

# Memorandum

**TO:** HONORABLE MAYOR AND  
CITY COUNCIL AND  
REDEVELOPMENT AGENCY BOARD

**FROM:** Sharon W. Erickson

**SUBJECT:** AGREEMENTS WITH MACIAS,  
GINI & O'CONNELL LLP TO  
PROVIDE ANNUAL FINANCIAL  
AND COMPLIANCE AUDITS

**DATE:** April 20, 2010

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Approved

Date

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## RECOMMENDATION

- (a) Approval by the City Council of an agreement with Macias Gini & O'Connell LLP to perform Annual Financial and Compliance Audit Services for fiscal years ending June 30, 2010, 2011, and 2012, and with two (2) one-year extension options for fiscal years ended June 30, 2013 and 2014, for a fee not to exceed \$495,554 for fiscal year 2010-11 and with annual increases adjusted by the CPI for each subsequent fiscal year, subject to annual increases adjusted by the CPI for each subsequent fiscal year, for a total amount not to exceed \$2,631,455 for a potential five year term subject to annual appropriation of funds by the City Council.
- (b) Approval by the Redevelopment Agency Board of an agreement with Macias Gini & O'Connell LLP to perform Annual Financial and Compliance Audit Services for fiscal years ending June 30, 2010, 2011, and 2012,, and with two (2) one-year extension options for fiscal years ended June 30, 2013 and 2014, for a fee not to exceed \$81,375 for fiscal year 2010-11 and with annual increases adjusted by the CPI for each subsequent fiscal year, subject to annual increases adjusted by the CPI for each subsequent fiscal year, for a total amount not to exceed \$432,112 for a potential five year term subject to annual appropriation of funds by the Redevelopment Agency Board.

## BACKGROUND

Section 805 of the San Jose City Charter requires that the independent Office of the City Auditor conduct or cause to be conducted annual post audits of all the fiscal transactions and accounts kept by or for the City. Section 805 specifies that such audits shall include but not be limited to the examination and analysis of fiscal procedures and the examination, checking, and verification of accounts and expenditures. The audits shall be conducted in accordance with generally accepted auditing standards and accordingly shall include tests of the accounting records and

other auditing procedures as may be considered necessary under the circumstances. The audits shall include the issuance of suitable reports of examination so the Council and the public.

Section 1215 of the San Jose City Charter further requires that the City Council employ an independent certified public accountant who shall audit the municipal books, records, accounts and fiscal procedures of all officers of the City who receive, administer or disburse public funds on behalf of the City.

In addition to the above requirements set forth in the City Charter, as a recipient of Federal, State, and local government financial assistance, the City is required to undergo a compliance audit in conformity with the provisions of the Single Audit Act of 1984, as amended in 1996, the United States Office of Management and Budget Circular A-133, Audits of State, Local Governments and Non-Profit Organizations and Government Auditing Standards issued by the Comptroller General of the United States.

Macias Gini and O'Connell, LLP (MGO) has conducted the annual financial and compliance audits of the City and its related entities for the past ten years. The contract with MGO ends on April 30, 2010. Accordingly, the independent Office of the City Auditor initiated a Request for Proposal (RFP) process to select a firm to provide financial and compliance audit services.

### ANALYSIS

With input from various departments, the independent Office of the City Auditor prepared an RFP for external audit services for the City and all its related entities. The RFP was posted on the BidSync e-Procurement system March 8, 2010 (RFP09-10-EA1).

As in previous years, the RFP covered the City, Airport, Convention and Cultural Facilities, Hayes Mansion, Deferred Compensation (separate contract), Redevelopment Agency (separate contract), Retirement Funds (separate contracts), and San Jose-Santa Clara Clean Water Financing Authority (separate contract). The intent of a consolidated RFP process for all of the City's related entities was improved timeliness, increased efficiency, and better pricing. Because auditor rotation is not mandatory, we encouraged participation in the RFP by all qualified firms, including MGO.

More than 100 inquiries and clarification requests were received, and answers were distributed on BidSync on March 22, 2010. Six (6) proposals were received by the due date on March 29, 2010. One proposal was determined to be non-responsive; a seventh proposal was received by email after the due date.

The remaining five (5) proposals were evaluated by an interdepartmental team consisting of staff from the City Auditor's Office, Finance, Airport, Housing, Redevelopment, and Retirement Services. Proposals were evaluated using the following criteria and weighting:

Criteria	Weight
Minimum qualifications	Pass/Fail
Organizational experience of the firm	15%
Project team	20%
Proposer capabilities and approach	30%
Local business enterprise preference	5%
Small business enterprise preference	5%
Cost	25%

In the first phase, the team evaluated respondents on the basis of their written proposals, and selected three (3) firms to be interviewed. After the interviews, the evaluation team finalized their rankings. The evaluation team recommended the selection of MGO to provide financial and compliance audit services and to enter into agreements with the firm. The table below provides a summary of the evaluation that was conducted in accordance with the process set forth in the RFP:

Rank	Firm	Experience of Firm	Project Team	Capabilities and Approach	Local Business Enterprise Preference	Small Business Enterprise Preference	Cost	TOTAL
	Weight	15%	20%	30%	5%	5%	25%	100%
1	Macias Gini & O'Connell	14.57	18.00	27.00	0.00	0.00	23.00	82.57
2	KPMG	13.07	17.71	20.14	5.00	0.00	17.00	72.93
3	Maze & Associates	10.93	15.71	22.71	0.00	0.00	22.00	71.36
4	Mayer Hoffman McCann	9.00	11.43	16.29	5.00	0.00	25.00	66.71
5	Vavrinek, Tine, Day & Co	8.79	11.14	17.57	5.00	0.00	21.00	63.50

A sixth firm, Moss Adams LLP, submitted a proposal, but was determined to be non-responsive because the proposal was not complete.

MGO is an experienced, government audit firm. In addition to having been San Jose's auditor for the last 10 years, MGO is the principal auditor for some of the largest cities in California including San Diego, San Francisco, Fresno, Sacramento, Oakland, and Santa Ana. MGO received an unqualified opinion (the highest level of assurance possible) during their 2009 quality control review. To keep things fresh, MGO is rotating in experienced partners and additional expertise to the San Jose engagement, including additional expertise in auditing retirement systems and Redevelopment Agencies.

The service specified in the RFP will be addressed in six separate agreements with **total annual compensation totaling \$688,000 for each of the first two years (a savings of \$130,859, or**

**16% less than MGO's 2009 contract fees of \$818,859).** The six agreements with the respective services and first-year compensation are shown below.

1. Agreement 1 is for general audit services with total annual compensation in the first and second years not to exceed \$495,554 (a savings of \$133,474 or 21% less than last year's agreement) to provide the following:
  - General City Audit, Basic Financial Statements, Financial Disclosures, and Comprehensive Annual Financial Report (CAFR)
  - Single Audit
  - Norman Y. Mineta San Jose International Airport Financial Audit
  - San Jose-Santa Clara Clean Water Financing Authority Compliance Audit
  - Dolce-Hayes Mansion Financial Audit and Agreed-Upon Procedures
  - Bicycle/Pedestrian Facilities Grant
  - Audit of the Financial Statements Prepared by Team San Jose for the San Jose Convention Center and Cultural Facilities
  - Parks Bond Funds Financial Statements and Report on Compliance with Measure "P"
  - Branch Library Bond Projects Fund Financial Statements and Report on Compliance with Measure "O"
  - Library Parcel Tax Fund Financial Statements and Report on Compliance with Measure "S"
  - Semi-Annual Investment Program Compliance Audit
  - City's 911, Fire, Police, Paramedic and Neighborhood Security Act (Public Safety Bonds) Financial Statements and Report on Compliance with Measure "O" (2002)
2. Agreement 2 is for the financial audit of the San Jose-Clean Water Authority, with total annual compensation for the first and second years of \$13,546 (a savings of \$3,762, or 22% less than last year's agreement). This agreement is within the City Auditor's signing authority.
3. Agreement 3 is for Deferred Compensation audit services with total annual compensation for the first and second years not to exceed \$7,373. The Deferred Compensation Committee will be asked to authorize this agreement.
4. Agreement 4 is with the Redevelopment Agency with total annual compensation for the first and second years not to exceed \$81,375 (a savings of \$13,393, or 14% less than last year's agreement). In the above resolution (b), the Redevelopment Agency Board is approving this agreement to provide the following:
  - General Agency Audit, Basic Financial Statements, Other Required Supplemental Information, and CAFR
  - Compliance Audit
5. Agreement 5 is for the comprehensive annual financial audit of the Federated City Employees' Retirement System, with total annual compensation for the first and second

years not to exceed \$45,076 (an increase of \$9,900 or 28% more than last year's agreement). The Federated City Employees' Retirement System Board of administration will be asked to approve this agreement on May 13, 2010.

It should be noted that on April 8<sup>th</sup>, the Federated Board discussed, but made no decision, whether to proceed with a separate RFP for the same services described here, beginning as early as the second year of the agreement. The proposed agreement with MGO allows flexibility to adjust the scope of the work for the retirement plans, if needed.

6. Agreement 6 is for the comprehensive annual financial audit of the Police and Fire Department Retirement Plan, with total annual compensation for the first and second years of \$45,076 (an increase of \$9,900 or 28% more than last year's agreement). The Police and Fire Department Retirement Plan Board Administration will be asked to approve this agreement on May 6, 2010.

It should be noted that on April 1<sup>st</sup>, the Police and Fire Board discussed, but made no decision, whether to proceed with a separate RFP for the same services described here. The proposed agreement with MGO allows flexibility to adjust the scope of the work for the retirement plans, if needed. On April 12<sup>th</sup>, Retirement staff issued an RFP for an audit of the Police and Fire Department Retirement Plan's comprehensive annual financial statements. Depending on the actions of the Police and Fire Board on May 6<sup>th</sup>, the City Auditor may return to the City Council for additional direction.

### **SUMMARY AND COST IMPLICATIONS**

MGO has conducted the financial and compliance audits the past ten years. Their contract ends on April 30, 2010. Accordingly, the City Auditor initiated an RFP process to select a firm to provide financial and compliance audit services. Five (5) firms were found to be responsive. The evaluation team found the MGO proposal to be complete and the firm highly qualified to perform the work. Moreover, MGO's cost proposal of \$688,000 is \$130,859 or 16% lower than the last year of our current contract. Accordingly, the evaluation team recommends that MGO be awarded the contracts to perform annual financial and compliance audits for fiscal years ended June 30, 2010, 2011, and 2012, with two (2) one-year extension options for fiscal years ended June 30, 2013 and 2014. The contract limits future annual cost increases to the Consumer Price Index Pacific and U.S. City Average, but shall not exceed 5 percent from year to year. In consideration of the City's significant budget shortfalls, MGO has agreed to waive CPI adjustments of the second year of the agreement, excepting for any additional work the City may request.

The following budget information addresses the compensation to be paid to MGO for the first year of the agreements involving the City, including the audits of the Airport, Deferred Compensation Plan, Convention Center, Dolce Hayes Mansion, and the San Jose-Santa Clara

Clean Water Financing Authority. The costs of futures years' audit services are subject to annual appropriation of funds by the City Council.

<b>Fund #</b>	<b>Appn. #</b>	<b>Appn. Name</b>	<b>Total Appn.</b>	<b>Cost</b>	<b>2009-2010 Adopted Budget</b>	<b>Last Budget Action (Date, Ord. No.)</b>
001	2029	Annual Audit	\$308,366	\$203,215	Operating Budget, Page IX-30	06/23/2009, Ord #28593
001	2042	Grant Compliance Single Audit	\$118,652	\$71,927	Operating Budget, Page IX-31	06/23/2009, Ord #28593
001	3727	Bond Project Audits	\$115,625	\$50,881	Operating Budget, Page IX-30	10/20/2009, Ord #28653
418	0722	Library Non-Personal/Equipment	603,500	\$11,395	Operating Budget, Page XI-52	10/20/2009, Ord #28653
523	2029	Annual Audit (Airport)	\$68,250	\$55,393	Operating Budget, Page XI-3	06/23/2009, Ord #28593
465	4292	Bicycle and Pedestrian Facilities	\$823,000	\$7,878	Capital Budget, Page V-962	10/20/2009, Ord #28653
541	0047	Clean Water Financing Authority Compliance Audit	\$30,000	\$21,049	Operating Budget, Page XI-82	06/23/2009, Ord #28593
422	3356	Hayes Consultant Services	120,199	\$30,401	Operating Budget, Page XI-24	02/09/2010, Ord #28698
536	0672	Convention Facilities Non-Personal/Equipment	\$5,104,549	\$43,415	Operating Budget, Page XI-25	02/09/2010, Ord #28698
001	0482	Human Resources Non-Personal/Equipment (Deferred Comp Audit)	\$1,257,275	\$7,373	Operating Budget, Page VIII-140	02/09/2010, Ord #28698
512	4341	Plant Reliability	\$20,900,000	\$13,546	Capital Budget, Page V-147	06/23/2009, Ord #28593

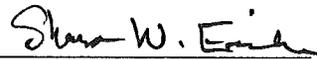
The proposed first year fee of \$45,076 for the City Employees' Retirement System financial audit will be paid out of the Federated Retirement Fund budget. The proposed first year fee of \$45,076 for the Police and Fire Department Retirement Plan financial audit will be paid out of

the Police and Fire Retirement Fund budget. The cost of future years' audit services is subject to approval of each Plan's annual budget by the respective Retirement boards.

The proposed first year fee of \$81,375 for the Redevelopment Agency financial audit will be paid out of the Agency's annual operating budgets. The cost of future years' audit services is subject to annual appropriation of funds by the Redevelopment Agency Board.

### COORDINATION

This memorandum has been coordinated with Purchasing, the City Attorney's Office, the Finance Department, Redevelopment Agency, and the Budget Office.



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