

Memorandum

TO: Honorable Mayor and City Council

FROM: Sharon W. Erickson,
City Auditor

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

DATE: January 26, 2018

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, 2018, 2019, and 2020 with three one-year extension options for fiscal years ended June 30, 2021, 2022, and 2023, with annual compensation not to exceed \$612,664 in year one and fees adjusted for subsequent years by the Consumer Price Index, not to exceed 3 percent per year in years two through six, for a total amount not to exceed \$3,952,789 for a potential six year term subject to annual appropriation of funds by the City Council.
- b) Approval by the Board of the Successor Agency to the Redevelopment Agency of an agreement with Macias, Gini & O'Connell LLP to perform annual financial and compliance audit services for fiscal years ending June 30, 2018, 2019, and 2020 with three one-year extension options for fiscal years ended June 30, 2021, 2022, and 2023, with annual compensation not to exceed \$55,132 in year one and fees adjusted for subsequent years by the Consumer Price Index, not to exceed 3 percent per year in years two through six, for a total amount not to exceed \$355,700 for a potential six year term subject to annual appropriation of funds by the Board of the Successor Agency.

BACKGROUND

Section 805 of the San José City Charter specifies that the 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. In addition, Section 1215 of the San José City Charter 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 November 2015 the City issued a Request for Proposal (RFP) for external audit services for the City and its related entities. The RFP covered the City, Airport, Convention and Cultural Facilities, Hayes Mansion, Deferred Compensation, Successor Agency to the Redevelopment Agency, Retirement Plans, and San José-Santa Clara Clean Water Financing Authority. Three proposals were received by the deadline and two were invited for an interview: Macias Gini and O'Connell LLP (MGO) and Grant Thornton LLP (Grant Thornton). Grant Thornton was selected and provided audit services for the fiscal years ended June 30, 2016 and 2017.

On January 8, 2018, the City Auditor terminated the agreements with Grant Thornton for audit services for the City, the Clean Water Financing Authority, the Deferred Compensation plan, and the Successor Agency to the Redevelopment Agency. The Federated Employees Retirement System and Police and Fire

Retirement Plan hold separate agreements with Grant Thornton and plan to keep those agreements in place.

In order to retain external audit services, the City Auditor asked MGO if it would honor the pricing in its RFP proposal and MGO has agreed to do so.

ANALYSIS

The City is currently analyzing its accounting practices to determine the potential impact on the financial statements of at least seven Governmental Accounting Standards Board (GASB) pronouncements that will be effective for the City's financial statements over the next three years. This includes GASB Statement No. 75, *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions*. Application of Statement No. 75 is effective for the City's fiscal year ending June 30, 2018. MGO is well experienced to provide both independent audit services to the City and to provide advice on the implementation of GASB 75 due to their experience, qualifications and demonstrated ability.

MGO's state and local government practice is one of the largest in the U.S. Their local government specialists have served over 100 cities in California. MGO is familiar with the City's operations and accounting systems, having previously conducted the annual financial and compliance audits of the City and its related entities.

SUMMARY AND COST IMPLICATIONS

The services will be addressed in four separate agreements as follows:

- Agreement #1 - General Contract including the City of San José Comprehensive Annual Financial Report (CAFR); Gann Report; Basic Financial Statements; Single Audit; Norman Y. Mineta San Jose International Airport CAFR; San Jose – Santa Clara Clean Water Financing Authority Compliance Audit; Dolce Hayes Mansion; Pedestrian/Bicycle Facilities; Convention Center & Visitors' Bureau; Branch Library Bond Projects Fund; Parks Bond Funds; Library Parcel Tax Fund; Semi-annual Investment Program Compliance; Public Safety Bonds; and South Bay Water Recycling project. The proposed annual compensation in the first year of the agreement is \$612,664 (total over six years not to exceed \$3,952,789).
- Agreement #2 – Successor Agency to the Redevelopment Agency. The proposed first year fee for the Successor Agency financial audit is \$54,080 (total over six years not to exceed \$344,148) to be paid out of the Successor Agency's annual operating budget. The cost of future years' audit services is subject to annual appropriation of funds by the Successor Agency Board. Currently, the Successor Agency's Administrative Budget and Recognized Obligation Payment Schedule (ROPS) include an enforceable obligation to make payments for financial audit services.

- Agreement #3 – Deferred Compensation. The proposed first year fee for the audit is \$8,542 (\$55,110 total over six years). These services will be performed under a separate agreement to be approved by the Deferred Compensation Board.
- Agreement #4 – San José-Santa Clara Clean Water Financing Authority. The proposed first year fee is \$16,241 (total over six years not to exceed \$104,785). These services will be performed under separate agreement to be approved by the Clean Water Financing Authority.

Annual compensation for all four agreements totals \$692,578 in the first year. The cost of future years' audit services are subject to annual cost of living adjustments (capped at 3 percent per year) and annual appropriation of funds by the City Council. This compares to expected 2018 fees of \$654,190 under the previous agreements.

BUDGET REFERENCE

The following budget information addresses the compensation to be paid to MGO for the first year of the three agreements involving the City, including the amounts approved by the Deferred Compensation Board and the Clean Water Financing Authority. Net-zero budget actions will be brought forward as part of the 2017-2018 Mid-Year Budget Review to shift funding between the General Fund appropriations to align the budgets with the anticipated costs.

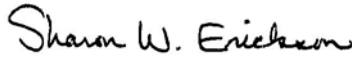
Fund #	Appn #	Appn Name	Total Appn	Cost	2017-18 Adopted Budget Operating/ Capital Page	Last Budget Action (Date, Ord. No.)
001	2029	Annual Audit	\$185,000	\$239,380	912	06/20/2017, 29962
001	2042	Grant Compliance Single Audit	\$125,000	\$84,166	913	06/20/2017, 29962
001	3727	Bond Project Audits and Semi-Annual Investment Compliance	\$110,000	\$60,486	912	10/17/2017, 30014
418	2029	Annual Audit (Library parcel tax)	\$17,000	\$13,387	1008	06/20/2017, 29962
523	2029	Annual Audit (Airport)	\$78,250	\$73,838	951	06/20/2017, 29962
422	3356	Hayes Consultant Costs	\$139,170	\$35,636	978	06/20/2017, 29962
541	0047	Clean Water Financing Authority Compliance Audit	\$30,750	\$24,695	1040	06/20/2017, 29962
512	6584	Payment For Clean Water Financing Authority Trustee	\$5,000	\$16,241	308	06/20/2017, 29962
465	4292	Bicycle and Pedestrian Facilities	\$2,892,000	\$9,135	1002	10/17/2017, 30014

Fund #	Appn #	Appn Name	Total Appn	Cost	2017-18 Adopted Budget Operating/ Capital Page	Last Budget Action (Date, Ord. No.)
001	0482	Human Resources Non-Personal/ Equipment (Deferred Compensation)	\$3,690,119	\$8,542	661	10/17/2017, 30014
536	3983	Convention Facilities Operations	\$5,679,000	\$50,928	981	06/20/2017, 29962
513	0762	Environmental Services Non-Personal Equipment (South Bay Water Recycling)	\$34,082,102	\$21,012	1037	10/17/2017, 30014

COORDINATION

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

Respectfully submitted,


Sharon W. Erickson
City Auditor

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