

City of Cupertino
Audit Committee Regular Meeting
Minutes
May 23, 2022

CALL TO ORDER

At 4:00 p.m., Chair Moore called the regular meeting to order. This was a teleconference meeting with no physical location.

ROLL CALL

Committee Members Present: Chair Kitty Moore, Vice Chair Angela Chen, Mayor Darcy Paul, Committeemember Hammer

City Staff Present: Dianne Thompson, Kristina Alfaro, Thomas Leung, Beth Viajar

Absent: Committeemember Song

Guests: Matt Morley, Susan Michael, Chelsea Ritchie (Moss Adams), Chris McCarry (Chandler), Annie Rose Favreau (Moss Adams), Colleen Rozillis (Moss Adams)

ORDERS OF THE DAY

Chair Moore asked to move item 8 after item 2 and item 3, 4, and 5 ahead of item 2 so the meeting would begin with item 3, 4, and 5, then 2 and 8. No public comment. Mayor Paul moved the item and Vice Chair Chen seconded. The motion carried unanimously.

1. APPROVAL OF MINUTES

Vice Chair Chen moved to approve the minutes with the edit. Mayor Paul seconded. The motion carried unanimously with Committeemember Hammer abstaining.

ORAL COMMUNICATIONS

None.

NEW BUSINESS

3. Receive Internal Audit Status Report and provide direction

Rozillis provided an overview of the internal audit status reports. She noted that they would present a proposed work program for next year at the next meeting. No public comment. Mayor Paul asked if there was a presentation or timetable in the packet for them to review. Rozillis confirmed that a memo was provided. Mayor Paul inquired if they would be looking to involve this Committee or Council in any policy-making activities between now and the beginning of next year. Rozillis said no, as these were the City's internal financial policies. If any policy updates came to the Committee for approval, they would be at the governance level. Mayor Paul asked if now was the time to provide policy recommendations. Rozillis noted that they did an inventory of the City's financial policies and looked at where they were compared to best practices. They did a gap analysis and provided recommendations for prioritized updates of those policies. In terms of building next year's internal audit work program, they had some ideas. They have a

regular meeting on Friday to discuss with management. The next step would be to reach out to members of the Committee to ask for input on potential projects they would like to see for the next fiscal year.

Mayor Paul inquired if the Procurement Officer was a part of the Fraud, Waste, and Abuse Program or separate. Rozillis confirmed it would be separate as this was about establishing policy, procedures, and training for more preventive and detective controls around fraud, waste, and abuse. Mayor Paul asked if they would be recommending any personnel adjustments or significant training. Rozillis said probably not personnel adjustments as these were easily absorbed in the regular workflow. She also stated that they regularly administered these hotlines for clients. They would work with the City to determine the appropriate ownership and develop training. Mayor Paul asked if the Capital Program Effectiveness Study was where they should expect discussion of a Procurement Officer. Rozillis said that procurement was a piece of the effectiveness of the capital program. Mayor Paul asked if the capital program was where we should be focusing on procurement or if we should be tracking it separately. Rozillis noted that the capital program depended on the City's procurement function. It was important to keep in mind their procurement report and recommendations. She said that if the City did not do some of the procurement stuff, it would hamper the ability to deliver some of the capital programs.

Mayor Paul asked if they should internalize the recommendations with existing staff. Mayor Paul asked if the recommendations were actionable, and should they start implementing training or looking for appropriate personnel for the function. Rozillis confirmed that the reports were actionable. Rozillis said they recommended a Procurement Manager, and the City could either add an FTE or find pieces from across the City. Mayor Paul asked if their firm would be available to help with identifying training programs for existing personnel or hiring personnel. Rozillis said that their firm helped clients with this all the time. Mayor Paul asked if they could agendize this item or how the Committee could have a more active role in formulating the job descriptions or identifying training. Rozillis noted that they would pull examples from other cities they liked, and the HR department would come up with the job description that the Committee would want. She noted that it would be up to the City Manager to come up with the job description as Council would not hire the Procurement Manager. Mayor Paul asked if it wouldn't be unusual for Council to interface with the City Manager's Office to get a sense of the best job descriptions. Rozillis said they could check in on the procurement study's implementation and status to see if the City was moving forward. It would be appropriate to ask for status updates. Chair Moore asked if this status update would go to City Council. Rozillis stated that status updates haven't typically been provided to the Council, but they could be provided. For other clients, they provide reports and an annual program update. Chair Moore noted that it was her preference that it goes to Council.

Chair Moore noted her concerns about the addition of a legislative strategy consultant in the City Manager's Office. Chair Moore wanted to ensure that a Procurement Officer was in the next budget. Alfaro noted that the position was being requested in the Administrative Services Department under the Finance division. Leung confirmed that it was a position under finance. Mayor Paul asked if the Purchasing Officer could be placed under the City Manager's Office. Rozillis noted that it could be. They see it more commonly within finance or equally with finance.

She noted that they want to ensure that whoever is in charge of procurement has appropriate authority to partner with departments. The Administrative Services Department behaved that way. Mayor Paul asked if half an FTE could be placed in the City Manager's Office. He noted the 14-year embezzlement and how he wanted more access to the staff accountant that discovered it. He was told by the Administrative Services Department/Finance Manager that the Mayor would not be able to talk to that person and would have to go through a transmittal of information. He stated that the municipal code said they could get direct information from any employee. To ensure that the public has a little more transparency into this function, he asked if the position should be within the City Manager's Office or should it be clarified that they can get that information from City staff. Rozillis noted that when this position is established, the job description should clearly state the Procurement Officer's level of authority, and that the position, if it reported to the Director of Administrative Services, had a dotted line relationship to the Assistant City Manager or City Manager. Chair Moore noted that this was direction from the Mayor to delineate the level of authority in the Procurement Officer's relationship with the Assistant City Manager. She noted that the City of Chico's budget policies were nice and concise and asked if Moss Adams could provide a comparison between their pages 8 and 14. Chair Moore mentioned that the City of Chico included a policy related to the movement of money within the budget and that the City of Cupertino was light on policies.

4. Receive Capital Program Effectiveness Study Report and provide direction

Favreau provided an overview of the report. She pointed out that the CIP division experienced significant staff turnover before this assessment. Current city staff is stabilized and making admirable progress towards improving the consistency and efficiency of their operations. Favreau provided an overview of the recommendations. No public comment. Mayor Paul asked what the redundancy in the Capital Program Manager's knowledge would look like. Would that be in a different department or multiple people within Public Works? Favreau stated the key one referenced was the Public Works Senior Management Analyst position, as the role supported much of the CIP division's work. Mayor Paul asked if that position would be in Public Works, somewhere else, or if it was not critical where this position was placed. Favreau confirmed that the recommendation would be within Public Works. Mayor Paul noted that we were losing opportunities if we did not have decent mobility in grant fundraising and asked if this was covered in the report. Favreau confirmed it was covered. They recommended having at least one enterprise-wide grant-related position, ideally with a background in Public Works. Mayor Paul inquired if the recommendation could be interpreted as a more general city-wide position out of the City Manager's Office. Favreau confirmed that they saw this as an enterprise-wide position that could support the City as a whole. Mayor Paul inquired if we had lost expertise in grant writing, as there was a Public Works position and an employee that was writing some grants. He noted that we were not systematically looking for these funding opportunities.

Favreau noted that grant writing and identification is currently a decentralized process where members of the team have expertise in this area, but it's not their singular job focus. If it were centralized, there would be benefits similar to centralized coordination for procurement. Mayor Paul agreed, adding that it is an added benefit not just logistically but also from the perspective of neutrality and completeness. He noted that in Community Development, a grant was obtained

a year ago and not brought back to the Council until a month and a half ago. During that time, we lost all our opportunities to go ahead with the grant. He inquired if centralization would help offset that tendency. Favreau noted that she was unsure. The primary benefit of centralization is increased consistency and dedicated time to focus on the topic. Mayor Paul asked if they had concerns about the grants, could they add to the administrative requirements that grant updates be provided every two or three months. Director Alfaro noted that in the Administrative Services budget under finance, we included a one-time special project for grant management using a portion of an analyst for the first year to help identify city-wide grants. Administrative Services would take the financial reporting piece, and the departments would take the operational reporting piece until we knew what would happen with our budget in the wake of the CDTFA Audit. Once we know the status of the audit, if appropriate, staff would ask for a Contract Analyst position who would work under the Purchasing Officer. Chair Moore noted a contract under the former Public Works Director for \$100k for grant writing. She didn't know if it was utilized much and whether a new contract had been initiated.

Chair Moore inquired about the recommendation to pursue retaining the two limited-term Project Managers as full-time city employees. She also noted that the report said to hire support for the Public Works Senior Management Analyst immediately. To her, this report should go to City Council ahead of the June 7 meeting for budget adoption so that the positions could be accounted for properly. Chair Moore also noted an issue with the policy, saying we were supposed to have a five-year plan. The plan is supposed to indicate where the funding will come from for various projects, and Council is supposed to prioritize these items. That piece of the policy hasn't been brought forward to Council or focused on. Director Alfaro noted that one of the limited-term positions was extended as part of the mid-year financial report. Because it is vacant, the second position will be brought forward next year after the status of the CDTFA audit is known. The Management Analyst position for Public Works is one of the 12 positions being recommended for the Council's consideration. Director Alfaro noted that it is recommended as a Management Analyst and not a Senior Management Analyst to provide that entry level.

Chair Moore inquired if there were any recommendations to the five-year plan as the policy states shall. Shall ordinarily means that we must do it. Favreau noted that the interpretation of policies would be left to the legal team and that it is best practice to have this because it will give the team a clearer insight into what is coming up and the major expenses anticipated in the next 5 to 10 years. Chair Moore wondered if funding was available or if funding strategies were planned for some of the CIP items as they are big-ticket items. She pointed out that there was a work plan and a CIP budget, and the work plan had some CIP projects. She encouraged those items to be removed to not muddy the waters. She noted that other cities did not have CIP projects embedded in the work plan and asked for guidance. When the CIP moved forward, she would like more information about how to know if we had adequate funding available, which would help the decision-making process. Director Alfaro noted that Leung covered this in his portion of the proposed budget presentation. There was a change in how we normally show transfers to the capital reserve. Historically, it was not shown in the budget, making it more difficult for CIP to do longer-term planning. We would transfer funds as part of mid-year once we closed out the previous fiscal year and identified how much fund balance we had. To make the CIP a better

planning tool, \$2.5 million is included annually for Council's consideration in the long-term forecast and the operating budget. CIP has planned that in their CIP budget as well.

Mayor Paul noted that we have a specialized, localized economy and inquired how we would conduct a localized economic analysis. In our forecasts, there is an assumption of recessions every so many years with the loss of fund balance. There is no historical precedence for that type of loss. If we look at the CIP, there are three houses where nothing is being done. We could be deriving income from that. Some of our peer jurisdictions have capital asset strategies to purchase properties as an income stream. He inquired how we would get the requisite evaluations done, whether these recommendations could be provided, and, budgetarily, what we should be setting aside. Mayor Paul noted that Mountain View had a Strategic Acquisition program, which is a significant revenue source for them. What kind of consultancy would be appropriate in this context? Rozillis noted there are folks who work with municipal real estate, and they have a real estate advisory director on the team to whom they can connect the City. The number one way that they have seen it is clients have commercial property. They provide subsidized rent to not-for-profits, community groups, and sometimes lower-income housing or affordable housing as ways to perpetuate community culture. She provided Santa Monica as an example of how they rent out a large portion of their real estate to arts organizations. Higher education also acquires real estate near campus like the private sector because they are often landlocked. She mentioned that the other piece is if these investments align with the City's mission and vision. As a Council, that is a good policy direction to think about. She recommended putting clear policy language around when to spend the money, what it's for, who gets to spend it, and how it's authorized as a future set of elected officials will spend it. Mayor Paul asked whether that began and ended with policy statements. Rozillis noted that at the policy level, they could look at the City's property inventory on an annual basis and see if it is at its highest and best use, currently vacant, or underutilized. Mayor Paul said it sounded like the recommendation would be to examine the policies first and determine the reason for the delay. If it wasn't one of those situations, then we should implement a policy related to real estate owned by the City. Rozillis confirmed and noted that a holistic approach is needed as it is also related to reserves and investments.

Chair Moore wanted to hear comments on funding for Enterprise Funds because the proposed budget revenues and expenditures for all four are negative. She would like guidance and advice on those. She noted that the Capital Improvement Fund, Stevens Creek Corridor Park Fund, and the Capital Reserve had \$42.8 million in the proposed budget ending fund balance. She also noted some IT improvements within Public Works. Because it's specialized project management, would someone from our IT department be best suited to select software or improvements? She mentioned that we funded this in our budget so Public Works can make these improvements. Favreau noted that the funding question is outside the scope of this assessment. Regarding the IT question, Public Works is actively working with IT to develop an in-house solution. Michael noted that they were working on developing new software, which is being managed by IT. Alfaro confirmed that the item for additional software was approved as part of the mid-year financial report. Leung added that the Enterprise Funds built up fund balance during the pandemic, which is why the transfers are slightly lower this year. Chair Moore mentioned that there was a policy

regarding how the fees would or would not cover what was provided and noted that in the future, this is something that they could look at with Moss Adams.

5. Receive Fiscal Policy Inventory and Gap Analysis Report and provide direction

Leung stated that policies and procedures are currently being reviewed by the City Manager and Director of Administrative Services and should be finalized by the end of this fiscal year. Ritchie provided an overview of the report and noted that management was proactive in completing and updating policies and procedures. Chair Moore wanted to see the prioritized work plan. Alfaro agreed with Moss Adams's comments and noted that staff had been documenting existing non-formalized procedures or security setups in our system and formalizing them. Once the policies were approved, staff would provide training sessions in July and August and refresher courses. No public comment.

Committeemember Hammer asked how the risk assessments were measured or evaluated: was it based on the risk of the area or the gap in the documentation. Ritchie noted that it was a mixture of both, and page 4 of the document explained this in further detail. Chair Moore pointed out that many high-risk areas were related to budgeting and wanted the Audit Committee to have full access to this report. Ritchie screen shared and provided an overview of the recommendations. Chair Moore wondered if the report mentioned the staffing level and if more staff was needed to implement these changes. Alfaro noted that, aside from the Purchasing Manager, the Budget Manager was requested to help alleviate the Finance Manager. Mayor Paul stated that the management responses were the same response pasted seven times over and inquired as to where the public was in this process and the Audit Committee's role. Ritchie noted that these are policies and procedures on what staff should be doing on a day-to-day basis. The Audit Committee has oversight but does not have to dabble that deep into management. They don't need to be as worried about the processes if the financial policies are being done correctly and they have reasonable assurances that the financial statements are correct. Mayor Paul noted that seven categories are being presented as high risk, and all they had to understand the corrective action is a statement that it is being worked on. How would they be able to get more of an understanding? He asked if he needed to submit a PRA asking for details. Rozillis noted that they have a recommendation tracking process where they provide the findings, recommendations, and status quarterly or annually. Mayor Paul asked if quarterly was the most frequent she had seen these types of updates. Rozillis confirmed. It hadn't been started for the Audit Committee because this is their first year. They could build it into the program for the next fiscal year. Chair Moore would like to see this item go to City Council. She was thinking of a budget audit, where someone would see, in regards to the entire budget, if funds coming in were attributed to departments correctly. Rozillis noted that there's a very important role that the external auditor plays in looking at how the City's funds are managed. Some of the questions are covered in that. She added that they could add value by looking at the City's budget process. Leung said that staff intended to bring both internal audit reports to City Council in June.

2. Review and consider accepting the Monthly Treasurer's Investment Report for April 2022

Leung provided an overview of how to review the reports. Chair Moore asked for the BNY Mellon statement and the Petty Cash and Change reports. Leung noted that staff would provide

the BNY Mellon statement moving forward and the Petty Cash and Change reports if requested. Chair Moore inquired about LAIF. She asked why the account value was not moving and for staff to provide any missing statements. Leung responded that the BNY Mellon account would be provided moving forward. Leung showed the bank statement balances. LAIF deposits interest quarterly, so the balance changes every quarter. McCarry provided an overview of their report and noted no recessionary trends. Mayor Paul motioned. Vice Chair Chen seconded. Motion carried unanimously by all members present.

8. Review Monthly Treasurer's Report for April 2022 and recommend filing with City Council

Leung provided an overview of the April 2022 reports. No public comment. Mayor Paul thanked Chair Moore for getting this information to the Audit Committee. Chair Moore asked how the accounts fit in with the fund statements and balances and how she should interpret them. She thinks the investment fund should be covering the \$228 million. The March report for workers' compensation had an ending balance of \$4 million. When she tried to compare it to the Wells Fargo account, it showed \$720k. Where is that \$4 million? She noted the same with parkland fees of \$22 million. We don't have a separate account somewhere for it. Where is that money sitting? Leung said that the City pooled funds for all of its accounts. All the funds, General Fund, Enterprise Funds, and Internal Services Funds, are pooled in the \$228 million. For example, worker's compensation funds would be transferred from the main checking account into those funds if transactions needed to be made. Chair Moore noted that the actual balance isn't high enough. Where would the money come from? We seemed to have more funds earmarked in the statement than in assets that could cover it. Leung noted that for all funds combined, the City has \$228.4 million. \$31.9 million is in cash in operating accounts, \$21 million is in cash equivalents in LAIF, and \$156.9 million was in our investment accounts with Chandler. Pooling the accounts allows the City to have greater liquidity and earn higher returns by allowing more funds to be allocated towards investments. Chair Moore noted that staff should anticipate that these questions may be asked again at City Council. Committeemember Hammer asked if Chair Moore was asking about cash flow and how we were monitoring it. Chair Moore confirmed.

Chair Moore asked how to interpret these fund balances when deciding on next year's budget. Alfaro noted that the \$43 million in fund balance was already tied up in existing projects because of how CIP was funded. CIP is funded completely in year one, and the funds are carried over to the next year. Staff will work with CIP to show the \$43 million and which projects have been allocated towards the remaining balance. Leung added that neither of these reports showed how much money was available to spend. Cash balance is different from fund balance because it is measured on a cash basis. Fund balance is the total fund balance for the entire fund, so it's not showing if funds have been earmarked for other projects. Monthly fund balances are based on what's been received and spent to date. Chair Moore requested if Special Revenue Funds 210, 215, and 230 should be rolled together. She requested if the funds could show the source of how the funds came to be (ex. resolution or municipal code by ordinance). She noted having the same question for Special Revenue Fund 270. She wondered how the Enterprise Funds were being kept in the black as it seemed they operated at a loss. Leung confirmed that the City transfers funds to these funds if they have a low fund balance on an annual basis as part of the proposed and

adopted budget process. Alfaro added that the fee study from Matrix Consulting recommended raising Parks and Recreation fees, but the City did not do that based on Council direction. Since then, they have been increasing it based on market data from the Parks and Recreation department. Leung added that for Parks and Recreation, fees are not increased based on CPI or other escalators. In 2016, Council voted to maintain the fees below cost-recovery levels. Mayor Paul motioned. Vice Chair Chen seconded. Motion carried unanimously by all members present.

6. Receive report on Interim Audit and AUP Engagements and provide direction

Chair Moore moved items 6, 7 (to include similar format to the April 2022 report) and 9 to a 5/24/22 continuation meeting. Mayor Paul seconded. Motion carried unanimously by all members present.

7. Review Monthly Treasurer's Report for March 2022 and recommend filing with City Council

Chair Moore moved items 6, 7 (to include similar format to the April 2022 report) and 9 to a 5/24/22 continuation meeting. Mayor Paul seconded. Motion carried unanimously by all members present.

9. Receive Audit Committee 2022 Schedule and Work Plan and provide direction to staff

Chair Moore moved items 6, 7 (to include similar format to the April 2022 report) and 9 to a 5/24/22 continuation meeting. Mayor Paul seconded. Motion carried unanimously by all members present.

OLD BUSINESS

None.

STAFF AND COMMITTEE REPORTS

FUTURE AGENDA SETTING

ADJOURNMENT

The meeting adjourned at 6:30 p.m.

Recording Secretary:

Janet Liang, Administrative Assistant