



Agenda Item 7a

March 17, 2015

ITEM NAME: External Auditor's 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, 2014.

EXECUTIVE SUMMARY

The Draft Management Letter, prepared by Macias Gini & O'Connell LLP (MGO), includes observations and recommendations related to strengthening internal controls over financial reporting and operating efficiency based on the audit of the June 30, 2014 financial statements. Importantly, no material weaknesses or significant deficiencies in internal controls over financial reporting were noted as a result of the audit. Management's concurrence, response, and proposed corrective action to the observations and recommendations are included in the Draft Management Letter. In addition, the Draft Management Letter contains the status of prior year recommendations. Management has appropriately resolved the prior year material weakness, significant deficiencies, and a majority of observations.

STRATEGIC PLAN

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

BACKGROUND

The Board of Administration's (Board's) independent financial statement auditor, MGO, completed its audit of CalPERS Financial Statements as of and for the year ended June 30, 2014 as required by Government Code Section 20228. The Board approved the basic financial statements and accepted the independent auditor's report on November 19, 2014. In connection with the audit of the financial statements, MGO prepared a Draft 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 approved by the Board and subsequently signed by MGO. The signed Management Letter will be distributed to the Board, executive staff and senior management.

ANALYSIS

Consistent with the Risk and Audit Committee’s Audit Resolution Policy, the status of the Management Letter observations will be reported to the Risk and Audit Committee until management has satisfactorily resolved each noted observation and MGO concurs that corrective action has been implemented.

The tables below summarize the comments and corresponding pages in the Draft Management Letter. It should be noted that management has appropriately resolved the prior year material weakness and significant deficiencies. The two remaining prior year observations are expected to be completed in fiscal year 2014-15.

Table 1 – Current Year Observations and Recommendations

Issue Number	Description	Page Number
Observation 1	Investment Valuation – Process related to accounting and reporting of estimated investment fair values	3-5
Observation 2	Actuarial Discount Rate Determination – Inconsistent with new accounting standards	6
Observation 3	Member Census Data – Discrepancies between the Actuarial Valuation System, my CalPERS and employer records.	7-8

Table 2 – Status of Prior Year Comments and Recommendations

Issue Number	Description	Status	Page Number
2013-1	Material Weakness – Completeness and Accuracy of Investment Related Disclosures	Resolved	9-12
2013-2	Significant Deficiency – Internal Controls over Accounting and Financial Reporting	Resolved	13-15
2012-3	Significant Deficiency – Implementation of my CalPERS	Resolved	15-20
2013	Observation 1 – Other Post-Employment Benefits Liability Allocation	Resolved	21
2013	Observation 2 – Member Census Data (formal process for communicating corrections)	In Progress	22
2012	Observation 2 – Investment Commitment Disclosures	In Progress	23-26
2012	Observation 4 – Self-Funded Healthcare Enrollment Reconciliation	Resolved	27-28

BENEFITS/RISKS

The primary benefit of approving the Draft Management Letter is to assist CalPERS in meeting its fiduciary responsibilities to plan participants by ensuring effectiveness of controls over financial reporting designed to prevent, or timely detect, errors that could result in material misstatements in the financial statements. The risk of not implementing recommendations is limiting the timely detection, prevention or correction of material misstatements in the financial statements.

ATTACHMENT

Attachment 1 – Draft Management Letter, prepared by MGO as of and for the fiscal year ended June 30, 2014.

YOUNG HAMILTON, Acting Chief
Office of Audit Services

MATTHEW G. JACOBS
General Counsel