

SAN JOSÉ OFFICE OF RETIREMENT SERVICES

**San José Federated City
Employees' Retirement System**

**San José Police and Fire
Department Retirement Plan**

Management Letter

Fiscal Year Ended June 30, 2025



Certified
Public
Accountants

SAN JOSÉ OFFICE OF RETIREMENT SERVICES

Management Letter

Fiscal Year Ended June 30, 2025

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October 31, 2025

To the Management of the San José Office of Retirement Services
San José, California

In planning and performing our audit of the financial statements of the San José Federated City Employees' Retirement System ("System") and San José Police and Fire Department Retirement Plan ("Plan") (together that "Plans") as of and for the fiscal year ended June 30, 2025, 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 (*Government Auditing Standards*), we considered the Plans' internal control over financial reporting (internal control) as a basis for designing audit procedures that are appropriate in the circumstances 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 Plans' internal control. Accordingly, we do not express an opinion on the effectiveness of Plans' internal control.

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 deficiency in design exists when (a) a control necessary to meet the control objective is missing, or (b) an existing control is not properly designed so that, even if the control operates as designed, the control objective would not be met. A deficiency in operation exists when a properly designed control does not operate as designed or when the person performing the control does not possess the necessary authority or competence to perform the control effectively.

A material weakness is a deficiency, or a 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.

A significant deficiency is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

We previously issued our report on internal control and compliance in accordance with *Government Auditing Standards* issued by the Comptroller General of the United States in a separate communication dated October 31, 2025. This communication does not affect that report.

Our current year comment and recommendation involving internal control are presented in the attached summary. In addition, the status of prior year comments and recommendations is also presented. Our comments and recommendations have been discussed with appropriate members of management and include management's response. Management's response to the internal control deficiency identified in our audit was not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on it.

This communication is intended solely for the information and use of management, the Audit Committees, the Boards of Administration, and others within the organization, and is not intended to be and should not be used by anyone other than these specified parties.

Respectfully,

Macias Gini & O'Connell LLP

Walnut Creek, California

SAN JOSÉ OFFICE OF RETIREMENT SERVICES

Current Year Comment and Recommendation

Fiscal Year Ended June 30, 2025

Fiscal Year 2025 Observation #1 – Completeness and Accuracy of Participant Census Data

Criteria

Management is responsible for accurate and complete participant census data, as codified in San José Municipal Code Chapter 3.36.430, which mandates that the Plan maintain records and accounts necessary for the determination of all member benefits. Compliance with this code section necessitates that the Plan Sponsor provides the Plan's actuary with verified error-free census data annually. Without accurate and current data (covering demographics, service history, and compensation), the annual actuarial valuation becomes fundamentally unreliable. This directly compromises the integrity of the Plan's reported accrued liabilities and the calculation of the required employer contribution rate, thereby failing to meet the foundational record-keeping standards required for responsible financial stewardship.

Condition

As part of our audit, we performed tests, on a sample basis, of the accuracy and completeness of active member census data. Our procedures included validating member status (e.g. active, vested, retired etc.), and recalculating service credits, pensionable payroll, and member contributions and interest, at the valuation date. The results of our testing identified 10 members with missing service credits, pensionable payroll, contributions and interest. Further, 10 out of the 10 members were incorrectly classified as inactive in the final data file used by the Plan's actuary.

Cause

Based on discussions with ORS management, these 10 members, at one time, were on military leave in accordance with the Uniformed Services Employment & Reemployment Rights Act (USERRA). When an active member goes on military leave their status is changed to "leave of absence" in the City's HR system and the ORS pension administration system. When these members return to active service with the City they should return to active status within both systems, according to the following process:

The process for returning members to active status from military leave is as follows:

1. **City Payroll & HR** prepare a reconciliation spreadsheet and share it with the ORS Benefits Team.
2. The **ORS Benefits Team** reviews the spreadsheet and makes the necessary updates in Pension Gold (service purchase contract).
3. The **ORS Benefits Team** then drafts a memo for ORS-IT.
4. **ORS-IT** then proceeds to clear all the exceptions and works closely with the ORS Benefits Team, as the exceptions could go back many years, and each case is different.

Based on discussion, it appears as though the ORS Benefit's team never received the reconciliation spreadsheet for the 10 members, thus, they were not able to process the member's military leave and subsequent data into the Pension Gold system.

SAN JOSÉ OFFICE OF RETIREMENT SERVICES
Current Year Comment and Recommendation (Continued)
Fiscal Year Ended June 30, 2025

Effect

At June 30, 2025, the overall effect was:

- 10 out of the 10 members were incorrectly classified as “on leave” instead of “active” in the census data file provided to the actuary
- Member accounts were understated by an estimated \$1,544,200 in salary, \$1,260,363 in contributions and interest, and 63.228 years of credited service
- 10 members continuously appeared on the bi-weekly exception reports generated every payroll cycle throughout the years (current and prior)

Incorrect classification of members in the census data file can lead to understatement of the total pension and total OPEB liabilities for accounting purposes, and the actuarial accrued liabilities for funding purposes. Our actuarial specialist estimated the potential impacts to the total pension and OPEB liabilities to be 0.02% and 0.1% understated, respectively, which was deemed immaterial to the financial statements as a whole.

Though the balances reviewed may not be significant to the overall valuation, the combination of incomplete and inaccurate data directly compromises the reliability of the annual actuarial valuation. This may lead to a potential material misstatement of the Plan's actuarial accrued liability, specifically resulting in an understated funding obligation and a misrepresentation of the Plan's true financial health. Additionally, Inaccurate records increase the risk of regulatory non-compliance, create significant administrative burdens for accurate benefit calculations, and pose a critical risk of issuing incorrect benefit payments to members.

Recommendation

We recommend ORS, working with the City, revise policies and procedures to ensure more timely processing of members returning from military leave.

Management Response

ORS agrees with the recommendation and acknowledges the importance of timely and accurate processing of members returning from military leave. As of December 2025, ORS has received reconciliation spreadsheets from City Payroll for three of the eleven outstanding military leave cases, and the affected members' accounts in the Pension Gold system have been updated accordingly.

ORS is actively collaborating with City Payroll and HR to address the remaining cases and to strengthen controls over the military leave reconciliation process. As part of these efforts, ORS is evaluating potential system programming enhancements within both the Pension Gold and City Payroll systems to reduce the volume military leave-related exceptions. Additionally, coordination meetings between ORS and the City have been increased from quarterly to monthly to improve communication, tracking, and timeliness of future reconciliations.

SAN JOSÉ OFFICE OF RETIREMENT SERVICES
Status of Prior Year Comment and Recommendation
Fiscal Year Ended June 30, 2025

Fiscal Year 2024 Observation #1 – Completeness and Accuracy of Investment Disclosures

Criteria

Management is responsible for the accuracy of the data and the completeness and fairness of the presentation of information in the financial statements, including disclosures. Governmental Accounting Standards Board Statement No. 72 (GASB 72), *Fair Value Measurement and Application*, requires disclosure of the amount of a government's unfunded commitments related to its investments in certain entities that calculate the net asset value (NAV) per share (or its equivalent).

Condition

As part of our audit, we performed tests, on a sample basis, of the accuracy and completeness of unfunded commitments related to investments whose fair value is measured at the NAV. Our procedures included confirming unfunded commitment amounts directly with third-party investment managers and reviewing their June 30th capital account statements. The results of our testing identified differences between the unfunded commitment amounts reported by management and amounts confirmed by investment managers. These amounts were as follows:

- Federated City Employees' Retirement System: For the samples tested, the investment manager reported higher amounts than those disclosed by management in the amount of \$10,115,561.
- Police and Fire Department Retirement Plan: For the samples tested, the investment manager reported higher amounts than those disclosed by management in the amount of \$20,464,467.

These amounts were immaterial overall to each Plan's financial statements, respectively.

Cause

Based on discussions, our understanding is that certain financial statement disclosures, including the unfunded commitments, are prepared by the San José Office of Retirement Services Investment Group (IG) and provided to the accounting division. The IG relies on investment consultants, Neuberger Berman for private equity, and Meketa for all other private asset classes, to keep track of unfunded commitments, who prepare reports of the balances at year-end, and provide their reports to IG. However, there is no independent verification or reconciliation performed between the reports and the manager's capital account statements and/or internal records.

Effect

Investment disclosures contained unreconciled differences and could be incomplete and/or inaccurate.

Recommendation

We recommend management implement policies and procedures to perform independent review and verification of the information provided to them for financial reporting purposes, including comparing or reconciling the reports to investment manager capital account statements and internal records as necessary.

SAN JOSÉ OFFICE OF RETIREMENT SERVICES
Status of Prior Year Comment and Recommendation (Continued)
Fiscal Year Ended June 30, 2025

Management Response

Management is on board with the recommendation. ORS has engaged Meketa (all private asset classes except private equity) and Neuberger Berman (private equity) to track unfunded commitments on a quarterly basis as part of the private markets reports. Due to the elongated timeframes for receiving valuations for alternative investments and time to reconcile data, these reports are lagged by one quarter and publicly reported and presented in Board meetings on the last month of the quarter (ex: June 30, 2024 reports presented on the first (P&F) and third (Fed) Thursday of December 2024). Staff will assess the current process with all parties involved and implement procedural changes as necessary to ensure that data is reconciled.

Fiscal Year 2025 Status

Based on the audit procedures performed, this recommendation has been fully implemented.