



DEBRA K. DAVENPORT, CPA
AUDITOR GENERAL

STATE OF ARIZONA
OFFICE OF THE
AUDITOR GENERAL

MELANIE M. CHESNEY
DEPUTY AUDITOR GENERAL

March 29, 2016

The Honorable John Allen, Chair
Joint Legislative Audit Committee

The Honorable Judy Burges, Vice Chair
Joint Legislative Audit Committee

Dear Representative Allen and Senator Burges:

Our Office has recently completed an initial followup of the Arizona State Retirement System (ASRS) regarding the implementation status of the 14 audit recommendations (including sub-parts of the recommendations) presented in the performance audit report released in August 2015 (Auditor General Report No. 15-106). As the attached grid indicates:

- 4 have been implemented;
- 9 are in the process of being implemented; and
- 1 has not been implemented.

Our Office will conduct an 18-month followup with the ASRS on the status of those recommendations that have not been or have not yet been fully implemented.

Sincerely,

Dale Chapman, Director
Performance Audit Division

DC:ka
Attachment

cc: Paul Matson, Director
Arizona State Retirement System

Arizona State Retirement System Board of Trustees

Arizona State Retirement System

Auditor General Report No. 15-106

Initial Follow-Up Report

Recommendation	Status/Additional Explanation
Finding 1: ASRS plan is not fully funded, but steps have been taken to improve its long-term sustainability	
1.1 The ASRS should continue with its plans to formally adopt its funding policy and make it publicly available by posting the policy on its Web site.	Implemented at 6 months
Finding 2: Additional actions can enhance ASRS plan's financial condition and long-term sustainability	
2.1 The ASRS and its Board should work with its actuary to develop a method for ensuring the cost of future benefit increases do not impact the ASRS plan's sustainability. In developing this method, the ASRS should ensure that it aligns with its funding policy's goals and objectives.	Implemented at 6 months
2.2 The ASRS and its Board should develop and implement a policy and procedure for periodically reviewing its actuarial cost method to determine which generally accepted actuarial cost method is appropriate for determining contributions and helping to meet its Funding Policy's objectives. In developing this procedure, the ASRS should ensure that its adopted policy and procedures:	
a. Establish a time frame to review the appropriateness of the actuarial cost method periodically, such as every 5 years when it conducts actuarial experience studies; and	Implemented at 6 months
b. Do not allow the Board and/or the actuary to change actuarial methods for the sole purpose of achieving a more favorable funding status, or fiscal result.	Implemented at 6 months

Recommendation

Status/Additional Explanation

2.3 The ASRS should enhance its procedures for identifying employer termination incentive programs and assessing the cost of any resulting unfunded liability to an employer. Further, depending on the final resolution of outstanding litigation, the ASRS may also need to adopt administrative rules in order to legally enforce A.R.S. §38-749. Specifically, the ASRS should:

- a. Determine a methodology for calculating when a 30 percent or greater increase in a member's compensation not attributable to a promotion has occurred;
- b. Develop and implement written policy and procedures executing the methodology to determine when a 30 percent or greater nonpromotion salary increase has occurred, and train staff on the policy and procedures;
- c. Assess the feasibility of implementing this procedure for all members who have retired since September 30, 2009. Accordingly, the ASRS should identify and investigate potential instances of employer termination incentive programs, including those involving nonpromotion salary increases of 30 percent or more. Further, when an instance is identified, the ASRS should assess the cost of any resulting unfunded liabilities to the employer;
- d. Include information in its retirement benefit processing procedures on how to identify and what ASRS staff should do when they identify salary increases that appear to be a result of an employer termination incentive program or an inappropriate preretirement salary increase, as well as which staff are responsible for conducting further investigations on such cases and for assessing the cost of the unfunded liability to the employer; and

Implementation in process

In October 2015, the Arizona Supreme Court denied the ASRS' petition for review (see Recommendation 2.3 for more information); therefore, the ASRS is in the process of determining which employer termination incentive program processes must be in administrative rules or can be clarified in its procedures. In January 2016, the ASRS began holding various meetings to complete the work for this set of recommendations, and it estimates that its work will be completed by September 2016.

Implementation in process

See explanation for Recommendation 2.3a.

Implementation in process

See explanation for Recommendation 2.3a.

Implementation in process

See explanation for Recommendation 2.3a.

Recommendation

Status/Additional Explanation

- e. Develop and implement a policy and procedures for regularly querying the ASRS contribution accounting system for increases in compensation that could indicate employer termination incentive programs. The adopted policy and procedures should also state which ASRS staff are responsible for conducting further investigations on potential cases identified through its queries, and which staff are responsible for assessing the cost of any unfunded liability to the employer.

Implementation in process

See explanation for Recommendation 2.3a.

Sunset factor #2: The ASRS should continue to improve IT policies and procedures

1. As part of its continuing efforts to enhance its IT practices, the ASRS should:
 - a. Develop a process for documenting the review and approval of IT system coding changes prior to implementing changes;
 - b. Periodically update its disaster recovery plan to ensure that all information pertaining to devices, personnel, software, and processes are as up to date as possible;
 - c. Continue enhancing its data access process to ensure that access is limited to appropriate personnel;
 - d. Develop a process to review logs for key activities on its networks and systems; and
 - e. Continue evaluating the recommendations it received from a 2014 limited security assessment and implement them as appropriate.

Implementation in process

The ASRS developed a policy to ensure that IT system coding changes go through a standardized process, that includes review. However, the policy does not include step-by-step procedures for the review process, including how to document the review analysis conducted by all required parties.

Implementation in process

The ASRS is working to obtain assistance in developing a Continuity of Operations Plan (COOP) (i.e., a disaster recovery plan) from the Department of Emergency and Military Affairs as allowed under Executive Order 2013-06 and anticipates the COOP will be completed in August 2016.

Implementation in process

The ASRS is in the process of enhancing its data access process, including reviewing lists of people who have access and revising its policies and procedures. The ASRS estimates this project will be completed in fiscal year 2017.

Not implemented

The ASRS intends to begin implementing this recommendation in fiscal year 2017 per its 5-year strategic plan.

Implementation in process

The ASRS is working on finalizing the process for reviewing and fixing the vulnerabilities identified from the 2014 security assessment and it is first focusing on the highest priority vulnerabilities. The ASRS indicated that once it has finalized its process and has additional staff, it will focus on lower-priority vulnerabilities.