

These are the minutes of the Texas Transportation Committee Audit Subcommittee quarterly meeting held May 26, 2010, in Austin, Texas. The meeting opened at 10:04 a.m. with the following members present:

Audit Subcommittee Members:

Fred Underwood Commissioner, Audit Subcommittee Chair
Ted Houghton Commissioner, Audit Subcommittee Member

Administrative Staff:

Bob Jackson, General Counsel
Owen Whitworth, Audit Office

Registration sheets listing others in attendance are on file with the Texas Department of Transportation 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 11:47 a.m. on May 18, 2010, as required by Chapter 551 of the Government Code, referred to as “The Open Meetings Act”.

Opening remarks were made by Commissioner Underwood. This is the first meeting of the Audit Subcommittee.

Item 1. Discussion of expectations and content of quarterly meetings

Mr. Owen Whitworth, Audit Director, presented agenda Item #1, and the following decisions were made by the subcommittee members present:

Future Meetings will be held in the Delegation Room, First Floor, Greer Bldg.

The agenda preparation process will include preparation of a draft agenda to be reviewed by the Office of General Counsel, then the members of the Subcommittee at least ten days prior to the meeting, and based on their approval, posted to the office of Secretary of State’s website. Routing the draft agenda through the Government and Public Affairs division, as done with regular commission meetings, was determined unnecessary.

Regular attendees at future meetings include the Audit Subcommittee, Deputy Executive Director, Audit Director, General Counsel, select Audit staff members, and auditees. The State Auditor’s Office will be invited to attend the meetings and will interact with the Subcommittee on an as needed basis. It was noted that a member from the SAO was present at this meeting.

Meetings will be taped and a set of minutes prepared. Upon approval of the minutes by the Subcommittee, the tape will be obsolete.

Agenda items proposed for upcoming quarterly meetings were presented, including the need for all members of the Transportation Commission to review and approve of the Fiscal Year 2011 Annual Audit Plan in August.

Item 2. Audit Office Peer Review Update

The Audit Office is required to have a peer review every three years. The peer review has been carried out through AASHTO for the last several years through a

reciprocity agreement. However, the peer review was delayed because other DOTs had limited travel dollars. These budget constraints still exist so the peer review is being carried out virtually, using electronic tools to transmit audit files and information. The peer review is currently in a review phase and a report should be available in the near future. This peer review did not include a review of the district auditors, but the next review will. Effectiveness of the virtual peer review process was discussed as well as the possibility of implementing guidelines for AASHTO based on lessons learned.

A brief discussion took place on other options for obtaining a peer review. These options include entering into a reciprocity agreement with other state agencies in Texas, or hiring an outside firm. The State Auditor would have to approve the hiring of an external auditor.

Item 3. FY 2011 Annual Audit Planning Process Overview

The 2011 annual audit planning process has just begun. The process determines the routine internal and external audits planned for the upcoming fiscal year. The key components of the process include soliciting input from management and stakeholders (District Engineers, Division Directors, Office Directors, Regional Directors, FHWA), conducting a risk analysis of department operations, and assessing audit resources. Once the list of potential audit areas is defined, the Audit Office meets with Administration to obtain their input.

The Commissioners are then provided the opportunity to comment on the draft annual audit plan. The plan will be presented to the Audit Subcommittee at the August quarterly meeting with a request that you recommend full commission approval. The final approval will be done by Minute Order.

Changes to the approved audit plan have generally been approved by the Administration and communicated to the Commission. Most of the audit plan changes are fairly small and require the Audit Office to look into alleged improprieties. Both members of the Subcommittee requested that they be notified immediately when the Administration approves a change to the audit plan. It was also noted that the Subcommittee can request an audit be conducted at any time.

Item 4. Audit Restructuring Status

A workgroup was formed to find ways to show enhanced independence on the part of district and division auditors. Starting July 1st, the district, division, and regional auditors will be reporting directly to the Audit Office Director. Standard Operating Procedures (SOPs) and new performance plans were developed and will be presented at the Annual Audit Conference in June.

The concept of regionalizing the audit function was broached by Commissioner Houghton. Bob Jackson, General Counsel, commented that his understanding was that a district auditor had to reside in that district, but they can perform audits in other parts of the state, i.e., other districts. Commissioner Houghton also proposed the idea that auditors audit other districts on a rotational basis. There was a brief discussion about auditor turnover and the actual number of auditors in each district.

District auditors are now being assigned the task of auditing District Engineers from other districts. Mr. Whitworth reminded the Subcommittee that the internal auditors assigned to headquarters audit the entire state.

Some discussion took place on the audit function restructuring efforts. Mr. Whitworth clarified that the plan is to put in place some oversight of the district, division, and regional auditors; a quality assurance function and annual performance plans. Also, Mr. Whitworth is now responsible for filling any vacancies in those positions and will coordinate his efforts with the respective District Engineers, Division Directors, and Regional Directors. The auditors' salaries are still being paid out of the district/division/region budgets, but the possibilities of moving some of the administrative functions, such as payroll and computer system access, will eventually be examined.

Item 5. Internal Audits Completed During the March 2010 – May 2010 Quarter

There have been 5 audit reports issued this quarter. Each Auditor-in-Charge (AIC) presented information from their respective audit(s).

Paula Bishir-Jensen, AIC, presented the results of the *Statewide Letting Management* audit. The objective of the Statewide Letting Management audit was to determine if the program maintains a competitive bidding environment that has controls in place to identify eligible builders, develop accurate and timely monthly letting schedules, securely receive and process bid documents and to detect bidding irregularities.

Commissioner Houghton inquired as to whether the audit looked strictly at TxDOT or if it included the RMA functions of sister agencies. The basis of his question comes from the fact that RMAs use state and federal dollars. A Local Government Oversight audit in progress may include some of the RMA functions, but currently TxDOT has not directly audited an RMA.

The overall opinion of the letting program is that it is carried out in a fashion that meets all the criteria of the audit objective. There were some minor controls that were not functioning as intended but nothing major. Commissioner Houghton inquired about complaints from contractors or people that go through this process. There were no complaints that came to light during the audit.

Currently the submission of electronic bids is optional on the part of the contractor. The process of the electronic bids submission and opening was explained to the Subcommittee. The plan is to eventually have all contractors submit bids electronically because it is much more cost efficient.

Commissioner Houghton inquired about the reliability of the electronic bidding system. Confidence in the system is high and security appears to be strong. There are two exceptions. To date, a site visit has not been performed at the vendor location(s). The agreement signed with the vendor did not require them to have a SAS 70 Audit performed, which is an audit of their information systems.

Commissioner Houghton inquired as to whether the EBS vendor was bonded, and if so, to what level. The AIC will look into this issue.

Paula Bishir-Jensen, AIC, presented the results of the *Dispute Resolution Change Order* audit. A brief example of a dispute resolution change order was provided. The audit objective was to determine if there was sufficient documentation to ensure appropriate approval authority and compensation. The audit also looked for significant statewide patterns or trends.

The audit revealed there is no code for dispute resolution change orders, as is used for other change orders, which made it difficult to identify which change orders were actually dispute resolution change orders or identify potential trends. The districts requested training from the Construction Division (CST) for handling dispute resolution change orders and the required supporting documentation.

Commissioner Underwood inquired as to whether TxDOT audits to determine if one district has more change orders than another. The AIC responded that CST does track changes orders, but it's usually on a project basis. However, Site Manager affords CST the ability to track change orders right down to the Area Engineer.

Paula Bishir-Jensen, AIC, presented the results of the *American Recovery and Reinvestment Act* (ARRA) audit. The audit objective was to coordinate with the Federal and State ARRA auditors and the USDOT agencies to provide early compliance evaluations of the ARRA funds. Overall the Department had complied with the ARRA reporting requirements and deadlines. There were some minor issues that management addressed as they came up. Commissioner Underwood added that issues found during an audit should be followed up much sooner than the following year.

Mr. Whitworth explained the new audit follow up procedures for the Audit Office. The new procedures resolve the issue of lengthy time gaps between original audit findings and the follow up audit. Commissioner Underwood commented that he would like the Subcommittee to be immediately notified if a finding is not properly addressed within the specified time period.

Donna Roberts was the auditor-in-charge of the *DBE Certification and Compliance Function* audit. The audit was not part of the original fiscal year audit plan. Steve Simmons, Deputy Executive Director, asked that it be put on the audit plan after receiving TxDOT watch complaints alleging companies were falsely operating as DBE companies. Problems were found with that particular company, and they have since been decertified.

The audit shed light on problems with the certification process itself. The Office of Civil Rights (OCR) is responsible for the certification of DBEs. A sample of OCR certification files was reviewed and problems were found. FHWA had also reviewed the certification process once in 2005 and again in 2008, and found problems. Recommendations were made to strengthen the certification process.

It was noted that FHWA is pleased with the monitoring TxDOT performs with respect to its DBE program.

Lee Stone was the auditor-in-charge of the *TxSmartBuy* audit. The audit objective was to verify the increased cost of purchasing through TxSmartBuy versus using TxDOT purchase orders. The General Services Division (GSD) did an extensive analysis on what their costs were going to be using TxSmartBuy, and the auditors were able to verify those figures. It will cost TxDOT \$17 million more to use TxSmartBuy versus the current purchase order process. Since the audit, the State Comptroller has invited TxDOT to participate in revising the RFPs for the next round of contracting, and GSD is participating.

Mr. Scott Burford, GSD Director, briefly explained to the Audit Subcommittee the traditional purchase process and how TxSmartBuy entered the picture.

The Comptroller is going to refresh the TxSmartBuy contract to hopefully spread the risk between the state and contractors a little more equitably.

Commissioners Houghton and Underwood both agreed that buying a product locally at a cheaper rate was good. The problem arises when the price to haul the product to another location actually causes the end price to become higher.

Commissioner Underwood commented that we need more people involved in the process.

Mr. Burford emphasized that the business and operational needs of TxDOT were met during the initial implementation period.

Closing Comments:

Commissioner Underwood reiterated that he and Commission Houghton wished to meet with representatives from the SAO. The members thanked all for a productive meeting.

The meeting adjourned at 11:25 a.m.

APPROVED:



Commissioner Fred Underwood, Chair
Texas Transportation Audit Subcommittee