



## Legislation Details (With Text)

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<b>Title:</b>	PRESENTATION FROM THE PORT AUDITOR ON BEST PRACTICES RELATED TO EXTERNAL AUDIT AND PUBLIC AUDIT OVERSIGHT COMMITTEE MEMBERS WITH DIRECTION TO STAFF				
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Date	Ver.	Action By	Action	Result
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**DATE:** June 15, 2021

**SUBJECT:**

**PRESENTATION FROM THE PORT AUDITOR ON BEST PRACTICES RELATED TO EXTERNAL AUDIT AND PUBLIC AUDIT OVERSIGHT COMMITTEE MEMBERS WITH DIRECTION TO STAFF**

### **EXECUTIVE SUMMARY:**

During the February 2021 Board of Port Commissioners (BPC) meeting, a request was made for the Port Auditor to give a presentation outlining the best practices for selecting external audit services through a competitive bid process and if firm rotation is required.

During the April 2021 BPC meeting, the Port Auditor was asked to give a presentation regarding best practices for term limits of public Audit Oversight Committee (AOC) members.

Based on a review of best practices related to external audit services, the Port Auditor recommends the Board to direct staff to conduct a request for proposal (RFP) for external audit services at the end of the contract period including any exercised option years. The requirement of a mandatory firm rotation (MFR) has not been widely recommended and leading accounting governing bodies have laid out alternatives to MFR such as partner rotation, and therefore, the Port Auditor does not recommend MFR.

Additionally, based on a review of best practices, the Port Auditor recommends the Board direct staff to return to the Board with a proposed amendment to BPC Policy Number 776, Audit Oversight Committee, to include language about term limits for public AOC members.

### **RECOMMENDATION:**

Receive presentation from the Port Auditor on best practices related to external audit and public Audit Oversight Committee member and provide direction to staff.

### **FISCAL IMPACT:**

This agenda has no fiscal impact in this fiscal year.

### **COMPASS STRATEGIC GOALS:**

This agenda item supports the following Strategic Goal(s).

- A Port that the public understands and trusts.
- A financially sustainable Port that drives job creation and regional economic vitality.

### **DISCUSSION:**

In March 2021, the Port Auditor submitted to the Board, a one-year extension of the current external audit services contract with Macias, Gini & O'Connell, LLP (MGO). The Board made a request to have more information and during discussion, the Board asked the Port Auditor to come back and provide best practices for government agencies on completing an RFP for external audit services and rotating external audit firms.

The Port of San Diego uses external audit services to complete the basic financial statement and single audits annually. The Port completed a request for proposal (RFP) for external audit services in 2013 and selected the audit firm MGO. The original agreement was for 5 years (three years with two one-year options). Since then, the agreement has been extended twice for an additional 4 years. Total years with MGO will be 9 years with completion of the FY21 audit. An RFP for external auditors will commence this summer for the FY22 audit. BPC Policy No. 776, Port Audit Oversight Committee, does not have a set RFP or rotation mandate.

After reviewing the Association of International Certified Professional Accountants and the Government Finance Officers Association's best practices, it is recommended that governmental entities should allow for a full-scale competitive process for the selection of auditors at the end of the audit contract. There should be a determined audit engagement term.

MFR was reviewed and has advantages that include increased independence and objectivity. Disadvantages include increased costs and a reduction in the quality of audits performed. While the European Union is moving to a system that includes MFR every ten years, with an additional ten years added if an RFP is performed that is won by the same firm, the Public Company Accounting Oversight Board (PCAOB) does not recommend MFR within the United States. However, there is a recommendation for partner rotation, and as of 2017 the PCAOB requires disclosures of the amount of years an external auditor has provided audit services.

The Institute of Internal Auditors only recommends MFR where circumstances such as significant frauds in the companies audited were found. Additionally, the state of California requires partner rotation every six years, which has occurred with the current contract with MGO.

The Port Auditor conducted a benchmark of member cities, regional agencies, and greater California agencies which determined that the standard frequency of competition for RFP was every three to

five years depending on the end of the contract or if option years were executed.

Therefore, the Port Auditor recommends that an RFP is conducted at the end of the contract including any exercised option years. The requirement of a MFR is currently not widely recommended but rather leading accounting governing bodies have recommended alternatives to MFR such as partner rotation, and therefore, the Port Auditor does not recommend MFR.

The Port Auditor was also asked during the April 2021 Board meeting to present the best practices related to the term public AOC members serve. During the April 2021 meeting, the Port Auditor submitted to the Board for approval a three-year re-appointment of one of the three public AOC members. The Board requested that the Port Auditor give a presentation at a later date discussing best practices for term limits for public committee members.

The AOC consists of five members: two Port of San Diego Port Commissioners and three public members. The AOC is governed by BPC Policy Number 776 which allowed public members to serve a staggered three-year term to ensure continuity. It does not, however, establish term limits for public members.

The Port Auditor reviewed best practices outlined by the IIA and the Government Finance Officers Association. Both organizations recommend that committee members range between three and five members which the majority being independent from the organization. All members should have sufficient knowledge of audit, finance, IT, the law, risk and controls. Both organizations agree that the terms should last three to four years and be staggered. Term limits, however, should be determined by the organization, allowing for new perspectives.

The Port Auditor benchmarked multiple agencies including the City of San Diego, SDCERS, the Port of Los Angeles and the Port of Seattle. Committee sizes ranged from two to eight members with term lengths between three and five years. All but the Port of Los Angeles had term limits which ranged between three and eight years.

The Port Auditor recommends the Board direct staff to return to the Board with a proposed amendment to BPC Policy Number 776 which sets term limits for public AOC members. It is recommended that public members serve a maximum of two, 3-year terms. Public members can reapply after a three-year break at the end of the second, 3-year term.

### **General Counsel's Comments:**

The Office of the General Counsel has reviewed and approved this agenda, as presented, as to form and legality.

### **Environmental Review:**

The proposed presentation and Board direction, including without limitation, a presentation from the Port Auditor and direction to staff, do not constitute a "project" under the definition set forth in California Environmental Quality Act (CEQA) Guidelines Section 15378 because they would not have the potential to result in a direct or indirect physical change in the environment and are, therefore, not subject to CEQA. No further action under CEQA is required.

The proposed presentation and Board direction comply with Section 35 of the Port Act, which allows the Board to do all acts necessary and convenient for the exercise of its powers. The Port Act was enacted by the California Legislature and is consistent with the Public Trust Doctrine. Consequently, the proposed presentation and Board direction are consistent with the Public Trust Doctrine.

The proposed presentation and Board direction do not allow for “development,” as defined in Section 30106 of the California Coastal Act, or “new development,” pursuant to Section 1.a. of the District’s Coastal Development Permit Regulations. Therefore, issuance of a Coastal Development Permit or exclusion is not required.

**Diversity, Equity, and Inclusion Program:**

Not applicable.

**PREPARED BY:**

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Attachment(s):  
Attachment A: Best Practices Presentation