



Memorandum

TO: HONORABLE MAYOR
AND CITY COUNCIL

FROM: Maria Öberg

SUBJECT: See Below

DATE: November 17, 2025

Approved

Date:

11/14/25

COUNCIL DISTRICT: Citywide

SUBJECT: External Auditor's Report: Report to Those Charged with Governance for the Year Ended June 30, 2025

RECOMMENDATION

Accept the External Auditor's Report to Those Charged with Governance for the year ended June 30, 2025, as issued by Macias Gini & O'Connell LLP, the City's external auditor.

SUMMARY AND OUTCOME

The Report to Those Charged with Governance is a required communication between the City of San José's external auditor and the City Council. It aims to enhance transparency, clarify responsibilities, disclose significant audit matters, and promote accountability in the auditing process.

BACKGROUND

The City's external auditor (Auditor) is responsible for communicating significant matters related to the audit that are relevant to the City Council's responsibility in overseeing the financial reporting process. The Report to Those Charged with Governance is presented concurrently with the Annual Comprehensive Financial Report.

ANALYSIS

Attached for the City Council's review is the Report to Those Charged with Governance for the Year Ended June 30, 2025.

Report to Those Charged with Governance

During the course of the audit, the Auditor conducted a limited examination of the City's internal controls and management practices. The Auditor looked for material weakness or reportable conditions that would require immediate disclosure to the City Council in accordance with generally accepted auditing standards. A deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements in a timely basis.

- Material weakness is a deficiency in internal control, such that there is a reasonable possibility that a material misstatement of the City financial statements will not be prevented, or detected and corrected, in a timely basis.
- Significant deficiency is less severe than a material weakness, yet important enough to merit attention by those charged with governance.
- Control deficiency is the least severe deficiency in that potential misstatements are not material. Control deficiencies still warrant identification and remediation.

The Auditor's Report to Those Charged with Governance for the Year Ended June 30, 2025, contains no reportable conditions.

This is the fourth consecutive year that the City received a favorable Report to Those Charged with Governance with no findings.

EVALUATION AND FOLLOW-UP

The Single Audit Report is currently being prepared and the final report will be issued by the federal reporting deadline of March 31, 2026. Once complete, an informational memorandum regarding the Single Audit will be prepared for the City Council to disclose any audit findings, as well as include a link to the final report.

COORDINATION

This memorandum has been coordinated with the City Attorney's Office and the City Manager's Budget Office.

HONORABLE MAYOR AND CITY COUNCIL

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PUBLIC OUTREACH

This memorandum will be posted on the City's Council Agenda website for the December 9, 2025 City Council meeting.

COMMISSION RECOMMENDATION AND INPUT

No commission recommendation or input is associated with this action.

CEQA

Not a Project, File No. PP17-009, Staff Reports, Assessments, Annual Reports, and Informational Memos that involve no approvals of any City action.

PUBLIC SUBSIDY REPORTING

This item does not include a public subsidy as defined in section 53083 or 53083.1 of the California Government Code or the City's Open Government Resolution.



MARIA ÖBERG
Director of Finance

For questions, please contact Maria Öberg, Director of Finance, at (408) 535-7000 or via email at maria.oberg@sanjoseca.gov.

ATTACHMENT: Report to Those Charged with Governance for the Year Ended June 30, 2025

CITY OF SAN JOSE

Report to Those Charged With Governance

For the Year Ended June 30, 2025



Certified
Public
Accountants

November 17, 2025

City Council
City of José, California

We are pleased to present this report related to our audit of the basic financial statements of the City of San José, California (City) as of and for the year ended June 30, 2025. This report summarizes certain matters required by professional standards to be communicated to you in your oversight responsibility for the City's financial reporting process.

In addition to the City's basic financial statements, we audit and separately report on the following financial statements as of and for the year ended June 30, 2025.

- Successor Agency to the Redevelopment Agency of the City of San José;
- San José Mineta International Airport (Airport);
- Parks and Recreation Bond Projects Fund;
- Branch Library Bond Projects Fund;
- Library Parcel Tax Special Revenue Fund;
- Pedestrian/Bicycle Facilities Grant;
- Public Safety and Infrastructure Bond Projects Fund;
- San José Clean Energy Enterprise Fund;
- South Bay Water Recycling Program and System;
- Wastewater Treatment System (Wastewater); and
- The City of San José Deferred Compensation Plans.

We also audit the financial statements of the City sponsored retirement plans, the Federated City Employees' Retirement System and the Police and Fire Department Retirement Plan, collectively, the Retirement Systems, and the San José Convention Center and Cultural Facilities. We issued separate communication reports to their respective boards.

This report is intended solely for the information and use of the Mayor, City Council and management, and is not intended to be, and should not be, used by anyone other than these specified parties. It will be our pleasure to respond to any questions you have about this report. We appreciate the opportunity to continue to be of service to the City.

A handwritten signature in black ink that reads "Macias Gini & O'Connell LLP". The signature is written in a cursive, flowing style.

Walnut Creek, California

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REQUIRED COMMUNICATIONS

Auditing standards generally accepted in the United States of America (AU-C 260, *The Auditor's Communication With Those Charged With Governance*) require the auditor to promote effective two-way communication between the auditor and those charged with governance. Consistent with this requirement, the following summarizes our responsibilities regarding the financial statement audits as well as observations arising from our audits that are significant and relevant to your responsibility to oversee the financial and related compliance reporting process.

Our Responsibilities With Regard to the Financial Statement Audits

Our responsibilities under auditing standards generally accepted in the United States of America and *Government Auditing Standards* have been described to you in our arrangement letter dated April 1, 2025. Our audit of the City's financial statements does not relieve management or those charged with governance of their responsibilities, which are also described in that letter.

Overview of the Planned Scope and Timing of the Financial Statement Audits

We previously issued our arrangement letter dated April 1, 2025 and a separate communication dated July 17, 2025, Fiscal Year 2025 Audit Service Plan, regarding the planned scope and timing of our audits and identified significant risk audit areas. We conducted our audits consistent with the planned scope and timing in our communications.

Accounting Policies and Practices

Preferability of Accounting Policies and Practices

Under accounting principles generally accepted in the United States of America, in certain circumstances, management may select among alternative accounting practices. In our view, in such circumstances, management has selected the preferable accounting practice.

Adoption of, or Change in, Accounting Policies

Management has the ultimate responsibility for the appropriateness of the accounting policies used by the City. A summary of the significant policies adopted by the City is included in Note I to the financial statements. As described in Note I.E. to the financial statements, the City implemented Governmental Accounting Standards Board (GASB) Statement No. 101, *Compensated Absences*, and GASB Statement No. 102, *Certain Risk Disclosures*. The implementation of GASB Statement No. 101 resulted in the restatements of the beginning net position of \$77.9 million as detailed at Note I.F.23 to the financial statements. The City also changed the classification of certain governmental and enterprise funds from major funds to nonmajor funds as detailed at Note I.F.23. The implementation of GASB Statement No. 102 did not have a significant impact on the City's financial statements for the year ended June 30, 2025.

Significant Accounting Policies

We did not identify any significant accounting policies in controversial or emerging areas for which there is a lack of authoritative guidance or consensus.

Significant Unusual Transactions

We did not identify any significant unusual transactions.

Management's Judgments and Accounting Estimates

Accounting estimates are an integral part of the preparation of financial statements and are based upon management's current judgment. The process used by management encompasses their knowledge and experience about past and current events, and certain assumptions about future events. You may wish to monitor throughout the year the process used to determine and record these accounting estimates.

The following is summary information about the process used by management in formulating particularly sensitive accounting estimates and about our conclusions regarding the reasonableness of those estimates:

Significant Accounting Estimates	
Measurement of investments at fair value	The City's investments are accounted for in accordance with the provisions of GASB Statement No. 72, <i>Fair Value Measurement and Application</i>, and accordingly, its fair value measurements are categorized within the fair value hierarchy established by the standard. The following levels indicate the hierarchy of inputs used to measure fair value and the primary valuation methodologies used for financial instruments measured at fair value on a recurring basis: ○ Level 1 – Investments whose values are based on quoted prices (unadjusted) for identical assets in active markets that a government can access at the measurement date. ○ Level 2 – Investments whose values are based on inputs – other than quoted prices including prices included within level 1 – that are observable for an asset, either directly or indirectly. ○ Level 3 – Investments whose values are based on unobservable inputs for an asset and may require a degree of professional judgment. MGO compared investment values from quoted market information and using pricing applications and models obtained from the custodian bank, fiscal agents or other sources and determined that they were reasonable.
Estimated allowance for losses on accounts receivable	Estimated allowance for losses on accounts receivable was based on historical experience. MGO evaluated the methodologies and assumptions used in estimating the allowance for losses and tested subsequent cash receipts of significant accounts receivable.
Estimated allowance for losses on loans receivable	Estimated allowance for loans receivable is comprised of an allowance for risk and an allowance for present value discount. The allowance for risk was based on the consideration of the changes in the portfolio character, evaluation of current economic conditions and such other factors that, in management's judgment, deserve recognition in estimating potential loan losses. The allowance for risk takes into consideration maturity dates, interest rates, and other relevant factors. The allowance for present value discount gives recognition to the economic cost of providing loans at interest rates below market and

Significant Accounting Estimates

	represents management's estimate of the present value of projected net cash flows to the City from the loan portfolio. MGO evaluated the methodologies and assumptions used in estimating the allowance and determined whether they are consistent with the City's Loan Loss Reserve Policies and Procedures and performed analytical procedures to determine the estimated allowance for losses was reasonable.
Depreciation and amortization of capital assets, including depreciation/amortization methods and useful lives assigned to depreciable/amortizable property	Useful lives, or in the case of intangible right-to-use lease and subscription-based information technology arrangement assets, the shorter of useful lives or the lease/subscription term, for depreciable/amortizable capital assets were determined by management based on the nature of the capital asset. Depreciation/amortization was calculated based on the straight-line method. MGO assessed the reasonableness of the useful lives based on the nature of the capital assets and performed substantive analytical procedures on depreciation/amortization expense and determined the estimates were reasonable.
Accrual of compensated absences	In accordance with the provisions of the newly adopted GASB Statement No. 101, <i>Compensated Absences</i>, the accrual of compensated absences is recognized for leave that has not been used and leave that has been used but not yet paid in cash or settled through noncash means. Certain compensated absences, including parental leave, military leave, and jury duty leave, are not recognized until the leave commences. The liability for compensated absences was based on accumulated hours of vacation, sick leave and other compensatory time at current pay rates for eligible employees, factoring in usage pattern and termination payout, and includes certain salary-related payments that are directly and incrementally associated with payments for leave. MGO evaluated the methodologies and assumptions used to develop the obligations, agreed the unused hours and pay rates at year-end to payroll reports, and determined the estimates were supported and reasonable.
Accrual and disclosure of self-insurance claims liabilities	Estimated liabilities for workers' compensation claims were based on management's estimate obtained from information derived from Intercare's (a third-party administrator) claims database system adjusted for a discounted projection at a rate of approximately 2% of the ultimate cost of known claims and unreported claims. Estimated liabilities for general liability and other claims were determined by the City Attorney's judgment about the ultimate outcome of the claims. MGO evaluated the methodologies and assumptions used to develop the workers' compensation claims estimate through data testing. For general liability and other claims, MGO obtained legal confirmation and obtained evidence relevant to the period in which the underlying cause

Significant Accounting Estimates

	for legal action occurred, the degree of probability of an unfavorable outcome and the amount or range of potential loss.
Accrual and disclosure of pollution remediation obligations	Accrual and disclosures of pollution remediation obligations were determined by the City's engineers and its environmental consultants' judgments about the ultimate outcome of the obligations. MGO evaluated the methodologies and assumptions used to develop the obligations, reviewed the assumptions used for reasonableness, and determined the estimates were supported and reasonable.
Measurement of the pension contributions, net pension liability, pension expense, and pension-related deferred outflows and inflows of resources	Pension plans' employer and employee contributions requirements, net pension liability, and related deferred outflows and inflows of resources were based on actuarial valuations prepared by the City's Retirement Systems and CalPERS. MGO agreed the calculations to actuarial valuations prepared by the Retirement Systems and CalPERS and tested the reasonableness of allocations to various City funds. The pension plan actuarial valuations for the Retirement Systems were tested in our separate audits of the Retirement Systems.
Measurement of the other postemployment benefits (OPEB) contributions, net OPEB liability, OPEB expense and OPEB-related deferred outflows and inflows of resources	OPEB plans' employer and employee contributions requirements, net OPEB liability, and related deferred outflows and inflows of resources were based on actuarial valuations prepared by the City's Retirement Systems. MGO agreed the calculations to actuarial valuations prepared by the City's Retirement Systems and tested for reasonableness the allocations to various City funds. The OPEB actuarial valuations for the Retirement Systems were tested in our separate audits of the Retirement Systems.
Discount rate used for the calculation of the lease and PPP receivables, and the lease and subscription liabilities	The discount rate used for the calculation of the lease and PPP receivables, and the lease and subscription liabilities are based on the City's estimated incremental borrowing rate using the national average fixed-rate loan index on the date of commencement. MGO evaluated the methodologies and assumptions used in making the accounting estimate and performed substantive procedures to determine that the discounted value was reasonable.
Rate stabilization reserve deferral for San José Clean Energy	The City adopted a policy for the establishment of a rate stabilization reserve to allow San José Clean Energy to defer revenues to future years in accordance with GASB Statement No. 62. The reserve is funded and a matching amount of cash is restricted. The reserve amount may periodically be adjusted based on the criteria stated in the policy. MGO evaluated the methodologies and assumptions used in estimating the reserve amount and determined whether they are consistent with the City's reserve policy and performed analytical procedures to determine whether the estimate is supported, reasonable, and calculated in accordance with the City's reserve policy.

Audit Adjustments and Uncorrected Misstatements

Professional standards require us to communicate to you all material, corrected misstatements that were brought to the attention of management as a result of our audit procedures. There were no corrected misstatements identified by us as a result of our audit procedures.

Uncorrected misstatements or matters underlying these uncorrected misstatements could potentially cause future-period financial statements to be materially misstated, even if we have concluded that the uncorrected misstatements are immaterial to the financial statements under audit. We are not aware of any uncorrected misstatements other than misstatements that are clearly trivial.

Departure From the Auditor's Standard Report

Our auditor's report includes an emphasis of matter paragraph describing the City's adoption of GASB Statement No. 101, *Compensated Absences*, effective July 1, 2024. Our opinions on the financial statements were not modified with respect to this matter.

Other Information Included in Annual Reports

Our responsibility for other information included in the annual reports for the City, the Airport, and the Wastewater is to read the information and consider whether its content or the manner of its presentation is materially inconsistent with the financial information covered by our auditor's report, whether it contains a material misstatement of fact or whether the other information is otherwise misleading. We read the City's and the Airport's introductory and statistical sections, and the Wastewater's other information section. We did not identify material inconsistencies with the audited financial statements.

Observations About the Audit Process

Disagreements With Management

We encountered no disagreements with management over the application of significant accounting principles, the basis for management's judgments on any significant matters, the scope of the audit or significant disclosures to be included in the City's financial statements.

Consultations With Other Accountants

We are not aware of any consultations management had with other accountants about accounting or auditing matters.

Significant Issues Discussed With Management

No significant issues arising from the audits were discussed or were the subject of correspondence with management.

Significant Difficulties Encountered in Performing the Audit

We did not encounter any significant difficulties in dealing with management during the audits.

Significant Matters That Required Consultation

We did not encounter any difficult or contentious matters that required consultation outside the engagement team and that are, in our professional judgment, significant and relevant to your responsibility to oversee the financial reporting process.

Shared Responsibilities for Independence

Independence is a joint responsibility and is managed most effectively when management, audit committees (or their equivalents), and audit firms work together in considering compliance with American Institute of Certified Public Accountants (AICPA) and *Government Accountability Office* (GAO) independence rules. For MGO to fulfill its professional responsibility to maintain and monitor independence, management, the Mayor and City Council, and MGO each play an important role.

Our Responsibilities

1. AICPA and GAO rules require independence both of mind and in appearance when providing audit and other attestation services. MGO is to ensure that the AICPA and GAO's General Requirements for performing non-attest services are adhered to and included in all letters of engagement.
2. Maintain a system of quality management over compliance with independence rules and firm policies.

The City's Responsibilities

1. Timely inform MGO, before the effective date of transactions or other business changes, of the following:
 - a. New affiliates, directors, or officers.
 - b. Changes in the organizational structure or the reporting entity impacting affiliates such as subsidiaries, partnerships, related entities, investments, joint ventures, component units, and jointly governed organizations.
2. Provide necessary affiliate information such as new or updated structure charts, as well as financial information required to perform materiality calculations needed for making affiliate determinations.
3. Understand and conclude on the permissibility, prior to the City and its affiliates, officers, directors, or persons in a decision-making capacity, engaging in business relationships with MGO.
4. Not entering into arrangements of nonaudit services resulting in MGO being involved in making management decisions on behalf of the City.
5. Not entering into relationships resulting in close family members of MGO covered persons, temporarily or permanently acting as an officer, director, or person in an accounting, financial reporting or compliance oversight role at the City.

Management Representations

We have requested certain written representations from management, which are included in the management representation letter dated November 17, 2025.

Internal Control and Compliance Matters

We have separately communicated on internal control and compliance over financial reporting identified during our audit of the financial statements, as required by *Government Auditing Standards*.

The financial and compliance audit of the City's major federal awards in accordance with the *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards at 2 CFR 200* (Uniform Guidance) is in process and will be issued no later than March 31, 2026.

EXHIBIT A
Recent Accounting Pronouncements

RECENT ACCOUNTING PRONOUNCEMENTS

The following accounting pronouncements have been issued as of the date of this communication but are not yet effective and may affect the future financial reporting by the City.

Pronouncement	Summary
GASB Statement No. 103, <i>Financial Reporting Model Improvements</i>	The objective of this statement is to improve key components of the financial reporting model to enhance its effectiveness in providing information that is essential for decision making and assessing a government's accountability. This statement also addresses certain application issues. Statement No. 103 is effective for the City's financial statements for the year ending June 30, 2026.
GASB Statement No. 104, <i>Disclosure of Certain Capital Assets</i>	The objective of this statement is to establish requirements for certain types of capital assets to be disclosed separately for purposes of note disclosures, and to establish requirements for capital assets held for sale and note disclosures for those capital assets. Statement No. 104 is effective for the City's financial statements for the year ending June 30, 2026.