

MEETING
STATE OF CALIFORNIA
PUBLIC EMPLOYEES' RETIREMENT SYSTEM
BOARD OF ADMINISTRATION
RISK AND AUDIT COMMITTEE
OPEN SESSION

ROBERT F. CARLSON AUDITORIUM
LINCOLN PLAZA NORTH
400 P STREET
SACRAMENTO, CALIFORNIA

TUESDAY, NOVEMBER 15, 2016

6:34 P.M.

JAMES F. PETERS, CSR
CERTIFIED SHORTHAND REPORTER
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A P P E A R A N C E S

COMMITTEE MEMBERS:

Mr. Ron Lind, Chairperson

Ms. Dana Hollinger, Vice Chairperson

Mr. J.J. Jelincic

Ms. Priya Mathur

Ms. Theresa Taylor

Ms. Betty Yee, represented by Mr. Alan Lofaso

BOARD MEMBERS:

Mr. Michael Bilbrey

Mr. John Chiang, represented by Mr. Eric Lawyer

STAFF:

Ms. Marcie Frost, Chief Executive Officer

Ms. Cheryl Eason, Chief Financial Officer

Mr. Matthew Jacobs, General Counsel

Ms. Beliz Chappuie, Chief Auditor

Mr. Forrest Grimes, Chief Risk Officer

Ms. Carrie Lewis, Committee Secretary

Ms. Kimberly Malm, Chief, Operations Support Services
Division

Ms. Kristin Montgomery, Controller

Ms. Marlene Timberlake D'Adamo, Chief Compliance Officer

A P P E A R A N C E S C O N T I N U E D

ALSO PRESENT:

Mr. Mark Baer, Crowe Horwath

Mr. Dan Barron, Grant Thornton

Mr. David Bullock, Macias, Gini & O'Connell

Mr. Jeff Burgess, Grant Thornton

Ms. Vanessa Burke, Grant Thornton

Mr. Roger Burton, Macias, Gini & O'Connell

Ms. Debbie Chan, Macias, Gini & O'Connell

Ms. Leah Cochran, Macias, Gini & O'Connell

Mr. David Driscoll, Buck Consultants

Mr. Craig Harner, Macias, Gini & O'Connell

Mr. Ric Jazaie, Macias, Gini & O'Connell

Mr. Tim Lee, Grant Thornton

Mr. Rick Green, Macias, Gini & O'Connell

Mr. Chris Moore, Crowe Horwath

Ms. Marilyn Oliver, Macias, Gini & O'Connell

Mr. Brad Ramirez, Segal

Mr. Jack Reagan, Grant Thornton

Mr. Bob Sanford, PRM Consulting

Mr. Brett Schwab, Grant Thornton

Mr. Aaron Shapiro, Buck Consultants

Mr. Kevin Smith, Crowe Horwath

Mr. Craig Sullivan, Crowe Horwath

A P P E A R A N C E S C O N T I N U E D

ALSO PRESENT:

Ms. Brenda Torres, Crowe Horwath

Ms. Caroline Walsh, Macias, Gini & O'Connell

Mr. Craig Yoder, Crowe Horwath

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1 P R O C E E D I N G S

2 CHAIRPERSON LIND: Good evening, everybody.

3 We're going to call the meeting to order -- call to order
4 the meeting -- it's getting late -- of the Risk and Audit
5 Committee. Roll Cal, please.

6 COMMITTEE SECRETARY LEWIS: Ron Lind?

7 CHAIRPERSON LIND: Here.

8 COMMITTEE SECRETARY LEWIS: Dana Hollinger?

9 VICE CHAIRPERSON HOLLINGER: Here.

10 COMMITTEE SECRETARY LEWIS: J.J. Jelincic?

11 COMMITTEE MEMBER JELINCIC: Here.

12 COMMITTEE SECRETARY LEWIS: Priya Mathur?

13 COMMITTEE MEMBER MATHUR: Here.

14 COMMITTEE SECRETARY LEWIS: Bill Slaton?

15 CHAIRPERSON LIND: Excused.

16 COMMITTEE SECRETARY LEWIS: Theresa Taylor?

17 COMMITTEE MEMBER TAYLOR: Here.

18 COMMITTEE SECRETARY LEWIS: Alan Lofaso for Betty
19 Yee?

20 ACTING COMMITTEE MEMBER LOFASO: Here.

21 CHAIRPERSON LIND: Thank you.

22 Cheryl, any executive report?

23 CHIEF FINANCIAL OFFICER EASON: Thank you. Good
24 evening, Mr. Chair, Committee members. Cheryl Eason. I
25 will keep my remarks very short. I did want to point out,

1 however, we do have 3 action items and a request has been
2 made that our finalist interviews for the independent
3 financial statement auditor, if the Committee so wishes,
4 that we would -- could do those first prior to the other
5 two, in the interests of time.

6 CHAIRPERSON LIND: Yeah. We are going to move up
7 C above A and B in Action Item number 5.

8 CHIEF FINANCIAL OFFICER EASON: Great. Okay.
9 Thank you. And then just wanted to point out that there
10 are 2 information items, one is Buck Consultants are here
11 to present their third-party valuation and certification
12 of the contracting public agency plan and we have a
13 follow-up for the Committee on the semi-annual enterprise
14 risk report, which we will keep brief.

15 And then a quick update housekeeping item. In
16 your handout folder, it had been pointed out that
17 Information Consent Agenda Item 4g, there was an error on
18 a graph. We've since corrected that graph. It's related
19 to ethic helpline complaints. Should have been 47 instead
20 of 61, and that's why you have that information in your
21 handout folder.

22 And with that, I conclude my report.

23 CHAIRPERSON LIND: Thank you.

24 Can I have a motion to approve the September 20th
25 minutes please.

1 COMMITTEE MEMBER MATHUR: So moved.

2 COMMITTEE MEMBER TAYLOR: Second.

3 CHAIRPERSON LIND: Moved by Mathur, second by
4 Taylor.

5 All in favor?

6 (Ayes.)

7 CHAIRPERSON LIND: Any opposed?

8 I see no requests to move anything off of
9 consent. So that moves to on to 5c. This is the finalist
10 interviews for the independent financial auditor. And I
11 want to apologize to everybody for you having to be here
12 when it's dark and late and all of that, but we had a long
13 agenda on the previous meeting. So, please, accept our
14 apologies.

15 A few points on this issue. Today, the Risk and
16 Audit Committee is interviewing the finalists for the
17 independent financial statement auditor requests for
18 proposal number 2015-8132.

19 In accordance with the RFP, we, as a group,
20 Committee members, will determine the interview score for
21 each finalist and make a motion to adopt the interview
22 score with a maximum of 700 points.

23 At this time, I'm going to ask Beliz Chappuie,
24 the Chief Auditor, to provide a summary of the RFP
25 activities to date and logistics of the interview process.

1 Beliz.

2 CHIEF AUDITOR CHAPPUIE: Thank you, Mr. Chair.

3 Before I start, please note the new interview
4 questions are in your hand-out folders.

5 CHAIRPERSON LIND: We do have the interview
6 questions and Committee members know what questions
7 they're going to ask.

8 Thank you.

9 CHIEF AUDITOR CHAPPUIE: Thank you.

10 The CalPERS Board of Administration has delegated
11 to this Committee the authority to conduct the selection
12 of the Board's independent financial statement auditor and
13 to recommend the finalist to the Board. On November 17th,
14 2015, staff obtained approve to issue the RFP, which
15 solicited bids from qualified firms to perform audits of
16 CalPERS financial statements for fiscal years 2016-17
17 through 2021.

18 In June 2016, at close of final filing date, our
19 four firms had submitted proposals. Three of the 4
20 proposals passed the preliminary review. Staff, with the
21 oversight of the Designated Risk and Audit Committee Board
22 members, evaluated and scored proposals as outlined in the
23 RFP, and presented all 3 firms -- qualified firms to the
24 Board in September 2016.

25 On September 20, 2016, the Board selected all 3

1 finalists, Crowe Horwath, Grant Thornton, and Macias, Gini
2 & O'Connell to move forward with the interviews scheduled
3 for today. I would like to take the time to update the
4 Committee on the preliminary total scores of the firms.
5 Crowe Horwath received 140 points, Grant Thornton received
6 122 points, and Macias, Gini & O'Connell received 300
7 points.

8 Each finalist will be allotted 30 minutes for an
9 interview, 10 minutes for presentation, and 20 minutes for
10 question and answers. All finalists should be asked the
11 same questions. Committee members may ask clarification
12 questions as needed.

13 At the conclusion of the interviews, the
14 Committee will determine an interview score as a group for
15 each finalist, and motion the interview scores. The
16 interview scores will be collected and combined with the
17 preliminary total scores to determine a total score for
18 each finalist.

19 The finalists will be ranked from highest to
20 lowest total score. The Committee will then be asked to
21 make a motion recommending the Board award the contract to
22 the finalist with the highest total score, subject to
23 final negotiations and satisfaction of all requirements.

24 At this time, I would like to remind the
25 finalists that each of your firms signed and submitted the

1 CalPERS full Board of Administration interview form with
2 your proposals. This form represents a pledge that each
3 of you will make -- will not make any attempt to listen to
4 or watch the interviews with other finalists, nor have
5 anyone do so on your behalf. Failure to adhere to this
6 requirement will result in your firm's disqualification
7 from this engagement.

8 Thank you, Mr. Chair.

9 CHAIRPERSON LIND: Thank you for the overview. I
10 want to remind Committee members that once we start,
11 please stay through the entire interview process. We now
12 have to take roll again, so the record reflects that the
13 Risk and Audit Committee members present and participated
14 in the interview and selection process for the contract.

15 Roll, please.

16 COMMITTEE SECRETARY LEWIS: Ron Lind?

17 CHAIRPERSON LIND: Here.

18 COMMITTEE SECRETARY LEWIS: Dana Hollinger?

19 VICE CHAIRPERSON HOLLINGER: Here.

20 COMMITTEE SECRETARY LEWIS: J.J. Jelincic?

21 COMMITTEE MEMBER MATHUR: J.J.?

22 COMMITTEE MEMBER JELINCIC: Yeah.

23 (Laughter.)

24 COMMITTEE SECRETARY LEWIS: Priya Mathur?

25 COMMITTEE MEMBER MATHUR: Here.

1 COMMITTEE SECRETARY LEWIS: Bill Slaton?

2 CHAIRPERSON LIND: Excused.

3 COMMITTEE SECRETARY LEWIS: Theresa Taylor?

4 COMMITTEE MEMBER TAYLOR: Here.

5 COMMITTEE SECRETARY LEWIS: Alan Lofaso for Betty
6 Yee?

7 ACTING COMMITTEE MEMBER LOFASO: Here.

8 CHAIRPERSON LIND: Thank you. So we're now going
9 to conduct the interviews in alphabetical order. Crowe
10 Horwath, LLC will be first, Grant Thornton, LLC will
11 second, and Macias, Gini & O'Connell, LLC will be the last
12 interview.

13 Each finalist will have 10 minutes for the
14 presentation, 20 minutes for question-and-answer period.
15 The clock in front of you that you can see will show the
16 remaining time in each segment.

17 Committee members, please note that the questions
18 we can ask all finalists are included in item 2, the
19 finalist interview packet actually have been given to you
20 tonight. The score is determined as a group. Beliz kind
21 of laid that out, so I don't think I need to repeat it.
22 Does anybody have any questions before we get started?

23 COMMITTEE MEMBER JELINCIC: Yes.

24 CHAIRPERSON LIND: Okay. Click your button.

25 J.J.

1 COMMITTEE MEMBER JELINCIC: On the questions, as
2 long as we ask the same question of everybody, it's fair,
3 because I've got a slight variation on the questions you
4 drafted.

5 COMMITTEE MEMBER MATHUR: Microphone.

6 CHIEF AUDITOR CHAPPUIE: Clarification questions
7 could be specific to the candidates. Does that help?

8 COMMITTEE MEMBER JELINCIC: My question is do I
9 have to ask exactly the question you gave me, or can I ask
10 essentially the same question, as long as I'm consistent
11 to everybody?

12 GENERAL COUNSEL JACOBS: The latter.

13 COMMITTEE MEMBER JELINCIC: Thank you.

14 CHAIRPERSON LIND: Any other questions?

15 Okay. We're going to begin the process. I'd
16 like to invite all representatives of the Crowe Horwath,
17 LLC to come forward, and ask that the Grant Thornton folks
18 and the Macias, Gini & O'Connell folks leave the
19 auditorium.

20 There's a lot of moving bodies out there.

21 We were worried about you guys catching a plane.
22 You probably chartered a plane, the size of your group,
23 right?

24 Okay. We're all settled in. The other groups
25 have left the auditorium. You are going to have 10

1 minutes for your presentation. If the staff would please
2 start the clock when the Crowe Horwath staff starts to
3 speak. So I'm not sure which of you is up, but take it
4 away.

5 MR. YODER: Hello, Mr. Chair and members of the
6 Committee. My name is Craig Yoder. I'm the office
7 managing partner for the Sacramento office of Crowe
8 Horwath, LLP. I'm also on the proposed engagement team.
9 I've been with Crowe my entire 32 year career. Most of
10 that time auditing financial services companies, and I'll
11 bring that experience to assisting in the audit of your
12 investment portfolio.

13 It's our pleasure to join you to share why Crowe
14 Horwath is the best choice to serve as CalPERS next
15 independent auditor. We're well equipped to audit an
16 entity as large and sophisticated as CalPERS, and
17 understand your obligation to provide transparency and
18 meaningful accurate financial statements to your
19 stakeholders.

20 We've invested a significant amount of time
21 scoping the engagement to offer fair and competitive fees,
22 and we would be happy to expand on that during the
23 question-and-answer discussion.

24 We're committed to audit quality and timely
25 delivery through our industry expertise, innovative

1 technology, and technical proficiency. In addition, we
2 have an independent internal quality control system, and
3 are one of 10 firms in the United States to be -- to
4 receive a full detailed annual inspection by the Public
5 Company Accounting Oversight Board.

6 Crowe has over 3,500 personnel, including more
7 than 300 people in our 4 California offices, and a
8 dedicated team of industry and technical specialists.

9 We also have a partnership model that allows us
10 to break down silos and assemble a team based upon the
11 deep industry expertise that is not predicated on where
12 those individuals organizationally or geographically.

13 I want to emphasize that exceptional client
14 service, along with independence, objectivity, and
15 professional skepticism are at the forefront of everything
16 we do. Thank you for this opportunity.

17 Brenda.

18 MS. TORRES: Thank you, Craig. Good evening.

19 CHAIRPERSON LIND: You need to hit your
20 microphone, please.

21 MS. TORRES: I apologize. Thank you Craig, and
22 good evening. My name is Brenda Torres. I have been with
23 Crowe for 23 years providing services to retirement
24 systems and qualified retirement plans. I would serve as
25 the signing engagement partner on the CalPERS audit, and

1 would lead a team of dedicated and specialized individuals
2 to provide CalPERS with exceptional client service.

3 MR. SMITH: Hello. My name is Kevin Smith. I've
4 spent my entire 25 year career serving State and local
5 governments. I am currently serving my second term on the
6 AICPA State and Local Expert Panel, where I interact
7 directly with both the AICPA and GASB on current
8 developments, many of which will have a direct impact upon
9 CalPERS.

10 As your client service partner, I will be working
11 closely with Brenda and the rest of the team throughout
12 the engagement. Utilizing our seek first approach, we
13 will work with management and this Committee to develop an
14 audit timeline and communication strategy that allows
15 timely issuance of our deliverables.

16 Your engagement team includes professionals with
17 expertise in investment valuation, IT audit and risk
18 services, state and local government accounting and
19 financial reporting, and actuarial specialists. We will
20 devote significant senior level time to -- in the
21 planning, supervision, execution, of the audit. The
22 people you see here tonight, you will see on the field at
23 the engagement.

24 In fact, our estimate assigns nearly 1 of every 2
25 hours to a professional at the manager level or above.

1 This degree of experience establishes a solid foundation
2 of veteran leadership, deep functional proficiency that we
3 believe is difficult to replicate.

4 MS. TORRES: Our accomplished professionals have
5 extensive industry knowledge working with the second
6 largest U.S. PERS, as well as working with over 290
7 CalPERS PERF B employers through our audit census test
8 data. We also have members of our proposed engagement
9 team that speak on behalf of the AICPA at conferences and
10 webinars. We also speak at the Public Pension Financial
11 Forum, and have also spoken at the Cal CPA local
12 government conference.

13 Our actuarial specialists have over 60 years of
14 combined actuarial service at the federal, State, and
15 local government levels. In addition Crowe has delivered
16 more than 400 California public sector projects, including
17 providing audit services to over 100 local governments on
18 an annual basis. This expertise and leadership will
19 facilitate a smooth audit transition with significant
20 focus on planning and minimizing disruption to the
21 organization.

22 We use emerging advanced technologies to benefit
23 our clients, our firm, and our people, which are embedded
24 in our audit process. We work in accordance with all
25 professional standards and our findings are based on true

1 objectivity and competency. We have and will continue to
2 monitor conflicts of interest, and can assure you that we
3 meet the independence requirements to be your next
4 external auditor.

5 MR. BAER: Good evening, Mr. Chairman and
6 Committee Members. Thank you again for your time today.
7 My name is Mark Baer. As managing partner of our firm's
8 national audit practice, I'm very proud to support our
9 team that's with you here today.

10 Crowe Horwath, LLP is one of the largest public
11 accounting, consulting, and technology firms in the United
12 States with an audit practice consisting of over 1,000
13 specialized professionals serving clients across our more
14 than 30 locations. We recognize your role as stewards of
15 CalPERS and the substantial obligation you hold to protect
16 the benefits and retirements of future generations.

17 Today, we've assembled a team of deeply
18 specialized professionals who will perform a rigorous and
19 objective audit to help assist the Board in fulfilling its
20 fiduciary responsibility. Our team is built on one simple
21 concept, how do we provide CalPERS the best service
22 possible?

23 We demonstrate a unique value proposition of this
24 team of deeply specialized individuals from across our
25 firm who have worked together and are the very best of the

1 best from Crowe to serve your organization.

2 We've proudly served clients and delivered
3 services for nearly 75 years by listening to needs and
4 developing a comprehensive understanding of your
5 organization, and we appreciate the opportunity to do the
6 same for you. Now, we'd like to introduce the rest of our
7 team members. Thank you.

8 MR. SANFORD: Good evening. My name is Bob
9 Sanford. I'm here tonight representing PRM Consulting
10 Group. PRM is proposed on the CalPERS engagement to be a
11 subcontractor to Crowe to provide the actuarial services.
12 PRM is a actuarial, employee benefits, and compensation
13 consulting firm in the Mid-Atlantic area. We have several
14 offices there. It was formed in 1999, and currently have
15 about 50 employees.

16 I joined the firm in 2008. I'm an actuary
17 specializing in the Pension and Health benefits area. And
18 for the proposed engagement, I would really be involved in
19 all the actuarial aspects of the audit. I have almost 40
20 years of actuarial -- work in the actuarial practice area.

21 Another area where I spend a great deal of time
22 is in the Education Committee of the Society of Actuaries.
23 I served as the chairman of that system in 2013. And I
24 continue to be involved on a committee that has the
25 responsibility of establishing the educational

1 requirements that actuaries must master in order to
2 practice in the retirement benefits area.

3 Our Committee is keenly aware of the myriad of
4 issues facing public retirement systems. We spent a lot
5 of time thinking about that, and are very diligent to make
6 sure our candidates are well educated and well tested, so
7 that they can practice in that area.

8 MR. MOORE: Good evening. I'm Chris Moore. I'm
9 the firm's partner in charge of investment security and
10 derivative valuation.

11 As part of that role, I supervise the firm's
12 pricing desk that centrally tests investment security and
13 derivative valuations across the entire firm supporting
14 teams and the various industries that we serve.

15 On the CalPERS engagement, I would supervise and
16 directly participate in the valuation and other
17 derivative -- other investment matters. I've got 26 years
18 of experience entirely with Crowe.

19 MR. SULLIVAN: Hi. I'm Craig Sullivan. I'll be
20 the partner responsible in the evaluation of information
21 technology controls at CalPERS. I have 32 years of
22 experience in that area, including large transaction
23 processors, both as a signing partner for SOC 1 and SOC 2
24 reports, including insurance, health care, investment, and
25 financial services accounting.

1 I'm also involved in the AICPA cyber security
2 reporting initiative, as that becomes more and more in the
3 press of issues that all companies are dealing with today.
4 I do have direct experience with the pension systems and
5 other related systems for PERS.

6 MS. TORRES: Also with us today in our audience
7 is Alexis Fitzpatrick. She's a senior manager that has 12
8 years of experience auditing financial services,
9 retirement systems, employee benefit plans. She would
10 serve as the overall project manager.

11 Rich Perilloux is also in the audience. He
12 specializes in IT risk, and would work with Craig on the
13 IT components of the engagement. And we have 2 managers
14 in the room, Dan O'Malley and Dorothy Somera. They would
15 serve as your on-site supervisors and both have relevant
16 experience to serve the CalPERS engagement.

17 Our entire engagement team is available to
18 address any of your questions, even those in the audience.

19 Thank you.

20 CHAIRPERSON LIND: Thank you very much for your
21 presentation. We're going to go now to the
22 question-and-answer session. I'm going to call on Ms.
23 Taylor for the first question.

24 COMMITTEE MEMBER TAYLOR: Hi. Thank you. Sorry
25 about that.

1 CHAIRPERSON LIND: Woops. There you go.

2 COMMITTEE MEMBER TAYLOR: Thank you very much for
3 being here today. Please describe financial statement
4 audits you have performed for large organizations with
5 complex investments services similar to CalPERS.

6 MR. MOORE: We've participated -- I've been
7 directly involved with the audit of the investment
8 portfolio at CalSTRS, the second largest PERS in the U.S.,
9 for the past 6 years. That includes every aspect of their
10 portfolio, global equities, the fixed income, the
11 derivatives, the private equity and real estate
12 investments.

13 CHAIRPERSON LIND: Thank you, Ms. Hollinger. You
14 have the second question.

15 VICE CHAIRPERSON HOLLINGER: Thank you. Thank
16 you. Describe your knowledge and experience relating to
17 auditing large and complex pension funds, including
18 implementation of GASB 67, 68.

19 MR. SMITH: Again to highlight what Chris said,
20 we significant experience gained from our audit of
21 California State Teachers' Retirement System, as well as a
22 variety of other defined benefit plans across the country.
23 I am again serving on my second rotation through the AICPA
24 State and Local Expert Panel. I was actually on one of
25 the subcommittees that adopted chapter 13 of the audit

1 guide, which spelled out all of the audit requirements
2 that firms are following now in order to opine both at the
3 plan level as well as what audit support the employer
4 audit engagements need.

5 So we have extensive experience in assisting
6 clients both from the employer and the employee side, and
7 have significant experience in developing of that
8 guidance.

9 CHAIRPERSON LIND: Thank you.

10 Ms. Mathur, you have the next question.

11 COMMITTEE MEMBER MATHUR: Thank you. Please
12 share your experience working with subcontracted health
13 and long-term care actuaries in performing audits of large
14 pension funds and the number of years that your firm has
15 been working with them, and describe your firm's actuarial
16 experience to conduct this audit. And if you could also
17 add any experience you have with integrated financial
18 statements, including environmental, social, and
19 governance issues.

20 MS. TORRES: So our subcontracted actuary that
21 would work on the CalSTRS engagement was scoped out of
22 this engagement due to independence conflicts. So we took
23 their recommendation very seriously with their knowledge
24 in the PERS arena to recommend a consulting actuary to
25 work with us with respect to your particular engagement.

1 And we selected PRM Consulting. The nature of
2 working with subcontractors as it relates to actuarial
3 services is very much a collaborative approach. Make no
4 mistake though, your auditor, in this case Crowe Horwath,
5 LLP, is responsible for the audit opinion. So we are
6 responsible for forming our final conclusions, as it
7 relates to all of the census data testing, as well as the
8 actuarial assumptions, and making sure the financial
9 statements are not materially misstated.

10 What we utilize our subcontracted actuary for is
11 for their deep industry expertise in all the significant
12 areas of the programs and plans offered by CalPERS. We
13 feel that PRM Consulting has diverse experience in all of
14 those areas and would really help us assess the expertise
15 of the actuaries that are determining -- or consulting
16 with you to determine your financial reporting.

17 They would also assess their capabilities, help
18 us assess the reasonableness of the actuarial assumptions,
19 help us conclude on any differences that we might find
20 throughout our audit testing to help us form our basis of
21 our opinion.

22 And with that, Bob, I think I'll turn it over to
23 you to talk more about your experience.

24 MR. SANFORD: Sure. You asked about our
25 experience with performing actuarial audits of plans

1 similar to CalPERS, as well as other post-employment
2 benefits and long-term care. We do a lot of work at the
3 federal government level. We work with the Civil Service
4 Retirement Plan and the Federal Employees Retirement
5 System.

6 We've done audits of the assumption sets that are
7 used in those things -- in those plans, and look at the
8 unique nature of the participants in those plans that are
9 covered by the U.S. Postal Service, and how assumptions
10 about their demographics, their salary increases, that
11 kind of thing can be different.

12 We do work for the retiree health for the postal
13 service as well. And actually for the Commonwealth of
14 Pennsylvania, we've done valuations of their long-term
15 care plan for the Judges' plan.

16 CHAIRPERSON LIND: I'm not sure anybody responded
17 to the ESG question that Priya asked.

18 MS. TORRES: Yeah, I was going to ask if we could
19 provide -- if you could go through that question again,
20 please?

21 COMMITTEE MEMBER MATHUR: Sure. Just -- there's
22 a movement around integrated reporting of sustainability
23 issues and material sustainability factors in -- in
24 corporate reporting. And I just -- I'm more -- I'm
25 curious whether that trend is taking off in the public

1 sector as well, and if that is something you have any
2 experience in?

3 MR. SMITH: I would love to say that we have more
4 experience in it than what we do. It is definitely
5 something that we see gaining ground within the public
6 sector arena. We are actually one of the proud sponsors
7 of the SASB. We make our annual contribution there and
8 continue to look for opportunities. We have a new partner
9 within Crowe Horwath in the State here located locally.
10 And one of her charges is to evaluate the ability to bring
11 over sustainability reporting, particularly as it relates
12 to the water districts within California.

13 I think it's something that we will continue to
14 see growth and expansion, and it's something that, as a
15 firm, we are embracing and moving forward with.

16 COMMITTEE MEMBER MATHUR: Okay. Thank you.

17 CHAIRPERSON LIND: Thanks.

18 So this is obviously a dynamic organization here.
19 And can you describe how you will ensure flexibility and
20 responsiveness to changes in CalPERS business, risks,
21 operations, programs, systems, and controls?

22 MR. SMITH: I think one of the reasons that we
23 believe that the team we've assembled is the right team
24 for you is primarily, to be honest, the amount of gray
25 hair that we have at this table, as well as going to be on

1 your engagement.

2 We have the ability to adapt, apply judgment at
3 any given moment, and shift focus when needed. We don't
4 believe that an audit the size of CalPERS with its
5 sophistication, complex organizational structure, as well
6 as so many stakeholders relying upon it, that it's an
7 engagement that you park a lot of young staff and senior
8 people -- or senior in-charges on.

9 Obviously, they had their role on the engagement,
10 but it is going to be led by managers, senior managers,
11 and partners on a daily basis. I think that experience
12 and judgment allows us to adapt and move with you as we
13 move forward.

14 CHAIRPERSON LIND: Anybody else want to respond
15 to that?

16 MS. TORRES: I would just add that as a part of
17 that senior level leadership, we would be involved in all
18 phases of the audit. From the very beginning, we were
19 involved extensively in scoping the engagement to
20 determine the pricing to assemble the team that is with
21 you today.

22 And, you know, you would see us on the ground and
23 meeting with you, talking with the executives of CalPERS
24 to make sure that we're addressing their concerns. What
25 we found in other organizations is each of the business

1 units, if you will, may operate a little bit differently.
2 They may have different needs, different expectations,
3 different timing, if you will. And so we want to be
4 respectful to their day jobs. And so we're deeply
5 specialized to really understand their part of the overall
6 business, and to work with them to be flexible, but also
7 to get the audit done in an efficient and timely manner.

8 MR. SULLIVAN: Brenda, if I could add to that
9 too, and for the Committee. From the information
10 technology side, as we know, it's always constantly
11 changing from production of member information, and PII,
12 and other information that's out there. Part of the
13 responsibility that we have as a team working together is
14 to ensure that we have the right people to look at those
15 controls, especially as it relates to the financial
16 reporting, and the other items that the audit team needs
17 to consider as they walk through with the audit.

18 So we do work with the PeopleSofts of the world,
19 and the large systems like that, and have direct
20 experience with those systems in other locations, some
21 both within PERS, as well as within other very similar
22 companies at this complexity level too. So we do have
23 that expertise, and that's one of the reasons I'm here
24 with the team to ensure that that's brought to bear for
25 the overall group.

1 MR. SMITH: I think the only thing I would add to
2 that is I think the other firms you'll speak to tonight
3 will also be able to talk about their involvement in a
4 variety of different ways.

5 But when Craig mentions that he's involved in the
6 ICPA's task force on cyber security, my involvement on the
7 State and Local Expert Panel, Chris is involved nationally
8 in various working groups as it relates to valuation, the
9 team we tried to pull together for you wasn't in order to
10 be able to tap the resources throughout the firm that has
11 knowledge of what's happening within the industry, we
12 tried to bring the people to you who have that insight and
13 who are interacting on a daily basis with the decision
14 makers that have some influence on the external operations
15 of CalPERS. So we've really tried to put together a team
16 that can adapt and grow with you.

17 CHAIRPERSON LIND: Great. Thank you.

18 Mr. Jelincic has the next question.

19 COMMITTEE MEMBER JELINCIC: Yeah. And it's a
20 multi-part question. I assume you've seen the fees
21 difference, and so it's not clear that everybody is
22 bidding on the same thing. How did you come with your
23 proposal for the hours identified in your fee proposal.
24 And I will tell you that the range was 3,856, 10,129, and
25 657.

1 And within that, can you explain the rationale
2 for the hours allocated to partners, and what work they
3 will be doing? And just so you're aware it's 476, 370,
4 and 800.

5 And then can you explain your fee proposal and
6 your rationale for allocating staff hours consistently
7 across all 5 years?

8 MR. SMITH: I did not write down all questions,
9 so I'm going to take my stab at it from memory, sir.

10 First and foremost, I think I can speak to our
11 fee proposal and not necessarily the other 2 firms' fee
12 proposals. I do think --

13 COMMITTEE MEMBER JELINCIC: I don't expect you to
14 respond to theirs.

15 MR. SMITH: Okay.

16 COMMITTEE MEMBER JELINCIC: I just gave you that
17 so you had a background.

18 MR. SMITH: No, I appreciate that.

19 One of the things that I have struggled with
20 since responding to -- or we have struggled with since
21 responding to your RFP is defining exactly what you were
22 asking for within the RFP.

23 One of the things that you asked for was for us
24 to price only the audit of the basic financial statements,
25 and not the audit or the support or the audit schedules as

1 it relates to those employer's schedules.

2 I can tell you that that creates a level of
3 confusion in -- for 2 primarily -- 2 primary aspects.
4 First and foremost, one of the central tenets within an
5 audit, it's all professional judgment, but it is very much
6 based upon your concept of materiality. We all know that
7 there are potential errors within the financial
8 statements. But what level of materiality would cause one
9 of your stakeholders to reach a different decision about
10 the credit worthiness, the sustainability of CalPERS?

11 So working with management, as well as applying
12 our own professional judgment, we have to deem to -- what
13 we believe to be a material error.

14 Now, where -- that's one of the first areas that
15 each firm can differentiate from themselves, what level of
16 granularity they're providing from an assurance
17 standpoint.

18 The other one is interestingly enough in about
19 2013, the AICPA published or promulgated audit -- the
20 clarity standards, particularly as it relates to group
21 audits. And one of the things that it said is any time
22 you have numerous components within a group, your risk of
23 material error goes up because you're applying an overall
24 group materiality when you should be applying a much more
25 granular level based upon the components.

1 Based upon my understand -- our understanding of
2 the CalPERS, I believe that PERF A, B, and C meet the
3 definition of a component, and therefore require a lower
4 level of materiality than what I might actually apply in
5 the audit of the overall CalPERS system.

6 In a traditional audit, if asked to opine upon
7 the basic financial statements, as well as the GASB 68, I
8 ultimately arrive in the same place, because I'm opining
9 at a lower level once I get to those schedules. But in
10 order to opine upon the basic financial statements, I
11 believe I've got to lower my materiality in order to
12 provide a certain level of assurance on the individual
13 columns.

14 I think another area where many people have
15 missed the boat as it relates to GASB 67 and 68,
16 particularly as it relates to PERF B and C, there are
17 significant financial statement disclosures embedded
18 within your financial statements, which are an integral
19 part of your financial statements. The census data that
20 we often hear about as it relates to GASB 68 also applies
21 to your financial statements because of those footnote
22 disclosures. So bifurcating between what was the price
23 for the basic financial statements, what is the price for
24 the additional procedures was very, very difficult.

25 We made our best estimate as to what we believed

1 was necessary in order to opine upon the basic financial
2 statements only. One could argue that there are
3 procedures that I believe necessary to -- or that we
4 believe necessary to opine upon that level will ultimately
5 also benefit the GASB 68 schedules. And perhaps an all-in
6 price is not dramatically different, but we did our best
7 estimate and we stand by the hours that we believe were
8 necessary in total.

9 In addition, one of your questions was related to
10 the partner level. You guys are a very complex,
11 sophisticated organization with vastly different agent,
12 multiple employer, cost-sharing plans following both
13 California code, GAS -- the various GASBs and Internal
14 Revenue Code requirements.

15 Again, this is not an audit we believe that are
16 performed by 3 and 4 year -- 3 and 4 year college -- 3 or
17 4 year -- professionals 3 or 4 years out of college.

18 We have significant partner involvement, and we
19 think it's necessary for the audit that you need from a
20 fiduciary standpoint.

21 Brenda, I'm sure I forgot several of the
22 questions, so help me out.

23 MS. TORRES: No. Thank you, Kevin. I was just
24 going to add and really support Kevin in his response.
25 We've drawn on similar experience, so it's not like we're

1 coming into this CalPERS proposal without having audited
2 similar organizations. And what we have found is that the
3 leadership of a team, as deeply specialized as we are, is
4 best adept at working with your organization and really
5 driving an effective and efficient audit process.

6 Aid so therefore, our leverage model may look a
7 little bit different, but we believe our results -- we
8 stand behind our results and we'll be able to meet timely
9 deliverables, and we'll have accurate financial reporting
10 to do so.

11 COMMITTEE MEMBER JELINCIC: And the one part that
12 you didn't address was the fact that the allocation of
13 staff was consistent through all 5 years.

14 MS. TORRES: The allocation of the staff hours
15 were consistent?

16 COMMITTEE MEMBER JELINCIC: Yeah, I mean, I would
17 have expected some ramp-up the first year, but -- and it's
18 just not there and I'm just wondering why?

19 MR. SMITH: We try to -- there are -- there are
20 definitely always first-year costs, but we try to
21 estimate, okay, so what will this audit take in years 2,
22 3, 4, and 5? We tend -- we price -- or base our hours
23 upon that belief versus a ramp up and a ramp down.

24 In essence, that means that we are -- in my mind,
25 we eat the first year cost.

1 COMMITTEE MEMBER JELINCIC: Thank you.

2 MS. TORRES: I guess I would also add to that,
3 that in our experience we don't necessarily expect the
4 status quo from CalPERS on an annual basis, meaning that
5 we also anticipate you to make changes within your
6 investment portfolio, perhaps in your actuarial
7 assumptions, new laws and regulations that are past that
8 impact the system in a very profound way.

9 And so, again, we think that senior level
10 leadership is important to navigate through that. And so
11 we account for that as we look at the entire allocation
12 over the 5 years.

13 COMMITTEE MEMBER JELINCIC: Thank you.

14 CHAIRPERSON LIND: Thank you.

15 Mr. Lawyer has the final question. You need to
16 push your button.

17 Okay. Allan, you can have the final question.

18 ACTING COMMITTEE MEMBER LOFASO: I'm happy to.
19 Thank you, Mr. Chairman. Am I on? Yeah, I'm on.

20 You've alluded to a little bit of this, but if
21 you would please expand on your experience in auditing
22 different classes of investments?

23 MR. MOORE: So as I mentioned earlier, I
24 supervise the firm's centralized pricing desk that covers
25 the full gamut of investment securities that all of our

1 clients firm-wide coast to coast hold for valuation
2 testing. More specifically, the first aspect that we
3 would have to understand is how the system prices those
4 varying classes of investment securities, and how that
5 stands relative to GASB 72.

6 And then from within that, we would test the
7 system's processes for assigning and arriving at those
8 values. Global equity securities are fairly
9 straightforward, in that they're compared to trades on an
10 exchange that are fairly readily available. Fixed income
11 securities are frequently priced from pricing services,
12 and those we would test ourselves or we utilize an
13 external specialization -- an external valuation
14 specialist for fixed income securities that we've had a
15 relationship with for, I think, the last 14 or 15 years
16 that uses their own proprietary models.

17 The more challenging areas would be private
18 equity and real estate. And that, again, would be
19 directly dependent upon how the system prices those types
20 of instruments. There are a variety of techniques and
21 ways to do that. For example, with the private equity you
22 can use -- even on multiples, or you can use audited
23 financial statements at fair value, or fund manager's
24 valuations at fair value. Ultimately, we would need to
25 understand how the system does that, first, before we

1 proceed into the details.

2 MS. TORRES: I would just add to Chris that our
3 audit approach is really based on understanding the
4 investment classification and applying a risk assessment
5 across each investment classification, and then deploying
6 a sampling model to perform our testing, thinking that
7 there's a higher risk associated with the hard-to-value
8 investments, a lower inherent risk for the global
9 equities, and those that are publicly traded, so in the
10 event that you find differences, you're not extrapolating
11 those differences across the entire portfolio. We found
12 that method to be extremely impactful when evaluating
13 audit differences.

14 CHAIRPERSON LIND: Thank you very much. That
15 concludes your interview today. We appreciate you being
16 here with us tonight. And I particularly again want to
17 apologize for the delay and thank you for your patience.

18 MS. TORRES: You're welcome. It's been a
19 pleasure to be here. And thank you very much.

20 CHAIRPERSON LIND: So we'll ask you to leave the
21 auditorium please.

22 And if staff can find the Grant Thornton folks
23 who are waiting in the wings.

24 All right. It looks like everybody is settled
25 in. I want to welcome Grant Thornton to the process.

1 Just a reminder, we're going to have 10 minutes for your
2 presentation. There's a clock in front of you. Then
3 we'll have a 20-minute question-and-answer session. The
4 clock will begin when you start speaking. Just a heads
5 up, you've got to push a little button to make your red
6 light turn on. So who's ever up first. Looks like you.
7 Please feel free to start.

8 MR. BARRON: Good evening, Chairman Lind, and
9 members the Risk and Audit Committee. We thank you, first
10 of all, for the opportunity to be here with you today. We
11 are pleased to present our qualifications and experiences
12 with you today.

13 We know how important this process is to you and
14 understand that changing an auditor can be difficult. And
15 we are here to demonstrate Grant Thornton's experience and
16 qualifications, and also the qualifications and experience
17 of our team members -- our key team members that are here
18 to -- that can help with a transition to make it seamless
19 and an easy transition.

20 I'm Dan Barron. I'm the engagement partner,
21 audit partner from our Dallas office and will serve as the
22 lead engagement partner for CalPERS. I've had extensive
23 experience working with State and local governmental
24 entities. I've spent my entire career working with State
25 and local governmental entities, and pension plans similar

1 to CalPERS, including the State of Texas, City of New
2 York, City of Dallas, City of Phoenix, and City of
3 Dallas's Employees' Retirement Fund.

4 With me today, we also have many of our key team
5 members. And we have carefully selected these team
6 members based on their professional experience and
7 qualifications, along lines of verticals that align with
8 your risks. We have actuaries. We have investment
9 experts, IT experts, and as well as governmental
10 accounting and auditing experts.

11 As I said, we have carefully assembled this team
12 to best serve CalPERS. With me today is Jeff Burgess to
13 my left who is our national partner, lead practice
14 partners for our audit services for the firm. To my right
15 is Brett Schwab who will serve as our lead actuary for the
16 firm. And to his right is Jack Reagan who will serve as
17 our engagement quality review partner.

18 We also have a number of other members of our
19 engagement -- key team members of our engagement team as
20 well here. They have all been selected for their
21 qualifications and experience and their practices in their
22 fields, and really are here to answer any questions we
23 may -- you may have for us and also to serve CalPERS in
24 the future, if selected. Bios for all of our team members
25 are available in our proposal.

1 One of the questions you're probably asking right
2 now is why Grant Thornton? What makes us different than
3 our competition? What makes us better?

4 We know that we are the highest bidder, and we
5 believe that we provide the value commensurate with those
6 fees. We believe we are worth our fees.

7 One thing that we want to show today is that we
8 can provide that value a number of ways. One of the ways
9 we would do is bring in a fresh perspective, new ideas,
10 innovative ideas. A fresh perspective is very important,
11 having dealing in the auditing world and we know that
12 that's critical.

13 We also bring a breadth and depth of knowledge
14 and experience, qualifications from a national firm. We
15 bring credibility. We are known and we are trusted in --
16 broadly in the markets, and we have a national reputation.
17 With that firm -- with our national firm, we can bring
18 that breadth of experience to CalPERS. We also will bring
19 industry insights and access to resources that we have
20 within our national firm.

21 At Grant Thornton, we value the public sector.
22 This is a focus of our firm. As a \$1.6 billion firm in
23 the U.S., we are the 5th largest firm in the United
24 States, and have committed and invested a significant
25 amount of resources in the public sector. This is not

1 part-time work for us. This is not a hobby of ours like
2 other firms. This is a significant focus of what we do in
3 our firm.

4 We have invested in nearly over 850 professionals
5 that serve federal, State, and local governmental entities
6 in the United States. And these people spend 100 percent
7 of their time committed to this industry. We have worked
8 with CalPERS, CalSTRS, and at the federal level, the PBGC,
9 which ensures private sector plans.

10 We also have a footprint in California. We have
11 6 offices in California, including right here in
12 Sacramento with over 575 personnel in the State, and over
13 325 auditors in the State of California.

14 And with that, I want to turn it over to Jeff
15 Burgess to talk a little bit about audit quality.

16 MR. BURGESS: Thank you, Dan. I am absolutely
17 delighted to be here. And on behalf of the senior
18 leadership team of Grant Thornton. I want to thank you
19 for the opportunity to present our proposal.

20 As Dan alluded to the public sector is very
21 important to our firm. It's important to our strategy,
22 and we're very excited about the opportunity. And I think
23 that you would absolutely be a very important client for
24 Grant Thornton.

25 In our firm, quality is the foundation for

1 everything that we do. It really drives our reputation,
2 our brand. It drives everything that we do. And I think
3 that the first part of a quality audit is really getting
4 to understand your risks, and your challenges. And I
5 think our team has done a pretty good job of doing that.

6 Among the numerous risks and challenges you face,
7 certainly a number of new accounting pronouncements,
8 challenges with respect to your discount rate, your
9 actuarial assumptions, the investment yields.

10 Those risks and challenges will be the focus of
11 our audit. We will challenge the status quo. Our
12 processes really drive us to take a deep look at your
13 internal controls, your actuarial assumptions, your
14 investment valuations, and the transparency and quality of
15 your financial reporting and disclosures.

16 Our team will draw on the vast experience that
17 they have working with other major benefit plans and
18 municipalities, and use that information to help our audit
19 and to help us provide value to you.

20 In the end, we're going to give you an honest
21 assessment. We're not going to tell you what you want to
22 hear necessarily, but we will tell you what we think you
23 need to hear. That's the fabric of our culture. That's
24 how we bring fresh perspective. That's how we add value.

25 So how do we do that?

1 It's through our people. It starts with our
2 people. Our partners and our team are deeply committed to
3 the industry. They all have substantial experience and
4 has seen firsthand how others do it. Our key leaders in
5 your risk verticals are all experts in their field, but it
6 doesn't stop with the engagement team. They're supported
7 by our firm, a strong industry program, a national office
8 a hundred strong who are invested in the industry, who sit
9 on key panels that set the standards for the industry,
10 manage the regulatory environment. And that really keeps
11 us on the leading edge and enables us to bring those
12 insights to you.

13 And the end of the day, I know this team. I know
14 they're capable and they're committed to deliver a high
15 quality value-added audit to CalPERS. I'm confident that
16 they'll do just that, and they'll do it timely,
17 transparently, and with minimal surprises.

18 I now want to turn it over to Brett Schwab to
19 talk about our actuarial services.

20 MR. SCHWAB: Well, thanks, Jeff. I'm the lead
21 actuary at Grant Thornton. And I'm headquartered in the
22 Chicago office. And I'm very excited to be back in the
23 Sacramento area. You know, I perform valuations for a
24 number of public sector organizations here in California.

25 And you probably have realized that we're the

1 only firm that you're going to be speaking today in this
2 regard that is dedicated, invested in having an in-house
3 actuarial practice, right? So we have an in-house
4 practice that performs these services to our clients.

5 Now, we present to boards, right, around changing
6 accounting standards and the likely implications. We
7 write papers. We lead webcasts. Recently, we led a
8 webcast and partnered with Pension360, who represents
9 those interested in public pension plans, around the --
10 around implementing GASB 67, 68, and the likely -- the
11 likely implications of that.

12 You know, in addition, we have subcontracted with
13 Segal that adds an additional layer of expertise and
14 resources that -- you know, because they're the largest
15 actuarial firm out there that focuses in the public
16 section -- the public sector work.

17 So the actuaries that would be assigned to this
18 engagement have decades of experience each individually.
19 And so I am the lead actuary in charge of project
20 management. And to make sure that the works that we do
21 follows our established peer review process, and also is
22 in accordance with the actuarial standards of practice.

23 Okay. Now, my actual group, and Segal, also
24 provides support for public sector audit clients. And we
25 assist in the review of assumptions, the methods, and the

1 procedures, so that we can make sure that -- that your
2 valuations are in accordance with the applicable
3 standards, and, of course, the actuarial standards of
4 practice.

5 And we have a big -- you know, you can see our
6 commitment to the public sector from this graph here.
7 Segal audits many states and their applicable pension
8 plans. Grant Thornton audits 5 of the 10 largest cities.

9 MR. BARRON: Thank you, Jeff. Thank you, Brett.

10 In summary, I just want to sum up that we believe
11 that Grant Thornton -- we don't believe -- we know that
12 Grant Thornton is the firm of choice. We have the perfect
13 balance. We bring the national perspective of a large
14 firm, but we're going to treat you as a small firm would.
15 We're going to treat you personally and you're going to
16 have a lot of partner and manager involvement from us, and
17 you're going to have excellent client service because of
18 that.

19 CHAIRPERSON LIND: Thank you for your
20 presentation. Perfect timing.

21 We're going to move on to the question-and-answer
22 session. And the first question is from Ms. Taylor.

23 COMMITTEE MEMBER TAYLOR: Thank you all for your
24 presentation, and thank you for being here so late. My
25 question is describe financial statement audits you have

1 performed for large organizations with complex investment
2 services similar to CalPERS?

3 MR. BARRON: I'll take that. I'll start and
4 then -- we audit a lot of State and local governmental
5 entities, a lot that have very diverse portfolios of
6 investments. We are very familiar with these type of
7 entities. Some of these entities include some large
8 municipalities, some other pension plans as well that have
9 all sorts of different investment risks similar to
10 CalPERS.

11 We -- and I don't know if, Tim, if you want to
12 add anything to that on our investments.

13 MR. LEE: With respect to investments, you know,
14 in addition to what Dan pointed, it's also worth
15 mentioning that we have done portfolio focused investments
16 for, perhaps the most prominent example is PBGC, where we
17 audit -- sorry, where we provide valuations of large
18 portfolios of often complex investments.

19 CHAIRPERSON LIND: Tim, for our record, what's
20 your last name, please?

21 MR. LEE: Tim Lee.

22 CHAIRPERSON LIND: Thank you.

23 Okay. Next question is Ms. Hollinger, who has to
24 push her button.

25 VICE CHAIRPERSON HOLLINGER: Thank you, and thank

1 you for being here so late.

2 Describe your knowledge and experience related to
3 auditing large and complex pension funds, including
4 implementation of GASB 67 and 68.

5 MR. BARRON: Yeah, I'll start -- I'll start that.
6 We -- as we have mentioned previously, we do audit public
7 employee -- other public employee pension systems as well
8 too. We are very familiar, not only from the pension
9 plans themselves, as far as GASB 68 -- 67 implementations,
10 but we are also familiar with the employer side of things
11 with the implementation of GASB 68 as well too. We audit
12 a number of municipalities and other State and local
13 agencies -- governmental agencies in the State of -- or
14 throughout the nation as well too.

15 So we are very familiar. Some of those include
16 the City of New York, City of Dallas. We also audit
17 the -- a number of employee retirement funds as well too,
18 where we helped our clients implement GASB 67 and GASB 68
19 as well too. A lot of our municipalities we do work with
20 large pension systems and State systems as well too, so we
21 are familiar from both sides of that as well too.

22 So I don't know if, Vanessa, you want to add
23 anything to that.

24 MS. BURKE: Yeah. Now, you can hear me. Sorry
25 about that.

1 Yeah, I would say -- I would just like to add on
2 to Dan's that I actually used to be auditor here at
3 CalPERS, early days, back in the late nineties, and was
4 your audit manager for 5 years here when I worked with
5 PricewaterhouseCoopers, so I'm familiar with your pension
6 plan, as well as I'm working currently on the City of San
7 Jose audit. And so, you know, their pension plan has been
8 in the news lately, and we are the auditors for San Jose's
9 pension plan.

10 CHAIRPERSON LIND: What's your last name,
11 Vanessa?

12 MS. BURKE: Burke.

13 CHAIRPERSON LIND: Thank you.

14 Okay. Ms. Mathur.

15 COMMITTEE MEMBER MATHUR: Thank you, Mr. Chair.

16 So please share your experience working with
17 subcontracted health and long-term care actuaries in
18 performing audits, and the number of years that your firm
19 has worked with them. And if you could also describe your
20 firm's actuarial experience to conduct this audit. I know
21 you've mentioned some of -- some of that already. And
22 then finally if you have any experience with integrated
23 reporting that incorporates sustain -- material
24 sustainability, governance factors into financial
25 statements, I'd appreciate that as well.

1 MR. BARRON: Okay. Well, this one I'm going to
2 turn over to our actuaries here that are part of our team.
3 And we did bring our subject matter experts in this, so
4 I'm going to turn it over and, Brett, let you answer that.

5 MR. SCHWAB: Yeah. Well, like I said, we have a
6 wealth of experience -- thank you. We have a wealth of
7 experience, you know, helping -- helping our audit teams.
8 You know, basically we audit valuations and the
9 assumptions, and the methods, procedures that are used by
10 outside actuaries in performing the valuations for the
11 pension schemes and also the health schemes.

12 So we're very comfortable with the GASB 67, 68,
13 the upcoming changes for the GASB 74, 75, because we
14 help -- we help our audit teams understand that as well as
15 consult with our audit clients around those implementation
16 issues.

17 I think that I'd also like to have Brad speak on
18 that.

19 MR. RAMIREZ: Sure. My name is Brad Ramirez for
20 the record. I'm with Segal, so I'm the outside actuary
21 that they speak of.

22 I -- we do have a lot of experience, and -- as
23 part of this relationship. I think it's -- you know, one
24 of the things that we've learned -- that I've learned
25 personally in doing my own consulting with retirement

1 systems has been how important the communication has been
2 with the implementation of 67, 68, not only the
3 communication between employers and systems, employers and
4 employees, but also between systems actuaries, employers
5 actuaries, and auditors.

6 So, I mean, that's something that we've really
7 gotten used to, I think, in the last few years, something
8 that we had to learn to do.

9 MR. BARRON: Now, although we are partnering with
10 Segal on this as subcontractors, you know, this all under
11 the Grant Thornton umbrella. So we -- you know, we all
12 worked cohesively as a team here, and -- in this audit and
13 in performing our audit. So it is one integrated audit.
14 As much as possible we do try to, you know, work together,
15 but -- in looking at your assumptions and auditing the
16 assumptions.

17 And at the end of the day, this all comes back to
18 one team, one opinion, and getting the financial
19 statements material correct at the end of the day.

20 So hopefully that answers your question.

21 COMMITTEE MEMBER MATHUR: That answers the first
22 part of my question. The second part of my question was
23 about integrated reporting and material sustainability
24 factors, et cetera, and whether you have any experience in
25 that type of reporting?

1 MR. REAGAN: Dan, I can take that one.

2 MR. BARRON: Okay.

3 MR. REAGAN: Hey. I'm Jack Reagan, R-e-a-g-a-n.
4 No relation. Partner at Grant Thornton.

5 You know, we've been working very closely. We've
6 got a member of the auditing standards board from our firm
7 that is working through the different sustainability
8 issues that are out there and how auditors report on it.
9 Certainly an emerging area.

10 And, you know, so we are getting, you know, the
11 information straight from the standard setters internally
12 and getting updates from -- from that team monthly. You
13 know, Jeff mentioned earlier the 100 plus people that
14 we've got in the national office. We've got that regular
15 communication back and forth. But by having us as your
16 auditors, you'll have a voice on the auditing standards
17 board to help advance, you know, some of your thoughts and
18 issues. But it's certainly something that is emerging.
19 It's changing, you know, monthly as we go through this.

20 COMMITTEE MEMBER MATHUR: Thank you.

21 CHAIRPERSON LIND: Mr. Jelincic.

22 COMMITTEE MEMBER JELINCIC: Looking at the fees,
23 it's not clear you're all bidding on the same thing.

24 How did you come up with your proposed number of
25 hours identified in your fee proposal? And just so you

1 have a context, the others were at 3,856, 10,127, and
2 6,757. And the subpart, how did you -- what's your
3 rationale for the number of hours allocated to partners,
4 and what will they be doing. And again for context, it
5 was 476, 370, and 800. And the third part of the question
6 is explain your fee proposal and your rationale for
7 allocating staff hours consistently across all 5 years?
8 And again just for context it's 1,113, 3,536, and 2,400.

9 MR. BARRON: Yeah, I'll start that and then I'll
10 ask Vanessa help me answer that question. But really what
11 we did is -- and I can't speak for the other firms. What
12 we do is we try to evaluate, based on the information that
13 we have, public information, limited information about
14 CalPERS. You know, we weren't able to come and talk with
15 everybody that we would might want to do, but we used the
16 information that we had to best kind of take a bottoms-up
17 approach to try to identify where are the risks, and what
18 scope, what effort is it going to take for us get
19 comfortable to issue a financial statement opinion. So we
20 really build a detailed budget from the ground up.

21 When you talk about allocation of our staff,
22 partner/manager, we definitely make sure -- ensure that
23 we've got the right mix partner, managing directors, and
24 directors involved in that, so that we do have enough of
25 that involvement, because there are a lot of critical

1 areas and critical issues that CalPERS deals with.

2 And so we do take that approach where we're
3 building our budget and our scope and really looking at
4 all the information that we have available to come up with
5 our best hours of scope.

6 Once we do that, we really look at, okay, what's
7 a -- what we would call a fair fee, fair rate that is
8 really mutually beneficial to both parties? And that's
9 where we've applied to that initial scoping or the initial
10 hours of the engagement. So that's kind of how we built
11 it up.

12 And hopefully that answers your question. If
13 not, Vanessa, you have a little bit more to add to that?

14 MS. BURKE: Yeah, I can add to that. Obviously,
15 you underwent your GASB 68 implementation, and so there --
16 in your first year of implementation there would have been
17 additional hours in that year, but we think that you're
18 going to roll into your year 2 of GASB 67, 68. There's
19 going to be some roll-over in our current year for that,
20 so we had to anticipate some things that we might know.

21 One of the things we do know is you have provided
22 actuarial valuations a year ago. Now, you're in this year
23 rolling forward and essentially, you know, giving
24 information out to the employers saying that, you know,
25 they're going to have to come up with their own actuarial

1 valuations at this point.

2 At that -- you know, last year, you had a really
3 hard look at your numbers with the actuaries in there.
4 Now, it's more of a roll-forward number. So in looking at
5 your unfunded liabilities as kind of a substantial number
6 in your financials in your disclosures, it really takes
7 kind of a higher level.

8 Yes, we'd like to work with a more leverage
9 model, but we think that having 30 percent or more of our
10 partner and managers directly here in the field working
11 with you, you're a complex organization, so yes, our hours
12 are much more leveraged probably higher towards that area.

13 In addition, we allocated substantial time to the
14 actuary. You lost your Chief Actuary recently. You have
15 a great department. He retired, but essentially you're
16 going through a key change there in your actuarial
17 department as well.

18 So any time there's changes with key personnel
19 within the organization, and as well adding on top of that
20 a new CEO added to the ranks, there's always some turnover
21 and change that we're going to have to look at. And you
22 work with the auditors in that.

23 In context of keeping the staff hours flat over
24 the next several years, you know, we would anticipate that
25 we would have a bump in hours for the OPEB implementation,

1 though it looks like you're early implemented that
2 already. So we're anticipating to keep our hours flat
3 with our staff, given the fact that there isn't anything
4 in the horizon coming on for auditing standards that we
5 think is substantial. You've already overcome your GASB
6 72 issues. So we're thinking once we get through the
7 hump, we can kind of level our staff out.

8 CHAIRPERSON LIND: Thank you. You mentioned that
9 we're a complex organization. So can you describe how
10 you'll ensure flexibility and responsiveness to changes in
11 CalPERS business risks, operations, programs, systems, and
12 controls?

13 MR. BARRON: Sure. I can start with that.
14 Really, the key here is understanding the organization,
15 being there. You know, we obviously keep our independence
16 and bring that fresh perspective, but we also see here --
17 you know, we know we report to the Board. We report to
18 the Audit and Risk -- Risk and Audit Committee. And so,
19 you know, we want to be involved in what's going on. We
20 want to know what's going on, where the risks lie, where
21 we're going to focus our attention on.

22 And I think that's what -- it's all about
23 communication, about understanding, about being out here
24 on a day-to-day basis and really understanding the
25 organizations and the risks there, and managing those

1 risks, and seeing how they could potentially affect the
2 financial statements -- materially affect the financial
3 statements.

4 MR. REAGAN: Well, and, Dan, to add to that, I
5 mean, that's why we created this leverage model. You
6 know, having such a large -- as Vanessa talked about,
7 having such a large percentage of our time at the partner,
8 managing director, senior manager, manager level allows us
9 to put that seasoned judgment. You've got a couple 100
10 years of governmental auditing experience here at the
11 table in front of you.

12 That's the type of experience you need to be
13 nimble in an organization of your size and in this
14 relationship with the complexities that are going to exist
15 in the audit.

16 CHAIRPERSON LIND: Thank you. And Mr. Lofaso has
17 our final question.

18 ACTING COMMITTEE MEMBER LOFASO: Thank you.

19 CHAIRPERSON LIND: I'm not seeing your name on my
20 screen yet.

21 COMMITTEE MEMBER TAYLOR: You're pushing mine.
22 (Laughter.)

23 CHAIRPERSON LIND: Try another button.
24 There we go.

25 ACTING COMMITTEE MEMBER LOFASO: Technical

1 difficulties.

2 Good evening, everybody. Would you please expand
3 on your experience with auditing various types of
4 investments.

5 MR. BARRON: Sure. The first thing we do is
6 obviously understand your process. And these are yours
7 and management's financial statements. And we're going to
8 get an understanding of what process management has in
9 place to value. Obviously, we look at existence by
10 confirming investments. But the bigger risk really is in
11 the valuation, primarily with your harder to value
12 investments.

13 And after we identify the process, gain an
14 understanding of management's process, then we go and
15 verify and do our own valuation testing on those to
16 determine whether those estimates are reasonable, and that
17 the methodologies are reasonable to. And because this is
18 such a significant risk and a significant focus of what
19 you do, you know, we do have our investment experts,
20 subject matter experts that are part of our engagement
21 team as well too. And I'll let Tim kind of expand a
22 little bit more on auditing investments as well to you.

23 MR. LEE: As far as --

24 CHAIRPERSON LIND: Push your button, Tim.

25 MR. LEE: There we are.

1 You know, as far as auditing investments, I can
2 point you to the direct experience we have auditing
3 sizeable portfolios. Again, perhaps the largest most
4 prominent example is the extensive work we've done for the
5 Pension Benefit Guarantee Corporation in the federal
6 government, you know, large pension assets that's, you
7 know, perhaps the most directly -- directly comparable
8 example.

9 But I think it's very important that, you know,
10 the fact that we have such a deep bench that -- you know,
11 that we're a global firm. We work with a wide range of
12 clients, including -- you know, including private equity
13 firms, including private sector portfolio managers. And
14 so, you know, what we -- you know, what we bring from that
15 and what we can offer for you is the experience of a
16 unified firm and a range of perspectives, and a deep bench
17 of expertise in -- you know, in everything from, you know,
18 very -- you know, very basic plain vanilla equities, all
19 the way up to the -- you know, the complex private equity
20 investments, and the -- you know, the contracts for that,
21 the structured -- the structured securitizations and
22 derivatives in which, you know, I have -- I have personal
23 experience.

24 So that -- you know, that range of -- that range
25 of experience and abilities I think is really what

1 characterizes us as a firm. I really, you know, don't
2 think anyone else you're speaking to can match that.

3 CHAIRPERSON LIND: Well, we have a follow-up from
4 Ms. Mathur.

5 COMMITTEE MEMBER MATHUR: Thank you. This is
6 getting back to the fee proposal. I note that a third of
7 your -- almost of third of your costs are listed under
8 other costs. Could you clarify what that pertains to?

9 MS. BURKE: Yes. When we put together the
10 proposal, we included our other costs for our outside
11 actuary that we're going to be using as part of those
12 costs, because we pass -- they basically bill us for their
13 services. And we anticipate those hours in -- the fee in
14 the hours. But they're not included, they're actually
15 counted as a cost of the audit.

16 COMMITTEE MEMBER MATHUR: And how many hours does
17 that represent?

18 MS. BURKE: I think we have, between our firm and
19 their firm combined, is nearly 700 hours combined between
20 the 2 firms. I know that their billing rate is going to
21 be higher. They are the -- one of the largest firms in
22 the country performing public sector experience. So they
23 are carrying, you know, typically a higher partner rate.

24 COMMITTEE MEMBER MATHUR: So for your firm, for
25 Grant Thornton, you have 300 -- in year 1, you have 321

1 hours for a total of \$72,000, and you have -- you haven't
2 articulated how many hours for the consulting actuary, but
3 it's almost \$600,000. So that's 9 times the amount.

4 MS. BURKE: Yeah, their billing rate is higher
5 than our internal billing rate for our services. In
6 addition, I think we may have had some other costs in
7 there for travel and those kinds of things.

8 COMMITTEE MEMBER MATHUR: Okay. Thank you.

9 MS. BURKE: But I could get the detail of the
10 expenses, if you needed it.

11 COMMITTEE MEMBER MATHUR: Okay. Thanks.

12 CHAIRPERSON LIND: Thank you.

13 This concludes our interview process. I want to
14 thank Grant Thornton for being with us tonight. And
15 again, I want to thank you for your patience and hanging
16 in here all day.

17 So if you'd please leave the auditorium.

18 Come on up Macias, Gini & O'Connell, and take a
19 seat. All right. Well, thank you for being here. Just a
20 reminder, you're going to have a 10 minute presentation,
21 then we're going to have a 20-minute question and answer
22 session. And the clock on your presentation will begin as
23 soon as you start speaking, so feel free to proceed.

24 COMMITTEE MEMBER JELINCIC: And encourage them to
25 tell them -- identify themselves.

1 CHAIRPERSON LIND: And 2 little tips, be sure to
2 identify yourself when you speak, and press the button to
3 turn your mic on.

4 There you go.

5 MS. WALSH: Am I on?

6 Yes. I am.

7 Hi. Good evening, Mr. Chairman and Committee
8 members. I am Caroline Walsh and I would serve as your
9 engagement partner on the CalPERS audit. I have
10 previously served for the last 5 years as the technical
11 review partner. I have assembled the interview team. And
12 David and I will focus on the introductory remarks, but
13 the other team members are here in the event that you have
14 some detailed audit related audit scope type questions.

15 And with that, I'd like to pass it off and we'll
16 do brief introductions of who we are and then we'll get
17 started with our introductory remarks.

18 MR. BULLOCK: I'm David Bullock. I'm the
19 consulting partner on the engagement. I've been with MGO
20 for over 20 years, and I'll be assisting Caroline.

21 MR. JAZAIE: I'm Ric Jazaie. I am the consult --
22 information technology consulting director and I'll be
23 working with the team

24 MS. OLIVER: I'm Marilyn Oliver --

25 CHAIRPERSON LIND: You forgot your button,

1 Marilyn. Thank you.

2 MS. OLIVER: Oh. Thank you.

3 I'm Marilyn Oliver. I'm the head of the
4 actuarial team that supports MGO in the audit. I've been
5 working on the audit for the last 10 years.

6 MS. CHAN: My name is Debbie Chan, and I'll be
7 the director on the engagement. I've been with the firm
8 for over 17 years.

9 MR. HARNER: I'm Craig Harner. I'm the senior
10 manager with MGO on the engagement. And I've been serving
11 CalPERS for the last 5 years.

12 MS. COCHRAN: I'm Leah Cochran. I am the manager
13 on the engagement and I've been serving CalPERS for 4
14 years.

15 MR. BURTON: Roger Burton, actuary.

16 CHAIRPERSON LIND: Missed your button, Roger.

17 I think you might be pushing the wrong one.

18 There you go. You're on.

19 MR. BURTON: Okay. Tricky button.

20 Roger Burton, actuary, and I will be reviewing
21 the I liabilities for the health and long-term care plans.
22 And I've been working on the current engagement for 3
23 years.

24 MS. WALSH: Thank you.

25 We'll proceed into the -- our introductory

1 remarks. And what we will attempt to do is to highlight
2 the 3 value propositions that create the MGO advantage in
3 serving you, or continuing to serve you on this audit.

4 First, I'd like to mention that institutional
5 knowledge is, in fact, a very good thing. I think it's
6 critical to performing, what I refer to as, a smart audit,
7 where you have identified appropriate risks and focused on
8 those risks in conducting your audit. And I also think it
9 creates some tangible benefits to the -- to CalPERS as a
10 result of having that institutional knowledge.

11 You know, because of our years of experience
12 here, we think we have an unmatched understanding of
13 CalPERS and the organization, of the governing law that
14 provides the guidance in what CalPERS can do. We call it
15 the PERL. You're quite familiar with it.

16 We're also familiar and keep on top of, you know,
17 emerging issues. We are -- we understand and know the
18 recent legislation at the State level, where they would
19 like to get transparency in reporting fees -- and
20 performance fees, carried interest, and the like that are
21 coming out of private equity funds, and that will require
22 CalPERS to publicly disclose that information, based on
23 certain criteria for the public equity funds. It's not
24 100 percent yet, but hopefully they'll move there.

25 I am quite aware that Mr. Jelincic has been

1 espousing that for -- prior to that legislation being
2 adopted. So we're quite familiar with that.

3 We understand the IT infrastructure that
4 surrounds the financial systems used. In an audit, we're
5 concerned with all the information, how it flows up into
6 the financial statements. So we understand how
7 information flows from your financial system, to your
8 actuarial system, from your investment systems, all the
9 way up to the ultimate financial reporting.

10 Of course, we're familiar with the laws and
11 regulations governing your pension plans, not only your
12 defined benefit plans, but also your defined contribution
13 plans.

14 Quite familiar with your OPEB Trust. We
15 implemented the new standard early this year, as it
16 relates to financial reporting, and that changed what you
17 see in your CAFR this year.

18 We're quite familiar with the Health Care
19 Program, you know both the PPO self-insured aspect of it,
20 and also the HMO insurance carrier provided insurance.

21 Now, the most important thing CalPERS can do is
22 establish an effective internal control system. And we
23 understand that -- the internal control systems, not only
24 over financial reporting but over fraud.

25 Now, one of the things is the advantages all of

1 this is a reduced risk of oversight and audit failures,
2 faster startup. We can hit the ground running and
3 complete the audit with really no learning curve. What
4 does no learning curve mean? It means that, in fact, we
5 reduce the burden on management from having to, what I
6 refer to as, train the auditors.

7 So there's a lot of time -- there's a time
8 benefit for management. It allows us to present, you
9 know, valuable insights to your operations, because the
10 better you know and understand it, the better you can
11 provide some useful insights. And it also translates into
12 reduced audit fees. We can do it more efficiently and
13 more effectively with experienced individuals.

14 Now, the concept of a mandatory audit rotation is
15 certainly a concern and a discussion among boards and
16 policymakers. And evidence and analysis has shown that --
17 that in evaluating that rotation requirement, the costs
18 frequently outweigh the benefits. And there's a lot of
19 legislative action that's taken, the House bill in
20 Congress passing the PCAOB, which governs SEC-registered
21 companies cannot mandate auditor rotation.

22 Also, the State has adopted legislation as it
23 relates to local agencies, where they only require a
24 partner rotation versus a mandatory audit firm rotation.

25 So, you know, proven performance is very

1 important. You know what to expect from us. You know
2 that we provide you with very timely, very responsive
3 service, especially even during the times of these
4 sweeping changes in pension and other post-employment
5 standards.

6 We've been able to provide you over our years of
7 service with 60 -- over 60 recommendations for best
8 practices, as it relates to improving operational
9 efficiencies for the organization. We have unmatched
10 experience with very large governmental agencies. And I
11 think we've listed them here in our fast facts.

12 You know we do the City and County of Los
13 Angeles, San Diego, San Francisco, but we also perform the
14 largest federal compliance audit in the United States by
15 auditing the federal grants of the State of California.

16 Now, everybody is going to espouse that their --
17 they have quality audit work. And certainly we stand on
18 that -- that position also. But I'd like to communicate
19 to you that we can now support the fact that we do a
20 quality audit.

21 CalPERS was, in fact, selected during our last
22 peer review. And it was -- it came out with absolutely no
23 comments on it. And secondly, the person who did the
24 review was a government expert who was actually the former
25 chair of the Auditing Standards Board. So that was --

1 that supports our position as to the quality of our audit.

2 National thought leadership.

3 MR. BULLOCK: Thank you, Caroline.

4 I think one of the things that makes our firm so
5 unique is our national footprint in thought leadership.
6 You know, Caroline mentioned our clients here in
7 California, some of the largest in the western United
8 States. And we're a California based firm, with over 10
9 offices throughout the State, but we participate at the
10 highest levels of generally accepted accounting
11 principles, and audit standards nationwide.

12 We've listed here 3 different panels and boards
13 that we participate in. The expert panel is probably one
14 of the most prestigious panels for CPAs to participate in.
15 They evaluate emerging issues for accounting, reporting
16 and audit matters. The audit quality control center is an
17 outlet for CPAs that audit governments. Very important.

18 As the name suggests, their whole purpose is to
19 improve audit quality. Caroline served on that panel as
20 well as the expert panel. And then finally, the GASB task
21 force. And I think this is important, because GASB
22 establishes GAAP as you know. During that due process,
23 they look for input from stakeholders. And our firm is
24 normally asked to participate in those task forces.
25 Caroline Walsh and Rick Green were asked to participate in

1 the pension standards, because GASB wanted to get the
2 perspective of both the plan side and the employer
3 reporting side.

4 I most recently was asked to join the task force
5 on emerging -- or, excuse me, the reexamination of the
6 reporting model. So that's an example of our
7 participation nationwide.

8 And why is that important?

9 Because it provides a voice for us and our
10 clients. It makes sure that your audit team is
11 knowledgeable, and in case emerging issues arise here at
12 CalPERS, we can help you address those.

13 CHAIRPERSON LIND: Thank you for your
14 presentation. We're going to move on to the question and
15 answer session.

16 MS. WALSH: Thank you.

17 CHAIRPERSON LIND: And the first question is from
18 Ms. Taylor.

19 COMMITTEE MEMBER TAYLOR: Hi. Thank you all for
20 staying so late. Sorry, it was quite this late.

21 Describe financial statement audits you have
22 performed for large organizations with complex investment
23 services similar to CalPERS.

24 Go ahead.

25 MS. WALSH: Well, I think -- I'll take -- well,

1 you know, maybe we could speak more granularly, but
2 certainly from auditing retirement systems. And really
3 those are the ones that have complex investments. You
4 know, you go to your regular vanilla investments that sit
5 at your cities and local governments, and those are --
6 those are pretty straightforward.

7 But in talking about retirement systems, not only
8 CalPERS, we do Oregon PERS. That's probably the second
9 largest engagement we do. We do the San Diego City
10 retirement system, the Orange County Retirement System.
11 We have done CalPERS -- CalSTRS in the past. City and
12 County of San Francisco, we do their retirement system.
13 So those are -- those are some of the big retirement
14 systems that we currently do.

15 And members of our team have either been on those
16 engagements or reviewed those engagements from a technical
17 perspective.

18 So, thanks.

19 CHAIRPERSON LIND: Okay. Ms. Hollinger.

20 VICE CHAIRPERSON HOLLINGER: Thank you. Thank
21 you guys for being here.

22 Describe your knowledge and experience related to
23 auditing large and complex pension funds, including
24 implementation of GASB 67 and 68.

25 MS. WALSH: You want to take it?

1 MR. BULLOCK: Yeah. So the -- Caroline just
2 mentioned in her response that the number of pension plans
3 that we do, you know, here at CalPERS, former auditors of
4 CalSTRS, Oregon pension plans.

5 What was the second part?

6 MS. WALSH: We implemented GASB 67. Except for
7 CalSTRS, we've implemented GASB 67 at all of our plans.
8 And also the GASB 68, which is the employer concern coming
9 out of these major retirement systems. We have actually
10 worked with them, and also attendant to our responsibility
11 with CalPERS, I set on a State governmental and accounting
12 committee, and they developed a white paper that provided
13 guidance to employers in California, as it relates to
14 their participation in the CalPERS things.

15 And the community, the auditor and employer
16 community, found those -- that information very useful.
17 The goal was to help CalPERS have everybody understand how
18 to use your information, and therefore, you know,
19 hopefully mitigate the time it would take CalPERS to
20 respond.

21 MR. BULLOCK: And I would just also add that for
22 our county clients, we do a lot of counties throughout the
23 State of California, and many of them have their own 1937
24 Act county plans.

25 MS. WALSH: Yes.

1 MR. BULLOCK: And we work very closely with those
2 pension plans, while we may not have been the auditors,
3 but very closely in the implementation of 67 for them and
4 68 for our client.

5 MS. CHAN: And, in addition, our experience with
6 the implementation of GASB 68 here at the CalPERS level
7 for the past 3 years. In that audit area, we audit over
8 1,500 school districts, as well as over 1,600 public
9 agency employers, leading to the GASB 68. And that's a
10 very extensive and require a lot of resources on our end
11 to complete that audit.

12 MS. WALSH: But I should add that that's not part
13 of the basic financial statement audit. Okay. So...

14 CHAIRPERSON LIND: Thank you.

15 Ms. Mathur.

16 COMMITTEE MEMBER MATHUR: Thank you.

17 Please provide and share your experience working
18 with subcontracted health and long-term care actuaries in
19 performing audits of large pension funds like CalPERS, and
20 the number of years that your firm has been working with
21 them. I think you mentioned it's been 10 years. And if
22 you could describe your firm's actuarial experience as it
23 applies to our audit. And then finally, my -- I have
24 another question about integrated reporting and the move
25 towards more sustain -- material sustainability factors in

1 financial reporting, and any experience you might have
2 with that.

3 MS. WALSH: Do you want to handle the actuarial
4 stuff?

5 MS. CHAN: Yes. So as Caroline mentioned on our
6 engagement team, we have -- we engage actuary specialists.
7 Marilyn Oliver, she actually has been on the pension side
8 for the past 10 years. She's very knowledgeable with a
9 large California actuarial firm.

10 The way we -- we work very closely with Marilyn.
11 Marilyn's worked is directed under us, and we have weekly
12 status meeting. In addition, Roger Burt, he's the
13 specialist in the Long-Term Care and the Health Care
14 plans. Roger has been on the engagement for the past 4
15 years. And again, we work very closely with our
16 specialists. We develop audit procedures, especially
17 looking at the actuarial assumptions and methods, and
18 making sure that it is consistent with the requirement of
19 the GASB standards, as well as the actuarial standards of
20 practice.

21 MS. WALSH: And sustainability.

22 COMMITTEE MEMBER MATHUR: Yeah.

23 MS. WALSH: Well, you know what, when you talk
24 about sustainability, certainly it's probably one of the
25 primary things that retirement systems all over the

1 country are concerned about, given the level of benefits,
2 investment performance, whatever.

3 Now, as part of a financial statement audit, you
4 know, really you don't look to, you know, offer -- from an
5 operational or an advisory position.

6 COMMITTEE MEMBER MATHUR: If I could, just to
7 clarify?

8 MS. WALSH: Sure.

9 COMMITTEE MEMBER MATHUR: I'm really thinking
10 about environmental -- material environmental other -- and
11 other environmental, social, governance factors that might
12 impact the long-term performance of an organization. You
13 see it a lot sort of evolving in the corporate sector.
14 I'm just wondering if you're seeing it at all in the
15 public sector, and if you have any experience with that.

16 MS. WALSH: I guess I'm not quite sure exactly
17 what you mean.

18 COMMITTEE MEMBER MATHUR: That's fine. Okay.
19 That's all right.

20 CHAIRPERSON LIND: You stumped them, Priya.
21 It's okay.

22 Question -- fourth questions. Obviously, you
23 know from experience this is a very dynamic organization,
24 so how will you ensure flexibility and responsiveness to
25 changes in our business in risks, operations, programs,

1 systems and controls?

2 MR. BULLOCK: Well, we evaluate the operations
3 every year, as we plan the audit. And that's really the
4 important part of the planning process is to understand,
5 you know, what you're doing and what might be different
6 from the previous year, what new laws and regulations are
7 coming up, what new audit standards, what new accounting
8 standards. And so all of that goes into our risk
9 assessment, in -- you know, for the purpose of
10 identifying, you know, what needs to be addressed, and
11 what significant changes there are.

12 And so through that planning process, we would
13 identify, you know, things that are important to the
14 organization, especially, you know, with, you know, your
15 risk mitigation policies and other things that you're
16 doing, decisions that you're making that need to be
17 implemented and how it would affect your financial
18 statements.

19 MS. WALSH: Right. I think one of the things we
20 experienced this past year is the funding risk mitigation
21 policy, and how one might look at that and determine how
22 that could impact your discount rate in the future, and at
23 what point in time would you consider this something that
24 would adjust the discount rate.

25 And so we went through several -- several

1 conversations with management about understanding it, and
2 the intent of it, and the like. And we made a conclusion
3 about it in conjunction with the audit.

4 CHAIRPERSON LIND: Thank you.

5 Mr. Jelincic.

6 COMMITTEE MEMBER JELINCIC: The -- looking at the
7 fees, I mean, it's not clear that everybody is bidding on
8 the same business, and -- but the big driver was hours.
9 So how did you come up with the proposed number of hours
10 identified in your proposal? And just so you have a
11 context, the numbers were 3,856, 10,127, and 6,575. And,
12 in particular, the partner hours and what the partners are
13 going to do with those hours? And again, just for
14 context, it was 476, 370, and 800. And then can you
15 explain why your fees and rationale for allocating staff
16 were consistent year after year? You would have expected
17 some variation. And again, at least at the manager level,
18 just for context, it's 1,113, 3,536, and 2,400.

19 MS. WALSH: From the other firms?

20 COMMITTEE MEMBER JELINCIC: Those are the 3 bids,
21 but I'm interested in your --

22 MS. WALSH: Okay. There's a lot of questions
23 there, so let me --

24 COMMITTEE MEMBER JELINCIC: I'm interested in
25 your proposal and I gave you the others just so you have

1 some sort of context.

2 MS. WALSH: Sure. Well, as far as the hours
3 there, those were the actual audit hours incurred in the
4 2015 audit.

5 Now, for the 2016 audit, we are actually not very
6 far away. I think we have about 3,900 hours. So those
7 are the actual hours incurred.

8 How they may differ from the other firms, I'm not
9 sure. One of the things I do want to point out is that we
10 take advantage, under our professional standards, and use
11 the work of the Office of Audit Services. And they
12 actually are performing the census data testing for us,
13 and we are directing the scope of that work, and we review
14 that work as permitted by our professional standards. So
15 we actually don't do all the physical hours associated
16 with that, so that could be -- that could account for some
17 disparity. I don't know how the other firms interpreted
18 that, but we certainly -- we certainly have a benefit from
19 using the Office of Audit Services.

20 And from year to year, you know, right now there
21 was nothing on the horizon that would impact the scope of
22 the work. So certainly in the future, if there's any new
23 standard that would come up, it certainly would be -- need
24 to be evaluated and determined what the impact would be.

25 MS. CHAN: And more importantly at the partner's

1 level, they make a conscious decision to reduce the fee as
2 they value CalPERS as a premier client.

3 MS. WALSH: So the hours and the rates that are
4 stated are our standard hourly rates. The hours are based
5 on what we spend. Partners have a responsibility under
6 professional standards. And we must be involved in the
7 planning and risk assessment aspect of the audit. We must
8 look at all key risk areas, and review that work. And
9 certainly we're involved in the reporting aspect of it.

10 So there's 3 key areas where we must do the work.
11 And, you know, we believe we do a good job in performing
12 that work.

13 COMMITTEE MEMBER JELINCIC: Thank you.

14 CHAIRPERSON LIND: Great. And we have the final
15 question from Mr. Lofaso.

16 ACTING COMMITTEE MEMBER LOFASO: Thank you, Mr.
17 Chairman.

18 CHAIRPERSON LIND: He's on.

19 You'e on.

20 ACTING COMMITTEE MEMBER LOFASO: I am on. Okay.
21 Thank you. Thank you, Mr. Chairman. We're almost done.
22 Would you please expand on your experience in auditing
23 different classes of investments?

24 MS. WALSH: Like equities versus fixed income
25 versus private versus derivatives?

1 ACTING COMMITTEE MEMBER LOFASO: For example.

2 MS. WALSH: Yeah. Well, I think maybe Debbie or
3 Dave can talk about that because all of our retirement
4 systems have those. Yeah, so --

5 MS. CHAN: Caroline mentioned earlier, so Oregon
6 PERS is one of our other big retirement systems and has
7 very similar investment classifications or investment
8 types, and even similar investment structure. So we have
9 been the external auditors for Oregon PERS for the past 5
10 years. In addition, CalSTRS we were the past auditor for
11 the past 7 years. And again, with just very similar
12 investment classification and structures, and similar in
13 size and volume as well. So that's -- you know, those are
14 the 2 big -- our experience in that area.

15 MS. WALSH: So we would say we have a lot of
16 experience in all the investment classifications that you
17 have currently in your investment portfolio.

18 Did that respond to your question?

19 ACTING COMMITTEE MEMBER LOFASO: Thank you very
20 much.

21 MS. WALSH: Oh, okay.

22 MR. BULLOCK: I would just PROBABLY add I guess
23 that, you know, the key assertions over investments is
24 looking at, you know, existence an ownership of those
25 assets, and the valuation and ensuring the valuation is

1 properly reported. We have at times -- you know,
2 internally we feel we have a team -- and audit team with a
3 lot of experience auditing large investment portfolios.
4 And we utilize that experience on these teams. We also
5 have a greater circle throughout the State of experts in
6 investments, and that we could expand and utilize those
7 resources when needed. And then finally, we have a wealth
8 management -- wealth advisory group who are experts in
9 investments. And if we ever had the need for evaluation
10 assistance or something of that nature, some complex
11 transaction that we needed some expertise, we have a lot
12 of resources within the firm to draw from.

13 CHAIRPERSON LIND: Great. Well, thank you very
14 much. This concludes our process. I want to thank you
15 for being with us tonight, and thanks a lot for your
16 patience and hanging with us into the evening.

17 MS. WALSH: Our pleasure.

18 Thank you.

19 CHAIRPERSON LIND: So we'll ask you to leave the
20 auditorium.

21 MS. WALSH: Thank you.

22 MR. BULLOCK: Thank you.

23 CHAIRPERSON LIND: Now, we're hear so late, they
24 turned off the clock up there.

25 (Laughter.)

1 VICE CHAIRPERSON HOLLINGER: Shut the door.

2 CHAIRPERSON LIND: Almost shut. Getting close.

3 Okay. So now we have to, as a group, determine
4 the interview score for each of the finalists. The
5 maximum number of points, as a reminder is 700. The way
6 we're going to do this is just take one firm at a time and
7 see if there's any discussion, and if anybody wants to
8 motion a score.

9 So the first one was Crowe Horwath -- Horwath, I
10 guess. Any discussion or anybody want to make a motion on
11 their score?

12 Mr. Lofaso.

13 ACTING COMMITTEE MEMBER LOFASO: Thank you, Mr.
14 Chairman. I just actually want to ask a question and I'm
15 hoping it's appropriate in this procurement context.
16 Crowe Horwath gave an answer on the fee proposal that was
17 sort of revolving around, I'll characterize it as, depth
18 and scope. And I'm wondering if it's appropriate for Ms.
19 Chappuie or Ms. Eason to comment on the scope and depth
20 question? I don't know if -- are they allowed to comment
21 on this stage of the --

22 CHAIRPERSON LIND: I see a lot of head shaking
23 yes from the legal eagle over there. So who wants to come
24 up and address that?

25 CHIEF AUDITOR CHAPPUIE: Their question or

1 confusion was related to GASB 67 audits that we have a
2 letter of engagement with our current auditor MGO. And we
3 pay for that separately, and we get reimbursed from the
4 public agency. So that's not part of the basic financial
5 statement audits. So that's separate.

6 CONTROLLER MONTGOMERY: Yeah. It was GASB 68.

7 CHIEF AUDITOR CHAPPUIE: 68.

8 CONTROLLER MONTGOMERY: 68, that's separate. So
9 they -- they put it as part of this bid, so -- and then --

10 CHIEF AUDITOR CHAPPUIE: But our proposal didn't
11 require that, because it's only for the basic financial
12 statement audit.

13 CONTROLLER MONTGOMERY: That's correct. It's not
14 part of the financial audit.

15 ACTING COMMITTEE MEMBER LOFASO: Understood.
16 Thank you very much. Thank you, Mr. Chairman.

17 CHAIRPERSON LIND: Ms. Hollinger.

18 VICE CHAIRPERSON HOLLINGER: Is -- can I ask
19 staff their opinion or no?

20 GENERAL COUNSEL JACOBS: (Shakes head.)

21 VICE CHAIRPERSON HOLLINGER: Or for insight, no.

22 GENERAL COUNSEL JACOBS: (Shakes head.)

23 CHAIRPERSON LIND: I see heads shaking the
24 opposite way on this one.

25 (Laughter.)

1 VICE CHAIRPERSON HOLLINGER: So, no.

2 GENERAL COUNSEL JACOBS: I think the idea is that
3 the staff has provided its input through the scoring that
4 it's already provided, and now it's up to the Board to
5 factor that in with your own review and thoughts and
6 analysis of the interviews.

7 CHAIRPERSON LIND: Right. The staff got us to
8 this point, so we're supposed to take it from here.

9 VICE CHAIRPERSON HOLLINGER: Okay. My impression
10 was that --

11 GENERAL COUNSEL JACOBS: I'm sorry. Kim reminds
12 me that there's an executive summary in the binder.

13 VICE CHAIRPERSON HOLLINGER: Okay. Thank you.

14 My impression is -- my thoughts were this,
15 that -- I keep opening it -- our current accounting firm
16 Macias, I didn't -- I don't get the feeling they're as
17 sophisticated as these others, and maybe -- however,
18 there's such a gross price disparity, that that's hard for
19 me to get my arms around. I felt the -- I know CalSTRS
20 used the second firm, and they were with Macias. I got
21 the feeling that they were maybe a little more
22 sophisticated, could take us to the next level, at least
23 the second two, not who we're currently using. But I'm
24 not sure if it's worth such a significant price
25 difference.

1 CHAIRPERSON LIND: Right. I think we all have
2 that concern. The pricing is sort of built into the
3 process here.

4 VICE CHAIRPERSON HOLLINGER: Right, right.

5 CHAIRPERSON LIND: There's already points around
6 price.

7 VICE CHAIRPERSON HOLLINGER: Right. So does --
8 I'm curious like your thoughts, do you think any of the
9 other firms justify the increase in price?

10 CHAIRPERSON LIND: So I think we've got a bunch
11 of people with an opinion on this and other things,
12 because I'm looking at a lot of green dots.

13 J.J..

14 COMMITTEE MEMBER JELINCIC: Actually, I thought
15 they've got more responsive as they went along. Maybe
16 that's just because of the hour. But, you know, I have
17 previously said that, you know, part of my background is
18 as investment analyst. And changing auditors is not
19 something that -- is actually kind of a red flag.

20 Changing the partner -- the engagement partner is really
21 important. But there is a real advantage to having
22 somebody who's worked with the system, who knows the
23 system, who, you know, there's not a learning curve.

24 And I -- you know, they want -- quite frankly
25 they want some points by mentioning private equity. But

1 the -- I just -- one, it was the most diverse of the
2 groups.

3 VICE CHAIRPERSON HOLLINGER: Yes, I agree.

4 COMMITTEE MEMBER JELINCIC: They clearly have
5 demonstrated they can do it. The -- you know, when
6 somebody comes in and says, oh, by the way, we need 3
7 times as many hours, you kind of go huh. And then they --
8 in their presentation, they say, and oh, by the way, in
9 that other cost is another 700 hours. So I actually would
10 rate MGO first, Grant second, and Crowe third.

11 CHAIRPERSON LIND: Okay. Now, keep in mind,
12 ultimately we have to do this by points.

13 So, Ms. Taylor.

14 OPERATIONS SUPPORT SERVICES DIVISION CHIEF MALM:

15 Yeah, May I suggest though, if what I understood
16 the answer that Kristin and Beliz gave you, that they
17 included in their -- if Crowe included in their price the
18 amount to do the GASB 68, then that would be a price that
19 we would be able to negotiate out, since they are not
20 doing that work.

21 So I think that the fee differentiation will
22 probably be different, if they understand that they're not
23 providing that work. I think since they added those hours
24 in is what made their price increase.

25 CHAIRPERSON LIND: Thank you.

1 Theresa.

2 COMMITTEE MEMBER TAYLOR: So first, how much
3 would the price increase, do you think? Is that a lot of
4 hours, do you think?

5 OPERATIONS SUPPORT SERVICES DIVISION CHIEF MALM:
6 Decrease, I don't know. We would have to ask for
7 a clarification on that. I'm just saying that might be
8 the difference --

9 COMMITTEE MEMBER TAYLOR: I just maybe we'd have
10 a ballpark.

11 OPERATIONS SUPPORT SERVICES DIVISION CHIEF MALM:
12 -- between 3,000 and 6,000 hours.

13 CHIEF AUDITOR CHAPPUIE: Currently we're paying
14 MGO to \$2.5 million for -- per year for the GASB 68 audit.

15 COMMITTEE MEMBER TAYLOR: In addition to the 2.5
16 for the -- okay. So it would lower -- okay. Maybe,
17 depending on their -- how they're pricing it. So the only
18 thing I will say is if we're going by -- I don't know how
19 to do the points yet, so I'll figure that out in a minute.
20 But I will say that the only group that knew what your
21 ESG -- what you ESG was was -- they didn't have it
22 included, was Crowe. And they at least acknowledged SASB.

23 VICE CHAIRPERSON HOLLINGER: Right.

24 COMMITTEE MEMBER TAYLOR: So that is the only
25 thing. However, I like the fact that MGO is very diverse.

1 They know our system. How long have they been our
2 auditors, and is that a problem?

3 CHIEF AUDITOR CHAPPUIE: Ten years.

4 COMMITTEE MEMBER TAYLOR: Ten years. I don't
5 know that I have a problem with engaging them again. And
6 we can discuss the points later, but I just feel like -- I
7 felt like they knew our system forward and backwards. So
8 when -- I mean I had a whole bunch of notes before we even
9 started asking questions, where the other ones were so
10 broad that I didn't -- I couldn't really take notes before
11 we started asking questions on their -- on their
12 introduction. So my recommendation is MGO, but I need to
13 know how we're going to be assigning the points.

14 CHAIRPERSON LIND: Thank you.

15 Ms. Mathur.

16 COMMITTEE MEMBER MATHUR: So let me start with
17 Grant Thornton. I was not very pleased with their answer
18 to my last question about a third of their costs, which
19 they couldn't really account for or they're hiring
20 actuaries is going to cost \$600,000. It just seemed like
21 preposterous answer. And they didn't seem to have a full
22 handle on it, which really bothered me, particularly given
23 that they were -- they already knew that they were highest
24 the bidder, so they should have been prepared for explicit
25 questions about that.

1 So, to me, that's a red flag that really concerns
2 me. I did think that Crowe Horwath, if I'm pronouncing it
3 correctly, did quite a good job. I was very pleased that
4 they brought so many senior partners. I thought that
5 demonstrated a certain commitment to this engagement, that
6 they had people in each sort of -- each area that pertains
7 to this engagement. I would be very interested to
8 understand how their pricing and hours would be different
9 if they fully appreciated the GASB 68 was not included.
10 I'm a little surprised that they didn't come during the
11 staff evaluation and didn't get clarified.

12 CHIEF AUDITOR CHAPPUIE: They actually did
13 clarify that

14 COMMITTEE MEMBER MATHUR: Oh, they did?

15 CHIEF AUDITOR CHAPPUIE: They did request
16 information.

17 COMMITTEE MEMBER MATHUR: So -- but they chose
18 not to revise their fee proposal --

19 CHIEF AUDITOR CHAPPUIE: I'm not sure.

20 COMMITTEE MEMBER MATHUR: -- or they were not
21 given the opportunity to do that?

22 CHIEF AUDITOR CHAPPUIE: I remember that legal
23 responded to their question. There was a request, and I
24 can go back and double check.

25 COMMITTEE MEMBER MATHUR: Okay.

1 CHIEF AUDITOR CHAPPUIE: I'm going with my memory
2 right now.

3 COMMITTEE MEMBER MATHUR: Yeah, it would be
4 helpful to know --

5 OPERATIONS SUPPORT SERVICES DIVISION CHIEF MALM:
6 You can clarify right now, Ms. Mathur, if you
7 wanted to.

8 COMMITTEE MEMBER MATHUR: I would like to do
9 that.

10 OPERATIONS SUPPORT SERVICES DIVISION CHIEF MALM:
11 We can call them in and tell them in and tell
12 them that GASB 68 is not part of this and does this have
13 an impact on their fee proposal or on what they have put
14 in their fee proposal.

15 COMMITTEE MEMBER MATHUR: And their hours. I
16 think that --

17 CHAIRPERSON LIND: I would say just bring one of
18 them in.

19 OPERATIONS SUPPORT SERVICES DIVISION CHIEF MALM:
20 Yeah. No, we're --

21 CHAIRPERSON LIND: The one that can answer that
22 questions. Before I do that, there's 2 pieces --

23 OPERATIONS SUPPORT SERVICES DIVISION CHIEF MALM:
24 It does not change the point structure. Let me
25 be very clear that it does not change the point structure

1 of the proposal that they turned in.

2 COMMITTEE MEMBER MATHUR: Sure.

3 OPERATIONS SUPPORT SERVICES DIVISION CHIEF MALM:
4 But it would -- it could have an impact on the
5 negotiations after you do your scoring. It would not have
6 a change --

7 COMMITTEE MEMBER MATHUR: Sure.

8 OPERATIONS SUPPORT SERVICES DIVISION CHIEF MALM:
9 -- to the 300 points, or the 90 points, or the,
10 right, because that's what they turned in.

11 CHAIRPERSON LIND: That was going to be my
12 questions.

13 CHIEF AUDITOR CHAPPUIE: One thing to clarify, so
14 we will engage them to conduct this GASB 68 audits later.
15 That's going to be a letter of engagement after we sign
16 this contract. So we need to make it clear that that will
17 be a --

18 COMMITTEE MEMBER MATHUR: That's a follow-up
19 piece of work.

20 VICE CHAIRPERSON HOLLINGER: But we need the
21 other --

22 CHAIRPERSON LIND: You've got to request.

23 COMMITTEE MEMBER MATHUR: I wasn't quite done,
24 but all right.

25 VICE CHAIRPERSON HOLLINGER: Macias, if we add

1 GASB 38[sic], it brings them up to 5 million, 5½, is that
2 about right?

3 CHIEF AUDITOR CHAPPUIE: So I'm going by --
4 you're looking at the total contract, but that 2.5 million
5 for GASB 68 work is annual cost at GASB -- MGO charges us.
6 And their basic financial statement audit cost per year is
7 about fix to six hundred thousand dollars, so total
8 \$3million per year, MGO.

9 VICE CHAIRPERSON HOLLINGER: Okay. So it's
10 significantly different.

11 OPERATIONS SUPPORT SERVICES DIVISION CHIEF MALM:
12 So I got some additional input from legal staff.
13 And we would not be able to call them back in, because
14 it's a second opportunity for interviewing, and we have a
15 set time for each one.

16 CHAIRPERSON LIND: Okay.

17 OPERATIONS SUPPORT SERVICES DIVISION CHIEF MALM:
18 But we -- that would be a discussion during
19 negotiations if they are the chosen vendor.

20 CHAIRPERSON LIND: Thank you.

21 Mr. Jelincic.

22 COMMITTEE MEMBER JELINCIC: I got lost, so.

23 CHAIRPERSON LIND: Okay. Any other discussion?

24 Again, we have to do this by points. From my
25 perspective, I would rank Crowe Horwath and Macias, Gini

1 equally. We know what the outcome of that would be, but
2 that's kind of what my take would be. And I feel the same
3 about Grant Thornton being in third based on their -- some
4 of their answers.

5 Further discussion or anybody want to try a
6 motion based on points, keeping in mind how that all
7 works.

8 Ms. Mathur.

9 COMMITTEE MEMBER MATHUR: Okay. I would
10 propose -- I would move the following scores:

11 For Crowe Horwath -- Howarth --

12 (Laughter.)

13 COMMITTEE MEMBER MATHUR: I'm sorry. I'm not
14 pronouncing it right. Crowe -- yeah, for CH, I would
15 propose -- I would move 600 points. For Macias, Gini, I
16 would move 550 points, and for Grant Thornton, I would
17 move 500 points.

18 CHAIRPERSON LIND: Okay. We have a motion. Does
19 anybody want to second that?

20 VICE CHAIRPERSON HOLLINGER: Second.

21 CHAIRPERSON LIND: We have a second on the
22 motion.

23 Is there discussion?

24 COMMITTEE MEMBER JELINCIC: Yeah, I have -- it's
25 a question.

1 CHAIRPERSON LIND: Go ahead, J.J.

2 COMMITTEE MEMBER JELINCIC: Do we have 700 points
3 total to allocate? So the problem -- so we couldn't very
4 well just use that, you know, because that's 1,800 points.

5 CHAIRPERSON LIND: Per firm.

6 OPERATIONS SUPPORT SERVICES DIVISION CHIEF MALM:
7 Per firm.

8 COMMITTEE MEMBER JELINCIC: Okay. We've --

9 COMMITTEE MEMBER MATHUR: Up to 700 per firm.

10 COMMITTEE MEMBER JELINCIC: Okay. I just need to
11 get that clarified.

12 VICE CHAIRPERSON HOLLINGER: Second.

13 CHAIRPERSON LIND: Okay. So --

14 COMMITTEE MEMBER JELINCIC: What was the fee
15 score?

16 (Discussion off the record.)

17 CHAIRPERSON LIND: Kim, do you have it memorized
18 the fee scores?

19 OPERATIONS SUPPORT SERVICES DIVISION CHIEF MALM:
20 I do.

21 CHAIRPERSON LIND: Go ahead, please.

22 I got Kim on the microphone, so she can do it.

23 OPERATIONS SUPPORT SERVICES DIVISION CHIEF MALM:

24 So Crowe Horwath was 90 points for fee, 50 points
25 for DVBE incentive for a subtotal of 140. Grant Thornton

1 was 72 points for fee, 50 points for DVBE incentive, for a
2 subtotal of 122. And Macias, Gini & O'Connell -- it's so
3 late -- 300 for a fee score, 0 for DVBE incentive, for a
4 total of 300 points.

5 CHAIRPERSON LIND: Thank you. Okay. I do have
6 some discussion going here.

7 Ms. Hollinger.

8 VICE CHAIRPERSON HOLLINGER: It was an accident.

9 CHAIRPERSON LIND: That was left over.

10 Mr. Lofaso

11 ACTING COMMITTEE MEMBER LOFASO: Yeah. Sorry. I
12 just miss hit my button.

13 CHAIRPERSON LIND: Ms. Taylor.

14 COMMITTEE MEMBER TAYLOR: Did I hit mine, too.

15 CHAIRPERSON LIND: Oh, man. Come on guys.

16 (Laughter.)

17 CHAIRPERSON LIND: All right. Mr. Jelincic, how
18 about you?

19 COMMITTEE MEMBER JELINCIC: Okay. I can
20 actually -- I can -- I'm comfortable with the 600 for CH,
21 550 for MGO, and 500 for Grant Thornton. Recognize --
22 and, you know, with the fee scores that means MGO will be
23 the selected.

24 CHAIRPERSON LIND: Okay. So we're going to move
25 on with this. You all know what the motion is.

1 All in favor say aye?

2 (Ayes.)

3 CHAIRPERSON LIND: Are there any opposed?

4 Okay. That motion carries. We've got a wait a
5 minute or two to calculate the score, and the overall
6 ranking. And then we're going to -- we have a recommended
7 motion that I'm going to give to Dana. We've got to wait
8 till they give us the official total score.

9 They's allowed to be in here for this part of it.

10 Yeah. Do we want to wait for everyone to come
11 in?

12 COMMITTEE MEMBER MATHUR: We should. They waited
13 for us all day.

14 CHAIRPERSON LIND: Yeah, that's true. All right.

15 Okay. I don't see any other bodies working their
16 way towards the door, so who's going to give us the score
17 total?

18 Beliz, is that you?

19 CHIEF AUDITOR CHAPPUIE: Yes. Thank you, Mr.
20 Chair. I will now read the interview scores for each
21 finalist in alphabetical order. Crowe -- oh, they're
22 still coming.

23 CHAIRPERSON CHAPPUIE: I think there's at least
24 one person from each firm in here and the door is closes,
25 so go ahead.

1 You can proceed, Beliz.

2 CHIEF AUDITOR CHAPPUIE: Thank you, Mr. Chair. I
3 will now read the interview scores for each finalist in
4 alphabetical order. Crowe Horwath received 600 points for
5 the interview score, Grant Thornton received 500 points
6 for their interview score, and Macias, Gini & O'Connell
7 received 550 points for their interview score.

8 Combined with their preliminary total scores,
9 Crowe Horwath received a total score of 740 points, Grant
10 Thornton received a total score of 622 points, and Macias,
11 Gini & O'Connell received a total score of 850 points.

12 Ms. Chair, the finalist with the highest total
13 score is Macias, Gini & O'Connell.

14 CHAIRPERSON LIND: Okay. Okay. Do you need a
15 clarification? Could you restate it please, Beliz? I
16 think there was --

17 COMMITTEE MEMBER MATHUR: The totals.

18 CHAIRPERSON LIND: Totals.

19 CHIEF AUDITOR CHAPPUIE: Total for all 3?

20 CHAIRPERSON LIND: Yeah.

21 CHIEF AUDITOR CHAPPUIE: Yes. Combined with
22 their preliminary total scores, Crowe Horwath received a
23 total score of 740 points, Grant Thornton received
24 total -- received a total score of 622 points, and Macias,
25 Gini & O'Connell received a total score of 850 points.

1 COMMITTEE MEMBER MATHUR: Thank you.

2 CHAIRPERSON LIND: All right. And Ms. Hollinger
3 has a motion.

4 VICE CHAIRPERSON HOLLINGER: I will now entertain
5 a motion for --

6 CHAIRPERSON LIND: I'm going to entertain it,
7 you're going to make it.

8 Sorry.

9 VICE CHAIRPERSON HOLLINGER: Oh, go ahead.

10 CHAIRPERSON LIND: Yeah, go ahead.

11 VICE CHAIRPERSON HOLLINGER: I will move that the
12 Committee recommend to the Board that the Board awards the
13 contract to MGO as the highest ranking finalist subject to
14 financial negotiations and satisfaction of all
15 requirements, and direct staff to begin contract
16 negotiations for the contract with MGO.

17 If staff, in its discretion, concludes that
18 negotiations are unsuccessful, staff shall begin contract
19 negotiations with Corvette[sic] -- the next highest
20 scoring finalist. I remind all members of the Committee
21 and the finalists of the restricted contact policy under
22 Government Code section 20153. The interviews are
23 adjourned. Thank you.

24 CHAIRPERSON LIND: I get to do that part.

25 So we've got a motion on the floor.

1 COMMITTEE MEMBER MATHUR: Second.

2 CHAIRPERSON LIND: It's getting late. There's a
3 second.

4 Is there any discussion?

5 All in favor say aye?

6 (Ayes.)

7 CHAIRPERSON LIND: Any opposed?

8 That motion carries. Thank you, everybody for
9 hanging with us tonight and going through this process.
10 It's late and we still have a lot of work to do.
11 So thanks everybody.

12 Anything else that we need to do on this, Beliz?
13 We're done for now, right, on this item?

14 Okay. Good. Oh, we have some more on this.
15 Okay.

16 CHIEF AUDITOR CHAPPUIE: We have two more action
17 items.

18 CHAIRPERSON LIND: No, I know that. I mean,
19 anything else on the process here.

20 CHIEF AUDITOR CHAPPUIE: No, not with the
21 interviews.

22 CHAIRPERSON LIND: All right. So we're moving
23 back to Item 5a, the Independent Auditor's report for the
24 fiscal year 2015-2016.

25 CHIEF AUDITOR CHAPPUIE: Good evening, Mr. Chair

1 and members of the Committee, Beliz Chappuie, CalPERS.

2 Agenda Item 5a is an action item. The Board's
3 independent financial statement auditor Macias, Gini &
4 O'Connell, MGO, completed its audit of CalPERS basic
5 financial statements for the fiscal year-ended June 30,
6 2016. Staff is requesting Risk and Audit Committee to
7 approve MGO's audit report and their report on required
8 communications. Presenting with me today, Rick Green, the
9 engagement partner with MGO, as well as Debbie Chan, the
10 director from the same firm.

11 CHAIRPERSON LIND: They just happen to be here.

12 CHIEF AUDITOR CHAPPUIE: It is getting late, so
13 we're moving slowly tonight.

14 With that said, I would like to turn it over to
15 Rick and Debbie to provide us the results of the financial
16 statement audit.

17 CHAIRPERSON LIND: Okay. Rick --

18 CHIEF AUDITOR CHAPPUIE: Oh, we have one more
19 presenter. I'm sorry. I wasn't --

20 MR. BULLOCK: David Bullock.

21 CHIEF AUDITOR CHAPPUIE: David Bullock.

22 CHAIRPERSON LIND: Okay. Guys, welcome. The two
23 of you welcome back. Rick, welcome here. You know what
24 time it is, so try to -- it's important. I don't want to
25 minimize it, but try to be as brief but effective.

1 MR. GREEN: Thank you. Dave, can you run the
2 PowerPoint.

3 MR. BULLOCK: Sure. Got it.

4 (Thereupon an overhead presentation was
5 Presented as follows.)

6 MR. GREEN: Mr. Chair, members of the Committee,
7 thank you very much for the opportunity to present the
8 results of our work. I understand it is late, so we'll be
9 brief.

10 The first slide I have is just a reiteration of
11 the scope of work. We performed the audit of the
12 financial statements for the year ending June 30th, 2016.
13 As a result of the scope of that work, we issued 3 reports
14 that you have before you, the independent auditor's
15 report, the risk -- the report to Risk and Audit
16 Committee, as well as the management letter.

17 As we venture into a work like this, we -- I like
18 to remind the group that it is the manager's
19 responsibility to prepare the financial statements in
20 accordance with GAAP and to design, implement, and
21 maintain a set of internal controls to ensure that those
22 financial statements are free of material misstatement,
23 whether that misstatement is caused by fraud or error.
24 Our job is to plan and perform the audit to obtain
25 reasonable assurance that, in fact, those financial

1 statements are free of material misstatement.

2 With that, I am going to now just turn it over to
3 Dave who will briefly just talk about the audit process at
4 a very high level, how we responded to the audit of
5 significant areas, and then turn it over to Debbie to
6 summarize the report to the Risk and Audit Committee, as
7 well as the management letter document.

8 So, Dave.

9 MR. BULLOCK: Thank you, Rick.

10 So the illustration that's on slide number 3
11 describes our audit approach in 3 separate phases,
12 planning, execution and completion. So the planning
13 phase, which is the time we spent on the front end to
14 ensure an efficient audit is going through the risk
15 assessments, our understanding of internal controls, and
16 developing audit -- an audit plan that's very tailored to
17 CalPERS, and what we believe addresses our audit risks for
18 material misstatement. And then we move into the
19 execution phase, and that's what we just completed.

20 We spent several months out here doing our field
21 work where we've performed tests of intern controls,
22 substantive procedures, and evaluated the results of
23 those.

24 --o0o--

25 MR. BULLOCK: And so we're here today as we're

1 finalizing the audit and into the completion stage of
2 reporting the results of the audit, rendering our
3 opinions, and issuing our auditor's report.

4 --o0o--

5 MR. BULLOCK: So as we go through, just -- I know
6 it's late, so we're going to quickly go through and
7 highlight to you what we felt were the priority areas and
8 some of the significant changes so you're aware of them.
9 So, you know, the first thing that we always do in any
10 audit is we evaluate fraud risk. And as you can see from
11 the response, we did a lot of procedures in that regard.
12 We met with a lot of staff here at CalPERS. We met with
13 members of the Board, and we did internal evaluations.
14 And we did a lot of procedures in regards to management
15 override. So looking at journal entries and so forth.

16 The next priority area was the implementation of
17 new standards. There was 2 new standards that were
18 implemented this year, 72 on the fair value. And you
19 probably noticed as a result of that, there was a new
20 footnote, or a lot more disclosure, note 4, at least on
21 the hierarchy of fair value, adding some transparency to
22 how the -- how observable the inputs are in determining
23 the fair values from the area. And those with the highest
24 level -- or highest observable inputs were a category or
25 hierarchy level 1 and things that are publicly traded and

1 easy to identify versus those that are less observable or
2 have no observable inputs at level 3, and a lot of
3 management estimates and things of that nature.

4 The -- CalPERS has also early implemented GASB 74
5 and OPEB. And so you may see some significant changes
6 there. A lot of the actuarial valuation disclosure came
7 out of the footnotes, and there was a change in how the
8 contributions were recognized in the financial statements.
9 And so that was the new standard that impacted CalPERS
10 this year.

11 On the investments, you know, because of the size
12 of the investment portfolio, there was a lot of emphasis
13 put on investments, and to ensure that the investments
14 exist, that the ownership is there, and that the
15 valuations were appropriate. And there was a lot of
16 procedures in that regard.

17 Further on the investments, we identified the
18 real assets and the private equity as having an additional
19 risk just due to the level of management estimates
20 involved in those valuations, and so there was a lot of
21 additional procedures in there. I know there's been a lot
22 of discussion on the, you know, separating the investment
23 expenses from the net investment income of those private
24 equities.

25 And, you know, we certainly appreciate that view.

1 We believe as auditors that transparency is very important
2 and we definitely encourage management to do that. And
3 they are in the process of doing that. You know, the
4 private equities are very complex. You know, there's a
5 lot of -- there's not a lot of standardization out there
6 in terms of how -- the total management fee versus the net
7 management fees are reported --

8 The performance fees are complex in nature.
9 There's fund of funds with an additional layer of
10 expenses. There's, you know, fund level and portfolio
11 company fees that aren't reported consistently from
12 manager to manager. So there's a lot of information in
13 there. And another added layer of complexity to that is
14 that the audited financial statements are calendar year,
15 so December 31. So there's going to have to be some level
16 of estimation involved in looking at Q1 and Q2. So
17 there's a lot of things that need to be considered before
18 we can believe that that information is reliable and the
19 integrity of that information is complete before it can be
20 separable.

21 So, you know, management has been working towards
22 developing those internal controls, so that that level of
23 reliability is there and that could be reported
24 separately. So I know that's the move that they're trying
25 to make, and they're in the process of that. And so --

1 and we definitely encourage that. And I just wanted to
2 just point that -- you know, just to recognize that the
3 information is being presented in accordance with GAAP, as
4 it stands now, and -- but the greater transparency is
5 coming up soon.

6 --o0o--

7 MR. BULLOCK: For the next priority area, benefit
8 payments, obviously, there's just a volume of transactions
9 in that. It's a very important area. We spend a lot of
10 time looking at the internal controls and doing analytics,
11 and also investigating, you know, lump sum payments and
12 other things that are -- that change the numbers
13 significantly.

14 The health care and long-term care liabilities.
15 You know, again, management estimates. Anytime there's a
16 management estimate involved, we like to bring in
17 specialist. We bring in an actuary and we evaluate the
18 information that goes into those estimates, and then the
19 assumptions used to take the data and come up with a
20 management estimate, And ensure that those valuations are
21 done in accordance with the actuarial standards of
22 practice, and in accordance with the GASB parameters.

23 And then finally, the last section that we just
24 wanted to point out is the employer's net pension
25 liability. So the actuarial valuations that go into

1 the -- into those cost-sharing plans and the single
2 Employer plans. And, you know, very similar to what we
3 just talked about with the other actuarial valuation. We
4 bring our specialists in for those. We test the census
5 data. We had a discussion on that during the interview.

6 We look at the census data, both -- for the
7 cost-sharing pools, we look at both from the employer
8 side, and we work with the Office of Audit Services. And
9 then we also look at how CalPERS itself manages the
10 retirees and beneficiaries and the inactives

11 --o0o--

12 MR. BULLOCK: So the results of all that is we're
13 happy to report that we had unmodified opinions, which is
14 the highest level of assurance that we could provide as
15 your auditors. We believe these financial statements are
16 fairly stated. We -- and also kudos to management. We
17 did not find any -- or identify any material weaknesses or
18 significant deficiencies in internal controls, so that
19 just goes to show that they have solid internal controls
20 in place and as they're producing the financial
21 statements.

22 We did have 3 observations that we wanted to
23 report on internal controls. And Debbie is going to talk
24 about that momentarily.

25 --o0o--

1 MS. CHAN: Thank you, Dave.

2 At this point, I'd like to turn your attention to
3 agenda Item 5a, attachment 2, which is the Report to the
4 Risk and Audit Committee. In the interests of time, I
5 just want to highlight 3 items there presented in that
6 report.

7 First and foremost, we did not encounter any
8 significant difficulties throughout our audit. For
9 example, you know, there was no difficulty with lack of
10 the availability of information that we requested for our
11 audit, or there was no issue with access to management
12 with respect to any audit inquiries.

13 We're also pleased to report to you that we did
14 not have any disagreements with management concerning
15 accounting, financial reporting, or any auditing matters.

16 Last, I want to bring to your attention that
17 included in this report, we have -- we do have 2
18 schedules. The first schedule is the schedule of
19 uncorrected financial statement misstatements. And the
20 second schedule is a summary of material financial
21 misstatements, which was corrected by management, and
22 reflected in the audited financial statements.

23 With respect to the uncorrected misstatement,
24 management has determined that those adjustments were
25 deemed immaterial, individually and in the aggregate to

1 the overall financial statements. And we concur with that
2 assessment. And those were not adjusted in the financial
3 statements.

4 So that concludes my summary of this report.
5 I'll be happy to answer any questions you have.

6 CHAIRPERSON LIND: Okay. It looks like we have
7 one from Mr. Jelincic.

8 COMMITTEE MEMBER JELINCIC: Yeah. On page 6 of
9 2[sic], the uncorrected financial report -- or uncorrected
10 financial statement misstatements, the -- if you -- the
11 net appreciation of fair value assessments shows up as an
12 increase, but it reconciles to lines -- to PERF lines 1
13 and 4. Is that -- I'm confused. What are you telling me?

14 MS. CHAN: Okay. So the first adjustment on that
15 schedule -- are you referring to the first adjustment on
16 that schedule?

17 COMMITTEE MEMBER JELINCIC: Yes.

18 MS. CHAN: Okay. So that first adjustment
19 represent true-up values relating to private equity and
20 real assets. And these values were based on the partner's
21 June 30th financial statements. What's reported in
22 CalPERS financial statements were based on the March
23 31st -- the partner's March 31st financials adjusted for
24 cash flow transactions from April through June of 2016.

25 So then when the partners financial statements,

1 as of June 30th, were available, which is very late in the
2 reporting process, late October, so we used that
3 information. We compared to what was reported in the
4 financials, and this -- and came up with this difference.
5 So this difference was not recorded in the financials.

6 COMMITTEE MEMBER JELINCIC: So we understated our
7 assets by 775 million in the financials?

8 MS. CHAN: Yes.

9 COMMITTEE MEMBER JELINCIC: Okay. And the -- and
10 I guess on the corrected that flows through.

11 I recognize that 67 allows for the use of net,
12 rather than separable. We have the data. I believe it is
13 separable. I understand that management's not comfortable
14 enough with it to say audit it. And I recognize it's
15 management's misstatement, not yours. What can we do to
16 get the accounting standards to -- instead of saying you
17 should report it separately, say that you must report it
18 separately?

19 MR. GREEN: What I would suggest is that you
20 contact GASB, either directly, and make an inquiry, or you
21 can use us to gather or arrange a phone call, so we can
22 talk to the leaders there, and make suggestions as to how
23 that change, or proposed change, would enhance the
24 decision usefulness of your financial statements, or --
25 actually, not your financial statements, but GAAP overall,

1 or the financial statements that are applying that GAAP.
2 That becomes the first step.

3 Now, we participate on many GASB committees and
4 have access to these individuals. So I would suggest that
5 you probably use us as the vehicle for those
6 communications, and see where it takes you.

7 COMMITTEE MEMBER JELINCIC: Okay. Thank you.

8 CHAIRPERSON LIND: Thank you. All right. I
9 would like to entertain a motion that we accept the
10 independent auditor's report.

11 COMMITTEE MEMBER TAYLOR: I'll make the motion.

12 CHAIRPERSON LIND: Thank you.

13 COMMITTEE MEMBER MATHUR: Second.

14 (Laughter.)

15 CHAIRPERSON LIND: Motion by Taylor, seconded by
16 Mathur.

17 Anything on the question?

18 All in favor say aye?

19 (Ayes.)

20 CHAIRPERSON LIND: Any opposed?

21 Motion carries.

22 Management letter.

23 MS. CHAN: Okay. I'm going to be very brief with
24 the management letter, Agenda Item 5b, attachment 1.

25 So resulting from our audit this year, we have 3

1 observations. The first one is relating to the accounting
2 and reporting for internal pool investments. The second
3 observation is relating to the replacement benefit fund
4 account reconciliation's receivable and payable. The last
5 one is relating to the timing of the Long-Term Care Fund
6 annual actuarial valuations.

7 Management concurs with our observations and
8 recommendations and have established corrective action
9 plans to address these items.

10 CHAIRPERSON LIND: Thank you. Are there any
11 questions from the Committee?

12 Can we have a motion to accept the management
13 letter?

14 COMMITTEE MEMBER MATHUR: So moved.

15 ACTING COMMITTEE MEMBER LOFASO: Second.

16 CHAIRPERSON LIND: We have a motion by Mathur,
17 and second by Lofaso -- did you have something else?

18 ACTING BOARD MEMBER GREENE-ROSS: No, we're done.

19 CHAIRPERSON LIND: Okay. All right.

20 All in favor say aye?

21 (Ayes.)

22 CHAIRPERSON LIND: Any opposed?

23 That motion carries.

24 Thank you very much. And I'm sorry you felt a
25 little rushed through this. It's been a long night, but

1 we know you did an outstanding job for us.

2 MR. GREEN: No. We thank you very much. And I'd
3 like to say, as I'm leaving, this is the 10th time in
4 which we've done -- I've done the presentation. I'll no
5 longer be doing it going forward. And I wanted to thank
6 this Committee, even though not everyone was here at the
7 beginning, for your hospitality and your guidance. And I
8 really truly appreciate the time serving CalPERS as the
9 engagement partner, so thank you very much.

10 CHAIRPERSON LIND: And Rick, thanks for your
11 service to us. We do appreciate it.

12 MR. GREEN: Thank you.

13 CHAIRPERSON LIND: Okay. We're now on to the
14 information agenda items, 6a, third-party valuation
15 certification, et cetera.

16 CHIEF AUDITOR CHAPPUIE: Good evening, Mr. Chair,
17 and members of the Committee. Beliz Chappuie, CalPERS.

18 Agenda Item 6a is an information item related to
19 actuarial parallel valuation of the contracting public
20 agency plans. The Board retains the services of an
21 outside actuarial firm to review the work of CalPERS
22 actuarial staff to certify that their work complies with
23 actuarial professional standards.

24 Buck Consultants, the third-party actuarial firm,
25 selected by the Board in November 2015 completed its

1 independent review of the contracting public agency plans
2 as of June 30, 2015. Presenting with me today are David
3 Driscoll and Aaron Shapiro from Buck Consultants. I would
4 like to turn it over to David and Aaron to present their
5 report and answer any questions that you may have.

6 MR. DRISCOLL: Thank you. Yeah, we appreciate
7 the opportunity to review with you our report, which is
8 attachment 1 for Agenda Item 6a in your package. I
9 will -- Aaron is going to give you an overview of the
10 examination we conducted as part of this first phase of
11 the parallel valuation audit project. I will talk about
12 some of our technical findings. And then Aaron will
13 finish up talking about some issues related to
14 professional standards that we wanted to raise in our
15 report.

16 MR. SHAPIRO: Thanks, David. In reviewing the
17 public agency plans, we selected the 10 largest public
18 agency plans as well as 10 random plans to ensure we
19 tested a variety of types of plans and size of plans and
20 cover all types of participants.

21 Our review included the technical review of the
22 liabilities and contribution rates, and all the
23 calculations that went into that, as well as a review of
24 the reports for compliance with all applicable actuarial
25 standards of practice as issued by the American Academy of

1 Actuaries.

2 I'll turn it back to David.

3 MR. DRISCOLL: Thank you.

4 Yeah. So in the course of our examination, we
5 compared key results for the 20 plans Aaron mentioned. We
6 looked at the present value of benefits, at the accrued
7 liability, at normal cost and at contribution rates.
8 We're pleased to report that we were within 5 percent of
9 the CalPERS' results for the 10 largest plans and for 6 of
10 the randomly selected plans.

11 For 4 of the randomly selected plans, we had
12 differences in one or more of these variables that
13 exceeded 5 percent and required reconciliation. We do
14 note that these discrepancies generally occurred in very
15 small plans, ones that had very, very small numbers of
16 participants, so that to the extent that these
17 discrepancies did arise, in part, they are a function of
18 the smallness of these plans, and, in some cases, are
19 indicative of immaterial differences in the handling in
20 our valuation system and in CalPERS' valuation system of
21 individual participants.

22 We also did compare individual results. As we
23 mentioned when we presented to you last year, our proposal
24 for conducting this service, we engage in something called
25 an enhanced reconciliation of results on a participant by

1 participant basis. We found that less than 6 percent of
2 the individuals covered, there were about 135,000 records,
3 contained in the censuses of the plans that we examined.
4 And among them less than 6 percent showed individual level
5 differences of over 5 percent in results.

6 Now, as I mentioned, the fact that a -- that
7 results for particular systems differed by more than 5
8 percent would trigger in this examination a reconciliation
9 of the reasons for the existence of such differences.

10 And in most cases, they were things that are
11 really quite trivial and were magnified, to the extent
12 that we encountered them, in reviewing results for very
13 small systems.

14 There was one issue that we did note, that in the
15 application of a certain decrement - a decrement is a
16 table of probabilities that is applied in an actuarial
17 valuation, to -- that indicates the likelihood that
18 something will happen to an individual that will trigger
19 his eligibility for a benefit or, in some cases,
20 extinguish that individual's eligibility for a benefit.

21 There was a difference in the way that we think a
22 particular decrement was being applied to certain people
23 and the way that it actually was applied in the valuation
24 process. Specifically, for people who are part-time
25 workers in certain systems, who accrue less than a full

1 year of credited service per 12-month period that they
2 work, we found that there was a table in use for vesting
3 for the contingency of terminating with a benefit that
4 either consists of a receipt of a vested benefit or a
5 refund of contributions.

6 That's obviously intended to be based upon
7 credited service that -- but that was applied on an
8 elapsed time basis, so that somebody who had worked say 5
9 years, but had only say 1.5 years of service was treated
10 as though they had 5 years of credited service.

11 This resulted for these individuals in a slight
12 overstatement of liabilities. We do not think that this
13 amounts to a material issue for the valuations conducted
14 by CalPERS as a whole, but we do recommend that it be
15 further investigated by actuarial staff to see if there
16 isn't some adjustment necessary in order to make the --
17 for a greater degree of consistency in the intended
18 application and actual application of this decrement in
19 the valuation process.

20 Our other observations included, as Aaron
21 mentioned earlier, some discussion of the ASOPs and the
22 way that they apply to the valuation reports we examined,
23 and of important changes in the ASOPs that will be
24 applicable valuation reports prepared at valuation dates
25 in the near future. And I'm going to let Aaron mention a

1 little bit about those now.

2 MR. SHAPIRO: Thank you, David. So we reviewed
3 the reports provided that were prepared as of June 30,
4 2014 to confirm that they were consistent with the
5 Actuarial Standards of Practice in effect as of June 30th,
6 2014, including ASOP 4, which is for measuring pension
7 obligations, ASOP 27 and 35 for selecting assumptions, and
8 determined that they were consistent with the ASOPs in
9 effect as of June 30th, 2014.

10 Subsequent to the valuation date, ASOP 4 was
11 revised to provide additional information. And we have
12 listed in the report some suggestions from the revised
13 ASOP 4 subsequent to the -- again, subsequent to the
14 valuation date for consideration for inclusion in future
15 valuation reports.

16 VICE CHAIRPERSON HOLLINGER: J.J..

17 Did you press it?

18 COMMITTEE MEMBER JELINCIC: Okay. When you did
19 your random sample of 10, 9 of them were in pools. Is
20 that what you would expect or was that a surprise?

21 MR. DRISCOLL: I think that's what we expected.

22 COMMITTEE MEMBER JELINCIC: Okay. And then
23 you've talked about the decrement tables, and you're
24 talking to staff. Has there been a meeting of the minds
25 on that or is it --

1 MR. DRISCOLL: My understanding is is that the
2 observation has been corroborated by staff, and it's being
3 looked at as the likely subject of a technical fix.

4 COMMITTEE MEMBER JELINCIC: Do you disagree?
5 Otherwise, just --

6 INTERIM CHIEF ACTUARY TERANDO: No. We agree
7 with the findings and we're looking into it.

8 COMMITTEE MEMBER JELINCIC: Okay.

9 VICE CHAIRPERSON HOLLINGER: Any other questions?

10 COMMITTEE MEMBER JELINCIC: No.

11 VICE CHAIRPERSON HOLLINGER: Okay. Thank you.

12 MR. DRISCOLL: Thank you.

13 VICE CHAIRPERSON HOLLINGER: It just says
14 information.

15 Okay. So -- and last, Cheryl and Forrest,
16 semiannual risk reports. Cheryl and Forrest.

17 CHIEF FINANCIAL OFFICER EASON: Thank you very
18 much. And thank you Committee, we'll keep this very, very
19 brief.

20 At the June Committee meeting, this Committee was
21 presented with a consolidation of 30 risks to the current
22 10-risk profiles. That's what you have currently in the
23 risk dashboard and risk profile reports. The profiles
24 focus on risk drivers, effective mitigations developed,
25 and implemented to address the potential risks that may

1 affect the organization. So I'm pleased to confirm that
2 each Committee -- Board Committee has now reviewed their
3 respective risk profiles, the latest being the Talent
4 Management risk profile at today's Performance,
5 Compensation and Talent Management Committee. And these
6 are presented for your information. And if there's
7 anything, Forrest, you wanted to add to that.

8 CHIEF RISK OFFICER GRIMES: You know, I think
9 during this late hour -- good evening. Forrest Grimes,
10 CalPERS team member -- I would really defer to your
11 questions. I know that Mr. Jelincic may have a question
12 or 2 that we discussed during breakfast briefly. But
13 other than, that I'm just going to defer to you.

14 CHAIRPERSON LIND: Great. And thanks for being
15 here, Forrest, this late --

16 CHIEF RISK OFFICER GRIMES: Certainly.

17 CHAIRPERSON LIND: -- and for all the great work
18 you're doing on this. We know about it. We don't want to
19 give you the rush here, and I -- so we appreciate it. And
20 there are a few questions.

21 Mr. Jelincic.

22 COMMITTEE MEMBER JELINCIC: On slide 6, there was
23 a consensus for everything except the compliance and the
24 health care administration. Can you talk a little bit
25 about what that is?

1 CHIEF RISK OFFICER GRIMES: Yes, certainly.
2 Basically, I do want to point out though that the top 3
3 scores were consistent among program leadership and
4 executive leadership, which was encouraging. I think that
5 was really an encouraging finding.

6 The compliance and health care scores, executive
7 leadership determined that they wanted to provide a
8 materiality threshold during discussions of scoring and
9 did so. Once program leadership was given the opportunity
10 to rescore with that materiality threshold, the compliance
11 scores were very similar to the executive team. However,
12 health care administration remained unchanged, and we
13 attribute that to the program's continued concerns
14 regarding the uncertainty of implementation of the
15 Affordable Care Act provisions.

16 Obviously, since that time, this risk will be
17 reassessed with the new administration once what they
18 determine should occur is more clear. So that's
19 uncertain.

20 COMMITTEE MEMBER JELINCIC: Okay. And in
21 Attachment 2, page 1 of 1, compliance, was a high impact,
22 understandably, but also a high probability. Can you shed
23 some insight onto that, particularly the high probability
24 part?

25 CHIEF RISK OFFICER GRIMES: Okay. Well, I

1 believe that that really, I think, goes to reputational
2 risk, as much as anything. That we think that -- and,
3 Marlene is here also to kind of correct me if I misstate
4 this in any way.

5 We think that the impact reputationally is quite
6 high to CalPERS, and would be picked up on immediately if
7 we were non-compliant with any laws, rules, or
8 regulations. And the probability, I think that that was
9 rated high, because there is so many complex regulations
10 and laws that we're subject to that we think that there is
11 definitely a high risk of noncompliance. And it's
12 difficult to keep track of all these many, many laws and
13 regulations that we're subject to. Marlene, do you have
14 anything to add to that.

15 CHIEF COMPLIANCE OFFICER TIMBERLAKE D'ADAMO:

16 Marlene Timberlake D'Adamo, CalPERS team member,
17 Chief Compliance Officer.

18 Thanks, Forrest.

19 So I think what I would add here is that the
20 compliance is, as Forrest mentioned, the reputation risk
21 is really great. The laws, rules, regs, and statutes that
22 we must comply with are, at times, complex and voluminous.
23 And so it was really with an acknowledgement of all of the
24 things that we have to deal with that there was this
25 scoring that was -- that took a look at the fact that

1 there is a likelihood at times that we are, you know,
2 trying to get there, but not always there. And I think
3 that was an acknowledgement by the senior staff and the
4 executive leaders that we're trying to get there, but
5 there is a lot to do. And it would probably be
6 disingenuous at times to say that we're always going to be
7 there. We are always there, but we are trying.

8 COMMITTEE MEMBER JELINCIC: Okay. I have some
9 others, but in light of the time, I'm leaving them alone.

10 CHAIRPERSON LIND: Thanks, J.J..

11 Ms. Mathur.

12 COMMITTEE MEMBER MATHUR: Thank you, Mr. Chair,
13 and thanks to all of you for sticking it out so late. My
14 question is I had -- I was the one who sort of asked that
15 we bring all of these risks to each of the individual
16 functional committees. And I'm interested in whether you
17 thought it was a useful exercise, and if you thought there
18 were any improvements to how the Committee has considered
19 these risks, that we could consider for next timing?

20 CHIEF RISK OFFICER GRIMES: Sure. That's an
21 interesting question, and I want to respond this way. I
22 Think it's -- I think it's valuable in 2 ways. It clearly
23 identifies ownership for each committee, and really
24 reinforces their delegated authority, and the
25 responsibilities associated with it. So I think it's very

1 important from that perspective.

2 And I think that it truly gave each committee the
3 opportunity to look at the mitigations, what's in place,
4 what they may want to see in place in the future. And
5 it's going to be very helpful when we start talking about
6 next steps, which is establishing risk appetite, and if
7 appropriate mitigations currently exist or we should be
8 doing more.

9 COMMITTEE MEMBER MATHUR: Okay. Thank you.

10 CHAIRPERSON LIND: Okay. Any other questions?

11 I'm not seeing any. Thank you very much for the
12 report, for your work. I know we'll be hearing more in
13 the future.

14 CHIEF RISK OFFICER GRIMES: Well, thank you. And
15 I would like to take a quick second to acknowledge the
16 great work that the risk team has done. Melissa Azevedo,
17 the Assistant Chief is here with me this evening. Rebecca
18 Franklin has done tremendous work. She had class tonight
19 or she would be here. And hopefully the rest of the team
20 is asleep and getting ready to work tomorrow, so --

21 (Laughter.)

22 CHAIRPERSON LIND: Great. Well, thank you,
23 Melissa, and pass our thanks on to the rest of the team.

24 CHIEF RISK OFFICER GRIMES: Certainly. Thank
25 you.

1 CHAIRPERSON LIND: Okay. That takes us on to
2 summary of committee direction. The only thing I have,
3 Cheryl, is exploring with our auditors a phone call to
4 GASB regarding the private equity fee issue, right?

5 CHIEF FINANCIAL OFFICER EASON: Yes. I have that
6 as well. I agree. We'll get that noted.

7 CHAIRPERSON LIND: Okay. Great. I don't have
8 any public comments, so we're going to adjourn this
9 meeting. We are going to do a closed session. We need
10 everybody out of the room except for our Board Service
11 Unit, the recorders, and Beliz you can stay here --
12 reporters, I should say. And Beliz, you can stay.

13 (Thereupon the California Public Employees'
14 Retirement System, Board of Administration,
15 Risk & Audit Committee open session
16 meeting adjourned at 9:07 p.m.)

1 C E R T I F I C A T E O F R E P O R T E R

2 I, JAMES F. PETERS, a Certified Shorthand
3 Reporter of the State of California, do hereby certify:

4 That I am a disinterested person herein; that the
5 foregoing California Public Employees' Retirement System,
6 Board of Administration, Risk & Audit Committee open
7 session meeting was reported in shorthand by me, James F.
8 Peters, a Certified Shorthand Reporter of the State of
9 California;

10 That the said proceedings was taken before me, in
11 shorthand writing, and was thereafter transcribed, under
12 my direction, by computer-assisted transcription.

13 I further certify that I am not of counsel or
14 attorney for any of the parties to said meeting nor in any
15 way interested in the outcome of said meeting.

16 IN WITNESS WHEREOF, I have hereunto set my hand
17 this 22nd day of November, 2016.

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20 

21
22 JAMES F. PETERS, CSR
23 Certified Shorthand Reporter
24 License No. 10063
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