

AGENDA

A REGULAR MEETING OF THE AUDIT COMMITTEE

AND/OR BOARD OF RETIREMENT AND/OR BOARD OF INVESTMENTS*

LOS ANGELES COUNTY EMPLOYEES RETIREMENT ASSOCIATION

300 N. LAKE AVENUE, SUITE 810, PASADENA, CALIFORNIA 91101

8:00 A.M., THURSDAY, NOVEMBER 30, 2017

*The Committee may take action on any item on the agenda
and agenda items may be taken out of order.*

2017 COMMITTEE MEMBERS

Joseph Kelly – *Chair*

Michael S. Schneider – *Vice Chair*

Vivian Gray – *Secretary*

David Green

Shawn R. Kehoe

AUDIT COMMITTEE CONSULTANT

Rick Wentzel

I. CALL TO ORDER

II. PLEDGE OF ALLEGIANCE

III. APPROVAL OF MINUTES

- A. Approval of the Minutes of the Regular Audit Committee Meeting of August 16, 2017

IV. REPORT ON CLOSED SESSION ITEMS

V. PUBLIC COMMENT

VI. NON-CONSENT ITEMS

- A. Recommendation that the Audit Committee approve the proposed changes to the Audit Committee Charter as submitted by Richard Bendall, *Chief Audit Executive*, Leisha Collins, *Principal Internal Auditor*, and Christina Logan, *Senior Internal Auditor*.
(Memo dated: November 15, 2017)
- B. Recommendation that the Audit Committee approve the proposed changes to the Internal Audit Charter as submitted by Richard Bendall, *Chief Audit Executive*, and Leisha Collins, *Principal Internal Auditor*, and Christina Logan, *Senior Internal Auditor*.
(Memo dated: November 15, 2017)
- C. Recommendation, as submitted by Richard Bendall, Chief Audit Executive, that the Audit Committee review and discuss the following engagement reports to take the following action(s):
1. Accept and file report and/or,
 2. Instruct staff to forward report to Boards or Committees and/or,
 3. Provide further instruction to staff.
(Memo dated: November 15, 2017)
 - a. Los Angeles County Rehired Retirees Audit
Nathan Amick, Internal Auditor
(Report issued: October 31, 2017)
 - b. Member Death Verification Process
Gabriel Tafoya, Senior Internal Auditor
(Report issued: October 31, 2017)

VII. REPORTS

- A. Plante Moran Presentation of the Reports – *June 30, 2017*
Agenda and Reports from Plante Moran et. al.
 - *Report on Internal Control Over Financial Reporting and on Compliance*
 - *Required Communications to the Audit Committee*
Michelle Watterworth, CPA, Managing Partner
Amanda Cronk, CPA, Senior Audit Manager
(Memo dated: October 12, 2017)

- B. Pensionable Pay Code Testing
Quoc Nguyen, Principle Internal Auditor
Gabriel Tafoya, Senior Internal Auditor
(Presentation dated: November 30, 2017)

- C. Internal Audit Staffing Report
Richard Bendall, Chief Internal Auditor
(Verbal presentation only)

- D. Audit Plan Status Report
Richard Bendall, Chief Audit Executive
(Report dated: October 31, 2017)

- E. Recommendation Follow-Up Report
Quoc Nguyen, Principal Internal Auditor
Gabriel Tafoya, Senior Internal Auditor
(Memo dated: October 31, 2017)

- F. Privacy Audit Recommendation Follow-Up
Richard Bendall, Chief Audit Executive
Darla Vidger, Internal Auditor
(Memo dated: November 14, 2017)

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G. **Attorney-Client Privilege/Confidential Memo**
Human Resources Compliance Audit [by Liebert Cassidy Whitmore]
Recommendation Follow-Up
Richard Bendall, Chief Audit Executive
(Memo dated: November 15, 2017)

H. Status of Other External Audits Not Conducted at the Discretion of
Internal Audit
Richard Bendall, Chief Audit Executive
(Verbal presentation)

VIII. CONSULTANT COMMENTS
Rick Wentzel, Audit Committee Consultant
(Verbal presentation)

IX. REPORT ON STAFF ACTION ITEMS

X. GOOD OF THE ORDER
(For information purposes only)

XI. ADJOURNMENT

****The Board of Retirement and Board of Investments have adopted a policy permitting any member of the Boards to attend a standing committee meeting open to the public. In the event five (5) or more members of either the Board of Retirement and/or the Board of Investments (including members appointed to the Committee) are in attendance, the meeting shall constitute a joint meeting of the Committee and the Board of Retirement and/or Board of Investments. Members of the Board of Retirement and Board of Investments who are not members of the Committee may attend and participate in a meeting of a Board Committee but may not vote on any matter discussed at the meeting. Except as set forth in the Committee's Charter, the only action the Committee may take at the meeting is approval of a recommendation to take further action at a subsequent meeting of the Board.***

Documents subject to public disclosure that relate to an agenda item for an open session of the Board and/or Committee that are distributed less than 72 hours prior to the meeting will be available for public inspection at the time they are distributed to a majority of the members of any such Board and/or Committee at LACERA's offices at 300 N. Lake Avenue, Suite 820, Pasadena, CA 91101 during normal business hours [e.g., 8:00 a.m. to 5:00 p.m. Monday through Friday].

Persons requiring an alternative format of this agenda pursuant to Section 202 of the Americans with Disabilities Act of 1990 may request one by calling Cynthia Guider at (626)-564-6000 extension 3327, from 8:00 a.m. to 5:00 p.m. Monday through Friday, but no later than 48 hours prior to the time the meeting is to commence. Assistive Listening Devices are available upon request. American Sign Language (ASL) Interpreters are available with at least three (3) business days notice before the meeting date.

MINUTES OF THE REGULAR MEETING OF THE AUDIT COMMITTEE
AND BOARD OF RETIREMENT AND/OR BOARD OF INVESTMENTS*
LOS ANGELES COUNTY EMPLOYEES RETIREMENT ASSOCIATION
300 N. LAKE AVENUE, SUITE 810, PASADENA, CALIFORNIA 91101

9:00 A.M., WEDNESDAY, AUGUST 16, 2017

PRESENT: Joseph Kelly, Chair
Michael S. Schneider, Vice Chair
Vivian Gray, Secretary
David Green

ABSENT: Shawn Kehoe

STAFF, ADVISORS, AND PARTICIPANTS

Richard Bendall, Chief Audit Executive
Steven Rice, Chief Legal Counsel
Rick Wentzel, Audit Committee Consultant
Quoc Nguyen, Principal Internal Auditor

I. CALL TO ORDER

The meeting was called to order at 9:00a.m., in the Boardroom of Gateway Plaza by Mr. Kelly, Chair of the Committee.

II. PLEDGE OF ALLEGIANCE

Mr. Green led the Board Members and staff in reciting the Pledge of Allegiance.

III. APPROVAL OF THE MINUTES

- A. Approval of the Minutes of the Regular Audit Committee Meeting of March 22, 2017.

Mr. Schneider made a motion, and Mr. Green seconded to approve the minutes of the regular Audit Committee meeting of March 22, 2017. The motion passed unanimously.

IV. REPORT ON CLOSED SESSION ITEMS

No items to report.

V. PUBLIC COMMENT

No items to report.

VI. NON-CONSENT ITEMS

- A. Recommendation, as submitted by Richard Bendall, Chief Audit Executive, that the Audit Committee review and discuss the following engagement reports to take the following action(s):

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1. Accept and file report and/or,
2. Instruct staff to forward report to Boards or Committees and/or,
3. Provide further instruction to staff.

(Memo dated July 31, 2017)

a. Retiree Healthcare Member Verification

Nathan Amick, Internal Auditor

(Report issued June 30, 2017)

b. Certificates Processing Review

Darla Vidger, Internal Auditor

(Report issued June 29, 2017)

c. Investment Fees Audit

Quoc Nguyen, Principal Internal Auditor

(Report issued June 28, 2017)

d. Duplicate Special Payments

Gabriel Tafoya, Senior Internal Auditor

(Report issued January 19, 2017)

Mr. Schneider directed questions to Internal Audit staff regarding item (c.) Mr. Bendall and Mr. Nguyen addressed investment Fees Audit, questions and concerns.

Mr. Kelly voiced questions/concerns regarding fee calculations. Mr. Grabel addressed Mr. Kelly's concerns.

Mr. Kehoe made a motion to accept and approved agenda items in addition to forwarding the Retiree Healthcare Member Verification Report to OOC and the Investment Fees Audit Report to BOI, Mr. Schneider seconded the approval of the agenda items with the mentioned additions. The motion passed unanimously.

- B. Recommendation that the Audit Committee review and approve the Audit Plan for Fiscal Year End 2018 as submitted by Richard Bendall, Chief Audit Executive, and Quoc Nguyen, Principal Internal Auditor (Memo dated July 31, 2017)

Mr. Kelly made a motion to approve the agenda item with the caveat of giving Internal Audit an opportunity to re-evaluate the plan and present goals that are more realistic if necessary, Mr. Green seconded the motion to approve the agenda item. The motion passed unanimously.

IV. REPORTS

- A. Internal Audit Staffing Report
Richard Bendall, Chief Audit Executive
(Verbal presentation)
- B. Internal Audit Annual Report – Fiscal Year End 2017
Richard Bendall, Chief Audit Executive
(Report dated June 30, 2017)
- C. Recommendation Follow-Up Report
Quoc Nguyen, Principal Internal Auditor
(Memo dated June 30, 2017)
- D. Privacy Audit Recommendation Follow-Up
Richard Bendall, Chief Audit Executive
Darla Vidger, Internal Auditor
(Memo dated July 31, 2017)
- E. **Attorney-Client Privilege/Confidential Memo**
Human Resources Compliance Audit [by Liebert Cassidy Whitmore]
Recommendation Follow-Up
Richard Bendall, Chief Audit Executive
(Memo dated July 31, 2017)
- F. Status of Other External Audits Not Conducted at the Discretion of Internal Audit

Richard Bendall, Chief Audit Executive (Verbal Presentation)

a. **Attorney-Client Privilege/Confidential Memo**

Audit Report of LACERA's Pay Practices [by Liebert Cassidy Whitmore]

Johanna Fontenot, Senior Staff Counsel

John Nogales, Human Resources Director

(Memo dated August 3, 2017)

G. Quality Assurance & Improvement Program Report

Richard Bendall, Chief Audit Executive

(Memo dated July 31, 2017)

H. Internal Audit Goal Report

Richard Bendall, Chief Audit Executive

(Memo dated July 31, 2017)

No questions or comment on
any of the listed reports.

V. CONSULTANT COMMENTS

Rick Wentzel, Audit Committee Consultant

There were no comments from
Mr. Wentzel.

VI. GOOD OF THE ORDER

There were no comments.

VII. CLOSED SESSION

A. Performance Evaluation – 2017 CAE Fiscal Year End Report
[Pursuant to Government Code Section 54957(b)(1)]

Title: Chief Audit Executive

B. Performance Evaluation – 2018 CAE Goals & Expectations
[Pursuant to Government Code Section 54957(b)(1)]

Title: Chief Audit Executive

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ADJOURNMENT

There being no further business to come before the Audit Committee, the meeting was adjourned at 9:45 a.m.

VIVIAN GRAY, SECRETARY


JOSEPH KELLY, CHAIR





November 15, 2017

TO: Each Member
2017 Audit Committee

Audit Committee Consultant
Rick Wentzel

FROM: Richard Bendall 
Chief Audit Executive

Leisha Collins 
Principal Internal Auditor

Christina Logan 
Senior Internal Auditor

FOR: November 30, 2017 | Audit Committee Meeting

SUBJECT: **UPDATES TO AUDIT COMMITTEE CHARTER**

RECOMMENDATION

Approve updates to the Audit Committee Charter

BACKGROUND

The Institute of Internal Auditors (IIA) recommends that Audit Committees formally define their purpose, authority, and responsibilities in a charter. In addition, the IIA recommends periodic reviews of the charter to ensure it is aligned with industry best practices and organizational changes. LACERA's Audit Committee Charter (Charter) was established in 2004, and has been updated several times, most recently in January 2017.

The IIA has not updated its model audit committee charter subsequent to the January 2017 Charter. However, staff has added a Conflicts and Ethics section to the Charter to align with the Board of Retirement's Charter. This update does not change the Committee's organization, authority, or responsibilities; staff believes the update is administrative and can therefore be approved by the Audit Committee. Provided with this memo is the proposed 2017 Audit Committee Charter (*Attachment A*) and an updated red-lined version (*Attachment B*).

CONCLUSION

Staff recommends the Audit Committee approve the proposed changes to the Audit Committee Charter.

RB:LC\CL
IA Charter Memo

Attachments:

- A: Proposed 2017 IA Charter
- B: Red-lined IA Charter

Audit Committee Charter

November 2017



2017



AUDIT COMMITTEE CHARTER

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 - G. OTHER RESPONSIBILITIES 6
- VI. APPROVAL 7**



AUDIT COMMITTEE CHARTER

I. PURPOSE

In November 2003, the Los Angeles County Employees Retirement Association's Board of Retirement and Board of Investments established the LACERA Audit Committee.

The purpose of this "Audit Committee Charter" is to govern the Audit Committee that assists the Boards of Retirement and Investments (Boards) in fulfilling their fiduciary oversight responsibilities for the financial reporting process, the system of internal controls, the audit processes, and the organization's method for monitoring compliance with laws and regulations. The Audit Committee Charter is a living document and may be amended for procedural and administrative matters upon majority vote of the Audit Committee.

II. AUTHORITY

The Audit Committee has the authority to conduct or authorize investigations into any matters within its scope of responsibility.

It shall have the following authorities:

- A. Meet with LACERA's officers, Internal Auditors, External Auditors, or consultants as necessary.
- B. Seek any information it requires from employees, all of whom are directed to cooperate with the Committee's requests, or consultants, as necessary.
- C. Resolve any disagreements or coordinate between Management, Internal Audit, and/or External Audit.
- D. Oversee the work of Internal and External Audit, and any other consultants hired to assist the Audit Committee in fulfilling its fiduciary duties.
- E. Make recommendations to the Boards regarding:
 1. The appointment, compensation, and work of the External Auditor employed to audit LACERA's financial statements.
 2. The appointment, compensation, and work of accountants or other consultants to perform audits, reviews, or investigations related to financial or operational matters (when the cost is expected to exceed the Chief Executive Officer's discretionary allowance for such contracts).
 3. Such other matters as the Committee encounters in its work.



III. AUDIT COMMITTEE COMPOSITION AND CONSULTANT

The Audit Committee will consist of the chair and vice-chair of the Boards of Retirement and Investments, plus one additional Board member elected annually by each Board, for a total of four to six members¹. Board chairs and vice-chairs that leave Board service will be replaced automatically on the Audit Committee, when the Board replaces its missing officer while other Committee membership remains intact. If any elected Audit Committee member leaves Board service, the Board of the departing member, will elect a new Audit Committee member at the next regularly scheduled Board meeting. If Audit Committee voting results in a tie, the Committee will forward the recommendation to the appropriate Board for consideration and final decision.

The Committee shall have the authority to approve the hiring of the audit consultant as an advisor. The audit consultant will be designated as the audit technical and financial expert, to advise the Committee on audit and financial matters. The audit consultant's contract will be for three years with the option for the Audit Committee to choose to extend the contract for an additional two-year period.

At the first Committee meeting of each calendar year, the Committee shall elect a Chairman, Vice Chair and Secretary, each to serve for a term of one year or until his or her successor is duly elected and qualified, whichever is less. In the event of a vacancy in the office of chair, the vice chair shall immediately assume the office of chair for the remainder of the term. In the event of a vacancy in the office of vice chair or secretary, the Committee shall elect one of its members to fill such vacancy for the remainder of the term, at its next regular meeting.

IV. AUDIT COMMITTEE MEETINGS

The Audit Committee will conduct regular meetings at least three times per year, with authority to convene additional meetings, as circumstances require. All Committee members are expected to attend each meeting.

Regular meeting notices and agendas will be posted at least 72 hours in advance of the regular meetings, and will be made available to the public in accordance with the Ralph M. Brown Act (Government Code Sections 54950, et seq.). Public documents referred to in the agenda will be made available for review at the office of the staff secretary to the Committee. The Committee will invite members of management, Internal Auditors, External Auditors, and/or others to attend meetings and provide pertinent information, as necessary.

Special meetings of the Committee may be called in the manner provided by Government Code Section 54956(a). The Committee will have such other powers as provided in the Brown Act.

¹ The number of Committee members is dependent upon the designated Chair and Vice Chair appointments to the Boards of Retirement and Investments. If both Boards were to elect the same individuals to the positions of Chair and/or Vice Chair, the Audit Committee would be comprised of four or five Board Members.



Robert's Rules of Order, except as otherwise provided herein, shall guide the Committee in its proceedings; however, the chair of the Committee shall have the same rights to vote and participate in discussions as any other member of the Committee without relinquishing the chair. The order of business shall be as determined by formal action of the Committee. Four members of a six-member Audit Committee or three members of a four or five-member Audit Committee, excluding the audit consultant, constitute a quorum.

The secretary of the Committee shall cause to be recorded in the minutes the time and place of each meeting of the Committee, the names of the members present, all official acts of the Committee, the votes given by members except when the action is unanimous, and when requested by a member, that member's dissent or approval with his or her reasons, and shall cause the minutes to be written forthwith and presented for approval at the next regular meeting.

V. RESPONSIBILITIES

The Audit Committee will carry out the following responsibilities to fulfill their fiduciary oversight responsibilities:

A. Internal Audit

1. Approve the Internal Audit Charter.
2. Ensure the independence of Internal Audit.
3. Approve the Annual Audit Plan and all major changes to the Plan. Review and monitor Internal Audit's activity relative to its Plan.
4. Review, with the Chief Audit Executive (CAE), Internal Audit's resource plan, activities, and organizational structure.
5. Monitor Internal Audit's recommendations to ensure Management has adequately addressed the risk(s) identified, either through implementing a new policy, procedure, or process, or accepting the associated risk.
6. Review and discuss engagement reports to take the following action(s):
 - a. accept and file report and/or,
 - b. instruct staff to forward report to Boards or Committees and/or,
 - c. provide further instruction to staff.

**B. Chief Audit Executive**

Since the CAE reports to the Chief Executive Officer (CEO) for administrative purposes, but to the Audit Committee for functional purposes, the Audit Committee will be responsible for the following:

1. Make recommendations to both Boards regarding the appointment, discipline, dismissal, and/or removal of the CAE, which will be addressed by the Boards in a joint meeting. Both Boards will make the final decisions as to the appointment, discipline, dismissal, and/or removal of the CAE. The CEO has authority to administer minor discipline, which is limited to counseling memos and written warnings, with notice of such discipline to be provided to the Committee and the Boards at their next meetings. Consideration by the Boards and the Committee concerning the appointment, discipline, dismissal, and/or removal of the CAE will be made in executive session under Government Code Section 54957(b).
2. Perform the CAE's annual assessment with qualitative input from the CAE and CEO. The Committee's discussion regarding the CAE's annual performance evaluation will be made in executive session under Government Code Section 54957(b).
3. Administer the CAE's annual salary adjustment using the Boards' established compensation structure.

C. External Audit

1. Make recommendations to the Board of Retirement regarding the appointment, compensation, and the work of the External Auditor.
2. Oversee the work of the External Auditor, including review of the External Auditor's proposed audit scope and approach, as well as coordination with Internal Audit and Management.
3. Review the findings and recommendations of the External Auditor, Management's responses, and actions taken to implement the audit recommendations.
4. Approve all non-compliance work.

D. Monitoring the Financial Reporting Process

1. Review significant accounting and reporting issues, including complex or unusual transactions and highly judgmental areas, recent professional and regulatory pronouncements, and understand their impact on the financial statements.
2. Review with Management and the External Auditors the results of the audit, including any difficulties encountered.
3. Review the annual financial statements, consider whether they are complete, consistent with information known to Committee members, and reflect appropriate accounting principles.



4. Review with Management and the External Auditors all matters required to be communicated to the Committee under *Generally Accepted Auditing Standards*.

E. Monitoring Management's System of Internal Controls

1. Consider the effectiveness of LACERA's internal control system, including information technology security and control.
2. Understand the scope of Internal and External Auditors' review of internal control over financial reporting, and obtain reports on significant findings and recommendations, together with Management's responses.

F. Monitoring Management's System of Compliance

1. Annually, review the effectiveness of Management's system of compliance with laws, regulations, policies, and procedures that are business critical.
2. As needed, review the findings of any examinations by regulatory agencies, and any auditor observations.
3. Annually, review Management's process for communicating LACERA's Code of Ethics to company personnel, and for monitoring compliance therewith.
4. Annually, review reported activity to ensure issues of fraud, noncompliance, and/or inappropriate activities are being addressed.

G. Conflicts and Ethics

Audit Committee members must comply with the BOR, BOI, and LACERA's Code of Ethics. Specific to the Audit Committee:

1. Avoid actual or potential conflict of interest or ethics issues. Members will notify the Audit Committee Chair and Vice Chair, the CEO, and Legal Counsel of such issues concerning themselves and other Audit Committee members related to the business of the Audit Committee.
2. Review reports received relating to conflict of interest and ethics issues, and if appropriate, make a recommendation to the Boards.

H. Other Responsibilities

1. Report to the Boards as needed about the Audit Committee's activities, issues, and related recommendations.
2. Provide an open avenue of communication between Internal Audit, the External Auditors, Management, and the Boards.
3. Perform other activities related to this Charter as requested by the Boards
4. Review and assess the adequacy of the Committee's Charter annually, requesting the Boards' approval for proposed changes, and ensure appropriate disclosure as may be required by law or regulation.



5. Communicates public disclosures related to the purpose, authority, function, and responsibility of the Audit Committee.

VI. APPROVAL OF PROCEDURAL AND ADMINISTRATIVE UPDATES

This Audit Committee Charter (“AC Charter”) was updated for procedural and administrative matters, and approved by the Audit Committee on November 30, 2017. This updated AC Charter is thereby effective this day and is hereby signed by the Audit Committee Chair,

Joseph Kelly

Chair, Audit Committee

Date

VII. APPROVAL OF AUDIT COMMITTEE CHARTER

This Audit Committee Charter (“AC Charter”) was reviewed by the Audit Committee on December 14, 2016, and approved by the Board of Retirement and Board of Investments on January 11, 2017 and January 12, 2017, respectively. This AC Charter is thereby effective January 12, 2017 and is hereby signed by the following persons who have authority and responsibilities under this Charter.

Shawn R. Kehoe

Chair, Board of Retirement

January 24, 2017

Date

David Green

Chair, Board of Investments

January 24, 2017

Date

Audit Committee Charter

November 2017



2017



AUDIT COMMITTEE CHARTER

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At the first Committee meeting of each calendar year, the Committee shall elect a Chairman, Vice Chair and Secretary, each to serve ~~At the first regular meeting of the Committee each calendar year, the Committee shall elect one of its members chair, another member vice chair, and a third member secretary, each to serve~~ for a term of one year or until his or her successor is duly elected and qualified, whichever is less. In the event of a vacancy in the office of chair, the vice chair shall immediately assume the office of chair for the remainder of the term. In the event of a vacancy in the office of vice chair or secretary, the Committee shall elect one of its members to fill such vacancy for the remainder of the term, at its next regular meeting.

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Special meetings of the Committee may be called in the manner provided by Government Code Section 54956(a). The Committee will have such other powers as provided in the Brown Act.

Robert's Rules of Order, except as otherwise provided herein, shall guide the Committee in its proceedings; however, the chair of the Committee shall have the same rights to vote and participate in discussions as any other member of the Committee without relinquishing the chair. The order of business shall be as determined by formal action of the Committee.

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V. RESPONSIBILITIES

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A. Internal Audit

1. Approve the Internal Audit Charter.
2. Ensure the independence of Internal Audit.
3. Approve the Annual Audit Plan and all major changes to the Plan. Review and monitor Internal Audit's activity relative to its Plan.
4. Review, with the Chief Audit Executive (CAE), Internal Audit's resource plan, activities, and organizational structure.
5. Monitor Internal Audit's recommendations to ensure Management has adequately addressed the risk(s) identified, either through implementing a new policy, procedure, or process, or accepting the associated risk.
6. Review and discuss engagement reports to take the following action(s):
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**B. Chief Audit Executive**

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2. Perform the CAE's annual assessment with qualitative input from the CAE and CEO. The Committee's discussion regarding the CAE's annual performance evaluation will be made in executive session under Government Code Section 54957(b).
3. Administer the CAE's annual salary adjustment using the Boards' established compensation structure.

C. External Audit

1. Make recommendations to the Board of Retirement regarding the appointment, compensation, and the work of the External Auditor.
2. Oversee the work of the External Auditor, including review of the External Auditor's proposed audit scope and approach, as well as coordination with Internal Audit and Management.
3. Review the findings and recommendations of the External Auditor, Management's responses, and actions taken to implement the audit recommendations.
4. Approve all non-compliance work.

D. Monitoring the Financial Reporting Process

1. Review significant accounting and reporting issues, including complex or unusual transactions and highly judgmental areas, recent professional and regulatory pronouncements, and understand their impact on the financial statements.
2. Review with Management and the External Auditors the results of the audit, including any difficulties encountered.
3. Review the annual financial statements, consider whether they are complete, consistent with information known to Committee members, and reflect appropriate accounting principles.



4. Review with Management and the External Auditors all matters required to be communicated to the Committee under *Generally Accepted Auditing Standards*.

E. Monitoring Management's System of Internal Controls

1. Consider the effectiveness of LACERA's internal control system, including information technology security and control.
2. Understand the scope of Internal and External Auditors' review of internal control over financial reporting, and obtain reports on significant findings and recommendations, together with Management's responses.

F. Monitoring Management's System of Compliance

1. Annually, review the effectiveness of Management's system of compliance with laws, regulations, policies, and procedures that are business critical.
2. As needed, review the findings of any examinations by regulatory agencies, and any auditor observations.
3. Annually, review Management's process for communicating LACERA's Code of Ethics to company personnel, and for monitoring compliance therewith.
4. Annually, review reported activity to ensure issues of fraud, noncompliance, and/or inappropriate activities are being addressed.

G. Conflicts and Ethics

Audit Committee members must comply with the BOR, BOI, and LACERA's Code of Ethics. Specific to the Audit Committee:

1. Avoid actual or potential conflict of interest or ethics issues. Members will notify the Audit Committee Chair and Vice Chair, the CEO, and Legal Counsel of such issues concerning themselves and other Audit Committee members related to the business of the Audit Committee.
2. Review reports received relating to conflict of interest and ethics issues, and if appropriate, make a recommendation to the Boards.

G.H. Other Responsibilities

1. Report to the Boards as needed about the Audit Committee's activities, issues, and related recommendations.
2. Provide an open avenue of communication between Internal Audit, the External Auditors, Management, and the Boards.
3. Perform other activities related to this Charter as requested by the Boards



4. Review and assess the adequacy of the Committee’s Charter annually, requesting the Boards’ approval for proposed changes, and ensure appropriate disclosure as may be required by law or regulation.
5. Communicates public disclosures related to the purpose, authority, function, and responsibility of the Audit Committee.

VI. APPROVAL OF PROCEDURAL AND ADMINISTRATIVE UPDATES

This Audit Committee Charter (“AC Charter”) was updated for procedural and administrative matters, and approved by the Audit Committee on November 30, 2017. This updated AC Charter is thereby effective this day and is hereby signed by the Audit Committee Chair, following persons who have authority and responsibilities under this Charter.

Joseph Kelly

Chair, Audit Committee

Date

VII. APPROVAL OF AUDIT COMMITTEE CHARTER

This Audit Committee Charter (“AC Charter”) was reviewed by the Audit Committee on December 14, 2016, and approved by the Board of Retirement and Board of Investments on January 11, 2017 and January 12, 2017, respectively. This AC Charter is thereby effective January 12, 2017 and is hereby signed by the following persons who have authority and responsibilities under this Charter.

Shawn R. Kehoe

Chair, Board of Retirement

January 24, 2017

Date

David Green

Chair, Board of Investments

January 24, 2017


Date





November 15, 2017

TO: Each Member
2017 Audit Committee

Audit Committee Consultant
Rick Wentzel

FROM: Richard Bendall 
Chief Audit Executive

Leisha Collins 
Principal Internal Auditor

Christina Logan 
Senior Internal Auditor

FOR: November 30, 2017 | Audit Committee Meeting

SUBJECT: **UPDATES TO INTERNAL AUDIT CHARTER**

RECOMMENDATION

Approve updates to the Internal Audit Charter

BACKGROUND

The Institute of Internal Auditors (IIA) requires internal audit functions to formally define the purpose, authority, and responsibilities of the group in a charter. The IIA requires a periodic review of the internal audit charter to ensure it is aligned with industry standards and organizational changes. LACERA's Internal Audit Charter (IA Charter) was established in 1996, and has been updated several times, most recently in January 2017.

In March 2017, the IIA updated its model template of the internal audit charter, and staff has incorporated these updates into the IA Charter. Staff has also further clarified content regarding IA's access to LACERA's records. The updates did not change IA's organization, authority, or responsibilities. Provided with this memo is the proposed 2017 IA Charter (*Attachment A*) and an updated red-lined version (*Attachment B*). Also attached to this memo is the 2017 IIA Internal Audit Charter (*Attachment C*).

CONCLUSION

Staff recommends the Audit Committee approve the proposed changes to the IA Charter.

RB:LC\CL
IA Charter Memo

Attachments:

- A: Proposed 2017 IA Charter
- B: Red-lined IA Charter
- C: 2017 IIA Internal Audit Charter Template

Internal Audit Charter

INTERNAL AUDIT SERVICES

November 2017



2017



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INTERNAL AUDIT CHARTER

I. PURPOSE AND MISSION

The purpose of Internal Audit is to provide independent and objective assurance services, and consulting services designed to add value and improve LACERA's operations. The mission of Internal Audit is to enhance and protect LACERA's organizational values by providing risk-based and objective assurance, advice, and insight. Internal Audit helps the organization accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of governance, risk management, and control processes.

II. ROLE

The internal audit activity is established by the Audit Committee. Internal Audit's responsibilities are defined by the Audit Committee as part of the Audit Committee's oversight role.

III. OBJECTIVES

A. Assurance Objectives

The goal of assurance services is to provide an objective examination of evidence for the purpose of providing an independent assessment to Management and the Audit Committee on governance, risk management, and control processes for LACERA. Assurance services include audits and continuous process testing to assess if the organization's assets are adequately safeguarded, operating efficiency is enhanced, and compliance is maintained with prescribed laws and LACERA policies. Assurance services also include the independent assessment of the organization's risk awareness, reliability, and integrity of the organization's data and the achievement of LACERA's goals and objectives.

B. Consulting Objectives

The objective of consulting services is to provide Management with formal assessments and advice for improving LACERA's governance, risk management, and control processes, without Internal Audit assuming Management responsibility. Internal Audit will participate as consultants in the assessment and review of controls, policies, procedures, and systems, both manual and electronic. In addition, opportunities for improving management controls, and LACERA's image may be identified during audits; and these will be communicated to the appropriate level of Management.

C. Advisory Objectives



The objective of advisory services is to provide informal advice to Management. Having Internal Audit consult at the beginning of a project, aids management in identifying and managing risks effectively, and designing adequate internal controls. Examples of advisory services include participating in various committees in an ex-officio capacity; providing routine advice on policies, establishing controls, providing training and risk management tools, and facilitating meetings.

IV. STANDARDS FOR THE PROFESSIONAL PRACTICE OF INTERNAL AUDITING

Internal Audit will govern itself by adherence to the mandatory elements of The Institute of Internal Auditors' International Professional Practices Framework, including the Core Principles for the Professional Practice of Internal Auditing, the Code of Ethics, *the International Standards for the Professional Practice of Internal Auditing*, and the Definition of Internal Auditing. The CAE will report periodically to executive management and the Audit Committee regarding Internal Audit's conformance to the Code of Ethics and the *Standards*.

Additionally, Internal Audit will obtain guidance from the professional standards and practices of other, relevant professional organizations, including but not limited to, the American Institute of Certified Public Accountants, the Information Systems Audit and Control Association, the Associate of Certified Fraud Examiners, and the Association of Public Pension Fund Auditors.

V. ORGANIZATION

The Chief Audit Executive (CAE) reports functionally to the Audit Committee of the Board of Investments and Board of Retirement, and administratively to the Chief Executive Officer. This reporting structure provides for Internal Audit's independence and objectivity as required by professional standards.

The Audit Committee's roles and responsibilities are defined in the Audit Committee Charter.

VI. AUTHORITY

Internal Audit, with strict accountability for confidentiality, and safeguarding of records and information, is authorized full, free, and unrestricted access to any and all of LACERA's hard copy and electronic records, data maintained within IT systems or databases, physical properties, and personnel pertinent to carrying out any engagement. All employees are requested to assist Internal Audit in fulfilling its roles and responsibilities.

The CAE will have unrestricted access to, and communicate directly with the Audit Committee and Boards, subject to the requirements of the Ralph M. Brown Act (Government Code Section 54950, et seq.).



VII. INDEPENDENCE AND OBJECTIVITY

Internal Audit will remain free from interference by any element in the organization, including matters of audit selection, scope, procedures, frequency, timing, or report content to permit maintenance of a necessary independent and objective mental attitude.

Internal Audit will be diligent in monitoring its own potential conflicts of interest in performing its Mission, Objectives, and Responsibility under this Charter. Where a conflict is identified, the Audit Committee will be advised and a determination will be made by the Committee as to whether to proceed and procure an independent outside auditor. Internal Auditors will have no direct operational responsibility or authority over any of the activities audited. Accordingly, they will not implement internal controls, develop procedures, install systems, prepare records, or engage in any other activity that may impair the Internal Auditor's judgment.

Internal Auditors will exhibit the highest level of professional objectivity in gathering, evaluating, and communicating information about the activity or process being examined. Internal Auditors will make a balanced assessment of all the relevant circumstances and not be unduly influenced by their own interests or by others in forming judgments.

The CAE will confirm to the Audit Committee, at least annually, the organizational independence of the Internal Audit division.

VIII. RESPONSIBILITY

The scope of internal auditing encompasses, but is not limited to, the examination and evaluation of the adequacy and effectiveness of LACERA's governance, risk management, and control processes as well as the quality of performance in carrying out assigned responsibilities to achieve the organization's stated goals and objectives.

This includes:

- A. Evaluating risk exposure relating to achievement of LACERA's strategic objectives.
- B. Evaluating the reliability and integrity of information and the means used to identify, measure, classify, and report such information.
- C. Evaluating the systems established to ensure compliance with those policies, procedures, laws, and regulations, which could have a significant impact on LACERA.
- D. Evaluating the means of safeguarding assets and, as appropriate, verifying the existence of such assets.



- E. Evaluating the effectiveness and efficiency with which resources are employed.
- F. Evaluating operations or programs to ascertain whether results are consistent with established objectives and goals and whether the operation or programs are being carried out as planned.
- G. Monitoring and evaluating governance processes.
- H. Monitoring and evaluating the effectiveness of LACERA's risk management processes.
- I. Evaluating the quality of performance of external auditors and the degree of coordination with Internal Audit.
- J. Performing assurance, consulting and, advisory services related to governance, risk management, and control processes as appropriate for LACERA.
- K. Reporting periodically on Internal Audit's purpose, authority, responsibilities, and performance relative to its Audit Plan.
- L. Reporting significant risk exposures and control issues, including fraud risks, governance issues, and other matters needed or requested by the Audit Committee or Boards.
- M. Evaluating specific operations at the request of the Audit Committee, Boards, or Management, as appropriate.

IX. ACCOUNTABILITY

The CAE, in the discharge of his/her duties, shall be accountable to Management and the Audit Committee to:

- A. Select, train, develop, and retain a competent Internal Audit staff that collectively has the abilities, knowledge, skills, experience, and professional certifications to meet the requirements of this Charter. Report to the Audit Committee significant changes in Internal Audit personnel.
- B. Annually develop a flexible audit plan using an appropriate risk-based methodology, including any risks or control concerns identified by Management, the Audit Committee, or the Boards. Submit the annual Audit Plan and significant interim changes to Executive Management and the Audit Committee for review and approval.
- C. Issue reports to Management and the Audit Committee, at the conclusion of each Internal Audit engagement. The written reports will include Management's responses, and if applicable, Management's timetable for implementing recommendations or corrective actions.
- D. Establish and maintain a follow-up system to monitor the disposition of results communicated to Management and ensure Management actions have been effectively implemented or that Executive Management has accepted the risk of not taking action.



- E. Provide annually an assessment on the adequacy and effectiveness of LACERA’s processes for controlling its activities and managing its risks in the areas set forth under the mission and scope of work.
- F. Report significant issues related to the processes for controlling the activities of LACERA and its affiliates, including potential improvements to those processes, and provide information concerning such issues through resolution.
- G. Periodically provide information on the status and results of the annual audit plan and the sufficiency of department resources.

X. QUALITY ASSURANCE AND IMPROVEMENT PROGRAM

Internal Audit will maintain a quality assurance and improvement program that covers all aspects of the division’s activities. The program will include an evaluation of the division’s conformance with the Definition of Internal Auditing and the Standards, and an evaluation of whether internal auditors apply the Code of Ethics. The program also assesses the efficiency and effectiveness of Internal Audit’s activity and identifies opportunities for improvement.

The CAE will communicate to Executive Management and the Audit Committee on the Internal Audit division’s quality assurance and improvement program, including the results of internal assessments and external assessments which are conducted at least once every five years by a qualified, independent assessor.

XI. APPROVAL

This Internal Audit Charter (“IA Charter”) was reviewed and adopted by the Audit Committee on November 30, 2017. This IA Charter is thereby effective this day and is hereby signed by the following persons who have authority and responsibilities under this Charter.

APPROVED AND ADOPTED BY:

Chair, Audit Committee	Date	Robert Hill <i>Chief Executive Officer, Interim</i>	Date
Richard Bendall <i>Chief Audit Executive</i>	Date		

Internal Audit Charter

INTERNAL AUDIT SERVICES

November 2017



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INTERNAL AUDIT CHARTER

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INTERNAL AUDIT CHARTER

I. PURPOSE AND MISSION

The ~~purpose~~ mission of Internal Audit is to provide independent and objective assurance services, and consulting services designed to add value and improve LACERA's operations. The mission of Internal Audit is to enhance and protect LACERA's organizational values by providing risk-based and objective assurance, advice, and insight. Internal Audit helps the organization accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of governance, risk management, and control processes.

II. ROLE

The internal audit activity is established by the Audit Committee. Internal Audit's responsibilities are defined by the Audit Committee as part of the Audit Committee's oversight role.

III. OBJECTIVES

A. Assurance Objectives

The goal of assurance services is to provide an objective examination of evidence for the purpose of providing an independent assessment to Management and the Audit Committee on governance, risk management, and control processes for LACERA. Assurance services include audits and continuous process testing to assess if the organization's assets are adequately safeguarded, operating efficiency is enhanced, and compliance is maintained with prescribed laws and LACERA policies. Assurance services also include the independent assessment of the organization's risk awareness, reliability, and integrity of the organization's data and the achievement of LACERA's goals and objectives.

B. Consulting Objectives

The objective of consulting services is to provide Management with formal assessments and advice for improving LACERA's governance, risk management, and control processes, without Internal Audit assuming Management responsibility. Internal Audit will participate as consultants in the assessment and review of controls, policies, procedures, and systems, both manual and electronic. In addition, opportunities for improving management controls, and LACERA's image may be identified during audits; and these will be communicated to the appropriate level of Management.

**C. Advisory Objectives**

The objective of advisory services is to provide informal advice to Management. Having Internal Audit consult at the beginning of a project, aids management in identifying and managing risks effectively, and designing adequate internal controls. Examples of advisory services include participating in various committees in an ex-officio capacity; providing routine advice on policies, establishing controls, providing training and risk management tools, and facilitating meetings.

IV. STANDARDS FOR THE PROFESSIONAL PRACTICE OF INTERNAL AUDITING**PROFESSIONALISM**

Internal Audit will govern itself by adherence to the mandatory elements of The Institute of Internal Auditors' International Professional Practices Framework, including the Core Principles for the Professional Practice of Internal Auditing, the Code of Ethics, the International Standards for the Professional Practice of Internal Auditing, and the Definition of Internal Auditing. The CAE will report periodically to executive management and the Audit Committee regarding Internal Audit's conformance to the Code of Ethics and the Standards.

Additionally, Internal Audit will obtain guidance from the professional standards and practices of other, relevant professional organizations, including but not limited to, the American Institute of Certified Public Accountants, the Information Systems Audit and Control Association, the Associate of Certified Fraud Examiners, and the Association of Public Pension Fund Auditors.

V. ORGANIZATION

The Chief Audit Executive (CAE) reports functionally to the Audit Committee of the Board of Investments and Board of Retirement, and administratively to the Chief Executive Officer. This reporting structure provides for Internal Audit's independence and objectivity as required by professional standards.

The Audit Committee's roles and responsibilities are defined in the Audit Committee Charter.

**VI. AUTHORITY**

Internal Audit, with strict accountability for confidentiality, and safeguarding of records and information, is authorized full, free, and unrestricted access to any and all of LACERA's hard copy and electronic records, data maintained within IT systems or databases, physical properties, and personnel pertinent to carrying out any engagement. All employees are requested to assist Internal Audit in fulfilling its roles and responsibilities.

The CAE will have unrestricted access to, and communicate directly with the Audit Committee and Boards. ~~Internal Audit will also have free and unrestricted access to the Audit Committee and Boards,~~ subject to the requirements of the Ralph M. Brown Act (Government Code Section 54950, et seq.).

VII. INDEPENDENCE AND OBJECTIVITY

Internal Audit will remain free from interference by any element in the organization, including matters of audit selection, scope, procedures, frequency, timing, or report content to permit maintenance of a necessary independent and objective mental attitude.

Internal Audit will be diligent in monitoring its own potential conflicts of interest in performing its Mission, Objectives, and Responsibility under this Charter. Where a conflict is identified, the Audit Committee will be advised and a determination will be made by the Committee as to whether to proceed and procure an independent outside auditor. Internal Auditors will have no direct operational responsibility or authority over any of the activities audited. Accordingly, they will not implement internal controls, develop procedures, install systems, prepare records, or engage in any other activity that may impair the Internal Auditor's judgment.

Internal Auditors will exhibit the highest level of professional objectivity in gathering, evaluating, and communicating information about the activity or process being examined. Internal Auditors will make a balanced assessment of all the relevant circumstances and not be unduly influenced by their own interests or by others in forming judgments.

The CAE will confirm to the Audit Committee, at least annually, the organizational independence of the Internal Audit division.

VIII. RESPONSIBILITY

The scope of internal auditing encompasses, but is not limited to, the examination and evaluation of the adequacy and effectiveness of LACERA's governance, risk management, and control processes as well as the quality of performance in carrying out assigned responsibilities to achieve the organization's stated goals and objectives.

This includes:

- A. Evaluating risk exposure relating to achievement of LACERA's strategic objectives.
- B. Evaluating the reliability and integrity of information and the means used to identify, measure, classify, and report such information.
- C. Evaluating the systems established to ensure compliance with those policies, procedures, laws, and regulations, which could have a significant impact on LACERA.
- D. Evaluating the means of safeguarding assets and, as appropriate, verifying the existence of such assets.
- E. Evaluating the effectiveness and efficiency with which resources are employed.
- F. Evaluating operations or programs to ascertain whether results are consistent with established objectives and goals and whether the operation or programs are being carried out as planned.
- G. Monitoring and evaluating governance processes.
- H. Monitoring and evaluating the effectiveness of LACERA's risk management processes.
- I. Evaluating the quality of performance of external auditors and the degree of coordination with Internal Audit.
- J. Performing assurance, consulting and, advisory services related to governance, risk management, and control processes as appropriate for LACERA.
- K. Reporting periodically on Internal Audit's purpose, authority, responsibilities, and performance relative to its Audit Plan.
- L. Reporting significant risk exposures and control issues, including fraud risks, governance issues, and other matters needed or requested by the Audit Committee or Boards.
- M. Evaluating specific operations at the request of the Audit Committee, Boards, or Management, as appropriate.

IX. ACCOUNTABILITY

The CAE, in the discharge of his/her duties, shall be accountable to Management and the Audit Committee to:

- A. Select, train, develop, and retain a competent Internal Audit staff that collectively has the abilities, knowledge, skills, experience, and professional certifications to



meet the requirements of this Charter. Report to the Audit Committee significant changes in Internal Audit personnel.

- B. Annually develop a flexible audit plan using an appropriate risk-based methodology, including any risks or control concerns identified by Management, the Audit Committee, or the Boards. Submit the annual Audit Plan and significant interim changes to Executive Management and the Audit Committee for review and approval.
- C. Issue reports to Management and the Audit Committee, at the conclusion of each Internal Audit engagement. The written reports will include Management's responses, and if applicable, Management's timetable for implementing recommendations or corrective actions.
- D. Establish and maintain a follow-up system to monitor the disposition of results communicated to Management and ensure Management actions have been effectively implemented or that Executive Management has accepted the risk of not taking action.
- E. Provide annually an assessment on the adequacy and effectiveness of LACERA's processes for controlling its activities and managing its risks in the areas set forth under the mission and scope of work.
- F. Report significant issues related to the processes for controlling the activities of LACERA and its affiliates, including potential improvements to those processes, and provide information concerning such issues through resolution.
- G. Periodically provide information on the status and results of the annual audit plan and the sufficiency of department resources.

X. QUALITY ASSURANCE AND IMPROVEMENT PROGRAM

Internal Audit will maintain a quality assurance and improvement program that covers all aspects of the division's activities. The program will include an evaluation of the division's conformance with the Definition of Internal Auditing and the Standards, and an evaluation of whether internal auditors apply the Code of Ethics. The program also assesses the efficiency and effectiveness of Internal Audit's activity and identifies opportunities for improvement.

The CAE will communicate to Executive Management and the Audit Committee on the Internal Audit division's quality assurance and improvement program, including the results of internal assessments and external assessments which are conducted at least once every five years by a qualified, independent assessor.

**XI. APPROVAL**

This Internal Audit Charter (“IA Charter”) was reviewed and adopted by the Audit Committee on November 30, 2017. This IA Charter is thereby effective this day and is hereby signed by the following persons who have authority and responsibilities under this Charter.

APPROVED AND ADOPTED BY:

Chair, Audit Committee

Date

Robert Hill

Date

*Chief Executive Officer,
Interim*

Richard Bendall

Date

Chief Audit Executive



International Professional
Practices Framework

Supplemental Guidance

Model Internal Audit Activity Charter

The Model Internal Audit Activity Charter is designed to illustrate common practices typically set out in an internal audit activity charter. The generic nature of this draft is intended to encourage customization.

The document may not reflect all legal or regulatory requirements that exist in the every jurisdiction. Additionally, stakeholder expectations may influence the inclusion or deletion of certain practices.

In drafting an internal audit activity charter, the chief audit executive should exercise care to customize the charter, including replacing bracketed, blue text with language that accurately reflects the user's situation.

Purpose and Mission

The purpose of [name of organization]'s internal audit [department/activity] is to provide independent, objective assurance and consulting services designed to add value and improve [name of organization]'s operations. The mission of internal audit is to enhance and protect organizational value by providing risk-based and objective assurance, advice, and insight. The internal audit [department/activity] helps [name of organization] accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of governance, risk management, and control processes.

Standards for the Professional Practice of Internal Auditing

The internal audit [department/activity] will govern itself by adherence to the mandatory elements of The Institute of Internal Auditors' International Professional Practices Framework, including the Core Principles for the Professional Practice of Internal Auditing, the Code of Ethics, the *International Standards for the Professional Practice of Internal Auditing*, and the Definition of Internal Auditing. The chief audit executive will report periodically to senior management and the [board/audit committee/supervisory committee] regarding the internal audit [department/activity]'s conformance to the Code of Ethics and the *Standards*.

Authority

The chief audit executive will report functionally to the [board/audit committee/supervisory committee] and administratively (i.e., day-to-day operations) to the [chief executive officer]. To establish, maintain, and assure that [name of organization]'s internal audit [department/activity] has sufficient authority to fulfill its duties, the [board/audit committee/supervisory committee] will:

- Approve the internal audit [department/activity]'s charter.
- Approve the risk-based internal audit plan.
- Approve the internal audit [department/activity]'s budget and resource plan.
- Receive communications from the chief audit executive on the internal audit [department/activity]'s performance relative to its plan and other matters.
- Approve decisions regarding the appointment and removal of the chief audit executive.
- Approve the remuneration of the chief audit executive.
- Make appropriate inquiries of management and the chief audit executive to determine whether there is inappropriate scope or resource limitations.

The chief audit executive will have unrestricted access to, and communicate and interact directly with, the [board/audit committee/supervisory committee], including in private meetings without management present.

The [board/audit committee/supervisory committee] authorizes the internal audit [department/activity] to:

- Have full, free, and unrestricted access to all functions, records, property, and personnel pertinent to carrying out any engagement, subject to accountability for confidentiality and safeguarding of records and information.
- Allocate resources, set frequencies, select subjects, determine scopes of work, apply techniques required to accomplish audit objectives, and issue reports.
- Obtain assistance from the necessary personnel of [name of organization], as well as other specialized services from within or outside [name of organization], in order to complete the engagement.

Independence and Objectivity

The chief audit executive will ensure that the internal audit [department/activity] remains free from all conditions that threaten the ability of internal auditors to carry out their responsibilities in an unbiased manner, including matters of audit selection, scope, procedures, frequency, timing, and report content. If the chief audit executive determines that independence or objectivity may be impaired in fact or appearance, the details of impairment will be disclosed to appropriate parties.

Internal auditors will maintain an unbiased mental attitude that allows them to perform engagements objectively and in such a manner that they believe in their work product, that no quality compromises are made, and that they do not subordinate their judgment on audit matters to others.

Internal auditors will have no direct operational responsibility or authority over any of the activities audited. Accordingly, internal auditors will not implement internal controls, develop procedures, install systems, prepare records, or engage in any other activity that may impair their judgment, including:

- Assessing specific operations for which they had responsibility within the previous year.
- Performing any operational duties for [name of organization] or its affiliates.
- Initiating or approving transactions external to the internal audit [activity/department].



- Directing the activities of any [name of organization] employee not employed by the internal audit [department/activity], except to the extent that such employees have been appropriately assigned to auditing teams or to otherwise assist internal auditors.

Where the chief audit executive has or is expected to have roles and/or responsibilities that fall outside of internal auditing, safeguards will be established to limit impairments to independence or objectivity.

Internal auditors will:

- Disclose any impairment of independence or objectivity, in fact or appearance, to appropriate parties.
- Exhibit professional objectivity in gathering, evaluating, and communicating information about the activity or process being examined.
- Make balanced assessments of all available and relevant facts and circumstances.
- Take necessary precautions to avoid being unduly influenced by their own interests or by others in forming judgments.

The chief audit executive will confirm to the [board/audit committee/supervisory committee], at least annually, the organizational independence of the internal audit [department/activity].

The chief audit executive will disclose to the [board/audit committee/supervisory committee] any interference and related implications in determining the scope of internal auditing, performing work, and/or communicating results.

Scope of Internal Audit Activities

The scope of internal audit activities encompasses, but is not limited to, objective examinations of evidence for the purpose of providing independent assessments to the [board/audit committee/supervisory committee], management, and outside parties on the adequacy and effectiveness of governance, risk management, and control processes for [name of organization]. Internal audit assessments include evaluating whether:

- Risks relating to the achievement of [name of organization]'s strategic objectives are appropriately identified and managed.
- The actions of [name of organization]'s officers, directors, employees, and contractors are in compliance with [name of organization]'s policies, procedures, and applicable laws, regulations, and governance standards.
- The results of operations or programs are consistent with established goals and objectives.



- Operations or programs are being carried out effectively and efficiently.
- Established processes and systems enable compliance with the policies, procedures, laws, and regulations that could significantly impact [name of organization].
- Information and the means used to identify, measure, analyze, classify, and report such information are reliable and have integrity.
- Resources and assets are acquired economically, used efficiently, and protected adequately.

The chief audit executive will report periodically to senior management and the [board/audit committee/supervisory committee] regarding:

- The internal audit [department/activity]'s purpose, authority, and responsibility.
- The internal audit [department/activity]'s plan and performance relative to its plan.
- The internal audit [department/activity]'s conformance with The IIA's Code of Ethics and *Standards*, and action plans to address any significant conformance issues.
- Significant risk exposures and control issues, including fraud risks, governance issues, and other matters requiring the attention of, or requested by, the [board/audit committee/supervisory committee].
- Results of audit engagements or other activities.
- Resource requirements.
- Any response to risk by management that may be unacceptable to [name of organization].

The chief audit executive also coordinates activities, where possible, and considers relying upon the work of other internal and external assurance and consulting service providers as needed. The internal audit [department/activity] may perform advisory and related client service activities, the nature and scope of which will be agreed with the client, provided the internal audit [department/activity] does not assume management responsibility.

Opportunities for improving the efficiency of governance, risk management, and control processes may be identified during engagements. These opportunities will be communicated to the appropriate level of management.

Responsibility

The chief audit executive has the responsibility to:

- Submit, at least annually, to senior management and the [board/audit committee/supervisory committee] a risk-based internal audit plan for review and approval.



- Communicate to senior management and the [board/audit committee/supervisory committee] the impact of resource limitations on the internal audit plan.
- Review and adjust the internal audit plan, as necessary, in response to changes in [name of organization]'s business, risks, operations, programs, systems, and controls.
- Communicate to senior management and the [board/audit committee/supervisory committee] any significant interim changes to the internal audit plan.
- Ensure each engagement of the internal audit plan is executed, including the establishment of objectives and scope, the assignment of appropriate and adequately supervised resources, the documentation of work programs and testing results, and the communication of engagement results with applicable conclusions and recommendations to appropriate parties.
- Follow up on engagement findings and corrective actions, and report periodically to senior management and the [board/audit committee/supervisory committee] any corrective actions not effectively implemented.
- Ensure the principles of integrity, objectivity, confidentiality, and competency are applied and upheld.
- Ensure the internal audit [department/activity] collectively possesses or obtains the knowledge, skills, and other competencies needed to meet the requirements of the internal audit charter.
- Ensure trends and emerging issues that could impact [name of organization] are considered and communicated to senior management and the [board/audit committee/supervisory committee] as appropriate.
- Ensure emerging trends and successful practices in internal auditing are considered.
- Establish and ensure adherence to policies and procedures designed to guide the internal audit [department/activity].
- Ensure adherence to [name of organization]'s relevant policies and procedures, unless such policies and procedures conflict with the internal audit charter. Any such conflicts will be resolved or otherwise communicated to senior management and the [board/audit committee/supervisory committee].
- Ensure conformance of the internal audit [department/activity] with the *Standards*, with the following qualifications:
 - If the internal audit [department/activity] is prohibited by law or regulation from conformance with certain parts of the *Standards*, the chief audit executive will ensure appropriate disclosures and will ensure conformance with all other parts of the *Standards*.
 - If the *Standards* are used in conjunction with requirements issued by [other authoritative bodies], the chief audit executive will ensure that the internal audit [department/activity] conforms with the *Standards*, even if the internal audit [department/activity] also conforms with the more restrictive requirements of [other authoritative bodies].



Quality Assurance and Improvement Program

The internal audit [department/activity] will maintain a quality assurance and improvement program that covers all aspects of the internal audit [department/activity]. The program will include an evaluation of the internal audit [department/activity]'s conformance with the *Standards* and an evaluation of whether internal auditors apply The IIA's Code of Ethics. The program will also assess the efficiency and effectiveness of the internal audit [department/activity] and identify opportunities for improvement.

The chief audit executive will communicate to senior management and the [board/audit committee/supervisory committee] on the internal audit [department/activity]'s quality assurance and improvement program, including results of internal assessments (both ongoing and periodic) and external assessments conducted at least once every five years by a qualified, independent assessor or assessment team from outside [name of organization].

Approval/Signatures

Chief Audit Executive

Date

[Board/Audit Committee/Supervisory Committee] Chair

Date

[Chief Executive Officer]

Date





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March 17



November 15, 2017

TO: Each Member
2017 Audit Committee
Audit Committee Consultant
Rick Wentzel

FROM: Richard Bendall 
Chief Audit Executive

FOR: November 30, 2017 | Audit Committee Meeting

SUBJECT: **AUDIT REPORTS**

RECOMMENDATION

In accordance with your current Audit Committee Charter, staff recommends that the Audit Committee review and discuss the current engagement reports, listed below and attached, to take the following action(s):

- 1. accept and file report and/or,**
- 2. instruct staff to forward report to Boards or Committees and/or,**
- 3. provide further instruction to staff.**

ENGAGEMENT REPORTS

- a. Los Angeles County Rehired Retirees Audit
Nathan Amick, Internal Auditor
(Report issued: October 31, 2017)

- b. Member Death Verification Process
Gabriel Tafoya, Senior Internal Auditor
(Report issued: October 31, 2017)

Attachments



LACERA INTERNAL AUDIT DIVISION

LOS ANGELES COUNTY REHIRED RETIREES AUDIT

October 31, 2017

AUDIT PERFORMED BY:

Nathan Amick
Internal Auditor

EXECUTIVE SUMMARY

The State of California's County Employees Retirement Law (CERL) has long provided that if Los Angeles County believes a retiree possesses special skills or knowledge, the County has the option to employ retirees. Under Government Code Section 31680.3, rehired retirees may work up to and not exceed 960 hours per fiscal year, on a strictly temporary basis, without affecting their retirement status or benefits. In addition, IRS regulations require a "bona fide" break in service after retirement before being rehired. To comply with the IRS regulation, LACERA's Board of Retirement adopted a resolution in 2006 stating that a member under the "normal retirement age", as defined in the body of this report, may not return to temporary County service within 90 days of his or her retirement date.

The California Public Employees' Pension Reform Act of 2013 ("PEPRA") added additional restrictions to the employment of retirees. The PEPRA regulations reinforced the 960-hour limit, and notwithstanding the 90-day break in service requirement, added a 180-day continuous break in service after their retirement date before being rehired.

Furthermore, PEPRA specifies the criteria under which the County may rehire retired employees, that being:

- 1) during an emergency to prevent stoppage of public business, or
- 2) because the retired person has skills needed to perform work of limited duration.

Failure to adhere to the PEPRA regulations and LACERA requirements not only violates the state law governing retirement benefits, but it could also jeopardize the qualified tax deferred status of LACERA under federal tax law.

Our audit was limited to testing only the County's compliance with the rehired retirees' 960-hour limit and break in service requirements for fiscal year ended ("FYE") June 30, 2017. We did not review the County's, or its departments' compliance with having adequate justification for rehiring the retirees.

For this fiscal year, as indicated in the table below, we noted an improvement in the County's compliance with the 960-hour limit relative to prior years.

Fiscal Year Ended June 30	Rehired Retirees	Noncompliant Rehired Retirees	Noncompliant Rehired Retirees as a Percentage	Total Overage Hours	Average Hours Over
2015	441	12	2.7%	127	10.6
2016	502	19	3.8%	597	31.4
2017	513	8	1.6%	121	15.2

For FYE June 30, 2017, we identified eight rehired retirees who violated the LACERA 90-day break in service requirement, and one individual who violated the PEPRA 180-day break in service requirement. This is a significant increase over the prior year but primarily due to a modification to the criteria used in identifying the length of the break in service. In years past, we used *the first day of compensated post-retirement work* as the measurement date but LACERA's Legal Office stated that it should be the *re-employment date in the County's payroll system*.

This change in testing criteria occurred during the course of the audit. As a result, the County was not made aware of our change in testing criteria until October 17, 2017.

Most of our exceptions appeared to be retired sworn safety officers (sheriffs), hired on immediately as reserve sheriff's officers the day of or day after retirement, and although none had any compensated hours worked before the respective breaks in service, they technically are in violation.

Only two of the nine exceptions this year had actual hours worked and all were after the respective break in service periods.

LACERA's Internal Audit Division provided the County CEO's Benefits, Classification and Compensation Policy (BCOMP) section with the specific policy violations identified in this audit. BCOMP Management and staff met with departments who had audit findings to talk through the findings and assist with a root cause analysis. In addition, BCOMP Management and staff collaborated with departments countywide, developed checklists and monitoring tools, and provided education and training to help ensure countywide compliance of these important regulations. These efforts are described in more detail at the conclusion of this report.

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INTRODUCTION

The State of California's County Employees Retirement Law (CERL) states if Los Angeles County believes a retiree possesses special skills or knowledge, the County has the option to employ retirees. Under Government Code Section 31680.3, rehired retirees may work up to and not exceed 960 hours per fiscal year, on a strictly temporary basis, without affecting their retirement status or benefits.

In addition, IRS regulations require a "bona fide" break in service after retirement before being rehired. To comply with the IRS regulation, LACERA's Board of Retirement adopted a resolution in 2006 stating that a member under the "normal retirement age", as defined in the "Objectives" section below, may not return to temporary County service within 90 days of his or her retirement date.

The California Public Employees' Pension Reform Act of 2013 ("PEPRA") added additional restrictions to the employment of retirees. The PEPRA regulations reinforced the 960-hours limit, and notwithstanding LACERA's 90-day break in service requirement, added a 180-day continuous break in service after their retirement date before being rehired.

Furthermore, PEPRA specifies the criteria under which the County may rehire retired employees, that being:

- 1) during an emergency to prevent stoppage of public business, or
- 2) because the retired person has skills needed to perform work of limited duration.

Our audit was limited to testing only the County's compliance with the rehired retirees' 960-hour work limit and break in service requirements. We did not review the County's compliance with having adequate justification for rehiring the retirees.

BACKGROUND

In 2009 LACERA's Internal Audit Division began performing these tests of the County's compliance with law and policy limits over the over the rehiring of retirees, and reporting the results to the County CEO. The CEO's office has successfully communicated with, educated and provided direction to the County departments continually improving compliance, with some minor exceptions noted from year to year.

For FYE June 30, 2015, the noncompliance rate with the 960-hour limit was 2.7 percent, marginally the same as the previous year. However, FYE June 30, 2016 marked an increase to 3.8 percent (19 violations). Testing in FYE June 30, 2016 also identified three individuals who violated the PEPRA 180-day break in service requirement.

AUDIT PROCESS

Objectives

The objectives of this review were:

1. To determine all rehired retirees were employed for no more than 960 hours in FYE June 30, 2017, as required by PEPRA.
2. For all retirees who were newly rehired during FYE June 30, 2017, determine compliance with LACERA's requirement that all retirees under the "*normal retirement age*" perform a 90-day break in service prior to their re-employment by the County.
 - Normal retirement age for LACERA members, as determined by LACERA's Board of Retirement, is as follows:
 - Age 57 for general members of Plan A, B, C, D, or G
 - Age 65 for general members of Plan E
 - Age 55 for safety members
3. Notwithstanding the 90-day break in service requirement noted above, for all retirees who were newly rehired during FYE June 30, 2017, determine compliance with PEPRA regulations requiring all retirees to meet a continuous 180-day break in service prior to their re-employment by the County.
 - PEPRA allows two possible exceptions to the 180-day requirement.
 - PEPRA Exception (1) - The hiring department can certify it is necessary to fill a critically-needed position and the hiring has been approved by the Board of Supervisors in a public meeting. The appointment may not be placed on a consent calendar; or
 - PEPRA Exception (2) - The retiree is a public safety officer or firefighter and is returning to perform public safety officer or firefighter duties.

Scope

LACERA's Internal Audit Division reviewed all LACERA retirees who were rehired by the County or were employed by the County during the FYE June 30, 2017

Note: We did not verify whether the County departments had documentation to justify that the department rehired the retired employee 1) during an emergency to prevent stoppage of public business, or 2) because the retired person has skills needed to perform work of limited duration.

Methodology

We requested and received from the LA County Auditor-Controller's Office a rehired retiree payroll report for the Fiscal Year Ended June 30, 2017. We used this report, which provides detailed hourly payroll information for each rehired retiree by payroll period and by days worked, to identify any non-compliance with the 960 hour limit.

Prior to our FYE June 30, 2017 testing, we used the rehired retirees' *first day of compensated post-retirement work* as their rehired date to calculate their break in service. In FYE June 30, 2017, we updated our criteria based on clarification from LACERA's Legal Office and instead used the rehired retirees' *re-employment date in the County's payroll system* to determine the break in service period after their retirement date.

To identify the newly rehired retirees, we isolated all rehired retirees who retired no more than 180 days prior to the beginning of the 2017 fiscal year (July 1, 2016), and documented their *re-employment date in*

the County's payroll system. Next, we calculated their break in service to identify those who violated the PEPRRA 180-day break in service requirement, and/or the LACERA 90-day break in service requirement.

Audit Observations

1. We identified 513 rehired retirees paid by the County during the FYE June 30, 2017, an increase of 11 over the prior fiscal year. We analyzed 100 percent of the records for possible 960 hour violations and identified the following;
 - Of the 513, we identified eight (1.6%) rehired retirees who exceeded the 960-hour limit.
 - One exceeded the limit by 58 hours.
 - Seven exceeded the limit by a range of 2.5 to 14 hours, for an average of 9 hours.
 - The eight exceptions took place in the following seven different county departments:
 - Child Services
 - County Counsel
 - Fire Department
 - Mental Health
 - Probation Department
 - Public Defender
 - Sheriff (2)

We tested 100 percent of newly retired payees (96) to assess compliance with break in service requirements.

2. We identified eight (8.3%) who violated the LACERA 90-day break in service requirement. All eight individuals were Sheriff's Department retirees under the normal retirement age (55), rehired within one day of their retirement date as Reserve Sheriffs. Two of the eight received compensation as rehired retirees during FYE June 30, 2017, but only after the 90-day break.
3. With regards to the PEPRRA 180-day break in service requirement, we identified one individual who violated the break in service requirement. This individual retired from the County's Department of Human Resources on 3/30/2017 and was rehired 63 days later on 6/02/2017, although did not work any hours by FYE June 30, 2017.

CONCLUSION

For this fiscal year (FYE June 30, 2017), as indicated in the table below, we noted an improvement in the County's compliance with the 960-hour limit relative to prior years.

Fiscal Year Ended June 30	Rehired Retirees	Noncompliant Rehired Retirees	Noncompliant Rehired Retirees as a Percentage	Total Overage Hours	Average Hours Over
2015	441	12	2.7%	127.6	10.6
2016	502	19	3.8%	597.0	31.4
2017	513	8	1.6%	121.5	15.2

We identified eight rehired retirees who violated the LACERA 90-day break in service requirement, and one individual who violated the PEPRRA 180-day break in service requirement. This is a significant increase over the prior year but primarily due to a modification to the criteria used in identifying the length of the break in service. In years past, we used *the first day of compensated post-retirement work* as the measurement date but LACERA's Legal Office stated that it should be the *re-employment date in the County's payroll system*.

Most of our exceptions were retired sheriffs, hired on immediately as reserve sheriffs the day of or day after retirement, and although none had any compensated hours worked before the respective breaks in service, they technically are in violation.

Only two of the nine exceptions this year had actual hours worked and all were after the respective break in service periods.

LACERA's Internal Audit Division provided the County CEO's Benefits and Compensation Policy (BCOMP) section with the results.

Los Angeles County Management Response

In 2016, BCOMP Management and staff launched a countywide outreach, collaboration and education program that was designed to improve and sustain compliance with these important regulations and preserve the County's tax-favored defined benefit plan for all former and current County employees.

BCOMP staff individually met and collaborated with departments who had audit findings to discuss current policies and procedures and provided suggested modifications or action plans to mitigate further policy violations and comply with established rules and regulations.

Additionally, BCOMP Management and staff collaborated with LACERA and County Counsel to develop and conduct educational presentations to explain the legal aspects and ramifications of not complying with the hours worked regulations and re-enforce action plans requiring County departments to monitor the rehiring of retirees to ensure adherence to break-in-service and the 960 hour rules. Various presentations were scheduled to reach a wide range of personnel that included administrative managers and supervisors, Information Technology Personnel, and Human Resources managers and personnel staff. Presentations were given at the August 2017 Departmental Human Resources Manager meeting, the September 2017 Enterprise Project Liaison User Meeting, and the October 2017 Enterprise Project Liaison Webinar. Accompanying the power point presentations were tools created to aide designated staff with adhering to policies and regulations. The tools, that were developed and disseminated countywide, included a rehire retiree checklist, suggested best practices, and a suggested monitoring timeline.

In addition, in 2016, standardized reports were created that enable Human Resources staff throughout the County to generate on demand monitoring reports of rehired retirees on an ad-hoc basis. The County CEO issued a memo to all Administrative Deputies advising them of the availability of the report, instructions on how to generate the report, and their responsibility for monitoring their rehired retiree hours on a monthly basis. BCOMP has access to all departmental reports and continues to regularly monitor the reports at a countywide level and contact departments who have employees that are close to reaching the hours worked limit so that appropriate proactive action can be taken to avoid non-compliance issues.

In October 2017, an update to the current Rehire-Retiree onboarding process was implemented to strengthen the break-in-service controls. This enhancement requires departments to obtain approval by the County CEO's Budget Division when they are attempting to rehire a retiree before the PEPRAs mandated 180-day waiting period. The system functionality essentially creates a warning flag to proactively alert departments and it will not permit hiring unless the CEO Budget Division approves an exception.

The creation of similar functionality for the 90-day break in service rule is in process. In the interim, manual monitoring is performed to ensure compliance.

NOTED AND CONCUR:



RICHARD BENDALL
Chief Audit Executive

Date: October 31, 2017

REPORT DISTRIBUTION

Sachi A. Hamai
Los Angeles County Chief Executive Officer
Susan Moomjean
*Manager - CEO Benefits, Classification and Compensation
Division*

2017 LACERA Audit Committee
Robert Hill
J.J. Popowich
Steven Rice
Fern Billingsy



LACERA INTERNAL AUDIT SERVICES

Member Death Verification Process

October 31, 2017

AUDIT PERFORMED BY:

Gabriel Tafoya, CISA
Senior Internal Auditor

EXECUTIVE SUMMARY

Per our fiscal year 2017-2018 audit plan, we performed an audit of the "member death verification process", which is a process where LACERA works with a vendor (aka the death verification contractor) to assist with detecting member deaths as timely as possible. Semi-annually, LACERA provides the death verification contractor a file with LACERA's membership data. The vendor compares the file to their internal resources and then notifies LACERA of possible death matches. The Benefits Protection Unit (BPU), a unit within the Benefits Division is responsible for following up on the possible death matches and stopping benefit payments to members verified as deceased. This process is important in preventing benefit overpayments.

The scope and objectives of our audit included assessing the adequacy of the process's design and key controls, determining if LACERA is employing the effective resources or technologies that are available, and verifying whether BPU staff are properly following-up on death match notifications from the vendor.

Internal Audit found that LACERA's member death verification process is designed effectively to proactively detect unreported deaths and assist with preventing overpayments. We noted the following positive observations:

- BPU's written procedures are comprehensive and adequately walk users through the member death verification process.
- BPU has a similar or more comprehensive process than other public pension funds we surveyed and reached out to.
- There were no known third party products or available technologies that provided more death search capability than what LACERA is already employing.
- For all 50 vendor death notifications tested, BPU followed-up timely and placed a payment hold on the member's account if the member was verified as deceased, which prevented the possibility of overpayments.

However, we noted an opportunity for management to strengthen their vendor monitoring controls. We noted that the Benefits Division, as the contract owner, was not monitoring the vendor's data security controls over LACERA's member data. We recommend that the Benefits Division develop an on-going process to ensure that the death verification contractor has adequate controls for securing, safeguarding, and ensuring the confidentiality of LACERA's member data.

We also noted an opportunity for management to strengthen a low risk part of the process, specifically in the rare instances where BPU staff has inconclusive evidence on whether the member is alive or deceased and cannot make contact with the member. In these instances, management should consider placing payment holds on the member's account and request that the member contact LACERA to be verified before continuing the monthly benefit. Management agreed with our recommendations and has developed an action plan for implementation. Internal Audit would like to thank BPU staff and Benefits management for their cooperation and assistance during this review.

Member Death Verification Process

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INTRODUCTION

Per our fiscal year 2017-2018 audit plan, we performed an audit of the "member death verification process", which is a process where LACERA works with a third party vendor to assist with detecting member deaths as timely as possible. This process is important for preventing benefit overpayments. Without timely notifications, payments to deceased members can potentially go on for months or years before being detected. The member death verification process is managed by the Benefits Protection Unit (BPU), a unit within the Benefits Division.

BACKGROUND

Member deaths are reported to LACERA by various parties including family, friends, past County department employers, funeral homes, coroners, hospitals, etc. However, these channels are not always effective in reporting deaths timely. Therefore, LACERA created the member death verification process to supplement the regular notification channels to ensure that deaths are identified as timely as possible.

Historically, Financial and Accounting Services Division (FASD) and Internal Audit were responsible for the member death verification process. In January 2016, the Benefits division took over this responsibility when the Benefits Protection Unit (BPU) was created.

The member death verification process consists primarily of BPU staff working with the "death verification vendor" (DVC), which is a company that provides death match services to pension funds and financial services firms. The DVC maintains a proprietary death record database which is a compilation of death records from the Social Security Administration (SSA), Railroad Retirement Board, Department of Veterans Affairs, the Civil Service Commission, and obituary data. The DVC also purchases vital statistics data that include state death records, marriage records, and birth records from public health agencies and vital statistics offices across the country.

The DVC is given a file with LACERA's membership information on a semi-annual basis. The DVC then reconciles that file on a weekly basis against the Social Security Administration (SSA), state vital records, obituary information, and vital statistics data that include the California Department of Public Health (CDPH). On a weekly basis, The DVC notifies BPU staff that death match report results are ready for retrieval on the DVC's secure site.

BPU staff will review the DVC's weekly report and investigate whether the members listed on the report are in fact deceased. The DVC also provides BPU with an obituary matching service. Obituary matches use various match fields such as the member name, address, zip code, and are considered lower probability type matches, since obituary information does not have social security numbers (SSNs) which can be matched against the SSA database. BPU determines if an

obituary matched member is in fact deceased by validating the SSN LACERA has on file against the SSA database, comparing the DVC's obituary information against Workspace, and using other analytical tools such as the CLEAR investigation application and Web searches.

Once all death matches are validated, a BPU analyst generates a listing of all accounts requiring an immediate payment hold. This report is provided to the Benefits Special Administrative Services (SAS) Unit supervisor, who places the payment holds on the member accounts and sends notification letters and "Request for Confirmation of Identity" forms to the members. If the member claims that he or she is alive, the member is required to complete the "Request for Confirmation of Identity" form and verification by a third-party (e.g., social security administration office), and return the completed form to LACERA. The payment hold is removed once BPU complete their validation of the form. The member also has the option of coming into the LACERA public counter for verification in person.

During the above process, BPU will also update the internal death match tracking database. The tracking database was developed in-house for tracking death case statuses, overpayment statuses, overpayment amounts, processing statuses and hold dates. FASD is the main user of this application. Overpayments that are collected by FASD are recorded into the internal death match tracking database as payment received. As a final control check, at the end of each month, BPU staff extracts a pending payment records report from the internal death match tracking database, and validates that the appropriate cases have been closed in Workspace.

OBJECTIVE(S)

Review the member death verification process and assess the following:

- The adequacy of the process's design
- Internal controls related to the member death verification process
- If any other process and/or technology is available but is not being used by staff that would improve the process of proactively detecting deceased members
- Whether staff properly follows-up on weekly death reconciliation reports from the DVC

AUDIT SCOPE

- All policies and procedures related to the member death verification process.
- Death Verification Contractor contracting agreement
- The entire design of the member death verification process
- Death match notifications sent from the DVC to BPU staff in calendar year 2016

AUDIT METHODOLOGY

Internal Audit:

- Interviewed BPU staff and Benefits management
- Performed a walkthrough of the member death verification process
- Reviewed the current Death Verification Contractor processing procedures and contract
- Contacted other public pension funds to learn their processes
- Tested 50 death notifications that staff received from the DVC in calendar year 2016 to verify that staff properly followed up on the notification. Specifically, we verified that:
 - Staff followed up on each notification timely to determine whether the member in the notification was deceased
 - If the member was deceased, that the member's monthly payment was suspended timely to prevent overpayments
 - If an overpayment occurred as a result of a late notification, the overpayment was recovered

AUDIT RESULTS

Overall Results

Internal Audit found that the member death verification process is designed effectively to proactively detect unreported deaths and assist with preventing overpayments. We noted the following positive observations:

- BPU has a more comprehensive process than other public pension funds we spoke with. We spoke with two state public pension funds who use a similar service provider as the DVC for monthly/quarterly death matching, and also perform Obituary and Health Department matching. We also solicited processes from other public pension funds and found that they were not as robust as LACERA's member death verification process.
- There were no known third party products or available technology that provided more death search capability than what LACERA is already employing.
- BPU's written procedures are comprehensive and adequately guide users through the DVC process.
- For all 50 DVC death notifications tested, BPU followed-up on the notification timely, and placed a payment hold within Workspace timely if the member was in fact deceased, which prevented the possibility of overpayments.

During our review, however, we noted opportunities for management to enhance the internal controls with respect to vendor management and data privacy. We also noted opportunity for strengthening the validation process for low probability death match results.

Data Confidentiality and Privacy

As mentioned, LACERA's membership data sent to the DVC includes personal information (PI) such as members' social security numbers, names, addresses, birth dates, beneficiary information, etc. LACERA's privacy policy requires that reasonable safeguards be implemented to ensure the privacy of PI, including controls on who can access the information, how the information is used, how it is obtained, stored, and shared, and how it is eventually discarded. It is critical for LACERA contract managers (i.e., division managers who have contractual relationships with the vendors) to ensure that vendors who maintain sensitive member information have strong controls for protecting LACERA's data. This can be done by:

- Requesting Service Organizational Controls (SOC2) reports from the vendor. A SOC2 report provides attestation, typically by a CPA firm, that sensitive client data maintained by a vendor is effectively safeguarded. SOC2s focus on Information Technology controls that address systems security, availability, processing integrity, confidentiality, and privacy.
- Performing site visits on a periodic basis.
- Contacting the vendor periodically to ensure no material changes have taken place with respect to how the data is used and/or stored.

During our review, we noted that management did not have a process for ensuring that the DVC has strong controls for securing and safeguarding LACERA's member data. Specifically:

- Management did not request a SOC2 report from the DVC. Internal Audit subsequently reached out to the DVC and found that they had a SOC2 audit performed in April, 2016.
- In reviewing the SOC2 report, we found that the DVC had recently changed the facility for where their servers are maintained and located, which houses LACERA's member data. However, LACERA management was unaware of the change and had not performed due diligence to ensure that the new facility was secure.
- Management does not have a process for performing on-going due diligence of the DVC information technology (IT) infrastructure to determine its adequacy.

LACERA places itself at risk of breaches of confidential membership data if management does not verify and get assurance that the vendors IT controls are suitably designed and operating effectively as they relate to data security and privacy.

RECOMMENDATION

- 1. The Benefits Division should consult the LACERA Compliance Program Team related to the enhanced requirements for managing and monitoring vendors that have custody of LACERA member data. This may include the need to**

revise contract language, enhance oversight and due diligence procedures, and coordinate a visit to the vendor(s).

Management Response

The Benefits Division concurs with the recommendation. LACERA's Compliance Program Team and Privacy Officer will develop a system for regularly verifying that LACERA's external partners who take custody of LACERA's confidential information maintain adequate protections over that information. It is anticipated that the control system will be in place by December 31, 2018.

Additionally, the Benefits Division will work with LACERA's Compliance Team and Privacy Officer to develop a system for monitoring the DVC and other external vendors with whom the Benefits Division contracts with to ensure LACERA's member data is secure. We anticipate completing this by March 31, 2018.

Lower Probability Death Matches

The DVC performs obituary matches in which LACERA membership data is matched against the DVC's obituary database. While the possibility of an actual death match with a member is relatively low, these obituary death matches should be investigated thoroughly, especially in cases where the SSA is not notified or notified late of a member's death.

Although staff follow-up on all death matches ranging from high to low probability, as was evident in the documentation from our test work, we noted an opportunity for management to strengthen the process for concluding that a member is in fact alive. For example, when the DVC provides LACERA with a lower probability death match, such as an obituary match, staff determines whether the member is alive or deceased by validating the SSN LACERA has on file against the SSA database, comparing the DVC's obituary information against Workspace, and using other analytical tools such as the CLEAR investigation application and Web searches. However, in rare cases where BPU cannot obtain substantive evidence that the member is alive or make contact with the member, BPU currently does not have a mechanism to place a hold on the member's monthly payments and request that the member confirm their status with LACERA before releasing the hold. Instead, BPU staff sends a letter to the member requesting that the member contact LACERA but allows their monthly benefits to continue.

In contrast to other LACERA processes such as in the Automatic Deposit Receipt (ADR) Process, staff will flag the member's account as a possible member death if LACERA receives several returned direct deposit notices (or ADRs) that were mailed to the member. LACERA will then send a letter to the member indicating that their account will be placed on temporary hold and requests that the member resolve the issue by completing and returning a "Request for Confirmation of Identity" form or other means of verification. With the DVC's lower probability

death matches where BPU cannot obtain substantive evidence that the member is alive, management should consider employing a process similar to the ADR process.

RECOMMENDATION

2. In instances where BPU staff cannot obtain substantive evidence that the member is alive or deceased, management consider implementing a similar payment hold process as the one used for the ADR Process.

Management Response

The Benefits Division concurs with the recommendation, and BPU will work with its partners within the Benefits Division and in Member Services to strengthen existing procedures for validating and following up on low-probability death reports. It is anticipated that this project will be completed by June 30, 2018.

We would like to thank Benefits Division and the BPU staff for their assistance in completing this audit.

NOTED AND APPROVED



Richard Bendall
Chief Audit Executive

Date: **October 31, 2017**

REPORT DISTRIBUTION

2017 Audit Committee	Robert Hill	Bernie Buenaflor
Rick Wentzel	James Brekk	Steve Rice
Internal Audit Staff	JJ Popowich	Sylvia Botros

October 12, 2017

To the Board of Retirement and Board of Investments
Los Angeles County Employees Retirement Association

We have audited the financial statements of Los Angeles County Employees Retirement Association (LACERA) as of and for the year ended June 30, 2017 and have issued our report thereon dated October 12, 2017. Professional standards require that we provide you with the following information related to our audit, which is divided into the following sections:

- Required Communications with Those Charged with Governance (Section I)
- Report on Internal Control over Financial Reporting (Section II)

Section I includes information that current auditing standards require independent auditors to communicate to those individuals charged with governance. We will report this information annually to the board of retirement and board of investments of LACERA.

Section II includes the required communication surrounding LACERA's controls over financial reporting.

We would like to take this opportunity to thank LACERA's staff for the cooperation and courtesy extended to us during our audit. Their assistance and professionalism are invaluable.

This report is intended solely for the use of the board of retirement, board of investments, and management of LACERA, and is not intended to be and should not be used by anyone other than these specified parties.


We welcome any questions you may have regarding the following communications and we would be willing to discuss any of these or other questions that you might have at your convenience.

Very truly yours,

Plante & Moran, PLLC



Michelle Watterworth, CPA
Partner



Amanda Cronk, CPA
Senior Manager

Section I - Required Communications with Those Charged With Governance

Our Responsibility Under U.S. Generally Accepted Auditing Standards

As stated in our engagement letter dated September 1, 2017, our responsibility, as described by professional standards, is to express an opinion about whether the financial statements prepared by management with your oversight are fairly presented, in all material respects, in conformity with U.S. generally accepted accounting principles. Our audit of the financial statements does not relieve you or management of your responsibilities. Our responsibility is to plan and perform the audit to obtain reasonable, but not absolute, assurance that the financial statements are free of material misstatement.

As part of our audit, we considered the internal controls of Los Angeles County Employees Retirement Association (LACERA). Such considerations were solely for the purpose of determining our audit procedures and not to provide any assurance concerning such internal controls.

We are responsible for communicating significant matters related to the audit that are, in our professional judgment, relevant to your responsibilities in overseeing the financial reporting process. However, we are not required to design procedures specifically to identify such matters.

Our audit of LACERA's financial statements has also been conducted in accordance with *Government Auditing Standards*, issued by the Comptroller General of the United States. Under *Government Auditing Standards*, we are obligated to communicate certain matters that come to our attention related to our audit to those responsible for the governance of LACERA, including compliance with certain provisions of laws, regulations, contracts, grant agreements, certain instances of error or fraud, illegal acts applicable to government agencies, and significant deficiencies in internal control that we identify during our audit. Toward this end, we issued a separate letter dated October 12, 2017 regarding our consideration of LACERA's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements.

Planned Scope and Timing of the Audit

We performed the audit according to the planned scope and timing previously communicated to you in our letter about planning matters dated September 1, 2017.

Significant Audit Findings

Qualitative Aspects of Accounting Practices

Management is responsible for the selection and use of appropriate accounting policies. In accordance with the terms of our engagement letter, we will advise management about the appropriateness of accounting policies and their application. The significant accounting policies used by LACERA are described in Note B to the financial statements.

Section I - Required Communications with Those Charged With Governance (Continued)

As described in Note N, LACERA changed financial reporting policies due to the required adoption of GASB Statement No. 74, *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans*, which addresses financial reporting of state and local governmental OPEB plans to provide more useful information about postemployment benefits other than pensions. Accordingly, the change has been retrospectively applied to all prior periods presented.

We noted no transactions entered into by LACERA during the year for which there is a lack of authoritative guidance or consensus.

There are no significant transactions that have been recognized in the financial statements in a different period than when the transaction occurred.

Accounting estimates are an integral part of the financial statements prepared by management and are based on management's knowledge and experience about past and current events and assumptions about future events. Certain accounting estimates are particularly sensitive because of their significance to the financial statements and because of the possibility that future events affecting them may differ significantly from those expected. The most significant estimates surround alternative investments and the assumptions within the pension and OPEB valuations, as more fully explained below:

Alternative Investments: As explained in Note P, the financial statements include investments valued at \$12,628,199,000 (24 percent of net position) at June 30, 2017, whose fair values have been estimated by management in the absence of readily determinable market values.

The valuation of alternative investments constitutes a sensitive and significant estimate affecting the financial statements. Management uses various means to estimate the fair value of these investments, including utilizing audited financial statements and quarterly investment manager reports. We believe management's estimates are in accordance with generally accepted accounting principles. We evaluated the key factors and assumptions used to develop these estimates in determining that the estimates are reasonable in relation to the financial statements taken as a whole.

Pension and OPEB Valuation Assumptions: Financial statement disclosures and required supplemental information schedules contain information about LACERA's total pension liability and total OPEB liability related to the OPEB Trust. In order to determine both these liabilities, the actuary must apply certain assumptions which are highly sensitive to estimation. The most sensitive estimates used in the valuations are as follows:

Pension Plan:

- Assumed long-term investment rate of return
- Calculation of the single discount rate
- Mortality assumptions

OPEB Trust:

- Assumed long-term investment rate of return
- Calculation of the single discount rate
- Healthcare cost trend rate
- Mortality assumptions

Section I - Required Communications with Those Charged With Governance (Continued)

Long-term Assumed Rate of Return - Pension Plan: For purposes of GASB 67, as of June 30, 2017, LACERA is currently using 7.38 percent for the assumed long-term expected rate of return (gross of administrative expense load of .13 percent). The return is based on the results of a 2016 Investigation of Experience. This assumed rate of return has decreased 7.63 percent from fiscal year 2016. The use of a 7.38 percent long-term assumed rate of return is based on the current approved asset mix and capital market assumptions.

Single Discount Rate - Pension Plan: The calculation of the single discount rate under GASB Statement No. 67, which is calculated using the long-term assumed rate of return as one of many inputs, is also highly sensitive to estimates the actuary makes about future contributions and future benefit payments. Given LACERA's funding policy and legal requirements under CERL and PEPR, the actuary determined that projected fiduciary net position to be sufficient compared to projected benefit payments.

Long-term Assumed Rate of Return - OPEB Trust: The actuary has used a 6.66 percent investment return assumption to project the OPEB liability, based on the OPEB Trust fund target asset allocations and market assumptions for those various asset classes.

Single Discount Rate - OPEB Trust: The calculation of the single discount rate under GASB Statement No. 74, which is calculated using the long-term assumed rate of return as one of many inputs, is also highly sensitive to estimates the actuary makes about future anticipated contributions and future benefit payments. Inherent in those assumptions is significant subjectivity surrounding the projection of future contributions. The actuary utilized the Los Angeles County Board of Supervisor's June 2015 meeting materials which establish a multi-year OPEB funding plan in determining anticipated future contributions to the Trust. Based on the actuarial projections, the discount rate within the OPEB Trust was set at 4.69 percent as of June 30, 2017.

OPEB Healthcare Cost Trend Rate: For purposes of projecting future OPEB benefit payments, the actuary utilized a medical cost trend rate assumption ranging from 4.40% to 7.20% based on the Society of Actuaries report entitled "Modeling Long-Term Healthcare Trends" by Professor Thomas E. Getzen.

Mortality Assumptions - Pension and OPEB: The pre- and postretirement mortality assumptions impact the total pension liability related to pensions under GASB 67 and the total OPEB liability related to healthcare under GASB 74. The assumptions about mortality were estimated by the actuary based on the results of an experience study that was performed during 2016 utilizing the actuarial experience of LACERA for the period from July 1, 2013 through June 30, 2016. Based on that experience study, in the 2016 valuation, the actuary has used the RP-2014 tables with the MP-2014 generational improvement scales.

Disclosure of these assumptions and resultant sensitivity of the discount rate can be found in Notes E and N to the financial statements.

Section I - Required Communications with Those Charged With Governance (Continued)

The disclosures in the financial statements are neutral, consistent, and clear. Certain financial statement disclosures are particularly sensitive because of their significance to financial statement users. The most sensitive disclosures affecting the financial statements are the disclosures related to GASB Statement No. 67 and GASB Statement No. 74, including the actuarial valuation results, as well as the GASB No. 72 fair value disclosures.

Difficulties Encountered in Performing the Audit

We encountered no significant difficulties in dealing with management in performing and completing our audit.

Disagreements with Management

For the purpose of this letter, professional standards define a disagreement with management as a financial accounting, reporting, or auditing matter, whether or not resolved to our satisfaction, that could be significant to the financial statements or the auditor's report.

We are pleased to report that no such disagreements arose during the course of our audit.

Corrected and Uncorrected Misstatements

Professional standards require us to accumulate all known and likely misstatements identified during the audit, other than those that are trivial, and communicate them to the appropriate level of management.

We did not detect any misstatements as a result of audit procedures.

Significant Findings or Issues

We generally discuss a variety of matters, including the application of accounting principles and auditing standards, business conditions affecting LACERA, and business plans and strategies that may affect the risks of material misstatement with management each year prior to our retention as LACERA's auditors. However, these discussions occurred in the normal course of our professional relationship and our responses were not a condition of our retention.

Management Representations

We have requested certain representations from management that are included in the management representation letter dated October 12, 2017.

**Section I - Required Communications with Those Charged With Governance
(Continued)**

Management Consultations with Other Independent Accountants

In some cases, management may decide to consult with other accountants about auditing and accounting matters, similar to obtaining a “second opinion” on certain situations. If a consultation involves application of an accounting principle to LACERA’s financial statements or a determination of the type of auditor’s opinion that may be expressed on those statements, our professional standards require the consulting accountant to check with us to determine that the consultant has all the relevant facts. To our knowledge, there were no such consultations with other accountants.

Other Information in Documents Containing Audited Financial Statements

Our responsibility for other information in documents containing the entity’s financial statements and report does not extend beyond the financial statements. We do not have an obligation to determine whether or not such other information is properly stated. However, we read the introductory, investment, actuarial, and statistical sections of the Comprehensive Annual Financial Report (CAFR) and nothing came to our attention that caused us to believe that such information, or its manner of presentation, is materially inconsistent with the information or manner of its presentation appearing in the financial statements.

Section II – Report on Internal Control over Financial Reporting

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

To Management, the Board of Retirement, and Board of Investments
Los Angeles County Employees Retirement Association

We have audited, in accordance with the 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 Los Angeles County Employees Retirement Association (LACERA), which comprise the statement of fiduciary net position as of June 30, 2017 and the related statement of changes in net position for the year then ended, and the related notes to the financial statements, and have issued our report thereon dated October 12, 2017.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered Los Angeles County Employees Retirement Association'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 opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of LACERA's internal control. Accordingly, we do not express an opinion on the effectiveness of LACERA'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 LACERA'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. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

To Management, the Board of Retirement, and Board of Investments
Los Angeles County Employees Retirement Association

Compliance and Other Matters

As part of obtaining reasonable assurance about whether Los Angeles County Employees Retirement Association'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*.

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 LACERA'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 LACERA's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Plante & Moran, PLLC

October 12, 2017

plante moran

**Los Angeles County
Employees Retirement
Association**

Audit Presentation
November 30, 2017



Introductions



Michelle Watterworth, CPA
Partner



Amanda Cronk, CPA
Senior Manager



Agenda

- ✓ Audit timeline
- ✓ Audit areas of focus
- ✓ Results of the audit
 - ✓ Audit opinion letter
 - ✓ Required communications
- ✓ Upcoming pronouncements
- ✓ Questions



Audit timeline

Our involvement began immediately upon contract inception.

- January 2017 – Began involvement on the GASB 74/75 task force
- January 2017 – Initial audit planning discussion with LACERA team to begin planning for the audit
- February/March 2017 – Initiated planning procedures
- May/June 2017 – Performed interim procedures, including on-site visit and testing
- July/August 2017 – Performed additional planning and audit procedures remotely
- September/October 2017 – On-site testing and review of financial statements
- October 12, 2017 – Timely issuance of audit opinion



Audit areas of focus

The ultimate goal of the audit is the expression of an opinion on your financial statements.

- Implementation of GASB 74
- Investment valuations
- Census data testing, particularly at the County level
- Actuarial assumptions and actuarial calculations
- Accuracy of benefit calculations and related payments, including disability payments
- Financial reporting



Results of the audit

Opinion

In our opinion, the basic financial statements referred to above present fairly, in all material respects, the fiduciary net position of the Los Angeles County Employees Retirement Association as of June 30, 2017, and the changes in fiduciary net position, thereof for the year then ended, in accordance with accounting principles generally accepted in the United States of America.

- ✓ Unmodified Opinion
- ✓ Emphasis of Matter
 - ✓ Valuation of Harder to Value Investments
 - ✓ GASB Statement No. 74 adoption



Results of the audit

Required Communication with Those Charged With Governance

- GASB 74 was adopted during the current year
- Management estimates included within the financial statements
 - Harder to value investments – based upon information obtained from various sources
 - Actuarial assumptions
 - Long-term expected rate of return and discount rate (Pension Plan and OPEB Trust)
 - Mortality assumptions (Pension Plan and OPEB Trust)
 - Healthcare cost trend rate (OPEB Trust)
- No difficulties or disagreements with management in performing the audit
- No corrected or uncorrected misstatements



Upcoming pronouncements

Below is a timeline of upcoming pronouncements that will impact LACERA (or its employers):

- GASB Statement No. 75 – *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions* - Employers will be required to implement in 2018
 - LACERA will be expected to provide reporting required by the employers to comply with this standard
- GASB Statement No. 87 – Leases – LACERA will be required to implement during the 6/30/21 fiscal year.
 - This Statement will require recognition of certain lease assets and liabilities for leases that previously were classified as operating leases



Questions?



Thank you!

For more information contact:

Michelle Watterworth, CPA

248-223-3520

Michelle.Watterworth@plantemoran.com

Amanda Cronk, CPA

810-766-6045

Amanda.Cronk@plantemoran.com

Testing of Plan Sponsor Pay Codes

November 30, 2017

Introduction

Following the Public Employees' Pension Reform Act of 2013 (PEPRA), LACERA's Board of Retirement ("BOR") became responsible for determining whether the components of a member's compensation is pensionable or non-pensionable while working as an active employee

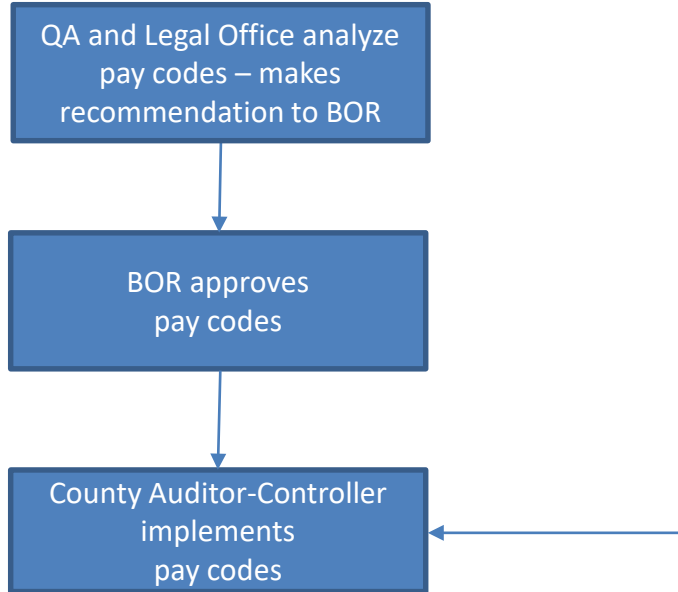
- To date, the BOR has made a determination on over 800 County pay codes
- It is CRITICAL that the County correctly implements each pay code according to the BOR's determination to ensure:
 - Compliance with PEPRA
 - Employee and employer contributions are accurate
 - Census data is accurate

Why are we testing pay codes?

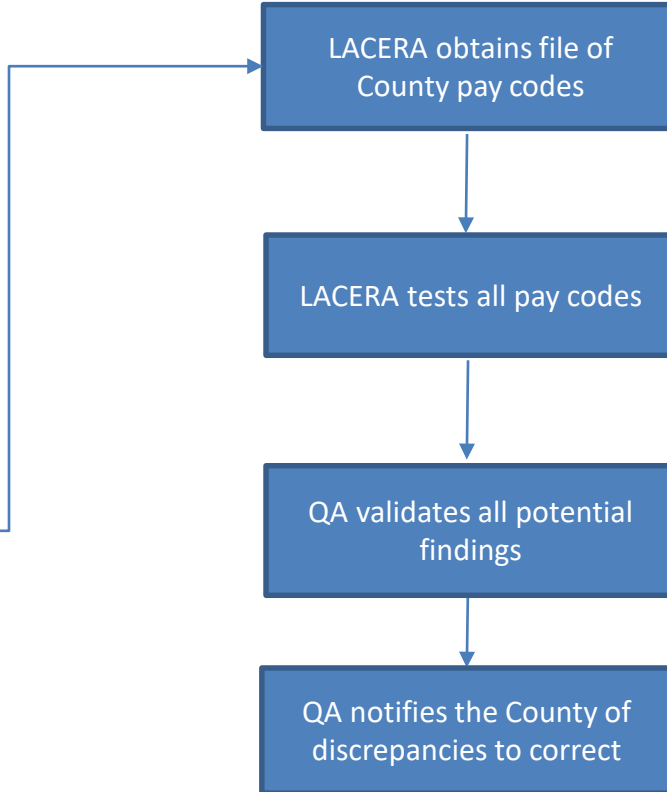
- ▶ **To prevent employer and employee contribution funding errors**
 - ▶ The County collects (or does not collect) contributions from each employee's pay component ("pay code") depending on the determination of its pensionability
 - ▶ If errors occur, LACERA would need to correct under and/or over-paid contributions to members and the plan sponsor

- ▶ **Verify the accuracy of census data (AICPA requirement)**
 - ▶ Accurate census data ensures that LACERA's actuary is provided good data for projecting LACERA's pension and healthcare benefit obligations

Pay Code Implementation Process:



Pay Code Testing Process:



Testing Intervals:

- ▶ Pay codes – quarterly
 - ▶ Divisions involved – Internal Audit, Quality Assurance, Benefits, and the Systems Division

- ▶ Census data – annually
 - ▶ Divisions involved – Internal Audit and Quality Assurance

Questions?

2018

Audit Plan Status Report

FYE 2018 Plan Status as of October 31, 2017

Submitted to the Audit Committee
November 30, 2017

In This Report

WORK COMPLETED & IN PROGRESS.....	3
ONGOING TESTING, MONITORING & CONSULTING.....	11



Los Angeles County Employees Retirement Association

AUDIT COMMITTEE

of the Board of Retirement & Board of Investments

Joseph Kelly – Chair

Michael S. Schneider – Vice Chair

Vivian Gray – Secretary

David Green

Shawn R. Kehoe

INTERNAL AUDIT DIVISION

Richard Bendall, CPA, CISA Chief Audit Executive

Leisha Collins, CPA Principal Internal Auditor

Quoc Nguyen, CPA, CFA Principal Internal Auditor

Christina Logan, CPA, CFE Senior Internal Auditor

George Lunde, CIA, CISA Senior Internal Auditor

Kathryn Ton, CPA, CFE Senior Internal Auditor

Gabriel Tafoya, CISA, ACDA Senior Internal Auditor

Nathan Amick Internal Auditor

Darla Vidger, MPA, CIA Internal Auditor

DeMetria Washington Senior Secretary

AUDIT COMMITTEE CONSULTANT

Rick Wentzel, CPA

EXECUTIVE SUMMARY

On behalf of the Internal Audit team, I am pleased to submit the **Internal Audit Work-In-Progress Report (Report)** of the Los Angeles County Employees Retirement Association (*LACERA*) for the period of July 1, 2017 to October 31, 2017. This Report provides information on the FYE 2018 Audit Plan, the assurance, consulting, and advisory projects completed as well as other Internal Audit activities.

The work performed by LACERA Internal Audit contributes toward accountability, integrity, and good management practices throughout LACERA's business units.

As of July 1, 2017, the FYE 2018 Audit Plan consisted of thirty-seven (37) projects. As the year progressed one (1) additional/unplanned projects was added to the Audit Plan, for a total of thirty-eight (38) audit projects for the FYE 2018 Audit Plan. Of the thirty-eight (38) total projects on the current Audit Plan, nineteen (19) projects have been initiated during the year with three (3) completed and sixteen (16) in various stages of progress toward completion.

The attached report contains the status on all projects undertaken this fiscal year including the objective of the project, the rationale for the work, and a brief synopsis on the "progress" or "conclusion" of each project. We also include the justification for initiating each of the unplanned projects. Any reports issued during the period since your last Audit Committee meeting are provided to your Committee under separate cover.

I would like to thank the Committee for your continued support of Internal Audit.

Sincerely,

A handwritten signature in blue ink, appearing to read 'Richard Bendall', written in a cursive style.

Richard Bendall, CPA, CISA
Chief Audit Executive

INTERNAL AUDIT PLAN FYE 2018

The following table provides a list of the planned Internal Audit projects for the **Fiscal Year End 2018**.

INTERNAL AUDIT PLAN FYE 2018		TOTAL HOURS: 10,600	
MANAGEMENT, GOVERNANCE & COMPLIANCE		EST. HOURS: 3,800	
PROJECT	TYPE	FREQUENCY	
1. Continuous Auditing Program	Audit	Ongoing	
• New Payee Validation	Audit	Periodic	
2. Contract Compliance Program - Administration	Audit	Planned	
3. Internal Controls Training	Consulting	Planned	
4. Privacy Training	Consulting	Planned	
5. Los Angeles County Rehired Retirees Audit (960 Hours Testing)	Audit	Periodic	
6. Pensionable Paycode Testing	Audit	Periodic	
7. Felony Convictions Plan Sponsor Reporting	Audit	Periodic	
8. Corporate Credit Card Audit	Audit	Planned	
9. Board and Staff Travel	Audit	Planned	
10. Inventory Controls	Audit	Planned	
11. Quality Assurance Improvement Program FYE 2018	Admin	Periodic	
12. Risk Assessment – FYE 2019	Admin	Annual	
13. County Medical Reimbursements	Audit	Planned	
14. Internal Audit Contractor Pool – RFP	RFP	Planned	
15. Compliance Committee	Consulting	Planned	
16. Privacy Audit Recommendation Monitoring	Consulting	Planned	
BENEFITS ADMINISTRATION		EST. HOURS: 2,000	
17. Benefits' Process Management Group	Consulting	Planned	
18. Benefits' Exception Report Review Process	Audit	Planned	
19. Active Death Process	Audit	Planned	
20. Member Death Verification Process	Audit	Planned	
21. New Benefits Tier Plan	Audit	Planned	
22. Member Accounts Settlements Process	Audit	Planned	
23. Physician Selection and Compensation	Audit	Planned	
INFORMATION SYSTEMS		EST. HOURS: 2,000	
24. Business Continuity/Disaster Recovery	Consulting	Planned	
25. Data Backup/Retention Testing	Audit	Planned	
26. Member Applications Change Control	Audit	Planned	
27. Systems Penetration Testing	External Audit	Periodic	
28. IT Risk Assessment	External Audit	Planned	
FINANCIAL & INVESTMENT OPERATIONS		EST. HOURS: 2,800	
29. External Financial Audit - Oversight	External Audit	Annual	
30. Actuarial Audit - Oversight	External Audit	Annual	
31. Foreign Tax Reclamation - Oversight	External Audit	Planned	
32. Wire Transfers Audit	Audit	Planned	
33. Real Estate Investment Operations	External Audit	Planned	
34. Real Estate Advisor Audits	External Audit	Periodic	
35. Securities Lending	Audit	Planned	
36. Real Estate Debt Program Review	External Audit	Planned	
37. Custodial Bank Review	Audit	Planned	
ADDITIONAL/UNPLANNED PROJECTS			
38. THC Financial Audit Oversight	External Audit	Unplanned	



In Progress



Completed

*FYE 2017 Project Rolled Over to Current Year

The following provides a more detailed narrative of both the planned and unplanned Internal Audit projects completed or in progress for the period of July 1, 2017 to October 31, 2017. The projects are ordered by Division. Project detail includes the objective, rationale, and a brief synopsis of the project’s conclusion or status as of October 31, 2017.

ADMINISTRATIVE SERVICES

Business Continuity Planning

DIVISION(S)	ADMINISTRATIVE SERVICES	REPORT DATE	TBD
OBJECTIVE	Provide consulting to Administrative Services management in their revision and upgrade of LACERA’s business continuity plan including: <ol style="list-style-type: none"> 1. Business impact analysis <ol style="list-style-type: none"> a. processes that are critical and order of importance b. recovery time objectives c. recovery point objectives 2. Develop crisis management plan roles and responsibilities 		
RATIONALE	Internal Audit is required to review the effectiveness of management's system of compliance with laws, regulations, policies and procedures that are business critical. The Business Continuity Plan is critical to the continuation of LACERA in the event of a disaster. Rather than perform an audit of the current plan, we determined together with the Executive Office and Administrative Services Management that it would be more appropriate for Administrative Services to engage a consultant to evaluate and possibly upgrade the current Business Continuity platform. This will include improving board and staff awareness of the plan as well as training LACERA staff on the plan and its deployment in the event of a disaster.		
PROGRESS	Internal Audit is participating in a cross-functional oversight committee made up of Executive Office, Legal, Systems Division, and Administrative Services Division staff, regarding the hiring of a Business Continuity Planning vendor.		

BENEFITS

Member Death Verification Process

DIVISION(S)	BENEFITS - BENEFITS PROTECTION UNIT (BPU)	REPORT DATE	OCT 31, 2017
OBJECTIVE	<p>To review the member death verification process and assess the following:</p> <ul style="list-style-type: none"> • The adequacy of the process's design • Internal controls related to the member death verification process • If any other process and/or technology is available but is not being used by staff that would improve the process of proactively detecting deceased members • Whether staff properly follows-up on weekly death reconciliation reports from the “death verification vendor” (DVC) • Whether staff properly follows-up on weekly death reconciliation reports from the “death verification vendor” (DVC) 		
RATIONALE	<p>The audit is part of our fiscal year 2016-2017 audit plan, added as a result of our risk assessment. The Benefits Protection Unit (BPU) was created within the Benefits Division back in January 2016 to coordinate LACERA's efforts in the detection, prevention, and reduction of payments to deceased members.</p> <p>The BPU works with a third party vendor (DVC) to assist LACERA in detecting member deaths as timely as possible. This process is important for preventing benefit overpayments. Without timely notifications or identification, payments to deceased members can potentially go on for months or years before being detected.</p>		
CONCLUSION	<p>Internal Audit found that LACERA’s member death verification process is designed effectively to proactively detect unreported deaths and assist with preventing overpayments. We noted the following positive observations:</p> <ul style="list-style-type: none"> • BPU's written procedures are comprehensive and adequately walk users through the member death verification process. • BPU has a similar or more comprehensive process than other public pension funds we surveyed and reached out to. • There were no known third party products or available technologies that provided more death search capability than what LACERA is already employing. • For all 50 vendor death notifications tested, BPU followed-up timely and placed a payment hold on the member’s account if the member was verified as deceased, which prevented the possibility of overpayments. <p>However, we noted an opportunity for management to strengthen their vendor monitoring controls. We noted that the Benefits Division, as the contract owner, was not monitoring the vendor’s data security controls over LACERA’s member data. We recommend that the Benefits Division develop an on-going process to ensure that the death verification contractor has adequate controls for securing, safeguarding, and ensuring the confidentiality of LACERA's member data.</p> <ul style="list-style-type: none"> • We also noted an opportunity for management to strengthen a low risk part of the process, specifically in the rare instances where BPU staff has inconclusive evidence on whether the member is alive or deceased and cannot make contact with the member. In these instances, management should consider placing payment holds on the member’s account and request that the member contact LACERA to be verified before continuing the monthly benefit. 		

BENEFITS

Benefits' Process Management Group

DIVISION(S)	BENEFITS	REPORT DATE	N/A
OBJECTIVE	Assess the internal control structure and process design of the Policy and Procedure development process.		
RATIONALE	<p>The purpose of the Program Management Group (PMG) audit was to assess the Benefits administration's set of policies and procedures in order to do the following:</p> <ul style="list-style-type: none"> • Determine whether PMG's policies and procedures can be implemented across all divisions and if so, • Expand on PMG's efforts to develop an organization-wide set of policies and procedures. <p>Currently LACERA follows a best practice performance metric rather than a formal, documented set of standards.</p>		
PROGRESS	<p>LACERA has established a cross-divisional team to create organization-wide policies and procedures. The compliance committee and sub-committee ("Policy on Policies") were created based on one of Alston & Bird's recommendations from the 2016 Privacy Audit. The committees are led by LACERA's Chief Counsel, and have established deliverables by calendar year-end. The Policies on Policies Committee will present the newly created policies and procedures to the Joint Organizational Governance Committee for review and approval. Because management has already moved forward with the establishment of policies and procedures, Internal Audit did not perform this audit and will not roll forward this audit for FY18.</p>		

Member Accounts Settlements Process

DIVISION(S)	BENEFITS	REPORT DATE	TBD
OBJECTIVE	The purpose of the Member Account Settlements Process audit is to assess internal controls and design of the process of recovering payments that members owe to the LACERA fund resulting from members underpaying their contributions to LACERA or LACERA overpaying benefits to members.		
RATIONALE	As part of our fiscal year 2017-18 Audit Plan and based on a request from Management to follow-up on a previous review, Internal Audit is performing a review of LACERA's Member Account Settlements Process (to ensure that collections are initiated from members within the statute of limitations).		
PROGRESS	Internal Audit is currently performing the initial planning for this Audit. We estimate completing the audit and issuing a report to your Committee by your March 2018 meeting.		

BENEFITS

Los Angeles County Rehired Retirees Audit (PEPRA 960 Hours Testing FYE 2017)

DIVISION(S)	EXECUTIVE OFFICE	REPORT DATE	OCT 31, 2017
OBJECTIVE	<p>To determine whether all retirees temporarily rehired, were done so in compliance with State and federal laws and LACERA policies.</p> <p>The State of California’s County Employees Retirement Law provides that Los Angeles County has the option to re-employ retirees for up to 120 days (960 hours) per fiscal year, on a strictly temporary basis, without affecting their retirement status or benefits. Additionally, the Public Employees Pension Reform Act of 2013 and LACERA policy requires a bona fide break in service prior to the retiree being rehired by the County.</p>		
RATIONALE	<p>Compliance with State law and LACERA policy helps ensure that LACERA retains its “qualified” tax deferred status. As this is a critical risk to LACERA, Internal Audit performs a 100 percent compliance test of all rehired retirees employed by the County each year.</p>		
CONCLUSION	<p>Internal Audit determined that for the Fiscal Year Ended June 30, 2017 there were some minor issues of non-compliance with legal requirements and LACERA policies. These issues were reported to the County's Chief Executive Office - Benefits, Compensation Policy, and Employee Relations Division and they are in the process of implementing workable solutions to mitigate these issues in the future.</p>		

EXECUTIVE OFFICE

Compliance Committee

DIVISION(S)	EXECUTIVE OFFICE	REPORT DATE	N/A
OBJECTIVE	<p>Provide consulting to the Executive Office and participate in the Compliance Committee in their development of a framework for a formal compliance program at LACERA.</p>		
RATIONALE	<p>Internal Audit has been requested by the Executive Office to assist with the development of a framework managements system of compliance. As part of the updates to the Audit Committee Charter, the Audit Committee will have responsibility for monitoring managements system of compliance</p>		
PROGRESS	<p>Internal Audit is continuing to meet and consult with Management and participate with the Compliance Committee on the development of the formal compliance program.</p>		

EXECUTIVE OFFICE

Pensionable Paycode Testing

DIVISION(S)	INTERNAL AUDIT, QUALITY ASSURANCE, BENEFITS, SYSTEMS DIVISION	REPORT DATE	N/A
OBJECTIVES	<ul style="list-style-type: none"> Verify that the pay codes used by the Plan Sponsor are codes that have been approved by the Board of Retirement. The Plan Sponsor should not be using a code that has not been determined by the Board of Retirement as either pensionable or non-pensionable. Verify that each pay code used is coded correctly by the Plan Sponsor (e.g., either “yes” as pensionable or “no” as non-pensionable) Verify, on a sample basis, that pay codes used by the County are applied to the correct group and/or sub-group of employees (e.g., pay codes intended for Sheriff’s deputies should only be used for Sheriff’s deputies) 		
RATIONALE	<p>In accordance with the Public Employees’ Pension Reform Act of 2013 (“PEPRA”), LACERA’s Board of Retirement (“BOR”) became responsible for determining whether the components of a member’s compensation are pensionable or non-pensionable while working as an active employee after 1/1/13. To date, the BOR has made a determination on over 800 County pay codes. Once these earnings pay codes are approved by the BOR, they are implemented by the Auditor-Controller and paid accordingly for eligible employees.</p> <p>It is critical that the County correctly implements each pay code according to the BOR’s determination to ensure compliance with PEPRA, employee and employer contributions are accurate, and census data is accurate.</p> <p>LACERA has developed a testing process for verifying that the pay codes used by the County Auditor-Controller are valid pay codes and coded correctly based on the determination of LACERA’s Board of Retirement.</p>		
PROGRESS	Internal Audit (IA) is currently testing pay codes and will provide any errors to QA for analysis and follow-up. IA will continue to test pay codes on a quarterly and annual interval.		

FINANCIAL AND ACCOUNTING SERVICES

FYE 2018 Actuarial Audit - Oversight

DIVISION(S)	FASD	REPORT DATE	N/A
OBJECTIVE	Facilitate LACERA's ongoing, external, audit of actuarial services.		
RATIONALE	External auditors require information data and documentation; also advice, direction, assistance; and with regard to inquiries, timely responsiveness from LACERA staff and management in order to complete their work satisfactorily in a suitable fashion.		
PROGRESS	Milliman and Segal have completed 2017 actuarial services. This is an ongoing project that will conclude June 30, 2018.		

HUMAN RESOURCES

LACERA Annual Financial Audit Facilitation – FYE 2017

DIVISION(S)	FASD	MEMO DATED	OCT 12, 2017
OBJECTIVE	Facilitate LACERA’s annual external financial statement audit for FYE 2017.		
RATIONALE	Internal Audit facilitates the External Audit by coordinating meetings with the Divisions, obtaining and facilitating information, data, and documentation exchanges, and ensuring timely responsiveness from LACERA management and staff concerning the timely completion of the external auditors work.		
PROGRESS	Plante Moran, LACERA’s new external auditor, completed its final fieldwork and issued its timely (1) opinion on LACERA’s 2017 financial statements and (2) “Management Letters” to LACERA. Plante Moran will formally present the results of its work during the November 30, 2017 meeting. The 2017 CAFR should be issued by LACERA in January 2018.		

INTERNAL AUDIT

Internal Audit Consultant Pool RFP (Real Estate Advisor Audits & Real Estate Debt Program Review)

DIVISION(S)	INTERNAL AUDIT	MEMO DATE	TBD
OBJECTIVE	Internal Audit will issue an RFP to hire a pool of audit consultants to perform audits of LACERA Real Estate Advisors and LACERA’s Real Estate Debt Program.		
RATIONALE	Internal Audit will use the consultants on an as needed basis to ensure appropriate resources are available to complete audits and projects included in the Audit Plan.		
PROGRESS	Staff anticipates issuing the RFP by November 30, 2017. In addition, to select, find and initiate contracts with most consultants by January 31, 2018.		

INVESTMENTS

Foreign Tax Reclamation RFP & Audit Oversight

DIVISION(S)	INVESTMENTS DIVISION	REPORT DATE	N/A
OBJECTIVE	Issue an RFP for foreign tax reclamation audit services.		
RATIONALE	The Board of Investments directed Staff to issue a Request for Proposals (RFP) for a firm to audit LACERA’s tax reclaim process, managed by State Street Bank, LACERA’s custodian, to verify that LACERA has reclaimed all foreign tax withholdings to which it is entitled.		
PROGRESS	The Board of Investments will interview two finalist firms at the December 2017 Board of Investments meeting for selection.		

INVESTMENTS

THC Financial Audit Oversight

DIVISION(S)	INVESTMENTS	REPORT DATE	N/A
ADDITIONAL PROJECT JUSTIFICATION	The audit project was initially included on the FY 2018 Audit Plan in the External Financial Oversight project, however, the CAE decided to track separately this project due to the significance of the project and extensive work that will be done by staff.		
OBJECTIVE	The objectives of this project are to hire firms to perform audit and tax services associated with LACERA’s wholly owned THCs. Staff will also oversee the THC audits to ensure that audits and financial reports are provided within established guidelines.		
RATIONALE	The purpose of the THC audit is to ensure that real estate advisors are providing accurate and appropriate financial reports to LACERA. IA serves as liaison between the audit firms and the key stakeholders: FASD, the Investment Office and the Legal Division to ensure that the audits comply with established procedures and financial reports are provided within established periods.		
PROGRESS	Staff plan to issue the RFP for the selection of audit firms by March 2018. The audits and oversight of the audits will begin in May 2018		

RETIREE HEALTH CARE

DIVISION(S)	RETIREE HEALTH CARE	REPORT DATE	TBD
OBJECTIVE	Assess the adequacy and effectiveness of controls for paying the monthly healthcare premiums to the insurance carriers for the LACERA-administered plans as well as the timely and accurate billing to the plan sponsor for its portion of the premium.		
RATIONALE	<p>These areas have not been reviewed by Internal Audit, and are included in the audit plan for fiscal year 2017-2018.</p> <p>LACERA administers the Retiree Healthcare Benefits Program for Los Angeles County, and subsidizes nearly \$575 million per year, or \$48 million per month in medical and dental/vision, Medicare Part B, and death benefits for retired members/survivors and eligible dependents enrolled in a LACERA-administered healthcare plan.</p>		
PROGRESS	Staff is performing fieldwork, and anticipates finalizing the report by December 4, 2017.		

SYSTEMS

Data Backup & Retention

DIVISION(S)	SYSTEMS	REPORT DATE	TBD
OBJECTIVE	To determine whether the retention period for audit records and logs complies with applicable good practice guidance, and also, to assess written policies and procedures for backing up and transporting files. Further, to review the contingency plan including the priority of service provisions.		
RATIONALE	Internal Audit has identified this as a key risk area. In order to minimize the probability and impact on key business functions and processes of a major Systems service interruption there is a need to ensure Systems management of backup arrangements and availability of business-critical information are adequately in effect. Systems, applications, data, and documentation all need to be backed up according to a defined schedule, considering Data types (e.g., voice, optical), Critical end-user computing data (e.g., spreadsheets), Physical and logical location of data sources, Security and access rights, and Encryption.		
PROGRESS	Work is in process and Internal Audit expects to bring the final report to your Committee at your March 2018 meeting.		

Systems Penetration Testing

DIVISION(S)	SYSTEMS	REPORT DATE	TBD
OBJECTIVE	To evaluate the controls preventing vulnerabilities on the internet accessible Web Portal which could be used to gain access to the LACERA internal network, view sensitive LACERA data, or potentially corrupt data that legitimate users may access. To determine if good practice standards and program code conventions are in effect for portal access authentication and authorization code.		
RATIONALE	Prior reviews have found network and application environments exhibit many strong security practices that provided a very robust security framework. However, to ensure the protection of access to LACERA and member data, best practice is to perform periodic IT security and penetration testing.		
PROGRESS	Fieldwork and testing a. Draft comments are under review validation. A December 30, 2017 completion date is anticipated.		

Information Technology Risk Assessment Consultant RFP

DIVISION(S)	SYSTEMS	REPORT DATE	TBD
OBJECTIVE	Internal Audit will issue a Request-For-Proposal (RFP) to select firm to conduct a Risk Assessment of the entire information technology operations area consisting of policy review, data security, and risk exposure in order to establish a baseline of opportunities for improvement.		
RATIONALE	Best Practice to address IT risk.		
PROGRESS	The RFP is in the development process stage. Several IT audit firms have expressed interest in providing services. We anticipate issuance of the RFP by January 31, 2018.		

ONGOING TESTING, MONITORING & CONSULTING

The following provides a brief narrative of ongoing Internal Audit projects for the period of July 1, 2017 to October 31, 2017. These recurring projects include testing, monitoring, and consulting assignments performed on an ongoing basis to prevent fraud and ensure compliance throughout LACERA’s business units. Project detail includes the objective, rationale, and a brief synopsis of the project’s status.

BENEFITS

New Payee Validation Continued Process Test (CPT)

DIVISION(S)	BENEFITS
OBJECTIVE	To assess validity of new payees added to the retirement payroll, Internal Audit performs an independent monthly continuous process test of scheduled benefit payments to new service and disability retirees and also new survivor payees. <ul style="list-style-type: none"> • Internal Audit staff confirm by reviewing supporting file documentation that new payments added to the retiree payroll are only to eligible former Los Angeles County employees or their beneficiaries. • Internal Audit examines 100% of the new benefit payees using computer assisted audit techniques.
RATIONALE	Internal Audit performs this monthly fraud test due to our independence from the operations.
PROGRESS	Internal Audit has tested 100 percent of all new benefit payees from July 2017 through October 2017. This an ongoing monitoring that will conclude June 30, 2018. No exceptions have been noted to date in our testing this year.

EXECUTIVE OFFICE

Privacy Audit Recommendation Monitoring

DIVISION(S)	EXECUTIVE OFFICE
OBJECTIVE	Internal Audit will participate in the cross-functional management oversight team and record the status of the implementation of recommendations in the external Privacy Audit final report.
RATIONALE	Internal Audit has an independent oversight role in validating the implementation of audit recommendations. Due to the attorney-client privilege manner in which the audit was performed and reported to the Audit Committee, Internal Audit performs this role and reports on the status of implementation to your Committee separately.
PROGRESS	<p>Executive Management has established a cross-functional team to address the implementation of the Privacy Audit recommendations, many of which will simultaneously assist in the formalization of the compliance function at LACERA. The team will coordinate the implementation and the standardization of policies and procedures and the establishment of a compliance framework. The team has identified specific divisions as the primary owners of the Privacy Audit recommendations.</p> <p>Internal Audit as a part of the team is working on those recommendations for which we have primary ownership. Internal Audit also records the status update of all recommendations and we are comfortable that Management is taking the recommendations and the implementation very seriously and has developed a good plan and a reasonable timeline in which to do so. We will be reporting the status of the Privacy Audit recommendation follow-up to your Committee at your November 30, 2017 meeting, under separate cover.</p>

Privacy Training

DIVISION(S)	EXECUTIVE OFFICE
OBJECTIVE	Internal Audit will review and revise LACERA’s Privacy Training to include new sections on Security and the Clean Desk Policy.
RATIONALE	Due to recent changes in policies and procedures related to security and privacy, LACERA will be updating its Privacy Training for all staff and new hires.
PROGRESS	Internal Audit is currently updating the Privacy Training. Once the new security and privacy policies are approved, Internal Audit will finalize the training to be delivered to staff in early 2018.

INTERNAL AUDIT**Recommendation Follow-up**

DIVISION(S)	INTERNAL AUDIT
OBJECTIVE	In compliance with the Institute of Internal Auditors' <i>International Professional Practices Framework</i> , the Chief Audit Executive must establish and maintain a system to monitor the disposition of audit results communicated to management.
RATIONALE	Internal Audit monitors the implementation status of prior audit recommendations made to LACERA Management to ensure that Management action plans have been effectively implemented or that Senior and Executive Management have accepted the risk of not taking action.
PROGRESS	The status of all, audit recommendation related, management action plans are reported to the Audit Committee regularly. The most recent review cycle was completed from July 1, 2017 through October 31, 2017. Project will continue through the Fiscal Year end of June 30, 2018.

Board and Committee Monitoring

DIVISION(S)	INTERNAL AUDIT
OBJECTIVE	To monitor all LACERA board and committee meetings, to stay abreast of board concerns and or identify emerging risks.
RATIONALE	Internal Audit's scope of work includes the monitoring of LACERA's network of risk management, control, and governance processes.
PROGRESS	Ongoing

General Consulting (< 2 hours)


DIVISION(S)	INTERNAL AUDIT
OBJECTIVE	Assist LACERA Management with advice and/or resources.
RATIONALE	Internal Audit is often consulted for advice or additional information on organizational processes, projects, and issues. Any consulting project requiring two hours or less of an auditor's time is placed in this category. Consulting projects requiring an excess of two hours are typically documented and reported as individual projects. The 289 hours spent this fiscal year to date, represents auditors providing consulting/advice in many different areas on various topics.
PROGRESS	Internal Audit maintains an open door policy for general consulting purposes. This is ongoing consulting that will conclude June 30, 2018.




October 31, 2017

TO: Each Member
2017 Audit Committee Members

Audit Committee Consultant
Rick Wentzel

FROM: Quoc Nguyen 
Principal Internal Auditor

Gabriel Tafoya 
Senior Internal Auditor

FOR: November 30, 2017 | Audit Committee Meeting

SUBJECT: **RECOMMENDATION FOLLOW-UP REPORT**

AUDIT RECOMMENDATION IMPLEMENTATION SUMMARY

From July 1, 2017 through October 31, 2017, the following audit recommendation activity occurred:

- Three (3) new recommendations were made during this reporting period. These recommendations resulted from the Member Death Verification Process audit.
- Two (2) recommendations were implemented:
 - One (1) was implemented by FASD.
 - One (1) was implemented by Investments.

A summary report containing the relevant audit recommendations for each Division can be found in **Attachment A**.

AUDIT RECOMMENDATIONS STATUS
 July 1, 2017 – October 31, 2017

Division	New Recommendations	Implemented/ Closed	Management Accepts Risk	Pending
Administrative Services:				6
Benefits Division:	3			10
Communications:				
Disability Litigation:				
Disability Retirement:				
Executive-Org. level:				
FASD:		1		
Human Resources:				
Internal Audit:				
Investments:		1		7
Legal:				
Member Services:				
Quality Assurance:				
Retiree Health Care:				2
Systems:				
Actuary:				
Total:	3	2	0	25

AUDIT RECOMMENDATIONS AGING REPORT

Internal Audit included an aging report to provide additional transparency into the amount of time it takes LACERA to fully implement audit recommendations. Audit recommendations made to address higher risk issues are most often implemented immediately or certainly within the first year whenever possible. As requested by the Audit Committee, Internal Audit has also included a status from Management for those recommendations that have been outstanding for longer than two years (see page 5).

To better understand any particular number, please refer to **Attachment A** and review the **Implemented** and **Pending** recommendations. Significantly more detail can be made available on each recommendation. Should you require such additional information, please contact me (qnguyen@lacera.com) or Mr. Bendall (rbendall@lacera.com) and we will be pleased to assist you.

BACKGROUND

The Institute of Internal Auditors' (IIA) Performance Standard #2500 pertains to monitoring the implementation progress of Internal Audit's recommendations made to Management. To be in compliance with the IIA Performance Standards, the Chief Audit Executive is required to establish and maintain a system to monitor the disposition of Management's corrective results and communicate those results to Executive Management.

During the audit process, Internal Audit, as well as external auditors (financial, fiduciary, actuarial, and IT), regularly identify areas where LACERA Management may implement changes to improve risk controls in its processes and Management provides action plans indicating how and when planned improvements will be made. These recommendations and action plans are included in each formal audit report. Additionally, Internal Audit makes recommendations and management identifies improvement plans during Internal Audit consulting assignments. All recommendations and management action plans are documented in Internal Audit's *Recommendation Follow-Up* database for tracking, monitoring, and follow-up reporting.

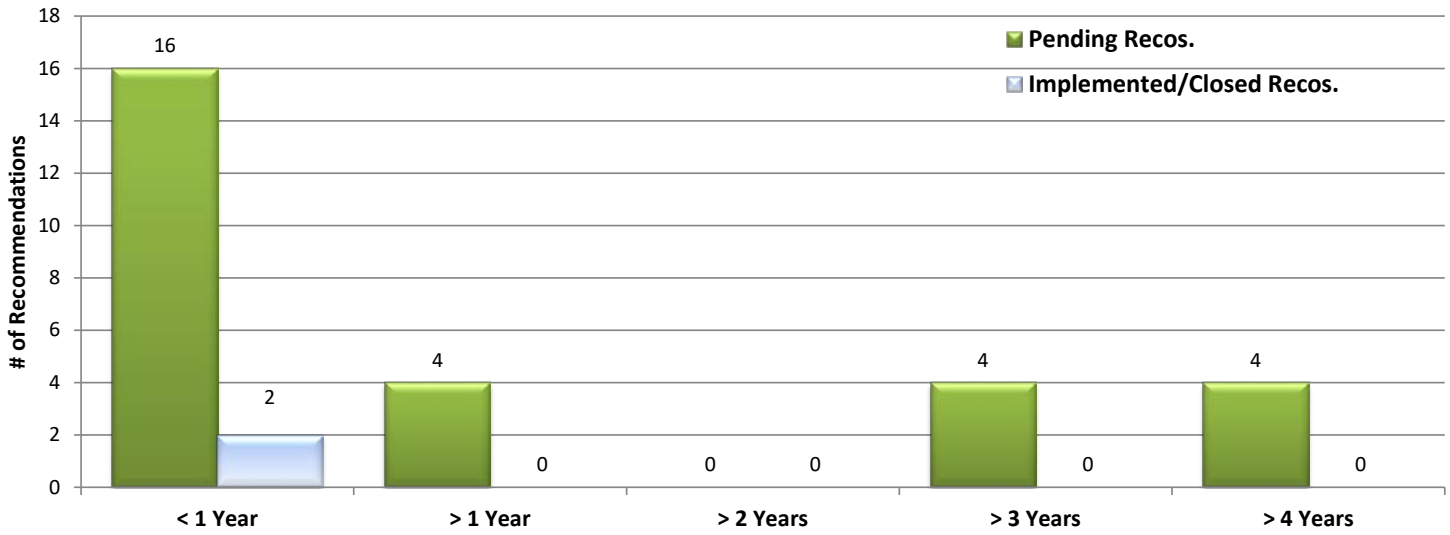
It is Internal Audit's responsibility to ensure that Management's action plans have been effectively implemented, or in the case of action plans that have yet to be implemented, to ensure that Management remains aware of the risks it has accepted by not taking action. In certain situations, if reported observations and recommendations are significant enough to require immediate action by Management, Internal Audit persistently monitors actions taken by Management until the observed risk is corrected and the recommendation implemented.

It is not the responsibility of the Chief Audit Executive to resolve the risks identified during audit work. However, in accordance with IIA Performance Standard #2600, it is Internal Audit's responsibility to communicate the acceptance of risks when the Chief Audit Executive concludes that Management has accepted a level of risk that may be unacceptable to the organization. As a result of this responsibility, Internal Audit communicates all pending *Management Action Plans* to LACERA's Executive Management for resolution. In this manner, Internal Audit escalates unsatisfactory responses or lack of Management actions - including the assumption of risk - to the appropriate levels of Executive Management.

QN/gt

Audit Recommendation Aged Report

July 1, 2017 through October 31, 2017



Pending Recos.	< 1 Year	> 1 Year	> 2 Years	> 3 Years	> 4 Years
Administrative Services	3				3
Benefits Division	6	2		4	1
FASD					
Human Resources					
Internal Audit					
Investments	5	2			
Legal					
Systems Division					
Retiree Healthcare	2				
Pending Total:	16	4	0	4	4

Implemented/Closed Recos.	< 1 Year	> 1 Year	> 2 Years	> 3 Years	> 4 Years
Administrative Services					
Benefits Division					
FASD	1				
Human Resources					
Internal Audit					
Investments	1				
Legal					
Systems Division					
Retiree Healthcare					
Implemented/Closed Total:	2	0	0	0	0

Status of Recommendations Outstanding For More Than Two Years

Division	Issue	Recommendation	Aging (years)	Revised Est. Implementation	Current status of implementation (Management's response)
Admin Services	Greater clarity & expansion needed in Purchasing Policy & the related Admin Manual	Admin Services Division should modify & expand both the Purchasing Policy and the related Admin Manual	5	1/5/2018	A policy draft was completed and presented to the Executive Office and key managers for review. The policy was not accepted and returned to staff for additional work. The additional development work was delayed due to staff being on approved leave. However, the recent appointment of an interim Division Manager will allow Admin Services to complete a revised draft for presentation to the Executive Office and key management staff within the next 90 days.
	Daily operating procedures ("desk procedures") need enhancement re control procedures	Procurement Unit should update & expand its written, daily operating procedures	5	1/5/2018	The desk procedure manual will be revised once the Board has adopted the new policy. We estimate the development of desk procedures will take an additional 90-180 days from the date the policy is approved. This includes development of the desk procedures, appropriate training for procurement staff, and training for management staff.
	"Sole-source" or bidding documentation not found	(1) Promulgate requirements to other Divisions (2) Update desk procedures & (3) Contact FASD & agree upon document retention	5	1/5/2018	The sole-sourcing documentation and process was completed and the requirements provided to other divisions via the LACERA Intranet. The documents are retained in Administrative Services Procurement by scanning all purchasing packages and housed on network.
Benefits	1st Payment - Separation of Duties	Implement secondary review	4	6/30/2018	The action plan for this recommendation is still in progress. In the meantime, independent audits of Agenda cases by QA and close monitoring of cases by Supervisors throughout the first payment process help mitigate this risk.
	Potential for input errors	Develop field for logging first payment and monthly payment data	3	6/30/2018	The action plan for this recommendation is still in progress. In the meantime, independent audits of Agenda cases by QA and close monitoring of cases by Supervisors throughout the first payment process help mitigate this risk.
	Need to review non-CIB transactions	Forward non-CIB cases to QA for review	3	6/30/2018	Until a Systems solution is available, Benefits Staff continue to work with QA to manually review selected non-CIB transactions.
	Recreating Timelines	Certify Member Timelines	3	6/30/2018	The ACE training program is currently being developed by a team made up of QA, Benefits, and the former QA Division Manager.
	Two Different Disability Databases	Eliminate Double Entry and Continue Reconciling Disability Status	3	6/30/2018	The action plan for this recommendation is still in progress. In the meantime, independent audits of Agenda cases by QA and close monitoring of cases by Supervisors throughout the first payment process help mitigate this risk.

Audit Recommendation Follow Up

Administrative Services

Status: **Pending**

Audit Project: **Office Renovation Projects (April 24, 2016)**

Issue:	Recommendation	Actual	Estimated	Revised
Vendor Justification Not Included in Master Project File or Addressed in Written Procedures	Update written procedures and process to include documenting vendor selection		12/31/2016	1/5/2018
Change Orders are not adequately documented or addressed in written procedures	Develop and codify process for managing Change Orders		12/31/2016	1/5/2018
Inconsistent levels of participation from key stakeholders	Improve Planning and communication of Office Renovation projects		12/31/2016	1/5/2018

Audit Project: **Purchasing/Procurement (May 8, 2011)**

Issue:	Recommendation	Actual	Estimated	Revised
Greater clarity & expansion needed in Purchasing Policy & the related Admin Manual	Admin Services Division should modify & expand both the Purchasing Policy and the related Admin Manual		12/30/2011	1/5/2018
Daily operating procedures ("desk procedures") need enhancement re control procedures	Procurement Unit should update & expand its written, daily operating procedures		12/31/2011	1/5/2018
"Sole-source" or bidding documentation not found	(1) Promulgate requirements to other Divisions (2) Update desk procedures & (3) Contact FASD & agree upon document retention		12/31/2011	1/5/2018

Audit Recommendation Follow Up

Benefits

Status: **New**

Audit Project: **Member Death Verification Process (October 31, 2017)**

Issue:	Recommendation	Actual	Estimated	Revised
Data Confidentiality and Privacy - External Partners Monitoring - Control System	Data Confidentiality and Privacy - External Partners Monitoring - Control System		12/31/2018	
Lower Probability Death Matches	Lower Probability Death Matches		6/30/2018	
Data Confidentiality and Privacy - Monitor Benefits External Vendors	Data Confidentiality and Privacy - Monitor Benefits External Vendors		3/31/2018	

Status: **Pending**

Audit Project: **Certificate Processing (June 29, 2017)**

Issue:	Recommendation	Actual	Estimated	Revised
Birth Certificate Missing for Options Retirees	Certificate Requirements Review		6/29/2018	
Controls over Certificates Processing	Organization-wide Certificates Policy		6/29/2018	

Audit Project: **Claims - Process Objectives, Risks, Controls, Process Flows, and Procedural Gaps (April 12, 2012)**

Issue:	Recommendation	Actual	Estimated	Revised
1st Payment - Separation of Duties	Implement secondary review		12/31/2012	6/30/2018

Audit Project: **Claims Payroll Supervisor Policies/Procedures (July 2, 2013)**

Issue:	Recommendation	Actual	Estimated	Revised
Potential for input errors	Develop field for logging first payment and monthly payment data		6/30/2014	6/30/2018

Audit Recommendation Follow Up

Benefits

Status: **Pending**

Audit Project: **Claims Payroll Supervisor Policies/Procedures (July 2, 2013)**

Issue:	Recommendation	Actual	Estimated	Revised
Need to review non-CIB transactions	Forward non-CIB cases to QA for review		12/31/2013	6/30/2018

Audit Project: **Duplicate Special Payments (January 19, 2017)**

Issue:	Recommendation	Actual	Estimated	Revised
Expand the Automation of Special Payment Approvals	Expand the Automation of Special Payment Approvals		12/31/2017	12/31/2018

Audit Project: **Member Minor Survivor Compliance (June 29, 2016)**

Issue:	Recommendation	Actual	Estimated	Revised
Incomplete Documentation	Develop Procedures manual and Improve Review process		6/30/2017	6/30/2018

Audit Project: **Previous service to contracts (QC/QA/CP) (February 26, 2014)**

Issue:	Recommendation	Actual	Estimated	Revised
Recreating Timelines	Certify Member Timelines		6/30/2014	6/30/2018

Audit Project: **Returned ADR Process Review (November 24, 2015)**

Issue:	Recommendation	Actual	Estimated	Revised
Documented Procedures	Need for Documented Procedures		6/30/2016	12/31/2017

Audit Project: **SCD Tax Indicator (July 3, 2012)**

Issue:	Recommendation	Actual	Estimated	Revised
Two Different Disability Databases	Eliminate Double Entry and Continue Reconciling Disability Status		6/30/2014	6/30/2018

Audit Recommendation Follow Up

FASD

Status: **Implemented**

Audit Project: **Education and Travel Compliance Audit (September 20, 2016)**

Issue:	Recommendation	Actual	Estimated	Revised
Training on Policy	Reinforce Policies and Procedures	7/13/2017	1/30/2017	4/15/2017

Audit Recommendation Follow Up

Investments

Status: **Implemented**

Audit Project: **Investment Fee Reporting and Validation (June 28, 2017)**

Issue:	Recommendation	Actual	Estimated	Revised
Underlying Hedge Fund Fees	Request GSAM to Validate Underlying Hedge Fund Fees	10/31/2017	12/31/2017	

Status: **Pending**

Audit Project: **Investment Fee Reporting and Validation (June 28, 2017)**

Issue:	Recommendation	Actual	Estimated	Revised
No Procedures for Fee Validation and Fee Disclosure	Develop Fee Validation and Disclosure Procedures		12/31/2017	
Commingled Real Estate Fund Fees	Validate Commingled Real Estate Fund Fees		12/31/2017	
Public Market Commingled Fund Fees	Communicate and Coordinate Fee Validation Roles		9/30/2017	12/31/2017
Actual Hedge Fund Performance Fee Data	Request for Actual Performance Fee Data Rather Than Accrued Performance Fee Data		12/31/2017	
Public Market Commingled Fund Fees	Validate fees for the fixed income commingled fund and fund-of-one.		9/30/2017	12/31/2017

Audit Project: **Investment Private Equity Operations (June 25, 2015)**

Issue:	Recommendation	Actual	Estimated	Revised
No formal Information Management System or CRM System to manage information	Consider implementing CRM System		6/30/2016	6/30/2018
Due Diligence Checklists	Include guidelines for checklists and sign-off on checklists		12/31/2015	12/31/2017

Audit Recommendation Follow Up

Retiree Healthcare

Status: **Pending**

Audit Project: **Member Verification (June 30, 2017)**


Issue:	Recommendation	Actual	Estimated	Revised
No HRV	Management develop Of Procedures		12/31/2017	
Insufficient HRV Policy and Procedure	Executive Office require that appropriate authentication steps		12/31/2017	



November 14, 2017

TO: Each Member
2017 Audit Committee

Audit Committee Consultant
Rick Wentzel

FROM: Richard Bendall 
Chief Audit Executive

FOR: November 30, 2017 | Audit Committee Meeting

SUBJECT: 2016 PRIVACY AUDIT (BY ALSTON & BIRD) - FOLLOW-UP

At the October 2016 Board of Investments and Board of Retirement meetings, your Boards were presented with the results of the 2016 Privacy Audit performed by Alston & Bird and their subcontractor, Stroz Friedberg. The final audit report, findings and conclusions presented at these meetings provided an overview of privacy practices at LACERA as well as recommendations.

While Alston & Bird found that LACERA generally conforms to the applicable privacy laws, regulations, and best practices in the areas identified through the audit, they provided a number of recommendations and advice to enhance prudent privacy practices.

As you know, Executive Management has established a cross-functional team to address the implementation of the Privacy Audit recommendations, many of which will simultaneously assist in the formalization of the compliance function at LACERA. The team will coordinate the implementation and the standardization of policies and procedures and the establishment of a compliance framework. The team has identified specific divisions as the primary owners of the Privacy Audit recommendations.

Internal Audit is continuing to monitor the status of each recommendation and verify implementation as well as complete the recommendations over which Internal Audit has primary ownership.

This table provides the statuses of the Privacy Audit recommendations as of October 31, 2017:

Privacy Audit Recommendations	July 31, 2017	October 31, 2017
Beginning Balance of Recommendations	65	65
Disagree	5	5
Completed	10	12
Remaining Recommendations in Progress	50	48

While the table above reflects that two recommendations have been completed since the last Audit Committee meeting, please be aware that a substantial effort is underway by the team to address all recommendations in a comprehensive and professional manner. A significant amount of progress has occurred toward addressing most of the remaining recommendations. An important next step in completing these will be for staff to bring certain policies to the Joint Oversight Committee (JOC) of the Boards for approval.

At the March 2018 Audit Committee meeting, we will summarize the status of all significant efforts completed and underway and provide your Committee with a timeline of any outstanding recommendations to be completed.

Staff will be available to address questions at your November Audit Committee meeting, but please remember that due to the privileged nature of the 2016 Privacy Audit Report, the specific recommendations should not be the subject of detailed discussion at the meeting.



Documents not attached are exempt from disclosure under the California Public Records Act and other legal authority.

**For further information, contact:
LACERA
Attention: Public Records Act Requests
300 N. Lake Ave., Suite 620
Pasadena, CA 91101**