



Audit Committee Meeting
May 11, 2022



Presented for Review and Approval
August 24, 2022

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**AUDIT COMMITTEE MEETING
EMPLOYEES RETIREMENT SYSTEM OF TEXAS
May 11, 2022**

TRUSTEES PRESENT

Neika Clark, Audit Committee Chair
Brian Barth, Member
Craig Hester, Member
Dr. James Kee, Member
Catherine Melvin, Member

ERS DIRECTORS PRESENT

Porter Wilson, Executive Director
Cathy Terrell, Deputy Executive Director
Jennifer Chambers, Director of Government Relations & Special Projects
Tony Chavez, Director of Internal Audit
Bernie Hajovsky, Director of Enterprise Planning
Cynthia Hamilton, General Counsel
Robin Hardaway, Director of Customer Benefits
Shack Nail, Special Projects & Policy Advisor
Machelle Pharr, Chief Financial Officer
Gabrielle Schreiber, Director of Office of Procurement and Contract Oversight
DeeDee Sterns, Director of Human Resources
Kathryn Tesar, Director of Benefits Communications
David Veal, Chief Investment Officer

ERS STAFF PRESENT

Jason Avants, Information Systems
Raquel Colón, Investments
Kurt Cressotti, Internal Audit
Anthony Curtiss, Investments
Kelley Davenport, Executive Office
Christi Davis, Customer Benefits
Lanesia Jones, Investments
Lauren Honza, Investments
Tressie Landry, Internal Audit
Greg Magness, Internal Audit
Mike McCray, Investments
Jonathan Puckett, Internal Audit
Robert Sessa, Investments
Ariana Whaley, Government Relations & Special Projects

ALSO PRESENT

Sam Austin, NEPC

Meeting of the ERS Board of Trustees Audit Committee

1. Call Meeting of the Audit Committee to Order

Ms. Neika Clark, Chair of the Audit Committee of the Employees Retirement System of Texas (ERS), noting a quorum was present, called the meeting to order at 8:33 a.m. on Wednesday, May 11, 2022 and read the following statement:

“A public notice of the ERS Board of Trustees Audit Committee meeting containing all items on the proposed agenda was filed with the Office of the Secretary of State at 9:56 a.m. on Tuesday, May 3, 2022, as required by Chapter 551 Texas Government Code, referred to as “The Open Meetings Act.”

2. Consideration of the Minutes to the March 9, 2022 Audit Committee Meeting – (ACTION)

Chair Neika Clark opened the floor for a motion on the approval of the minutes from the March 9, 2022 ERS Audit Committee meeting.

Move that the ERS Board of Trustees Audit Committee of the Employees Retirement System of Texas approve the minutes to its meeting held on March 9, 2022.

Motion by Craig Hester, second by Catherine Melvin

Final Resolution: Motion Carries

Aye: Craig Hester, Brian Barth, Neika Clark, Jim Kee, Catherine Melvin

3. Consideration of Internal Audit Reports

Public Equity – External Advisor Program Audit

The audit objective was to determine if investments in externally advised public equity are in accordance with ERS Investment Policy.

The External Advisor Program is one of three programs within the External Public Equity Asset Composite. As of December 31, 2021 there were 15 funded advisors that managed a net asset value of \$4.4 billion. Investment advisors are procured through a process where selected advisors are placed into a pool from which they are funded.

The overall result was Needs Improvement because controls are in place to protect the assets of ERS; however, improvements are needed to assess the value added by the External Advisors. One observation was reported:

Observation 1: Process to evaluate and assess the value added by external advisors needs improvement. (Significant)

Investment benchmarks incorporated into contracts varied from those used during the selection process without documentation of the rationale for the change and the methodology used to determine the investment benchmark was inconsistent. In addition, the manager scorecard used to assess external advisors had not yet been fully developed. Monitoring calls and reviews were completed for the external advisors.

Internal Audit recommended that the External Advisor should establish criteria for assessing the performance of external advisors, establish criteria for and implement the manager scorecard and determine actions to be taken when performance does not meet established criteria.

Administrative Budgeting Audit

The audit objective was to evaluate the planning and management of the ERS Operating Budget.

The Operating Budget includes administrative costs that are not included in the Legislative Appropriations Request or other major contracts, such as investments or third-party administrative costs for benefits.

The overall result was Satisfactory because the system of controls provides reasonable assurance that key goals and objectives will be achieved. However, three observations were reported:

Observation 1: Formally establish and define costs that should be included in the Board approved Operating Budget. (Significant)

All costs are appropriately approved, however, not all costs required to deliver services to members are included in the Operating Budget. No policy has been established to define the purpose of the Operating Budget. It can either serve as a comprehensive summary in order to show total costs necessary to deliver benefits administered by the agency or as is currently, a listing of all proposed budget costs that were not previously approved by the Board (through contract awards, for instance), or appropriated by the Legislature for which the Board has no approval authority.

Internal Audit recommended that Finance work with the Board members to establish a policy that defines the purpose of the Operating Budget and decide which cost should be presented in the document.

Observation 2: Establish a linkage between organizational goals, costs and performance through enhanced performance reporting. (Moderate)

The proposed budget is presented with a focus on the agency's organizational structure, instead of a focus on the total cost of benefit delivery. Performance information highlights tasks or outputs rather than effectiveness and efficiency performance measures.

Internal Audit recommended the inclusion of effectiveness and efficiency measures in the Operating Budget as well as a presentation of the costs by major program in addition to the organizational cost breakdown. In addition, Finance should enhance the list of major projects to include expected return on investment and projected total costs.

Observation 3: Provide historical budget data (actual expenses) to help assess future spending. (Moderate)

Actual expenses are not presented with the historical budget amounts in an exhibit in the Operating Budget. In addition, forecasted amounts are used to support the proposed budget amounts, but there are no procedures to compare the forecasted amounts to the actuals (when finalized) to ensure that forecasts are accurate. Actual amounts lag the forecast by several months, so the information could include the previous year's finalized budgeted versus spent amount.

Internal Audit recommended including the actual expenses in the Operating Budget so users could see the trend of actual expenses. In addition, Finance should implement procedures to assess the variances between forecasts and actual expenses.

4. Adjournment of the Audit Committee Meeting

The Audit Committee meeting adjourned at 9:15 a.m. on Wednesday, May 11, 2022