

April 11, 2011

Kevin Faulconer
Councilmember, Second District Chairperson, Audit Committee
City of San Diego
202 C Street
San Diego, CA 92101

Dear Councilmember Faulconer:

The Audit Committee has requested a written proposal regarding additional audit procedures required to complete the City of San Diego's (City's) 2010 financial statement audit due to delays in the audit process and a re-assessment of the risk related to the SAP implementation issues and reducing any reliance on internal controls.

In our proposal dated March 27, 2009, we proposed an all inclusive fee of \$880,252 for the 2010 financial statement audit, which was a \$105,517 reduction from the 2009 proposed fee of \$985,769. The fee reduction anticipated that beginning with the 2010 fiscal year we will begin a transition to a more efficient controls based audit. Following the rollout of each application within the ERP and the City's related risk assessment of controls over financial reporting we will incorporate control testing into our audit approach. In addition our proposed fees and hours are based on the assumption that no significant changes occur in the professional standards and that the accounting records are complete and accurate to present the financial statements in accordance with accounting principles generally accepted in the United States of America.

During fiscal year 2010, the City implemented the payroll module of their new ERP system, SAP. Soon after the City's fiscal yearend June 30, 2010, the City identified various system generated allocation issues resulting in errors in payroll expense allocations to department and funds. In considering the SAP implementation issues and the delay in the audit process we are in process of evaluating the effect of these issues on the audit process and the additional resource needs to complete procedures not previously anticipated in our fee proposal for 2010.

To date, we have identified additional procedures related to the IT review of SAP involving further risk assessment and testing of the causes and corrections of the payroll expense allocation errors that we consider to be beyond the initial scope of our audit. These procedures will be performed by our IT Consulting Director. Our estimate of these additional procedures is 220 hours at a cost of \$51,260.

We are still in process of evaluating the impact of the payroll allocation issues on our general audit approach outside of our IT review and expect additional procedures related to risk assessment, subsequent events review, expense analytical reviews. We will complete this evaluation report to the City Auditor and Independent Budget Analysts Office by April 18, 2011.

Furthermore, our fee proposal for fiscal year 2010 for the Single Audit was \$93,192. This fee anticipated a review of approximately 8 major programs. The 2010 risk assessment under OMB Circular A-133 identified 13 major programs that were required to be tested. The significant increase in major programs selected was primarily due to the requirements of the American Recovery and Reinvestment Act of 2009 (ARRA). The ARRA requirements were not contemplated as part of our proposal are required a significant increase in audit effort for 2010. We would appreciate your consideration of our request of a fee adjustment of \$30,000 for the work performed related to the additional major programs required to be tested.

We would be happy to answer any questions or discuss any of these items further at your request.

Very truly yours,

A handwritten signature in cursive script that reads "Linda Hurley".

Linda Hurley, Engagement Partner
Macias Gini & O'Connell LLP

Cc: Mr. Eduardo Luna, City Auditor
Mr. Jeff Kavar, Fiscal and Policy Analyst, IBA