

MINUTES OF THE MEETING OF THE
ADMINISTRATIVE AND AUDIT COMMITTEE OF THE BOARD OF TRUSTEES OF THE
EMPLOYEES' RETIREMENT SYSTEM OF THE STATE OF HAWAII

JUNE 9, 2020

CITY FINANCIAL TOWER
201 MERCHANT STREET, SUITE 1500
HONOLULU, HAWAII 96813

Trustees present: Dr. Genevieve Ley, Chair
(by teleconference) Mr. Benntt Yap, Vice Chair
Mr. Wesley Machida
Mr. Jerome Rauckhorst

Staff present: Mr. Thomas Williams, Executive Director
(City Financial Tower Ms. Kanoë Margol, Deputy Executive Director
by teleconference) Ms. Elizabeth Burton, Chief Investment Officer
Ms. Donna Curry, Program Specialist
Mr. Bart Asato, Program Specialist
Ms. Dale Kehau Kanae, Recording Secretary

Attorney present: Mr. Ivan Torigoe, Deputy Attorney General
(by teleconference)

Guests present: Mr. Peter Hanashiro, KMH LLP
(by teleconference) Mr. Tyson Suehiro, KMH LLP
Mr. Lane Suzuki, KMH LLP

QUORUM/CALL TO ORDER

A quorum being present (Chair Ley, Vice Chair Yap, Trustees Machida and Rauckhorst), Chair Ley called the meeting of the Administrative and Audit Committee (Committee) of the Board of Trustees (Board) of the Employees' Retirement System of the State of Hawaii (ERS) to order at 1:30 p.m.

On a motion made by Trustee Machida, seconded by Vice Chair Yap, and unanimously carried, to be able to hold a meeting closed to the public and allow Trustees to participate by teleconference or other remote meeting technology, pursuant to the Governor of the State of Hawaii's Supplementary Proclamation dated May 18, 2020, in order to implement social distancing measures.

PUBLIC COMMENT

Chair Ley called for public comment. There were no members of the public present by teleconference, therefore no public comments. There was also no public testimony received by e-mail for this Committee meeting.

REVIEW ADMINISTRATIVE
AND AUDIT COMMITTEE,
AND INTERNAL AUDIT
CHARTERS

Chair Ley reviewed and discussed with the Committee and KMH LLP (KMH) Internal Auditor's a draft of the Administrative and Audit Committee Charter and Internal Audit Charters.

After review and discussion of the Administrative and Audit Committee Charter, the Committee decided that due to the numerous proposed edits,

REVIEW ADMINISTRATIVE
AND AUDIT COMMITTEE,
AND INTERNAL AUDIT
CHARTERS (CONT'D)

the Charter would be revised and presented at the next Committee meeting.

Also, after review and discussion of the Internal Audit Charter, the Committee accepted the noted changes as presented.

On a motion made by Trustee Machida, seconded by Vice Chair Yap, and unanimously carried, the Committee accepted the modifications to the Internal Audit Charter as presented and will recommend the revised Charter to the Board for final approval. (A revised Internal Audit Charter is attached for clarification).

KMH's Peter Hanashiro provided the Committee with an updated Internal Audit Report and mentioned that at the request of ERS Management and approval by the Administrative and Audit Committee Chair, KMH deferred IA project activities directly with the ERS from April 1, 2020 to July 1, 2020 in order to allow ERS' staff to focus solely on their daily workload and other organizational priorities during the statewide shutdown due to the SARS CoV-2 pandemic. In compliance with the State Government's work restrictions, KMH is working remotely on existing projects in the 2020 Audit Plan during this time while relying on limited assistance from ERS' staff.

The Committee also discussed and requested KMH provide a statement in their report relating to being within their contracted total budgeted hours. KMH agreed and will provide a statement in the report that they will be under the allotted budgeted hours due to project deadlines being pushed back possibly to the following year.

REVIEW OF DRAFT
EMPLOYEES' RETIREMENT
SYSTEM INTERNAL AND
EXTERNAL
COMMUNICATIONS PLAN

Program Specialist (PS) Donna Curry provided an oral and written report on the ERS Internal and External Communications Plan.

PS Curry discussed with the Committee the ERS Communication Plan's Purpose, Goals and Objectives of External and Internal Communications, Periodic Evaluation of Communications Plan for Revision, Relevance, and Improvement; and the 2020-2024 Strategic Plan Timelines and Target Dates.

The Committee requested that taxpayers be identified as a primary stakeholder as it relates to External Communications and suggested other changes to the Plan. PS Curry will add taxpayers as a stakeholder and requested the Committee suggest possible methods of communication and will also include the suggested changes.

After review and discussion of the ERS Communication Plan, the Committee decided that they will review the Plan at the next meeting, after the changes have been made.

UPDATE ON HAWAII
DOMESTIC RELATIONS
ORDERS, EFFECTIVE JULY 1,
2020

Program Specialist (PS) Bart Asato provided an oral and written report on an Update of the Hawaii Domestic Relations Orders.

PS Asato presented an overview to the Committee of the process and procedures of the Hawaii Domestic Relations Order discussing topics such as Laws, Branch Involvement, What the HiDRO Specifies, Pre- vs.

UPDATE ON HAWAII
DOMESTIC RELATIONS
ORDERS, EFFECTIVE JULY 1,
2020 (CONT'D)

Post- Retirement HiDROs, HiDRO Does Not, HiDRO Qualification,
How to Get Started, and On July 1.

The Committee requested possibly monitoring the process and ask that
the Internal Auditors do an initial assessment in 2021. ERS Staff will
provide further updates at the next Committee meeting.

APPROVAL OF MINUTES
- FEBRUARY 7, 2020

On a motion made by Trustee Rauckhorst, seconded by Trustee
Machida, and unanimously carried, the Committee approved the minutes
of the February 7, 2020, Administrative & Audit Committee meeting, as
presented.

ADJOURNMENT

On a motion made by Trustee Machida, seconded by Vice Chair Yap,
and unanimously carried, Chair Ley adjourned the meeting at 3:03 p.m.

REDACTED SIGNATURE

Thomas Williams
Executive Director

TW:dkik



Employees' Retirement System of the State of Hawaii
BOARD OF TRUSTEES
INTERNAL AUDIT CHARTER

I. INTRODUCTION

Internal auditing is an independent, objective assurance and consulting activity¹ designed to add value and improve an organization's operations. It helps an organization accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control, and governance processes.

II. ROLE OF INTERNAL AUDIT

The Internal Audit function of the Employees' Retirement System ("ERS") is established by the ERS Board of Trustees ("Board") and its responsibilities are defined in this charter which is approved by the Board. The Chief Audit Executive ("CAE"), which may be an individual employee or a firm contracted to outsource or co-source the internal audit function, reports functionally to the ERS Administrative & Audit Committee ("Audit-Committee") and administratively to the ERS Executive Director ("ED") or designee. Approval from the Board is required for the hiring, compensation, removal, or replacement of the CAE.

The objectives of Internal Audit are to assist management and employees of the ERS in the effective discharge of their responsibilities by providing them with analyses, appraisals, recommendations, counsel, and information concerning the activities reviewed and to promote effective internal controls at a reasonable cost.

III. AUTHORITY

The CAE and the Internal Audit staff are authorized to:

- A. Review all areas of the ERS;

¹As defined by the Institute of Internal Auditors, an *assurance* activity is an examination of evidence for the purpose of providing an independent assessment on governance, risk management, and control processes for the organization, while *consulting* refers to advisory and related client service activities intended to add value and improve an organization's processes.



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- B. Have full, free, and unrestricted access to all of the ERS's activities, records, physical property, and personnel necessary to complete their work;
- C. Have full, free, and unrestricted access to the Board, ~~Audit~~ Committee, ED, Deputy ED, Chief Investment Officer, Branch Chiefs, and all members of management;
- D. Allocate resources, set frequencies, select subjects, determine scopes of work, and apply the techniques required to accomplish audit objectives; and
- E. Obtain the necessary assistance of personnel in units of the ERS where they perform audits, as well as other specialized services from within or outside the ERS.

The CAE and the Internal Audit staff are not authorized to:

- A. Perform any operational duties for the ERS;
- B. Initiate or approve accounting transactions external to the internal audit function; nor
- C. Direct the activities of any ERS employee not employed by the internal audit function, except to the extent such employees have been appropriately assigned to auditing teams or to otherwise assist the internal auditors.

IV. INDEPENDENCE & OBJECTIVITY

Internal auditors have no direct responsibility or any authority over any of the activities or operations that they review. They should not develop and install procedures, prepare records, or engage in activities that would normally be reviewed by internal auditors.

Internal Audit's objectivity is not adversely affected, however, by recommending standards of controls to be applied in developing systems and procedures, or by evaluating existing or planned financial and operating systems and related procedures, and making recommendations for modification and improvements thereto in order to improve controls and/or enhance operational effectiveness.



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INTERNAL AUDIT CHARTER

V. SCOPE OF WORK

The scope of work of the Internal Audit function is to determine whether the ERS's network of risk management, control, and governance processes, as designed and represented by management, is adequate and functioning in a manner to ensure:

- Risks are appropriately identified and managed.
- Interaction with the various governance groups occurs as needed.
- Significant financial, managerial, and operating information is accurate, reliable, and timely.
- Employee actions are in compliance with policies, standards, procedures, and applicable laws and regulations.
- Resources are acquired economically, used efficiently, and adequately protected.
- Programs, plans, and objectives are achieved.
- Quality and continuous improvement are fostered in the ERS's control process.
- Significant legislative or regulatory issues impacting the ERS are recognized and addressed properly.

Opportunities for improving management control, process efficiency, and the ERS's image may be identified during audits. They will be communicated to the appropriate level of management.



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VI. RESPONSIBILITIES

Internal Audit is responsible for the following activities:

Standards

- A. The CAE is responsible for ensuring that all activities of the internal audit function are carried out in compliance with the Institute of Internal Auditors' ("IIA") mandatory guidance including the "Definition of Internal Auditing," the "Code of Ethics," and applicable standards found in the "International Standards for the Professional Practice of Internal Auditing."
- B. Conduct a periodic risk assessment for the ERS and present the results to the ~~Audit~~ Committee.
- C. Develop a flexible annual Internal Audit Plan using an appropriate risk-based methodology, which considers risks or control concerns identified by management, and submit the plan to the ~~Audit~~ Committee and the Board for review and approval.
- D. Implement the annual Internal Audit Plan, as approved, including, and as appropriate, any special tasks or projects requested by management, the ~~Audit~~ Committee, and the Board.

Ethics

- E. Review the adequacy of the ERS's adopted code of conduct activities, including the process to receive, retain, and treat complaints received on accounting and auditing matters.
- F. Monitor management's process for ensuring compliance with Hawaii Revised Statutes – Chapter 84, *Standards of Conduct* ("State Ethics Code").



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Monitoring & Follow-Up

- G. Evaluate any plans to correct reported conditions for satisfactory improvement of the business process.
- H. Provide adequate follow-up to ensure corrective action is taken and evaluate its effectiveness before recommending closure of an issue.
- I. Monitor and evaluate the effectiveness of the organization's risk management processes.

Reporting

- J. Prepare and issue a written report following the conclusion of each audit and follow-up audit. This report shall include significant findings, recommendations to management, and management's ~~remediation-action~~ plan. A copy of the report will be forwarded to the ~~Audit~~ Committee, ED, Deputy ED, ~~Chief Investment Officer~~, and appropriate members of management.
- K. Inform and advise management and the ~~Audit~~ Committee as to significant deficiencies or other substantive issues noted in the course of its activities.
- L. Provide periodic reports on Internal Audit's progress on implementing the annual Internal Audit Plan, including management's progress on addressing previously reported matters, the impact of resource limitations, and significant interim changes.
- M. On a regular basis, the CAE will meet separately with the ~~Audit~~ Committee to discuss any matters that is deemed necessary by the ~~Audit~~ Committee or Internal Audit.



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Other

- N. Conduct special examinations at the request of management or the ~~Audit~~ Committee.
- O. Perform consulting services, beyond internal auditing assurance services, to assist management in meeting its objectives. Examples may include facilitation, consultation on internal control improvement initiatives, training, and advisory services.
- P. Assist in the investigation of significant suspected fraudulent activities within the organization and notify management and the ~~Audit~~ Committee of the results.
- Q. Coordinate audit efforts with those of the ERS's external auditors and other regulatory agencies.
- R. Evaluate and assess significant merging/consolidating functions and new or changing services, processes, operations, and control processes coincident with their development, implementation, and/or expansion.
- S. Keep the ~~Audit~~ Committee informed of emerging trends and successful practices in internal auditing.
- T. Review this Internal Audit Charter on a periodic basis to ensure the purpose, authority, and responsibilities of Internal Audit continue to be adequate in accomplishing its objectives. Modify as appropriate, and submit to the ~~Audit~~ Committee and ED for review and approval.

Adopted: June 12, 2012

Last Revised: June 9, 2020

Approved by the Board: