

**County Employees Retirement System
and Kentucky Retirement Systems
Joint Audit Committee
May 25, 2023 at 10:00 a.m. Eastern Time
Live Video Conference/Facebook Live**

AGENDA

- | | | |
|-----|--|----------------------|
| 1. | Call to Order | Bill O'Mara |
| 2. | Opening Video Teleconference Statement | Legal Representative |
| 3. | Roll Call | Sherry Rankin |
| 4. | Public Comment | Sherry Rankin |
| 5. | Approval of February 28, 2023 Joint Audit Committee Minutes* | Bill O'Mara |
| 6. | Financial Reporting Updates | Michael Lamb |
| | a. Quarterly Financial Statements for Quarter Ended March 31, 2023 | |
| | i. Contribution Report | |
| | ii. Administrative Expenses | |
| 7. | Joint Audit Committee Administrative Updates | |
| | a. Information Disclosure Incidents | Carrie Bass |
| | b. Anonymous Tips | Carrie Bass |
| | c. Internal Audit Budget as of March 31, 2023 | Kristen Coffey |
| | d. Status of Current Internal Audit Projects | Kristen Coffey |
| | e. Update on Open Audit Findings/Recommendations | Kristen Coffey |
| | f. Review of Issued Reports | Kristen Coffey |
| | i. Accuracy of Information Sent to DEI | Matthew Daugherty |
| | ii. Plan Liquidity – Phase 3 | Madeline Perry |
| 8. | Update on Structure of Audit Committee | Michael Board |
| 9. | Professional Article: Crowe Horwath <i>Strengthening Corporate Governance with Internal Audit</i> [White paper] | Kristen Coffey |
| | Internal Audit Awareness Month | Madeline Perry |
| 10. | Adjourn* | Bill O'Mara |

***Action may be taken by the Joint Audit Committee**

**MINUTES OF MEETING
COUNTY EMPLOYEES RETIREMENT SYSTEM
AND KENTUCKY RETIREMENT SYSTEMS
BOARD OF TRUSTEES JOINT AUDIT COMMITTEE
FEBRUARY 28, 2023, 10:00 A.M., E.T.
VIA LIVE VIDEO TELECONFERENCE**

At the February 28, 2023 meeting of the Joint Audit Committee of the Board of Trustees of the County Employees Retirement System and the Kentucky Retirement Systems, the following Committee members were present: William O’Mara (Chair), Betty Pendergrass, Lynn Hampton, and William Summers, V. Staff members present were Rebecca Adkins, Erin Surratt, Michael Board, Victoria Hale, Michael Lamb, Connie Davis, Kristen Coffey, Madeline Perry, Matthew Daugherty, Carrie Bass, Melinda Wofford, William Prince, Steve Willer, Ann Case, Elizabeth Smith, Ashley Gabbard, Phillip Cook, Katie Park, and Sherry Rankin. Others present included CERS CEO Ed Owens, III, KRS CEO John Chilton, and Allen Norvell and Ryan Graham with Blue & Co.

Mr. O’Mara called the meeting to order.

Ms. Hale read the Opening Video Teleconference Statement.

Ms. Rankin called roll.

There being no **Public Comment**, Mr. O’Mara introduced the agenda item **Approval of Minutes – November 28, 2022** (Video 00:07:28 to 00:08:04). Ms. Hampton made a motion and was seconded by Ms. Pendergrass to approve the minutes as presented. The motion passed unanimously.

Mr. O’Mara introduced the agenda item **External Audit Update** (Video 00:08:05 to 00:23:00). Mr. Ryan Graham with Blue and Co. provided an overview of the draft GASB 68 and GASB 75 Proportionate Share Audits. Ms. Pendergrass made a motion to accept the draft GASB 68 and GASB 75 Proportionate Share Audits. The motion was seconded by Ms. Hampton and passed unanimously.

Mr. Mike Lamb, Chief Financial Officer, presented the item Updating the Audit Report Presentation for FY2023. On November 28, 2022, the Joint Audit Committee discussed the June 30, 2022, ACFR and the presentation of the financial statements. It was requested that the totals of the financial statements be edited to report totals for each retirement system. Changes in formatting were also discussed to reflect separate CERS and KRS opinions in 2023. The Committee requested that further research be conducted regarding these suggested formatting changes. Mr. Lamb provided the Joint Audit Committee with a memorandum and proposed timeline for the implementation of these requested formatting changes.

Mr. O'Mara introduced the agenda item *Financial Reporting Updates* (Video 00:23:01 to 00:46:37). Mr. Lamb reviewed the Combining Statement of Fiduciary Net Position of the Pension Funds as of December 31, 2022. Next, Mr. Lamb briefly reviewed the Combining Statement of Changes in Fiduciary Net Position of the Pension Funds for the six-month period ending December 31, 2022, Combining Statement of Fiduciary Net Position of Insurance Funds as of December 31, 2022, and the Combining Statement of Changes in Fiduciary Net Position of Insurance Funds for the six-month period ending December 31, 2022, with the Joint Audit Committee. Mr. Lamb went on to present the CERS, KERS, and SPRS Pension and Insurance Funds Contribution Reports for six-month period ending December 31, 2022. Lastly, he presented the KPPA Administrative Budget FY 2022-2023 for the six-month period ending December 31, 2022. Mr. O'Mara asked if the administrative expenses would be within budget by year-end before the reserve amount. Mr. Lamb stated that he would be able to have a better idea within the next quarter.

Ms. Connie Davis, Division Director of Accounting, presented item Fiscal Year End June 30, 2022, End of Year Audit Requirements. Ms. Davis stated that KPPA is required to submit its audited financial statements to the Legislative Research Commission (LRC), and the Auditor of Public Accounts (APA). Therefore, in accordance with Kentucky Revised Statute 45.149(2)(a), the Annual Comprehensive Financial Statements (ACFR), including the audited financial statements were electronically sent to LRC and the APA on December 8, 2022. Also, the ACFR was posted on KPPA's website. She also advised that the APA would conduct the Fiscal Year End Financial Statement Audit as required every five years.

Mr. O'Mara introduced the agenda item *Joint Audit Committee Administrative Updates* (Video 00:46:38 to 01:25:32). Ms. Carrie Bass stated that the Information Disclosure Incidents and Anonymous Tips reports would be provided and presented to the Joint Audit Committee at a future meeting. She advised that two additional employees have recently joined the KPPA Office of Legal Services and will assist in the preparation of these reports for Committee meetings.

Ms. Kristen Coffey presented the Internal Audit Budget as of December 31, 2022, Status of Current Internal Audit Projects, Open Audit Findings and Recommendations, and Review of Chase Accounts Audit. Mr. O'Mara stated that the Summary of Audit Results, item #1 Use of non-custodial accounts, has been discussed at length for about a year; therefore, he encouraged Staff to shorten the presented timetable of 12 to 24 months.

Ms. Pendergrass added that she was concerned with the timeline on a variety of items. She made the below motion in response to item, Review of Chase Accounts Audit.

Correction of key deficiencies should be a high priority for KPPA accounting, finance, and investment staff and should be accelerated to ensure accuracy of the FY 2023 external financial reports as well as efficient management and reporting for FY 2024. I move for the following timelines to facilitate upgrades and corrections:

1. Policies that need Board attention should be requested at the March and/or April 2023 Board meetings.
2. Internal controls should be designed by June 30, 2023.
3. Implementation process should be designed by September 30, 2023.
4. Final changes should be complete by December 31, 2023.
5. The CFO should provide written, monthly updates to the Joint Audit Chair with requests for special meetings as necessary to address policy questions for Trustees to resolve.

There was no second to the motion; therefore, the motion failed.

Mr. O'Mara introduced the agenda item *Professional Articles* (Video 1:25:33 to 1:27:07). Mr. Matthew Daugherty with the KPPA Division of Internal Audit presented an article entitled

American Institute of Certified Public Accountants – Evolution of Auditing: From the Traditional Approach to the Future Audit – White Paper November 2012.

There being no further business, a motion to *adjourn* was made by Ms. Pendergrass and seconded by Mr. Summers, the meeting adjourned.

The remainder of this page left blank intentionally

CERTIFICATION

I do certify that I was present at this meeting, and I have recorded above the action of the Committee on the various items considered by it at this meeting. Further, I certify that all requirements of KRS 61.805-61.850 were met in connection with this meeting.

Recording Secretary

I, as Chair of the Joint Audit Committee of the Board of Trustees of the County Employees Retirement System and the Kentucky Retirement Systems, do certify that the Minutes of the meeting held on February 28, 2023, were approved by the Joint Audit Committee on May 25, 2023.

Committee Chair

I have reviewed the Minutes of the Audit Committee Meeting on February 28, 2023, for form, content, and legality.

Executive Director
Office of Legal Services



Combining Statement of Fiduciary Net Position - Pension Funds
 As of March 31, 2023, with Comparative Totals as of March 31, 2022 (\$ in Thousands) (Unaudited)

ASSETS	CERS		KERS		SPRS	KPPA TOTAL		Percentage of Change	Note
	Nonhazardous	Hazardous	Nonhazardous	Hazardous		FY 2023	FY 2022		
CASH AND SHORT-TERM INVESTMENTS									
Cash Deposits	\$1,137	\$121	\$863	\$99	\$25	\$2,244	\$751	198.94%	1
Short-term Investments	229,862	96,223	653,139	71,204	132,907	1,183,335	1,502,663	(21.25)%	2
Total Cash and Short-term Investments	230,999	96,345	654,001	71,303	132,932	1,185,579	1,503,414	(21.14)%	
RECEIVABLES									
Accounts Receivable	66,223	22,912	88,210	4,195	5,276	186,816	175,344	6.54%	
Accounts Receivable - Investments	54,853	19,565	22,893	6,166	4,488	107,966	159,956	(32.50)%	3
Total Receivables	121,077	42,477	111,103	10,361	9,764	294,782	335,300	(12.08)%	
INVESTMENTS, AT FAIR VALUE									
Core Fixed Income	813,224	302,469	644,763	107,193	113,858	1,981,508	2,156,382	(8.11)%	
Public Equities	4,184,544	1,432,065	1,061,428	376,178	187,206	7,241,421	6,859,605	5.57%	
Private Equities	681,432	227,671	155,140	62,367	16,367	1,142,977	1,303,761	(12.33)%	4
Specialty Credit	1,739,345	597,784	606,019	180,621	94,025	3,217,794	3,078,942	4.51%	
Derivatives	986	360	769	126	135	2,375	(6,542)	(136.31)%	5
Real Return	262,663	87,071	69,014	24,154	10,045	452,947	426,266	6.26%	
Real Estate	519,206	165,278	175,894	48,159	20,857	929,393	844,242	10.09%	6
Total Investments, at Fair Value	8,201,400	2,812,697	2,713,027	798,798	442,493	14,968,414	14,662,656	2.09%	
Securities Lending Collateral Invested	198,614	68,437	79,620	20,591	13,647	380,909	463,606	(17.84)%	7
CAPITAL/INTANGIBLE ASSETS									
Capital Assets	1,701	153	929	91	11	2,885	2,885	0.00%	
Intangible Assets	9,961	827	5,920	494	100	17,301	17,301	0.00%	
Accumulated Depreciation	(1,701)	(153)	(929)	(91)	(11)	(2,885)	(2,885)	0.00%	
Accumulated Amortization	(9,931)	(826)	(5,893)	(493)	(100)	(17,242)	(16,889)	2.09%	
Total Capital Assets	30	1	27	1	-	59	412	(85.71)%	
Total Assets	8,752,120	3,019,956	3,557,778	901,053	598,836	16,829,743	16,965,387	(0.80)%	
LIABILITIES									
Accounts Payable	4,855	803	2,449	523	54	8,684	5,988	45.03%	8
Investment Accounts Payable	53,931	19,182	26,880	6,044	5,204	111,240	331,634	(66.46)%	9
Securities Lending Collateral	198,614	68,437	79,620	20,591	13,647	380,909	463,606	(17.84)%	10
Total Liabilities	257,399	88,422	108,948	27,158	18,905	500,832	801,228	(37.49)%	
Total Fiduciary Net Position Restricted for Pension Benefits	\$8,494,721	\$2,931,534	\$3,448,829	\$873,896	\$579,931	\$16,328,911	\$16,164,159	1.02%	

NOTE - Variance Explanation Differences due to rounding

- 1) The variance is a result of continuous fluctuation of deposits and transactions that flow through the cash account. As a result of an Internal Audit finding, we continue to evaluate the optimum cash balances at JP Morgan Chase.
- 2) Short term investments are primarily comprised of cash on hand at the custodial bank, the variance in the balance is a result of the cash flows of each plan.
- 3) The variance in Investment Accounts Receivable is the result of pending trades.
- 4) The decline in private equity is a result of unrealized losses and distributions. Note: KRS pension funds did not commit to any new private equity funds from 2011-2020, therefore, there are less contributions and appreciation from newer funds to offset the distributions from the older funds.
- 5) The variance in Derivatives is a result of hedging and arbitration of risk within the portfolios.
- 6) The increase in Real Estate is due to additional funding of current managers.
- 7) The variance is a result of the demand of the Securities Lending Program.
- 8) The variance in Accounts Payable is due to an increase in outstanding employer credit invoices.
- 9) The variance in Investment Accounts Payable is due to pending trades.
- 10) The variance is a result of the demand of the Securities Lending Program.



Combining Statement of Changes In Fiduciary Net Position - Pension Funds

For the nine month period ending March 31, 2023, with Comparative Totals for the nine month period ending March 31, 2022 (\$ in Thousands) (Unaudited)

	CERS	CERS	KERS	KERS	SPRS	KPPA Total		Percentage	
	Nonhazardous	Hazardous	Nonhazardous	Hazardous		FY 2023	FY 2022	of Change	Note
ADDITIONS									
Member Contributions	\$142,280	\$54,856	\$78,368	\$19,258	\$5,027	\$299,790	\$272,661	9.95%	
Employer Contributions	461,766	199,583	84,888	47,067	42,185	835,490	793,925	5.24%	
Actuarially Accrued Liability Contributions (AALC)	-	-	673,831	-	-	673,831	684,575	(1.57)%	
General Fund Appropriation	-	-	180,000	-	-	180,000	-	100.00%	1
Pension Spiking Contributions	36	150	9	29	-	224	92	142.96%	2
Health Insurance Contributions (HB1)	(18)	(20)	(9)	(4)	(6)	(57)	(2)	2,811.07%	3
Employer Cessation Contributions	-	-	-	-	-	-	50,464	(100.00)%	4
Total Contributions	604,064	254,570	1,017,088	66,350	47,207	1,989,279	1,801,715	10.41%	
INVESTMENT INCOME									
From Investing Activities									
Net Appreciation (Depreciation) in FV of Investments									
	398,006	137,055	79,039	35,879	16,785	666,764	64,955	926.51%	5
Interest/Dividends	170,462	59,311	72,470	18,928	12,806	333,976	313,891	6.40%	
Total Investing Activities Income	568,468	196,366	151,509	54,807	29,591	1,000,740	378,846		
Less: Investment Expense	36,153	12,096	10,211	3,429	1,515	63,403	53,899	17.63%	6
Less: Performance Fees	1,295	206	(264)	112	43	1,391	81,858	(98.30)%	7
Net Income from Investing Activities	531,020	184,064	141,562	51,267	28,033	935,945	243,089		
From Securities Lending Activities									
Securities Lending Income	6,223	2,173	2,039	603	343	11,380	758		
Less: Securities Lending Borrower Rebates (Income)/Expense	5,441	1,900	1,755	523	297	9,916	(960)		
Less: Securities Lending Agent Fees	117	41	43	12	7	220	257		
Net Income from Securities Lending	665	233	241	68	39	1,245	1,460	(14.72)%	8
Net Investment Income	531,685	184,296	141,803	51,334	28,072	937,191	244,549	283.23%	
Total Additions	1,135,749	438,867	1,158,891	117,684	75,279	2,926,470	2,046,264	43.02%	
DEDUCTIONS									
Benefit Payments	667,835	238,504	767,922	58,869	47,892	1,781,022	1,744,058	2.12%	
Refunds	18,054	4,217	8,845	3,058	165	34,340	32,238	6.52%	
Administrative Expenses	17,485	1,539	10,038	1,098	217	30,377	28,499	6.59%	
Total Deductions	703,374	244,260	786,805	63,025	48,274	1,845,738	1,804,795	2.27%	
Net Increase (Decrease) in Fiduciary Net Position Restricted for Pension Benefits									
	432,375	194,606	372,087	54,659	27,004	1,080,731	241,469		
Total Fiduciary Net Position Restricted for Pension Benefits									
Beginning of Period	8,062,346	2,736,928	3,076,743	819,237	552,926	15,248,180	15,922,691	(4.24)%	
End of Period	\$8,494,721	\$2,931,534	\$3,448,829	\$873,896	\$579,931	\$16,328,911	\$16,164,159	1.02%	

NOTE - Variance Explanation

Differences due to rounding.

- 1) General Fund Appropriation 3rd Quarter (KERS only): HB1 \$101,250,000; HB604 \$78,750,000;
- 2) Pension Spiking contributions increased due to an increase in KERS Hazardous and CERS Hazardous.
- 3) Health Insurance Contributions continue to fluctuate in the Pension accounts due to Tier 2 and Tier 3 retiree health insurance system costs as well as corrections being processed to previous fiscal years.
- 4) Employer Cessation payment received from Kentucky Housing Corporation FY2022.
- 5) The increase in Net Appreciation in Fair Value of Investments is the result of unrealized gains in public equity.
- 6) The increase in Investment Expense is primarily the result of increased management fees and partnership expenses for Specialty Credit.

NOTE - Variance Explanation continued on next page.

- 7) *The decrease in performance fees is the result in less than favorable market conditions causing returns to drop, impacting those fees directly related to performance most notably Private Equity, Real Estate and Specialty Credit.*
- 8) *The variance is a result of the demand of the Securities Lending Program.*



Combining Statement of Fiduciary Net Position - Insurance Funds

As of March 31, 2023, with Comparative Totals as of March 31, 2022 (\$ in Thousands) (Unaudited)

ASSETS	CERS		KERS		SPRS	KPPA Total		Percentage of Change	Note
	Nonhazardous	Hazardous	Nonhazardous	Hazardous		FY 2023	FY 2022		
CASH AND SHORT-TERM INVESTMENTS									
Cash Deposits	\$531	\$10	\$196	\$9	\$20	\$767	\$255	201.24%	1
Short-term Investments	81,259	31,774	178,246	20,172	7,343	318,793	681,607	(53.23)%	2
Total Cash and Short-term Investments	81,790	31,784	178,442	20,181	7,363	319,560	681,862	(53.13)%	
RECEIVABLES									
Accounts Receivable	11,731	3,541	13,187	570	982	30,012	35,064	(14.41)%	3
Investment Accounts Receivable	23,823	10,297	9,980	3,738	1,652	49,491	69,251	(28.53)%	4
Total Receivables	35,554	13,838	23,167	4,309	2,634	79,503	104,315	(23.79)%	
INVESTMENTS, AT FAIR VALUE									
Core Fixed Income	322,291	145,930	161,379	70,696	27,743	728,039	805,268	(9.59)%	
Public Equities	1,577,082	769,964	602,807	266,175	105,582	3,321,609	3,177,676	4.53%	
Private Equities	267,458	150,445	89,906	53,312	23,790	584,911	621,667	(5.91)%	
Specialty Credit	656,811	326,856	278,843	133,284	52,886	1,448,680	1,395,527	3.81%	
Derivatives	398	184	194	91	33	900	(2,314)	(138.88)%	5
Real Return	79,171	42,379	29,799	17,308	6,459	175,116	165,360	5.90%	
Real Estate	179,983	98,669	56,515	41,452	15,857	392,478	356,748	10.02%	6
Total Investments, at Fair Value	3,083,194	1,534,428	1,219,443	582,318	232,350	6,651,733	6,519,932	2.02%	
Securities Lending Collateral Invested	48,831	24,067	21,255	9,200	8,781	112,133	152,038	(26.25)%	7
Total Assets	3,249,369	1,604,117	1,442,307	616,008	251,128	7,162,928	7,458,147	(3.96)%	
LIABILITIES									
Accounts Payable	156	15	126	14	1	312	308	1.29%	
Investment Accounts Payable	19,692	8,972	9,973	3,764	1,642	44,043	139,255	(68.37)%	8
Securities Lending Collateral	48,831	24,067	21,255	9,200	8,781	112,133	152,038	(26.25)%	9
Total Liabilities	68,678	33,053	31,354	12,978	10,424	156,488	291,601	(46.33)%	
Total Fiduciary Net Position Restricted for OPEB	\$3,180,690	\$1,571,064	\$1,410,953	\$603,030	\$240,703	\$7,006,441	\$7,166,546	(2.23)%	

NOTE - Variance Explanation Differences due to rounding

- 1) The variance is a result of continuous fluctuation of deposits and transactions that flow through the cash account. As a result of an Internal Audit finding, we continue to evaluate the optimum cash balances at JP Morgan Chase.
- 2) Short term investments are primarily comprised of cash on hand at the custodial bank, the balance decline is the result of cash being invested.
- 3) The decrease in Accounts Receivable is due to a decrease in the member/employer month-end accrual due to the decreased insurance transfer rate.
- 4) The variance in Investment Accounts Receivable is the result of pending trades.
- 5) The variance in Derivatives is a result of hedging and arbitration of risk within the portfolios.
- 6) The increase in Real Estate is due to additional funding of current managers.
- 7) The variance is a result of the demands of the Securities Lending Program.
- 8) The variance In Investment Accounts Payable is due to pending trades.
- 9) The variance is a result of the demands of the Securities Lending Program.



Combining Statement of Changes In Fiduciary Net Position - Insurance Funds

For the nine month period ending March 31, 2023, with Comparative Totals for the nine month period ending March 31, 2022 (\$ In Thousands) (Unaudited)

	CERS Non-hazardous	CERS Hazardous	KERS Non-hazardous	KERS Hazardous	SPRS	KPPA Total		Percentage of Change	Note
						FY 2023	FY 2022		
ADDITIONS									
Employer Contributions	\$72,337	\$34,077	\$26,329	\$38	\$6,875	\$139,657	\$202,211	(30.94)%	1
Actuarially Accrued Liability Contributions (AALC)	-	-	65,748	-	-	\$65,748	\$76,233	(13.75)%	2
Medicare Drug Reimbursement	-	-	3	-	-	3	3	0.00%	
Insurance Premiums	286	(370)	49	(56)	(96)	(187)	201	(193.14)%	3
Humana Gain Share Payment	5,951	914	4,851	368	224	12,308	18,381	(33.04)%	4
Retired Re-employed Healthcare	3,599	1,178	4,232	1,046	-	10,055	9,369	7.33%	
Health Insurance Contributions (HB1)	12,600	2,952	6,111	1,158	260	23,081	20,020	15.29%	5
Employer Cessation Contributions	-	-	-	-	-	-	9,536	(100.00)%	6
Total Contributions	94,774	38,751	107,322	2,554	7,263	250,664	335,954	(25.39)%	
INVESTMENT INCOME									
From Investing Activities									
Net Appreciation (Depreciation) in FV of Investments	151,759	72,760	61,836	25,584	10,183	322,122	73,755	336.75%	7
Interest/Dividends	67,411	33,016	30,177	13,003	5,239	148,846	136,673	8.91%	
Total Investing Activities Income	219,170	105,776	92,013	38,587	15,422	470,968	210,428		
Less: Investment Expense	13,400	7,041	5,102	2,752	1,104	29,400	24,882	18.16%	8
Less: Performance Fees	65	(62)	1,315	107	17	1,443	43,500	(96.68)%	9
Net Income from Investing Activities	205,705	98,796	85,596	35,728	14,301	440,126	142,047		
From Securities Lending Activities									
Securities Lending Income	1,949	938	786	321	137	4,131	319		
Less: Securities Lending Borrower Rebates (Income)/Expense	1,686	810	673	277	118	3,564	(378)		
Less: Securities Lending Agent Fees	40	19	17	7	3	85	104		
Net Income from Securities Lending	224	108	96	37	16	482	592	(18.69)%	10
Net Investment Income	205,929	98,904	85,692	35,765	14,317	440,607	142,639	208.90%	
Total Additions	300,703	137,656	193,014	38,319	21,580	691,271	478,593	44.44%	
DEDUCTIONS									
Healthcare Premiums Subsidies	98,092	70,049	81,719	15,043	10,823	275,725	279,793	-1.45%	
Administrative Expenses	707	391	583	93	55	1,830	1,847	(0.91)%	
Self-Funded Healthcare Costs	2,437	129	1,280	56	13	3,915	4,011	(2.37)%	
Excise Tax Insurance	-	-	-	-	-	-	9	(100.00)%	11
Total Deductions	101,237	70,569	83,582	15,191	10,892	281,471	285,660	(1.47)%	
Net Increase (Decrease) in Fiduciary Net Position Restricted for OPEB	199,466	67,087	109,432	23,128	10,689	409,801	192,933		
Total Fiduciary Net Position Restricted for OPEB									
Beginning of Period	2,981,224	1,503,977	1,301,522	579,902	230,015	6,596,640	6,973,613	(5.41)%	
End of Period	\$3,180,690	\$1,571,064	\$1,410,953	\$603,030	\$240,703	\$7,006,440	\$7,166,546	(2.23)%	

NOTE - Variance Explanation. Differences due to rounding

1) Employer Contributions decreased due to a decrease in the employer insurance rate as well as the CERS/CERH correction.

NOTE - Variance Explanation. Differences due to rounding

- 2) *AALC will fluctuate year to year based on the actuarial valuation.*
- 3) *Health Insurance Premiums decreased primarily due to refunds processed to hazardous retirees for premiums paid for dependents that should have been covered by KPPA.*
- 4) *The Humana Gain Share payment will fluctuate year to year based on claims paid.*
- 5) *Health Insurance Contributions will continue to rise as Tier 2 and Tier 3 members increase.*
- 6) *Employer Cessation payment received from Kentucky Housing Corporation FY2022.*
- 7) *The increase in Net Appreciation in Fair Value of Investments is the result of unrealized gains in public equity.*
- 8) *The increase in Investment Expense is primarily the result of increased management fees and partnership expenses for Specialty Credit.*
- 9) *The decrease in performance fees is the result in less than favorable market conditions causing returns to drop, impacting those fees directly related to performance most notably Private Equity, Real Estate and Specialty Credit.*
- 10) *The variance is a result of the demand of the Securities Lending Program.*
- 11) *The Excise Tax will fluctuate based on the timing of the posting of the payment.*

Pension Funds Contribution Report

For the nine month period ending March 31, 2023, with Comparative Totals for the nine month period ending March 31, 2022 (\$ in Millions)



County Employees Retirement System

	Nonhazardous		Hazardous	
	FY23	FY22	FY23	FY22
Member Contributions	\$142.3	\$135.4	\$54.9	\$51.6
Employer Contributions	461.8	405.4	199.7	157.1
Net Investment Income	133.7	95.2	47.2	34.1
Total Inflows	737.8	636.0	301.8	242.8
Benefit Payments/Refunds	685.9	656.4	242.7	232.6
Administrative Expenses	17.5	17.0	1.5	1.5
Total Outflows	703.4	673.4	244.2	234.1
NET Contributions	34.4	(37.4)	57.6	8.7
Realized Gain/(Loss)	(25.1)	358.0	(10.3)	120.8
Unrealized Gain/(Loss)	423.1	(294.7)	147.3	(103.1)
Change in Net Position	432.4	25.9	194.6	26.4
Beginning of Period	8,062.3	8,670.7	2,736.9	2,934.4
End of Period	\$8,494.7	\$8,696.6	\$2,931.5	\$2,960.8

Differences due to rounding.

Net Contributions*	(\$99.3)	(\$132.6)	\$10.4	(\$25.4)
Cash Flow as % of Assets	(1.17)%	(1.52)%	0.35%	(0.86)%
Net Investment Income	\$133.7	\$95.2	\$47.2	\$34.1
Yield as % of Assets	1.57%	1.09%	1.61%	1.15%

**Net Contributions are less Net Investment Income.*

Pension Funds Contribution Report

For the nine month period ending March 31, 2023, with Comparative Totals for the nine month period ending March 31, 2022 (\$ in Millions)

	Kentucky Employees Retirement System				State Police Retirement System	
	Nonhazardous		Hazardous		FY23	FY22
	FY23	FY22	FY23	FY22		
Member Contributions	\$78.4	\$67.0	\$19.2	\$15.1	\$5.0	\$3.5
Employer Contributions	84.9	140.8	47.1	44.3	42.2	46.3
Actuarially Accrued Liability Contributions	673.8	684.6	-	-	-	-
Employer Cessation Contributions	-	50.4	-	-	-	-
General Fund Appropriations	180.0	-	-	-	-	-
Net Investment Income	62.8	35.8	15.5	10.4	11.3	4.2
Total Inflows	1,079.9	978.6	81.8	69.8	58.5	54.0
Benefit Payments/Refund	776.8	777.6	61.9	61.3	48.1	48.3
Administrative Expenses	10.0	8.8	1.1	1.0	0.2	0.2
Total Outflows	786.8	786.4	63.0	62.3	48.3	48.5
NET CONTRIBUTIONS	293.1	192.2	18.8	7.5	10.2	5.5
Realized Gain/(Loss)	(21.3)	93.4	(3.5)	34.5	(4.3)	10.9
Unrealized Gain/(Loss)	100.3	(110.0)	39.4	(32.5)	21.1	(12.3)
Change in Net Position	372.1	175.6	54.7	9.5	27.0	4.1
Beginning of Period	3,076.7	3,085.0	819.2	874.9	552.9	357.7
End of Period	\$3,448.8	\$3,260.6	\$873.9	\$884.4	\$579.9	\$361.8

Differences due to rounding.

Net Contributions*	\$230.3	\$156.4	\$3.3	\$(2.9)	\$(1.1)	\$1.3
Cash Flow as % of Assets	6.68%	4.80%	0.38%	(0.32)%	(0.18)%	0.37%
Net Investment Income	\$62.8	\$35.8	\$15.5	\$10.4	\$11.3	\$4.2
Yield as % of Assets	1.82%	1.10%	1.77%	1.18%	1.95%	1.15%

*Net Contributions are less Net Investment Income.

Insurance Fund Contribution Report

For the nine month period ending March 31, 2023, with Comparative Totals for the nine month period ending March 31, 2022 (\$ in Millions)



County Employees Retirement System



	Nonhazardous		Hazardous	
	FY23	FY22	FY23	FY22
Employer Contributions	\$72.3	\$118.3	\$34.1	\$52.3
Insurance Premiums	0.3	0.4	(0.4)	(0.3)
Humana Gain Share	5.9	8.9	0.9	1.3
Retired Reemployed Healthcare	3.6	3.5	1.2	1.2
Health Insurance Contributions	12.6	11.4	3.0	2.7
Net Investment Income	54.2	31.3	26.1	15.3
Total Inflows	148.9	173.8	64.9	72.5
Healthcare Premiums	100.5	102.0	70.2	66.5
Administrative Expenses	0.7	0.7	0.4	0.4
Total Outflows	101.2	102.7	70.6	66.9
NET Contributions	47.7	71.1	(5.7)	5.6
Realized Gain/(Loss)	(10.2)	126.9	(3.9)	67.8
Unrealized Gain/(Loss)	161.9	(88.6)	76.7	(42.3)
Change in Net Position	199.4	109.4	67.1	31.1
Beginning of Period	2,981.2	3,141.8	1,504.0	1,607.8
End of Period	\$3,180.6	\$3,251.2	\$1,571.1	\$1,638.9

Differences due to rounding.

Net Contributions*	\$(6.5)	\$39.9	\$(31.8)	\$(9.7)
Cash Flow as % of Assets	(0.20)%	1.23%	(2.03)%	(0.59)%
Net Investment Income	\$54.2	\$31.3	\$26.1	\$15.3
Yield as % of Assets	1.70%	0.96%	1.66%	0.94%

*Net Contributions are less Net Investment Income.

Insurance Fund Contribution Report
 For the nine month period ending March 31, 2023, with Comparative Totals for the nine month period ending March 31, 2022 (\$ in Millions)

 	Kentucky Employees Retirement System				State Police Retirement System	
	Nonhazardous		Hazardous		FY23	FY22
	FY23	FY22	FY23	FY22		
Employer Contributions	\$26.3	\$25.1	\$-	\$-	\$6.9	\$6.5
Actuarially Accrued Liability						
Contributions	65.7	76.2	-	-	-	-
Employer Cessation Contributions	-	9.5	-	-	-	-
Insurance Premiums	0.1	0.1	(0.1)	0.0	(0.1)	-
Humana Gain Share	4.9	7.3	0.4	0.5	0.2	0.3
Retired Reemployed Healthcare	4.2	3.7	1.0	1.0	-	-
Health Insurance Contributions	6.1	4.9	1.2	0.9	0.3	0.2
Net Investment Income	23.9	13.9	10.2	6.1	4.1	2.3
Total Inflows	131.2	140.7	12.7	8.5	11.4	9.3
Healthcare Premiums	83.0	89.1	15.1	15.5	10.8	10.7
Administrative Expenses	0.6	0.6	0.1	0.1	0.1	0.1
Total Outflows	83.6	89.7	15.2	15.6	10.9	10.8
NET Contributions	47.6	51.0	(2.5)	(7.1)	0.5	(1.5)
Realized Gain/(Loss)	(8.8)	41.0	(1.6)	24.9	(0.8)	10.5
Unrealized Gain/(Loss)	70.7	(43.3)	27.2	(16.4)	11.0	(6.7)
Change in Net Position	109.5	48.7	23.1	1.4	10.7	2.3
Beginning of Period	1,301.5	1,353.1	579.9	624.9	230.0	246.0
End of Period	\$1,411.0	\$1,401.8	\$603.0	\$626.3	\$240.7	\$248.3

Differences due to rounding.

Net Contributions*	\$23.7	\$37.2	\$(12.6)	\$(13.2)	\$(3.6)	\$(3.8)
Cash Flow as % of Assets	1.68%	2.65%	(2.09)%	(2.11)%	(1.51)%	(1.53)%
Net Investment Income	\$23.9	\$13.9	\$10.2	\$6.1	\$4.1	\$2.3
Yield as % of Assets	1.69%	0.99%	1.69%	0.98%	1.72%	0.92%

*Net Contributions are less Net Investment Income.

KPPA ADMINISTRATIVE BUDGET FY 2022-2023						
BUDGET-TO-ACTUAL ANALYSIS						
FOR THE NINE MONTH PERIOD ENDING MACH 31, 2023, WITH COMPARATIVE TOTALS FOR THE NINE MONTH PERIOD ENDING MARCH 31, 2022						
Account Name	Budgeted	FY 2023 Expense	Remaining	Percent Remaining	FY 2022 Expense	Percent Difference
PERSONNEL						
Staff						
Salaries/Wages	\$17,000,000	\$12,181,863	\$4,818,137	28.34%	\$11,779,326	3.42%
Wages (Overtime)	285,000	161,741	123,259	43.25%	147,766	9.46%
Emp Paid Retirement	14,865,100	9,300,601	5,564,499	37.43%	9,404,829	(1.11)%
Emp Paid Health Ins	2,700,000	1,757,627	942,373	34.90%	1,876,528	(6.34)%
Emp Paid Sick Leave	115,000	213,594	(98,594)	(85.73)%	73,621	190.13%
Adoption Assistance Benefit	8,000	-	8,000	100.00%	-	0.00%
Workers Compensation	75,000	11,116	63,884	85.18%	75,163	(85.21)%
Unemployment	8,000	8,009	(9)	(0.11)%	-	100.00%
Other Personnel	1,273,448	896,204	377,244	29.62%	841,179	6.54%
Employee Training	18,000	8,041	9,959	55.33%	7,264	10.70%
Bonds	-	-	-	0.00%	81	(100.00)%
Staff Subtotal	36,347,548	24,538,797	11,808,751	32.49%	24,205,757	1.38%
LEGAL & AUDITING SERVICES						
Legal Hearing Officers	100,000	129,545	(29,545)	(29.55)%	52,541	146.56%
Legal (Stoll, Keenon)	150,000	51,775	98,225	65.48%	78,867	(34.35)%
Frost Brown (Tax Advisor)	80,000	113,219	(33,219)	(41.52)%	21,397	429.13%
Reinhart	25,000	276	24,724	98.90%	-	0.00%
Ice Miller	300,000	91,866	208,134	69.38%	34,775	164.17%
Johnson, Bowman, Branco LLC	150,000	76,195	73,805	49.20%	53,008	43.74%
Dentons Bingham & Greenebaum	150,000	34,136	115,864	77.24%	-	100.00%
Legal Expense	25,000	23	24,977	99.91%	92	(75.00)%
Auditing	200,000	100,479	99,521	49.76%	85,655	17.31%
Total Legal & Auditing Services	1,180,000	597,515	582,485	49.36%	326,335	83.10%
CONSULTING SERVICES						
Medical Reviewers	1,800,000	660,075	1,139,925	63.33%	1,037,696	(36.39)%
Escrow for Actuary Fees	-	(28,866)	28,866	0.00%	-	(100.00)%
Total Consulting Services	1,800,000	631,209	1,168,791	64.93%	1,037,696	(39.17)%
CONTRACTUAL SERVICES						
Miscellaneous Contracts	100,000	19,295	80,705	80.70%	16,179	19.26%
Human Resources Consulting	8,000	-	8,000	100.00%	5,794	(100.00)%
Actuarial Services	500,000	252,280	247,720	49.54%	362,868	(30.48)%
Facility Security Charges	80,000	28,003	51,997	65.00%	57,162	(51.01)%
Tuition Assistance	8,000	-	8,000	100.00%	-	0.00%
Contractual Subtotal	696,000	299,578	396,422	56.96%	442,003	(32.22)%
PERSONNEL SUBTOTAL	\$40,023,548	\$26,067,098	\$13,956,450	34.87%	\$26,041,669	0.10%
OPERATIONAL						
Natural Gas	35,000	28,796	6,204	17.73%	24,556	17.27%
Electric	125,000	85,321	39,679	31.74%	82,521	3.39%
Rent-Non State Building	56,000	37,982	18,018	32.18%	37,982	0.00%
Building Rental - PPW	1,000,000	721,573	278,427	27.84%	721,573	0.00%
Copier Rental	67,000	62,939	4,061	6.06%	60,765	3.58%
Rental Carpool	5,500	3,174	2,326	42.29%	2,911	9.03%
Vehicle/Equip. Maint.	1,000	-	1,000	100.00%	249	(100.00)%
Postage	420,000	293,304	126,696	30.17%	321,650	(8.81)%
Freight	200	41	159	79.28%	155	(73.55)%
Printing (State)	12,000	995	11,005	91.71%	4,548	(78.12)%
Printing (non-state)	105,000	50,640	54,360	51.77%	57,405	(11.78)%
Insurance	12,000	5,572	6,428	53.57%	5,422	2.77%
Garbage Collection	6,000	4,512	1,488	24.79%	4,412	2.27%
Conference Expense	35,000	10,868	24,132	68.95%	8,657	25.54%
Conference Exp. Investment	-	64	(64)	0.00%	-	100.00%
Conference Exp. Audit	2,000	714	1,286	64.30%	-	100.00%
MARS Usage	50,000	20,325	29,675	59.35%	20,325	0.00%

KPPA ADMINISTRATIVE BUDGET 2022-23						
BUDGET-TO-ACTUAL ANALYSIS						
FOR THE NINE MONTH PERIOD ENDING MARCH 31, 2023, WITH COMPARATIVE TOTALS FOR THE NINE MONTH PERIOD ENDING MARCH 31, 2022						
Account Name	Budgeted	FY 2023 Expense	Remaining	Percent Remaining	FY 2022 Expense	Percent Difference
COVID-19 Expenses	12,000	2,421	9,579	79.83%	9,733	(75.13)%
Office Supplies	75,000	71,446	3,554	4.74%	67,451	5.92%
Furniture & Office Equipment	20,000	204	19,796	98.98%	300	100.00%
Travel (In-State)	15,000	10,264	4,736	31.57%	4,792	114.19%
Travel (In-State) Investment	1,000	41	959	95.94%	39	0.00%
Travel (In-State) Audit	500	-	500	100.00%	-	0.00%
Travel (Out of State)	75,000	21,542	53,458	71.28%	382	5,539.27%
Travel (Out of State) Investment	100,000	10,578	89,422	89.42%	-	100.00%
Travel (Out of State) Audit	500	1,077	(577)	(115.40)%	-	100.00%
Dues & Subscriptions	70,000	49,607	20,393	29.13%	36,719	35.10%
Dues & Subscriptions Invest	17,000	11,542	5,458	32.11%	12,228	(5.61)%
Dues & Subscriptions Audit	1,500	400	1,100	73.33%	265	50.94%
Miscellaneous	70,000	43,344	26,656	38.08%	32,591	32.99%
Miscellaneous Investment	-	-	-	0.00%	-	0.00%
Miscellaneous Audit	200	-	200	100.00%	-	0.00%
COT Charges	25,000	14,435	10,565	42.26%	15,760	(8.41)%
Telephone - Wireless	7,000	5,143	1,857	26.53%	4,063	26.58%
Telephone - Other	150,000	74,975	75,025	50.02%	91,667	(18.21)%
Telephone - Video Conference	-	4,836	(4,836)	0.00%	-	100.00%
Computer Equip./Software	3,500,000	1,609,836	1,890,164	54.00%	1,788,674	(10.00)%
Comp. Equip./Software Invest	-	-	-	0.00%	-	0.00%
Comp. Equip./Software Audit	3,000	24,407	(21,407)	(713.56)%	-	100.00%
OPERATIONAL SUBTOTAL	\$6,074,400	\$3,282,918	\$2,791,482	45.95%	\$3,419,455	(3.99)%
SUB-TOTAL	\$46,097,948	\$29,350,017	\$16,747,931	36.33%	\$29,461,124	(0.38)%
Reserve	4,086,552	-	4,086,552	100.00%	-	0.00%
TOTAL	\$50,184,500	\$29,350,017	\$20,834,483	41.52%	\$29,461,125	(0.38)%

Differences due to rounding

Plan	Budgeted	FY 2023 Expense	% of Total KPPA FY 2023 Expense
CERS Nonhazardous	\$28,896,235	\$16,899,740	57.58%
CERS Hazardous	2,559,410	1,496,851	5.10%
KERS Nonhazardous	16,543,320	9,675,233	32.965%
KERS Hazardous	1,824,207	1,066,873	3.635%
SPRS	361,328	211,320	0.720%
TOTAL	\$50,184,500	\$29,350,017	

**JP MORGAN CHASE CREDIT EARNINGS AND FEES
FOR THE NINE MONTH PERIOD ENDING MARCH 31, 2023**

	Earnings	Fees	Net Earnings
June-22	\$5,289	\$(5,906)	\$(616)
July-22	8,921	(5,814)	3,107
August-22	17,621	(6,185)	11,436
September-22	17,026	(6,033)	10,993
October-22	24,574	(6,031)	18,543
November-22	59,589	(5,070)	54,519
December-22	10,556	(6,884)	3,673
January-23	10,331	(6,550)	3,781
February-23	1,707	(6,524)	(4,817)
March-23	2,825	(6,510)	(3,685)
Total	\$143,576	\$(41,922)	\$101,654

**JP MORGAN CHASE HARD INTEREST EARNED
FOR THE NINE MONTH PERIOD ENDING MARCH 31, 2023**

	Clearing Account	CERS	KERS	Total
February-23	\$20,504	\$5,149	\$3,415	\$29,068
March-23	15,428	6,688	4,505	\$26,621
Total	\$35,931	\$11,837	\$7,920	\$55,689



KENTUCKY PUBLIC PENSIONS AUTHORITY

David L. Eager, Executive Director
 1260 Louisville Road • Frankfort, Kentucky 40601
 kyret.ky.gov • Phone: 502-696-8800 • Fax: 502-696-8822



MEMORANDUM

TO: Kristen Coffey, Director of Internal Audit Administration

FROM: Carrie Bass, Staff Attorney Supervisor, Office of Legal Services
 Beth Camic, Staff Assistant to Executive Director of Legal Services

DATE: May 17, 2023

SUBJECT: Potential Information Disclosures/Breaches
 4th Quarter Calendar Year 2022 / 2nd Quarter Fiscal Year 2023

This memo outlines potential disclosure incidents made by the Kentucky Public Pensions Authority (“KPPA”), or any of its external vendors, during the 4th Quarter of Calendar Year 2022 (October through December) (also known as 2nd Quarter in Fiscal Year 2023), and compares them to previous each quarter in Calendar Year 2021.

SUMMARY OF POTENTIAL DISCLOSURES
4TH QUARTER OF CALENDAR YEAR 2022 (2ND QUARTER FISCAL YEAR 2023)

Total potential disclosures investigated: 08

- 1 Implicated HIPAA/HITECH
- 2 Implicated state law
- 3 Implicated internal Data Disclosure Notification Policy
- 2 Found to not be a disclosure

Information Disclosures/Breaches								
Number of Disclosures by Type	Calendar Year 2021				Calendar Year 2022			
	1st Q	2nd Q	3rd Q	4th Q	1st Q	2nd Q	3rd Q	4th Q
Email	1	1	1	5	2	11	0	0
Postal Mail	4	2	3	0	6	2	5	3
Fax	0	0	0	0	0	0	0	0
Other	0	2	3	3	3	0	0	3
TOTAL	5	5	7	8	11	13	5	6
Members Affected - -- KRS & CERS	5	3	73	8	6	2	3	5
Members Affected - -- External	0	2	65	0	27	11	2	120

Number of Incidents by Source								
KPPA, KRS, & CERS	3	3	4	4	7	2	4	5
External Entity (e.g. Bus. Assocs)	2	2	3	2	4	11	1	1
TOTAL	5	5	7	6	11	13	5	6

DISCLOSURES/BREACHES BY THE KPPA IN THE 4TH QUARTER OF CALENDAR YEAR 2022 / 2ND QUARTER IN FISCAL YEAR 2023

Federal law (HIPAA/HITECH): There were no breaches of protected health information by the KPPA during the 4th Quarter of Calendar Year 2022/2nd Quarter of Fiscal Year 2023.

State law (KRS 61.931, et seq.): There were two incidents in which changes were made to a member account by someone other than the member. Both occurrences were a result of the member’s identify being previously compromised in situations and locations outside of KPPA. Despite these incidents being caused by issues outside of the KPPA, the KPPA still was required to follow certain requirements under KRS 61.931, et seq.

- **Background:** Member called to state they received an email from KPPA regarding a notice of a change to their account. Member stated they did not initiate or authorize the changes. The change was a request for direct deposit change. Member confirmed they had not requested a change in their banking information.
 - **Root Cause:** KPPA received direct deposit change request on the appropriate KPPA form which included an image of a voided check to a new bank with the member’s name and address. Investigation by KPPA staff revealed that the member’s information likely had been compromised outside of KPPA for a bank account to be set up with the member’s personal information.
 - **Follow Up:** The direct deposit change that the member indicated they did not make was deactivated before any direct deposits were made to that bank account. KPPA management deactivated the member’s self-service account, and limited changes to the member’s KPPA internal account to management only. Member was sent a copy of the ID Theft Resource. Member’s account had no interruptions to benefit services.

- **Background:** Member called to state they had significant identity security issues in most aspects of their life. They called KPPA as precaution to bar any future changes from occurring to their account.
 - **Root Cause:** Member provided a history of identity theft documents which include several court cases against the bad-actor. The identity theft originated several years ago by an individual and a location unrelated to KPPA.
 - **Follow Up:** Per member’s request, member made an in person appointment to provide proof of driver’s license and passport. KPPA management deactivated the member’s self-service account, and limited changes to the member’s KPPA internal

account to management only. Member was given a copy of the ID Theft Resource. Member's account had no interruptions to benefit services.

Internal Data Disclosures:

- **Background:** Member received correspondence with documentation requested as well as documentation for another member. Recipient member immediately contacted KPPA and returned documentation belonging to the other member. Affected member was notified of the disclosure.
 - **Root Cause:** Unknown, but likely due to automatic mailer.
 - **Follow Up:** Correspondence team notified of incident.

- **Background:** Beneficiary of a member received an envelope with her address, but the envelope and its contents refer to another member. The recipient beneficiary immediately contacted KPPA and returned documentation belonging to the other member. Recipient beneficiary was resent proper information and affected member was notified of the disclosure.
 - **Root Cause:** Unknown, but likely due to automatic mailer.
 - **Follow Up:** Correspondence team notified of incident.

- **Background:** An attorney called KPPA to state they received a letter for a member who is not their client.
 - **Root Cause:** Unknown
 - **Follow Up:** The attorney returned the information at the request of KPPA. Affected member has been notified of the disclosure.

**EXTERNAL DISCLOSURES/BREACHES IN THE 4TH QUARTER OF CALENDAR
YEAR 2022 / 2ND QUARTER IN FISCAL YEAR 2023**

The Centers for Medicare & Medicaid Services (CMS) reported to the KPPA that in October 2022 120 retirees were affected by a HIPAA breach by a CMS vendor. In December 2022, CMS notified all 120 retirees of the breach and offered credit monitoring. CMS is also working with Humana to issue new ID numbers. KPPA is awaiting further updates from CMS and Humana.

RECOMMENDATION

This memorandum is provided for informational purposes only.



KENTUCKY PUBLIC PENSIONS AUTHORITY

David L. Eager, Executive Director
 1260 Louisville Road • Frankfort, Kentucky 40601
 kyret.ky.gov • Phone: 502-696-8800 • Fax: 502-696-8822



MEMORANDUM

TO: Kristen Coffey, Director of Internal Audit Administration

FROM: Carrie Bass, Staff Attorney Supervisor, Office of Legal Services
 Jennifer Korth, Legal Secretary, Office of Legal Services

DATE: May 17, 2023

SUBJECT: Potential Information Disclosures/Breaches
 1st Quarter Calendar Year 2023 / 3rd Quarter Fiscal Year 2023

This memo outlines potential disclosure incidents made by the Kentucky Public Pensions Authority (“KPPA”), or any of its external vendors, during the 1st Quarter Calendar Year 2023 (January through March) (also known as 3rd Quarter Fiscal Year 2023), and compares them to previous each quarter in Calendar Year 2022.

SUMMARY OF POTENTIAL DISCLOSURES

1ST QUARTER OF CALENDAR YEAR 2023 (3RD QUARTER FISCAL YEAR 2023)

Total potential disclosures investigated: 07

- 0 Implicated HIPAA/HITECH
- 0 Implicated state law
- 6 Implicated internal Data Disclosure Notification Policy
- 1 Found to not be a disclosure

Information Disclosures/Breaches								
Number of Disclosures by Type	Calendar Year 2022				Calendar Year 2023			
	1st Q	2nd Q	3rd Q	4th Q	1st Q	2nd Q	3rd Q	4th Q
Email	2	11	0	0	1			
Postal Mail	6	2	5	3	4			
Fax	0	0	0	0	0			
Other	3	0	0	3	1			
TOTAL	11	13	5	6	6			
Members Affected - -- KRS & CERS	6	2	3	6	6			
Members Affected - -- External	27	11	2	0	0			

Number of Incidents by Source								
KPPA, KRS, & CERS	7	2	4	6	6			
External Entity (e.g. Bus. Assocs)	4	11	1	0	0			
TOTAL	11	13	5	6	6			

POTENTIAL DISCLOSURES/BREACHES BY THE KPPA IN THE 1ST QUARTER OF CALENDAR YEAR 2023 / 3RD QUARTER IN FISCAL YEAR 2023

Federal law (HIPAA/HITECH): There were no breaches of protected health information by the KPPA during the 1st Quarter Calendar Year 2023/3rd Quarter of Fiscal Year 2023.

State law (KRS 61.931, et seq.): There were no “security breaches” of “personal information” as defined by state law by the KPPA during the 1st Quarter Calendar Year 2023/3rd Quarter of Fiscal Year 2023.

Internal Data Disclosures:

- **Background:** A member received their requested pin number, as well as another member’s documentation which included retirement estimates. The recipient member contacted the KPPA and was sent a pre-paid envelope to return the documents. The affected member was notified of the disclosure. The recipient member was sent an affidavit to confirm the contents were not shown to another individual.
 - **Root Cause:** Both members requested items on 2/2/2023 that were generated by batch printing and were likely intermingled during this stage.
 - **Follow Up:** Correspondence team notified of incident.

- **Background:** A KPPA staff member inadvertently attached a report to an email to an employer that was not intended for that employer. Upon receipt, the recipient employer immediately responded to the KPPA staff member stating the report did not belong to their agency. Upon notice of the disclosure, KPPA asked the recipient employer not to view the report contents and to delete/destroy the email. KPPA notified the affected member of the disclosure.
 - **Root Cause:** The KPPA staff member sent the report to an incorrect employer with an employer ID that is very similar to the correct employer. The KPPA staff member likely confused the two employer IDs when locating contact information to send the report.
 - **Follow Up:** The appropriate supervisor followed up with the KPPA staff member regarding the disclosure incident.

- **Background:** A member received their correspondence as well as another member’s documentation which included a general letter. Upon receipt, the recipient member immediately contacted KPPA. The recipient returned the disclosed information at an in-

person retirement counsel session at KPPA. KPPA notified the affected member of the disclosure.

- **Root Cause:** Both correspondence pieces were generated by batch printing and were printed approximately 30 seconds apart. Likely correspondence became intermingled during this stage.
- **Follow Up:** Correspondence team notified of incident.

- **Background:** A member received an envelope with their mailing address, but named another member. The envelope contained another member's general information on refunds and a blank Beneficiary Designation Form. The recipient member called KPPA and was sent a pre-paid envelope to return the information. KPPA notified the affected member of the disclosure. The recipient member was sent an affidavit to confirm no other individuals had viewed the contents.
 - **Root Cause:** Unknown, likely a template error.
 - **Follow Up:** Recipient member has been contacted for follow-up information.

- **Background:** A member received another member's envelope stuck to the back of their envelope. The recipient member contacted KPPA and verbally confirmed they did not open the envelope. The recipient member was sent a pre-paid envelope to send the envelope back to KPPA. Disclosure notification letter to the affected member and affidavit for the recipient member to confirm no individual viewed the contents of the envelope have been prepared.
 - **Root Cause:** Two pieces of mail were stuck together during mailing process.
 - **Follow Up:** KPPA staff confirmed that affected member did not receive the envelope. Staff member resent information to the affected member.
 -

- **Background:** A KPPA employee provided information concerning a member's mailing address, benefit information, and records on file at the KPPA to an unauthorized third party. KPPA notified the affected member of the disclosure. The unauthorized recipient was sent an affidavit to confirm that the affected member's information was not misused and that no other individuals had viewed the information.
 - **Root Cause:** KPPA employee did not follow KPPA policies concerning confidentiality of member account information.
 - **Follow Up:** Supervisor of the KPPA employee followed-up with employee concerning KPPA policies and confidentiality of member account information.

**EXTERNAL DISCLOSURES/BREACHES IN THE 1ST QUARTER OF CALENDAR
YEAR 2023 / 3RD QUARTER IN FISCAL YEAR 2023**

There were no external disclosures/breaches reported to the KPPA for the 1st Quarter Calendar Year 2023/3rd Quarter of Fiscal Year 2023.

RECOMMENDATION

This memorandum is provided for informational purposes only.



KENTUCKY PUBLIC PENSIONS AUTHORITY

David L. Eager, Executive Director
 1260 Louisville Road • Frankfort, Kentucky 40601
 kyret.ky.gov • Phone: 502-696-8800 • Fax: 502-696-8822



MEMORANDUM

TO: Kristen Coffey, Director of Internal Audit Administration
FROM: Carrie Bass, Staff Attorney Supervisor, Office of Legal Services
DATE: May 17, 2023
SUBJECT: Tips Received Regarding Fraud, Waste, and Abuse

The chart at the end of this Memorandum provides updated information on tips relating to fraud, waste, and abuse against the Kentucky Retirement Systems prior to April 1, 2021 or the Kentucky Public Pensions Authority on and after April 1, 2021.

To summarize the information contained in the chart below, since the Joint Audit Committee of the Board of Trustees of the Kentucky Retirement Systems and the Board of Trustees of the County Employees Retirement System met on November 28, 2022,¹ eight (8) cases have been opened and eight (8) cases have been opened and closed.

Additionally, the current open cases as of the date of this Memorandum can be summarized as follows:

- One (1) related to multiple retired members allegedly continuing to provide the same services to their former employers via contract arrangements;
- Seven (7) related to an alleged prearranged agreement for an employee to retire and return to work for the same employer;
- One (1) related to the alleged misreporting of an employee in a hazardous position;
- One (1) related to the alleged failure of an employer to report all employees in regular full-time positions;
- One (1) related to alleged disability fraud; and
- One (1) related to an alleged prearranged agreement for an employee to retire and return to work for the same employer and an alleged failure to observe required break in service between retirement and reemployment.

Date Reported	Issue	Current Action	Status²
Various	Possible fraudulent disability payments.	This tip involved two members. For one member, an administrative hearing	Closed

¹ The Joint Audit Committee met on February 28, 2023, but no update on tips received regarding fraud, waste, or abuse against or within the KPPA was presented at that meeting.

² The status reflected for each tip is as of the date of this Memorandum.

		process was initiated. The final result of that hearing process was that no fraudulent activity by this member was verifiable. For the second member reported via the same tip, the Office of Legal Services was unable to corroborate the tip.	
3/2/2022	Multiple retired members allegedly continuing to provide the same services to their former employers via contract arrangements	The Office of Legal Services is reviewing compiled information to determine if any action can or should be taken regarding the retired members.	Open
4/25/2022 (previously listed as 5/5/2022)	Alleged prearranged agreement for an employee to retire and return to work for the same employer	The Office of Legal Services is waiting on additional information.	Open
5/17/2022	Alleged misreporting of employee in hazardous position	The Office of Legal Services is investigating.	Open
8/18/2022	Alleged prearranged agreement for an employee to retire and return to work for the same employer	The Office of Legal Services was unable to substantiate this tip.	Closed
9/22/2022	Alleged prearranged agreement for an employee to retire and return to work for the same employer	The Office of Legal Services was unable to substantiate this tip.	Closed
10/3/2022 10/28/2022	Alleged prearranged agreement for an employee to retire and return to work for the same employer	The Office of Legal Services is waiting on additional information.	Open
12/13/2022	Alleged failure of an employer to report all employees in regular full-time positions	The Office of Legal Services is investigating.	Open
12/27/2022	Alleged prearranged agreement for an employee to retire and return to work for the same employer	The Office of Legal Services is waiting on additional information.	Open

1/5/2023	Alleged prearranged agreement for an employee to retire and return to work for the same employer	The Office of Legal Services was unable to substantiate this tip.	Opened, then closed
1/16/2023	Alleged disability fraud	The Office of Legal Services was unable to substantiate this tip.	Opened, then closed
1/30/2023	Alleged member pension spike, alleged reporting errors, and alleged disqualification for position	The KPPA had already handled all relevant issues appropriately.	Opened, then closed
2/2/2023	Alleged disability fraud	The Office of Legal Services is waiting on additional information.	Open
2/4/2023	Alleged prearranged agreement for an employee to retire and return to work for the same employer	The Office of Legal Services is investigating.	Open
2/11/2023	Alleged prearranged agreement for an employee to retire and return to work for the same employer	The Office of Legal Services is investigating.	Open
2/18/2023	Alleged attempt to commit mail fraud by imitating the KPPA	The letter that prompted the tip was determined to be a legitimate letter from the KPPA.	Opened, then closed
2/27/2023	Alleged fraud related to multiple issues with member account	The Office of Legal Services was unable to substantiate this tip.	Opened, then closed
2/28/2023	Alleged prearranged agreement for an employee to retire and return to work for the same employer	The Office of Legal Services is investigating.	Open
2/28/2023	Alleged prearranged agreement for an employee to retire and return to work for the same employer	The Office of Legal Services was unable to substantiate this tip.	Opened, then closed
3/5/2023	Alleged attempt to commit mail fraud by imitating the KPPA	The letter that prompted the tip was determined to be a legitimate letter from the KPPA	Opened, then closed
4/14/2023	Alleged fraud by an employer	The Office of Legal Services is investigating.	Opened, then closed

4/20/2023	Alleged prearranged agreement for an employee to retire and return to work for the same employer	The Office of Legal Services is waiting on additional information.	Open
4/25/2023	Alleged prearranged agreement for an employee to retire and return to work for the same employer; alleged failure to observe required break in service between retirement and reemployment	The Office of Legal Services is investigating.	Open



Kentucky Public Pensions Authority
Internal Audit Administration



To: Members of the Joint Audit Committee
 From: Kristen N. Coffey, CICA *KNC*
 Division Director, Internal Audit Administration
 Date: May 25, 2023
 Subject: Fiscal Year 2023 Internal Audit Budget as of March 31, 2023

Items in yellow are corrections from the previously presented budget.

- The expense in the first quarter was for four licenses to the new audit software. This was previously coded as a non-audit expense.
- The salary report provided to Internal Audit staff for the 2nd Quarter contained a formula error. Line items 111 and 121 have been updated to reflect actual expenses for the 2nd quarter.

Account Number	Account Name	FYE 2022 Actual	FYE 2023 Budget	FYE 2023 Adjusted Budget	Variance of Budget Compared to Actual Prior Year	FY 2023 Actual Expenditures	Remaining Budget	Percent Remaining
111	Salaries	\$ 188,512.19	\$ 243,145.00	\$ 275,872.24	\$ 87,360.05	\$ 203,220.75	\$ 72,651.49	26.34%
121	Employer Paid FICA	13,978.72	18,600.59	21,104.23	7,125.51	15,222.74	5,881.49	27.87%
122	Employer Paid Retirement	155,602.13	196,611.56	231,649.92	76,047.79	155,182.53	76,467.39	33.01%
123	Employer Paid Health Insurance	32,958.24	40,000.00	40,000.00	7,041.76	29,297.88	10,702.12	26.76%
124	Employer Paid Life Insurance	43.00	46.00	55.00	12.00	38.00	17.00	30.91%
133T	Employee Training	-	1,000.00	1,000.00	1,000.00	-	1,000.00	100.00%
259T	Conference Expenses	-	2,000.00	2,000.00	2,000.00	714.00	1,286.00	64.30%
361T	Travel - In State	2,072.00	500.00	500.00	(1,572.00)	-	500.00	100.00%
362T	Travel - Out State	-	500.00	500.00	500.00	1,076.98	(576.98)	-115.40%
381T	Dues & Subscriptions	-	1,500.00	1,500.00	1,500.00	1,250.00	250.00	16.67%
399T	Miscellaneous	738.33	200.00	200.00	(538.33)	-	200.00	100.00%
847T	Computer Equipment	-	3,000.00	35,000.00	35,000.00	35,698.98	(698.98)	-2.00%
Total		\$ 393,904.61	\$ 507,103.15	\$ 609,381.39	\$ 215,476.78	\$ 441,701.86	\$ 65,401.29	12.90%

259T Conference Expenses

- 2nd Quarter - \$350 APPFA Conference (1 employee) and \$289 AGA Conference (all staff)
- 3rd Quarter - AGA Spring Conference (all staff)

362T Out of State Travel

- 1st Quarter - APPFA Conference (1 employee)

381T Dues and Subscriptions

- 2nd Quarter - \$100 AGA Membership (2 staff) and \$500 APPFA Membership (KPPA)
- 3rd Quarter - AGA membership (all staff) and IIA membership (Madeline and Matthew)

847T Computer Equipment

- 1st Quarter - Audit Software licenses (4 staff)
- 2nd Quarter - One-time initial set-up fee. Future years will not include this fee.

Joint Audit Committee Meeting - Joint Audit Committee Administrative Updates



Kentucky Public Pensions Authority
Internal Audit Administration



To: Members of the Joint Audit Committee
 From: Kristen N. Coffey, CICA
 Division Director, Internal Audit Administration
 Date: May 25, 2023
 Subject: Status of Current Audit Projects

Project Code	Project Name	State	Opinion	Phase	Scheduled Start	Actual Start	Scheduled End	Actual End	Actual Hours	Estimated Hours	Estimated Hours Variance	Notes
2022-1.3	Plan Liquidity Phase 3 - Available Cash Balance/Cash Projection	Closed	High Risk Items Still Open	Completion	11/1/2021	11/1/2021	5/16/2023	5/15/2023	1,087.50	1,000.00	87.50	
2022-2	Employer Penalty Waiver (used as implementation test)	Closed	Low Risk Items Still Open	Completion	7/8/2021	7/8/2021	11/19/2021	11/19/2021	69.50	150.00	-80.50	
2022-4	Review of Chase Accounts	Closed	High Risk Items Still Open	Completion	6/2/2022	6/2/2022	1/31/2023	2/20/2023	2,673.25	2,100.00	573.25	
2022-5	Accuracy of Information Sent to Humana and DEI	Closed	Findings Noted, But Already Corrected	Completion	4/5/2022	4/5/2022	3/31/2023	4/14/2023	545.25	500.00	45.25	
2023-1	Follow-up on Open Issues	Closed	Low Risk Items Still Open	Completion	11/1/2022	11/1/2022	5/16/2023	4/26/2023	370.35	300.00	70.35	
2022-Other-1	KPPA Inventory Project	Open		Planning	2/28/2022	2/28/2022	3/31/2023		11.50	75.00	-63.50	This project is being led by another division. Internal Audit participates on the team. Anticipated completion date has been updated to 6/30/2023.
2022-Other-2	2023 State Police Retirement System Trustee Election	Closed		Completion	5/2/2022	4/1/2022	4/28/2023	3/15/2023	28.40	45.00	-16.60	
2023-Other-1	Audit Committee Meetings	Open		Fieldwork	7/1/2022	7/1/2022	6/30/2023		24.00	65.00	-41.00	
2023-Other-2	FY 2024 KPPA Risk Assessment/Audit Plan	Open		Fieldwork	7/1/2022	7/1/2022	5/12/2023		99.00	300.00	-201.00	Risk Assessment and Audit Plan is completed, but needs to be approved.
2023-Other-3	August 2022 - Hiring Auditor 1	Closed		Completion	8/3/2022	8/2/2022	9/9/2022	9/7/2022	42.75	86.00	-43.25	
2023-Other-4	Review FY 2023 Annual Financial Report and Summary Financial Report	Closed		Completion	9/1/2022	8/8/2022	11/16/2022	11/16/2022	116.50	112.00	4.50	
2023-Other-5	Microsoft 365 Implementation	Closed		Completion	8/15/2022	8/15/2022	1/31/2023	2/17/2023	22.00	85.00	-63.00	
2023-Other-6	2023 IT Governance Review	Closed		Completion	9/1/2022	9/7/2022	3/16/2023	9/28/2022	2.00	2.00	0.00	
2023-Other-7	Update Audit Charters	Open		Fieldwork	11/1/2022	9/30/2022	6/28/2023		12.50	34.00	-21.50	
2023-Other-8	Trustee Election Policy Updates	Open		Planning	11/1/2022	10/6/2022	4/4/2023		1.00	22.00	-21.00	Election Policy Updates will be completed in the new fiscal year. This was delayed to work on the implementation of HB 587.
2023-Other-9	FY 2023 Process Documentation	Open		Fieldwork	3/1/2023	3/1/2023	6/30/2023		136.00	300.00	-164.00	
2023-Other-10	2023 Intern - Hiring Information	Open		Fieldwork	3/14/2023	3/14/2023	5/31/2023	5/16/2023	87.75	35.00	52.75	Intern started on May 16, 2023. Estimated hours was based on hours for hiring prior year intern. This year, five staff members were involved in the process and it was the first interview process for two of the team members. Additional time was spent explaining the process and reviewing the candidates.
2024-Other-5	Trustee Election RFP	Open		Fieldwork	12/1/2022	1/26/2023	12/29/2023		7.00	125.00	-118.00	
2024-Other-6	Self Assessment for Peer Review	Open		Planning	3/14/2023	3/14/2023	7/21/2023		6.75	500.00	-493.25	
	ERCE Receiving and Balancing Contributions	Closed		Deferred/Cancelled	10/2/2023		3/15/2024		119.75	300.00	-180.25	
	Follow-up: Reconciliation of Great Plains to eMARS	Closed		Deferred/Cancelled	9/26/2022	9/21/2022	4/28/2023		332.50	600.00	-267.50	

Available Hours FY 2023 (including holidays)	8,856.25
Available Hours Remaining in FY 2023 (including holidays) as of 5.13.2023	1,312.50
Project Hours Charged as of 5.13.2023	5,867.25
FY 2022 Project Hours Reported in TeamMate FY 2023	(1,170.50)
Administrative Hours as of 5.13.2023	2,088.25
Holidays and Time Off as of 5.13.2023	839.25
Actual Hours Charged for FY 2023	7,624.25
Overtime Worked in FY 2023	80.50
Average Overtime Worked in FY 2023, per employee	16.10



KENTUCKY PUBLIC PENSIONS AUTHORITY

David L. Eager, Executive Director

1260 Louisville Road • Frankfort, Kentucky 40601
kyret.ky.gov • Phone: 502-696-8800 • Fax: 502-696-8822



To: Members of the Joint Audit Committee

From: Kristen N. Coffey, CICA *KNC*
Division Director, Internal Audit Administration

Date: May 25, 2023

Subject: Fiscal Year 2024 Risk Assessment and Audit Plan

Internal Audit has performed a risk assessment for fiscal year (FY) 2024. This assessment was conducted based on past risks noted within KPPA and audits conducted during fiscal year 2023. After the risks were identified, they were ranked based on inherent risk and inherent likelihood. A scale of 0-10 was used (0 = less inherent risk/unlikely to occur, 10 = high inherent risk/probable to occur). The scores were then averaged to obtain an overall risk score. The items were then sorted based on the risk score (highest to lowest). The following audits are being recommended in response to the completed risk assessment

FY 2024 Audit Plan

1. Review of investment administrative fees.
2. Review of investment manager fees, including reconciliation process and fee reporting process.*
3. Review of outstanding employer invoices.
4. Review of process to ensure new legislation is properly implemented.
5. Review of interest calculated and applied to member accounts.
6. Review of employer contributions, including the balancing process.*
7. Review of member/employer information utilized for retirement (addressing risk that information may be altered to increase benefits).
8. Review of correspondence process (to address risk of personal information disclosures).
9. Review of refund calculations.
10. Review of administrative expense allocation.*

* These projects have been previously approved by the Joint Audit Committee.

FY 2024 Other Projects

In addition to the audits above, Internal Audit staff will also work on the following projects throughout fiscal year 2024.

1. Completion of self-assessment for peer review.
2. Review of the FY 2024 Annual Comprehensive Financial Report.
3. Review of the FY 2024 Summary Annual Financial Report.
4. Participation on the Trustee Election Vendor selection panel.
5. Completion of FY 2025 Risk Assessment and Audit Plan.
6. Updating audit related charters.
7. Updating Board Election policies.
8. Completion of process documentation for audit procedures.
9. Participation on various KPPA projects/work groups (e.g., IT Governance Group)
10. Preparation for and presentation to various Board and Committee meetings.

The Division of Internal Audit currently has one director and four additional staff members. Staff are expected to complete 2-3 audits a year, in addition to work completed on other projects. While this audit plan contains a substantial number of projects, it is feasible.

Carry-over from approved FY 2023 Audit Plan

The items below were included on the FY 2023 audit plan but were not recommended as a part of the FY 2024 audit plan because they were assessed at a lower risk during the FY 2024 risk assessment. Multiple higher risk items for the divisions were recommended for the FY 2024 audit plan. Should all above audits be completed, staff will work on the items below.

1. Review of reconciliation between Great Plains and BNY Mellon.
2. Review of investment direct repo process.
3. Review of cash receipt process.
4. Review of the accounts payable process (follow-up audit).
5. Review of investment contract process.

Joint Audit Committee Action Needed: The Division of Internal Audit has completed most of the audits from the FY 2023 audit plan. Without approval of the FY 2024, staff are unable to start any new projects. The Division of Internal Audit is requesting that the Joint Audit Committee take one of the following actions:

1. Approve the full FY 2024 Audit Plan.
2. Approve of the two items highlighted in yellow and submit the full FY 2024 Audit Plan to the KPPA Audit Committee and/or full KPPA Board for approval.

KPPA Internal Audit Risk Assessment Report

High Risk	Item being recommended for the FY 2024 audit plan.
Medium Risk	Carry-over from prior plan. Will be included on FY 2024 plan.
Low Risk	Included as a part of every audit.

Entity Path	Strategic Risk Title	Inherent	Reviewed in the Past 5 years?	Notes
Office of Investments	Lack of Oversight of Investment Admin Fees	8.00	No	Recommended for FY 2024 Audit Plan
Office of Investments	Lack of Oversight of Manager Fees	8.00	No	Recommended for FY 2024 Audit Plan
Office of Investments	Lack of Oversight of Performance Fees	8.00	No	Tentatively recommended for FY 2024 Audit Plan. If the other two investment audits are able to be completed quickly, without too much burden on investment staff, this will also be completed in FY 2024. Otherwise this will be included on the FY 2025 plan.
Office of Investments	Proxy Voting does not Comply with Policy	8.00	No	Two other audits are scheduled with Investments. Additionally, this is a new process. This is recommended for the FY 2025 plan.
Division of Accounting > Cash Management Branch	Pension and Insurance Contributions Split Correctly	8.00	No	This is related to an issue previously reported to the Audit Committee. Requesting that the Audit Committee weigh-in on whether to make this item a priority for the FY 2024 audit plan.
Division of Employer Reporting, Compliance, and Education	Outstanding Employer Invoices	8.00	No	Recommended for FY 2024 Audit Plan
Board of Trustees	Perimeter Park West, Inc	7.00	Yes	Recently audited, will not be on the FY 2024 plan.
Executive Director	Board of Trustees May Not Receive Proper Information Timely	7.00	No	This is not audited separately, but combined in every audit.
Executive Director	New Legislation Not Implemented	7.00	No	Recommended for FY 2024 Audit Plan
Executive Director	Segregation of Duties	7.00	Yes	This is not audited separately, but combined in every audit.
Office of Investments	Establishment and Usage of Retirement Allowance Account	7.00	Yes	Recently audited, will not be on the FY 2024 plan.
Office of Investments	Insufficient Cash Balance	7.00	Yes	Recently audited, will not be on the FY 2024 plan.
Office of Investments	Tier 3 Calculation May Be Inaccurate	7.00	No	Two other audits are scheduled with the Office of Investments. So as not to over burden one group, we will revisit this item for the FY 2025 plan.
Division of Accounting > Cash Management Branch	Accounts not Properly Reconciled	7.00	Yes	Recently audited, will not be on the FY 2024 plan.
Division of Accounting > Cash Management Branch	Manual Journal Entry Process	7.00	No	This could be impacted based on the Chase audit from FY 2023. Will revisit for the FY 2025 audit plan.
Division of Accounting > Cash Management Branch	Manual Mailing of Checks Processed by Treasury	7.00	No	This could be impacted based on the Chase audit from FY 2023. Will revisit for the FY 2025 audit plan.
Division of Accounting > Cash Management Branch	Overpayment Invoices may not be Monitored	7.00	No	This could be impacted based on the Chase audit from FY 2023. Will revisit for the FY 2025 audit plan.
Division of Accounting > Investment Operations Branch	Custodial Bank does not Reconcile to Great Plains	7.00	No	This could be impacted based on the Chase audit from FY 2023. Will revisit for the FY 2025 audit plan.
Division of Accounting > Investment Operations Branch	Interest on Member Accounts Calculated Improperly	7.00	No	Recommended for FY 2024 Audit Plan
Division of Employer Reporting, Compliance, and Education	Delinquent Employers	7.00	No	Two other audits are scheduled with ERCE. So as not to over burden one group, we will revisit this item for the FY 2025 plan.
Division of Employer Reporting, Compliance, and Education	Employer Contributions are Inaccurate	7.00	No	Recommended for FY 2024 Audit Plan (carry-over)
Division of Employer Reporting, Compliance, and Education	Inactive Employers not Reporting	7.00	No	Two other audits are scheduled with ERCE. So as not to over burden one group, we will revisit this item for the FY 2025 plan.
Division of Enterprise and Technology Services > Security	Mission Critical Systems are Compromised	7.00	No	This is addressed by a third party vendor audit each year.
Division of Enterprise and Technology Services > Security	Staff have Improper System Access	7.00	Yes	Recently audited, will not be on the FY 2024 plan.

KPPA Internal Audit Risk Assessment Report

High Risk	Item being recommended for the FY 2024 audit plan.
Medium Risk	Carry-over from prior plan. Will be included on FY 2024 plan.
Low Risk	Included as a part of every audit.

Entity Path	Strategic Risk Title	Inherent	Reviewed in the Past 5 years?	Notes
Division of Enterprise and Technology Services > Enterprise Project Management	COOP is Outdated, Inaccurate, or Insufficient	7.00	Yes	Recently audited, will not be on the FY 2024 plan.
Division of Procurement and Office Services > Procurement Branch	Inventory Process	7.00	No	This process is currently being established. It will likely be included as a part of the FY2025 plan.
Division of Procurement and Office Services > Office Services Branch	Disclosures Occur During Correspondence	7.00	No	Recommended for FY 2024 Audit Plan
Division of Member Services > Finals	Member Information Altered Prior to Uploading to Their Account	7.00	No	Recommended for FY 2024 Audit Plan
Division of Membership Support	Refunds may be Processed Inaccurately	7.00	No	Recommended for FY 2024 Audit Plan
Division of Membership Support	Retirement/Recalculations Amounts are Inaccurate	7.00	No	FY 2024 plan complete, will re-evaluate for FY 2025.
Executive Director	Disclosure of Personal Information	6.00	Yes	Recently audited, will not be on the FY 2024 plan.
Executive Director	Lack of Back-ups in Key Areas of KPPA	6.00	Yes	This is not audited separately, but considered a risk in every audit.
Executive Director	Manual Workarounds Required for Outstanding IT Issues	6.00	No	FY 2024 plan complete, will re-evaluate for FY 2025.
Executive Director	Policies and Procedures not Accurate	6.00	Yes	This is not audited separately, but considered a risk in every audit.
Executive Director	Staff not Properly Trained to Perform Job Duties	6.00	No	This is not audited separately, but considered a risk in every audit.
Executive Director	Use of Signature Stamp (including access to Digital Signature)	6.00	No	This is not audited separately, but considered a risk in every audit.
Executive Director	Violation of Record Retention Policy	6.00	No	FY 2024 plan complete, will re-evaluate for FY 2025.
Office of Investments	Inconsistent Payment of Vendors	6.00	No	This could be impacted based on the Chase audit from FY 2023. Will revisit for the FY 2025 audit plan.
Office of Investments	Investment Procurement Policy not Followed	6.00	No	FY 2024 plan complete, will re-evaluate for FY 2025.
Office of Investments	Investment Transactions Not Approved Properly	6.00	Yes	Recently audited, will not be on the FY 2024 plan.
Office of Investments	Number of Transfers Between Accounts	6.00	Yes	Recently audited, will not be on the FY 2024 plan.
Office of Legal Services - Non-Advocacy	Violation of Retired/Re-Employed Statutes	6.00	No	FY 2024 plan complete, will re-evaluate for FY 2025.
Division of Communications	Forms on the Website may be Inaccurate	6.00	No	FY 2024 plan complete, will re-evaluate for FY 2025.
Division of Communications	Inaccurate Information Communicated to Members	6.00	No	FY 2024 plan complete, will re-evaluate for FY 2025.
Division of Human Resources	Hiring Process is Inefficient	6.00	No	FY 2024 plan complete, will re-evaluate for FY 2025.
Division of Human Resources	HR Policies not Applied Consistently	6.00	No	FY 2024 plan complete, will re-evaluate for FY 2025.
Division of Accounting > Cash Management Branch	Accounts Receivable Process	6.00	No	FY 2024 plan complete, will re-evaluate for FY 2025.
Division of Accounting > Cash Management Branch	Accurate Financial Statements not Prepared Timely	6.00	Yes	Recently audited, will not be on the FY 2024 plan.
Division of Accounting > Cash Management Branch	Allocation of Expenses may be Inaccurate	6.00	No	Recommended for FY 2024 Audit Plan (carry-over)
Division of Accounting > Cash Management Branch	Service Purchases Processed Improperly	6.00	No	FY 2024 plan complete, will re-evaluate for FY 2025.
Division of Accounting > Investment Operations Branch	New Investment Accounts not Set-up Accurately	6.00	No	FY 2024 plan complete, will re-evaluate for FY 2025.
Division of Employer Reporting, Compliance, and Education	Employer Report Process	6.00	No	FY 2024 plan complete, will re-evaluate for FY 2025.
Division of Employer Reporting, Compliance, and Education	Pension Spiking	6.00	No	FY 2024 plan complete, will re-evaluate for FY 2025.
Division of Enterprise and Technology Services	Disaster Recovery Plan is Insufficient	6.00	No	FY 2024 plan complete, will re-evaluate for FY 2025.
Division of Enterprise and Technology Services > Security	Staff not Properly Trained on IT Security	6.00	No	FY 2024 plan complete, will re-evaluate for FY 2025.
Division of Procurement and Office Services > Procurement Branch	Procurement Process	6.00	Yes	Recently audited, will not be on the FY 2024 plan.
Division of Procurement and Office Services > Office Services Branch	Electronic Faxes not Handled Properly	6.00	No	FY 2024 plan complete, will re-evaluate for FY 2025.
Division of Procurement and Office Services > Office Services Branch	Imaging Process is Inefficient/Inaccurate	6.00	No	FY 2024 plan complete, will re-evaluate for FY 2025.

KPPA Internal Audit Risk Assessment Report

High Risk	Item being recommended for the FY 2024 audit plan.
Medium Risk	Carry-over from prior plan. Will be included on FY 2024 plan.
Low Risk	Included as a part of every audit.

Entity Path	Strategic Risk Title	Inherent	Reviewed in the Past 5 years?	Notes
Division of Procurement and Office Services > Office Services Branch	Incoming Mail is not Handled Properly	6.00	No	FY 2024 plan complete, will re-evaluate for FY 2025.
Division of Disability and Survivor Benefits > Disability Branch	Applications Voided Incorrectly	6.00	No	FY 2024 plan complete, will re-evaluate for FY 2025.
Division of Disability and Survivor Benefits > Disability Branch	Cost/Benefit of Medical Review Vendor	6.00	Yes	Currently under review by Benefits
Division of Disability and Survivor Benefits > Disability Branch	Disability Claims not Reviewed Timely/Accurately	6.00	No	Likely tied into a review recently performed by Benefits related to medical officers. Will revisit for the FY 2025 plan.
Division of Disability and Survivor Benefits > Disability Branch	Disability Recipient Working at Unapproved Job	6.00	No	FY 2024 plan complete, will re-evaluate for FY 2025.
Division of Disability and Survivor Benefits > Survivor Benefits Branch	Overpayment Process	6.00	No	FY 2024 plan complete, will re-evaluate for FY 2025.
Division of Membership Support	Phone Calls not Answered Timely	6.00	No	FY 2024 plan complete, will re-evaluate for FY 2025.
Division of Member Services > Counseling	Service Purchases are Calculated Incorrectly	6.00	No	FY 2024 plan complete, will re-evaluate for FY 2025.
Division of Member Services > Finals	Final Retirements Not Processed Timely or Accurately	6.00	No	FY 2024 plan complete, will re-evaluate for FY 2025.
Division of Member Services > Finals	QDRO Process	6.00	No	FY 2024 plan complete, will re-evaluate for FY 2025.
Division of Quality Assurance > Post-Retirement Branch	Post Retirement Audits not Completed Timely or Accurately	6.00	No	FY 2024 plan complete, will re-evaluate for FY 2025.
Division of Quality Assurance > Pre-Retirement Branch	Pre-Retirement Audits not Completed Timely or Accurately	6.00	No	FY 2024 plan complete, will re-evaluate for FY 2025.
Division of Retiree Health Care	Medicare as Secondary Payer Process	6.00	No	FY 2024 plan complete, will re-evaluate for FY 2025.
Division of Retiree Health Care	Premiums Paid are Inaccurate	6.00	No	FY 2024 plan complete, will re-evaluate for FY 2025.
Division of Retiree Health Care	Retiree Insurance Payments Processed Incorrectly	6.00	No	FY 2024 plan complete, will re-evaluate for FY 2025.
Division of Retiree Services Payroll	Benefit Payment is not Accurate	6.00	No	FY 2024 plan complete, will re-evaluate for FY 2025.
Division of Retiree Services Payroll	Benefits Received by Wrong Individual	6.00	No	FY 2024 plan complete, will re-evaluate for FY 2025.
Division of Retiree Services Payroll	Dependent Child Payments are Inaccurate	6.00	No	FY 2024 plan complete, will re-evaluate for FY 2025.
Division of Retiree Services Payroll	Monthly Payroll is Inaccurate	6.00	No	FY 2024 plan complete, will re-evaluate for FY 2025.
Division of Retiree Services Payroll	Supplemental Payroll is Inaccurate	6.00	No	FY 2024 plan complete, will re-evaluate for FY 2025.
Board of Trustees	Lack of Training for Board of Trustees	5.00	No	FY 2024 plan complete, will re-evaluate for FY 2025.
Board of Trustees	Violation of Open Meetings	5.00	No	FY 2024 plan complete, will re-evaluate for FY 2025.
Executive Director	Cash Receipt Process	5.00	No	FY 2024 plan complete, will re-evaluate for FY 2025.
Office of Investments	Capital Call Process	5.00	No	FY 2024 plan complete, will re-evaluate for FY 2025.
Office of Investments	Investment Services Provided by Duplicate Vendors	5.00	Yes	Currently being reviewed by Investments
Office of Investments	Repo Process	5.00	No	FY 2024 plan complete, will re-evaluate for FY 2025.
Office of Legal Services - Advocacy	Non-compliance with HIPAA.	5.00	Yes	Recently audited, will not be on the FY 2024 plan.
Office of Legal Services - Non-Advocacy	Administrative Regulations may be Expired	5.00	Yes	FY 2024 plan complete, will re-evaluate for FY 2025.
Office of Legal Services - Non-Advocacy	Violation of Open Records Request	5.00	No	FY 2024 plan complete, will re-evaluate for FY 2025.
Division of Communications	Communications to Legislatures may not be Timely	5.00	No	FY 2024 plan complete, will re-evaluate for FY 2025.
Division of Human Resources	Non-compliance with FMLA	5.00	No	FY 2024 plan complete, will re-evaluate for FY 2025.
Division of Human Resources	Non-Compliance with Worker's Compensation	5.00	No	FY 2024 plan complete, will re-evaluate for FY 2025.
Division of Accounting > Cash Management Branch	Accounts Payable Process	5.00	Yes	Recently audited, will not be on the FY 2024 plan.
Division of Accounting > Cash Management Branch	Accrual Process	5.00	No	FY 2024 plan complete, will re-evaluate for FY 2025.
Division of Accounting > Cash Management Branch	Excise Tax Calculation and Payment Process	5.00	No	FY 2024 plan complete, will re-evaluate for FY 2025.
Division of Accounting > Cash Management Branch	Expenditures Coded Improperly	5.00	Yes	Recently audited, will not be on the FY 2024 plan.
Division of Accounting > Investment Operations Branch	Transfers to Mellon may not be Routed to Proper Account	5.00	Yes	Recently audited, will not be on the FY 2024 plan.

KPPA Internal Audit Risk Assessment Report

High Risk	Item being recommended for the FY 2024 audit plan.
Medium Risk	Carry-over from prior plan. Will be included on FY 2024 plan.
Low Risk	Included as a part of every audit.

Entity Path	Strategic Risk Title	Inherent	Reviewed in the Past 5 years?	Notes
Division of Enterprise and Technology Services > Application Services	System Build Process is Inefficient	5.00	No	FY 2024 plan complete, will re-evaluate for FY 2025.
Division of Disability and Survivor Benefits > Disability Branch	Additional Disability Payments not Reported to KPPA	5.00	No	FY 2024 plan complete, will re-evaluate for FY 2025.
Division of Disability and Survivor Benefits > Survivor Benefits Branch	Benefit Payments not Properly Supported	5.00	No	FY 2024 plan complete, will re-evaluate for FY 2025.
Division of Disability and Survivor Benefits > Survivor Benefits Branch	Members/Beneficiaries Reported as Deceased are Still Living	5.00	Yes	Recently audited, will not be on the FY 2024 plan.
Division of Disability and Survivor Benefits > Survivor Benefits Branch	Members/Beneficiaries Reported as Living are Deceased	5.00	No	FY 2024 plan complete, will re-evaluate for FY 2025.
Division of Membership Support	Forms are not User Friendly	5.00	No	FY 2024 plan complete, will re-evaluate for FY 2025.
Division of Retiree Health Care	Inaccurate Enrollment Numbers	5.00	No	FY 2024 plan complete, will re-evaluate for FY 2025.
Division of Retiree Services Payroll	1099-R Process	5.00	Yes	Recently audited, will not be on the FY 2024 plan.
Division of Communications	Print Vendor is not Efficient	4.00	No	FY 2024 plan complete, will re-evaluate for FY 2025.
Division of Human Resources	Badge System	4.00	No	FY 2024 plan complete, will re-evaluate for FY 2025.
Division of Human Resources	Improper Handling of Classified versus Unclassified Employees	4.00	No	FY 2024 plan complete, will re-evaluate for FY 2025.
Division of Human Resources	Time Reporting may not be Accurate	4.00	No	FY 2024 plan complete, will re-evaluate for FY 2025.
Division of Accounting > Cash Management Branch	Budget Process	4.00	No	FY 2024 plan complete, will re-evaluate for FY 2025.
Division of Accounting > Cash Management Branch	Employer Penalty Invoices Waived Improperly	4.00	Yes	Recently audited, will not be on the FY 2024 plan.
Division of Accounting > Cash Management Branch	ProCard Process	4.00	Yes	Recently audited, will not be on the FY 2024 plan.
Division of Accounting > Cash Management Branch	Travel Reimbursement Process	4.00	Yes	Recently audited, will not be on the FY 2024 plan.
Division of Employer Reporting, Compliance, and Education	Hazardous Duty Classification is Inaccurate	4.00	No	FY 2024 plan complete, will re-evaluate for FY 2025.
Division of Enterprise and Technology Services	Hardware/Software is Outdated	4.00	No	FY 2024 plan complete, will re-evaluate for FY 2025.
Division of Procurement and Office Services > Procurement Branch	Contracts not Tracked Properly	4.00	Yes	Recently audited, will not be on the FY 2024 plan.
Division of Procurement and Office Services > Office Services Branch	Building not Physically Secure	4.00	Yes	Recently audited, will not be on the FY 2024 plan.
Division of Disability and Survivor Benefits > Disability Branch	Reasonable Accommodations Requirement not Met	4.00	No	FY 2024 plan complete, will re-evaluate for FY 2025.
Division of Disability and Survivor Benefits > Survivor Benefits Branch	Unclaimed Account Process	4.00	No	FY 2024 plan complete, will re-evaluate for FY 2025.
Division of Retiree Health Care	Ineligible Dependents on Insurance	4.00	No	FY 2024 plan complete, will re-evaluate for FY 2025.
Division of Retiree Services Payroll	Deductions Entered Inaccurately	4.00	No	FY 2024 plan complete, will re-evaluate for FY 2025.
Division of Retiree Services Payroll	EFT Return Process	4.00	No	FY 2024 plan complete, will re-evaluate for FY 2025.
Division of Enterprise and Technology Services > Desktop Support	Support Tickets not Resolved Timely	3.00	Yes	Recently audited, will not be on the FY 2024 plan.
Board of Trustees	Improper Board of Trustees Composition	2.00	Yes	Reviewed with each Trustee change.
Division of Communications	Legislation that Impacts KPPA may not be Tracked	2.00	Yes	Reviewed by Communications



Kentucky Public Pensions Authority
Internal Audit Administration



To: Members of the Joint Audit Committee
 From: Kristen N. Coffey, CICA *KNC*
 Division Director, Internal Audit Administration
 Date: May 25, 2023
 Subject: Open Audit Findings and Recommendations

The Division of Internal Audit Administration (Internal Audit) has been working on a project to review all open internal audit findings. As of May 13, 2023, the following recommendations remain open. Internal Audit staff will continue to track these items and updates on the status of these items will be made to the Audit Committee quarterly.

This is presented for informational purposes only.

Entity	Project Name	Business Contact	Issue Title	Recommendation Title	Revised Implementation Due Date
Office of Investments	2022-1.1 Plan Liquidity Phase 1	Steve Willer	Duplicate Services may be Provided	Determine if Duplicate Investment Services are Being Provided by Vendors	This is currently under review. Revised date is unknown.
Procurement Branch	2020-1 Procurement and Contract Management	Kathy McNaughton	Training not Provided for Contract Monitoring	Provide Training to Those Responsible for Contract Monitoring	This is planned for early in the fiscal year.
Office Services Branch	2019-1 Building Security	Anne Baker	Policy Manual not Developed	Develop Policy Manual Specific to Building Security	6/30/2023
Security	2021-3 System Access	Chris Johnson	Manual Reviews not Completed Timely	Establish Deadline for Completing Manual Reviews	8/31/2023
Security	2021-3 System Access	Chris Johnson	Security Access Reviews not Completed Timely	Establish Deadline for Completing Security Access Reviews	8/31/2023
Office Services Branch	2019-1 Building Security	Anne Baker	Additional Security Training Needed	Provide Additional Security Training to Staff	9/29/2023



Kentucky Public Pensions Authority

Internal Audit Administration



Kentucky Public
Pensions Authority

To: Members of the Joint Audit Committee

From: Kristen N. Coffey, CICA *KNC*
Division Director, Internal Audit Administration

Date: May 25, 2023

Subject: Final Audit Report Released

Please find attached the final audit report entitled **Accuracy of Information Sent to Humana and DEL**. The report is dated April 14, 2023. The Division of Internal Audit Administration noted three findings, all verbal, which are summarized below. The final audit report is attached for your review.

Summary of Audit Results

1. It was found that several procedures still referred to Kentucky Retirement Systems. The procedures have since been updated, resolving this issue.
2. During review of procedures, it was found that the output names for several semi-automated processes were incongruent with what was indicated by the procedures. The procedures have since been updated.
3. During calendar year 2021, several discrepancies and issues reported to Retiree Health Care were not resolved in a timely manner, with an average open time of 275 days. Management is currently determining a deadline for resolving discrepancies. Procedures will be updated to reflect the new process.

Attachment

No action is required of the Committee.

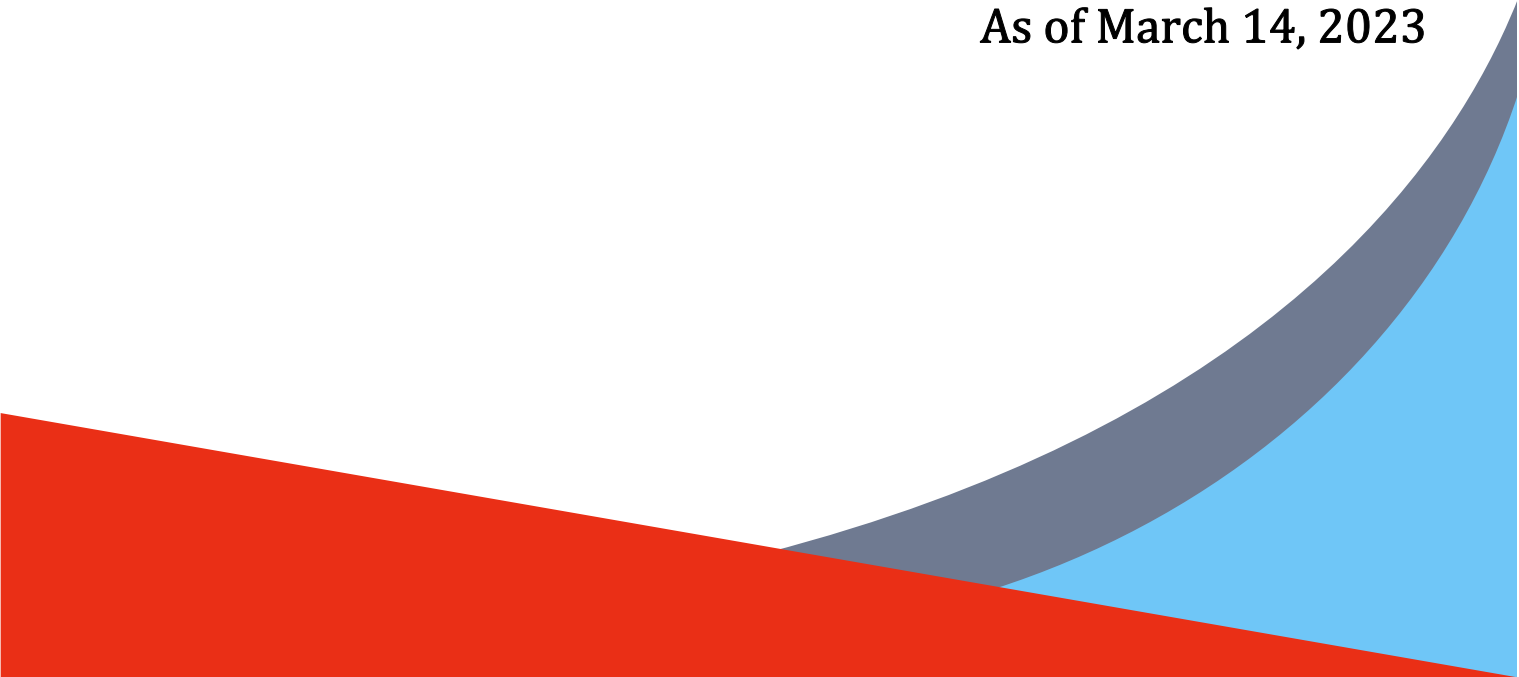


KPPPA

Kentucky Public Pensions Authority

Accuracy of Information Sent to Humana and DEI

As of March 14, 2023



Acronyms

The following acronyms will be used throughout the report:

1. KPPA - Kentucky Public Pensions Authority
2. CERS - County Employees Retirement System
3. KRS - Kentucky Retirement System
4. DETS – Division of Enterprise Technology Services
5. RHC – Retiree Health Care
6. DEI – Department of Employee Insurance
7. LOB – Line of Business
8. KPPA Executive Management team - KPPA Executive Director, KPPA Deputy Executive Director, KPPA CIO, KPPA Executive Director-Office of Legal Services, and KPPA Executive Director-Office of Benefits

Objective

The objectives of our review of the Accuracy of Information Sent to Humana and DEI were to ensure internal controls have been designed and are operating effectively and efficiently. We also ensured compliance with applicable state and federal statutes and regulations as well as policies established by the CERS and KRS Boards and procedures developed by KPPA staff.

Executive Summary

Our review found that processes related to Accuracy of Information Sent to Humana and DEI are operating effectively and efficiently and comply with state and federal statutes and regulations as well as agency policies and procedures. Additional information is noted in the Commendations section of the report.

Commendations

We would like to acknowledge both RHC and DETS for their cooperation and prompt responses during this audit, despite the latter not being the main subject of the audit. Our interactions with RHC over the course of this audit have shown us that they strive to exhibit excellent customer service with everyone, not just our members.

In addition to our interactions with RHC during this audit, we would also like to acknowledge their achievements as a department. Since the start of the COVID-19 pandemic, RHC has reduced overtime, met deadlines, and maintained a consistent level of customer service despite increasing numbers of members and their dependents. They have also implemented several successful tele-services including Telehealth, retiree webinars, and retiree outreach with the goal of keeping retirees informed about their benefits.

Risks Identified During the Project

Risks that were identified and tested during the audit are listed below. For each risk identified, auditors determined if a control had been established to mitigate the risk. If so, auditors ensured the internal controls established were designed and operating effectively and efficiently. Where applicable, auditors ensured the process complied with applicable statutes, regulations, and policies.

1. Files are not sent to DEI/Humana at all or are not sent timely.
2. Batches do not run each night.
3. Files are transferred to DEI/Humana prematurely during open enrollment and other events.
4. Remittance files not submitted timely to DEI and Humana after monthly payroll.
5. Changes could occur to a file in the time between when it is generated and when it is transferred to DEI/Humana or some changes to member profiles are not captured by the Master Schedule.
6. Changes needed in response to DEI and Humana files are not made in a timely manner.
7. Member information in START differs from the information held by DEI/Humana.
8. Members are signed up for plans for which they do not qualify.

Scope, Sampling, and Methodology

The scope of the audit was January 1, 2021 through December 31, 2021. During that time frame, there were 1,243 reports, which included over 12,000 KPPA members.

While most of our testing featured the complete populations of relevant data, some tests required sampling due to the size and manual nature of the review.

In populations where a sample was determined to be appropriate, the population was broken down by unique individuals, rather than individual appearances of members on the reports. The unique individuals were then assigned a number by order of appearance and randomly selected for testing.

The following steps were performed to ensure the processes and procedures surrounding the information flowing between KPPA, DEI, and Humana complied with applicable state and federal guidelines as well as policies and procedures established by the KPPA Board and management.

- Reviewed current KPPA policies and procedures to determine if they were accurate and properly reflected the actual processes being followed.
- Verified the inclusion of files meant to synchronize data between KPPA and DEI in the monthly batch schedule.
- Ensured that files communicated daily to DEI and Humana had an appropriate file archived.
- Determined the plausibility of changes occurring to the archived files before they were sent to DEI and Humana
- Reviewed employee access to archived files.
- Compared data from DEI and Humana to member profiles to determine if changes were appropriate and if so, ensured the changes were made.
- Ensured changes to member information were made in a timely manner and documented appropriately.

Recommendations for Future Audits

During this audit, we noted one item that has been recommended for review in a future audit.

- Reimbursements of Overpayments Related to DEI and Humana

Background

To ensure member information is consistent between KPPA, DEI, and Humana, DETS facilitates the near daily communication of the updates RHC makes to member information to DEI and Humana. In turn, DEI and Humana provide regular reports to RHC regarding discrepancies between themselves and the information contained in LOB. RHC counselors identify all issues indicated in these reports and investigate the discrepancies. During their research, they may find that updates need to be made to the member's profile in LOB or that information needs to be updated on file at DEI or Humana.

This report is intended solely for use by the Joint Audit Committee; the CERS and KRS Boards; the Executive Management teams for KPPA, CERS, and KRS; the Division of Retiree Health Care; and the Division of Enterprise Technology Services. This report is not intended to be, and should not be, used by anyone other than the specified parties. All final reports are subject to Open Records Requests.



Kentucky Public Pensions Authority

Internal Audit Administration



Kentucky Public
Pensions Authority

To: Members of the Joint Audit Committee

From: Kristen N. Coffey, CICA *KNC*
Division Director, Internal Audit Administration

Date: May 25, 2023

Subject: Final Audit Report Released

The Division of Internal Audit Administration recently completed the Plan Liquidity – Daily Cash Review audit. Two findings were noted, which are summarized below. The final audit report, which includes detailed findings and recommendations as well as management’s responses are attached for your review. We have also included a copy of the Management Letter issued as a part of this audit.

Summary of Audit Results

1. Investment fees not allocated correctly.
2. Reconciliation failed to detect errors (management letter item).

Attachment

No action is required of the Joint Audit Committee.



KPPA

Kentucky Public Pensions Authority

**Plan Liquidity Phase 3 - Available Cash Balance/Cash
Projection**

Issued May 15, 2023

Acronyms

The following acronyms will be used throughout the report:

1. KPPA - Kentucky Public Pensions Authority
2. CERS - County Employees Retirement System
3. KRS - Kentucky Retirement System
4. KPPA Executive Management team - KPPA Executive Director, KPPA Deputy Executive Director, KPPA CIO, KPPA Executive Director-Office of Legal Services, and KPPA Executive Director-Office of Benefits
5. Investment Operations – KPPA Division of Accounting, Investment Operations branch
6. Internal Audit – KPPA Division of Internal Audit Administration
7. Repo -Repurchase Agreement
8. ISF – Institutionally Secured Funding
9. BNY Mellon/custodial bank - Bank of New York Mellon

Objective

The objectives of our Plan Liquidity Phase 3 – Available Cash Balance/Cash Projection audit were to ensure internal controls have been designed and are operating effectively and efficiently. We also ensured compliance with applicable state statutes and regulations as well as policies established by the CERS and KRS Boards and procedures developed by KPPA staff.

Executive Summary

The following findings were noted during our review of Plan Liquidity Phase 3 – Available Cash Balance/ Cash Projection. The related recommendations can be found in the Audit Results section of the report.

1. Investment fees allocated incorrectly

We noted one other matter that we communicated to Investment Operations in a separate letter dated May 15, 2023.

Commendations

Internal Audit staff appreciate the cooperation of the KPPA Investment Operations staff. This audit involved multiple meetings and questions to clarify the established internal controls. Investment Operations took initiative to correct errors found during the audit and they began developing procedures to address the risks identified.

Sampling, Risks, Methodology, and Testing Results

No sampling was used. 100% of the 4,160 transactions were reviewed.

Methodology Matrix	
Risk: BNY Mellon cash projection differs from the Investment Operation's cash projection.	
Control	Testing
Investment Operations compares the daily cash projection worksheet to the cash projection worksheet from BNY Mellon. The acceptable variance threshold is \$100,000 between the two projections. If the difference is above the acceptable variance, Investment Operations staff determine what is causing the difference and this is noted in the investable cash email.	Auditor compared the two projections and found the difference between the Investment Operations and BNY Mellon calculations. If the variance was more than \$100,000 then auditor requested an explanation for the difference to determine if the variance was reasonable.
Results of testing: No exceptions noted.	

Risk: The same person who affirmed a repo is the same person who reviewed BNY cash projection against OPS projection.	
Control	Testing
To create a segregation of duties, the same person should not be preparing the investable cash email and affirming repos.	Auditor compared initials of staff who prepped the investable cash email and who affirmed the day's repo.
Results of testing: No exceptions noted.	
Risk: Investable cash email is sent to the Investment directors late causing the Repo investment to be delayed.	
Control	Testing
Investable cash email is sent around 10:00 am.	Compared time stamp of "Investable cash email" from Investment Operations staff to Investment Portfolio Managers against the target time of 10:00 a.m. Auditor considered the email to be sent timely if it was sent by 10:30 (allowed 30-minute window). If the email for any day was sent outside of this window, auditor requested an explanation of why the email was late to determine if the delay was reasonable.
Results of testing: No exceptions noted.	
Risk: Transactions flow through cash account incorrectly.	
Control	Testing
Investment Operations staff saves all backup documentation and records the transaction in the Cash Projection Worksheet and Cashflow Worksheet. BNY Mellon's Cash Projection Worksheet is compared against Investment Operations Daily Cash Projection Worksheet and BNY Mellon's Settled Cash Statement is compared against Investment Operations Cashflow Worksheet.	Auditor compared all transaction backup documents to the Settled Cash Statement to confirm that the total and date were accurate according to the corresponding supporting documents.
Results of testing: One distribution was approved by BNY for the wrong total and the corresponding day's reconciliation did not catch the error. (Addressed in a management letter)	
Risk: Transaction is not approved appropriately.	
Control	Testing
Appendix C of the contract with BNY Mellon specifies access and approval capabilities within Nexen.	Auditor compared the approving user ID to the Authorized Signer List. Auditor noted who sent KPPA Accounting wires to verify that appropriate staff sent the wires.
Results of testing: No exceptions noted.	
Risk: Transactions are allocated across the 5 plans incorrectly.	
Control	Testing
The daily cash reconciliation procedures compare the Plan Percent report cash balances from the prior day and current day activity against current day's closing balance from corresponding Plan Percent report. These two sums should match indicating that all custom allocations were applied correctly by BNY Mellon staff.	Auditor created a database with all transactions showing the total and the breakdown between the five plans. Using this database, Auditor reconciled all 261 business days for the Pension and Insurance master trust funds. This was to verify custom allocations. For non-custom allocations, Auditor compared the manager's accounting number from the plan schematics against the account number shown on the settled cash statement.
Results of testing:	
1. Sixteen daily reconciliations did not catch that investment fees were allocated incorrectly. (See finding #1: Investment fees allocated incorrectly)	

2. Two capital calls for L-A VII were approved for L-A VII B. The total of the capital calls was keyed correctly but the allocation was applied to the incorrect manager. The corresponding daily reconciliations did not catch this error. (Addressed in a management letter)	
Risk: Plan accounts or the master trust accounts are overdrawn.	
Control	Testing
Projected end of day cash balance is calculated using the Cash Projection worksheet, which captures all known incoming and outgoing transactions.	During testing of daily reconciliations, Auditor verified that plan accounts and master trust accounts were not overdrawn by confirming that these accounts never had a \$0 balance.
Results of testing: No exceptions noted.	
Risk: Details for Repos are approved for incorrect REPO details.	
Control	Testing
Investment Operations staff approving the repo compares the Letter of Direction from the Investment team to information entered into Cantor Fitzgerald portal. If total, interest rate and interest at maturity match, then Investment Operations staff approves the trade. Investment Operations staff then takes a screenshot of the approved repo.	Auditor compared the Letter of Direction to the screenshot of the approved repo to confirm that all details matched.
Results of testing: No exceptions noted.	

Recommendations for Future Audits

1. Evaluate how each manager balance is monitored on an individual basis to ensure that management fees, performance fees and capital calls follow the agreed upon investment relationship.
2. Investment fee re-calculation and reconciliation.
3. Repo and ISF creation process by Investment Portfolio Managers.
4. Monthly reconciliation between BNY Mellon and Great Plains.

This report is intended solely for use by the Joint Audit Committee; the CERS and KRS Boards; the Executive Management teams for KPPA, CERS, and KRS; and Investment Operations. This report is not intended to be, and should not be, used by anyone other than the specified parties. All final reports are subject to Open Records Requests.

Audit Results

1. Investment fees allocated incorrectly

Responsible Area(s):	Investment Operations																												
Condition:	<p>Sixteen daily reconciliations (8 Pension and 8 Insurance) did not detect that investment fees were allocated in a manner differently than directed by the custom allocations provided by Investment Operations. After auditor reconciled KRS AVG reports against interest income and investments fees, the residual difference explained by fees being allocated incorrectly across the plans is shown in the following charts.</p> <table border="1" style="width: 100%; border-collapse: collapse;"> <thead> <tr> <th>Total residual difference</th> <th>KERS</th> <th>KHAZ</th> <th>CERS</th> <th>CHAZ</th> <th>SPRS</th> <th>PEN Total</th> </tr> </thead> <tbody> <tr> <td>\$</td> <td>(274,692.82)</td> <td>\$ 4,735.83</td> <td>\$ 238,608.79</td> <td>\$ 65,158.41</td> <td>\$ (33,951.30)</td> <td>\$ (141.09)</td> </tr> </tbody> </table> <table border="1" style="width: 100%; border-collapse: collapse;"> <thead> <tr> <th>Total residual difference</th> <th>KERS</th> <th>KHAZ</th> <th>CERS</th> <th>CHAZ</th> <th>SPRS</th> <th>INS Total</th> </tr> </thead> <tbody> <tr> <td>\$</td> <td>(30,654.12)</td> <td>\$ 15,284.01</td> <td>\$ (6,660.95)</td> <td>\$ 20,724.53</td> <td>\$ 5,306.74</td> <td>\$ 4,000.21</td> </tr> </tbody> </table>	Total residual difference	KERS	KHAZ	CERS	CHAZ	SPRS	PEN Total	\$	(274,692.82)	\$ 4,735.83	\$ 238,608.79	\$ 65,158.41	\$ (33,951.30)	\$ (141.09)	Total residual difference	KERS	KHAZ	CERS	CHAZ	SPRS	INS Total	\$	(30,654.12)	\$ 15,284.01	\$ (6,660.95)	\$ 20,724.53	\$ 5,306.74	\$ 4,000.21
Total residual difference	KERS	KHAZ	CERS	CHAZ	SPRS	PEN Total																							
\$	(274,692.82)	\$ 4,735.83	\$ 238,608.79	\$ 65,158.41	\$ (33,951.30)	\$ (141.09)																							
Total residual difference	KERS	KHAZ	CERS	CHAZ	SPRS	INS Total																							
\$	(30,654.12)	\$ 15,284.01	\$ (6,660.95)	\$ 20,724.53	\$ 5,306.74	\$ 4,000.21																							
Criteria:	Investment Operations staff prepare a custom allocation and provide these via email to the BNY Mellon Cash Management and Accounting teams. The BNY Mellon Accounting team then copies and pastes the values from the email into a spreadsheet used to apply custom allocations.																												
Cause:	<ol style="list-style-type: none"> 1. Investment Operations did not include BNY Mellon Accounting team on the email showing how the fee should be allocated. 2. BNY Mellon Cash Management team did not forward the email from Investment Operations to the BNY Mellon Accounting team. 3. Investment Operations did not reconcile investment fees to the KRS AVG report generated mid-month, which shows allocations for investment fees, litigation income, and interest. 																												
Effect:	Each plan was charged the wrong amount for investment fees causing a misstatement on financial records. Since the KRS AVG report is not reviewed and is only taken as realized/loss gain, inaccurate transactions may go undetected.																												
Recommendations:	<ol style="list-style-type: none"> 1. Investment Operations staff should continue working with BNY Mellon staff to determine how far back this issue has persisted. Once the total amount is known, Investment Operations should ensure correcting entries are made to the plan accounts. 2. Investment Operations should establish procedures to ensure that the allocation of investment fees shown in the KRS AVG report matches the allocation from Investment Operation emails. 																												
Recurring Issue:	No																												
Management Response:	We concur with the finding and have taken action to ensure the allocation of investment administrative expenses are properly reviewed. This was implemented in fiscal year 2023. We are currently working with BNY Mellon to quantify and correct any historical discrepancies. Depending on the availability of historical data from BNY Mellon we expected to have this completed by June 30, 2023.																												
Implementation Date:	12/29/2023																												

Exhibit A

Background

Section A: Daily cash projection procedures

There are a total of ten worksheets and statements used in this process. Six worksheets and statements are created by BNY Mellon Cash Management or BNY Mellon Accounting staff. The remaining four worksheets were created by KPPA Investment Operations staff.

BNY Mellon Worksheet Descriptions

Every morning BNY Mellon automatically sends one email with a zip file that contains the *Plan Percent* and *Unit Trade* spreadsheets. BNY Mellon Cash Management team then sends Investment Operations two additional excel files pertaining to the prior business day: *Cash Account Accruals* and *Unit Trade Details*. These files are saved to the Office of Investments shared drive.

1. *Unit Trade Details*- This shows the total incoming and outgoing transfers for each system for the prior business day. The first two tabs show incoming and outgoing wires for the day, which would capture transactions such as the daily qualification wire, recurring/supplemental payroll, and Department of Employee Insurance/Humana payments. The next two tabs called "Pension Strip" and "Insurance Strip" provide the BNY Mellon account number, total amount, asset class/name of the manager for all other types of transactions. To the right of this information there is the allotment percentage used to breakdown the total into the system specific amount for each fund. The "strip" tabs show the allocation across the five systems for all non-custom transactions and trade transfer requests (custom and non-custom).
2. *Unit Trade* - This spreadsheet reports the purchase and sale of cash units and any realized gain/loss associated with those transactions.
3. *Plan Percent* - This spreadsheet provides each system's ownership of each unit at the end of the prior day.
4. *Cash Account Accruals* - This spreadsheet provides the posting of accruals for anticipated income. The information in this worksheet is generated based on work performed by the BNY Mellon Accounting team.

The above reports are all general ledger reports prepared by the BNY Mellon Accounting team utilizing the same data set. As such, a comparison of these reports is not a true reconciliation because the data is not being compared to an independent, original source document.

In addition to the four reports explained above, Investment Operations staff also log into BNY Mellon Nexen to generate two *Settled Cash Statements* of all non-zero balances, one for the prior day and one for the current business day, as well as a *Current Projected Cash Worksheet* for the current business day. The information in these documents is generated based on work performed by the BNY Cash Management team.

Description of Transactions

While the six worksheets and statements above are being sent by BNY Mellon or generated in Nexen, the backup documentation for other account activity is being sent to Investment Operations. As of the completion of fieldwork for Phase III, this audit reviewed 12 types of transactions that move through the investment cash accounts at BNY Mellon. Most have backup documentation, but some are automatic transactions handled by BNY Mellon Cash Management and/or Accounting teams that do not have independent backup documentation.

The chart below shows the 12 types of transactions reviewed; the required backup documentation; and which groups are responsible for preparing, keying, approving, recording, and allocating each transaction.

Definition of actions:

- Prepare – This group reviewed the data to create the transaction type and has notified Investment Operations of what will happen in the cash accounts. If a custom allocation is needed, then the breakdown is provided. A custom allocation is a breakdown of a transaction that is not predetermined in BNY Mellon’s system.
 - KPPA groups who “prepare” a transaction type have separate procedures on SharePoint or the group’s KPPA drive to explain the review conducted of the data involved. Specific questions about how these transactions are created should be directed to the appropriate group.
- Key – This group took action in Nexen to create a movement to or from the cash accounts at BNY Mellon.
- Approve – This group reviewed what was keyed into Nexen and matched it to the details in the Nexen system.
- Record – This group added a transaction to one of the four worksheets used by Investment Operations to track and monitor the cash accounts.
- Allocate – This group split a transaction up across the five systems (KERS, KHAZ, CERS, CHAZ, SPRS) in the BNY Mellon cash accounts according to the predetermined percent breakdown in the Nexen system or by the given custom allocation.
- No action – This group has no involvement in the actions described above.

#	Transaction type	Required Backup Documents	Team Actions			
			KPPA Cash Management	KPPA Investment OPS	KPPA Investment Directors	BNY Staff
1	Daily Qualification Wires		Prepare	Record	No Action	Key & Approve from flow thru, Allocate
2	DEI, Humana and WEX Health Payments	Email from KPPA cash management with custom allocation	Prepare, Key, Approve	Record	No Action	Allocate
3	Recurring Supplemental Payments		Prepare, Key, Approve	Record	No Action	Allocate
4	KPPA Admin Expenses		Prepare, Key, Approve	Record	No Action	Allocate
5	Trade Transfer Requests	Email from KPPA Investment Director with direction on allocation type. Either "At current allocation" or a given custom allocation.	No Action	Record	Prepare	Key, Approve, Allocate
6	Repo/ ISF trades	Repo - Letter of direction from Investment directors ISF - Trade ticket submitted by Investment Directors	No Action	Approve Repo Only, Record Both	Prepare	Key Both, Approve ISF, Allocate Both
7	Capital Calls	Notification from Investment Manager	No Action	Approve (LP Only) and Record	No Action	Prepare, Key, Approve (Non-LP), Allocate
8	Distribution, Shares and Redemptions		No Action	Record	No Action	Prepare, Key, Approve, Allocate
9	Investment Fees	Invoice from vendor	No Action	Prepare, Key, Approve	No Action	Allocate
10	Residual Cash	No independent documentation due to automatic process	No Action	Record	No Action	Prepare, Key, Approve, Allocate
11	Interest Earned on Cash accounts		No Action	Record	No Action	Prepare, Key, Approve, Allocate
12	Foreign Exchange Transactions		No Action	Record	No Action	Prepare, Key, Approve, Allocate

Description of KPPA created worksheets and how they achieve Investment Operations objectives

The main objective of Investment Operations is to ensure that there is enough cash available to cover expenses and to complete daily investment activities. The secondary objective of Investment Operations is to confirm that BNY Mellon staff has correctly applied and allocated each deposit and expense according to the percent breakdown for each manager or KPPA created custom allocation. To keep track of all these transactions and to confirm the accuracy of BNY Mellon daily investable cash, Investment Operations created four worksheets: the Daily Cash Projection Worksheet, the Cashflow Worksheet, the Daily Cash Reconciliation Worksheet, and the Working Database.

Cash flow worksheets

	KERS	KERS HAZ	CERS	CHAZ	SPRS	TOTAL		
<i>Make sure to correctly label the transaction in column H for cash flow tracking (see bottom of sheet) - it must exactly match the descriptions</i>								
<i>Monday Dividend Sweeps</i>								
<i>Recurring Humana wire for Insurance every 30th</i>								
<i>Fill in first business day in cell below- all other days will populate - beware of holidays - copy this tab each month</i>						Repo Interest Due	TODAY'S REPO PURCHASE	0.00
July 1, 2020						0.00	at Cantor	
						0.00	ISF Note/ Muni Interest & Maturity	
						0.00	ISF Note/ Muni Interest & Maturity	
							ISF Purchase	
							ISF Purchase	
July 1, 2020	(0.01)	(18,303.72)	(202,300.89)	(69,049.19)	(5,770.19)	(295,424.00)	Capital Call	NMP IV
July 1, 2020	(56,369.93)	(17,361.50)	(191,472.35)	(65,937.72)	(6,729.77)	(337,871.27)	Capital Call	IFM USIDF
July 1, 2020	(0.01)	(15,037.07)	(166,196.47)	(56,726.06)	(4,740.39)	(242,700.00)	Capital Call	BHEP III
July 1, 2020	(3.94)	(0.50)	(4.71)	(1.47)	(0.26)	(10.87)	Investment Cash Outflow	Keyhaven Capital III
July 1, 2020	1,644,423.68					1,644,423.68	Accounting Contributions	Wire
July 1, 2020	0.39	0.12	1.34	0.46	0.05	2.36	Investment Cash Inflow	PIMCO All Asset
July 1, 2020	2,229,587.84	691,236.98	7,624,760.21	2,520,627.59	275,397.54	13,341,610.16	Investment Cash Inflow	ArrowMark

Figure 1: Right side of 7/1/2020 Pension Cashflow. This displays how each transaction was split up between the five systems (KERS, KHAZ, CERS, CHAZ, SPRS). The Keyhaven Capital III and PIMCO All

Asset transactions are examples of undocumented automatic transactions handled by BNY Mellon staff.

TODAY'S REPO PURCHASE		0.00						
TODAY'S INTEREST RATE	0.00							
at Cantor								
ISF Note/ Muni Interest & Maturity								
ISF Note/ Muni Interest & Maturity								
ISF Purchases								
ISF Purchases								
Capital Call	NMP IV							
Capital Call	IFM USDF							
Capital Call	BHEP III							
Investment Cash Outflow	Keyhaven Capital III							
Accounting Contributions	Wire							
Investment Cash Inflow	PIMCO All Asset							
Investment Cash Inflow	ArrowMark							

PE 2013	0.00000003	0.06195745	0.68478149	0.23372913	0.01953190
KRS IFM INFRASR DEBT	0.16683848	0.05138495	0.56670209	0.19515633	0.01991816
RE 2013	0.00000003	0.06195745	0.68478149	0.23372913	0.01953190
PE 2010	0.36251457	0.04584496	0.43299215	0.11478691	0.02386141
REAL RET	0.16683847	0.05138495	0.56670208	0.19515633	0.01991816
ARROWMARK	0.16711535	0.05181061	0.57150225	0.18892979	0.02064200

Figure 2: Left Side of 7/1/2020 Pension Cashflow. This displays the percent of each transaction assigned to the five systems (KERS, KHAZ, CERS, CHAZ, SPRS). The total of the decimal numbers equal 1 showing that 100% of a transaction has been accounted for by BNY Mellon Accounting team. These values are copied and pasted from the Unit Trades Detail worksheet. The “wire” transaction is the daily qualification wire, which is a custom allocation prepared by KPPA Accounting-Cash Management staff. BNY Mellon account numbers have been redacted for security purposes.

These worksheets are saved on the Office of Investments shared drive. This file is saved for each month and each day has its own section in the Pension and Insurance tabs. Transactions are only recorded on this worksheet when the transaction actually takes place. This worksheet also shows the plan percent breakdown for each manager with a transaction on any given day on the right-hand side of the worksheet. This is the first worksheet completed each day using the following steps.

1. KPPA’s Cashflow worksheet is opened and the section for the prior business day is compared against the corresponding BNY Mellon Settled Cash Statement. Anything on the prior business day’s Settled Cash Statement that is not already on KPPA’s Cashflow worksheet is added at this time. These two may not match for the prior business day because distributions may occur after the cutoff time and not appear on BNY Mellon’s statement until the following day.
 - i. This is how automatic transactions such as the ones mentioned in the caption of figure one above are added to the Cashflow worksheet.
2. Investment Operations inputs all known incoming and outgoing transactions for the current business day and future dates. For example, a manager sends a capital call notice that is due in a week. This notice will be keyed in the appropriate business day’s section of the Cashflow worksheet so when that day is the current business day, the reviewer knows to expect this on that day’s Settled Cash Statement.
3. The current business day is reviewed next. The current business day’s Settled Cash Statement should match the known transactions for the current business day on KPPA’s Cashflow worksheet. Usually these are already filled in because of step 2 but there may be an incoming wire created by KPPA Accounting-Cash Management that needs to be added.
 - i. Since the current day’s Settled Cash Statement is generated in the morning, there will most likely be transactions that happen after this is generated. Ideally, all steps in this section need to be completed around 10:00 a.m. so the Investment Portfolio Managers know how much can be invested in repos and ISFs. Some days this email may be sent later but the reason for the delay should be documented.

- ii. Any transactions that occur after the investable cash email is sent to Short Term Investment Fund (STIF) accounts by BNY Mellon staff because they will not be included in the repo calculation.

The **Daily Cash Projection Worksheet** is filled out next. The worksheet and all back up documentation for each day is saved on the Office of Investments shared drive. Each month has its own workbook and a tab is created for each business day. All transactions scheduled to take place "today" are posted in the top portion of the worksheet. The transactions in this section are separated into their assigned fund/system specific amount designated by the **Plan Percent Worksheet** or custom allocation. The sum of this section is called "Current Projected Cash." Transactions not yet due to be withdrawn or deposited are posted in the bottom section also separated into fund/system specific amounts, again, designated by the plan percent or the given custom allocation. The sum of this section is called "Future Projected Cash."

		KERS	KHAZ	CERS	CHAZ	SPRS	
6.30.20		124,045,671.57	23,007,485.04	184,178,597.56	69,269,422.26	9,931,110.13	410,432,286.56
7.1.20 - Wire		1,644,423.68					1,644,423.68
7.1.20 - NMP IV - Capital Call	PE 2013	(0.01)	(18,303.72)	(202,300.89)	(69,049.19)	(5,770.19)	(295,424.00)
7.1.20 - IFM USIDF - Capital Call	IFM INFRA DEBT	(56,369.88)	(17,361.48)	(189,112.84)	(66,300.33)	(6,729.77)	(337,871.27)
7.1.20 - BHEP III - Capital Call	PE 2013		(15,037.07)	(166,196.47)	(56,726.06)	(4,740.39)	(242,700.00)
Current Projected Cash Balance		125,633,725.36	22,956,782.77	183,620,987.36	69,077,346.68	9,913,869.78	411,200,714.97
Current Projected Cash Balance		125,633,725.36	22,956,782.77	183,620,987.36	69,077,346.68	9,913,869.78	411,200,714.97
7.2.20 - Reurring/Supplemental		(300,023.41)	(56,316.91)	(272,326.05)	(45,363.39)	(5,000.00)	(679,029.76)
7.7.2 - - SVSS IV - Capital Call	PE 2018		(75,991.50)	(932,032.51)	(290,976.00)		(1,299,000.00)
7.10.20 - VEP VI - Capital Call							(133,523.00)
7.13.20 - VEP III - Capital Call							(35,454.00)
7.13.20 - VEP IV - Capital Call							(106,306.00)
7.15.20 - Patron - Capital Call							(€ 195,100.00)
7.15.20 - LLCP V - Capital Call							(251,774.00)
7.15.20 - LLCP VI - Capital Call							(328,125.00)
7.16.20 - BHEP III - Capital Call							(177,980.00)
Future Projected Cash		125,333,701.95	22,824,474.36	182,416,628.80	68,741,007.29	9,908,869.78	407,994,423.21
Anticipated Cash Inflow							
7.7.20 - MWREIF - Dist							349,081.97
Future Projection with Inflow		125,333,701.95	22,824,474.36	182,416,628.80	68,741,007.29	9,908,869.78	408,343,505.18

Figure 3: Screen shot of 7/1/2020 Pension Daily Cash Projection worksheet. The Cashflow worksheet and the Daily Cash Projection worksheet differ because the automatic transactions from Keyhaven Capital III and PIMCO All Assets have not yet occurred on the morning of 7/1/2020.

- 4. An Investment Operations staff member then opens the Daily Cash Projection worksheet for the day and keys in the same known incoming and outgoing transactions in the appropriate sections for each day that were keyed in step #2. For example, Investment Operations receives a capital call notice on 7/1/2020 that is not due until 7/10/2020. This capital call will be recorded in the "Future Projected Balance" section from 7/1/2020 until 7/9/2020.

On 7/10/2020 the posting then moves up to the "Current Projected" section. This is the final posting of this call.

5. After all known information is keyed in the Daily Cash Projection worksheet, the preparing Investment Operations staff member will compare the sum of everything in the "Current Projected Balance" section to the Projected Cash Worksheet from BNY Mellon generated in Nexen by an Investment Operations staff member. The "Current Projected Balance" and the balance on BNY Mellon's projected cash worksheet should be similar. During this audit, it was noted that a variance of \$100,000 was deemed acceptable. As of February 2022, this threshold was dropped to \$25,000. If the difference is outside the acceptable threshold, the preparing Investment Operations staff researches the discrepancy to determine the cause of the difference. The reason for the difference should be noted on the spreadsheet. KPPA staff may need to contact BNY Mellon for assistance identifying the cause of the difference. Typically, the difference is the result of accruals in the cash account, which is a result of the anticipated interest due for outstanding cash investments such as repo, ISF and STIF.
 - i. The acceptable variance threshold will change over time due to the cash balance and interest earned on STIF accounts.
 1. The cash balance is influenced by Investment Portfolio Manager actions. Sometimes it will be high if investment staff are wanting to fund new managers. Other times it will be low to balance out asset classes.
 2. The interest earned on STIF accounts is not an item that KPPA can control or predict. This is also not documented, which means it will not show up in the Daily Cash Projection worksheet, which will cause a difference.
6. The preparing Investment Operations staff member will send an email as soon as possible to KPPA Investment Portfolio Managers with the BNY Mellon projected cash amounts. If Investment Operations staff run into issues during step #5, Investment Portfolio Managers will be notified that investable cash email will be sent later during the day. BNY Mellon is the custody of all the above KPPA financial information which means that their projected cash should be correct. This projected cash is used in a calculation by Investment Portfolio Managers to determine how much can be invested in the short-term vehicles, Repos and Institutional Secure Funding Program (ISFs). In the event of negative cash balances in the future, Investment Operations staff should alert the Office of Investments.

Finally, the ***Daily Cash Reconciliation Worksheet*** is completed for the prior business day and saved on the Office of Investments shared drive. Each month has its own file, and each day has its own section for Pension and Insurance. In the following steps, true current business day will be referred to as T and prior business days will be T-1 and T-2.

PENSION FUND						
	KERS	KHAZ	CERS	CHAZ	SPRS	Total
June 30, 2020	123,598,994.28	22,980,879.27	184,544,927.37	69,414,663.29	9,887,952.49	410,427,416.70
wire in	1,644,423.68	0.00	0.00	0.00	0.00	1,644,423.68
wire out	0.00	0.00	0.00	0.00	0.00	0.00
PIMCO All Asset	0.39	0.12	1.34	0.46	0.05	2.36
IVP XII	177,589.36	22,458.62	212,115.06	66,029.68	11,689.28	489,882.00
BDCM IV	0.00	10.97	121.21	41.37	3.46	177.00
LLCP VI	0.00	1,218.54	14,302.78	4,454.64	0.00	19,975.96
ArrowMark	2,229,587.84	691,236.98	7,624,760.21	2,520,627.59	275,397.54	13,341,610.16
NMP IV	(0.01)	(18,303.72)	(202,300.89)	(69,049.19)	(5,770.19)	(295,424.00)
IFM USIDF	(56,369.93)	(17,361.50)	(191,472.35)	(65,937.72)	(6,729.77)	(337,871.27)
BHEP III	(0.01)	(15,037.07)	(166,196.47)	(56,726.06)	(4,740.39)	(242,700.00)
	127,594,225.61	23,645,102.20	191,836,258.26	71,814,104.06	10,157,802.45	425,047,492.59
July 1, 2020	127,594,225.60	23,645,102.21	191,836,258.26	71,814,104.06	10,157,802.47	425,047,492.60
Daily Total	0.01	(0.01)	(0.00)	0.00	(0.02)	(0.01)
Unit Trades Realized Gain/Loss	0.00	0.00	0.00	0.00	0.00	0.00
Final	0.01	(0.01)	(0.00)	0.00	(0.02)	(0.01)

Figure 4: Screen shot of 7/1/2020 daily cash reconciliation worksheet. The Keyhaven Capital III automatic transaction is not included in this reconciliation because it was not included on the 7/1/2020 Unit Trades Detail report which means that this transaction has not yet been allocated across the systems by BNY accounting group on 7/1/20.

7. Closing balance is retrieved from the **Plan Percent Report** of the T-2 business day using the values in the base cost column for KRS Cash Unit (Pension) and KRS INS Cash Unit (Insurance).
8. Closing ending balance for T-1 is retrieved from the corresponding Plan Percent Report using the same column and units from step #7.
9. "Wires In" and "Wires Out" on the pension and insurance wire tabs are copied and pasted into the Daily Reconciliation Worksheet from the Unit Trade Details Worksheet for day T-1 from BNY Mellon.
10. All incoming and outgoing transactions on the pension and insurance strip tabs are copied and pasted into the Daily Reconciliation Worksheet from the Unit Trade Details Worksheet for day T-1 from BNY Mellon.
11. Realized loss/gain is calculated for day T-1 by finding the difference between base transaction amount and the base cost of system/fund specific cash account on the Unit Trades Worksheet. Realized Loss/Gain recorded during the middle of the month represents investment fees and interest being allocated across the plans.
12. The sum of all the above information should be zero, meaning that there is no discrepancy in what has been calculated verses what is being reported by BNY Mellon. If a difference is detected, the Investment Operations staff member assigned to this task on business day T will research the outage and may need to contact BNY Mellon Cash Management team for an explanation.

Working Database Worksheets are saved on the Office of Investments shared drive. This worksheet shows a running history of all capital calls, distributions and redemptions in the "Cash Flows" tab. This database was not tested in this audit because the same information is recorded elsewhere in the three other worksheets described above.

Section B: Capital call approvals

Investment managers send capital call notifications to BNY Mellon Cash Management, KPPA Investment Operations, and Investment Portfolio Managers. BNY Mellon Cash Management team keys the total of the call in BNY Mellon Nexen system after Investment Operations emails the notice to the BNY Mellon Cash Management team to ensure receipt from the Limited Partnership (LP) was received.

- If the call is a LP manager, Investment Operations compares the capital call notification letter to the information in Nexen to ensure the total, fund (Pension or Insurance), Investment Manager name, and due date match.
 - If the capital call exceeds \$25,000,000, it will take two members of the Investment Operations team to approve.
- If the call is from a commingled fund, BNY Mellon Cash Management team keys and approves the capital call in Nexen.

Capital calls involving foreign currency need to be approved in Nexen exactly two days before the due date. All other calls are approved in Nexen as soon as they are available to be approved and the scheduled withdraw happens automatically on the assigned due date.

Section C: Affirming Repo procedures

Investment Portfolio Managers send a Letters of Direction to Investment Operations staff to use when confirming that what was keyed in BNY Mellon Access system is correct. The fund (Pension/Insurance), total, trade date, maturity date, and interest due at maturity must match between the Letter of Direction and the trade in BNY Mellon Access. The Investment Operations staff member who approves the repo saves a screen shot of the match trade window to the day's folder on the Office of Investments shared drive. The Investment Operations staff member then replies to the repo email sent from the Investment Portfolio Manager with the receipt.

As of June 2021, the Investment Operations staff member who reviewed the daily cash following the steps in Section A of this report should not be affirming that day's repo unless necessary (e.g., staffing issues that day). Investment Operations staff review the Settled Cash Statement each day to ensure all cash transactions have settled.



KPPA

Kentucky Public Pensions Authority

**Plan Liquidity Phase 3 - Available Cash Balance/Cash
Projection**

Issued May 15, 2023



Acronyms

The following acronyms will be used throughout the report:

1. KPPA - Kentucky Public Pensions Authority
2. CERS - County Employees Retirement System
3. KRS - Kentucky Retirement System
4. KPPA Executive Management team - KPPA Executive Director, KPPA Deputy Executive Director, KPPA CIO, KPPA Executive Director-Office of Legal Services, and KPPA Executive Director-Office of Benefits
5. KPPA Accounting – KPPA Division of Accounting
6. Investment Operations – KPPA Division of Accounting, Investment Operations branch

Objective

The objectives of our Plan Liquidity Phase 3 - Available Cash Balance/Cash Projection audit were to ensure internal controls have been designed and are operating effectively and efficiently. We also ensured compliance with applicable state statutes and regulations as well as policies established by the CERS and KRS Boards and procedures developed by KPPA staff.

Other Matters Noted

In addition to the recommendations included in our Plan Liquidity Phase 3 - Available Cash Balance/Cash Projection audit report dated May 15, 2023, we noted one recommendation that we wanted to communicate to management. This item will be reviewed during follow engagements and/or during the annual review of open recommendations.

- 1. Investment Operations staff should review the various reconciliations that are being performed to determine if these reconciliations can be completed in a manner that avoids duplication of work as well as ensures discrepancies are caught immediately. Investment Operations staff should consider analyzing the reconciliation method utilized by audit staff during the engagement to determine if a similar method would be beneficial to the Investment Operations team.**

Three initial reconciliations failed to detect the following errors. Compensating controls were in place that eventually caught these errors:

1. The distribution from Adams Street SPC II B1 settled for \$1 more than it should have at \$1,630,518 on June 11, 2021. Transaction ID is 4903599435701002-10. The discrepancy was noted in a second reconciliation on June 16, 2021.
2. Two capital calls from L-A VII settled correctly by total but were allocated across the plans incorrectly because the capital call was assigned to L-A VII B. The March 25, 2021, reconciliations for pension and insurance did not catch this error. The discrepancy was found by BNY Mellon staff and communicated on June 16, 2021.

There are three worksheets used in the various processes to monitor the cash accounts; however, each worksheet reviews the same type of information. Initial reconciliation procedures instruct the reader to copy and paste details from the Unit Trade's Detail report; however, the following actions are not required:

1. Wires in and out are not required to be compared to the source documents, which are emails from KPPA Accounting.
2. Transactions on the strip tabs are not required to be compared to the back-up documents. Inaccurate activity may go undetected and uncorrected.

This report is intended solely for use by the KPPA Board and KPPA Audit Committee; the CERS and KRS Boards; the Executive Management teams for KPPA, CERS, and KRS; and the Division of Accounting. This report is not intended to be, and should not be, used by anyone other than the specified parties. All final reports are subject to Open Records Requests.



September 2011

Strengthening Corporate Governance With Internal Audit

A Crowe White Paper by Rick Julien and Larry Rieger



Audit | Tax | Advisory | Risk | Performance

A focus on corporate governance offers internal audit the opportunity to become a more active and strategic team player. Recent surveys have shown that management and boards of directors are looking for greater contributions from the chief audit executive (CAE) and internal auditors. Internal auditors can meet the heightened expectations by taking a more holistic view of corporate governance and aligning internal audit skills and activities to assess, improve, and monitor their organizations' corporate governance capabilities. The CAE must understand all of the components of corporate governance and how internal audit can support them.

Strengthening Corporate
Governance With Internal Audit



Corporate governance is seen largely as the province of boards of directors and legal compliance officers, and that narrow view can restrict improvements to the corporate governance process. Good governance is a journey that begins with a broad, organizational perspective. Making steady progress requires committed senior leadership, integrated planning, coordinated execution, and constant monitoring.

Internal audit's responsibilities are growing due to increased regulatory scrutiny as well as directives from executives to strengthen controls and improve risk management. Increasingly, business leaders expect internal audit to play a more strategic – rather than merely tactical – role in the governance process. In fact, that role is consistent with the definition of “internal audit” sanctioned by The Institute of Internal Auditors (IIA). However, the internal audit function continues to play only a minor role in many organizations.

At a high level, corporate governance can be thought to have seven interrelated components: board of directors and committees, legal and regulatory, disclosure and transparency, business practices and ethics, enterprise risk management, monitoring, and communication. Internal audit performs critical roles in all aspects of corporate governance by:

- Supporting the audit committee in fulfilling its heightened responsibilities;
- Participating in the organization's disclosure committee;
- Reviewing the effectiveness of the organization's code of conduct, ethics policies, and whistle-blower provisions;
- Helping assess risks and gauge performance across the organization;
- Monitoring corporate governance activities and compliance with the organization's policies;
- Facilitating and enhancing communications with the chief executive officer, general counsel, chief financial officer, chief information officer, and other oversight executives; and
- Evaluating the effectiveness of the corporate governance activities and recommending areas for enhancements.

The rewards of improved corporate governance encompass more than a greater sense of personal accomplishment or company pride. Researchers at the University of Michigan Business School, along with other business and academic studies, have found a strong correlation between effective governance and profitable investment opportunities. Internal audit plays a pivotal role in this process by fostering an integrated, well-planned, and progressive governance program.

A Changing Role

During the boom times of the 1990s, people's trust in business grew along with rising stock prices. Serious interest in risks, controls, and ethics on the part of the media and many investors was limited. Although internal audit began to allocate resources based on risks and the function's visibility increased, staffing levels were relatively constrained and audits often focused on performance improvement opportunities.

Recent regulations, including an emphasis on anti-fraud and whistle-blower provisions and the potential impact on stock prices, have compelled auditors to take a more active role in governance. In 2003, the U.S. Securities and Exchange Commission approved

Internal auditing requires business knowledge, insight, good judgment, and effective communication. Consequently, CAEs with many years of business experience and insight are becoming highly valued.

final versions of revised New York Stock Exchange (NYSE) and Nasdaq requirements. The NYSE now requires that listed companies have an internal audit function. The IIA has clarified roles and responsibilities by affirming the importance of risk management and corporate governance. Internal

auditing, according to the institute, "helps an organization accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control and governance processes." The institute's revised International Professional Practices Framework calls upon internal auditors to evaluate and offer recommendations to improve governance processes.¹

Multifaceted Challenges

Internal audit will always have the challenge of remaining independent and objective while being part of the organization. In this age of intense scrutiny of business motives and ethics, the last thing a company needs is a passive internal audit function. But no organization wants an internal auditor group whose only response to risk is an attempt to eliminate it entirely. There are risks in any business venture, and closing off all risks also closes off any rewards.

Internal auditing requires business knowledge, insight, good judgment, and effective communication. Consequently, CAEs with many years of business experience and insight are becoming highly valued, and internal auditors must continue to increase their skill levels in order to contribute greater value, help strengthen governance, and improve company performance.

The biggest challenge facing companies and their internal auditors is the lack of a one-size-fits-all method to improve corporate governance. Each organization must tailor an individual solution that considers its industry, maturity, business strategy, capabilities, corporate culture, and competitive position. Since there is no quick solution for addressing this multifaceted challenge, keeping the focus on good governance over the long term is an important goal for most organizations.

A Focus on Corporate Governance

Investors and other stakeholders value companies that anticipate problems and show evidence of strong internal oversight. Internal audit should be a champion in assessing opportunities where corporate governance can be strengthened and suggesting corrective action as needed.

But, first, a definition to clarify the concept of governance:

Corporate governance is the systems and processes an organization has in place to protect and enhance the interests of its diverse stakeholder groups.

The best governance addresses the needs of all of an organization's stakeholders – shareholders, employees, customers, lenders, vendors, and the community – because all of these groups share a common interest in perpetuating the business. Well-governed organizations recognize that balancing the interest of them all is critical for a sustainable organization.

Auditing the effectiveness of an organization's corporate governance systems, practices, and performance requires a reliable framework and methodology. The following is an analysis of the seven essential and interrelated components of the Crowe Corporate Governance Framework. These components emerged during extensive research and practical experience with governance issues.



© 2009 Crowe Horwath LLP

The Crowe Corporate Governance Framework

These seven components give a comprehensive view of the complexity, interrelationships, and variables organizations must manage in order to strengthen their governance. When all components operate effectively and are efficiently coordinated, corporate governance provides a platform to help improve business performance and enhance stakeholder value. Each of the seven components discussed in the rest of this white paper is accompanied by examples of actions internal audit should take to meet stakeholders' expectations.

Board of Directors and Committees

The primary responsibility for effective corporate governance rests with the board of directors. The board establishes the direction and values of an organization, oversees performance, and protects shareholder interests.

Board responsibilities are formally defined in bylaws and charters. Listed corporations are required, by law, to include a minimum of three board committees, which are in charge of overseeing audits, regulating compensation, and managing nomination and corporate governance policies. The number of additional committees and members is up to the organization.

The committee of greatest interest to internal audit is the audit committee, which reports regularly to the full board and meets separately and periodically with management as well as internal and external auditors. At least one member of the audit committee should function as a “financial expert.”

Ideally, a board of directors establishes benchmarks for its performance against peer boards and best practices to improve corporate governance. Section 301 of the *Sarbanes-Oxley Act* (SOX) states that all members of the audit committee panel must be independent.

Internal Audit

- Assists the board of directors and committees with their self-assessment and best practices;
- Assesses audit committee effectiveness and compliance with regulations;
- Reviews the audit committee charter with the help of legal counsel;
- Is interactive on the subject of governance, bringing best-practice ideas about internal controls and risk management processes to audit committee members;
- Establishes the accuracy of information used in decisions by the compensation committee; and
- Assists the board with its proxy reporting on oversight of risk management.

Legal and Regulatory

This component speaks to the legal boundaries within which a company operates and the requirements set forth by current laws as well as international, federal, and state regulations. The issues are complex, especially for large corporations engaged in specialized and highly regulated businesses.

The elements in this component deserve special attention because the cost of compliance continues to increase. Leading organizations are striving to improve their compliance responses and manage the costs more effectively. Many look for opportunities to aggregate and leverage certain compliance activities and capabilities to achieve improved performance at a reduced cost.

Internal Audit

- Verifies – with legal guidance – that the organization has identified requirements, assigned responsibilities, and addressed all of the key legal and regulatory requirements; and
- Looks for opportunities to leverage compliance activities and capabilities to reduce long-term costs and improve performance.

Leadership must set the tone from the top. Good governance has the best chance of taking root when embedded in the culture and seen in executives' daily activities.

Business Practices and Ethics

Business practices are the operational tactics and measures a company uses to achieve its purpose and strategy. The overriding goal is to maintain consistency, predictability, and accountability in conduct, decision making, and performance.

Ethics are the moral boundaries an organization believes it should observe when pursuing competitive objectives. Ethics and a well-defined code of conduct are cornerstones for building a strong foundation for good corporate governance. Due to the SOX whistle-blower provisions, companies need systems to field complaints and investigate potentially illegal and unethical conduct.

The goals for rules of conduct are the fair treatment by the organization and its employees of the interests of all stakeholders and staying within applicable laws and societal expectations. The code of conduct encourages employees at all levels to pursue business in fair and honest ways and to comply with government rules and regulations.

The tone needs to be set from the top. Good governance has the best chance of taking root when based on sound principles embedded in the organization's culture and seen in executives' day-to-day actions.

Internal Audit

- Reviews the code of conduct and ethics policies, verifying that they are periodically updated and communicated to management and employees;
- Performs a behavioral sciences ethics review to assess the understanding and perception of compliance at all levels of the organization (geographic and departmental, for example);
- Helps management and the audit committee hold people at all levels accountable, listening to their words but also looking at their actions;
- Serves in an ethics oversight role or confers with the organization's ethics officer;
- Participates in whistle-blower and other ethics complaints investigation processes;
- Conducts annual audits of hotline and follow-up processes, reporting results (for example, compliance with policies and consistency of actions) to the audit committee; and
- Assesses the linkage of ethics to goal-setting and performance evaluation processes.

Disclosure and Transparency

This component refers to the nature and timing of information an organization provides to its stakeholders. SOX requires executives of publicly traded companies to certify financial statements. Financial reports must meet legal expectations for clarity, relevance, reliability, and comparability. The legislative intent is to provide shareholders with information that is complete, objective, and timely. In many cases, however, organizations need to think more broadly than they do about what is appropriate disclosure and transparency to all stakeholders, not just shareholders. In fact, most states mandate timely disclosures when lapses in customer information privacy occur.

Internal Audit

- Conducts testing of financial disclosures and confers with the CFO;
- Understands concern for disclosure and transparency, aligning risk assessment with stakeholder expectations;
- In the annual audit plan, addresses disclosure and transparency objectives;
- Understands the breadth and depth – that is, the spectrum – of disclosure and transparency possibilities and where the organization strives to be or should be on the spectrum;
- Actively participates in the disclosure committee, including evaluating its effectiveness; and
- Reviews the subcertification process.

Enterprise Risk Management

In many organizations, control activities are narrowly focused on compliance. Enterprise risk management (ERM) encourages organizations to take a broader view. The ERM framework of the Committee of Sponsoring Organizations of the Treadway Commission² (COSO) is an integrated approach to managing risk and reinforces the need for a comprehensive approach to mitigating risk and improving corporate governance.

SOX is having the effect of pushing ownership of controls to process owners throughout the business. Process owners are in the best position to monitor operational risks and benefit greatly from a better understanding of internal controls over financial reporting.

The process and risk-assessment-related evaluation skills that internal audit must have to understand the best mix of controls provide the foundation for assessing governance processes. Thus, internal audit can provide recommendations that manage risk, enhance performance, and improve governance.

Internal Audit

- Proactively advocates and participates in an organization's ERM efforts, including establishing a practical ERM governance structure having a commitment to common methodologies and tools;
- Facilitates identification of important risk areas for the organization as well as its most important processes;
- Ensures the business strategy is linked to the ERM process;
- Assists process owners with understanding, assessing, designing, and documenting controls;
- Inventories organizational risk and compliance activities and strives to integrate them into a common methodology; and
- Evaluates business and process owners on taking responsibility for ERM.



Monitoring

Monitoring tactics vary by company, but methods share a common objective: to evaluate whether components of the governance framework are operating as intended and provide reporting to various levels of the organization. At the most fundamental level, monitoring systems look at “what is” versus “what should be.”

To identify gaps, organizations employ a variety of monitoring functions, including internal auditors, regulatory or legal compliance officers, ethics officers, internal management reporting, and self-assessments.

Timely risk and performance monitoring has a positive impact on an organization and the sustainability of corporate governance. With better integration among monitoring functions, methodologies, and systems, company leaders receive more relevant reports, thereby enabling them to take corrective action promptly. Effective integration contributes to better-trained individuals and enhances reporting capabilities and operational efficiencies.

Internal Audit

- Understands what monitoring activity is taking place in the organization for each of the other components of the governance framework;
- Facilitates the implementation of a common risk monitoring methodology across all corporate governance functions, thus feeding an integrated reporting system;
- Performs a strategic-level corporate governance audit or sees that one is conducted;
- Incorporates tactical-level corporate governance aspects into audit plans; and
- Develops an assurance scorecard and reports on it quarterly.

Internal audit participates in ongoing conversations with the general counsel, CFO, and other senior management officers.

Communication

The increasing complexity of legal requirements, compliance activities, and governance best practices requires good communication. Communication holds together the various components of the governance framework and keeps the process improving over time. A single announcement in a routine memorandum is not enough to ensure that everyone is getting the message about good governance.

Because corporate governance permeates virtually every area of an organization, it is important to have a shared set of terms people can understand and use productively in discussions. In essence, a common language is needed to discuss governance issues. A common governance language facilitates productive dialogue so that everyone can work together to strengthen governance and company performance.

Maintaining the focus on good governance is one of the key elements for improving it over time. Internal audit plays a pivotal role in communicating that focus throughout the organization.

Internal Audit

- Participates in ongoing dialogues with the general counsel, chief financial officer, and other senior management officers;
- Maintains steady communication with audit committee members and oversight executives (for example, depending on the organization's size and internal oversight structure, the chief risk officer, chief compliance officer, and/or ethics officer);
- Includes information about corporate governance in audit reports; and
- Assists in establishing a corporate governance communications calendar and solicits input about needs across the organization.



Costs to improving governance can include enhancing internal audit staffing, adopting ERM, and further developing the financial expertise of audit committee members.

Looking Ahead

It is in an organization's best interest to evaluate and improve its governance policies now. Auditing the effectiveness of its governance systems, practices, and performance requires a rigorous methodology and comprehensive view of the organization. With the understanding that corporate governance provides a compass for the journey, the internal audit charter should be aligned with the organization's long-term interests. There are costs to improving governance, whether through enhancing internal audit staffing, adopting ERM, or further developing financial expertise among members of the audit committee.

The returns may not be immediately measurable, but the long-term results of a successful governance program include better brand and reputation management, enhanced market value, compliance with regulations, sound business practices, and a more solid foundation for growth. Strong governance is part of a successful business strategy, and good governance can enhance an organization's competitive position, assist in retaining superior employees, attract top-notch directors, and contribute to long-term improved financial performance. Anticipation of improved stakeholder returns, therefore, can help to justify the investment.



Contact Information

Rick Julien, CPA, is a partner with Crowe Horwath LLP in the Chicago office. He can be reached at 630.586.5280 or rick.julien@crowehorwath.com.

Larry Rieger, CPA, is a partner with Crowe Horwath LLP in the Chicago office. He can be reached at 630.586.5150 or larry.rieger@crowehorwath.com.

¹ The Institute of Internal Auditors, International Professional Practices Framework (IPPF), 2011, <http://www.theiia.org/guidance/standards-and-guidance/interactive-ippf/?search=IPPF>

² COSO, Guidance on Risk Management, <http://www.coso.org/ERM.htm>

www.crowehorwath.com

MOHAWK windpower 

When printed by Crowe Horwath LLP, this piece is printed on Mohawk Color Copy Premium, which is manufactured entirely with Green-e® certified wind-generated electricity.

The Mohawk Windpower logo is a registered trademark of Mohawk Fine Papers Inc.

Green-e is a registered trademark of Center for Resource Solutions.

Crowe Horwath LLP is an independent member of Crowe Horwath International, a Swiss Verein. Each member firm of Crowe Horwath International is a separate and independent legal entity. Crowe Horwath LLP and its affiliates are not responsible or liable for any acts or omissions of Crowe Horwath International or any other member of Crowe Horwath International and specifically disclaim any and all responsibility or liability for acts or omissions of Crowe Horwath International or any other Crowe Horwath International member. Accountancy services in Kansas and North Carolina are rendered by Crowe Chizek LLP, which is not a member of Crowe Horwath International. This material is for informational purposes only and should not be construed as financial or legal advice. Please seek guidance specific to your organization from qualified advisers in your jurisdiction. © 2005, 2011 Crowe Horwath LLP

RISK12911



Fiducia non imperium means trust is not a control. A seasoned fellow auditor from Arizona gave me this piece of advice during the fall conference of 2022 hosted by the Association of Public Pension Fund Auditors (APPFA) in San Antonio, Texas.

By standards set by the Institute of Internal Auditors, Internal audit is “an independent, objective assurance and consulting activity designed to add value and improve an organization's operations. It helps an organization accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control, and governance processes”.

I asked internal audit staff for their personal definition of internal auditing and these are the given definitions:

Kristen - “To me the job of the role of internal audit is not only to protect the assets of the company, but also the organization’s reputation.”

Matthew - “Internal audit is a function that helps to ensure that other functions within the organization are working towards achieving the objectives of the organization and that the organization is meeting the needs of the stakeholders.”

William – “To me, Internal Audit provides an organization with risk protection and prevention, assures compliance with all applicable laws, regulations, and procedures, and thorough review offers improvements to organizational processes.”

Melinda - “Checks and Balances. If you have nothing to hide, you have nothing to fear.”

Riley - “Internal auditing to me is ensuring that a business functions efficiently and that its operations are sound. Internal auditing is a proactive unit crucial to a business' improvement and success.”

As for me, I see Internal audit as the oil in the gears of an organization which keeps processes running efficiently while smoothing out rough edges, hence the gear in the logo.

A black swan was added to represent a black swan event which is thought to be an unexpected or unpredictable event due to the history of this rare bird because, until Willem de Vlamingh’s discovery of a black swan in 1697 during his Australian expedition, it was believed that all swans were white.

An article by Sanat Pai Raikar from Britannica says that “the metaphor is analogous to the fragility of any system of thought and a testament to the fallacy of assumption. A set of conclusions can be undone once any of its fundamentals is proved false. In this case, the observation of a single black swan negated the long-held presumption about the species. Any logic that followed the assumption that swans must be white was also invalidated by the discovery.”

When it comes to business operations, historical patterns are used to predict the future trends but sometimes history can mask factors causing “unforeseen” issues. The idea that swans were only white came from a European perspective, but perhaps black swans were an ordinary thing to the Australian natives and white swans were the rarity.

KPPA’s internal audit team intends to uphold the core principles established by the IIA by enriching the perspectives of controls in place by imagining the possibility of black swan events that defy the trust placed in current process across all aspects of the agency.