
OFFICE OF THE INDEPENDENT BUDGET ANALYST REPORT

Date Issued: July 15, 2009

IBA Report Number: 09-64

Audit Committee and City Council Docket Date: July 20, 2009

Item Number: AC # 2 & CC # 202

Second Annual Report of Independent Consultant to the City of San Diego

OVERVIEW

Stanley Keller, the City's Independent Consultant issued his Second Annual Report to the City on April 24, 2009 in accordance the Cease-And-Desist Order (Order) of the United States Securities and Exchange Commission (SEC) dated November 14, 2006. Mr. Keller will be presenting his Second Annual Report to the Audit Committee and the City Council on July 20, 2009. This report provides background with respect to the SEC Order, reports issued by the Independent Consultant to date and responses sent to the SEC following the receipt of reports from the Independent Consultant.

FISCAL/POLICY DISCUSSION

SEC Cease-And-Desist Order

The SEC entered an order sanctioning the City for committing securities fraud by failing to disclose to the investing public important information about its pension and retire health care obligations in the sale of municipal bonds in 2002 and 2003. To settle the action, the City agreed to cease and desist from future securities fraud violations and to retain an independent consultant for three years to foster compliance with its disclosure obligations under the federal securities laws. The City consented to the issuance of the Order without admitting or denying the findings of the Order.

Requirements and Reports of the Independent Consultant

The Order required the City to hire an Independent Consultant within 60 days. The City entered into an Agreement with the firm of Edwards Angell Palmer & Dodge LLP for independent consultant services on January 16, 2007. The Agreement designates Stanley Keller as having lead and principal responsibility for Independent Consultant services. The Agreement will terminate no later than March 1, 2010, unless both parties agree to an extension.

The Order and the Agreement require the Independent Consultant to provide an Initial Report (within 120 days after the date of engagement) and three Annual Reports to the City. To date, the Independent Consultant has provided the following reports to the City in compliance with the Order:

June 7, 2007:	Initial Report of Independent Consultant
March 25, 2008:	First Annual Report of Independent Consultant
April 24, 2009:	Second Annual Report of Independent Consultant

City Correspondence to the SEC in Response to Annual Reports

In his First Annual Report, the Independent Consultant provided the City with 36 recommendations with respect to specific areas that related to the adequacy of the City's disclosures, financial reporting and internal control structure. On May 15, 2008, the Mayor sent correspondence to the SEC responding to each of the 36 recommendations commenting on actions that had been taken, actions that were in progress, or plans for future action with respect to each recommendation. On May 21, 2009, Council President Peters sent a separate letter to the SEC, supplementing the Mayor's correspondence, which explained specific actions taken by the City Council in relation to 13 of the 36 recommendations.

Following receipt of the Second Annual Report of Independent Consultant, the City could again elect to have the Mayor and the City Council respond with separate letters to the SEC. Alternatively, a consolidated response could be developed for City Council consideration. The CFO is in the process of developing a draft response that will be ready for City Council review in September 2009. The IBA will be drafting responses to the recommendations from the Report that pertain specifically to the City Council.

CONCLUSION

The Independent Consultant will be presenting his Second Annual Report to the Audit Committee and the City Council on July 20, 2009. Several of the recommendations of the Independent Consultant have been implemented and others are in the process of being addressed. In order to convey this information and the City's plan to be responsive to all of the Independent Consultant's recommendations, a detailed response should be developed for the SEC.

Depending on the City Council's direction, the IBA stands ready to develop either a separate response to the SEC for the City Council or work with the CFO to develop an integrated

response for Council review. We anticipate that a draft SEC response letter will be docketed for Council consideration in September 2009.

[SIGNED]

Jeff Kavar
Fiscal & Policy Analyst

[SIGNED]

APPROVED: Andrea Tevlin
Independent Budget Analyst