

These are the minutes of the Texas Transportation Commission Audit Subcommittee quarterly meeting held on March 26, 2014, at 125 E. 11th Street, Austin, Texas 78701. The meeting convened at 1:30 p.m. with the following members present:

Audit Subcommittee Members:

Fred Underwood	Commissioner, Audit Subcommittee Chair
Jeff Austin, III	Commissioner, Audit Subcommittee Member

Administrative Staff:

Benito Ybarra	Chief Audit & Compliance Officer
John Barton	Deputy Executive Director
Jeff Graham	General Counsel
Bob Kaufman	Chief Communications Officer

A sign-in sheet listing others in attendance is on file with TxDOT's Audit Office.

A public notice of this meeting containing all items on the proposed agenda was filed in the office of the Secretary of State at 4:59 p.m. on March 18, 2014, as required by Chapter 551 of the Government Code, referred to as "The Open Meetings Act."

Opening remarks were made by **Commissioner Underwood**.

Item 1. Approval of Minutes from the February 19, 2014, Meeting

The Minutes were presented by Benito Ybarra, Chief Audit & Compliance Officer, and approved by the Audit Subcommittee.

Item 2. Approval of Chief Audit & Compliance Officer 2014 Performance Plan

The Plan was approved.

Item 3. External Quality Assessment/Peer Review Results

The Audit Office is audited every three years by an external entity, as required by Professional Auditing Standards. The AASHTO Peer Review Committee performed the external quality assessment/peer review for FY 2013. The Audit Office received the highest possible rating: *Pass/Generally Conforms*. One finding was identified by AASHTO; it indicated the need to finalize the audit policy manual; all other observations relate to documentation issues.

A discussion ensued about the need for improved record keeping of the continuing education credits for auditors. When asked by **Commissioner Austin**, Mr. Ybarra stated that existing HR software is not set up to accommodate profession-specific continuing education records. **Commissioner Austin** asked DED John Barton how engineers record their continuing education requirements and called for the process to be kept as simple as possible.

Mr. Barton joined **Commissioner Austin** in underscoring that TxDOT staff is the Department's greatest asset; however, a central repository for continuing education records is not currently available.

Mr. Barton suggested that offices with professional education/certification requirements explore when it is more efficient to bring in a trainer rather than send multiple employees to the same event.

Another observation addressed the fact that TxDOT's final audit reports contain a *Management Action Plan* but not the auditors' recommendation(s). While not a requirement, this does deviate from standard practice. The reason is that the corrective actions are more useful to the audited entity; recommendations would draw the focus away from the action. Also, recommendations are communicated throughout the process. **Commissioner Underwood** asked if the audit team ever accepted "corrected on site" as closure on an item, as this would show the entity's readiness to address the issue. Mr. Ybarra confirmed that this happens and is documented in the final report.

Mr. Ybarra pointed out that the remaining documentation issues stemmed from the fact that the Audit Office had purchased software to manage the audits while transitioning from e-mails and network folders. This meant that some of the documentation could not be produced as fluidly as should have been the case.

Commissioner Austin asked who else could conduct such a peer review (other than AASHTO). Potential reviewers could be the Institute of Internal Auditors; the Texas State Agency Internal Audit Forum, or consulting firms.

Commissioner Austin commented further that the reciprocal nature of the AASHTO peer review program also gives reviewers the opportunity to bring back good ideas from the entities reviewed.

Item 4. External Audits and Advisory Services for Discussion

a. Spirit of Sarbanes Oxley Disclosures Engagement

Tony Rose, External Audit & Advisory Services Section Director, offered a differentiation between audits and advisory services. The latter are conducted based on a request for assistance by management, within the parameters set by management – it is a service not an audit. It is conducted in accordance with the International Standards for the Professional Practice of Internal Audits (Red Book), with Generally Accepted Government Auditing Standards safeguards to eliminate/reduce threats to the independence of the provider of advisory services.

The Sarbanes-Oxley (SOX) disclosure project was one of seven scheduled advisory services for FY 2014 and had the purpose of collaboratively supporting the Finance Division and the Chief Financial Officer in developing and implementing the next phase of the Spirit of

Sarbanes-Oxley at TxDOT. The key deliverables were the development of a methodology to rate and rank key controls for testing and a proposal to adopt certain modifications to the “Spirit of SOX” requirements.

The next project is the SOX Controls Testing; planning is currently underway.

Benito Ybarra thanked the Commissioners for their support in having the Audit Office expand beyond its traditional role to one of partnering with management to further improve TxDOT.

Item 5. Spirit of Sarbanes-Oxley Update

Brian Ragland, Director of the Finance Division, introduced the newly appointed Manager of Financial Reporting, Stephen Stewart. Mr. Ragland explained that the essence of Sarbanes-Oxley (SOX) is quality internal controls that render financial information reliable.

Mr. Stewart then laid out the changes in the adaptation of the Spirit of SOX since the 2009 Minute Order 111785. Starting in FY 2014, these refinements were in place:

- the Financial Controls risk assessment identified 71 key controls, down from 304 in 2009.
- the implementation of a revised framework that will include annual risk assessment, control design evaluation, and rotating operational effectiveness testing. The CFO is charged with reporting the effectiveness results to the Audit Subcommittee and the Executive Director.
- this represents a reduction in the cost of implementation from \$650K to \$98K.

Commissioner Austin asked if the mention of cost was a request or just informational. Mr. Stewart responded that it was purely informational and Mr. Ragland added that the anticipated return on investment for the outlay is the increased reliability of TxDOT financial information and that outside auditors appreciate that TxDOT, unlike most other governmental entities, has such a program in place.

Commissioner Underwood observed that the implementation of the program highlights that TxDOT is a good steward of the taxpayers’ money.

Elements unchanged since the 2009 Minute Order are that the CFO (or designee) shall

- develop and implement an expansion to the practice of providing certifications of TxDOT financial reports.
- establish and maintain an adequate internal control structure, assess the effectiveness of the internal control structure, and report the results of the effectiveness testing to the Audit Subcommittee.
- develop a code of ethics for senior finance personnel.

Commissioner Austin asked why there was a need for a Code of Ethics for finance personnel and how it would differ from TxDOT's general Code of Ethics. Mr. Stewart explained that the need for the Code of Ethics stems from the fact that SOX assigns specific roles, responsibilities, and duties to senior finance professionals. The Code is to make those professionals aware of their specific responsibilities.

Mr. Stewart then listed the two recommended modifications to Minute Order 111785. The modifications remove broad and undefined language, reduce the certification requirements to the 71 key control areas, eliminate certification duplication, and make the Audit Subcommittee the recipient of the internal reporting. Overall, the modifications are to strengthen TxDOT's Spirit of SOX program and provide clarity in Finance's role in complying with the program.

Mr. Stewart provided a timeline for the next steps in the process:

- *April*: Development of the revised Minute Order as described earlier. (FIN)

In response to **Commissioner Austin's** interjection, Mr. Stewart explained that the process is a proactive approach to avoid the potential for "false impressions."

- *May*: Development of policies and procedures (FIN)
Testing of key controls (AUD)
Presentation of revised Minute Order to the Transportation Commission (FIN)
- *September*: Presentation of results of key control effectiveness testing to the Audit Subcommittee (FIN)
- *November*: Certifications signed by the Executive Director and the CFO.

Commissioner Underwood added that Sarbanes Oxley was designed for business, so refining is needed to make it applicable to government.

Commissioner Austin stated that the need for fine-tuning notwithstanding, the Spirit of SOX is still good and needed.

Mr. Ybarra summarized that the preceding presentation laid out what the plans are. Implied is the question by the Finance Division whether this is a feasible and reasonable approach that will result in changes to the Minute Order, and to make sure that this approach has been vetted and approved by the Audit Subcommittee.

Commissioner Austin agreed with the approach but wants to make sure that the terminology used reinforces that this is to further strengthen the Spirit of Sox program.

Mr. Ragland added that another large governmental entity working on the implementation of SOX is UT's MD Anderson in Houston. FIN and AUD staff spent a day with their counterparts at MD Anderson.

Commissioner Austin, referring to the mention of MD Anderson, asked if the UT System could perform a peer review on TxDOT. Mr. Ybarra confirmed that, indeed, they could.

Mr. Ybarra asked for the Audit Subcommittee's recommendation to proceed. The Audit Subcommittee gave the recommendation without further comment.

Item 6. Executive Session

An Executive Session was not deemed necessary.

Closing Comments

Commissioner Underwood stated that this concludes our agenda for today. The next Audit Subcommittee Meeting will be held on May 28, 2014, in Austin. The members thanked all for attending the meeting.

The meeting was adjourned at 2:13p.m.

APPROVED:



Commissioner Fred Underwood, Chair
Texas Transportation Audit Subcommittee