

**THE AUDIT COMMITTEE  
of the  
BOARD OF TRUSTEES  
MARYLAND STATE RETIREMENT AND PENSION SYSTEM**

**MINUTES OF THE MEETING OF April 16, 2019**

The Audit Committee met on Tuesday April 16, 2019 at 10:55 a.m., in the Board Room of the Maryland State Retirement Agency at 120 East Baltimore Street, Baltimore, Maryland.

Committee members present were: Richard E. Norman, Chairman  
David B. Hamilton  
F. Patrick Hughes  
Theresa Lochte (by phone)

MSRA attendees were: R. Dean Kenderdine, Executive Director  
David Rongione, Chief Internal Auditor  
Harvey Raitzyk, Retirement Administrator  
Andrew Palmer, Chief Investment Officer  
Rachel Cohen, Principal Counsel  
Melody Countess, Chief Operating Officer  
Patricia Wild, Managing Dir. Inv. Admin. & Accounting  
Lauren Smith, Internal Audit Contract Manager  
Richa Sultana, Internal Audit Supervisor  
Jody Shaw, Deputy Counsel

BD & Co attendees were: Scott Freinberg, Engagement Partner  
Jeff Binford, Senior Manager

**A. Minutes of the November 13, 2018 Audit Committee Meeting**

On a motion made by Mr. Hamilton, and seconded by Ms. Hughes, the minutes of the November 13, 2108 Audit Committee meeting were ratified.

**B. Presentation of the Management Fee Operational Audit by BD & Co.**

Mr. Binford of BD&Co presented the results of the Management Fee Audit. Mr. Binford advised the committee that the audit found no instances of incorrect fees. During the audit, BD&Co did identify five (5) areas of improvement related to control enhancements. BD&Co believe these control enhancements will further ensure the correct calculation of fees.

Mr. Binford noted that the scope period included \$400 million in management fees. BD&Co reviewed the adequacy of policies and procedures as well as control design and effectiveness.

Mr. Binford briefly explained the findings from the Management Fee Audit that include:

- 1) Independent review is not consistently performed for all fee
- 2) Management fee variances in excess of tolerance limits were not investigated
- 3) Overarching spreadsheet controls are not in place to limit errors in the process
- 4) Monitoring of carried interest process not clearly defined
- 5) Private and hedge fund asset fees are reviewed on a best effort's basis.

Mr. Hughes advised that the calculation of management fees is a sensitive risk area especially with the Agency moving toward in-house managing. He expressed the need to ensure the process is functioning correctly at the point of implementation; advising that processes will have to be revisited to ensure we have the correct resources in place to ensure compliance, which means additional funding will be needed for audit. Mr. Rongione advised that the budget request for additional funding for investment audits was denied by DBM.

Mr. Freinberg from BD&Co explained that front-end advisory work would need to be executed before in-house management begins; the changes in processes will have to be documented including any new systems for the purpose of in-house management. Mr. Hughes expressed concern of safeguarding worksheet formulas. Mr. Binford of BD&Co explained that identifying the most significant and complex spreadsheets will be key.

Mr. Hughes inquired with the staff that currently oversee external managers, as to their role in management fee approval. Andrew Palmer and Pat Wild of Investments advised that those that oversee the external managers are involved in the initial contract creation and the established fee schedule. Mr. Hamilton inquired whether the Agency had a Compliance Officer that assists with oversight of the process. Mr. Rongione stated that the Investment department has a Compliance Officer, and not the Agency as a whole. Mr. Rongione also referred back to the Investment Summer Study that was performed, which identified the reporting structure of the Compliance Officer as an item to consider, to either report to Legal, Internal Audit or directly to the Board. Rachel Cohen of Legal explained that the Legal Division is part of the Attorney General Office, and that compliance cannot report to Legal. Mr. Kenderdine agreed and explained that the Agency may have to go back to Legislation for compliance oversight.

#### **C. Internal Quality Assurance Program Results**

Mr. Rongione presented the results of the Internal Audit Division's quality assurance efforts for calendar year 2018. There were two components to the quality assurance efforts – reviews of selected audits, and a review for compliance with general internal audit standards. There were no recommendations for the general standards review.

#### **D. Internal Audit Staffing Update**

Mr. Rongione noted that the Internal Audit Division is currently operating at 75%, with 3 of 4 positions active. Internal Audit conducted interviews for the open Internal Auditor II position; however, an offer was not extended to potential candidates. During the budget process, Internal Audit requested additional funds for IT and Investment audits, in order to address risks the current resources are unable to address. These funds were denied during the budget process, and it was recommended that the open Internal Auditor II pin be reclassified. Internal Audit has completed

the process with DBM to reclassify the position as an IT Audit Manager. Internal Audit is hopeful that the position will be filled prior to the next fiscal year; however, this will be difficult given the salary constraints. This reclass will also leave a void in the responsibilities of the current Internal Auditor II PIN.

Mr. Hamilton inquired about cyber security risks and controls, and whether it will be addressed. Mr. Rongione confirmed that this is the intent of the IT Audit Manager position, especially given the increased risk with the MPAS project.

**E. Revised FY19 Audit Plan**

Mr. Rongione explained that in developing the annual audit plan, consideration is given to the results of the risk assessment and available staff audit hours. Mr. Rongione explained that he had anticipated filling the vacant Internal Auditor II position in October 2018, and had allotted for those vacant hours in developing in audit plan. Since this position has now been vacant for 7 additional months, the audit plan had to be revised. Mr. Hughes stated that the meeting minutes need to reflect that two audits are being removed from the audit plan due to lack of resources. Mr. Kenderdine explained that five (5) new positions were created in IT and were needed for support due to member portal. Mr. Kenderdine stated that the Agency should be in a better position in the coming year to obtain audit positions.

Motion made to approve the revised audit plan by Mr. Hughes and seconded by Mr. Hamilton. Passed unanimously.

**F. Status of FY 2019 Audit Plan**

Mr. Rongione provided the Committee with a status update for the FY 2019 audit plan. For full-scope audits, the Death Benefit Processing audit is complete and the Administrative Fee audit is in progress. For outsourced audits, the Management Fee audit is complete, and the Valuation and Performance audit is in progress. There are 52 audits of participating employers to be completed in FY 2019. Of these, 22 are complete, and 30 are currently in progress.

**G. Status of Open Issues Log**

Mr. Rongione noted that Internal Audit has closed 13 issues, 9 new issues were added based on recently completed audits, which leaves 11 open issues. Mr. Rongione noted that the 2 legacy open issues related to a COMAR update and a review of SOC2 reports.

**H. Annual Agency Wide Risk Assessment**

Mr. Rongione explained that Internal Audit would begin the risk assessment process in the coming month. The process includes questionnaires sent to the Audit Committee, the Executive Director, Executive Staff and Unit Directors. The results will be compiled and incorporated into the risk assessment, which will be used to generate the FY20 audit plan.

**I. Completed Audits**

Mr. Rongione summarized the results of the recently completed audit of the Death Benefit process. He noted that the audit had an overall rating of “yellow” with five (5) identified issues. Three (3) issues were moderate risk, and two (2) were low risk. Agency management has agreed to implement corrective actions to address the issues identified in the audit.

**J. Other Business**

The next Audit Committee meeting will be held on July 16, 2019.

**K. Motion to Adjourn**

On a motion by Mr. Hughes, and seconded by Mr. Hamilton, the Committee adjourned the meeting at 11:35 a.m.

Respectfully submitted,

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David Rongione, Secretary