

Texas Municipal Retirement System

Review and Discussion of the 2018 Plan for External Financial Statement and System and Organization Controls Audits

March 28-29, 2019

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Engagement Principal

WEALTH ADVISORY | OUTSOURCING | AUDIT, TAX, AND CONSULTING

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Create Opportunities

Agenda

- Engagement Team and Scope
- Required Governance Communications
- Work Plan – System and Organization Controls (SOC) Audit
- Work Plan – Financial Statement Audit
- Board of Trustees' Discussion

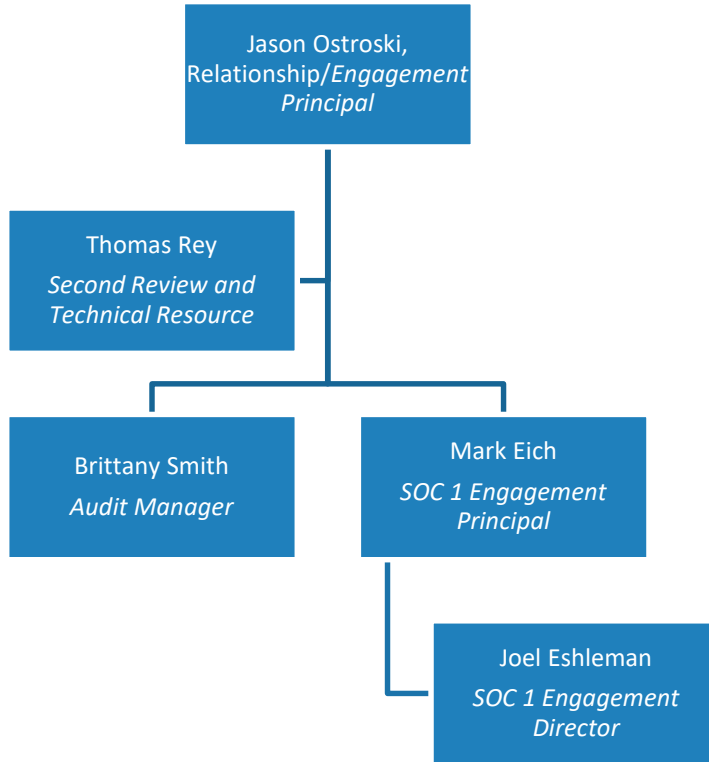


Engagement Team and Scope

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2018 Engagement Team



2018 Engagement Scope

- Audit of TMRS' financial statements as of December 31, 2018
- Audit of TMRS' Schedule of Changes in Fiduciary Net Position by Participating Municipality (GASB 68 schedule) as of December 31, 2018
- System and Organization Controls Report on TMRS' Description of NextGen MBS Pension Management System and the Suitability of the Design and Operating Effectiveness of Controls (SOC 1 Type 2) for the period May 1, 2018 to April 30, 2019.
- Written Communications with the Board





Required Governance Communications

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Required Governing Body Communications

- Auditor's Responsibilities - Opinion
 - Responsible for forming and expressing an opinion about whether the financial statements that have been prepared by management, with the oversight of those charged with governance are presented fairly, in all material respects, in conformity with generally accepted accounting principles in the United States of America.



Required Governing Body Communications

- Auditor's Responsibilities - Standards
 - Responsible for performing the audit in accordance with generally accepted auditing standards. The audit is designed to obtain reasonable, but not absolute, assurance about whether the financial statements are free of material misstatement.



Required Governing Body Communications

- Auditor's Responsibilities – Internal Control
 - In planning and performing our audit, we will consider internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of internal control over financial reporting.



Required Governing Body Communications

- Management Responsibilities
 - Preparation and fair presentation of the financial statements and GASB 68 schedule.
 - The design, implementation and maintenance of internal controls relevant to the fair presentation of the financial statements and GASB 68 schedule.





Work Plan – System and Organization Controls (SOC) Audit

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Audit Standards and Approach

- Audit to be conducted in accordance with Statement of Standards for Attestation Engagements (SSAE) 18 by the AICPA
- Phased Approach – Planning, Interim Control Testing, Final Control Testing and Reporting



SOC Audit Timeline

Key Milestones	Dates
Planning	Completed in November 2018
Interim Control Testing	Completed in November/December 2018
Final Control Testing	March and April 2019
Issue SOC Report	May 2019



Planning

- Understanding the entity and entity level controls
- Assess changes from prior SOC report

Control Objectives - Scope

Business Processes

- Census Reports
- Contributions
- Income Allocation
- Fund Balances
- Distributions

General Controls

- System Maintenance
- Application Maintenance
- Logical Access
- Backups
- Physical Access



Work Plan – Financial Statement Audit

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Audit Standards and Approach

- Audit to be conducted in accordance with auditing standards generally accepted in the United States of America (U.S. GAAS)
- Phased Approach – Planning, Internal Control, Substantive Test Work and Reporting

Planning

- Understanding the entity and entity level controls
- Preliminary analytical procedures
- Establish planning materiality
 - Apply professional judgment
 - Consider decisions that users make
 - Use appropriate benchmarks, such as % of assets or revenue



Planning (cont'd)

- Fraud procedures
 - Interviews
 - Journal Entry Testing
 - Brainstorming
 - Unpredictable procedures
- Risk assessment procedures

Auditor Objective – Risk Assessment

- Identify and assess the risks of material misstatement, whether due to fraud or error, at the financial statement and relevant assertion levels through understanding the entity and its environment, including the entity's internal control, thereby providing a basis for designing and implementing responses to the assessed risks of material misstatement.



What is Risk Assessment in a Financial Statement Audit?

Risk Assessment

- Obtain an understanding of TMRS, including internal control
- Identify and assess risks of material misstatement of the financial statements
- Evaluate both overall risks and risks that affect only specific assertions



Audit Procedures

- Concentrate audit effort in high risk areas
 - Inherent risk
 - Control risk
- Perform less extensive procedures in low risk areas

Significant Processes and Audit Areas

- We have identified the following areas as significant processes and audit areas:
 - **Investments and Investment Income**
 - ◇ Investments – Alternative/Non-Custodial
 - ◇ Investments – Publicly Traded/Custodial
 - **Contributions/Member Testing**
 - ◇ Employer and Member
 - **Benefit Payments**
 - ◇ Annuity and lump sum benefit payment testing
 - ◇ Data analytic procedures over benefit payments
 - **Financial Statement Process**



Investment and Investment Income

- Investments
 - Understanding of internal controls
 - ◇ Walkthroughs
 - Financial Reporting/Reconciliation procedures
 - Initial due diligence and on-going monitoring
 - Compliance monitoring
 - ◇ Review custodial bank's SSAE 18 report
 - Substantive procedures
 - ◇ Confirmation of custodial and non-custodial investments
 - ◇ Price testing of equity and fixed income securities
 - ◇ Review of audited financial statements and roll-forwards of non-custodial (alternative) investments, if not 12/31 year ends
 - ◇ Analytical procedures



Contributions/Member Testing

- Understanding of internal controls
 - Walkthroughs of contribution and purchase of service processes
 - Test of controls over the contributions process performed as part of SOC testing
- Substantive procedures
 - Reconciliation of contributions from general ledger to NextGen
 - Confirm member and employer amounts contributed to TMRS for selected employers
 - Recalculate selected contributions for accuracy and completeness
 - Analytical procedures



Benefit Payments

- Understanding of internal controls
 - Walkthroughs of benefit payments processes; separate walkthroughs for disability, survivor, regular retirement and refund processes
 - Test of controls over the benefit payment processes performed during SOC testing
- Substantive Procedures
 - Reconciliation of benefit payments from general ledger to NextGen
 - Analytical procedures



Information Technology

- General Control areas that will be reviewed include:
 - Logical Access Controls
 - Application Development and Change Control Procedures
 - Business Continuity Planning
 - System Integration
- Procedures performed during SOC testing were also utilized in financial statement audit

Government Pension Data Analytics

Your assigned audit team is versed in the use of data analytics. We have successfully utilized data analytics in our overall audit approach in the areas of:

- ◇ Contributions
 - ◇ Payments/Distributions
-
- Potential management/internal audit benefits (Continuous auditing tools and training)

Data Analysis Methodology

1. Plan	2. Identify Risk	3. Access Data	4. Technical Analysis	5. Interpret Results	6. Reporting
<ul style="list-style-type: none">• Identify engagement objectives and client needs• Understand the client's systems• Match data analytic capabilities to objectives• Understand professional guidance	<ul style="list-style-type: none">• Discuss known risks and weaknesses• Identify risks by carefully considering the internal control environment and managements tone at the top• Conduct meetings with management to identify risks• Rank risks from high to low	<ul style="list-style-type: none">• Have conversations with the organization to understand system detail• Planning the data extraction• Prepare the data request list• Assist/monitor client data extraction if necessary	<ul style="list-style-type: none">• Ensure proper import• Completeness testing• Normalize data and prepare for analysis• Design analytics to address identified risk and accomplish objectives	<ul style="list-style-type: none">• Continuously interpret results and compare them with your expectations• Corroborate results to identified risks• Identify anomalies• Continuously reassess risk and improve procedures	<ul style="list-style-type: none">• Provide impactful results to client• Document procedures and results

Financial Statement & GASB 68 Audit Timeline

Key Milestones	Dates
Planning	Completed in January 2019
Understanding and Testing of Internal Controls	November 2018 through January 2019
Substantive Procedures & GASB 68 Audit Procedures	April and May 2019
Issue Financial Statement & GASB 68 Audit Reports	June 2019





Board of Trustees' Discussion

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Board of Trustees' Discussion

- Recognizing the importance of two-way communication, we encourage you to provide us with information you consider relevant to the audit. This may include, but is not limited to the following:
 - TMRS' objectives and strategies and the related business risks that may result in material misstatements.
 - Your understanding of risks of fraud and controls in place to prevent and detect fraud.
 - Other matters you believe are relevant to the audit of the financial statements.





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