



June 20, 2019

TO: 2019 Audit Committee
Joseph Kelly, Chair
Gina Sanchez, Vice Chair
Herman Santos, Secretary
Alan Bernstein
Shawn Kehoe
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Audit Committee Consultant
Rick Wentzel

FROM: Richard Bendall 
Chief Audit Executive

Christina Logan 
Senior Internal Auditor

FOR: July 11, 2019 Audit Committee Meeting

SUBJECT: **Board and Staff Education & Travel Audit**

RECOMMENDATION

In accordance with your current Audit Committee Charter, staff recommends that the Audit Committee review and discuss the following engagement report to take the following action(s):

- 1. accept and file report and/or,**
- 2. instruct staff to forward report to Boards or Committees and/or,**
- 3. provide further instruction to staff.**

ENGAGEMENT REPORTS

- a. Board and Staff Education & Travel Audit
Christina Logan, Senior Internal Auditor
(Report issued: June 20, 2019)

Please note: attached to the report is another version of the report that includes questions and comments that staff received from your Committee as well as Internal Audit's responses.

Attachments



LACERA INTERNAL AUDIT DIVISION

**Board and Staff
Education & Travel Audit**

June 20, 2019

AUDIT PERFORMED BY:
Christina Logan, CPA, CFE
Senior Internal Auditor

EXECUTIVE SUMMARY

LACERA incurs education and travel expenditures to ensure Board members and staff are properly educated in monitoring the administration and investments of the Trust, and advocating positions that protect and further the interests of the Trust. LACERA has an Education and Travel Policy (Policy), which the Boards last updated in March 2017, to facilitate Boards and staff in balancing their fiduciary responsibilities to be knowledgeable advocates and to be fiscally prudent with the Trust's funds.

We completed this audit as part of the Fiscal Year (FY) 2019 (July 2018 – June 2019) Audit Plan. Internal Audit periodically performs a compliance audit of the Policy to address the operational risks associated with travel. We last audited Board and staff education and travel expenditures in FY 2016.

In determining the scope of the audit, we considered the following:

- The Boards' education travel expenditures had increased, while staff's education travel expenditures had decreased, over the last three fiscal years.

Fiscal Year	Board education travel expenditures	Change over base year (FY 2016)	Staff education travel expenditures	Change over base year (FY 2016)
2016	\$269,861	-	\$497,918	-
2017	\$303,320	11% increase	\$433,349	13% decrease
2018	\$403,267	49% increase	\$381,671	23% decrease

- The Boards' budget for all travel and education was \$411,000 in FY 2018. The budget rose to \$529,000 for FY 2019 and to \$569,000 for FY 2020 (a 38% increase over 2 years).
- Peer public pension fund board education travel was more limited in frequency and costs than LACERA's Board education travel.
- A public data request for the Board of Investments' travel was made in August 2018.

To address the above risks and to assess if internal controls related to Board and staff education and travel expenditures are effective in mitigating the associated risks of fraud, operational, compliance, and reputational risk, we included the following objectives in our audit:

Section 1: Compliance with the Policy

Section 2: Review of the effectiveness and adequacy of the Policy

We observed that Board and staff were generally compliant with the Policy although we identified areas that could be improved through better communication by key stakeholders, more complete travel files, and updates and/or revisions to the Policy. However, we also

identified that the Policy allowed for a broad array of practices that are not effective in controlling costs. Some examples include but are not limited to the following:

- Individual Board members incurred annual travel costs ranging from less than \$1,000 to more than \$55,000
- Individual Board members purchased airfare as high as \$12,500 for a single international trip
- Individual Board members attending anywhere from one to 16 educational events (local and non-local) per year

Our survey of peer public pension plans both within California and throughout the United States supported our concern that LACERA is a significant outlier in costs incurred for Board educational (non-administrative) travel. Most notably, LACERA incurred significantly higher costs for Board educational travel in FY 2018 than either CALPERS, a \$350 Billion fund as of June 2018, or CALSTRS, a \$226.1 Billion fund as of May 2019. We found that these two funds were the most supportive of Board education and travel, including some international travel, among the funds in the peer group. Based on the data provided to us, we did not identify any peer funds in the survey that exceeded either CALPERS or CALSTRS in expenditures for board educational travel.

Overall, we found opportunities for LACERA Boards and management to achieve a Policy with more effective measures of education and training while minimizing costs. We observed that the Policy could be more effective and better aligned with published best practices and peer pension funds by focusing on an organization-wide educational strategy.

See the following table on the next page for a summary of the issues and recommendations identified during the audit.

Summary of Issues and Recommendations

Page(s)	Issues	Recommendations
Section 1: Compliance with the Policy		
A. Assessment of travelers and FASD's review process		
10 – 13	Compliance Exceptions	<ol style="list-style-type: none"> 1. FASD management should assess the need to obtain missing documentation and/or recover amounts from travelers for noncompliant transactions that were identified during the audit. 2. FASD management should ensure that its staff consistently enforces the Policy and escalates to FASD management any areas of the Policy requiring interpretation or clarification. 3. Management should periodically provide training to the Boards and staff on the Policy to ensure travelers and approvers are aware and compliant with the Policy requirements. 4. To improve the effectiveness and efficiency and to consistently enforce the review process, FASD, the Legal Office, and the Executive Office should meet periodically to determine a joint understanding of the Policy, how to address and document when questionable charges occur, and if updates or revisions should be suggested to the Boards. 5. To be consistent with the section "Authorized Expenses" (705.02) of the Policy, that expenses should be "reasonable and necessary," Boards and management should: <ol style="list-style-type: none"> a. Revise the Policy to reflect current economical transportation services, like public transportation, taxis, or ride-share services. The Policy should still require the traveler to provide written justification if an upgraded ground transportation service is used. b. Update the Policy to address if and when the use of an executive car service is acceptable.
14	FASD does not have complete files for each travel event	<ol style="list-style-type: none"> 6. To improve the effectiveness and efficiency of FASD's review process, FASD should: <ol style="list-style-type: none"> a. Provide instructions for the Travel Expense Voucher (payment request), so travelers can provide a complete travel file. b. Work with the Systems Division and the Executive Office to explore solutions that would allow travelers to upload and allocate travel receipts, and that would allow FASD to review and store complete travel files in a central location.
B. Completeness and accuracy of Monthly and Quarterly Travel Reports		
15	Accuracy of Quarterly Travel Reports	<ol style="list-style-type: none"> 7. To improve the accuracy of the Quarterly Travel Reports, FASD should: <ol style="list-style-type: none"> a. Ensure all members of FASD's Disbursements Unit are adequately trained and supervised. b. Instruct travelers on providing a complete travel file, and work with the Systems Division and the Executive Office to explore having traveler's upload and allocate travel receipts to a central location
16 – 17	Administrative travel is not clearly addressed in the current Policy	<ol style="list-style-type: none"> 8. To strengthen the Policy, the Boards and management should revise the Policy to better clarify "Administrative Travel," to define controls regarding when administrative travel is authorized, if there is a limit to administrative travel, and how administrative travel should be categorized for Board members.
17 – 18	"Local Educational Conferences" per the Policy are difficult to categorize	<ol style="list-style-type: none"> 9. To ensure conferences are consistently and accurately categorized, conference limitations are applied, and to assist Board members in planning their educational conferences, Boards and management should revise the Policy to provide a standardized definition of "local educational conferences" - for example, limiting local education to Los Angeles County, Southern California, or a set distance from LACERA.

Summary Continued

Summary of Issues and Recommendations (continued)

Page(s)	Issues	Recommendations
Section 2: Review of the Effectiveness and Adequacy of the Policy		
21 -23	The Policy does not have an organizational-wide educational strategy	10. To improve the effectiveness and adequacy of the Policy, Boards and management should: a. Review the Clapman report's educational policy for a template of best practices. b. Consider adopting an organizational-wide educational strategy and incorporating the "Trustee (Fiduciary) Knowledge Self-Assessment." c. Consider working with LACERA's Training Coordinator to develop a process to create a stakeholder's educational plan, monitor the broader educational needs of the Board for in-house training opportunities, and review and evaluate educational conferences.
23 – 24	Board airfare has increased substantially	11. To reduce LACERA's total airfare costs and the high exposure to headline risk, Boards and management should: a. Re-evaluate the use of business class airfare. b. Evaluate stronger enforcement of prudent procurement practices, including prohibiting the purchase of refundable tickets.

See Results Section of the report for Management's Responses.

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INTRODUCTION

The Board of Retirement, Board of Investments, and designated staff have a fiduciary duty to obtain education about public pension administration and investments, to monitor the administration and investments of the Trust, and to advocate positions that protect and further the interests of the Trust. LACERA has an Education and Travel Policy (Policy), which was last updated in March 2017, to facilitate the Boards and staff in executing this fiduciary duty and to ensure LACERA's funds are used in a manner consistent with LACERA's overall mission. Authorized education and travel expenses include, but are not limited to, expenses related to the attendance at industry conferences and various educational and training seminars, legislative meetings, and on-site due diligence visits for existing and potential service providers.

We completed this audit as part of the Fiscal Year (FY) 2019 (July 2018 – June 2019) Audit Plan. Internal Audit periodically performs a compliance audit of the Policy to address the operational risks associated with travel. We last audited Board and staff education and travel expenditures in FY 2016. For this audit, we reviewed FY 2018 (July 2017-June 2018) education and travel expenditures:

Category of Travel Events	Boards	Staff
Education	\$403,267	\$381,671
Administrative	<u>\$23,153</u>	<u>\$227,409</u>
Total	\$426,420	\$609,080

BACKGROUND

Pre-Travel Authorization

Board members are pre-approved to attend conferences listed on Attachment C of the Policy, and local conferences that have a registration fee less than \$500 and no common carrier travel or lodging. However, Board members must seek Board approval to attend conferences not included on Attachment C or any international conferences. Staff members must obtain approval from the Chief Executive Officer (CEO) for education and travel. Once travel has been authorized, Financial & Accounting Services Division (FASD) will create an event number in the Travel Manager program to record the event name, official travel dates, location, and travelers. FASD then assigns staff the event number so all related expenditures can be allocated correctly.

Travel Arrangements

Board and staff are encouraged to make travel arrangements as far in advance as possible to take advantage of early bird registrations, conference room rates, and lower fares. Executive Board Assistants (Assistants) and Division Managers generally use their LACERA corporate credit card to pay for conference registration, lodging, and airfare. FASD requires corporate cardholders to provide receipts and allocate these expenditures to the correct event number. Managers review and approve the purchases on a monthly basis. FASD then reconciles the monthly corporate credit card statements against the receipts and researches any discrepancies or missing documentation.

Reimbursements

Generally, travelers request reimbursement for expenses incurred while traveling such as meals, mileage, parking, and airline baggage fees. Individuals are required to submit a Reimbursement Expense Voucher (Expense Voucher) within 90 days of completing the travel, or 30 days after the fiscal year-end, whichever occurs first. For Board members, the Assistants will review the Expense Vouchers for general compliance and then the CEO will approve them. For staff, division managers review and approve the Expense Vouchers. Approved Expense Vouchers are then routed to FASD for an additional review, approval, and processing.

FASD's Review

FASD is responsible for reviewing the Expense Vouchers and monthly corporate card receipts to ensure the expenditures are consistent with the Policy. FASD reviews the receipts provided to ensure date, times, and amounts are consistent with the corresponding conference and travel agendas. FASD also recalculates the mileage amount, ensures the per diem is calculated based on the correct General Services Administration rate and Meal & Incidental Breakdown, and allocates expenses that are shared between travelers (e.g., a shared meal or a shared taxi ride) to the appropriate divisions. If FASD has questions or needs additional documentation, they email either the Assistants or staff.

Travel Reports

On a monthly basis, FASD prepares the Monthly Education and Travel Expenditures Report (Travel Report), which details the completed, anticipated, and canceled education and travel for Board and staff for the fiscal year. This report does not reflect costs. On a quarterly basis, FASD prepares the Quarterly Travel Report, which details the education and travel expenditures paid / reimbursed by LACERA for Board and staff. These reports are distributed monthly and quarterly to Board and staff.

Since the Policy limits Board members to 8 (or 12 if on both Boards) conferences but does not limit the number of local educational conferences per fiscal year (Section 705.07), FASD categorizes the Travel Reports for Board travel as:

- "A" - Pre-approved conferences listed on Attachment C of the LACERA Education and Travel Policy and/or Board approved conferences.
- "B" - Administrative conferences and/or local educational conferences that do not require common carrier travel and lodging totaling less than \$1,500.
- "X" - Canceled events for which expenses have been incurred.

AUDIT OBJECTIVES & METHODOLOGY

The audit objectives were to assess if internal controls related to Board and staff education and travel expenditures are effective in mitigating the associated risks of fraud, operational, compliance, and reputational risk. Specifically, we reviewed the following:

SECTION 1: Compliance with the Education and Travel Policy

- A. Assessment of travelers and FASD's review process
 - Reviewed LACERA's Education and Travel Policy dated March 2017.
 - Sampled Board's and staff's travel to verify the expenditures were compliant with the Policy, accurate, and valid, and reviewed the travel events for fraudulent activity.
 - Sampled payment requests to ensure FASD thoroughly reviewed requests, questioned charges that appeared inconsistent, rejected out of compliance charges, and processed payment requests timely.
- B. Completeness and accuracy of Travel Reports
 - Reviewed the Travel Reports to determine if educational conferences were correctly categorized as local educational conferences, and to ensure the 8/12 conference limitation was applied consistently and accurately to all Board members.
 - Reviewed canceled trips to ensure they were documented in the Travel Reports, individuals who canceled provided valid reasons in a timely manner, and if fees were incurred, they were either pardoned by the Board chair or repaid to the fund.

SECTION 2: Review of the Effectiveness and Adequacy of the Education and Travel Policy

- Reviewed best practice guidance.
- Reviewed peer public pension funds' education and travel policies and travel reports (if available).
- Reviewed current news articles about governmental agencies' travel.
- Discussed Policy, procedures, process, and controls with FASD, the Legal Office, and the Executive Office.

AUDIT SCOPE

The audit scope for compliance testing included Board and staff education and travel expenditures for FY 2018. We tested approximately 10% of Board education and administrative travel, 20 events totaling \$122,435. We tested approximately 10% of staff education and administrative travel, 34 events totaling \$84,863.

The audit scope for the review of the effectiveness and adequacy of the Policy was limited to Board education travel. We limited the scope to Board education travel, after considering the following:

- The Boards' education travel expenditures had increased, while staff's education travel expenditures had decreased, over the last three fiscal years.

Fiscal Year	Board education travel expenditures	Change over base year (FY 2016)	Staff education travel expenditures	Change over base year (FY 2016)
2016	\$269,861	-	\$497,918	-
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- The Boards' budget for all travel and education was \$411,000 in FY 2018. The budget rose to \$529,000 for FY 2019 and to \$569,000 for FY 2020 (a 38% increase over 2 years).
- Peer public pension fund board education travel was more limited in frequency and costs than LACERA's Board education travel.
- A public data request for the Board of Investments' travel was made in August 2018.

RESULTS

We have categorized the results of our audit into two separate and distinct sections. The first section, “**Compliance with the Education and Travel Policy**,” discusses our findings from the test work performed and includes recommendations to strengthen either the Policy or the processes. The second section, “**Review of the effectiveness and adequacy of the Education and Travel Policy**,” presents our findings from researching best practice guidance, peer comparisons, and recent media headlines and includes recommendations to better align with industry practices.

SECTION 1: **COMPLIANCE WITH THE POLICY**

A. ASSESSMENT OF TRAVELERS AND FASD’S REVIEW PROCESS

We tested the selected sample travel events against the Policy and related procedures. See the chart below for a summary of our testing. We concluded travelers were generally compliant with Policy and related procedures, and FASD generally performs a thorough, detailed review of payment requests and credit charges. We did not find any instances of fraud in our testing but did find areas where the Policy and/or related payment processes could be strengthened.

Attribute Tested	Compliance Assessment Good = No exceptions Fair = 1-10% exceptions Weak = more than 10% exceptions
Educational conference or administrative travel was pre-approved	Fair
Educational conference met 5-hour education requirement	Good
Airfare and ancillary costs were consistent with the Policy	Good
Airfare purchased / reimbursed by LACERA was the airfare the travel used	Good
Lodging was consistent with the conference hotel rate and/or 3 times approved government rate for that city for non-conference travel, for a standard room, and consistent with the travel itinerary	Fair
Meal charges were consistent with conference and travel itinerary	Fair
Ground transportation was consistent with the conference and travel itinerary	Weak
Incidentals and miscellaneous charges were reasonable	Good
Mileage charges were accurate and consistent with travel itinerary	Good
Parking charges were consistent with conference and travel itinerary	Good
Reimbursement request was submitted timely	Good
Thorough review – receipts support charge, per diem rates and Meal & Incidental breakdown verified, calculations checked for accuracy, questionable charges resolved.	Fair
Canceled travel included a written valid reason provided by the traveler, and any associated costs over \$50 were pardoned by Board chair	Good

Issue: Compliance Exceptions

- I. A traveler attended an educational conference with only verbal approval from the CEO. When the traveler submitted a payment request for the trip, FASD staff notified the traveler the event had not been created in the Travel Manager because no written approval had been submitted. Subsequently, the CEO provided written approval for the trip. Although the Education and Travel Policy stipulates, "The CEO, or designee, shall approve staff education and travel," the expectation is for staff to receive written approval prior to making travel arrangements, from the CEO. The traveler explained the CEO had provided verbal approval, but the traveler did not obtain written approval prior to making or taking the trip. The traveler said it was an oversight and the traveler has not made the mistake again.
- II. A traveler attended an educational conference and stayed for additional personal days. The traveler's additional personal days of lodging were charged to the corporate credit card. Although the Policy does not specifically address personal expenditures, LACERA's Corporate Credit Card Policy (Section 4.2) dated April 2016, which was in effect during this time period, does address personal expenditures. It stated, "In order to promote the public's confidence in the integrity of the Corporate Card Program and avoid any appearance of commingling of business-related expenditures with personal expenditures, use of the Corporate Card for personal purchases is strictly prohibited at any time." When the traveler returned, the traveler immediately reimbursed LACERA for the personal portion of the lodging. The traveler explained the hotel had mistakenly charged all the lodging days to LACERA's card, instead of only charging the conference days. The traveler stated that for upcoming trips the traveler would clarify which cards to use when checking-in to the hotel. Although LACERA was able to recoup the personal portion of hoteling timely, this practice does not comply with the Corporate Credit Card Policy and FASD does not have the resources to track payments owed to LACERA by individual travelers. FASD addressed this issue by providing Corporate Credit Card training to all staff in March 2019.
- III. A traveler attended an educational conference and booked an upgraded room. The Policy (Attachment A: Lodging – A. Room Cost) limits room rates to "a standard class single room rate. We noted a price difference of approximately \$50/night between the two rooms when we priced the hotel for the same month but the following year. The traveler did not provide a written justification for the upgrade and staff did not identify or question the upgrade.
- IV. When a traveler attended an educational conference, he/she reserved a room, which included breakfast not provided with standard room. Although the hotel rate included breakfast, the traveler requested the breakfast per diem for all the travel days. The Policy (Attachment A: Meals) specifically states, "LACERA will not reimburse the traveler for a meal which has been pre-paid by LACERA whether or not the traveler consumed the meal" unless written justification is provided to document if the traveler had either special dietary restriction or had to conduct LACERA business during the meal. The traveler did not provide a written justification for the breakfast per diem. Staff did not question the request justification for the breakfast per diem since the hotel receipt was not included with the

payment request documentation but was instead included with the credit card documentation.

- V. A traveler requested authorization to have LACERA pay for a personal item that was lost while attending an approved conference and the Executive Office approved the expenditure. We noted the Policy does not address payment for personal items lost while traveling for LACERA business but the Executive Office approved the payment, without seeking guidance from either the Legal Office or FASD.
- VI. The current Policy states in section 705.11, "Individuals are expected to use group shuttle service to and from metropolitan destinations...Reimbursement of an alternative mode of transportation will be limited to the cost of the group shuttle service unless otherwise justified." However, our audit disclosed that travelers do not use group shuttle services for ground transportation nor do travelers provide a business justification when using an alternative method. Travelers generally use taxis or ride sharing service for ground transportation needs. Internal Audit noted FASD does not question the use of alternative methods of transportation nor does FASD limit reimbursement to the cost of the group shuttle service as stated in the Policy. Per discussion with staff, FASD did not enforce the Ground Transportation section of the Policy because using alternative transportation methods, instead of group transportation, had become the common and accepted practice. However, this change in practice should have been discussed with the Executive Office and Legal Office, and the Policy should have been revised.

Additionally, we observed some Board members used an executive car service for ground transportation needs. We noted several times the executive car service was used domestically, including for transportation to and from the local airport. The travelers did not provide a business justification for using the executive car service and FASD did not question the charges.

Recommendations:

1. FASD management should assess the need to obtain missing documentation and/or recover amounts from travelers for noncompliant transactions that were identified during the audit.

Management Response

Management concurs with the recommendation. FASD management will have staff review the audit exceptions, and follow-up with travelers to obtain missing documentation and/or recover any amounts owed, as applicable, due to non-compliant transactions. This recommendation is expected to be completed by January 31, 2020.

2. FASD management should ensure that its staff consistently enforces the Policy and escalates to FASD management any areas of the Policy requiring interpretation or clarification.

Management Response

Management concurs with the recommendation. FASD will evaluate a monitoring mechanism to ensure consistent Policy enforcement. In addition, Management re-emphasized to staff the importance of elevating exceptions to the Policy for guidance and resolution. This recommendation is partially implemented and is expected to be completed upon the approval of the revised Policy.

3. Management should periodically provide training to the Boards and staff on the Policy to ensure travelers and approvers are aware and compliant with the Policy requirements.

Management Response

Management concurs with the recommendation. FASD will work with the Executive and Legal Offices to schedule Travel Policy training for the Boards and staff at least annually or when the Policy is revised. This recommendation is expected to be completed by June 30, 2020.

4. To improve the effectiveness and efficiency and to consistently enforce the review process, FASD, the Legal Office, and the Executive Office should meet periodically to determine a joint understanding of the Policy, how to address and document when questionable charges occur, and if updates or revisions should be suggested to the Boards.

Management Response

Management concurs with the recommendation. FASD management will schedule joint meetings with FASD, the Executive and Legal Offices when there are Policy updates. In addition, this core group will convene at least bi-annually to review the Policy and related issues of non-compliance to determine if such issues warrant Board consideration for Policy revision. This recommendation is expected to be completed upon the approval of the revised Policy.

5. To be consistent with the section "Authorized Expenses" (705.02) of the Policy, that expenses should be "reasonable and necessary," Boards and management should:
 - a. Revise the Policy to reflect current economical transportation services, like public transportation, taxis, or ride-share services. The Policy should still require the traveler to provide written justification for using an upgraded ground transportation service if used.
 - b. Update the Policy to address if and when the use of an executive car service is acceptable.

Management Response

Management concurs with this recommendation. Management will bring the issue to the JOGC for further discussion. This recommendation is expected to be completed by January 31, 2020.

Issue: FASD Does Not Have Complete Files for Each Travel Event

During our test work, we noted FASD does not have a complete physical or electronic file for each travel event but instead maintains several platforms of information; a binder with all approved conferences and related agendas, a corporate credit card database, and Great Plains, a financial and accounting software system. Not having a complete file for each travel event decreases the effectiveness of the review process, an operational risk. For example, when a traveler submits a payment request it is generally shortly after returning from the trip. If the payment request includes a per diem for breakfast, even though the traveler's lodging included breakfast, FASD at that time would not have the receipt for lodging. The receipt for lodging would be submitted several weeks later if the lodging was paid using LACERA's corporate credit card. In this scenario, FASD is reviewing the payment request but they do not have a complete understanding of all the expenditures related to the travel event.

Additionally, not having a complete travel file makes it more difficult for FASD to provide accurate numbers on the Travel Reports.

Recommendation

6. To improve the effectiveness and efficiency of FASD's review process, FASD should:
 - a. Provide instructions for the Travel Expense Voucher (payment request), so travelers can provide a complete travel file.

Management Response

Management concurs with the recommendation. FASD will update the Travel Expense Voucher to include clear written instructions for completing the document. This recommendation is expected to be completed by June 30, 2020.

- b. Work with the Systems Division and the Executive Office to explore solutions that would allow travelers to upload and allocate travel receipts, and that would allow FASD to review and store complete travel files in a central location.

Management Response

Management concurs with the recommendation. FASD held preliminary discussions with the Systems Division and the Executive Office to evaluate the feasibility of implementing a travel receipt capture and storage tool. This recommendation is partially implemented and expected to be completed by June 30, 2020.

B. COMPLETENESS AND ACCURACY OF TRAVEL REPORTS

Per our review of FY 2018 Travel Reports, Internal Audit found several areas that could be strengthened to improve the completeness and/or accuracy of the reports.

Issue: Accuracy of Quarterly Travel Reports

We noted several instances where the Quarterly Travel Report did not accurately reflect the travel expenditures for a traveler's trip. Examples of the errors were:

- Registration Fees included registration for the correct event and a future event.
- No airfare recorded since a credit from a previously canceled flight was used.
- Lodging included hotel and associated parking fees.

In addition to the inaccuracies that Internal Audit identified, we learned from discussions with FASD, the Executive Board Assistants, and the Legal Office that the FY 2018 Quarterly Travel Reports were significantly revised for inaccurate reporting of travel expenditures before a public data request was fulfilled. Based on discussions with FASD, many of the inaccuracies in the Reports were caused by having a key member of FASD's Disbursements Unit out of the office for the majority of the year, and not having a complete travel file, as discussed in the prior section.

Recommendation

7. To improve the accuracy of the Quarterly Travel Reports, FASD should:
 - a. Ensure all members of FASD's Disbursements Unit are adequately trained and supervised.

Management Response

Management concurs with the recommendation. FASD management instructed supervisors and staff to review and consistently refer to the current Policy. When changes to the Policy occur, the supervisor will ensure staff are aware of those changes and are adequately trained on such changes. This recommendation is expected to be completed by January 31, 2020.

- b. Instruct travelers on providing a complete travel file, and work with the Systems Division and the Executive Office to explore having traveler's upload and allocate travel receipts to a central location.

Management Response

Management agrees with the recommendation. FASD will provide instructions for complete travel files to travelers. In addition, FASD held preliminary discussions with the Systems Division and the Executive Office to evaluate the feasibility of implementing a travel receipt capture and storage tool. This recommendation is expected to be completed by June 30, 2020.

Issue: Administrative Travel Is Not Clearly Addressed In the Current Policy

During FY 2018, LACERA spent approximately \$23,000 on administrative, non-educational travel for Board members. Board members traveled for administrative purposes to meet with Congress and to execute duties as a SACRS board member. During FY 2018, LACERA spent approximately \$243,000 on administrative travel for staff. The Investment Office's travel for due diligence reviews made up most of staff's administrative travel.

On the Travel Reports, staff categorized Board travel as either:

- "A - Pre-approved conferences or conferences not listed in Attachment C of the LACERA Education and Travel Policy" or
- "B - Administrative conferences and/or local educational conferences that do not require common carrier travel and lodging totaling less than \$1,500"

For FY 2018, the Executive Office and FASD categorized the following administrative travel as "B - Administrative conferences and/or local education conferences":

Travel Date	Conference and Location	Board Members and Total Cost	Approval
Five travel events during FY 2018	SACRS Board Meetings, Sacramento, CA	1 Board member with a total cost of approximately \$5,000	No approval – Staff carried forward the interpretation that attending SACRS Board meetings qualified as administrative travel. In March 2019, the Board of Retirement authorized the travel from July 2014 through 2019 as administrative thus not counting towards the annual conference limits.
May 2018	IFEBP Legislative Update & Federal Engagement - Washington D.C.	3 Board members attended with a total aggregate cost of approximately \$14,000	April 2, 2018 Memo – The Board of Retirement approved the reimbursement of travel costs but does not address how to categorize the travel.

As the current Policy does not clearly address the definition of administrative travel, how administrative meetings should be categorized, or if administrative travel should count towards a Board member's annual conference limit, staff excluded administrative travel from the annual conference limits. Staff consistently applied this interpretation to all Board members and all Travel Reports have reflected this interpretation since July 2014. However, during our audit, we noted stakeholders were unclear if staff's interpretation of the Policy was correct. The Policy should be revised to more clearly address "Administrative Travel."

Recommendation

8. To strengthen the Policy, the Boards and management should revise the Policy to clarify “Administrative Travel” to define controls regarding when administrative travel is authorized, if there is a limit to administrative travel, and how administrative travel should be categorized for Board members.

Management Response

Management concurs with this recommendation. Management will bring the issue to the JOGC for further discussion. This recommendation is expected to be completed by January 31, 2020.

Issue: “Local Educational Conferences” Per the Policy Are Difficult to Categorize

Per the Policy, local educational conferences are conferences where there is no common carrier travel and lodging is under \$1,500, and these conferences should not be counted towards the annual 8/12 conference limit. We observed that it is difficult to categorize which conferences should be considered “local educational conferences”, not subject to the 8/12 limit, as this determination needs to be made for each traveler’s individual travel expenditures.

When we reviewed the 4th Quarter FY 2018 Travel Report, we noted that staff had categorized several trips as “local educational conferences” but these trips included either airfare or lodging was over \$1,500.

If FASD had applied the current Policy definition of local educational conferences, the following conferences should be re-categorized based on each Board members’ travel:

- **Fall SACRS Conference, November 14-17, 2017** – Three Board members flew to San Francisco so for those travelers, the conference should have counted towards the 8/12 educational conference limit. One Board member drove to San Francisco so for that traveler, the conference was correctly categorized as a local educational conference, and not counted toward the educational conference limit.
- **IFEBP Public Employees Benefits Institute, June 25-27, 2018** – One Board member flew to Las Vegas so for that traveler, the conference should have counted towards the 8/12 educational conference limit. One Board member drove to Las Vegas so for that traveler, the conference was correctly categorized a local educational conference, and not counted toward the educational conference limit.
- **Milken Conference, April 29 – May 2, 2018** – One Board member’s lodging for the conference in Los Angeles was over \$1,500 so for that traveler, the conference should have counted towards the 8/12 educational limit. Nine other Board members’ lodging for the conference was under \$1,500 so for those travelers, the conference was correctly categorized as a local educational conference, and not counted toward the educational limit.

Recommendation

9. To ensure conferences are consistently and accurately categorized, conference limitations are applied, and to assist Board members in planning their educational conferences, Boards and management should revise the Policy to provide a standardized definition of “local educational conferences” – for example, limiting these to Los Angeles County, Southern California, or a set distance from LACERA.

Management Response

Management concurs with this recommendation. Management will bring the issue to the JOGC for further discussion. This recommendation is expected to be completed by January 31, 2020.

SECTION 2:

REVIEW OF THE EFFECTIVENESS AND ADEQUACY OF THE POLICY

When we evaluated the effectiveness and adequacy of the Education and Travel Policy, Internal Audit recognized Board and staff must balance their fiduciary responsibilities to be knowledgeable advocates and to be fiscally prudent with the Trust's funds. Travel expenditures represent a high-risk area to government entities as travel is scrutinized by the media and there is an expectation that funds are used efficiently, effectively, and transparently. To evaluate our Policy, we reviewed industry best practices, compared other public pension funds' education and travel policies and if available, published travel reports, and recent media articles regarding travel by governmental agencies.

Best Practices

Internal Audit found three relevant published reports regarding best governance practices for public pension funds:

- a. Clapman Peter & Waddell, Christopher. **"Clapman Report 2.0 (Clapman): Model Governance Provisions to Support Pension Fund Best Practice Principles."** *Stanford Institutional Investor's Forum Committee on Fund Governance (SIIF)*. May 2013.
<https://law.stanford.edu/event/the-clapman-2-0-report-fulfilling-public-pension-board-fiduciary-duties-through-the-adoption-of-governance-best-practices/>
- b. Regan, Julian. **"Best Governance Practices for Public Retirement Systems."** *National Conference on Public Employee Retirement Systems (NCPERS)*. March 2012.
<https://www.ncpers.org/content.asp?contentid=755>
- c. Waddell, Christopher. **"Enhancing Public Pension Plan Security: Best Practice Policies for Trustees and Pension Systems."** *American Federation of State, Municipal, and County Employees (AFMSCE)*. December 2009. <https://www.afscme.org/news/press-room/press-releases/2009/afscme-releases-best-practices-guide-for-pension-systems>

Each of these reports discussed the need to have an effective board education policy, which encourages fiduciaries to improve continuously upon the skills needed to be an effective fiduciary. The report published by NCPERS does not provide further detail but the reports by SIIF and AFMSCE include a template of their recommended educational policy. Both of these reports focus their policy guidance on 1) developing core competency expectations for board members, 2) evaluating the board members core competencies through a self-assessment, and 3) the organization working with the board and individual members to develop a strategic, effective, and documented organizational and individual education plan for the upcoming year(s).

Peer Comparison

We compared LACERA's Board education and travel to that of other 37 Act Funds within California, CALPERS, CALSTRS and various other State public pension plans including those we believe are leading organizations such as Wisconsin SWIB, Texas TRS, Oregon PERS, State of Washington Investment Board, NYSTRS, Florida State Investment Board and others. Our peer

comparison included reviewing the websites of each fund, reviewing the travel policies, interviewing Chief Audit Executives and obtaining data, where available on budget and expense information related to board member education and travel. Peer summary results are below:

	Travel Category	Peer Summary
1	International Travel	Most Funds do not provide for board members to travel internationally. However, those that allow international travel are more restrictive than LACERA. NYSTRS permits international travel for board education in their policy but limits total expenses per board member for travel and education to \$6,000 each per year. CALSTRS and CALPERS do approve international board travel although significantly less than LACERA.
2	Business Class Air Travel	Most funds either do not allow for business class travel or restrict it to flights with a minimum duration of at least 6 to 14 hours. CALPERS for example, only permits business class for international board travel.
3	Conferences Limits	Most funds do not have policy limits on the number of educational conferences board members can attend. Those that did ranged from limits of two to five events per year.
4	Dollar Limits	Most funds do not have dollar limits per board member for education and travel. Funds that did had limits ranging from \$6,000 per board member to \$13,500 per board member annually. For funds that did not have dollar limits per board member, we did not find funds whose total board education costs would have exceeded \$13,500 if averaged among the board members of the fund.
5	Peer range of budget/actual expenditures	Board educational travel expense data for the peer funds for FY 2018 ranged from below \$50,000 to \$137,000 (CALPERS). CALSTRS recently increased its annual budget from \$100,000 to \$120,000 for its board educational travel.

Media Articles

Government entities are held to a high standard in ensuring that public funds are used efficiently and effectively, and the uses of such funds are transparent to the public. Towards this objective, Board-related travel expenses should be reasonable and in line with what a prudent person would incur when conducting official business. Absent controls to ensure prudent spending, Board members are at a greater risk of creating the perception of impropriety (whether perceived or actual); reputation risk, from not only the media, but also our plan sponsors and members. Media coverage regarding travel by pension fund trustees focuses mainly on travel destination, premium class airfare, luxury lodging, entertainment and meals. Article headlines have included:

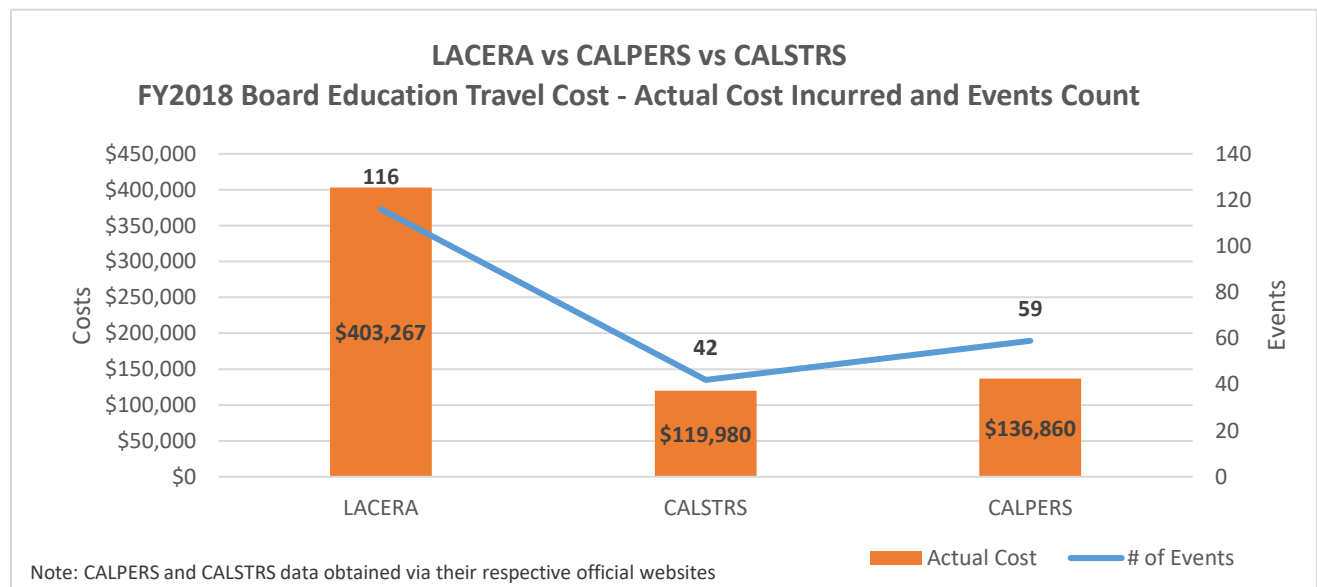
- a. Broadwater, Luke & Wenger, Yvonne. **“City Pension Officials Spend Nearly \$100,000 on Trips.”** *Baltimore Sun*. March 18, 2015 www.baltimoresun.com/maryland/baltimore-city/bs-md-ci-pension-travel-20150318-story.html

- b. Avila, Jale. **“Trustees Spending Fire and Police Pension Funds on Expensive Travel.”** *News 4 San Antonio*. May 3, 2018. www.news4sanantonio.com/news/trouble-shooters/news-4-trouble-shooters-uncover-abuse-of-travel-at-fire-and-police-pension-fund
- c. Einhorn, Erin & Lesser, Benjamin. **“Globetrotting Pension Fund Officials Racked up \$400,000 in Costs as Retirees, Taxpayers Foot Bill.”** *New York Daily News*. April 10, 2010. www.nydailynews.com/new-york/globetrotting-pension-fund-officials-racked-400-000-costs-retirees-taxpayers-foot-bill-article-1.167070

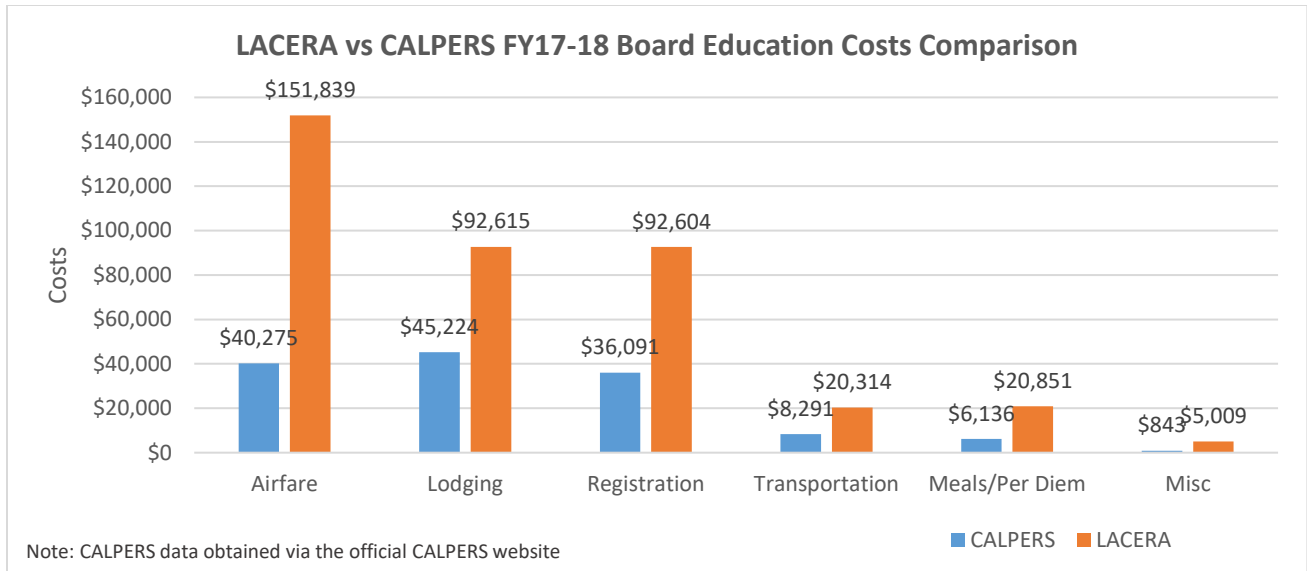
Issue: The Policy Does Not Have an Organizational-Wide Educational Strategy

In our assessment of the current Policy, we noted it does not have an overarching educational strategy that focuses on developing and improving key skills that fiduciaries generally need. Instead, the Policy focuses more on the transactional activities related to education and travel, like conference limits, lodging, and meals. The focus on transactional activities is meant to restrict the costs to reasonable and necessary expenditures but we found that for FY 2018, LACERA's Board education travel expenditures for 15 Board Members significantly exceeded a peer comparison with CALSTRS, who had 10 board members, and CALPERS, who had 13 board members.

Due to the different number of board members of each fund, we calculated the average cost per Board Member: 1) \$26,884 for LACERA, 2) \$11,998 for CALSTRS, and 3) \$10,528 for CALPERS.



We noted LACERA Board Members attended between 1 to 16 educational conferences each (local and non-local), with a total travel cost ranging from less than \$1,000 to over \$55,000 per traveler. Seven Board members listed on the 4th quarter Travel Log, spent over \$25,000 for the Fiscal Year and their combined totals accounted for 79% (\$310,173) of Board educational travel.



The *Clapman* report identified concerns about relying on educational conferences as the primary form of education. The report states:

There is no lack of educational opportunities available to public pension fund trustees, and trustees as a rule are diligent about attending them. However, while trustees “devote considerable time and effort to education, primarily by attending a variety of conferences that are geared to public funds and that focus on investments,” such programs as a rule “neither encourage trustees to develop the broad vision they need to set policy, nor do they provide the practical grounding a board needs to oversee a fund’s operations.” Also, in our view many programs do not maximize “in seat” education. They may rely heavily on for-profit commercial sponsorships. Programs may also tilt the balance towards recreation and entertainment. (Attachment A, pg. 14)

The *Clapman* report accurately summarizes the reputational and operational risks that Internal Audit has identified by relying so heavily on these types of conferences for education.

Furthermore, the current Policy does not establish an educational strategy that encourages continuously improving the skills a fiduciary should possess. A significant piece of the *Clapman* report’s proposed policy includes a “Trustee Knowledge Self-Assessment” which is used to assess and then develop an educational plan. Incorporating this best practice would address both an operational risk by ensuring all Board members receive an adequate amount of education in the areas needed, and a reputational risk by ensuring education expenditures can be supported.

Recommendation

10. To improve the effectiveness and adequacy of the Policy, Boards and management should:
 - a. Review the *Clapman* report’s education policy for a template of best practices.
 - b. Consider adopting an organizational-wide educational strategy and incorporating the “Trustee (Fiduciary) Knowledge Self-Assessment.” Texas Teacher Retirement System and CalSTRS have both hired a consultant to assess the organizations’

requirements and preferences and to provide guidance in developing an effective educational strategy.

- c. Consider working with LACERA's Training Coordinator to develop a process to create a stakeholder's educational plan, monitor the broader educational needs of the Board for in-house training opportunities, and review and evaluate educational conferences.

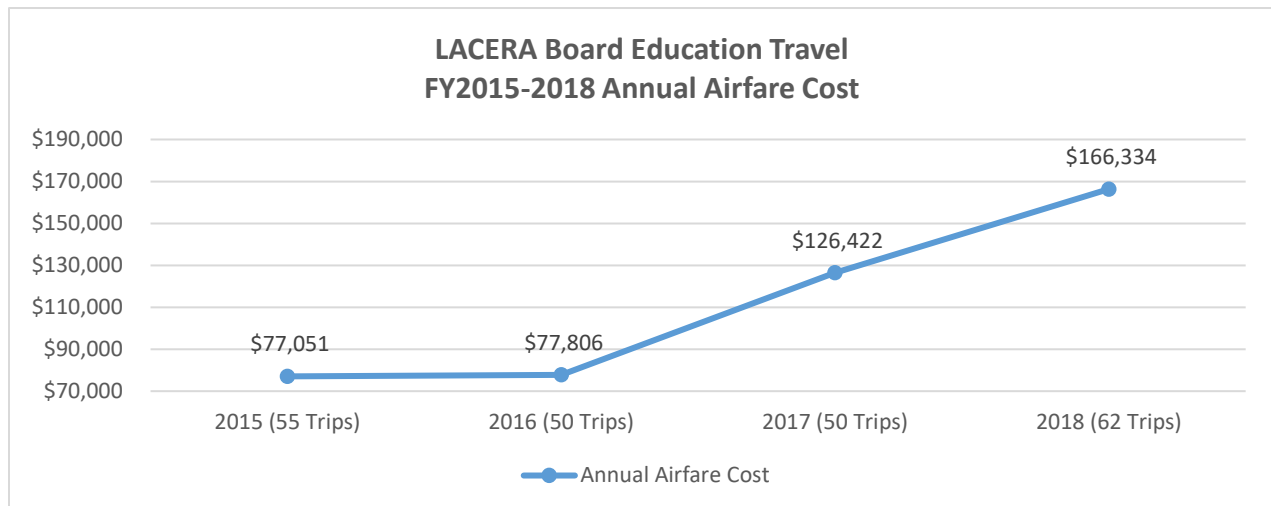
Management Response

Management concurs with this recommendation. Management will bring the issue to the JOGC for further discussion. This recommendation is expected to be completed by January 31, 2020.

Issue: Board Airfare Has Increased Substantially

Internal Audit analyzed the costs of registration, airfare, and lodging, for the last four fiscal years to gain a better understanding of the increase in Board education travel expenditures. Based on the analysis, the cost of airfare has sharply increased (see chart below). We believe LACERA's airfare costs could be reasonably reduced by:

- Amending the Policy to reduce the frequency of business class travel, and
- Amending the Policy to revise how airline tickets are procured.



Business Class Airfare

As the chart above indicates, Board airfare has increased substantially in part due to the Policy revisions in March 2017 to allow business class travel when travel time exceeds five hours.

We noted the cost of the specific airline tickets below to show the cost of business class versus economy class for air travel that is generally six hours or less:

- A Board member's airfare for a domestic flight in December 2017 was approximately \$5,400. When Internal Audit priced this for a trip 14 days in advance, the most expensive direct, non-refundable, economy ticket on a major carrier was almost \$600 (Google Flights), which is 800% less than what LACERA paid.

- A Board member's airfare for a domestic flight in March 2018 was almost \$3,000. When Internal Audit priced this for a trip 14 days in advance, the most expensive direct, non-refundable, economy ticket on a major carrier was \$240 (Google Flights), which is 1150% less than what LACERA paid.
- A Board member's airfare for a domestic flight in June 2018 was approximately \$2,400. When Internal Audit priced this for a trip 14 days in advance, the most expensive direct, non-refundable, economy ticket on a major carrier was \$550. (Google Flights), which is 336% less than what LACERA paid.

Procurement of Airline Tickets

We observed from our testing that refundable tickets were purchased for some travel events. Since the current Policy does not address if or when purchasing refundable tickets is allowed, the purchases were not out of compliance with the Policy. However, since refundable tickets are often two to three times the cost of non-refundable tickets, it seems inconsistent with the Policy's general commentary on Attachment A of the Policy, "Travelers are encouraged to schedule travel in a way that minimizes LACERA's travel expenses." Staff reported that cancelations of trips are rare and that the cost of non-refundable tickets, less a nominal change fee, can be applied to future travel by the Board member.

Additionally, we noted that prudent procurement practices, such as comparing prices among at least three airlines flying to the destination, modifying dates and times of travel, and prohibiting Board members from limiting their travel to one specific airline, are not encouraged or enforced. Due to some airlines not offering business class, this sometimes results in Board members flying first class (as permitted by the policy if business class is not available) on their preferred airline and LACERA incurring costs up to \$12,500 for airfare. We did not obtain information on specific airfare procurement practices at CALPERS or CALSTRS but did not identify any airfares above \$3,000 for international business class travel.

Recommendation

11. To reduce LACERA's total airfare costs, Boards and management should:
 - a. Re-evaluate the use of business class airfare.
 - b. Evaluate stronger enforcement of prudent procurement practices as described above, including prohibiting the purchase of refundable tickets.

Management Response

Management concurs with this recommendation. Management will bring the issue to the JOGC for further discussion. This recommendation is expected to be completed by January 31, 2020.

Other Best Practices Noted

We identified the following additional best practices in our review of peer public pension funds board travel practices for the Board and management to consider in future revisions to the Policy:

1. Transparency – Best practices included having the Education and Travel Policy on the Fund’s public-facing website, inclusion of full estimated costs for travel in board memos requesting the board approval for travel, and providing a summary by traveler with all associated costs of all travel.
2. Centralized airline ticketing and cost management practices including the requirement that award miles earned are first used to upgrade tickets when the traveler is eligible for an upgrade to business class before the Fund incurs additional cost to upgrade the traveler.
3. Emphasis on in-house and local education first, with travel permitted when specific education is not locally available.
4. Separate the education policy from the travel procurement and reimbursement policy with all travelers required to comply with a centralized organizational policy for the procurement of travel and reimbursement of expenses. This establishes a more appropriate system of checks and balances.

We thank FASD, the Legal Office, and the Executive Office management and staff for their cooperation with our audit.

REVIEWED AND APPROVED



Richard Bendall
Chief Audit Executive

Date: June 20, 2019

REPORT DISTRIBUTION

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LACERA INTERNAL AUDIT DIVISION

**Board and Staff
Education & Travel Audit**

Version with Audit Committee Comments & Internal Audit Responses

June 20, 2019

AUDIT PERFORMED BY:
Christina Logan, CPA, CFE
Senior Internal Auditor

EXECUTIVE SUMMARY

LACERA incurs education and travel expenditures to ensure Board members and staff are properly educated in monitoring the administration and investments of the Trust, and advocating positions that protect and further the interests of the Trust. LACERA has an Education and Travel Policy (Policy), which the Boards last updated in March 2017, to facilitate Boards and staff in balancing their fiduciary responsibilities to be knowledgeable advocates and to be fiscally prudent with the Trust's funds.

We completed this audit as part of the Fiscal Year (FY) 2019 (July 2018 – June 2019) Audit Plan. Internal Audit periodically performs a compliance audit of the Policy to address the operational risks associated with travel. We last audited Board and staff education and travel expenditures in FY 2016.

In determining the scope of the audit, we considered the following:

- The Boards' education travel expenditures had increased, while staff's education travel expenditures had decreased, over the last three fiscal years.

Fiscal Year	Board education travel expenditures	Change over base year (FY 2016)	Staff education travel expenditures	Change over base year (FY 2016)
2016	\$269,861	-	\$497,918	-
2017	\$303,320	11% increase	\$433,349	13% decrease
2018	\$403,267	49% increase	\$381,671	23% decrease

- The Boards' budget for all travel and education was \$411,000 in FY 2018. The budget rose to \$529,000 for FY 2019 and to \$569,000 for FY 2020 (a 38% increase over 2 years).
- Peer public pension fund board education travel was more limited in frequency and costs than LACERA's Board education travel.
- A public data request for the Board of Investments' travel was made in August 2018.

To address the above risks and to assess if internal controls related to Board and staff education and travel expenditures are effective in mitigating the associated risks of fraud, operational, compliance, and reputational risk, we included the following objectives in our audit:

Section 1: Compliance with the Policy

Section 2: Review of the effectiveness and adequacy of the Policy

We observed that Board and staff were generally compliant with the Policy although we identified areas that could be improved through better communication by key stakeholders, more complete travel files, and updates and/or revisions to the Policy. However, we also identified that the Policy allowed for a broad array of practices that are not effective in controlling costs. Some examples include but are not limited to the following:

- Individual Board members incurred annual travel costs ranging from less than \$1,000 to more than \$55,000
- Individual Board members purchased airfare as high as \$12,500 for a single international trip
- Individual Board members attending anywhere from one to 16 educational events (local and non-local) per year

Our survey of peer public pension plans both within California and throughout the United States supported our concern that LACERA is a significant outlier in costs incurred for Board educational (non-administrative) travel. Most notably, LACERA incurred significantly higher costs for Board educational travel in FY 2018 than either CALPERS, a \$350 Billion fund as of June 2018, or CALSTRS, a \$226.1 Billion fund as of May 2019. We found that these two funds were the most supportive of Board education and travel, including some international travel, among the funds in the peer group. Based on the data provided to us, we did not identify any peer funds in the survey that exceeded either CALPERS or CALSTRS in expenditures for board educational travel.

Overall, we found opportunities for LACERA Boards and management to achieve a Policy with more effective measures of education and training while minimizing costs. We observed that the Policy could be more effective and better aligned with published best practices and peer pension funds by focusing on an organization-wide educational strategy.

See the following table on the next page for a summary of the issues and recommendations identified during the audit.

Summary of Issues and Recommendations

Page(s)	Issues	Recommendations
Section 1: Compliance with the Policy		
A. Assessment of travelers and FASD's review process		
10 – 13	Compliance Exceptions	<ol style="list-style-type: none"> 1. FASD management should assess the need to obtain missing documentation and/or recover amounts from travelers for noncompliant transactions that were identified during the audit. 2. FASD management should ensure that its staff consistently enforces the Policy and escalates to FASD management any areas of the Policy requiring interpretation or clarification. 3. Management should periodically provide training to the Boards and staff on the Policy to ensure travelers and approvers are aware and compliant with the Policy requirements. 4. To improve the effectiveness and efficiency and to consistently enforce the review process, FASD, the Legal Office, and the Executive Office should meet periodically to determine a joint understanding of the Policy, how to address and document when questionable charges occur, and if updates or revisions should be suggested to the Boards. 5. To be consistent with the section "Authorized Expenses" (705.02) of the Policy, that expenses should be "reasonable and necessary," Boards and management should: <ol style="list-style-type: none"> a. Revise the Policy to reflect current economical transportation services, like public transportation, taxis, or ride-share services. The Policy should still require the traveler to provide written justification if an upgraded ground transportation service is used. b. Update the Policy to address if and when the use of an executive car service is acceptable.
14	FASD does not have complete files for each travel event	<ol style="list-style-type: none"> 6. To improve the effectiveness and efficiency of FASD's review process, FASD should: <ol style="list-style-type: none"> a. Provide instructions for the Travel Expense Voucher (payment request), so travelers can provide a complete travel file. b. Work with the Systems Division and the Executive Office to explore solutions that would allow travelers to upload and allocate travel receipts, and that would allow FASD to review and store complete travel files in a central location.
B. Completeness and accuracy of Monthly and Quarterly Travel Reports		
15	Accuracy of Quarterly Travel Reports	<ol style="list-style-type: none"> 7. To improve the accuracy of the Quarterly Travel Reports, FASD should: <ol style="list-style-type: none"> a. Ensure all members of FASD's Disbursements Unit are adequately trained and supervised. b. Instruct travelers on providing a complete travel file, and work with the Systems Division and the Executive Office to explore having traveler's upload and allocate travel receipts to a central location
16 – 17	Administrative travel is not clearly addressed in the current Policy	<ol style="list-style-type: none"> 8. To strengthen the Policy, the Boards and management should revise the Policy to better clarify "Administrative Travel," to define controls regarding when administrative travel is authorized, if there is a limit to administrative travel, and how administrative travel should be categorized for Board members.
17 – 18	"Local Educational Conferences" per the Policy are difficult to categorize	<ol style="list-style-type: none"> 9. To ensure conferences are consistently and accurately categorized, conference limitations are applied, and to assist Board members in planning their educational conferences, Boards and management should revise the Policy to provide a standardized definition of "local educational conferences" - for example, limiting local education to Los Angeles County, Southern California, or a set distance from LACERA.

Summary Continued

Summary of Issues and Recommendations (continued)

Page(s)	Issues	Recommendations
Section 2: Review of the Effectiveness and Adequacy of the Policy		
21 -23	The Policy does not have an organizational-wide educational strategy	10. To improve the effectiveness and adequacy of the Policy, Boards and management should: a. Review the Clapman report's educational policy for a template of best practices. b. Consider adopting an organizational-wide educational strategy and incorporating the "Trustee (Fiduciary) Knowledge Self-Assessment." c. Consider working with LACERA's Training Coordinator to develop a process to create a stakeholder's educational plan, monitor the broader educational needs of the Board for in-house training opportunities, and review and evaluate educational conferences.
23 – 24	Board airfare has increased substantially	11. To reduce LACERA's total airfare costs and the high exposure to headline risk, Boards and management should: a. Re-evaluate the use of business class airfare. b. Evaluate stronger enforcement of prudent procurement practices, including prohibiting the purchase of refundable tickets.

See Results Section of the report for Management's Responses.

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INTRODUCTION

The Board of Retirement, Board of Investments, and designated staff have a fiduciary duty to obtain education about public pension administration and investments, to monitor the administration and investments of the Trust, and to advocate positions that protect and further the interests of the Trust. LACERA has an Education and Travel Policy (Policy), which was last updated in March 2017, to facilitate the Boards and staff in executing this fiduciary duty and to ensure LACERA's funds are used in a manner consistent with LACERA's overall mission. Authorized education and travel expenses include, but are not limited to, expenses related to the attendance at industry conferences and various educational and training seminars, legislative meetings, and on-site due diligence visits for existing and potential service providers.

We completed this audit as part of the Fiscal Year (FY) 2019 (July 2018 – June 2019) Audit Plan. Internal Audit periodically performs a compliance audit of the Policy to address the operational risks associated with travel. We last audited Board and staff education and travel expenditures in FY 2016. For this audit, we reviewed FY 2018 (July 2017-June 2018) education and travel expenditures:

Category of Travel Events	Boards	Staff
Education	\$403,267	\$381,671
Administrative	<u>\$23,153</u>	<u>\$227,409</u>
Total	\$426,420	\$609,080

BACKGROUND

Pre-Travel Authorization

Board members are pre-approved to attend conferences listed on Attachment C of the Policy, and local conferences that have a registration fee less than \$500 and no common carrier travel or lodging. However, Board members must seek Board approval to attend conferences not included on Attachment C or any international conferences. Staff members must obtain approval from the Chief Executive Officer (CEO) for education and travel. Once travel has been authorized, Financial & Accounting Services Division (FASD) will create an event number in the Travel Manager program to record the event name, official travel dates, location, and travelers. FASD then assigns staff the event number so all related expenditures can be allocated correctly.

Travel Arrangements

Board and staff are encouraged to make travel arrangements as far in advance as possible to take advantage of early bird registrations, conference room rates, and lower fares. Executive Board Assistants (Assistants) and Division Managers generally use their LACERA corporate credit card to pay for conference registration, lodging, and airfare. FASD requires corporate cardholders to provide receipts and allocate these expenditures to the correct event number. Managers review and approve the purchases on a monthly basis. FASD then reconciles the monthly corporate credit card statements against the receipts and researches any discrepancies or missing documentation.

Reimbursements

Generally, travelers request reimbursement for expenses incurred while traveling such as meals, mileage, parking, and airline baggage fees. Individuals are required to submit a Reimbursement Expense Voucher (Expense Voucher) within 90 days of completing the travel, or 30 days after the fiscal year-end, whichever occurs first. For Board members, the Assistants will review the Expense Vouchers for general compliance and then the CEO will approve them. For staff, division managers review and approve the Expense Vouchers. Approved Expense Vouchers are then routed to FASD for an additional review, approval, and processing.

FASD's Review

FASD is responsible for reviewing the Expense Vouchers and monthly corporate card receipts to ensure the expenditures are consistent with the Policy. FASD reviews the receipts provided to ensure date, times, and amounts are consistent with the corresponding conference and travel agendas. FASD also recalculates the mileage amount, ensures the per diem is calculated based on the correct General Services Administration rate and Meal & Incidental Breakdown, and allocates expenses that are shared between travelers (e.g., a shared meal or a shared taxi ride) to the appropriate divisions. If FASD has questions or needs additional documentation, they email either the Assistants or staff.

Travel Reports

On a monthly basis, FASD prepares the Monthly Education and Travel Expenditures Report (Travel Report), which details the completed, anticipated, and canceled education and travel for Board and staff for the fiscal year. This report does not reflect costs. On a quarterly basis, FASD prepares the Quarterly Travel Report, which details the education and travel expenditures paid / reimbursed by LACERA for Board and staff. These reports are distributed monthly and quarterly to Board and staff.

Since the Policy limits Board members to 8 (or 12 if on both Boards) conferences but does not limit the number of local educational conferences per fiscal year (Section 705.07), FASD categorizes the Travel Reports for Board travel as:

- "A" - Pre-approved conferences listed on Attachment C of the LACERA Education and Travel Policy and/or Board approved conferences.
- "B" - Administrative conferences and/or local educational conferences that do not require common carrier travel and lodging totaling less than \$1,500.
- "X" - Canceled events for which expenses have been incurred.

AUDIT OBJECTIVES & METHODOLOGY

The audit objectives were to assess if internal controls related to Board and staff education and travel expenditures are effective in mitigating the associated risks of fraud, operational, compliance, and reputational risk. Specifically, we reviewed the following:

SECTION 1: Compliance with the Education and Travel Policy

- A. Assessment of travelers and FASD's review process
 - Reviewed LACERA's Education and Travel Policy dated March 2017.
 - Sampled Board's and staff's travel to verify the expenditures were compliant with the Policy, accurate, and valid, and reviewed the travel events for fraudulent activity.
 - Sampled payment requests to ensure FASD thoroughly reviewed requests, questioned charges that appeared inconsistent, rejected out of compliance charges, and processed payment requests timely.
- B. Completeness and accuracy of Travel Reports
 - Reviewed the Travel Reports to determine if educational conferences were correctly categorized as local educational conferences, and to ensure the 8/12 conference limitation was applied consistently and accurately to all Board members.
 - Reviewed canceled trips to ensure they were documented in the Travel Reports, individuals who canceled provided valid reasons in a timely manner, and if fees were incurred, they were either pardoned by the Board chair or repaid to the fund.

SECTION 2: Review of the Effectiveness and Adequacy of the Education and Travel Policy

- Reviewed best practice guidance.
- Reviewed peer public pension funds' education and travel policies and travel reports (if available).
- Reviewed current news articles about governmental agencies' travel.
- Discussed Policy, procedures, process, and controls with FASD, the Legal Office, and the Executive Office.

AC QUESTION: Such as?

IA RESPONSE: The Clapman Report – See reference on page 21

AUDIT SCOPE

The audit scope for compliance testing included Board and staff education and travel expenditures for FY 2018. We tested approximately 10% of Board education and administrative travel, 20 events totaling \$122,435. We tested approximately 10% of staff education and administrative travel, 34 events totaling \$84,863.

The audit scope for the review of the effectiveness and adequacy of the Policy was limited to Board education travel. We limited the scope to Board education travel, after considering the following:

AC QUESTION: The second sentence in the preceding paragraph stated you tested “Board education and administrative travel”

IA RESPONSE: Yes, the first paragraph referred to the compliance section of the audit which did include administrative travel.

- The Boards’ education travel expenditures had increased, while staff’s education travel expenditures had decreased, over the last three fiscal years.

Fiscal Year	Board education travel expenditures	Change over base year (FY 2016)	Staff education travel expenditures	Change over base year (FY 2016)
2016	\$269,861	-	\$497,918	-
2017	\$303,320	11% increase	\$433,349	13% decrease
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- The Boards’ budget for all travel and education was \$411,000 in FY 2018. The budget rose to \$529,000 for FY 2019 and to \$569,000 for FY 2020 (a 38% increase over 2 years).
- Peer public pension fund board education travel was more limited in frequency and costs than LACERA’s Board education travel.
- A public data request for the Board of Investments’ travel was made in August 2018.

RESULTS

We have categorized the results of our audit into two separate and distinct sections. The first section, “**Compliance with the Education and Travel Policy,**” discusses our findings from the test work performed and includes recommendations to strengthen either the Policy or the processes. The second section, “**Review of the effectiveness and adequacy of the Education and Travel Policy,**” presents our findings from researching best practice guidance, peer comparisons, and recent media headlines and includes recommendations to better align with industry practices.

SECTION 1: **COMPLIANCE WITH THE POLICY**

A. ASSESSMENT OF TRAVELERS AND FASD'S REVIEW PROCESS

We tested the selected sample travel events against the Policy and related procedures. See the chart below for a summary of our testing. We concluded travelers were generally compliant with Policy and related procedures, and FASD generally performs a thorough, detailed review of payment requests and credit charges. We did not find any instances of fraud in our testing but did find areas where the Policy and/or related payment processes could be strengthened.

Attribute Tested	Compliance Assessment Good = No exceptions Fair = 1-10% exceptions Weak = more than 10% exceptions
Educational conference or administrative travel was pre-approved	Fair
Educational conference met 5-hour education requirement	Good
Airfare and ancillary costs were consistent with the Policy	Good
Airfare purchased / reimbursed by LACERA was the airfare the travel used	Good
Lodging was consistent with the conference hotel rate and/or 3 times approved government rate for that city for non-conference travel, for a standard room, and consistent with the travel itinerary	Fair
Meal charges were consistent with conference and travel itinerary	Fair
Ground transportation was consistent with the conference and travel itinerary	Weak
Incidentals and miscellaneous charges were reasonable	Good
Mileage charges were accurate and consistent with travel itinerary	Good
Parking charges were consistent with conference and travel itinerary	Good
Reimbursement request was submitted timely	Good
Thorough review – receipts support charge, per diem rates and Meal & Incidental breakdown verified, calculations checked for accuracy, questionable charges resolved.	Fair
Canceled travel included a written valid reason provided by the traveler, and any associated costs over \$50 were pardoned by Board chair	Good

Issue: Compliance Exceptions

- I. A traveler attended an educational conference with only verbal approval from the CEO. When the traveler submitted a payment request for the trip, FASD staff notified the traveler the event had not been created in the Travel Manager because no written approval had been submitted. Subsequently, the CEO provided written approval for the trip. Although the Education and Travel Policy stipulates, "The CEO, or designee, shall approve staff education and travel," the expectation is for staff to receive written approval prior to making travel arrangements, from the CEO. The traveler explained the CEO had provided verbal approval,

but the traveler did not obtain written approval prior to making or taking the trip. The traveler said it was an oversight and the traveler has not made the mistake again.

AC QUESTION: It would be helpful if you delineated your findings between Board and staff travel. This exception is staff travel?

IA RESPONSE: Yes, this exception was a staff traveler

- II. A traveler attended an educational conference and stayed for additional personal days. The traveler's additional personal days of lodging were charged to the corporate credit card. Although the Policy does not specifically address personal expenditures, LACERA's Corporate Credit Card Policy (Section 4.2) dated April 2016, which was in effect during this time period, does address personal expenditures. It stated, "In order to promote the public's confidence in the integrity of the Corporate Card Program and avoid any appearance of commingling of business-related expenditures with personal expenditures, use of the Corporate Card for personal purchases is strictly prohibited at any time." When the traveler returned, the traveler immediately reimbursed LACERA for the personal portion of the lodging. The traveler explained the hotel had mistakenly charged all the lodging days to LACERA's card, instead of only charging the conference days. The traveler stated that for upcoming trips the traveler would clarify which cards to use when checking-in to the hotel. Although LACERA was able to recoup the personal portion of hoteling timely, this practice does not comply with the Corporate Credit Card Policy and FASD does not have the resources to track payments owed to LACERA by individual travelers. FASD addressed this issue by providing Corporate Credit Card training to all staff in March 2019.

AC QUESTION: I don't disagree. But FASD should have the resources to review payment requests prior to issuing payment. This is another reason to cancel the Corporate Credit Card in the agency.

IA RESPONSE: Noted

- III. A traveler attended an educational conference and booked an upgraded room. The Policy (Attachment A: Lodging – A. Room Cost) limits room rates to "a standard class single room rate. We noted a price difference of approximately \$50/night between the two rooms when we priced the hotel for the same month but the following year. The traveler did not provide a written justification for the upgrade and staff did not identify or question the upgrade.

AC QUESTION: How would staff know? Did the invoice say "UPGRADED ROOM"?

IA RESPONSE: No, the invoice would not but the traveler should disclose and pay the difference or provide justification for the upgrade, such as document that the standard rooms were booked and the traveler booked the next available room.

- IV. When a traveler attended an educational conference, he/she reserved a room, which included breakfast not provided with standard room. Although the hotel rate included breakfast, the traveler requested the breakfast per diem for all the travel days. The Policy (Attachment A: Meals) specifically states, "LACERA will not reimburse the traveler for a meal which has been pre-paid by LACERA whether or not the traveler consumed the meal" unless

written justification is provided to document if the traveler had either special dietary restriction or had to conduct LACERA business during the meal. The traveler did not provide a written justification for the breakfast per diem. Staff did not question the request justification for the breakfast per diem since the hotel receipt was not included with the payment request documentation but was instead included with the credit card documentation.

- V. A traveler requested authorization to have LACERA pay for a personal item that was lost while attending an approved conference and the Executive Office approved the expenditure. We noted the Policy does not address payment for personal items lost while traveling for LACERA business but the Executive Office approved the payment, without seeking guidance from either the Legal Office or FASD.

AC QUESTION: \$ value? Did the traveler file a police report?

IA RESPONSE: \$413.00. Since the item was lost, the traveler did not file a police report

- VI. The current Policy states in section 705.11, "Individuals are expected to use group shuttle service to and from metropolitan destinations...Reimbursement of an alternative mode of transportation will be limited to the cost of the group shuttle service unless otherwise justified." However, our audit disclosed that travelers do not use group shuttle services for ground transportation nor do travelers provide a business justification when using an alternative method. Travelers generally use taxis or ride sharing service for ground transportation needs. Internal Audit noted FASD does not question the use of alternative methods of transportation nor does FASD limit reimbursement to the cost of the group shuttle service as stated in the Policy. Per discussion with staff, FASD did not enforce the Ground Transportation section of the Policy because using alternative transportation methods, instead of group transportation, had become the common and accepted practice. However, this change in practice should have been discussed with the Executive Office and Legal Office, and the Policy should have been revised.

Additionally, we observed some Board members used an executive car service for ground transportation needs. We noted several times the executive car service was used domestically, including for transportation to and from the local airport. The travelers did not provide a business justification for using the executive car service and FASD did not question the charges.

Recommendations:

1. FASD management should assess the need to obtain missing documentation and/or recover amounts from travelers for noncompliant transactions that were identified during the audit.

Management Response

Management concurs with the recommendation. FASD management will have staff review the audit exceptions, and follow-up with travelers to obtain missing documentation and/or recover any amounts owed, as applicable, due to non-

compliant transactions. This recommendation is expected to be completed by January 31, 2020.

2. FASD management should ensure that its staff consistently enforces the Policy and escalates to FASD management any areas of the Policy requiring interpretation or clarification.

Management Response

Management concurs with the recommendation. FASD will evaluate a monitoring mechanism to ensure consistent Policy enforcement. In addition, Management re-emphasized to staff the importance of elevating exceptions to the Policy for guidance and resolution. This recommendation is partially implemented and is expected to be completed upon the approval of the revised Policy.

3. Management should periodically provide training to the Boards and staff on the Policy to ensure travelers and approvers are aware and compliant with the Policy requirements.

Management Response

Management concurs with the recommendation. FASD will work with the Executive and Legal Offices to schedule Travel Policy training for the Boards and staff at least annually or when the Policy is revised. This recommendation is expected to be completed by June 30, 2020.

AC QUESTION: As it is now, so much of the expenditures are handled by the Board secretaries and trustees see or sign off on none of it. It is hard to hold trustees accountable under that framework. Perhaps the route to to is to charge trustees with the completion of travel expense reports and then hold them accountable to the reports they submit.

IA RESPONSE: Agree with the suggestion.

4. To improve the effectiveness and efficiency and to consistently enforce the review process, FASD, the Legal Office, and the Executive Office should meet periodically to determine a joint understanding of the Policy, how to address and document when questionable charges occur, and if updates or revisions should be suggested to the Boards.

AC QUESTION: That's a waste of resources. Clarify as necessary, charge trustees with completion of an expense report, require Board secretary review and sign off.

IA RESPONSE: It is a board policy and updates to the policy for purposes of clarification need to be brought to the boards for adoption and approval.

Management Response

Management concurs with the recommendation. FASD management will schedule joint meetings with FASD, the Executive and Legal Offices when there are Policy updates. In addition, this core group will convene at least bi-annually to review the Policy and related issues of non-compliance to determine if such issues warrant Board

consideration for Policy revision. This recommendation is expected to be completed upon the approval of the revised Policy.

5. To be consistent with the section “Authorized Expenses” (705.02) of the Policy, that expenses should be “reasonable and necessary,” Boards and management should:
 - a. Revise the Policy to reflect current economical transportation services, like public transportation, taxis, or ride-share services. The Policy should still require the traveler to provide written justification for using an upgraded ground transportation service if used.

AC QUESTION: It depends. If I arrive in Tokyo at 2:30 in the morning, I am not walking around the airport in search of a shuttle service, calling one, and then waiting in line to book a shuttle service to take me to my hotel. I am going to hop in a taxi. If that taxi charge is more than LACERA will reimburse, publish that clearly so I know the increment I will need to pay.

IA RESPONSE: That would be an appropriate justification for taking a taxi and should be documented in the expense claim by the traveler under the current Policy.

- b. Update the Policy to address if and when the use of an executive car service is acceptable.

Management Response

Management concurs with this recommendation. Management will bring the issue to the JOGC for further discussion. This recommendation is expected to be completed by January 31, 2020.

Issue: FASD Does Not Have Complete Files for Each Travel Event

During our test work, we noted FASD does not have a complete physical or electronic file for each travel event but instead maintains several platforms of information; a binder with all approved conferences and related agendas, a corporate credit card database, and Great Plains, a financial and accounting software system. Not having a complete file for each travel event decreases the effectiveness of the review process, an operational risk. For example, when a traveler submits a payment request it is generally shortly after returning from the trip. If the payment request includes a per diem for breakfast, even though the traveler’s lodging included breakfast, FASD at that time would not have the receipt for lodging. The receipt for lodging would be submitted several weeks later if the lodging was paid using LACERA’s corporate credit card. In this scenario, FASD is reviewing the payment request but they do not have a complete understanding of all the expenditures related to the travel event.

Additionally, not having a complete travel file makes it more difficult for FASD to provide accurate numbers on the Travel Reports.

Recommendation

6. To improve the effectiveness and efficiency of FASD’s review process, FASD should:
 - a. Provide instructions for the Travel Expense Voucher (payment request), so travelers can provide a complete travel file.

AC QUESTION: I have never seen this, but if you develop a comprehensive and well referenced expense report, the great majority of your problems will disappear.

IA RESPONSE: Agree

Management Response

Management concurs with the recommendation. FASD will update the Travel Expense Voucher to include clear written instructions for completing the document. This recommendation is expected to be completed by June 30, 2020.

AC QUESTION: If the risks are as you stated, a year is far too much time.

IA RESPONSE: Agree, we will work with management to ensure this is addressed as soon as possible.

- b. Work with the Systems Division and the Executive Office to explore solutions that would allow travelers to upload and allocate travel receipts, and that would allow FASD to review and store complete travel files in a central location.

Management Response

Management concurs with the recommendation. FASD held preliminary discussions with the Systems Division and the Executive Office to evaluate the feasibility of implementing a travel receipt capture and storage tool. This recommendation is partially implemented and expected to be completed by June 30, 2020.

B. COMPLETENESS AND ACCURACY OF TRAVEL REPORTS

Per our review of FY 2018 Travel Reports, Internal Audit found several areas that could be strengthened to improve the completeness and/or accuracy of the reports.

Issue: Accuracy of Quarterly Travel Reports

We noted several instances where the Quarterly Travel Report did not accurately reflect the travel expenditures for a traveler's trip. Examples of the errors were:

- Registration Fees included registration for the correct event and a future event.
- No airfare recorded since a credit from a previously canceled flight was used.
- Lodging included hotel and associated parking fees.

In addition to the inaccuracies that Internal Audit identified, we learned from discussions with FASD, the Executive Board Assistants, and the Legal Office that the FY 2018 Quarterly Travel Reports were significantly revised for inaccurate reporting of travel expenditures before a public data request was fulfilled. Based on discussions with FASD, many of the inaccuracies in the Reports were caused by having a key member of FASD's Disbursements Unit out of the office for the majority of the year, and not having a complete travel file, as discussed in the prior section.

AC QUESTION: I don't know what this means. Are you stating that after receipt of a public data request, staff determined the information in the reports was inaccurate? If so, did staff then dedicate the resources necessary to compile information that was correct?

IA RESPONSE: That is correct. Yes, staff dedicated the resources to correct the reports.

Inaccuracies in management reports in an indication that staff do not reconcile the reports to the books and records. Is that true?

IA RESPONSE: Yes, and this is also a consequence of not having a single complete travel file.

Where is the recommendation that FASD develop and implement a staff coverage plan for circumstances like this?

IA RESPONSE: Noted

Recommendation

7. To improve the accuracy of the Quarterly Travel Reports, FASD should:
- Ensure all members of FASD's Disbursements Unit are adequately trained and supervised.

Management Response

Management concurs with the recommendation. FASD management instructed supervisors and staff to review and consistently refer to the current Policy. When changes to the Policy occur, the supervisor will ensure staff are aware of those changes and are adequately trained on such changes. This recommendation is expected to be completed by January 31, 2020.

- Instruct travelers on providing a complete travel file, and work with the Systems Division and the Executive Office to explore having traveler's upload and allocate travel receipts to a central location.

Management Response

Management agrees with the recommendation. FASD will provide instructions for complete travel files to travelers. In addition, FASD held preliminary discussions with the Systems Division and the Executive Office to evaluate the feasibility of implementing a travel receipt capture and storage tool. This recommendation is expected to be completed by June 30, 2020.

Issue: Administrative Travel Is Not Clearly Addressed In the Current Policy

During FY 2018, LACERA spent approximately \$23,000 on administrative, non-educational travel for Board members. Board members traveled for administrative purposes to meet with Congress and to execute duties as a SACRS board member. During FY 2018, LACERA spent approximately \$243,000 on administrative travel for staff. The Investment Office's travel for due diligence reviews made up most of staff's administrative travel.

On the Travel Reports, staff categorized Board travel as either:

- "A - Pre-approved conferences or conferences not listed in Attachment C of the LACERA Education and Travel Policy" or
- "B - Administrative conferences and/or local educational conferences that do not require common carrier travel and lodging totaling less than \$1,500"

For FY 2018, the Executive Office and FASD categorized the following administrative travel as “B - Administrative conferences and/or local education conferences”:

Travel Date	Conference and Location	Board Members and Total Cost	Approval
Five travel events during FY 2018	SACRS Board Meetings, Sacramento, CA	1 Board member with a total cost of approximately \$5,000	No approval – Staff carried forward the interpretation that attending SACRS Board meetings qualified as administrative travel. In March 2019, the Board of Retirement authorized the travel from July 2014 through 2019 as administrative thus not counting towards the annual conference limits.
May 2018	IFEBP Legislative Update & Federal Engagement - Washington D.C.	3 Board members attended with a total aggregate cost of approximately \$14,000	April 2, 2018 Memo – The Board of Retirement approved the reimbursement of travel costs but does not address how to categorize the travel.

AC QUESTION: We need a shift in this organization to a focus on “legal authority.” The idea that an “interpretation” is legal authority to spend in just plain silly.

IA RESPONSE: Noted

As the current Policy does not clearly address the definition of administrative travel, how administrative meetings should be categorized, or if administrative travel should count towards a Board member’s annual conference limit, staff excluded administrative travel from the annual conference limits. Staff consistently applied this interpretation to all Board members and all Travel Reports have reflected this interpretation since July 2014. However, during our audit, we noted stakeholders were unclear if staff’s interpretation of the Policy was correct. The Policy should be revised to more clearly address “Administrative Travel.”

Recommendation

8. To strengthen the Policy, the Boards and management should revise the Policy to clarify “Administrative Travel” to define controls regarding when administrative travel is authorized, if there is a limit to administrative travel, and how administrative travel should be categorized for Board members.

Management Response

Management concurs with this recommendation. Management will bring the issue to the JOGC for further discussion. This recommendation is expected to be completed by January 31, 2020.

Issue: “Local Educational Conferences” Per the Policy Are Difficult to Categorize

Per the Policy, local educational conferences are conferences where there is no common carrier travel and lodging is under \$1,500, and these conferences should not be counted towards the annual 8/12 conference limit. We observed that it is difficult to categorize which conferences should be considered “local educational conferences”, not subject to the 8/12 limit, as this determination needs to be made for each traveler’s individual travel expenditures.

When we reviewed the 4th Quarter FY 2018 Travel Report, we noted that staff had categorized several trips as “local educational conferences” but these trips included either airfare or lodging was over \$1,500.

AC QUESTION: Simple criteria for which we could control through a well designed expense report.

IA RESPONSE: Noted. We emphasize the recommendation below.

If FASD had applied the current Policy definition of local educational conferences, the following conferences should be re-categorized based on each Board members’ travel:

- **Fall SACRS Conference, November 14-17, 2017** – Three Board members flew to San Francisco so for those travelers, the conference should have counted towards the 8/12 educational conference limit. One Board member drove to San Francisco so for that traveler, the conference was correctly categorized as a local educational conference, and not counted toward the educational conference limit.
- **IFEBP Public Employees Benefits Institute, June 25-27, 2018** – One Board member flew to Las Vegas so for that traveler, the conference should have counted towards the 8/12 educational conference limit. One Board member drove to Las Vegas so for that traveler, the conference was correctly categorized a local educational conference, and not counted toward the educational conference limit.
- **Milken Conference, April 29 – May 2, 2018** – One Board member’s lodging for the conference in Los Angeles was over \$1,500 so for that traveler, the conference should have counted towards the 8/12 educational limit. Nine other Board members’ lodging for the conference was under \$1,500 so for those travelers, the conference was correctly categorized as a local educational conference, and not counted toward the educational limit.

Recommendation

9. To ensure conferences are consistently and accurately categorized, conference limitations are applied, and to assist Board members in planning their educational conferences, Boards and management should revise the Policy to provide a standardized definition of “local educational conferences” – for example, limiting these to Los Angeles County, Southern California, or a set distance from LACERA.

Management Response

Management concurs with this recommendation. Management will bring the issue to the JOGC for further discussion. This recommendation is expected to be completed by January 31, 2020.

SECTION 2:

REVIEW OF THE EFFECTIVENESS AND ADEQUACY OF THE POLICY

When we evaluated the effectiveness and adequacy of the Education and Travel Policy, Internal Audit recognized Board and staff must balance their fiduciary responsibilities to be knowledgeable advocates and to be fiscally prudent with the Trust's funds. Travel expenditures represent a high-risk area to government entities as travel is scrutinized by the media and there is an expectation that funds are used efficiently, effectively, and transparently. To evaluate our Policy, we reviewed industry best practices, compared other public pension funds' education and travel policies and if available, published travel reports, and recent media articles regarding travel by governmental agencies.

AC QUESTION: Where was this input on the front end?

IA RESPONSE: Most of this is included in the Executive Summary including a statement about reputational risk but you are correct, we did not specifically mention the media or headline risk in the Executive Summary.

Best Practices

Internal Audit found three relevant published reports regarding best governance practices for public pension funds:

- a. Clapman Peter & Waddell, Christopher. **"Clapman Report 2.0 (Clapman): Model Governance Provisions to Support Pension Fund Best Practice Principles."** *Stanford Institutional Investor's Forum Committee on Fund Governance (SIIF)*. May 2013.
<https://law.stanford.edu/event/the-clapman-2-0-report-fulfilling-public-pension-board-fiduciary-duties-through-the-adoption-of-governance-best-practices/>
- b. Regan, Julian. **"Best Governance Practices for Public Retirement Systems."** *National Conference on Public Employee Retirement Systems (NCPERS)*. March 2012.
<https://www.ncpers.org/content.asp?contentid=755>
- c. Waddell, Christopher. **"Enhancing Public Pension Plan Security: Best Practice Policies for Trustees and Pension Systems."** *American Federation of State, Municipal, and County Employees (AFMSCE)*. December 2009. <https://www.afscme.org/news/press-room/press-releases/2009/afscme-releases-best-practices-guide-for-pension-systems>

Each of these reports discussed the need to have an effective board education policy, which encourages fiduciaries to improve continuously upon the skills needed to be an effective fiduciary. The report published by NCPERS does not provide further detail but the reports by SIIF and AFMSCE include a template of their recommended educational policy. Both of these reports focus their policy guidance on 1) developing core competency expectations for board members, 2) evaluating the board members core competencies through a self-assessment, and 3) the organization working with the board and individual members to develop a strategic, effective, and documented organizational and individual education plan for the upcoming year(s).

Peer Comparison

We compared LACERA's Board education and travel to that of other 37 Act Funds within California, CALPERS, CALSTRS and various other State public pension plans including those we believe are leading organizations such as Wisconsin SWIB, Texas TRS, Oregon PERS, State of Washington Investment Board, NYSTRS, Florida State Investment Board and others. Our peer comparison included reviewing the websites of each fund, reviewing the travel policies, interviewing Chief Audit Executives and obtaining data, where available on budget and expense information related to board member education and travel. Peer summary results are below:

	Travel Category	Peer Summary
1	International Travel	Most Funds do not provide for board members to travel internationally. However, those that allow international travel are more restrictive than LACERA. NYSTRS permits international travel for board education in their policy but limits total expenses per board member for travel and education to \$6,000 each per year. CALSTRS and CALPERS do approve international board travel although significantly less than LACERA.
2	Business Class Air Travel	Most funds either do not allow for business class travel or restrict it to flights with a minimum duration of at least 6 to 14 hours. CALPERS for example, only permits business class for international board travel.
3	Conferences Limits	Most funds do not have policy limits on the number of educational conferences board members can attend. Those that did ranged from limits of two to five events per year.
4	Dollar Limits	Most funds do not have dollar limits per board member for education and travel. Funds that did had limits ranging from \$6,000 per board member to \$13,500 per board member annually. For funds that did not have dollar limits per board member, we did not find funds whose total board education costs would have exceeded \$13,500 if averaged among the board members of the fund.
5	Peer range of budget/actual expenditures	Board educational travel expense data for the peer funds for FY 2018 ranged from below \$50,000 to \$137,000 (CALPERS). CALSTRS recently increased its annual budget from \$100,000 to \$120,000 for its board educational travel.

AC QUESTION: Why "significantly less"? Quote the figure.

IA RESPONSE: Noted, we provided data comparing total costs of all three funds on page 23, although not specific to international travel. The International travel comparison between the three funds for FY 2018 is as follows:

LACERA - 14 trips totaling \$160,637 (Avg trip cost - \$11,474)

CALSTRS - 5 trips totaling \$15,100 (Avg trip cost - \$3,020)

CALPERS - 12 trips totaling \$59,940 (Avg trip cost - \$4,995)

AC QUESTION: This isn't materially different than our policy, with the exception I believe that we allow business class for domestic coast to coast travel.

IA RESPONSE: LACERA's Policy provides for business class for trips (not flights) exceeding 5 hours.

AC QUESTION: and we do, which is a good thing?

IA RESPONSE: Due to local educational events, which include trips to as far away as San Francisco or Las Vegas, not counting toward the limits, LACERA travelers often far exceed these limits in practice. Again, most of the peer funds we reviewed did not have any limits in their policies and their board travel expenditures are substantially less than LACERA.

AC QUESTION: This total \$ figure approach is just silly, as the size of the boards can vary. You need to quote these in a per capita figure for comparative purposes.

IA RESPONSE: See per capita results on page 22. LACERA incurred costs of \$26,884 per capita versus \$11,998 for CALSTRS and \$10,528 for CALPERS.

Media Articles

Government entities are held to a high standard in ensuring that public funds are used efficiently and effectively, and the uses of such funds are transparent to the public. Towards this objective, Board-related travel expenses should be reasonable and in line with what a prudent person would incur when conducting official business. Absent controls to ensure prudent spending, Board members are at a greater risk of creating the perception of impropriety (whether perceived or actual); reputation risk, from not only the media, but also our plan sponsors and members. Media coverage regarding travel by pension fund trustees focuses mainly on travel destination, premium class airfare, luxury lodging, entertainment and meals. Article headlines have included:

AC QUESTION: This borders on sensationalism. Did you find any comparison between the circumstances outline in these articles and the travel you reviewed in this audit?

IA RESPONSE: Yes

- a. Broadwater, Luke & Wenger, Yvonne. **"City Pension Officials Spend Nearly \$100,000 on Trips."** *Baltimore Sun*. March 18, 2015 www.baltimoresun.com/maryland/baltimore-city/bs-md-ci-pension-travel-20150318-story.html
- b. Avila, Jale. **"Trustees Spending Fire and Police Pension Funds on Expensive Travel."** *News 4 San Antonio*. May 3, 2018. www.news4sanantonio.com/news/trouble-shooters/news-4-trouble-shooters-uncover-abuse-of-travel-at-fire-and-police-pension-fund
- c. Einhorn, Erin & Lesser, Benjamin. **"Globetrotting Pension Fund Officials Racked up \$400,000 in Costs as Retirees, Taxpayers Foot Bill."** *New York Daily News*. April 10, 2010. www.nydailynews.com/new-york/globetrotting-pension-fund-officials-racked-400-000-costs-retirees-taxpayers-foot-bill-article-1.167070

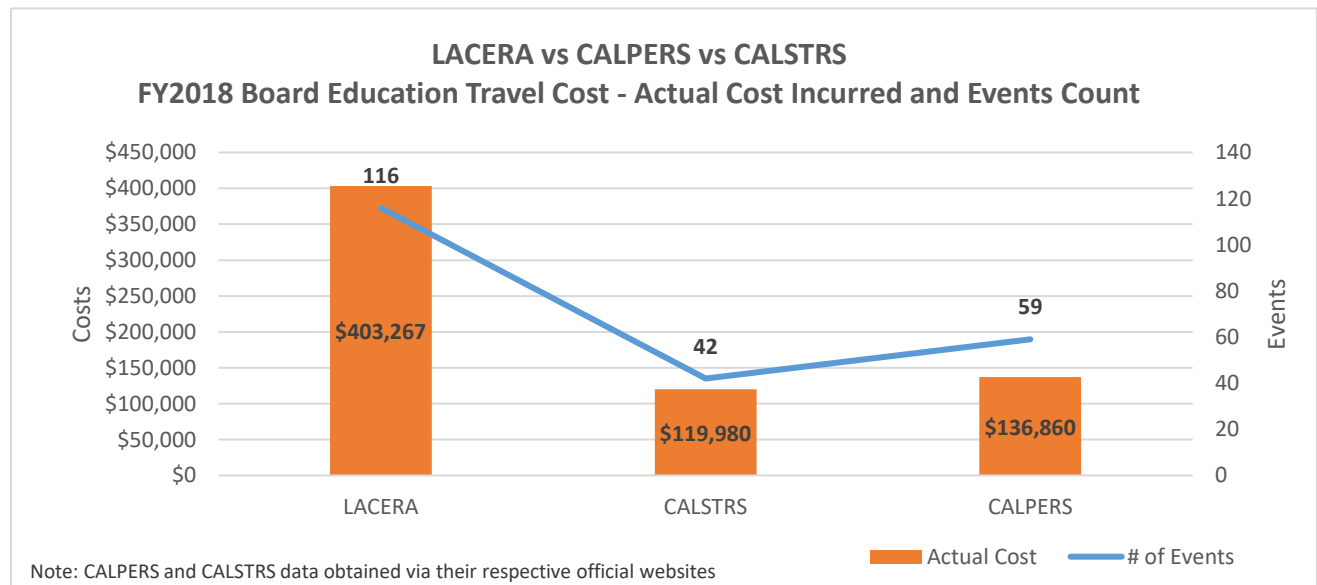
Issue: The Policy Does Not Have an Organizational-Wide Educational Strategy

In our assessment of the current Policy, we noted it does not have an overarching educational strategy that focuses on developing and improving key skills that fiduciaries generally need. Instead, the Policy focuses more on the transactional activities related to education and travel, like conference limits, lodging, and meals. The focus on transactional activities is meant to restrict the costs to reasonable and necessary expenditures but we found that for FY 2018, LACERA's Board education travel expenditures for 15 Board Members significantly exceeded a peer comparison with CALSTRS, who had 10 board members, and CALPERS, who had 13 board members.

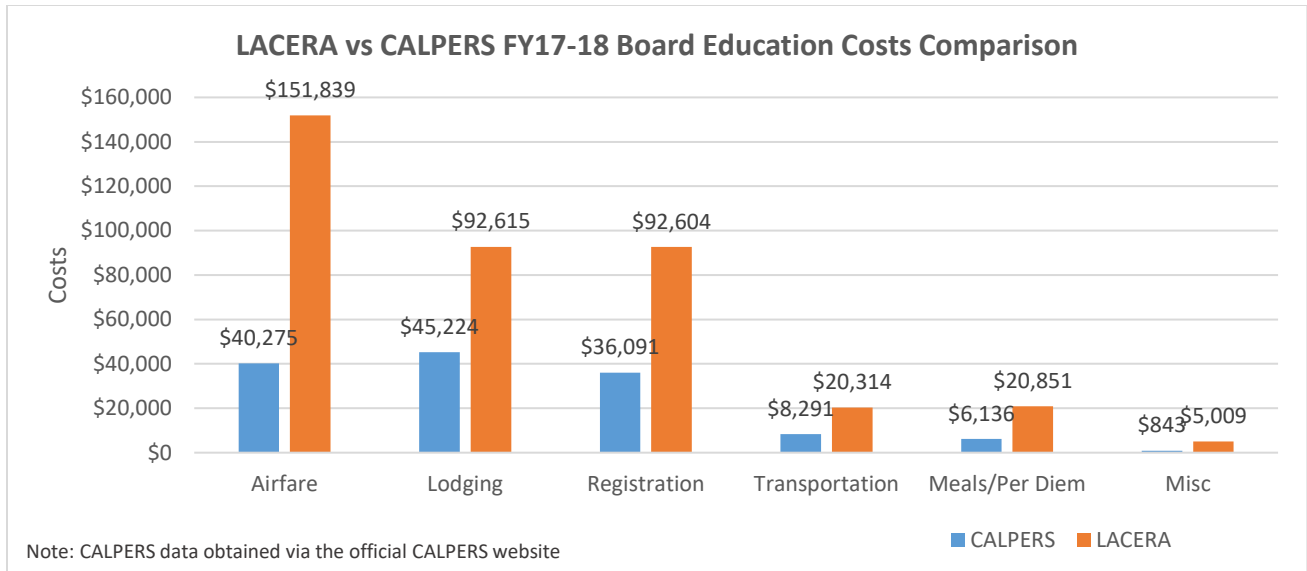
AC QUESTION: I disagree with this statement. The policy includes a value statement on the areas important for trustees – that statement are the approved conferences in the attachments. It is then up to each trustee to determine if he or she believes there is a need for him or her to enhance skills sets in those areas.

IA RESPONSE: Noted. Recommendation 10 on page 23 provides additional clarity to the statement above.

Due to the different number of board members of each fund, we calculated the average cost per Board Member: 1) \$26,884 for LACERA, 2) \$11,998 for CALSTRS, and 3) \$10,528 for CALPERS.



We noted LACERA Board Members attended between 1 to 16 educational conferences each (local and non-local), with a total travel cost ranging from less than \$1,000 to over \$55,000 per traveler. Seven Board members listed on the 4th quarter Travel Log, spent over \$25,000 for the Fiscal Year and their combined totals accounted for 79% (\$310,173) of Board educational travel.



The *Clapman* report identified concerns about relying on educational conferences as the primary form of education. The report states:

There is no lack of educational opportunities available to public pension fund trustees, and trustees as a rule are diligent about attending them. However, while trustees “devote considerable time and effort to education, primarily by attending a variety of conferences that are geared to public funds and that focus on investments,” such programs as a rule “neither encourage trustees to develop the broad vision they need to set policy, nor do they provide the practical grounding a board needs to oversee a fund’s operations.” Also, in our view many programs do not maximize “in seat” education. They may rely heavily on for-profit commercial sponsorships. Programs may also tilt the balance towards recreation and entertainment. (Attachment A, pg. 14)

The *Clapman* report accurately summarizes the reputational and operational risks that Internal Audit has identified by relying so heavily on these types of conferences for education.

AC QUESTION: You have not presented evidence to substantiate the statement that trustees are “relying on these types of conferences.”

IA RESPONSE: The LACERA Policy and practices demonstrate an emphasis on these types of conferences for education.

Furthermore, the current Policy does not establish an educational strategy that encourages continuously improving the skills a fiduciary should possess. A significant piece of the *Clapman* report’s proposed policy includes a “Trustee Knowledge Self-Assessment” which is used to assess and then develop an educational plan. Incorporating this best practice would address both an operational risk by ensuring all Board members receive an adequate amount of education in the areas needed, and a reputational risk by ensuring education expenditures can be supported.

Recommendation

10. To improve the effectiveness and adequacy of the Policy, Boards and management should:
 - a. Review the *Clapman* report’s education policy for a template of best practices.

- b. Consider adopting an organizational-wide educational strategy and incorporating the “Trustee (Fiduciary) Knowledge Self-Assessment.” Texas Teacher Retirement System and CalSTRS have both hired a consultant to assess the organizations’ requirements and preferences and to provide guidance in developing an effective educational strategy.

AC QUESTION: Define organization wide.

IA RESPONSE: LACERA

- c. Consider working with LACERA’s Training Coordinator to develop a process to create a stakeholder’s educational plan, monitor the broader educational needs of the Board for in-house training opportunities, and review and evaluate educational conferences.

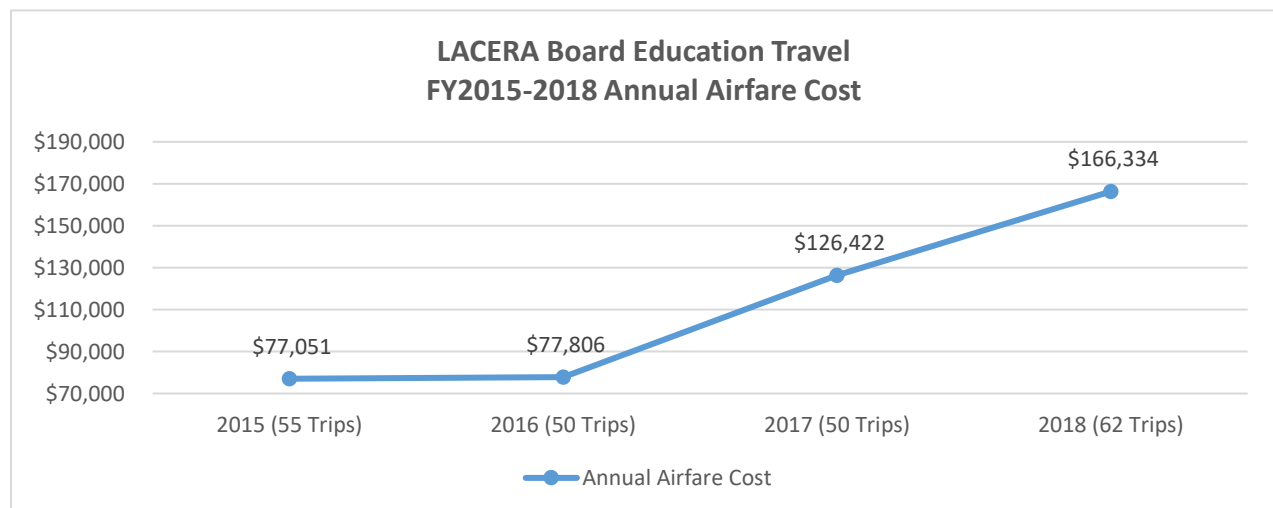
Management Response

Management concurs with this recommendation. Management will bring the issue to the JOGC for further discussion. This recommendation is expected to be completed by January 31, 2020.

Issue: Board Airfare Has Increased Substantially

Internal Audit analyzed the costs of registration, airfare, and lodging, for the last four fiscal years to gain a better understanding of the increase in Board education travel expenditures. Based on the analysis, the cost of airfare has sharply increased (see chart below). We believe LACERA’s airfare costs could be reasonably reduced by:

- Amending the Policy to reduce the frequency of business class travel, and
- Amending the Policy to revise how airline tickets are procured.



Business Class Airfare

As the chart above indicates, Board airfare has increased substantially in part due to the Policy revisions in March 2017 to allow business class travel when travel time exceeds five hours.

AC QUESTION: That chart provides no information that would allow the reader to conclude that business class is a source of the increase.

IA RESPONSE: We should have phrased it more clearly that we determined business class to be a source of the increase.

We noted the cost of the specific airline tickets below to show the cost of business class versus economy class for air travel that is generally six hours or less:

- A Board member's airfare for a domestic flight in December 2017 was approximately \$5,400. When Internal Audit priced this for a trip 14 days in advance, the most expensive direct, non-refundable, economy ticket on a major carrier was almost \$600 (Google Flights), which is 800% less than what LACERA paid.

AC QUESTION: and this was a business class ticket?

IA RESPONSE: Yes

- A Board member's airfare for a domestic flight in March 2018 was almost \$3,000. When Internal Audit priced this for a trip 14 days in advance, the most expensive direct, non-refundable, economy ticket on a major carrier was \$240 (Google Flights), which is 1150% less than what LACERA paid.
- A Board member's airfare for a domestic flight in June 2018 was approximately \$2,400. When Internal Audit priced this for a trip 14 days in advance, the most expensive direct, non-refundable, economy ticket on a major carrier was \$550. (Google Flights), which is 336% less than what LACERA paid.

Procurement of Airline Tickets

We observed from our testing that refundable tickets were purchased for some travel events. Since the current Policy does not address if or when purchasing refundable tickets is allowed, the purchases were not out of compliance with the Policy. However, since refundable tickets are often two to three times the cost of non-refundable tickets, it seems inconsistent with the Policy's general commentary on Attachment A of the Policy, "Travelers are encouraged to schedule travel in a way that minimizes LACERA's travel expenses." Staff reported that cancelations of trips are rare and that the cost of non-refundable tickets, less a nominal change fee, can be applied to future travel by the Board member.

Additionally, we noted that prudent procurement practices, such as comparing prices among at least three airlines flying to the destination, modifying dates and times of travel, and prohibiting Board members from limiting their travel to one specific airline, are not encouraged or enforced. Due to some airlines not offering business class, this sometimes results in Board members flying first class (as permitted by the policy if business class is not available) on their preferred airline and LACERA incurring costs up to \$12,500 for airfare. We did not obtain information on specific airfare procurement practices at CALPERS or CALSTRS but did not identify any airfares above \$3,000 for international business class travel.

Recommendation

11. To reduce LACERA's total airfare costs, Boards and management should:
- a. Re-evaluate the use of business class airfare.
 - b. Evaluate stronger enforcement of prudent procurement practices as described above, including prohibiting the purchase of refundable tickets.

Management Response

Management concurs with this recommendation. Management will bring the issue to the JOGC for further discussion. This recommendation is expected to be completed by January 31, 2020.

Other Best Practices Noted

We identified the following additional best practices in our review of peer public pension funds board travel practices for the Board and management to consider in future revisions to the Policy:

1. Transparency – Best practices included having the Education and Travel Policy on the Fund's public-facing website, inclusion of full estimated costs for travel in board memos requesting the board approval for travel, and providing a summary by traveler with all associated costs of all travel.
2. Centralized airline ticketing and cost management practices including the requirement that award miles earned are first used to upgrade tickets when the traveler is eligible for an upgrade to business class before the Fund incurs additional cost to upgrade the traveler.
3. Emphasis on in-house and local education first, with travel permitted when specific education is not locally available.
4. Separate the education policy from the travel procurement and reimbursement policy with all travelers required to comply with a centralized organizational policy for the procurement of travel and reimbursement of expenses. This establishes a more appropriate system of checks and balances.

We thank FASD, the Legal Office, and the Executive Office management and staff for their cooperation with our audit.

REVIEWED AND APPROVED



Richard Bendall
Chief Audit Executive

Date: June 20, 2019

REPORT DISTRIBUTION

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