



Fairfax County Internal Audit Office

Retirement Administration Agency
Asset Administration Audit
Final Report

June 2007

"promoting efficient & effective local government"

Executive Summary

Our audit of the Retirement Administration Agency (RAA) found that sufficient controls were in place over the wiring of funds at the custodian bank and the processing refund/exit payments. The procedures for hiring and terminating investment manager firms were well documented and based on industry best practices. An area in which we noted opportunities for improvement included the following:

The monthly reconciliation process for the investment assets did not document the reconciliation of the investments asset units held by the custodian bank to the investment asset units held by the investment managers. In addition, reconciliation procedures performed by the investment accountant were not documented.

Scope and Objectives

This audit was performed as part of our fiscal year 2006 Annual Audit Plan and was conducted in accordance with generally accepted government auditing standards. Our audit objectives were to ensure:

- Funds with custodial banks were properly reconciled to RAA records
- Sufficient controls were in place over wiring of funds
- RAA investment managers had effective, documented procedures for hiring and terminating external managers and that procedures were based on best practices
- Adequate controls were placed over the payments of benefits outside the regular payroll procedures (exception payments)

Our audit scope was limited to a review of the RAA's accounting of the investment assets and its compliance of the county's Accounting Technical Bulletins and examination of their procedures regarding the replacement of investment managers during the fiscal year 2006 to determine whether the process was documented and based on industry best practices. We did not visit the custodian bank's office to perform transaction testing and our review of the controls over the wiring of funds was limited to a telephone interview with their staff followed by a request for supporting documents to verify the claims made during the telephone interview. Therefore, this was a scope limitation. The potential impact of this circumstance on our findings was that the controls over the wiring of funds may be weak and our procedures may have not detected the exposure. In addition, due to the ongoing implementation of the Pension Gold (the retirement management system) we did not test system controls. Our transaction testing did rely on those controls; therefore, this was a scope limitation. The potential impact of this circumstance on our findings was that some portion of our transaction data may have been erroneous.

Methodology

Our audit approach included interviewing appropriate staff, observing employees' work functions, detailed transaction testing, and evaluating the processes for compliance with sound internal controls, government regulations, and departmental policies and procedures.

The Fairfax County Internal Audit Office is free from organizational impairments to independence in our reporting as defined by generally accepted government auditing standards. We report directly and are accountable to the county executive. Organizationally, we are outside the staff or line management function of the units that we audit. We report the results of our audits to the county executive and the Board of Supervisors, and reports are available to the public.

Findings, Recommendations, and Management Response

Reconciliation of Investment Assets

The market value reconciliation reports did not document the reconciliation of the number of shares of different types of investment held by the investment manager firms to the records of the custodian. These reconciliation reports were prepared for the management of the Retirement Administration Agency (RAA) for review and were submitted to the Board of Trustees. This type of reconciliation is particularly important since the market value reconciliation always shows variances that stem from (according to RAA management) pricing and timing differences. Without the documented reconciliation of the number of each investment share held by the custodian to the investment manager firms, the RAA senior management and the board of trustees would be unable to verify the explanation being provided for the variance in the market value reconciliation reports.

In addition, while the RAA management has submitted a reconciliation plan to the Department of Finance for the monthly investment activities, the detail level reconciliation procedures, used to prepare the monthly journal entries to FAMIS, were not documented. As a result, neither the investment accountant assistant nor the investment manager, who reviewed the reconciliation package, was familiar with the steps the investment accountant (who was no longer there) had taken to verify Mellon Bank's statements before recording the journal entries in FAMIS.

Well documented reconciliation procedures allow for a more transparent process and could be used as training material for the training of new staff.

Recommendation: RAA management should develop and document monthly reconciliation procedures that define the steps needed to be performed in order to reconcile/verify the investment statements from the custodian. These procedures should also document the reconciliation of the records between the custodian and the investment manager firms at the number of shares level to ensure that both the RAA management as well the board of trustees know that pricing and timing are the only causes of the variance in the reconciliation report.

Management Response: It had been RAA's understanding that the custodian bank was

performing a reconciliation which included shares held and comparing their records to those of each portfolio manager. However, prior to the audit, RAA was not receiving any documentation from the custodian bank regarding share to share reconciliations. Since the onset of the audit, RAA is now receiving CDs each month from the custodian bank which provide evidence of reconciliation's performed, including a verification of shares held. RAA is in the process of updating reconciliation procedures and these are expected to be submitted to the Department of Finance by July 2007.