



Agenda Item 7a

June 16, 2015

ITEM NAME: 2015-17 Audit Plan – Office of Audit Services

PROGRAM: Audit Services

ITEM TYPE: Action

RECOMMENDATION

Approve the proposed Audit Plan for Fiscal Year 2015-16 and 2016-17.

EXECUTIVE SUMMARY

Each year, the Office of Audit Services presents to the Risk & Audit Committee a proposed audit plan for the Committee's review and approval. Our proposed audit plan is attached to this agenda item as Attachment 1, covering audits to be performed in Fiscal Year 2015-16 and a preliminary audit plan for Fiscal Year 2016-17.

STRATEGIC PLAN

This item is not a specific product of the Strategic Plan.

BACKGROUND

The International Standards for the Professional Practice of Internal Auditing (Standards) require us to establish a risk-based plan to determine the priorities of the internal audit activity, consistent with the organization's goals. The Standards also require us to consider input of the Board of Administration (Board) and senior management during an annual risk assessment and consider accepting proposed consulting engagements based on the engagement's potential to improve risk management, add value, and improve the organization's operations.

ANALYSIS

The Standards require internal audit activity to evaluate and contribute to the improvement of governance, risk management, and control processes using a systematic and disciplined approach. Specifically, the internal audit activity must evaluate risk exposures relating to, and the adequacy and effectiveness of controls within, the organization's governance, operations, and information systems regarding the:

- Achievement of the organization's strategic objectives;
- Reliability and integrity of financial and operational information;
- Effectiveness and efficiency of operations and programs;
- Safeguarding of assets; and
- Compliance with laws, regulations, policies, procedures, and contracts.

Audit Universe

In developing a risk-based audit plan, we first established an audit universe. The audit universe is a list of all the possible audits that could be performed. To establish the audit universe, we considered components of the CalPERS strategic plan, California Public Employees' Retirement Law (PERL), CalPERS basic financial statements, information security program and information technology services management. We also considered inputs from the Board, executive management and senior management. By incorporating components of the strategic plan, the audit universe reflects consideration of the environment in which CalPERS operates and the organization's attitude toward managing the risks.

We developed the risk-based audit plan based on the audit universe, input from the Board and management, and an assessment of risks and exposures affecting the organization.

Input from the Board and Management

To obtain input from the Board and management, we conducted Board surveys and coordinated our risk assessment activity with the Enterprise Compliance Division and Enterprise Risk Management Division. We interviewed division chiefs and executive management. Inputs from the Board and management are incorporated into our assessment of risks and exposures. The risk assessment methodology utilized for public agency reviews and internal audits differs based on the scope and overall audit objectives.

Public Agency Risk Assessment Methodology

The Office of Audit Services performs compliance reviews of contracting public agencies, including cities, counties, special purpose districts and authorities, schools, state agencies, California state universities, and agricultural districts. The primary objective of the review is to assess whether the contracting agencies comply with applicable sections of the PERL and prescribed reporting and enrollment procedures as they relate to the agencies' contracts with CalPERS.

The Office of Audit Services performed an annual risk assessment to select, and determine the priorities of, contracting agencies for review in fiscal year 2015-16. For each contracting public agency, we evaluated multiple risk factors, assigned a risk value and weight to each risk factor, and calculated an overall risk score for each agency. The risk factors included number of years since last audit, input from the Board and management, agency attributes (e.g. enhanced retirement contract, annual covered payroll, contract for safety members), employee attributes (e.g. high monthly payrate, high special compensation), agency size, and agency type.

We ranked the agency overall risk scores to develop a risk-based audit plan. For fiscal year 2015-16, we plan to allocate two full time positions to perform targeted

review of agencies identified through business intelligence data analyses. We will apply 80 percent of the remaining public agency audit resources to the highest ranked agencies and 15 percent to the remaining agencies. We will reserve 5 percent of the remaining public agency audit resources for special requests by management. Overall, we plan to complete 100 compliance reviews and 25 targeted reviews.

Internal Audit Risk Assessment

The Office of Audit Services performs internal audits that evaluate risks and the adequacy and effectiveness of controls designed and implemented in response to the risks regarding the achievement of the organization's strategic objectives, reliability and integrity of financial and operational information, effectiveness and efficiency of operations and programs, safeguarding of assets, and compliance with laws, regulations, policies, procedures, and contracts.

The Office of Audit Services performed an annual risk assessment to select, and determine the priorities of, auditable activities for fiscal year 2015-16. For each auditable activity, we evaluated multiple risk factors, assigned a risk value and weight to each risk factor, and calculated an overall risk score for each auditable activity. The risk factors included character of activity (e.g. core business activity), character of information (e.g. health-related information), dollar size, transaction volume, changes in process, system, and people, prior audit and findings, process and controls, strategic goals and objectives, and degree of Board and executive interest or concerns. We ranked the auditable activities' overall risk scores to develop a preliminary risk-based audit plan.

Additional factors considered in developing the internal audit plan include recent audits and findings, known risks and planned mitigation in progress, value-added consulting engagements, logical sequencing of audits, coverage provided by other assurance functions, impact on business areas, and available audit resources. Taking all these into account and applying the professional judgment of experienced auditors, we selected the areas to include in our audit plan.

Since one of the goals of the audit function is to not only provide assurance to the Board, but also provide assistance to management, we also allocate resources toward responding to special requests and consulting projects. In addition to our planned audit activities, the Office of Audit Services also coordinates contracted external audits and reviews, including the financial statement audit, Governmental Accounting Standards Board Statement No. 68 audit, real estate and other contracted specialty investment audits, and actuarial valuation and certification service reviews.

Looking Ahead to Fiscal Year 2016-17

In addition to the detailed 2015-16 Plan presented for approval, the Office of Audit Services also looked to the horizon and developed a preliminary plan for Fiscal Year 2016-17.

To remain flexible and responsive to changes in the organization's business, risks, operations, programs, systems, and controls, we will review and adjust the fiscal year 2015-16 and 2016-17 plans, as necessary. Additionally, the new Chief Auditor, who starts in late July, will review the plans and may choose to alter them. Proposed modifications to the audit plans will be presented to the Risk & Audit Committee as needed during the year.

BUDGET AND FISCAL IMPACTS

Not Applicable.

BENEFITS/RISKS

The proposed audit plan will set the direction and priorities of the internal audit activities for the next fiscal year. Implementation of this audit plan will result in compliance with the Standards while providing the Board and management a higher level of assurance that appropriate controls are in place and working as intended, and contracting public agencies comply with the PERL and prescribed procedures. Not implementing the audit plan would result in non-compliance with the Standards, decreased levels of assurance, and reduced ability to detect non-compliance with the PERL and prescribed procedures by public agencies.

ATTACHMENTS

Attachment 1 – Proposed Audit Plan for Fiscal Year 2015-16 and Preliminary Audit Plan for Fiscal Year 2016-17

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