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BROWN ARMSTRONG
*Certified Public Accountants*

# INDEPENDENT AUDITOR'S REPORT

To the Audit Committee and Board of Retirement of
Fresno County Employees' Retirement Association
Fresno, California

## Report on the Financial Statements

We have audited the accompanying Statement of Fiduciary Net Position of the Fresno County Employees' Retirement Association (FCERA) as of fiscal years ended June 30, 2015 and 2014, the related Statement of Changes in Fiduciary Net Position for the fiscal years then ended, and the related notes to the financial statements, which collectively comprise FCERA's basic financial statements as listed in the table of contents.

## Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

## Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards,* issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to FCERA's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of FCERA's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the basic financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

## Opinion

In our opinion, the basic financial statements referred to above present fairly, in all material respects, the fiduciary net position of FCERA as of fiscal years ended June 30, 2015 and 2014, and the changes in fiduciary net position for the fiscal years then ended in conformity with accounting principles generally accepted in the United States of America.

## Emphasis of Matter

As discussed in Note 2 to the basic financial statements, the total pension liability of the participating employers as of June 30, 2015, was $5,117,241,000. The fiduciary net position as a percentage of the total liability as of June 30, 2015, was 78.79%. The actuarial valuations are very sensitive to the underlying actuarial assumptions, including a discount rate of 7.25%, which represents the long-term expected rate of return. Our opinion is not modified with respect to this matter.

Additionally, as discussed in Note 2 to the financial statements, the financial statements include investments that are not listed on national exchanges or for which quoted market prices are not available. These investments include private equity, real estate, hedge funds, and private credit. Such investments totaled $724,239,000 (17.1% of total assets) at June 30, 2015. Where a publicly listed price is not available, the management of FCERA uses alternative sources of information including audited financial statements, unaudited interim reports, independent appraisals, and similar evidence to determine the fair value of the investments. Our opinion is not modified with respect to these matters.

## Other Matters

*Required Supplementary Information*

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis and required supplementary information, as listed in the table of contents, be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

*Other Supplementary Information*

Our audit was conducted for the purpose of forming an opinion on the financial statements of FCERA that collectively comprise FCERA's basic financial statements. The other supplementary information and the introductory, investment, actuarial, and statistical sections, as listed in the table of contents, are presented for purposes of additional analysis and are not a required part of the basic financial statements.

The other supplementary information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used in the basic financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the other supplementary information is fairly stated, in all material respects, in relation to the basic financial statements as a whole.

The introductory, investment, actuarial, and statistical sections have not been subjected to the auditing procedures applied in the audit of the basic financial statements and, accordingly, we do not express an opinion or provide any assurance on them.

**Other Reporting Required by *Government Auditing Standards***

In accordance with *Government Auditing Standards*, we have also issued our report dated December 9, 2015, on our consideration of FCERA's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and other matters. The purpose of that report is 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 internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering FCERA's internal control over financial reporting and compliance and should be considered in assessing the results of our audit.

BROWN ARMSTRONG
ACCOUNTANCY CORPORATION

Brown Armstrong
Accountancy Corporation

Bakersfield, California
December 9, 2015

# FRESNO COUNTY EMPLOYEES' RETIREMENT ASSOCIATION

## REPORT TO THE AUDIT COMMITTEE AND BOARD OF RETIREMENT

## FOR THE FISCAL YEAR ENDED JUNE 30, 2015

**FRESNO COUNTY EMPLOYEES'**
**RETIREMENT ASSOCIATION**

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BROWN ARMSTRONG
*Certified Public Accountants*

# INDEPENDENT AUDITOR'S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH *GOVERNMENT AUDITING STANDARDS*

To the Audit Committee and Board of Retirement of
Fresno County Employees' Retirement Association
Fresno, California

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the Fresno County Employees' Retirement Association (FCERA), as of and for the fiscal year ended June 30, 2015, and the related notes to the financial statements, which collectively compromise FCERA's basic financial statements, and have issued our report thereon dated December 9, 2015.

**Internal Control Over Financial Reporting**

In planning and performing our audit of the financial statements, we considered FCERA's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of FCERA's internal control. Accordingly, we do not express an opinion on the effectiveness of FCERA's internal control.

A *deficiency in internal control* 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. A *material weakness* is a deficiency, or a combination of deficiencies in internal control, such that there is a reasonable possibility that a material misstatement of FCERA's financial statements will not be prevented, or detected and corrected on a timely basis. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

**Compliance and Other Matters**

As part of obtaining reasonable assurance about whether FCERA's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, and contracts, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

We noted certain matters that we reported to management of FCERA in a separate letter dated December 9, 2015.

**Purpose of this Report**

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

BROWN ARMSTRONG
ACCOUNTANCY CORPORATION

Brown Armstrong
Accountancy Corporation

Bakersfield, California
December 9, 2015

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# REQUIRED COMMUNICATION TO THE AUDIT COMMITTEE AND BOARD OF RETIREMENT IN ACCORDANCE WITH PROFESSIONAL STANDARDS

To the Audit Committee and Board of Retirement of
Fresno County Employees' Retirement Association
Fresno, California

We have audited the financial statements of the Fresno County Employees' Retirement Association (FCERA) for the fiscal year ended June 30, 2015, and have issued our report thereon dated December 9, 2015. Professional standards require that we provide you with information about our responsibilities under auditing standards generally accepted in the United States of America and *Government Auditing Standards*, as well as certain information related to the planned scope and timing of our audit. We have communicated such information in our engagement letter to you dated June 19, 2014. Professional standards also require that we communicate to you the following information related to our audit.

## Significant Audit Findings

*Qualitative Aspects of Accounting Practices*
Management is responsible for the selection and use of appropriate accounting policies. The significant accounting policies used by FCERA are described in Note 2 to the financial statements. No new accounting policies were adopted and the application of existing policies was not changed during the fiscal year. We noted no transactions entered into by FCERA during the fiscal year for which there is a lack of authoritative guidance or consensus. All significant transactions have been recognized in the financial statements in the proper period.

Accounting estimates are an integral part of the financial statements prepared by management and are based on management's knowledge and experience about past and current events and assumptions about future events. Certain accounting estimates are particularly sensitive because of their significance to the financial statements and because of the possibility that future events affecting them may differ significantly from those expected. The most sensitive estimate affecting the financial statements was the fair value of investments.

- Management's estimate of the fair value of investments is derived by various methods as detailed in Note 2 to the financial statements. We evaluated the key factors and assumptions used to develop the fair value of investments in determining that it is reasonable in relation to the financial statements taken as a whole.

- The contribution amounts and net pension liability is based on the actuarially-presumed interest rate and assumptions. We evaluated the key factors and assumptions used to develop the net pension liability in determining the reasonableness in relation to the financial statements taken as a whole.

Certain financial statement disclosures are particularly sensitive because of their significance to financial statement users. The most sensitive disclosures affecting the financial statements were:

- The disclosures for deposits and investments in Notes 2 and 3 to the financial statements, Summary of Significant Accounting Policies and Deposits and Investments, respectively, were derived from FCERA's investment policy. Management's estimate of the fair value of investments was derived by various methods as detailed in the notes.

- Additionally, the disclosures related to the funding policies, net pension liability, and actuarial methods and assumptions in Note 2 Summary of Significant Accounting Policies, Note 6 Contributions and Reserves, and Note 7 Actuarial Valuations, were derived from the actuarial valuations, which involved estimates of the value of reported amounts and probabilities about the occurrence of future events far into the future.

*Difficulties Encountered in Performing the Audit*
We encountered no significant difficulties in dealing with management in performing and completing our audit.

*Corrected and Uncorrected Misstatements*
Professional standards require us to accumulate all known and likely misstatements identified during the audit, other than those that are clearly trivial, and communicate them to the appropriate level of management. Management has corrected all such misstatements. The attached schedule summarizes the misstatements detected as results of our audit procedures that were corrected by management.

*Disagreements with Management*
For purposes of this letter, professional standards define a disagreement with management as a financial accounting, reporting, or auditing matter, whether or not resolved to our satisfaction, that could be significant to the financial statements or the auditor's report. We are pleased to report that no such disagreements arose during the course of our audit.

*Management Representations*
We have requested certain representations from management that are included in the Management Representation Letter dated December 9, 2015.

*Management Consultations with Other Independent Accountants*
In some cases, management may decide to consult with other accountants about auditing and accounting matters, similar to obtaining a "second opinion" on certain situations. If a consultation involves application of an accounting principle to the FCERA financial statements or a determination of the type of auditor's opinion that may be expressed on those statements, our professional standards require the consulting accountant to check with us to determine that the consultant has all the relevant facts. To our knowledge, there were no such consultations with other accountants.

*Other Audit Findings or Issues*
We generally discuss a variety of matters, including the application of accounting principles and auditing standards, with management each year prior to retention as FCERA's auditors. However, these discussions occurred in the normal course of our professional relationship and our responses were not a condition to our retention.

*Other Matters*
We applied certain limited procedures to the Schedule of Employer Contributions, Schedule of Investment Returns, Latest Actuarial Valuation Methods, and Schedule of Changes in Net Pension Liability and Related Ratios, which are required supplementary information (RSI) that supplements the basic financial statements. Our procedures consisted of inquiries of management regarding the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during the audit of the basic financial statements. We did not audit the RSI and do not express an opinion or provide any assurance on the RSI.

We were engaged to report on the Schedule of Administrative Expenses, Administrative Budget Analysis, Schedule of Investment Expenses, and Schedule of Payments to Consultants, which accompany the financial statements but are not RSI. With respect to this other supplementary information, we made certain inquiries of management and evaluated the form, content, and methods of preparing the information to determine that the information complies with accounting principles generally accepted in the United States of America, the method of preparing it has not changed from the prior period, and the information is appropriate and complete in relation to our audit of the financial statements. We compared and reconciled the supplementary information to the underlying accounting records used to prepare the financial statements or to the financial statements themselves.

We were not engagement to report on the introductory, investment, actuarial, and statistical sections, which accompany the financial statements but are not RSI. We did not audit or perform other procedures on this other information and we do not express an opinion or provide any assurance on it.

**Restricted on Use**

This report is intended solely for the information and use of the Audit Committee, Board of Retirement, and management of FCERA, and is not intended to be and should not be used by anyone other than these specified parties.

BROWN ARMSTRONG
ACCOUNTANCY CORPORATION

Brown Armstrong
Accountancy Corporation

Bakersfield, California
December 9, 2015

**FCERA**
**SUMMARY OF ADJUSTED AUDIT DIFFERENCE**
**6/30/2015**

| Adjusting Journal Entries JE # 1 | Adjustment |
|---|---|
| Securites lending adjustment to remove Non-Cash Collateral. | |
| 10277 - Cash Collateral Held for Loaned Securities Lending | (37,267,689) |
| 10801 - Cash Collateral Payable Held for Loaned Securities Lending | 37,267,689 |

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## AGREED UPON CONDITIONS REPORT DESIGNED TO INCREASE EFFICIENCY, INTERNAL CONTROLS, AND/OR FINANCIAL REPORTING

To the Audit Committee and Board of Retirement of
Fresno County Employees' Retirement Association
Fresno, California

In planning and performing our audit of the financial statements of Fresno County Employees' Retirement Association (FCERA) for the year ended June 30, 2015, in accordance with auditing standards generally accepted in the United States of America; we considered FCERA's internal control structure over financial reporting (internal control) as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of FCERA's internal control. Accordingly, we do not express an opinion on the effectiveness of FCERA's internal control.

A deficiency in internal control 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. A material weakness is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis.

Our consideration of internal control was for the limited purpose described in the first paragraph 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 such deficiencies have been identified. In addition, because of inherent limitations in internal control, including the possibility of management override of controls, misstatements due to error or fraud may occur and not be detected by such controls. We did not identify any deficiencies in internal control that we considered to be material weaknesses.

However, during our audit we became aware of three matters that are opportunities for strengthening internal controls and operating efficiency. The recommendations that are listed in this report summarize our comments and suggestions regarding these matters.

We will review the status of these comments during our next audit engagement. We have already discussed these comments and suggestions with various FCERA personnel, and we will be pleased to discuss them in further detail at your convenience, to perform any additional study of these matters, or to assist you in implementing the recommendations.

## I. CURRENT YEAR CONDITIONS AND RECOMMENDATIONS

### Condition Number 1 – Pension System

At January 1, 2013, Tier V was mandated by the State and implemented by FCERA in April 2013 retroactively to January 2013. FCERA was in the process of implementing a new pension administration system and elected to not update the existing pension administration system to accommodate the Tier V requirements. As a result. FCERA's posting of payroll transmittal imports into the pension system that tracks participant's salary and contributions were delayed since December 31, 2012. It was determined the new pension system, Arrivos, would be programmed, tested, and used to implement Tier V. During the prior year, FCERA implemented manual procedures for processing withdrawals and retirements which will need to be recorded and verified once the new pension system's programming and implementation is finished.

Since the information recorded in the pension system is used as the source for updating the member data to be used by FCERA staff for calculation of retirement and withdrawal of contributions, failure to keep accurate member data might result in over (under) payments of benefits.

Recommendations

Once programming and implementation for the new pension system is completed and member information can be imported into the system, we recommend FCERA re-calculate all withdrawal of contributions, new retirements, and new pension rates implemented since January 1, 2013.

Views of Responsible Officials and Planned Corrective Action

The Payroll Unit has recalculated the withdrawal of contributions from June 30, 2012 to November 2014. The recalculation of new retirements has been started by the Benefits Unit. The coordinators have prioritized the adjustments, processing the adjustments that have a large dollar or hour amount first. This prioritization will change each month, moving the next highest dollar or hour amount up. The last adjustments will be for the reserve funding, as these do not impact the retirees benefit payment. With limited staff, this is expected to be completed in August 2016. The tables for all pension rates have been reviewed.

### Condition Number 2 – Dynamics NAV Financial Reporting System User Access

During the Information Technology (IT) review of Dynamics NAV financial reporting system, we noted the user accounts needing to post transactions in Dynamics NAV have been granted administrative rights to the application. Administrative rights to the Dynamics NAV application increases the risk that unauthorized activities could occur undetected.

Recommendations

We recommend FCERA create a new security role in Dynamics NAV which allows users to post transactions, but does not grant administrative access which allows full access to the program including modification, which is not needed for daily procedures. This approach will allow users to have the access they need to complete their job duties, but does not increase the risk for unauthorized activities.

Views of Responsible Officials and Planned Corrective Action

FCERA has added a second Systems and Procedures Analyst, Kim Zepeda, to directly assist the Accounting Unit with Dynamics NAV related issues. Ms. Zepeda has been tasked with working with FCERA's Dynamics NAV vendor, SCS, to create the appropriate security role in Dynamics NAV, which allows the Accountants to post transactions but prevents SUPER (Administrative) access. Ms. Zepeda will be attended Dynamics NAV specific training in August 2015. Following this training, the new security role will be created, tested, and implemented by December 31, 2015.

**Condition Number 3 – Pension Administration System User Access**

During our review of the newly implemented Pension Administration System, Arrivos, we noted that the assistant retirement administrator, benefits manager, systems and procedures analysts were assigned to the Arrivos Admin role, which grants the users full access to all system functionality including security administration of user accounts and assigned permissions. Security administration duties should be segregated from processing transaction responsibilities to ensure that unauthorized activities occur undetected.

Recommendations

It is recommended that FCERA consider creating a new role which allows users appropriate access to process transactions without having security administrative access. This approach will ensure that users have the access they need to complete their job duties but doesn't increase the risk for unauthorized activities.

Views of Responsible Officials and Planned Corrective Action

FCERA will explore options that would further reduce access between administration and transactional activity within the Arrivos Pension Administration System.

## II. DISPOSITION OF PRIOR YEAR CONDITIONS AND RECCOMENDATIONS

**Condition Number 1 – Pension System**

At January 1, 2013, Tier V was mandated by the State and implemented by FCERA in April 2013 retroactively to January 2013. FCERA was in the process of implementing a new pension administration system and elected to not update the existing pension administration system to accommodate the Tier V requirements. As a result FCERA's posting of payroll transmittal imports into the pension system that tracks participant's salary and contributions were delayed since December 31, 2012. It was determined the new pension system, Arrivos, would be programmed, tested, and used to implement Tier V. During the prior year, FCERA implemented manual procedures for processing withdrawals and retirements which will need to be recorded and verified once the new pension system's programming and implementation is finished.

Since the information recorded in the pension system is used as the source for updating the member data to be used by FCERA staff for calculation of retirement and withdrawal of contributions, failure to keep accurate member data might result in over (under) payments of benefits.

Recommendations

Once programming and implementation for the new pension system is completed and member information can be imported into the system, we recommend FCERA re-calculate all withdrawal of contributions, new retirements, and new pension rates implemented since January 1, 2013.

Views of Responsible Officials and Planned Corrective Action

FCERA began uploading the payroll transmittal files in November 2014 with an anticipated finish to be current by mid-January 2015. Once the Arrivos system is current, staff will be re-calculating the withdrawals of contributions and retirements effective from January 1, 2013.

Current Year Status

See current year recommendation #1.

**Condition Number 2 – Travel Expenses**

When processing travel expenses for employees, we noted the controls in place are not sufficient to prevent over-reimbursement due to expenses paid on FCERA issued credit cards. One employee included in their personal expenses a receipt from his FCERA issued credit card in the amount of $7.18. Employees are not to receive reimbursements for company issued credit cards.

Recommendations

We recommend FCERA implement a procedure to compare expense report receipts to the credit card statement that pertains to the employee's charge. This will eliminate the oversight of the employee giving a receipt for a personal expense when in fact it is a charge on an FCERA issued credit card, which cannot be reimbursed. This would occur during the current review in place that has department approval sign off on the travel expense claim and will need access to credit card statements for their review.

Views of Responsible Officials and Planned Corrective Action

FCERA appreciates the recommendation. Instead of reviewing statements, FCERA views reviewing the last 4 of the credit card on the receipts against FCERA's credit card list sufficient to prevent a FCERA expense from being reimbursed to an employee.

Current Year Status

Receipts are compared to the credit card statement that pertains to the employee to eliminate mistakes of the employee giving a receipt for an expense when in fact it is a FCERA issued credit card expense. Card holder expenses are reviewed by someone other than the card holder. For example – the Administrator's expenses are reviewed by the Chair of the Board.

**Condition Number 3 – User Access**

During the Information Technology (IT) review of Dynamics NAV financial reporting system, we noted the user accounts needing to post transactions in Dynamics NAV have been granted administrative rights to the application. Administrative rights to the Dynamics NAV application increases the risk that unauthorized activities could occur undetected.

Recommendations

We recommend FCERA create a new security role in Dynamics NAV which allows users to post transactions, but does not grant administrative access which allows full access to the program including modification which is not needed for daily procedures. This approach will allow users to have the access they need to complete their job duties, but does not increase the risk for unauthorized activities.

Views of Responsible Officials and Planned Corrective Action

FCERA accounting staff believes the risk that unauthorized activities could occur are extremely low due to existing review procedures currently in place. However, FCERA- will work with its Dynamics NAV vendor, SCS, to evaluate available options to set additional security levels for the Accountants. Improved security levels might allow for posting journal entries, creation of account numbers and descriptions, creation of dimension values and year end close processing while preventing full access if possible.

Current Year Status

See current year recommendation #2.

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This information is intended solely for the use of the Audit Committee, Board of Retirement, and management of FCERA and is not intended to be, and should not be, used by anyone other than these specified parties.

BROWN ARMSTRONG
ACCOUNTANCY CORPORATION

Brown Armstrong
Accountancy Corporation

Bakersfield, California
December 9, 2015