



ARIZONA STATE RETIREMENT SYSTEM

3300 NORTH CENTRAL AVENUE • PO BOX 33910 • PHOENIX, AZ 85067-3910 • PHONE (602) 240-2000
7660 EAST BROADWAY BOULEVARD • SUITE 108 • TUCSON, AZ 85710-3776 • PHONE (520) 239-3100
TOLL FREE OUTSIDE METRO PHOENIX AND TUCSON 1 (800) 621-3778
EMAIL ADDRESS: ASKMAC@AZASRS.GOV • WEB ADDRESS: WWW.AZASRS.GOV

Paul Matson
Director

MINUTES OF A PUBLIC MEETING OF THE ARIZONA STATE RETIREMENT SYSTEM OPERATIONS AND AUDIT COMMITTEE

HELD ON
Tuesday, August 12, 2014
10:30 a.m., Arizona Time

The Operations and Audit Committee (OAC) of the Arizona State Retirement System (ASRS) met in public session in the 14th Floor Conference Room of the ASRS Office, 3300 North Central Avenue, Phoenix, Arizona 85012. Mr. Jeff Tyne, Chair, called the meeting to order at 10:30 a.m.

1. Call to Order; Roll Call; Opening Remarks

Present: Mr. Jeff Tyne, Chair
Mr. Mike Smarik, Vice-chair
Dr. Richard Jacob

Absent: Mr. Brian McNeil

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

2. Approval of the Public Session and Executive Session of the April 30, 2014 Minutes of the OAC Meeting

Motion: Mr. Michael Smarik moved to approve the public session and executive session of the April 30, 2014 OAC meeting. Dr. Richard Jacob seconded the motion.

By a vote of 3 in favor, 0 opposed, 0 abstentions, and 1 excused, the motion was approved.

3. Presentation, Discussion and Appropriate Action Regarding the 2015 ASRS Retiree Medical Benefits Program Request for Proposal (RFP)

Mr. Paul Matson, Director, presented the item by commenting on the important items considered by the Evaluation Committee when reviewing the contract submissions for a new contract. The items included 1) Benefit coverage, 2) Access/Network, 3) Premium cost, and 4) Medical cost ratio.

Dr. Richard Jacob stated he served on the Evaluation Committee and was disappointed there was not more competition for the contract and he would like to see more offers received the next time the ASRS goes out to bid. Mr. Paul Matson, stated that staff concurs with Dr. Jacob and feels part of the reason for so few offers is the state of healthcare in the U.S. right now. Mr. Matson also mentioned that though this is a five-year contract, to begin on January 1, 2015, there are four one-year renewals, and the ASRS does not need to remain in the contract for the full five years if other options become available.

Motion: Mr. Mike Smarik moved to go into Executive Session for the purpose of considering or discussing records exempt by law from public inspection. Dr. Richard Jacob seconded the motion.

By a vote of 3 in favor, 0 opposed, 0 abstentions, and 1 excused, the motion was approved.

The Committee convened to Executive Session at 10:35 a.m.

The Committee reconvened to Public Session at 10:54 a.m.

Motion: Mr. Mike Smarik moved to accept the Evaluation Committee's recommendation and forward it to the ASRS Board of Trustees for approval. Dr. Richard Jacob seconded the motion.

By a vote of 3 in favor, 0 opposed, 0 abstentions, and 1 excused, the motion was approved.

4. Presentation, Discussion and Appropriate Action Regarding an ASRS Risk Assessment of Agency Technology Development, Security, and Continuity of Operations

Mr. Anthony Guarino, Deputy Director and Chief Operations Officer, provided a topic overview, stating the purpose of the presentation was to provide a candid assessment of the ASRS' risks and the goals established to mitigate those risks. Mr. Guarino introduced Mr. Kent Smith, Assistant Director Technology Services Division, who discussed the assessment of the ASRS' risks as well as the strategies planned or in place to control these risks. Further discussion of agency risk assessments and remediation plans required discussion in Executive Session.

Motion: Mr. Mike Smarik moved to go into Executive Session for the purpose of considering or discussing records exempt by law from public inspection. Dr. Richard Jacob seconded the motion.

By a vote of 3 in favor, 0 opposed, 0 abstentions, and 1 excused, the motion was approved.

The Committee convened to Executive Session at 11:16 a.m.

The Committee reconvened to Public Session at 12:00 p.m.

5. Presentation, Discussion and Appropriate Action Regarding the ASRS Budget Related Topics Including:

A. Presentation of the ASRS Appropriated Budget and the Estimated Administrative and Investment Spending Plan for Fiscal Year (FY) 2015

B. Presentation of the ASRS Appropriated Budget Request and Estimated ASRS Administrative and Investment Spending Plans for FY 2016 and FY 2017

Ms. Martha Rozen, Chief of Administrative Services, explained the budget numbers and the materials presented for this agenda item. Ms. Rozen reviewed the materials included for 5B, explaining the ASRS is requesting only the FY 2016 budget amount at this time.

Motion: Dr. Richard Jacob moved to accept and forward to the ASRS Board an appropriated budget request for FY 2016 in the amount of \$28,106,200; an administrative spending plan of \$33,137,200 within a total spending plan of \$315,036,200, and an appropriated budget request for FY 2017 in the amount of \$27,659,200; an administrative spending plan of \$32,779,200 within a total spending plan of \$337,410,200. Mr. Mike Smarik seconded the motion.

By a vote of 3 in favor, 0 opposed, 0 abstentions, and 1 excused, the motion was approved.

The order of the agenda was changed to address the following item.

6. Presentation, Discussion and Appropriate Action Regarding Elimination of One Audit From Year Two Audit Plan in Order to Test Census Data for the External Auditor of the ASRS

Mr. Bernard Glick, Chief Internal Auditor, requested the Committee approve removal of the WEB Services Social Media Audit from the ASRS FY15 Audit Plan and replace it with the ASRS Compliance with GASB 68 Census Audit. The WEB Services Social Media Audit would then be moved to the FY16/17 Biennial Audit Plan.

In 2012, the Governmental Accounting Standards Board (GASB) recognized as the authoritative body for establishing and improving financial accounting and reporting standards of state governmental entities, issued "GASB 68." GASB 68 addresses the role of census data for multiple-employer-defined benefit plans and the external auditors' responsibility for such census data.

To comply with GASB 68, the ASRS external auditors, Clifton, Larson Allen, will select 27 ASRS employers to perform the necessary census data tests (age of member, date of membership, salary). To lower the cost of the external auditor performing this work, the ASRS Internal Audit Division (IAD) will assist by performing the field work under the supervision of Clifton, Larson Allen. This GASB field work will require 300 hours of IAD audit time, which requires moving the WEB Services Social Media Audit to the 2016-17 Biennial Audit Plan.

Motion: Mr. Mike Smarik moved to remove the WEB Services Social Media Audit from the ASRS FY15 Audit Plan and replace it with the ASRS Compliance with GASB 68 Census Audit and move the WEB Services Social Media Audit to the FY16-17 Biennial Audit Plan. Dr. Richard Jacob seconded the motion.

By a vote of 3 in favor, 0 opposed, 0 abstentions, and 1 excused, the motion was approved.

Mr. Mike Smarik departed the meeting at 12:24 p.m., resulting in a loss of a quorum for the meeting.

7. Presentation, Discussion and Appropriate Action Regarding Approaches and Legal Implications of Service and Account Balance Reinstatement for Members Who May be Defrauded

Mr. Guarino introduced Ms. Nancy Bennett, Chief Financial Officer, who reviewed the current Risk Assessment on Disbursements. Ms. Sarah Korish, Member Services Program Manager, explained the strength of the ASRS controls for member refunds.

Ms. Bennett discussed indemnity issues raised as a result of a recent alleged fraud against a member account. Dr. Jacob asked if the staff was looking for input or guidance on how to handle this type of alleged fraud. Mr. Matson clarified that yes, staff was looking for input and guidance to result in a policy on how to handle member account fraud.

Dr. Jacob said he sees the member as well as the ASRS as victims if there is member account fraud; the risk and the loss are shared. He then stated that shared risk is changed if either the member or the ASRS did not act prudently with the account information, resulting in the fraud.

Mr. Jeff Tyne, Chair of the Committee requested Ms. Jothi Beljan, Assistant Attorney General, to provide legal advice regarding this agenda item. The Committee went into Executive Session for this advice.

Because the quorum was lost with the departure of Mr. Smarik, no motion was made to go into Executive Session.

The Committee convened to Executive Session at 12:38 p.m.

The Committee reconvened to Public Session at 12:55 p.m.

8. Presentation, Discussion and Appropriate Action Regarding the Audit Update for Year One of the Audit Plan

Mr. Glick presented the status of audit hours used for the FY 2014 Audit Plan.

9. Review of Recently Conducted Audits

Mr. Glick reviewed the following audits conducted by the Internal Audit Division:

- **Graham County Employer Audit**

The audit revealed Graham County did not remit ASRS contributions for thirty-eight employees who worked or were engaged to work at least twenty hours per week for at least twenty weeks in one or more fiscal years. The County appealed the audit finding, stating they believed there were only six staff for which the county owes contributions and not the full 38 staff identified in the audit report.

ASRS Management found the County's explanation reasonable and acceptable in light of established protocols to administer the hours worked for new employees; that new employees in select county positions are enrolled in CORP after a probationary period, not the ASRS.

- **ASRS Investment Management Division (IMD) Order Management System**

IMD's Bloomberg AIM Order Management System was tested. The system electronically links portfolio holdings to market data as well as the custodial bank and has reduced errors, expedited trade processing, and compliance review. The audit revealed potential segregation of duties (SOD) conflicts with regard to AIM system administration and equity trades being approved by equity staff rather than fixed income staff.

Management will implement the IAD recommendations regarding potential SOD conflicts.

- **Long Term Disability Program**

IAD completed the audit of the ASRS Long-Term Disability (LTD) program and related processes on January 31, 2014. The audit objectives were: 1) the reliability and integrity of information; 2) compliance with policies, plans, procedures, laws, and regulations; 3) the safeguarding of assets; 4) the economical and efficient use of resources; 5) the accomplishment of established objectives and goals for operations and programs.

The audit resulted in six recommendations to staff; Management agreed to many of them and has already taken steps through scheduled IT projects as well as staff training to remedy them.

10. Request for Future Agenda Items

There were no items requested by Committee members.

