



## Audits & Risk Management Committee

### Item Number 6 – Open Session

**Subject:** 2021 Management Letter

**Presenter(s):** Larry Jensen & Julie Underwood

**Item Type:** Information

**Date & Time:** November 4, 2021 – 10 minutes

---

**Attachment(s):** Attachment 1 – 2021 Management Letter

**PowerPoint(s):** None

---

#### **PURPOSE**

The purpose of this item is to provide the Management Letter for the year ended June 30, 2021, as prepared by Crowe LLP.

#### **DISCUSSION/SUMMARY**

During an audit, the auditor may become aware of deficiencies in internal control while obtaining an understanding of the entity and its internal control environment. A deficiency in internal controls exists when the design or operation of a control does not allow management or staff, in the normal course of performing their assigned functions, to prevent or detect and correct misstatements on a timely basis. Any material and significant deficiencies are included in the Report on Internal Control over Financial Reporting. Otherwise, deficiencies that are not considered significant or material are included in a Management Letter, which is not required to be reported to the Board by the auditor. However, to promote transparency, CalSTRS' management presents the 2021 Management Letter (Attachment 1).

Crowe LLP observed an opportunity to strengthen internal controls over financial reporting related to the completeness and accuracy of member data while conducting the financial statement audit. The external auditor discussed the observation with management of the related business area and the executive team, who agrees with the recommendation and has prepared a response to the observation.

CalSTRS management is responsible for implementing the corrective actions outlined in the management letter. Audit Services will provide the committee with periodic reports on the progress of implementing the corrective actions. The independent financial statement auditor, Crowe LLP, will validate implementation of management's corrective actions and report the status to the committee at the November 2022 ARM Committee meeting.



Members of Management  
California State Teachers' Retirement System  
West Sacramento, California

In the planning and performing of our audit of the financial statements of California State Teachers' Retirement System (the "System" or "CalSTRS") as of and for the year ended June 30, 2021, in accordance with auditing standards generally accepted in the United States of America and *Government Auditing Standards*, we considered the System's internal control over financial reporting ("internal control") as a basis for designing our auditing procedures for the purpose of issuing our report on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the System's internal control. Accordingly, we do not express an opinion on the effectiveness of the System's internal control.

In planning and performing our audit of the Schedule of Proportionate Share of Contributions for Employers and Nonemployer Contributing Entity of State Teachers' Retirement Plan (the "STRP"), a plan administered by CalSTRS, for the year ended June 30, 2021, and the captions titled total net pension liability as of June 30, 2021, total deferred outflows of resources, and total deferred inflows of resources (specified caption totals) included in the Schedule of Aggregate Pension Amounts for Employers and Nonemployer Contributing Entity as of June 30, 2021, we considered the STRP's internal control as a basis for designing our auditing procedures for the purpose of expressing our opinions on the Schedule of Proportionate Share of Contributions for Employers and Nonemployer Contributing Entity and the specified caption totals included in the Schedule of Aggregate Pension Amounts for Employers and Nonemployer Contributing Entity, but not for the purpose of expressing an opinion on the effectiveness of the STRP's internal control. Accordingly, we do not express an opinion on the effectiveness of the STRP's internal control.

Our consideration of internal control was for the limited purpose described in the preceding paragraphs and was not designed to identify all deficiencies in internal control that might be significant deficiencies or material weaknesses and therefore, there can be no assurance that all deficiencies, significant deficiencies, or material weaknesses have been identified. However, as discussed below, we identified certain matters that we wish to communicate to you. Matters communicated in this letter are classified as follows:

- Deficiency – A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect and correct misstatements on a timely basis

Control Deficiency	Active Member Data – Completeness and Accuracy (Repeat Finding)
Applicability of Impact	CalSTRS Financial Statements  STRP - Other Pension Information <ul style="list-style-type: none"><li>• Schedule of Proportionate Share of Employers and Nonemployer Contributing Entity</li><li>• Net Pension Liability as of June 30, 2021</li></ul>

### Description of Deficiency:

Member data is fundamental to financial reporting of contributions, benefit payments, and the Total and Net Pension Liability of the STRP. Internal controls are critical to ensure the completeness and accuracy of financial reporting as CalSTRS is dependent upon information from the contributing entities.

We commend management for the significant steps taken over the past several years related to the controls over member data, however, we continue to identify errors in the reported data that were not identified by CalSTRS' internal control structure. Common findings include:

- Continued misapplication of Limited Term Enhancements-
- Prior year earnings reported in the current year unrelated to retro pay
- Unreported extra duty
- Extra duty reported incorrectly, e.g. as salary or special compensation
- Incorrect pay rate impacting the calculation of earnable compensation
- Incorrect pay code, e.g. 10 pay reported as 11 pay

### Recommendation:

Due to the reliance on the contributing entities for the completeness and accuracy of active member data, it is probable that there will continue to be errors in reported data.

Crowe recommends that management continue to enhance its internal controls through development and/or improvement of data analytics to identify data anomalies and potential systemic errors based on historical experience, modify employer training strategies to improve effectiveness of training resulting in fewer reporting errors and continue to focus on employer readiness for the implementation of Benefit Connect, which includes functionality and file format regulations intended to reduce errors in reporting and provide immediate feedback to employers regarding potential errors upon submitting their contribution data. Management's evaluation of potential improvements should always consider the cost/benefit of any new enhancements related to the risk of incorrect member data.

### Management's Response:

Management continues to improve in the areas mentioned in the recommendation. Specifically, CalSTRS continues to expand its employer training audience and channels for training, adding self-serve computer-based training modules on a learning management system. For fiscal year 20/21, CalSTRS provided 45 virtual training sessions that served 2,134 employer staff across 1,091 districts on the most critical employer reporting topics. The expanded training channels include seven new computer-based training modules for core Teachers' Retirement Law topics. 158 employer partner staff representing 108 different employer reporting entities took these modules with an average knowledge assessment score of 96%. CalSTRS also evolved the training material concepts by developing nine new job aids for the most important reporting laws, providing the employers with additional self-serve education opportunities.

CalSTRS continues to respond to ad-hoc inquiries from employers and will pilot a formal quality management program for those inquiries in fiscal year 21/22. Additionally, CalSTRS has instituted a practice of regular outreach to our largest reporting sources, conducting 64 conference calls/virtual meetings with our employer partners to build our relationships with them to learn their needs, answer requests and identify potential training opportunities.

To prepare employer partners for the new Secure Employer Website/BenefitConnect, CalSTRS completed all 92 Pension Solution Readiness Visits in fiscal year 20/21, introducing our report sources (county offices of education, direct reports and their payroll system vendors) to the Employer Readiness Environment that they will use to submit test contribution data into a test environment to prepare them for reporting in the new Secure Employer Website. CalSTRS plans to engage employers with webinars and additional information sessions during the project delay, ramping up again for full, formal training and readiness six to eight months before go-live.

As part of the Employer Reporting to Final Benefit project, a cross-functional team across seven business areas is investigating improved employer information, piloting programs to analyze member data prior to retirement, evaluating current laws and regulations related to common audit findings, and six-month follow-up after audits among other improvements and efforts directly related to accurate employer reporting. CalSTRS has started monthly meetings with business officials and superintendents to discuss these improvements and collaborate with that audience to find ways to get better training penetration to districts and charters in their counties.

The purpose of this letter is solely to describe the scope of our testing of internal control over financial reporting and compliance, and the results of that testing, and not to provide an opinion on the effectiveness of the System's and the STRP's internal control over financial reporting. This letter is an integral part of audits performed in accordance with *Government Auditing Standards* in considering the System's and the STRP's internal control over financial reporting and compliance. Accordingly, this letter is not suitable for any other purpose.

The System's written responses to the deficiencies identified in our audits was not subjected to the auditing procedures applied in the audits of the System's financial statements and the STRP's Other Pension Information and, accordingly, we express no opinion on them.

This communication is intended solely for the information and use of the Audits and Risk Management Committee, Teachers' Retirement Board, and other members of CalSTRS management, and the System's regulatory agencies and is not intended to be and should not be used by anyone other than these specified parties.

A handwritten signature of the company name "Crowe LLP" in black ink.

Crowe LLP

Sacramento, California  
October 11, 2021