



M E M O R A N D U M

Date: December 3, 2008

To: California State Lottery Commission

From: Joan M. Borucki
Director

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Internal Audits

Subject: Item 9(c) – KPMG LLP Contract Extension for Financial Services

ISSUE

Should the California State Lottery Commission (Commission) exercise the two one-year options to extend contract number 10564 with KPMG LLP (KPMG) for an additional two years and add necessary expenditure authority to the contract to cover that period for financial auditing and related services?

RECOMMENDATION

Staff recommends that the Commission approve an extension of the current financial auditing and related services contract with KPMG for an additional two years and add \$289,500 in expenditure authority.

BACKGROUND

The California State Lottery Act requires that the California State Lottery (Lottery) contract with an independent certified public accounting firm to conduct an annual audit of all accounts and transactions of the Lottery. Government Code Section §8880.43 requires that the Lottery's audited financial statements be presented to the Commission, the Governor, the Controller, the Treasurer, the Attorney General and the Legislature not more than 120 days after the close of the fiscal year. The fiscal year ends June 30; with the audited financial statements due October 31.

Since January 1, 2006, the Lottery has contracted with KPMG to provide financial audits and other services. In addition, KPMG provides, upon request, other accounting consultation related to financial matters.

The current contract with KPMG began on January 1, 2006 and will expire on December 31, 2008. The contract includes the provision that, "The Lottery may unilaterally extend the term of the contract for up to two additional one-year terms under the same terms and conditions." The total dollar amount of the original contract is \$675,950. The current contract has an escalation rate of six percent per year.

DISCUSSION

The Lottery has been satisfied with the services provided by KPMG. Audit reports and other services have been received timely and professionally. KPMG has assisted the Lottery in meeting its deadlines on the financial statement audits as well as giving independent and objective assurances that its fiscal responsibilities are sound.

The Lottery discussed the option of unilaterally extending the contract for one year with KPMG. However, during discussions, KPMG requested that the two one-year options be exercised concurrently. KPMG agrees to a nominal three percent increase for the next fiscal year, and to no increase for the following fiscal year. In addition, KPMG will agree to keep the hourly rates the same as those included in the contract for the 2007/2008 fiscal year with respect to agreed upon procedure reviews. The current contract has KPMG receiving an increase of six percent each of the past three years.

Exercising the two one-year options concurrently with KPMG will allow the Commission to take advantage of a nominal three percent increase compared to past years at six percent and secure KPMG for a second year with no additional increase. Also, the Commission will receive uninterrupted service for the coming year ensuring that annual financial audits will be satisfied on time.

With the approval of these extensions, and the additional \$289,500, the contract term would be extended to December 31, 2010 and bring the total contract expenditure authority to \$965,450.