



MINUTES OF THE
TEXAS MUNICIPAL RETIREMENT SYSTEM
JOINT MEETING OF THE INTERNAL AUDIT COMMITTEE
AND THE BOARD OF TRUSTEES

August 23, 2018 – 9:00 a.m.

On August 23, 2018, the Internal Audit Committee of the Texas Municipal Retirement System (TMRS) convened a joint meeting with the Board of Trustees at 9:00 a.m. at TMRS Headquarters, located at 1200 North IH-35 in Austin, Texas, with the following members present:

Committee Members and Trustees

James “Jim” Paul Jeffers, Chair
David Landis, Vice Chair
Bill Philibert, TMRS Trustee
Jesús Garza, TMRS Trustee

Present also were:

David Gavia, Executive Director
Sandra Vice, Director of Internal Audit
Andi Focht-Williams, Senior Auditor
Eric Davis, Deputy Executive Director
Christine Sweeney, General Counsel
Dan Wattles, Director of Governmental Relations
Leslee Hardy, Director of Actuarial Services
Debbie Munoz, Director of Member Services
Leslie Ritter, Director of Human Resources
Scott Willrich, Director of Information Resources
Rhonda Covarrubias, Director of Finance
Jesse Pittman, Senior Project Manager
Kurt Cressotti, Investment Compliance
Michelle Mellon-Werch, Assistant General Counsel
Candace Nolte, Assistant Finance Director
Peter Jeske, Project Specialist
Pete Krnavek, Information Systems Manager
Kenneth Oliver, Actuarial Analyst
Stacy White, Executive Assistant
Susan Warren, Partner, KPMG
Suzette Longfellow, Managing Director, KPMG
Diana Mayes-Gonzales, Senior Manager, KPMG
Eddie Holt, Partner, KPMG
Chris Stone, Director, KPMG
Toby Ruda, Director, KPMG
Jason Ostroski, Engagement Principal, CLA



Thomas Rey, Second Reviewer, CLA
Brittany Smith, Audit Manager, CLA
Joel Eshleman, SOC 1 Engagement Director, CLA
Amy McDuffee, Mosaic Governance Advisors

Mr. Jeffers called the meeting to order at 9:00 a.m.

1. **Receive Presentation on and Discuss Proposals to Provide Professional Auditing Services to TMRS**

Mr. Jeffers announced that this was not an action item, but that the committee would meet in closed session following presentations and deliver a recommendation to the full Board later that day.

Staff Presentation

Ms. Focht-Williams began staff's presentation by reviewing the three phases of the process for procuring the external auditing services. For Phase One, she reviewed the cross-functional composition of the evaluation team, development of the Request for Proposal (RFP), and how potential firms were identified and contacted. She also described how proposals were reviewed to ensure compliance with minimum requirements and how it was determined that Firms were licensed in Texas. She also discussed how Firm's proposals were review and scored. Finally, Ms. Focht-Williams contacted the references of the top two Firms. In Phase Two, three more members who typically have direct contact with the external auditors were added to the original evaluation team. The expanded team interviewed the top two firms and scored the interviews. This scoring led to staff's recommendation to the Executive Director and the Internal Audit Committee. Phase Three includes the top two Firms' presentations to the committee and the committee making a recommendation to the Board.

Mr. Philibert asked if it was a requirement for the Firm to have experience with multi-employer pension plans. Ms. Focht-Williams said it was a preference but not a requirement, and that both Firms had this experience.

KPMG Presentation

The first firm to present was KPMG. Ms. Longfellow introduced those team members present and additional resources who were not present and their relevant experience. She reviewed that KPMG has a national dedicated government and SOC practice to support the client service team, and she discussed highlights of the firm's services to the public pension industry.

Mr. Ruda discussed the firm's national qualifications with regard to Investment Management.

Mr. Holt reviewed the firm's experience and SOC capabilities, including his involvement with the AICPA SOC taskforce. He also discussed what makes the KPMG audit different.

Mr. Stone discussed KPMG's use of technology in the audit process, highlighting the firm's proprietary platforms. Mr. Stone also discussed how transition would occur if KPMG is not selected.



Ms. Mayes-Gonzales discussed the communications required by AICPA with the Board and keeping two-way communication channels open.

Ms. Warren discussed the firm's fees, and the difference between fees and value. She noted that, because of history with TMRS, the fees in certain areas have been reduced.

Ms. Warren concluded with reasons why KPMG values the work they do with TMRS and reasons for selecting KPMG.

KPMG Question and Answer

Mr. Garza requested clarification on fees. Ms. Warren noted that fees would not increase by more than 3% per year. Ms. Vice noted that projected fees were provided in the Board materials.

Mr. Landis asked about KPMG's partner rotation policy. Ms. Warren, Mr. Holt and Mr. Ruda discussed the "fresh set of eyes" concept. They noted that this is a firm policy and one that not all firms have. This allows a fresh perspective and different questions to be asked.

Ms. Vice asked for clarification on the services provided to the 70% of plans in the public plan environment. Ms. Warren did not have a breakdown of Financial Audit, SOC, and consulting engagements.

Mr. Jeffers asked, hypothetically, if KPMG was not the current auditor, why should TMRS change? Ms. Warren responded that it usually comes down to TMRS feeling they are not getting the service they desire from the current provider. Mr. Holt discussed that from the SOC perspective and since this is an auditor-to-auditor communication, customer service and helping improve the control environment.

Mr. Gavia asked about the value added that KPMG has brought to the engagement. Ms. Warren discussed the finance department's investment fee review, application of GASB 74, and advice when TMRS changed its payroll cycle. Mr. Stone also discussed cyber security questions they have received from TMRS and information they have provided to the TMRS team.

CLA Presentation

The next firm to present was Clifton Larson Allen (CLA). Their presentation team of Jason Ostroski, Thomas Rey, Joel Eshleman and Brittany Smith introduced themselves, reviewing relevant public pension experience. CLA is a top 10 accounting firm focused on private firms and the public sector, but not SEC firms. They have a specifically dedicated public pension team with over 17 years serving government pension plans. They work with over 25 public pension plans. Their firm provides a SOC audit to one other pension system, the Pennsylvania Municipal Retirement System. They are beginning to work with Kansas Public Employees Retirement System. They have been working on SOC audits for approximately 12 years.



Mr. Ostroski reviewed the fees and hours presented in the proposal, provided under separate cover.

Mr. Ostroski discussed their audit methodology, which is a risk-based audit approach. The focus will be on investments, contributions, and benefits. He briefly discussed data analytics. He promised continual communications, and said they want no surprises. They work with actuarial specialists and have worked with GRS through other clients. They will bring in IT specialists, where appropriate, especially during the SOC.

Mr. Ostroski reviewed the four-phase audit approach to the financial audit.

Mr. Eshleman discussed the approach to the SOC audit.

Mr. Ostroski discussed their approach to transitioning from the preceding auditor. He discussed their industry specialized team, minimizing TMRS' workload, investing in the relationships (putting in additional time), and arriving prepared. Mr. Garza asked how many other transitions may be going on in addition to TMRS, if selected. For TMRS' fiscal year, there would be no other transitions going on for the firm. Mr. Philibert asked for clarification on "arriving prepared." The team addressed the work they would do in advance of coming on site.

Mr. Ostroski discussed the technology tools they will use on the audit, including their internally developed audit program application, paperless audit product, and data analytics software. Mr. Gavia asked if the data analytics software IDEA was proprietary. Mr. Ostroski responded that it was not. Ms. Smith further discussed how the data analytics program has been used to uncover errors and anomalies in the data.

Mr. Ostroski finally discussed communication with the governing body, including open two-way communication with the governing body. He discussed the format of communication, timing, and required communications. He concluded that the team is available to the client year-round.

CLA Question and Answer

Mr. Landis asked where the team was located and how much time they spend on-site. Mr. Ostroski responded that the team is located in Baltimore and Seattle, and has offices in Texas.

Mr. Landis asked about rotation of the principal. Mr. Ostroski responded that the firm does not have a rotation policy. Standards suggest 10 years but CLA will rotate at 5 or 10 years, depending on the Board's preference.

Ms. Vice asked about potential transition fees. Ms. Rey discussed that there would be no additional fees charged to TMRS.

Mr. Garza asked for the elevator presentation (30 second sales pitch). Mr. Ostroski discussed that CLA is a top 10 firm dedicated to the public sector, and the teams' focus and passion is public pensions. They have the depth and skills to provide quality services.



Mr. Jeffers asked, in five years, why should we decide not to change auditors. Mr. Ostroski replied that now that CLA knows TMRS, they are on a stronger footing and still bring a team of industry experts.

Trustee Discussion

Mr. Jeffers asked Mr. Garza and Mr. Philibert for their observations. Mr. Philibert stated that either firm is capable. He wanted to see auditor rotation as a policy. Mr. Garza noted a substantial difference in fees between the Firms and asked how this affects the Board's decision, if at all. He also asked for clarification in scoring and why CLA scored higher than KPMG. Ms. Vice reviewed the differences in scores.

There being no further business, the meeting was adjourned at 10:53 a.m.

A handwritten signature in cursive script, appearing to read 'David Gavia', written over a horizontal line.

David Gavia
Executive Director

A handwritten signature in cursive script, appearing to read 'Jim Parrish', written over a horizontal line.

Jim Parrish
Chair, Board of Trustees

A handwritten signature in cursive script, appearing to read 'James Paul Jeffers', written over a horizontal line.

James Paul Jeffers
Chair, Internal Audit Committee