2022 Independent Financial Statement Auditor's Management Letter Progress Report as of January 2023

DESCRIPTION OF DEFICIENCY:

Member Data is fundamental to financial reporting of contributions, benefit payments, and the Total and Net Pension Liability of the State Teachers Retirement Plan (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 the 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 risk of incorrect member data.

IMPLEMENTATION UPDATE

CalSTRS continues to maintain focus on providing education and continuing improvements to tools and resources for employers to assist them in their ultimate responsibility for the accurate reporting of member data, with an emphasis on common and avoidable misreporting and reaching larger audiences of employer partners (e.g., charter schools).

Data Analytics

The Financial Services Branch continues to conduct periodic reviews of cash contributions from employer report sources. In these reviews, management analyzes the cash contributions for anomalies and variances that could indicate misreported contribution information. Management applies thresholds for common reporting error types, such as special compensation, monitoring for trends or unexpected changes from past cash contributions. Financial Services then partners with Employer Services who reach out to employers to seek more information about the nature of the potentially incorrect reporting and provide guidance to correct any errors.

Leadership, in conjunction with Technology Services peers, created new tools to increase productivity related to analyzing the employer reporting that triggers exceptions based on business rules. Analysis of these system edits can result in follow-up inquiries to our employer partners about the reporting to verify the basis for the exceptions. Management will be implementing the recommendations from the project, increasing the frequency, efficiency, and quality of our Employer Approved Edit review process during the remainder of FY22/23.

The Employer Help team follows up on completed audits six months after an audit closes to validate that the employer continues to report accurately based on the audit findings. This mitigates the risk of employers continued misreporting after being audited. If staff discovers any errors, they notify the employer requesting changes to comply with the previously completed audit. The Employer Help team completed 27 of these follow-up reviews from October 2022 through January 2023.

In addition, to support the outcomes from the Employer Reporting to Final Benefit project, management plans to formalize the proof-of-concept approach to review members' accounts for accuracy prior to receiving a benefit. Each year, staff would sample a significant percentage of accounts for members who have submitted retirement applications. This way, any potential errors or inaccuracies could be resolved with the employer prior to the benefit starting and reducing the risk of a change after retirement. The Teachers' Retirement Board approved the FY23/24 budget that includes positions to formally establish this effort, with recruitment planned for July 2023.

Training and Education Strategies

The most complex reporting inquiries related to educating employer partners on complicated topics escalate to the Training and Development (TaD) team. Shifting this work from Employer Help to TaD has improved response time and consistency of the responses. From October 2022 to January 2023, the team received 467 of these complex inquiries. During this period, management began surveying our employer partners about their satisfaction with the service, resulting in a 95% satisfaction rate. The team uses these complex inquiries to inform employer training needs and identify trends.

Management continues its pilot of a quality management program to, initially, review 10% of the complex inquiry responses for accuracy. From October 2022 to December 2022, staff reviewed

54 inquiries against standards and 98% of them met the standards set in the pilot plan. Beginning in February, the pilot is expanding to include larger volumes and more types of employer inquiries and interactions. There will be four staff participating in reviews. The approach remains to extend the process to other parts of our reporting including Employer Approved Edits, standardizing employer communication, the work order process and many of our workloads that impact employer reporting in Employer Help and the division. The Teachers' Retirement Board approved the FY23/24 budget that includes positions to formally establish this Quality Management team, with recruitment planned for July 2023.

Employer training staff in Employer Services delivered 16 trainings from October 2022 through January 2023, serving 264 employer attendees. Staff have added new computer-based training modules to the learning management system and the training team has updated our existing job aids and created more interactive job aids to assist employers in determining the credibility of compensation.

Employer Readiness

The Employer Readiness Team in Employer Services continues to support our employer partners in submitting test New File Format reporting into the Employer Readiness Environment for the new Benefit Connect system. The Team assists both employer partners with custom systems and those who use payroll system vendors. Using the readiness environment allows employers to understand the new format and business rules for contribution data and it can uncover unexpected system behavior which management escalates to the project for fixes and enhancements. The Employer Readiness Team conducted state-wide webinars in late summer to provide project and system status updates to maintain employer engagement with the effort.