



PUBLIC WORKS DEPARTMENT

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CITY COUNCIL STAFF REPORT

Meeting: July 16, 2024

Subject

Receive the FY 2022-23 Annual Comprehensive Financial Report (ACFR)

Recommended Action

Receive the FY 2022-23 Annual Comprehensive Financial Report (ACFR)

Reasons for Recommendation

Background

In June 2023, the City appointed The Pun Group LLP (TPG) as its new external auditors following a comprehensive selection process. This decision came after the City's previous auditors, Crowe LLP, completed a five-year contract with an additional one-year extension, covering fiscal years 2016-17 to 2021-22. The selection process began with a Request for Proposal (RFP) issued in February 2023, which garnered seven proposals from various auditing firms. The proposals were evaluated based on technical qualifications by a subcommittee of the Audit Committee, including two audit committee members and City staff representatives, and the top three firms—Crowe LLP, Maze and Associates, and The Pun Group LLP—were interviewed.

TPG was ultimately selected due to their ability to provide a fresh perspective on the City's financial reports, their innovative use of artificial intelligence for sample selection, and their workflow management software, which enhances audit tracking. The Pun Group has a strong track record with local municipalities and offers the necessary governmental auditing experience and technical capabilities to ensure timely and accurate audits and reports. The FY 2022-23 ACFR marks the first audit conducted by The Pun Group for the City.

Annual Comprehensive Financial Report

TPG audited the City's accompanying financial statements as of and for the year ended June 30, 2023. During the audit, procedures were performed to obtain audit evidence regarding amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statement, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design appropriate audit

procedures. Audit procedures are not designed to express an opinion on the effectiveness of the entity's internal control.

TPG expressed an unmodified (or clean) opinion, stating "the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the City, as of June 30, 2023, and the respective changes in financial position, and, where applicable, cash flows thereof for the year then ended in accordance with accounting principles generally accepted in the United States of America. (see FY 2022-23 ACFR, page 1).

TPG also issued an Independent Auditor's Report on Internal Control Over Financial Reporting and Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with *Government Auditing Standards* (GAGAS Report). The purpose of this report is solely to describe the scope of the auditor's testing of internal control over financial reporting and the results of that testing and not to provide an opinion on the effectiveness of the entity's internal control or compliance. The report disclosed no instances of noncompliance or other matters required to be reported under *Government Auditing Standard*.

The completion of the FY 2022-23 ACFR has taken longer than usual due to a three-month delay in the audit commencement following the RFP process and the inherent challenges of contracting with a new public accounting firm. While the ACFR structure and content have remained mainly the same, the following three key points contributed to the delay and are worth noting:

- **Prior Period Adjustment:** This adjustment records interest receivable from two housing development loans that were historically unrecorded, ensuring accurate financial reporting. Details are provided in Notes 3 and 14.
- **GASB 96 – Subscription-Based Information Technology Arrangements:** Effective FY 2022-23, this standard defines accounting and financial reporting guidelines for subscription-based IT arrangements, ensuring accurate reflection in the City's financial statements.
- **GASB 77 – Tax Abatement Disclosures:** Although effective since FY 2015-16, information on a tax-sharing agreement did not meet TPG's standards. Additional language has now been proposed to meet reporting requirements, providing transparency about tax abatements and their effects on the City's revenue.

The financial section of the ACFR was presented to the City's Audit Committee on June 24, 2024. Staff informed the Committee that the complete ACFR, including the Transmittal Letter, Management Discussion and Analysis (MD&A), and Statistical Section, would be emailed to them immediately, likely the following day. Any questions arising from the report will be answered and provided to the Council via a supplemental report. The

Committee unanimously approved the report to be received and forwarded to the Council.

Revisions and Additional Information

Following the preparation and initial completion of the ACFR for the July 2, 2024, City Council meeting, staff made four additional changes to the ACFR as recommended by the Audit Committee. The following redlines reflect these changes:

- **Page 5, seventh bullet point:** The City's change in net position was \$28.2 million for governmental activities reflecting the continued positive experience in ~~sales and~~ property tax and modest departmental spending.
- **Page 5, eighth bullet point:** The City's Net Pension Liability for June 30, 2022, (measurement date) was \$55.8 million, increased by \$21.8 million from June 30, 2021, or 64%. The Plan Fiduciary Net Position as a Percentage of the Total Pension Liability for the City's pension plan with CalPERS ~~maintained at~~ decreased by 68%...
- **Page 6, second bullet point:** As of June 30, 2023, the City reported an increase in Net OPEB Liability of \$7.9 million primarily due to the investment return being less than the service cost plus interest on Total OPEB Liability (TOL). The City's actuarial valuation generated a Net OPEB Liability of ~~\$0.5~~ \$0.6 million
- **Page 22, Capital Assets:** At June 30, 2023, the City had \$221 million, net of depreciation, invested in a broad range of capital assets used in governmental and business-type activities, as shown in Table 9 and in Note 6 to the Basic Financial Statements. This reflects the City's continued investment into capital projects dedicated to street and transportation improvements, storm drain improvements, and maintenance of and improvements to City facilities, resulting in an increase in net capital assets of ~~\$4.2~~ \$4.3 million, after depreciation and amortization.

Additionally, there were two questions posed by the City Council relating to the "legal deadline" requirements and the status of the FY 2023-24 audit. In California, there is no "legal deadline" for the ACFR. However, the GFOA's Certificate of Achievement for Excellence in Financial Reporting deadline is December 31 following the end of a June 30 fiscal year unless an extension is filed, which the City has submitted. The City's debt covenants require a draft by March 31, and the City has been working closely with its consultant to ensure compliance. Lastly, the FY 2023-24 audit is on schedule to be completed and presented to the Audit Committee in a special meeting in December.

Agreed-Upon-Procedures

The City of Cupertino engaged TPG to perform an Agreed-Upon-Procedures (AUP) on the City's Appropriations Limit (GANN) Worksheet related to the City's compliance with Section 1.5 of Article XIII B of the California Constitution during the period ending June 30, 2022. City Council adopted Resolution 21-054, establishing an Appropriations Limit of \$114,666,491 for FY 2021-22. The AUP is set to be completed and presented to Audit

Committee on the next regularly scheduled meeting, July 22, 2024, and will be presented to Council thereafter

The City of Cupertino engaged TPG to perform an AUP on the 2019 Clean Water and Storm Protection Fee for the City of Cupertino. The AUP is set to be completed and presented to Audit Committee on the next regularly scheduled meeting, July 22, 2024, and will be presented to Council thereafter.

The City of Cupertino engaged TPG to perform an AUP on the City's investment policy dated May 2022. The AUP is set to be completed and presented to Audit Committee on the next regularly scheduled meeting, July 22, 2024, and will be presented to Council thereafter.

Single Audit

Lastly, the City of Cupertino engaged TPG to perform a Single Audit on the City's federally funded programs, including COVID-19 – American Rescue Plan Act of 2021 and Community Development Block Grant (CDBG), in accordance with GAAS, *Government Auditing Standards*, and requirements under Title 2 U.S. Code of Federal Regulations Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards*. The audit is set to be completed and presented to Audit Committee on the next regularly scheduled meeting, July 22, 2024, and will be presented to Council thereafter.

Sustainability Impact

No sustainability impact.

Fiscal Impact

No fiscal impact.

California Environmental Quality

Not applicable.

Prepared by: Jonathan Orozco, Finance Manager

Reviewed by: Kristina Alfaro, Director of Administrative Services

Approved for Submission by: Pamela Wu, City Manager

Attachments:

A – FY 2022-23 ACFR