How ASRS employees deliver service with PRIDE

PROFESSIONALISM
“Promote, strive for and expect individuals, teams, and divisions to possess professional qualities and skills to lead the organization”

- Friendly, respectful and courteous
- Proactive and responsive
- Good communicator / active listener
- Trusted contributor / teammate
- Personally accountable
- Subject matter expert
- Critical thinker
- Honest, fair, non-judgmental
- Adaptable to change
- Adhere to the Code of Conduct

RESULTS
“We appreciate individuals, teams or divisions who drive the agency forward with new, innovative ideas and solutions”

- Completes projects
- Attains individual accomplishments
- Meets goals and objectives
- Satisfies customers
- Produces quality work products
- Manages risks successfully

IMPROVEMENT
“We promote, strive for and expect individuals, teams, and divisions to possess professional qualities and skills to lead the organization”

- Promotes new ideas
- Enhances morale
- Enhances outcomes and performance
- Improves relationships
- Solves problems
- Increases efficiency, effectiveness or reduces costs

DIVERSITY
“We recognize that utilizing different talents, strengths and points of view, strengthens the agency and helps propel outcomes greater than the sum of individual contributors”

- Encourages the free flow of ideas and opinions
- Treats all people with dignity and respect
- Works effectively with dissimilar individuals
- Recognizes and promotes new skills in others

EXCELLENCE
“We celebrate individuals, teams and divisions who exceed expectations and deliver service with a PRIDE that permeates the organization”

- Surpasses expectations
- Engenders a positive public image
- Celebrates /reward accomplishments and contributions of others
- Embraces change in a manner which inspires others
- Promotes teamwork /collaboration through communication
- Accepts personal responsibility and challenges with enthusiasm

ARIZONA STATE RETIREMENT SYSTEM

Celebrating Sixty Five Years
1953 2018
AGENDA

NOTICE OF COMBINED PUBLIC MEETING AND POSSIBLE EXECUTIVE SESSION
OF THE ARIZONA STATE RETIREMENT SYSTEM
OPERATIONS, AUDIT, AND LEGISLATIVE COMMITTEE

3300 North Central Avenue, 14th Floor Conference Room
Phoenix, AZ 85012

July 10, 2019
2:30 p.m.

Pursuant to A.R.S. § 38-431.02(F), notice is hereby given to the Trustees of the Arizona State Retirement System (ASRS) Operations, Audit, and Legislative Committee (OALC) and to the general public that the ASRS OALC will hold a meeting open to the public on Wednesday, July 10, 2019, beginning at 2:30 p.m. in the 14th Floor Conference Room of the ASRS office, 3300 North Central Avenue, Phoenix, AZ 85012. Trustees of the Committee may attend either in person or by telephone conference call.

This is a regularly scheduled meeting of the OALC; however, due to possible attendance by other ASRS Board Trustees, this meeting may technically become a meeting of the Board or one of its committees. Actions taken will be consistent with OALC governance procedures. Actions requiring Board authority will be presented to the full Board for final decision.

The Chair may take public comment during any agenda item. If any member of the public wishes to speak to a particular agenda item, they should complete a Request to Speak form indicating the item and provide it to the Committee Administrator.

This meeting will be teleconferenced to the ASRS Tucson office conference room at 4400 E. Broadway Boulevard, Suite 200, Tucson, Arizona 85711. The conference call to Tucson will be disconnected after 15 minutes if there are no attendees in the Tucson audience.

The agenda for the meeting is as follows:

1. Call to Order; Roll Call; Opening Remarks ..................................................... Mr. Jim Hillyard
   OALC Chair

2. Approval of the Minutes of the April 10, 2019, Public Meeting and Executive Session of the
   OALC ............................................................................................................. Mr. Jim Hillyard
3. Presentation, Discussion, and Appropriate Action Regarding ASRS Budget-Related Topics Including:


b. Presentation of the ASRS Appropriated and Continuously Appropriated Budget Request and the ASRS Administrative and Investment Spending Plans for FY 2021.

...................................................................................................................... Mr. Anthony Guarino
Deputy Director and Chief Operations Officer

...................................................................................................................... Ms. Martha Rozen
Chief of Administrative Services

...................................................................................................................... Mr. Chris Gustafson
Procurement and Budget Manager

...................................................................................................................... Ms. Kerry White
Assistant Chief Investment Officer

4. Presentation, Discussion, and Appropriate Action Regarding the Internal Audit Quarterly Update ................................................................................................... Mr. Anthony Guarino
...................................................................................................................... Mr. Harold Mackey
Chief Internal Auditor

5. Review of Recently Conducted Audits ........................................................... Mr. Anthony Guarino
...................................................................................................................... Mr. Harold Mackey

• Espiritu Schools – Employer Audit
• Vendor Efficacy – Internal Process

6. Requests for Future Agenda Items ................................................................. Mr. Jim Hillyard
...................................................................................................................... Mr. Anthony Guarino

7. Call to the Public ............................................................................................. Mr. Hillyard

Those wishing to address the ASRS OALC are required to complete a Request to Speak form before the meeting indicating their desire to speak. Request to Speak forms are available at the sign-in desk and should be given to the Committee Administrator. Trustees of the Committee are prohibited by A.R.S. § 38-431.01(H) from discussing or taking legal action on matters raised during an open call to the public unless the matters are properly noticed for discussion and legal action. As a result of public comment, the Committee Chair may direct staff to study and/or reschedule the matter for discussion and decision at a later date.

8. The next regular public OALC meeting is scheduled for Wednesday, October 9, 2019, at 2:30 p.m., at 3300 N. Central Avenue, in the 14th Floor Conference room, Phoenix, Arizona.
9. Adjournment of the OALC

A copy of the agenda background material provided to the OALC Trustees (with the exception of material relating to possible executive sessions) is available for public inspection at the ASRS offices located at 3300 North Central Avenue, 14th Floor, Phoenix, Arizona and 4400 East Broadway Boulevard, Suite 200, Tucson, Arizona. The agenda is subject to revision up to 24 hours prior to meeting. These materials are also available on the ASRS website (https://www.azasrs.gov/content/board-and-committee-meetings) approximately 48 hours prior to the meeting.

Persons(s) with disabilities may request a reasonable accommodation such as a sign language interpreter or alternate formats of this document by contacting Tracy Darmer, ADA Coordinator at (602) 240-5378 in Phoenix, at (520) 239-3100, ext. 5378 in Tucson or 1-800-621-3778, ext. 5378 outside metro Phoenix or Tucson. Requests should be made as early as possible to allow time to arrange the accommodations.

Dated July 3, 2019

ARIZONA STATE RETIREMENT SYSTEM

Melanie Alexander  Anthony Guarino
Committee Administrator  Deputy Director and Chief Operations Officer
Agenda Item #2
A quorum of the Operations, Audit & Legislative Committee (OALC) of the Arizona State Retirement System (ASRS) met in public session in the 14th Floor Conference Room of the ASRS Office, 3300 N. Central Avenue, Phoenix, Arizona 85012.

Mr. Clark Partridge, Vice-chair of the OALC, called the meeting to order at 2:31 p.m.

The meeting was teleconferenced to the ASRS office at 4400 E. Broadway, Tucson, Arizona 85711.

1. Call to Order; Roll Call; Opening Remarks

Mr. Clark Partridge, Vice-chair, welcomed the attendees.

Present:  Mr. Jim Hillyard, Chair (joined the meeting at 2:32 p.m.)
          Mr. Clark Partridge, Vice-chair
          Mr. Michael Miller

A quorum of the Committee was present for the purpose of conducting business.

2. Approval of the Minutes of the January 9, 2019 Public Meeting of the OALC

Motion: Mr. Michael Miller moved to approve the Minutes of the January 9, 2019, Public Meeting of the OALC. Mr. Clark Partridge seconded the motion.

By a vote of 2 in favor, 0 opposed, 0 abstentions, and 1 excused, the motion was approved. The Trustee votes were as follows:

   Mr. Jim Hillyard – excused
   Mr. Clark Partridge – approved
   Mr. Michael Miller – approved
3. Presentation, Discussion, and Appropriate Action Regarding an Update of the 2018 ASRS Rulemaking

Ms. Jessica Thomas, Government Relations Officer and Rules Writer, reviewed the status of the 2018 ASRS Regulatory Agenda as follows:

- 2 A.A.C. 8, Article 5: Service Purchase – rulemaking has been completed and became effective March 18, 2019
- 2 A.A.C. 8, Article 7: Contributions Not Withheld – rulemaking has been completed and became effective March 18, 2019
- 2 A.A.C. 8, Article 1: Retirement application and options – staff is still currently working on this initiative

Ms. Thomas also provided an update to the Committee regarding the repeal of the one remaining rule for the Deferred Compensation Committee. Mr. Paul Matson, ASRS Director, is a member and Chair of this Committee and had been asked if the ASRS could manage this repeal. This action has been completed and will be effective in early June.

Mr. Jim Hillyard joined the meeting at 2:32 p.m.

4. Presentation, Discussion, and Appropriate Action Regarding an Update of the ASRS Employer Compliance

Mr. Anthony Guarino, Deputy Director and Chief Operations Officer, introduced the topic stating it has been 14 months since the Internal Audit Division discontinued performing employer audits and employer compliance was moved to the Member Services Division, Employer Relations Unit. Mr. Guarino turned the presentation over to Ms. Michele Briggs, Employer Relations Manager and Mr. Dave King, Assistant Director, Member Services Division.

Mr. King opened the discussion by indicating the goal is to engage at least 100 employers a year regarding a contribution anomaly or question based on data currently reported to the ASRS. The team reviewed fiscal year 2018 contributions of all 701 employers focusing on one trigger – did each member pay enough contributions to at least potentially be working 20 hours a week. As the program progresses there will be additional triggers implemented.

Ms. Briggs took a moment to introduce the Employer Relations team members. In attendance were, Ms. Marina Keith, Mr. Michael McCarthy and Mr. Michael Carr. Ms. Wendy Tobin was unable to attend but completes the team. Ms. Briggs reviewed the reports prepared by Ms. Courtney Micheau, Management and Benefits Analyst that were provided to the Committee. The team has currently exceeded their strategic goal of engaging at least 100 employers. They have engaged 180 employers to date with 159 employers needing some corrective action and communication with the Employer Relations Unit. The team has resolved 91 of the 159 issues. Ms. Briggs shared the engagement with Employers has been very positive. The Employers feel the ASRS is taking a proactive approach and working with them. Ms. Briggs concluded with the plan for this year which is to compare the 2018 report with 2019 to see if there are repeat Employers with the same anomalies and will add two new triggers in the review process. The two new triggers will be Return to Work and Alternate Contribution Rate.
5. Presentation, Discussion, and Appropriate Action Regarding the Internal Audit Quarterly Update

Mr. Harold Mackey, Chief Internal Auditor, reviewed the quarterly audit report with the Committee and provided the status of projects Internal Audit Division (IAD) is currently working on. Mr. Mackey noted he is currently recruiting to fill the Internal Auditor position recently vacated. Mr. Mackey advised he has placed a hold on the Biennial Audit Plan for FY2020-2021 until he finishes his recruitment so he has a better understanding of the skillset the incumbent brings to the team which will determine the type of audits the team will be able to perform. Mr. Mackey also advised he is re-evaluating the strategic plan for IAD to ensure the potential loss of a team member in the future will not impact their ability to meet goals.

Mr. Mackey advised two audits were in their final stages. The Vendor Efficacy audit is pending final management responses and the Espiritu Schools audit is pending the closing conference which will be held on Thursday, April 11, 2019. All other audit activities are moving forward.

6. Presentation, Discussion, and Appropriate Action Regarding the ASRS Information Security Program Update

Mr. Guarino provided an introduction of this topic indicating the ASRS recently completed its second annual internal risk assessment with Clearwater of which the results will be shared with the Committee in executive session.

Motion: Mr. Clark Partridge moved to go into executive session pursuant to A.R.S. § 38-431.03(A)(2) for the purpose of discussion or consideration of records exempt by law from public inspection. Mr. Michael Miller seconded the motion.

By a vote of 3 in favor, 0 opposed, 0 abstentions, and 0 excused, the motion was approved. The Trustee votes were as follows:

- Mr. Jim Hillyard – approved
- Mr. Clark Partridge – approved
- Mr. Michael Miller – approved

The Committee convened to Executive Session at 2:56 p.m.

The Committee reconvened to Public Session at 3:51 p.m.

7. Requests for Future Agenda Items

None were requested.

8. Call to the Public

No members of the public requested to speak.
9. The next regular public OALC meeting is scheduled for Wednesday, July 10, 2019, at 2:30 p.m., at 3300 N. Central Avenue, in the 14th Floor Conference room, Phoenix, Arizona.

Mr. Jim Hillyard noted the next OALC meeting is scheduled for Wednesday, July 10, 2019 at 2:30 p.m.

10. Adjournment of the OALC

Motion: Mr. Michael Miller moved to adjourn the meeting at 3:52 p.m. Mr. Clark Partridge seconded the motion.

By a vote of 3 in favor, 0 opposed, 0 abstentions, and 0 excused, the motion was approved. The Trustee votes were as follows:

- Mr. Jim Hillyard – approved
- Mr. Clark Partridge – approved
- Mr. Michael Miller – approved

Respectfully Submitted,

Melanie A. Alexander
Committee Administrator
ARIZONA STATE RETIREMENT SYSTEM
Agenda Item 2
Confidential Executive Session
Minutes were provided to the Trustees and not included in this book
Agenda Item #3
MEMORANDUM

TO: Mr. Jim Hillyard, Chair, Arizona State Retirement System (ASRS) Operations, Audit and Legislative Committee (OALC)

FROM: Mr. Anthony Guarino, Deputy Director and Chief Operations Officer
Ms. Martha N. Rozen, Chief of Administrative Services
Mr. Chris Gustafson, Procurement and Budget Program Manager
Ms. Kerry White, Assistant Chief Investment Officer

DATE: June 26, 2019

RE: Agenda Item #3: Presentation, Discussion, and Appropriate Action Regarding ASRS Budget-Related Topics Including:


Purpose
To review the ASRS appropriated and continuously appropriated budgets and the ASRS administrative and investment spending plans for fiscal years (FY) 2020 and 2021.

Recommendation
For agenda item 3.b, staff recommends that the OALC accept and forward to the ASRS Board of Trustees the following:

1) An appropriated budget request for FY 2021 in the amount of $24,194,000, with an understanding there may ultimately be changes to the total appropriated budget amount due to legislative and executive recommendations.

2) The proposed administrative spending plan of $30,033,300 and continuously appropriated investment spending plan of $138,267,200 for FY 2021 subject to revised management projections, and to include private markets performance incentives and other fees when identified and paid.
The ASRS vision includes being a leader in the area of operational effectiveness, and our values describe the culture we believe is necessary to achieve that vision. Through a formalized budget process, and in partnership with the executive and legislative branches, the ASRS historically has been able to develop and implement fiscally responsible spending plans that are flexible and support key agency strategic objectives and priorities as well as reflect a commitment to achieving efficiencies through maximizing resources and constraining costs.

Both the vision and the values serve as guideposts to the ASRS Strategic Plan, which establishes priorities, goals, and key performance indicators (KPIs) in support of overall purpose and mission. In accordance with Strategic Priority #4 – Optimize Operational Effectiveness, during the last three fiscal years the ASRS has continued to focus on targeted reductions to achieve budget and staffing goals.

As a result of strategic planning, the agency is on target to achieve or stay within the risk tolerance of established Key Performance Indicators (KPI) as planned by June 30, 2020.

<table>
<thead>
<tr>
<th>Category</th>
<th>Base Administrative Budget</th>
<th>Total Administrative Budget</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Actual and Projected Spend</td>
<td>Projected Spend</td>
</tr>
<tr>
<td></td>
<td>Dollars in Thousands</td>
<td>Dollars in Thousands</td>
</tr>
<tr>
<td></td>
<td>FY 2017</td>
<td>FY 2020</td>
</tr>
<tr>
<td>PS and ERE</td>
<td>$17,938.5</td>
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<td>P&amp;O</td>
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<td>Travel</td>
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<td>OOE</td>
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<td>$4,146.6</td>
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<tr>
<td>Equipment</td>
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<tr>
<td>Total</td>
<td>$28,521.9</td>
<td>$27,444.4</td>
</tr>
</tbody>
</table>

KPI - Percent reduction in base administrative expenses from July 1, 2017 to June 30, 2020 (excluding special line item expenditures)
Standard and Risk Tolerance = -3.0%

KPI - Total annual administrative expense variance (including special line item expenditures for service/security enhancements and anticipated cost reductions)
Standard = -1.5% Risk Tolerance = +3.0%

Building the FY 2020 and FY 2021 Budget
The ASRS has focused a great deal of time and attention on the future to manage budgets and implement strategies designed to improve operational effectiveness and/or make the ASRS more cost effective. This has set in motion a full review of the spending plan – with a new objective of remaining relatively flat in base administrative expenditures for the next several fiscal years. This includes aligning resources and dollars with the appropriate funding as outlined in the Arizona Revised Statutes.

For FY 2020 and FY 2021, the ASRS leadership through its efforts to build the spending plans, identified two critical components to the success of the agency: 1) Data, transactional and network security and 2) Information technology applications development and infrastructure architecture enhancements. As technology rapidly changes the ASRS has determined that targeted investments are needed to ensure the agency is positioned to implement future changes in an agile, resilient and secure manner.

Data, Transactional and Network Security Program
Beginning in July 2016, the agency began building a development and support security team by reallocating resources and focusing on the areas of data and network security and fraud. Because fraud efforts center on functions, applications, and processes related to the disbursement of pension-related
benefits, the ASRS utilizes continuously appropriated funds for the associated personal services, employee related expenses, and professional and outside services costs.

The team’s activities and related projects are a component of the entire cadre of security efforts, however only portions of the team’s expenses are currently funded with continuously appropriated funds; the remainder are paid for with appropriated dollars. Data, transactional and network security requires a significant amount of multi-faceted resources and this dual allocation of resources between budget sources creates a fiscal disconnect in groups that are, in reality, interconnected.

In order to maintain a robust data, transactional and network security program, staff recommends shifting all resources allocated to the security team to continuous appropriations. In doing so, the amount of funding attributed to this shift - an estimated $694,300 - is identified in the Base Administrative Budget as expected unspent funds for projected reversion.

**Information Technology Applications Development and Infrastructure Architecture Enhancements**

Information technology provides the framework for the ASRS business model. As the landscape continues to change and gain sophistication, IT organization, skills, processes, and tools, particularly as they relate to security levels and risk mitigation, need to continue to progress to effectively support and align business and service requirements. The ASRS requires resources who are dedicated subject matter experts to:

- Implement and execute identified improvement initiatives;
- Configure and optimize the use of new or existing tools;
- Stay relevant and establish new measures as IT security and risk are redefined;
- Ensure compliance with regulatory requirements.

The following projects are currently in progress or have been supported previously by the OALC and the ASRS Board of Trustees:

- Benefits Disbursement project – to reduce the annual costs, over time, for all categories of disbursements. FY 2020 represents the final year of this project.
- Automation Upgrades and Oracle Modernization project – to achieve a standards-based set of technologies by re-engineering business process to increase productivity, reduce costs, mitigate risks, and improve member service. FY 2021 represents the final year of this project.
- Information Protection and Security project – to increase the security of Personally Identifiable Information (PII) and create a more robust data logging system and stronger monitoring tools for internal applications. This will reduce access and exposure to PII during the course of performing business functions, as well as improve the ASRS’s privacy and security posture.
A. FY 2020 Appropriated Budget and Spending Plans

The ASRS FY 2020 and FY 2021 administrative spending plans, as presented in sections A. and B. of this document, further support system and technology modernizations and re-engineering of processes, with the goal of avoiding future costs associated with more costly transactions and processes.

Staff recommends amending the FY 2020 spending plan to include the following projects:

- Technology Improvements project – to achieve operational efficiency as well as to position the agency for a successful migration to the cloud by re-designing the ASRS application architecture into a continuous integration continuous deployment (CICD) pipeline or implementing a DevOps methodology. By setting up the required infrastructure and environment, the agency will be able to develop, build, and deploy on a more agile and frequent implementation schedule – reducing business delays and manual processes while optimizing the utilization of future cloud services.

  As projected unspent appropriations funding is identified for FY 2020, this recommendation does not require an increase in appropriations.

- Risk Mitigation project – to mature the ASRS data, transactional and network security program by implementing a long-term strategy and continuous processes for mitigating any security gaps and reducing the time to vulnerability remediation. For several years, the ASRS has, in consultation with external firms, assessed its security and privacy maturity and has implemented processes to improve physical, data, transactional, privacy, and cash control security. Information, privacy and system security requires a sustained effort to maintain and expand fraud detection capabilities; to minimize, identify, and remove vulnerabilities; and to integrate approaches and practices across agency functions.

In summary, the following highlights the changes staff is recommending in the spending plans for FY 2020:

- A shift of $694,300 from the Base Operating Appropriations to Continuous Appropriations for data and network security services that the agency and board have deemed consistent with continuously appropriated services as outlined in A.R.S 38-721(C)(4).
- Expenditures of approximately $270,000 for the Technology Improvements project utilizing Base Operating Appropriations.
- Expenditures of approximately $280,000 for the Risk Mitigation project utilizing Continuous Appropriations.

These changes to FY 2020 allow the agency to expedite needed projects, as well as keep the agency within the budget/spending plans from the ASRS Administrative and the Investment Spending Plans for FY 2020 as approved by the Board on August 31, 2018.

See Attachments A and B for a summary and associated detail of the ASRS administrative spending plan for FY 2020.

FY 2020 Investment Spending Plan

The ASRS FY 2020 investment spending plan includes expenditures for the following in order to meet investment objectives:

- Internal investment management
  - ASRS Investment Management Division (IMD) staff base salaries and employer-paid expenses (benefits and payroll taxes), travel, education and training, rent, and other operational costs.
External investment management

- Public Markets
  - Investment management fees. The majority of quarterly investment management fees are calculated based on the market value of the investments, using the assumption of a 7.5% annual rate of return less estimated net cash flows of 2.5%. Accordingly, the fees are directly correlated with both investment performance as well as net cash flows. A number of external investment managers employ an overlay strategy and have structured agreements to pay fees only when targeted results are achieved. Such fees are not projected and are only reported, on a cash basis, when identified and paid.

  - Transactional and other fees include foreign taxes and commissions on derivatives and other incidental costs.

- Private Markets - Private Equity, Real Estate, and Private Credit
  - Investment management fees. These fees are calculated based on the percentage of committed capital to the program. These fees are correlated to capital commitments in the program and are calculated on a cash basis.

  - Performance incentive and other fees include performance incentives and carried interest, which are only paid if earned - upon successful performance of the manager after other return criteria are met – or incurred, and other contractually agreed-upon fees and expenses. Due to the nature of the investments and contingent variables, estimated annual performance incentive and other fees are not projected and are only reported, on a cash basis, when identified and paid.

Consulting fees

- Investment-related consulting and legal fees, electronic information services and subscriptions, custodial banking administrative fees, and external auditing service fees. In order to gain insight into portfolios, investment performance, compliance, and investment opportunities, the ASRS utilizes supplemental, coordinated services of external professionals and data platforms.

See Attachment C for a summary and associated detail of the ASRS investment spending plan.

B. FY 2021 Appropriated Budget Request and Spending Plans

The ASRS FY 2021 appropriated budget request is $24,194,000, which maintains current appropriations levels. Additionally, please note, the base administrative budget is projected to experience a slight reduction in continuous appropriations.

Staff also recommends the FY 2021 spending plan to include budget for the final year of the following projects:

- Automation Upgrades and Oracle Modernization project
- Technology Improvements project
- Risk Mitigation project

Continuing and new projects include:

- Information Protection and Security project. FY 2021 represents the second year of the three-plus year project.
- Retiree Payroll Applications project - to update the pension payroll application coding to achieve
efficiency in producing timely and accurate payments. The current payroll processing applications are written in aging code and are batch based, which increases support costs and creates delays in pension payroll processing. FY 2021 represents the first year of the approximately four-year project.

See Attachment D for a summary of the ASRS FY 2021 appropriated budget request and Attachment E for the FY 2021 administrative spending plan.

FY 2021 Investment Spending Plan
The ASRS FY 2021 investment spending plan includes the following:

- Continuously appropriated funding for the ASRS investment management program. Expenditures include investment management, consulting, legal, custodial banking, and external financial services fees; data subscriptions and analytics services; and FTE salaries and benefits, as well as travel, education, and other operational costs.

See Attachment C for a summary and associated detail of the ASRS investment spending plan.

Attachments

*Agenda Item 3.a*
A: FY 2020 ASRS Administrative Spending Plan
B: Administrative Projects Detail
C: ASRS Investment Spending Plan

*Agenda Item 3.b*
D: FY 2021 Appropriated Budget Request
E: FY 2021 ASRS Administrative Spending Plan
C: ASRS Investment Spending Plan
## FY 2020 ASRS Administrative Spending Plan

### Base Administrative Budget

<table>
<thead>
<tr>
<th>Long Term Disability Appropriations</th>
<th>Base Administrative Budget Subtotal</th>
<th>Technology Services Improvements Projected Unspent of Base Appropriations</th>
<th>Administrative Projects Budget</th>
<th>Obj YOY: -1.50% Projected: 1.12%</th>
</tr>
</thead>
<tbody>
<tr>
<td>Salaries and wages, employer costs for benefits</td>
<td>17,067,200</td>
<td>-</td>
<td>1,650,700</td>
<td>18,717,900</td>
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<tr>
<td>Taxes, and ADOA Charges</td>
<td>276,000</td>
<td>-</td>
<td>-</td>
<td>276,000</td>
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<tr>
<td>Investment Incentive Compensation Plan payments to employees</td>
<td>309,400</td>
<td>-</td>
<td>-</td>
<td>309,400</td>
</tr>
<tr>
<td><strong>Total PS and ERE</strong></td>
<td>17,652,600</td>
<td>-</td>
<td>1,650,700</td>
<td>19,303,300</td>
</tr>
</tbody>
</table>

### Professional and Outside Services (P&O)

| IT security professional services and consulting | 188,000 | - | - | - | - | - | - | - | 280,000 | 468,000 |
| Legal fees for external counsel, attorney general charges/staff, administrative hearing costs | 188,000 | - | - | - | - | - | - | - | 280,000 | 468,000 |
| Other outside services | 55,000 | - | - | 55,000 | - | - | - | - | - | 55,000 |
| **Total P&O** | 1,265,400 | 660,000 | 225,000 | 1,661,800 | - | 225,000 | 132,600 | 189,400 | - | 5,014,800 |

### Travel

| In-state travel for member and employer outreach | 30,000 | - | - | 30,000 | - | - | - | - | 30,000 |
| Out-of-state travel to pension industry and educational conferences | 49,000 | - | - | 49,000 | - | - | - | - | 49,000 |
| **Total Travel** | 79,000 | - | - | 79,000 | - | - | - | - | 79,000 |

### Other Operating Expenditures (OOE)

| Office rent | 1,363,900 | - | 1,554,100 | 276,000 | - | 276,000 | - | - | - | 1,554,100 |
| Software licenses and support | 276,000 | - | 276,000 | - | - | - | - | - | - | 276,000 |
| ADOA Risk Management insurance premiums | 279,600 | - | 279,600 | - | - | - | - | - | - | 279,600 |
| Advertisement and promotions | 30,000 | - | 30,000 | - | - | - | - | - | - | 30,000 |
| Equipment repair and maintenance | 20,000 | - | 20,000 | - | - | - | - | - | - | 20,000 |
| **Total OOE** | 2,313,200 | 1,833,400 | 4,144,600 | 45,000 | - | 4,144,600 | 45,000 | - | - | 4,191,600 |

### Equipment

| Agency furniture purchases/replacement | 20,000 | - | 20,000 | - | - | - | - | - | - | 20,000 |
| Network, server, PC and related devices replacement and additions | 369,500 | - | 369,500 | - | - | - | - | - | - | 369,500 |
| **Total Equipment** | 389,500 | - | 389,500 | - | - | - | - | - | - | 389,500 |

### TOTAL

| 21,699,700 | $ 1,600,000 | $ 4,144,600 | $ 21,444,400 | $ 270,000 | $ 1,669,500 | $ 284,100 | $ 484,200 | $ 280,000 | $ 31,056,500 |

### Appropriated/Budgeted Amounts

| 22,394,000 | 1,800,000 | 4,144,700 | 28,338,700 | 270,000 | 1,669,500 | 284,100 | 484,200 | 280,000 | 31,056,500 |

**Notes:**
- Appendix A
- Revised Statute § 38-721(C) lists specific expenditures that are continuously appropriated in the amount deemed necessary by the Board, including rent, actuarial consulting fees, and costs associated with administering retiree pension benefits and disbursements.
## Administrative Projects Detail

### FY 2014 to FY 2021

**Automation Upgrades and Oracle Modernization Project Special Line Item Appropriations (Non-Lapsing) (PIJ RT13001: Oracle Forms and Reports Modernization)**

Objective: Evolve legacy technologies to newer standards-based technologies and re-engineer business processes to increase productivity, reduce costs, mitigate risks, protect and secure information, improve member satisfaction and improve service turnaround time to members.

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<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Totals</td>
<td>1,390,000</td>
<td>4,484,500</td>
<td>2,270,000</td>
<td>2,070,000</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>10,214,500</td>
</tr>
</tbody>
</table>

**APPROPRIATED LINE ITEM BUDGET**

**ACTUAL AND ESTIMATED SPEND**

<table>
<thead>
<tr>
<th></th>
<th></th>
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<th></th>
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<th></th>
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<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>1,117,400</td>
<td>1,736,200</td>
<td>909,100</td>
<td>1,041,100</td>
<td>1,364,200</td>
<td>1,470,200</td>
<td>1,669,500</td>
<td>906,800</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>10,214,500</td>
</tr>
</tbody>
</table>

### FY 2016 to FY 2020

**Benefits Disbursement Project Continuous Appropriations (PIJ RT15003: ASRS Benefits Disbursement)**

Objective: Develop platform and disbursement-related processes to administer the entire benefit cycle in-house, which includes benefit calculations, electronic payment transmission, printing/mailing checks and remittance advice, and tax withholding/reporting.

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Totals</td>
<td>950,400</td>
<td>658,100</td>
<td>676,800</td>
<td>696,000</td>
<td>35,500</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>3,016,800</td>
</tr>
</tbody>
</table>

**PIJ FUNDING PROJECTION**

**ACTUAL AND ESTIMATED SPEND**

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Totals</td>
<td>637,700</td>
<td>691,700</td>
<td>843,200</td>
<td>560,100</td>
<td>284,100</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>3,016,800</td>
</tr>
</tbody>
</table>

### FY 2020 to FY 2023

**Information Protection and Security Project Continuous Appropriations (PIJ RT19002: Information Protection and Security)**

Objective: Increase the security of Personally Identifiable Information (PII) and create a more robust data logging system for internal applications.

<table>
<thead>
<tr>
<th>Project</th>
<th>FY 2020</th>
<th>FY 2021</th>
<th>FY 2022</th>
<th>FY 2023</th>
<th>FY 2024</th>
<th>Project Totals</th>
</tr>
</thead>
<tbody>
<tr>
<td>Totals</td>
<td>484,200</td>
<td>765,600</td>
<td>758,600</td>
<td>758,600</td>
<td>-</td>
<td>2,767,000</td>
</tr>
</tbody>
</table>

**PIJ FUNDING PROJECTION**

**ESTIMATED SPEND**

<table>
<thead>
<tr>
<th></th>
<th>FY 2020</th>
<th>FY 2021</th>
<th>FY 2022</th>
<th>FY 2023</th>
<th>FY 2024</th>
<th>Project Totals</th>
</tr>
</thead>
<tbody>
<tr>
<td>Totals</td>
<td>484,200</td>
<td>765,600</td>
<td>758,600</td>
<td>758,600</td>
<td>-</td>
<td>2,767,000</td>
</tr>
</tbody>
</table>

### New Project Requests

### FY 2020 to FY 21

**Technology Services Improvements Project Base Operating Appropriations (Projected Unspent)**

Objective: To achieve operational efficiency as well as to position the agency for a successful migration to the cloud by implementing continuous integration continuous deployment (CI/CD) or DevOps methodology, setting up the required infrastructure and environment, and migrating some ASRS data center components to the ADOA Shared Hosted Data Center.

<table>
<thead>
<tr>
<th>Project</th>
<th>FY 2020</th>
<th>FY 2021</th>
<th>FY 2022</th>
<th>FY 2023</th>
<th>FY 2024</th>
<th>Project Totals</th>
</tr>
</thead>
<tbody>
<tr>
<td>Totals</td>
<td>270,000</td>
<td>381,000</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>651,000</td>
</tr>
</tbody>
</table>

**FUNDING PROJECTION**

**ESTIMATED SPEND**

<table>
<thead>
<tr>
<th></th>
<th>FY 2020</th>
<th>FY 2021</th>
<th>FY 2022</th>
<th>FY 2023</th>
<th>FY 2024</th>
<th>Project Totals</th>
</tr>
</thead>
<tbody>
<tr>
<td>Totals</td>
<td>270,000</td>
<td>381,000</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>651,000</td>
</tr>
</tbody>
</table>

### FY 2020 to FY 21

**Risk Mitigation Project Continuous Appropriations**

Objective: Mature the ASRS security program by implementing a long-term strategy and continuous processes for mitigating any security gaps and reducing the time to vulnerability remediation.

<table>
<thead>
<tr>
<th>Project</th>
<th>FY 2020</th>
<th>FY 2021</th>
<th>FY 2022</th>
<th>FY 2023</th>
<th>FY 2024</th>
<th>Project Totals</th>
</tr>
</thead>
<tbody>
<tr>
<td>Totals</td>
<td>280,000</td>
<td>280,000</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>560,000</td>
</tr>
</tbody>
</table>

**PIJ FUNDING PROJECTION**

**ESTIMATED SPEND**

<table>
<thead>
<tr>
<th></th>
<th>FY 2020</th>
<th>FY 2021</th>
<th>FY 2022</th>
<th>FY 2023</th>
<th>FY 2024</th>
<th>Project Totals</th>
</tr>
</thead>
<tbody>
<tr>
<td>Totals</td>
<td>280,000</td>
<td>280,000</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>560,000</td>
</tr>
</tbody>
</table>

### FY 2021 to FY 24

**Retiree Payroll Application Project Continuous Appropriations (PIJ in process)**

Objective: Update the pension payroll application coding to achieve efficiency in producing timely and accurate payments.

<table>
<thead>
<tr>
<th>Project</th>
<th>FY 2021</th>
<th>FY 2022</th>
<th>FY 2023</th>
<th>FY 2024</th>
<th>Project Totals</th>
</tr>
</thead>
<tbody>
<tr>
<td>Totals</td>
<td>329,700</td>
<td>659,300</td>
<td>659,300</td>
<td>214,200</td>
<td>1,862,500</td>
</tr>
</tbody>
</table>

**PIJ FUNDING PROJECTION**

**ESTIMATED SPEND**

<table>
<thead>
<tr>
<th></th>
<th>FY 2021</th>
<th>FY 2022</th>
<th>FY 2023</th>
<th>FY 2024</th>
<th>Project Totals</th>
</tr>
</thead>
<tbody>
<tr>
<td>Totals</td>
<td>329,700</td>
<td>659,300</td>
<td>659,300</td>
<td>214,200</td>
<td>1,862,500</td>
</tr>
</tbody>
</table>
## ASRS Investment Spending Plan

<table>
<thead>
<tr>
<th></th>
<th>FY 2019 ESTIMATED</th>
<th>FY 2020 PROJECTION</th>
<th>FY 2021 PROJECTION</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Investment Management Expenses</strong>*</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Internal Investment Management</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Salaries and benefits</td>
<td>$1,494,000</td>
<td>$1,547,300</td>
<td>$1,547,300</td>
</tr>
<tr>
<td>Investment Incentive Compensation Plan (ICP)(^1)</td>
<td>$293,800</td>
<td>$309,400</td>
<td>$309,400</td>
</tr>
<tr>
<td>Travel, education and training, rent, and other operational expenses</td>
<td>$266,400</td>
<td>$265,100</td>
<td>$266,000</td>
</tr>
<tr>
<td><strong>Public Markets</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>External investment management fees</td>
<td>$12,858,800</td>
<td>$4,416,000</td>
<td>$4,642,000</td>
</tr>
<tr>
<td>Transactional and other fees(^2)</td>
<td>$5,181,600</td>
<td>$5,000,000</td>
<td>$5,000,000</td>
</tr>
<tr>
<td><strong>Private Markets(^3)</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Private Equity management fees</td>
<td>$53,746,000</td>
<td>$58,646,000</td>
<td>$61,845,000</td>
</tr>
<tr>
<td>Real Estate management fees</td>
<td>$10,297,200</td>
<td>$18,062,000</td>
<td>$18,262,000</td>
</tr>
<tr>
<td>Private Credit management fees</td>
<td>$26,575,900</td>
<td>$28,015,300</td>
<td>$29,177,700</td>
</tr>
<tr>
<td><strong>Custodial Banking, Security Lending and Master Cash STIF Fees</strong></td>
<td>$3,000,000</td>
<td>$4,030,500</td>
<td>$4,030,500</td>
</tr>
<tr>
<td><strong>Investment Management Expenses Subtotal</strong></td>
<td>$113,713,700</td>
<td>$120,291,600</td>
<td>$125,079,900</td>
</tr>
<tr>
<td><strong>Investment Related Consulting, Legal and Information Services Expenses</strong>*</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Investment Consulting Services</td>
<td>$4,469,900</td>
<td>$5,342,300</td>
<td>$5,370,300</td>
</tr>
<tr>
<td>Investment Related Legal Services</td>
<td>$3,830,800</td>
<td>$4,240,000</td>
<td>$4,240,000</td>
</tr>
<tr>
<td>Investment Electronic Information Services</td>
<td>$2,828,000</td>
<td>$3,204,500</td>
<td>$3,457,000</td>
</tr>
<tr>
<td>External Financial Consulting Services</td>
<td>$121,500</td>
<td>$120,000</td>
<td>$120,000</td>
</tr>
<tr>
<td><strong>Services Expenses Subtotal</strong></td>
<td>$11,250,200</td>
<td>$12,906,800</td>
<td>$13,187,300</td>
</tr>
<tr>
<td><strong>Total Continuously Appropriated Investment Expenses</strong></td>
<td>$124,963,900</td>
<td>$133,198,400</td>
<td>$138,267,200</td>
</tr>
</tbody>
</table>

---

\(^1\) The ICP is paid with base operating budget appropriated dollars.

\(^2\) Fees for investment managers employing an overlay strategy are not projected and are only reported, on a cash basis, when identified and paid.

\(^3\) Due to the nature of the investments and contingent variables, estimated annual performance incentive and other certain fees and expenses that are contractually agreed upon are not projected and are only reported, on a cash basis, when identified and paid. The ASRS has paid approximately $73,562,800 in performance incentive and other fees in FY 2019.

*Arizona Revised Statute § 38-721(C) specific expenditures are continuously appropriated in the amount necessary to meet the Board's investment objectives, including investment management and related consulting fees.
## FY 2021 Appropriated Budget Request

<table>
<thead>
<tr>
<th></th>
<th>FY 2019 Appropriations</th>
<th>FY 2020 Appropriations</th>
<th>Request FY 2021 Appropriations</th>
</tr>
</thead>
<tbody>
<tr>
<td>Appropriated FTEs</td>
<td>245.9</td>
<td>240.9</td>
<td>240.9</td>
</tr>
<tr>
<td>Personal Services &amp; Employee Related Expenditures</td>
<td>$18,281,900</td>
<td>$18,346,900</td>
<td>$18,346,900</td>
</tr>
<tr>
<td>Professional and Outside Services</td>
<td>$1,277,400</td>
<td>$1,265,400</td>
<td>$1,265,400</td>
</tr>
<tr>
<td>Travel - In State</td>
<td>$30,000</td>
<td>$30,000</td>
<td>$30,000</td>
</tr>
<tr>
<td>Travel - Out of State</td>
<td>$49,000</td>
<td>$49,000</td>
<td>$49,000</td>
</tr>
<tr>
<td>Other Operating Expenditures</td>
<td>$2,302,500</td>
<td>$2,313,200</td>
<td>$2,313,200</td>
</tr>
<tr>
<td>Equipment</td>
<td>$389,500</td>
<td>$389,500</td>
<td>$389,500</td>
</tr>
<tr>
<td>Base Operating Budget Subtotal</td>
<td>$22,330,300</td>
<td>$22,394,000</td>
<td>$22,394,000</td>
</tr>
<tr>
<td>Long Term Disability Program Administration (LTD)</td>
<td>$2,200,000</td>
<td>$1,800,000</td>
<td>$1,800,000</td>
</tr>
<tr>
<td>Total Appropriated Operating Budget</td>
<td>$24,530,300</td>
<td>$24,194,000</td>
<td>$24,194,000</td>
</tr>
<tr>
<td>Special Line Item Appropriations One-time IT Expenses</td>
<td>$500,000</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Total Appropriated Budget</td>
<td>$25,030,300</td>
<td>$24,194,000</td>
<td>$24,194,000</td>
</tr>
</tbody>
</table>

### Changes to Appropriations

- **FY 2020 - FTE Resource Reallocation:** -5.0%, -2.0%
- **FY 2020 - Statewide Adjustments (increase in retirement, IT pro rata, and health insurance employer costs):** $63,700, 0.3%
- **FY 2020 - LTD Administration Fees:** $(400,000), -1.6%
- **FY 2020 - Remove One-time IT Expenses:** $(500,000), -2.0%
- **Subtotals:** $(836,300), -3.2%

- **FY 2021:** 0.0%, 0.0%

---

**Attachment D**
## FY 2021

### ASRS Administrative Spending Plan

#### Base Administrative Budget

<table>
<thead>
<tr>
<th>Description</th>
<th>Base Operating Appropriations</th>
<th>Long Term Disability Appropriations</th>
<th>Pension Payroll, Rent, and Actuarial Fees Continuous Appropriations*</th>
<th>Total Budget Subtotal</th>
</tr>
</thead>
<tbody>
<tr>
<td>Personal Services (PS) and Employee Related Expenses (ERE)</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Salaries and wages, employer costs for benefits, taxes, and ADOA charges</td>
<td>17,067,200</td>
<td></td>
<td>1,690,700</td>
<td>18,757,900</td>
</tr>
<tr>
<td>Variable Compensation Strategies Plan payments to employees</td>
<td>276,000</td>
<td></td>
<td></td>
<td>276,000</td>
</tr>
<tr>
<td>Investment Incentive Compensation Plan payments to investment management employees</td>
<td>309,400</td>
<td></td>
<td></td>
<td>309,400</td>
</tr>
<tr>
<td>Total PS and ERE</td>
<td>17,652,600</td>
<td></td>
<td>1,690,700</td>
<td>19,343,300</td>
</tr>
<tr>
<td>Professional and Outside Services (P&amp;O)</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>LTD Program administrative costs for claim processing</td>
<td>-</td>
<td>1,600,000</td>
<td>-</td>
<td>1,600,000</td>
</tr>
<tr>
<td>Pension payroll disbursement plan</td>
<td>-</td>
<td>112,100</td>
<td>-</td>
<td>112,100</td>
</tr>
<tr>
<td>IT Development support and business applications</td>
<td>627,600</td>
<td></td>
<td>1,600,000</td>
<td>2,227,600</td>
</tr>
<tr>
<td>Actuarial and benefit consulting services</td>
<td>-</td>
<td>340,000</td>
<td>-</td>
<td>340,000</td>
</tr>
<tr>
<td>IT Security professional services and consulting</td>
<td>188,000</td>
<td></td>
<td></td>
<td>188,000</td>
</tr>
<tr>
<td>Legal fees for external counsel, attorney general</td>
<td>359,800</td>
<td></td>
<td></td>
<td>359,800</td>
</tr>
<tr>
<td>Total P&amp;O</td>
<td>1,265,400</td>
<td>1,600,000</td>
<td>506,600</td>
<td>3,372,000</td>
</tr>
<tr>
<td>Travel</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>In-state travel for member and employer outreach</td>
<td>30,000</td>
<td></td>
<td></td>
<td>30,000</td>
</tr>
<tr>
<td>Out-of-state travel to pension industry and educational conferences</td>
<td>49,000</td>
<td></td>
<td></td>
<td>49,000</td>
</tr>
<tr>
<td>Total Travel</td>
<td>79,000</td>
<td></td>
<td></td>
<td>79,000</td>
</tr>
<tr>
<td>Other Operating Expenditures (OOE)</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Office rent</td>
<td>-</td>
<td>1,589,000</td>
<td>1,589,000</td>
<td>1,589,000</td>
</tr>
<tr>
<td>Software licenses and support</td>
<td>1,376,000</td>
<td></td>
<td>13,766,000</td>
<td>145,000</td>
</tr>
<tr>
<td>Telecom communications</td>
<td>276,000</td>
<td></td>
<td></td>
<td>276,000</td>
</tr>
<tr>
<td>ADOA Risk Management insurance premiums</td>
<td>279,600</td>
<td></td>
<td></td>
<td>279,600</td>
</tr>
<tr>
<td>Newsletter printing and mailing</td>
<td>130,000</td>
<td></td>
<td></td>
<td>130,000</td>
</tr>
<tr>
<td>Professional dues, subscriptions, and publications</td>
<td>80,000</td>
<td></td>
<td>197,300</td>
<td>277,300</td>
</tr>
<tr>
<td>Postage and delivery</td>
<td>80,000</td>
<td></td>
<td></td>
<td>86,900</td>
</tr>
<tr>
<td>Education, training and conferences; employee tuition</td>
<td>30,000</td>
<td></td>
<td>30,000</td>
<td>11,000</td>
</tr>
<tr>
<td>Total OOE</td>
<td>2,313,200</td>
<td></td>
<td></td>
<td>4,186,400</td>
</tr>
<tr>
<td>Equipment</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Agency furniture purchases/replacement</td>
<td>39,500</td>
<td></td>
<td></td>
<td>39,500</td>
</tr>
<tr>
<td>Network, server, PC and related devices replacement and additions</td>
<td>350,000</td>
<td></td>
<td></td>
<td>350,000</td>
</tr>
<tr>
<td>Total Equipment</td>
<td>389,500</td>
<td></td>
<td></td>
<td>389,500</td>
</tr>
<tr>
<td>TOTAL</td>
<td>$21,699,700</td>
<td>$1,600,000</td>
<td>$4,070,500</td>
<td>$27,370,200</td>
</tr>
</tbody>
</table>

#### Administrative Projects Budget

<table>
<thead>
<tr>
<th>Description</th>
<th>Technology Services Improvements Projected Unspent of Base Appropriations</th>
<th>Automation Upgrades and Oracle Modernization Special Line Item Appropriations</th>
<th>Information Protection Security Continuous Appropriations*</th>
<th>Retiree Payroll Application Continuous Appropriations*</th>
<th>Risk Mitigation Continuous Appropriations*</th>
<th>Total Administrative Budget Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>APPROPRIATED/BUDGETED AMOUNTS</td>
<td>22,394,000</td>
<td>28,264,500</td>
<td>173,300</td>
<td>2,012,600</td>
<td>513,300</td>
<td>$30,533,300</td>
</tr>
<tr>
<td>FY 2021 PROJECTED SPEND</td>
<td>21,699,700</td>
<td>27,370,200</td>
<td>173,300</td>
<td>2,012,600</td>
<td>513,300</td>
<td>$30,533,300</td>
</tr>
</tbody>
</table>

*Arizona Revised Statute § 38-721(C) lists specific expenditures that are continuously appropriated in the amount deemed necessary by the Board, including rent, actuarial consulting fees, and costs associated with administering retiree pension benefits and disbursements.
Agenda Item #4
MEMORANDUM

TO: Mr. Jim Hillyard, Chair, ASRS Operations, Audit and legislative Committee (OALC)
FROM: Mr. Anthony Guarino, Deputy Director and Chief Operations Officer
       Mr. Harold Mackey, Chief Internal Auditor
DATE: June 28, 2019
RE:  Agenda Item #4: Presentation, Discussion, and Appropriate Action Regarding the Quarterly Audit Update

Purpose
To provide Internal Audit (IA) Division’s current status of the annual audit plan for FY 2019 Q4. This quarterly report contains the budgeted and actual hours for each audit and audit-related services as well as notable IA services performed over the reporting period.

Recommendation
Information only, no action required.

Background
The IA Audit Plan covering FY 2019 is an annual plan modeled after prior year’s plans. The plan is based on most current agency risk assessments conducted by the ASRS executive and senior managers, under the oversight of the Operations, Audit and Legislative Committee (OALC) and in collaboration with IA.

Significant audit plan changes from Q3 reporting:
- Initial draft of the Biennial Audit Plan prepared for FYs 2020-2021
- Re-engagement of Risk management Committee
- Completed initial draft of an IA strategic plan to provide divisional guidance in support of agency-wide initiatives
- Reassigned two Audits: Management/Investment Fees and Health Insurance Supplements
- Total hours available to perform audits or audit-related work is 5,520 hours
  - Estimated 853 hours consumed during Q4
  - Estimated 3,487 hours remaining

The plan is based on an audit staff of one Chief Auditor and two Audit Officers (Internal auditors).

The OALC reserves the right to re-evaluate the plan and recommend changes at any time during the fiscal year.
Arizona State Retirement System
Internal Audit Division
FY 2019/Q4
Quarterly Report
July, 2019
• Executive Summary
• Status – Current Activities
• Status – Work Plan Hours
Professional and Statutory Requirements

This document provides the Quarterly update to the Fiscal Year 2019 Audit Plan (Audit Plan) as required by professional auditing standards, the Arizona State Retirement System Internal Audit Charter as follows:

PS 2030—Resource Management
- The chief audit executive must ensure that internal audit resources are appropriate, sufficient, and effectively deployed to achieve the approved plan.

PS 2060—Reporting to Senior Management and the Board
- The chief audit executive must report periodically to senior management and the board on the internal audit activity’s purpose, authority, responsibility, and performance relative to its plan and on its conformance with the Code of Ethics and the Standards. Reporting must also include significant risk and control issues, including fraud risks, governance issues, and other matters that require the attention of senior management and/or the board.

Changes Subsequent to Approval

Interim changes to the Audit Plan will occur from time to time due to changes in business risks, timing of ASRS' initiatives, and staff availability. We will report Audit Plan changes to executive management and present changes to the OALC at the next quarterly Committee meeting. Amendments to the approved Audit Plan deemed to be significant (based on discussions with the executive director and OALC chair) will be submitted to the OALC for recommendation to the Board for approval.
<table>
<thead>
<tr>
<th>Title</th>
<th>Status</th>
</tr>
</thead>
<tbody>
<tr>
<td>Update IAD Charter</td>
<td>Completed</td>
</tr>
<tr>
<td>Realign communications process with MSD/FSD</td>
<td>Completed</td>
</tr>
<tr>
<td>Update IA procedures to align with enhanced audit functions</td>
<td>Working</td>
</tr>
<tr>
<td>Reassess IA staff strategic goals and objectives</td>
<td>Completed</td>
</tr>
<tr>
<td>Training/Skills realignment for IA staff</td>
<td>On-going</td>
</tr>
<tr>
<td>Evaluate Quality Reviews</td>
<td>Completed</td>
</tr>
<tr>
<td>Re-engage the Risk Management Committee</td>
<td>On-going</td>
</tr>
<tr>
<td>Wrap-up existing Employer Audits</td>
<td>On-going</td>
</tr>
<tr>
<td>Perform quality reviews for the balance of FY 2018</td>
<td>Completed</td>
</tr>
<tr>
<td>Complete existing audits per audit plan</td>
<td>Working</td>
</tr>
<tr>
<td>Develop the FYs 2020-2021 Biennial Plan</td>
<td>Working</td>
</tr>
</tbody>
</table>
• Health Insurance Subsidies – Audit has been reassigned, restructured and restarted.
• Vendor Efficacy – Audit activities are complete.
• Espiritu Schools – Audit activities are complete.
• Service Purchase/CNW QR – Recommenced monthly quality review of the new SP/CNW beginning with month-end January 2019 data. IA to provide a recommendation to continue/discontinue testing at the conclusion of June 2019 testing. Preliminary report: No significant finding.
• Management fees – Audit has been reassigned and restarted.
• Follow up Audits – Recent activities from a previous ER audit of Griffin Foundation requires additional follow-up activities.
QUARTERLY ACTIVITIES

• ERM – Continue to monitor development including the loading of risks into the ERM tool. Test of application (ARM) feasibility appears to be successful. Further testing is on-going.
• IRM – Continue to monitor.
• Employer Updates – Actively monitoring activities including work products development, issues and concerns.
• In-House Disbursements – Monitoring production. Need to assess risk identification and internal controls development.
• Fraud Hotline – Updated the SOP. Reviewed alternative methods for reporting potential fraud activities.

Advisory Services
• Biennial Audit Plan – Preliminary review of initial draft plan by EMT. Addresses fiscal years (2020-2021). Specifies IA services (Audit, Advisory/Consultation, and Oversight) and other activities. To be updated based on a reevaluation of preliminary agency-related risks.

• IA Strategic Plan – Draft completed. Defines IA services to support the ASRS Strategic Plan with a focus on critical success factors, new audit methods and programs, and metrics to evaluate success.

• Year-end Assessment – Draft in process. Will provide a recap of IA activities over the FY 2019 audit period.

• Quality Assurance and Improvement Program (QAIP) – Program development in-process.
### QUARTERLY ACTIVITIES

<table>
<thead>
<tr>
<th>Title of Activity</th>
<th>Budgeted Hours</th>
<th>Actual Hours Worked</th>
<th>Remaining</th>
<th>% Hours Utilized</th>
<th>Status</th>
<th>Comments</th>
</tr>
</thead>
<tbody>
<tr>
<td>Audit/Audit Related</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Management / Investment Fees</td>
<td>500</td>
<td>168</td>
<td>332</td>
<td>34%</td>
<td>In-progress</td>
<td>Reassigned</td>
</tr>
<tr>
<td>Cash Controls Audit</td>
<td>500</td>
<td>22</td>
<td>478</td>
<td>4%</td>
<td>In-progress</td>
<td></td>
</tr>
<tr>
<td>Health Insurance Supplements</td>
<td>300</td>
<td>140</td>
<td>160</td>
<td>47%</td>
<td>In-progress</td>
<td>Reassigned</td>
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<tr>
<td>GASB 68 Testing</td>
<td>400</td>
<td>221</td>
<td>179.5</td>
<td>55%</td>
<td>In-progress</td>
<td></td>
</tr>
<tr>
<td>Agency Incoming Correspondence</td>
<td>360</td>
<td>449</td>
<td>51</td>
<td>90%</td>
<td>Completed</td>
<td></td>
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<tr>
<td>Vendor Efficacy Testing ²</td>
<td>500</td>
<td>51</td>
<td></td>
<td></td>
<td>In-progress</td>
<td></td>
</tr>
<tr>
<td>Espiritu Schools³</td>
<td>200</td>
<td>224</td>
<td>-24</td>
<td>112%</td>
<td>Completed</td>
<td></td>
</tr>
<tr>
<td>Military Call-up Service Credit ²</td>
<td>960</td>
<td>240</td>
<td>720</td>
<td>25%</td>
<td>Completed</td>
<td></td>
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<tr>
<td>Follow Up of Previous Year’s Audits</td>
<td>100</td>
<td>150</td>
<td></td>
<td></td>
<td>On-Hold</td>
<td>Due To IA Restructuring</td>
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<tr>
<td>Quality Reviews</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Refunds Process Testing</td>
<td>150</td>
<td>150</td>
<td></td>
<td></td>
<td>On-Hold</td>
<td>Discontinued</td>
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<tr>
<td>Service Purchase &amp; CNW Testing</td>
<td>150</td>
<td>62</td>
<td>88.25</td>
<td>41%</td>
<td>In-progress</td>
<td>New tool under dev.</td>
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<tr>
<td>Advisory/Consultation &amp; Oversight Services</td>
<td></td>
<td></td>
<td></td>
<td></td>
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<td></td>
</tr>
<tr>
<td>Continuity of Operations (COOP)</td>
<td>300</td>
<td>36</td>
<td>264</td>
<td>12%</td>
<td>In-progress</td>
<td>Monitoring</td>
</tr>
<tr>
<td>In-house Disbursements</td>
<td>400</td>
<td>48</td>
<td>352</td>
<td>12%</td>
<td>In-progress</td>
<td>Monitoring</td>
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<tr>
<td>Unspecified Advisory / Oversight Services</td>
<td>200</td>
<td>20</td>
<td>180</td>
<td>10%</td>
<td>In-progress</td>
<td>AG support</td>
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<tr>
<td>Other Activities</td>
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<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Fraud Hotline</td>
<td>150</td>
<td>16</td>
<td>134</td>
<td>11%</td>
<td>In-progress</td>
<td>Correction; active activity</td>
</tr>
<tr>
<td>Audit plan 2020/2021</td>
<td>150</td>
<td>140</td>
<td>10</td>
<td>93%</td>
<td>In-progress</td>
<td>Reassessed</td>
</tr>
<tr>
<td>IA Process / Planning updates</td>
<td>200</td>
<td>240</td>
<td>-40</td>
<td>120%</td>
<td>In-progress</td>
<td>Reassessed</td>
</tr>
<tr>
<td><strong>Total Hours</strong></td>
<td>5520</td>
<td>2033.25</td>
<td>3486.75</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

**Notes:**

1. Provide an explanation of actual hours that exceed budget by more than 10%
2. Director/Board request
3. Employer Audit request
4. Engagement start date pre-FY19

<table>
<thead>
<tr>
<th>Auditor</th>
<th>Projects</th>
<th>Hours Allocated</th>
<th>Status</th>
<th>Projects</th>
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<tbody>
<tr>
<td>Adel</td>
<td>1</td>
<td>960</td>
<td>Not-Started</td>
<td>0</td>
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<tr>
<td>Andrew</td>
<td>1</td>
<td>300</td>
<td>In-progress</td>
<td>12</td>
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<tr>
<td>Rosie</td>
<td>5</td>
<td>1750</td>
<td>Completed</td>
<td>3</td>
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<tr>
<td>Harold</td>
<td>9</td>
<td>1668</td>
<td>On-Hold</td>
<td>2</td>
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</table>

Work Plan Hours

6/28/2019
Agenda Item #5
Espiritu Schools Audit
A REPORT TO THE
ARIZONA STATE RETIREMENT SYSTEM
OPERATIONS, AUDIT AND LEGISLATIVE COMMITTEE

ARIZONA STATE RETIREMENT SYSTEM
INTERNAL AUDIT

ESPIRITU COMMUNITY DEVELOPMENT CORPORATION
NFL YET COLLEGE PREP ACADEMY

APRIL 11, 2019
The audit of Espiritu Community Development Corporation, NFL YET College Prep Academy (Academy) was completed on April 11, 2019 for the period July 1, 2013 through June 30, 2018.

The audit objectives were to determine whether the Academy is in compliance with ASRS statutes governing the following:

- Proper employer organizational structure for ASRS eligibility.
- Eligible compensation and required contributions reported to the ASRS.
- Accurate and timely enrollment of all eligible employees.
- Reporting and remitting of the employees’ and employer’s share of contributions.

This audit was limited in scope to an examination of employee eligibility, enrollment and proper reporting of contributions and an evaluation of the Employer Agreement (contract) with the Arizona State Retirement System (ASRS).

After an employer determines that an employee meets membership in the ASRS, the employer provides an enrollment code to the member so that the member can enroll in ASRS using the online registration process. The member enters the enrollment code and then the member provides the member’s demographic information, including name, SSN, address, gender and marital status, and designates beneficiaries. The information is important because it enables the member to keep their account secure, and it is also needed by the ASRS actuary for purposes of actuarial valuation and determining future contribution rates. When the employer sends the member’s contributions, the name and SSN can be matched to the information that already has been provided by the member. Accurate and timely enrollment of all eligible employees was tested by running reports of contributing employees to identify those who had not enrolled at all as well as those who had provided only partial information. This information was also compared to the list of ineligible employees before determining which eligible members had not completed their enrollment.

**SUMMARY OF FINDINGS:**

The proper organizational structure was verified by reviewing documents in the ASRS files regarding initial applications and the Academy’s restructuring requests to the Arizona State Board for Charter Schools (ASBCS), and the approvals found in the minutes of ASBCS’ public meetings. This led to the determination that only the Academy is covered by the charter that has a current ASRS contract.

Based on the results of the work performed to meet the listed audit objectives, the following statements summarize the findings presented to Espiritu Community Development Corporation, NFL YET College Prep Academy:

1. Espiritu Community Development Corporation, NFL YET College Prep Academy reported 62 employees of non-ASRS employers as eligible members in one or more fiscal years resulting in the remittance of contributions on ineligible compensation.

   The Academy should have remitted contributions only for its own employees after the reorganization, and not included any employees of the other charters. The other charters
were eligible to apply for ASRS membership, but did not do so when they first became eligible as separate entities. The charter that covers Reyes Maria Ruiz Leadership Academy (Reyes Maria Ruiz) has since applied for ASRS membership.

2. Espiritu Community Development Corporation, NFL YET College Prep Academy did not ensure proper enrollment of all its members.

BACKGROUND

The charter holder joined the ASRS on July 1, 1995 by executing an Application and Social Security 218 Agreement. This was one of the first charter schools to join the ASRS. The Social Security 218 Agreement properly lists the original charter school, Esperanza Montessori Academy, as the political subdivision and Espiritu Community Development Corporation as its governing body. The charter holder completed the ASRS agreement using the names Esperanza Montessori Academy and Espiritu Community Development Corporation interchangeably, even though only the charter school is an eligible political subdivision. Espiritu Community Development Corp does not, and never did, meet the statutory definition of an eligible ASRS employer. It is the charter school itself that meets the statutory definition of an ASRS employer.

This audit was requested by the ASRS’ Employer Relations after they noticed that the Academy had restructured and added new charters, but its contributions to the ASRS did not decrease accordingly. This charter school had originally been admitted to the ASRS as a single school, Esperanza Montessori Academy. The charter eventually also covered NFL YET Prep Academy and Reyes Maria Ruiz Leadership Academy (Reyes Maria Ruiz). These schools added another charter effective July 1, 2013. Esperanza Montessori Academy ceased to exist as a separate entity when it merged into Reyes Maria Ruiz, which was then transferred to the new charter. An associated school, Aim Higher Prep Academy (Aim Higher), did not commence operations until the 2016 fiscal year, which started on July 1, 2015. Aim Higher was organized under a different non-profit and charter. The Academy is the only school that remained under the original charter and therefore currently has an ASRS contract. The Academy currently has approximately 35 eligible members contributing to the ASRS. The Academy improperly continued reporting most of the employees of the other schools as if they were employed by the Academy.

DESCRIPTION OF AUDIT WORK PERFORMED

The audit work performed during the engagement was conducted in conformance with the *International Standards for the Professional Practice of Internal Auditing*. The audit work completed consisted of an examination of the employer’s payroll and personnel records for the time period July 1, 2013 through June 30, 2018. The auditor reviewed pertinent documentation and interviewed Academy personnel from the Human Resources and Payroll departments. The auditor performed substantive tests of the employees’ employment and payroll records to provide sufficient assurance that the employer is accurately reporting and remitting ASRS retirement and Long Term Disability (LTD) contributions. An employee who is eligible to participate in ASRS retirement must also participate in the LTD program.

The following audit tests were performed:

- Review of the employer payroll records and related ASRS reports.
• Review of employees’ time and payroll records to determine compliance with the 20 hour, 20 week eligibility criteria.
• Review of reports regarding proper enrollment of members.
• Other detailed testing as required to meet the audit objectives.

NOTEWORTHY OBSERVATIONS
Espiritu Community Development Corporation, NFL YET College Prep Academy; Reyes Maria Ruiz Leadership Academy and Aim Higher Prep Academy share common administration and so collectively will be referred to as Espiritu Schools.

Espiritu Schools used the same payroll system for the corporation as well as the different charters without differentiating services performed for the separate employers. This could result in improper financial reporting because the payroll expenses are not properly allocated to the correct employer. The audited combined financial statements that are published on the ASBCS web site improperly identified all full-time employees of the various charters as eligible for the ASRS. This is not correct because ASRS eligibility is not based on whether an employee works full-time, but whether the employee works at least 20 weeks of at least 20 hours in a fiscal year for an ASRS employer. Also, the employees of Aim Higher were generally not included in the ASRS reporting, unless the employee worked part-time for the Academy or for Reyes Maria Ruiz and part-time for Aim Higher.

Ineligible contributions for both the employee and employer are generally credited back to the employer at the same time. ASRS procedures require that an employer return employees’ ineligible contributions before requesting this credit from the ASRS.

The ASRS will have to expend time and resources to correct the accounts for proper service and salary credit for each affected person by pay period over the five years included in the scope of the audit.

AUDITOR COMMENTS:
Academy personnel were cooperative, informative and helpful in providing time reports, payroll records, and other information for the fiscal years under review that were necessary to effectively complete the ASRS audit. Audit findings and recommendations were discussed.
A REPORT TO THE
ARIZONA STATE RETIREMENT SYSTEM
OPERATIONS, AUDIT AND LEGISLATIVE COMMITTEE

ARIZONA STATE RETIREMENT SYSTEM
INTERNAL AUDIT

ESPIRITU COMMUNITY DEVELOPMENT CORPORATION
NFL YET COLLEGE PREP ACADEMY

FINDINGS AND RECOMMENDATIONS

APRIL 11, 2019
FINDING 1:
Espiritu Community Development Corporation, NFL YET College Prep Academy reported 62 employees of non-ASRS employers as eligible members in one or more fiscal years resulting in the remittance of contributions on ineligible compensation.

Condition
NFL YET College Prep Academy (Academy) is one of a group of three schools (Espiritu Schools) that used to be operated under a single charter. As of the start of fiscal year 2014, the schools reorganized. Two schools merged and were transferred to a separate charter. Another affiliated school started operations in fiscal year 2016 under a different charter. The Academy is the only school that remained under the charter that currently has an ASRS agreement, but the Academy reported most of the employees of the other schools as if they were employed by the Academy. It is unclear if the hours worked by the administrative personnel were properly allocated among the different schools. In some cases, employees worked for more than one of these related schools and either did not meet the 20/20 eligibility criteria at the Academy or reported all compensation as being earned solely at the Academy when the compensation should have been allocated among the various employers with only the Academy compensation reported. The incorrect reporting of ineligible wages will require an adjustment of salary credit. In most cases, it will also result in an adjustment of service credit for these affected individuals.

Espiritu Schools used the same payroll system for the different charters without differentiating services performed for the separate schools. This could result in improper financial reporting because the payroll expenses are not properly allocated to the correct schools.

Cause
A.R.S. § 38-711(23) defines an employee eligible to be a member in part as “an employee of an employer” who is “engaged to work at least twenty weeks in each fiscal year and at least twenty hours each week.” This is the basis for what is called the 20/20 eligibility criteria. The Academy is not allowed to withhold and remit contributions for persons who are not the Academy’s own employees.

Affected persons include 54 active or inactive non-retired employees, three retired employees and five refunded employees. All these persons have ineligible contributions that the employer should not have remitted to the ASRS. The persons affected may have been members in other fiscal years; other persons never met eligibility at any ASRS employer. These should all be corrected as soon as practicable so that these persons do not continue to rely on these incorrect figures. Different statutes apply to different groups.

The number of eligible and ineligible employees during the years tested, as determined by this audit are as follows:
ARIZONA STATE RETIREMENT SYSTEM
EMPLOYER SCHOOL DISTRICT
RECOMMENDATIONS

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Employees</td>
<td>87</td>
<td>80</td>
<td>61</td>
<td>85</td>
<td>54</td>
</tr>
<tr>
<td>Eligible members</td>
<td>44</td>
<td>42</td>
<td>26</td>
<td>27</td>
<td>24</td>
</tr>
<tr>
<td>% Eligible</td>
<td>50.6%</td>
<td>52.5%</td>
<td>42.6%</td>
<td>46.6%</td>
<td>44.4%</td>
</tr>
<tr>
<td>Ineligible</td>
<td>43</td>
<td>38</td>
<td>35</td>
<td>31</td>
<td>30</td>
</tr>
<tr>
<td>Non-retired</td>
<td>39</td>
<td>34</td>
<td>30</td>
<td>24</td>
<td>25</td>
</tr>
<tr>
<td>Retired</td>
<td>1</td>
<td>1</td>
<td>1</td>
<td>3</td>
<td>2</td>
</tr>
<tr>
<td>Refunded</td>
<td>3</td>
<td>3</td>
<td>4</td>
<td>4</td>
<td>3</td>
</tr>
</tbody>
</table>

Effect

A.R.S. § 38-765 requires the ASRS to correct errors to recover monies that have been overpaid. “If any change or error in the records results in any member or beneficiary receiving from ASRS more or less than the member or beneficiary would have been entitled to receive if the records had been correct, ASRS shall correct the error”. A.R.S. § 38-740(G) addresses errors in overpayments to refunded persons. “If a member receives more than the amount due to a member pursuant to this section, the member shall repay the amount of the overpayment together with interest”. A.R.S. § 38-738(A) discusses a return of ineligible contributions for the associated salary and service adjustments to be made for non-retired persons. “If more than the correct amount of employer or member contributions is paid into the ASRS by an employer through a mistake of law, the ASRS shall return those contributions to the employer if the employer requests return of the contributions through an employer credit.”

Eight persons have already been overpaid as a result of these incorrect contributions. Three of the affected employees have retired with incorrect calculations. One retired employee will lose her monthly benefits altogether and instead will receive an actuarially determined lump sum. The two other members who have already retired will lose an estimated 7% and 27% of their pension benefits, respectively. All retired members will have to return the overpayments they have already received, either in a lump sum or by accepting actuarially reduced payments in the future. The recalculations will be performed by the ASRS’ Financial Services Division before final amounts will be known. The five members who refunded their accounts have already received the principal, but owe repayments on the interest they were erroneously paid. The remaining non-retired members have incorrect estimates of the future benefits due to them. The bulk of the ineligible employees are 54 non-retired active or inactive persons with current retirement accounts that will need to be reduced or possibly returned in their entirety without interest.

If non-retired persons have ineligible service or salary credit, those persons’ estimated pension benefit will not be correct. Members who have chosen to refund their accounts have received ineligible interest accruals with their return of contributions. Affected persons include 54 active or inactive non-retired employees, three retired employees and five refunded employees. All these persons had ineligible contributions improperly withheld and remitted to the ASRS. These should all be corrected as soon as practicable so that these persons do not continue to rely on these incorrect figures.

The gross ineligible earnings and employer and employee contributions to be credited to the employer’s account, as determined by this audit are as follows:
Total Ineligible Gross Earnings $5,307,629
Ineligible Member Pension Contributions 602,871
Ineligible Member LTD Contributions 8,219
Ineligible Employer Pension Contributions 602,871
Ineligible Employer LTD Contributions 8,219
Total Estimated to be Credited to Employer $1,222,180

Recommendations:

1. The employer should not remit ineligible funds. The employer should discontinue remitting any contributions for the employees of the non-ASRS employers, including partial amounts attributed to members who allocated some of their hours to non-ASRS employers. The employer should return the employees’ ineligible contributions back to the employees to correct this error as soon as possible so that no additional liability accrues.

2. The employer should report compensation and remit contributions only for its own employees who work 20/20. The employer should notify each employee when there is a change in eligibility status. ASRS contributions should not be withheld from part-time employees’ earnings when an employee is not engaged to work at least 20 weeks in each fiscal year and at least 20 hours per week (20/20 membership criteria) for that employer. For those employees who work irregularly from one week to the next, contributions should not be withheld until the beginning of the 20th week of working 20 or more hours.

3. While the employer should generally not change employees of an ASRS employer from eligible to ineligible until the end of the fiscal year, employees’ eligibility to continue participating in the ASRS should be reassessed at the beginning of each new fiscal year.

4. The employer should request a credit for these ineligible contributions for the employees and the employer match.

5. The employer should contact the ASRS to ensure that the credits are processed properly.

Employer Response:
The ASRS requested that Espiritu CDC provide an employer response to the Internal Audit Findings and Recommendations. Espiritu CDC, through counsel, provided a lengthy response and exhibits that are maintained in the ASRS Employer Audit File. Within the employer response, Espiritu CDC stated the following:

- On June 11, 2013, Espiritu CDC and the Arizona State Board for Charter Schools entered into a new Charter Contract for ‘Transfer of School Site to a Separate Charter.’ The result of this was Espiritu CDC continued to operate schools at the same campus but now there were two separate CTDS numbers.”
- “Espiritu CDC does not dispute the numerical findings associated with the audit, including the number of employees affected (54 non-retired active or inactive persons, three retired, and five refunded persons).”
FINDING 2:
Espiritu Community Development Corporation, NFL YET College Prep Academy did not ensure proper enrollment of all its members.

A.R.S. § 38-716(1) requires employers to cooperate and collaborate with the ASRS and follow all ASRS procedures to ensure the proper enrollment of members in the system. Members who properly enroll provide the ASRS with enough personal and demographic data to accurately identify them and to communicate with them as needed. This also helps to make their accounts more secure. A.R.S. § 38-737 says that employer contributions will be determined by the ASRS actuary every year. The actuary requires full demographic information in order to make a correct calculation of the contribution rate.

The employer reported contributions for 87 employees in fiscal year 2018, but only the 44 eligible members were tested for missing demographic information. Most members had all required demographic information. The employer was informed that it had 16 employee members who had failed to enroll in the ASRS. Another single member was missing one or more of the following items of demographic information: date of birth, marital code, gender or address. The employer was advised to have its members properly enroll and update all required information.

Recommendations:
1. The employer should have its members properly enroll or update all required information.
2. The employer should ensure that all eligible members complete online enrollment prior to submitting contributions so that this information will be collected for all new employees.

Employer Response:
The ASRS requested that Espiritu CDC provide an employer response to the Internal Audit Findings and Recommendations. Espiritu CDC, through counsel, provided a lengthy response and exhibits that are maintained in the ASRS Employer Audit File. Within the employer response, Espiritu CDC stated the following:

“Espiritu CDC does not dispute, and has already resolved, the Findings and Recommendations in Finding 2.”
Vendor Efficacy
Internal Audit
A REPORT TO THE
ARIZONA STATE RETIREMENT SYSTEM
OPERATIONS, AUDIT AND LEGISLATIVE COMMITTEE

ARIZONA STATE RETIREMENT SYSTEM
INTERNAL AUDIT

VENDOR EFFICACY

MARCH 6, 2019
We completed our audit of Vendor Efficacy at the Arizona State Retirement System (“ASRS”) on March 6, 2019.

Our audit objectives were to determine and ensure the following:

1. The extent of utilization and the benefits of each service contract to the ASRS.
2. The ASRS is paying only for services contracted for with the Vendor.
3. The performance of the services is being monitored.
4. The accuracy of the billings is monitored.

The ASRS uses vendors to achieve its strategic objectives. The ASRS purchases goods, such as software and hardware, and services, such as a third-party to administer its LTD program. Some purchases are required as a state agency, such as legal advice from the Attorney General or use of the state-wide accounting system or cyber risk insurance from the ADOA. Some purchases are on state-wide purchasing contracts, such as actuarial, auditing or temporary contractor services. Investment contracts are scheduled for a separate audit, so only administrative vendors were tested in this audit. At the request of the Chief Internal Auditor, the scope of the audit was expanded to perform a more extensive examination of Skillsoft usage at the ASRS.

NOTEWORTHY OBSERVATIONS

Discussions with approvers of purchases revealed a high level of satisfaction with the vendors selected. All invoice approvers who were interviewed said that they were either satisfied or very satisfied with vendors used. The approvers usually said that the goods and services were meeting expectations and providing an appropriate level of service. Users had very few issues to report, and most vendors were reported to have characteristics such as very responsive, open to new ideas and easy to work with. One vendor was adding additional services that would reduce the work load for ASRS personnel. Some approvers stated that the money spent on certain professional services had been more than made up in the money saved when the ASRS acted on expert opinions that had been requested.

The ASRS changed LTD administrators during the fiscal year that was tested, and saved a significant amount of money by doing so. The previous administrator’s average monthly cost was about $206,565 for the period from 2013 through most of 2016. The current administrator’s average monthly cost from late 2016 through 2018 was around $131,461. The average monthly savings of $75,104 represents a 36% savings over the former administrator.

The LTD administrator must meet certain performance goals each quarter or pay a monetary penalty. The goals include a 90% or better compliance with decision timeliness, delivery of reports, financial accuracy, calls answered, etc. A team in Member Services Division reviews the monthly and quarterly reports provided by the administrator regarding these service goals. The administrator has missed these goals several times. In their first year, they underperformed on ten quarters of metrics across five categories, resulting in charges of $32,402.90. They improved in fiscal year 2018, and underperformed in only two quarters across two categories,
resulting in charges of $11,135.48. The new vendor is improving in its service to the ASRS while saving us money.

SUMMARY OF FINDINGS:

1. One vendor is not providing the extensive services promised.
   - The ASRS uses a software reseller for its software purchases. The software reseller has failed to live up to all its promises, such as its promise to make recommendations for software that would meet our needs, after taking into account the software already being used by the ASRS.
   - The software reseller also does not always respond timely to requests from the ASRS, and sometimes has to be contacted multiple times before a response is received.

2. The ASRS should establish a policy regarding regular reviews of active vendors.
   - Vendors are reviewed on an ad hoc basis rather than an annual basis, which can result in inactive vendors remaining in an active status even though they have not provided any goods or services for several years.
   - At least two vendor names were misspelled in the ASRS records.
   - Vendors were sometimes listed by initials, rather than fully spelled out.
   - A vendor that was known to have gone out of business was not reported to procurement so that its status could be changed to stop immediately.

3. The ASRS is underutilizing its available training for Skillsoft classes.
   - The ASRS has purchased 50 seats, so up to 50 people can use the software at once, but only 31 employees used it in a recent 12 month period.
   - The ASRS has a Professional Development Program (PDP) Charter which allows each ASRS employee in good standing to take at least 24 hours per year of training, but the PDP requires all training to be approved by the employee’s supervisor or manager, even classes taken before or after the employee’s normal work hours.

BACKGROUND

This audit was requested by the director to explore whether the ASRS is obtaining full value from its vendors. We reviewed whether the ASRS is paying for goods or services it does not receive or paying more than appropriate for goods or services it does receive. We reviewed the contracts for non-standard clauses such as automatic increases. We interviewed purchasers to determine their processes for ensuring that goods and services were received before invoices were approved for payment.

DESCRIPTION OF AUDIT WORK PERFORMED

The audit work performed during the engagement was conducted in conformance with the International Standards for the Professional Practice of Internal Auditing. The audit work completed consisted of an examination of the ASRS’ vendor, procurement and accounts payable records for the time period July 1, 2016 through June 30, 2017. Contracts for all administrative vendors with payments at or exceeding the predetermined threshold were reviewed for any automatic increases. None were noted. All increases were agreed to in separate addenda. The fiscal year’s invoices for the identified vendors were also reviewed and selected invoices were subjected to additional testing procedures.
The auditor reviewed pertinent documentation and interviewed ASRS personnel from the Procurement area and the Financial Services division. In addition, approvers from other divisions such as Investment Management, Technical Services and the Director's Office were interviewed regarding their use of procurement and their approval of expenses for their areas. The auditor performed substantive tests of the records to provide sufficient assurance that the ASRS is obtaining full value for its purchases of goods and services.

Some of the tests performed were:

- Reviewed contracts, Requests for Proposal contract responses and amendments to contracts.
- Identified all 2017 invoices of $30,000 or more, reviewed for evidence of recalculation before payment and recalculated selected invoices.
- Identified and interviewed all approvers of every invoice of $30,000 or more.
- Identified service providers with significant changes over fiscal years and identified reasons for the changes.
- Surveyed users of training software and collated responses.
A REPORT TO THE
ARIZONA STATE RETIREMENT SYSTEM
OPERATIONS, AUDIT AND LEGISLATIVE COMMITTEE

ARIZONA STATE RETIREMENT SYSTEM
INTERNAL AUDIT

VENDOR EFFICACY

INTERNAL RECOMMENDATION SUPPLEMENT

MARCH 6, 2019
INTERNAL FINDINGS AND RECOMMENDATIONS:

1. One vendor, CDW-Government (CDW-G), is not providing the extensive services promised.

References: TE – 10.8 Vendor Efficacy CDW Government Inc. Master Agreement
ADSPO16—130652
FI – 10.1.1 Vendor Efficacy CDW Concerns
FI – 10.1.2 Discussion with Molly Mahai Re CDW-G Software Vendor
TE – 10.2.3 Vendor Efficacy Discussions With Invoice Approvers

Our testing revealed the following:

CONDITION:

- CDW-G’s Master Agreement TE – 10.8 stated that they “know our customers’ systems and offer recommendations tailored to best fit your needs” and would “advise the Purchasing Entity in making strategic software application decisions by providing evaluation copies, product comparisons, needs analysis, product information and application recommendations.”

- I was unable to verify that the vendor has reviewed our current software to ensure that there are no gaps or redundancies. I found no evidence that this vendor ever made recommendations so that the ASRS does not purchase new software when current software already contains needed capabilities.

- The vendor does not respond to requests for information or quotes as quickly as promised. According to page 19 of CDW-G’s Master Agreement, vendor representatives are required to respond within two business days. ASRS employees do not always receive responses within this time frame, and sometimes have to make repeated requests before they receive an answer.

CAUSE: The vendor probably has the expertise for less sophisticated clients, but the ASRS has a large Technology Services Division with a great deal of expertise regarding software. The questions that the ASRS would like to refer to CDW-G require considerably more competency than CDW-G has demonstrated.

EFFECT: ASRS does not have experts at CDW-G to which it can refer all its questions and concerns, and receive a timely answer.

RECOMMENDATIONS:

1. ASRS should annually perform a survey of purchased and open sourced software to determine if what is installed meets the needs of the ASRS, and verify that there are no gaps or redundancies. If other divisions request new software, TSD would readily be able to assess whether ASRS can provide the capabilities needed with software that has already been purchased.
2. ASRS should assign an employee the job of becoming familiar with all current software, and all software approved for purchase each year, monitoring the software to see if it continues to meet the agency’s needs. That employee should review current capabilities and could also review requests for new software to see if any current software could be used for the purpose specified.

**MANAGEMENT RESPONSE:**

1. When the ASRS does not receive contractual services from a State contracted vendor we file a statement of dissatisfaction with the state procurement office; this statement is taken into consideration internally by the state procurement office when evaluating the contract in the future. The ASRS also has the option to file a formal complaint against the vendor, at which point the vendor has to respond and/or resolve the issue. On the ASRS business side of procurement we are currently improving our processes to better include research of vendor capabilities and use of existing available resources and vendor tools in order to determine “best fit” prior to engaging procurement. This will encourage a sharing of best practices within the agency and help identify vendor services that are high performing, which should increase the use of vendors that are a better fit for the business needs of the ASRS.

ASRS staff constantly reviews the efficacy of software in place and the team that uses each software has the responsibility to regularly research better options on the market for their needs. TSD management and Strategic Communications will discuss doing an annual survey to ASRS staff, possibly in line with the survey sent out in spring 2019 to all staff asking about their satisfaction with various ASRS support teams.

2. To a varying degree, the vendor (CDW) is responsible for ensuring software sold to ASRS performs to the standards deemed necessary by the agency and for giving guidance on software when ASRS is considering the purchase and renewal of software. TSD has expressed concerns to ASD - Procurement about the performance of the ADOA-State Procurement Office contract awarded vendor (re-seller) for software purchases. ASD is aware of the issues, primarily significant delays for information in order to renew software that is scheduled to expire.

The agency (ASD procurement) has filed a report regarding these performance issues with the state procurement office – who administers this contract; highlighting examples where TSD has experienced repeated emails and communications with the vendor but without success.

The goal is to improve timeliness of service.

Additionally, it is understood that the vendor may be able to provide solutions for specific technology needs; however the agency has not benefitted from this service.

As well, TSD management will work with Strategic Communications on planning regular surveys to staff regarding the efficacy of third party and open source software.
2. The ASRS should establish a policy regarding regular reviews of active vendors.

References:  
TE – 10.4 Vendor Efficacy Names Numbers and Active Status 
TE – 10.7 Vendor Efficacy Vendors Retaining Active Status 
TE – 10.7.1 Vendor Efficacy Vendors Without Recent Activity

Our testing revealed the following:

CONDITION:

- The vendor names are not reviewed regularly, but on an ad hoc basis, which results in some vendors with an active status even though the agency has not purchased their goods or services in a number of years. A review during the period of the audit testing showed that shortly before the end of field work, 38 vendors had their status changed from active to stop. A number of the remaining active vendors should be changed to inactive or stop.
  - Nine vendors had not received an ASRS payment since before FY 2013.
  - One vendor had not received an ASRS payment since FY 2013.
  - Two vendors had not received an ASRS payment since FY 2014.
  - Six vendors had not received an ASRS payment since FY 2016.
- At least two vendor names were misspelled.
  - Institutional Shareholder Svcs Inc should be Institutional Shareholder Services Inc.
  - Frank Russell Compan should be Frank Russell Company
- Some of the vendors are listed under initials rather than the full name, which makes those payments less secure.
  - LSS, LLC is listed as the company name, but it is listed with as doing business as Lightstone Solutions, LLC.
  - MHI Global, Inc. is listed as doing business as Achieve Global, Inc.
  - Berkeley Research Group is listed as BRG.
- One vendor has gone out of business, but was not reported right away, and only changed to a stop status near the end of the audit testing.

CAUSE: The agency does not review its vendor’s records on a scheduled basis.

EFFECT: Inactive accounts can be renamed or have their addresses updated. Inactive addresses could be subject to a change of address form that directs the checks to a completely different address. Misspelled vendors could have several possibilities for changed names to unintended alternates. All these things create opportunities for diversions of budgeted funds which may not be recoverable.

RECOMMENDATIONS:

1. The vendor list should be reviewed annually for vendors that should be changed from active to inactive or stop, or from inactive to stop.
2. Vendors should be reviewed for correct spelling.

3. If an ASRS employee becomes aware that a vendor is no longer doing business, that employee should notify procurement so that the vendor can be changed to a stop status promptly rather than waiting for it to be noted in a review.

**MANAGEMENT RESPONSE:**

1. ASD believes it is important to maintain a vendor database that is up-to-date. Our team regularly updates Munis to remove expired vendors and inaccurate information. The most recent update was completed at the beginning of FY 2019. ASD will continue to perform these updates at the start of each fiscal year.

2. See #1 above.

3. See #1 above.

3. The ASRS is underutilizing its available training for Skillsoft classes.

**References:**  
*TE – 10.9.1 Vendor Efficacy Skillsoft Usage Memo*
*TE – 10.9.2 Vendor Efficacy Professional Development Program - Charter*
*TE – 10.9.3 Vendor Efficacy PDP Process Steps Flow Chart*
*TE – 10.9.7 PO 19336 Skillsoft Invoice*

Our testing revealed the following:

**CONDITION:**

- Skillsoft software is underutilized in the ASRS. The agency has purchased 50 seats, so up to 50 people can use the software at once. Its library of available courses is extensive. However, only 31 employees used it during a recent twelve-month period.
- The Professional Development Program Charter allows each ASRS employee in good standing to take at least 24 hours per year of training, but it has to be approved by the employee’s supervisor or manager. One of the options available for this training is Skillsoft. The ASRS has over 220 employees. Only 31, or 14%, of these employees used Skillsoft for any of their training needs. A total of 122 classes were taken, but two individuals were responsible for 58 of those, or almost half of the classes taken. The classes vary from less than half an hour to several hours in length, so it is impossible to know what percentage of the allowable hours were spent on Skillsoft.

**CAUSE:**

- The agency has an approval process before employees can use this software, and it has caused some employees to not consider it.
- Not every employee is aware of this available training or how to access it. When I sent out surveys to last year’s users one of the responses I received included a request to help a new employee gain access. I referred the employee to training.
• The library is so extensive that some employees are overwhelmed and unable to determine which classes would be the most beneficial for their ASRS career.

EFFECT: The agency has not fully realized its intended purpose for the Professional Development Program. The business case in the Professional Development Program Charter was that it would:

• Improve employee morale, engagement, and retention
• Increase efficiency and effectiveness
• Develop new leaders
• Prepare employees for future job opportunities at the ASRS
• Improve business literacy

The agency has already purchased this software, so other training costs could be reduced when Skillsoft is more fully utilized.

RECOMMENDATIONS:
1. Make elective classes available without restriction at lunch or before or after employees’ work hours. If an employee wants to learn new skills or sharpen existing skills, and is willing to take classes outside the employee’s regular work hours, they should be encouraged to take the opportunity to do so.

2. Review whether some or even most employees in different work groups could be given one or two hours per month for taking classes without obtaining permission to do so.

3. Ask managers and supervisors to review the classes available in Skillsoft to identify classes that they believe would be most beneficial to their staff. Post this somewhere so that their staff, and other employees who aspire to be their staff, can locate the suggested classes.

4. Because ASRS employees in good standing are allowed to use 24 hours per year for training, continue reminding employees about the availability of Skillsoft from time to time. It has already been purchased; ASRS will obtain better value if it’s used more frequently

MANAGEMENT RESPONSE:
Human Resources & Development (HR & D) recognizes that professional development of staff impacts employee engagement. We agree that the Skillsoft suite of educational resources is currently underutilized by ASRS staff. To that end, HR & D is implementing plans to promote greater engagement and increased use of this resource:

• HR & D presented information about Professional Development and Skillsoft at the March 2019 ASRS Management Team Meeting; requested that supervisors share the information with their business units and allow staff time to complete Skillsoft modules.
• More frequent reminders to supervisors and staff of Skillsoft’s offerings via Daily IQ, emails, and Supervisor Support Group.
• Reminders to managers who supervise employees identified in the Workforce Planning initiative that competencies have been matched to Skillsoft modules; modules are an excellent starting point to move employees along in their development.
• Monitoring engagement survey trends regarding professional development opportunities; awaiting 2019 survey results; will adjust communication strategy as results dictate.

Operational continuity is a priority and is dependent upon high engagement scores. Providing opportunity for staff to complete Skillsoft modules and then build on new skills will lead to increased engagement scores. The following is in response to the audit recommendations:

1. This has the potential to expose the agency to unnecessary risk in that non-exempt (hourly) employees should not be encouraged to complete Skillsoft training modules on their own time as this could violate the Fair Labor Standards Act (FLSA). Employees who are directed to complete training on their own time must be compensated at regular rate or at time-and-half rate (whichever applies per each unique situation) depending upon their FLSA status. Time should be provided during the workday for employees, exempt and non-exempt, to complete training.

2. ASRS supervisors must not be excluded from the approval process or from guiding employees’ professional development. All time spent during the workday should be subject to supervisor oversight to ensure the appropriate training is completed and to ensure that business unit, division, and agency goals are met.

3. This is achievable and presents no risk to the agency as supervisors can post their selected courses on their business unit’s IQ page.

4. As part of the Professional Development Program and Workforce Planning initiative, staff are reminded of Skillsoft’s availability. Human Resources will produce and publish periodic reminders and ask supervisors to mention the program in their regular meetings.