



# CITY AND COUNTY OF SAN FRANCISCO

## FY 2016-17

## Audit Service Plan

PRESENTED BY:  
**MACIAS GINI & O'CONNELL LLP**

**MAY 17, 2017**



Certified  
Public  
Accountants



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# Transmittal Letter

May 17, 2017

On behalf of Macias Gini & O'Connell LLP (MGO), we are pleased to present our 2017 Audit Service Plan (Plan) for the City and County of San Francisco (City) for the year ended June 30, 2017. In preparing our Plan we have drawn on our experience in serving the City in prior years and numerous governmental entities within California. This Plan presents our engagement service teams; timeline for deliverables; highlights our audit approach, scope and objectives; incorporates some of the key audit issues facing the City; and summarizes audit responsibilities under *Government Auditing Standards*, issued by the Comptroller General of the United States. Also included in this document is a summary of recent technical developments in governmental accounting and financial reporting that may impact the City over the next few years.

We are committed to serving the City so that citizens, elected officials, management, grantor agencies and creditors continue to have the utmost confidence in the City's financial statements, internal control systems and compliance with laws and regulations. We dedicate the resources of our team and provide ongoing access to our very best resources to exceed the City's expectations.

We appreciate the opportunity to be of service and look forward to discussing the highlights of our Plan with the City.

Very truly yours,



**Cynthia Pon, CPA, CGMA**  
MGO Partner



SECTION 1

# Executive Summary

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Our goal is to continuously exceed the expectations of the City and to focus the resources of our firm in providing efficient, cost effective and high-quality services to the City.

### **MGO OBJECTIVES**

Our mission is to be the professional service firm that consistently exceeds the expectations of our clients and our people. Our objective is to deliver seamless, high quality, timely service to the City in all areas in which we provide professional services. In addition to assurance services these include accounting and consultation, advisory, tax, and other specialized services. We will meet our objectives by identifying opportunities to provide value-added services to the City.

In order to accomplish this, we will:

- Identify and resolve reporting, accounting and audit issues timely and effectively;
- Regularly communicate with City management;
- Complete our audits on a timely basis;
- Provide seamless service across the organization;
- Understand your organization, culture, programs and services;
- Provide the suited experienced professionals;
- Utilize specialists where unique skill sets are required;
- Apply our technical knowledge to identify solutions to organizational and financial issues;
- Respond to critical issues with a sense of urgency;
- Act as another set of “eyes and ears”;
- Meet all deadlines; and
- Communicate key findings to the oversight bodies and management.

### **OUR FOCUS IS ON THE CITY'S CRITICAL AUDIT AREAS AND OPERATION CHANGES**

Through planned face-to-face meetings with members of the Chair of the Government Audit & Oversight Committee, the Retirement Board, the Mayor's Office, the Controller's Office, and key management personnel throughout the year, we will directly ascertain the City's expectations of us and we will communicate our responsibilities under professional standards. We will listen to what members of management expect from us and ask them to tell us what service attributes are most important to them. We will use this information to develop a comprehensive audit approach to respond to identified issues and service needs for the City.

### **AUDIT SERVICES**

Our audit services emphasize comprehensive planning and risk assessment to fulfill our professional responsibilities and enable us to be responsive to the needs of the City.

### **OUR SERVICE TEAMS**

An important part of successfully implementing our plan is identifying and utilizing the appropriate resources. We have selected engagement teams that are committed to carrying out our service plan. Cynthia Pon, Lead Partner, leads our service team and will coordinate the audits performed by MGO. The Engagement Team section lists the key individuals assigned to the City's individual funds and component units.

### **QUALITY AND RESPONSIVE SERVICE**

We provide service, which stresses responsive attention year-round. Close communication with our clients is one of our top service qualities – it is the only way we serve our clients. We will work with you as business advisors, and we will place special emphasis on being actively involved in understanding all significant financial and reporting matters. Accordingly, we will meet with you regularly to stay abreast of your service needs and special concerns. You can call upon us as a resource at any time.

### **AUDIT APPROACH**

Our audit approach carefully considers the identification of key risk areas and allocation of appropriate resources. Professionals with extensive auditing and accounting experience lead all phases of our audit. With our experienced leaders in the field, our efficiency and effectiveness increase when dealing with complex accounting and auditing issues.

Our audit procedures include analytical reviews, verification of balances and transactions based on independent supporting documentation using statistical and judgmental sampling techniques, confirmation of key balances, and analysis of key assumptions supporting significant estimates made by management.

This document further presents discussions on our approach to the services we will provide to the City, details our framework for planning and performing the audit, and sets forth our audit scope and timing.

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SECTION 2

# The Engagement Team

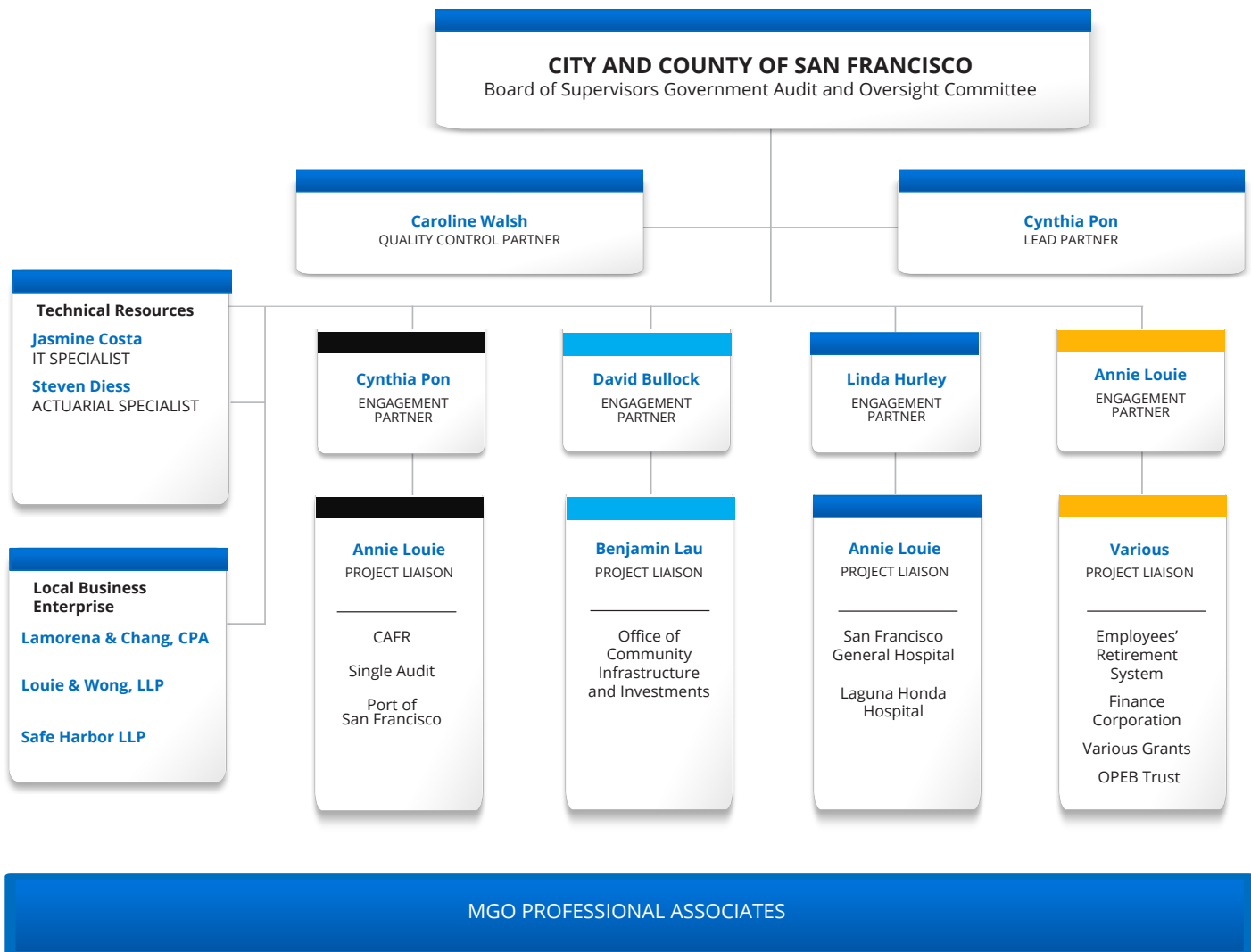
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# Engagement Team

The engagement teams selected to serve the City represents the strong, balanced blend of talent, professional skills, and industry experience that is most critical to working effectively with local governments of your size and complexity. The MGO Team is integrated to allow us to respond to your needs. We are committed to providing the resources necessary to meet the timeline that has been established by the City. This commitment includes providing the appropriate number and level of staffing to meet your needs.



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SECTION 3

# Audit Timing

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We recognize the importance of timely completion of audit tasks and deliverables. The timing of our audit procedures will be coordinated with management to minimize disruption of City operations and to ensure timely delivery of all reports by your deadlines.

Government-related entities often depend on a structure of interlocking relationships for managing broad programs and resources. Our philosophy for a successful engagement is based on organization,

communication, and coordination between the two parties responsible for the completion of the audit – the accounting firm and the client. We take coordination seriously and regard it as an integral factor to the relationship. We welcome the City's involvement in the planning process and believe that monitoring progress will result in timely financial reporting.

We are committed to delivering the City's various reports according to the City's proposed time plan.

AUDIT TIMELINE	Group 1 - General City	Group 2 - Employees' Retirement System	Group 3 - Successor Agency	Group 5 - Hospitals	Group 7 - Port	Group 8 - Finance Corporation	Group 11 - State of California Grants	Group 12 - Retiree Health Benefit Trust
<b>Planning and Execution of Tests of Controls</b>								
Planning meetings with key management and governing boards	May - July	May - July	May - July	May - July	May - July	May - July	May - July	May - July
Submit Audit Plan to the Board's Government Audit and Oversight Committee	05/17	05/17	05/17	05/17	05/17	05/17	05/17	05/17
On-site planning and execution of tests of controls	May - June	July	July	May - June	July	May - June	09/26 - 10/07	May - June
Single Audit planning and preliminary program compliance tests	May - Aug	n/a	July	n/a	n/a	n/a	n/a	n/a
<b>Execution of Substantive Procedures</b>								
Auditors' receipt of draft financial statements, including notes, management's discussion and analysis (MD&A), and all other client-prepared documents	10/02	09/25	09/18	09/11	09/11	10/02	09/18	10/02
On-site year-end fieldwork	10/02 - 11/17	09/25 - 10/06	09/18 - 9/29	09/11 - 10/06	09/11 - 10/06	10/02 - 11/17	09/18 - 09/29	10/02 - 11/17
Completion of Single Audit tests	12/29	n/a	n/a	n/a	n/a	n/a	n/a	n/a
Completion of Gann Agreed-Upon Procedures	07/28	n/a	n/a	n/a	n/a	n/a	n/a	n/a
<b>Completion Procedures and Communications</b>								
Issuance of final basic financial statements	11/17	10/20	10/20	(1)	10/20	10/20	10/20	11/17
Issuance of Gann Agreed-Upon Procedures Report	07/28	n/a	n/a	n/a	n/a	n/a	n/a	n/a
Issuance of Single Audit Reports	01/26/18	n/a	01/26/18	n/a	n/a	n/a	n/a	n/a
Issuance of management letter comments, if applicable	12/19	10/20	(2)	(2)	(2)	(2)	(2)	(2)
Present Audit Results to the Board's Government Audit & Oversight Committee	March 2018	March 2018	March 2018	March 2018	March 2018	March 2018	March 2018	March 2018

(1) The hospitals' financial statements are incorporated into and reported with the General City's basic financial statements.

(2) Management letter comments for these groups, if applicable, will be combined with Group 1's letter.

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SECTION 4

# The Audit Process

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## PLANNING

### TIMELY INVOLVEMENT WITH RISKS AND ISSUES

Planning the City's audits is a continuous process. Our ongoing attention to changes in the City's economic and operating environment enables us to react to changing circumstances and unanticipated events and enhances our understanding of the City. The objectives of the planning phase are to develop an audit plan that 1) effectively and efficiently meets our professional responsibilities and 2) meets or exceeds the expectations and needs of City management, the Mayor, and the governing boards.

To accomplish our planning objectives, we will:

- Document our understanding of the internal and external factors affecting the City, which enables us to identify and evaluate relevant areas of risk.
- Document our understanding of the City's control environment, accounting systems and control procedures for significant audit areas and transaction streams.
- Finalize an audit plan that identifies critical audit areas and procedures to address identified risks.
- Ensure that our plan provides appropriate audit coverage.
- Coordinate our audit services with the support of management for maximum efficiency.
- Develop and execute an audit plan that is designed to deliver our services effectively and efficiently and provides a basis for the issuance of our opinions.
- Strive to add value.

### CLIENT SERVICE PROGRAM

Through our client service program, the City receives the direct attention of one of our most knowledgeable and experienced professionals, Cynthia Pon.

Cynthia will review our annual client service plan and the reports prepared on the results of each year's work, and the assignment of personnel to the engagement. In addition, she will assure that your specialized needs receive priority access to top resources from anywhere in our organization.

### ENVIRONMENTAL ASSESSMENT

In addition, our planning process evaluates the City's financial reporting risks based on the broader environment, drawing upon our knowledge of economic and operational changes affecting the City, including the impact of:

- Fiscal condition of the state and local governments
- Legislative and regulatory developments
- Emerging pension issues

## EXECUTION

### PERFORMANCE - EXECUTION OF AUDIT PLAN

Our audit scope must be designed to provide sufficient audit coverage to enable us to express an opinion on the City's financial statements, as well as addressing all known audit risks, which could materially impact the City's financial statements.

Execution generally includes the following steps:

- Performance of audit tests and evaluation of results
- Development of organizational insights
- Review of financial statements, financial statement disclosures and subsequent events
- Obtaining management representations

During the course of the audit, we use our knowledge gained during the planning phase related to your current organizational strategies, economic conditions, internal control, and the identified risks to tailor our audit procedures.

## APPROACH TO CRITICAL AUDIT AREAS

We have identified certain critical audit areas facing the City. During our planning phase of the audit, we expand our understanding of these critical audit areas and obtain further information as needed in order to appropriately design audit procedures to address these issues.

### Other Postemployment Benefits

**(OPEB)** – The City administers an agent multiple employer, defined benefit OPEB plan. In FY 2016-17, the OPEB Plan will implement the provisions of GASB Statement No. 74 *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans*. This statement requires more extensive note disclosures and Required Supplementary Information (RSI) related to the measurement of the OPEB liabilities for which assets have been accumulated, including information about the annual money-weighted rates of return on plan investments. Our audit approach will focus on the reasonableness of actuarial assumptions in the actuarial valuation, calculations for other postemployment benefits, and adherence to the new financial reporting standard.

**Single Audit - Uniform Guidance** – Effective December 26, 2014, state and local governments receiving federal awards were subject to the new Title 2 U.S. Code of Federal Regulations (CFR) Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance), issued by the Office of Management and Budget (OMB). As a result, expenditures of federal awards under grant awards and revisions made after this date were subject to these new requirements. As your auditors, we have a responsibility to determine if the City complied with laws, regulations, and the provisions of contracts or grant agreements pertaining to federal awards that have a direct and material effect on each major program. We will consider the policies and procedures implemented to ensure

applicable compliance requirements, including those pertaining to the new Uniform Guidance.

**Investment Valuations** – The Retirement System manages an investment portfolio that includes derivatives and other alternative investments. Fair value determination for these investments involve significant judgment. We will apply audit procedures to the valuation of investments and evaluate key factors and assumptions used to develop the estimates.

**Patient Service Revenues** – Net patient services revenues are recorded at the estimated net realizable amounts from patients, third-party payors, and others for services rendered, including a provision for doubtful accounts and estimated retroactive adjustments under reimbursement agreements with federal and state government programs and other third-party payors. We will apply audit procedures to the revenue estimates and cost recognition methods related to reimbursement rates, third party payors, health care contracts or commitments and guarantees.

**Long Term Debt** – The primary function of the City's Finance Corporation is to act as a financing vehicle for the City. To finance these projects, the Finance Corporation relies on base payments received from the City. Our audit approach will include an assessment of compliance with the significant terms of the bond covenants.

#### **TIMING OF OUR WORK**

We have timed our work to coincide with key activities that are taking place in the City throughout the year. The Audit Timing section of this Plan outlines the timing of our procedures.

#### **THE RESULT**

Our process is designed to enable us to issue the independent auditor's report within the agreed upon timeline. The result of our work will also include the timely delivery of observations and suggestions regarding the control environment and operations of your organization. Such communications will be delivered both formally, through the report to management, as well as informally through regular meetings with management.

#### **REPORTING**

##### **SCOPE AND RESPONSIBILITY**

Our audit will be conducted in accordance with auditing standards generally accepted in the United States of America (GAAS) and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States for the purpose of expressing opinions on the fair presentation of the City's financial statements in conformity with U.S. generally accepted accounting principles. In addition, we will perform certain limited procedures involving required supplementary information mandated by the Governmental Accounting Standards Board as required by GAAS. Our audits are designed to obtain reasonable (as opposed to absolute) assurance about whether the financial statements are fairly presented.

The City's Comprehensive Annual Financial Report (CAFR) presents financial information on the activities of the City for which the Mayor and the Board of Supervisors have oversight, governing, and budgeting responsibilities. The CAFR encompasses the basic financial statements and other financial and statistical information including combining statements of individual funds, supporting schedules, ten-year trend data, and various other statistical data.

#### **FINANCIAL STATEMENTS AUDITED BY OTHER AUDITORS**

Separate financial statements for certain funds and organizations that are presented in the City's CAFR are audited by other firms:

- San Francisco County Transportation Authority
- Group 4 – Health Service System
- Group 6 – San Francisco International Airport
- Group 9 – Public Utilities Commission (PUC) including the Water Department, Hetch Hetchy Water and Power, and the Wastewater Enterprise
- Group 10 – Municipal Transportation Agency which includes the parking garage nonprofit organizations

The audit plans for these entities are not included in this document. Our report on the City's basic financial statements will make reference to the reports of the auditors of the City's individual fund and component unit reports not audited by MGO as noted above.

The basic financial statements are the responsibility of management. In this regard, management has the responsibility for properly recording transactions in the accounting records, for adjusting the financial statements to correct material misstatements, for making appropriate accounting estimates, for safeguarding assets, and for the overall accuracy of the financial statements and their conformity with accounting principles generally accepted in the United States of America.

In addition, we will conduct a single audit of the City in accordance with the Uniform Guidance. The audit will be the financial and compliance type described in *Government Auditing Standards*. The Single Audit will not include federal expenditures of the San Francisco County Transportation Authority, the International Airport, the Municipal Transportation Agency (MTA), and the Successor Agency to the Redevelopment Agency, which issue separate single audit reports.

## REPORTING RESPONSIBILITY UNDER AUDITING STANDARDS GENERALLY ACCEPTED IN THE UNITED STATES OF AMERICA

We will also report directly to management and to you matters coming to our attention during the course of our audit that we believe are deficiencies. A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A *material weakness* is a deficiency, or combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

In addition to communications about our responsibilities under U.S. generally accepted auditing standards and the planned scope and timing of the audit, we will communicate to you certain other matters related to the conduct of our audit, including where appropriate the following matters:

- Qualitative Aspects of Accounting Practices
- Difficulties Encountered in Performing the Audit
- Corrected and Uncorrected Misstatements
- Disagreements with Management
- Management Representations
- Management Consultations with Other Independent Accountants
- Other Audit Findings or Issues
- Required Supplementary Information

- Other Supplementary Information
- Other Information in Documents Containing Audited Financial Statements

## MANAGEMENT COMMENTS

One of the primary service objectives is to make constructive and timely recommendations and to provide advice to you and management on matters we believe warrant attention. We have tailored our audit approach to focus on those risks that are important to achieving control and reporting objectives. We have the benefit of being objective outsiders in considering the information we gather. The result is that we are able to add the perspective of our experience and expertise to translate our audit findings into recommendations and insights concerning existing or potential problems. We will keep management and you apprised of any matters that we believe warrant consideration whenever they come to our attention.

## ASSESSMENT – CLIENT SERVICE SATISFACTION

Annually we obtain direct feedback from our clients about their satisfaction level with MGO services. We have partnered with a satisfaction research firm, Inavero, to conduct brief 3-question surveys that allow you to rate our services and share your valuable input. In addition to communicating with management regarding the effectiveness of our services, we use the survey results to identify areas to focus on in order to increase your satisfaction with our service delivery.

Once we receive your response and feedback, we'll identify opportunities to add value; to identify the most experienced people within our organization to best respond to the City's needs; and to monitor the delivery of such services to ensure we exceed your service expectations.

In addition, we will hold recurring meetings between MGO and the City's management to discuss emerging issues. The key objective of these meetings is to consolidate our combined knowledge of the City's organizational changes and new programs or initiatives. These meetings will result in a better understanding of the challenges facing the City and will enable us to proactively identify opportunities and bring creative ideas to the attention of the City's management.

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SECTION 5

# Engagement Communications

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We are pleased to confirm our understanding of the services we are to provide the City and County of San Francisco (City) for the year ended June 30, 2017. We will audit the financial statements of the governmental activities, each major fund, and the aggregate remaining fund information and the discretely presented component unit, including the related notes to the financial statements, which collectively comprise the basic financial statements, of the City as of and for the year ended June 30, 2017. Our report on the City's basic financial statements will make reference to the auditors' reports on the City's individual funds and component units not audited by Macias Gini & O'Connell LLP (MGO).

In addition to our audit of the basic financial statements of the City, we will also perform the following:

- Audit and separately report on the individual financial statements of the San Francisco City and County Employees' Retirement System, the Successor Agency to the Redevelopment Agency, Port of San Francisco, the San Francisco Finance Corporation, and the Retiree Health Benefit Trust.
- Audit and separately report on compliance with federal award programs in accordance with Office of Management and Budget (OMB) *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* set forth in Title 2 CFR, Subtitle A, Chapter II, Part 200 (Uniform Guidance).
- Separately audit the San Francisco General Hospital and the San Francisco Laguna Honda Hospital enterprise major funds. Separate stand-alone reports are not required by the City.
- Agreed-upon procedures to review compliance with appropriations limit requirements of Section 1.5 Article XIII B of the California Constitution (commonly referred to as the Gann Limit) in accordance with the procedures agreed to management and recommended by the California Committee on Municipal Accounting (as presented

in the CCMA White Paper titled *Agreed-upon Procedures Applied to the Appropriations Limitation Prescribed by Article XIII B of the California Constitution*).

- Audit and separately report on the Statements of Source and Status of Cash and the related Statements of Budget and Cumulative Expenditures of the Automobile Insurance Fraud Program and the Workers' Compensation Insurance Fraud Program that are funded by grants from the State of California Department of Insurance.
- Audit and separately report on the financial statements of the Local Transportation Fund and on compliance in accordance with applicable statutes, rules and regulations of the Transportation Development Act (TDA), including section 6661 of Title 21 of the California Administrative Code.
- Audit and separately report on the financial statements of TDA grant funds from the Metropolitan Transportation Commission and on compliance with applicable statutes, rules and regulations of the TDA, including section 6664 of Title 21 of the California Code of Regulations, and the allocation instructions and resolutions of the Metropolitan Transportation Commission.

Accounting standards generally accepted in the United States of America provide for certain required supplementary information (RSI), such as management's discussion and analysis (MD&A), to supplement the City's basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. As part of our engagement, we will apply certain limited procedures to the City's RSI in accordance with auditing standards generally accepted in the United States of America. These limited procedures will consist of inquiries of management regarding the methods of preparing the information

and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We will not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance. The following RSI is required by generally accepted accounting principles and will be subjected to certain limited procedures, but will not be audited:

- Management's Discussion and Analysis
- Pension Plans – Schedule of the City's Proportionate Share of the Net Pension Liability
- Pension Plans – Schedule of Changes in Net Pension Liability and Related Ratios
- Pension Plans – Schedule of the Employer Contributions
- Other Postemployment Healthcare Benefits – Schedules of Funding Progress and Employer Contributions
- Other Postemployment Healthcare Benefits - Schedule of Moneyweighted Rate of Return

We have also been engaged to report on supplementary information other than RSI that accompanies the City's financial statements. We will subject the following supplementary information to the auditing procedures applied in our audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America and will provide an opinion on it in relation to the financial statements as a whole:

- Combining and individual fund financial statement schedules
- Schedule of expenditures of federal awards

The City's Comprehensive Annual Financial Report (CAFR) will also include introductory and statistical sections prepared by the City that will not be subjected to the auditing procedures applied in our audit of the financial statements, and our auditor's report will not provide an opinion or any assurance on that other information.

### AUDIT OBJECTIVES

The objective of our audit is the expression of opinions as to whether the City's basic financial statements are fairly presented, in all material respects, in conformity with U.S. generally accepted accounting principles and to report on the fairness of the supplementary information referred to in the second paragraph when considered in relation to the financial statements as a whole. The objective also includes reporting on—

- Internal control over financial reporting and compliance with provisions of laws, regulations, contracts, and award agreements, noncompliance with which could have a material effect on the financial statements in accordance with *Government Auditing Standards*.
- Internal control over compliance related to major programs and an opinion (or disclaimer of opinion) on compliance with federal statutes, regulations, and the terms and conditions of federal awards that could have a direct and material effect on each major program in accordance with the Single Audit Act Amendments of 1996 and Title 2 U.S. Code of Federal Regulations (CFR) Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance).

The *Government Auditing Standards* report on internal control over financial reporting and on compliance and other matters will include a paragraph that states that (1) the purpose of the report is solely to describe the scope of testing of internal control and compliance and the results of that testing, and not to

provide an opinion on the effectiveness of the entity's internal control or on compliance, and (2) the report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. The Uniform Guidance report on internal control over compliance will include a paragraph that states that the purpose of the report on internal control over compliance is solely to describe the scope of testing of internal control over compliance and the results of that testing based on the requirements of the Uniform Guidance. Both reports will state that the report is not suitable for any other purpose.

Our audit will be conducted in accordance with auditing standards generally accepted in the United States of America; the standards for financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; the Single Audit Act Amendments of 1996; and the provisions of the Uniform Guidance, and will include tests of accounting records, a determination of major program(s) in accordance with the Uniform Guidance, and other procedures we consider necessary to enable us to express such opinions. We will issue written reports upon completion of our single audit. Our reports will be addressed to the Mayor and the Board of Supervisors of the City. We cannot provide assurance that unmodified opinions will be expressed. Circumstances may arise in which it is necessary for us to modify our opinions or add emphasis-of-matter or other-matter paragraphs. If our opinions on the financial statements or the single audit compliance opinions are other than unmodified, we will discuss the reasons with management in advance. If, for any reason, we are unable to complete the audit or are unable to form or have not formed opinions, we may decline to express opinions or issue reports, or we may withdraw from the engagement.

### AUDIT PROCEDURES—GENERAL

An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements; therefore, our audit will involve judgment about the number of transactions to be examined and the areas to be tested. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements. We will plan and perform the audit to obtain reasonable rather than absolute assurance about whether the financial statements are free of material misstatement, whether from (1) errors, (2) fraudulent financial reporting, (3) misappropriation of assets, or (4) violations of laws or governmental regulations that are attributable to the government or to acts by management or employees acting on behalf of the government. Because the determination of abuse is subjective, *Government Auditing Standards* do not expect auditors to provide reasonable assurance of detecting abuse.

Because of the inherent limitations of an audit, combined with the inherent limitations of internal control, and because we will not perform a detailed examination of all transactions, there is a risk that material misstatements or noncompliance may exist and not be detected by us, even though the audit is properly planned and performed in accordance with U.S. generally accepted auditing standards and *Government Auditing Standards*. In addition, an audit is not designed to detect immaterial misstatements or violations of laws or governmental regulations that do not have a direct and material effect on the financial statements or major programs. However, we will inform the appropriate level of management of any material errors, any fraudulent financial reporting, or misappropriation of assets that come to our attention. We will also inform the appropriate level of management of any violations of laws or governmental regulations that come to our attention,

unless clearly inconsequential, and of any material abuse that comes to our attention. We will include such matters in the reports required for a single audit. Our responsibility as auditors is limited to the period covered by our audit and does not extend to any later periods for which we are not engaged as auditors.

Our procedures will include tests of documentary evidence supporting the transactions recorded in the accounts, and may include tests of the physical existence of inventories, and direct confirmation of receivables and certain other assets and liabilities by correspondence with selected individuals, funding sources, creditors, and financial institutions. We will request written representations from the City's attorneys as part of the engagement, and they may bill the City for responding to this inquiry. At the conclusion of our audit, we will require certain written representations from management about management's responsibilities for the financial statements; schedule of expenditures of federal awards; federal award programs; compliance with laws, regulations, contracts, and grant agreements; and other responsibilities required by generally accepted auditing standards.

#### AUDIT PROCEDURES—INTERNAL CONTROL

Our audit will include obtaining an understanding of the government and its environment, including internal control, sufficient to assess the risks of material misstatement of the financial statements and to design the nature, timing, and extent of further audit procedures. Tests of controls may be performed to test the effectiveness of certain controls that we consider relevant to preventing and detecting errors and fraud that are material to the financial statements and to preventing and detecting misstatements resulting from illegal acts and other noncompliance matters that have a direct and material effect on the financial statements. Our

tests, if performed, will be less in scope than would be necessary to render an opinion on internal control and, accordingly, no opinion will be expressed in our report on internal control issued pursuant to *Government Auditing Standards*.

As required by the Uniform Guidance, we will perform tests of controls over compliance to evaluate the effectiveness of the design and operation of controls that we consider relevant to preventing or detecting material noncompliance with compliance requirements applicable to each major federal award program. However, our tests will be less in scope than would be necessary to render an opinion on those controls and, accordingly, no opinion will be expressed in our report on internal control issued pursuant to the Uniform Guidance.

An audit is not designed to provide assurance on internal control or to identify significant deficiencies or material weaknesses. However, during the audit, we will communicate to management and those charged with governance internal control related matters that are required to be communicated under AICPA professional standards, *Government Auditing Standards*, and the Uniform Guidance.

#### AUDIT PROCEDURES—COMPLIANCE

As part of obtaining reasonable assurance about whether the financial statements are free of material misstatement, we will perform tests of the City's compliance with provisions of applicable laws, regulations, contracts, and agreements, including grant agreements. However, the objective of those procedures will not be to provide an opinion on overall compliance and we will not express such an opinion in our report on compliance issued pursuant to *Government Auditing Standards*.

The Uniform Guidance requires that we also plan and perform the audit to obtain reasonable assurance about whether the auditee has complied with applicable federal statutes, regulations, and the terms and conditions of federal awards applicable to major programs. Our procedures will consist of tests of transactions and other applicable procedures described in the OMB Compliance Supplement for the types of compliance requirements that could have a direct and material effect on each of the City's major programs. The purpose of these procedures will be to express an opinion on the City's compliance with requirements applicable to each of its major programs in our report on compliance issued pursuant to the Uniform Guidance.

#### MANAGEMENT RESPONSIBILITIES

Management is responsible for (1) establishing and maintaining effective internal controls, including internal controls over federal awards, and for evaluating and monitoring ongoing activities, to help ensure that appropriate goals and objectives are met; (2) following laws and regulations; (3) ensuring that there is reasonable assurance that government programs are administered in compliance with compliance requirements; and (4) ensuring that management and financial information is reliable and properly reported. Management is also responsible for implementing systems designed to achieve compliance with applicable laws, regulations, contracts, and grant agreements. Management is also responsible for the selection and application of accounting principles; for the preparation and fair presentation of the financial statements, schedule of expenditures of federal awards, and all accompanying information in conformity with U.S. generally accepted accounting principles; and for compliance with applicable laws and regulations (including federal statutes) and the provisions of contracts and

grant agreements (including award agreements).

Management is also responsible for making all financial records and related information available to us and for the accuracy and completeness of that information. Management is also responsible for providing us with (1) access to all information of which management is aware that is relevant to the preparation and fair presentation of the financial statements, (2) access to personnel, accounts, books, records, supporting documentation, and other information as needed to perform an audit under the Uniform Guidance, (3) additional information that we may request for the purpose of the audit, and (4) unrestricted access to persons within the government from whom we determine it necessary to obtain audit evidence.

Management's responsibilities also include identifying significant contractor relationships in which the contractor has responsibility for program compliance and for the accuracy and completeness of that information. Management's responsibilities include adjusting the financial statements to correct material misstatements and confirming to us in the management representation letter that the effects of any uncorrected misstatements aggregated by us during the current engagement and pertaining to the latest period presented are immaterial, both individually and in the aggregate, to the financial statements taken as a whole.

Management is responsible for the design and implementation of programs and controls to prevent and detect fraud, and for informing us about all known or suspected fraud affecting the government involving (1) management, (2) employees who have significant roles in internal control, and (3) others where the fraud could have a material effect on the financial statements. Management's

responsibilities include informing us of their knowledge of any allegations of fraud or suspected fraud affecting the government received in communications from employees, former employees, grantors, regulators, or others. In addition, management is responsible for identifying and ensuring that the government complies with applicable laws, regulations, contracts, agreements, and grants. Management is also responsible for taking timely and appropriate steps to remedy fraud and noncompliance with provisions of laws, regulations, contracts, and grant agreements, or abuse that we report. Additionally, as required by the Uniform Guidance, it is management's responsibility to evaluate and monitor noncompliance with federal statutes, regulations, and the terms and conditions of federal awards; take prompt action when instances of noncompliance are identified including noncompliance identified in audit findings; promptly follow up and take corrective action on reported audit findings; and prepare a summary schedule of prior audit findings and a separate corrective action plan.

Management is responsible for identifying all federal awards received and understanding and complying with the compliance requirements and for the preparation of the schedule of expenditures of federal awards (including notes and noncash assistance received) in conformity with the Uniform Guidance. Management agrees to include our report on the schedule of expenditures of federal awards in any document that contains and indicates that we have reported on the schedule of expenditures of federal awards. Management also agrees to include the audited financial statements with any presentation of the schedule of expenditures of federal awards that includes our report thereon. Management's responsibilities include acknowledging to us in the written representation letter that (1) management is responsible for

presentation of the schedule of expenditures of federal awards in accordance with the Uniform Guidance; (2) management believes the schedule of expenditures of federal awards, including its form and content, is stated fairly in accordance with the Uniform Guidance; (3) the methods of measurement or presentation have not changed from those used in the prior period (or, if they have changed, the reasons for such changes); and (4) management has disclosed to us any significant assumptions or interpretations underlying the measurement or presentation of the schedule of expenditures of federal awards.

Management is also responsible for the preparation of the other supplementary information, which we have been engaged to report on, in conformity with U.S. generally accepted accounting principles. Management agrees to include our report on the supplementary information in any document that contains, and indicates that we have reported on, the supplementary information. Management also agrees to include the audited financial statements with any presentation of the supplementary information that includes our report thereon. Management's responsibilities include acknowledging to us in the written representation letter that (1) management is responsible for presentation of the supplementary information in accordance with GAAP; (2) management believes the supplementary information, including its form and content, is fairly presented in accordance with GAAP; (3) the methods of measurement or presentation have not changed from those used in the prior period (or, if they have changed, the reasons for such changes); and (4) management has disclosed to us any significant assumptions or interpretations underlying the measurement or presentation of the supplementary information.



Management is responsible for establishing and maintaining a process for tracking the status of audit findings and recommendations. Management is also responsible for identifying and providing report copies of previous financial audits, attestation engagements, performance audits, or other studies related to the objectives discussed in the Audit Objectives section. This responsibility includes relaying to us corrective actions taken to address significant findings and recommendations resulting from those audits, attestation engagements, performance audits, or studies. Management is also responsible for providing management's views on our current findings, conclusions, and recommendations, as well as management's planned corrective actions, for the report, and for the timing and format for providing that information.

Management agrees to assume all management responsibilities relating to the financial statements, schedule of expenditures of federal awards, and related notes, and any other nonaudit services we provide, if applicable. Further, management agrees to oversee any nonaudit services by designating an individual, preferably from senior management, with suitable skill, knowledge, or experience; evaluate the adequacy and results of those services; and accept responsibility for them.

## ENGAGEMENT ADMINISTRATION

We may from time to time, and depending on the circumstances, use third-party service providers in serving the City. We may share confidential information about the City with these service providers, but remain committed to maintaining the security and confidentiality and security of the City's information. Accordingly, we maintain internal policies, procedures, and safeguards to protect the security and confidentiality of the City's personal information. In

addition, we will secure confidentiality agreements with all service providers to maintain the confidentiality of the City's information and we will take reasonable precautions to determine that they have appropriate procedures in place to prevent the unauthorized release of the City's confidential information to others. In the event that we are unable to secure an appropriate confidentiality agreement, management will be asked to provide consent prior to the sharing of the City's confidential information with the third-party service provider. Furthermore, we will remain responsible for the work provided by any such third-party service providers.

Macias Gini & O'Connell LLP (MGO) is the U.S. firm of our network of separate and independent MGO firms. MGO may, in its discretion, draw on resources of its subsidiaries, its affiliates, and/or third-party contractors, in each case within or outside the United States, in connection with the provision of services. The City agrees that MGO may provide access to information it receives in connection with this agreement to our other resources. MGO maintains all of the City's data within the U.S. and represents that it has internal policies, procedures, and safeguards to protect the security and confidentiality of City's information. MGO will be solely responsible for the provision of the services.

We understand that City employees will prepare all cash, accounts receivable, or other confirmations we request and will locate any documents selected by us for testing.

At the conclusion of the engagement, we will complete the appropriate sections of the Data Collection Form that summarizes our audit findings. It is management's responsibility to electronically submit the reporting package (including financial statements, schedule of expenditures of federal awards, summary schedule of prior audit findings, auditors' reports, and

corrective action plan) along with the Data Collection Form to the federal audit clearinghouse. We will coordinate with management the electronic submission and certification. If applicable, we will provide copies of our report for management to include with the reporting package management will submit to pass-through entities. The Data Collection Form and the reporting package must be submitted within the earlier of 30 calendar days after receipt of the auditor's reports or nine months after the end of the audit period. We will provide copies of our reports to the City; however, management is responsible for distribution of the reports and the financial statements. Unless restricted by law or regulation, or containing privileged and confidential information, copies of our reports are to be made available for public inspection.

The audit documentation for this engagement is the property of MGO and constitutes confidential information. However, subject to applicable laws and regulations, audit documentation and appropriate individuals will be made available upon request and in a timely manner to the City's cognizant agency or its designee, a federal agency providing direct or indirect funding, or the U.S. Government Accountability Office for purposes of a quality review of the audit, to resolve audit findings, or to carry out oversight responsibilities. We will notify management of any such request. If requested, access to such audit documentation will be provided under the supervision of MGO personnel. Furthermore, upon request, we may provide copies of selected audit documentation to the aforementioned parties. These parties may intend, or decide, to distribute the copies or information contained therein to others, including other governmental agencies.

The audit documentation for this engagement will be retained for

a minimum of seven years after the report release date or for any additional period requested by the City's cognizant agency. If we are aware that a federal awarding agency, pass-through entity, or auditee is contesting an audit finding, we will contact the party(ies) contesting the audit finding for guidance prior to destroying the audit documentation. Upon expiration of the seven-year period, MGO will be free to destroy our records related to this engagement. However, MGO does not keep any original client records, so we will return those to management at the completion of the services rendered under this engagement. When records are returned to management, it is management's responsibility to retain and protect the records for possible future use, including potential examination by any government or regulatory agencies.

In the performance of our professional services, we may communicate with the City and/or with others via email transmission. As emails can be intercepted and read, disclosed, or otherwise used by an unintended third party, we cannot guarantee that such email communication will be properly delivered and read only by the addressee. While we will use our best efforts to keep such communications secure in accordance with our obligations under applicable laws and professional standards, the City recognizes and accepts that we have no control over the unauthorized interception of these communications once they have been sent. Therefore, the City hereby waives any liability whatsoever for any unintended interception or unintentional disclosure of email transmissions in connection with the performance of our professional services. MGO uses cloud-based computing services, including the storage of data and files, at third party, offsite, secure facilities. In that regard, the City agrees that we shall have no liability for any loss or damage to any person or entity resulting from the

use of email transmissions and cloud-based computing, including any direct or indirect damages that may result from any inadvertent or unanticipated disclosure of confidential or proprietary information, or disclosure through third party criminal conduct (e.g., hackers or hacking activities).

With regards to the electronic dissemination of audited financial statements, including financial statements published electronically on the City's website, management understands that electronic sites are a means to distribute information and, therefore, we are not required to read the information contained in these sites or to consider the consistency of other information in the electronic site with the original document.

Professional and certain regulatory standards require us to be independent, in both fact and appearance, with respect to the City in the performance of our services. Any discussions that the City has with personnel of our firm regarding employment could pose a threat to our independence. Therefore, the City agrees to inform us prior to any such discussions that we can implement appropriate safeguards to maintain our independence.

Our 2015 peer review report is provided for your reference on the following page.





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September 17, 2015

### System Review Report

To the Partners of Macias Gini & O'Connell LLP  
 and the National Peer Review Committee

We have reviewed the system of quality control for the accounting and auditing practice of Macias Gini & O'Connell, LLP (the firm) applicable to engagements not subject to PCAOB permanent inspection in effect for the year ended March 31, 2015. Our peer review was conducted in accordance with the Standards for Performing and Reporting on Peer Reviews established by the Peer Review Board of the American Institute of Certified Public Accountants. As a part of our peer review, we considered reviews by regulatory entities, if applicable, in determining the nature and extent of our procedures. The firm is responsible for designing a system of quality control and complying with it to provide the firm with reasonable assurance of performing and reporting in conformity with applicable professional standards in all material respects. Our responsibility is to express an opinion on the design of the system of quality control and the firm's compliance therewith based on our review. The nature, objectives, scope, limitations of, and the procedures performed in a System Review are described in the standards at [www.aicpa.org/prsummary](http://www.aicpa.org/prsummary).

As required by the standards, engagements selected for review included engagements performed under *Government Auditing Standards* and audits of employee benefit plans.

In our opinion, the system of quality control for the accounting and auditing practice of Macias Gini & O'Connell, LLP applicable to engagements not subject to PCAOB permanent inspection in effect for the year ended March 31, 2015, has been suitably designed and complied with to provide the firm with reasonable assurance of performing and reporting in conformity with applicable professional standards in all material respects. Firms can receive a rating of *pass*, *pass with deficiency(ies)* or *fail*. Macias Gini & O'Connell, LLP has received a peer review rating of *pass*.

*Carr, Riggs & Ingram, LLC*

CARR, RIGGS & INGRAM, LLC

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SECTION 6

# Recent Developments in Governmental Accounting

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**mGO**



The following is a summary of the more recent and relevant Governmental Accounting Standards Board (GASB) and other pronouncements that may have an impact on the City in the current and future periods. We will have ongoing discussions with management about these as well as other developments in an effort to be prepared in advance for their implementation.

## NEW PRONOUNCEMENTS

### FISCAL YEAR 2017 IMPLEMENTATION

#### **GASB Statement No. 74 – Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans**

This statement addresses the financial reports of defined benefit OPEB plans that are administered through trusts that meet specified criteria. It follows the framework for financial reporting of defined benefit OPEB plans in the Statement No. 45 by requiring a statement of fiduciary net position and a statement of changes in fiduciary net position. It requires more extensive note disclosures and Required Supplementary Information (RSI) related to the measurement of the OPEB liabilities for which assets have been accumulated, including information about the annual money-weighted rates of return on plan investments. This statement also sets forth note disclosure requirements for defined contribution OPEB plans. This statement is effective for fiscal years beginning after June 15, 2016.

#### **GASB Statement No. 77 – Tax Abatement Disclosures**

This statement addresses financial reporting about the nature and magnitude of tax abatements of governmental entities. It requires that governments that enter into tax abatements disclose more comprehensive information about the agreements to make these transactions more transparent to financial statement users. Users will be better equipped

to understand (1) how tax abatements affect a government's future ability to raise resources and meet its financial obligations and (2) the impact those abatements have on a government's financial position and economic position. The requirements of this statement are effective for financial statements for periods beginning after December 15, 2015.

#### **GASB Statement No. 78 – Pensions Provided through Certain Multiple-Employer Defined Benefit Pension Plans**

This statement addresses a practice issue regarding the scope and applicability of Statement No. 68, *Accounting and Financial Reporting for Pensions*. This issue is associated with pensions provided through certain multiple-employer defined benefit pension plans and to state or local governmental employers whose employees are provided with such pensions. The requirements of this statement are effective for financial statements for periods beginning after December 15, 2015.

This statement amends the scope and applicability of Statement No. 68 to exclude pensions provided to employees of state or local governmental employers through a cost-sharing multiple-employer defined benefit pension plan that (1) is not a state or local governmental pension plan, (2) is used to provide defined benefit pensions both to employees of state or local governmental employers and to employees of employers that are not state or local governmental employers, and (3) has no predominant state or local governmental employer (either individually or collectively with other state or local governmental employers that provide pensions through the pension plan). This statement establishes requirements for recognition and measurement of pension expense, expenditures, and liabilities; note disclosures; and required supplementary

information for pensions that have the characteristics described above.

#### **GASB Statement No. 80 – Blending Requirements for Certain Component Units—an amendment of GASB Statement No. 14**

This statement is to improve the financial reporting by clarifying the financial statement presentation requirements for certain component units. This statement amends the blending requirements established in Statement No. 14, *The Financial Reporting Entity*, as amended, for the financial statement presentation of component units of all state and local governments. The additional criterion requires blending of a component unit incorporated as a not-for-profit corporation in which the primary government is the sole corporate member. The additional criterion does not apply to component units included in the financial reporting entity pursuant to the provisions of Statement No. 39, *Determining Whether Certain Organizations Are Component Units*. The requirements of this statement are effective for financial statements for periods beginning after June 15, 2016.

**FISCAL YEAR 2018 IMPLEMENTATION****GASB Statement No. 75 – Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions**

This Statement is intended to make OPEB accounting and financial reporting consistent with the pension standards outlined in GASB Statement No. 68.

Similar to the changes made to the pension standards, these new OPEB Standards provide a more comprehensive picture of what state and local governments have committed to their employees and the associated costs. Accordingly, the OPEB standards will affect the City's financial statements in the following ways:

- Change how the long-term obligation and the annual expense of OPEB are measured,
- Recognize the net OPEB liability on the face of the financial statements, and
- Present more extensive note disclosures and related supplemental schedules.

This statement is effective for fiscal years beginning after June 15, 2017. This statement applies to government employers who provide OPEB plans to their employees and basically parallels GASB Statement No. 68 and replaces GASB Statement No. 45.

**GASB Statement No. 81 – Irrevocable Split-Interest Agreements**

This statement is to improve accounting and financial reporting for irrevocable split-interest agreements by providing recognition and measurement guidance for situations in which a government is a beneficiary of the agreement. The requirements of this statement are effective for financial statements for periods beginning after December 15, 2016, and should be applied retroactively.

The requirements of this statement will enhance comparability of financial statements by providing accounting and financial reporting guidance for irrevocable split-interest agreements in which a government is a beneficiary. This statement also enhances the decision-usefulness of general purpose external financial reports, and their value for assessing accountability, by more clearly identifying the resources that are available for the government to carry out its mission.

**FISCAL YEAR 2019 IMPLEMENTATION****GASB Statement No. 83 – Certain Asset Retirement Obligations**

This Statement addresses accounting and financial reporting for certain asset retirement obligations (AROs). An ARO is a legally enforceable liability associated with the retirement of a tangible capital asset. A government that has legal obligations to perform future asset retirement activities related to its tangible capital assets should recognize a liability based on the guidance in this Statement.

This Statement also requires disclosure of information about the nature of a government's AROs, the methods and assumptions used for the estimates of the liabilities, and the estimated remaining useful life of the associated tangible capital assets. If an ARO (or portions thereof) has been incurred by a government but is not yet recognized because it is not reasonably estimable, the government is required to disclose that fact and the reasons therefor. This Statement requires similar disclosures for a government's minority shares of AROs.

This Statement will enhance comparability of financial statements among governments by establishing uniform criteria for governments to recognize and measure certain AROs, including obligations that may not have been previously reported. This Statement also will enhance the decision-usefulness of the information provided to financial statement users by requiring disclosures related to those AROs.

The requirements of this Statement are effective for reporting periods beginning after June 15, 2018. Earlier application is encouraged.

**FISCAL YEAR 2020 IMPLEMENTATION****GASB Statement No. 85 – Omnibus 2017**

The objective of this Statement is to address practice issues that have been identified during implementation and application of certain GASB Statements. This Statement addresses a variety of topics including issues related to blending component units, goodwill, fair value measurement and application, and postemployment benefits (pensions and other postemployment benefits [OPEB]).

The requirements of this Statement are effective for reporting periods beginning after June 15, 2017. Earlier application is encouraged.

**GASB Statement No. 84 – Fiduciary Activities**

This Statement established criteria for identifying fiduciary activities of all state and local governments. The focus of the criteria generally is on (1) whether a government is controlling the assets of the fiduciary activity and (2) the beneficiaries with whom a fiduciary relationship exists. Separate criteria are included to identify fiduciary component units and postemployment benefit arrangements that are fiduciary activities.

This Statement also provides for recognition of a liability to the beneficiaries in a fiduciary fund when an event has occurred that compels the government to disburse fiduciary resources. Events that compel a government to disburse fiduciary resources occur when a demand for the resources has been made or when no further action, approval, or condition is required to be taken or met by the beneficiary to release the assets.

The requirement of this Statement enhance consistency and comparability by (1) establishing specific criteria for identifying activities that should be reported as fiduciary activities and (2) clarifying whether and how business-type activities should report their fiduciary activities. Greater consistency and comparability enhances the value provided by the information reported in financial statements for assessing government accountability and stewardship.

The requirements of this Statement are effective for reporting periods beginning after December 15, 2018. Earlier application is encouraged.

# Questions?

**The West Coast is our home.**

WE HAVE CHEERFUL OFFICES THROUGHOUT CALIFORNIA.

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The logo for MGO, featuring the letters 'mgo' in a bold, lowercase, sans-serif font. The 'm' and 'g' are connected, and the 'o' is a simple circle. The color is a solid blue.