



## Agenda Item 7a

March 20, 2013

**ITEM NAME:** Management Letter

**PROGRAM:** Audit Services

**ITEM TYPE:** Action

### **RECOMMENDATION**

Approve the Draft Management Letter as prepared by Macias Gini & O'Connell LLP for the year ended June 30, 2012.

### **EXECUTIVE SUMMARY**

The Draft 2012 Management Letter, prepared by Macias Gini & O'Connell LLP, identifies several significant deficiencies in controls over financial reporting as well as opportunities for strengthening internal controls and operating efficiency. Macias Gini & O'Connell LLP discussed the observations and recommendations in the Draft Management Letter with management who have concurred with the observations and prepared a response to each recommendation. Management's responses are included in this Draft Management Letter.

### **STRATEGIC PLAN**

This item is not a specific product of the Strategic Plan.

### **BACKGROUND**

The Board of Administration's independent external financial statement auditor, Macias Gini & O'Connell LLP, completed its audit of CalPERS Financial Statements as of and for the year ended June 30, 2012 as required by Government Code Section 20228. The Board of Administration approved the basic financial statements on December 12, 2012. In connection with the audit of the financial statements, Macias Gini & O'Connell LLP prepared a Management Letter that includes observations and recommendations to enhance accounting and administrative internal controls as well as operational processes (Attachment 1). The draft management letter also includes updated status on prior year observations.

The Management Letter is considered a draft until it is accepted by the Board of Administration and subsequently signed by Macias Gini & O'Connell LLP. The signed Management Letter will be distributed to the Board of Administration, executive staff and senior management.

**ANALYSIS**

Consistent with the Risk and Audit Committee's Audit Resolution Policy, the status of the observations in the 2012 Management Letter will be reported to the Risk and Audit Committee until such time as management has satisfactorily resolved each noted observation and Macias Gini & O'Connell concurs that corrective action has been implemented.

MGO Issue No.	Summary of Observations	Mgmt. Letter Page No.
<b>Current Year Significant Deficiencies</b>		
2012-1	Completeness and Accuracy of Investment Related Disclosures	3-4
2012-2	Account Analysis and Financial Reporting	4-5
2012-3	Implementation of my CalPERS	6-9
<b>Current Year Other Comments and Recommendations</b>		
Obs.#1	Investment Classification	10
Obs.#2	Investment Commitment Disclosures	11-12
Obs.#3	Internal Controls Over Benefit Processing	13
Obs.#4	Self-Funded Health Enrollment Reconciliation	13-14
Obs.#5	Access to Programs and Data	14
<b>Prior Year Significant Deficiencies</b>		
2011-1	Implemented except for ensuring Executive inquiries and revisions to the basic financial statements are addressed prior to the Risk and Audit Committee	15-16
2011-2	Implemented. Securities Lending	16-18
2011-3	Implemented except for other matters related to the classification of unitized pooled investments presented in 2011-2012 Obs.#1	18-20
2011-4	Implemented. New or Unique Transactions	20-22
<b>Prior Year Other Comments and Recommendations</b>		
2010-2011 Obs.#1	Not Implemented. Refer to current year Significant Deficiency 2012-1 findings and recommendations on the completeness and accuracy of investment related disclosures	23-24
2010-2011 Obs.#2	Not Implemented. Reconciliation of Benefit Payments	25-26
2008-2009 Obs.#4	Implemented except for ensuring a formal Real Estate Appraisal process to review partnerships' financial information and fair values are properly reported	27-31

**BENEFITS/RISKS**

The benefit of approving the draft Management Letter is that appropriate corrective action to the noted observations will result in significant improvement of internal controls over financial reporting. If not mitigated, the risk is that internal controls over financial reporting may not prevent, detect or correct misstatements on a timely basis.

**ATTACHMENT**

Attachment 1 – Draft Management Comments and Recommendations, prepared by Macias Gini & O’Connell LLP as of and for the fiscal year ended June 30, 2012.

---

MARGARET JUNKER, Chief  
Office of Audit Services

---

PETER H. MIXON  
General Counsel