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AUDITOR GENERAL

STATE OF ARIZONA
OFFICE OF THE
AUDITOR GENERAL

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DEPUTY AUDITOR GENERAL

September 18, 2018

The Honorable Anthony Kern, Chair
Joint Legislative Audit Committee

The Honorable Bob Worsley, Vice Chair
Joint Legislative Audit Committee

Dear Representative Kern and Senator Worsley:

Our Office has recently completed a 36-month followup of the Arizona State Retirement System 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:

- 11 have been implemented;
- 1 is substantially implemented;
- 1 is partially implemented; and
- 1 is in the process of being implemented.

Unless otherwise directed by the Joint Legislative Audit Committee, this concludes our follow-up work on the Arizona State Retirement System's efforts to implement the recommendations from the August 2015 performance audit report.

Sincerely,
Dale Chapman, Director
Performance Audit Division

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

36-Month 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
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;	Implemented at 24 months

Recommendation**Status/Additional Explanation**

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| 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; | Implemented at 36 months |
| 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; | Implemented at 24 months |
| 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 | Implemented at 36 months |
| 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. | Implemented at 36 months |

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

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| 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; | Implemented at 24 months |

Recommendation

Status/Additional Explanation

- 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

ASRS staff continue to work with the Arizona Department of Emergency and Military Affairs (DEMA) to develop its Continuity of Operations Program (COOP) plan, including attending COOP development training in February 2018. To help agencies respond to disasters or other emergencies, DEMA's COOP provides agencies with tools and resources to help them create and update business continuity plans. These plans identify an agency's essential functions and key personnel and systems, including IT systems, that are needed to perform these functions. ASRS anticipates completing its COOP plan by the end of 2018 and expects to review and update its COOP plan annually.

Implemented at 24 months

Partially implemented at 36 months

The ASRS implemented a logging and monitoring tool and defined key network activities to be captured using this tool. The tool emails alerts to an ASRS network team and its help desk when a key event is logged. On September 17, 2018, the ASRS developed procedures for reviewing and investigating these alerts and taking corrective action if necessary, but auditors were not able to obtain evidence that the ASRS was following these procedures because this change was recently made.

Substantially implemented at 36 months

As reported in the 24-month followup, the ASRS addressed most of the recommendations it received from the 2014 security assessment. According to the ASRS, one recommendation—that it develop information security policies and procedures—remains unimplemented as of September 2018. In January 2018, the ASRS contracted with a vendor to help implement a comprehensive information security program, and it may use this vendor to address the remaining recommendation. However, according to the ASRS, it completed a risk assessment with its vendor's assistance and determined that completing security policies and procedures falls below the ASRS' current risk threshold, and therefore, it has not set a time frame for doing so.