

SOUND TRANSIT AUDIT AND REPORTING COMMITTEE MEETING

**Summary Minutes
December 20, 2018**

CALL TO ORDER

The meeting was called to order at 11:03 a.m. by Committee Chair Rob Johnson, in the Ruth Fisher Boardroom, 401 South Jackson Street, Seattle, Washington.

ROLL CALL

Chair

(P) Rob Johnson, Seattle Councilmember

Vice Chair

(A) Bruce Dammeier, Pierce County Executive

Committee Members

(A) Nancy Backus, Auburn Mayor

(P) David Baker, Kenmore Mayor

(P) Joe McDermott, King County Councilmember

(A) Dave Earling, Edmonds Mayor

(P) Fred Auch, COP Chair

Paige Armstrong, Board Coordinator, announced that there was a quorum of the Committee present at roll call.

REPORT OF THE CHAIR

Mr. Johnson announced that this meeting is the last meeting of the Audit and Reporting Committee. The Board has taken action to update its Committee structure, and this committee will be sunsetted at the end of 2018. Mr. Johnson thanked Mr. Fred Auch, Citizen Oversight Panel Chair, for his service on this committee, and commented that the future Finance and Audit Committee will continue to engage the COP on a regular basis.

PUBLIC COMMENT

Alex Tsimmerman

BUSINESS ITEMS

Minutes of the September 20, 2018, Audit and Reporting Committee Meeting

It was moved by Boardmember McDermott, seconded by Boardmember Baker, and carried by unanimous vote that the minutes of the September 20, 2018, Audit and Reporting Committee Meeting be approved as presented.

AGENDA OVERVIEW

Tracy Butler, Chief Financial Officer, provided an overview of the meeting agenda. Ms. Butler commented that the State Auditor's Office has representatives in attendance, as they have recently released their exit report for the 2017 accountability audit. In addition, the agency has a newly selected financial auditor, Moss Adams, who has a representative in attendance to introduce their work for the coming year.

ANNUAL EXTERNAL REPORTING

State Accountability Audit Results

Kelly Priestley, Deputy Executive Director of Financial Operations, presented the State Auditors. Representatives from the state office included Joseph Simmons, Audit Manager, Sherry Chang, Audit Supervisor, and Sophia Sullam, Lead Auditor. The State Auditor's Office presented their findings from the 2017 agency audit.

Ms. Sullam presented the audit finding of a clean audit. The focus areas of the audit included credit card payments, vendor payments, procurement, the asset management system, and some payroll elements. The work of the other auditors, including the financial auditors and the federal auditors, was reviewed, and no issues were found. Ms. Chang commented that the State Auditor's Office will be working with the new financial auditors, Moss Adams, to queue up the audit for this year.

Financial Audit Entrance Presentation

Laurie Tish, Lead Client Service Partner for Moss Adams, provided the presentation. Moss Adams will be providing audit services for fairness of the agency's financial statements, internal controls, and compliance with Generally Accepted Accounting Principles and Government Accounting Standards. In addition, they will be auditing the data and reporting associated with the Federal Transit Administration National Transit Database.

Required communications relevant to these audits include a presentation regarding the scope and timing, which is the current topic, followed by a presentation of any significant audit findings, qualitative aspects of accounting practices, any issues or difficulties encountered while performing the audit work, any necessary corrections to reports or statements, and reporting on management consultations during the process.

Chair Johnson asked about Moss Adams' significant experience in auditing other transit agencies of a similar size to Sound Transit, and if this work will allow for Moss Adams to provide best practices and recommendations on internal controls and other audit topics, even where there isn't a significant finding but where there is room for strengthening. Ms. Tish responded that indeed, Moss Adams will be contributing advice and recommendations throughout the process, through consultations with management and staff, and using their experience to improve internal controls. She added that these recommendations will be included in audit reporting, even when they are not raised to the level of an audit finding.

Ms. Tish continued to explain Moss Adams' philosophy regarding materiality, which they define as a measure of the amount of misstatement that could influence the economic decisions of users, taken based on the financial statements.

The timing of this year's audit is on track for completion in May of 2019, and therefore representatives will be back at a second or third quarter meeting of the new Finance and Audit Committee to discuss any findings. Ms. Tish commented that Moss Adams is also performing audit services for the ORCA financial statements.

Citizen Oversight Panel Chair Fred Auch asked about the number of interviews typically conducted as a part of this auditing process. Ms. Tish responded that typically 8-12 members of management are interviewed, in addition to approximately 30-40 members of agency staff in general.

Boardmember McDermott asked about the guidelines and general approach that the agency has for subarea equity, and if Moss Adams' team found them to be clear and have a clear approach for auditing this work. Ms. Tish responded that yes, the team is feeling very comfortable with understanding the

nuance of subarea equity, and that the engagement letter for this particular focus area has been completed.

FINANCIAL REPORTING

Third Quarter Financial Performance

Ann Sheridan, Director of Budget, provided the report. Ms. Sheridan began by introducing a new element of the financial report, which is an abbreviated statement of net position. There have been new revenues in the third quarter, and revenue totals \$1.6 billion for the first three quarters of 2018. The revenue forecast for the year in total is \$2.3 billion. Restricted asset balances and cash have increased due to the timing of capital spending, and the spending will catch up to the higher revenue levels.

Chair Johnson paused the presentation to clarify that although revenues are up, and higher than expected, the bills to pay for the ST3 program are coming in higher than expected as well, and the rising revenue is still not on track to match the increased spending. Ms. Butler commented that that is accurate, higher costs mostly due to increased right-of-way acquisition costs and construction costs are putting pressure on the agency's financial capacity moving forward. Ms. Butler continued that with the formation of the new Finance and Administration Committee, there will be an increased role for Board members on risk management and financial capacity.

Ms. Sheridan continued with the financial presentation. The agency is overall under budget for the third quarter, which is in large part due to a higher than anticipated vacancy rate, timing of consulting services contracts, delayed agency-wide training costs, and lower maintenance security and expenses than anticipated for the Downtown Seattle Transit Tunnel (DSTT). These numbers are expected to increase in the fourth quarter, and it is predicted that the agency will come in at 94 percent of spending for the year overall.

Transit mode expenses are at 24 percent, and this underspending is in large part due to lower fuel costs than were budgeted, in addition to lower than anticipated fare collection and maintenance services. Most of this underspending is permanent savings. Ridership and fare revenue is up for year-over-year. Both Sounder and Link have experienced rider increases, and Tacoma Link and ST Express have experiences slight decreases.

Chair Johnson asked what comprises the revenue category 'other operating revenue.' Ms. Sheridan replied that that category is hitting over \$3 million in revenue when it was only predicted to bring in around \$2 million, and that this revenue is comprised of a large number of small sources including advertising, bike locker rentals, cell-service lease revenue, and property licensing and leasing.

Project spending is at 93 percent for the first three quarters, but is forecast to be at only 84 percent at the end of the year. This is due to a constraint on staff resources and the timing of right-of-way acquisitions, and the timing of some construction projects.

Link system expansion comprised 87 percent of all the project budgets, and this is in large part due to the East Link Extension Project, which is current at 116 percent for its budget for 2018. The enhancement and State of Good Repair (SOGR) budgets are at 25 percent at the end of the third quarter, and are forecast to be at 39 percent at year-end. Much of the underspend for the SOGR budget is due to the delay of replacement bus purchases which have been delayed to 2019.

Mr. Auch commented on the reporting for percent of year to date budget for various project spending, and asked if there may be a better indicator available for if an over or under spend is due to savings, schedule difficulties, or if there could be a qualitative indicator for the spending amounts.

Boardmember McDermott asked about the difficulties with property acquisition, and why that has been an area of underspending. Mr. Rogoff commented that the issue with this year for property acquisition was the expansive volume of parcels needing staffing for acquisition, and that issue has been remedied by increasing consulting contracts for resources for this need, and additionally increasing staffing for right-of-way acquisition.

Asset and Liability Management Report

Jessica Jaegar, Agency Treasurer, provided the report. The overall performance outlook is positive for the third quarter report of 2018. Agency investments total approximately \$2 billion, with \$1.5 of those dollars qualifying as unreserved. Debt is currently at \$3.2 billion outstanding, which included the first of the TIFIA Loan draws for the Northgate Link Extension in January of 2018, which totaled \$56 million. The agency has a newly adopted Asset and Liability Management policy, which was Board adopted in July of 2018, which is being implemented. Over \$150 million in variable rate bonds were successfully remarketed in July of 2018, which reduced some interest rate expense, and increased the agency's flexibility for future bond remarketing.

The four key performance indicators for Asset and Liability Management, Investment Performance, Interest Rate Risk, Credit Risk, and Liquidity Risk, remained in the green performance classification, with no changes occurring from third quarter 2018.

Mr. Auch asked about if there is a report with a similar stop light indicator appearance for expenditures versus revenues. Ms. Butler commented that a risk report is being developed with a visual depiction of revenues and expenses, and staff will be eager to review that report when drafted with the Finance and Administration Committee in the coming months.

Quarterly Contract Reports

Ted Lucas, Director of Procurements and Contracts, provided the contract reports. The contract reports show contracts within four categories:

- Contracts awarded by the CEO below 200,000 dollars
- Sole source contracts awarded by the CEO that exceed 100,000 dollars
- Proprietary contracts awarded by the CEO in excess of 100,000 dollars
- Competitive open contract awards

These contract reports are required by the current Board policy R78-2, which will be replaced in 2019 with Board Resolution No. R2018-40. The contract reporting for the newly formed Finance and Administration Committee will be slightly different, but still show contracts authorized under the CEO's delegated authority.

INTERNAL AUDIT UPDATE

Chair Johnson introduced Jack Hutchinson, Director of Internal Audit, to present the update.

Completed Audits

- Asset Disposal
- Small Capital Project Management

Mr. Hutchinson introduced Gana Byambaa, Senior Internal Auditor, to present the audit of Asset Disposals.

The objective of the audit was to determine if management has effective controls to ensure:

- Policies and procedures are comprehensive and provide clear guidance for asset disposals
- Disposal decisions are timely and based on comprehensive support or methodology
- Disposal records are complete and accurate

The audit concluded that the agency lacks adequate asset and spare parts disposal procedures.

Mike Perry, Deputy Executive Director of Transportation and Maintenance, provided comment on management's response to the audit finding. Mr. Perry stated that the auditor's identified a number of areas for improvements to the asset disposal management policy, and that operations is working closely with Finance to update that policy, and to move forward with developing stronger procedures around asset disposal. One challenge has been work with partners wherein there is disagreement about obsolete or not obsolete parts, and staff is also working with partners to ensure collaboration on that issue.

Mr. Hutchinson introduced Soon Kwon, Senior Internal Auditor, to speak to the audit on Small Capital Project Management. The objectives of this audit were to determine whether the agency has effective controls to ensure:

- Realistic budget planning and practical scheduling
- Adequate performance monitoring for reasonable progress within the established budget

The audit found that the controls over realistic budget planning and performance monitoring for reasonable progress are not adequate.

Brian de Place, Director of Operations Support Services, provided comment on management's response to this audit finding. Mr. de Place agreed with the audit finding, commenting that this was an area staff was aware of needing to improve control in. He continued that centralizing project controls, identifying efficiencies and needed resources, are some of the processes being undertaken in early 2019. Process improvements between departments for the small capital project teams are being implemented, for example accounting processes are being made uniform for both small and large capital projects, to ensure accurate reporting.

Internal Audits In-Progress

Mr. Hutchinson then presented the list of internal audits still in progress:

- PLA Compliance Management
- Customer Complaints Management

2019 Internal Audit Work Plan

- IT Information Security Governance

- Partner Cost Monitoring – Pierce Transit
- Budgeting During Project Development
- Construction Configuration Management
- Partner Cost Monitoring – King County Metro
- Work Order Process at the Operations and Maintenance Facility (OMF)
- Small and Attractive Assets Process
- Quality Assurance and Quality Control Program
- Continuous Process Improvement Program
- IT Project Management
- Construction Progress Payment Processing
- Use of Construction Contingency
- Continuous Monitoring of Cash Disbursements
- Prior Audit Issue Follow-Up
- Management Requests

2018 Performance Audit Update

In March of 2018, the committee selected project controls during construction as the 2018 performance audit topic. Mr. Hutchinson reported that the performance audit contractor has largely completed their fieldwork, and that the final audit report is being drafted. The report is anticipated to be completed in January of 2019, and will be presented to the future Finance and Administration Committee.

2019 Performance Audit Topics

Mr. Hutchinson presented a list of recommendations for possible selection for the 2019 performance audit.

- Phase Gate Process
- Workforce Performance Management

Chair Johnson commented that with the committee changes being made in the coming year, the selection of a performance audit topic would be left to the discretion of the new committee.

EXECUTIVE SESSION

None.

NEXT MEETING


No further meetings of the Audit and Reporting Committee.

ADJOURN

The meeting adjourned at 12:28 p.m.

ATTEST:


 Kathryn Flores
 Board Administrator


 John Marchione
 Board Chair

APPROVED January 24, 2019 PIA.