



CITY OF MOUNTAIN VIEW

MEMORANDUMFinance and Administrative
Services Department

DATE: February 28, 2022

TO: Council Finance Committee

FROM: Jesse Takahashi, Finance and Administrative Services Director

SUBJECT: **Extend the City's External Auditors' Contract and Amend the Contract to Include GASB 87 Consultation Service**

PURPOSE

This memorandum discusses the contract for external audit services and staff's intention to extend the contract up to two years. This memorandum also discusses amending the auditing contract to include consulting services related to the implementation of Governmental Accounting Standard Board Statement No. 87 (GASB 87).

BACKGROUND

Section 1106 of the City Charter states that the City Council shall employ an independent certified public accountant to examine the City's books, records, inventories, and reports. In 2015, in accordance with the City Charter and Council Policy No. B-6 (Attachment 1), Selection of External Independent Auditor, the City Council appointed Macias Gini & O'Connell, LLP (MGO), to serve as the City's independent certified public accountant. The contract period with MGO was for four years with an option to extend for two 1-year periods. In April 2020, the City exercised the option to extend the contract for two years, Fiscal Years 2019-20 and 2020-21. The contract extension period ended with the completion of the audit for Fiscal Year 2020-21.

In addition to the annual financial audits, the Council's external independent auditors also conduct other audit-related assignments, including special agreed-upon procedures regarding compliance review for certain aspects of the City's operations.

ANALYSIS

Contract Extension

The Government Finance Officers Association (GFOA) has issued a best practices recommendation for procurement of audit services. This best practice memorandum is attached (Attachment 2).

The GFOA recommends a full-scale competitive bidding process after the end of each contract term. While they recognize that ideally, auditor independence would be enhanced by a change in auditors at the end of the term, it may be counterproductive to make a mandatory change in the public sector. The private sector often changes auditors at the end of each term; however, there are a limited number of firms that are fully qualified to perform public-sector audits, and a frequent lack of competition among those firms may not result in lower costs. Costs will also increase for the disruption and time it takes the new auditor to become familiar with the City's operations and controls.

The City of Mountain View has used a four-year term with the optional extensions for the last three audit contracts. The GFOA recommends that multi-year agreements for audit services be for a period of at least five years. This allows for greater continuity and helps minimize the potential for disruption. It can also reduce the overall cost of audits by allowing auditors to recover "start-up" costs over several years.

The GFOA best practice memorandum also addresses the issue of an automatic renewal of an audit contract. It indicates that an automatic renewal for a second term would be consistent with their recommendations if the auditor's performance is satisfactory.

Additionally, since this is the first year of implementing GASB 87, it will be a challenge for staff to handle implementing both GASB 87 and changing auditors, which would be a significant undertaking.

MGO's performance over the past six years has proven satisfactory. MGO has submitted a proposal extending the current contract for two more years and proposed a 3% cost-of-living adjustment for the first year (Fiscal Year 2022-23) and NO price increase for the second year (see Attachment 1 for details). This is particularly noteworthy given the recent increase in inflation.

If the CFC does not recommend extending the contract, then the external auditor selection process described in City Council Policy B-6 should begin right away.

GASB 87 Consultation Service

Governmental Accounting Standards Board Statement No. 87, Leases (GASB 87), was issued in June 2017 and is effective for reporting periods beginning after June 15, 2021. GASB 87 substantially changes the way government entities account for leases. The City has many complex lease agreements, including Google leases, MV 101 Development, LLC (Ameswell) leases, RGC Mountain View I, and LLC (Hope Street) leases. All of these leases will need research and review as well as computations to determine the required information needed to report annually.

Considering the complexity and workload of the GASB 87 implementation project, many governmental entities have retained consultation services of accounting firms to help them with the implementation. Because MGO has been the City's auditor for the past six years and is familiar with the City's numerous land leases, staff believes procuring MGO's GASB 87 consulting services will greatly facilitate the process and ensure this important GASB statement is implemented successfully.

MGO proposed a not-to-exceed amount of \$20,000 for its GASB 87 consultation services (Attachment 3). The actual amount may be lower than this amount based on the actual time spent by the MGO staff. A budget appropriation was approved by the City Council as part of the midyear budget update on February 22, 2022.

Based on the complexity of the GASB 87, it is a significant challenge to implement the new GASB standard and, at the same time, change auditors. Changing auditors results in a substantial workload increase as staff will need to take additional time to provide historical documents and educate the new auditors on the City's processes, financial system records, accounts, and statements.

RECOMMENDATION

Staff recommends:

1. Extend the contract of Macias Gini & O'Connell, LLP (MGO) an additional two years for Fiscal Years 2021-22 and 2022-23.
2. Amend the auditing contract to include consulting services for GASB 87 implementation. The total audit contract amount, including additional services, will be \$167,974 for Fiscal Year 2021-22 and \$147,974 for Fiscal Year 2022-23.

ALTERNATIVES

1. Recommend to the City Council an extension of the contract with MGO for only one year.
2. Recommend to the City Council to initiate the Council Policy B-6 process to issue an RFP and select the external independent auditors.
3. Recommend to the City Council not to amend the audit contract to include GASB 87 consultation services.

JT/HH/1/FIN

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- Attachments:
1. Council Policy B-6, Selection of the External, Independent Auditor
 2. GFOA Best Practices Audit Procurement
 3. MGO's Proposed Fee Schedule

CITY COUNCIL POLICY

SUBJECT: SELECTION OF THE EXTERNAL, INDEPENDENT
AUDITOR

NO.: B-6

PURPOSE:

City Charter Section 1106 requires the City Council to annually employ an independent, external auditor to perform an audit of the records of financial transactions at the end of each fiscal year and to report the conclusions of the audit to the Council and other City officers. An independent audit also confirms the adequacy of controls upon and proper accounting for the use of public funds. In addition to the requirements of the City Charter, the independent auditor renders an opinion on whether or not the City's financial statements present fairly the financial position of the City in accordance with generally accepted accounting principles.

This policy specifies the process for selecting the independent auditor, or audit firm, by the City Council. It also requires the independent auditor to present the results of the annual audit and any findings to the Council Finance Committee (CFC) prior to being formally accepted by the City Council.

POLICY:

1. Selection Process:

- a. The CFC will meet with Finance and Administrative Services Department staff to review and approve the evaluation criteria and other components of the Request for Proposals (RFP) to be used in selecting the recommended independent auditor or audit firm. Staff will then finalize and distribute to qualified audit firms a Request for Proposals (RFP) to conduct the annual financial audit and other special procedure reviews.
- b. Staff will evaluate proposals submitted by interested firms and determine those most highly qualified based upon the evaluation criteria approved by the CFC and the comparative merits of each firm. Reference and background checks will be conducted and the most qualified firms forwarded to the CFC along with the reasons for not recommending other proposers.
- c. The CFC and staff will interview the firms forwarded to the Committee. Following interviews, the CFC will determine the firm to be recommended to the City Council to serve as the independent auditor.

CITY COUNCIL POLICY

SUBJECT: SELECTION OF THE EXTERNAL, INDEPENDENT
AUDITOR

NO.: B-6

2. Presentation of Audit Results:

- a. Annually, at the conclusion of the audit, the independent auditor will present their observations, conclusions, and any findings discovered during the course of the audit to the CFC.
- b. The CFC will make a recommendation to the City Council whether to accept the audit results which will then be presented to the City Council for their consideration and formal acceptance.

Revised: November 10, 2020, Resolution No. 18516

Effective Date: December 2, 2003

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Audit Procurement

Select services that include a broad scope of financial presentations and perform their audits in accordance with the Generally Accepted Government Auditing Standards. Governments should enter into multiyear agreements and undertake a full-scale competitive selection process.

The Government Finance Officers Association (GFOA) has long recommended that state and local governmental entities obtain independent audits of their financial statements, and single audits, if required based on the entity’s use of federal or state grant funds, performed in accordance with the appropriate professional auditing standards. Properly performed audits play a vital role in the public sector by helping to preserve the integrity of the public finance functions, and by maintaining citizens’ confidence in their elected leaders.

GFOA makes the following recommendations regarding the selection of auditing services:

- The scope of the independent audit should encompass not only the fair presentation of the basic financial statements, but also the fair presentation of the financial statements of individual funds and component units. Nevertheless, the selection of the appropriate scope of the independent audit ultimately remains a matter of professional judgment. Accordingly, those responsible for securing independent audits should make their decision concerning the appropriate scope of the audit engagement based upon their particular

government's specific needs and circumstances, consistent with applicable legal requirements.

- Governmental entities should require in their audit contracts that the auditors of their financial statements perform their audits in accordance with the audit standards promulgated in the U.S. Government Accountability Office's Government Auditing Standards. Government Auditing Standards, also known as Generally Accepted Government Auditing Standards (GAGAS), provide a higher level of assurance with regard to internal control than Generally Accepted Audit Standards (GAAS), which are fully incorporated into GAGAS.
- Governmental entities should enter into multiyear agreements of at least five years in duration when obtaining the services of independent auditors. Such multiyear agreements can take a variety of different forms (e.g., a series of single-year contracts), consistent with applicable legal requirements. Such agreements allow for greater continuity and help to minimize the potential for disruption in connection with the independent audit. Multiyear agreements can also help to reduce audit costs by allowing auditors to recover certain "startup" costs over several years, rather than over a single year.
- Governmental entities should undertake a full-scale competitive process for the selection of independent auditors at the end of the term of each audit contract, consistent with applicable legal requirements. While there is some belief that auditor independence is enhanced by a policy requiring that the independent audit firm be replaced at the end of each multiyear agreement, unfortunately, the frequent lack of competition among audit firms fully qualified to perform public-sector audits could make a policy of mandatory audit firm rotation counterproductive. In such cases, it is recommended that a governmental entity actively seek the participation of all qualified firms, including the current auditors, assuming that the past performance of the current auditors has proven satisfactory. Where audit firm rotation does not result from this process, governments may consider requesting that senior engagement staff, such as engagement partners and senior managers, be rotated to provide a fresh perspective. Except in cases where a multiyear agreement has taken the form of a series of single-year contracts, a contractual provision for the automatic renewal of the audit contract (e.g., an automatic second term for the auditor upon satisfactory performance) is inconsistent with this recommendation.
- Professional standards allow independent auditors to perform certain types of nonaudit services for their audit clients. Any significant nonaudit services should always be approved in advance by a governmental entity's audit committee. Furthermore, governmental entities should routinely explore the possibility of alternative service providers before making a decision to engage

their independent auditors to perform significant nonaudit services.

- The audit procurement process should be structured so that the principal factor in the selection of an independent auditor is the auditor's ability to perform a quality audit. Price should not be allowed to serve as the sole criterion for the selection of an independent auditor, rather an independent auditor should have a demonstrated commitment to the state and local government audit practice.

Notes:

Contract Issues for Governmental Audits - The AICPA State and Local Government Expert Panel and GFOA worked together to develop this joint article intended to educate both governments and their auditors about clauses in contracts and engagement letters in the governmental environment that may not meet AICPA professional standards and that may create uncertainty about the auditor's independence.

References:

- *CPA Audit Quality: A Framework for Procuring Audit Services*, U.S. Government Accountability Office, August 1987.
- *Governmental Accounting, Auditing and Financial Reporting (GAAFR)*, Stephen J. Gauthier, GFOA, 2012.

Board approval date: Friday, March 8, 2019

Additional resources

Attachment 3

Audit Cost Proposal By Deliverable					
Task or Report to be Completed	Fiscal Year				
	2019-20	2020-21	2021-22	2022-23	Total
Annual Comprehensive Financial Report (ACFR), including Compilation	\$ 82,390	\$ 84,862	\$ 87,408	\$ 87,408	\$ 342,068
Single Audit Report (up to 2 major programs)	16,429	16,922	17,430	17,430	68,211
Shoreline Regional Park Community Report	7,993	8,233	8,480	8,480	33,186
Compliance Audit - Transportation Development Act	3,265	3,363	3,464	3,464	13,556
Gann Appropriation Limit Calculation	1,123	1,157	1,192	1,192	4,664
Subtotal (All-inclusive Maximum Price)	\$ 111,200	\$ 114,537	\$ 117,974	\$ 117,974	\$ 461,685
Electable Options:					
CAFR Compilation	-	-	-	-	-
Grant Total (All-inclusive Maximum Price)	\$ 111,200	\$ 114,537	\$ 117,974	\$ 117,974	\$ 461,685

Audit Staff Hourly Billing Rates by Classification					
Classification	Hours	Billing Rates for Fiscal Year:			
		2019-20	2020-21	2021-22	2022-23
Engagement Partner	44	\$ 333	\$ 343	\$ 353	\$ 364
Professional Standards Reviewer	10	\$ 333	\$ 343	\$ 353	\$ 364
Engagement Director	87	\$ 279	\$ 287	\$ 296	\$ 305
IT Consulting Manager	20	\$ 203	\$ 209	\$ 215	\$ 221
Senior Assurance Associates	182	\$ 136	\$ 140	\$ 144	\$ 148
Staff and Experience Assurance Associates	362	\$ 110	\$ 113	\$ 116	\$ 119
Administrative Assistants	5	\$ 88	\$ 91	\$ 94	\$ 97
Total Hours (including CAFR Compilation)	710				

GASB 87 Implementation - Staff Hourly Billing Rates and Estimated Fee by Classification			
Classification	Hours	Hourly Billing Rates	Estimated Fee
Engagement Partner	30	\$ 360	\$ 10,800
Engagement Manager	26	\$ 219	\$ 5,694
Senior Associates	15	\$ 147	\$ 2,205
Staff and Experience Assurance Associates	11	\$ 119	\$ 1,301
Total	82		20,000