



John Arntz
Director

Memorandum

To: Honorable Gavin Newsom, Mayor
Honorable Members, Board of Supervisors

From: John Arntz, Director of Elections

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Date: October 31, 2006

RE: Update on Request for Proposal for Implementation of New Voting System in 2007

This memorandum provides an update on the Department of Elections' (Department) efforts to secure a contract to provide voting systems and services for use in San Francisco after the November 2006 election.

WHY THE DEPARTMENT NEEDS A NEW VOTING SYSTEMS CONTRACT

The Department of Elections issued an RFP on March 31, 2005 seeking bids from all vendors with voting systems certified for use in California by the Secretary of State to provide the City with voting equipment and services for at least a four-year period. The contract negotiations under this RFP have not yet been completed for the reasons stated below and the contract with the current voting system vendor, Elections System and Software (ES&S), effectively expires at the completion of services necessary to conduct and certify the November 2006 general election.¹ Therefore, the City must secure a contract for services to be used in future elections.

NEGOTIATIONS WITH SEQUOIA VOTING SYSTEMS

After the March 2005 RFP was issued, of the seven qualified vendors, two vendors submitted bids by the June 3, 2005 deadline: Sequoia Voting Systems (Sequoia) and ES&S. After panel review, scoring of the bids and a two-week pilot program during which the public was invited to use and compare the two systems, Sequoia was the top-ranked bidder and received the privilege to negotiate a contract with the City.

On September 30, 2005, the Department sent Sequoia a letter of intent to negotiate a contract and soon thereafter the Department entered good faith contract negotiations with Sequoia. As noted in the attached memorandum of March 7, 2006, the Department of Elections, upon consideration of concerns expressed by members of the Board of Supervisors' Rules Committee regarding the efficacy of completing the process to finalize Sequoia's contract, temporarily suspended efforts to finalize the contract. One concern expressed by the Committee was that Sequoia had not yet been certified by the

¹ Although the City's contract with ES&S expires on July 31, 2007, the contract only provides for voting services through the November 2006 elections. Furthermore, the Secretary of State has granted only a provisional certification for ES&S' system to conduct ranked-choice voting elections (RCV) for the November election. This provisional certification disallows ES&S' present equipment from being used in San Francisco to conduct RCV elections after this November.

Secretary of State for the June 2006 election. The vendor, however, had progressed through each phase of both the federal and State testing protocols and ultimately received certification from the Secretary of State in time for the June election.

In order to conduct the June 2006 primary election and to be in compliance with the federal Help America Vote Act (HAVA) to have accessible voting equipment in each polling place, the Department amended its existing contract with ES&S. This contract amendment was meant only as a temporary solution for the immediate elections. The Department continued discussions with Sequoia and encouraged Sequoia to continue to pursue the development and certification of RCV for its system. Without a contract, however, Sequoia was not able to commit the resources necessary to complete RCV in time for the November 2006 election when the ballot would contain RCV contests for both citywide and district offices. Throughout this time the RFP process remained intact and the Department of Elections continued discussions with Sequoia regarding finalizing a contract under the RFP process for future elections.

At this time, the Department of Elections is nearing the final stages of negotiations with Sequoia for comprehensive services related to the implementation of the new system. The Department expects to reach a final agreement soon and bring the contract to the Board of Supervisors for its approval.

FUNDING

The RFP requires the City to use funds provided under the Help America Vote Act (HAVA) and from Proposition 41 to purchase the new voting system.

Originally, the HAVA and Proposition 41 funds allocated to San Francisco consisted of \$5.7 million from each source, for a total funding amount of \$11.4 million. In 2003, the City used \$2.4 million in Proposition 41 funds to reimburse costs associated with the 2000 purchase of an optical scan system from ES&S.

For all elections after January 1, 2006, San Francisco, like all jurisdictions, had to comply with the HAVA requirement that at least one accessible voting machine be available in every polling place. Because the City was not able to complete the contracting process with Sequoia before the June 2006 election, the City contracted with its existing vendor, ES&S, to purchase accessible voting machines, called the AutoMARK.

On March 21, 2006, the Board of Supervisors passed a resolution authorizing the Department of Elections to accept and expend funds provided under HAVA and Proposition 41 in an amount not to exceed \$3.5 million from the California Secretary of State to purchase the AutoMARK for use in the June 6, 2006 election. S.F. Res. 156-06. The total cost of the purchase of the AutoMARK, including the sales tax, amounted to \$3.8 million. The Voting Modernization Board (VMB), which allocates Proposition 41 funds to the counties, awarded San Francisco \$2.6 million for the purchase of the AutoMARK and required San Francisco to provide an additional 25% of this amount in matching funds, amounting to approximately \$900,000. The City indicated that the required matching funds of \$900,000 would be drawn from the \$5.7 million of HAVA funds allocated to San Francisco from the Secretary of State for the purchase of new voting equipment. This total amounted to \$3.5 million and the City earmarked the remaining balance of \$300,000 to be paid by using HAVA funds.

With \$1.2 million in HAVA funds directed towards the purchase of the AutoMARK, the City has \$4.5 million remaining from its HAVA allocation. Further, of the original \$5.4 million of Proposition 41 funds allocated to San Francisco, approximately \$928,000 remains. Therefore, the City has approximately \$5.4 million in remaining federal and State grant funds to purchase the Sequoia system.

Any contract with Sequoia will require the vendor to provide a rebate for the City's current voting system, including the AutoMARK. The Department will use this rebate plus the remaining \$5.4 million in HAVA and Proposition 41 monies to fund the purchase of a new voting system from Sequoia under the RFP.² If the projected expense of the Sequoia system is greater than the total amount of these funds, the Department will ask the Board of Supervisors for a supplemental appropriation from the General Fund to cover the cost difference.

BOARD ACTIONS REQUIRED

In order to secure a contract with Sequoia, the top bidder in the RFP process, the Department will seek three actions from the Board of Supervisors.

- First, the Department will ask the Board to pass a resolution authorizing the Department of Elections to accept and expend the remaining monies from the HAVA grant, approximately \$4.5 million. As noted above, the Board passed an initial resolution authorizing the Department to accept and expend up to \$3.5 million in combined HAVA and Proposition 41 funds. In addition, on August 15, 2006, the Board of Supervisors passed a resolution approving the application of funds under the Help America Vote Act. S.F. Res. 0497-06. The Board now needs to pass another resolution authorizing the Department to accept and expend the remainder of the HAVA funds.
- Second, if the contract with Sequoia for voting systems and services exceeds \$10 million, the Department will ask the Board to pass a resolution approving the contract. S.F. Ch. § 9.118(b).
- Finally, if there is a shortfall in the amount the Department receives from HAVA and Proposition 41 funds and the sale of the AutoMARK, then the Department will seek a supplemental appropriation from the Board of Supervisors.

QUESTIONS REGARDING SEQUOIA'S CORPORATE STRUCTURE

Recent attention of Sequoia's parent company, Smartmatic Corp., has resulted in both companies requesting a federal review of their ownership structures by the Committee on Foreign Investment in the United States (CFIUS), which is an inter-agency committee chaired by the Secretary of Treasury. Concerns have been raised that since Smartmatic Corp.'s principle owners are from Venezuela and the company provided voting equipment for Venezuela's recent presidential election while partnering with a small Venezuelan company named Bizta. Bizta received a \$200,000 loan from the Venezuelan government, and in return the government held a 28% stake

² Both the Proposition 41 funds and the HAVA funds have not yet been released to the City for the purchase of the AutoMARK. San Francisco is waiting for the California Department of Finance to submit an amended spending plan for HAVA allocations to a joint legislative budget committee requesting funds to be released. The State will not release the Proposition 41 funds until the matching funds from HAVA are available.

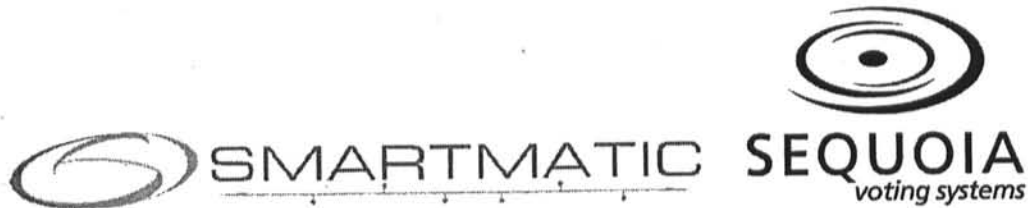
in Bizta. The nationality of Smartmatic Corp.'s principle owners and its association with Bizta has created worries that Smartmatic Corp. has potential links to the Venezuelan government that could allow Venezuelan President Hugo Chavez' administration to influence elections in the United States conducted on Sequoia equipment. In response to such concerns, Smartmatic Corp. and Sequoia requested SFIUS to review the companies' ownership and business structures for an official finding that the Venezuelan government does not hold any control over Smartmatic Corp. or Sequoia. At this time nothing suggests that Sequoia or its voting systems have in any way been designed or operated according to any influence from the Venezuelan government. Attached to this memorandum please find information from Sequoia regarding the investigation.

NEXT STEPS

The Department of Elections is continuing its negotiations with the top-bidder in the RFP process, Sequoia Voting Systems. We expect to complete these negotiations within the next several weeks and then work with the Board to receive approval of the contract and the necessary funds to complete the purchase of a voting system for use in future elections.

I would be happy to meet with you or your staff to answer any questions about the information provided in this memorandum or any other questions you may have about the voting systems and the City's need to secure a contract for future elections.

cc: Dennis Herrera, City Attorney
Ed Harrington, Controller
Steve Kawa, Chief of Staff, Mayor's Office
Noelle Simmons, Budget Director, Mayor's Office
Greg Wagner, Budget Analyst, Mayor's Office
Elections Commission



FOR IMMEDIATE RELEASE

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**SMARTMATIC AND SEQUOIA VOTING SYSTEMS ANNOUNCE
VOLUNTARY CFIUS FILING**

**SMARTMATIC CEO ANTONIO MUGICA TO HOLD PRESS
CONFERENCE**

BOCA RATON, FLORIDA, October 29, 2006 – Sequoia Voting Systems, Inc. (“Sequoia”) and its parent, the Smartmatic Corporation (“Smartmatic”), today announced that, contrary to reports, the companies have voluntarily submitted a notice to the U.S. Committee on Foreign Investment in the United States (CFIUS). The companies filed voluntarily in order to allow the U.S. Government to review Smartmatic’s acquisition of Sequoia.

“No foreign government or entity – including Venezuela – has ever held an ownership stake in Smartmatic, and we have voluntarily filed with CFIUS to put to rest the baseless but persistent rumors about our ownership,” said Antonio Mugica, Chief Executive Officer, Smartmatic.

The firm is owned primarily by three young entrepreneurs: Antonio Mugica, a dual-Spanish-Venezuelan national (78.8%); Alfredo Anzola (3.87%); and Roger Pinate (8.47%). The other main investor is Jorge Massa (5.97%), a well-known French-Venezuelan businessman. Smartmatic employees and friends and family own the remainder of the firm (2.89%).

As part of the CFIUS process, Smartmatic and Sequoia have voluntarily provided significant information to CFIUS on all aspects of the two firms’ businesses and ownership and the security and integrity of Sequoia’s voting solutions.

“As a company, we sought out a CFIUS review because we are confident it will clear the air so we can focus on what we do best – making the world’s most secure and auditable voting solutions,” added Antonio Mugica.

Press Conference: 2:00pm, Washington, DC, October 30th, 2006.

Smartmatic and Sequoia will hold a press conference tomorrow – Monday, October 30 – to present additional information on their voluntary filing, the company's ownership and operating structure and to take questions.

The press conference will be held at Sutherland Asbill and Brennan LLP, 1275 Pennsylvania Avenue NW, Washington DC 20004 at 2:00PM, Monday, October 30th, 2006.

A call-in number for journalists will be distributed tomorrow.

About Smartmatic (www.smartmatic.com) and Sequoia (www.sequoiavote.com)

Smartmatic and Sequoia are leaders in the provision of secure and reliable voting solutions and pioneers in the introduction of electronic voting systems with a Voter Verifiable Paper Audit Trail.

A privately-held, independent corporation with 300 employees worldwide, Smartmatic is an international leader in the provision of secure, reliable and auditable voting systems.

Sequoia Voting Systems is an American company, based in Oakland, California with a 100-year history of providing accurate, reliable, state-of-the-art voting solutions dating back to the nation's first lever-based mechanical voting equipment in the 1890s. Sequoia provides election technology, services and support to state and local government including precinct-based optical scan ballot readers, high-speed central count optical scan ballot readers, ballot layout and printing services, and full-face and paginating electronic voting equipment with optional printers that produce voter verifiable paper records. The company has hundreds of customers throughout the country and its voting equipment will be used on November 7th, 2006 in 16 states plus the District of Columbia.

Sequoia has been providing electronic voting equipment for twenty-five years and leads the industry with our AVC Advantage full-face push button electronic voting system and the AVC Edge touchscreen system.

Sequoia - Smartmatic Questions and Answers (THIS IS MATERIAL PROVIDED TO OUR CUSTOMERS BY SEQUOIA)

This Q&A provides an overview of the acquisition of Sequoia Voting Systems Inc. (“Sequoia”) by Smartmatic Corporation (“Smartmatic”).

Who is Sequoia?

Sequoia is a 100 year old American company which has a successful record of providing reliable voting systems and services. Sequoia currently has clients for its voting machines in 16 states and the District of Columbia, including California, New Jersey, Nevada, Colorado, Florida, Louisiana and Washington.

Sequoia is based in Oakland, California with major offices in New York and Colorado.

Sequoia was the first U.S. company to successfully implement an electronic voting system with a Voter Verifiable Paper Audit Trail (VVPAT) utilized on our AVC Edge line of electronic voting equipment. This technology was used successfully throughout Nevada beginning in the November 2004 election.

Sequoia’s senior managers, including its CEO, are U.S. citizens; most of its workforce is also comprised of U.S. citizens and permanent residents.

Who is Smartmatic?

Smartmatic is a privately-held, independent corporation which is an international leader in the provision of secure, reliable and auditable voting systems.

No foreign government or entity – including Venezuela – has ever had an ownership stake in Smartmatic. Smartmatic has an international ownership structure comparable to other multinationals, such as Shell, which allows Smartmatic to function efficiently and effectively in different markets and regions around the world. The use of Netherlands and Netherlands Antilles corporate entities for their businesses is standard operating procedure in the international business arena.

The firm is owned primarily by three young entrepreneurs: Antonio Mugica, a dual-Spanish-Venezuelan national (78.8%); Alfredo Anzola (3.87%); and Roger Pinate (8.47%). The other main investor is Jorge Massa (5.97%), a well-known French-Venezuelan businessman. Smartmatic employees and friends and family own the remainder of the firm (2.89%).

The three primary owners, like other families, have created personal trusts (foundations) and own their interests in Smartmatic through these trusts. These trusts are standard vehicles for the ownership and transfer of assets and there are no undisclosed third party beneficiaries of these trusts. The beneficial interests are all held by the primary owners and their families.

When was Sequoia acquired by Smartmatic?

In March 2005, Sequoia was purchased by Smartmatic for \$16 million. This merger brought together two of the world's leaders in providing election solutions and services. Prior to its acquisition by Smartmatic, Sequoia was owned by two foreign companies – U.K.-based De La Rue and Dublin-based Jefferson Smurfit.

How does Sequoia and U.S. citizens benefit by its merger with Smartmatic?

The public trust in the U.S. election systems, including electronic voting systems and Sequoia's future success, depends upon the provision of auditable and reliable voting systems of which Smartmatic is a world leader. Smartmatic has enhanced Sequoia's R&D capability and is committed to grow its business and add jobs to the U.S. economy. Smartmatic recognizes that its success in the marketplace is tied to its ability to provide secure and effective voting solutions to its customers.

Why is CFIUS involved?

Sequoia and Smartmatic voluntarily submitted a notice to the Committee on Foreign Investment in the United States (CFIUS) in order to allow the U.S. Government to review the merger and determine whether the acquisition of Sequoia by Smartmatic presents any national security concerns in the United States.

Sequoia and Smartmatic elected to submit a voluntary notice to allow the U.S. government to review and put to rest the unfounded press allegations about Smartmatic's ownership. Smartmatic/Sequoia have nothing to hide and have provided full information to CFIUS on anything about the two firms' businesses.

CFIUS is doing a very thorough investigation. The companies have provided thousands of pages of documents, provided its officials for discussions/meetings, and has answered many written questions. Sequoia has provided detailed, sensitive documents on its software and reports of independent testing agencies.

Sequoia and Smartmatic have co-operated fully with the U.S. government with respect to their merger and both companies are committed to satisfying all legitimate concerns raised by CFIUS in connection with its review of the acquisition.

Why should this transaction be permitted to proceed?

Sequoia has a successful record of providing reliable voting systems and services while under foreign ownership for 24 years. Sequoia has successfully provided voting solutions while under the ownership of Smartmatic Corporation for the past eighteen months.

Sequoia does not manage elections or tabulate votes. State and local governments do. It only provides the voting machines and support services.

There is no foreign government ownership or control over or involvement in Sequoia or Smartmatic, direct or indirect.

Sequoia and Smartmatic have an exemplary security record.

- There are no substantiated allegations of tampering with voting results on Sequoia or Smartmatic equipment.
- There are no formal investigations against either company (past or present).
- There have been no civil/criminal fines levied against either company for fraud.
- Customers have been pleased with the performance of Sequoia's voting systems.

The acquisition of Sequoia by Smartmatic poses no national security risk. Numerous robust checks and balances ensure the security and accuracy of Sequoia voting machines used in this election cycle and preserve and enhance the integrity and transparency of our elections. *There are multiple, independent tests, reviews and procedures for certifying and approving use of Sequoia's voting systems at federal, state and local levels which prevent the use of malevolent code or other actions that affect the counting of votes.*

- **Virtually all of Sequoia's voting systems in use in the November 2006 election cycle have been certified to be in compliance with rigorous federal standards adopted in 2002 (The word "virtually" is used because this is dependent upon individual state requirements for certification.).** This includes Sequoia's Edge2Plus (used in Chicago/Cook County) and HAAT device (used in Chicago/Cook County and limited jurisdictions elsewhere), which were developed collaboratively by Smartmatic and Sequoia.
- **All of Sequoia's voting machines in use in the November 2006 election cycle are also certified by the states in which they will be used.**
- **Virtually all of Sequoia's voting machines in use this election cycle have been tested (component level, including source code, and end-to-end functional testing) by independent testing authorities (ITAs) certified by the National Association of State Election Directors. (Again, the word "virtually" is used because this is dependent upon individual state requirements for certification.).**
- **Sequoia products have robust built-in security features, including locks, data encryption, other security features built into system software, and authentication protection.**
- **At the local level, Sequoia's voting machines are subject to physical security and chain of custody rules** that limit access to the machines and ensure their integrity prior to and during elections; they are locked, sealed and secured until Election Day and not accessible by Smartmatic or Sequoia after their delivery to customers. Election security is not just about technology, but people and processes.

- Sequoia's voting machines also are subject to additional local testing and election day parallel testing to any problems or malfunctions.
- Sequoia's voting systems are stand-alone; they are not accessible over internet or through external ports. Thus, they are not subject to hacker vulnerabilities.
- Sequoia has submitted the executable code, support files and electronic signatures for all of its voting software and firmware in use this election cycle to the National Software Reference Library ("NSRL"). This allows any customer to conduct a comparison between federally certified software and software used in a specific system and would show if the software has been altered since its federal certification.
- The source code for all of Sequoia's software and firmware in use this election cycle has been or will be escrowed by election day with all states that require such escrow (either directly or with third parties designated by the states).
- Sequoia's internal assurance program, managed by a U.S. citizen who serves as the Vice President for Quality Assurance, offers additional protection, including programming security and anti-tampering, physical security and access at Sequoia sites, employee screening (pre and post hire), and security and quality assurance at manufacturing partners.

Weren't there allegations of vote tampering and other controversies involving Smartmatic during Venezuela's recent Presidential Recall Referendum?

Smartmatic SBC Consortium – Smartmatic, Bizta and CANTV – was selected by Venezuela to handle voting after competitive bidding by multiple teams. SBC bid offered security, transparency and auditability (paper trail) & cost savings; first ever use of voter-verified paper trail.

The National Electoral Commission conducted multiple tests to ensure accuracy & integrity of voting systems; Organization American States and multiple international bodies acted as witness.

The Carter Center's final report on the election put any allegations of tampering to rest: "The audit concluded the voting machines did accurately reflect the intent of the voters as evidenced by the recount of the paper ballots in a sample of machines ... The Center found no evidence of fraud."

Will foreign nationals from Venezuela or elsewhere participate in the upcoming election?

No foreign nationals working for or on behalf of Sequoia or Smartmatic will be at any polling places or operations/central count rooms where votes are tabulated. Under the direction of Sequoia's American management, a small number of foreign nationals will assist Sequoia at its offices and other sites in providing support to customers (answering technical questions that may arise).