

RESOLUTION NUMBER R- 300139

ADOPTED ON FEB 14 2005

WHEREAS, in February of 2004, the Securities and Exchange Commission [SEC] and the U. S. Attorney's Office, informed the City that they were undertaking investigations into certain financial disclosure practices by the City, which investigations are on-going; and

WHEREAS, early in 2004 the City retained the services of the law firm Vinson & Elkins LLP [V&E] to conduct an investigation and provide a report on disclosure practices of the City from 1996 to the present, and V&E completed its investigation and issued its report in September of 2004; and

WHEREAS, in the spring of 2004 the City retained the services of the accounting firm KPMG to perform the outside audit of the City's FY 2003 financial statements; and

WHEREAS, in furtherance of the FY 2003 audit, the City has undertaken two separate further investigations; one by V&E and one by the City Attorney; and

WHEREAS, the City Attorney issued an interim report on January 14, 2005, and it is expected that other reports will be issued following the completion of both investigations; and

WHEREAS, it is necessary and appropriate for the City to designate the person or body to receive the investigative reports, review and evaluate them, and make appropriate recommendations to the City Council; and

WHEREAS, it is also necessary and appropriate for the City to provide for a review of the City's internal controls pertaining to proper reporting and disclosure pursuant to applicable disclosure laws; and

WHEREAS, it recently came to the attention of the City that Mr. Lynn E. Turner is available for this important assignment; and

WHEREAS, Mr. Turner, a copy of who's resume is attached as Exhibit A, is currently a senior advisor to Kroll Zolof Cooper [Kroll, Inc.], a company specializing in corporate advisory and restructuring issues, and forensic accounting and litigation; and is the managing director of research at Glass Lewis & Co., a company that provides objective evaluation of corporate integrity and financial transparency for public companies; and

WHEREAS, Mr. Turner is also the former Chief Accountant for the SEC, serving in that position from 1998 to 2001, and in that capacity he was the principal advisor to the SEC Chairman and the full Commission on financial reporting and disclosure by public companies; and

WHEREAS, the City Council proposes to retain Kroll, Inc. and Mr. Turner for the purposes set forth above, and on the terms and conditions set forth in the proposed agreement attached hereto as Exhibit B; NOW THEREFORE,

BE IT RESOLVED, by the Council of the City of San Diego, that the Mayor, City Manager, and City Attorney are hereby authorized and directed to execute the agreement with Kroll, Inc., attached hereto as Exhibit B. When executed the agreement will be on file in the Office of the City Clerk as document No. RR- 300139.

BE IT FURTHER RESOLVED, that the initial amount of \$250,000 from the Public Liability Fund No. 81140 is hereby authorized for the above entitled purpose on the condition that the City Auditor and Comptroller first certify that the funds are in the treasury and available for these purposes, although additional sums may be necessary to be authorized from time to time by the City Council.

BE IT FURTHER RESOLVED, that the City Auditor and Comptroller is hereby authorized and directed, upon consultation with the City Attorney, to allocate the above described expenditure between the General Fund, the Sewer Fund (No. 41506) and the Water Fund (No. 41500) based upon an appropriate and lawful allocation method.

APPROVED: MICHAEL AGUIRRE, City Attorney

By Anita M. Noone for Leslie J. Girard
Leslie J. Girard
Assistant City Attorney

LJG:km
2/07/05
2/11/05 COR. COPY
Or.Dept:City Manager
R-2005-820

Lynn E. Turner

Mr. Turner has the unique perspective of having been the Chief Accountant of the Securities and Exchange Commission, a professor of accounting, a corporate board member, a partner in one of the major international accounting firms, the managing director of a research firm and a chief financial officer and executive in industry.

Mr. Turner served as the Chief Accountant of the Securities and Exchange Commission (SEC) from his appointment by the SEC Chairman in July 1998 to August 2001. As Chief Accountant, Mr. Turner was the principal advisor to the SEC Chairman and Commission on financial reporting and disclosure by public companies in the U.S. capital markets as well as the related corporate governance matters. These issues included the oversight and development of U.S. accounting, disclosure and auditing standards, the development and coordination of international accounting standards, as well as matters affecting audit committees of public companies. In this capacity, Mr. Turner worked regularly with Congress, various federal and state government agencies, international regulators, representatives of industry, and the accounting profession.

Mr. Turner is currently the managing director of research at Glass Lewis & Co. Glass Lewis is an analytical proxy and financial research firm that uses proprietary research and extensive analysis to objectively evaluate the corporate integrity and financial transparency of public companies. Glass Lewis advises investors who manage over \$10 trillion in assets. Mr. Turner also serves as a senior advisor to Kroll Zolfo Cooper. Kroll Zolfo Cooper specializes in Corporate Advisory and Restructuring and Forensic and Litigation. Mr. Turner is also a member of the Board of Directors of Sun Microsystems and a member of the Standards Advisory Group of the Public Companies Accounting Oversight Board.

Lynn Turner joined the faculty of Colorado State University where he was a professor of accounting and the Director of The Center for Quality Financial Reporting in the College of Business from 2001 to 2004.

From June of 1996 to June of 1998, Mr. Turner was the Chief Financial Officer and Vice President of Symbios, Inc., an international semiconductor and storage manufacturer. Mr. Turner was responsible for the company's financial and management reporting, risk management and budgeting processes. He also worked closely with the Chief Executive Officer and the Board of Directors in the development and implementation of the company's business strategy.

Before joining Symbios, Mr. Turner was a partner with Coopers & Lybrand, (now PricewaterhouseCoopers). Mr. Turner served as one of the firm's national SEC review partners. He was the National Practice Leader responsible for the national C&L High Technology Audit Practice. Mr. Turner joined C&L in July 1976 and remained with the firm until 1996 with the exception of a two-year appointment to a Fellowship with the SEC from 1989 to 1991.

Mr. Turner has served as an expert witness for and testified before Congress on several occasions. He was actively involved in the legislative process leading up to passage of the Sarbanes-Oxley Act. He has appeared on National Public Radio and all the major television networks including NBC, ABC, CBS, CNN, CNBC, CNNfn, Bloomberg TV and MSNBC. Mr. Turner has also served as one of six members of the Panel of Experts for the International Monetary Fund (IMF). This panel of international experts was responsible for making recommendations to the IMF with respect to improving controls over its international lending practices.

Mr. Turner has received honorary doctorates in Business Administration from Central Michigan University and Grand Valley State University. He has also twice been a recipient of the SEC Chairman's Award for Excellence. He has been the Colorado State University College of Business Alumni of the Year, and has received from Beta Alpha Psi, the National Accounting Honorary Society, the national award for Business Information (Accountant) Professional of the Year.

EXHIBIT A

Q-300139

Mr. Turner is a member of the Colorado Society of Certified Public Accountants (CSCPA), the American Institute of Certified Public Accountants, and the Financial Executives International. Mr. Turner holds an MA in Accounting from the University of Nebraska and a BA in Business Administration, with a concentration in Accounting, from Colorado State University.

EXHIBIT A

R 300139

**PRIVILEGED AND CONFIDENTIAL
ATTORNEY WORK-PRODUCT**

February 10, 2005

Mayor of San Diego
City Council of San Diego
212 C Street
San Diego, CA 92101

Re: Independent Services for the City of San Diego

Dear Mr. Ewell:

This letter confirms our understanding of the scope and terms of the engagement of Kroll Inc. ("Kroll") by the San Diego City Council ("the Council"). It is understood that although we are being hired by the Council, we will perform our services with complete independence from the Council, the City of San Diego ("the City"), the City's departments, the City's agencies including the San Diego Employees' Retirement System ("SDCERS"), the City's elected officials or any other party that is involved with this matter.

Background

On January 27th, 2004, the City of San Diego California made a voluntary disclosure filing with the four Nationally Recognized Municipal Securities Information Repositories recognized by the Securities and Exchange Commission (SEC). The first provided a description of the unfunded accrued actuarial liability of the San Diego City Employees' Retirement System together with projections anticipating the growth in the liability, an estimate of the accrued liability for post retirement health care benefits conferred on the City's retired workers, as well as a description of the mechanics by which the City funded the system. The second described numerous errors discovered in the footnotes of the City's audited annual financial statements. Subsequently, rating agencies have downgraded the rating of the City's debt and investigations have been commenced by the SEC and U.S. Attorney.

We understand the City has engaged KPMG to perform an independent audit of its 2003 annual financial statements. We also understand Vinson & Elkins (V&E) issued an investigative report dated September 16, 2004 entitled "The City of San Diego,

California's Disclosures of Obligation to Fund the San Diego City Employees' Retirement System and Related Disclosure practices 1996-2004 with Recommended Procedures and Changes to the Municipal Code." Subsequent to the issuance of this report we understand that KPMG has requested additional competent evidential matter it deems necessary to complete its audit in accordance with applicable accounting, auditing and professional standards and that further investigation be made into certain matters. We also understand V&E has been engaged to perform this additional work. It is our understanding KPMG has requested the results of the V&E investigations, as well as the results of an ongoing investigation by the City Attorney, be received, reviewed and evaluated by an independent third party,

Scope of Project.

The City has requested that Kroll (1) receive, review and evaluate the findings of the investigations by V&E and the City Attorney. The City has also requested Kroll provide consulting assistance in assessing internal control deficiencies affecting matters discussed in the investigation reports.

The scope of this engagement will be in two phases. The first phase of the engagement will be for Kroll to serve as an Independent Investigator for matters relating to (1) the unfunded liability of the SDCERS and (2) errors discovered in the footnotes of the City's audited annual financial statements. We expect this phase of the project will include:

- Working with KPMG to understand their concerns and attempt to reach a satisfactory work program that will assist them in obtaining the necessary evidence and documentation required by applicable accounting, auditing and professional standards.
- Receive, review and evaluate the reports of investigations of this matter we currently understand will be issued by V&E and the City Attorney. We understand that the Council will direct V&E and the City Attorney to provide us access to whatever information they have related to their investigations. This shall include (a) reading and reviewing these reports, (b) recommending changes in scope of the work performed that will meet the needs of KPMG and where we deem necessary (c) performing additional procedures we consider necessary to reach conclusions or obtain evidential matter that is required by KPMG. In doing so, we will require unconditional access to all information gathered, by the personnel and documents of the City, SDCERS, V&E, the City Attorney and any other parties involved with this matter. We also may direct V&E to perform additional investigative procedures we deem necessary. Should we deem it necessary we may also retain legal counsel. We will attempt not to duplicate work that has already been performed, unless we believe that additional work needs to be done to complete our investigation and provide KPMG with evidence they require in order to issue an opinion on the financial statements. A lack of access to the

information or personnel we require may impact our ability to complete our investigation and ability to complete this project.

- We will report our findings to the Council.

Our work will be based on the investigation reports and any additional procedures we deem necessary. However, we are not responsible for the work performed by V&E or the City Attorney. We are also not responsible for the issuance of audited statements by KPMG or any other external accounting firm the city has hired to audit its' financial statements.

You have also requested a second phase to our engagement, which we will not be prepared to commence until the first phase is complete. In the second phase, we may be engaged to consult with personnel of the City to establish internal controls that if implemented and operated properly by the City could provide reasonable assurance that the transactions identified in the reports in phase one are properly reported and disclosed in the financial statements of the City. We could coordinate our work with the City Auditor and Comptroller, the head of the internal audit department and the City's outside independent auditors as to the scope and nature of the internal controls that the City would need to assess, document, implement and test.

The City's internal control over financial reporting includes those policies and procedures that pertain to its ability to initiate, record, process and report financial data consistent with the assertions embodied in either its annual or interim financial statements and accompanying disclosures. Management of the City is responsible for evaluating the effectiveness of the Company's internal control over financial reporting using suitable control criteria and supporting its assessment with sufficient evidence including documentations. Management will also be responsible for presenting a written assessment of the effectiveness of the City's internal controls.

The work performed in connection with phase one and two of this project will be completed in accordance with the applicable professional standards, for consultants, set forth by the American Institute of Certified Public Accountants.

The Council agrees that any written reports, schedules, other materials, or documents prepared or provided by Kroll are to be used only for this matter and will not be disclosed, published, or used by the Council or any representatives of the City for any other purpose without Kroll's prior written permission.

Kroll agrees that all working papers and other documents prepared or received by us pursuant to this engagement will be maintained by us as confidential material and we agree not to disclose our work or work product hereunder to third parties without the Council's consent, except as may be required by law, regulation, or judicial or administrative process, or in connection with litigation arising hereunder. We also agree to abide by any court orders provided to us in writing and signed by us regarding

confidentiality. We will, at your request, transmit information to you by facsimile, e-mail, or over the Internet. If any confidentiality breaches occur because of data transmission, you agree that this will not constitute a breach of any obligation of confidentiality. If you wish to limit such transmission to information that is not highly confidential, or seek more secure means of communication for highly confidential information, you will need to inform us. If access to any of the materials in our possession relating to this engagement is sought by a third party, we will promptly notify you of such action, tender to you our defense responding to such request and cooperate with you concerning our response thereto. In the event that we are subpoenaed as the result of any work performed for you in connection with this engagement, the City will compensate us for our time involved in responding to such subpoenas.

Our fees are based on the actual hours plus expenses incurred and are not contingent on the completion or outcome of the investigation. We will bill you at the rates for the professionals that work on this matter. Our rates currently range from \$125 to \$750 per hour. Our engagement team will be lead by Mr. Lynn Turner and Mr. Troy Dahlberg and under the oversight of Arthur Levitt.

Their respective rates are \$750, \$450 and \$900 per hour, respectively. Our hourly rates are periodically revised. You will pay us for expenses that we incur for this matter, including but not limited to travel costs, lodging, outside research, copy costs, telephone and messengers. We shall be paid for our time and our expenses, including any legal expenses that we may incur, associated with any subsequent testimony or response to any process that is required of us as a result of our services related to this engagement.

We will be pleased to start work upon receiving a \$75,000 retainer that will be applied to the last invoice. We understand that the Council will initially approve \$250,000 for our engagement, but will consider approving additional funds on an as needed basis in order to complete the engagement. We bill at a summary level, generally on a monthly basis, based on the fees and expenses incurred. Payment is due upon invoicing without regard to the current status of this matter, and a late payment fee of 1 ½ percent per month may be charged for any indebtedness. We require full payment of any indebtedness prior to the issuance of any report. We may stop work at any time in the event of any delinquency of indebtedness. We may resign this engagement at our sole discretion at any time.

The scope of this engagement does not constitute a rendering by Kroll or its employees of any legal advice, and because our engagement is limited in nature and scope it cannot be relied upon to discover all documents and other information or provide all analyses which may have importance to this matter. This engagement does not anticipate the compilation, review, or audit of financial records or financial statements. No representative of the City will hold us responsible for any loss or liability, which may result from the nondiscovery of any matters which may otherwise have an influence on this matter.

We have undertaken a limited inquiry of Kroll's records to determine if there are any conflicts with this engagement, and currently we are aware not found any. However, the very nature, diversity, magnitude, and volume of Kroll and its past and present clients and professional relationships does not allow us to be certain that each and every possible relationship or potential conflict has come to our attention. In the event that additional relationships or potential conflicts come to our attention, we will promptly notify you. The Counsel agrees that it will inform Kroll of additional parties to the matter. Kroll is a separately operated wholly owned company of the Marsh & McLennan Companies.

The Council and City agree that the City or any other party or affiliate acting on their behalf will not hold Kroll its affiliates, its representatives or its employees legally responsible for any loss or liability to the City or any of its representative or personnel for any claims, liabilities, or expenses relating to this engagement. Additionally, the City agrees to indemnify and hold harmless, Kroll, its affiliates, its representatives and its employees from any and all claims, liabilities, or expenses arise as a result of Kroll performing services pursuant to this Agreement. This provision and other provisions in this Agreement will survive the completion or termination of this engagement.

If any portion of this Agreement is held to be void, or otherwise unenforceable, in whole or part, the remaining portions of this Agreement shall remain in effect.

Need to note which jurisdiction this contract is to be interpreted under.

We appreciate the opportunity to assist you on this matter. If this Agreement meets with your approval and your client's approval, please sign below. Please return the signed letter to Troy Dahlberg at the above address, retaining a copy for yourself and your client.

Very truly yours,

Mr. Troy Dahlberg
Managing Director
Kroll Inc.

Acknowledged by: _____
Mayor

Date: _____

Acknowledged by: _____
City Manager

Date: _____

Acknowledged by: _____
City Attorney

Date: _____