



YOUR PARTNER



Presentation to the Audit Committee
October 5, 2017





INTRODUCTIONS

KNOWLEDGE

QUALITY

CLIENT SERVICE



Engagement Team Leadership

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SB & Company, LLC

- **William Seymour, Engagement Partner**
- **Graylin Smith, Advisory Partner**
- **Sisilia Mo, Audit Partner**





SUMMARY OF RESULTS

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Scope of Services

- Audit as of June 30, 2017, financial statements
- Review of Comprehensive Annual Financial Report (CAFR)
- Audit of Schedule of Employer and Allocations Collective Pension Amounts (Pension and OPEB)
- Recommendations and observations noted during the audit process
- Year-round discussions on accounting and auditing issues



Summary of the Results

- Issued an unmodified opinion on the financial statements
- We did not discover and were not made aware of any instances of fraud
- No material weaknesses identified
- Received full cooperation from management



AUDIT APPROACH

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FORCAM Audit Approach

“Focus on Risk, Controls and Misstatement”

FORCAM Audit Approach

Focus on Risk, Controls, and Account Misstatement

Agree on Expectations and Deliverables

Planning - Understand the Business & Risk

Client Acceptance • Client Environment • Tone at the Top
Materiality • Initial Risk Assessment • Audit Plan • Client Expectations

Assess & Test Design & Operations of Controls

What Can Go Wrong? • Test Key Controls • Walkthrough
Map Accounts & Transactions • Identify Key Controls

Financial Close & Reporting Misstatement Analysis

Analyze Balances • Financial Close Process
Principles Applied • Management's Verification

Substantive Testing

Negative Account Analysis • Negative Financial Close
Firm & GAAS Required • Significant Estimates
Negative Operating Controls • Unusual Transactions

GAAS Compliance & Reporting

GAAS Checklist • Review Reports • Wrap Up
Draft Board/Management Presentation
Did We Meet Your Expectations?

Goals:

Detect Financial Statement Misstatement Risk
Detect Error

- Accounting Principle
- Estimate
- Information Processing
- Account Balances

Fraud

Business Failure

Business Improvement Opportunities

Client Expectations

Communicate Value Delivered and Measure Satisfaction





Significant Risk Audit Areas

- Participant data completeness & accuracy of census data provided to the actuary
- Actuarial assumptions
- Employer and member contribution process
- Cash disbursement process
- Investment valuation process
- Investment concentration
- Eligibility process
- Benefit payments process
- Change in makeup of investment portfolio




Assessment of Control Environment

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Area	Points to Consider	Result
Control Environment	<ul style="list-style-type: none"> ▪ Key executive integrity, ethics and behavior ▪ Control consciousness and operating style ▪ Commitment to competence ▪ Exercise oversight responsibility ▪ Organizational structure and assignment of authority and responsibility ▪ Enforce accountability 	
Risk Assessment	<ul style="list-style-type: none"> ▪ Define objectives and risk tolerances ▪ Identify, analyze, and respond to risk ▪ Assess fraud risk ▪ Mechanisms to anticipate, identify, and react to significant events ▪ Processes and procedures to identify changes in GAAP, business practices and internal control 	
Control Activities	<ul style="list-style-type: none"> ▪ Design control activities ▪ Design activities for information system ▪ Implement control activities ▪ Existence of necessary policies and procedures ▪ Clear financial objectives with active monitoring ▪ Logical segregation of duties ▪ Adequate safeguards of documents, records and assets ▪ Access controls in place 	

	Not effective
	Suggested Improvements
	Effective



Assessment of Control Environment (continued)

Area	Points to Consider	Result
Information and Communication	<ul style="list-style-type: none">▪ Use quality information▪ Communicate internally▪ Communicate externally▪ Adequate performance reports produced from information system▪ Information systems are connected with business strategy▪ Commitment of the agency to develop, test and monitor IT systems and programs▪ Business continuity/disaster plan for IT▪ Established communication channels for employees to fulfill responsibilities▪ Adequate communication across organization	
Monitoring	<ul style="list-style-type: none">▪ Perform monitoring activities▪ Remediate deficiencies▪ Periodic evaluations of internal controls (annual audit)▪ Implementation of improvement recommendations▪ Internal audit department	





Evaluation of Key Processes

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Process	Function	A	B	C	D	E	Design	Operation
Financial Reporting	<ul style="list-style-type: none"> Accounting Principles and Disclosure Closing the Books General Ledger and Journal Entry Processing Verification and Review of Results 	✓	✓	✓		✓		
Investments	<ul style="list-style-type: none"> Cash Management Investment Accounting Investment Valuation Policy Compliance Investment Manager Monitoring 	✓	✓	✓	✓	✓		
Investment Income	<ul style="list-style-type: none"> Estimation Reporting Methodology 	✓	✓	✓	✓	✓		

A	Understand the Process
B	Walk-Through
C	What Can Go Wrong

D	Test of Controls
E	Substantive Testing

	Not effective
	Suggested improvements
	Effective



Evaluation of Key Processes

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Process	Function	A	B	C	D	E	Design	Operation
Estimation	<ul style="list-style-type: none"> Methodology Information Calculation 	✓	✓	✓		✓		
Benefit Payable	<ul style="list-style-type: none"> Calculation Verification Disbursement 	✓	✓	✓	✓	✓		
Actuarial Information	<ul style="list-style-type: none"> Participant Data and Census Data Estimation and Assumption Reporting Methodology Calculation 	✓	✓	✓	✓			
Contributions	<ul style="list-style-type: none"> Employer Reporting/ Accounting Cash Receipts 	✓	✓	✓	✓			

A	Understand the Process
B	Walk-Through
C	What Can Go Wrong

D	Test of Controls
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	Not effective
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Evaluation of Key Processes

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Process	Function	A	B	C	D	E	Design	Operation
Information Technology	<ul style="list-style-type: none"> Program Integrity and Change Management Information Security and Transaction Authorization Segregation of Duties and Management Oversight Computer Operations 	✓	✓	✓	✓			
Administrative Expenditures	<ul style="list-style-type: none"> Purchasing Receiving Accounts Payable/Cash Disbursement 	✓	✓	✓	✓			

A	Understand the Process
B	Walk-Through
C	What Can Go Wrong

D	Test of Controls
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	Not effective
	Suggested improvements
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AUDIT RESULTS

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Statements of Fiduciary Net Position

As of June 30, 2017

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	Pension	Postemployment Healthcare		Totals
		Premium Assistance	Health Options Program	
Assets:				
Receivables:				
Members	\$ 346,618	\$ 3,057	\$ 36	\$ 349,711
Employers	1,067,100	30,540	-	1,097,640
Investment income	150,626	112	84	150,822
Investment proceeds	864,326	-	-	864,326
CMS Part D and Prescriptions	-	-	67,126	67,126
Interfund receivable	-	7,217	-	7,217
Total Receivables	2,428,670	40,926	67,246	2,536,842
Investments, at fair value:				
Short-term	5,804,352	82,917	219,751	6,107,020
Fixed income	4,961,284	-	-	4,961,284
Common and preferred stock	11,337,865	-	-	11,337,865
Collective trust funds	12,816,147	-	-	12,816,147
Real estate	5,340,555	-	-	5,340,555
Alternative investments	11,922,940	-	-	11,922,940
Total Investments	52,183,143	82,917	219,751	52,485,811
Securities lending collateral pool	2,016,063	-	-	2,016,063
Capital assets (net of accumulated depreciation)	24,001	-	-	24,001
Miscellaneous	16,903	255	93	17,251
Total Assets	56,668,780	124,098	287,090	57,079,968
Liabilities:				
Accounts payable and accrued expenses	92,777	272	2,288	95,337
Benefits payable	529,833	83	24,539	554,455
HOP participant premium advances	-	-	32,396	32,396
Investment purchases and other liabilities	800,996	-	-	800,996
Obligations under securities lending	2,016,063	-	-	2,016,063
Interfund Payable	7,217	-	-	7,217
Other liabilities	66,558	-	-	66,558
Total Liabilities	3,513,444	355	59,223	3,573,022
Net position held in trust for pension and postemployment healthcare benefits:	\$ 53,155,336	\$ 123,743	\$ 227,867	\$ 53,506,946



Statements of Changes In Fiduciary Net Position For the Year Ended June 30, 2017

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	Pension	Postemployment Healthcare		Totals
		Premium Assistance	Health Options Program	
Additions:				
Contributions:				
Members	\$ 1,013,847	\$ -	\$ -	\$ 1,013,847
Employers	3,832,773	110,985	-	3,943,758
Total contributions	4,846,620	110,985	-	4,957,605
HOP participant premiums	-	-	336,646	336,646
Centers for Medicare & Medicaid Services premiums	-	-	73,771	73,771
Investment income:				
From investing activities:				
Net appreciation (depreciation) in fair value of investments	4,204,585	(337)	-	4,204,248
Short-term	67,694	1,024	704	69,422
Fixed income	156,837	-	-	156,837
Common and preferred stock	295,427	-	-	295,427
Collective trust funds	3,379	-	-	3,379
Real estate	236,650	-	-	236,650
Alternative investments	493,426	-	-	493,426
Total investment activity income	5,457,998	687	704	5,459,389
Investment expenses	(474,441)	(24)	(26)	(474,491)
Net income from investing activities	4,983,557	663	678	4,984,898
From securities lending activities:				
Securities lending income	21,395	-	-	21,395
Securities lending expense	(9,590)	-	-	(9,590)
Net income from securities lending activities	11,805	-	-	11,805
Total net investment income	4,995,362	663	678	4,996,703
Total Additions	9,841,982	111,648	411,095	10,364,725
Deductions:				
Benefits	6,452,651	110,229	340,096	6,902,976
Refunds of contributions	20,928	-	-	20,928
Administrative expenses	45,127	2,239	37,071	84,437
Total Deductions	6,518,706	112,468	377,167	7,008,341
Net increase (decrease)	3,323,276	(820)	33,928	3,356,384
Net position held in trust for pension and postemployment healthcare benefits:				
Balance, beginning of year	49,832,060	124,563	193,939	50,150,562
Balance, end of year	\$ 53,155,336	\$ 123,743	\$ 227,867	\$ 53,506,946



New Accounting Pronouncements

GASB Statement No. 74, Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans

- Implemented fiscal year June 30, 2017
- Similar to the requirements for the pension
- Additional disclosure for sensitivity of medical cost inflation
- Additional schedules to be provided to employers to allocate liabilities, deferred inflow/outflow, and OPEB expenses.



New Accounting Pronouncements

GASB Statement No. 75, Accounting and Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans

- Effective fiscal year June 30, 2018
- Similar to the requirements for the pension
- Recording of allocated liabilities, deferred inflow/outflow, and OPEB expenses
- Additional required supplemental information



REQUIRED COMMUNICATION

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Required Communications

1. Auditor's Responsibilities Under Generally Accepted Auditing Standards (GAAS)

The financial statements are the responsibility of management. Our audit was designed in accordance with auditing standards generally accepted in the United States of America, and provide for reasonable, rather than absolute, assurance that the financial statements are free of material misstatement.

2. Significant Accounting Policies

Management has the responsibility for selection and use of appropriate accounting policies. In accordance with the terms of our engagement letter, we will advise management about the appropriateness of accounting policies and their application.

The significant accounting policies used by management are described in the notes to the financial statements.

3. Auditor's Judgments About the Quality of Accounting Principles

We discuss our judgments about the quality, not just the acceptability, of accounting principles selected by management, the consistency of their application, and the clarity and completeness of the financial statements, which include related disclosures.

We have reviewed the significant accounting policies adopted by the Public School Employees' Retirement System (PSERS), and have determined that these policies are acceptable accounting policies.



Required Communications (continued)

4. Audit Adjustments

We are required to inform PSERS oversight body about adjustments arising from the audit (whether recorded or not) that could in our judgment either individually or in the aggregate have a significant effect on the entity's financial reporting process. We also are required to inform PSERS oversight body about unadjusted audit differences that were determined by management to be individually and in the aggregate, immaterial.

There were no significant adjustments identified during the audit process.

5. Fraud and Illegal Acts

We are required to report to PSERS oversight body any fraud and illegal acts involving senior management and fraud and illegal acts (whether caused by senior management or other employees) that cause a material misstatement of the financial statements.

Our procedures identified no instances of fraud or illegal acts.

6. Material Weaknesses in Internal Control

We are required to communicate all significant deficiencies in the PSERS's systems of internal controls, whether or not they are also material weaknesses.

There were no material weaknesses noted during the audit.



Required Communications (continued)

7. Other Information in Documents Containing Audited Financial Statements

None.

8. Disagreements with Management on Financial Accounting and Reporting Matters

None.

9. Serious Difficulties Encountered in Performing the Audit

None.

10. Major Issues Discussed with Management Prior to Acceptance

None.

11. Management Representations

We received certain written representations from management as part of the completion of the audit.

12. Consultation with Other Accountants

To our knowledge, there were no consultations with other accountants since our appointment as the PSERS's independent public accountants.



Required Communications (continued)

13. Independence

As part of our client acceptance process, we go through a process to ensure we are independent of the PSERS.

We are independent of PSERS.

14. Non-attest Services

None.



Required Communications (continued)

15. Our Responsibility Related to Fraud

- Plan and perform the audit to obtain reasonable assurance that there is no material misstatement caused by error or fraud;
- Comply with AU-C Section 240: Consideration of Fraud in a Financial Statement Audit;
- Approach all audits with an understanding that fraud could occur in any entity, at any time, by anyone; and
- Perform mandatory procedures required by GAAS and our firm policies.

Examples of Procedures Performed

- Discuss thoughts and ideas on where the financial statements might be susceptible to material misstatement due to fraud;
- Understand pressures on the financial statement results;
- Understand the tone and culture of the organization;
- Look for unusual or unexpected transactions, relationships, or procedures;
- Discussions with individuals outside of finance;
- Evaluate key processes and controls; and
- Consider information gathered throughout the audit.



QUESTIONS

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