



Continuous Audit of Final Average Salary Calculations (Q3 2022)

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Audit Objective and Scope

The objective of this audit was to provide an independent review of Final Average Salary (FAS) calculations used in new benefit payments setup by OCERS' Member Services, on a continuous basis.

In response to Internal Audit's 2020 Audits of FAS Calculations, Member Services reorganized the Retirement Program Specialist Team and modified the FAS calculation process including an updated retirement transaction excel spreadsheet as part of the Management Action Plan. The action plan was implemented in Q2 2021.

In this current audit's scope of Q3 2022, Member Services processed a total of 151 new service and disability retirement benefits. Internal Audit reviewed the FAS calculations for 40 of these benefits.

The audit was conducted in conformance with the International Standards for the Professional Practice of Internal Auditing issued by the International Internal Audit Standards Board.

Conclusion / Executive Summary

Opinion: *Satisfactory*

During our review, Internal Audit did not note any FAS calculation errors with our test sample for a 100% accuracy rate.

Background

To finalize each retiree's FAS, Member Services uses a retirement transaction Excel spreadsheet. In the spreadsheet, Member Services inputs a preliminary FAS number calculated by the pension administration system (PAS) software after reviewing it, and inputs other manually calculated pensionable pay amounts not captured or calculated by the PAS software. To calculate these amounts, the Retirement Program Specialist (RPS) must reference a variety of external data sources provided by employers, such as hourly rate history, timesheet data, reciprocal salary data, and relevant Employer MOUs. A Member Services Quality Assurance team member then reviews the final FAS calculated by the RPS.

Internal Audit independently tested 40 of the 151 FAS benefit calculations from the July through September 2022 benefit payroll months, and performed the following:

- Recalculated and traced the preliminary FAS used in the spreadsheet back to the preliminary FAS number calculated by the PAS software.

- Reviewed Member Service’s manual calculations of other pensionable pay item amounts (typically pensionable paid time off, or PTO) manually added to the preliminary FAS and the documentation used by Member Services to support their calculations.

Below is a summary of IA’s error rate noted in the current 2022 audit, plus error rates noted in prior 2020, 2021, and 2022 audits:

Quarter	Benefit Applications	Tested by Internal Audit (IA)	IA Error Count	IA Error Rate
Q1/2020	149	82	6	5.8%
Q2/2020	514	56	2	
Q3/2020	108	10	1	8.0%
Q4/2020	466	65	5	
Q2/2021	182	60	4	6.7%
Applications Subject to the Revised FAS Calculation Procedure				
Q3/2021	75	75	6	8.0%*
Q4/2021	154	134	2	1.5%*
Q1/2022	196	50	2	4.0%*
Q2/2022	607	41	1	2.4%*
Q3/2022	151	40	0	0.0%*

*Each of the quarters contained at least month with 100% accuracy

The following months were **100% accurate** in IA’s test samples:

2021 – August, October

2022 – February, April, June, July, August, September

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Categories of Observations (Control Exceptions):

Priority Observations:

These are observation(s) that represent critical exceptions to the audit objective(s) and/or business goals. Such conditions may involve either actual or potential large dollar errors or be of such a nature as to compromise OCERS' reputation or integrity. Management is expected to address Priority Observations brought to its attention immediately.

Important Observations:

These items are important to the process owner and they do impact the control environment and/or could be observations for improving the efficiency and/or effectiveness of OCERS' operations. Management is expected to address within six to twelve months.

Management's Responsibility for Internal Control

Management has primary responsibility for establishing and maintaining the internal control system. All levels of management must be involved in assessing and strengthening internal controls. Control systems shall be continuously evaluated by Management and weaknesses, when detected, must be promptly corrected. The criteria for evaluating an entity's internal control structure are the Committee of Sponsoring Organizations of the Treadway Commission (COSO) Internal Control – Integrated Framework. Our Internal Control Audit enhances and complements, but does not substitute for department management's continuing emphasis on control activities and self-assessment of control risks.

Internal Control Limitations

Because of inherent limitations in any system of internal control, errors or irregularities may nevertheless occur and not be detected. Specific examples of limitations include, but are not limited to, resource constraints, unintentional errors, management override, circumvention by collusion, and poor judgment. Also, projection of any evaluation of the system to future periods is subject to the risk that procedures may become inadequate because of changes in conditions or the degree of compliance with the procedures may deteriorate. Accordingly, our audit would not necessarily disclose all weaknesses in the department's operating procedures, accounting practices, and compliance with OCERS' policies.

Audit Report Opinions:

Satisfactory:

No issues or a limited number of “Important Observations” (typically no more than two Important Observations).

Opportunities for Improvement:

Multiple issues classified as “Important Observations” (typically two or more Important Observations) with no more than one “Priority Observations”.

Inadequate:

Usually rendered when multiple issues are classified as “Priority” ” (typically one or more Priority Observations), together with one or more other issues classified as “Important Observations”. The Priority Observations identified have a major effect on processes, plan sponsors/members, financials, and/or regulatory requirements.