

Audit Report

*Peace Officers' Annuity and Benefit Fund of Georgia
Fiscal Year Ended June 30, 2016*



The photograph on the cover was taken by Lacey Mitchell at Jekyll Island, Georgia.

PEACE OFFICERS' ANNUITY AND BENEFIT FUND OF GEORGIA
(A Component Unit of the State of Georgia)

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SECTION I - FINANCIAL

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DEPARTMENT OF AUDITS AND ACCOUNTS

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GREG S. GRIFFIN
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Independent Auditor's Report

The Honorable Nathan Deal, Governor of Georgia
Members of the General Assembly of the State of Georgia
Members of the Peace Officers' Annuity and Benefit Fund of Georgia
Mr. Robert Carter, Secretary/Treasurer

Report on the Financial Statements

We have audited the accompanying financial statements of the Peace Officers' Annuity and Benefit Fund of Georgia (the Fund), a component unit of the State of Georgia, as of and for the year ended June 30, 2016, and the related notes to the financial statements, which collectively comprise the Fund's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express opinions on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of

expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinions.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the fiduciary net position of the Fund as of June 30, 2016, and the changes in fiduciary net position for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis of Matter

As discussed in Note 2 to the basic financial statements, in 2016 the Fund adopted Governmental Accounting Standards Board (GASB) Statement No. 72, *Fair Value Measurement and Application*. Our opinion is not modified with respect to this matter.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the Schedule of Employers' and Nonemployers' Net Pension Liability, Schedule of Changes in Employers' and Nonemployers' Net Pension Liability, Schedule of Employer and Nonemployer Contributions, and Schedule of Investment Returns on pages 22-25 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Management has omitted the management's discussion and analysis that accounting principles generally accepted in the United States of America require to be presented to supplement the basic financial statements. Such missing information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate

operational, economic, or historical context. Our opinion on the basic financial statements is not affected by this missing information.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated June 16, 2017 on our consideration of the Fund's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Fund's internal control over financial reporting and compliance.

Respectfully submitted,

A handwritten signature in blue ink that reads "Greg S. Griffin". The signature is written in a cursive style with a prominent "G" and "S".

Greg S. Griffin
State Auditor

June 16, 2017

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BASIC FINANCIAL STATEMENTS

PEACE OFFICERS' ANNUITY AND BENEFIT FUND OF GEORGIA
(A Component Unit of the State of Georgia)

Statement of Fiduciary Net Position

June 30, 2016

Assets			
Cash and cash equivalents		\$	31,630,353
Receivables			
Due from brokers for securities sold			14,136,793
Investments - at fair value:			
Obligations:			
Municipal bonds	\$	2,296,038	
U.S. Treasury obligations		14,945,918	
U.S. Agency obligations		40,994,859	
Foreign government obligations		896,612	
Corporate bonds/notes/debentures			
Domestic		41,265,393	
International		4,867,540	
Asset-backed securities		13,069,451	
Mortgage investments		<u>14,087,870</u>	\$ 132,423,681
Equities:			
Mutual funds		388,085,855	
Stocks			
Domestic		159,096,977	
International		2,177,806	
Real estate investment trusts		<u>914,132</u>	<u>550,274,770</u>
Total investments			682,698,451
Capital assets, net			<u>652,622</u>
Total assets			<u>729,118,219</u>
Liabilities			
Due to brokers for securities purchased			40,030,074
Withholdings payable			20,241
Notes payable			<u>46,994</u>
Total liabilities			<u>40,097,309</u>
Net position restricted for pensions		\$	<u><u>689,020,910</u></u>

See accompanying notes to financial statements.

PEACE OFFICERS' ANNUITY AND BENEFIT FUND OF GEORGIA
(A Component Unit of the State of Georgia)

Statement of Changes in Fiduciary Net Position

Year ended June 30, 2016

Additions:		
Contributions:		
Nonemployer	\$	14,712,821
Member		3,526,325
Net investment income:		
Net decrease in fair value of investments	\$	(14,951,372)
Interest, dividends, and other		17,305,276
Less investment expense		<u>(3,190,491)</u>
Miscellaneous		<u>65,501</u>
Total additions		<u>17,468,060</u>
Deductions:		
Benefit payments		30,696,141
Refunds of member contributions		412,644
Administrative expenses, net		<u>873,870</u>
Total deductions		<u>31,982,655</u>
Net decrease in net position		(14,514,595)
Net position restricted for pensions:		
Beginning of year		<u>703,535,505</u>
End of year	\$	<u><u>689,020,910</u></u>

See accompanying notes to financial statements.

PEACE OFFICERS' ANNUITY AND BENEFIT FUND OF GEORGIA
(A Component Unit of the State of Georgia)

Notes to Financial Statements

June 30, 2016

Note 1: Plan Description

The Peace Officers' Annuity and Benefit Fund of Georgia (the Fund) was created in 1950 by the Georgia General Assembly to provide retirement benefits for qualifying peace officers. The Fund administers a cost-sharing, multiple-employer defined benefit pension plan as defined in Governmental Accounting Standards Board (GASB) Statement No. 67, *Financial Reporting for Pension Plans – an amendment of GASB Statement No. 25*.

The Fund is governed by its Board of Commissioners. The Board is comprised of the Governor of the State of Georgia or his designee; an appointee of the Governor other than the Attorney General; the Commissioner of Insurance or his designee; and three active or retired peace officers appointed by the Governor. The Board of Commissioners is ultimately responsible for the administration of the Fund.

Eligibility and Membership

Individuals eligible to apply for membership in the Fund are defined in the *Official Code of Georgia Annotated* (O.C.G.A.) 47-17-1 and generally include: any individual employed by the State of Georgia or any municipality, county, or other political subdivision thereof for the preservation of public order, the protection of life and property or the detection of crime; wardens and correction officers of correctional institutions; full-time parole officers; other individuals employed full-time for the purpose of law enforcement; and full-time employees of the Fund.

As of June 30, 2016, participation in the Fund is as follows:

Inactive members and beneficiaries currently receiving benefits	5,515
Terminated members not yet receiving benefits, vested	1,261
Active plan members	12,938
Total	<u>19,714</u>

Participating Employers and Other Contributing Entities

At June 30, 2016, the active members of the Fund were employed by 609 employers. The Fund also had 1 nonemployer contributing entity, which is the State of Georgia.

Retirement Benefits

The Fund provides retirement as well as disability and death benefits. Title 47 of the O.C.G.A. assigns the authority to establish and amend the provisions of the Fund to the General Assembly. A member is eligible to receive retirement benefits with 30 years of service, regardless of age. A member is also eligible to receive retirement benefits at age 55 with 10 years of service; however, members joining on or after July 1, 2010, must have 15 years of service to be eligible for benefits. A member must have terminated his or her active employment as a peace officer to receive benefits.

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June 30, 2016

The monthly benefit is a single life annuity payable in monthly payments for the life of the member only. The monthly payment amount at June 30, 2016, was \$24.41 per month (plus 1/12 of this amount for each month of any partial year) for each full year of creditable service up to a maximum of 30 years of total service. The Board of Commissioners is authorized to provide for increases effective as of January 1 and July 1 of each year up to 1.5% of the maximum monthly retirement benefit then in effect. Members may elect, as an alternate to the benefit described above, to receive a 100% joint life annuity payable during the life of the member or the member's spouse, or a contingency life annuity with a 50% monthly payment to the surviving spouse. The amount of the benefit for these options is an actuarially reduced portion of the single life annuity benefit described above.

Death and Disability Benefits

Any dues paying member who became a member prior to July 1, 1993, and becomes totally and permanently disabled is entitled to receive disability benefits, the amount of which is dependent upon the date of application for disability benefits.

If a member dies before retirement, the beneficiary is entitled to a lump sum of \$3,500. If a member dies in the line of duty and has a designated beneficiary, that beneficiary is eligible to receive a lump sum benefit of \$5,500 to be reduced (to no less than \$2,500) by the amount of any disability benefits received for the causative injury, as described above. If a member dies after retirement, the death benefit of the designated beneficiary is dependent on the amount of retirement benefits previously received by the deceased member. If the deceased member had received \$1,000 or more, the beneficiary is entitled to receive a lump sum of \$2,500. If the deceased member had received less than \$1,000, the beneficiary is entitled to receive an amount that when added to the amount previously received by the deceased member will total \$3,500.

Terminations

At any time before a member begins drawing retirement benefits, the member may request a refund of 95% of all member contributions paid into the Fund during creditable service. No interest is paid on these withdrawals.

Contributions

The Fund is funded by member and nonemployer contributing entity (Nonemployer) contributions. Contribution provisions are established by statute and may be amended only by the General Assembly.

Member Contributions: Member contribution requirements are set forth in O.C.G.A. 47-17-44 and are not actuarially determined. Each member must contribute \$20 per month, to be paid no later than the tenth day of each month.

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June 30, 2016

Nonemployer Contributions: In accordance with O.C.G.A. 47-17-60, the State of Georgia provides nonemployer contributions to the Fund through the collection of fines and forfeitures. For each criminal and quasi-criminal case involving the violation of State of Georgia laws, county ordinances, or municipal ordinances, courts collect and remit the following amounts:

For fines and bond forfeitures in excess of \$4, but not more than \$25	\$3
For fines and bond forfeitures in excess of \$25, but not more than \$50	\$4
For fines and bond forfeitures in excess of \$50, but not more than \$100	\$5
For fines and bond forfeitures in excess of \$100	5%

The fines and forfeitures are considered employer contributions for the purpose of determining whether the Fund has met minimum funding requirements specified in O.C.G.A. 47-20-10. This statute also prohibits any action to grant a benefit increase until such time as the minimum annual contribution requirements meet or exceed legislative requirements. The actuarial valuation as of June 30, 2016, calculated the minimum employer contribution for the fiscal year ended June 30, 2016, as \$18,082,091. The fines and forfeitures revenue of \$14,712,821 for the fiscal year ended June 30, 2016, did not meet the minimum required fund contribution.

Administrative Expenses

Administrative expenses are generally funded from current member and nonmember contributions. Investment earnings may be utilized to fund any expenses in excess of contributions.

Note 2: Summary of Significant Accounting Policies and Plan Asset Matters

Basis of Accounting

The Fund's financial statements are prepared on the accrual basis of accounting, except for the collection of contributions, which are recognized when collected from the members and the courts. Any accrual of these contributions would be immaterial to the Fund's financial statements. Retirement and refund payments are recognized as deductions when due and payable.

Reporting Entity

The Fund is a component unit of the State of Georgia; however, it is accountable for its own fiscal matters and presentation of its separate financial statements. The Fund has considered potential component units under GASB Statements No. 61, *The Financial Reporting Entity's Omnibus – an amendment of GASB Statements No. 14 and No. 34*, and GASB Statement No. 39, *Determining Whether Certain Organizations are Component Units*, and determined there were no component units of the Fund.

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June 30, 2016

Cash and Cash Equivalents

Cash and cash equivalents, reported at cost, include cash on deposit at banks, cash on deposit with the investment custodian earning a credit to offset fees, and short-term highly liquid financial securities with original maturities of three months or less from the date of acquisition.

Investments

Investments are reported at fair value. Equity securities traded on a national or international exchange are valued at the last reported sales price. Fixed income securities are valued based primarily on quoted market prices provided by independent pricing sources. Global foreign exchange holdings are translated using a third party vendor. Investment income is recognized as earned by the Fund. There are no investments in, loans to, or leases with parties related to the Fund.

The Fund utilizes various investment instruments. Investment securities, in general, are exposed to various risks, such as interest rate, credit, foreign currency, and overall market volatility. Due to the level of risk associated with certain investment securities, it is reasonably possible that changes in the values of investment securities will occur in the near term and that such changes could materially affect the amounts reported in the financial statements.

The Fund maintains an investment policy that may be amended by its Board of Commissioners both upon its own initiative and upon consideration of the advice and recommendations of its investment managers. There were no significant changes in the investment policy for the Fund during the fiscal year.

The Fund's policy in regard to the allocation of invested assets is established on a cost basis in compliance with State law. Plan assets are managed on a total return basis with a long-term objective of achieving and maintaining a fully funded status for the benefits provided through the pension plan. The following was the Fund's adopted asset allocation policy as of June 30, 2016:

<u>Asset Class</u>	<u>Target Allocation</u>
Fixed income	20% - 40%
Equities	30% - 75%
Cash and cash equivalents	0% - 10%
Total	100%

Approximately 8.2% of the investments held in trust for pension benefits are invested in debt securities of the U.S. government and its instrumentalities, of which 2.2% are U.S. government debt securities and 6.0% are debt securities of the U.S. government instrumentalities. The Fund has no investments in any one organization, other than those issued by the U.S. government and its instrumentalities, that represent 5% or more of the Fund's net position restricted for pensions.

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June 30, 2016

For the year ended June 30, 2016, the annual money-weighted rate of return on pension plan investments, net of pension plan investment expense, was 0.08%. The money-weighted rate of return expresses investment performance, net of investment expense, adjusted for the changing amounts actually invested.

Use of Estimates

The preparation of financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of fiduciary net position and changes therein. Actual results could differ from those estimates.

New Accounting Pronouncements

During fiscal year 2016, the Fund adopted the provisions of GASB Statement No. 72, *Fair Value Measurement and Application*. This Statement addresses accounting and financial reporting issues related to fair value measurements and requires disclosures to be made about fair value measurements, the level of fair value hierarchy and valuation techniques. See note 3 for disclosures related to GASB Statement No. 72.

During fiscal year 2016, the Fund adopted the provisions of GASB Statement No. 73, *Accounting and Financial Reporting for Pensions and Related Assets that are Not Within the Scope of GASB Statement 68, and Amendments to Certain Provisions of GASB Statements 67 and 68*. The objective is to improve the usefulness of information about pensions included in external financial reports for making decisions and assessing accountability. The implementation of GASB Statement No. 73 did not impact the recorded amounts in the financial statements. However, this Statement did provide additional clarification on the reporting requirements of the Fund's required supplementary information.

During fiscal year 2016, the Fund adopted the provisions of GASB Statement No. 76, *The Hierarchy of Generally Accepted Accounting Principles for State and Local Governments* which supersedes GASB Statement No. 55. The objective of this Statement is to identify the hierarchy of generally accepted accounting principles (GAAP) used to prepare financial statements for the purpose of improving the usefulness and comparability of those statements among governments. The implementation of GASB Statement No. 76 did not impact the recorded amounts in the financial statements.

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Notes to Financial Statements

June 30, 2016

Note 3: Investment Program

The Fund maintains sufficient cash to meet its immediate liquidity needs. Cash not immediately needed is invested as directed by the investment policy of the Fund. All investments are held by agent custodial banks in the name of the Fund. State statutes and the Fund's investment policy authorize the Fund to invest in a variety of short-term and long-term securities.

Cash and Cash Equivalents

The Fund had cash on hand of \$200 at June 30, 2016.

The carrying amount of the Fund's operating account totaled \$230,413 at June 30, 2016, with an actual bank balance of \$1,047,742. The Fund's cash balance of \$250,000 is fully insured through the Federal Deposit Insurance Corporation, an independent agency of the U.S. Government. The remaining balance of \$797,742 is exposed to risk and is collateralized with securities held by the financial institution, or by its trust department of agent, not in the entity's name.

The carrying amount of the Fund's cash balances maintained within an investment account is \$310,978, at June 30, 2016. This balance includes \$4,317, which is fully insured through the Securities Investors Protection Corporation, an independent agency of the U.S. Government. This balance also includes \$306,661, which is held in British Pounds and is uncollateralized.

The Fund's investment policy authorizes investment in short-term highly liquid financial securities. At June 30, 2016, the Fund held \$25,954 in money market mutual funds and \$31,062,808 in short term investment funds.

Investments

Fixed income investments are maintained in municipal bonds, U.S. Treasury obligations, obligations unconditionally guaranteed by agencies of the U.S. Government, obligations of foreign governments, investment-grade corporate bonds, asset-backed securities, and mortgage-related securities.

Equity investments are maintained in mutual funds, domestic equities, international equities, and real estate investment trusts. Domestic equities are those securities considered by the O.C.G.A. to be domiciled in the United States. International equities are not considered by the O.C.G.A. to be domiciled in the United States.

The equity portfolio is managed by the Fund in conjunction with independent advisors. Buy/sell decisions are based on securities meeting rating criteria established by the investment policy of the Fund. Equity trades are approved and executed by the independent advisors. Common stocks eligible for investment must meet the Objectives and Policies of the Fund's investment policy. State law limits the total investment in equity securities to 75% of the total invested assets calculated on a historical cost basis.

PEACE OFFICERS' ANNUITY AND BENEFIT FUND OF GEORGIA
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Notes to Financial Statements

June 30, 2016

Interest Rate Risk

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. The Fund does not have a formal policy for managing interest rate risk. The following table provides information about the Fund's interest rate risk:

Investment type	Total Fair Value	Maturity Period				More than 10 Years
		Less than 3 Months	4 - 12 Months	1 - 5 Years	6 - 10 Years	
Cash and Cash Equivalents Subject to Interest Rate Risk:						
Money market mutual funds	\$ 25,954	25,954				
Short term investment funds	31,062,808	31,062,808				
Total Cash and Cash Equivalents Subject to Interest Rate Risk:	\$ 31,088,762	31,088,762				
Debt Securities Subject to Interest Rate Risk:						
Municipal bonds	\$ 2,296,038		122,942	260,573		1,912,523
U.S. Treasury obligations	14,945,918			6,276,935	3,711,884	4,957,099
U.S. Agency obligations	40,994,859		15	64,972	9,140	40,920,732
Foreign government obligations	896,612				548,182	348,430
Corporate debt						
Domestic	41,265,393	377,918	1,425,031	12,462,853	14,531,942	12,467,649
International	4,867,540			2,561,944	1,668,185	637,411
Asset-backed securities	13,069,451			2,694,117	6,672,404	3,702,930
Mortgage-backed securities	14,087,870			376,592	1,949,336	11,761,942
Total Debt Securities Subject to Interest Rate Risk:	\$ 132,423,681	377,918	1,547,988	24,697,986	29,091,073	76,708,716

Credit Risk

Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations to the Fund. State law limits investments to investment grade securities. The Fund's investment policy requires that the bond portfolio be of high quality and chosen primarily with respect to the safety and liquidity of the investment and only secondarily by the yield available. The Fund's investment policy also requires that purchases of bonds be restricted to bonds rated as investment grade or higher quality as defined by a nationally recognized rating agency. Obligations of the U.S. Government or obligations explicitly guaranteed by the U.S. Government are not considered to have credit risk and do not require disclosure of credit quality. The quality ratings of investments in fixed income securities at June 30, 2016, as described by Standard & Poor's, which is a nationally recognized statistical rating organization, are shown in the following table:

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Notes to Financial Statements

June 30, 2016

<u>Investment Type</u>	<u>Total Fair Value</u>	<u>AAA</u>	<u>AA</u>	<u>A</u>	<u>BBB</u>	<u>Unrated</u>
Cash and Cash Equivalents Subject to Credit Risk:						
Money market mutual funds	\$ 25,954	25,954				
Short term investment funds	<u>31,062,808</u>					<u>31,062,808</u>
Total Cash and Cash Equivalents Subject to Credit Risk	\$ <u>31,088,762</u>	<u>25,954</u>				<u>31,062,808</u>
Debt Securities Subject to Credit Risk:						
Municipal bonds	\$ 2,296,038		1,735,820	384,417	175,801	
Foreign government obligations	896,612			548,182	348,430	
Corporate debt						
Domestic	41,265,393	684,065	2,187,559	12,854,975	25,225,576	313,218
International	4,867,540			1,250,325	3,617,215	
Asset-backed securities	13,069,451	8,081,707	689,177	553,922		3,744,645
Mortgage-backed securities	<u>14,087,870</u>	<u>3,582,575</u>	<u>1,516,134</u>	<u>507,931</u>		<u>8,481,230</u>
Total Debt Securities Subject to Credit Risk	\$ 76,482,904	<u>12,348,347</u>	<u>6,128,690</u>	<u>16,099,752</u>	<u>29,367,022</u>	<u>12,539,093</u>
Debt Securities Not Subject to Credit Risk:						
U.S. Treasury obligations	14,945,918					
U.S. Agency obligations	<u>40,994,859</u>					
Total Debt Securities	\$ <u>132,423,681</u>					

Fair Value Measurement

The Fund categorizes its fair value measurements within the fair value hierarchy established by generally accepted accounting principles. The hierarchy is based on the inputs used in valuation and gives the highest priority to unadjusted quoted prices in active markets and requires that observable inputs be used in the valuations when available. The disclosure of fair value estimates in the hierarchy is based on whether the significant inputs into the valuation are observable. In determining the level of the hierarchy in which the estimate is disclosed, the highest level, Level 1, is given to unadjusted quoted prices in active markets and the lowest level, Level 3, to unobservable inputs. These guidelines recognize a three-tiered hierarchy, as follows:

Level 1 – Valuations based on unadjusted quoted prices for identical instruments in active markets.

Level 2 – Valuations based on quoted prices for similar instruments in active markets; quoted prices for identical or similar instruments in markets that are not active; and model-derived valuations in which all significant inputs are observable.

Level 3 - Valuations based on inputs that are unobservable and significant to the overall fair value measurement.

In instances where inputs used to measure fair value fall into different levels in the fair value hierarchy, fair value measurements in their entirety are categorized based on the lowest level input that is significant to the valuation. The Fund's assessment of the significance of particular inputs

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Notes to Financial Statements

June 30, 2016

to these fair value measurements requires judgement and considers factors specific to each investment. The following table shows the fair value leveling of the Fund's investments.

Investments by fair value level	Total	Fair value measures using		
		Quoted prices in active markets for identical assets Level 1	Significant other observable inputs Level 2	Significant unobservable inputs Level 3
Cash and Cash Equivalents:				
Money market mutual funds	\$ 25,954		25,954	
Short term investment funds	31,062,808		31,062,808	
Total Cash and Cash Equivalents by fair value level	\$ 31,088,762		31,088,762	
Debt Securities:				
Municipal bonds	\$ 2,296,038		2,296,038	
U.S. Treasury obligations	14,945,918		14,945,918	
U.S. Agency obligations	40,994,859		40,994,859	
Foreign government obligations	896,612		896,612	
Corporate debt				
Domestic	41,265,393		41,265,393	
International	4,867,540		4,867,540	
Asset-backed securities	13,069,451		13,069,451	
Mortgage-backed securities	14,087,870		14,087,870	
Equities:				
Mutual funds	388,085,855	147,329,447	240,756,408	
Stocks				
Domestic	159,096,977	159,096,977		
International	2,177,806	2,177,806		
Real estate investment trusts	914,132	914,132		
Total Investments by fair value level	\$ 682,698,451	309,518,362	373,180,089	

Equity securities classified in Level 1 are valued using prices quoted in active markets for those securities.

Debt securities classified in Level 1 are valued using prices quoted in active markets. Debt securities classified in Level 2 are valued using either a bid evaluation or a matrix pricing technique. Bid evaluations may include market quotations, yields, maturities, call features and ratings. Matrix pricing is used to value securities based on the securities' relationship to benchmark quoted prices. These securities have nonproprietary information that was readily available to market participants, from multiple independent sources, which are known to be actively involved in the market.

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June 30, 2016

Mutual funds classified in Level 1 are valued using prices quoted in active markets for those investment types. Mutual funds classified in Level 2 are valued using observable underlying inputs that are market corroborated.

The Fund did not have any Net Asset Value (NAV) investments at June 30, 2016.

Foreign Currency Risk

Foreign currency risk is the risk that changes in exchange rates will adversely impact the fair value of an investment. The Fund's currency risk exposures, or exchange rate risks, primarily reside within the Fund's international cash and equity investment holdings. As of June 30, 2016, the Fund's exposure to foreign currency risk derives from its cash and investments denominated in British Pounds. The market value of these holdings as of June 30, 2016 totaled \$21,594,486. The Fund does not have a formal policy for managing foreign currency risk.

Concentration of Credit Risk

Concentration of credit risk is the risk of loss that may be attributed to the magnitude of the Fund's investment in a single issue. On June 30, 2016, the Fund did not have debt investments in any one organization, other than those issued or guaranteed by the U.S. Government or its agencies, which represented greater than 5% of plan's total investments.

The Fund's investment policy requires that fixed income investments in securities of a single issuer, with the exception of the U.S. Government and its agencies, may not exceed 5% of the fixed income portfolio's cost basis. On June 30, 2016, the Fund did not have fixed income investments in a single issuer, other than those issued or guaranteed by the U.S. Government or its agencies, which exceeded 5% of fixed income portfolio's cost basis.

Note 4: Net Pension Liability of Employers and Nonemployers

The components of the collective net pension liability of the participating employers and nonemployers at June 30, 2016, were as follows:

Total pension liability	\$ 747,483,662
Plan fiduciary net position	<u>(689,020,910)</u>
Net pension liability	<u>\$ 58,462,752</u>

Plan fiduciary net position as a percentage of total pension liability 92.18%

Actuarial assumptions

The total pension liability was determined by an actuarial valuation as of June 30, 2015, with update procedures used to roll forward the total pension liability to June 30, 2016. The roll forward

PEACE OFFICERS' ANNUITY AND BENEFIT FUND OF GEORGIA
(A Component Unit of the State of Georgia)

Notes to Financial Statements

June 30, 2016

calculation adds the normal cost (also called service costs), subtracts the actual benefit payments and refunds for the plan year, and then applies the discount rate for the year. This actuarial valuation used the following actuarial assumptions, applied to all periods included in the measurement:

Inflation	3.0%
Salary increases	N/A
Investment rate of return	7.00%, net of pension plan investment expense, including inflation

Mortality rates were based on the RP 2014 Healthy Mortality Table with blue collar adjustment and generational mortality projection using Scale MP 2014 for healthy lives and the RP 2014 Disabled Retiree Mortality Table with generational mortality projection using Scale MP 2014 for disabled lives.

The long-term expected rate of return on pension plan investments was calculated by the Fund's investment manager as 6.66% using a Monte Carlo simulation in which best-estimate ranges of expected future real rates of return (expected nominal returns, net of pension plan investment expense and the assumed rate of inflation) are developed for each major asset class. These ranges are combined to produce the long-term expected rate of return by weighting the expected future real rates of return by the target asset allocation percentage. The Fund's administrator determined that 7.00% was a reasonable assumption for the long-term rate of return on plan assets based on the calculation by the Fund's investment manager. The target asset allocation and best estimates of arithmetic real rates of return for each major asset class are summarized in the following table:

<u>Asset class</u>	<u>Target allocation</u>	<u>Long-term expected real rate of return*</u>
Domestic fixed income	20 %	2.7 %
International fixed income	5	4.0
Domestic large equities	35	7.5
Domestic mid equities	8	8.4
Domestic small equities	7	8.6
Global equities	10	8.2
International equities	10	8.8
Commodities	5	6.4
Total	<u>100 %</u>	

* Rates shown are net of the 2.50% assumed rate of inflation.

PEACE OFFICERS' ANNUITY AND BENEFIT FUND OF GEORGIA
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Notes to Financial Statements

June 30, 2016

Discount Rate

The discount rate used to measure the total pension liability was 7.00%, based on the expected long-term rate of return on pension investments of 6.66%, but assuming an annual rate of inflation of 3.00%. The projection of cash flows used to determine the discount rate assumes revenues will remain level. Based on those assumptions, the pension plan's fiduciary net position was projected to be available to make all projected future benefit payments of current plan members. Therefore, the long-term expected rate of return on pension plan investments was applied to all periods of projected benefit payments to determine the total pension liability.

Sensitivity of the net pension liability to changes in the discount rate

The following table presents the net pension liability of the Fund, calculated using the discount rate of 7.00%, as well as what the Fund's net pension liability would be if it were calculated using a discount rate that is 1-percentage-point lower (6.00%) or 1-percentage-point higher (8.00%) than the current rate:

	1% Decrease (6.00%)	Current discount rate (7.00%)	1% Increase (8.00%)
	<u> </u>	<u> </u>	<u> </u>
Employer's and nonemployers' net pension liability (asset)	\$ <u>150,657,357</u>	<u>58,462,752</u>	<u>(18,137,966)</u>

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REQUIRED SUPPLEMENTARY INFORMATION (UNAUDITED)

PEACE OFFICERS' ANNUITY AND BENEFIT FUND OF GEORGIA
(A Component Unit of the State of Georgia)

Required Supplementary Information

Schedule of Employers' and Nonemployers' Net Pension Liability

For the year ended June 30

(Unaudited)

	2016	2015	2014
Total pension liability	\$ 747,483,662	720,212,697	674,724,912
Plan fiduciary net position	689,020,910	703,535,505	698,888,740
Employers' and nonemployers' net pension liability (asset)	\$ 58,462,752	16,677,192	(24,163,828)
Plan fiduciary net position as a percentage of the total pension liability	92.18%	97.68%	103.58%
Covered-employee payroll	N/A	N/A	N/A
Employers' and nonemployers' net pension liability as a percentage of covered-employee payroll	N/A	N/A	N/A

Note: Schedule is intended to show information for 10 years. Additional years will be displayed as they become available.

See accompanying notes to required supplementary information and accompanying independent auditor's report.

PEACE OFFICERS' ANNUITY AND BENEFIT FUND OF GEORGIA
(A Component Unit of the State of Georgia)

Required Supplementary Information

Schedule of Changes in Employers' and Nonemployers' Net Pension Liability

For the year ended June 30

(Unaudited)

	2016	2015	2014
Total pension liability:			
Service cost	\$ 12,825,926	13,084,414	17,889,962
Interest	50,242,311	47,138,110	43,876,585
Changes of benefit terms	0	0	0
Differences between expected and actual experience	(4,688,487)	0	0
Changes of assumptions	0	14,576,503	0
Benefit payments	(30,696,141)	(28,878,531)	(27,263,352)
Refunds of member contributions	(412,644)	(432,711)	(436,639)
Net change in total pension liability	27,270,965	45,487,785	34,066,556
Total pension liability - beginning	720,212,697	674,724,912	640,658,356
Total pension liability - ending (a)	747,483,662	720,212,697	674,724,912
 Plan fiduciary net position:			
Contributions - nonemployer	14,712,821	15,340,930	15,342,296
Contributions - member	3,526,325	3,537,427	3,531,388
Net investment income	(836,587)	15,770,563	103,599,538
Miscellaneous	65,501	64,546	90,040
Benefit payments	(30,696,141)	(28,878,531)	(27,263,352)
Refund of member contributions	(412,644)	(432,711)	(436,639)
Administrative expense	(873,870)	(755,459)	(730,002)
Net change in plan fiduciary net position	(14,514,595)	4,646,765	94,133,269
Plan fiduciary net position - beginning	703,535,505	698,888,740	604,755,471
Plan fiduciary net position - ending (b)	689,020,910	703,535,505	698,888,740
Net pension liability (asset) - ending (a) - (b)	\$ 58,462,752	16,677,192	(24,163,828)

Note: Schedule is intended to show information for 10 years. Additional years will be displayed as they become available.

See accompanying notes to required supplementary information and accompanying independent auditor's report.

PEACE OFFICERS' ANNUITY AND BENEFIT FUND OF GEORGIA
(A Component Unit of the State of Georgia)

Required Supplementary Information
Schedule of Employer and Nonemployer Contributions

For the year ended June 30
(Unaudited)

	2016	2015	2014	2013	2012	2011	2010	2009	2008	2007
Actuarially determined employer and nonemployer contribution	\$ 18,082,091	17,814,948	22,340,743	22,343,059	19,760,211	19,760,211	14,034,429	14,034,429	12,936,344	12,936,344
Contributions in relation to the actuarially determined contribution	14,712,821	15,340,930	15,342,296	15,471,981	16,256,050	16,185,126	17,281,914	16,144,705	17,595,669	17,334,701
Contribution deficiency (excess)	\$ 3,369,270	2,474,018	6,998,447	6,871,078	3,504,161	3,575,085	(3,247,485)	(2,109,276)	(4,659,325)	(4,398,357)
Covered-employee payroll	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
Contributions as a percentage of covered-employee payroll	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A

See accompanying notes to required supplementary information and accompanying independent auditor's report.

PEACE OFFICERS' ANNUITY AND BENEFIT FUND OF GEORGIA
(A Component Unit of the State of Georgia)

Required Supplementary Information

Schedule of Investment Returns

For the year ended June 30

(Unaudited)

	<u>2016</u>	<u>2015</u>	<u>2014</u>
Annual money-weighted rate of return, net of investment expense	0.08%	2.53%	18.49%

Note: Schedule is intended to show information for 10 years. Additional years will be displayed as they become available.

See accompanying notes to required supplementary information and accompanying independent auditor's report.

PEACE OFFICERS' ANNUITY AND BENEFIT FUND OF GEORGIA
(A Component Unit of the State of Georgia)

Notes to Required Supplementary Information

June 30, 2016

(Unaudited)

Note 1: Schedule of Employers' and Nonemployers' Net Pension Liability

The components of the net pension liability as of the fiscal year end and the fiduciary net position as a percentage of the total pension liability as of that date are presented in this schedule. This trend information will be accumulated to display a ten year presentation.

Note 2: Schedule of Changes in Employers' and Nonemployers' Net Pension Liability

Net pension liability which is measured as the total pension liability less the amount of the fiduciary net position is presented in this schedule. This trend information will be accumulated to display a ten year presentation.

Note 3: Schedule of Employer and Nonemployer Contributions

The schedule presents the required contributions and the percentage of required contributions actually contributed.

Note 4: Schedule of Investment Returns

The schedule presents historical trend information about the annual money-weighted rate of return on plan investments, net of plan investment expense. This trend information will be accumulated to display a ten year presentation.

Note 5: Actuarial Methods and Assumptions

Benefit changes: None

Changes of assumptions: For fiscal year 2015, the mortality table was changed to the RP 2014 Healthy Mortality Table with blue collar adjustment and generational mortality projection using Scale MP 2014 for healthy lives and to RP 2014 Disabled Retiree Mortality Table with generational mortality projection using Scale MP 2014 for disabled lives.

Methods and assumptions used in calculations of actuarially determined contributions: For fiscal years ending before June 30, 2015, the actuarially determined contribution in the schedule of employer and nonemployer contributions are calculated as of June 30, two years prior to the end of the fiscal year in which contributions are reported. Beginning with the June 30, 2015 fiscal year, the actuarially determined contribution is calculated as of June 30 of the prior fiscal year.

PEACE OFFICERS' ANNUITY AND BENEFIT FUND OF GEORGIA
(A Component Unit of the State of Georgia)

Notes to Required Supplementary Information

June 30, 2016

(Unaudited)

The following actuarial methods and assumptions were used to determine the most recently calculated actuarially determined contribution reported in the Schedule of Employer and Nonemployer Contributions:

Valuation date	June 30, 2015
Actuarial cost method	Entry age normal
Amortization method	Level dollar, open
Remaining amortization period	30 years
Asset valuation method	Actuarial value
Inflation rate	3.0%
Salary increases	N/A
Investment rate of return	7.0%, net of pension plan investment expense, including inflation

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**SECTION II – REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING
AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF
FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH *GOVERNMENT
AUDITING STANDARDS***

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DEPARTMENT OF AUDITS AND ACCOUNTS

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GREG S. GRIFFIN
STATE AUDITOR
(404) 656-2174

Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with *Government Auditing Standards*

Independent Auditor's Report

The Honorable Nathan Deal, Governor of Georgia
Members of the General Assembly of the State of Georgia
Members of the Peace Officers' Annuity and Benefit Fund of Georgia
Mr. Robert Carter, Secretary/Treasurer

We have audited, in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the Peace Officers' Annuity and Benefit Fund of Georgia (the Fund), a component unit of the State of Georgia, which include the statement of fiduciary net position as of June 30, 2016, the related statement of changes in fiduciary net position for the year then ended, and the related notes to the financial statements, which collectively comprise the Fund's basic financial statements, and have issued our report thereon dated June 16, 2017.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered the Fund's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Fund's internal control. Accordingly, we do not express an opinion on the effectiveness of the Fund's internal control.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. *A material weakness* is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. *A significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. We did identify a certain deficiency in internal control, described in the accompanying *Schedule of Findings and Questioned Costs* as FS-947-16-01 that we consider to be a significant deficiency.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Fund's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

Peace Officers' Annuity and Benefit Fund of Georgia's Response to Findings

The Fund's response to the findings identified in our audit are described in the accompanying *Schedule of Findings and Questioned Costs*. The Fund's response was not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on it.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Respectfully submitted,



Greg S. Griffin
State Auditor

June 16, 2017

SECTION III – SCHEDULE OF FINDINGS AND QUESTIONED COSTS

FS-947-16-01 Improve Documentation and Performance of Controls

Internal Control Impact: Significant Deficiency
Compliance Impact: Nonmaterial Noncompliance

The Peace Officers' Annuity and Benefit Fund of Georgia (POAB) should comply with the statewide guidance for documenting its internal control framework and improve performance of its change management and logical access controls.

Background Information:

The State of Georgia has adopted the standards presented in the U.S. Government Accountability Office's (GAO) Green Book that provide an overall framework for establishing and maintaining an effective system of internal control. The State Accounting Office (SAO) has issued guidance to state organizations for implementing the Green Book framework.

During our fiscal year 2015 audit, we noted that POAB has an informal internal control framework in place over financial reporting and compliance processes. The POAB personnel could generally describe control policies and procedures; however, controls were not consistently documented, and they were not designed based on a thorough analysis of business objectives and risks related to operational, financial reporting, and compliance requirements. During our fiscal year 2016 audit, we followed up on POAB's efforts to update, document, and monitor its system of internal control.

Criteria:

The POAB management is responsible for establishing and maintaining a system of internal control over financial reporting and compliance processes, including relevant information systems, that provides reasonable assurance of accurate financial reporting and compliance with applicable laws and regulations as well as statewide policies and procedures. The statewide internal control guidance issued by SAO required POAB to update and document the Control Environment component of its internal control framework and to submit that documentation to SAO.

Condition:

The POAB did not comply with SAO's established timeline for updating and documenting the Control Environment component of its internal control framework and submitting that documentation to SAO. The Control Environment documentation was due on April 15, 2016; the POAB submitted its documentation to SAO on May 12, 2017.

We also noted POAB has not yet updated and documented the Risk Assessment and Control Activities components of its internal control framework. The guidance SAO issued for these components included reporting and recording templates, which are intended to provide documentation of the organization's internal control system in accordance with the statewide guidance. Documentation for the reporting template was due to SAO by October 31, 2016, and the recording template was due by February 28, 2017.

In addition, we noted inconsistent compliance with existing controls related to change management and logical access related to POAB's information systems.

Cause:

The POAB has a small staff and did not assign sufficient resources to fully follow SAO's guidance and timeline for implementing the Green Book's internal control framework standards. In addition, the POAB has not allocated sufficient resources to monitor compliance with existing information system controls.

Effect or Potential Effect:

Without adequately documenting and implementing each component of an internal control system in accordance with the statewide guidance, management cannot ensure POAB's internal control framework will comply with the Green Book standards or that a material misstatement of the POAB's financial information would be prevented or detected and corrected in a timely manner. This may also impede management's ability to gain reasonable assurance that POAB will achieve its operational, financial reporting, and compliance objectives.

Recommendation:

The POAB should review the resources available within its existing staff to determine whether additional internal resources could be assigned to implementing the Green Book's internal control framework standards and monitoring performance of the existing information system controls. If sufficient internal resources are not available, the POAB should consider obtaining additional resources on either a permanent or temporary basis.

When implementing its comprehensive internal control structure, an organization such as POAB should:

- Establish appropriate Tone at the Top; have clear, documented policies and procedures outlining those charged with governance and authority; and set responsibility and expectations for a system of internal control throughout the organization.
- Conduct risk assessments to determine risks that would prohibit the organization from achieving its operational, reporting, and compliance objectives. The risk assessment framework should:
 - Establish objectives related to operational, reporting, and compliance requirements across the organization.
 - Assess the suitability of the objectives and analyze risks (including fraud) to achieving each objective.
 - Consider possible changes from internal and external environments and their impact.
- Define control activities to manage the objectives and mitigate risks identified during the risk assessment process. Control activities should be:
 - Linked to each objective and risk.
 - Established through documented policies and procedures.
 - Performed at every level of the organization and applied at the appropriate stages within the business process and IT environment.
 - Assessed periodically to determine their overall effectiveness in mitigating risks to achieving objectives.

- Identify information needed to assess the internal control environment. This information should be collected and communicated both internally and externally to support the effectiveness of internal controls.
- Put on-going monitoring and evaluation processes in place to determine whether components of internal control are present and functioning effectively.

A robust system of internal control over financial reporting and compliance processes, including relevant information systems, is critical to gain assurance in meeting operational, reporting, and compliance requirements. It also serves as a way to enhance control activities, have safeguards in place to prevent or detect fraud and abuse, and gain efficiencies in operations.

Views of Responsible Officials:

Management concurs with the finding.

Corrective Action Plan:

Management has started to review the U.S. Government Accountability Office's Green Book as well as reviewing the guidance issued by SAO. Management is presently working on the Risk Assessment and Control Activities templates from SAO. Management is in the process of formalizing policies and procedures for better internal control.

Management is concurrently developing and revising policies and procedures as it relates to the internal control matters for relevant information systems as it relates to change management and logical access. Management is developing logical access policies to ensure proper documentation is in place, to ensure parameters are appropriately set and updated, and to ensure proper deprovisioning documentation. Management is reviewing change management policies to ensure workflow changes are authorized, tested, and approved.

Estimated Completion Date:

December 30, 2017

Contact Person: Robert W. Carter / Kimberly Avery

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