

NHRS Board of Trustees, Audit Committee
July 14, 2015

NOTE: These minutes from the July 14, 2015 Audit Committee meeting were approved and executed at the September 8, 2015 regular Meeting of the NHRS Audit Committee.

**Audit Committee
Board of Trustees
July 14, 2015**

The Public Minutes

**New Hampshire Retirement System
54 Regional Drive
Concord, NH 03301**

Committee Members: John Beardmore, Chair; Bill Dwyer; Germano Martins; David McCrillis. Maureen Kelliher, absent.

Staff: George Lagos, Executive Director; Denise Call, Director of Employer Services; Frank Clough, Director of information Technology; Timothy Crutchfield, Esq., Chief Legal Counsel; Jack Dianis, Director of Finance; Marty Karlon, Public Information Officer; Larry Johansen, Director of Investments; Nancy Miller, Director of Member Services; Heather Fritzky, Controller; Mark Cavanaugh, Esq., Associate Counsel and Compliance Officer; and John Browne, Internal Auditor. Also in attendance was David T. Kausch of Gabriel Roeder Smith and Company (GRS).

Chair Beardmore called the meeting to order at 8:00 AM. Upon a request from the Chair, a motion was made by Mr. McCrillis to accept the minutes of the Audit Committee meeting of June 9, 2015. Mr. Martins seconded the motion and it carried unanimously.

The Chair then asked Mr. Browne to provide an update on the Open Audit Issues Tracking System. He noted there were five issues outstanding from the prior month. Two issues had scheduled completion dates, but were deferred. He noted that for the completion of the State Audit issue, recent staff changes at the Department of Administrative Services had impacted the scheduling of field work. He stated that Mr. Cavanaugh, Associate Counsel and Compliance Officer, would make a presentation to the Committee in September to outline how the issue will be addressed and also discuss the overall employer audit process. Mr. Browne also noted that for the Member Termination Date issue, Member Services and IT have identified the required correction, and that a revised completion date of December 2015 had been established due to multiple and competing IT projects.

Next the Chair asked Mr. Dianis and Mr. Kausch to provide an update on the implementation of the Government Accounting Standard Board (GASB) Statement 68 - Accounting and Financial Reporting for Pension Systems. Mr. Kausch started the presentation by reviewing the June 30, 2014 Employer Reporting Accounting Schedules prepared by GRS. Specifically, he discussed the Executive Summary noting

the Net Pension Liability, the Total Pension Expense, and the Deferred Outflows and Inflows of Resources that must be allocated to all the employers of the System. Per a question from Mr. Beardmore on Deferred Outflows and Inflows, Mr. Kausch explained that the net difference between projected and actual earnings on Plan investments gains/losses is an example of a deferred resource in that only one fifth of the gains/losses are recognized in the current year, and the difference is spread over the following four years. Next Mr. Kausch reviewed Schedule E where the net pension liability, pension amounts, deferred inflows/outflows are allocated by each individual employer. He explained these numbers are broken down by each employer's proportionate share of the total employer contributions and each section of Schedule E are the required balances each employer will need to reconcile their net pension liability each year. In response to a question from Mr. McCrillis, Mr. Kausch explained that the breakout is based strictly on the total contributions paid by the employer and there was no impact if a member was Group I or Group II. Mr. Dianis further clarified that each employer's contributions reflected the routine contributions paid monthly. If an employer had a subsequent adjustment or a penalty, this was not included in the base as it might distort the allocation.

Next Mr. Dianis reviewed with the committee KPMG's audit report of the Schedules of Employer Allocations and Schedules of Pension Amounts by Employer. He started by reviewing the Opinion Section of the report, noting that KPMG had given the System an unmodified, clean opinion, and that the schedules presented fairly in all material respects the employer allocations and net pension liability, total deferred inflows/outflows of resources, and total pension expense. He emphasized that KPMG's opinion was related to the total contributions. While KPMG had expanded its audit testing of individual employers, AICPA guidelines put the responsibility for reviewing and auditing employer specific information on the employer's independent auditor. Mr. Lagos added that in addition to this GASB 68 testing, KPMG and the NHRS Employer auditors had performed GASB 67 census data testing which validated the contribution records of the system.

Mr. Dianis then reviewed with the Committee the Notes Section of the Report, which describes the Schedules of Employer Allocations and Pension Amounts. He stated the employers would use parts of the Notes Section in preparing their reports, and they would be able to reference some of the numbers, i.e. contributions, investment amounts, etc. directly to the System's Comprehensive Annual Financial Report (CAFR). He briefly discussed the discount rate, 7.75%, which is used to measure the collective total pension liability, and how a table is included in the report to illustrate the sensitivity of the collective net pension liability to changes in the discount rate. He also pointed out the importance of Note 5, which gives the definitions of columns used in the various schedules.

Mr. Dianis then reviewed the Schedules of Pension Amounts by Employer using a handout the System had prepared breaking the amounts into four sections: Net Pension Liability, Deferred Outflows of Resources, Deferred Inflow of Resources, and the Pension Expense.

Mr. Karlon then outlined public informational materials the System had prepared for distribution at the Board meeting relating to GASB 68. Specifically, he noted there was a press release that would go out after the Board had accepted the GRS and

KPMG 68 reports. He advised that an eleven page document on how to read the reports had been prepared and a detailed guide for financial statement preparers was in process and would be released shortly. He also noted these materials would also be available on the System website. Lastly the System had prepared a two page background document on GASB reporting changes that would also be available to the Board.

Based on the presentation and discussion above, a motion was made by Mr. McCrillis to recommend to the full Board that it accept both the GRS and KPMG GASB 68 reports. Mr. Dwyer seconded the motion and it carried unanimously. On behalf of the Committee, Chair Beardmore thanked and congratulated Mr. Dianis, Ms. Fritzky, Mr. Karlon, and the NHRS staff on the completion of this project.

Mr. Browne then reviewed internal audit activity for the past month, stating that the focus of his work in June was again completing the review of the GASB 67 census data audit work the Compliance Auditors had performed. He stated that thanks to the hard work of the auditors, presently twenty-seven of the thirty-two employers had been tested and the workpapers reviewed. He noted of the five audits remaining, all have been scheduled over the next four weeks, and it was expected that all GASB audit work will be completed by the end August. No material exceptions have been identified, and all employers have been very cooperative. Mr. Browne also noted he had started work on the audit of the PensionGold Change Control Process. He had performed a preliminary review of controls, and felt that the change process was strong, and the testing of these controls would be his focus for the next month.

Next Mr. Browne reviewed the draft Internal Audit plan for fiscal year 2016 that he had presented to the Committee in June. He commented that in reviewing it over the last few weeks, he felt it was a very solid plan which addresses areas critical to NHRS processing as well as areas that had either not been reviewed or not been reviewed in a numbers of years. Based on a question from Mr. McCrillis as to whether higher risk systems are assigned a specific audit interval for review, Mr. Browne stated that he has not done that in the past but rather annually he evaluates all systems, and then based on discussions with the Executive Team and other parameters, selects areas for audit. He stated that he would consider this as a part of one of his action plans in the coming year which was to enhance the risk assessment method utilized. The Chair then accepted a motion from Mr. Martins to approve the 2016 Internal Audit Plan as submitted. Mr. McCrillis seconded the motion, which carried unanimously.

As part of other business, Mr. Lagos briefly reviewed the New Employer Membership Letter included in the Audit Committee package. He pointed out an additional paragraph which had been added to the revised letter to make clear to new employers applying to participate that there are specific provisions and requirements in the event they were to later seek to withdraw from NHRS. Mr. Lagos also gave an update on the System's ongoing efforts to assure the confidentiality and security of NHRS data. He explained that as part of the contract the System has with Systems Engineering (SE), SE performs security training. As part of that training, the System had its first test of what is known as "email spear-phishing", where a fake email was sent to staff. A number of staff clicked on the link in the test email. As a follow up, those who clicked on the link were sent a short training video to assist them in recognizing unauthorized

intrusion efforts. Mr. Lagos felt the overall training exercise was very positive, and he had encouraged all management staff to review the video.

As there being no further business, the Committee scheduled the next meeting for 8:15 AM immediately prior to the Board meeting on Tuesday, September 8, 2015.

A motion to adjourn was made by Mr. Dwyer, seconded by Mr. Martins, and it carried unanimously.

Respectfully submitted,
John F. Browne