

**CITY OF SAN JOSE
LIBRARY PARCEL TAX FUND
(A Fund of the City of San José)**

Independent Auditor's Reports,
Financial Statements,
Required Supplementary Information,
and Independent Accountant's Report

For the Year Ended June 30, 2014



Certified Public Accountants.

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CITY OF SAN JOSE
LIBRARY PARCEL TAX FUND
(A Fund of the City of San José)
For the Year Ended June 30, 2014

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Independent Auditor's Report

City Council and
Members of the Citizen's Oversight Committee
City of San José, California

Report on the Financial Statements

We have audited the accompanying financial statements of the Library Parcel Tax Fund, a fund of the City of San José (City), as of and for the year ended June 30, 2014, and the related notes to the financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

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

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

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

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Library Parcel Tax Fund as of June 30, 2014, and the changes in financial position thereof for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis of a Matter

As discussed in Note 2 to the financial statements, the financial statements present only the Library Parcel Tax Fund and do not purport to, and do not, present fairly the financial position of the City as of June 30, 2014, and the changes in its financial position, or, where applicable, its cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America. Our opinion is not modified with respect to this matter.

Other Matters

Required Supplementary Information

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

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated November 14, 2014, on our consideration of City’s internal control over the Library Parcel Tax Fund’s financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the City’s internal control over financial reporting and compliance.



Walnut Creek, California

November 14, 2014

CITY OF SAN JOSE
LIBRARY PARCEL TAX FUND
(A Fund of the City of San José)
Balance Sheet
June 30, 2014

Assets

Equity in pooled cash and investments held in the City Treasury	\$ 10,089,114
Accounts receivable	107
Accrued interest receivable	8,647
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Total assets	<u>\$ 10,097,868</u>

Liabilities and Fund Balance

Liabilities:	
Accounts payable	\$ 40,732
Accrued salaries, wages and payroll taxes	80,122
	<hr/>
Total liabilities	120,854
Fund balance:	
Restricted for neighborhood library services	9,977,014
	<hr/>
Total liabilities and fund balance	<u>\$ 10,097,868</u>

See accompanying notes to the financial statements.

CITY OF SAN JOSE
LIBRARY PARCEL TAX FUND

(A Fund of the City of San José)

Statement of Revenues, Expenditures and Changes in Fund Balance
For the Year Ended June 30, 2014

Revenues:

Library parcel tax	\$ 7,914,158
Investment income	61,214
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Total revenues	7,975,372
	<hr/>

Expenditures:

Personal services	3,134,925
Materials acquisition	1,570,614
Non-personal services/equipment	625,320
Automation projects	1,365,442
Annual audit	12,006
Intergovernmental	12,855
	<hr/>
Total expenditures	6,721,162
	<hr/>
Change in fund balance	1,254,210
Fund balance, beginning of year	8,722,804
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Fund balance, end of year	\$ 9,977,014
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See accompanying notes to the financial statements.

CITY OF SAN JOSE
LIBRARY PARCEL TAX FUND
(A Fund of the City of San José)
Notes to the Financial Statements
For the Year Ended June 30, 2014

NOTE 1 – DESCRIPTION OF REPORTING ENTITY

In November 2004, registered voters of the City of San José (City) approved Measure S, a parcel tax for library specific purposes. The parcel tax replaced the ten-year Library Benefit Assessment District that ended on June 30, 2005. Beginning on July 1, 2005, the parcel tax is collected with the annual Santa Clara County property taxes for each fiscal year until June 30, 2015. Proceeds from the library parcel tax may only be expended for library purposes, including the following:

- the acquisition of library books and materials and related costs to maintain library collections at all libraries;
- the development and delivery of homework and educational programs for all age groups to support literacy and lifelong learning;
- the repair, equipping and staffing of libraries; and
- the cost of collection and administration of the library parcel tax.

The City Council may, by resolution of the City Council, increase the library parcel tax rates if the City Council finds that the cost of living in the City as shown on the Consumer Price Index (CPI) has increased over the preceding period. The increase in the library parcel tax rate shall not exceed the increase in the CPI for the applicable period, but in no event shall the increase exceed 3 percent. For the year ended June 30, 2014, the increase in the library parcel tax rate was 2.45 percent.

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation

The accompanying financial statements present only the financial position and the changes in financial position of the Library Parcel Tax Fund (Fund) and do not purport to, and do not, present fairly the City's financial position as of June 30, 2014, and the changes in its financial position, or, where applicable, its cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

A special revenue fund (governmental fund) is used to account for the City's library parcel tax activities. Special revenue funds are used to account for and report the proceeds of specific revenue sources that are restricted or committed to expenditures for specified purposes other than debt service or capital projects. Proceeds of specific revenue sources establish that one or more specific restricted or committed revenues should be the foundation for a special revenue fund.

Basis of Accounting

The Fund's activity is reported using the current financial resources measurement focus and the modified accrual basis of accounting. Revenues are recognized as soon as they are both measurable and available. Revenues are considered to be available when they are collectible within the current period or soon enough thereafter to pay liabilities of the current period. The City considers parcel tax (property tax) revenues and investment income to be available if they are collected within 60 days of the end of the current fiscal period. Expenditures are generally recorded when a liability is incurred, as under accrual accounting. However, expenditures related to vacation, sick leave, claims and judgments are recorded only when payment is due.

CITY OF SAN JOSE
LIBRARY PARCEL TAX FUND
(A Fund of the City of San José)
Notes to the Financial Statements
For the Year Ended June 30, 2014

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Fund Balance

Under GASB Statement No. 54, *Fund Balance Reporting and Governmental Fund Type Definitions*, the balance sheets of governmental funds classify fund balances based primarily on the extent to which the City is bound to honor constraints on the specific purposes for which those funds can be spent. The Fund only has restricted fund balance at June 30, 2014. Restricted fund balances are amounts when constraints placed on use of resources are either: (1) externally imposed by creditors (such as through debt covenants), grantors, contributors, or laws or regulations of other governments; or (2) imposed by law through constitutional provisions or enabling legislation.

Use of Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make certain estimates and assumptions that affect the reported amounts and disclosures. Accordingly, actual results may differ from those estimates.

NOTE 3 – CASH AND INVESTMENTS

Cash and investments balances of the Fund are pooled and invested in the City's investment pool. The Fund's portion of this pool is displayed on the balance sheet as "equity in pooled cash and investments held in the City Treasury." The amounts held in the City's investment pool can be withdrawn upon demand. Income earned or losses arising from pooled investments are allocated on a monthly basis by the City's Finance Department to the Fund based on the average weekly cash balances. These investments are reported at fair value generally based on quoted market prices in the accompanying financial statements and the corresponding change in fair value of investments are reported in the year in which the change occurred.

It is not possible to disclose relevant information about the Fund's separate portion of the investment pool. At June 30, 2014, the City's investment pool invested in U.S. government and agency securities, commercial paper, negotiable certificates of deposit, corporate medium-term notes, and California's Local Agency Investment Fund as authorized by the City's investment policy. The weighted average maturity of the City's investment pool is 532 days. Additional information regarding the characteristics of the City's entire investment pool can be found in the City's basic financial statements for the year ended June 30, 2014. A copy of that report may be obtained by contacting the City's Finance Department, 200 East Santa Clara Street, 13th Floor, San José, CA, 95113 or can be found at the City's Finance Department website at <http://www.csjfinance.org/>.

NOTE 4 – INTERGOVERNMENTAL EXPENDITURES

The City issued lease revenue bonds and commercial paper notes to pay for the City Hall construction costs. The Fund's share of the debt service is calculated as a percentage of library staff occupying City Hall coupled with an estimated use of the Council Chambers and other City Hall offices. For the year ended June 30, 2014, the Fund's share of the debt service paid to the City was \$12,855.

CITY OF SAN JOSE
LIBRARY PARCEL TAX FUND
(A Fund of the City of San José)
Notes to the Financial Statements
For the Year Ended June 30, 2014

NOTE 5 – OTHER COMMITMENTS

At June 30, 2014, the Fund has outstanding encumbrances for the following activities:

<u>Activity</u>	<u>Amount</u>
Materials acquisition	\$ 114,974
Non-personal services/equipment	15,285
Automation projects	31,422
Total encumbrances	<u><u>\$ 161,681</u></u>

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CITY OF SAN JOSE
LIBRARY PARCEL TAX FUND

(A Fund of the City of San José)

Schedule of Revenues, Expenditures and Changes in Fund Balance - Budget and Actual
 Budgetary Basis

For the Year Ended June 30, 2014

	Original Budget	Final Budget	Budgetary Basis Actual	Variance Over (Under)	GAAP Adjustments	GAAP Basis
Revenues:						
Library parcel tax	\$ 7,887,000	\$ 7,887,000	\$ 7,914,158	\$ 27,158	\$ -	\$ 7,914,158
Investment income	20,000	20,000	37,100	17,100	24,114	61,214
Total revenues	<u>7,907,000</u>	<u>7,907,000</u>	<u>7,951,258</u>	<u>44,258</u>	<u>24,114</u>	<u>7,975,372</u>
Expenditures:						
Personal services	4,189,270	3,837,070	3,134,925	(702,145)	-	3,134,925
Materials acquisition	1,992,000	2,292,000	1,685,588	(606,412)	(114,974)	1,570,614
Non-personal services/equipment	845,500	1,225,500	640,605	(584,895)	(15,285)	625,320
Automation projects	1,400,000	1,400,000	1,396,864	(3,136)	(31,422)	1,365,442
Annual audit	13,000	13,000	12,006	(994)	-	12,006
Intergovernmental	29,591	12,855	12,855	-	-	12,855
Total expenditures	<u>8,469,361</u>	<u>8,780,425</u>	<u>6,882,843</u>	<u>(1,897,582)</u>	<u>(161,681)</u>	<u>6,721,162</u>
Excess of revenues over expenditures	(562,361)	(873,425)	1,068,415	1,941,840	185,795	1,254,210
Change in fund balance	<u>\$ (562,361)</u>	<u>\$ (873,425)</u>	<u>1,068,415</u>	<u>\$ 1,941,840</u>	<u>185,795</u>	<u>1,254,210</u>
Fund balance, beginning of year			8,668,615		54,189	8,722,804
Liquidation of prior year encumbrances			75,802		(75,802)	-
Fund balance, end of year			<u>\$ 9,812,832</u>		<u>\$ 164,182</u>	<u>\$ 9,977,014</u>

See accompanying note to the required supplementary information.

CITY OF SAN JOSE
LIBRARY PARCEL TAX FUND
(A Fund of the City of San José)
Note to the Required Supplementary Information
For the Year Ended June 30, 2014

Budgetary Information

The adopted budget represents the financial and organizational plan by which the policies and programs approved by the City Council will be implemented. It includes: (1) the programs, projects, services and activities to be provided during the fiscal year; (2) estimated revenues available to finance the operating plan; and (3) the estimated spending requirements of the operating plan. The City Charter requires that the City establish a budgetary system for general operations and prohibits expending funds for which there is no legal appropriation. Annual budgets are prepared for the Library Parcel Tax Fund.

The annual appropriation ordinance adopts the budget at the appropriation level by expenditure category (personal services, non-personal services) within departments. Accordingly, the lowest level of budgetary control exercised by the City Council is the appropriation level within a department.

Budgetary Results Reconciled to GAAP

The budgetary process is based upon accounting for certain transactions on a basis other than the accounting principles generally accepted in the United States of America (GAAP) basis. The results of operations are presented in the accompanying budget and actual comparison schedule in accordance with the budgetary process (budgetary basis) to provide a meaningful comparison with the budget.

The major differences between the budgetary basis actual and GAAP basis are as follows:

- Certain accounts such as the change in fair value of investments included in the City's GAAP basis amounts, for which no formal budgets are prepared, are excluded from the budgetary basis comparison schedule.
- Year-end encumbrances are recognized as the equivalent of expenditures in the budgetary basis comparison schedule, while encumbered amounts are not recognized as expenditures on the GAAP basis until the equipment, supplies, or services are received.

**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 and
Members of the Citizen’s Oversight Committee
City of San José, California

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the Library Parcel Tax Fund (Fund), a fund of the City of San José (City), as of and for the year ended June 30, 2014, and the related notes to the financial statements, and have issued our report thereon dated November 14, 2014.

Internal Control Over Financial Reporting

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

Our consideration of internal control was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. However, as described in the accompanying schedule of findings and responses, we identified a deficiency in internal control that we consider to be a material weakness.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A *material weakness* is a deficiency, or combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity’s financial statements will not be prevented, or detected and corrected on a timely basis. We consider the deficiency described as item 2014-001 in the accompanying schedule of finding and response to be a material weakness.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Fund’s financial statements are free from 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 an instance of noncompliance that is required to be reported under *Government Auditing Standards* and which is described in the accompanying schedule of finding and response as item 2014-001.

City's Response to the Finding

The City's response to the finding identified in our audit is described in the accompanying schedule of finding and response. The City's response was not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on it.

Purpose of this Report

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

Macias Gini & O'Connell LLP

Walnut Creek, California
November 14, 2014

Independent Accountant's Report on Compliance with Measure S

City Council and
Members of the Citizen's Oversight Committee
City of San José, California

We have examined the City of San José's (City) compliance with certain provisions of Measure S during the year ended June 30, 2014 as follows:

- Parcel tax is used for the acquisition of library books and materials and related costs to maintain library collections at all libraries; the development and delivery of homework and educational programs for all age groups to support literacy and lifelong learning; the repair, equipping and staffing of libraries; and the cost of collection and administration of the library parcel tax.
- The City's annual parcel tax, \$25 (2006 annual parcel tax) for single-family residences and proportional for other properties, will be adjusted for inflation capped at 3% annually and will be limited to ten years.
- Independent audits will be performed.
- A citizen oversight committee will be established.

Management is responsible for the City's compliance with those requirements. Our responsibility is to express an opinion on the City's compliance based on our examination.

Our examination was conducted in accordance with attestation standards established by the American Institute of Certified Public Accountants and, accordingly, included 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 examination provides a reasonable basis for our opinion. Our examination does not provide a legal determination on the City's compliance with specified requirements.

In our opinion, the City complied, in all material respects, with the aforementioned requirements for the year ended June 30, 2014.

This report is intended solely for the information and use of the City Council, the Citizen's Oversight Committee, the City Auditor and the City's management and is not intended to be and should not be used by anyone other than these specified parties.



Walnut Creek, California
November 14, 2014

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CITY OF SAN JOSE
LIBRARY PARCEL TAX FUND
(A Fund of the City of San José)
Schedule of Finding and Response
For the Year Ended June 30, 2014

Item 2014-001 - Material Weakness in Internal Control, Material Noncompliance

Criteria:

In November 2004, registered voters of the City of San José (City) approved Measure S, a parcel tax for library specific purposes. Proceeds from the library parcel tax may only be expended for library purposes, including the following:

- the acquisition of library books and materials and related costs to maintain library collections at all libraries;
- the development and delivery of homework and educational programs for all age groups to support literacy and lifelong learning;
- the repair, equipping and staffing of libraries; and
- the cost of collection and administration of the library parcel tax.

Condition:

As part of the City's year-end closing process, the City recorded expenditures in the amount of \$257,000 in the Library Parcel Tax Fund related to the costs associated with the Library Parcel Tax Ballot Measure B inclusion in the June 2014 Primary elections. City Administration believed that the use of Library Parcel Tax funds was consistent with the fund's eligible uses based on the City's Budgeted Funds Guide. However, upon further inquiry the City Attorney's Office and the Finance Department did not believe that this was an eligible use of Measure S funds.

Cause and Effect:

The error was due to a misinterpretation of the intent of Measure S. While the cost of collection and administration of the current library parcel tax is appropriate, the cost of collection of a future potential tax does not appear appropriate. The impact of the error was an audit adjustment to correct the inappropriate charge to the Library Parcel Tax fund in the amount of \$257,000. The financial statements were subsequently corrected.

Recommendation:

The City should improve its communication between its departments, City Attorney's Office, and the Finance Department to better understand the restrictions on the use of Library Parcel Tax funds.

Management Response:

The City agrees that the communication between its departments, City Attorney's Office and the Finance Department should be coordinated to better understand the restrictions on the use of the Library Parcel Tax funds. As stated earlier, the City appropriately corrected the error.

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