

**MINUTES OF MEETING
COUNTY EMPLOYEES RETIREMENT SYSTEM
AND KENTUCKY RETIREMENT SYSTEMS
BOARD OF TRUSTEES JOINT AUDIT COMMITTEE
AUGUST 25, 2022, 10:00 A.M., E.T.
VIA LIVE VIDEO TELECONFERENCE**

At the August 25, 2022 meeting of the Joint Audit Committee of the Board of Trustees of the County Employees Retirement System and the Kentucky Retirement Systems, the following Committee members were present: William O'Mara, Betty Pendergrass, Lynn Hampton, and William Summers, V. Staff members present were David Eager, Rebecca Adkins, Erin Surratt, Michael Board, Victoria Hale, Connie Davis, Madeline Perry, Matthew Daugherty, Kristen Coffey, Carrie Bass, Steve Willer, Ann Case, Elizabeth Smith, Ashley Gabbard, Phillip Cook, Katie Park, and Sherry Rankin. Others present included CERS CEO Ed Owens, III, KRS CEO John Chilton, KRS Trustee Ramsey Bova, and Allen Norvell with Blue and Co.

Mr. O'Mara called the meeting to order.

Mr. Board read the Opening Video Teleconference Statement.

Ms. Rankin called roll.

Mr. O'Mara welcomed Mr. William Summers, V. to the Committee.

There being no *Public Comment*, Mr. O'Mara introduced the agenda item *Approval of Minutes – May 24, 2022*. Ms. Hampton made a motion and was seconded by Ms. Pendergrass to approve the minutes as presented. The motion passed unanimously.

Mr. O'Mara introduced the agenda item *Overview of Fiscal Year 2022 External Audit*. Mr. Allen Norvell with Blue & Co. presented the material. Mr. Norvell briefly presented a memo required by professional standards which describes important information relating to the audit. He advised the Committee that the role of Blue & Co. is to express an opinion about whether the financial statements prepared by management are fairly presented and are in accordance with

accounting principles generally accepted in the United States. Mr. Norvell directed the Trustees to the memo (meeting materials, pp. 7-9) for further detail and information.

Mr. O'Mara introduced the agenda item *Financial Reporting Updates*. Ms. Adkins presented unaudited Financial Statements for Fiscal Year Ended June 30, 2022 beginning with the Combining Statement of Fiduciary Net Position of the Pension Funds. She stated that all assets were down 4.57% and advised that footnotes were included in the report to clarify any increases or decreases of 10% or more. Ms. Adkins also reviewed the Combining Statement of Changes in Fiduciary Net Position of the Pension Funds. CERS Nonhazardous was down 7.5% and CERS Hazardous was down 7.09% for the entire fiscal year, said Ms. Adkins. KERS Nonhazardous was down .25% and KERS Hazardous was down 6.37%. She advised that SPRS received a 215 million dollar appropriation to pension which was received at the end of FY 22 and would have been down 5.52% without those funds. Mr. Summers asked for clarification regarding the footnote which stated that corrections were being processed. Ms. Adkins advised that health insurance contribution was reported into the pension fund for some time as required by statute. This was corrected once there were changes to the statute which required the funds to be reported to insurance. Next, Ms. Adkins presented the Fiduciary Net Position of the Insurance Funds for FY 22. She reported that returns had decreased by 4.65% for the fiscal year. The Combining Statement of Changes in Fiduciary Net Position for Insurance Funds was also reviewed with the Committee. CERS Nonhazardous was down 3.76% and CERS Hazardous was down 5.79%. KERS Nonhazardous was down 3.81% and KERS Hazardous was down 7.2%. Next, Ms. Adkins reviewed the CERS Pension Funds Contribution Report and stated that CERS Nonhazardous was cash flow negative and CERS Hazardous was cash flow positive. KERS Nonhazardous, KERS Hazardous, and SPRS were all cash flow positive, said Ms. Adkins. The Insurance Fund Contribution Report for CERS illustrated a positive cash flow across plans. KERS Nonhazardous was cash flow positive, however, KERS Hazardous and SPRS had negative cash flows. Ms. Hampton asked when contributions will continue to be made into KERS Hazardous. Ms. Adkins stated that the Actuary makes the decision regarding the pension-insurance split. Further, Ms. Hampton asked if the Actuary has projected when they will begin contributing to that plan. Ms. Adkins advised that she did not have that information. Ms. Hampton also asked what percent the plan is funded. Ms. Adkins stated that the plan was funded 130% in 2021. Ms. Adkins reviewed the budget-to-actual analysis for the FY 21-22 KPPA Administrative Budget with the Committee and reported that about 15% of the budget remained

at the end of the fiscal year; 8.5% under budget without the reserve. Adoption Assistance, Ice Miller (legal), Medical Reviewers, and Miscellaneous were over budget, said Ms. Adkins. Ms. Pendergrass asked for a summary regarding the two million dollar increase shown in the Staff Subtotal. Ms. Adkins believed the increase to be attributed to the addition of the CERS and KRS CEOs, increased salaries for positions within the Office of Investments, and an increased salary for the KPPA employees. Ms. Adkins stated that she would need to conduct a study to decipher the details of the increase. Mr. Eager stated that the analysis can be broken down into three issues: headcount, Investment CEOs, and increased compensation for active employees. Ms. Adkins stated that overtime was also a contributor to the increase. Mr. O'Mara suggested that the recent analysis presented to the working group for the Administrative Budget would be a starting point for the requested analysis. Ms. Adkins reviewed the Plan Specific Expenses and Hybrid Percentages for FY 2022. Ms. Adkins advised that Board Separation Expenses for FY 21 and FY 22 would be included in FY 2023. Ms. Hampton asked why Ms. Adkins had not included the Board Separation Expenses as an adjustment since the audit had yet to be finalized. Ms. Connie Davis stated that this was due to the books being closed at BNY Mellon and because the total was not a material amount. Ms. Hampton and Ms. Pendergrass expressed concern and advised that Ms. Davis consult with Blue & Co. to determine if an adjustment can be made. Mr. O'Mara concurred. Ms. Adkins agreed to research and confirm.

Ms. Connie Davis reviewed the drafted timetable for the Fiscal Year 2022 Annual Comprehensive Financial Report (ACFR) and Summary of the Annual Financial Report (SAFR) with the Committee. Ms. Davis reported that she is working with the auditors to meet the required deadlines for these reports. The evaluation and draft are due to the Public Pension Oversight Board (PPOB) by mid-November and the final actuarial evaluation is due by the December meeting of the PPOB, said Ms. Davis. Additionally, the ACFR is due to the State of Kentucky by December 7, 2022 and the SAFR will be released in January of 2023. Ms. Davis stated that the GASB 67 and 74 reports are required for the financial statements and are typically drafted by September or October; therefore, the ACFR and SAFR drafts can be completed in November. The GASB 68 and 75 reports are scheduled to be presented to the CERS and KRS Board of Trustees in March of 2023. Ms. Pendergrass asked Ms. Davis if Blue & Co. understands the critical nature of the GASB 68 and 75 reports for water districts to comply with State law. Ms. Davis stated that they do understand and that she will meet with them several times to ensure that deadlines are met. Ms. Adkins added that a Project Manager had been

included this year which would aid in the tracking of deadlines. Mr. Allen Norvell with Blue & Co. confirmed that he and his team are aware of all deadlines. Lastly, Ms. Davis announced that an achievement award and certificate were received for the 2021 ACFR and thanked all involved.

Mr. O'Mara introduced the agenda item *Joint Audit Committee Administrative Updates*. Ms. Carrie Bass with the Office of Legal Services presented the Information Disclosure Incidents for the second quarter of the 2022 calendar year. She reported that there was one incident which implicated HIPAA/HITECH. In this incident, a medical review report related to disability was sent to an incorrect member. The Disclosure Response Team quickly reached out to the member who received the report in error. An affidavit was completed and returned confirming that no other individual had access to the documentation while in their possession and the affected member was notified. There was also an incident which implicated KPPA's Internal Data Disclosure Notification Policy, said Ms. Bass. A member reported receiving a blank Form 6000 with a pre-populated name and ID for another member in addition to receiving their own documentation from KPPA. The recipient completed an affidavit to confirm that no other individual had access to the documentation while in their possession and returned the documentation to KPPA. The affected member was notified. Lastly, a vendor, Managed Medical Review Organization (MMRO), sent 11 auto-generated emails related to KPPA members and two employees of another state retirement system. MMRO immediately stopped all auto-generated emails and reached out to the two email recipients employed at the other state retirement system. The recipients confirmed destruction of the emails that were received in error. Ms. Bass stated that MMRO took quick action to resolve the breach and has since taken action to ensure no reoccurrence. Ms. Pendergrass indicated that MMRO costs four-times the amount of the previous vendor in this position and caused 11 incidents in the second quarter. Next, Ms. Bass reviewed the Anonymous Tips Report. These anonymous tips were received by the Kentucky Retirement Systems prior to April 1, 2021 and the Kentucky Public Pensions Authority on and after April 1, 2021. It was reported that one case had been closed, one case had been opened, and two cases had been opened and then closed. Additional detail on these cases may be viewed on pages 29-30 of the meeting materials.

Ms. Kristen Coffey reported on the Internal Audit Budget as of June 30, 2022 and Proposed Budget for 2023. She stated that approximately 13% of the budget remained at the end of the

fiscal year. Staffing/Salaries was the primary cause of this variance, said Ms. Coffey. Ms. Pendergrass expressed concern regarding staffing within the Division of Internal Audit Administration. It was mentioned that one full-time employee and one intern would be recruited in the near future. Ms. Pendergrass asked if additional Staff would be needed. Ms. Coffey advised that she has been working with Mr. Eager on recruitment within the Division and would report any updates at the next meeting of the Joint Audit Committee. Mr. Eager added that KPPA Human Resources was assisting with those recruitments. Next, Ms. Coffey reviewed the Proposed Fiscal Year 2023 Budget with the Committee. She advised that the presented budget had been included in the Administrative Budget which had already been approved by the KPPA Board of Trustees. Ms. Coffey stated that the Proposed Fiscal Year Budget for the Division of Internal Audit Administration can be presented to the Joint Audit Committee prior to KPPA Board approval of the Administrative Budget going forward, if that is the will of the Committee. Mr. O'Mara stated that the Joint Audit Committee would like to review the proposed budget in May of the fiscal year to express their endorsement or opposition. Ms. Hampton and Ms. Pendergrass agreed with Mr. O'Mara. Ms. Coffey agreed to prepare the budget for review by the Joint Audit Committee in May of each fiscal year. Mr. O'Mara asked for further explanation regarding the \$110,000 increase in the budget. Ms. Coffey explained that this increase included the 8% raise for active employees which was effective July 2022, the salary for a new full-time position, as well as additional compensation increases for current employees. Lastly, Ms. Coffey provided a status update on current Internal Audit Projects. The Division has purchased TeamMate, an electronic audit software tool. Ms. Coffey stated that this tool will increase efficiency within the Division and assist in the tracking of risks across the Agency and within Divisions. Controls to mitigate the identified risk can also be applied via the tool. Ms. Hampton inquired as to what agencies also use the TeamMate software. Ms. Coffey stated that TeamMate is a premiere auditing software and is used by agencies and companies across the country including the Kentucky Transportation Cabinet. Ms. Coffey briefly reviewed the Status of Fiscal Year 2023 Internal Audit Assignments table (meeting material, p. 34). Ms. Pendergrass stated that she is pleased with the addition of the estimated hours and actual hours columns to track time spent on each assignment. Ms. Coffey discussed the Review of the JP Morgan Chase Accounts audit which the Division has been working on. She advised that recommendations for improvements will be presented in the near future.

Ms. Adkins presented the Plan Liquidity Phase I Update. She stated that there were two

recommendations remaining on the Plan Liquidity Phase I Audit. The first recommendation is that KPPA leadership should document a clear definition of how the Retirement Allowance Account (RAA) has been established. The second recommendation is that funds deposited into JP Morgan Chase (JPM) be transferred immediately upon receipt to BNY Mellon, the trust custodial bank. Ms. Adkins reviewed the memo with the Committee and advised that these issues would take time to remediate. There was discussion regarding the ideal JPM account balance and sweep account processes. Mr. Summers asked for the timeline of hiring the new Chief Financial Officer (CFO). Ms. Adkins stated that the position is posted and will close at the end of August. Mr. Summers suggested that the hired CFO make recommendations to the Committee regarding sweep accounts and account balances at JPM. Ms. Hampton stated that she would like Ms. Adkins to continue evaluating cash management and then the CFO may review the details and make their recommendation. Ms. Adkins stated that she will work with the hired CFO on the matter when they arrive. Mr. O'Mara summarized the discussion. He stated that this is an open issue which requires further analysis to evaluate what is the best organization and flow with our banking partners. Additionally, the Committee understands that the issues will take time to be resolved and are pending the onboarding of a new CFO; however, the Committee would like periodic updates on the matter. Mr. Summers also asked if it is required that the agency utilize JPM since that is the bank of the Commonwealth. Ms. Adkins stated that she and Staff are researching that question. Mr. O'Mara added that he is hopeful that KPPA will be able to partner with the Finance Cabinet and JPM to design what is best for the agency.

Mr. O'Mara introduced the agenda item *Strategic Audit Plan*. Ms. Pendergrass stated that the provided Strategic Audit Plan is informational and outlines the goals and objectives that the CERS Board would like to accomplish through governance over the next several years. Ms. Hampton asked how Ms. Pendergrass will execute Objective A: Evaluate system risks and identify potential internal audit projects to assess controls designed to manage risks. Ms. Pendergrass stated that this objective is required and that the Committee of Sponsoring Organizations (COSO) requests that governing Boards identify risk that they believe to be important to the system. Management evaluates the risk and determines if controls may be utilized to mitigate the identified risk. Further, Ms. Pendergrass stated that Ms. Coffey has created and sent a survey to Trustees and Staff in the past to identify potential risks within the system. There was discussion of who would evaluate the system risks – Staff or the CERS Board. Ms. Pendergrass stated that both parties would be responsible for the evaluation.

Ms. Erin Surratt stated that the Committee requested a report on the number of member invalid addresses and how Staff reaches out to those members. She advised that the material was placed into the Board Books, but was not included on the meeting agenda; therefore, Ms. Surratt advised that the informational item would be placed on the agenda for the November meeting of the Joint Audit Committee.

Ms. Rebecca Adkins wished to answer a question asked about the salary line item of the Administrative Budget. She advised that the extra funds spent was likely the 25th payroll which occurred in fiscal year 2022. Ms. Adkins stated that she will conduct an analysis to confirm.

Ms. Coffey advised that she has begun drafting the agenda for the November meeting and has added the Invalid Addresses item.

Mr. O'Mara introduced the agenda item *Professional Articles*. Ms. Coffey presented an article entitled *Achieving Governmentwide Enterprise Risk Management*. This article provides information on accessing risk and best practices to identify risk. Additionally, Ms. Coffey presented the article, *Creating Value in Government*, and stated that it may be helpful in the development of a Strategic Plan. Mr. Eager added that these articles may fulfill Trustee Education requirements, if approved by their CEO.

There being no further business, a motion to adjourn was made by Ms. Pendergrass and seconded by Mr. Summers, the meeting adjourned.

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CERTIFICATION

I do certify that I was present at this meeting and I have recorded above the action of the Committee on the various items considered by it at this meeting. Further, I certify that all requirements of KRS 61.805-61.850 were met in connection with this meeting.


Recording Secretary

I, as Chair of the Joint Audit Committee of the Board of Trustees of the County Employees Retirement System and the Kentucky Retirement Systems, do certify that the Minutes of the meeting held on August 25, 2022 were approved by the Joint Audit Committee on November 28, 2022.


Committee Chair

I have reviewed the Minutes of the Audit Committee Meeting on August 25, 2022 for form, content, and legality.


Executive Director
Office of Legal Services