CALIFORNIA PUBLIC EMPLOYEES' RETIREMENT SYSTEM

Report to the Risk and Audit Committee

For the Year Ended June 30, 2012

December __, 2012

To the Risk and Audit Committee
California Public Employees' Retirement System
Sacramento, California

We have audited the financial statements of the fiduciary activities and proprietary activities of the California Public Employees' Retirement System (the System) for the year ended June 30, 2012. Professional standards require that we provide you with information about our responsibilities under generally accepted auditing standards, as well as certain information related to the planned scope and timing of our audit. We have communicated such information to you in our meeting on August 15, 2012 with the Chair and Vice Chair of the Risk and Audit Committee. Professional standards also require that we communicate to you the following information related to our audit.

Qualitative Aspects of Accounting Practices

Management is responsible for the selection and use of appropriate accounting policies. The significant accounting policies used by the System are described in Note 1 to the basic financial statements. No new accounting policies were adopted and the application of existing policies was not changed during fiscal year 2012. We noted no transactions entered into by the System during the year for which there is a lack of authoritative guidance or consensus. All significant transactions have been recognized in the financial statements in the proper period.

Accounting estimates are an integral part of the financial statements prepared by management and are based on management's knowledge and experience about past and current events and assumptions about future events. Certain accounting estimates are particularly sensitive because of their significance to the financial statements and because of the possibility that future events affecting them may differ significantly from those expected. The most sensitive estimates affecting the System's financial statements were:

- Actuarial valuations of pension and other postemployment benefit assets, liabilities and required contributions
- Fair value of real assets and private equity investments and related income
- Estimated insurance claims due in the Health Care Fund
- Estimated liability for future policy benefits in the Long-Term Care Fund

The actuarial pension data contained in Note 9 to the basic financial statements and required supplementary information is based on actuarial calculations performed in accordance with the parameters set forth in GASB Statement No. 25, *Financial Reporting for Defined Benefit Pension Plans and Note Disclosures for Defined Contribution Plans.* The actuarial data for other postemployment benefits contained in Note 9 to the basic financial statements and required supplementary information is based on actuarial calculations performed in accordance with GASB Statement No. 43, *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans* and the CalPERS OPEB Assumption Model.

Qualitative Aspects of Accounting Practices (Continued)

Real assets consisted of real estate, forestland and infrastructure investments. Directly held and joint venture real estate investment fair values are based on recent estimates provided by the System's contract real estate advisors or independent appraisers. Commingled fund real estate investment fair values are based on the related partnership's June 30, 2012 financial statements. Forestland, infrastructure, and private equity investment fair values were determined by management, in consultation with the general partner and investment advisors, based on the related partnership's June 30, 2012 financial statements or the most recent financial information adjusted for cash flow activities through June 30, 2012.

The estimated insurance claims due in the Health Care Fund are based on incurred but not reported (IBNR) claims, disability extension claims and administrative expenses associated with those claims, as determined by the System's third-party administrator. The estimated liability for future policy benefits in the Long-Term Care Fund is based on the present value of future benefits and expenses less the present value of future premiums, as determined by the System's independent actuary.

We evaluated the key factors and assumptions used to develop these estimates in determining that they are reasonable in relation to the financial statements taken as a whole.

Certain financial statement disclosures are particularly sensitive because of their significance to financial statement users. The most sensitive disclosures affecting the financial statements were the schedule of funded status for the Public Employees' Retirement Fund (PERF) based on the most recent actuarial valuations as of June 30, 2011, and the estimated liability for future policy benefits of the Long-Term Care Fund. As described in Note 9 to the basic financial statements, the actuarial valuation involves estimates of the value and probability assumptions of events far into the future, and these amounts and assumptions are subject to continual revision as actual results are compared to past expectations. In addition, the most recent actuarial valuation for the PERF does not reflect the remaining deferred investment losses from fiscal year 2008/2009 that will be recognized in future valuations. As described in Note 8 to the basic financial statements, the estimated liability for future policy benefits is very sensitive to the underlying actuarial assumptions.

The financial statement disclosures are neutral, consistent, and clear.

Difficulties Encountered in Performing the Audit

We encountered no significant difficulties in dealing with management in performing and completing our audit.

Corrected and Uncorrected Misstatements

Professional standards require us to accumulate all known and likely misstatements identified during the audit, other than those that are trivial, and communicate them to the appropriate level of management. Management has corrected all such misstatements. In addition, none of the misstatements detected as a result of audit procedures and corrected by management were material, either individually or in the aggregate, to each opinion unit's financial statements taken as a whole.

Disagreements with Management

For purposes of this letter, a disagreement with management is a financial accounting, reporting, or auditing matter, whether or not resolved to our satisfaction, that could be significant to the financial statements or the auditor's report. We are pleased to report that no such disagreements arose during the course of our audit.

Management Representations

We have requested certain representations from management that are included in the management representation letter dated December __, 2012.

Management Consultations with Other Independent Accountants

In some cases, management may decide to consult with other accountants about auditing and accounting matters, similar to obtaining a "second opinion" on certain situations. If a consultation involves application of an accounting principle to the System's financial statements or a determination of the type of auditor's opinion that may be expressed on those statements, our professional standards require the consulting accountant to check with us to determine that the consultant has all the relevant facts. To our knowledge, there were no such consultations with other accountants.

Other Audit Findings or Issues

We generally discuss a variety of matters, including the application of accounting principles and auditing standards, with management each year prior to retention as the System's auditors. However, these discussions occurred in the normal course of our professional relationship and our responses were not a condition to our retention.

Other Matters

With respect to the supplementary information accompanying the financial statements, we made certain inquiries of management and evaluated the form, content, and methods of preparing the information to determine that the information complies with accounting principles generally accepted in the United States of America, the method of preparing it has not changed from the prior period, and the information is appropriate and complete in relation to our audit of the financial statements. We compared and reconciled the supplementary information to the underlying accounting records used to prepare the financial statements or to the financial statements themselves.

This information is intended solely for the use of the Risk and Audit Committee, Board of Administration and the System's management and is not intended to be and should not be used by anyone other than these specified parties.

Sacramento, California
December __, 2012