

PENNSYLVANIA PUBLIC SCHOOL EMPLOYEES' RETIREMENT SYSTEM INTERNAL AUDIT OFFICE CHARTER

Audit/Compliance Committee Approval Date:

PURPOSE

The purpose of this Internal Audit Charter is to assist the Internal Audit Office (IAO) in fulfilling its mission and fiduciary responsibilities.

MISSION

The mission of IAO is to provide independent, objective assurance, and consulting activity designed to add value and improve the Pennsylvania Public School Employees' Retirement System's (PSERS) operations. It helps PSERS accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control, and governance processes. The IAO:

- Provides a wide range of quality independent internal auditing services for the Audit/Compliance Committee and executive management.
- Performs independent assessments of the systems of risk management, internal controls and operating efficiency, guided by professional standards and using innovative approaches.
- Supports the PSERS' efforts to achieve its objectives through independent assurance and consulting services.
- Routinely monitors compliance with established laws, rules, regulations, policies and procedures.

AUTHORITY

The IAO will function under the governance policies established by the PSERS Board (Board). The Internal Auditor, Assistant Internal Auditors, and the Executive Director shall abide by all aspects of the governance policies as they relate to the duties of the IAO. The IAO charter, and all future amendments to it, is to be approved by the Audit/Compliance Committee through a majority vote. The IAO charter shall be reviewed at least every two years and updated as necessary.

The Internal Auditor is delegated the authority to manage the Internal Audit Office. The Internal Auditor is authorized to allocate resources, set project frequencies, select audit subjects, determine scope of work, and apply the techniques necessary to accomplish the audit objectives. The Internal Auditor is authorized to hire, retain, train, and terminate internal audit staff, when necessary, to achieve the objectives of Internal Audit.

The internal auditors are not authorized to perform operational duties for PSERS and/or its affiliates and contractors.

INDEPENDENCE AND OBJECTIVITY

A. Organizational Independence

The Internal Auditor has a dual reporting requirement as follows:

Functionally - Audit/Compliance Committee of the Board

Administratively - Executive Director

B. Professional Standards of Independence

The Audit/Compliance Committee recognizes that professional independence requires that the internal auditors have knowledge of operations and appropriate expertise in the subject matter that is audited. Internal auditors will have no direct operational responsibility or authority over any of the activities audited. The Internal Auditor shall periodically discuss standards of professional audit independence with the Audit/Compliance Committee.

C. Impairment of Independence

The Internal Auditor shall discuss any potential issues regarding impairment of independence and/or conflicts of interest and their mitigation(s) with the Audit/Compliance Committee as necessary. If objectivity or independence is impaired in fact or appearance, the details of the impairment should be disclosed to the appropriate parties.

D. Objectivity

Internal Audit will remain free from interference regarding matters relating to audit selection, scope, procedures, frequency, or report content in order to maintain an independent and objective mental attitude. Internal auditors must exhibit the highest level of professional objectivity in gathering, evaluating and communicating information about the activity or process being examined. Internal auditors must make a balanced assessment of all relevant circumstances and not be unduly influenced by their own interests or by others in forming judgments.

ACCESS

The Internal Audit Office, as appropriate, shall have full and unrestricted access to all of PSERS' functions, records, documents, files, information systems, personnel, contractors, physical properties, and any other item relevant to the function, process, or department under review. All contracts with vendors shall contain the Commonwealth's standard audit language enabling PSERS's internal auditors, external auditors and specialists to have access to relevant records and information. All of the employees of PSERS are required to assist the IAO in fulfilling their function.

The Internal Auditor shall have free and unrestricted access to the Audit/Compliance Committee and all members of the Board. The Internal Auditor shall also have free and unrestricted access to the Executive Director, management, all personnel, contractors, vendors, employers, members, retirees and beneficiaries of the organization.

Documents and information given to Internal Audit shall be handled in the same prudent and confidential manner as by those employees normally accountable for them. The Internal Auditor shall ensure the internal audit staff is adequately trained in safeguarding and the handling of confidential information.

OBJECTIVES AND SCOPE

A. Assurance Objectives

The objectives of assurance services are to provide formal, independent assurance to the Board, Audit/Compliance Committee and management that the organization's assets are safeguarded, operating efficiencies are enhanced, and compliance is maintained with prescribed laws, rules, regulations, PSERS policies and procedures. Assurance objectives also include independent assessment of the organization's governance, risk awareness and management, and control processes.

B. Consulting and Advisory Services Objectives

The objectives of consulting and advisory services, the nature and scope are agreed with management, are to provide assessments and advice for improving the organization's governance, risk management, and control without the IAO assuming management's responsibility. In particular, the consulting objectives are to provide assessments and advice at the beginning of a project so that risks may be identified, managed and internal controls may be designed appropriately.

C. Scope

The scope of work of the IAO is to determine whether the organization's network of risk management, internal control, and governance processes, as designed and represented by management, is adequate and functioning to ensure:

- Programs are operating within the fiduciary standards and are in compliance with laws, rules, regulations, policies, and procedures.
- Risks, within and outside the organization, are appropriately identified and managed.
- Significant financial, managerial, and operating information is accurate, reliable, and timely.
- Significant legislative or regulatory issues impacting the organization are recognized and addressed appropriately.
- Existing policies and procedures are appropriate and updated.
- Employee actions are in compliance with policies, standards, procedures, and applicable laws.
- Operations, processes, and programs are consistent with established missions, objectives, and goals and whether they are being carried out as planned.
- Resources are acquired economically, used efficiently, and adequately protected.
- Internal controls are in place and are functioning effectively to accomplish business and strategic objectives.

- Quality and continuous improvement are fostered in the organization's control process; which includes ensuring that processes are consistent with industry best practices, using the best public and private examples as benchmarks.
- Information technology controls including information system security controls are in place and are functioning effectively.
- Contractors, including third-party administrators, are meeting the objectives of the contracts while in conformance with applicable laws, rules, regulations, policies, procedures, and best practices.
- Specific operations, processes, or programs are reviewed at the request of management.

RESPONSIBILITIES AND ACCOUNTABILITY

The Internal Auditor is responsible for the following in order to meet the objectives and scope of this Charter:

1. Establish policies for conducting the IAO activities and directing its technical and administrative functions according to the organization's policies and direction which are provided by the Audit/Compliance Committee and professional standards.
2. Submit a flexible, risk-based, annual internal audit plan to the Audit/Compliance Committee for their review and approval and ensure the plan is prepared and executed in accordance with industry best practices and standards. Performance of the audit plan will be reviewed quarterly and reported to the Audit/Compliance Committee. The audit plan may be updated, as necessary.
3. Prepare a budget (included in the Executive Office budget) that is complementary to the implementation of the audit plan.
4. Perform independent analyses of significant operations to evaluate the adequacy and effectiveness of existing systems of internal control.
5. Conduct special projects at the request of the PSERS Board of Trustees, Audit/Compliance Committee, or management, as appropriate, which may include specific reviews of operations, processes, or programs.
6. Issue reports to the Audit/Compliance Committee summarizing results of the audit activities and the status of follow-up related to prior audit recommendations.
7. Routinely monitor compliance with applicable laws, rules, regulations and internal policies and procedures.
8. Lead/participate in the selection of external audit firms. Coordinate/manage the contract(s) with any external audit firms and evaluate their performance. Report to the Audit/Compliance Committee on all activities performed by the external audit firms.
9. Act as the liaison related to audits, investigations, or inquiries of the Auditor General's Office and other external audit groups, as requested.
10. Assist in the investigation of suspected fraudulent activities within the organization, and notify the Audit/Compliance Committee, Executive Director and other Executive Management, as appropriate, of the results.
11. Report any fraudulent, unethical and/or improper activity to the Audit/Compliance

Committee Chair and the other members of the Audit/Compliance Committee.

12. Assess periodically whether the purpose, authority, and responsibility, as defined in this Charter, continue to be adequate to enable the IAO to accomplish its mission, objectives and scope.
13. Implement a quality assurance and improvement program. Obtain an external assessment no less frequently than every five years. Results of the quality assurance and improvement program shall be reported to the Audit/Compliance Committee.
14. Ensure all meetings of the Audit/Compliance Committee are attended by the Internal Auditor and/or staff to review the results of audit activities completed, in process, and planned.
15. Select, train, develop, and/or retain professional audit staff (internal or external) who have the knowledge, skills, experience, expertise, and professional certifications to meet the requirements of this charter.
16. Prepare and maintain the internal audit manual.
17. Keep the Audit/Compliance Committee and management informed of emerging trends and successful practices through training or other forms of communication.

PROFESSIONAL STANDARDS AND ETHICS

The Institute of Internal Auditors' (IIA) Code of Ethics and International Standards for the Professional Practice of Internal Auditing will serve as guidelines for the IAO. As appropriate, the IAO will also comply with the applicable standards outlined within:

- Generally Accepted Auditing Standards (GAAS) of the American Institute of Certified Public Accountants (AICPA)
- Governmental Auditing Standards (GAS) of the Government Accountability Office (GAO)
- GAO Standards for Internal Control in the Federal Government
- IS Auditing Standards, Guidelines, and Procedures and the Code of Ethics of the Information Systems Audit and Control Association (ISACA)

RELATIONSHIP TO THE RISK MANAGEMENT AND INTERNAL CONTROL PROGRAMS

Management is responsible for the operation and implementation of a system of risk management and an internal control system. The IAO's role is to provide an independent and objective assurance on the effectiveness of the risk management system and that the internal control system is operating effectively.