

AUDIT COMMITTEE AGENDA 7-20-11

LACERA

300 N. Lake Ave., Suite 810
Pasadena, CA 91101

9:00 AM

2011 COMMITTEE MEMBERS

Simon S. Russin, Chair
Michael Schneider, Vice Chair
John M. Barger, Secretary
Ed C. Morris
Les Robbins

CONSULTANT

Timothy O'Brien — Audit Committee Consultant

I. APPROVAL OF THE MINUTES OF THE REGULAR AUDIT COMMITTEE MEETING OF MARCH 16, 2011

II. PUBLIC COMMENT

III. REPORTS

- A. Supplemental Targeted Adjustment Program for Retirees
(Presentation dated July 20, 2011)
(Report dated November 24, 2010)
Eric S. Berman, MSA, CPA, Partner
Connie M. Perez, CPA, Partner
Brown Armstrong Accountancy Corporation
- B. GASB Pension Exposure Draft (Presentation dated July 20, 2011)
Eric S. Berman, MSA, CPA, Partner
Connie M. Perez, CPA, Partner
Brown Armstrong Accountancy Corporation
- C. Internal Audit Staffing Report
Richard Bendall, Chief Internal Auditor (Verbal presentation only)
- D. June 2011, Audit Reports
Richard Bendall, Chief Audit Executive (For information only)
 - a. LACERA Internal Audit Quality Assurance Update
 - b. Investment Funding Approval Process (May 31, 2011)
 - c. Retiree-Payroll Validation Process Testing (June 9, 2011)
 - d. Systems Transaction Authentication Controls (June 21, 2011)
 - e. LACERA-Investment "Proof of Ownership" Document Preservations (June 30, 2011)
 - f. Network Access Vulnerability Assessment (June 29, 2011)
- E. Summary of Work In-Progress [As of June 30, 2011]
Richard Bendall, Chief Audit Executive
Sylvia Botros, Internal Auditor (Memo dated June 30, 2011)
- F. Audit Plan Status Report — Fiscal Year ended June 30, 2011
Richard Bendall, Chief Audit Executive
Sarah Marks, Principal Internal Auditor (Memo dated July 8, 2011)
- G. Risk Management Process Assessment and Internal Audit Risk Assessment
Richard Bendall, Chief Audit Executive
Sarah Marks, Principal Internal Auditor (Memo dated July 8, 2011)
- H. Status of Other External Audits Not Conducted at the Discretion of Internal Audit
Richard Bendall, Chief Audit Executive (Verbal Presentation Only)

IV. ACTION ITEMS

- A. Recommendation as submitted by Gregg Rademacher, Chief Executive Officer: the Audit Committee forward the 2010-2011 Civil Grand Jury's report "Whoa! The State of Public Pensions in Los Angeles County" to the Board of Retirement

and Board of Investments for response. (Memo dated June 29, 2011)

- B. Recommendation as submitted by Richard Bendall, Chief Audit Executive and Sarah Marks, Principal Internal Auditor, that the Audit Committee approve the Fiscal Year 2011-2012 Audit Plan (Memo dated July 8, 2011)

V. FOR INFORMATION ONLY

- A. None

VI. CONSULTANT COMMENTS

Timothy O'Brien — Audit Committee Consultant (Oral presentation only)

VII. GOOD OF THE ORDER

(For discussion purposes only)

VIII. ADJOURNMENT

AUDIT COMMITTEE MINUTES 7-20-11

2011 COMMITTEE MEMBERS

PRESENT

Simon S. Russin, Chair
Michael Schneider, Vice Chair
Les Robbins

ABSENT

John Barger, Secretary
Ed C. Morris

ALSO ATTENDING:

BOARD MEMBERS AT LARGE

None

AUDIT COMMITTEE CONSULTANT

Timothy O'Brien

STAFF, ADVISORS, PARTICIPANTS

Gregg Rademacher
Janice Golden
Robert Hill
Richard Bendall
Kimberly Hines
Jeannine Smart
Sarah Marks
Ted Granger
Ruwen Liu
George Lunde
David Redman
Leisha Collins
Nathan Amick
Sylvia Botros
Elvia Gonzalez

I. APPROVAL OF THE MINUTES OF THE REGULAR AUDIT COMMITTEE MEETING OF MARCH 16, 2011

A motion was made by Vice Chair Schneider and seconded by Chairman Russin, to approve the Audit Committee minutes prepared for the March 16, 2011 meeting as presented. The motion passed with Chair Russin and Vice Chair Schneider voting aye, and Mr. Robbins abstaining.

II. PUBLIC COMMENT

None noted.

III. REPORTS

A. Supplemental Targeted Adjustment Program for Retirees

(Presentation dated July 20, 2011)

(Report dated November 24, 2010)

Eric S. Berman, MSA, CPA, Partner

Connie M. Perez, CPA, Partner

Brown Armstrong Accountancy Corporation

Mr. Berman presented to the Audit Committee an executive summary of the November 24, 2010 "View of Whether the Los Angeles County Employees Retirement Association's Supplemental Targeted Adjustment for Retiree's Program (STAR) Constitutes Net Assets Available for Plan Benefits in Accordance With Generally Accepted Accounting Principles for Governments in the United States of America." The executive summary included: background information on the topic, communication between LACERA Executive Management and Los Angeles County Executive Management, and various standards of County Employees Retirement Law (CERL) code, GAAP, and GASB. Based on the information provided by LACERA and the research performed by Mr. Berman, it was his view that the STAR Cola benefits do constitute net assets available for plan benefits. He stated this is not a legal or audit opinion, and it is the prerogative of LACERA's management and boards as to whether or not the presented view is valid, and it is the

responsibility of the boards and management to decide how to account for these assets. However, he emphasized the importance of consistent accounting treatment for the assets from year to year.

Vice Chair Schneider asked Mr. Berman his opinion on how to record the corresponding liability. Mr. Berman stated, he would first need to perform a due diligence process in order to understand all the variables of the situation including an actuarial calculation to value the liability. Only after a thorough review is performed would he attest to the reliability of the resources used in the due diligence process, and the accuracy of the actuarial valuation.

B. GASB Pension Exposure Draft

(Presentation dated July 20, 2011)

Eric S. Berman, MSA, CPA, Partner
Connie M. Perez, CPA, Partner
Brown Armstrong Accountancy Corporation

Mr. Berman gave a review of Governmental Accounting Standards Board (GASB) Exposure Drafts #25 and #27. These Drafts govern the accounting treatment for Other Post Employment Benefits (OPEB), including both postemployment healthcare benefits as well as other forms of non-pension post employment benefits such as life insurance or long term disability benefits. In short, #25 and #27 require the measurement and recognition of annual OPEB liabilities on an accrual basis. Currently OPEB benefits are reported on a pay-as-you-go basis and not recorded in financial statements until paid. Mr. Berman discussed how, if implemented as written, the new standards would affect the following:

- Implementation timeline
- Comment Period
- Public Hearing
- Investments stated at fair value
- Unallocated annuities
- Discount rates
- Historical rate of return
- Required supplementary information
- Definition of "long term"
- Proposed reporting schedules
- Changes in actuarial assumptions
- Cost sharing plans
- Layered amortization

C. Internal Audit Staffing Report

Richard Bendall, Chief Internal Auditor

(Verbal presentation only)

Richard Bendall, Chief Audit Executive, briefly discussed the following Internal Audit staffing issues:

- Bernie Buenaflor, Principal Internal Auditor, is eleven months into his one year assignment as the Acting Division Manager of the Claims Processing department.
- Ted Granger, former Senior Internal Auditor, took a position in FASD as the Assistant Financial Officer.
- Ruwen Liu, Senior Internal Auditor, who took part in a trial basis staff exchange with the Investment Office, has now returned to Internal Audit.
- Currently Internal Audit is down one open position and possibly two in the near future. Internal Audit has begun working with Human Resources and is making plans to fill those positions.

At this point in the meeting the Committee, at Mr. Bendall's suggestion, decided to skip forward to Agenda Section IV, Action Item A.

D. June 2011, Audit Reports

Richard Bendall, Chief Audit Executive

(For information only)

1. LACERA Internal Audit Quality Assurance Update
2. Investment Funding Approval Process (May 31, 2011)
3. Retiree-Payroll Validation Process Testing (June 9, 2011)
4. Systems Transaction Authentication Controls (June 21, 2011)
5. LACERA-Investment "Proof of Ownership" Document Preservations (June 30, 2011)
6. Network Access Vulnerability Assessment (June 29, 2011)

Mr. Bendall outlined each project mentioned above and addressed questions and comments from the Committee Members.

Committee inquiries included:

As a result of the audits/reviews performed, has internal audit uncovered any fraud or misappropriation of assets? Mr. Bendall stated that Internal Audit has not uncovered any such issues as a result of work performed. However, there is the Internal Audit Hotline and Internal Audit does receive tips from staff. Those tips have led to special investigations and disciplinary actions.

Does LACERA perform any kind of check to ensure prospective employees are not felons? Mr. Bendall stated that LACERA Human Resources does perform background checks on prospective employees.

Currently what is LACERA's policy on scanning documents for record retention? Robert Hill, LACERA Assistant Executive Officer, stated that in the past, LACERA has performed backlog document image conversion projects for membership documents and Board of Retirement documents, and continues to scan, image, and archive related documents. Currently, LACERA is evaluating the feasibility of converting its disability, committees, and Board of Investment documents.

What is LACERA's exposure to hacking? James Pu, LACERA's Information Systems Division Manager, stated that technology is dynamic, with every change and improvement there is a new risk to mitigate. Mr. Pu stated that he believes our members' private information is currently very secure.

E. Summary of Work In Progress [As of June 30, 2011]

Richard Bendall, Chief Audit Executive

Sylvia Botros, Internal Auditor

(Memo dated June 30, 2011)

Mr. Bendall stated that the Work In Progress Report covers much of the same material as discussed in Agenda Section D above (June 2011, Audit Reports), and unless the Committee had any additional questions, he would like to move on to Agenda Section F.

The Committee had no questions.

F. Audit Plan Status Report — Fiscal Year ended June 30, 2011

Richard Bendall, Chief Audit Executive

Sarah Marks, Principal Internal Auditor

(Memo dated July 8, 2011)

Mr. Bendall stated that the Audit Plan Status Report covers all work completed for the fiscal year ended June 30, 2011. Internal Audit completed 83% of the unadjusted 2011 Audit Plan.

Chair Russin asked if Internal Audit was monitoring overpayment cases forwarded to the County Treasurer's office for collections, and of those cases has LACERA identified any repeat offenders. Ted Granger, LACERA Assistant Financial Officer, stated cases are forwarded to the County Treasurer and Tax collector only after all resources to recoup overpayments have been completely exhausted. Currently, Internal Audit does not monitor the process. Mr. Bendall stated that in the case of repeat offenders, the member's account is locked down and a verification process is performed to identify and resolve the issue.

G. Risk Management Process Assessment and Internal Audit Risk Assessment

Richard Bendall, Chief Audit Executive

Sarah Marks, Principal Internal Auditor

(Memo dated July 8, 2011)

Mr. Bendall reviewed the process and procedures performed to accumulate the content and to report on the status of LACERA's risk management and assessment. The review included the following:

- Interviewing Executive, and Division management.
- Review of management's strategic plans
- Internal Audit assessment of risks and risk management
- Change in how Internal Audit presents risk to the Audit Committee
- Aligning LACERA's risk assessment with its strategic plan
- Inherent risk vs. residual risk

Committee inquiries included:

What is the difference between Investments and the Board of Investments categories? Mr. Bendall stated that the two categories exist because they relate to two separate bodies with differing risks.

What is the relationship between the amount of external oversight over a particular area and its risk ranking? Mr. Bendall stated that areas receiving external oversight are generally lower risk.

H. Status of Other External Audits Not Conducted at the Discretion of Internal Audit

Richard Bendall, Chief Audit Executive

I. (Verbal Presentation Only)

None Noted

IV. ACTION ITEMS

- A.** Recommendation as submitted by Gregg Rademacher, Chief Executive Officer: The Audit Committee forward the 2010-2011 Civil Grand Jury's report "Whoa! The State of Public Pensions in Los Angeles County" to the Board of Retirement and Board of Investments for response.

(Memo dated June 29, 2011)

Gregg Rademacher, LACERA Chief Executive Officer, explained to the Committee that the Grand Jury is requesting LACERA respond to the findings and recommendations directed to LACERA within the report. In Mr. Rademacher's attached memo, he outlined the findings and recommendations, and identified the board responsible for response.

Vice Chair Schneider moved to forward the 2010-2011 Civil Grand Jury's report to the Board of Retirement and Board of Investments for response. The motion was seconded by Mr. Robbins, and passed with a unanimous vote.

- B.** Recommendation submitted by Richard Bendall, Chief Audit Executive and Sarah Marks, Principal Internal Auditor, that the Audit Committee approve the Fiscal Year 2011-2012 Audit Plan

(Memo dated July 8, 2011)

Vice Chair Schneider moved to approve the Year 2011-2012 Audit Plan as presented. Mr. Robbins seconded the motion and it passed with a unanimous vote.

V. FOR INFORMATION ONLY

None

VI. CONSULTANT COMMENTS

Timothy O'Brien — Audit Committee Consultant

(Oral presentation only)

No items to report

VII. GOOD OF THE ORDER

(For discussion purposes only)

No items to report

VIII. ADJOURNMENT