Director of Internal Audit*

**Recommendation:** Approve the RFP for an actuarial firm to perform an audit of OCERS' consulting actuary.

E. [REVIEW OF 2016 AUDIT PLAN](#)

*Presentation by David James, Director of Internal Audit*

**Recommendation:** Receive and file the *2016 Audit Plan*.

F. [CONSIDERATION OF 2017 RISK ASSESSMENT AND 2017 AUDIT PLAN](#)

*Presentation by David James, Director of Internal Audit*

**Recommendation:** Approve the *2017 Risk Assessment and 2017 Audit Plan*.

**G. OVERVIEW OF AUDIT COMMITTEE OVERSIGHT OF OCERS' SECURITY**

*Presentation by Steve Delaney, CEO; Brenda Shott, Assistant CEO, Internal Ops; and Gina Ratto, Chief Legal Officer*

**Recommendation:** Receive and file.

**\*\*\*\*\* END OF INDIVIDUAL ITEMS AGENDA \*\*\*\*\***

**PUBLIC COMMENTS:** The public, plan members, beneficiaries, and/or representatives may speak to any subject matter contained in the agenda *either* at the time the item is addressed *or* at this time, provided that no action may be taken on any item not appearing on this agenda unless authorized by law. Persons who want to address items on the agenda should provide written notice to the Secretary of the Committee prior to the Committee's discussion on the item by filling out the Public Comment Form located in the back of the room. When addressing the Committee, please state your name for the record prior to providing your comments. Speakers will be limited to three minutes.

**COMMITTEE MEMBER COMMENTS**

**CHIEF EXECUTIVE OFFICER/STAFF COMMENTS**

**ADJOURNMENT**

**NOTICE OF NEXT MEETINGS**

**REGULAR BOARD MEETING**

**March 20, 2017**

**9:00 a.m.**

**ORANGE COUNTY EMPLOYEES RETIREMENT SYSTEM**

**2223 E. WELLINGTON AVENUE, SUITE 100**

**SANTA ANA, CA 92701**

*All supporting documentation is available for public review in the retirement office during regular business hours, 8:00 a.m. – 5:00 p.m., Monday through Thursday and 8:00 a.m. – 4:30 p.m. on Friday.*

It is OCERS' intention to comply with the Americans with Disabilities Act ("ADA") in all respects. If, as an attendee or participant at this meeting, you will need any special assistance beyond that normally provided, OCERS will attempt to accommodate your needs in a reasonable manner. Please contact OCERS via email at [adminsupport@ocers.org](mailto:adminsupport@ocers.org) or by calling 714-558-6200 as soon as possible prior to the meeting to tell us about your needs and to determine if accommodation is feasible. We

Audit Committee Meeting  
February 28, 2017

would appreciate at least 48 hours' notice, if possible. Please also advise us if you plan to attend meetings on a regular basis.

A



# Memorandum

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**DATE:** February 17, 2017  
**TO:** Members of the Audit Committee  
**FROM:** David James, CPA, Director of Internal Audit  
**SUBJECT:** **AUDIT COMMITTEE ORIENTATION**

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## **Recommendation**

Receive and file the *Audit Committee Orientation*.

## **Background/Discussion**

The following Audit Committee Orientation presentation is meant to familiarize new Audit Committee members with the role of the Audit Committee. The Audit Committee Manual contains updated information and reference documents for Audit Committee members.

## **Submitted by:**

The OCERS logo is repeated here, with the text "D.J. - Approved" to its right.

D.J. - Approved

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David James, CPA  
Director of Internal Audit

# Audit Committee Orientation



**February 28, 2017**

# Contents

## Audit Committee

- Purposes
- Law & Ethics
- Oversight
- Internal Controls & Risk Management
- Reporting to the Board
- AC Charter Review & History

## Internal Audit Division

- Mission
- Independence of Internal Audit
- Objectives of Internal Audit
- Scope
- Responsibilities
- IA Charter Review & History

## Internal Audit Activities

- Hotline Policy
- Hotline Investigations
- Internal Audits' Impacts

# Audit Committee's Purposes

Provide oversight of OCERS' internal and external audit activities

Assist Board in ensuring the independence of internal audit functions

Promote & enhance effective internal controls for OCERS' operations

Ensure that appropriate action is taken on audit recommendations

Oversee communication between external auditors, internal auditors, and management



# Audit Committee Responsibilities

## Law & Ethics

- Provide the policy and framework for
  - Compliance with laws and regulations
  - Mechanisms for assessment of compliance
  - Communication with the Board on policies

# Audit Committee Responsibilities

## Oversight of Financial Reporting Process

- Review audited financial statements with external auditor and senior management
- Review findings or comments of regulatory agencies regarding financial statements or other OCERS' information
- Review external auditor's assessments of the appropriate application of accounting principles by OCERS' management and discuss necessary financial statement disclosures
- Discuss with management the effectiveness of the internal financial and operational control policies

# Audit Committee Responsibilities

## Oversight of External Auditors

- Appoint, compensate, retain, and oversee the work of external auditors
- Review the engagement of the external auditor at least every three years
- Approve other audits, agreed upon procedures, and non-audit work conducted by the external auditors

# Audit Committee Responsibilities

## Oversight of Internal Audit

- Approve all decisions regarding the performance evaluation, appointment, or removal of the Director of Internal Audit
- Review charters and policies assigned to Audit Committee at least once every three years
- Review and approve the risk assessment and annual Internal Audit Plan
- Receive and review internal and external audit reports and management responses

# Audit Committee Responsibilities

## Internal Controls & Risk Management

- Review management responsibilities for:
  - Adequacy of internal controls
  - Material risks facing OCERS and management's actions to minimize risk
  - Risks from external organizations
  - Special investigations and whistleblower mechanisms

## Reporting to the Board

- The Audit Committee:
  - Reports to the Board its activities and the results of its reviews
  - Reviews significant changes in accounting standards, policies, or practices that may impact OCERS and reports the results of that review to the Board

## AC Charter Review & History

- Reviews at least once every three years and recommends any amendments to the Board for approval as necessary
- Adopted by the Board of Retirement on November 18, 2002, and amended on January 17, 2012, and July 20, 2015

## Mission

- Provide reliable, independent and objective evaluations and consulting services to the Audit Committee and management relating to business and financial operations



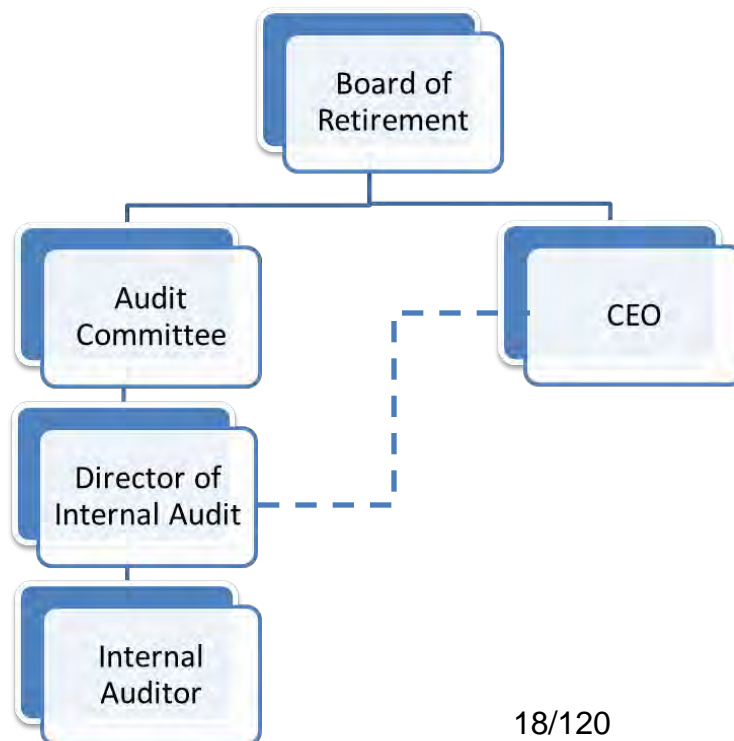
## Independence of Internal Audit

- Internal auditors must be independent and objective in performing their work
- Follows professional standards, is free of operational and management responsibilities conflicting with standards
- Any potential impairment to independence is communicated to the Audit Committee 17/120

# Internal Audit Division

## Independence of Internal Audit

- **Functionally** report to Audit Committee
- **Administratively** report to CEO



# Internal Audit Division

## Objectives of Internal Audit

- Assist the Board and management in the effective discharge of their fiduciary responsibilities
- Internal Audit furnishes audits, analysis, evaluations, recommendations, and information
- Objectives include:
  - Promoting effective internal controls
  - Helping provide assurance that assets are safeguarded
  - Compliance is maintained with prescribed laws, Board and management policies
  - Reliability and integrity of OCERS' data is maintained
  - Procedures and operating efficiency are enhanced

# Internal Audit Division

## Scope

- Evaluating adequacy of OCERS' system of internal controls, risk management and governance processes
- Reviewing the systems and processes
- For consulting and advisory services, Internal Audit may provide assessments and advice to identify risks and internal controls

## Scope (continued)

- Except where prohibited by law, Internal Audit will have complete and unrestricted access to all OCERS' personnel, records, files, information systems, and assets
- The Director of Internal Audit will inform the Audit Committee whenever there are significant barriers or resistance to access to personnel or information

# Internal Audit Division

## Responsibilities

- Preparing an annual audit plan of audit projects addressing areas of highest risk
- Producing reports on the results of audits, including findings and recommendations to management
- Following-up on management's actions to correct deficiencies
- Conducting special investigations (i.e. fraud hotline) and analysis

## IA Charter Review & History

- AC reviews at least once every three years and recommends any amendments to the Board for approval as necessary
- Adopted by the Board of Retirement on November 18, 2002 and amended on August 19, 2008, January 17, 2012, and July 20, 2015

# Hotline Policy

## Ethics, Compliance, & Fraud Hotline established October 2012

- Facilitates anonymous reporting by employees, members, and public to report concerns about potential misconduct or inappropriate activities
- Director of Internal Audit is responsible for conducting investigations
- The CEO makes the determination regarding action to be taken against the accused individual upon completion of investigation



# Hotline Investigations



11 cases investigated by IA since inception of the hotline.

Most were unsubstantiated allegations, one a misunderstanding of benefits, one a customer service issue.

Two cases were referred to OCERS Disability Division.

The Hotline received one report in 2016, a complaint about suspected benefit payment fraud. IA determined that the claim was unsubstantiated.

# Internal Audits' Impacts

## Plan Sponsors Audits

- Orange County: recommended several process improvements to reduce payroll transmittal errors that have recurred on a regular basis
- OCSD: recommended automated and manual controls to reduce payroll transmittal errors that have recurred on a regular basis
- TCA: recommended automation of manually maintained payroll spreadsheets
- OCTA: recommended controls to evidence management review of payroll and payroll transmittal errors
- San Juan Capistrano: recommended improved oversight over the recording of paid time-off
- All plan sponsors review: reported on current financial condition

# Internal Audits' Impacts

## Member Services Audits

- Process improvement to better track and monitor the status of member reciprocity requests & contribution refunds
- Benefit setup process recommendations:
  - Automated reporting to capture manually adjusted Final Average Salary calculations
  - Identified over/under-payment of benefits to members that needed to be recovered or paid
  - Identified member data inconsistencies that needed correction before implementation of V3
  - Updated procedures manuals to reflect current practices
  - Incorporate certain automated procedures and checklists in V3 to replace manual steps performed in PensionGold

# Internal Audits' Impacts

## Finance / IT Audits

- Improved controls over the investment portfolio reconciliation process
- Actuarial extract process recommendations:
  - Recommended proper procedures documentation of various departmental roles
  - Recommended automation of manually generated supplemental schedules
  - Recommended audit trail documentation of data testing performed by staff

# Internal Audits' Impacts

## Investments Audits

- Improved transparency of derivative investments reporting to Investment Committee
- Recommended improvements in the due diligence process
- Improved controls over wire transfers
- Validated management fees of a long-term money manager



## **Audit Committee Manual**

**2017**

# Audit Committee Manual

## Contents

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## Orange County Employees Retirement System Audit Committee Charter

### **1. Introduction**

The Board of Retirement has established an Audit Committee to assist it in overseeing the audit function within OCERS. The Audit Committee is an advisory committee to the Board of Retirement, and its recommendations are subject to final approval by the Board. Notwithstanding the preceding sentence, with respect to those matters expressly assigned to it in this Audit Committee Charter, the Audit Committee has final authority.

### **2. Purpose**

The Audit Committee provides oversight of OCERS' internal and external audit activities. The Audit Committee assists the Board in ensuring the independence of the internal audit functions and ensuring that appropriate action is taken on audit recommendations. The Audit Committee helps promote and enhance effective internal controls for OCERS operations, and oversees communication between external auditors, internal auditors, and management.

### **3. Membership**

The Audit Committee will consist of four members of the Board of Retirement. The Board Chair will appoint members of the Audit Committee as provided in the OCERS By-Laws and designate one member to serve as the Committee Chair.

Ideally, members should have expertise in accounting, auditing, financial reporting, and internal control. Although these desired traits are not mandatory, members should be sufficiently knowledgeable about these topics to make informed decisions with the assistance of a financial expert.

### **4. Meetings**

The Audit Committee will meet at least quarterly, with authority to convene additional meetings as circumstances require. All Audit Committee members are expected to attend each meeting. The Director of Internal Audit will attend all Audit Committee meetings. Meeting notices will be provided to interested parties in conformance with applicable laws, regulations, customs, and practices. All meetings are subject to the Brown Act. Meeting agendas will be prepared and provided in advance to members, along with appropriate briefing materials. Minutes of meetings will be prepared. Minutes of the meeting will contain a record of persons present, decisions taken, and a high-level summary of the discussion.



## 5. Responsibilities and Duties

The Audit Committee's key areas of responsibility are:

- a) *Law and Ethics*: The Audit Committee will provide the policy and framework for compliance with laws and regulations, mechanisms for assessment of compliance, and communication with the Board on OCERS policies.
  
- b) *Financial Reporting Process*: The Audit Committee will:
  - 1) Oversee the reporting of all financial information, including reviewing with the external auditor their scope, plan, duties, responsibilities, and the timing and engagement fee of the annual financial audit;
  - 2) Resolve disagreements between the internal auditor, external auditor, and /or management regarding financial reporting and internal control risks identified in the audit;
  - 3) Review the audited financial statements with the external auditor and senior management;
  - 4) Review management letters with management;
  - 5) Review the findings or comments of regulatory agencies concerning financial statements or other information regarding OCERS;
  - 6) Review the external auditor's assessments of the appropriate application of accounting principles by OCERS management;
  - 7) Review all matters required to be disclosed by accounting standards, including significant changes in those standards; and
  - 8) Meet with senior management, at least annually, to discuss the effectiveness of the internal financial and operational control policies.
  
- c) *Oversight of the External Auditors*: The Audit Committee will:
  - 1) Appoint, compensate, retain, and oversee the work of external auditors engaged for the purpose of issuing an independent audit report or performing other independent audits, reviews, or attest services;
  - 2) Select external audit services for the Comprehensive Annual Financial Report;
  - 3) Review the engagement of the external auditor at least every three years for performance, independence, and the impact of non-audit services; and
  - 4) Approve other audits, agreed upon procedures, and non-audit work to be conducted by the external auditors.

**d) Oversight of Internal Audit:** The Audit Committee will:

- 1) Approve all decisions regarding the performance evaluation, appointment, or removal of the Director of Internal Audit;
- 2) Approve the compensation and salary adjustments of the Director of Internal Audit;
- 3) Review the charters and policies assigned to Audit Committee at least once every three years in accordance with the schedule set forth in the *OCERS Charters and Policies Review Schedule* and recommend the same for approval by the Board of Retirement;
- 4) Review and approve the risk assessment and annual Internal Audit Plan prepared by the Director of Internal Audit;
- 5) Receive and review internal and external audit reports and management responses;
- 6) Review significant recommendations from audits during the year and management's responses, and make appropriate recommendations to the Board; and
- 7) Make appropriate inquiries of the Director of Internal Audit to determine whether there is audit scope or budgetary limitations that impede the ability of the internal audit activity to carry out its responsibilities.

**e) Internal Control and Risk Management:** The Audit Committee will review management responsibilities for:

- 1) The adequacy of OCERS' internal controls, including information systems;
- 2) Material risks facing OCERS and management's actions to minimize risk;
- 3) Risks from external organizations such as service providers, vendors, investment managers, consultants, and plan sponsors; and
- 4) Special investigations and whistleblower mechanisms. The Audit Committee can retain independent counsel, accountants, or other specialists to assist in the conduct of an investigation.

## **6. Reporting**

The Audit Committee will:

- a)** Report to the Board of Retirement its activities and the results of its reviews; and
- b)** Review significant changes in accounting standards, policies, or practices that may impact OCERS and report the results of that review to the Board of Retirement.

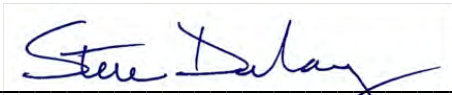
## 7. Review and Amendment of the Charter

The Audit Committee will review this Charter at least once every three (3) years and recommend any amendments to the Board for approval as necessary to ensure that the Charter remains relevant and appropriate.

The Audit Committee Charter was adopted by the Board of Retirement on November 18, 2002, and amended on January 17, 2012, and July 20, 2015.

### Secretary's Certificate

I, the undersigned, the duly appointed Secretary of the Orange County Employees Retirement System, hereby certify the adoption of this Charter.



Steve Delaney, Secretary to the Board

7/20/15

Date



## Orange County Employees Retirement System Internal Audit Charter

### INTRODUCTION

The Audit Committee of OCERS oversees the Internal Audit Division under the following provisions:

#### 1. MISSION OF THE INTERNAL AUDIT DIVISION

The mission of the Internal Audit Division is to provide reliable, independent and objective evaluations and consulting services to the Audit Committee and OCERS management relating to business and financial operations. Internal Audit assists the Board of Retirement and management to achieve their objectives by testing and reporting on the effectiveness of internal control systems, risk management, and governance processes.

#### 2. INDEPENDENCE OF THE DIRECTOR OF INTERNAL AUDIT

The internal audit activity must be independent, and internal auditors must be objective in performing their work. Independence is the freedom from conditions that threaten the ability of Internal Audit to carry out its responsibilities in an unbiased manner.

Independence is the fundamental principle that guides the reporting relationship of the internal auditor. Internal auditor independence is strongly emphasized by authoritative bodies such as the Institute of Internal Auditors, the American Institute of Certified Public Accountants, and the Government Accountability Office. The Director of Internal Audit will follow recognized professional standards established by the Institute of Internal Auditors and be free of operational and management responsibilities that would conflict with the standards. Any potential impairment to independence will be communicated to the Audit Committee.

#### 3. ORGANIZATIONAL REPORTING

To achieve the degree of independence necessary to effectively carry out the responsibilities of the internal audit activity, the Director of Internal Audit will have direct access to senior management and the Board of Retirement. This can be achieved by a dual-reporting relationship. The Director of Internal Audit will report functionally to the Audit Committee and administratively to the Chief Executive Officer.

Functionally reporting to the Audit Committee involves the Audit Committee:

1. Reviewing and recommending changes to the Internal Audit Charter to the Board of Retirement;

2. Approving the risk-based Internal Audit plan;
3. Receiving communications from the Director of Internal Audit on the results of audit activities;
4. Approving all decisions regarding the performance evaluation, appointment, or removal of the Director of Internal Audit;
5. Approving the compensation and salary adjustments of the Director of Internal Audit;
6. Making appropriate inquiries of the Director of Internal Audit to determine whether there is audit scope or budgetary limitations that impede the ability of Internal Audit to carry out its responsibilities.

Administrative reporting is the reporting relationship within the OCERS management structure that facilitates the daily operations of the internal audit activity, which includes:

1. Budgeting and management accounting;
2. Human resource administration, including personnel evaluations, leave request approval, and compensation;
3. Internal communications and information flows;
4. Administration of the Internal Audit Division's policies and procedures.

#### **4. OBJECTIVES AND SCOPE**

The objective of Internal Audit is to assist the Board of Retirement and management in the effective discharge of their fiduciary responsibilities. Internal Audit will furnish them with audits, analysis, evaluations, recommendations, and information. Objectives include promoting effective internal controls, helping provide assurance that the organization's assets are safeguarded; compliance is maintained with prescribed laws, Board, and management policies; the reliability and integrity of OCERS' data is maintained; and procedures and operating efficiency are enhanced.

The scope of Internal Audit includes the examination and evaluation of the adequacy of OCERS' system of internal controls, risk management and governance processes. The scope includes:

1. Reviewing the reliability and integrity of financial and business information systems, and the means used to identify, measure, classify and report such information;
2. Reviewing the systems and processes established to ensure compliance with those policies, plans, procedures, laws, and regulations that are fundamental to the operations of OCERS and could have a significant impact on operations, financial reports, and disclosures;
3. Reviewing the means of safeguarding assets and verifying the existence of such assets;
4. Monitoring and evaluating the effectiveness of OCERS' risk management systems, including identifying internal and external risks;
5. Reviewing the accuracy of data transmitted to OCERS by external parties.
6. Evaluating the quality of performance of external auditors and the degree of coordination with Internal Audit;

7. For consulting and advisory services, Internal Audit may provide assessments and advice to identify risks and internal controls for projects.

## **5. AUTHORITY AND RESPONSIBILITY**

The Internal Audit Division is established by the OCERS Board of Retirement pursuant to applicable laws and regulations, customs of corporate governance, and best practices. This Charter and all future amendments are approved by the Audit Committee and adopted by the Board of Retirement by a majority vote.

The responsibility of OCERS Internal Audit is to serve the Board of Retirement in a manner that is consistent with the International Professional Practices Framework of the Institute of Internal Auditors, as required by California Government Code 1236. In addition, when appropriate, OCERS Internal Audit follows professional standards promulgated by the Government Accountability Office, the American Institute of Certified Public Accountants, and the Information Systems Audit and Control Association.

OCERS Internal Audit is responsible for:

1. Establishing policies and procedures for auditing, and directing and performing its technical and administrative functions;
2. Developing and executing a comprehensive audit program for the evaluation of internal controls established over OCERS' financial and business activities;
3. Preparing an annual audit plan that identifies audit projects addressing areas of highest risk to OCERS operations;
4. Assisting management in their stewardship of OCERS' trust funds and resources and their compliance with policies and procedures;
5. Recommending improvements in internal controls to help:
  - a. Safeguard trust funds and resources,
  - b. Ensure data is not compromised,
  - c. Ensure compliance with laws and regulations;
6. Reviewing procedures and records for accuracy and completeness to accomplish and report on intended objectives;
7. Producing reports on the results of audits, including findings and recommendations;
8. Following-up on actions taken to correct reported deficiencies;
9. Conducting special investigations and analysis as needed;
10. Creating and maintaining a mechanism for reporting financial statement fraud, other fraud, and inappropriate activities.

## **6. INTERNAL AUDIT ACCESS TO PERSONNEL AND INFORMATION**

Except where prohibited by law, Internal Audit will have complete and unrestricted access to all

OCERS personnel, records, files, information systems, and assets. The Director of Internal Audit will inform the Audit Committee whenever significant barriers or resistance to access to personnel or information occurs.

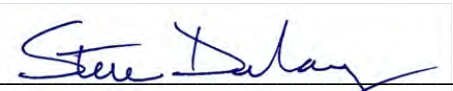
**7. POLICY HISTORY**

The Audit Committee will review this Charter at least once every three (3) years and recommend any amendments to the Board for approval as necessary to ensure that the Charter remains relevant and appropriate.

The OCERS Internal Audit Charter was adopted by the Board of Retirement on November 18, 2002 and amended on August 19, 2008, January 17, 2012, and July 20, 2015.

**Secretary's Certificate**

I, the undersigned, the duly appointed Secretary of the Orange County Employees Retirement System, hereby certify the adoption of this Charter.

  
\_\_\_\_\_  
Steve Delaney, Secretary to the Board

7/20/15  
\_\_\_\_\_  
Date



## **OCERS Ethics, Compliance, and Fraud Hotline Policy**

### **PURPOSE AND BACKGROUND**

1. The OCERS Ethics, Compliance, and Fraud Hotline (the Hotline) was established in October 2012 to aid management in the detection of activities that are unethical, fraudulent, or not in compliance with the policies of OCERS. The Hotline facilitates anonymous reporting by employees, contractors, members, and the general public to report concerns about potential misconduct or inappropriate activities, including but not limited to, harassment, conflict of interest, violation of policy, fraud, and waste of resources.
2. The Hotline reinforces OCERS efforts to ensure transparency, accountability, fairness, and integrity in the workplace.

### **OBJECTIVE**

3. The purpose of this document is to establish a policy for conducting an investigation when a report of potential misconduct or inappropriate activity is made through the Hotline, and for assigning responsibility for taking appropriate actions as a result of the investigation.

### **POLICY**

4. OCERS management is responsible for the implementation of procedures and controls designed to prevent and detect fraud, misappropriations, deception, wrongdoing, and other inappropriate conduct. Fraud is defined by the Association of Certified Fraud Examiners as any intentional act to deprive another of property or money by acts of guile, deception, or other unfair means. Fraud can include conflict of interest, theft, or breach of fiduciary duty. Each member of the OCERS management team must be familiar with the types of improprieties that might occur within his or her area of responsibility, and be alert for any indication of irregularity.
5. All allegations of potential misconduct or inappropriate activity raised by any source will be taken seriously and properly investigated. Retaliation against anyone who reports suspected misconduct or inappropriate activity will not be tolerated.
6. OCERS Director of Internal Audit will be responsible for conducting an investigation as a result of a report being filed on the Hotline. The investigation will be conducted without regard to the alleged wrongdoer's length of service, position, title, or relationship with OCERS.



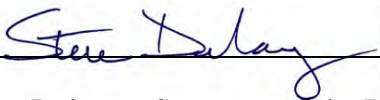
7. If an accusation is made against the Director of Internal Audit, then the Director of Internal Audit or Internal Auditor, as appropriate, will inform the Chief Executive Officer, who will then be responsible for directing an investigation.
8. Depending on the nature of the complaint, some investigations regarding human resources matters such as matters related to performance appraisals or harassment may be turned over to the Manager of Administrative Services. Internal Audit may also seek the assistance of Legal or other informed parties in conducting an investigation.
9. The Chief Executive Officer will make the final determination regarding action to be taken against the accused individual upon completion of the investigation.
10. In some cases, the final report of the outcome of an investigation may be submitted to the Audit Committee, or Chair of the Audit Committee. This may occur if an accusation has been against executive management, or if the results of an investigation indicate criminal acts have occurred, or there are high-level policy implications resulting from an investigation. The Audit Committee will make the determination for corrective action, if any, as it deems appropriate.
11. If a report to the hotline indicates that illegal acts may have been committed, Internal Audit will refer those reports to the appropriate law enforcement agency or the district attorney. If a report to the hotline indicates that a violation of the Political Reform Act has occurred, such as a conflict of interest, illegal acceptance of gifts or honorarium, or restrictions on activities of former investment officials, then Internal Audit will refer the report to the California Fair Political Practices Commission (FPPC).
12. OCERS will maintain the confidentiality, to the extent that it is legally possible, of any individual reporting any detected or suspected fraudulent activity, ethics violations, or compliance failures.

#### **POLICY REVIEW**

13. This policy will be reviewed every three years.

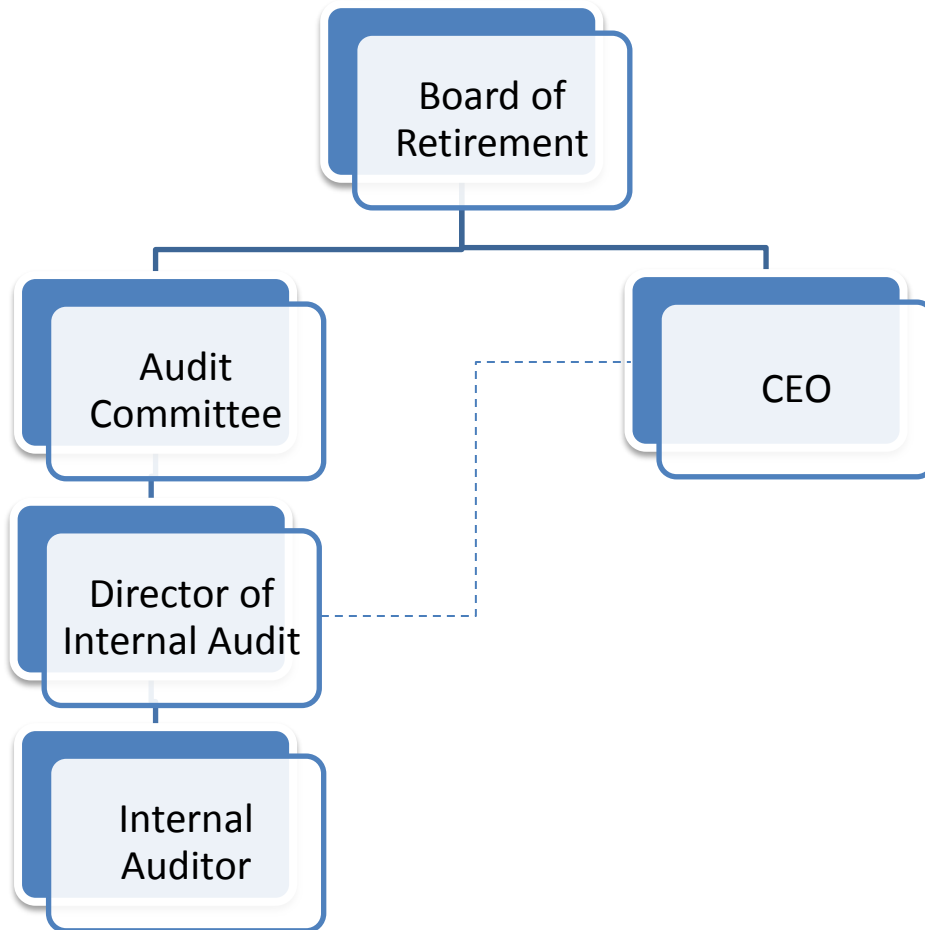
#### **POLICY HISTORY**

14. The Board adopted this policy on June 06, 2013.

  
\_\_\_\_\_  
Steve Delaney, Secretary of the Board

06/20/2013  
\_\_\_\_\_  
Date

# Organizational Chart



## **INTERNAL AUDITOR PROFILES**

**David James, CPA**  
**DIRECTOR OF INTERNAL AUDIT**

Years with OCERS: 6

Years of Auditing Experience: 17

Prior to Joining OCERS: City of Los Angeles

Education: MBA, UCLA

**Mark Adviento, CPA**  
**INTERNAL AUDITOR**

Years with OCERS: 5

Years of Auditing Experience: 14

Prior to Joining OCERS: Southern California Edison

Education: BA, Cal State Fullerton

# The Institute of Internal Auditors Code of Ethics

## Principles

Internal auditors are expected to apply and uphold the following principles:

### 1. Integrity

The integrity of internal auditors establishes trust and thus provides the basis for reliance on their judgment.

### 2. Objectivity

Internal auditors exhibit the highest level of professional objectivity in gathering, evaluating, and communicating information about the activity or process being examined. Internal auditors make a balanced assessment of all the relevant circumstances and are not unduly influenced by their own interests or by others in forming judgments

### 3. Confidentiality

Internal auditors respect the value and ownership of information they receive and do not disclose information without appropriate authority unless there is a legal or professional obligation to do so.

### 4. Competency

Internal auditors apply the knowledge, skills, and experience needed in the performance of internal audit services.

## Rules of Conduct

### 1. Integrity

Internal auditors:

- 1.1. Shall perform their work with honesty, diligence, and responsibility.
- 1.2. Shall observe the law and make disclosures expected by the law and the profession.
- 1.3. Shall not knowingly be a party to any illegal activity, or engage in acts that are discreditable to the profession of internal auditing or to the organization.
- 1.4. Shall respect and contribute to the legitimate and ethical objectives of the organization.

### 2. Objectivity

Internal auditors:

- 2.1. Shall not participate in any activity or relationship that may impair or be presumed to impair their unbiased assessment. This participation includes those activities or relationships that may be in conflict with the interests of the organization.

2.2. Shall not accept anything that may impair or be presumed to impair their professional judgment.

2.3. Shall disclose all material facts known to them that, if not disclosed, may distort the reporting of activities under review.

### **3. Confidentiality**

Internal auditors:

3.1. Shall be prudent in the use and protection of information acquired in the course of their duties.

3.2. Shall not use information for any personal gain or in any manner that would be contrary to the law or detrimental to the legitimate and ethical objectives of the organization.

### **4. Competency**

Internal auditors:

4.1. Shall engage only in those services for which they have the necessary knowledge, skills, and experience.

4.2. Shall perform internal audit services in accordance with the *International Standards for the Professional Practice of Internal Auditing*.

4.3. Shall continually improve their proficiency and the effectiveness and quality of their services.

# The Institute of Internal Auditors Practice Standards

## International Standards for the Professional Practice of Internal Auditing (*Standards*)

### Introduction to the International 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 with 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:

- 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.
- Interpretations, which clarify terms or concepts within the Statements.

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.

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.

Implementation Standards are also provided to expand upon the Attribute and Performance standards, by providing the requirements applicable to assurance (A) or consulting (C) activities. 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, and (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, and (2) the person or group seeking and receiving the advice — the engagement client. When performing consulting services the internal auditor should maintain objectivity and not assume management responsibility.

The Standards apply to individual internal auditors and internal audit activities. All internal auditors are accountable for conforming with the Standards related to individual objectivity, proficiency, and due professional care. In addition, internal auditors are accountable for conforming with the Standards, which are relevant to the performance of their job responsibilities. Chief audit executives are accountable for overall conformance with the Standards.

The review and development of the *Standards* is an ongoing process. The International Internal Audit Standards Board engages in extensive consultation and discussion prior to issuing the *Standards*. This includes worldwide solicitation for public comment through the exposure draft process. All exposure drafts are posted on The IIA's Web site as well as being distributed to all IIA institutes.

## Attribute Standards

### **1000 – Purpose, Authority, and Responsibility**

The purpose, authority, and responsibility of the internal audit activity must be formally defined in an internal audit charter, consistent with the Definition of Internal Auditing, the Code of Ethics, and the *Standards*. The chief audit executive must periodically review the internal audit charter and present it to senior management and the board for approval.

#### **Interpretation:**

*The internal audit charter is a formal document that defines the internal audit activity's purpose, authority, and responsibility. The internal audit charter establishes the internal audit activity's position within the organization, including the nature of the chief audit executive's functional reporting relationship with the board; authorizes access to records, personnel, and physical properties relevant to the performance of engagements; and defines the scope of internal audit activities. Final approval of the internal audit charter resides with the board.*

**1000.A1** – The nature of assurance services provided to the organization must be defined in the internal audit charter. If assurances are to be provided to parties outside the organization, the nature of these assurances must also be defined in the internal audit charter.

**1000.C1** – The nature of consulting services must be defined in the internal audit charter.

### **1010 – Recognition of the Definition of Internal Auditing, the Code of Ethics, and the Standards in the Internal Audit Charter**

The mandatory nature of the Definition of Internal Auditing, the Code of Ethics, and the *Standards* must be recognized in the internal audit charter. The chief audit executive should discuss the Definition of Internal Auditing, the Code of Ethics, and the *Standards* with senior management and the board.

### **1100 – Independence and Objectivity**

The internal audit activity must be independent, and internal auditors must be objective in performing their work.

#### **Interpretation:**

*Independence is the freedom from conditions that threaten the ability of the internal audit activity to carry out internal audit responsibilities in an unbiased manner. To achieve the degree of independence necessary to effectively carry out the responsibilities of the internal audit activity, the chief audit executive has direct and unrestricted access to senior management and the board. This can be achieved through a dual-reporting relationship. Threats to independence must be managed at the individual auditor, engagement, functional, and organizational levels. Objectivity is an unbiased mental attitude that allows internal auditors to perform engagements in such a manner that they believe in their work product and that no quality compromises are made. Objectivity requires that internal auditors do not subordinate their judgment on audit matters to others. Threats to objectivity must be managed at the individual auditor, engagement, functional, and organizational levels.*

### **1110 – Organizational Independence**

The chief audit executive must report to a level within the organization that allows the internal audit activity to fulfill its responsibilities. The chief audit executive must confirm to the board, at least annually, the organizational independence of the internal audit activity.

#### **Interpretation:**

*Organizational independence is effectively achieved when the chief audit executive reports functionally to the board. Examples of functional reporting to the board involve the board:*

- *Approving the internal audit charter;*
- *Approving the risk based internal audit plan;*
- *Approving the internal audit budget and resource plan;*
- *Receiving communications from the chief audit executive on the internal audit activity's performance relative to its plan and other matters;*
- *Approving decisions regarding the appointment and removal of the chief audit executive;*
- *Approving the remuneration of the chief audit executive; and*



- *Making appropriate inquiries of management and the chief audit executive to determine whether there are inappropriate scope or resource limitations.*

**1110.A1** – The internal audit activity must be free from interference in determining the scope of internal auditing, performing work, and communicating results.

#### **1111 – Direct Interaction with the Board**

The chief audit executive must communicate and interact directly with the board.

#### **1120 – Individual Objectivity**

Internal auditors must have an impartial, unbiased attitude and avoid any conflict of interest.

##### **Interpretation:**

*Conflict of interest is a situation in which an internal auditor, who is in a position of trust, has a competing professional or personal interest. Such competing interests can make it difficult to fulfill his or her duties impartially. A conflict of interest exists even if no unethical or improper act results. A conflict of interest can create an appearance of impropriety that can undermine confidence in the internal auditor, the internal audit activity, and the profession. A conflict of interest could impair an individual's ability to perform his or her duties and responsibilities objectively.*

#### **1130 – Impairment to Independence or Objectivity**

If independence or objectivity is impaired in fact or appearance, the details of the impairment must be disclosed to appropriate parties. The nature of the disclosure will depend upon the impairment.

##### **Interpretation:**

*Impairment to organizational independence and individual objectivity may include, but is not limited to, personal conflict of interest, scope limitations, restrictions on access to records, personnel, and properties, and resource limitations, such as funding.*

*The determination of appropriate parties to which the details of an impairment to independence or objectivity must be disclosed is dependent upon the expectations of the internal audit activity's and the chief audit executive's responsibilities to senior management and the board as described in the internal audit charter, as well as the nature of the impairment.*

**1130.A1** – Internal auditors must refrain from assessing specific operations for which they were previously responsible. Objectivity is presumed to be impaired if an internal auditor provides assurance services for an activity for which the internal auditor had responsibility within the previous year.

**1130.A2** – Assurance engagements for functions over which the chief audit executive has responsibility must be overseen by a party outside the internal audit activity.

**1130.C1** – Internal auditors may provide consulting services relating to operations for which they had previous responsibilities.

**1130.C2** – If internal auditors have potential impairments to independence or objectivity relating to

proposed consulting services, disclosure must be made to the engagement client prior to accepting the engagement.

## **1200 – Proficiency and Due Professional Care**

Engagements must be performed with proficiency and due professional care.

### **1210 – Proficiency**

Internal auditors must possess the knowledge, skills, and other competencies needed to perform their individual responsibilities. The internal audit activity collectively must possess or obtain the knowledge, skills, and other competencies needed to perform its responsibilities.

#### **Interpretation:**

*Knowledge, skills, and other competencies is a collective term that refers to the professional proficiency required of internal auditors to effectively carry out their professional responsibilities. Internal auditors are encouraged to demonstrate their proficiency by obtaining appropriate professional certifications and qualifications, such as the Certified Internal Auditor designation and other designations offered by The Institute of Internal Auditors and other appropriate professional organizations.*

**1210.A1** – The chief audit executive must obtain competent advice and assistance if the internal auditors lack the knowledge, skills, or other competencies needed to perform all or part of the engagement.

**1210.A2** – Internal auditors must have sufficient knowledge to evaluate the risk of fraud and the manner in which it is managed by the organization, but are not expected to have the expertise of a person whose primary responsibility is detecting and investigating fraud.

**1210.A3** – Internal auditors must have sufficient knowledge of key information technology risks and controls and available technology-based audit techniques to perform their assigned work. However, not all internal auditors are expected to have the expertise of an internal auditor whose primary responsibility is information technology auditing.

**1210.C1** – The chief audit executive must decline the consulting engagement or obtain competent advice and assistance if the internal auditors lack the knowledge, skills, or other competencies needed to perform all or part of the engagement.

### **1220 – Due Professional Care**

Internal auditors must apply the care and skill expected of a reasonably prudent and competent internal auditor. Due professional care does not imply infallibility.

**1220.A1** – Internal auditors must exercise due professional care by considering the:

- Extent of work needed to achieve the engagement’s objectives;
- Relative complexity, materiality, or significance of matters to which assurance procedures are applied;
- Adequacy and effectiveness of governance, risk management, and control processes;

- Probability of significant errors, fraud, or noncompliance; and
- Cost of assurance in relation to potential benefits.

**1220.A2** – In exercising due professional care internal auditors must consider the use of technology-based audit and other data analysis techniques.

**1220.A3** – Internal auditors must be alert to the significant risks that might affect objectives, operations, or resources. However, assurance procedures alone, even when performed with due professional care, do not guarantee that all significant risks will be identified.

**1220.C1** – Internal auditors must exercise due professional care during a consulting engagement by considering the:

- Needs and expectations of clients, including the nature, timing, and communication of engagement results;
- Relative complexity and extent of work needed to achieve the engagement’s objectives; and
- Cost of the consulting engagement in relation to potential benefits.

### **1230 – Continuing Professional Development**

Internal auditors must enhance their knowledge, skills, and other competencies through continuing professional development.

### **1300 – Quality Assurance and Improvement Program**

The chief audit executive must develop and maintain a quality assurance and improvement program that covers all aspects of the internal audit activity.

#### **Interpretation:**

*A quality assurance and improvement program is designed to enable an evaluation of the internal audit activity’s conformance with the Definition of Internal Auditing and the Standards and an evaluation of whether internal auditors apply the Code of Ethics. The program also assesses the efficiency and effectiveness of the internal audit activity and identifies opportunities for improvement.*

### **1310 – Requirements of the Quality Assurance and Improvement Program**

The quality assurance and improvement program must include both internal and external assessments.

### **1311 – Internal Assessments**

Internal assessments must include:

- Ongoing monitoring of the performance of the internal audit activity; and
- Periodic self-assessments or assessments by other persons within the organization with sufficient knowledge of internal audit practices.

#### **Interpretation:**

*Ongoing monitoring is an integral part of the day-to-day supervision, review, and measurement of the internal audit activity. Ongoing monitoring is incorporated into the routine policies and practices used to manage the internal audit activity and uses processes, tools, and information considered*

*necessary to evaluate conformance with the Definition of Internal Auditing, the Code of Ethics, and the Standards.*

*Periodic assessments are conducted to evaluate conformance with the Definition of Internal Auditing, the Code of Ethics, and the Standards.*

*Sufficient knowledge of internal audit practices requires at least an understanding of all elements of the International Professional Practices Framework.*

### **1312 - External Assessments**

External assessments must be conducted at least once every five years by a qualified, independent assessor or assessment team from outside the organization. The chief audit executive must discuss with the board:

- The form and frequency of external assessment; and
- The qualifications and independence of the external assessor or assessment team, including any potential conflict of interest.

#### **Interpretation:**

*External assessments can be in the form of a full external assessment, or a self-assessment with independent external validation.*

*A qualified assessor or assessment team demonstrates competence in two areas: the professional practice of internal auditing and the external assessment process. Competence can be demonstrated through a mixture of experience and theoretical learning. Experience gained in organizations of similar size, complexity, sector or industry, and technical issues is more valuable than less relevant experience. In the case of an assessment team, not all members of the team need to have all the competencies; it is the team as a whole that is qualified. The chief audit executive uses professional judgment when assessing whether an assessor or assessment team demonstrates sufficient competence to be qualified.*

*An independent assessor or assessment team means not having either a real or an apparent conflict of interest and not being a part of, or under the control of, the organization to which the internal audit activity belongs.*

### **1320 – Reporting on the Quality Assurance and Improvement Program**

The chief audit executive must communicate the results of the quality assurance and improvement program to senior management and the board.

#### **Interpretation:**

*The form, content, and frequency of communicating the results of the quality assurance and improvement program is established through discussions with senior management and the board and considers the responsibilities of the internal audit activity and chief audit executive as contained in the internal audit charter. To demonstrate conformance with the Definition of Internal Auditing, the Code of Ethics, and the Standards, the results of external and periodic internal assessments are communicated upon completion of such assessments and the results of ongoing monitoring are communicated at least annually. The results include the assessor's or assessment team's evaluation with respect to the degree of conformance.*

### **1321 – Use of “Conforms with the International Standards for the Professional Practice of Internal**

## **Auditing”**

The chief audit executive may state that the internal audit activity conforms with the *International Standards for the Professional Practice of Internal Auditing* only if the results of the quality assurance and improvement program support this statement.

### **Interpretation:**

*The internal audit activity conforms with the Standards when it achieves the outcomes described in the Definition of Internal Auditing, Code of Ethics, and Standards. The results of the quality assurance and improvement program include the results of both internal and external assessments. All internal audit activities will have the results of internal assessments. Internal audit activities in existence for at least five years will also have the results of external assessments.*

### **1322 – Disclosure of Nonconformance**

When nonconformance with the Definition of Internal Auditing, the Code of Ethics, or the *Standards* impacts the overall scope or operation of the internal audit activity, the chief audit executive must disclose the nonconformance and the impact to senior management and the board.

### **International Standards for the Professional Practice of Internal Auditing (Standards)**

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## **Performance Standards**

### **2000 – Managing the Internal Audit Activity**

The chief audit executive must effectively manage the internal audit activity to ensure it adds value to the organization.

### **Interpretation:**

*The internal audit activity is effectively managed when:*

- *The results of the internal audit activity’s work achieve the purpose and responsibility included in the internal audit charter;*
- *The internal audit activity conforms with the Definition of Internal Auditing and the Standards;*  
*and*
- *The individuals who are part of the internal audit activity demonstrate conformance with the Code of Ethics and the Standards.*

*The internal audit activity adds value to the organization (and its stakeholders) when it provides objective and relevant assurance, and contributes to the effectiveness and efficiency of governance, risk management, and control processes.*

### **2010 – Planning**

The chief audit executive must establish a risk-based plan to determine the priorities of the internal audit activity, consistent with the organization’s goals.

### **Interpretation:**

*The chief audit executive is responsible for developing a risk-based plan. The chief audit executive takes into account the organization's risk management framework, including using risk appetite levels set by management for the different activities or parts of the organization. If a framework does not exist, the chief audit executive uses his/her own judgment of risks after consideration of input from senior management and the board. The chief audit executive must review and adjust the plan, as necessary, in response to changes in the organization's business, risks, operations, programs, systems, and controls.*

**2010.A1** – The internal audit activity's plan of engagements must be based on a documented risk assessment, undertaken at least annually. The input of senior management and the board must be considered in this process.

**2010.A2** – The chief audit executive must identify and consider the expectations of senior management, the board, and other stakeholders for internal audit opinions and other conclusions.

**2010.C1** – The chief audit executive should consider accepting proposed consulting engagements based on the engagement's potential to improve management of risks, add value, and improve the organization's operations. Accepted engagements must be included in the plan.

#### **2020 – Communication and Approval**

The chief audit executive must communicate the internal audit activity's plans and resource requirements, including significant interim changes, to senior management and the board for review and approval. The chief audit executive must also communicate the impact of resource limitations.

#### **2030 – Resource Management**

The chief audit executive must ensure that internal audit resources are appropriate, sufficient, and effectively deployed to achieve the approved plan.

#### **Interpretation:**

*Appropriate refers to the mix of knowledge, skills, and other competencies needed to perform the plan. Sufficient refers to the quantity of resources needed to accomplish the plan. Resources are effectively deployed when they are used in a way that optimizes the achievement of the approved plan.*

#### **2040 – Policies and Procedures**

The chief audit executive must establish policies and procedures to guide the internal audit activity.

#### **Interpretation:**

*The form and content of policies and procedures are dependent upon the size and structure of the internal audit activity and the complexity of its work.*

## **2050 – Coordination**

The chief audit executive should share information and coordinate activities with other internal and external providers of assurance and consulting services to ensure proper coverage and minimize duplication of efforts.

## **2060 – Reporting to Senior Management and the Board**

The chief audit executive must report periodically to senior management and the board on the internal audit activity's purpose, authority, responsibility, and performance relative to its plan. Reporting must also include significant risk exposures and control issues, including fraud risks, governance issues, and other matters needed or requested by senior management and the board.

### **Interpretation:**

*The frequency and content of reporting are determined in discussion with senior management and the board and depend on the importance of the information to be communicated and the urgency of the related actions to be taken by senior management or the board.*

## **2070 – External Service Provider and Organizational Responsibility for Internal Auditing**

When an external service provider serves as the internal audit activity, the provider must make the organization aware that the organization has the responsibility for maintaining an effective internal audit activity.

### **Interpretation**

*This responsibility is demonstrated through the quality assurance and improvement program which assesses conformance with the Definition of Internal Auditing, the Code of Ethics, and the Standards.*

## **2100 – Nature of Work**

The internal audit activity must evaluate and contribute to the improvement of governance, risk management, and control processes using a systematic and disciplined approach.

## **2110 – Governance**

The internal audit activity must assess and make appropriate recommendations for improving the governance process in its accomplishment of the following objectives:

- Promoting appropriate ethics and values within the organization;
- Ensuring effective organizational performance management and accountability;
- Communicating risk and control information to appropriate areas of the organization; and
- Coordinating the activities of and communicating information among the board, external and internal auditors, and management.

**2110.A1** – The internal audit activity must evaluate the design, implementation, and effectiveness of the organization's ethics-related objectives, programs, and activities.

**2110.A2** – The internal audit activity must assess whether the information technology governance of the organization supports the organization's strategies and objectives.

## **2120 – Risk Management**

The internal audit activity must evaluate the effectiveness and contribute to the improvement of risk management processes.

**Interpretation:** *Determining whether risk management processes are effective is a judgment resulting from the internal auditor's assessment that:*

- *Organizational objectives support and align with the organization's mission;*
- *Significant risks are identified and assessed;*
- *Appropriate risk responses are selected that align risks with the organization's risk appetite; and*
- *Relevant risk information is captured and communicated in a timely manner across the organization, enabling staff, management, and the board to carry out their responsibilities.*

*The internal audit activity may gather the information to support this assessment during multiple engagements. The results of these engagements, when viewed together, provide an understanding of the organization's risk management processes and their effectiveness.*

*Risk management processes are monitored through ongoing management activities, separate evaluations, or both.*

**2120.A1** – The internal audit activity must evaluate risk exposures relating to the organization's governance, operations, and information systems regarding the:

- Achievement of the organization's strategic objectives;
- Reliability and integrity of financial and operational information;
- Effectiveness and efficiency of operations and programs;
- Safeguarding of assets; and
- Compliance with laws, regulations, policies, procedures, and contracts.

**2120.A2** – The internal audit activity must evaluate the potential for the occurrence of fraud and how the organization manages fraud risk.

**2120.C1** – During consulting engagements, internal auditors must address risk consistent with the engagement's objectives and be alert to the existence of other significant risks.

**2120.C2** – Internal auditors must incorporate knowledge of risks gained from consulting engagements into their evaluation of the organization's risk management processes.

**2120.C3** – When assisting management in establishing or improving risk management processes, internal auditors must refrain from assuming any management responsibility by actually managing risks.

## **2130 – Control**

The internal audit activity must assist the organization in maintaining effective controls by evaluating their effectiveness and efficiency and by promoting continuous improvement.

**2130.A1** – The internal audit activity must evaluate the adequacy and effectiveness of controls in responding to risks within the organization's governance, operations, and information systems



regarding the:

- Achievement of the organization’s strategic objectives;
- Reliability and integrity of financial and operational information;
- Effectiveness and efficiency of operations and programs;
- Safeguarding of assets; and
- Compliance with laws, regulations, policies, procedures, and contracts.

**2130.C1** – Internal auditors must incorporate knowledge of controls gained from consulting engagements into evaluation of the organization’s control processes.

## **2200 – Engagement Planning**

Internal auditors must develop and document a plan for each engagement, including the engagement’s objectives, scope, timing, and resource allocations.

### **2201 – Planning Considerations**

In planning the engagement, internal auditors must consider:

- The objectives of the activity being reviewed and the means by which the activity controls its performance;
- The significant risks to the activity, its objectives, resources, and operations and the means by which the potential impact of risk is kept to an acceptable level;
- The adequacy and effectiveness of the activity’s governance, risk management, and control processes compared to a relevant framework or model; and
- The opportunities for making significant improvements to the activity’s governance, risk management, and control processes.

**2201.A1** – When planning an engagement for parties outside the organization, internal auditors must establish a written understanding with them about objectives, scope, respective responsibilities, and other expectations, including restrictions on distribution of the results of the engagement and access to engagement records.

**2201.C1** – Internal auditors must establish an understanding with consulting engagement clients about objectives, scope, respective responsibilities, and other client expectations. For significant engagements, this understanding must be documented.

### **2210 – Engagement Objectives**

Objectives must be established for each engagement.

**2210.A1** – Internal auditors must conduct a preliminary assessment of the risks relevant to the activity under review. Engagement objectives must reflect the results of this assessment.

**2210.A2** – Internal auditors must consider the probability of significant errors, fraud, noncompliance, and other exposures when developing the engagement objectives.

**2210.A3** – Adequate criteria are needed to evaluate governance, risk management, and controls. Internal auditors must ascertain the extent to which management and/or the board has established

adequate criteria to determine whether objectives and goals have been accomplished. If adequate, internal auditors must use such criteria in their evaluation. If inadequate, internal auditors must work with management and/or the board to develop appropriate evaluation criteria.

**2210.C1** – Consulting engagement objectives must address governance, risk management, and control processes to the extent agreed upon with the client.

**2210.C2** – Consulting engagement objectives must be consistent with the organization's values, strategies, and objectives.

### **2220 – Engagement Scope**

The established scope must be sufficient to achieve the objectives of the engagement.

**2220.A1** – The scope of the engagement must include consideration of relevant systems, records, personnel, and physical properties, including those under the control of third parties.

**2220.A2** – If significant consulting opportunities arise during an assurance engagement, a specific written understanding as to the objectives, scope, respective responsibilities, and other expectations should be reached and the results of the consulting engagement communicated in accordance with consulting standards.

**2220.C1** – In performing consulting engagements, internal auditors must ensure that the scope of the engagement is sufficient to address the agreed-upon objectives. If internal auditors develop reservations about the scope during the engagement, these reservations must be discussed with the client to determine whether to continue with the engagement.

**2220.C2** – During consulting engagements, internal auditors must address controls consistent with the engagement's objectives and be alert to significant control issues.

### **2230 – Engagement Resource Allocation**

Internal auditors must determine appropriate and sufficient resources to achieve engagement objectives based on an evaluation of the nature and complexity of each engagement, time constraints, and available resources.

### **2240 – Engagement Work Program**

Internal auditors must develop and document work programs that achieve the engagement objectives.

**2240.A1** – Work programs must include the procedures for identifying, analyzing, evaluating, and documenting information during the engagement. The work program must be approved prior to its implementation, and any adjustments approved promptly.

**2240.C1** – Work programs for consulting engagements may vary in form and content depending upon the nature of the engagement.

**2300 – Performing the Engagement**

Internal auditors must identify, analyze, evaluate, and document sufficient information to achieve the engagement's objectives.

**2310 – Identifying Information**

Internal auditors must identify sufficient, reliable, relevant, and useful information to achieve the engagement's objectives.

**Interpretation:**

*Sufficient information is factual, adequate, and convincing so that a prudent, informed person would reach the same conclusions as the auditor. Reliable information is the best attainable information through the use of appropriate engagement techniques. Relevant information supports engagement observations and recommendations and is consistent with the objectives for the engagement. Useful information helps the organization meet its goals.*

**2320 – Analysis and Evaluation**

Internal auditors must base conclusions and engagement results on appropriate analyses and evaluations.

**2330 – Documenting Information**

Internal auditors must document relevant information to support the conclusions and engagement results.

**2330.A1** – The chief audit executive must control access to engagement records. The chief audit executive must obtain the approval of senior management and/or legal counsel prior to releasing such records to external parties, as appropriate.

**2330.A2** – The chief audit executive must develop retention requirements for engagement records, regardless of the medium in which each record is stored. These retention requirements must be consistent with the organization's guidelines and any pertinent regulatory or other requirements.

**2330.C1** – The chief audit executive must develop policies governing the custody and retention of consulting engagement records, as well as their release to internal and external parties. These policies must be consistent with the organization's guidelines and any pertinent regulatory or other requirements.

**2340 – Engagement Supervision**

Engagements must be properly supervised to ensure objectives are achieved, quality is assured, and staff is developed.

**Interpretation:**

*The extent of supervision required will depend on the proficiency and experience of internal auditors and the complexity of the engagement. The chief audit executive has overall responsibility for supervising the engagement, whether performed by or for the internal audit activity, but may designate appropriately experienced members of the internal audit activity to perform the review.*

*Appropriate evidence of supervision is documented and retained.*

#### **2400 – Communicating Results**

Internal auditors must communicate the results of engagements.

#### **2410 – Criteria for Communicating**

Communications must include the engagement’s objectives and scope as well as applicable conclusions, recommendations, and action plans.

**2410.A1** - Final communication of engagement results must, where appropriate, contain the internal auditors’ opinion and/or conclusions. When issued, an opinion or conclusion must take account of the expectations of senior management, the board, and other stakeholders and must be supported by sufficient, reliable, relevant, and useful information.

**Interpretation:** *Opinions at the engagement level may be ratings, conclusions, or other descriptions of the results. Such an engagement may be in relation to controls around a specific process, risk, or business unit. The formulation of such opinions requires consideration of the engagement results and their significance.*

**2410.A2** – Internal auditors are encouraged to acknowledge satisfactory performance in engagement communications.

**2410.A3** – When releasing engagement results to parties outside the organization, the communication must include limitations on distribution and use of the results.

**2410.C1** – Communication of the progress and results of consulting engagements will vary in form and content depending upon the nature of the engagement and the needs of the client.

#### **2420 – Quality of Communications**

Communications must be accurate, objective, clear, concise, constructive, complete, and timely.

#### **Interpretation:**

*Accurate communications are free from errors and distortions and are faithful to the underlying facts. Objective communications are fair, impartial, and unbiased and are the result of a fair-minded and balanced assessment of all relevant facts and circumstances. Clear communications are easily understood and logical, avoiding unnecessary technical language and providing all significant and relevant information. Concise communications are to the point and avoid unnecessary elaboration, superfluous detail, redundancy, and wordiness. Constructive communications are helpful to the engagement client and the organization and lead to improvements where needed. Complete communications lack nothing that is essential to the target audience and include all significant and relevant information and observations to support recommendations and conclusions. Timely communications are opportune and expedient, depending on the significance of the issue, allowing management to take appropriate corrective action.*

#### **2421 – Errors and Omissions**

If a final communication contains a significant error or omission, the chief audit executive must communicate corrected information to all parties who received the original communication.

#### **2430 – Use of “Conducted in Conformance with the International Standards for the Professional Practice of Internal Auditing”**

Internal auditors may report that their engagements are “conducted in conformance with the *International Standards for the Professional Practice of Internal Auditing*”, only if the results of the quality assurance and improvement program support the statement.

#### **2431 – Engagement Disclosure of Nonconformance**

When nonconformance with the Definition of Internal Auditing, the Code of Ethics or the *Standards* impacts a specific engagement, communication of the results must disclose the:

- Principle or rule of conduct of the Code of Ethics or *Standard(s)* with which full conformance was not achieved;
- Reason(s) for nonconformance; and
- Impact of nonconformance on the engagement and the communicated engagement results.

#### **2440 – Disseminating Results**

The chief audit executive must communicate results to the appropriate parties.

##### **Interpretation:**

*The chief audit executive is responsible for reviewing and approving the final engagement communication before issuance and for deciding to whom and how it will be disseminated. When the chief audit executive delegates these duties, he or she retains overall responsibility.*

**2440.A1** – The chief audit executive is responsible for communicating the final results to parties who can ensure that the results are given due consideration.

**2440.A2** – If not otherwise mandated by legal, statutory, or regulatory requirements, prior to releasing results to parties outside the organization the chief audit executive must:

- Assess the potential risk to the organization;
- Consult with senior management and/or legal counsel as appropriate; and
- Control dissemination by restricting the use of the results.

**2440.C1** – The chief audit executive is responsible for communicating the final results of consulting engagements to clients.

**2440.C2** – During consulting engagements, governance, risk management, and control issues may be identified. Whenever these issues are significant to the organization, they must be communicated to senior management and the board.

#### **2450 – Overall Opinions**

When an overall opinion is issued, it must take into account the expectations of senior

management, the board, and other stakeholders and must be supported by sufficient, reliable, relevant, and useful information.

**Interpretation:**

*The communication will identify:*

- *The scope, including the time period to which the opinion pertains;*
- *Scope limitations;*
- *Consideration of all related projects including the reliance on other assurance providers;*
- *The risk or control framework or other criteria used as a basis for the overall opinion; and*
- *The overall opinion, judgment, or conclusion reached.*

*The reasons for an unfavorable overall opinion must be stated.*

**2500 – Monitoring Progress**

The chief audit executive must establish and maintain a system to monitor the disposition of results communicated to management.

**2500.A1** – The chief audit executive must establish a follow-up process to monitor and ensure that management actions have been effectively implemented or that senior management has accepted the risk of not taking action.

**2500.C1** – The internal audit activity must monitor the disposition of results of consulting engagements to the extent agreed upon with the client.

**2600 – Communicating the Acceptance of Risks**

When the chief audit executive concludes that management has accepted a level of risk that may be unacceptable to the organization, the chief audit executive must discuss the matter with senior management. If the chief audit executive determines that the matter has not been resolved, the chief audit executive must communicate the matter to the board.

**Interpretation:**

*The identification of risk accepted by management may be observed through an assurance or consulting engagement, monitoring progress on actions taken by management as a result of prior engagements, or other means. It is not the responsibility of the chief audit executive to resolve the risk.*

B



## Memorandum

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**DATE:** February 17, 2017  
**TO:** Members of the Audit Committee  
**FROM:** David James, CPA, Director of Internal Audit  
**SUBJECT:** **CONSIDERATION OF INTERNAL AUDIT CHARTER AND AUDIT COMMITTEE CHARTER**

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### Recommendation

Take appropriate action.

### Background/Discussion

Attached for the Committee's annual review are the Audit Committee Charter and Internal Audit Charter. Internal Audit recommends no changes to the charters. Both the Audit Committee Charter and the Internal Audit Charter were last updated in July 20, 2015.

### Submitted by:

The logo for Orange County OCSERS (Employees Retirement System) is repeated here, followed by the text "D.J. - Approved".

D.J. - Approved

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David James, CPA  
Director of Internal Audit



## Introduction

1. The Board of Retirement has established an Audit Committee to assist it in overseeing the audit function within OCERS. The Audit Committee is an advisory committee to the Board of Retirement, and its recommendations are subject to final approval by the Board. Notwithstanding the preceding sentence, with respect to those matters expressly assigned to it in this Audit Committee Charter, the Audit Committee has final authority.

## Purpose

2. The Audit Committee provides oversight of OCERS' internal and external audit activities. The Audit Committee assists the Board in ensuring the independence of the internal audit functions and ensuring that appropriate action is taken on audit recommendations. The Audit Committee helps promote and enhance effective internal controls for OCERS operations, and oversees communication between external auditors, internal auditors, and management.

## Membership

3. The Audit Committee will consist of four members of the Board of Retirement. The Board Chair will appoint members of the Audit Committee as provided in the OCERS By-Laws and designate one member to serve as the Committee Chair.

Ideally, members should have expertise in accounting, auditing, financial reporting, and internal control. Although these desired traits are not mandatory, members should be sufficiently knowledgeable about these topics to make informed decisions with the assistance of a financial expert.

## Meetings

4. The Audit Committee will meet at least quarterly, with authority to convene additional meetings as circumstances require. All Audit Committee members are expected to attend each meeting. The Director of Internal Audit will attend all Audit Committee meetings. Meeting notices will be provided to interested parties in conformance with applicable laws, regulations, customs, and practices. All meetings are subject to the Brown Act. Meeting agendas will be prepared and provided in advance to members, along with appropriate briefing materials. Minutes of meetings will be prepared. Minutes of the meeting will contain a record of persons present, decisions taken, and a high-level summary of the discussion.

## Responsibilities and Duties

5. The Audit Committee's key areas of responsibility are:
  - a. *Law and Ethics*: The Audit Committee will provide the policy and framework for compliance with laws and regulations, mechanisms for assessment of compliance, and communication with the Board on OCERS policies.
  - b. *Financial Reporting Process*: The Audit Committee will:

## Audit Committee Charter

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1. Oversee the reporting of all financial information, including reviewing with the external auditor their scope, plan, duties, responsibilities, and the timing and engagement fee of the annual financial audit;
  2. Resolve disagreements between the internal auditor, external auditor, and /or management regarding financial reporting and internal control risks identified in the audit;
  3. Review the audited financial statements with the external auditor and senior management;
  4. Review management letters with management;
  5. Review the findings or comments of regulatory agencies concerning financial statements or other information regarding OCERS;
  6. Review the external auditor's assessments of the appropriate application of accounting principles by OCERS management;
  7. Review all matters required to be disclosed by accounting standards, including significant changes in those standards; and
  8. Meet with senior management, at least annually, to discuss the effectiveness of the internal financial and operational control policies.
- c. *Oversight of the External Auditors:* The Audit Committee will:
1. Appoint, compensate, retain, and oversee the work of external auditors engaged for the purpose of issuing an independent audit report or performing other independent audits, reviews, or attest services;
  2. Select external audit services for the Comprehensive Annual Financial Report;
  3. Review the engagement of the external auditor at least every three years for performance, independence, and the impact of non-audit services; and
  4. Approve other audits, agreed upon procedures, and non-audit work to be conducted by the external auditors.
- d. *Oversight of Internal Audit:* The Audit Committee will:
1. Approve all decisions regarding the performance evaluation, appointment, or removal of the Director of Internal Audit;
  2. Approve the compensation and salary adjustments of the Director of Internal Audit;
  3. Review the charters and policies assigned to Audit Committee at least once every three years in accordance with the schedule set forth in the OCERS Charters and Policies Review Schedule and recommend the same for approval by the Board of Retirement;
  4. Review and approve the risk assessment and annual Internal Audit Plan prepared by the Director of Internal Audit;
  5. Receive and review internal and external audit reports and management responses;

## OCERS Board Charter

# Audit Committee Charter

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6. Review significant recommendations from audits during the year and management's responses, and make appropriate recommendations to the Board; and
  7. Make appropriate inquiries of the Director of Internal Audit to determine whether there is audit scope or budgetary limitations that impede the ability of the internal audit activity to carry out its responsibilities.
- e. *Internal Control and Risk Management:* The Audit Committee will review management responsibilities for:
1. The adequacy of OCERS' internal controls, including information systems;
  2. Material risks facing OCERS and management's actions to minimize risk;
  3. Risks from external organizations such as service providers, vendors, investment managers, consultants, and plan sponsors; and
  4. Special investigations and whistleblower mechanisms. The Audit Committee can retain independent counsel, accountants, or other specialists to assist in the conduct of an investigation.

## Reporting

6. The Audit Committee will:
  - a. Report to the Board of Retirement its activities and the results of its reviews; and
  - b. Review significant changes in accounting standards, policies, or practices that may impact OCERS and report the results of that review to the Board of Retirement.

## Charter Review

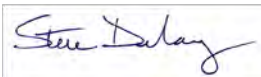
7. The Audit Committee will review this Charter at least once every three (3) years and recommend any amendments to the Board for approval as necessary to ensure that the Charter remains relevant and appropriate.

## Charter History

8. The Audit Committee Charter was adopted by the Board of Retirement on November 18, 2002, and amended on January 17, 2012, and July 20, 2015.

## Secretary's Certificate

I, the undersigned, the duly appointed Secretary of the Orange County Employees Retirement System, hereby certify the adoption of this policy.



Steve Delaney, Secretary of the Board

7/20/15

Date

## **Introduction**

The Audit Committee of OCERS oversees the Internal Audit Division under the following provisions:

## **Mission of the Internal Audit Division**

1. The mission of the Internal Audit Division is to provide reliable, independent and objective evaluations and consulting services to the Audit Committee and OCERS management relating to business and financial operations. Internal Audit assists the Board of Retirement and management to achieve their objectives by testing and reporting on the effectiveness of internal control systems, risk management, and governance processes.

## **Independence of the Director of Internal Audit**

2. The internal audit activity must be independent, and internal auditors must be objective in performing their work. Independence is the freedom from conditions that threaten the ability of Internal Audit to carry out its responsibilities in an unbiased manner.

Independence is the fundamental principle that guides the reporting relationship of the internal auditor. Internal auditor independence is strongly emphasized by authoritative bodies such as the Institute of Internal Auditors, the American Institute of Certified Public Accountants, and the Government Accountability Office. The Director of Internal Audit will follow recognized professional standards established by the Institute of Internal Auditors and be free of operational and management responsibilities that would conflict with the standards. Any potential impairment to independence will be communicated to the Audit Committee.

## **Organizational Reporting**

3. To achieve the degree of independence necessary to effectively carry out the responsibilities of the internal audit activity, the Director of Internal Audit will have direct access to senior management and the Board of Retirement. This can be achieved by a dual-reporting relationship. The Director of Internal Audit will report functionally to the Audit Committee and administratively to the Chief Executive Officer.

Functionally reporting to the Audit Committee involves the Audit Committee:

1. Reviewing and recommending changes to the Internal Audit Charter to the Board of Retirement;
2. Approving the risk-based Internal Audit plan;
3. Receiving communications from the Director of Internal Audit on the results of audit activities;
4. Approving all decisions regarding the performance evaluation, appointment, or removal of the Director of Internal Audit;
5. Approving the compensation and salary adjustments of the Director of Internal Audit;

## OCERS Board Charter

# Internal Audit Charter

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6. Making appropriate inquiries of the Director of Internal Audit to determine whether there is audit scope or budgetary limitations that impede the ability of Internal Audit to carry out its responsibilities.

Administrative reporting is the reporting relationship within the OCERS management structure that facilitates the daily operations of the internal audit activity, which includes:

1. Budgeting and management accounting;
2. Human resource administration, including personnel evaluations, leave request approval, and compensation;
3. Internal communications and information flows;
4. Administration of the Internal Audit Division's policies and procedures.

## Objectives and Scope

4. The objective of Internal Audit is to assist the Board of Retirement and management in the effective discharge of their fiduciary responsibilities. Internal Audit will furnish them with audits, analysis, evaluations, recommendations, and information. Objectives include promoting effective internal controls, helping provide assurance that the organization's assets are safeguarded; compliance is maintained with prescribed laws, Board, and management policies; the reliability and integrity of OCERS' data is maintained; and procedures and operating efficiency are enhanced.

The scope of Internal Audit includes the examination and evaluation of the adequacy of OCERS' system of internal controls, risk management and governance processes. The scope includes:

1. Reviewing the reliability and integrity of financial and business information systems, and the means used to identify, measure, classify and report such information;
2. Reviewing the systems and processes established to ensure compliance with those policies, plans, procedures, laws, and regulations that are fundamental to the operations of OCERS and could have a significant impact on operations, financial reports, and disclosures;
3. Reviewing the means of safeguarding assets and verifying the existence of such assets;
4. Monitoring and evaluating the effectiveness of OCERS' risk management systems, including identifying internal and external risks;
5. Reviewing the accuracy of data transmitted to OCERS by external parties.
6. Evaluating the quality of performance of external auditors and the degree of coordination with Internal Audit;
7. For consulting and advisory services, Internal Audit may provide assessments and advice to identify risks and internal controls for projects.

## Authority and Responsibility

5. The Internal Audit Division is established by the OCERS Board of Retirement pursuant to applicable laws and regulations, customs of corporate governance, and best practices. This Charter and all

future amendments are approved by the Audit Committee and adopted by the Board of Retirement by a majority vote.

The responsibility of OCERS Internal Audit is to serve the Board of Retirement in a manner that is consistent with the International Professional Practices Framework of the Institute of Internal Auditors, as required by California Government Code 1236. In addition, when appropriate, OCERS Internal Audit follows professional standards promulgated by the Government Accountability Office, the American Institute of Certified Public Accountants, and the Information Systems Audit and Control Association.

OCERS Internal Audit is responsible for:

1. Establishing policies and procedures for auditing, and directing and performing its technical and administrative functions;
2. Developing and executing a comprehensive audit program for the evaluation of internal controls established over OCERS' financial and business activities;
3. Preparing an annual audit plan that identifies audit projects addressing areas of highest risk to OCERS operations;
4. Assisting management in their stewardship of OCERS' trust funds and resources and their compliance with policies and procedures;
5. Recommending improvements in internal controls to help:
  - a. Safeguard trust funds and resources,
  - b. Ensure data is not compromised,
  - c. Ensure compliance with laws and regulations;
6. Reviewing procedures and records for accuracy and completeness to accomplish and report on intended objectives;
7. Producing reports on the results of audits, including findings and recommendations;
8. Following-up on actions taken to correct reported deficiencies;
9. Conducting special investigations and analysis as needed;
10. Creating and maintaining a mechanism for reporting financial statement fraud, other fraud, and inappropriate activities.

### **Internal Audit Access to Personnel and Information**

6. Except where prohibited by law, Internal Audit will have complete and unrestricted access to all OCERS personnel, records, files, information systems, and assets. The Director of Internal Audit will inform the Audit Committee whenever significant barriers or resistance to access to personnel or information occurs.

## OCERS Board Charter Internal Audit Charter

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### Charter History

7. The Audit Committee will review this Charter at least once every three (3) years and recommend any amendments to the Board for approval as necessary to ensure that the Charter remains relevant and appropriate.
8. The OCERS Internal Audit Charter was adopted by the Board of Retirement on November 18, 2002 and amended on August 19, 2008, January 17, 2012, and July 20, 2015.

### Secretary's Certificate

I, the undersigned, the duly appointed Secretary of the Orange County Employees Retirement System, hereby certify the adoption of this policy.



7/20/15

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Steve Delaney, Secretary of the Board

Date

C



## Memorandum

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**DATE:** February 17, 2017  
**TO:** Members of the Audit Committee  
**FROM:** David James, CPA, Director of Internal Audit  
**SUBJECT:** REVIEW OF THE CHIEF INVESTMENT OFFICER (CIO) POSITION

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### Recommendation

Receive and file the report *Review of the Chief Investment Officer (CIO) Position*.

### Background/Discussion

OCERS' Internal Audit Division has completed an independent review of the CIO position and its responsibilities. Internal Audit recommends that the Investment Committee and management consider changes to the CIO Charter and Investment Policy Statement. Internal Audit also recommends improvements to reporting of the CIO's investment activities to the Investment Committee. Internal Audit also recommends improved communications between the CIO, Investments' staff, and the Investments Committee.

### Submitted by:

 D.J. - Approved  
EMPLOYEES RETIREMENT SYSTEM

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David James, CPA  
Director of Internal Audit



**Review of the Chief Investment Officer (CIO)  
Position**

**Report Date: February 17, 2017**

**Internal Audit Department**

**Director of Internal Audit: David James, CPA, MBA**

**Internal Auditor: Mark Adviento, CPA**

**OCERS Internal Audit  
Review of the CIO Position  
February 17, 2017**

**Table of Contents**

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## **Executive Summary**

OCERS' Internal Audit Division has completed an independent review of the CIO position and its responsibilities. Internal Audit recommends that the Investment Committee and management consider changes to the CIO Charter and Investment Policy Statement. Internal Audit also recommends improvements to reporting of the CIO's investment activities to the Investment Committee. Internal Audit also recommends improved communications between the CIO, Investments' staff, and the Investments Committee. The details are discussed in the "Findings and Recommendations" section of the report.

## **Objective and Scope**

The objective of this review is to assess the key responsibilities of the CIO position, determine risks to meeting those responsibilities, and evaluate internal controls that mitigate those risks.

This is not an audit of past performance of OCERS' CIOs. Rather it is a review of the CIO position itself, and the risks and controls for the position.

The scope includes a review of the amendments to the CIO Charter approved by the Board of Retirement and amendments to the IPS statement approved by the Investment Committee made since 2012.

## **Review Procedures**

In carrying out this review, Internal Audit performed the following:

- Reviewed the CIO Charter, Investment Committee Charter, and Investment Policy Statement (IPS).
- Interviewed Investments' staff, the CEO, investment consultants, and the CIO of a comparable retirement system.
- Reviewed the Investment Division's monthly and quarterly reporting to the Investment Committee.
- Reviewed the job description of the CIO position.

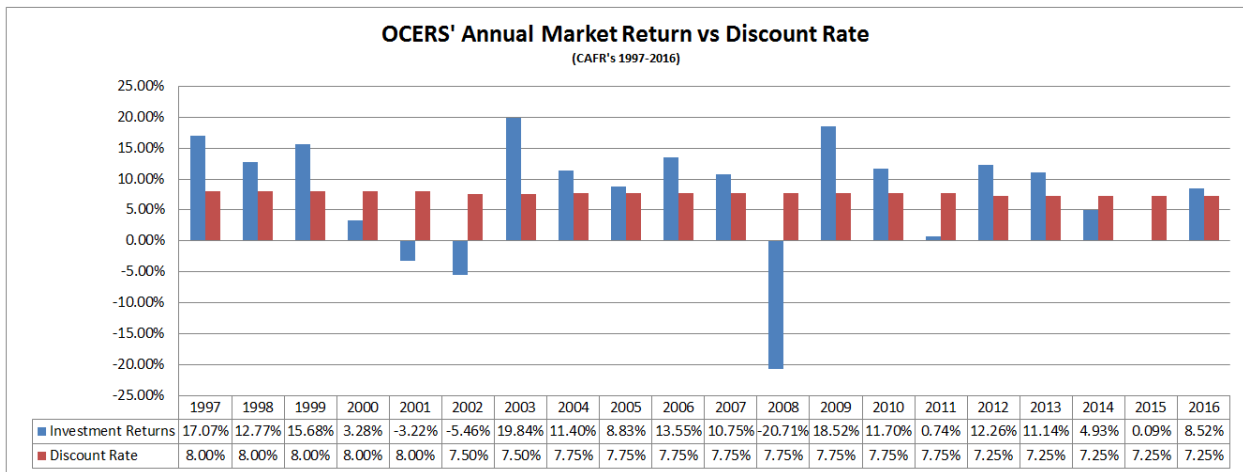
This review was conducted in accordance with generally accepted auditing standards. These standards require that auditors plan and perform the review to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on review objectives. Internal Audit believes that the evidence obtained in the course of this review provides a reasonable basis for its findings and conclusions.

## Acknowledgements

Internal Audit would like to thank OCERS' management, Investments' staff and consultants for their cooperation and time throughout this review process.

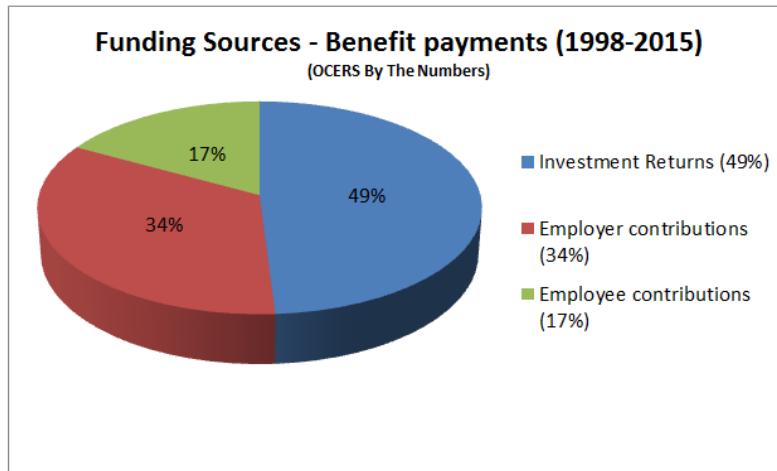
## Background

According to its charter, the Investment Committee was established by the Board to administer all matters relating to the investment of the OCERS' assets and investment management. The Investment Committee, which comprises the entire Board, *approves* policies, strategies, portfolio guidelines, and mandates to achieve investment objectives. The Investment Committee establishes policies for the CIO, Investments' staff, and investment consultants to implement Investment Committee decisions and ensure compliance with Investment Committee policies and guidelines. According to the IPS, the CIO *implements* policies, strategies, and portfolio guidelines approved by Investment Committee. For recommendations regarding the CIO Charter and the IPS, see Finding #1 on page 6.



## CIO Responsibilities and Risks

The CIO function is charged with managing the investment assets of the retirement system for the primary purpose of helping to pay member benefits. The CIO is responsible for leading the management and operation of OCERS' investment program. The position's goals include maximizing investment returns while minimizing the risk of investment losses to meet the Board approved required rate of return. The CIO function is critical to the success of the retirement system. If the CIO does not succeed in its goals and objectives of producing required returns, then overall risk for the retirement system significantly increases.



OCERS has six investment staff, including the CIO. Staff does not directly make investments. The system has assets of \$13.24 billion, with two investment consultants, and currently 68 investment managers.

The CIO skill set includes asset allocation, investment manager selection, implementation of investment strategy, reporting to the Investment Committee, keeping the Investment Committee appropriately informed about the current status of investments, managing Investments' staff, working with investment consultants, performing investment analysis, carrying out due diligence, and Investments Committee education.

Key CIO responsibilities and risks addressed include:

- The CIO reviews asset allocations and authorizes rebalancing as needed according to investments policy. This addresses the risk that values of asset classes may not match the approved asset class allocation, which may prevent the portfolio from achieving expected and planned results.
- The CIO monitors investment fees. The risk addressed is that excessive, unexpected, or unknown fees could prevent OCERS from achieving its investment objectives as mandated by the Investment Committee.
- The CIO contracts with fund managers, and reviews and signs those contracts. The risk addressed is that contract terms may be unfavorable to OCERS or prevent OCERS from achieving its investment objectives.
- The CIO conducts and reviews staff's on-site due diligence of investment managers. The risk addressed is that if adequate due diligence is not done, investment managers may not perform as expected. (*See Internal Audit's report **Audit of OCERS' Due Diligence Process**, August 2015, for risks and controls related to this function. Our report found that OCERS has adequate controls over the due diligence process. However, Internal Audit recommended improvements to the process, such as the hiring an operational due diligence vendor.*)

- The CIO reviews and approves all fund transfers such as investment funding, rebalancing, and withdrawal in writing before forwarding to the custodian bank for execution. The risk addressed is unauthorized movement of funds. (See *Internal Audit's report **Audit of OCERS' Bank Wire and ACH Transfer Process**, November 2016, for risks and controls related to this function. Our report found that OCERS has adequate controls over both manual and automated procedures required for a wire transfer. However, Internal Audit recommended improvements to the staff review over wire transfers related to the funding of new investment managers and investment portfolio rebalancing, as well as other control improvements.*)
- Transactions such as cash and securities transfers are initiated by staff, approved by the CIO or CEO, and executed by Finance. Transactions such as capital calls are initiated by staff, approved by the CIO or Director in Investment Operations or Investment Officer, and executed by Finance. This separation of duties allows for controls to help prevent errors, collusion, or fraud.

### **Internal Controls Related to CIO Functions**

In addition to the internal controls described above, OCERS has functioning internal controls related to the key responsibilities carried out by the CIO. They include:

- The CIO Charter defines the CIO's responsibilities and authority. All charters and policies are reviewed at least every three years by the Board.
- The Investment Committee Charter defines the Committee's responsibilities and authority.
- The IPS guides the Investment Committee and management in handling investment activities. The IPS defines investment objectives, policies, strategies, risk tolerance, decision making process, and asset class allocation.
- The Investment Committee members, CIO, CEO, and investment consultants are fiduciaries, and by law, must discharge their duties with respect to the system solely in the interest of, and for the exclusive purposes of providing benefits to, members of the system and their beneficiaries.
- The Board adopted a due diligence policy to discharge the fiduciary responsibilities of the Investment Committee.
- The Manager Monitoring Subcommittee meets with each investment manager at least once every three years to review performance.
- There are numerous desk procedures within the Investments Division and cross-departmental procedures with the Finance Division to provide internal controls for the movement of cash, account openings, and performance reporting to the Investment Committee.

## **Communications with the Board**

Board members' time and attention should be considered by the CIO as a precious resource. Therefore the CIO should focus on communication of long-term goals and growth of the system, as determined by the Board, to provide sufficient funds to pay future benefits. The CIO should first keep the Investments Committee informed about the asset allocation status and risk of the portfolio, secondly on cash on hand to make benefit payments, and third about new investments and opportunities.

Ideally the CIO will keep the focus on an investments strategy that is long-term in nature, such as 20 years or longer, as considered appropriate by the trustees. The CIO should emphasize macro risk factors, such as asset allocation and asset-liability matching.

As such, the Investment Committee needs fuller explanation and context for cash transfers described in the monthly Portfolio Activity Report and their possible effects on compliance with the asset allocation, as well as with any tactical trading decisions made by the CIO, and compliance with OCERS' Investment policies. For recommendations regarding further reporting to the Investment Committee, see Finding #2 on page 8.

## **Investments' Staff Support of CIO**

The Investments Division has a staff of six, including the CIO. The staff does not directly make trades and investments, but implements investments strategy. Given the volume of information to process and report to the Investment Committee, transactions to approve, fees to monitor, with investments in 68 funds, the staff should be fully utilized to also prepare support and analysis for investment decisions and to present information and recommendations to the Investment Committee. For recommendations regarding Investments' staff management, see Finding #3 on page 9.



## Findings and Recommendations

### Finding #1 – Amendments to CIO Duties in the IPS and CIO Charter

On January 25, 2017, the Investment Committee voted to remove several substantive changes made to the IPA since 2012, which had effectively expanded the Investment Committee's provision of discretion to make investment decisions to the CIO position.

There are two sections in the CIO Charter that are not clear in regards to the CIO's review of investment performance and an Investments Division Staff requirement to adhere to the Chartered Financial Analyst (CFA) Institute's Code of Ethics and Standards of Professional Conduct.

### Recommendation (Significant)

In light of OCERS' long-held view that the Investment Committee "has the sole authority over the investment portfolio," the Investment Committee should also consider reviewing the following amendments to the IPS for consistency with the Committee members' views regarding the CIO's responsibilities.

1. The IPS was amended in February 2015 to delegate to the CIO "extraordinary risk reduction and liquidation." Internal Audit recommends the Investment Committee consider deleting all or part of this section, depending on the Committee's view of the degree of flexibility to allow the CIO. In particular, for item b) below regarding hedge funds, the Committee may wish to leave this item in place.

f) Extraordinary risk-reduction and liquidation protocols

i. When developing market events or trends present a cogent reason to exit or modify a strategy to de-risk the portfolio, the CIO, in consultation with staff, the responsible consultant, and the CEO, is authorized take the following tactical actions:

a) Currency hedges - The CIO is authorized to liquidate or reduce currency hedges when developing market events or trends present an imminent risk or reason to exit or modify a strategy.

b) Hedge funds - The CIO may liquidate, redeem or reduce a hedge fund position between meetings of the Committee if timely action is deemed to be in OCERS' best interest. A full redemption shall require the concurring opinion of the responsible consultant.

c) Cash overlay - The CIO may liquidate all or an at-risk component of the cash overlay if extraordinary market conditions would favor higher cash exposure to protect capital.

ii. Before taking such extraordinary tactical actions, the CIO is expected to confer with staff, relevant consultants, the CEO, the risk advisor and, to the extent they are reasonably accessible and such consultation can be completed on a timely basis without jeopardizing the portfolio, the Committee Chair and Vice Chair. Such actions by the CIO shall be reported as soon as reasonably practicable to the Committee Chair and Vice Chair (if prior consultation does not take place) and at the next scheduled meeting of the Investment Committee.

iii. The CIO and CEO may jointly request a special meeting of the Investment Committee if extreme market conditions or extraordinary circumstances arise that compel an inter-sessional decision, deliberation, or guidance by the Committee.

2. For the section below, the Investment Committee should consider adding a specific definition of “long-term,” such as 20 years, 30 years, or 50 years. This would help direct the CIO to focus on presenting to the Investment Committee material affecting the long-term investment objectives of the system.

## II. Statement of Objectives

### 2. The long-term performance objective for the portfolio...

#### **From the CIO Charter:**

3. In section 2.e., the Investment Committee should consider deleting “If applicable” from the statement.

If applicable, maintain commitment to the Chartered Financial Analyst (CFA) Institute’s Code of Ethics and Standards of Professional Conduct.

This assumes the Committee wants Investments staff to follow the CFA Code of ethics. Alternatively, the reference can be deleted.

4. In section 4.d., the CIO Charter says:

The CIO will... review the investment performance of the staff, the consultants, investment managers, and custodian.

The CIO should review the investment performance of the Plan and its managers, but consultants and staff do not have investment performance to review. The CIO should monitor the investment performance and risk levels of

the investment program, the component asset classes, and the individual portfolios.

## **Finding #2 – Activity Reporting to the Investment Committee**

The Investment Committee needs fuller explanation and context for cash transfers described in the monthly Portfolio Activity Report and their possible effects on compliance with the asset allocation. For example, the September 2014 Portfolio Activity Report describes a liquidation of \$40 million from the JP Morgan Global Equities Portfolio. In January 2015, it was reported that OCERS transferred \$25 million to the same fund. The JP Morgan fund increased 7.7% during this five month period. However, the Investment Committee was not provided necessary context to understand why these two related transactions were executed by the CIO.

If the CIO engages in tactical trading or timing of transactions, the Investment Committee should fully understand and approve such actions, and be informed about the progress of such actions by staff. For example, in January 2015, the Investment Committee approved a yen hedge on a notional value of approximately \$90 million. Rather than a single entry point for the hedge, the hedge had multiple entry points starting from January 28 through March 25, 2015. The futures contracts for the yen were sold at prices ranging from 117.7216 to 121.109362. Although there was not an instruction from the Committee about when to reduce or liquidate the hedge, the Committee was not regularly informed about the status of such tactical actions until they were closed out by staff.

## **Recommendations (Significant)**

1. A report should be presented monthly to the Investment Committee on actions taken by the CIO and Investments staff regarding compliance with Investments' policies. This monthly report should be prepared independently by OCERS' investment consultant, Meketa.

The report should describe clearly and adequately all items completed by Investments' staff under delegated authority. The report should describe the investment, amount involved, and reference the delegation. OCERS should formally track all delegations approved by the Committee. The report should also summarize investment proposal activity.

Policy exceptions should be tracked monthly. Reporting should reference which policy section is effected, describe the exception, and resolution or next steps. This reporting should continue to the Investment Committee until the exception is completed.

The report should include investment transactions by investment category such as purchases, sales, contributions, distributions, or changes in market value.

See Appendix A on page 12 for an example of the report.

2. In the Portfolio Activity Report, Investments' staff should explain changes in funding for individual managers so that the Investment Committee can better understand the reasons those changes were implemented by staff.

Monthly reporting should be developed or highlighted to show the month-to-month effects of any "extraordinary risk-reduction, liquidation, and portfolio management protocols" enacted by the CIO, as is currently authorized by the IPS to ensure a complete accounting of such actions to the Investment Committee. Such protocols currently delegated to the CIO by the IPS include:

- Currency - liquidate or reduce currency hedges when developing market events or trends present an imminent risk or reason to exit or modify a strategy.
- Hedge Funds - liquidate, redeem or reduce a hedge fund position between meetings of the Committee if timely action is deemed to be in OCERS' best interest. A full redemption shall require the concurring opinion of the responsible consultant.
- Cash Overlay - liquidate all or an at-risk component of the cash overlay if extraordinary market conditions would favor higher cash exposure to protect capital.

### **Finding #3 – The CIO and Investments' Staff**

The Investments Division has a staff of six, including the CIO. The staff does not directly make trades and investments, but implements investments strategy. The division has a large volume of information to process and report to the Investment Committee, transactions to approve, and fees to monitor, with investments in 68 funds. We found that the CIO position could more fully utilize staff to assist with investments recommendations and presenting recommendations to the Investment Committee.

### **Recommendation (Minor)**

The Investment Committee should encourage the CIO to have frequent communication with Investment's staff, involve staff in supporting any recommendations to the Investment Committee, and have staff present recommendations to the Committee in various circumstances. Staff should be involved and voice their views regarding

important recommendations made to the Investment Committee. Analysis by staff should be used to help support all important recommendations. The entire department should function as a team with frequent communication between staff and the CIO.

Finding #	Findings	Rec #	Recommendations
1	Since 2012, several substantive amendments have been made to the Investment Policy Statement and CIO Charter, some of which expanded the Investment Committee's provision of discretion to make investment decisions to the CIO position.	1	<b>(Significant)</b> The Investment Committee should consider reviewing amendments to the Investment Policy Statement and CIO Charter for consistency with the Committee members' views regarding the CIO's responsibilities.
2	The Investment Committee needs fuller explanation and context for cash transfers described in the monthly Portfolio Activity Report and their possible effects on compliance with the asset allocation. If the CIO engages in tactical trading or timing of transactions, the Investment Committee should fully understand and approve such actions, and be informed about the progress of such actions by staff.	2	<b>(Significant)</b> A report should be presented monthly to the Investment Committee on actions taken by the CIO and Investments' staff regarding compliance with Investments' policies. This monthly report should be prepared independently by OCERS' investment consultant, Meketa.  In the Portfolio Activity Report, Investments staff should explain changes in funding for individual managers so that the Investment Committee can better understand the reasons those changes were implemented by staff.
3	The CIO position could more fully utilize staff to assist with investments recommendations and presenting recommendations to the Investment Committee.	3	<b>(Minor)</b> The Investment Committee should encourage the CIO to have frequent communication with Investment's staff, involve staff in supporting any recommendations to the Investment Committee, and have staff present recommendations to the Committee in various

			circumstances. Staff should be involved and voice their views regarding important recommendations made to the Investment Committee.
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**Report Item Classifications**

For reporting our audit findings and recommendations, we classify the report items in three categories:

**Critical** - a control deficiency that is a critical exception to a business process or goal. Management should address immediately.

**Significant** - a significant deficiency in the design or operation of internal controls. Management should address promptly with corrective action.

**Minor** – will meaningfully enhance the design or operation of specific internal controls or improve upon a general business process. Management should address in a reasonable amount of time.

## Appendix A: Sample Investment Compliance Report to the Investment Committee

### 1. Items Completed Under Delegated Authority

<i>Program Area</i>	<i>Name of Investment</i>	<i>\$ Commitment</i>	<i>Initial Funding Date</i>	<i>Complies with Delegation #</i>
Private Equity	Sample	\$	Oct-2016	INV-001

### 2. Investment Proposal Activity Summary

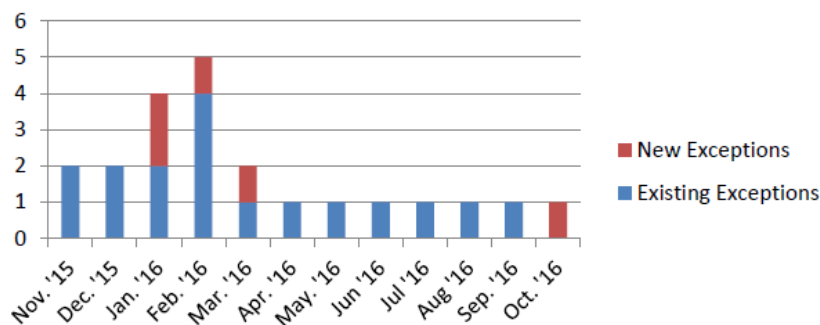
	Private Equity	Infrastructure	Real Estate	Total
Start of Month Proposals				
New Proposals During the Month				
Decisions During the Month				
End of Month Proposals				

### 3. Policy Exceptions

According to policy requirements, the following is a summary of investment policy exceptions as reported by the Investment Office program areas. The following program areas had no exceptions to report for the month:

- Private Equity
- Diversified Credit
- Absolute Return
- Real Estate
- Asset Allocation and Risk Management
- Investment Risk and Performance

### Number of Monthly Policy Exceptions



<i>Program Area or Asset Class</i>	<i>Event Date</i>	<i>Resolution Date</i>	<i>Policy</i>	<i>Exception Description</i>	<i>Event Description and Resolution or Next Steps</i>

**4. Investment Transactions**

	<b>Public Markets</b>	<b>Private Markets</b>	<b>Total Fund</b>
<b>Beginning Market Value</b>			
<b>Contributions</b>			
<b>Distributions</b>			
<b>Other Changes in MV</b>			
<b>Ending Market Value</b>			



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## Memorandum

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**DATE:** February 17, 2017  
**TO:** Members of the Audit Committee  
**FROM:** David James, CPA, Director of Internal Audit  
**SUBJECT:** RFP FOR AN ACTUARIAL FIRM TO PERFORM AN AUDIT OF OCERS' CONSULTING ACTUARY

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### Recommendation

Approve the RFP for an actuarial firm to perform an audit of OCERS' consulting actuary.

### Background/Discussion

Attached is an RFP inviting proposals from actuarial firms familiar with public employee retirement systems to perform an audit of OCERS' current consulting actuary, The Segal Company.

The audit is part of OCERS' regular cycle of performing audits of its consulting actuary every five years. Segal has acted as OCERS consulting actuary since 2004. The most recent audit was completed in 2012 by Milliman.

The audit will determine the accuracy of the December 31, 2015 valuation performed by Segal. The audit will also assess the actuarial assumptions and funding methodologies used, including a comparison to industry standards. The purpose of the audit is to provide an opinion regarding the reasonableness and accuracy of the actuarial assumptions, actuarial cost methods, valuation results, and contribution rates.

The audit will be a full replication parallel valuation audit, including a full re-run of the December 31, 2015 actuarial valuation and a review of detailed output on certain select test lives from the valuation group.

The full replication parallel valuation should allow the auditing firm to determine whether:

1. The current valuation system used by Segal is accurately applying the assumptions as stated and is accurately valuing the appropriate benefits;
2. The current valuation system used by Segal is properly allocating the present value of benefits between normal cost and actuarial accrued liability; and
3. The current valuation system used by Segal is adding together liabilities appropriately for each decrement, for each member, and over the entire population so that there is reasonable assurance that no segment of the population is being ignored and no particular liabilities are being omitted.

## Memorandum

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The proposed Schedule of Events is:

Deliverable	Date	Time
Release of RFP	3/1/17	
Questions From Vendors Due	3/15/17	5 p.m. (Pacific Time Zone)
Answers to Vendor Questions Posted	3/22/17	
RFP Submission Deadline	4/3/17	5 p.m. (Pacific Time Zone)
OCERS Review of RFP Submissions	4/14/17	
Vendor Interviews (est.)	5/1/17	
Vendor Selection (est.)	5/1/17	
Project Commencement (est.)	5/3/17	
Project Conclusion (est.)	9/29/17	

**Submitted by:**



D.J. - Approved

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David James, CPA  
 Director of Internal Audit

Actuarial Audit

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# Request for Proposal

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*February 2017*



Orange County Employees Retirement System (OCERS)  
2223 E Wellington Avenue Suite 100  
Santa Ana, CA 92701 USA  
1-(714)-558-6200  
<http://www.ocers.org>

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## Section 1: Introduction

The Orange County Employees Retirement System (OCERS) was established in 1945 under the provisions of the County Employees Retirement Law of 1937, and provides members with retirement, disability, death, and cost-of-living benefits. There are approximately 40,000 members served by OCERS, of which over 14,000 are retirees. The Board of Retirement consists of nine members, four of whom are appointed by the County's Board of Supervisors, four who are elected by the active members of OCERS, and one, the County Treasurer, who serves as an ex officio member. There is also one elected alternate member. The Board of Retirement is responsible for establishing policies, regulations and guidelines for the investment of the assets of the pension fund. OCERS has one physical location with approximately 70 employees spread throughout the following departments:

- ▶ Administrative Services
- ▶ Communications
- ▶ Executive
- ▶ Finance
- ▶ Information Technology
- ▶ Internal Audit
- ▶ Investments
- ▶ Legal
- ▶ Member Services

## Section 2: Project Background

The Orange County Employees Retirement System ("OCERS") invites proposals from actuarial firms familiar with public employee retirement systems to perform an audit of OCERS current consulting actuary - The Segal Company ("Segal").

The audit is part of OCERS' regular cycle of performing audits of its consulting actuary every five years.

Segal has acted as OCERS consulting actuary since 2004. The most recent audit was completed in 2012.

## Section 3: General Information

All terms, conditions, requirements and procedures included in the RFP must be met for a response to be qualified as responsive. A submission that fails to meet any material term, condition, requirement or procedure of this RFP may be disqualified. OCERS reserves the right to waive or permit cure of non-material errors or omissions. OCERS reserves the right to modify, amend, or cancel the terms of the RFP at any time. All responses must be submitted in accordance with the specific terms of this RFP. The submission requirements for this RFP are set forth below. A proposal shall constitute an irrevocable offer for 90 business days following the deadline for submission. Reference to a certain number of days in this RFP shall mean business days unless otherwise specified.

## Section 4: Proposed Scope of Work

The audit will determine the accuracy of the December 31, 2015 valuation performed by Segal.

The audit will also assess the actuarial assumptions and funding methodologies used, including a comparison to industry standards. The purpose of the audit is to provide an opinion regarding the reasonableness and accuracy of the actuarial assumptions, actuarial cost methods, valuation results, and contribution rates.

The audit will be a full replication parallel valuation audit, including a full re-run of the December 31, 2015 actuarial valuation and a review of detailed output on certain select test lives from the valuation group.

The audit will not include a parallel experience analysis. Rather, the audit will focus on comparing OCERS' assumptions to industry norms as well as reviewing the structure and application of the assumptions based upon the test lives.

The review of actuarial methods should be based on industry standards as well as the auditing firm's experience with similar retirement systems.

The full replication parallel valuation, complimented by review of test lives, should allow the auditing firm to determine whether:

1. The current valuation system used by Segal is accurately applying the assumptions as stated and is accurately valuing the appropriate benefits;
2. The current valuation system used by Segal is properly allocating the present value of benefits between normal cost and actuarial accrued liability; and
3. The current valuation system used by Segal is adding together liabilities appropriately for each decrement, for each member, and over the entire population so that there is reasonable assurance that no segment of the population is being ignored and no particular liabilities are being omitted.

## Section 5: OCERS' Point of Contact

From the date of issuance of this RFP until the selection of a vendor is completed and announced, vendors are not permitted to communicate, for any reason, with any OCERS staff member or Board Member regarding this procurement, except through the Point of Contact named herein. For violation of this provision, OCERS shall reserve the right to disqualify the offending vendor from further participation in this procurement.

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### The Point of Contact for questions and all matters relating to this RFP is:

<b>Name:</b>	David James
<b>Title:</b>	Director of Internal Audit
<b>Address:</b>	OCERS 2223 E Wellington Ave., Suite 100 Santa Ana, CA 92701
<b>Telephone:</b>	(714) 569-4895
<b>Email:</b>	<a href="mailto:Djames@ocers.org">Djames@ocers.org</a>



## Section 6: Vendor Questions Regarding RFP

Vendors may submit questions regarding this RFP in writing to the Point of Contact listed in *Section 5* through 5 p.m. (Pacific Time Zone) on **March 15, 2017**. Email is the preferred method of communication. All written questions must include the name of the firm and the person submitting the question(s). A compilation of all questions and answers, along with any RFP addenda, will be posted on OCERS' website, [www.ocers.org](http://www.ocers.org), no later than 5 p.m. (Pacific Time Zone) on **March 22, 2017**.

## Section 7: Vendor Response

It is the responsibility of the vendor to ensure that the proposal arrives on or before the specified time and date. Failure to comply with this provision will result in disqualification of the RFP response.

Proposals must be submitted to OCERS by 5 p.m. (Pacific Time Zone) on **April 3, 2017**. Make sure the point of contact name is included in the address.

Submit five hard copies to the address noted in *Section 5*. In addition, email an electronic copy in Microsoft Word or Adobe Acrobat PDF format to the email address noted in *Section 5*.

Note that vendor responses will be subject to disclosure to the public upon written request under the California Public Records Act. See *Section 14: Notice Regarding the California Public Records Act and the Brown Act* later in this document for additional information.

## Section 8: Consulting Services Proposal

Proposals must include the following information:

1. A description of your firm including location, number of years in business and scope of services.
2. A description of your firm's financial stability and economic capability to demonstrate the likelihood of completing/supporting the project. In addition, submit copies of any pertinent licenses required to deliver your company's product or service.
3. A recommendation of services to provide OCERS with a fair, cost effective and quality product package.
4. Details illustrating how and why your company will best serve OCERS.
5. A copy of your company's standard professional services contract.
6. A named Project Lead who has demonstrated successful management of at least one project of similar size and scope; should the Project Lead become unavailable at any point in the project, his or her replacement must be mutually agreed upon by OCERS and your company.
7. Names and qualifications of fully trained and qualified staff that may be assigned to OCERS; should any team member become unavailable at any point in the project, his or her replacement must be mutually agreed upon by OCERS and your company.

Additionally, the proposal submission should indicate if the firm meets all of the following minimum qualifications to the satisfaction of the OCERS review panel in order to be considered. Failure to meet any of the minimum qualifications will result in immediate rejection of a respondent's proposal.

1. As of April 3, 2017, the respondent must be a professional actuarial services firm providing actuarial valuations, actuarial experience analysis, actuarial auditing, and pension consulting services for a minimum on one year.

2. As of April 3, 2017, the respondent must be a legal business entity licensed to do business in California.
3. Within the past five years, a respondent must have conducted at least one actuarial valuation and at least one actuarial experience analysis for a retirement system with a population in excess of 10,000 retired, active, and deferred members and at least one actuarial valuation and at least one actuarial experience analysis for a retirement system with assets in excess of one billion dollars at the time the valuation and analysis was performed. The retirement systems evaluated must be defined benefit plans that provide ancillary death and disability benefits. Respondents may use one or up to four valuations and analyses to meet this criteria.
4. Respondent must document in writing any pending litigation and litigation that has been settled or had a judgment issued within the three years preceding April 3, 2017 brought against the respondent by any person or entity for fraud, malpractice, misrepresentation (intentional or negligent), negligence, or similar cause of action.

In addition to certifying the above, respondents shall provide three (3) client references. One reference must be a defined benefit retirement system with a population in excess of 10,000 retired, active, and deferred members and assets in excess of \$1 billion for whom the respondent has provided professional actuary and consulting services with the past five years.

## **Section 9: Review and Evaluation of Proposals**

OCERS will convene a review panel consisting of OCERS Board of Retirement Audit Committee members, the Chief Executive Officer and the Director of Internal Audit to evaluate all proposals and develop recommendations. One or more of the respondents may be requested to make an oral presentation to the committee.

## **Section 10: Right to Reject Proposal**

By submitting a proposal, vendors acknowledge that they have read this RFP, understand it, and agree to be bound by its requirements unless clearly and specifically noted in the response submitted. OCERS reserves the right without prejudice to reject any and all responses. OCERS reserves the right to modify the terms and requirements of this RFP. Any such changes or corrections will be posted on OCERS' website, available at [www.ocers.org](http://www.ocers.org).

## **Section 11: Incomplete Responses**

If the information in the firm's response is deemed to be insufficient for evaluation, OCERS reserves the right to request additional information or to reject the submittal outright. False, incomplete or unresponsive statements in connection with a submittal may be sufficient for its rejection. The selection of the fulfillment of the requirements will be determined by OCERS and such judgment shall be final.

## Section 12: Schedule of Events

OCERS reserves the right to modify this schedule at any time.

Deliverable	Date	Time
Release of RFP	3/1/17	
Questions From Vendors Due	3/15/17	5 p.m. (Pacific Time Zone)
Answers to Vendor Questions Posted	3/22/17	
RFP Submission Deadline	4/3/17	5 p.m. (Pacific Time Zone)
OCERS Review of RFP Submissions	4/14/17	
Vendor Interviews (est.)	5/1/17	
Vendor Selection (est.)	5/1/17	
Project Commencement (est.)	5/3/17	
Project Conclusion (est.)	9/29/17	

## Section 13: Addenda

OCERS may modify the RFP prior to the date fixed for submission by posting, mailing, emailing or faxing an addendum to the bidders known to be interested in submitting a proposal. If any bidder determines that an addendum unnecessarily restricts its ability to bid, it must notify OCERS in writing no later than three days before the deadline for submitting proposals. Failure of a bidder to receive or acknowledge receipt of any addendum shall not relieve the bidder of the responsibility for complying with the terms thereof.

## Section 14: Notice Regarding the California Public Records Act and the Brown Act

The proposal your firm submits in response to this RFP will become the exclusive property of OCERS. It will not be returned to you, and it will be subject to public disclosure pursuant to the California Public Records Act (California Government Code Sections 6250 et. seq., the "Act"). The Act provides generally that all records relating to a public agency's business are open to public inspection and copying, unless specifically exempted under one of several exemptions set forth in the Act.

If you believe that any portion of your proposal is exempt from public disclosure under the Act, such portion must be marked "TRADE SECRET," "CONFIDENTIAL," or "PROPRIETARY." OCERS will deny public disclosure of any portions so designated, provided that such designation is, in OCERS' reasonable discretion, in accordance with applicable law. Proposals marked "TRADE SECRET," "CONFIDENTIAL," or "PROPRIETARY" in their entirety will not be honored, and OCERS will not deny public disclosure of all or any portion of proposals so marked. By submitting a proposal with specifically selected portions marked "TRADE SECRET," "CONFIDENTIAL," or "PROPRIETARY" you represent you have a good faith belief that such material is exempt from disclosure under the Act, and you agree to reimburse OCERS for, and to indemnify, defend

and hold harmless OCERS, its officers, fiduciaries, employees and agents from and against: (a) any and all claims, damages, losses, liabilities, suits, judgments, fines, penalties, costs and expenses including, without limitation, attorneys' fees, expenses and court costs of any nature whatsoever (collectively, "Claims") arising from or relating to OCERS' non-disclosure of any such designated portions of your proposal; and (b) any and all Claims arising from or relating to OCERS' public disclosure of any such designated portions of your proposal if OCERS reasonably determines disclosure is deemed required by law, or if disclosure is ordered by a court of competent jurisdiction.

In addition to the foregoing, OCERS Board and committee meetings are subject to California open-meeting requirements set forth in the Ralph M. Brown Act (Gov. Code §§ 54950-54962) (the "Brown Act"). Your proposal and/or contract (if your firm is selected) may be presented or discussed at a public meeting of the OCERS Board of Retirement (or at a Board committee meeting). Among other things, that means that, regardless of whether you mark portions of your proposal as "TRADE SECRET," "CONFIDENTIAL," or "PROPRIETARY," that information may be discussed or presented at a meeting that is open to the public under the Brown Act.

OCERS appreciates your time and looks forward to receiving your proposal.

All RFP packages should be submitted to:  
Orange County Employees Retirement System  
Attention: **David James, Director of Internal Audit**  
2223 E Wellington Ave., Suite 100  
Santa Ana, CA 92701

E

## Memorandum

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**DATE:** February 17, 2017  
**TO:** Members of the Audit Committee  
**FROM:** David James, CPA, Director of Internal Audit  
**SUBJECT:** REVIEW OF 2016 AUDIT PLAN

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### Recommendation

Receive and file the *2016 Audit Plan*.

### Background/Discussion

Attached is the 2016 Audit Plan with the status of audits and hours applied in 2016.

The audits completed were:

- **Private Equity Review:** Review of private equity firm for operations and expenses. Internal Audit recommended Investments provide Finance with expected management fees and Finance compare these fees against statements, and Finance ensure State Street includes stated fees in information for journal entries.
- **Death Comparison Audit:** Review membership data for deaths not reported to OCERS. Internal Audit recommended OCERS download member deaths from Small World and compare with V3's membership data, and improve data security controls.
- **Wire Transfer Audit:** Audit to ensure OCERS' wire transfers are properly authorized. Internal Audit recommended that before sending a wire request to State Street to fund a new manager or rebalance the investment portfolio, Investments obtain approval from authorized initiators in Finance.
- **Service Credit Purchases Audit:** Review contracts for accuracy and completeness, and adequate supporting documentation. Internal Audit recommended recommended OCERS implement work in process summary reporting and improve service buyback datasheet.
- **Benefit Setup Audit:** Audit a sample of benefit setups with the new procedures and V3. Internal Audit recommended that V3's electronic retirement workflow process be uniformly used by all staff for each benefit setup.
- **Plan Sponsor Review for 2016:** Annual update of Plan Sponsor report to assess the financial conditions of OCERS' plan sponsors, and their ability to continue to meet their obligations to OCERS and to continue to make contributions to the plan.

The audits continued to 2017 were:

- **CIO Position Review:** Review CIO position's internal controls and risks.
- **San Juan Capistrano Payroll Transmittal Audit:** Review payroll transmittals and employee data.
- **V3 Data Conversion Audit:** Review of data used in system conversion from PensionGold to V3.

## Memorandum

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- **Reciprocity Claims Audit:** Review reciprocity claims for accuracy, completeness, and supporting documentation.
- **OCFA Payroll Transmittal Audit:** Review payroll transmittals and employee data.

Non-Audit projects performed in 2016 include:

- **Risk and Control Matrix:** Review and update Risk and Control Matrix.
- **2016 Risk Assessment and 2016 Audit Plan:** Annual preparation of the risk assessment and Audit Plan.
- Miscellaneous investigations of reports to the hotline reporting system.

### Submitted by:

ORANGE COUNTY  
**OCERS** D.J. - Approved  
EMPLOYEES RETIREMENT SYSTEM

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David James, CPA  
Director of Internal Audit

**Orange County Employees Retirement System  
Internal Audit Division  
2016 Internal Audit Plan**

Audit Activity	Description	Priority (A, B, or C)	Planned Hours - Original Budget	Revised Hours	Actual Hours as of 12/31/16	Comments	No. of Findings
<b>Internal Audits</b>							
Private Equity Review	Review private equity firm for operations and expenses.	B	200		200	Completed in January 2016.	2 - "Significant" 2 - "Minor"
Plan Sponsor Review	Annual update of Plan Sponsor report.	B	0		46	Completed in January 2016.	-
Death Comparison Audit	Review membership data for deaths not yet reported to OCERS.	B	200		212	Completed in July 2016.	6 - "Significant" 1 - "Minor"
Benefit Setup Audit	Audit a sample of benefit setups with the new procedures and V3.	B	300		316	Completed in July 2016.	2 - "Significant"
Wire Transfer Audit	Audit to ensure OCERS' wire transfers are properly authorized.	A	0	300	299	Completed November 2016. Audit added to Audit Plan in July 2016.	5 - "Significant"
Service Credit Purchases Audit	Review contracts for accuracy and completeness, and adequate supporting documentation.	B	300		264	Completed November 2016.	2 - "Minor"
San Juan Capistrano Payroll Transmittal	Review payroll transmittals and employee data.	B	0	200	229	Fieldwork complete. Awaiting management response.	4 - "Significant"
V3 Data Conversion Audit	Review of certain key data used in system conversion from PensionGold to V3.	A	400		355	Fieldwork complete.	-
Reciprocity Claims Audit	Review reciprocity claims for accuracy, completeness, and supporting documentation.	B	250		49	Audit in progress.	-
OCFA Payroll Transmittal	Review payroll transmittals and employee data.	B	200	0	0	Audit delayed until 2017.	-
Asset Allocation	Review procedures for asset allocation.	B	300	0	0	Audit cancelled.	-
CIO Position Review	Review CIO position internal controls and risks.	A	0		0	Added to Audit Plan in December 2016.	2 - "Significant" 1 - "Minor"



**Orange County Employees Retirement System  
Internal Audit Division  
2016 Internal Audit Plan**

Audit Activity	Description	Priority (A, B, or C)	Planned Hours - Original Budget	Revised Hours	Actual Hours as of 12/31/16	Comments
	<b>Internal Audits Subtotal</b>		2,150		1,970	<b>21 - "Significant" 6 - "Minor"</b>

**Orange County Employees Retirement System  
Internal Audit Division  
2016 Internal Audit Plan**

Audit Activity	Description	Priority (A, B, or C)	Planned Hours - Original Budget	Revised Hours	Actual Hours as of 12/31/16	Comments
<b>Non-Audit Projects</b>						
Miscellaneous Investigations	Use of hotline reporting system.	B	50		43	Includes member ID fraud investigation.
Risk and Control Matrix	Review and update Risk and Control Matrix.	A	60		30	Completed.
Risk Assessment and Audit Plan	Annual preparation of the Audit Plan, updates to the current Audit Plan.	A	65		64	Completed.
	<b>Non-Audit Projects Subtotal</b>		175		137	
<b>Administration</b>						
Board and Committee Meetings	Board meetings, Audit Committee, Investment Committee, Governance Committee.	A	300		230	Includes preparation time for meetings.
General Administration	Attending staff and other meetings, administrative duties.	B	935		1,207	Includes various ad hoc projects.
	<b>Administration Subtotal</b>		1,235		1,437	
	<b>Total Hours</b>		<b>3,560</b>		<b>3,544</b>	

**Orange County Employees Retirement System  
Internal Audit Division  
2016 Internal Audit Plan**

Audit Activity	Description	Priority (A, B, or C)	Planned Hours - Original Budget	Revised Hours	Actual Hours as of 12/31/16	Comments
<b>Other</b>						
Miscellaneous Leave	Holidays, Sick Leave, Time off, etc.		432		454	
Training / Conferences	Required to maintain CPA certification. SACRS, APPFA.		168		162	
Total Hours off			600		616	
	<b>Total Hours Available for Two Auditors</b>		<b>4,160</b>		<b>4,160</b>	

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## Memorandum

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**DATE:** February 17, 2017  
**TO:** Members of the Audit Committee  
**FROM:** David James, CPA, Director of Internal Audit  
**SUBJECT:** **CONSIDERATION OF 2017 RISK ASSESSMENT AND 2017 AUDIT PLAN**

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### **Recommendation**

Approve the *2017 Risk Assessment and 2017 Audit Plan*.

### **Background/Discussion**

Internal Audit has completed the annual risk assessment process and the 2017 Audit Plan. Attached are the 2017 Risk Assessment and the proposed 2017 Audit Plan with estimated hours.

### **Risk Assessment Process**

It is the responsibility of OCERS' management to identify, assess, and manage risk. Risks are events, actions, or inactions that could cause key business objectives to not be achieved. To mitigate and manage these risks, OCERS' management implements internal controls, plans for disruptions, develops risk management programs, and engages in risk mitigation programs. It is Internal Audit's responsibility to facilitate management's identification and assessment of risk, and to monitor and report on how well risks are being managed. We used the objectives of the Strategic Plan and the Business Plan as guidance in assessing risks to OCERS' programs and processes.

### **Risk Assessment Methodology**

Internal Audit established the structure of the risk assessment by identifying key programs, projects, and processes (auditable entities). We then identified the following categories of risk:

1. Materiality / Financial Impact / Compliance – The magnitude of financial exposure, the degree of regulatory oversight, possible financial penalties.
2. Strategic / Operational Impact – The significance of this process to OCERS' strategic success, impact of process disruption.
3. Change / Stability – How much the process has been altered and the change of personnel carrying out the process.
4. Complexity of Operations or Regulations – The number of individuals, entities, and processes involved, and the degree to which professional judgment or technical expertise is applied.
5. Political / Reputation – The degree of public interest and awareness, the visibility of the process to the media.
6. Last Audit: Time and Results – The length of time since the last audit or review was conducted and the results of that audit or review.

## Memorandum

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Internal Audit then developed the following rankings for risk:

High	High to Medium	Medium	Medium to Low	Low
5	4	3	2	1

### Internal Audit Plan Development

Recognizing the extent of OCERS’ activities and the constraints of Internal Audit’s resources, Internal Audit sought to maximize its effectiveness by engaging in a risk assessment process to establish its priorities for 2017.

Although a primary factor in the development of the Audit Plan, risk assessment was not the sole factor used in the selection of audit projects for 2017. We considered the resources required to perform certain audits and the available audit staff in our audit selections to maximize the effective usage of available resources.

An audit of business continuity / disaster recovery will be performed when OCERS staff has had sufficient time to fully implement this program. The risks of OCERS’ data security are to some extent mitigated by the system penetration testing performed by a consultant. Additional audits of high risk Investments’ processes will be performed in the future as time permits.

Following are audits and projects for the 2017 Audit Plan:

- **2017 Plan Sponsor Review:** Report and presentation of plan sponsors' financial status. This review was completed in February.
- **CIO Position Review:** Review responsibilities of CIO Position. This review was completed in February.
- **San Juan Capistrano Payroll Transmittal Audit:** Review payroll transmittals and employee data. The draft report of this audit is complete, and we are awaiting a written management response.
- **V3 Data Conversion Audit:** Review key data used in system conversion from PensionGold to V3. We are awaiting a written management response.
- **Reciprocity Claims Audit:** Review reciprocity claims for accuracy and completeness, and adequate supporting documentation. Fieldwork is in progress.
- **Finance Investments Transfers Review:** Role of Investments’ staff in assessing and approving investments fundings, balancings, transactions, valuations.
- **Investments Rebalancing Review:** Review rebalancing processes.
- **Payroll Transmittal - Sheriff’s Department Audit:** Review payroll transmittals and employee data of selected plan sponsor.
- **OCFA Payroll Transmittal Audit:** Review payroll transmittals and employee data.
- **Actuarial Audit RFP:** audit of Segal's 2015 valuation.
- **Risk and Control Matrix:** Review and update Risk and Control Matrix.
- **Miscellaneous Investigations** of reports from hotline reporting system.



# Memorandum

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**Submitted by:**



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David James, CPA  
Director of Internal Audit

### Internal Audit Risk Assessment Matrix for 2017

<b>Risk Rankings</b>	High	High to Medium	Medium	Medium to Low	Low
<b>Definitions</b>	5	4	3	2	1

Division	Auditable Entity	Materiality / Financial Impact / Compliance	Strategic / Operational Impact	Change / Stability	Complexity of Operations or Regulations	Political / Reputation	Last Audit - Time and Results	Average Risk Ranking
<b>Enterprise</b>	Business continuity / disaster recovery	5	5	5	5	5	5	5.0
<b>Actuary</b>	Net Pension Liability	5	5	4	5	5	5	4.8
<b>Investments</b>	Asset allocation	5	5	5	5	4	5	4.8
<b>IT</b>	IT Systems	4	5	5	5	4	5	4.7
<b>IT</b>	Pension administration system (V3) new reports	4	5	5	5	4	5	4.7
<b>Investments</b>	Rebalancing	5	5	5	5	3	5	4.7
<b>IT</b>	Cybersecurity	5	5	5	5	5	2	4.5
<b>IT</b>	Network Security	4	5	5	5	5	3	4.5
<b>Plan Sponsors</b>	Contribution transmittals	5	5	5	3	5	3	4.3
<b>Communications</b>	Communications Technology	4	4	4	4	5	5	4.3
<b>Admin Services</b>	Succession Planning	4	5	4	3	5	5	4.3
<b>Board</b>	Ethics	4	4	3	5	5	5	4.3
<b>IT</b>	Data security with external vendors	3	3	5	5	5	5	4.3
<b>IT</b>	IT governance	3	4	5	5	4	5	4.3
<b>IT</b>	Web-based network vulnerabilities, penetration test	5	5	5	5	5	1	4.3
<b>Investments</b>	Absolute return	5	5	3	5	3	5	4.3
<b>Investments</b>	Investment manager selection, monitoring	5	5	4	3	4	5	4.3
<b>Enterprise</b>	Data privacy	4	4	4	4	5	5	4.3
<b>Member Services</b>	Benefits setup / calculations / payments	5	5	5	4	5	1	4.2
<b>Finance</b>	GASB 72: fair value measurement	4	4	4	4	4	5	4.2



**Internal Audit Risk Assessment Matrix for 2017**

Division	Auditable Entity	Materiality / Financial Impact / Compliance	Strategic / Operational Impact	Change / Stability	Complexity of Operations or Regulations	Political / Reputation	Last Audit - Time and Results	Average Risk Ranking
Finance	GASB 74 & 75: reporting post employment benefit plans	4	4	4	4	4	5	4.2
Finance	Payroll for retirees	5	4	4	4	5	3	4.2
IT	Cloud-based Systems	4	4	5	5	4	3	4.2
Investments	Due diligence	5	5	5	5	4	1	4.2
Investments	Investment consultant review	5	5	4	5	4	2	4.2
Investments	Operations of investment managers	5	5	3	5	3	4	4.2
Investments	Infrastructure Investments	4	4	5	4	3	5	4.2
Investments	Real estate	5	4	4	4	3	5	4.2
Member Services	Interest posting / crediting	4	4	5	3	4	5	4.2
Communications	Public Records Requests	4	4	3	3	5	5	4.0
Admin Services	Staff Turnover	4	4	5	3	3	5	4.0
Board	Governance	4	5	3	5	5	2	4.0
Investments	Fixed income	5	4	3	4	3	5	4.0
Investments	Private equity	5	4	5	5	4	1	4.0
Investments	Public equity	5	5	2	4	3	5	4.0
Investments	Risk management	4	4	4	5	4	3	4.0
Investments	Securities lending	5	4	3	4	3	5	4.0
Legal	Compliance review	4	4	3	4	4	5	4.0
Member Services	Member eligibility	4	4	4	4	4	4	4.0
Investments	Investment manager fees	5	5	4	4	4	2	4.0
Admin Services	Recruitment	3	4	5	3	3	5	3.8
Finance	Budgets	4	4	3	4	3	5	3.8
Finance	Cash management	4	4	3	4	3	5	3.8
Finance	General Ledger	3	5	3	4	3	5	3.8
Investments	Derivatives	5	5	4	5	3	1	3.8
Investments	Direct lending	5	4	5	4	4	1	3.8

### Internal Audit Risk Assessment Matrix for 2017

Division	Auditable Entity	Materiality / Financial Impact / Compliance	Strategic / Operational Impact	Change / Stability	Complexity of Operations or Regulations	Political / Reputation	Last Audit - Time and Results	Average Risk Ranking
Investments	Hedge fund / alternative manager	5	5	4	5	3	1	3.8
Legal	Record management and retention	4	4	3	3	4	5	3.8
Member Services	1099s	3	3	5	3	4	5	3.8
Member Services	Dependent eligibility	3	4	5	3	3	5	3.8
Member Services	Lump sum payments	3	3	5	3	4	5	3.8
Member Services	Member refunds	3	3	5	3	4	5	3.8
Member Services	Reciprocity	3	3	5	3	4	5	3.8
Actuary	Actuarial extract	5	4	5	4	3	1	3.7
Disability	Disability process	4	3	3	3	4	5	3.7
Enterprise	RFP process	3	3	4	3	4	5	3.7
Enterprise	Vendor contract compliance	4	4	3	3	3	5	3.7
Finance	Investment accounting, valuation	5	3	5	3	3	3	3.7
IT	Process Documentation	3	3	5	5	1	5	3.7
Investments	Accuracy of costs allocated by external managers to OCERS	4	3	3	5	2	5	3.7
Investments	Cash overlay	5	4	3	4	3	3	3.7
Investments	Cash Processing	5	4	3	4	5	1	3.7
Investments	Reporting to the Board	3	3	3	3	5	5	3.7
Member Services	IRS 415 limits calculation	3	3	5	3	3	5	3.7
Enterprise	Procurement	3	3	4	3	3	5	3.5
Enterprise	Signature authority	3	3	4	3	3	5	3.5
Finance	Accounts Payable	3	3	5	3	2	5	3.5

### Internal Audit Risk Assessment Matrix for 2017

Division	Auditable Entity	Materiality / Financial Impact / Compliance	Strategic / Operational Impact	Change / Stability	Complexity of Operations or Regulations	Political / Reputation	Last Audit - Time and Results	Average Risk Ranking
Finance	Contributions - member, employer	3	5	5	3	4	1	3.5
Finance	Financial reporting	3	4	3	4	4	3	3.5
Finance	Spreadsheet controls	3	3	3	4	3	5	3.5
Plan Sponsors	Pension Spiking (PEPRA)	3	3	5	4	5	1	3.5
Plan Sponsors	Retiree Rehires (PEPRA)	3	3	5	4	5	1	3.5
Member Services	Survivor claims	2	2	5	3	4	5	3.5
Investments	Investment reconciliations	5	5	2	3	3	2	3.3
Member Services	COLA	3	3	5	3	4	2	3.3
Investments	Investment policy compliance	5	5	2	3	3	1	3.2
Admin Services	Process Documentation	3	3	3	3	1	5	3.0
Legal	Domestic Relations Orders	2	3	2	3	3	4	2.8
Member Services	Death comparison process	2	3	5	3	3	1	2.8
Member Services	Service purchases	2	2	5	3	4	1	2.8
Investments	Personal Trading Policy compliance	2	3	3	3	4	1	2.7
Finance	Travel expenses	2	1	1	1	5	5	2.5

**Legend:**

New auditable entity added to the matrix.
Included in the 2017 Audit Plan.

**Orange County Employees Retirement System  
Internal Audit Division  
2017 Internal Audit Plan**

<b>Audit Activity</b>	<b>Description</b>	<b>Priority (A, B, or C)</b>	<b>Planned Hours - Original Budget</b>	<b>Actual Hours as of 2/17/17</b>	<b>Hours Estimated to Complete</b>	<b>Comments</b>
<b>Internal Audits</b>						
Plan Sponsor Review	Report and presentation of plan sponsors' financial status.	A	50	45	0	Completed in February.
CIO Position Review	Review responsibilities of CIO Position.	A	200	157	0	Completed in February.
San Juan Capistrano Payroll Transmittal	Review payroll transmittals and employee data.	B	50	32	18	Awaiting management response.
Reciprocity Claims Audit	Review reciprocity claims for accuracy and completeness, and adequate supporting documentation.	A	250	176	74	Fieldwork in progress.
V3 Data Conversion Audit	Review data used in system conversion from PensionGold to V3.	A	50	0		Awaiting management response.
Finance Investments Transfers Review	Role of Investments' staff in assessing and approving investments fundings, balancings, transactions, valuations.	A	300	0		
Investments Rebalancing Review	Review rebalancing processes.	A	300	0		
Payroll Transmittal - Sheriff's Dept.	Review payroll transmittals and employee data.	A	300	0		
OCFA Payroll Transmittal	Review payroll transmittals and employee data.	B	300	0		
	<b>Internal Audits Subtotal</b>		1,800	410		

**Orange County Employees Retirement System  
Internal Audit Division  
2017 Internal Audit Plan**

Audit Activity	Description	Priority (A, B, or C)	Planned Hours - Original Budget	Actual Hours as of 2/17/17	Hours Estimated to Complete	Comments
<b>Non-Audit Projects</b>						
Actuarial Audit	RFP - audit of Segal's 2015 valuation.	A	60			
Miscellaneous Investigations	Use of hotline reporting system.	B	50			
Risk and Control Matrix	Review and update Risk and Control Matrix.	A	50			
Risk Assessment and Audit Plan	Annual preparation of the Audit Plan, updates to the current Audit Plan.	A	50	37	0	Completed in January.
	<b>Non-Audit Projects Subtotal</b>		210	37		
<b>Administration</b>						
Board and Committee Meetings	Board meetings, Audit Committee, Investment Committee, Governance Committee.	A	300	18	282	Includes preparation time for meetings.
General Administration	Attending staff and other meetings, administrative duties.	B	1,250	42	1,208	Includes various ad hoc projects.
	<b>Administration Subtotal</b>		1,550	60		
	<b>Total Hours</b>		<b>3,560</b>	<b>507</b>		

**Orange County Employees Retirement System  
Internal Audit Division  
2017 Internal Audit Plan**

<b>Audit Activity</b>	<b>Description</b>	<b>Priority (A, B, or C)</b>	<b>Planned Hours - Original Budget</b>	<b>Actual Hours as of 2/17/17</b>	<b>Hours Estimated to Complete</b>	<b>Comments</b>
<b>Other</b>						
Miscellaneous Leave	Holidays, Sick Leave, Time off, etc.		432	58		
Training / Conferences	Required to maintain CPA certification. SACRS, APPFA.		168	36		
Total Hours off			600	94		
	<b>Total Hours Available for Two Auditors</b>		<b>4,160</b>	<b>601</b>		

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## Memorandum

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**DATE:** February 22, 2017  
**TO:** Members of the Audit Committee  
**FROM:** Steve Delaney, Chief Executive Officer  
**SUBJECT:** **OVERVIEW OF AUDIT COMMITTEE OVERSIGHT OF OCERS' SECURITY**

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### Recommendation

Receive and file.

### Background/Discussion

The Audit Committee Charter, Section 5, directs that the committee oversee OCERS' "internal control and risk management". One particular risk that staff routinely reported to the Audit Committee were the results of our annual "penetration test" (when we contract with an outside vendor to attempt to penetrate our computer network) to assist us in closing any weaknesses that may be identified in our information and system security efforts.

Because we did not want to give the bad guys a road map into our system, staff would prepare a high-level summary report of the results and share that with the Audit Committee in public session.

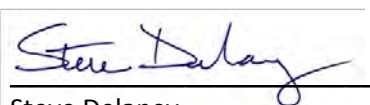
While staff continues with our annual "penetration test", somehow over the past several years the practice of bringing a summary report of the results to the Audit Committee ceased. This change in reporting process most likely occurred during the V3 Implementation.

We are back on track and will schedule a regular annual report to the Audit Committee.

On February 28, Ms. Brenda Shott will verbally review with the committee current activities of OCERS' security team.

Also on February 28, Ms. Gina Ratto will explore with the committee the process that permits the committee to go into closed session and receive a full report of any results coming out of our ongoing risk management efforts.

### Submitted by:



Steve Delaney  
Chief Executive Officer