

# State Teachers' Retirement System

## 2015 SLAA REPORT

---

December 23, 2015

Marybel Batjer, Secretary  
California Government Operations Agency  
915 Capitol Mall, Suite 200  
Sacramento, CA 95814

Dear Ms. Batjer,

In accordance with the State Leadership Accountability Act (SLAA), the State Teachers' Retirement System submits this report on the review of our systems of internal control and monitoring processes for the biennial period ended December 31, 2015.

Should you have any questions please contact Robin Madsen, Chief Financial Officer, at (916) 414-4385, [rmadsen@calstrs.com](mailto:rmadsen@calstrs.com).

### **BACKGROUND**

Annually, CalSTRS establishes a business plan based on a Teachers' Retirement Board approved multi-year strategic plan. The annual business plan includes a SWOT analysis and goals and objectives built on the foundation of CalSTRS mission, vision and core values. The paragraphs that follow outline these components.

**MISSION**-Securing the financial future and sustaining the trust of California's educators.

**VISION**-Your Reward—A Secure Retirement  
Our Reward—Getting You There

### **CORE VALUES**

The CalSTRS core values are a set of attitudes, beliefs and behaviors that define CalSTRS and its employees.

**CUSTOMER SERVICE**-We never compromise on quality as we strive to meet or exceed the expectations of our customers.

**ACCOUNTABILITY**-We operate with transparency and accept responsibility for our actions.

**LEADERSHIP**-We model best practices in our industry and innovate to achieve higher standards.

**STRENGTH**-We ensure the strength of our system by embracing a diversity of ideas and people.

**TRUST**-We conduct ourselves with integrity, acting ethically in every endeavor.

**RESPECT**-We respect the needs of our members, co-workers and others, treating everyone with fairness, honesty and courtesy.

**STEWARDSHIP**-We recognize our fiduciary responsibility as the foundation for all decision-making.

### **BOARD STRATEGIC GOALS**

#### **GOAL 1—FINANCIAL**

Ensure a financially sound retirement system.

#### **GOAL 2—RISK MANAGEMENT**

Responsibly manage risk to the organization.

**GOAL 3—MEMBER/CUSTOMER**

Enhance services to members and customers.

**GOAL 4—WORKFORCE & PROCESS IMPROVEMENT**

Improve the work environment and internal efficiency

**STRATEGIC GOALS AND OBJECTIVES**

**GOAL 1 - FINANCIAL**

Ensure a financially sound retirement system.

**OBJECTIVE A**

Secure and implement legislation to adjust contributions and establish long-term financial viability of the CalSTRS benefit programs.

**OBJECTIVE B**

Achieve the long-term performance objectives established within the Investment Policy and Management Plan.

**OBJECTIVE C**

Implement the Diversity in the Management of Investments business plan.

**OBJECTIVE D**

Increase participation in global securities litigation.

**OBJECTIVE E**

Educate regulatory standard-setting organizations, policymakers and stakeholders on the unique characteristics of the CalSTRS benefit programs.

**GOAL 2 - RISK MANAGEMENT**

Responsibly manage risk to the organization.

**OBJECTIVE A**

Create a culture of risk awareness by incorporating enterprise risk management into business operations.

**OBJECTIVE B**

Enhance CalSTRS audit activities so that the quality of audits is in line with best practices.

**OBJECTIVE C**

Enhance the investment risk management platform and reporting capabilities.

**OBJECTIVE D**

Demonstrate the value of integrating environmental, social and governance opportunities into CalSTRS' culture and strategies.

**GOAL 3 - MEMBER/CUSTOMER**

Enhance services to members and customers.

**OBJECTIVE A**

Increase members' understanding of the role of the CalSTRS hybrid benefit program elements in achieving financial security for retirement.

**OBJECTIVE B**

Expand member and business partner e-services

**OBJECTIVE C**

Complete transition of contracted counseling services to CalSTRS' internal operations.

**GOAL 4 - WORKFORCE & PROCESS IMPROVEMENT**

Improve the work environment and internal efficiency.

**OBJECTIVE A**

Successfully implement all scheduled phases of BusinessRenew.

**OBJECTIVE B**

Develop and maintain a workforce plan for an evolving organization.

**OBJECTIVE C**

Develop strategies to manage the portfolio in an efficient and cost-effective manner.

**OBJECTIVE D**

Develop better ways to evaluate the success of the organization.

**OBJECTIVE E**

Analyze and adopt ways to become more cost-effective while still achieving the board's desired level of service to members and business partners.

While focused on meeting these annual objectives, CalSTRS understands the organization must be aware of impediments to success, our enterprise risks.

**RISK ASSESSMENT PROCESS**

CalSTRS performs a comprehensive enterprise level risk assessment annually. Quarterly, executive staff revisit the enterprise risk matrix and provide individual updates to particular areas of responsibility. The executive team, information security officer, human resources and communications directors then meet to review the status of enterprise risks. During this discussion, the executive team considers current events to determine if the risk matrix, and the corresponding mitigation efforts need to be expanded, revised or removed. Twice a year, the Teachers' Retirement receives a report during open session on the status of CalSTRS specific mitigation efforts.

Some of the key components of the enterprise risk matrix are:

- All Risk categories are tied to Business Goals and Objectives
- A determination of the Impact, Probability, and Velocity of the risk. There are ten risk categories where CalSTRS currently focuses its mitigation efforts.
- Subrisks reflect current specific areas of concern and targeted mitigation efforts
- Mitigation efforts show status, any challenges/concerns, and owner's confidence of risk response

Additionally, a "heat map" reflects risks' ratings in the context of the current environment.

The information contained in the "Evaluation of Risks and Controls" section reflects CalSTRS risks as reported to the Teacher's retirement board in September 2015.

**EVALUATION OF RISKS AND CONTROLS**

**Operations- External- Technology—Data Security**

**CalSTRS Goal** - Responsibly manage risk to the organization.

**CalSTRS Business Objective** - Protect the confidentiality, integrity, and availability of CalSTRS systems, networks, and information assets.

**Associated Overall Risk** - Loss of information security or compliance violations as a result of unauthorized or unintentional breaches.

**Subrisk A**

- An information security breach or incident at CalSTRS as it relates to the lack of Security Awareness.

**Subrisk B**

- An information security breach or incident at CalSTRS as it relates to Information Security Program Management/Oversight.

**Subrisk C**

- An information security breach or incident at CalSTRS as it relates to CyberSecurity.

Subrisk A, Mitigation Strategy 1

- Expand and enhance awareness of information security.

Subrisk B, Mitigation Strategy 1

- Establish information security policies to ensure security requirements, controls, and responsibilities are defined.
- Target Implementation date - November 2016

Subrisk B, Mitigation Strategy 2

- Stay current with security threats, zero day attacks, and industry trends

Subrisk C, Mitigation Strategy 1

- Perform an annual assessment of CalSTRS Cybersecurity Risk Profile
- Annual financial audit

**Operations- Internal- Oversight, Monitoring, Internal Control Systems**

**CalSTRS Goal** - Improve the work environment and internal efficiency.

**CalSTRS Business Objective** - Ensure cost effective, efficient and sustainable processes and systems that enable CalSTRS to serve its members and beneficiaries now and in the future.

**Associated Overall Risk** - Untimely and/or inaccurate delivery of benefits and services due to failure of or inadequate: processes, technology systems, staff actions or data.

**Subrisk A**

- The current technology platform is difficult to manage, expensive to maintain, and increasingly limited as the external environment continues to change. The situation with the current platform steadily risks CalSTRS ability to pay timely and accurate benefits.

**Subrisk B**

- Inability to deliver timely benefits and services due to inaccurate, untimely and incomplete employer reporting including contributions due that are not calculated, reported or remitted by employers

Subrisk A, Mitigation Strategy 1

- Implementation of business practices, and controls required to accurately and efficiently manage benefits and services. Reduce use of overrides, where appropriate. Use estimated payments as allowed under Teachers' Retirement Law
- Target Implementation date - June 2017

Subrisk A, Mitigation Strategy 2

- Deploy additional post-payment review processes to identify outliers using Audit Control Language (ACL) developed (audit sampling and analysis tool)

Subrisk B, Mitigation Strategy 1

- Complete compensation Review Unit reviews

Subrisk B, Mitigation Strategy 2

- Establish monthly analytical reviews of creditable compensation and associated state, employer, and member contributions and establish monthly analytical review packet for creditable employer/member contributions by employer
- Target Implementation date – June 2016

Subrisk B, Mitigation Strategy 3

- Secure Employer Website edits in effect

Subrisk B, Mitigation Strategy 4

- Enforce and Collect Penalties & Interest per Regulations

Subrisk B, Mitigation Strategy 5

- Enhance employer Audits

Subrisk B, Mitigation Strategy 6

- Research availability of payroll information from external sources/pilot submission of payroll control data from volunteer employer.

**Operations- Internal- New System Implementation (Other Than FI\$Cal)**

**CalSTRS Goal** - Transform CalSTRS Pension Administration business processes and tools to a new platform that incorporates current industry best practices.

**CalSTRS Business Objective** - Successfully implement business processes and technology tools to facilitate cost effective, efficient and sustainable processes and systems that enable CalSTRS to serve its members and beneficiaries now and in the future.

**Associated Overall Risk** - Unable to successfully transform the data and business processes within established scope, schedule and budget.

**Subrisk A**

- CalSTRS is unable to implement a new Pension Administration system.

**Subrisk B**

- Lack of cohesive governance practices could result in uninformed and/or lack of decision making on transformational efforts

**Subrisk C**

- Lack of preparation for new system due to inconsistent business practices and policies.

**Subrisk D**

- CalSTRS lacks the ability to successfully implement BusinessRenew due to potential loss of Subject Matter Experts, lack of CalSTRS knowledge, and challenges to recruit for needed skillsets.

**Subrisk E**

- The Pension Solution project will fail to achieve desired results because of a lack of acceptance / project-supporting behaviors from stakeholders.

Subrisk A, Mitigation Strategy 1

- Complete data preparation analysis project, define conversion policies and approach for identified data anomalies, and complete pre-conversion data cleansing.
- Target Implementation date - July 2019

Subrisk A, Mitigation Strategy 2

- Complete the Pension Solution procurement for project.

Subrisk A, Mitigation Strategy 3

- Initiate Pension Solution implementation Project.

Subrisk A, Mitigation Strategy 4

- Utilize Independent Project Oversight Consultant (IPOC).

Subrisk A, Mitigation Strategy 5

- Procure Independent Verification and Validation (IV&V vendor).

Subrisk B, Mitigation Strategy 1

- Utilize Independent Project Oversight Consultant (IPOC).

Subrisk B, Mitigation Strategy 2

- Enterprise Project Governance Committees

Subrisk B, Mitigation Strategy 3

- Board and Executive reporting.

Subrisk B, Mitigation Strategy 4

- Procure IV&V vendor.

Subrisk B, Mitigation Strategy 5

- Implement the Enterprise Information Management (EIM) program.

Subrisk C, Mitigation Strategy 1

- Document inconsistent business practices

Subrisk C, Mitigation Strategy 2

- Implement work plan, schedule, and action plan

Subrisk C, Mitigation Strategy 3

- Submit Enhancement requests to project governance committees

Subrisk C, Mitigation Strategy 4

- Complete policies (new/changes) relating to inconsistent business practices recommendations

Subrisk C, Mitigation Strategy 5

- Identify/Create Procedures for business processes impacted by Inconsistent Business Practice (IBP) recommendations.

Subrisk D, Mitigation Strategy 1

- Acquisition of additional positions through the Budget Change Proposal and spending plan process.

Subrisk D, Mitigation Strategy 2

- Initiate pilot of knowledge transfer and transition resources services.
- Target Implementation date - June 2016

Subrisk D, Mitigation Strategy 3

- Establish and/or modify classification specifications to align with needed competencies within the organization.
- Target Implementation date - June 2016

Subrisk D, Mitigation Strategy 4

- Training and Development plans for staff

Subrisk E, Mitigation Strategy 1

- Organizational Change Management (OCM) Strategy

Subrisk E, Mitigation Strategy 2

- Perform Change Readiness Assessments

Subrisk E, Mitigation Strategy 3

- Communication strategy for Pension Solution project

Subrisk E, Mitigation Strategy 4

- Implementation of recommendations from readiness Assessment and Plan
- Target Implementation date - December 2016

Subrisk E, Mitigation Strategy 5

- Tactical Communication Plan for each Pension Solution project phase

Subrisk E, Mitigation Strategy 6

- Training through out the project lifecycle

**Operations- Internal- Staff—Training, Knowledge, Competence**

**CalSTRS Goal** - Improve the work environment and internal efficiency.

**CalSTRS Business Objective** - Ensure the sustainability of critical business processes and systems.

**Associated Overall Risk** - Inability to achieve business objectives due to lack of compliance with internal controls, lack of accessibility to technology systems, and/or loss of critical staff knowledge.

**Subrisk A**

- In the event of a disaster or disruption CalSTRS may not be able to provide mission critical business processes to our members because CalSTRS does not have DR solutions for some of the critical technology systems identified in the 2008 Business Impact Analysis (BIA).

**Subrisk B**

- CalSTRS does not have solutions in place to mitigate a major technology system outage or partial building outage (e.g. floors not accessible for mission critical business areas) that requires a failover to the secondary infrastructure without bringing down all of the HQ systems. CalSTRS only has the ability to fail over to the Business Resumption Center / Secondary Infrastructure during a full outage of the HQ building. This does not provide solutions to resolve partial building or technology outages.

**Subrisk C**

- Recruitment: CalSTRS lacks the ability to meet critical business functions due to recruitment challenges.

**Subrisk D**

- Knowledge Transfer: CalSTRS lacks the ability to meet critical business functions due to potential loss of Subject Matter Experts and lack of CalSTRS knowledge transfer.

**Subrisk E**

- Employee Turnover: Staff and Leadership turnover could result in lack of long term business

stability and sustainability.

**Subrisk F**

- Missed opportunities to prevent or mitigate risk (for example: due to lack of risk appetite - statements and residual risk metrics)

**Subrisk G**

- Employee health and safety compromised

**Subrisk H**

- Lack of rigorous project management practices could result in increased cost, decreased project activity and inability to meet business objectives.

**Subrisk I**

- Lack of adequate office space for long term growth

Subrisk A, Mitigation Strategy 1

- Create a matrix of 2008 BIA results (critical process and corresponding IT systems) and identify gaps. The information will be used in preparation for the 2015 BIA. (Technology Services, Disaster Recovery)

Subrisk A, Mitigation Strategy 2

- Hire a consultant and conduct a Business Impact Analysis to document all business processes for the organization. After the processes are identified, ascertain which are mission critical processes and their corresponding critical IT systems. (Administrative Services, Business Continuity)

Subrisk A, Mitigation Strategy 3

- Develop a business case/project plan to implement new DR solutions based on 2015 BIA results. (Technology Services)
- Implementation date to be determined after the completion of BIA in December 2015

Subrisk B, Mitigation Strategy 1

- Conduct Risk Assessment of HQ and BRC locations to identify most likely disaster/emergency events and update recovery options for partial building outages where a critical business area is displaced/affected.
- Target Implementation date - December 2015

Subrisk B, Mitigation Strategy 2

- Conduct Technology Risk Assessment for HQ and secondary infrastructure location to identify most likely outage scenarios and determine recovery options for major technology system outages.
- Implementation date to be determined after the completion of BIA in December 2015

Subrisk B, Mitigation Strategy 3

- Fund and implement new recovery options for partial building outages and major technology system outages.
- Implementation date to be determined after the completion of BIA in December 2015

Subrisk C, Mitigation Strategy 1

- Establish and/or modify classification specifications to align with needed competencies within the organization.
- Target Implementation date - July 2016

Subrisk C, Mitigation Strategy 2

- Continue to enhance recruitment strategy to attract a fully diversified workforce.
- Target Implementation date - June 2016

Subrisk D, Mitigation Strategy 1

- Initiate pilot of knowledge transfer and transition resources services.



- Target Implementation date - June 2016

Subrisk D, Mitigation Strategy 2

- Acquisition of temporary positions to support knowledge transfer transition gap.
- Target Implementation date - June 2016

Subrisk D, Mitigation Strategy 3

- Completion of BIA to identify critical functions and business knowledge loss to determine who will be the back-up.
- Target Implementation date - June 2016

Subrisk E, Mitigation Strategy 1

- Implement the Professional Development Program projects identified for year one.

Subrisk E, Mitigation Strategy 2

- Implement the Master Series Development Program
- Target Implementation date - June 2016

Subrisk E, Mitigation Strategy 3

- Implement a pilot Leadership training.
- Target Implementation date - June 2016

Subrisk E, Mitigation Strategy 4

- Develop Manager Onboarding for leadership positions.
- Target Implementation date - June 2016

Subrisk E, Mitigation Strategy 5

- Continue diversity and inclusion efforts.
- Target Implementation date - June 2016

Subrisk F, Mitigation Strategy 1

- Formalize practices for effective oversight of risk.
- Target Implementation date - June 2016

Subrisk F, Mitigation Strategy 2

- Assess and respond to risk at all levels of the organization.
- Target Implementation date - June 2016

Subrisk G, Mitigation Strategy 1

- Ongoing management and oversight of the access to all CalSTRS facilities
- Target Implementation date - Jan 2016

Subrisk G, Mitigation Strategy 2

- Review the workplace violence policy for external threats and update at necessary
- Target Implementation date - December 2016

Subrisk G, Mitigation Strategy 3

- Continue to enhance employee wellness program at all CalSTRS facilities
- Target Implementation date - July 2016

Subrisk G, Mitigation Strategy 4

- Continue performing annual fire drills and training of BERT team at all CalSTRS facilities

Subrisk H, Mitigation Strategy 1

- Enhance schedule, risk/issue, resource methodologies to be in alignment with current Project Management best practices and the Project Management Body of Knowledge

(PMBOK).

- Target Implementation date - February 2016

Subrisk H, Mitigation Strategy 2

- Develop implementation plan to enhance CalSTRS Project Management methodology as a result of the Internal Audit recommendations and action plan.
- Target Implementation date - February 2016

Subrisk H, Mitigation Strategy 3

- Enhance project methodology based on audit recommendations.
- Target Implementation date - To be determine after outcome of Mitigation Strategy 2 of Subrisk H

Subrisk H, Mitigation Strategy 4

- Enhance Clarity based on audit recommendations
- Target Implementation date - To be determine after outcome of Mitigation Strategy 2 of Subrisk H

Subrisk H, Mitigation Strategy 5

- Provide training for all PMO staff and project participants on enhanced project management methodologies

Subrisk I, Mitigation Strategy 1

- Examine alternate forms of work organization and workforce planning. Contract with outside vendor to provide workspace strategy options.
- Target Implementation date - December 2015

**Operations- External- Political, Reputation, Media**

**CalSTRS Goal** - Responsibly manage risk to the organization

**CalSTRS Business Objective** - Sustain the trust of our members, stakeholders and the public..

**Associated Overall Risk** - Loss of confidence in CalSTRS as a respected fiduciary of public funds.

**Subrisk A**

- CalSTRS investments might be perceived by the public, media, members and/or stakeholders to be conducting business in an imprudent, unethical, and non-transparent manner.

**Subrisk B**

- Inaccurate external reporting of long-term financial assumptions.

**Subrisk C**

- Perceived pension abuses (i.e., spiking)

**Subrisk D**

- CalSTRS is unable to meet member service expectations

**Subrisk E**

- Board member or staff member engages in unethical behavior

**Subrisk F**

- Failure to implement transformational efforts could impact public confidence.

Subrisk A, Mitigation Strategy 1

- Crisis communication policy requires early identification of problems and development of mitigation strategies.

Subrisk A, Mitigation Strategy 2

- Continue 21 Risk Factor Committee meetings to review sensitive investments.

Subrisk B, Mitigation Strategy 1

- Ensure various assumptions are periodically reviewed, tested and updated

Subrisk B, Mitigation Strategy 2

- Conduct periodic audit of actuarial procedures

Subrisk B, Mitigation Strategy 3

- Respond to need for education (i.e. board, media, constituents.)

Subrisk C, Mitigation Strategy 1

- Conduct thorough investigations of reported abuses (annual whistle blower report)

Subrisk C, Mitigation Strategy 2

- Robust employer reporting Audit program

Subrisk C, Mitigation Strategy 3

- Improve internal controls (i.e. Data mining triggering desk reviews)

Subrisk C, Mitigation Strategy 4

- Planned communication strategy regarding pension abuse

Subrisk C, Mitigation Strategy 5

- Increase News release or posting of activities on spiking on CalSTRS dot com.

Subrisk D, Mitigation Strategy 1

- Flexible and responsive business management plans to shift resources and workload, where needed

Subrisk E, Mitigation Strategy 1

- Set strong ethical tone for the organization through stated and communicated core values.

Subrisk F, Mitigation Strategy 1

- Execute Pension Solution Project communication plan

Subrisk F, Mitigation Strategy 2

- Board and/or Management authority for availability of funds (i.e., Annual spending plan)

Subrisk F, Mitigation Strategy 3

- Integrate lessons learned from other projects and/or failures of similar size and complexity.

Subrisk F, Mitigation Strategy 4

- Create and implement a framework for vendor management
- Target Implementation date - December 2015

## **Operations- External- Economic Volatility**

**CalSTRS Goal** - Ensure a financially sound retirement system

**CalSTRS Business Objective** - Provide for present and future benefit payments

**Associated Overall Risk** - Fund performance objectives not achieved as set in the Investment Policy and Management Plan

### **Subrisk A**

- The fund will not achieve the actuarially expected return over the long term (30 years/Absolute return)

### **Subrisk B**

- The fund will not add value above the total fund benchmarks return over the long term (Relative return)

**Subrisk C**

- CalSTRS will not be able to implement the strategies and tools necessary to manage the risk associated with the more complex and volatile investment environment.

**Subrisk A, Mitigation Strategy 1**

- Coordinate the timing of the asset/liability study and experience study to ensure that the two are in lock-step and that the actuarial investment assumptions reflect the asset allocation policy.

**Subrisk A, Mitigation Strategy 2**

- Continuous oversight and monitoring of fund and asset class strategies and positions using risk management tools and platforms designed for the unique nature of the underlying securities.

**Subrisk A, Mitigation Strategy 3**

- Implement new enterprise (i.e., Investment branch) risk management and reporting platform to capture risk factors and exposures across the Portfolio to complement the asset class risk management tools and platforms. Implementation took place in Fall/Winter 2014 and evaluation started after implementation and will continue through calendar year 2015.
- Target Implementation date - December 2017

**Subrisk B, Mitigation Strategy 1**

- Continuous oversight and monitoring of fund and asset class strategies and positions using risk management tools and platforms designed for the unique nature of the underlying securities.

**Subrisk B, Mitigation Strategy 2**

- Implement new enterprise (i.e., Investment branch) risk management and reporting platform to capture risk factors and exposures across the Portfolio to complement the asset class risk management tools and platforms. Implementation took place in Fall/Winter 2014 and evaluation started after implementation and will continue calendar year 2015.
- Target Implementation date - December 2017

**Subrisk B, Mitigation Strategy 3**

- Monitor costs and operate the Defined Benefit Fund in an efficient and cost effective manner to reduce the drag on fund performance.

**Subrisk C, Mitigation Strategy 1**

- Recruit and retain well qualified staff with a diverse range of skills.

**Subrisk C, Mitigation Strategy 2**

- Continuously engage with our Institutional partners and the academic community regarding best practices in risk management. Review suitability and implementation of best practices at CalSTRS.

**Subrisk C, Mitigation Strategy 3**

- Deploy cross functional/asset class teams with a wide range of expertise and knowledge to review new tools and strategies prior to implementation.

**Subrisk C, Mitigation Strategy 4**

- Secure legislation to improve procurement of investment related products and services.
- Target Implementation date - 2017

### **Operations- External- Political, Reputation, Media**

**CalSTRS Goal** - Ensure a financially sound retirement system

**CalSTRS Business Objective** - Ensure defined benefit program continues to be a foundational component of teacher' retirement.

**Associated Overall Risk** - Negative impacts to funded status of the plan & members' retirement security caused by Legislative changes.

#### **Subrisk**

- Pension reform legislation or initiatives could substantially reduce guaranteed defined benefit provided to members or compromise contractual rights of members thereby creating litigation challenges
- Educate stakeholders and policymakers on the value of the CalSTRS Defined Benefit Program in achieving retirement security.
- Conduct legal review of proposed ballot initiatives and impact of members contractual rights.
- Conduct legal research on contractual provisions of CalSTRS' plans
- Respond to research reports, articles, etc. that assert benefit changes are legally permissible that alter members' contractual rights or challenge the viability of teachers' defined benefit plan.

### **Reporting- Internal- Information Collected—Inadequate, Inaccurate, Misinterpreted, Untimely**

**CalSTRS Goal** - Ensure a financially sound retirement system

**CalSTRS Business Objective** - Ensure accurate and timely financial reporting in compliance with the Teachers' Retirement Law and Governmental Fiscal Standards.

**Associated Overall Risk** - Incomplete or inaccurate financial information; weaknesses in internal control jeopardize an unqualified audit opinion or result in significant non-compliance with standards.

#### **Subrisk A**

- Information received from subsidiary systems is recorded incorrectly for financial statement presentation.

#### **Subrisk B**

- Current staff do not have the adequate resources and training to analyze financial results and research and correct identified issues.

#### **Subrisk C**

- Controls over financially significant systems are inadequate or not consistently operating as designed.

#### **Subrisk D**

- Taxes are not remitted or reported correctly or on a timely basis.

#### **Subrisk A, Mitigation Strategy 1**

- Complete monthly analytical reviews for significant accounts

#### **Subrisk A, Mitigation Strategy 2**

- Monitor clearing account balances daily

Subrisk A, Mitigation Strategy 3

- Consistently reconcile general ledger balances to subsidiary systems and information

Subrisk A, Mitigation Strategy 4

- Research and process non-clearing and reconciling items

Subrisk A, Mitigation Strategy 5

- Monitor SSAE16 review of third parties

Subrisk A, Mitigation Strategy 6

- Prepare for implementation of new GASB Statement regarding Fair Value disclosures.
- Target Implementation date - August 2016

Subrisk A, Mitigation Strategy 7

- Conduct monthly review of the results as presented on CalSTRS financial statements and in Other Pension Information (OPI)

Subrisk B, Mitigation Strategy 1

- Test transactions for control compliance

Subrisk B, Mitigation Strategy 2

- Review and periodically update system documentation and accounting policies for focus on controls

Subrisk B, Mitigation Strategy 3

- Develop an approach related to retaining current employees that have significant analytical and accounting skills.

Subrisk B, Mitigation Strategy 4

- Ensure staff develop and implement annual training plan

Subrisk C, Mitigation Strategy 1

- Perform monthly reviews of access

Subrisk C, Mitigation Strategy 2

- Complete documentation of approvals for all system changes

Subrisk D, Mitigation Strategy 1

- Monitor tax clearing general ledger accounts and proactively monitor zero balance tax sweep bank accounts. Perform analytical reviews of tax reporting and remittances

Subrisk D, Mitigation Strategy 2

- Validate tax withholding compliance for vendor payments made

**Operations- External- Funding—Sources, Levels**

**CalSTRS Goal** - Ensure a financially sound retirement system

**CalSTRS Business Objective** - Ensure the contribution rates provide for long term viability of CalSTRS defined benefit plan

**Associated Overall Risk** - Contribution rates are insufficient to amortize unfunded actuarial liability.

**Subrisk A**

- Failure of board's authority to change contribution rates to be adequate to fully fund the defined benefit program

**Subrisk B**

- Failure of the Board to exercise their authority to adequately fund the Defined Benefit Program to its fullest extent.

**Subrisk C**

- Enactment of Pension Initiative in 2016 could undermine the viability of the Funding Plan.

Subrisk A, Mitigation Strategy 1

- Implement enacted funding legislation.

Subrisk A, Mitigation Strategy 2

- Communicate funding changes to all members and employers.

Subrisk A, Mitigation Strategy 3

- Closely monitor funding levels and communicate to impacted parties.

Subrisk B, Mitigation Strategy 1

- Implement enacted funding legislation.

Subrisk B, Mitigation Strategy 2

- Communicate funding changes to all members and employers.

Subrisk C, Mitigation Strategy 1

- Analyze actuarial impact of current ballot initiative

**Operations- Internal- Oversight, Monitoring, Internal Control Systems**

CalSTRS Goal - Ensure a financially sound retirement system

CalSTRS Business Objective - Ensure accuracy and validity of actuarial methodologies, studies and assumptions.

Associated Overall Risk - Inaccurate actuarial methodologies and assumptions

**Subrisk A**

- Invalid actuarial methodologies negatively affect the fund (Timeframe defined as audit period of five years)

**Subrisk B**

- Incorrect information underlying the actuarial assumptions negatively affects the fund (Short-term defined as next four years; Long-term defined as 75 years)

Subrisk A, Mitigation Strategy 1

- Conduct an Actuarial audit every five years.

Subrisk A, Mitigation Strategy 2

- Maintain the currency of desk manual and procedures.

Subrisk B, Mitigation Strategy 1

- Conduct regular experience studies

Subrisk B, Mitigation Strategy 2

- Continue to follow Governmental Accounting Standards Board rules associated with

assumptions rates for financial reporting valuations.

## **ONGOING MONITORING**

Through our ongoing monitoring processes, the State Teachers' Retirement System reviews, evaluates, and improves our systems of internal controls and monitoring processes. As such, we have determined we comply with California Government Code sections 13400-13407.

### **Roles and Responsibilities**

As the head of State Teachers' Retirement System, Jack Ehnes, Chief Executive Officer, is responsible for the overall establishment and maintenance of the internal control system. We have identified Robin Madsen, Chief Financial Officer, as our designated agency monitor(s).

### **Frequency of Monitoring Activities**

CalSTRS performs ongoing operational quality assurance reviews throughout the organization. Consultants to the Teachers' Retirement Board provide ongoing assessments of the value of the system's assets with particular focus on asset classes where greater risk is anticipated to provide greater returns. An external actuary conducts studies and valuations to assess the funding status of the State Teachers Retirement Plan and associated programs. Every year, Audit Services performs risk based internal audits to ensure operational compliance with applicable policies and procedures.

### **Reporting and Documenting Monitoring Activities**

CalSTRS quality assurance teams share the results of their reviews with management. These reports become part of the enterprise risk assessment process used to identify any deficiencies and mitigate the associated risks of potential weakness in an internal control. The results of internal audits are also shared with management teams and executive staff. They are also part of regular reporting to the Teachers Retirement Board.

### **Procedure for Addressing Identified Internal Control Deficiencies**

Depending on the risk associated with a given identified control deficiencies, CalSTRS approach to addressing an internal control weakness may vary. For example, an identified control deficiency may become part of the enterprise risk management matrix and reported to the board on a semi-annual basis. Audit Services provides the Teachers Retirement Board Audit and Risk Management Committee reports on that status of internal audit findings as well as a report entitled "Progress on the External Financial Auditor's Report on Internal Control - Corrective Actions".

## **CONCLUSION**

The State Teachers' Retirement System strives to reduce the risks inherent in our work through ongoing monitoring. The State Teachers' Retirement System accepts the responsibility to continuously improve by addressing newly recognized risks and revising risk mitigation strategies. I certify our systems of internal control and monitoring processes are adequate to identify and address material inadequacies or material weaknesses facing the organization.

Jack Ehnes, Chief Executive Officer

cc: Department of Finance



Legislature  
State Auditor  
State Library  
State Controller  
Secretary of Government Operations