



Risk and Audit Committee

Agenda Item 6b

November 14, 2018

Item Name: Review of Independent Auditor's Management Letter

Program: Audit Services

Item Type: Action

Recommendation

Approve the CalPERS Board of Administration's (Board) Independent Financial Statement Auditor's (Independent Auditor) Draft Management Letter for the fiscal year ended June 30, 2018.

Executive Summary

The Draft Management Letter, prepared by the Board's Independent Auditor, KPMG LLP (KPMG), includes comments and recommendations related to strengthening internal controls over financial reporting based on the audit of the June 30, 2018 financial statements. Management's concurrence, response, and proposed corrective actions to the observations and recommendations are included in the Draft Management Letter. In addition, management reported that the prior year comments and recommendations were resolved.

Strategic Plan

This item is not a specific product of the Strategic Plan. The Government Code section 20228 requires the Board to annually employ a certified public accountant to audit the financial statements.

Background

KPMG completed its audit of CalPERS Basic Financial Statements for the fiscal year ended June 30, 2018 as required by Government Code section 20228. In connection with the audit of the financial statements, KPMG prepared a Draft Management Letter that includes comments and recommendations to enhance internal controls over financial reporting (Attachment 1).

The Management Letter is considered a draft until it is approved by the Board and subsequently signed by KPMG. The signed Management Letter will be distributed to the Board, executive staff and senior management.

Analysis

Consistent with the Office of Audit Services Audit Resolution Policy, the status of the Management Letter observations will be reported to the Risk and Audit Committee until management has resolved each noted observation. The tables below summarize the current and prior year observations.

Table 1 – Current Year Observations

Issue	Description
Observation 1	Non-GAAP Policies – Documentation of non-Generally Accepted Accounting Principles (GAAP) policies
Observation 2	Third Party Administrators (TPA) – Oversight controls over TPA
Observation 3	Actuarial Certifications – Documentation of TPA actuarial certifications
Observation 4	Accounting Position Statement (APSs) – Update of APSs to reflect current CAFR treatment and/or supplemental language
Observation 5	Census Data – Analysis of data errors related to census data and enhancement internal controls to ensure timely and accurate reporting of census data

Table 2 – Status of Prior Year Observations

Issue	Description	Status ¹
Observation 1 FY 2017	Service Organization Control (SOC) Reports – Formal procedures for identifying, tracking, receiving, and reviewing of SOC 1 reports	Resolved
Observation 2 FY 2017	Accounting and Reporting for OPEB Contributions and Reimbursements Outside of the California Employers' Retiree Benefit Trust Fund (CERBTF) – Completeness and accuracy of financial information submitted by participating employers	Resolved
Observation 3 FY 2017	Accounting and Reporting for the Replacement Benefit Fund – Reconciliation of account balances and accuracy and consistency between the general ledger and my CalPERS	Resolved
Observation 2 FY 2016	Replacement Benefit Fund Account Reconciliation – Discrepancies between the general ledger and my CalPERS	Resolved
Observation 3 FY 2016	Long-Term Care Fund Annual Actuarial Valuation – Timeliness of member census data for the preparation of the annual actuarial valuation report	Resolved
Observation 3 FY 2015	my CalPERS Functionality – Data integrity	Resolved

¹ Management reported that the prior year comments and recommendations were resolved.

Budget and Fiscal Impacts

The fees for the basic financial statements audit is anticipated to total \$1,500,000. Funding was already identified within budgetary resources as is consistent with the Board approved contract.

Benefits and Risks

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

Attachments

Attachment 1 – Draft Management Letter (including CalPERS management’s responses), prepared by KPMG for the fiscal year ended June 30, 2018

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