

## **AGENDA ITEM DETAILS**

- Subject:** Review of Internal Audit Reports
- Qualified Domestic Relations Orders Audit
  - Alternative Investments Funding Audit
  - Status of Audit Recommendations
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As part of the approved FY21 Audit Plan, Internal Audit completed the Qualified Domestic Relations Order Audit included as Exhibit A, the Alternative Investments Funding Audit included as Exhibit B and a Status of Audit Recommendations report, included as Exhibit C.

### Qualified Domestic Relations Order Audit

Qualified Domestic Relations Orders (QDRO) are legal assignments for an alternate payee to receive a portion of benefits with respect to a member or retiree under a public retirement system.

Based on the audit scope areas reviewed, the system of internal controls provides reasonable assurance that key goals and objectives will be achieved. The audit also identified control gap corrections and improvement opportunities.

1. Establish timeliness targets for reviews (qualifications/denials) of domestic relations orders (DROs) (Moderate)
2. Refine procedures to enhance accuracy of manual calculations. (Moderate)

**Audit Objective:** To determine if benefits are processed in accordance with legal orders following a divorce or legal separation.

Sub-objectives included the following:

### **Qualification**

1. Are qualified domestic relations orders processed in accordance with laws and regulations?
2. Are affected parties provided adequate information to allow for qualification?
3. Are QDROs with pending payments prioritized for processing?

### **Benefit Estimates and Payments**

1. Are members provided complete and accurate details of their estimated QDRO related distribution?
2. Are QDRO related distributions properly determined?
3. Are QDRO related distributions remitted accurately?

### Alternative Investments Funding Audit

For alternative investments, ERS commits funds (Committed Capital) to Investment Partners for investments in private equity, private real estate, private infrastructure, private fixed income and hedge funds. ERS' Investment Partners consist of both General Partners (GP) in alternative investments and hedge fund managers. These partners select investments to pursue and determine when capital calls will occur.

Based on the audit scope areas reviewed, internal controls are effective and sustainable, and substantially address significant risks related to financial reporting reliability, operational execution, and regulatory compliance.

The organization's system of internal controls provides reasonable assurance that key goals and objectives will be achieved. The audit identified minor enhancements that would improve achievement of (control/business) objectives, but are not currently resulting in negative impacts to the organization.

**Audit Objective:** To determine if contributions and distributions of funds for ERS' alternative investments are properly accounted for and processed.

Sub-objectives included the following:

### **Processing**

1. Are funds submitted to eligible alternative investment/hedge funds?
2. Are total contributions within agreed-upon limits (capital commitments)?
3. Are capital contributions processed according to the contractual requirements?

### **Accounting**

1. Are capital contributions/distributions accurately recorded in key financial/investment systems?
2. Do fund balances accurately reflect capital contribution/distribution activity?

### Status of Audit Recommendations

Internal Audit (IA) has completed procedures to monitor and report on the status of management action plans (MAPs) to address open audit recommendations. Implementation status was based on management's self-assessment and IA's review of supporting documentation to corroborate the self-assessment. Supporting documentation included, but was not limited to, revised documented policies/procedures, worksheets, management status reports and reconciliations. The audit did not verify the effectiveness of management actions to determine if controls were working as intended. Future audit engagements in these areas will confirm the effectiveness of the controls implemented.

1. **Temporary Workers Contract Management Audit**  
Observation 1 has been implemented by revising policies and forms related to background checks to align with information security policies.
2. **Profit Share Audit**
  1. Observation 1: Implemented. Reporting periods now account for a full year of Hedge Fund profit share and continued reconciliations for Private Real Estate
  2. Observation 2: Partially implemented. An escalation process now occurs when variances exist between ERS and general partner calculations, as well as enhanced contract terms that require necessary documentation to correctly calculate the complex allocations of profit share. Some preventive controls have yet to be established in the areas of profit share calculation models and ensuring reconciling items in Private Real Estate are updated across all tracking systems.
3. **Survivor Benefits Audit –**  
Management has accepted the risk for Observation 1 related to the timeliness of lump sum benefits payments. Several factors contributed to the decision, including the significant cost to increase staffing, desire to provide all survivor benefits within the same timeframe, and reduced need to provide the benefit in seven days, given a change to the statute in January 2020 which allows beneficiaries to assign certain benefits to funeral home so there is no delay in payment of burial expenses.

ATTACHMENTS:

1. Exhibit A – Qualified Domestic Relations Order Audit
2. Exhibit B – Alternative Investments Funding Audit
3. Exhibit C – Status of Audit Recommendations
4. Slides – Internal Audit Reports