

Summary of Financial Statement Audit Management Letter Comments
Prior Year Report
As of September 30, 2019

Audit Management Letter Comments for the Year Ended 06/30/18

Observation #1: Non-GAAP Policies

Division Responsible: Financial Report and Accounting Services Division

Entities often determine that certain generally accepted accounting principles (GAAP) are not material and therefore excluded from presentation in their audited financial statements. CalPERS has selected to also not reflect certain immaterial items from its Comprehensive Annual Financial Report (CAFR), for example certain cut-off reporting of accruals.

CalPERS should formally document all of its non GAAP policies as well as annually evaluate and determine that said policies continue to be immaterial to its CAFR.

Financial Office's Current Update: RESOLVED. The Financial Reporting and Accounting Services (FRAS) team has ensured all non-GAAP policies and procedures necessary have been completed.

Observation #2: Third Party Administrations

Division Responsible: Health Plan Administration Division

CalPERS' proprietary funds include the activities of the Health Claims Funds (HCF) and the Long-Term Care Fund (LTCF) and the related oversight and monitoring of claims activity administered by third-party administrators (TPAs). During the audit, KPMG noted that CalPERS did not have access to nor routinely reviewed or reconciled the detail claims activity processed by the TPAs to what was reflected in the books and records of either the HCF or the LTCF.

CalPERS should review its oversight controls of the TPAs and update its controls as deemed necessary. At a minimum, KPMG would recommend that CalPERS should reconcile summary TPA claim activity to the detail claim activity on a regular basis.

Financial Office's Current Update: OPEN. For the LTCF, the Health Plan Administration Division (HPAD) team has completed the procedure and process for detailed claims reconciliation which has been implemented since the January 2019 monthly financial activities. For the HCF, the HPAD team in coordination with the State Controller's Office are currently documenting, implementing and testing the TPA reconciliation of the claims summary to the detail claims for the new Preferred Provider Organization Contract Period: January 1, 2020 – December 31, 2024. The implementation phase for the new claims process is April 2019 through December 2019 with a programmed go live date of January 1, 2020.

Observation #3: Actuarial Certifications

Division Responsible: Actuarial Office/ Health Plan Administration Division

CalPERS reports an incurred but not reported (IBNR) liability related to its HCF activity. The process for establishing the IBNR at year-end includes accumulating actuarial certifications provided by the various TPAs. While it's apparent that management monitors and reviews those TPA provided certifications, CalPERS does not evidence that monitoring and review in a formal document or memorandum.

CalPERS should summarize the collected TPA certifications and have one of its health actuaries certify the year-end IBNR accrual in a formal document in accordance with the provisions Actuarial Standards of Practice No. 41, Actuarial Communications. Such a formal communication would clarify management's responsibility for the IBNR reported at year-end.

Financial Office's Current Update: RESOLVED. The Actuarial Office (ACTO) and HPAD team created a formal documentation and process that summarizes and certifies the year-end IBNR effective June 30, 2019.

Observation #4: Accounting Position Statement

Division Responsible: Financial Report and Accounting Services Division

As evidence of a best practice approach to documenting key accounting decisions, CalPERS prepares accounting position statements (APSs). KPMG has reviewed several of these APSs during the initial audit this fiscal year. In an effort to improve the contents of these APSs, KPMG has recommended some be updated to reflect current CAFR treatment (e.g. APS No. 2014/15-1 related to GASB 68 recognition on the CAFR) and/or suggested supplemental language (e.g. APS No. 2013/14-1 related to GASB 67 PERF breakout as PERF A, B and C). In other situations (e.g. APS No. 2015/16-1 related to GASB 68 NPL allocations to Public Agencies), KPMG noted that certain APSs focused more on the conclusions reached than the process and laws and /or accounting literature considered in arriving at its conclusions.

CalPERS should review its past APSs and update as deemed necessary. On a go-forward basis, KPMG encourages CalPERS to include a robust analysis of the laws and or accounting literature considered in arriving at and supporting its final conclusions.

Financial Office's Current Update: RESOLVED. APSs have all been updated, reviewed, and approved by management. Going forward, this review and update process has been added to the list of annual tasks, and staff assigned to analyze newly effective governance.

Observation #5: Census Data

Division Responsible: Actuarial Office

CalPERS is responsible for maintaining census data for the approximately 2 million members (active and retired) who participate in CalPERS' defined benefit pension plans. Significant elements of census data include: date of birth; years of service; eligible compensation; and gender among other elements.

Effective management of the census data for active employees include procedures to verify the underlying payroll records of the participating employers to determine that the information provided is complete and accurate as this census information is utilized by CalPERS' actuaries to calculate a total pension liability for each of the various defined benefit plans, a significant accounting estimate that is part of the financial reporting process.

In accordance with audit procedures promulgated by the American Institute of Certified Public Accountants (AICPA), KPMG subjected certain Schools and Public Agencies whose employees are active members of the PERFs to census testwork that included comparing such information to the census file used by CalPERS. The results of testwork indicated approximately 100 data quality issues such as incorrect date of birth, understated eligible compensation and/or incorrect years of service. Such data quality issues are not unusual for a public employee retirement system with nearly 1.3 million active members.

KPMG understands that the CalPERS continually updates both the information technology and manual controls over its member management system, my|CalPERS.

CalPERS should conduct a root cause analysis for all its known errors and adjust its internal controls accordingly to address any common causes related to data errors. One potential common cause is the timeliness of data submitted through the my|CalPERS portal. Accordingly, KPMG is also recommending that CalPERS enhance its existing internal controls to ensure the timely and accurate reporting of census data by the participating employers.

Financial Office's Current Update: OPEN. ACTO delivered most errors to the appropriate program area by August. Program areas have reviewed all errors sent and taken appropriate action. This includes data correction, explanation back to ACTO of why data is correct, or referral to other program areas to fully resolve issue. ACTO is going through the remaining errors and will continue to work with program areas. Most errors are expected to be resolved by December 31, 2019, while some errors involve action from business partners or updates to my|CalPERS and therefore will take longer to resolve.