
OFFICE OF THE INDEPENDENT BUDGET ANALYST REPORT

Date Issued: December 31, 2008

IBA Report Number: 08-125

City Council Docket Date: January 6, 2009

Item Number: # 330

Continued Retention of Hawkins Delafield & Wood LLP as City Disclosure Counsel

OVERVIEW

On February 11, 2004, the City Council commissioned Vinson & Elkins LLP to review the City's disclosure practices from January 1996 through February 2004 and investigate whether the City failed to meet its disclosure obligations related to the funding of SDCERS. In their report to the City dated September 16, 2004, Vinson and Elkins recommended that the City retain a law firm to serve as the City's general disclosure counsel. In March 2004, the City selected the law firm of Hawkins, Delafield & Wood LLP (Hawkins) to serve as the City's general disclosure counsel.

The City Council is being asked to adopt an ordinance authorizing an additional \$180,000 to continue to retain Hawkins as the City's general disclosure counsel. This would be the fourth amendment to the original agreement with Hawkins that was executed on May 11, 2004. The IBA issued Report # 07-109 regarding the proposed third amendment to the agreement with Hawkins in November 2007. This report briefly reviews the history of the Hawkins contract, comments on the requested amendment and follows up on our previous recommendations.

FISCAL/POLICY DISCUSSION

In their capacity as the City's general disclosure counsel, Hawkins provides:

- Expert securities law advice to City staff regarding the requirements of securities laws for City financings (private placements and public offerings), continuing disclosure agreements and other disclosure matters,

- Training for elected officials and staff with regard to the requirements of federal securities laws, and
- Guidance and insights as a non-voting member of the Disclosure Practices Working Group (DPWG) as required by the Municipal Code (Chapter 2, Article 2, Division 41).

History of the Agreement with Hawkins

The City initiated an agreement (Agreement) with Hawkins “for legal services related to general disclosure and continuing disclosure matters” on May 11, 2004. The initial agreement was for an amount not to exceed \$100,000 and contained a broad 14-item scope of services section focusing on City disclosure matters. Citing a need for additional general disclosure counsel services from Hawkins, the City has subsequently amended the Agreement three times. The agreement history is provided below:

<u>Agreement</u>	<u>Date Executed</u>	<u>Amount</u>
Original	May 11, 2004	\$100,000
1 st Amendment	December 2, 2004	\$150,000
2 nd Amendment	March 8, 2005	\$500,000
3 rd Amendment	November 13, 2007	<u>\$500,000</u>
		\$1,250,000

Requested \$180,000 Extension of the Agreement

Based on workload expectations, the City Attorney’s Office expects that the additional \$180,000 requested for a fourth amendment to the Agreement will cover general disclosure counsel services for most of calendar 2009. In calendar 2008, invoices from Hawkins averaged approximately \$27,000 a month. If this trend were to continue, the IBA estimates an additional \$180,000 would roughly last until the end of FY 2009 which would require additional funding to be considered for FY 2010.

As noted in the staff report, the City’s financial departments recommend apportioning the additional \$180,000 cost based on a Full Time Equivalent (FTE) staffing methodology. This results in the General Fund bearing approximately 75% of the expense with the remaining 25% apportioned to the City’s various Enterprise Funds. The Financial Management Department utilized staffing levels in the FY 2009 budget to reevaluate FTE cost apportionment percentages and determine the 75%/25% split.

The Mayor proposed and the City Council adopted a Cost Allocation Policy on March 20, 2006. The Policy calls for a review of cost allocation parameters at least on a bi-annual basis, and any recommended changes to the policy shall be submitted to the City Council for approval. As it has been more than two years since adoption, the IBA recommends that the Policy be brought forward to the City Council for review and discussion.

In the FY 2009 budget, the IBA understands that some funding was budgeted for disclosure counsel in the General Fund (as a line item within Special Consulting Services within Citywide Program Expenditures); however, this money was subsequently redirected to cover other unanticipated consulting services. As it is uncertain what services were provided with the redirected funds, the City Council may wish to clarify how these funds were used.

As shown in the proposed cost apportionment that is attached to the staff report, approximately 75% of the \$180,000 (\$135,000) has been allocated to Citywide Program Expenditures within the General Fund. Table 1 on page 4 of the Mayor's FY 2009 Budget Amendment Report (#08-166) therefore has a corresponding line item of approximately \$130,000 for disclosure counsel services. This \$130,000 was included in the current year budget shortfall of \$43 million which was addressed with the November budget actions. The Financial Management department indicates that the expense to be apportioned to the City's Enterprise Funds (25% or approximately \$45,000) was not budgeted and will need to be absorbed within current year budgets.

Recommendations Made in IBA Report # 07-109

The IBA reviewed the request for a third amendment to the Agreement in November 2007. At that time, the IBA and the City Council were concerned that the Agreement had expired approximately two years earlier and that expenses had been authorized (invoices received, but not submitted for payment) well in excess of appropriated funds. The IBA recommended that "general disclosure counsel services should be thoughtfully contemplated on a regular basis and accounted for in the annual budget process so as not to unnecessarily deplete appropriated reserves."

The current Agreement is valid and approximately \$3,000 remains from the \$500,000 that was allocated in November 2007. It should be noted that the City Attorney's Office expects to receive an invoice in January 2009 from Hawkins for the month of December 2008 that will likely be in excess of the \$3,000 in remaining funds. Although approval is being sought just before existing funding runs out, the IBA continues to recommend that annual disclosure counsel expenses be better anticipated and budgeted for during the annual budget process.

As the City's general disclosure counsel work had not been competitively bid for a number of years, the IBA further recommended that "the City competitively bid disclosure counsel services well before this new Agreement expires." The Office of the City Attorney subsequently issued an Request for Qualifications (RFQ) for Bond Counsel and General Disclosure Counsel on May 16, 2008. In response to the RFQ, 10 of 13 proposals received expressed interest in providing general disclosure counsel services. Based on the City Attorney's Office evaluation of the proposals received, John McNally of Hawkins was selected as the best qualified individual/firm to provide general disclosure counsel services to the City.

CONCLUSION

The IBA continues to believe that the City needs continued general disclosure counsel services. Based on the competitive selection process that was undertaken by the City Attorney's Office, we recommend that the ordinance authorizing the continued retention of Hawkins be approved. The General Fund portion of the additional \$180,000 expense (approximately \$130,000) was included in the projected current year budget shortfall of \$43 million which was addressed with the November 2008 budget actions.

We believe that the processes for anticipating and budgeting for general disclosure counsel expenditures can and should be improved so as not to 1) receive services that exceed appropriated funds and 2) result in the need for mid-year budget adjustments which can exacerbate mid-year budget deficits. The IBA commends the Office of the City Attorney for issuing a RFQ for general disclosure counsel services in May 2008, well before funding for the current Agreement expired.

[SIGNED]

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[SIGNED]

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Attachment: IBA Report # 07-109