



BOARD REPORT 18-51

Date: December 18, 2018

To: Board of Deferred Compensation Administration (Board)

From: Staff

Subject: Evaluation of Responses to Procurement for Financial Auditing Services

Board Members

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Chairperson

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Recommendation:

That the Board (a) approve the selection of Crowe LLP (Crowe); (b) instruct staff to negotiate a contract with a three-year term incorporating annual audits; and (c) authorize the Board Chairperson to execute said contract on behalf of the Board, subject to agreement between the City and the provider as to all applicable terms and conditions and all necessary approvals.

Discussion:

This report contains recommendations related to the selection of a provider for Deferred Compensation Plan (DCP) financial auditing services pursuant to the Plan's previously issued Request for Proposal (RFP). Following completion of its evaluation of RFP responses, staff recommends that Crowe be selected to provide DCP audit services. In addition, given the price proposal relative to the Plan's resources, and after considering information previously discussed regarding the practices of other governmental defined contribution plan sponsors, staff recommends that the contract provide for annual DCP audits. This report will review key findings from its evaluation process and the basis for its recommendations for audit frequency and contract term.

A. Background

At the Board's January 16, 2018 meeting, staff indicated one of its key objectives for 2018 was developing a project plan for conducting DCP audits. At the Board's March 20, 2018 meeting, staff presented its proposed plan.

Staff indicated that the last DCP audit occurred in 2003 at a cost of \$38,000. Staff further indicated that the Board at that time, after considering the audit results and a number of other factors, elected not to pursue additional audits.

Staff further reported that since 2003 ongoing financial audits, particularly for larger plans, have become more commonplace, and provided feedback from a query of governmental members of the National Association of Governmental Defined Contribution Administrators (NAGDCA), including colleagues at the County of Los Angeles and State of California, who indicated they conduct annual audits. Staff also indicated that some plans, such as the City/County of San Diego, do not perform audits. Staff shared feedback from the DCP Third-Party Administrator (TPA), Voya, indicating that approximately 50% of their large public sector plans, as well as approximately 90% of their large private sector plans, conduct regular audits, the vast majority of which are also done annually. Furthermore, Wendy Young-Carter from Segal Consulting, the Plan's administrative consultant, informed staff that retirement plans governed by the Employee Retirement Income Security Act (ERISA) conduct audits on an annual basis, and that although ERISA requirements do not apply to the City's DCP, those requirements are often used as guidance for best practice.

Staff indicated that because of the variability in the structure of governmental defined contribution plans it was unclear what the potential costs of ongoing audits might be. Staff indicated that RFP responses would inform Board decisions as to audit frequency. The Board directed staff to draft an RFP for auditing services. In connection with staff's review of the responses, staff is also providing its recommendation as to audit frequency.

B. Request for Proposal and Recommended Provider

At its May 15, 2018 meeting, the Board authorized the release of an auditing services RFP. The RFP was released on August 14, 2018. On September 12, 2018, a mandatory pre-proposal conference was held. The following firms attended (in alphabetical order):

- 1) ACAP Accounting Services
- 2) Crowe LLP
- 3) Turner, Warren, Hwang & Conrad AC
- 4) Williams Adley
- 5) Vasquez & Company, LLP

Responses were due on October 4, 2018 and resulted in two proposal submissions from the firms Crowe and TWHC. A review of the proposal submissions by the Personnel Department's Administrative Services Division found both respondents to be compliant with the City's general contracting requirements. Evaluation and scoring of the service components of the RFP were completed by staff members Matthew Vong and Daniel Powell according to the RFP review criteria adopted by the Board. Of the rated categories, 1,000 points were possible.

The review criteria and summary scoring are indicated as follows:

Evaluation Category	Crowe	TWHC	Points Possible
Organizational Background and Reliability	81	76	100
Regulatory and Contractual Actions	42.5	49	50
Client Reviews	50	50	50
Auditing Experience and Client Services	485	374.5	500
Compensation and Performance Guarantees	178.5	185	200
Performance Exam	50	45	100
TOTAL-->	887	779.5	1,000

The summary scoring as well as highlighted components of each firm’s written responses are included in **Attachment A**.

The RFP process included performance exams in which staff and Segal met with each proposer to discuss certain detailed topics related to the auditing services requested in the RFP. During the performance exams, discussion focused on each firm’s auditing methodologies and requirements, including their respective approaches to project plan development and execution.

Defined Contribution Plan Auditing Experience

Staff’s evaluation assessed each firm’s institutional knowledge, experience, and capabilities as they relate to providing financial auditing services for Internal Revenue Code (IRC) Section 457 plans and the City’s DCP specifically. Crowe scored higher in these areas as their responses indicated that they have broad organizational resources dedicated to, and deep expertise within, the institutional auditing services universe, including specifically defined contribution plans. Crowe demonstrated a comparatively broader and more diverse resume of comparable client auditing experience. Crowe indicated that they audit over 1,200 plans annually, 900 of which are defined contribution plans and several of which are IRC Section 457 plans. TWHC indicated they provide auditing services to 30 private sector 401(k) and defined benefit plans but did not indicate the number of IRC Section 457 plans. Crowe’s scoring advantage in this category was further strengthened by their experience in coordinating and interfacing with a multitude of TPAs and trustees/custodians, including Voya.

Auditing Process, Project Planning, and Methodology

Another area of focus in the proposal evaluations related to understanding how each vendor plans and executes a financial audit. Staff’s review determined that both providers have similar approaches to project planning, audit methodology, and audit execution. The steps to an overall audit process generally include (1) investing time in understanding the structure of the City’s Plan; (2) designing and developing, in coordination with City staff, an appropriate audit plan and timeline; and (3) executing the audit.

Relative to audit execution, both vendors communicated that this step includes coordinating and interfacing with the Plan’s TPA and City Staff to request, for test and validation, pertinent financial statements/documents relative to Plan transactions. Crowe communicated that they

currently have available a proprietary web portal/tool that can be utilized by City staff and TPA staff for facilitation of efficient and secure data exchanges while also providing, through a written communications log, a means for clients to monitor activity throughout the audit process. TWHC emphasized their commitment to protecting sensitive data and explained their established security protocols, systems encryption, and security practices currently in place to protect the storage, transmission and deletion of confidential client data.

Crowe and TWHC communicated that in execution of an audit, the different types of Plan transactions and processes that are validated include participant eligibility, auto-enrollments, contributions, distributions, loans, hardships, Qualified Domestic Relations Orders (QDROs), contribution changes, and participant investment valuations. Validation testing would entail randomly extracting appropriate sample sizes, which can range anywhere from 20 to 60 participant records. An audit will also include an auditor review of a TPA’s Service Organization Control (SOC) 1 report, which is an external auditor report on a TPA’s internal controls over financial reporting. A SOC 1 report from Voya would basically provide the Plan assurance that their internal controls are designed appropriately to serve the needs of the Plan.

Although both vendors displayed similar approaches in process, planning and methodology, Crowe’s advantage in this area ultimately stems from their larger defined contribution plan and public sector auditing experience. The dialogue which occurred during the performance exam suggested that this experience would likely provide greater opportunities for the City and Crowe to proactively engage on not merely execution of the audit but also related DCP functions that could help to improve and evolve operations.

Staff noted in the RFP the Plan’s change in its TPA effective October 1, 2017 and requested recommendations, if any, from respondents regarding incorporating a review of the transition data to validate the proper transfer and reporting of assets. Crowe and TWHC both indicated that they could, in accordance with their normal auditing procedures, administer transactional validation testing and a review of financial statements for the transition.

Compensation, Performance Guarantees, and Contract Term

TWHC’s scoring advantage in this category is attributable to a moderately lower annual price proposal. The proposed fees are inclusive of all costs related to the audit engagement, including travel, meetings, and report copies. In addition to TWHC’s proposed annual project fee, they indicated that they may add mileage cost from their local office as well as parking expenses as allowed. A comparison of the fee proposals is indicated as follows:

Year	Crowe LLP	TWHC
Year 1	\$45,000	\$40,770
Year 2	\$45,000	\$41,585
Year 3	\$47,000	\$42,417
Year 4	\$47,000	\$43,265
Year 5	\$47,000	\$44,131
TOTAL-->	\$231,000	\$212,168

Over five years, Crowe’s price proposal is approximately 8% higher than TWHC’s. TWHC provided a performance guarantee in their proposal that places their engagement fee at risk of a 10% reduction for every week a reporting deadline is not met. Crowe indicated in their proposal that they are open to a performance guarantee tied to the timing and delivery of reports or other performance criteria, but did not offer more specific information.

C. Audit Frequency

As indicated previously, the practice of providing ongoing financial audits, particularly for larger plans, appears more commonplace than the last time an audit was performed for the DCP. Moreover, the size and complexity of the DCP’s financial transactions have grown significantly since the 2003 audit, as indicated by several data comparisons provided in the following table:

Data Metric	Year-End 2003	2018 (through 3rd quarter 2018)
Total Participants	33,528	46,488
Contributing Participants	25,141	32,288
Assets	\$1,737,260,679	\$6,623,087,594
Outstanding Loans	N/A	19,318
Roth Contributions	N/A	\$23,371,110
Annual Payroll Contributions	\$141.6 million	\$199.4 million

Transaction volumes will only continue to grow in coming years. Institutionalizing an annual audit process will ensure the highest level of validation of work processes and financial transactions, assist the Board and staff in ongoing monitoring and identifying opportunities for improving oversight, and provide assurance to DCP participants that their accounts are being properly administered.

The DCP Reserve Fund has adequate resources to fund annual audits. As indicated separately in Board Report 18-54, the projected long-term surplus for the Reserve Fund is substantially above the target amount. Staff therefore recommends that the Board provide for annual DCP audits under the service contract.

D. Contract Term

Under Los Angeles Administrative Code Section 10.5(a), the Board has the authority to enter into contract terms of up to five years in length. Given that this is a new service provider relationship, staff recommends that the Board establish an initial term of three years with an option for the Board to extend the contract for up to two additional years.

E. General Contracting Requirements

Both vendors indicated they are able to comply with the City’s general contracting requirements, including the Standard Provisions.

F. Conclusion

Following staff’s evaluation, staff recommends that the Board (a) approve the selection of Crowe LLP (Crowe); (b) instruct staff to negotiate a contract with a three-year term incorporating annual audits; and (c) authorize the Board Chairperson to execute said contract on behalf of the Board, subject to agreement between the City and the provider as to all applicable terms and conditions and all necessary approvals. Approvals include from the office of the Mayor and City Attorney.

Submitted by: _____
Matthew Vong

Approved by: _____
Steven Montagna

Attachment A

Financial Auditing Services RFP

City of Los Angeles Deferred Compensation Plan

Organizational Background and Reliability

100 Points Possible



- Privately held public accounting, consulting, and technology firm headquartered in Chicago, Illinois.
- Over 75 years of auditing experience.
- Serves over 11,000 clients.
- Indicated their 2016, 2017, and 2018 FY revenue to be approximately \$700, \$800 and \$850 million respectively.
- Not a subsidiary or affiliate of another company.
- Indicated they have not undertaken any material divestures in the past three years.
- Indicated that within the past three years, they have seen personnel from other entities join their ranks due to acquisitions of other firms.
- No substantial changes in senior management in the past five years.
- Average tenure of employees is 12.5 years.
- Maintains a management philosophy that defines success as having a thorough understanding and being responsive to the needs of the client, the individual and the firm. Indicated that no hierarchy is placed among the needs of each stakeholder.
- Indicated that no services solicited in this RFP will be sub-contracted to other firms.

81 Points



- TWHC has provided auditing, consulting, and tax services to financial institutions, small businesses, and government agencies for over 30 years.
- Local in scope and headquartered in Burbank, CA.
- Serve over 150 financial institutions, non-profits and government agencies in audit and consulting.
- Serve over 1,000 individual estate and small business clients.
- Past three calendar year revenues were \$6.2, \$6.5, \$6.8 million respectively.
- Not a subsidiary or affiliate of another company.
- A BDO Alliance USA member. This is an association of accounting and professional service firms that TWHC indicated provides them with more technical resources
- Average tenure of senior management is 15 years.
- TWHC's strategic plan involves focusing their business on industries including governments, benefit plans, credit unions, and nonprofits.
- Indicated their firm does not plan on outsourcing or subcontracting any of the services solicited.

76 Points

Regulatory & Contractual Actions

50 Points Possible



- Indicated that Crowe, its partners, managers, and/or other key staff members have not been subject to any disciplinary action in the past five (5) years with the state board of accountancy or other regulatory authorities.
- Indicated their firm has been subject to claims from time to time, however, it is their policy not to discuss pending litigation.
- Indicated that they have been subject to contract disputes or issues where contracts may be terminated for a variety of reasons including lack of client funding, disputes over the scope of work, or payment disputes. They did not site specific examples.
- Indicated they never filed for or petitioned into bankruptcy or insolvency.
- Indicated they have a dedicated unit within their organization (ethics and independence group at their firm's national office), which is responsible for managing and communicating independence and ethics guidance and firm protocol.
- Indicated all their professional personnel follow rules and regulations of the American Institute of Certified Public Accountancy (AIPCA), the SEC, U.S. Government Accountability Office, and other regulatory agencies.

42.5 Points



- Indicated that TWHC, its partners or staff have never been subject to disciplinary actions by any regulatory authority.
- Indicated they have no pending claims or litigation, however a lawsuit was settled in December 2015, the terms of settlement of which are confidential.
- Indicated they have never engaged in judicial or administrative litigation against a client.
- Indicated they have never had a contract terminated for default (notice to stop performance due to organization's non-performance or poor performance).
- Indicated they have never filed or petitioned into bankruptcy or insolvency.
- Indicated it is their policy that all professional personnel understand and adhere to the independence, integrity and objectivity rules, regulations, interpretations and rules of the AIPCA, the State of CA, Board of Accountancy, the State of CA CPA society, and state statutes.

49 Points

Client Reviews

50 Points Possible



- No major issues or concerns were communicated regarding Crowe's services.
- No problems or concerns regarding Crowe being able to meet deadlines.
- Strengths include that they provide regular status. updates and proactively address any areas of concern
- Easy to work with.
- Professional.
- Crowe provides a good web portal that can be utilized for communications.

50 Points



- No major issues or concerns were communicated regarding TWHC's services.
- Knowledgeable in conducting private sector plan audit.
- No problems or concerns regarding TWCH being able to meet deadlines.
- Good communication.
- Proactive in communicating issues.
- Auditor went above and beyond duty in providing corrective advice and solutions.

50 Points

Auditing Experience and Client Services

500 Points Possible



- Crowe has provided auditing services for over 75 years
- Over 1,000 employees focus on auditing.
- Government services team consists of 200 individuals that serve thousands of governmental organizations nationwide.
- Indicated they have an employee benefit plan audit practice and audit more than 1,200 plans annually, 900 of which are defined contribution (DC) plans. 100 plan audits were in CA, nearly all of them being DC plans.
- Indicated they are specialized in auditing defined contribution, defined benefit, and health and welfare plans.
- Currently provide auditing services to over 3,400 clients.
- Provided an extensive client list, which includes the following public sector clients: CA State Teachers Retirement System (CALSTRS) and Cities of Los Angeles, Anaheim, Beverly Hills, Burbank, Long Beach, and Santa Monica.
- Have local office in Sherman Oaks.
- Have substantial experience preparing draft financial statements in accordance with the reporting and disclosure requirements under generally accepted accounting principles (GAAP).
- Provided an extensive list of Third-Party Administrators (TPA) with whom they do business in conjunction with institutional clients; the list includes the DCP's current TPA, Voya.

485 Points



- TWHC has provided auditing services for over 30 years.
- 30 employees dedicated to financial audits.
- Currently have over 100 clients for whom they perform audits.
- Notable public sector clients they currently provide auditing services include City of Los Angeles, Office of Finance and Los Angeles Convention Center.
- Currently performs 401(k) and defined benefit auditing services for 30 clients.
- Have local office in Burbank, CA.
- Indicated auditors will be made available anytime as needed as they are close in proximity.
- Did not indicate in their response any defined contribution TPAs and trustees/custodians they currently work with.

374.5 Points

Compensation and Performance Guarantees

200 Points Possible



- **Year 1:** \$45,000.
- If contract is extended, the annual fee would increase as follows:
 - Year 2:** \$45,000
 - Year 3:** \$47,000
 - Year 4:** \$47,000
 - Year 5:** \$48,750
- Indicated that they reserve the right to revise fees if there is a significant change in the Plan's organizational structure or size due to acquisitions or other events.
- Confirmed the proposed annual fees are inclusive of the cost of travel, meetings, and report copies.
- Indicated that they are agreeable to offering a performance guarantee tied to the timing and delivery of reports or other performance criteria, but did not further detail.

178.5 Points

- **Year 1:** \$40,770 (plus mileage from Burbank office and parking expenses as allowed).
- 2% increase in annual fee if contract is extended to:
 - Year 2:** \$41,585
 - Year 3:** \$42,417
 - Year 4:** \$43,265
 - Year 5:** \$44,131
- Indicated that there are no known exceptions or qualifications to their proposed fee.
- Confirmed the annual fees presented are inclusive of the cost of travel, meetings, and report copies.
- Guarantee on-time delivery of deliverables if requested information has been provided timely. Should a deadline be missed, the engagement fee will be reduced by 10% for every week that it is late.

185 Points

Performance Exam

100 Points Possible



- Attendees from Crowe included Audit Managing Director, Jen Aras and Manager, Joseph Trone.
- Provided a detailed overview of their auditing process, which includes investing time to understand the City's Plan and subsequently designing appropriate and effective auditing procedures.
- Their project plan steps include meeting with management to determine the engagement timeline; and coordinating with the TPA and City for information requests relating to plan transactions that are to be tested.
- Indicated a DCP audit would include testing and validating participant enrollments including auto-enrollment; contributions; and distributions including QDROs, hardships; loans, and participant investment valuations.
- Indicated they have a proprietary and secure online web portal that can enable DCP and TPA staff to communicate with Crowe's audit team and securely exchange information as well as stay informed of audit process.
- Have extensive experience in auditing defined benefit and defined contribution plans.
- Indicated they have interfaced with multiple recordkeepers, including Voya, in requesting information and audit packages.
- Audit process would include a review of Voya's Service Organization Control (SOC) 1 report (report on internal controls over financial reporting).
- Capable of validating transfer of assets relative to the TPA transition.

50 Points



- Attendees from TWHC included Managing Partner, Kian Moshirzadeh, Director and Project Manager, Golnaz Kia, and Director and Field Services Supervisor, Dan O Shea.
- In administration of a Plan audit, TWHC indicated their transaction testing would include: participant eligibility, contributions, distributions, loans, QDROs, hardships, deferral changes, investment changes, change in interest rates, and auto-enrollment.
- Indicated their auditing process would include reviewing the Plan document in order to understand all the rules which govern the Plan's transactions.
- Emphasized their firm's commitment to protecting sensitive and confidential client data. Described the security protocols, systems encryption, resources, and practices in place that protect the transmission, storage, and deletion of confidential data.
- Cited their experience in working with multiple banks and credit unions.
- Indicated they have experience working with recordkeepers in requesting information and audit packages.
- Audit process would include a review of Voya's Service Organization Control (SOC) 1 report (report on internal controls over financial reporting).
- Capable of validating transfer of assets relative to the TPA transition.

45 Points

Final Scores

1,000 Points Possible



887 Points



784.5 Points