




**OPERS Ohio Public Employees Retirement System**

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January 5, 2009

Mr. Aristotle Hutras  
Ohio Retirement Study Council  
88 East Broad Street, Room 1175  
Columbus, OH 43215

Dear  Aristotle:

Pursuant to R.C. 145.095, enclosed please find the 2008 annual Audit Committee Report of the OPERS Retirement Board. This report summarizes internal audit activities and identifies actions taken by the Audit Committee during the preceding year.

Please feel free to contact me if you have any questions.

Sincerely,



Chris DeRose  
Executive Director



## **Audit Committee Annual Report**

**To:** Ohio Retirement Study Council (ORSC)

**Subject:** **OPERS Audit Committee Report- 2008**

**Date:** January 5, 2009

The following report documents the activities of the OPERS Audit Committee and Internal Audit Department for 2008. This summary outlines:

- Major Audit Reviews Completed (please see attached schedule)
- Audit Committee Meetings and Actions Taken
- 2009 Annual Audit Plan (priority review areas)
- Special Reviews Completed

### **Summary of OPERS Audit Committee Meetings and Actions**

The OPERS Audit Committee met on the following dates with any specific considerations addressed:

**March 18, 2008-** The audit committee met for the first time in 2008. The composition of the newly appointed audit committee includes one new board member. . The committee reviewed audit committee responsibilities outlined in the OPERS Audit Committee charter. Suggested changes to the existing charter on reporting requirements were approved by the audit committee. The committee also received the quarterly status report of significant audit issues and recommendations.

**May 21, 2008** – The Clifton Gunderson auditors presented the results of the 2007 OPERS financial examination. In addition, management letter comments on internal controls were presented and discussed with the audit committee.

The committee also received the executive summary of reviews completed during the previous six months with significant audit issue comments presented.

The committee also discussed the OPERS Travel Policy review completed.

**June 18, 2008-** The audit committee received a report and presentation on the co sourced review of Global Bonds related processes and controls from Investment Training and Consulting Institute (ITCI) and internal audit staff. This review utilized a comprehensive and different investment audit approach and methodology, for reviews of internal investment operations. Investment audit findings and recommendations presented were reviewed with the audit committee.

**October 8, 2008-** The audit committee reviewed and approved the proposed 2009 Audit Plan and risk assessment. The committee also reviewed and discussed the proposed 2009 internal audit operating budget and staffing. This departmental budget will be approved as part of the OPERS overall annual budget process in December, 2008.

The audit committee received a report on the custody transition review from State Street to JPMorgan completed by Deloitte & Touche (D&T). This report had been distributed previously at the August, 2008 Board meeting. At the board's request, audit staff provided a status update on the internal review findings and management actions taken as a result of observations made by D&T.

**December 16, 2008-** Clifton Gunderson external auditors were present for a preliminary discussion of the 2008 OPERS financial examination with the Audit Committee.

Internal Audit management also provided updates on results of the 2008 audit plan.

The audit committee reviewed and approved the 2008 draft of the OPERS Audit Committee Annual Report to ORSC. The committee also received an executive summary report of major audit activities for the prior six months.

In addition, committee reports provided included: the annual report of OPERS Personal Trading compliance; the annual disclosure of all fees paid to external auditor; D&T Due Diligence and Operational Review of PIMCO external manager; Crowe and Horwath IT Review on Insider Threat to Member Data Security and the quarterly status report of significant audit issues and recommendations.

## **2009 Annual Audit Plan**

The 2009 audit plan and risk assessment was reviewed and approved by the OPERS Audit Committee at the October 8, 2008 meeting. The priority review areas are summarized on the attached audit plan document.

### **Special Reviews**

The following major review was completed during 2008 with appropriate comments indicated.

An internal review was completed in response to allegations raised by a terminating OPERS employee. The allegations were directed toward a specific vendor being used and overall compliance with OPERS purchasing policy. A preliminary review was initiated consistent with OPERS Reporting of Suspected Policy. The review confirmed general compliance with policy, as well as determining no evidence of wrongdoing. No further review was necessitated.

Please let me know if you would like any additional information.

Respectfully submitted:

Gregory M. Januszewski  
OPERS Director- Internal Audit  
(614)- 222-0080

**OPERS INTERNAL AUDIT  
2008 AUDITS COMPLETED**

AUDIT AREA	STATUS OF RECOMMENDATIONS	SIGNIFICANT COMMENTS
Investments Gap Analysis (D&T)	Recommendations Substantially Implemented	Several recommendations still pending implementation with ongoing monitoring to OPERS Board. Alternative investments valuation requires understanding of external manager price methodologies.
It Security Policy and Incidence Reporting	Recommendations Implemented	Security Incidence Policy developed.
IT Security Policies- Gap Analysis- Unicon	Recommendations addressed and requiring multi year action plan	OPERS does not have an overarching security policy framework. This is not uncommon for organizations with a risk management program of similar age, size and experience.
Travel Policy Expense Review	Recommendations Implemented	Ohio Ethics Commissions approved the revised Staff and Board Policy.
Transfer of Purchased Service Credit (TOPS) review	Recommendations Implemented	None
Investments Internal Review	No Recommendations Presented	None
Investments Trading Process Controls	Recommendations Implemented	Overall trading controls were reviewed in light of European Bank trader where lack of proper segregation of duties resulted in significant loss to the financial institution.
Administrative Expenses	No Recommendations Presented	None
Personal Trading and Transition Issues	No Recommendations Presented	Personal Trading compliance responsibilities transferred to Investment Compliance effective 3 <sup>rd</sup> quarter, 2008 reporting. Internal audit will continue annual reviews.
Member Directed Policy Review	No Recommendations Presented	None
Actuarial Data Review	Recommendations Implemented	None
Incentive Compensation Review	Recommendations Implemented	2009 Investment Incentive compensation plan includes suggested changes discussed.
Investment Opportunistic Policy Review	Recommendations Implemented	Policy will be reviewed in light of recent discussions with the board on this asset class.
Pension Overpayments	No Recommendations Presented	OPERS management continues to seek a revision to ORC 145.561 that will clarify and seek recovery of all benefits overpaid subsequent to change.
Global Bonds Comprehensive processes review (ITCI)	Recommendations Substantially Implemented	Investment staff should implement risk management change to monitor credit exposure across all portfolios. This is scheduled to occur during 2009.

**OPERS INTERNAL AUDIT  
2008 AUDITS COMPLETED**

<b>AUDIT AREA</b>	<b>STATUS OF RECOMMENDATIONS</b>	<b>SIGNIFICANT COMMENTS</b>
Survivor Benefits Review	Recommendations Implemented	None
TGM Real Estate Manager	Recommendations Implemented	None
Custody Transition Review (D&T) and follow up	Custody transition from State Street to JPMorgan Chase completed	Initial JPMorgan Chase system and accounting issues have been resolved at the transition cutoff with cash, positions, pricing and securities classifications.
Cash Management Review	No Recommendations Presented	None
Real Estate Transactions	No Recommendations Presented	None
Service Retirement Benefits	Recommendations Implemented	None
Voluntary Excess Beneficiary Association (VEBA) Review	Recommendations Implemented	None
Investment Account Openings and Closing	Recommendations either implemented or to be completed by year end	Private Equity and Private Real Estate should adapt formal account process similar to External Manager.
Defined Contribution Policy Review	Recommendations Substantially Implemented	Monthly performance report for DC options is scheduled to be completed by year end.
Internal Review- Publication Consulting Expenses	No Recommendations Presented	None
emPower (Imaging) System Review	A number of high risk issues were identified, critical to operations and requiring comprehensive corrective action plan. Several were implemented, with one recommendation projected for completion by March 31, 2009.	Employee access to case file records has not been limited, that could impact safeguarding of protected health information.
Pension Tax Reporting	No Recommendations Presented	None
External Business Partners Security Breach Review	No Recommendations Presented	None
External Public Manager Evaluation Policy	Recommendations pending policy review discussion	None
Legal Contracts Review	Recommendations pending management review and 2009 action plan	Purchasing office is to be established to provide consistency over enterprise contract review as well as ensure central filing of executed contracts.
Corporate Proxy Policy Reporting	No Recommendations Presented	None

**OPERS INTERNAL AUDIT  
2008 AUDITS COMPLETED**

AUDIT AREA	STATUS OF RECOMMENDATIONS	SIGNIFICANT COMMENTS
IT Security Internal Member Threats Review	A number of high risk issues were identified, requiring comprehensive corrective action plan. Several are ongoing, with development occurring throughout 2009.	Security logging on actions taken or changes to member data is minimal; alerts to be developed.
Futures Guidelines Compliance Review	No Recommendations Presented	Discussions occurred between Investments and Finance ( Investment Accounting to address process.
Oaktree General Partner Review	No Recommendations Presented	None
Real Estate Valuations	No Recommendations Presented	Pricewaterhouse Coopers external review of property valuations did not identify any significant valuation issues.
Investment Health Care Policy Compliance Review	Review Ongoing	
Human Resources Administrative Review	No Recommendations Presented	None
Bloomberg Global Bonds Trading System	Report Pending Review of Recommendations Presented	None
CEM Global Pension and Member Data	Review Ongoing	
Investment Relationships-Ethics Confirmation Letters	Review Ongoing	
Cash Movements Review	Review Ongoing	

**OPERS Internal Audit Plan  
Detail on Critical Audit Priority Reviews - 2009**

<b>Reporting Entity</b>	<b>Audit Area's)</b>	<b>Objective</b>
Investments/Internal Asset Mgt.	US Domestic Equities	This review will be co-sourced with the Investment Training and Consulting Institute and will verify that internal controls effectively mitigate the risks (operational, accounting, reporting, etc.) associated with the lifecycle processing of equity trades.
Investments/Internal & External Asset Mgt.	Investment Consultant and Manager Relationships	Internal Oversight, Fees, Due Diligence and Operational Processes will be reviewed for both internal and external manager portfolios
Investments/External Asset Mgt.	* Public Manager Review * Private Equity Manager Review * Private Real Estate Manager Review	These internal and external reviews focus on investment management agreement compliance, due diligence documentation, investment valuation policy compliance, management reporting, etc.
Investments/Investment Policies	* Securities Lending Policy Review * Brokerage Policy Review * Responsible Contractor Policy Review	These reviews will focus on compliance and management reporting for Board approved investment policies.
Investments/Total Fund	* Incentive Compensation * Performance Reporting	These internal reviews are intended to ensure that investment performance reporting is both accurately and consistently reflected based upon investment accounting and custodian bank reporting and reflected in proper incentive compensation payments.
Investment Portfolio Guideline Approval Process	Investment portfolio guideline compliance	Investment staff compliance with the internal and external portfolio guidelines developed by staff ( and not requiring board approval) will be reviewed
Investments Implementation	Trade Order Management System	New Charles River Trade Order Management (TOMS) solution, scheduled for implementation in 2009, will be reviewed.
Private Markets Information System	Private Equity and Private Real Estate	New Private Markets solution, for reporting, analysis and monitoring, will be reviewed as implementation occurs.



**OPERS Internal Audit Plan  
Detail on Critical Audit Priority Reviews - 2009**

Reporting Entity	Audit Area's)	Objective
Strategic Initiatives	2009 Strategic Plan Enterprise Planning Enterprise Balanced Scorecard Investments Business Process Data Scrubbing HR Payroll Solution	Initial year of Strategic Plan will require audit allocations to review controls and processes established on strategies, business process measurement and data validation; judgment may be required in final areas selected for review due to timing and finalization of 2009 plan Key focus include: reviewing Balanced Scorecard application controls over data validity, accuracy and integrity; data scrubbing will examine how incomplete member data situations are addressed; and strategies to manage zero balance data accounts
IT- Finance	Great Plains G/L Reporting and accounting solution enhancements	This review will consist of both a financial and IT component, to address major system controls, reporting by plan system enhancements as well as enhanced subsidiary reporting details/requirements .
IT-Finance	New Payroll System Solution	IT and Administrative controls for the Human Resources solution will be reviewed with modules for employee resource and timesheet tracking, benefit enrollment and project tracking.
IT Security	Follow up review IT Security	Follow up review will be completed that will address actions necessitated based on the results of the Crowe Chizek Insider Threat to Member Data Security review
Finance- Accounting	Centralized Purchasing	Organizational change to a centralized function requires a comprehensive assessment of overall compliance and adequacy of control network and potential solutions.
Finance- Accounting	Employer Billing and Penalty Process	Separate Reviews will focus on employer billing, accounting and reporting as well as the delinquent billing penalty process and penalty review situations.
Benefits Admin- Health Care	Health Care Accounting and Reporting	Focus will be directed toward extensive review of health care costs reporting, accounting and reconciliation controls within various health care cash flow components.
Benefits Admin- Health Care	Medical RMA	Review will examine process for paying medical expenditures through these retiree medical accounts and overall controls, compliance with all regulatory and policy guidelines.

**OPERS Internal Audit Plan**  
**Detail on Critical Audit Priority Reviews - 2009**

Reporting Entity	Audit Area's)	Objective
Benefits Admin- Pension	Continuous Reviews	This focused review will regularly examine automated benefit data for outliers, potential representing issues of concern.
OPERS	Pension System Business Process Evaluation	This consulting is a participation in the OPERS assessment of proposed changes in the pension business process model. This represents the core area of focus for the end to end initiative.
OPERS	Strategic Planning and Enterprise Risk Management	Their assessment will be directed to determining how best to integrate a reasonable solution of ERM into overall Strategic Planning in subsequent years
OPERS	Ethics	This ongoing review will verify that OPERS managers, business partners and vendors are in compliance with Ohio Ethics laws prohibiting gifts to OPERS staff and board.