

IV (B)(1)

Audit Reports

[Informational]



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**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**

City Council
City of San José, California

We have audited the financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the City of San José, California (the City) as of and for the year ended June 30, 2009, which collectively comprise the City's basic financial statements, and have issued our report thereon dated November 4, 2009. Our report contains an explanatory paragraph describing the City's adoption of the provisions of Governmental Accounting Standards Board (GASB) Statement No. 49, *Accounting and Financial Reporting for Pollution Remediation Obligations* and an emphasis of a matter regarding an uncertainty related to a recently passed State legislation. 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.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the City's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the City's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the City's internal control over financial reporting.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and would not necessarily identify all deficiencies in internal control that might be significant deficiencies or material weaknesses. However, as discussed below, we identified certain deficiencies in internal control that we consider to be significant deficiencies.

A control 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 misstatements on a timely basis. A significant deficiency is a control deficiency, or a combination of control deficiencies, that adversely affects the City's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the City's financial statements that is more than inconsequential will not be prevented or detected by the City's internal control. We consider the deficiencies described in the accompanying Federal Awards Schedule of Findings and Questioned Costs as findings #2009-A and #2009-B to be significant deficiencies in internal control over financial reporting.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the City's internal control.

Our consideration of the internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in the internal control that might be significant deficiencies and, accordingly, would not necessarily disclose all significant deficiencies that are also considered to be material weaknesses. However, we believe that none of the significant deficiencies described above is a material weakness.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the City's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, 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 the City in a separate letter dated November 4, 2009.

The City's response to the findings identified in our audit is described in the accompanying Federal Awards Schedule of Findings and Questioned Costs. We did not audit the City's response and, accordingly, we express no opinion on it.

This report is intended solely for the information and use of the City Council, the City's management, and federal awarding agencies and pass-through entities and the State Controller's Office, and is not intended to be and should not be used by anyone other than these specified parties.

Macias Gini & C Counsel LLP
Certified Public Accountants

Walnut Creek, California
November 4, 2009





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**Independent Auditor's Report on Compliance with Requirements
Applicable to Each Major Program, the Passenger Facility Charges Program and
the Internet Crimes Against Children State Grant Program and on
Internal Control over Compliance in Accordance with OMB Circular A-133**

City Council
City of San José, California

Compliance

We have audited the compliance of the City of San José, California (the City) with the types of compliance requirements described in the U.S. Office of Management and Budget (OMB) *Circular A-133 Compliance Supplement*, the *Passenger Facility Charge Audit Guide for Public Agencies* issued by the Federal Aviation Administration (*PFC Guide*), and the *Recipient Handbook* issued by the California Emergency Management Agency (CalEMA) that are applicable to each of its major federal programs, the passenger facility charges program, and the Internet Crimes Against Children (ICAC) State Grant program, respectively, for the year ended June 30, 2009. The City's major federal programs are identified in the summary of auditor's results section of the accompanying Federal Awards Schedule of Findings and Questioned Costs. Compliance with the requirements of laws, regulations, contracts, and grants applicable to each of its major federal programs, the passenger facility charges program and the ICAC State Grant program is the responsibility of the City's management. Our responsibility is to express an opinion on the City's compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*; the *PFC Guide*; and the *Recipient Handbook*. Those standards, OMB Circular A-133, the *PFC Guide* and the *Recipient Handbook* require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program, the passenger facility charges program and the ICAC State Grant program occurred. An audit includes examining, on a test basis, evidence about the City's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination of the City's compliance with those requirements.

In our opinion, the City complied, in all material respects, with the requirements referred to above that are applicable to each of its major federal programs, the passenger facility charges program and the ICAC State Grant program for the year ended June 30, 2009. However, the results of our auditing procedures disclosed an instance of noncompliance with those requirements, which is required to be reported in accordance with OMB Circular A-133 and which is described in the accompanying Federal Awards Schedule of Findings and Questioned Costs as finding #2009-01.

Internal Control Over Compliance

The management of the City is responsible for establishing and maintaining effective internal control over compliance with the requirements of laws, regulations, contracts, and grants applicable to federal programs, the passenger facility charges program and the ICAC State Grant program. In planning and performing our audit, we considered the City's internal control over compliance with the requirements that could have a direct and material effect on a major federal program, the passenger facility charges program, and the ICAC State Grant program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the City's internal control over compliance.

Our consideration of internal control over compliance was for the limited purpose described in the preceding paragraph and would not necessarily identify all deficiencies in the City's internal control that might be significant deficiencies or material weaknesses as defined below. However, as discussed below, we identified a deficiency in internal control over compliance that we consider to be a significant deficiency.

A *control deficiency* in an entity's internal control over compliance 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 noncompliance with a type of compliance requirement of a federal program on a timely basis. A *significant deficiency* is a control deficiency, or combination of control deficiencies, that adversely affects the entity's ability to administer a federal program such that there is more than a remote likelihood that noncompliance with a type of compliance requirement of a federal program that is more than inconsequential will not be prevented or detected by the City's internal control. We consider the deficiency in internal control over compliance described in the accompanying Federal Awards Schedule of Findings and Questioned Costs as finding #2009-01 to be a significant deficiency.

A *material weakness* is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that material noncompliance with a type of compliance requirement of a federal program, the passenger facility charges program, or the ICAC State Grant program will not be prevented or detected by the City's internal control. We do not consider the deficiency described in the accompanying Federal Awards Schedule of Findings and Questioned Costs to be a material weakness.

The City's response to the findings identified in our audit is described in the accompanying Federal Awards Schedule of Findings and Questioned costs. We did not audit the City's response, and accordingly, we express no opinion on it.

This report is intended solely for the information and use of the City Council, the City's management, the Federal Aviation Administration, federal awarding agencies and pass-through entities, and the State Controller's Office, and is not intended to be and should not be used by anyone other than these specified parties.

Macias Gini & Cannelo LLP
Certified Public Accountants
Walnut Creek, California

January 5, 2010

CITY OF SAN JOSE, CALIFORNIA
Schedule of Expenditures of Federal Awards
Year Ended June 30, 2009

Federal Grantor/Pass-Through Grantor/Program	Federal Catalog Number	Grant Identifying Number	Grant Amount	Expenditures	
				Federal Grant	Other
U.S. Department of Housing and Urban Development					
Community Development Block Grants/Entitlement Grants	14.218	B06-07-08 MC-06-0021	\$ 30,543,910	\$ 14,995,026	\$ -
Community Development Block Grants/Entitlement Grants	14.218	Prior Year Ending Loan Balance	-	6,883,411	-
Subtotal Community Development Block Grants/Entitlement Grants			30,543,910	21,878,437	-
Emergency Shelter Grants Program	14.231	S08-MC-060021	469,642	469,636	-
Home Investment Partnerships Program	14.239	M01-02 MC06215	8,637,000	62,543	-
Home Investment Partnerships Program	14.239	M03-04 MC06215	10,321,912	1,413,787	-
Home Investment Partnerships Program	14.239	M05-06 MC06215	9,185,083	75,000	-
Home Investment Partnerships Program	14.239	M07-08 MC06215	8,612,627	4,343,023	-
Home Investment Partnerships Program	14.239	Prior Year Ending Loan Balance	-	39,612,448	-
Subtotal Home Investment Partnerships Program			36,756,622	45,506,801	-
Housing Opportunities for Persons with AIDS	14.241	CA-39-H06-F069	738,000	18,830	-
Housing Opportunities for Persons with AIDS	14.241	CA-H07-F0-04	739,000	148,598	-
Housing Opportunities for Persons with AIDS	14.241	CA-H08-F0-04	765,180	522,839	-
Housing Opportunities for Persons with AIDS	14.241	CA-H107-0003	1,226,500	416,685	-
Subtotal Housing Opportunities for Persons with AIDS			3,468,680	1,106,952	-
Total U.S. Department of Housing and Urban Development			71,238,854	68,961,826	-
U.S. Department of Justice					
Pass-through Office of Justice Programs:					
Missing Children Assistance	16.543	2008-MC-CX-K002	550,141	349,493	-
Edward Byrne Memorial State and Local Law Enforcement Assistance Discretionary Grants Program	16.580	2005-VT-BX-1155	225,000	1,305	-
Edward Byrne Memorial State and Local Law Enforcement Assistance Discretionary Grants Program	16.580	2007-DD-BX-0005	394,890	125,497	-
Edward Byrne Memorial State and Local Law Enforcement Assistance Discretionary Grants Program	16.580	2008-JL-FX-0161	469,494	160,961	-
Edward Byrne Memorial State and Local Law Enforcement Assistance Discretionary Grants Program	16.580	2008-VT-BX-0005	250,000	88,137	100,216
Subtotal Edward Byrne Memorial State and Local Law Enforcement Assistance Discretionary Grants Program			1,339,384	376,900	100,216
Community Capacity Development Office	16.595	2007-WS-Q7-0046	200,000	170,698	214,295
Community Capacity Development Office	16.595	2007-WS-Q7-0024/2008-WS-QX-0142	40,625	24,529	1,159
Community Capacity Development Office	16.595	2008-WS-QX-0184	150,000	31,743	-
Subtotal Community Capacity Development Office			390,625	226,970	215,454

See accompanying notes to the Schedule of Expenditures of Federal Awards and
Schedule of Revenues and Expenditures of Passenger Facility Charges

CITY OF SAN JOSE, CALIFORNIA
Schedule of Expenditures of Federal Awards (Continued)
Year Ended June 30, 2009

Federal Grantor/Pass-Through Grantor/Program	Federal Catalog Number	Grant Identifying Number	Grant Amount	Expenditures	
				Federal Grant	Other
U.S. Department of Justice (continued)					
Public Safety Partnership and Community Policing Grants	16.710	2003INWX001	3,692,162	2,683,736	894,582
Edward Byrne Memorial Justice Assistance Grant Program	16.738	DC08190430	100,681	100,546	-
Edward Byrne Memorial Justice Assistance Grant Program	16.738	2005-DJ-BX-1720	395,243	723	-
Edward Byrne Memorial Justice Assistance Grant Program	16.738	2006-DJ-BX-0883	270,939	5,191	-
Edward Byrne Memorial Justice Assistance Grant Program	16.738	2007-DJ-BX-0531	303,923	14,610	-
Subtotal Edward Byrne Memorial Justice Assistance Grant Program			1,070,786	121,070	-
Convicted Offender and/or Arrestee DNA Backlog Reduction Program	16.748	2007-WP-BX-0008	250,000	111,697	29,374
Total U.S. Department of Justice			7,293,098	3,869,866	1,239,626
U.S. Department of Labor					
WIA Cluster:					
Pass-through State of California, Employment Development Department:					
WIA Adult Program	17.258	R865486	2,786,942	858,313	-
WIA Youth Activities	17.259	R865486	2,562,904	2,288,451	-
WIA Dislocated Workers	17.260	R865486	1,339,754	1,339,754	-
WIA Adult Program	17.258	R970569	3,567,075	3,567,075	-
WIA Youth Activities	17.259	R970569	3,713,904	1,545,155	-
WIA Dislocated Workers	17.260	R970569	4,186,728	2,359,465	-
ARRA - WIA Adult Program	17.258	R970569	2,026,103	8,431	-
ARRA - WIA Youth Activities	17.259	R970569	4,744,413	255,835	-
ARRA - WIA Dislocated Workers	17.260	R970569	4,448,400	8,431	-
Subtotal WIA Cluster			29,376,223	12,230,910	-
Total U.S. Department of Labor			29,376,223	12,230,910	-
U.S. Department of Transportation					
Federal Aviation Administration:					
Airport Improvement Program	20.106	3-06-0226-61	3,400,000	33,616	8,096
Airport Improvement Program	20.106	3-06-0226-63	6,000,000	95,491	23,000
Airport Improvement Program	20.106	3-06-0226-64	1,000,000	1,617	389
Airport Improvement Program	20.106	3-06-0226-66	2,467,466	-	594,286
Airport Improvement Program	20.106	3-06-0226-67	6,000,000	1,441,930	347,287
Airport Improvement Program	20.106	3-06-0226-68	870,372	83,256	20,046
Airport Improvement Program	20.106	3-06-0226-69	1,800,341	1,800,341	433,610
Airport Improvement Program	20.106	3-06-0226-70	3,000,000	2,394,555	572,772
Airport Improvement Program	20.106	3-06-0226-71	1,039,286	829,090	199,685
Airport Improvement Program	20.106	3-06-0226-72	1,122,816	474,627	114,313
Airport Improvement Program	20.106	3-06-0226-73	4,628,099	131,338	31,632
Subtotal Airport Improvement Program			31,328,380	7,285,861	2,345,116

See accompanying notes to the Schedule of Expenditures of Federal Awards and
Schedule of Revenues and Expenditures of Passenger Facility Charges

CITY OF SAN JOSE, CALIFORNIA
Schedule of Expenditures of Federal Awards (Continued)
Year Ended June 30, 2009

Federal Grantor/Pass-Through Grantor/Program	Federal Catalog Number	Grant Identifying Number	Grant Amount	Expenditures	
				Federal Grant	Other
U.S. Department of Transportation (Continued)					
Highway Planning and Construction Cluster:					
Pass-through California Department of Transportation:					
Federal-Aid Highway Program:					
SVSC ITS Enhancement	20.205	ITS99-5005(058)	1,187,204	178,984	176,792
Safe Routes to School (SRTS)	20.205	SRTSL-5005(091)	770,366	137,130	-
SVSC West Corridor - Stevens Creek - CMAQ	20.205	CML-5005(064)	4,748,000	1,282,252	165,852
Community Design and Transportation	20.205	CML-5005(094)	1,300,000	-	272,962
TEA-21-ITS: New CQ TMC (Web II)	20.205	ITS03-5005(073)	579,123	105,705	105,693
Federal Street Maintenance	20.205	SCL 050028	16,300,666	3,722,242	2,223,567
TIMC (HPP 2017)	20.205	HPP2017	5,400,000	175,658	35,269
HBRR Seismic Bridge Retrofit - Julian Street	20.205	BRLZ 5005(080)	769,443	580,045	79,563
HBRR Seismic Bridge Retrofit - Southwest Expressway	20.205	BRLZ 5005(079)	671,058	198,686	161,556
HBRR Seismic Bridge Retrofit - William Street	20.205	BRLZ 5005(081)	521,795	123,118	97,435
Traffic Synchronization	20.205	TLSP-5005(095)	15,000,000	3,365,739	1,126,399
Subtotal Federal-Aid Highway Program			47,247,655	9,889,559	4,445,088
Recreational Trails Program:					
SAFETEA-LU Trail: Lower Guadalupe	20.219	SCL 050081 HPLUL-5005(084)	175,000	175,000	43,849
SAFETEA-LU Trail: Lower Guadalupe	20.219	SCL 050081 VTP 2030-30-B3 #B31	1,377,000	1,010,535	317,817
SAFETEA-LU Trail: Bay Reach 7/9	20.219	SCL 050082 HPLUL-5005(086)	675,000	254,758	86,239
SAFETEA-LU Trail: Coyote Creek	20.219	SCL 050083 HPLUL-5005(087)	1,317,999	208,042	68,923
SAFETEA-LU Trail: Almaden Express	20.219	SCL 050089 DEMO05-5005(088)	496,000	35,768	3,646
Subtotal Recreational Trails Program			4,040,999	1,684,103	520,474
Subtotal pass-through California Department of Transportation			51,288,654	11,573,662	4,965,562
Pass-through the Metropolitan Transportation Commission					
HBRR - Willow Glen Way Bridge	20.205	BRLS 5005(038)	3,428,354	330,937	141,168
Subtotal Highway Planning and Construction Cluster			54,717,008	11,904,599	5,106,730
State and Community Highway Safety					
Pass-through the California Department of Transportation:					
2008 Sobriety Checkpoint Mini-Grant	20.600	SC08372	91,814	32,692	-
2009 Sobriety Checkpoint Mini-Grant	20.600	SC09372	107,246	70,212	-
2009 Click it or Ticket Grant	20.600	CT-09372	45,054	36,980	-
Avoid the 13	20.600	AL0980	153,119	17,155	69,896
Elk Grove Police Department - Street Racing	20.600	PT0816	5,400	3,543	137
Subtotal State and Community Highway Safety			402,633	160,582	70,033
Total U.S. Department of Transportation			86,448,021	19,351,042	7,521,879

See accompanying notes to the Schedule of Expenditures of Federal Awards and
Schedule of Revenues and Expenditures of Passenger Facility Charges

CITY OF SAN JOSE, CALIFORNIA
Schedule of Expenditures of Federal Awards (Continued)
Year Ended June 30, 2009

Federal Grantor/Pass-Through Grantor/Program	Federal Catalog Number	Grant Identifying Number	Grant Amount	Expenditures	
				Federal Grant	Other
National Endowment for the Humanities					
Pass-through the California State Library					
Promotion of the Humanities_Public Programs	45.164	LT-50052-08	2,500	1,635	-
Grants to States Program:					
Staff Education 2008-09	45.310	40-7050	13,808	13,808	-
Outreach to Latino Communities	45.310	40-7209	4,991	4,991	-
Self Directed Interest Groups	45.310	40-7142	20,000	3,747	-
Libraries as Community Resources	45.310	40-7089	39,933	36,848	-
California of Past Digital Storytelling	45.310	40-7129	10,000	10,000	-
Survey and Analysis of San Jose Teens	45.310	40-7210	5,000	5,000	-
Subtotal Grants to States Program			93,732	74,394	-
Total National Endowment for the Humanities			96,232	76,029	-
Environmental Protection Agency					
Congressionally Mandated Projects	66.202	XP-96942501-0	673,000	70,291	281,162
Brownfields Assessment and Cleanup Cooperative Agreements	66.818	BF-96922201-2	200,000	40,000	-
Total Environmental Protection Agency			873,000	110,291	281,162
U.S. Department of Energy					
Energy Efficiency and Renewable Energy Information Dissemination, Outreach, Training and Technical Analysis/Assistance	81.117	DE-FC36-08GO18099	200,000	25,768	23,392
Total U.S. Department of Energy			200,000	25,768	23,392
U.S. Department of Education					
Fund for the Improvement of Education	84.215	U215K080307	191,593	139,188	-
Fund for the Improvement of Education	84.215	U215K080308	277,074	38,173	-
Total U.S. Department of Education			468,667	177,361	-
U.S. Department of Health and Human Services					
Pass-through from Council on Aging - Silicon Valley					
Aging Cluster:					
Special Programs for the Aging_Title III, Part B _ Grants for Supportive Services and Senior Centers	93.044	Contract 1200 (2008)	10,800	10,800	-
Special Programs for the Aging_Title III, Part B _ Grants for Supportive Services and Senior Centers	93.044	Contract 1200 (2009)	10,800	10,800	-
Nutrition Services Incentive Program	93.053	Contract 1200	96,000	23,516	-
Subtotal Aging Cluster			117,600	45,116	-
Social Services Research and Demonstration	93.647	90XPO27401	191,593	92,818	-
Total U.S. Department of Health and Human Services			309,193	137,934	-

See accompanying notes to the Schedule of Expenditures of Federal Awards and
Schedule of Revenues and Expenditures of Passenger Facility Charges

CITY OF SAN JOSE, CALIFORNIA
Schedule of Expenditures of Federal Awards (Continued)
Year Ended June 30, 2009

Federal Grantor/Pass-Through Grantor/Program	Federal Catalog Number	Grant Identifying Number	Grant Amount	Expenditures	
				Federal Grant	Other
Corporation for National and Community Services					
Retired and Senior Volunteer Program	94.002	06SRPCA017	277,855	72,871	184,649
Retired and Senior Volunteer Program	94.002	09SRPCA014	91,533	20,815	55,037
Subtotal Retired and Senior Volunteer Program			369,388	93,686	239,686
Senior Companion Program	94.016	06SCPCA007	388,651	128,033	168,335
Total Corporation for National and Community Services			758,039	221,719	408,021
U.S. Department of Homeland Security					
National Explosives Detection Canine Team Program	97.072	HSTS0208HCAN452	301,000	201,000	513,220
Law Enforcement Officer Reimbursement Agreement Program	97.090	HSTS0208HSLR344	776,366	362,410	481,639
Pass-through the County of Santa Clara Emergency Management Performance Grants	97.042	N/A	92,142	92,142	95,881
Homeland Security Cluster:					
Pass-through the County of Santa Clara					
FY 07 Urban Areas Security Initiative	97.008	n/a	3,098,659	2,695,314	-
FY 07 Urban Areas Security Initiative	97.008	n/a	1,000,000	721,765	-
FY 09 Urban Areas Security Initiative	97.008	n/a	335,189	62,346	-
FY 07 Metropolitan Medical Response System	97.067	2007-0008	258,145	12,038	-
FY06 State Homeland Security Grant Program	97.067	2006-0071	47,772	619	-
FY07 State Homeland Security Grant Program	97.067	n/a	52,922	5,034	-
State Homeland Security Grant program	97.067	n/a	43,898	23,856	10,055
Subtotal pass-through the County of Santa Clara			4,836,585	3,520,972	10,055
Subtotal Homeland Security Cluster			4,836,585	3,520,972	10,055
Airport Checked Baggage Screening Program	97.100	HSTS04-08-H-CT1234	18,135,000	9,495,782	1,055,117
Total U.S. Department of Homeland Security			24,141,093	13,672,306	2,155,912
Total Federal Awards			\$ 221,202,420	\$ 118,835,052	\$ 11,629,992
State of California - Internet Crimes Against Children State Grant Program					
Internet Crimes Against Children Grant	n/a	IC07017928	\$ 500,000	\$ -	\$ 311,138

See accompanying notes to the Schedule of Expenditures of Federal Awards and
Schedule of Revenues and Expenditures of Passenger Facility Charges

CITY OF SAN JOSE, CALIFORNIA
 Schedule of Revenues and Expenditures of Passenger Facility Charges
 Year Ended June 30, 2009

Passenger Facility Charges Project Number/Description	Identifying Number	Passenger Facility Charges Project Amount	Expenditures	Revenue Recognized
Total Passenger Facility Charges Collection Revenues				
Passenger Facility Charges Collections				\$ 17,415,668
Interest Earned on PFC Program				1,498,633
Passenger Facility Charges Projects				
#1	Communication Center Upgrade	\$ 528,691	\$ -	-
#2	Fire Truck Replacement	599,826	-	-
#3	Handlift Replacement	103,000	-	-
#4	Noise Attenuation	47,792,121	192,353	-
#5	Noise Monitoring System Upgrade	184,000	-	-
#6	Noise Remedy/Land Acquisition	5,133,000	-	-
#7	Security Access Control System	1,032,000	-	-
#40a	Runway 30L Reconstruction	72,022,700	-	-
#40b	Runway 30L Extension	38,671,724	-	-
#41	Aircraft Noise & Operation Management System	100,000	-	-
#42	Emergency Command Post Relocation & Equipment	150,000	-	-
#43	Interim Federal Inspection Service (FIS) Facility	36,879,750	62,193	-
#44	Airfield Lighting Control System	200,000	-	-
#46	Ewert Road Improvements	408,208	-	-
#47	Skyport Access to Airport Boulevard	1,083,000	-	-
#48	Taxiway Y Pavement Reconstruction	2,100,000	-	-
#49	Transportation Access Plan, Terminal Area Concept	1,200,401	-	-
#50	Terminal C Ramp Lighting Improvement	37,000	-	-
#51	Acoustical Treatment of Four Eligible Schools	7,500,000	-	-
#52	Taxiway Z - Apron Reconstruction (Phase II)	825,000	-	-
#53	Terminal C Fire Protection	580,000	10,064	-
#54	Fiber Optic Cable to ARC & Fire Station 29	87,345	-	-
#55	Green Island Bridge	825,000	-	-
#56	Replacement of AACS and CCTV	4,418,645	-	-
#57	Skyport Grade Separation	18,218,154	-	-
#58	Terminal Drive Improvements	1,146,165	-	-
#59	Replacement of PASSUR	221,000	-	-
#60	Terminal C Restroom	2,485,000	267	-
#61	Interim Air Cargo Ramp Extension	1,100,000	-	-
#62	Runway 30R/12L Reconstruction	84,105,103	-	-
#63	Noise Attenuation Category II & III	4,500,000	725	-
#64	Taxiway Y Extension	12,890,000	-	-
#65	Extended Noise Attenuation	61,589,000	1,474,625	-
#66	Taxiway Y Reconstruction	39,131,000	142,925	-
#67	Terminal B - North Concourse	495,095,000	-	-
#68	Terminal B Extension, Phase I	110,159,000	39,333,847	-
#69	Roadway Improvements: Grade Separations	10,244,000	10,242,443	-
Total Passenger Facility Charge Projects		<u>\$ 1,063,344,833</u>	<u>\$ 51,459,442</u>	<u>\$ 18,914,301</u>

See accompanying notes to the Schedule of Expenditures of Federal Awards and
 Schedule of Revenues and Expenditures of Passenger Facility Charges

CITY OF SAN JOSE, CALIFORNIA

Notes to the Schedule of Expenditures of Federal Awards and Schedule of Revenues and Expenditures of Passenger Facility Charges (Continued)

Year Ended June 30, 2009

(1) GENERAL

The accompanying Schedule of Expenditures of Federal Awards (SEFA) presents the activity of the federal award programs and the State of California - Internet Crimes Against Children State Grant Program of the City of San José, California (the City). The City's reporting entity is defined in Note 1 to its basic financial statements. The SEFA includes all federal awards received directly from federal agencies and federal awards passed-through other governmental agencies. In addition, the SEFA includes local, state and other expenditures matched along with the federal award expenditures.

The Schedule of Revenues and Expenditures of Passenger Facility Charges (PFCs) presents only the activity of the passenger facility charges program of the Norman Y. Mineta San José International Airport (Airport), an enterprise fund of the City. PFCs are fees imposed on enplaned passengers by the Airport for the purpose of generating revenue for Airport projects that increase capacity, increase safety, mitigate noise impact and enhance competition between and among air carriers in accordance with Federal Aviation Administration approvals.

(2) BASIS OF PRESENTATION

The accompanying schedules are presented using the modified accrual basis of accounting for program expenditures accounted for in the governmental funds and the accrual basis of accounting for program expenditures accounted for in the proprietary funds as described in Note 1 to the City's basic financial statements, with the exception of the City's loan programs (see Note 7). For reimbursable grants, except for the San José Water Reclamation & Reuse Program as discussed in Note 9, which revenues are recognized upon Congressional appropriations, the City recognizes revenues commencing on the date of grant approval since this is when the City is eligible to claim expenditures for reimbursements. As a result, prior year expenditures are included in the current year SEFA because these expenditures only become eligible when the grant was approved.

(3) RELATIONSHIP TO THE BASIC FINANCIAL STATEMENTS

Expenditures of federal awards and PFCs are reported in the City's basic financial statements as expenditures in the general, special revenue and capital projects funds and as expenses for non-capital expenditures and as additions to capital assets for capital related expenditures in the enterprise funds. Federal award expenditures agree or can be reconciled with the amounts reported in the City's basic financial statements.

(4) RELATIONSHIP TO FEDERAL FINANCIAL REPORTS

Amounts reported in the SEFA and Schedule of Revenues and Expenditures of Passenger Facility Charges agree to or can be reconciled with the amounts reported in the related federal financial reports.

(5) AIRPORT EXPENDITURES

The Federal Aviation Administration reimburses the Airport for approximately 80% of allowable Airport Improvement Program (AIP) grant expenditures. The remaining unreimbursed portion of grant expenditures, if eligible, are reimbursed from PFC revenue. Total allowable AIP expenditures are presented in the accompanying SEFA.

CITY OF SAN JOSE, CALIFORNIA

Notes to the Schedule of Expenditures of Federal Awards and
Schedule of Revenues and Expenditures of Passenger Facility Charges (Continued)

Year Ended June 30, 2009

The accompanying Schedule of Revenues and Expenditures of Passenger Facility Charges includes approximately 20% of expenditures reimbursed by PFC revenue for AIP approved projects and 100% for non-AIP approved projects.

(6) AMOUNTS PROVIDED TO SUBRECIPIENTS

Included in the total expenditures of federal awards are the following amounts passed through to subrecipients:

<u>Program Title</u>	<u>Federal Catalog Number</u>	<u>Provided to Subrecipients</u>
Community Development Block Grants/Entitlement Grants	14.218	\$3,611,042
Emergency Shelter Grants Program	14.231	469,636
Housing Opportunities for Persons with AIDS	14.241	940,469
Workforce Investment Act (WIA) Adult Program	17.258	897,299
Workforce Investment Act (WIA) Youth Activities	17.259	1,363,675
Workforce Investment Act (WIA) Dislocated Workers	17.260	2,132,358
Highway Planning and Construction	20.205	330,937

(7) LOANS OUTSTANDING

The City participates in certain federal award programs that sponsor revolving loan programs, which are administered by the City. These programs maintain servicing and trust arrangements with the City to collect loan repayments. The funds are returned to the programs upon repayment of the principal and interest. The federal government has imposed certain continuing compliance requirements with respect to the loans under the Community Development Block Grants/Entitlement Grants (CDBG) and the HOME Investment Partnership Program (HOME). In accordance with Subpart B, Section 205 of the Office of Management and Budget Circular A-133, the City has reported the outstanding balance of loans from previous years that have continuing compliance requirements as of June 30, 2009 along with the value of total outstanding and new loans made during the current year in the schedule. The following is a summary of the loan programs maintained by the City and their balances at June 30, 2009:

<u>Program Title</u>	<u>CFDA Number</u>	<u>Amount Outstanding</u>	<u>Prior year loans with continuing compliance requirements</u>	<u>New loans</u>
Community Development Block Grants/Entitlement Grants	14.218	\$ 7,214,337	\$ 6,883,411	\$ 330,926
HOME Investment Partnerships Program	14.239	44,218,973	39,612,448	4,606,525
		<u>\$ 51,433,310</u>	<u>\$ 46,495,859</u>	<u>\$ 4,937,451</u>

CITY OF SAN JOSE, CALIFORNIA

Notes to the Schedule of Expenditures of Federal Awards and
Schedule of Revenues and Expenditures of Passenger Facility Charges (Continued)

Year Ended June 30, 2009

(8) PROGRAM TOTALS

The SEFA does not summarize all programs that receive funding from various funding sources or grants by Catalog of Federal Domestic Assistance (CFDA) number. The following table summarizes these programs by CFDA numbers.

CFDA Number - Program Title Grant Identifying Number or Pass-through Grantor	Federal Expenditures
WIA Cluster, pass-through State of California Employment Development Department	
CFDA No. 17.258 - WIA Adult Program	
R865486	\$ 858,313
R970569	3,567,075
R970569 - American Recovery and Reinvestment Act of 2009	<u>8,431</u>
CFDA No. 17.258 - WIA Adult Program Total	<u>4,433,819</u>
CFDA No. 17.259 - WIA Youth Activities Program	
R865486	2,288,451
R970569	1,545,155
R970569 - American Recovery and Reinvestment Act of 2009	<u>255,835</u>
CFDA No. 17.259 - WIA Youth Activities Program Total	<u>4,089,441</u>
CFDA No. 17.260 - WIA Dislocated Workers Program	
R865486	1,339,754
R970569	2,359,465
R970569 - American Recovery and Reinvestment Act of 2009	<u>8,431</u>
CFDA No. 17.260 - WIA Dislocated Workers Program Total	<u>3,707,650</u>
Total WIA Cluster	<u>\$ 12,230,910</u>
CFDA No. 20.205 - Federal-Aid Highway Program	
Pass-through California Department of Transportation	\$ 9,889,559
Pass-through Metropolitan Transportation Commission	<u>330,937</u>
CFDA No. 20.205 - Federal-Aid Highway Program	<u>\$ 10,220,496</u>

CITY OF SAN JOSE, CALIFORNIA

Notes to the Schedule of Expenditures of Federal Awards and
Schedule of Revenues and Expenditures of Passenger Facility Charges (Continued)

Year Ended June 30, 2009

(9) SAN JOSE AREA WATER RECLAMATION & REUSE PROGRAM

The San José Area Water Reclamation & Reuse Program assists the City and tributary agencies of the San José-Santa Clara Water Pollution Control Plant in protecting endangered species habitats, achieving federally mandated water quality standards and reducing reliance on area surface, ground water, and imported water supplies. The U.S. Department of Interior – Bureau of Reclamation awarded the City \$32.5 million in federal fiscal year 1995 and approved an increase of \$2.5 million in federal fiscal year 2000. Funding for subsequent years, up to \$35 million, is contingent upon subsequent Congressional appropriations acts. As a result of the timing of the subsequent funding approvals, the City requests reimbursements for costs incurred in prior fiscal years.

As of September 30, 2009, Congress appropriated \$31,650,300 and the City has cumulative reimbursements of \$28,070,300 of which \$970,000 was claimed in fiscal year 2009 for expenditures incurred in prior fiscal years. The City accrued the revenue and has in process a \$3,580,000 reimbursement request for fiscal year ended June 30, 2009 that is awaiting final funding approval from the State Water Resources Control Board, the administering agent for the U.S. Department of the Interior.

**(10) SPECIAL PROGRAMS FOR THE AGING TITLE III,
PART B GRANTS FOR SUPPORTIVE SERVICES AND SENIOR CENTERS GRANT**

The City receives various pass-through grants from the Council on Aging of Silicon Valley. During fiscal year 2009, the Council on Aging of Silicon Valley noted that the City underreported its fiscal year 2008 expenditures in the amount of \$10,800 related to the Special Programs for the Aging III, Part B Grants for Supportive Services and Senior Centers (CFDA #93.044) grant. As a result, the City included this expenditure amount reported in the fiscal year 2009 SEFA.

CITY OF SAN JOSE, CALIFORNIA

Notes to the Schedule of Expenditures of Federal Awards and
Schedule of Revenues and Expenditures of Passenger Facility Charges (Continued)

Year Ended June 30, 2009

(11) INTERNET CRIMES AGAINST CHILDREN (ICAC) STATE GRANT

The following schedule represents expenditures for the Internet Crimes Against Children Task Force Program from the U.S. Department of Justice and the State of California Governor's Office of Emergency Service (OES) for the year ended June 30, 2009. This information is included in the City's Single Audit Report at the request of OES.

Program Title and Expenditure Category	Grant Number Grant Period	Cumulative Expense through June 30, 2008	Actual 7/1/08-6/30/09		Cumulative Expense through June 30, 2009	Revenue
			Non-match	Match		
Internet Crimes Against Children Task Force Program (Federal)	2008 MC CX K002					
Personnel Services	7/1/08 - 12/31/2009	\$ -	\$ 63,173	\$ -	\$ 63,173	\$ 63,173
Operating Expenses		-	209,420	-	209,420	209,420
Equipment		-	76,902	-	76,902	76,902
Total		\$ -	\$ 349,495 ¹	\$ -	\$ 349,495	\$ 349,495
Internet Crimes Against Children Task Force Program (State)	IC07017928					
Personnel Services	1/1/2008-6/30/2010	\$ -	\$ -	\$ -	\$ -	\$ -
Operating Expenses		4,400	256,929	-	261,329	256,929
Equipment		-	54,209	-	54,209	54,209
Total		\$ 4,400	\$ 311,138 ²	\$ -	\$ 315,538	\$ 311,138

1 Amount is reported as federal expenditures in the SEFA under CFDA number 16.543 for the Missing Children Assistance Grant, from the U.S. Department of Justice.

2 Amount is reported as other expenditures in the SEFA under the State of California - Internet Crimes Against Children Task Force Program. This grant is a State grant from the Law Enforcement and Victim Services Division of the Governor's Office of Emergency Services.

(12) SUBSEQUENT EVENT

On September 28, 2009, the Transportation Security Administration (TSA) executed a federal grant agreement, HSTS04-09-HREC161 (Agreement) with the City of San José. The estimated project cost is \$23,240,400, of which TSA agreed to reimburse ninety percent (90%) of the allowable, allocable and reasonable costs of the Baggage Handling System Terminal B project (Project) including design and construction management in addition to construction costs but not to exceed a total reimbursement of \$20,916,360. Although this grant agreement was executed in fiscal year 2009-2010, the Agreement provides a provision that the cost recognition date for the Project be effective in April 2009. Upon execution of the TSA grant agreement, the City has prepared information for reimbursement requests for eligible expenditures incurred from April 2009 and recognition of the related revenues from the date of the grant approval (September 28, 2009) will be reported in subsequent years' City financial statements.

CITY OF SAN JOSE, CALIFORNIA

Federal Awards Schedule of Findings and Questioned Costs

Year Ended June 30, 2009

Section I Summary of Auditor's Results

Financial Statements

Type of auditor's report issued on the basic financial statements of the City: Unqualified

Internal control over financial reporting:

- ◆ Material weakness (es) identified? No
- ◆ Significant deficiencies identified that are not considered to be material weaknesses? Yes

Noncompliance material to the financial statements noted? No

Federal Awards

Internal control over major programs:

- ◆ Material weakness (es) identified? No
- ◆ Significant deficiencies identified that are not considered to be material weaknesses? No

Type of auditor's report issued on compliance for major programs: Unqualified

Any audit findings disclosed that are required to be reported in accordance with section 510(a) of OMB Circular A-133? Yes

Identification of major programs:

Federal Catalog Number	Name of Federal Program or Cluster
14.218	Community Development Block Grants/Entitlement Grants
14.231	Emergency Shelter Grants Program
14.239	Home Investment Partnerships Program
16.543	Missing Children Assistance
17.258, 17.259, 17.260	Workforce Investment Act Cluster
20.106	Airport Improvement Program
97.100	Airport Checked Baggage Screening Program

Dollar threshold used to distinguish between type A and type B programs: \$2,170,176

Auditee qualified as a low-risk auditee? No

CITY OF SAN JOSE, CALIFORNIA

Federal Awards Schedule of Findings and Questioned Costs (Continued)

Year Ended June 30, 2009

Section II Financial Statement Findings

Finding #2009-A – Accounting for Variable Rate Demand Obligations

Criteria

Accounting standards require bonds that have *demand provisions exercisable at the balance sheet date* be reported as a liability of the fund used to account for proceeds of the bond issue unless the following conditions are met:

- Before the financial statements are issued, the issuer has entered into an arm's-length financing (take-out) agreement to convert bonds "put", but not resold, into some other form of long-term obligation.
- The take-out agreement does not expire within one year from the date of the issuer's balance sheet or statement of net assets.
- The take-out agreement is not cancelable by the lender or the prospective lender during that year, and obligations incurred under the take-out agreement are not callable by the lender during that year.
- The lender or the prospective lender is expected to be financially capable of honoring the take-out agreement.

If these conditions are met, such bonds should be reported by the issuer as a long-term liability.

Condition

Variable rate demand obligations (VRDOs) are bonds that by their terms have *demand provisions exercisable at the balance sheet date* (June 30, 2009) or within one year from the date of that statement (June 30, 2010). At June 30, 2009, the City and the San José Redevelopment Agency (RDA) combined had \$411.2 million of VRDOs outstanding. The key elements in determining classification of the VRDOs as current or noncurrent are the standby liquidity agreement (credit facility) and/or the take-out agreement. In order for the VRDOs to qualify as noncurrent obligations under Generally Accepted Accounting Principles (GAAP), the credit facility must provide short-term funds to redeem the bonds "put" by the bondholder pending resale by the remarketing agent and the take-out agreement must provide assurance that the issuer will be able to repay any borrowings under the credit facility in a manner that preserves the long-term nature of the obligation.

At June 30, 2009, the RDA had \$56.6 million of variable-rate Tax Allocation Bonds, Series 2003A/B outstanding. These VRDOs were supported by a credit facility provided by JPMorgan Chase Bank, N.A. (JP Morgan) with an expiration date of August 27, 2009. The Series 2003 A/B Bonds did not have a take-out agreement in place (as described above). On July 31, 2009, JP Morgan extended the RDA's credit facility for these bonds to November 26, 2009. However, the extension did not meet the requirements under GAAP for continuing to report the bonds as noncurrent obligations. If the Series 2003A/B Bonds were reclassified as current, the RDA would be required to report a fund liability in its capital projects fund of \$56.6 million, which would reduce its fund balance by the same amount. In order to preserve the long-term nature of the bonds, the RDA negotiated a one-year extension of this credit facility to November 26, 2010. However, the terms of the extension included a mandatory reduction of \$5.3 million in the aggregate amount of letters of credit that JP Morgan provided to the RDA. As a result, we proposed an audit adjustment to record \$5.3 million as a fund liability as of June 30, 2009. In addition to the mandatory reduction to the credit facility, other terms of the credit facility extension are less favorable as compared with the credit facility's prior terms including:

- Increasing the Series 1996 A/B credit facility fees from 0.45% to 2.10%
- Increasing the Series 2003 A/B credit facility fees from 1.50% to 2.30%

CITY OF SAN JOSE, CALIFORNIA

Federal Awards Schedule of Findings and Questioned Costs (Continued)

Year Ended June 30, 2009

Finding #2009-A – Accounting for Variable Rate Demand Obligations (Continued)

- Requiring a new debt coverage covenant
- Increasing the interest rates of the amounts drawn on the credit facility from the greater of prime or the sum of the federal funds rate plus 0.5% to an interest rate the greater of 8.5%, prime plus 1.5%, or federal funds rate plus 2.0%.

Cause

Over the past year, the extreme turmoil in the financial markets resulted in considerable pressures on the supply of credit facilities for the VRDO market. As a result, credit facilities have recently been issued for shorter durations and with more stringent terms thereby increasing the risk that the City or RDA may misclassify these potential short-term obligations as long-term obligations.

Recommendation

Given the City's and RDA's reliance on third party VRDO credit facilities and the trends and pressures noted above in the VRDO market, we recommend evaluating the financial and operational implications should conditions related to the availability of such credit facilities worsen in the future. Additionally, we suggest expanding the traditional finance focused monitoring efforts related to bond obligations (e.g., covenant compliance and disclosure) to include coordination with the City's GAAP reporting unit to ensure changes impacting classifications or display are properly considered and reflected in the financial statements.

Management's Response

With respect to the City's debt portfolio, Debt Management staff meets with Specialized Accounting staff on approximately a bimonthly basis to coordinate activities related to the City's debt portfolio. These meetings will be updated to include discussions related to the renewal of credit facilities supporting outstanding debt.

Additionally, the City continually monitors the City's credit facilities and counterparty risks. Well in advance of any renewal request date, such as three to six months prior the commitment expiration, staff contacts the credit provider to better understand their willingness to renew a credit facility. Based on the City's very high credit ratings, including a AAA rating from S&P, and its long-standing relationships with numerous credit providers, staff anticipates that it will be possible to either renew existing credit facilities, acquire new credit facilities, or refund debt in a timely manner. For example, staff was able to successfully refund all of the City's long-term variable-rate debt within a 12 month period to address challenges in the financial markets. These refundings included two series of Airport Revenue Bonds, eight series of Lease Revenue Bonds, and one series of Sewer Revenue Bonds.

With respect to the Agency's debt and the related variable rate demand obligations, the Agency began working to extend the Letter of Credit before the expiration date of August 27, 2009. However, the negotiation with JP Morgan was longer than expected due to changes in the Letter of Credit market as a result of the current worldwide economic and financial market disruptions. Negotiations were not completed until October. On October 27, 2009, the Agency Board approved the new terms and conditions for extending the 2003 Bond's Letter of Credit including extending the Letter of Credit for the 1996 Bonds to November 26, 2010.

The new terms and conditions also required a mandatory reduction of \$5.3 million on the outstanding 1996 and 2003 bonds, which required an early redemption of \$5.3 million by November 27, 2009. This redemption required recognition of a \$5.3 million short-term liability for these variable rate demand obligations, which was included in the June 30, 2009 financial statements along with the required disclosures.

CITY OF SAN JOSE, CALIFORNIA

Federal Awards Schedule of Findings and Questioned Costs (Continued)

Year Ended June 30, 2009

Finding #2009-B – Housing Loan Reserves Calculations

Criteria

The City considers Governmental Fund resources to be available if they are collected within 60 days after year-end. The availability criterion principle requires that the related receivable be offset with a liability when the receivable is not collectible within the current period or soon enough thereafter. In addition to the offsetting of the governmental fund's loan receivables, the City also prepares a loan portfolio analysis and computes a valuation allowance using a complex spreadsheet to record against its loans receivable.

Condition

During our audit, we noted that the City recorded both an offset to the inclusionary and developer loans' receivable balance and a valuation allowance in the amount of \$11.5 million. As a result, the fund balance of the Housing Activities Fund was understated by \$11.5 million at June 30, 2009. In addition, we noted that the Housing Department's loan portfolio analysis included errors in the maturity dates which led to potential understatement of the loan portfolio's discount reserve by \$0.9 million.

Cause

During the past two years, we noted that City departments worked together collaboratively and made significant progress towards improving the Housing Department's loan reserve calculations. The City's loan committee composed of members from the Finance Department and the Housing Department re-analyzed the loan loss reserve calculation with the main goal of re-analyzing the loan loss reserve worksheet to accurately record the maturity date stated on the promissory notes. However, the Housing Department continues to experience accounting and clerical errors and requires additional training on these complex and non-routine year-end loan loss reserve computations and analysis.

Recommendation

We recommend the Finance Department continue to train its financial statement preparers and reviewers on the recording of its loan balances and allowances on these balances and its related deferred revenues and reserved fund balances.

Management Response

As noted above, the Housing and Finance Departments have worked together collaboratively and made significant progress towards improving the Housing Department's loan reserve calculations. In addition, the Housing Department has implemented controls to review the maturity dates of all existing loans in order to ensure that the loan loss reserve calculations are accurate. The conditions noted in this finding were detected through the audit process and the appropriate adjustment was included in the financial statements as of June 30, 2009. The Housing Department will continue to train their staff to prevent clerical errors in the computations from happening in the future. The Housing and Finance Department management will also continue to stress the importance of providing the appropriate level of training and oversight in preparing and reviewing loan loss reserve schedules and fund financial statements.

CITY OF SAN JOSE, CALIFORNIA

Federal Awards Schedule of Findings and Questioned Costs (Continued)

Year Ended June 30, 2009

Section III Federal Award Findings and Questioned Costs

Finding 2009-01 Schedule of Expenditures of Federal Awards (SEFA) Completeness

U.S Department of Health and Human Services
Special Programs for the Aging Title III, Part B Grants for Supportive
Services and Senior Centers, CFDA #93.044
Passthrough Council on Aging of Silicon Valley
Corporation for National and Community Services
Senior Companion Program, CFDA #94.016

Criteria

The U.S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments and Non-Profits Organizations* (OMB Circular A-133), requires that the City prepare a schedule showing total expenditures for the year for each federal program. Further, OMB Circular A-133 requires that the auditor identify and audit all high-risk type A federal programs. The City's Type A programs are those with current year expenditures exceeding \$2,170,176

Condition

During our audit, we noted that the City included the following misstatements in its draft schedule of expenditures of federal awards (SEFA):

- CFDA #93.044 Special Programs for the Aging Title III, Part B Grants for Supportive Services and Senior Centers understated prior year federal expenditures in the amount of \$10,800. In addition, the SEFA incorrectly reported this grant as a direct federal grant instead of indicating that this grant is pass-through the Council on Aging of Silicon Valley.
- CFDA #94.016 Senior Companion Program overstated prior year other expenditures by \$10,800. These expenditures should have been reported as federal expenditures under CFDA #93.044, as discussed above.

The City subsequently corrected the expenditure amounts reported in its fiscal year 2009 SEFA.

Effect

The City's SEFA serves as the basis in determining the number of major programs required to be audited in a fiscal year. Inaccuracy in its SEFA reporting may result in high-risk Type A programs not captured for testing and Type B programs not subject to the required audit risk assessment.

Questioned Costs

N/A

Recommendation

The City should develop a grants manual to provide guidance to grant administrators in City departments. In addition to completing the grants manual, we recommend the City develop and implement a mandatory single audit training program that is conducted at least annually. The training program should address expectations of the single audit, provide for changes and updates in available resources (e.g. the OMB Circular A-133 Compliance Supplement) and requirements, and provide guidance and updates on identification of funding source (federal, state and other) and on when to record revenues and expenditures in the general ledger. In addition, the City should improve its process in requiring the preparation and review of each grant reconciliations of its expenditures (both claimed and unclaimed) reported in the SEFA to the general ledger and related revenues.

CITY OF SAN JOSE, CALIFORNIA

Federal Awards Schedule of Findings and Questioned Costs (Continued)

Year Ended June 30, 2009

Section III Federal Award Findings and Questioned Costs (Continued)

Management Response and Corrective Action Plan

Finance staff will work with department personnel City-wide to ensure that grant administration staff receive appropriate training and guidance associated with the Single Audit reporting requirements. In fiscal year 2007-08, the Finance Department implemented a new internal process requiring City departments to provide a reconciliation of reimbursable grant expenditures reported on the SEFA schedule to expenditures recorded in the City's accounting system. Finance staff will continue to provide assistance to City-wide grant administration staff to ensure that year end grant reports accurately report grant expenditures on the SEFA and that appropriate documentation is provided during the grant program testing process (was corrected).

CITY OF SAN JOSE, CALIFORNIA

Passenger Facility Charges Schedule of Findings and Questioned Costs

Year Ended June 30, 2009

Section I Summary of Auditor's Results

Financial Statements

Type of auditor's report issued on the basic financial statements of the City: Unqualified

Internal control over financial reporting:

- ◆ Material weakness (es) identified? No
- ◆ Significant deficiencies identified that are not considered to be material weaknesses? Yes

Noncompliance material to the financial statements noted? No

Passenger Facility Charges

Internal control over Passenger Facility Charges:

- ◆ Material weakness (es) identified? No
- ◆ Significant deficiencies identified that are not considered to be material weaknesses? None reported

Type of auditor's report issued on compliance for the Passenger Facility Charges program: Unqualified

Any audit findings disclosed that are required to be reported in accordance with section 510(a) of OMB Circular A-133 in relation to the Passenger Facility Charge program? No

Section II Financial Statement Findings

See Financial Statement Findings Items #2009-A and #2009-B in Federal Awards Schedule of Findings and Questioned Costs.

Section III Passenger Facility Charges Findings and Questioned Costs

None reported.

CITY OF SAN JOSE, CALIFORNIA

Summary Schedule of Prior Audit Findings

Year Ended June 30, 2009

Reference Number: 2008-A - Workers' Compensation Claims Control

Audit Finding:

The City should continue to evaluate its process of closing of cases to ensure that all close cases are properly removed from the Claims Management Systems to avoid overstatement of the reserve balance and the worker's compensation claims liability. The City should also evaluate its training program to ensure that it has the appropriate level of expertise to ensure that the controls over the database system claims information are adequate to meet financial reporting and State compliance requirements.

Status of Corrective Action:

Corrected in during the year ended June 30, 2009.

Memorandum

TO: HONORABLE MAYOR AND
CITY COUNCIL

FROM: Sharon W. Erickson,
City Auditor

SUBJECT: *REVIEW OF AMERICAN RECOVERY
AND REINVESTMENT ACT FIRST
QUARTERLY REPORTS*

DATE: November 12, 2009

RECOMMENDATION

We recommend that the City Council accept the City Auditor's report on the "Review of American Recovery and Reinvestment Act First Quarterly Reports".

SUMMARY

Through September 30, 2009, the City of San José (City) has been awarded over \$77 million in American Recovery and Reinvestment Act (Recovery Act) funds¹ and spent approximately \$6.1 million. Approximately \$3.2 million has been reimbursed or advanced to the City. Thus far, the City's Recovery Act programs have created approximately 250 full-time equivalent jobs.²

In June 2009, the City Auditor's Office assessed the City's readiness to receive Recovery Act funding and determined that the City was making appropriate progress.³ Since that report, the City:

- Submitted its reports prior to October 10, 2009, thus meeting the Recovery Act's reporting deadline.
- Established accounting controls to track Recovery Act expenditures.
- Established an internal checklist to ensure compliance with Recovery Act requirements.
- Made progress towards implementing Recovery Act tracking and reporting software.
- Posted relevant information on the City's website, including the Recovery Act certifications.

Based on our review, the City met the Recovery Act's transparency and accountability requirements for quarterly reporting. The City Auditor's Office will continue to monitor Recovery Act spending and internal controls.

¹ In October 2009, the City was awarded a grant through the Department of Energy's Solar Market Transformation program, bringing the City's total awards to over \$78 million.

² The 250 full-time equivalent positions included over 900 part-time jobs in a summer youth employment program.

³ City of San Jose City Auditor, *American Recovery and Reinvestment Act Preliminary Report on Internal Controls*, June 18, 2009, <http://www.sanjoseca.gov/auditor/AuditMemos/0695/0695M.pdf>.

- May 11, 2009, *Payments to State Grantees for Administrative Costs of Recovery Act Activities*. Office of Management and Budget Memorandum (http://www.whitehouse.gov/omb/assets/memoranda_fy2009/m09-18.pdf)
- June 22, 2009, *Implementing Guidance for the Reports on Use of Funds Pursuant to the American Recovery and Reinvestment Act of 2009*. Office of Management and Budget Memorandum (<http://www.whitehouse.gov/omb/asset.aspx?AssetId=1412>)
- September 10, 2009, *The American Recovery & Reinvestment Act: DOJ Recovery Act Reporting – Grants and Cooperative Agreements*. Department of Justice Recipient Webinar (<http://www.ojp.gov/recovery/rawebinar.htm>)
- October 13, 2009, *Payments to State Grantees for their Administrative Costs for Recovery Act Funding – Alternative Allocation Methodologies*. Office of Management and Budget Memorandum (http://www.whitehouse.gov/omb/assets/memoranda_2010/m10-03.pdf)
- As of October 16, 2009, *Frequently Asked Questions: American Recovery and Reinvestment Act of 2009*. Office of Management and Budget (http://www.whitehouse.gov/omb/recovery_faqs/)

Since our last report, the City has implemented or is in the process of implementing the following accounting and transparency controls:

- *Registered and entered first quarter reports via www.FederalReporting.gov*. The federal Office of Management and Budget (OMB) clarified the Recovery Act's data reporting requirements and the methodology for calculating jobs created by Recovery Act expenditures. The OMB also provided guidance for recipients to conduct required data quality reviews of submitted data and introduced a new data portal for reporting, www.FederalReporting.gov. The City has registered with www.FederalReporting.gov and submitted its required quarterly reports in accordance with the reporting requirements. Staff in the CMO met directly with program leads to discuss program activity to ensure data quality prior to submitting reports.
- *Established accounting controls to track Recovery Act expenditures*. Special funds, called memo funds, either have been or will be established within FMS for all programs to separately track Recovery Act activity to ensure transparency of Recovery Act funding.
- *Established an internal checklist to ensure compliance with Recovery Act requirements*. The CMO developed an internal checklist for departments to request CMO approval to submit grant applications for Recovery Act funds. The CMO requires departments to complete the checklist to provide the status of key Recovery Act requirements such as:
 - The project received a full review and vetting,
 - It is an appropriate use of taxpayer dollars,
 - The associated goods and services will be procured in a competitive manner,
 - The project will comply with prevailing wage requirements,

Exhibit 1: Recovery Act Program Activity Reported to FederalReporting.gov as of September 30, 2009

Program	Award	Reported Expenditures	Reimbursements/Advances	Number of Jobs Created/Retained
Airport Terminal B Checked Baggage Screening Project ⁶	\$20,916,360	\$3,344,903	\$0	10.4
Airport Taxiway "W" Extension	\$5,178,291	\$0	\$0	0
Homeless Prevention and Rapid Re-Housing Program (HPRP)	\$4,128,763	\$1,716	\$0	0
Community Development Block Grant (CDBG) ⁷	\$2,700,463	\$0	\$0	0
Internet Crimes Against Children (ICAC)	\$863,930	\$14,662	\$0	0.4
Total	\$33,787,807	\$3,361,281	\$0	10.8

Source: City Auditor-prepared based on reports submitted to www.FederalReporting.gov, the City's Financial Management System, award documentation, and other City data.

\$2.76 Million in Activity for Programs with Funding Passed Through State or County Agencies

The City has been awarded additional Recovery Act funds that are passed through the State of California or Santa Clara County. For these programs, the City does not report expenditures or project data directly to www.FederalReporting.gov. Instead, the programs comply with State or County reporting requirements. Exhibit 2 shows activity on these programs.

Exhibit 2: Recovery Act Activity as of September 30, 2009 for Programs with Funding passed through State or County Agencies

Program	Award	Expenditures ⁸	Reimbursements/Advances	Number of Jobs Created/Retained
Department of Transportation – Street Resurfacing	\$15,144,000	\$23,863	\$0	0
Work Investment Act (WIA) – Adult, Youth, and Dislocated Worker Programs	\$11,857,306	\$2,738,141	\$1,863,682	240
Justice Assistance Grant (JAG) ⁹	\$1,353,687	\$0	\$1,353,687	0
Total	\$28,354,993	\$2,762,004	\$3,217,369	240

Source: City Auditor-prepared based the City's Financial Management System, award documentation, and other City data.

⁶ The City received approval for the Airport Baggage Screening Project on September 28, 2009 retroactive to April 2009. As of September 30, 2009, no reimbursements had been received.

⁷ The City allocated \$1,122 in oversight costs to the CDBG program. These costs will be reported in the next reporting period.

⁸ Expenditures reported by the State may not align with the FMS because of timing issues related to reimbursements or reporting schedules.

⁹ The federal Department of Justice advances JAG grant funds and considers interest earned as program income that can be spent only on allowable JAG activities. Interest earned as of September 30, 2009 was \$2,305.

the website has not been updated regularly because of a combination of factors including limited staffing resources and unexpected technology glitches. CMO staff is working on solutions to update the website more frequently, such as training additional non-technical staff to do the routine uploads. Since we discussed this issue with the CMO, the website has been updated.

3. Procedures for Quarterly Reporting

After the Recovery Act reports were submitted, the City identified several minor changes. Although the minor corrections will be performed in accordance with federal Recovery Act guidance, the CMO can improve the consistency of the corrections process by tracking corrections and establishing procedures.

According to the federal Department of Justice (DOJ) which oversees the JAG and ICAC grants, agencies should establish written internal procedures to limit or prevent errors when collecting, reviewing, submitting or changing data. Furthermore, according to the DOJ, documentation should be included in formal policy, standard operating procedures and/or official operations manuals. The Police Department has indicated that it will establish written procedures as described in the guidance. These procedures may be applicable to other City programs.

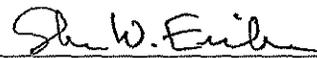
4. Timely Reimbursement of Funds

A potential issue is the timeliness of reimbursement requests. Recovery Act funds available to the City are received primarily on a reimbursement basis. Program leads are aware that they need to seek reimbursement in a timely manner in order to minimize interest costs to the City budget. As more programs expend Recovery Act funds, we will monitor the timeliness of reimbursement requests to minimize the City's interest costs.

CONCLUSION

Based on our review, the City met the Recovery Act's transparency and accountability requirements for quarterly reporting as of September 30, 2009. The City continues to make progress on establishing key internal controls. Future audits will verify compliance with Recovery Act requirements and provisions and assess the accuracy and appropriateness of expenditures.

We reviewed this report with the City Manager's Office and the pertinent City departments. The City Auditor's Office thanks the management and staff from the City Manager's Office, the Finance Department, the City Manager's Budget Office, and departments with Recovery Act programs for their time, information, insight and cooperation during the preparation of this report. The City Auditor's staff who participated in the preparation of this report are Steven Hendrickson, Ruth Merino and Joe Rois.



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