



Alameda County Employees' Retirement Association
Internal Audit Department

Actuarial Process Audit
Report Date: September 2010

INTERNAL AUDIT DEPARTMENT

**REPORT PREPARED FOR:
THE ACERA BOARD OF RETIREMENT**

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CONTROL SUMMARY

CONTROLS TESTED

#	Control	Risk Level	Owner	Effectiveness
1	COORDINATED ACTUARIAL PROCESS	Medium	ADMINISTRATION	PARTIALLY EFFECTIVE
2	MEMBER COUNTS ARE ACCURATE	Medium	PRISM, BENEFITS, ACCOUNTING	PARTIALLY EFFECTIVE
3	ACTUARIAL REPORTS ARE CONSISTENT WITH THE CAFR	Low	ACCOUNTING	EFFECTIVE
4	CONTRIBUTION RATES ANNUAL SET-UP	Low	PRISM, ACCOUNTING	EFFECTIVE
5	NET MARKET VALUE OF ASSETS RECONCILES TO FINANCIAL STATEMENTS	High	ACCOUNTING	EFFECTIVE
6	INVESTMENT RATE OF RETURN COMPARISON	High	INVESTMENTS	PARTIALLY EFFECTIVE
7	CONFIRM ACTUAL CONTRIBUTIONS EQUAL'S EXPECTED CONTRIBUTIONS	High	ADMINISTRATION, ACCOUNTING	EFFECTIVE
8	30 YEAR MEMBER SERVICE	Low	PRISM, BENEFITS	REMEDIATED
9	COST/BENEFIT ANALYSIS ON UNKNOWN MARITAL STATUS	Medium	PRISM, BENEFITS	IMPROVEMENT OPPORTUNITY
10	YEAR-END MEMBER DATA RECONCILIATION	Low	PRISM, ACCOUNTING	REMEDIATED
11	TIMELY UPDATE OF BENEFICIARY INFORMATION	Low	BENEFITS	PARTIALLY EFFECTIVE
12	NO DUPLICATION OF MEMBERS IN PENSIONGOLD	Medium	BENEFITS	EFFECTIVE
13	POST- ACTUARIAL VALUATION REVIEW	Medium	ADMINISTRATION, BENEFITS, ACCOUNTING	IMPROVEMENT OPPORTUNITY
14	PRIVACY AND SECURITY OF MEMBER DATA	High	PRISM	EFFECTIVE
15	LAWS AND REGULATIONS ARE REVIEWED PERIODICALLY	High	ADMINISTRATION, ACCOUNTING	REMEDIATED

RISK LEVEL

High Risk Controls:

Controls associated with critical processes within an organization. Typically they are associated with overall monitoring controls or valued in key controls or numerous processes. They can be controls that had significant findings in previous years. A high risk control failing could result in a material weakness. Material weakness includes material misstatements in the financial statements, significant process errors and misuse of ACERA resources.

Medium Risk Controls:

Controls associated with important processes within an organization, where a deficiency in the control could cause financial loss or breakdown in process, but in most cases do not lead to a critical systemic failure. Typically, these controls had minimal or no findings in previous years, but are integral to the process and necessary to test on a regular basis. A medium risk control failing could result in a significant deficiency, and in some instances, a material weakness. Significant deficiencies can include staff competency, lack of consistent business process and poor utilization of ACERA resources.

Low Risk Controls:

Controls associated with process optimization and non-critical processes. Typically they represent controls that did not have findings in the previous year's testing and have not changed in how they operate or in the personnel performing the controls. Low risk controls are inherent in the current control environment, but are unlikely to cause a material misstatement, unless there is a failure of several low risk controls within the same process.

CONTROL EFFECTIVENESS

Effective:

The control is fully operating as designed.

Partially Effective:

The control is operating as designed with modification necessary due to a change in business process, change in personnel, inadequate documentation, the control has not been fully implemented, or the control requires additional enhancements to be effective. Often new controls will fall in this category.

Improvement Opportunity:

The control is only marginally effective and should be redesigned or implemented. Typically these controls require review due to an ineffective design, which will prevent the control from detecting control risk.

Ineffective:

The control is not operating as designed, and could lead to a significant risk to the organization, if not remediated.

Remediated:

The control was previously ineffective, partially effective, or an improvement opportunity. A remediation plan is in place to correct the deficiency. Note that reliance can be placed on the remediated control, once retested by internal audit, which typically occurs in the following audit cycle.

AUDIT OBJECTIVE

The overall audit objective is to determine if ACERA's process for gathering and providing actuarial data to the actuary is sufficient and complete. The audit will examine the internal process used by ACERA Management (Staff) to capture financial and member data and the steps taken to review the data for accuracy prior to submitting the information to the actuary for preparation of the annual Actuarial Valuation Report.

SCOPE

The scope of the audit will cover the information provided by ACERA to prepare the Actuarial Valuation and Review as of December 31, 2008. We will examine the actuarial relevant data that was provided by ACERA through both formal and informal communications, data the actuary deemed inconsistent or inaccurate, and the adequacy of the source of data.

Please note the scope of this audit has been limited to examining if the process for providing data to the actuary can be reasonably relied on. Therefore, the audit will not be focused on the quality or accuracy of the detailed data. Although, if an inaccuracy or inconsistency in the data is discovered during the course of the audit, it will be reported as a deficiency and an action item will be recommended. In addition, we have not evaluated all third party data provided to ACERA or the actuary (i.e. employer data on expected salary increases). Further, the scope of this audit will not include an evaluation of how the actuary uses this data to design their actuarial assumptions and whether these assumptions are correct. Finally, we are not opining on whether the actuarial calculations performed by the actuary based on the data provided is accurate and complete.

AUDIT STRATEGY

To meet our audit objective and gain an understanding of ACERA's process for providing information to the actuaries, we reviewed the following areas:

- (1) Sources of Data
- (2) Departmental Responsibilities
- (3) Review and Reasonableness Checks

SOURCES OF DATA

The actuary typically provides ACERA with an Actuarial Document Request, detailing what information is necessary to complete the Annual Actuarial Valuation. The request consists of standard recurring items that are required every year and additional items that are requested based on new information or a change in process.

The sources of data range from IT reports generated from PensionGold, Great Plains and BERT (an MS Access Database that captures specific data from PensionGold in a user-friendly format), MS Excel Spreadsheets, and data from third parties (i.e. SIS).

Our audit tested whether the appropriate source was used to provide the data to the actuary, since there may be instances where the same information may be tracked in two different systems or manually by two different groups. This could lead to inconsistency in the data, and the possibility of providing the wrong information to the actuary.

We were also concerned about the date parameters that were used to capture the system data, since the actuary is given member data as of 11/30/XX and financial data as of 12/31/XX.

DEPARTMENTAL RESPONSIBILITIES

Based on our understanding of the process on how data was provided to the actuary, we understand that each department is allocated responsibility to answer specific individual requests from the Actuarial Document Request. Since the requests are standardized, each department is typically aware of the type and source of data necessary to fulfill the request. Each year, there are also new requests for information made by the actuary which represent process improvement opportunities and data enhancements from the prior year.

The audit tested whether the overall effort is coordinated, to ensure that all information requests are met timely and appropriate coordination between departments takes place on cross-functional informational requests.

We were also interested in determining if departments were facing specific bottlenecks or other inefficiencies in providing timely information to the actuary that can be identified and corrected.

REVIEW AND REASONABLENESS CHECKS

Although the actuarial computations are complex and beyond the expected technical expertise of Staff, we believe a process should be in place to ensure that ACERA performs a coordinated high-level management review of the information prior to furnishing it to the actuary. In addition, a second review should be completed after the actuarial valuation report has been prepared, to ensure Staff can verify at a high level, that the report appears reasonable and complete.

To complete the review process, Staff should have a basic understanding of how the data provided will be used in the actuarial valuation, what assumptions used by the actuary will change from the previous year and why, and how changes in law affect the current valuation. Further, Staff should validate each year if we are using the right data

source and if the information we are providing is complete. Although the actuary performs limited reasonableness checks and comparisons to prior year for significant differences, they are clear that ACERA owns the data, and it is up to Staff to confirm the data is correct and complete. Other staff validation should include confirming that the information used in the actuarial valuation is consistent with other public financial documents (i.e. CAFR). ACERA does perform specific checks, but the process used should be documented.

IIA AUDIT GUIDANCE AND STANDARDS

Internal auditing is conducted in diverse legal and cultural environments; within organizations that vary in purpose, size, complexity, and structure; and by persons within or outside the organization. While differences may affect the practice of internal auditing in each environment, conformance with The IIA's *International Standards for the Professional Practice of Internal Auditing (Standards)* is essential in meeting the responsibilities of internal auditors and the internal audit activity.

If internal auditors or the internal audit activity is prohibited by law or regulation from conformance with certain parts of the *Standards*, conformance with all other parts of the *Standards* and appropriate disclosures are needed.

If the *Standards* are used in conjunction with standards issued by other authoritative bodies, internal audit communications may also cite the use of other standards, as appropriate. In such a case, if inconsistencies exist between the *Standards* and other standards, internal auditors and the internal audit activity must conform to the *Standards*, and may conform with the other standards if they are more restrictive. The purpose of the *Standards* is to:

- (1) Delineate basic principles that represent the practice of internal auditing.
- (2) Provide a framework for performing and promoting a broad range of value-added internal auditing.
- (3) Establish the basis for the evaluation of internal audit performance.
- (4) Foster improved organizational processes and operations.

The *Standards* are principles-focused, mandatory requirements consisting of:

- (1) Statements of basic requirements for the professional practice of internal auditing and for evaluating the effectiveness of performance, which are internationally applicable at organizational and individual levels.
- (2) Interpretations, which clarify terms or concepts within the Statements. The Standards employ terms that are specific. Specifically, the Standards use the word "must" to specify an unconditional requirement and the word "should" where conformance is expected unless, when applying professional judgment, circumstances justify deviation. It is necessary to consider the Statements and their Interpretations as well as the specific meanings from the Glossary to understand and apply the Standards correctly.

- (3) The structure of the *Standards* is divided between Attribute and Performance Standards. Attribute Standards address the attributes of organizations and individuals performing internal auditing. The Performance Standards describe the nature of internal auditing and provide quality criteria against which the performance of these services can be measured. The Attribute and Performance Standards are also provided to apply to all internal audit services.

Assurance services involve the internal auditor's objective assessment of evidence to provide an independent opinion or conclusions regarding an entity, operation, function, process, system, or other subject matter. The nature and scope of the assurance engagement are determined by the internal auditor. There are generally three parties involved in assurance services:

- (1) The person or group directly involved with the entity, operation, function, process, system, or other subject matter - the process owner
- (2) The person or group making the assessment - the internal auditor
- (3) The person or group using the assessment - the user.

Consulting services are advisory in nature, and are generally performed at the specific request of an engagement client. The nature and scope of the consulting engagement are subject to agreement with the engagement client. Consulting services generally involve two parties:

- (1) The person or group offering the advice - the internal auditor
- (2) The person or group seeking and receiving the advice - the engagement client.

When performing consulting services the internal auditor should maintain objectivity and not assume management responsibility.

CONTROLS TESTED

CONTROL 1 – COORDINATED ACTUARIAL PROCESS

Risk Level - Medium

Control:

All requested actuarial information is systematically gathered, logged and reviewed prior to providing the information to the Actuary to ensure ACERA has delivered all of the required documents.

Risk:

Incomplete or inaccurate information is provided to the actuary due to lack of coordination between ACERA departments.

Owner:

Administration

Test:

Overall, ACERA has coordinated well in their effort to provide information to the Actuaries, in previous years. Typically, an internal “Coordinator” was selected each year and this individual was responsible for reviewing the master information request from the Actuary, determining which individual/department could provide the information, and then farming out the individual information requests to the appropriate department. Typically the actuarial requests are generic and consistent from year to year, with a few additional questions specific to clarifications in the current year or follow up on issues encountered in previous years. The specific departments will then provide the data back to the coordinator, who then passes it on to the Actuary.

- (1) We surveyed the ACERA Coordinators for 2008 and 2009 to determine if any of the departments were late in providing information or provided incomplete data to the Actuary. (W/P 1-1 – No late or incomplete submissions)
- (2) We inquired with Segal to determine if there have been problems with all requested information being submitted on a timely basis. (W/P 1-7 – Segal responded that ACERA provides data in an efficient manner per email dated 7/1/10)
- (3) We inquired with each department to determine if there have been reviews prior to delivery of the information to the actuary. (W/P 1-1 Each department was responsible for conducting their own review. No cross functional review or overall review was conducted to ensure common data was validated and consistent across departments. Further, no review was complete of the actuarial data extract, which contained ACERA member data from PensionGold, prior to sending the data to the Actuaries).

One area of concern discovered in the audit was that there was no process in place for reviewing member data from PensionGold prior to sending the information to the Actuary. Since these data files include financial and personal data for both retired and active members, and a critical input for the Actuary in developing the actuarial assumptions, this data should be reviewed for reasonableness by ACERA prior to sending the information to the Actuary. In 2008, the Accounting Department did find a difference in the member count after discovering deceased members were included in the retired member count. This was communicated to the Actuary. More details on this finding are detailed in Control 2 – Member Counts are Accurate.

In 2009, we observed the Coordinator had documented the actuarial process and had created an excellent system to track the department responsible for the requested items, the information requested, due date, when the coordinator received the information from the department, and when the information was delivered to Segal. **Please refer to W/P 1-12 and 1-13 which demonstrate a coordinated process for managing the process.**

Results:

Partially Effective

Recommendation:

- (1) The coordinator should be responsible for asking each department manager for changes in processes that may have occurred during the year. Any change should be communicated to all departments and the Actuary.
- (2) All information should go through the ACERA Coordinator. The Coordinator should serve as a gatekeeper for all information sent to or received from the actuary. This ensures all data sent and received is validated internally first.
- (3) The process should be fully documented with a communication plan and review plan.
- (4) The Coordinator should organize a review of the actuarial document request to discuss any new actuarial requests, changes in the source of information, or changes to business process.
- (5) The Actuary should be contacted to confirm the requirements and discuss any changes from the previous year or new requests.
- (6) A final review should be held prior to sending the documents to the Actuary. In addition, a post-mortem meeting should be held to determine ways to improve the process for the following year. **(W/P 1-14 to 1-18)**

Remediation Plan:

<p><u>Administration Department Response:</u> Staff agrees that a more coordinated process across departments should be implemented with a Central Coordinator, where there is better communication between departments on requests</p>	<p><u>Auditor's Response:</u> We agree with the Administrative Staff's remediation plan, and feel the implementation of a more coordinated process will benefit ACERA in ensuring we provide the Actuary the correct</p>
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requiring the a joint departmental review, any new changes to process or data sources will be discussed, and a final interdepartmental review will be conducted. The current process will be discussed and reviewed between all departments involved with the process and improved accordingly.

information on a timely basis.

CONTROL 2 – MEMBER COUNTS ARE ACCURATE

Risk Level - Medium

Control:

Member counts for active, terminated, and retired members in the Actuarial Valuation are consistent or can be reconciled with the member counts in PensionGold.

Risk:

Incomplete or inaccurate member counts are provided to the actuary resulting in incorrect actuarial assumptions.

Owner:

PRISM/Benefits/Accounting

Test:

As part of the Actuarial Request for information, the Actuaries request member data including member counts by various categories of retired and active members. ACERA's BASS (Business Application Service and Support) Team provides the Actuary with a disk containing data files representing all active and retired members sorted by member categories.

The data files are created from data in the PensionGold data base, using an Actuarial Data File Wizard (Extract Tool) that was programmed by an ACERA consultant. The tool captures the data from PensionGold in accordance with the Actuary's requirements which are specified in the document request. Member categories include Active Members, Service Retired Members, Disability Retired Members, Beneficiaries, Vested Terminated Members, and Deceased Members. (W/P A-G, 2-2 to 2-7, and Data Disk) Please note that the BASS Unit has recently updated the tool (6/9/2010), to enhance reporting related to the 30 year member flag, final average salary, and other related issues.

We used the Audit tool ACL to validate total member counts by category, to confirm we had a complete population. We then reviewed correspondence between the Accounting Department and Segal, where it was discovered that the Accounting Department had found that certain retired member counts had included deceased members. We inquired with the Actuary to determine if they were aware of the issue, and they replied that they were and that they had removed the deceased members or duplications based on the findings made by ACERA's Accounting Department. The corrections were made in 2008, and represented on page 34 of the 2008 Actuarial Valuation as "ACERA data cleanup".

Please find the breakdown as follows (ACERA Member Count Information is stored on the Data Disk and 2-2 to 2-7. Segal Count is on W/P 2-1 and 2-14 to 2-15):

	ACERA Original Count per PG Extract	Difference	Segal Count	
Active Members	11173	0	11173	
Retired Members				
Service Retired	5436	-32	5404	C
Disability Retired	793	-5	788	C
Beneficiaries	1169	-115	1054	B
Total	7398	-152	7246	
		0		
Vested Terminated	1775	-2	1773	A
		0		
Total	20346	-154	20192	

A. 2 duplicate records/1 record deleted in each case.

B. 17 matched with deceased file/98 were coded as deceased on list of beneficiaries.

C. 28 Members were deceased; 8 additional were deceased from prior year; 1 was a deceased beneficiary.

We confirmed the ACERA member counts from PensionGold against the final member counts published in the 2008 Actuarial Valuation (Segal) and determined the counts were correctly reflected by Segal in their Actuarial Valuation.

Results:

Partially Effective

Recommendation:

We feel the following controls should be adopted and performed on an annual basis to prevent data discrepancies in future years.

- (1) Final member counts for the current year are compared to final member counts of the previous year to determine if there are differences and why the difference occurred. This control will ensure staff has reviewed any changes in the member counts from year to year to validate whether the changes in the member data seems reasonable.
- (2) In the current year, compare ACERA member counts from PensionGold to the final member counts derived by the Actuary to determine if there are differences and why the difference occurred.
- (3) Research members in PensionGold with the status of suspended, inactive, deferred, or another miscellaneous status to ensure all member types are correctly categorized and reported to the Actuary.
- (4) Provide correct up-to-date information on retired members (i.e. has a beneficiary pre-deceased a member) this recommendation was made by the Actuaries as a

process improvement opportunity based on their experience with how ACERA provides data.

- (5) The Actuarial Data Wizard in PensionGold will be checked and reprogrammed (if needed) to insure that any legal or process changes are addressed prior to the annual actuary study. This recommendation is already being performed by Staff.

Remediation Plans:

<p><u>Benefits Department Response:</u> Items #1 to #3 have the same response. A reconciliation process can be developed to determine the differences and why the differences occurred. During the process, research will be done to review a member’s status, which will account for differences. In December 2010 when the actuarial file is developed, a reconciliation of last year’s member counts and this year’s changes will be done.</p> <p>This is currently part of the process. Most retired changes are payroll related, therefore, their PensionGold account needs to be updated within payroll deadlines. Beneficiary changes are updated upon receipt due to retired statements are mailed in mid-October.</p>	<p><u>Auditor’s Response:</u> We agree with the Benefit Department’s plan of action. It is a comprehensive plan and demonstrates their high level of commitment to remediate this control.</p>
<p><u>PRISM Department (BASS) Response:</u> Inaccuracies found in Internal Auditor’s report:</p> <ol style="list-style-type: none"> 1. The Actuarial Data Extract Wizard is part of ACERA’s Pension Administration System, PensionGold, which was created by Levi, Ray and Shoup, Inc. (LRS). The Actuarial Data Extract Wizard was created to meet ACERA’s and the Actuary’s membership data reporting needs used for the annual Actuarial Study. 	<p><u>Auditor’s Response:</u> We agree with the PRISM Department’s recommendation. Our use of the word “consultant” in the report should have been clear and definitive as to whom the consultant was.</p>
<p><u>PRISM Department (BASS) Response:</u> Inaccuracies found in Internal Auditor’s report:</p> <ol style="list-style-type: none"> 2. There were no issues related to 30 year member flag, final average salary or other 	<p><u>Auditor’s Response:</u> The Actuary had discovered differences when they compared the 30 year member report to the valuation census data (PensionGold Actuarial Extract).</p>

related issues. As a result of the Actuary's request for these additional data elements in 2008 and 2009, a business decision was made to modify the Actuarial Data Extract Wizard to include these items as part of the data files generated for the annual data request from the Actuary. This modification was put into place on 6/9/2010. Prior to this modification, BASS used multiple ACCESS queries to gather these items from PensionGold and provide them to the Actuary.

The dates of hire and/or membership were different for certain members.

We followed up with the Actuary as to why these differences were not communicated back to ACERA.

The Actuary responded that they were aware that the dates of hire in the census data may not be correct for 30 year members due to service purchase credits that may not be reflected in the original date of entry in the census. Therefore they used the 30 Year Report provided by ACERA. Since they made no changes to the data, they had no reason to contact ACERA.

PRISM Department (BASS) Response:

Response to the Internal Auditor's Recommendations:

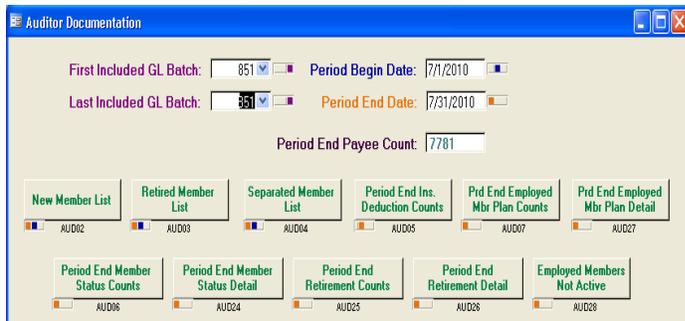
Member counts are expected to be different from year to year. There are reports in BERT that can be used to validate the differences between the counts if necessary. Reports AUD02, AUD03, AUD04, AUD06, AUD24, AUD25, and AUD26 shown below can be used and are used by Accounting Department for this validation.

Auditors Response:

The BERT reports are generated as Microsoft Access queries against the tables in the PensionGold database to capture member count according to member type (active, retired, etc.)

Although the BERT reports are a good validation tool and can be used to help verify member counts, there is a possibility of exceptions if the PensionGold program is updated or changed and these queries are no longer capturing the full population.

We suggest that the actual PensionGold Actuarial Extract Data that is sent to the Actuary be reviewed and tested against the BERT reports to confirm that the data is correct and consistent between both types of reports.



1. Currently Accounting department will validate the differences in the counts provided by the Actuary and PensionGold data.

It was determined that the Accounting Department was not previously responsible for validating the counts. They performed the count validation in 2008 for a different purpose (validate the member count for the CAFR). It was decided that going forward PRISM

	(BASS), the Accounting Department and the Benefits Department will work together to create a process to validate the member count <u>prior</u> to sending the information to the Actuary.
<p><u>PRISM Department (BASS) Response:</u></p> <p>2. Please provide clarification as to what this research should entail.</p>	<p><u>Auditor's Response:</u></p> <p>Due to the unique status of deferred, inactive and suspended members, we would like to ensure these member types are counted correctly. Also please confirm the correct classification is used when a member changes status during the year (i.e. member passes away or retires), for divorced individuals, and for beneficiaries.</p>
<p><u>PRISM Department (BASS) Response:</u></p> <p>3. Member information that is provided to the Actuary is up to date information that is contained in PensionGold as provided by the members.</p> <p>4. This is currently part of the process.</p>	<p><u>Auditor's Response:</u></p> <p>We agree with the recommendations and feel this is also in line with the recommendations made by the Benefits Department.</p>

CONTROL 3 - ACTUARIAL REPORTS ARE CONSISTENT WITH THE CAFR

Risk Level - Low

Control:

Actuarial Valuation Reports are consistent with the Comprehensive Annual Financial Report (CAFR).

Risk:

Independent financial and actuarial reports do not reconcile on key information leading third parties to lose confidence in financial reporting.

Owner:

Accounting

Test:

We cross-referenced key data from the 2008 Actuarial Valuation Report against the information in the 2008 CAFR, to ensure the same information was consistent in both documents.

Test	CAFR Source	Page #	CAFR Verification	Actuarial Source	Page #	Actuarial Verification	Result
Number of Active Members Reconciles	Letter of Transmittal	3	11136	Valuation Summary	vi	11173	Difference
Number of Active Members Reconciles	Acera Membership	29	11136	Valuation Summary	vi	11173	Difference
Number of Active Members Reconciles	Active Member Valuation Data	80	11173	Valuation Summary	vi	11173	Pass
Number of Retired Members Reconciles	Letter of Transmittal	3	7193	Valuation Summary	vi	7246	Difference
Number of Retired Members Reconciles	Acera Membership	29	7193	Valuation Summary	vi	7246	Difference
Fund Value Decline (Market Value of Assets)	Letter of Transmittal	20	1.768B	Valuation Summary	vi	1.768B	Pass
Actuarial Accrued Liability (2007)	Financial Reporting	4	5112.4	Valuation Summary	v	5112.4	Pass
Actuarial Value of Assets (2007)	Financial Reporting	4	4560.2	Valuation Summary	v	4560.2	Pass
Unfunded Actuarial Accrued Liability	Financial Reporting	4	552.2	Supplemental	40	552.19	Pass
Unfunded Actuarial Accrued Liability	Actuarial Analysis of Financial Experience	82	552	Supplemental	40	552	Pass
Current Year Funded Ratio	Financial Reporting	4	89.2	Valuation Results	23	89.2	Pass
Net Assets	MDA	16	3.8B	Valuation Results	6	3.8B	Pass
Actuarial Assumed Interest Rate	Notes to Required Supplementary Schedules	53	8%	Valuation Summary	v	8%	Pass
Actuarial Assumed Interest Rate	Summary of Assumptions and Funding Method	78	8%	Valuation Summary	v	8%	Pass
Assumed Inflation Rate	Notes to Required Supplementary Schedules	53	3.75%	Valuation Summary	v	3.75%	Pass
Assumed Inflation Rate	Summary of Assumptions and Funding Method	78	3.75%	Valuation Summary	v	3.75%	Pass
Assumed Inflation Rate	Consumer Price Index	79	3.75%	Valuation Summary	v	3.75%	Pass
Assumed Across the Board Salary Increase	Notes to Required Supplementary Schedules	53	0.25%	Valuation Summary	v	0.25%	Pass

We found exceptions in our analysis where the CAFR information is reported differently from the Actuarial Valuation. One of the key reasons is that the Actuary projects member counts for December 31st, based on November 30th data. For the CAFR the member counts are based on actual December 31st data. In addition, there are changes in member count between these dates, since people continue to retire, pass away and get hired in the month of December.

We inquired with Staff as to why November 30th member data is provided to the Actuary instead of December 31st. We were informed that ACERA made a business decision to use the November 30th date, since there would be significant delay in providing data files to the Actuary, because currently the Active member data files provided by employers are not received by ACERA until the end of January. Once

these files are received, they are loaded into PensionGold. Then any generated exceptions are cleared, which can take an additional two weeks.

The Actuary confirmed the November 30th date was due to ACERA's business process and they have made adequate disclosures (Actuarial Standard of Practice Statement 4 - Measuring Pension Obligations) on their actuarial certification (Actuary's Certification Letter in Footnote 1) to inform financial statement users of the difference. Although this would mean that the member count sections of the CAFR will not reconcile with the Actuarial Valuation on member count, we agree with Staff that a higher priority should be ensuring the Actuarial Valuation is completed timely.

However, we do believe that ACERA and the employers should challenge the timeline and determine if there is a way to shorten the review process, so that both financial and member data can be reported as of December 31, XXXX ,in the future. **(Please refer to CAFR in Section O and the Actuarial Valuation in Section M to the appropriate page numbers above. Also refer to W/P 3-4).**

Results:

Effective

Recommendation:

We agree with Staff and recommend that ACERA continue the process of reporting member data as of 11/30/XX and financial data as of 12/31/XX. But we do believe a reconciliation process should be in place to determine the difference in counts between 11/30/XX and 12/31/XX and to communicate that difference to the Actuaries. Please refer to Control 10 – Year-End Member Data Reconciliation.

Remediation Plan:

No remediation required

CONTROL 4 –CONTRIBUTION RATES ANNUAL SET-UP

Risk Level - Low

Control:

Employer and Employee Contribution Rates in the Actuarial Valuation reconcile to the rates inputted into the PensionGold System.

Risk:

Since PensionGold has a direct general ledger feed, if the contribution rates in PensionGold are misstated, the exception count will be unmanageable.

Owner:

PRISM/Accounting

Test:

Each year, the Actuaries provide ACERA with the contribution percentage rates for employer and employee contributions. These changes in rates are authorized under California Code Section 31454, and based on the percentage of payroll. These contribution rates are loaded into the PensionGold System by PRISM (BASS Unit), and verified using the Rate Verification Tool. The Rate Verification Tool enables ACERA to load the Safety and General Member rates into the system and set the effective date for when those rates will apply. Subsequently the BASS Analyst can run a comparison of Contribution Rate Data from PensionGold to the same data that has been loaded into the Rate Verification Tool, to ensure that complete and accurate rate information has been entered. Typically the rate modifications are made in either pay period 19 or 20 in the calendar year. In 2008, it was made in pay period 19.

Please note that due to resource and time constraints, we only tested Alameda County. We tested the configuration settings for the 2008 employer contribution rate entry in PensionGold to match it to the rates established by the Actuary. We confirmed that annual settings in PensionGold matched the rates.

Please see attached documentation detailing the Employer Contribution Rate Update Process in PensionGold (W/P 4-9 to 4-19).

Please note that in addition, this is a compensating control to call attention to incorrect employer contribution rates entered by the employer. Employers independently enter the employer contribution rate information into their own payroll system which they use to fund ACERA with contributions. An exception would be generated in PensionGold if the employer paid a contribution on the employer transmittal that did not match the rates in PensionGold. There is an Access data base tool called "TETRA" that tracks these exceptions. If the employer used the wrong rate, the exceptions in that transmittal would be listed and would inform ACERA that the employer should be contacted to deal with the situation. In addition, the Accounting department performs an analysis using Microsoft Excel for each transmittal using current contribution rates in

order to validate the reasonableness of the contribution rate used in calculating the employer rate.

We tested Alameda County's transmittal payment for pay period 09-19. This was the time when the new contribution rates went into effect. There were minor differences in the exception file which were primarily related to minor variances and vacation cash-out payments. These exceptions are routinely researched and cleared by the Accounting Department. This process was effective. We looked at contribution rate exceptions in the TETRA system and verified that the new contribution rates were correctly entered by PensionGold and Alameda County. (W/P 4-1 to 4-8).

Results:
Effective

Recommendation:
None

Remediation Plan:
No remediation required

CONTROL 5 – NET MARKET VALUE OF ASSETS RECONCILES TO FINANCIAL STATEMENTS

Risk Level - High

Control:

Net Market Value of Assets in the Actuarial Valuation reconciles to the Great Plains Balance Sheet

Risk:

Incorrect valuation of assets could lead to incorrect contribution estimates and to an over or under funding of ACERA retirement contributions.

Owner:

Accounting

Test:

We tested whether the Net Market Value of Assets in the Actuarial Valuation was equal to the ACERA 2008 Balance Sheet in Great Plains. This test was to confirm that the Net Market Value Assets amount used to support the CAFR can be traced back to the system generated balance sheet, and no manual manipulations were made to the system generated balance, without proper authorization and documentation. (W/P 5-1 to 5-5)

Our test process was to generate a balance sheet report as of December 31, 2008 from Great Plains and compare the Net Market Value of Assets amount in the balance sheet report to the amount listed in the Actuarial Valuation. We determined that the valuation matched.

Test	ACERA 2008 Balance Sheet	Actuarial 2008 Valuation	Difference
Net Market Value of Assets	\$3,805,950,089	\$3,805,950,089	0

Results:

Effective

Recommendation:

None

Remediation Plan:

No remediation required

CONTROL 6 – INVESTMENT RATE OF RETURN COMPARISON

Risk Level - High

Control:

Compare the real rate of return computed by SIS (Investment Advisor) with the real rate of return computed by Segal (Actuary) using the target asset allocation for ACERA. The control will also test the differences in the real rate of return between different asset classes.

Risk:

Lack of reconciliation between the Actuary and Investment Consultants on key financial assumptions will lead to an unrealistic investment rate of return.

Owner:

Investments

Test:

Per the memo dated February 3, 2009, the Actuaries provided an explanation for their economic assumptions for the valuation prepared December 31, 2008. (W/P Segal 2008 Assumptions – Section H)

They explained that they were adopting the 2007 Actuarial Assumptions, due to the volatility in the marketplace in 2008. They also explained that typically investment advisors use a shorter time frame (5-15 years) for their investment return assumptions versus an actuarial approach which uses (30-40 years).

Our objective was to determine if the average real rate of return rates based on the composite average of nine investment advisory firms who serve Segal's public sector clients (including SIS) were in line with the investment return rates projected by the Investment Advisor (SIS) on its own. We were also interested in understanding what steps does Staff take to reconcile rate data between these different sources.

We tested the difference between the rates used by the Actuary and those provided by the Investment Consultant to see if there were significant differences in the investment rates. Please note that the only effective way to test the rates of return was to review the real rate of return, which is the rate of return without consideration for inflation rate. Therefore in the calculation for SIS, we subtracted the inflation rate assumption of 2.4% to achieve a real rate of return, since SIS used a different inflation rate than Segal. In the case of Segal, the inflation rate had been already subtracted out.

The portfolio percentage (Portfolio %) reflects the long-term asset allocation model used by ACERA, and is broken out between asset classes. To enhance this test, we also compared the rates of return at the asset class level, to determine if there were significant differences between the projections at the asset class level, and if so, how does ACERA reconcile the differences.

Please refer to the following analysis: (W/P 6-2, 6-9, 6-17)

Asset Class	Segal Projections			SIS Projections			Difference
	Segal 2009 Expected Real Rate of Return	Portfolio %	Weighted Ave. Rate of Return	SIS 2009 Expected Real Rate of Return	Portfolio %	Weighted Ave. Rate of Return	
Domestic Large Cap Equity	6.45	0.2960	1.9092	7.39	0.2960	2.1874	-0.2782
Domestic Small Cap Equity	6.98	0.0740	0.5165	8.54	0.0740	0.6320	-0.1154
Developed International Equity	6.95	0.2070	1.4387	7.47	0.2070	1.5463	-0.1076
Emerging Market Equity	9.29	0.0230	0.2137	10.58	0.0230	0.2433	-0.0297
Domestic Bonds	1.77	0.1800	0.3186	1.70	0.1800	0.3060	0.0126
International Bonds	1.81	0.0360	0.0652	2.17	0.0360	0.0781	-0.0130
High Yield Bonds	5.04	0.0240	0.1210	4.56	0.0240	0.1094	0.0115
Commodities	5.66	0.0250	0.1415	7.50	0.0250	0.1875	-0.0460
Real Estate	4.83	0.0600	0.2898	5.13	0.0600	0.3078	-0.0180
Absolute Return	4.07	0.0250	0.1018	4.07	0.0250	0.1018	0.0000
Private Equity	13.55	0.0500	0.6775	13.55	0.0500	0.6775	0.0000
Total		1.0000	5.7933		1.0000	6.3771	-0.5838

(1) Asset allocation by asset class based on Actuarial Assumptions which reflects the SIS Allocation Model.

(2) Absolute Return and Private Equity weighted average rates of return were the same for Segal and SIS (note 2 on page 5 of the Review of Economic Actuarial Assumptions for 2009)

(3) In 2008, Segal did not prepare a similar analysis of the Average Real Rate of Return due to the turmoil in the 2008 market. Therefore used 2009 analysis for comparison purposes.

The results of the analysis showed a difference in weighted average real rate of return between Segal and SIS of less than .6%. ($6.3771 - 5.7933 = .5838$). Although we are comfortable with the conservative methodology used by the Actuary, of averaging the investment rates using data provided by several investment advisory firms, we urge Staff to perform this analysis to understand the differences in investment rates and to determine if the overall variance or variance at the asset class level is significant enough to challenge the investment rate assumptions.

Results:

Partially Effective

Recommendation:

- (1) Continue the practice of using the conservative methodology used by the Actuary of using average investment rates using data from a sample of investment advisors, but possibly augmenting the analysis by comparing the data to other investment indexes and benchmarks. In our opinion, the Actuary's methodology is acceptable and will typically lead to a conservative estimate in the long-term investment rate projection.
- (2) Staff should perform a comparison to ensure there are no significant differences at the asset class level or with the weighted average rate of return.
- (3) It might be beneficial to have our investment consultants (SIS) provide ACERA with a 30-40 year real rate of return projection to compare with the actuarial projections.

Remediation Plan:

Investment Department Response:

The Investment Department agrees with the overall recommendation, but recommended Internal Audit change the language in recommendations 2 and 3 as follows.

- (1) Continue the practice of using the conservative methodology used by the Actuary of using average investment rates using data from a sample of investment providers, but possibly augmenting the analysis by comparing the data to other investment indexes and benchmarks. In our opinion, the Actuary's methodology is acceptable and will typically lead to a more conservative estimate in the long-term investment rate projection.
- (2) Staff should perform a comparison to evaluate and monitor whether or not there are any significant differences in the real rate of returns at the asset class level or at the weighted average level.
- (3) It might be beneficial to investigate whether or not our investment consultants (SIS) could provide ACERA with a 30-40 year real rate of return projection to compare with the actuarial projections.

Auditor's Response:

We agree with these changes in language as recommended by the Investment Department and feel their suggestions add much better clarity.

CONTROL 7 - CONFIRM ACTUAL CONTRIBUTIONS EQUAL'S EXPECTED CONTRIBUTIONS

Risk Level - High

Control:

Confirm actual employer and employee contributions equal's expected contributions.

Risk:

Adequate funding contributions are not made which reduces the viability of the plan.

Owner:

Administration/Accounting

Test:

Dec YTD 2009 - YTD 2008 Analysis					
Description	Employer (ER)	Dec YTD 2009	Dec YTD 2008	Increase / (Decrease)	Percent Increase / (Decrease)
Based on Transmittals	Total Pensionable Wages	\$ 841,498,324.82	\$ 817,533,320.13	\$ 23,965,004.69	2.93% (A)
Based on Actuary	Average Actuarial Rate	15.59%	15.71%	-0.12%	
Calculated Employee Contributions: (Pensionable Wages X Actuarial Rate)		\$ 131,151,400.32	\$ 128,395,715.49	\$ 2,755,684.84	2.15% (B)
Change Due to Wages	(Wage Change X 2008 Rate)			3,763,765.77	2.93%
Change Due to Rates	(Rate Change X 2009 Wages)			(1,008,080.93)	-0.79%
Per GL Balances	Actual Employer Contributions	\$132,198,602.05	\$129,660,362.93	\$2,538,239.12	1.96% (C)
Per PG GL Export	Non Transmittal Corrections	\$530.00	(\$98,282.49)	\$98,812.49	0.00%
Adjusted Actual Contributions	Net Actual Employer Contributions	\$132,198,072.05	\$129,758,645.42	\$ 2,439,426.63	1.88% (C)
Actual Rate	(Actual / Pensionable)	15.71%	15.87%	-0.16%	(C) / (A)
Dec YTD 2009 - YTD 2008 Analysis					
Description	Employee (EE)	Dec YTD 2009	Dec YTD 2008	Increase / (Decrease)	Percent Increase / (Decrease)
Based on Transmittals	Total Pensionable Wages	\$ 841,498,324.82	\$ 817,533,320.13	\$ 23,965,004.69	2.93% (A)
Based on Actuary	Average Actuarial Rate	8.66%	8.64%	0.02%	
Calculated Employee Contributions: (Pensionable Wages X Actuarial Rate)		\$ 72,873,754.93	\$ 70,636,543.23	\$ 2,237,211.69	3.17% (B)
Change Due to Wages	(Wage Change X 2008 Rate)			2,070,625.19	2.93%
Change Due to Rates	(Rate Change X 2009 Wages)			166,586.50	0.24%
Per GL Balances	Actual Employee Contributions	\$77,270,662.00	\$75,607,686.24	\$1,662,975.76	2.20%
Per PG GL Export	Non Transmittal Contributions	\$2,160,600.94	\$1,978,026.93	\$182,574.01	9.23%
Adjusted Actual Contributions	Net Actual Employee Contributions	\$75,110,061.06	\$73,629,659.31	\$ 1,480,401.75	2.01% (C)
Actual Rate	(Actual / Pensionable)	8.93%	9.01%	-0.08%	(C) / (A)
	Other difference	\$2,236,306.13	\$2,993,116.08	(\$756,809.94)	-1.00%

Bi-weekly contributions are made by employers in accordance with the contribution percentage table, provided by the Actuary. This data is verified by the Accounting

Department Staff which reconciles employer contributions with expected contributions to ensure adequate and timely funding has occurred. This reasonableness check allows ACERA to confirm that actual contributions are in line with what is expected. The calculation is performed on a monthly basis and based on pensionable wages for employers and employees.

We reviewed the accounting analysis for 2008/2009 year-end and determined that the actual contributions met or exceeded the expected contributions for 2008. (W/P 7-1 to 7-2)

Results:

Effective

Recommendation:

None

Remediation Plan:

No remediation required

CONTROL 8 – 30 YEAR MEMBER SERVICE

Risk Level - Low

Control:

Verify only qualified members are exempt from making contributions due to attaining 30 years of service.

Risk:

Incomplete or inaccurate member counts are provided to the actuary resulting in incorrect actuarial assumptions. In addition, contributions can be halted for members who have not qualified for 30 year service or not halted on those who have qualified for 30 year service.

Owner:

PRISM/Benefits

Test:

We asked the Actuary to review the list of 30 year members provided by ACERA to determine if the list was accurate. The Actuary responded as follows:

Actuary's Response:

I have attached to this e-mail the list of 134 members originally sent by ACERA for the December 31, 2008 valuation (note that the count should actually be 133, as the first line contains header information). Since the attached file contains SSNs, I have password protected the file and will call you with the password.

You noted that the distribution charts in our December 31, 2008 valuation report show 307 General members with at least 30 years of service, compared to the 133 (corrected) General and Safety members on the contribution exemption file sent by ACERA. However, out of the 307 General members with 30 or more years of service, only 115 of them had an original date of hire on or before March 7, 1973 (a requirement for contribution exemption). In comparison, out of the 133 records on the contribution exemption file, 23 were Safety members and 110 were General members.

When comparing the 115 records in the valuation data with the 110 records in the contribution exemption file, 15 of the 115 valuation records did not match the contribution exemption file and 10 of the 110 contribution exemption records did not match the valuation data. I have included additional tabs on the attached file that provides names and SSNs of these unmatched records.

Based on the Actuary's response, we wanted to understand why there were differences in the number of 30 year members between the PensionGold Actuarial Extract (census data) and the 30 year member list provided by ACERA. Therefore, we asked the Benefits Department to review exceptions found by the Actuary to determine

if the Actuary was correct. The Benefits Department determined that there were no exceptions to the 30 year member report, but did determine that ACERA does need to clarify their 30 year member policy with the Actuary, since ACERA's policy allows for special treatment for divorce cases, reciprocal service, and completed redeposit, which the Actuary may not be aware of. Further, the dates of entry for these types of members may not be reflected in the PensionGold Actuarial Data Extract (census data) given to the Actuary. To identify true 30 year members in PensionGold, a 30 year member flag must be selected, which marks which members with 30 years of service qualify to have their contributions halted (W/P 8-1 to 8-13).

We also confirmed with the Actuary that they did use the 30 year member list provided by ACERA, since they were aware that the PensionGold Actuarial Data Extract (census data) was not always correct for the 30 year member count for contribution exemptions. We believe in any event, a process must be put in place where the Actuary communicates any discrepancies they find in the data back to ACERA for confirmation. (W/P 8-1 to 8-13)

7/9/2010: Please note that the remediation was initiated by the Benefits/BASS team, and modifications to the 30 year member report were made. The report will now allow for the report to be run using the a 30 year flag which will be added to the Active member and Deferred Retirement extract files at Field 178, Position 1434. Field length will be 1. True = 30 Year flag is Checked. False = 30 year flag is not checked. With the changes to the report configuration, we strongly believe the new report will accurately reflect the 30 year members. (W/P 8-14)

Results:

Remediated

Recommendation:

The revised 30 year report will need to be tested in the next audit cycle.

Remediation:

No additional remediation required. The Benefits Department will coordinate with the Actuary to ensure they are aware of the 30 Year Member Policy at ACERA.

CONTROL 9 – COST/BENEFIT ANALYSIS ON UNKNOWN MARITAL STATUS

Risk Level - Medium

Control:

Formal resolution on why certain information requested by the actuary was not provided. This may include a cost/benefit analysis.

Risk:

Incorrect or incomplete information provided to the actuary could result in inaccurate actuarial assumptions.

Owner:

PRISM/Benefits

Test:

Actuary requested information on 523 retired members whose marital status was listed as “unknown”. ACERA did not provide the information and therefore the actuary used the marital status field from previous valuations.

We tested the list of 523 names and sampled selected members to see if we could determine the marital status using other information stored in the member record found in the PensionGold system. We found that some member records had a marital history or a spouse listed in the beneficiary screen, but the marital status in the personal information screen was still listed as “unknown”. In other instances it appeared as though the member was “domestic partner” which was not one of the choices in the marital status screen. We inquired with the actuary to determine how the marital status field should be categorized. The Actuary responded by indicating “DOMST” should be used for domestic partners, and the beneficiary relationship as “OTHER”.

Based on input from the Actuary, they felt this information is necessary and an improvement if ACERA was able to provide the information. They will be able to assist in defining the requirements more clearly.

Results:

Improvement Opportunity

Recommendation:

A cost/benefit analysis should be completed to determine the cost of updating the marital status on these records in PensionGold. If the benefits outweigh the costs, a formal investigation of all 523 names should be completed and the marital status corrected prior to the next actuarial study. In the future, the retirement specialist who updates a member record affecting marital status should be made aware that they will also need to update the marital status field on the personal information screen, to ensure consistency. Further, consideration should be given to determine if the PensionGold system should be updated to include domestic partnerships and/or any other state mandated change to marital status.

Remediation Plans:

<p><u>Benefits Department Response:</u> Benefits were not aware of Actuary's request of information on 523 retired members. If Benefits were alerted to the impacts of the marital status, further discussion/changes in procedure would have taken place</p>	<p><u>Auditor's Response:</u> The Benefits Department should have been notified of this requirement. The process failed and needs to include validation that all of the Actuary's requests have been answered by the right party.</p>
<p><u>Benefits Department Response:</u> To address the 523 retired members, benefits can begin updating PensionGold after all of the retired member files have been imaged, otherwise, retired member files would need to be pulled and not all retired files are available. The backfile for the retired files is due to be completed on September 24, 2010. In October 2010, support staff will update the necessary fields in PensionGold and complete by November 30, 2010.</p> <p>A couple of concerns that need further discussion:</p> <ol style="list-style-type: none">1. Marital status changes can only be done on deferred and retired members. Updates to active member's status will be overridden when a transmittal file is imported into PensionGold and updates the member's account.2. Marital status of retired and deferred members is only updated upon the request of the member.	<p><u>Auditors Response:</u> We agree with the Benefit Staff's Assessment. This is a well thought out remediation strategy which takes into account EDMS Project constraints and raises issues that will need to be addressed on working with employers to correct the transmittal files for marital status.</p>
<p><u>PRISM Department (BASS) Response:</u> Inaccuracies found in Internal Auditor's report:</p> <ol style="list-style-type: none">1. The write up states Domestic Partner is not a marital status option. In fact, Domestic Partner is a selectable marital status in PensionGold. See screen shot	<p><u>Auditor's Response:</u> We agree with the PRISM Staff's assessment. The selectable marital status was available for selection for the status of Domestic Partner.</p>

<p>below.</p> 	
<p><u>PRISM Department (BASS) Response:</u> Inaccuracies found in Internal Auditor's report:</p> <p>2. In the write up, it is stated the Actuary is requesting that members who are domestic partners should have their marital status reported as "DOMST" and the beneficiary relationship as "OTHER". Further, it is stated that the Actuary felt this information is necessary and an improvement if ACERA was able to provide this information. In the Retiree data file domestic partners' marital status is reported as "DOMST", and the beneficiary relationship as "OTHER". This information has been reported to the Actuary since the 2007 Actuarial study.</p>	<p><u>Auditor's Response:</u></p> <p>We disagree with the assessment. There are over 500 members identified with a marital status of "unknown", where no marital status is indicated in the member record under the Marital Status Field. In our review, some members should have been identified as Domestic Partners, as the record shows the beneficiary as the member's domestic partner under the Nominated Beneficiary Tab, which is another tab in the same member record. Just because the marital status field is available, does not mean it is being populated correctly.</p>
<p><u>PRISM Department (BASS) Response:</u> BASS's Response to the Internal Auditor's Recommendations:</p> <ol style="list-style-type: none"> 1. Benefits will need to determine if researching and updating the marital status for these 523 members is feasible. 2. PensionGold currently has domestic partner as a marital status type and meets current Federal and State mandates for marital status 	<p><u>Auditor's Response:</u></p> <p>We agree with PRISM Department's assessment and this also appears to be in line with the recommendation from the Benefits Department.</p>

CONTROL 10 – YEAR-END MEMBER DATA RECONCILIATION

Risk Level - Low

Control:

Year-end member data is reconciled for significant increases or decreases in member count.

Risk:

There may be a significant difference in the Actuary's projected December end member counts and the actual December end member counts, which is not communicated to the Actuary.

Owner:

PRISM/Accounting

Test:

ACERA provides to the Actuary active and retired members as of November 30, 2008. The Actuary used this data to project December 31, 2008 data. We were concerned that a possibility exists that a significant increase or decrease in member counts could have occurred between the projected December 31, 2008 member counts and the actual December 31, 2008 member counts, causing a variance in total active and retired members for the year.

In our inquiry to the Actuary, to determine why ACERA is reporting member counts as of November 30th, instead of December 31st, they mentioned that it was an ACERA request to prepare the counts earlier, to facilitate the data gathering for the CAFR. We confirmed with Staff that the date was not established to facilitate the data gathering for the CAFR, but rather to ensure that the member data files from the employers were complete. If the date range for the data files were to be changed to include data up to 12/31/XX, there would be a significant delay in providing these data files to the Actuary, because the Active member data files provided by employers are not received by ACERA until the end of January. Once these files are received, they are loaded into PensionGold. Then any generated exceptions are cleared, which can take up to two weeks. (W/P 10-1 to 10-2)

The Actuary projects November 30th data forward to December 31, which is the "as of date" for the financial data. They have not had the need to make adjustments for increases or decreases in membership in December because they were not aware of any significant changes which would warrant such adjustments. Segal was aware that the relevant actuarial standard allowed and may call for these adjustments if deemed significant. Any changes in the December data not deemed to be significant would normally be reflected in the following valuation. Segal is willing to use the actual December count to reflect a more precise Actuarial Valuation as of December 31, XXXX, assuming they receive notification from ACERA prior to the release of the valuation. This can be explored by Staff, as long as the benefits outweigh the costs.

PensionGold is a dynamic database that can only report on current data. Since the active and retired reports were not run as of year-end, we were unable to determine the true member counts as of 12/31/2008. Please note that in the current process, the Accounting Department runs the member count to perform a reasonableness check as of 12/31/XXXX. Based on the member counts in 2009, we feel there wasn't a significant increase or decrease in member counts between 11/30/08 and 12/31/08.

Results:

Remediated

Recommendation:

If we continue to report member counts as of November 30th, 20XX, we recommend that a second PensionGold Actuarial Report for member counts be run on December 31, 20XX, to get an accurate count of members as of year-end. This report should be furnished to Segal to provide confirmation on any significant changes to the member counts.

Remediation Plan:

<p><u>PRISM Department (BASS) Response:</u> Any date range can be entered in the Actuarial Data Extract Wizard to create the data files. As directed by Senior Management, BASS uses the date range of 12/1/xx to 11/30/xx. Please keep in mind that if the date range for the data files were to be changed to include data up to 12/31/xx, there will be significant delay in providing these data files to the Actuary, because the Active member data files provided by employers are not received by ACERA until the end of January. Once these files are received, they are loaded into PensionGold. Then any generated exceptions are cleared, which can take up to two weeks. Under the direction of Senior Management the date range used to create the membership data files for the annual Actuarial study can and will be changed.</p>	<p><u>Auditors Response:</u> We agree with PRISM Department's in their assessment that any change in process could affect the timeline to complete the Actuarial Valuation. Regardless, we should have tested the member count on 12/31/08 to see if the count differed significantly from the projected count used by the Actuary. Per the Actuary, they expect ACERA to notify them if there is a significant difference in count in the last month of the year. This control was not part our process in the past, so we can implement in the future. Please note that "significant change" has not been defined, so we should apply a conservative approach where any change in member count should be communicated to the Actuary.</p>
<p><u>Accounting Department Response:</u> Reconciliation is being performed by the Accounting Department between 11/30/XXX and 12/31/XXXX member data and therefore control is remediated.</p>	<p><u>Auditors Response:</u> Control Remediated.</p>

CONTROL 11 - TIMELY UPDATE OF BENEFICIARY INFORMATION

Risk Level - Low

Control:

Provide correct up-to-date beneficiary information on current retired members (i.e. has the beneficiary pre-deceased a member).

Risk:

Incomplete or inaccurate member counts are provided to the actuary resulting in incorrect actuarial assumptions.

Owner:

Benefits

Test:

We inquired with the Actuary (Segal) about areas where ACERA can improve in providing better information to aid Segal in preparing the Actuarial Valuation. They stated that ACERA should provide better information on beneficiaries of retired members (i.e. has a beneficiary pre-deceased a member). They are willing to provide ACERA with guidance on best practices to determine beneficiary status. (W/P 12-1)

Results:

Partially Effective

Recommendation:

Staff should work with the Actuary to put in place a process to better monitor and report beneficiaries that have pre-deceased the member.

Remediation Plan:

Benefits Department:

This is currently part of the process. Most retired changes are payroll related, therefore, their PensionGold account needs to be updated within payroll deadlines. Beneficiary changes are updated upon receipt due to retired statements are mailed in mid-October. Please provide clarification as to the Actuary's needs.

Auditor Comments:

We agree with the Benefits Department that a good process is currently in place, but there may be an opportunity to provide better data to the Actuary. This control can be best remediated through a discussion with the Actuary on how best to capture the beneficiary information to meet their needs.

CONTROL 12 – NO DUPLICATION OF MEMBERS IN PENSIONGOLD

Risk Level - Medium

Control:

Members are not duplicated in the PensionGold system and receiving multiple benefits.

Risk:

Members or their beneficiaries are receiving benefits they are not entitled to.

Owner:

Benefits

Test:

Using the ACL program, we compared the social security numbers between the active member files and inactive files (retired, deferred, death, and beneficiary member files) to determine if duplicate members existed in the files.

We did find duplicate members in the death, beneficiary and deferred files, but these duplicates were acceptable because they represented members who were in an active status for part of the year and inactive status for the other part of the year (i.e. member had passed away during the year, so they were an active member in the active file for part of the year and then a deceased member in the deceased file). These types of members are identified and reported to the Actuary.

We found no reportable exceptions and felt the business process is effective. (W/P 13-1 to 13-14)

Results:

Effective

Recommendation:

None

Remediation Plan:

No remediation required

CONTROL 13 – POST- ACTUARIAL VALUATION REVIEW

Risk Level - Medium

Control:

Post - Actuarial Valuation Review is conducted in which ACERA evaluates and reviews key actuarial assumptions and significant changes from the previous year.

Risk:

Incomplete or inaccurate actuarial assumptions will jeopardize the long-term viability of the plan.

Owner:

Administration/Accounting/Benefits

Test:

Key actuarial assumptions and significant issues should be reviewed and confirmed by ACERA Staff for reasonableness. In the current business process, significant emphasis is placed on the Actuary's expertise and experience in developing the actuarial valuation, with ACERA playing a passive role. Going forward, we feel Staff should develop a process for challenging assumptions and making recommendations to the Board of Retirees on a suggested course of action in adopting the Actuarial Valuation. We did not find evidence of this occurring in our review of the 2008 Actuarial Valuation.

For example, we feel the following assumptions and changes should be reviewed:

- (1) Significant issues identified by the Actuary in the valuation year.
- (2) Assumptions where the Actuary states they are relying on information provided by ACERA.
- (3) Changes in actuarial assumptions or methods (i.e. rate of inflation, investment rate of return)
- (4) Changes in statutory provisions
- (5) Employer assumptions for increases or decreases in salary.

Results: Improvement Opportunity

Recommendation:

- (1) Set up an annual meeting with the Actuary to discuss and review key assumptions and changes made in the Actuarial Valuation for the current year.
- (2) Determine if there have been any changes in ACERA's internal process or business that may impact actuarial assumptions.
- (3) Review changes to the external business environment or legislation (i.e. health reform) to determine the effects on the variables selected for use in the actuarial estimate.

(4) Compare assumptions made in the current period with those of prior periods and have Actuary explain any differences.

Remediation Plan:

<p><u>Administration/Accounting Department Response:</u> The opportunity is for ACERA Staff to better understand the impact of changes in contributions, investment returns and benefits on the actuarial valuation.</p>	<p><u>Auditors Response:</u> All three departments have come up with excellent remediation plans. This will help ACERA become more familiar with a complicated process which is critical to ACERA's success.</p>
<p><u>Benefits Department Response:</u> On a yearly basis, benefits can review any internal process changes that may impact actuarial assumptions. Benefits will confirm these changes with the Actuary. In addition, Benefits will seek assistance from the BASS and HR departments to develop reports on assumptions for increases or decreases in salary. Similar to internal changes, benefits can review changes to the external business environment or legislation to determine whether the assumptions made are accurate and confirm with the Actuary.</p>	<p><u>Auditors Response:</u> See above</p>

CONTROL 14 – PRIVACY AND SECURITY OF MEMBER DATA

Risk Level - High

Control:

Designate responsibility for managing confidential information within the agency and establishing and maintaining security over such information.

Risk:

Inadequate security for member data could lead to privacy violations leading to harm to the member or agency.

Owner:

PRISM

Test:

We inquired with the PRISM (BASS Unit) on what data security measures were taken when member data was sent to the actuary. We were pleased to understand PRISM was proactive and have taken proper precautions by confirming that data is zipped and encrypted, and then burned onto a CD and delivered via courier. (W/P 15-1)

Since the member data information is privileged and could result in a significant breach if the data fell in the wrong hands, we would suggest that all data requests made by the Actuary be coordinated through the Coordinator and PRISM, who can ensure that all data is sent and received in encrypted fashion.

Results:

Effective

Recommendation:

Written procedures on how data should be transmitted (i.e. encryption) should be communicated to all departments involved in providing information to the Actuaries. This will highlight the risks of the departments responding to the actuary directly versus going through the Coordinator, who can ensure that any privileged data is sent via a highly secured method. Further, data security practices should be shared with third parties (i.e. employers) to ensure they are aware of best practices in sending or receiving member data from ACERA.

Remediation Plan:

No remediation required.

CONTROL 15 – LAWS AND REGULATIONS ARE REVIEWED PERIODICALLY

Risk Level - High

Control:

New, proposed and existing laws and regulations (i.e. IRS, GASB, California, 1937 ACT, and Healthcare Reform) are reviewed to determine impact to the plan.

Risk:

Laws and regulations change and ACERA is no longer in compliance with the new standards. Changes in rules and regulations and/or ACERA's adoption of a policy or interpretation of a statute are not properly communicated to the Actuary.

Owner:

Administration/Accounting/Legal

Test:

Throughout the year, information related to changes in laws and regulations should be reviewed and discussed with the Actuary. Appropriate outside counsel or subject matter expert should be used when appropriate, similar to the work performed by Tax Counsel on determining if ACERA has met all qualified plan requirements. In the 2008 Actuarial Valuation and Review (Pg. 41), the Actuaries provided a synopsis of the Section 415 Limitation regarding the maximum benefits that can be paid to an individual from a defined benefit plan. Their disclaimer in this section states that "Legal Counsel's review and interpretation of the laws and regulations should be sought on any questions in this regard". We did not observe a formal documented process in 2008 on the use of outside counsel/advisors to address laws and regulations affecting ACERA.

In our discussion with the Assistant CEO, we were pleased to note that in recent years, ACERA has sought outside counsel to help evaluate compliance with IRS rules and regulations. It is also noted that outside counsel did raise specific concerns, and ACERA is dealing with the issues proactively. Per our inquiry with Staff, ACERA has become more proactive in their analysis of the potential impact of changes to laws and regulations and often works with Outside Legal Counsel, External Auditors and the Actuaries to understand the issues and recommended resolutions, and will take steps to document key decisions made.

Results:

Remediated

Recommendation:

We believe an additional best practice step can be to create a formal issue log that states how key issues were communicated and resolved so we have a sufficient paper trail. Further, documentation should be retained detailing how a specific regulation was interpreted and the position ACERA is taking in response to the issue.

CONCLUSION

Overall, based on our audit testing, we believe ACERA's process for providing complete and accurate actuarial data to the actuary is adequate. We did find opportunities for improvement, which can be summarized as follows:

- (1) ACERA does not have an adequate review process where information is reviewed in detail prior to sending it to the actuary. In most cases the verification is performed at the department level, but no verification is performed across departments.
- (2) ACERA should also perform a post actuarial valuation review, where the actuarial valuation is reviewed for key assumptions and significant changes from the previous year. This will enable Staff to learn more about the actuarial calculations and provide better data to the actuary in the future.
- (3) The Coordinator of the actuarial process should ensure a high level of cross-department communication takes place, so any change in a business process in one department will be communicated to other departments. For example, we evidenced the collaboration between the Benefits Department and PRISM Department with regards to ensuring better member data reports were delivered from PensionGold.