TEXAS MUNICIPAL RETIREMENT SYSTEM
INTERNAL AUDIT CHARTER

PURPOSE AND MISSION

The Texas Municipal Retirement System (TMRS) Board of Trustees (Board) established the internal audit activity for this purpose:

> The Internal Audit Department (Internal Audit) is to provide independent, objective assurance, and consulting services designed to add value and improve the organization's operations. Internal Audit helps TMRS accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of governance, risk management, and control processes.

The mission of internal audit is to enhance and protect organizational value by providing risk-based and objective assurance, advice, and insight.

PROFESSIONAL STANDARDS

Internal Audit will govern itself by adherence to The Institute of Internal Auditors' mandatory guidance, which includes the Definition of Internal Auditing, the Code of Ethics, and the *International Standards for the Professional Practice of Internal Auditing* (*Standards*). This mandatory guidance encompasses the fundamental requirements for the professional practice of internal auditing and the principles against which to evaluate the effectiveness of the internal audit activity's performance. Internal Audit is also recommended to use The Institute of Internal Auditors' Implementation Guidance and Supplementary Guidance as applicable to guide operations.

Internal Audit also may use or may be required to use other professional standards and guidance along with the *Standards* including--but not limited to--the following:

- ISACA's Information Security Auditing Standards, Guidelines, and Procedures, and the Code of Professional Ethics
- The American Institute of Certified Public Accountants Professional Standards and Code of Ethics
- The U.S. Government Accountability Office's *Government Auditing Standards*
- The Public Company Accounting Oversight Board auditing standards

AUTHORITY

The TMRS Internal Audit is established by the Board in accordance with its authority to hire other employees for the efficient administration of the retirement system (Texas Government Code §855.206). The Board created an Internal Audit Committee to assist in fulfilling the Board's fiduciary responsibility with respect to the internal audit process. The Internal Audit's responsibilities are defined by the Internal Audit Committee as part of its oversight role.

Internal Audit can provide a wide range of quality, independent internal auditing services and consulting services for the Board, Internal Audit Committee, and executive management.

Assurance Objectives: To provide independent assurance over TMRS' governance, risk management, and control process with the goal of safeguarding assets, enhancing operational efficiency, and complying with applicable laws and the agency's policies. This includes assessing the reliability and integrity of financial and operating information.

Consulting and Advisory Objectives: To provide assessments and advice for improving TMRS' governance, risk management, and control with management's agreement on the nature and scope of the service. Examples of advisory services include participating on internal workgroups or committees in a non-voting capacity, providing routine advice on policies and internal controls, and providing training.

Investigations: To conduct or assist in the investigation of suspected fraud, waste, or abuse within TMRS.

ORGANIZATION AND REPORTING STRUCTURE

The Chief Audit Executive (the Director of Internal Audit, hereafter referred to as Director) reports functionally to the Board's Internal Audit Committee and administratively to the Chief Executive Officer (Executive Director). The Board delegates management of Internal Audit to the Director, who fulfills the activity's mission and objectives through authorization to:

- Free and unrestricted access to the Board, the Internal Audi Committee, and the Executive Director
- Allocate resources, set project frequencies, select audit subjects, determine scope of work, and apply the techniques necessary to accomplish assurance and consulting objectives
- Hire, retain, train, and terminate internal audit staff, when necessary

The Director and Internal Audit staff will:

- Have unrestricted access to all TMRS departments, personnel, activities, confidential and non-confidential data and records, information systems, physical property, and contractors relevant to the performance of engagements and subject to applicable state and federal laws
- Have access to contractors and their records and files in accordance with contract terms
- Obtain timely reports from management on actions proposed and taken pertaining to audit recommendations
- Be prudent in the use and safeguarding of information acquired in the course of their duties

The Director and Internal Audit staff is not authorized to direct the activities of any TMRS employee not employed by Internal Audit, except to the extent such employees have been appropriately assigned to auditing teams or to otherwise assist the internal auditors.

INDEPENDENCE AND OBJECTIVITY

Internal auditors shall be free from personal or external impairments to independence and perform their duties with objectivity in order that opinions, conclusions, and recommendations will be impartial and will be viewed as impartial by knowledgeable third parties.

Organizational Placement

Internal Audit's organizational and reporting structure provides for its independence and objectivity as required by professional standards. The Director shall freely discuss audit policies, audit findings and recommendations, audit follow-up, and other matters as necessary.

Operational Duties

To maintain independence and objectivity, the Director and Internal Audit staff are not authorized to:

- Perform operational duties for the organization and/or its affiliates and contractors
- Initiate or approve accounting transactions external to Internal Audit

Potential Impairment of Independence

The Director will discuss with the Internal Audit Committee any potential issues regarding impairment of independence and their mitigation(s), as necessary. If objectivity or independence is impaired in fact or appearance, the details of the impairment should be disclosed to the appropriate parties. The nature of the disclosure will depend on the impairment. Internal Audit will annually confirm to the Internal Audit Committee they have no actual or perceived conflicts of interest that would impair their objectivity or independence.

RESPONSIBILITIES

Certain roles and responsibilities of the Board, Internal Audit Committee, Executive Director, and Director of Internal Audit are critical to the success of the Internal Audit function.

TMRS Board and Internal Audit Committee

The Internal Audit Committee or its successor entity will review and recommend to the Board for its approval of the following:

1. This Internal Audit Charter (Charter) and all future amendments

2. Appointment, replacement, and dismissal of the Director with input from the Executive Director if desired
3. The internal audit plan
4. The Director's performance evaluation and adjustments to compensation
5. Internal Audit's staffing and resource needs

The Internal Audit Committee will review and monitor the following:

1. The Director's work plan and status of ongoing engagements
2. Draft and final internal audit reports
3. Investigations of suspected fraud, waste, and abuse within TMRS

TMRS Senior Management

Management is responsible for implementing and maintaining a system of risk management and internal control. Internal Audit provides independent and objective assurance on the effectiveness of the risk management and internal control systems. Key responsibilities of TMRS management related to Internal Audit activities include:

1. Cooperating with Internal Audit staff during the performance of internal audits and advisory projects by providing full and unrestricted access to all activities, personnel, property, records, information, and systems requested by auditors, including contractor and subcontractor resources
2. Reviewing draft Internal Audit reports and providing timely, written management responses to address issues and recommendations, including management actions planned, responsible manager, and target implementation dates
3. Notifying the Director of contacts from external organization auditors, reviewers, and inspectors
4. Coordinating with Internal Audit staff to respond to issues and recommendations contained in external audit reports
5. Providing status updates to the Director regarding management action plans that address prior internal and external audit recommendations

Director of Internal Audit

The Director is responsible for the following:

1. Establishing an Internal Audit Charter for Board review and approval; reviewing the Charter periodically and proposing updates as necessary
2. Establishing policies for conducting Internal Audit activities according to the organization's policies, direction provided by the Internal Audit Committee, and professional standards

3. Establishing a quality assurance and improvement program that covers all aspects of the internal audit activity. The Director will communicate to the Board and senior management on this program, including results of ongoing internal assessments and external assessments conducted at least every five years
4. Maintaining a professional staff with sufficient knowledge, skills, and experience. If the Director needs to rely on expertise outside of Internal Audit or TMRS, the Director will consider the competence, independence, and objectivity of the person(s)
5. Preparing an annual department budget that supports accomplishing the audit plan
6. Conducting risk assessments using a risk-based methodology and with Board and senior management input
7. Submitting an Internal Audit Plan to the Board and the Executive Director
8. Conducting engagements as indicated in the approved Internal Audit Plan and communicating any substantial changes to the Board
9. Preparing a written report at the conclusion of each audit engagement and distributing the report as appropriate
10. Monitoring the disposition of results communicated to management and the status of planned corrective actions
11. Providing updates on Internal Audit activities, including presentations and status reports to the Board and the Executive Director
12. Performing investigations at the request of the Board, Internal Audit Committee, or Executive Director
13. Supporting the primary TMRS director by serving as a liaison with external auditors or reviewers during any audit or review conducted of TMRS

Internal Audit Charter

Approved this date Dec. 9, 2016.

Jim Parrish
Chair, TMRS Board of Trustees

Jim Jeffers
Chair, TMRS Internal Audit Committee

David Gavia
TMRS Executive Director

Sandra Vice
TMRS Director of Internal Audit