

AGENDA

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, CA 91101**

December 6, 2012 – 9:00 a.m.

2012 COMMITTEE MEMBERS:

Simon S. Russin, 2012 Chair
Michael Schneider, 2012 Vice Chair
Ed C. Morris
Les Robbins
Herman B. Santos
Leonard Unger

CONSULTANT:

Timothy O'Brien – Audit Committee Consultant

- I. APPROVAL OF THE MINUTES OF THE REGULAR AUDIT COMMITTEE MEETING OF July 18, 2012 (see attachment)
- II. PUBLIC COMMENT
- III. REPORTS
 - A. Brown Armstrong Presentation of the Reports for Fiscal Year Ended June 30, 2012
Reports and Agenda from Brown Armstrong et. al.
(Memo dated October 23, 2012)

Presentation by: Brown Armstrong, Certified Public Accountants
Andrew Paulden, Managing Partner
Connie Perez, Partner
 - B. Audit Plan Status Report (As of October 31, 2012)
Richard Bendall, Chief Internal Auditor
Nathan Amick, Internal Auditor
(Memo dated November 21, 2012)

Presentations by: Internal Audit Staff

- C. Audit Reports
 - a. Understated Previous Service Contracts (Nov. 16, 2012)
 - b. Disability Retirement Process Review (Nov. 20, 2012)
 - c. Excess Non-Elective Leave Buybacks (Nov. 20, 2012)
 - d. Special Death Benefits Owed to Member Survivors (Nov. 16, 2012)
 - e. Agency Deductions Reconciliations (Nov. 21, 2012)
 - f. TriPacific Review Cancellation (Aug. 9, 2012)
 - g. IRIS System Table Change Error (Oct. 30, 2012)

- D. Internal Audit Project – Computer Assisted Auditing Techniques
Richard Bendall, Chief Audit Executive
George Lunde, Senior Internal Auditor
(Presentation)

- E. Status of Other External Audits Not Conducted at the Discretion of Internal
Richard Bendall, Chief Audit Executive
(Verbal Presentation Only)

IV. FOR INFORMATION ONLY

- A. Risk Assessment (Issued July 2012)

V. CONSULTANT COMMENTS

Timothy O'Brien – Audit Committee Consultant
(Verbal presentation only)

VI. GOOD OF THE ORDER

(For discussion purposes only)

VII. CLOSED SESSION (Pursuant to Government Code Section 54957) –

- A. PUBLIC EMPLOYEE PERFORMANCE EVALUATION
Title: Chief-Internal Audit

VIII. ADJOURNMENT

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].

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Minutes of the Audit Committee

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, CA 91101**

December 6, 2012 – 9:00 a.m.

2012 COMMITTEE MEMBERS:

Present: Simon S. Russin, 2012 Chair
Michael Schneider, 2012 Vice Chair
Ed C. Morris
Herman B. Santos
Leonard Unger

Absent: Les Robbins

CONSULTANT:

Timothy O'Brien – Audit Committee Consultant

STAFF, ADVISORS, PARTICIPANTS

Gregg Rademacher	Elvia Gonzalez
Robert Hill	Sarah Marks
Leisha Collins	George Lunde
Vivian Grey	Quoc Nguyen
Richard Bendall	Nathan Amick
Bernie Buenaflor	Sylvia Botros
James Pu	Andy Paulden
Roxana Castillo	Eric Berman
Beulah Auten	Connie Perez
Ted Granger	
Gloria Harriel	
David Kushner	
Robb Van Der Volgen	

I. APPROVAL OF THE MINUTES OF THE REGULAR AUDIT COMMITTEE MEETING OF July 18, 2012

A motion was made by Mr. Morris and seconded by Mr. Santos, to approve the Audit Committee minutes prepared for the July 18, 2012 meeting as presented. All Committee Members voted aye and the motion passed unanimously.

II. PUBLIC COMMENT

None

AGENDA ADJUSTMENTS:

Richard Bendall, Chief Audit Executive, noted that due to scheduling issue at Brown Armstrong's request, the presentation of the annual audit will be taken out of order and discussed later in the meeting. Chairman Russin concurred.

Mr. Bendall also noted that his performance evaluation will not be done in closed session as indicated by the agenda but will be in open session as required by the Brown Act.

III. REPORTS

A. Brown Armstrong Presentation of the Reports for Fiscal Year Ended June 30, 2012

Reports and Agenda from Brown Armstrong et. al.
(Memo dated October 23, 2012)

Presentation by: Brown Armstrong, Certified Public Accountants
Andrew Paulden, Managing Partner
Connie Perez, Partner
Eric Berman, Partner

A presentation was given by Mr. Paulden, CPA and Managing Partner for Brown Armstrong, Ms. Perez, Partner, and Eric Berman, Partner, in relation to Brown Armstrong's audit of LACERA's fiscal year end June 30, 2012 financial statements. Their presentation covered the purpose of the audit, audit process, significant audit areas/scope of work, and the audit reports.

The issued presented were as follows:

- Purpose of the Audit
- The audit process
- Significant audit areas
- Scope of audit work
- Audit reports
- Going Concern
- Contributions and benefits
- Plan Sponsor's reliance on LACERA Audit
- Updated pension standards
- Changes in Financial Statement reporting

- Changes in reporting language
- LACERA implementation task force

Mr. Berman provided an overview of changes related to the coming financial statements. The following changes were discussed:

- Titles on the Financial Statements
- Net Position Format
- Audit Opinion
- Independence Framework
- July 1, 2013 -new financial reporting standards and new audit standards for Pension Plans

Mr. Berman stated that along with the management of LACERA and the County, Brown Armstrong has put together a task force to figure out a timeline and deliverables for the financial statements.

Following Brown Armstrong's presentation, the Audit Committee addressed a few questions to Timothy O'Brien, Audit Committee Consultant, regarding the presentation. Chairman Russin asked if Mr. O'Brien had any additional comments or questions regarding the Brown Armstrong presentation and Mr. O'Brien replied that he felt the Committee was asking all the proper questions, and that if there is an issue that needs to be addressed he will make the necessary comments to facilitate such a discussion.

Mr. Santos asked how Mr. O'Brien felt about retaining Brown Armstrong's services for the OPEB trust implementation. Mr. O'Brien said he thought that was a good decision and feels Brown Armstrong provides high quality services for LACERA.

B. Audit Plan Status Report (As of October 31, 2012)
Richard Bendall, Chief Internal Auditor
Nathan Amick, Internal Auditor
(Memo dated November 21, 2012)

Mr. Bendall gave an overview of the risk assessment process and how it leads to the creation of the annual audit plan. He then explained that in the past, Internal Audit would go through the audit plan and discuss their progress towards completing the Audit plan with the Audit Committee at each meeting. Audit Committee members would then have an opportunity to ask questions regarding the projects and the audit plan at the time of the meeting.

Mr. Bendall stated that Internal Audit would be doing things differently going forward, in that staff would be focusing their audit hours in the most high risk

areas which are determined by the annual risk assessment. The five highest risk areas determined are as follows: 1) Systems, 2) Claims Processing, 3) Member Services, 4) Investments, and 5) Financial and Accounting Services Division (FASD). Mr. Bendall explained that staff would be presenting an update to the Committee on the areas and status of their projects in these high risk areas. This will be done in order to provide a more in depth view of the work performed in each division and how it relates to the annual audit plan and risk assessment.

STAFF PRESENTATION:

Mr. Bendall gave a brief introduction and overview of the Claims Processing Division's operations and the related key risks.

Understated Previous Service Contracts - Quoc Nguyen, Senior Internal Auditor, presented an overview of risks, controls, audit objectives and audit findings related to the Understated Previous Service Contracts audit.

Mr. Santos inquired as to how many members were identified as having understated previous service contracts. Mr. Nguyen stated that prior to the audit, Claims Processing staff had already identified 160 possible understated previous service contracts.

Mr. Unger inquired as to how staff became aware of the error and the understated previous services contracts. Mr. Nguyen stated that staff was performing their normal manual check of the system calculation. During the manual check, staff realized that the spread sheet being used was an outdated spread sheet with incorrect information. However, the calculation with the outdated information was the same as the system calculation. This prompted some additional research and identification of the error.

George Lunde, Senior Internal Auditor, added that each year the actuaries provide new calculation tables and these are updated in the month of July. Hence, the error would have most likely been discovered and corrected upon the next yearly update at latest.

Mr. Schneider inquired of Internal Audit's role in uncovering these types of system errors. Mr. Bendall stated that the Systems Division continuously updates numerous tables and they have controls in place for verifying that updates are processed correctly. For the particular error in question, there was a breakdown in the procedures and improvements have been made in which Mr. Lunde would be providing more information in his later presentation.

Mr. Nguyen concluded his presentation with a review of Internal Audit recommendations and related Management action plans.

Special Death Benefits Owed to Member Survivors – Mr. Nguyen presented an overview of the types of special death benefits, and the required eligibility for such a benefit payment. Five cases were brought to Internal Audit's attention by the Executive Office for review. These cases consisted of safety members who died violently in the performance of their jobs from 1996-2006. This review was done to determine the status of special death benefits that may be due to the members' survivors and/or dependants. Claims Processing had performed a review of these Active Death cases earlier in the year and identified five cases where survivors were potentially eligible for a special death benefit payment. According to Mr. Nguyen, the payments to the survivors and/or dependants were being reviewed and then processed accordingly. Chairman Russin asked if these payments were being made with interest. Mr. Bendall stated the possibility is being considered.

Review of Active Death Process-

Mr. Nguyen discussed the current review in progress for the Active Death Process. The review is being done to provide some assurance that this type of special death benefit oversight does not occur in the future.

Gregg Rademacher, Chief Executive Officer, stated that over the past decade LACERA has been working towards improving the Active Death Processes as historically this has been an area of struggle for staff. He explained that as soon as these cases were brought to his attention by Claims Processing, he asked Internal Audit to step in to review the process and identify the failures in the process in relation to the five cases. One failure identified was the communication and "hand-off" of cases between the Disability Retirement and Claims Processing staff. Improvements operationally have been made by both divisions and Member Services, including additional staff resources to manage cases throughout the Active Death Process.

Bernie Buenaflor, Claims Processing Manager, emphasized that it is LACERA's obligation to make survivors and/or dependants aware of the death benefits they could potentially be eligible for upon a member's death.

Mr. Russin inquired of the 5k death benefit in relation to the Active Death cases and Mr. Nguyen responded that he would also be including a review of this benefit during the Active Death process review.

STAFF PRESENTATION:

Mrs. Marks gave a brief introduction and overview of the Systems Division's operations and the related key risks.

IRIS System Table Change Error - Mr. Lunde discussed the actuary table change error in July 2011. George explained that he wanted to determine what caused the error and how it could be prevented in the future. Mr. Lunde determined that the error occurred because the process for changing actuary tables was outside of the normal change control process and the end user did not verify and test the tables for accuracy.

Mr. Schneider expressed a concern as to how the tables are updated, manually vs. automated downloads.

The following topics were discussed with the Audit Committee:

- Programming changes vs. table changes
- Actuarial table values
- Change control process
- Design controls and end user testing
- Updated Process controls
- Errors and Omissions legislation

A discussion between the staff and the committee members ensued and the following topics were discussed:

- Process controls
- Identifying cases involving death
- Member education
- Interdivisional communication

Mr. Lunde expressed that Systems has incorporated controls related to the end-user verification of tables to ensure this type of error does not occur in the future.

Chairman Russin inquired about the cost related to the actuary table change error. Mr. Nguyen stated that 23 contracts were revised, with a total of approximately 16k needed from the members to complete the contract. Quoc added that there are 133 contracts still pending review. Mr. Bendall stated any cost related to these contracts is not a loss to the organization but amounts to the additional cost required from the member to complete the contract as the contracts were initially understated.

Mr. Santos inquired of the errors and omissions law and if it was enacted in these understated contracts. Robert Hill, Assistant Executive Officer, stated that this law does not apply to these contracts because the member must pay the Additional Retirement Credit contract amount, but he emphasized that options will be provided to the members for payment.

Web Portal Authentication-

Mr. Lunde provided an overview of the Web Portal Authentication review he is currently working on. The Systems Division has recently made some changes to the program code for the MyLACERA web application in relation to member authentication. Internal Audit will be hiring an outside vendor specializing in code review to test the authentication program code for vulnerabilities to outsiders.

Systems Access Procedures-

Mr. Lunde discussed the System Access procedure review he is currently working on. The audit addresses system access procedures as they pertain to member data in the following areas: 1) Identity Management Procedures and 2) User Account Management Procedures. This review is being done to ensure that the appropriate staff and management have access to the appropriate network files to fulfill their job responsibilities.

STAFF PRESENTATION:

Mr. Bendall gave a brief introduction and overview of the Member Services Division's operations and the related key risks.

Agency Deductions Reconciliations - Nathan Amick, Internal Auditor, gave a brief presentation on the reconciliation of the various withholding of retiree amounts for payment to a third party, performed by the Member Services Division. The Issues presented were as follows:

- Member requested deduction
- Third party requested deductions
- Reconciliation process analysis
- Review of internal controls

High Risk Member Verification Process – Sylvia Botros, Internal Auditor, gave a brief presentation on the different actions taken to verify high risk members, such as members over the age of ninety, members living abroad and members who we have lost contact with. The issues presented were as follows:

- Member verification
- Special Investigations
- ICS Merrill
- Returned mail
- Fraud prevention

Mr. Santos inquired of the verification process for members living internationally. Mrs. Botros explained the verification options briefly, which included verification by phone, completion of a verification form, and an in-person visit by an investigator.

STAFF PRESENTATION:

Mr. Bendall described the fifteen month Leadership Development Program, for the Member Services Division manager position, that Leisha Collins, Senior Internal Auditor, is currently participating in and commends and supports her role in this aspect of the organization.

Mrs. Marks gave a brief introduction and overview of the Investments Division's operations and the key business objectives and risks.

A discussion was stimulated by Mrs. Mark's presentation on risks faced by the Investments Division. Mr. Schneider, Mr. Santos, Tim O' Timothy O'Brien, and David Kushner, Chief Investments Officer, all took part in the discussion.

Title Holding Company Management Audit – Mrs. Collins gave a presentation on the Title Holding Company structure for LACERA's real estate investments. The following issues were presented as follows:

- Tax exemptions
- Management controls
- Real Estate advisors
- Advisor audits
- Legal Filings
- Tax return fillings
- Monetary contributions and distributions
- Documented policies and procedures

Mrs. Collins expressed that this audit is still underway and expects to have the fieldwork completed and a report issued by the end of January 2013. At this time, Mrs. Collins has no audit related issues to report.

Mrs. Collins also gave an update to the Audit Committee on LACERA's Request for Proposal for Real Estate External Auditors. The RFP will be issued by January 2013. From the RFP, LACERA will pick four to five audit firms who will be part of the auditor pool. Every two years the selected firms bid on the various audits. The Selection of auditors is scheduled for the end of March 2013.

C. Audit Reports

- a. Understated Previous Service Contracts (Nov. 16, 2012)
- b. Disability Retirement Process Review (Nov. 20, 2012)
- c. Excess Non-Elective Leave Buybacks (Nov. 20, 2012)
- d. Special Death Benefits Owed to Member Survivors (Nov. 16, 2012)
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D. Internal Audit Project – Computer Assisted Auditing Techniques
Richard Bendall, Chief Audit Executive
George Lunde, Senior Internal Auditor
(Presentation)

George Lunde gave a demonstration of the use of Audit Command Language (ACL). George walked the Audit Committee through a live data filtering example to demonstrate the use and capabilities of ACL for data mining. In the demonstration, he took 8,000 plus payroll time records of retirees under the 120 day / 960 hour work program. He used six ACL data filters to narrow the records to 23 possibly exceeding maxim limits, in just a few short minutes.

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

None noted

IV. FOR INFORMATION ONLY

A. Risk Assessment (Issued July 2012)

V. CONSULTANT COMMENTS

Timothy O'Brien – Audit Committee Consultant
(Verbal presentation only)

None

VI. GOOD OF THE ORDER

(For discussion purposes only)

None

VII. CLOSED SESSION (Pursuant to Government Code Section 54957) –

A. PUBLIC EMPLOYEE PERFORMANCE EVALUATION
Title: Chief-Internal Audit

At this time the Audit Committee, with the exception of Mr. Santos and Mr. Unger, discussed Richard Bendall, Chief Audit Executive, annual performance evaluation.

VIII. ADJOURNMENT

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***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.**

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