

SOUND TRANSIT AUDIT AND REPORTING COMMITTEE MEETING
Summary Minutes
June 17, 2010

Call to Order

The meeting was called to order at 11:38 a.m. by Committee Chair Richard Conlin, in the Ruth Fisher Boardroom, 401 South Jackson Street, Seattle, Washington.

Roll Call

Chair

(P) *Richard Conlin, Seattle Council President*

Committee Members

(P) *Fred Butler, Issaquah Deputy Council President* (P) *Claudia Thomas, Lakewood Councilmember*

(P) *Dave Enslow, Sumner Mayor* (P) *Paul Wiesner, Citizen Oversight Panel Chair*

(P) *Joe Marine, City of Mukilteo Mayor*

Ms. Katie Flores, Board Coordinator, announced that a quorum of the Committee was present at roll call.

Report of the Chair

Chair Conlin reviewed the contract reports included in Committee members packets; the reports cover all contracts opened in the 1st Quarter of 2010, all open contracts awarded in excess of \$10,000, all open contracts that have been open over five years, and all sole source contracts awarded in the 1st Quarter of 2010. Real Estate reports were also included that list properties that Sound Transit leases to other parties and properties where Sound Transit is the lessee.

2009 Year-end Financial Statements and Schedule of Subarea Equity

Kelly Priestley, Controller, reviewed the 2009 Financial Statements. There were two significant impacts to the financial statements in 2009, the start of light rail service and the beginning of additional .5% sales tax collection in April to support the ST2 program. The Agency also issued new debt in 2009 in three issuances, one was refunding a portion of the 2005 bonds. The refunding resulted in a net savings of \$2.5 million and reduced debt service payments by \$3.6 million. Build America Bonds were also issued in 2009, the bonds are taxable, but the agency receives a direct subsidy to make the rate comparable.

Agency net revenue increased by \$2 million, mainly due to the start of Link light rail. Revenues for ST Express and Sounder were relatively flat. Operating and maintenance costs increased in 2009 due to higher operating and maintenance costs and depreciation. Since 2009 is the start-up year for Central Link, it may not be reflective of ongoing operations and maintenance costs. Sales tax revenue was increased by the addition of the ST2 tax, but decreased because of the economy. With the new ST2 sales tax revenue, revenues were increased by 46.6%, without adding ST2 taxes the agency would have experienced a 6.4% decline in tax revenues. The completion of light rail has resulted in a 7.2% increase in assets.

Ms. Priestley reviewed the balance sheet; the agency has \$919 million in current assets compared to \$167 million in current liabilities. The overall net asset position is \$3.6 billion; including \$2.8 billion invested in capital assets, \$78.3 million in restricted assets, and \$778 million in unrestricted assets. All subareas increased net assets in 2009. Ms. Priestley reviewed judgments and estimates; the capitalization of Central Link assets was reviewed including air space leases, and the life of the asset. Useful lives were adopted by Sound Transit management for the Central Link assets including 150 years for the tunnel, 100 years for the pedestrian bridges, 75 years for the Operations and Maintenance yard, 70 years for the stations, 50 years for the at-grade guideway and O&M facility and 30 years for train control, power and light rail vehicles. A capital replacement plan is also being developed and will be brought to the Board in the future.

Ms. Priestley also reviewed changes to the financial statements. Non-operating payments were reclassified from the capital section of the cash flow to the operating section. A new accounting pronouncement for subsequent event reporting was also adopted by Sound Transit. A new column is also being added to see the transfers between assets or contributions to other governments.

2009 Year-end Financial & Federal Auditor's Reports

Tom Evert, Tara Crawford and Karissa Lackey from KPMG gave the presentation on the 2009 Year-end Financial Audit. The auditors issued an unqualified opinion on the overall financial statements; no material weaknesses in internal control were noted and the A133 federal grant audit also had no findings. The balance sheet was reviewed; over the last three years \$2.3 billion in equipment, property and vehicles that moved from construction into the agency's capital assets. The ORCA system is new in 2009, the auditors looked at the program and tested the revenues. The audit showed that Sound Transit followed generally accepted auditing standards, and no material errors or illegal acts were noted.

Construction claims are estimated by management and those estimates were reviewed by the auditors. In addition, investments were evaluated and overhead amounts allocated to capital projects. There were no audit adjustments or past adjustments as a result of any of the areas reviewed by the audit.

A single audit was conducted to look at federal grant funds received by the agency; 2009 funding was down slightly. There were no findings as a result of the audit, but the audit observed that Sound Transit corrected an item noted in 2007 and 2008 related to the Davis Bacon Act. The audit issues two reports, a subarea equity report and National Transit Database (NTD) report. The subarea report involves 29 procedures, including testing 176 transactions there were a couple small items that were misallocated, the issues totaled \$3,000. The NTD report has not yet been completed, it will be completed in December 2010. Brian McCartan, CFO, noted that the Federal Transit Administration also conducts an audit on the NTD report that will be discussed in the third quarter.

Mr. Evert also talked about a study called "Success and Failure in Urban Transport Infrastructure Projects" that was included in Committee members packets as an informational piece. Mr. McCartan noted that one of the key failure areas listed in the study deals with Board governance and political support. Clear governance and political consensus can be a risk to infrastructure projects.

Review of Proposed Audit & Reporting Committee Charter

Chair Conlin noted that because of the new committee structure of the Board, the Audit and Reporting Committee charter is being reviewed. Mr. McCartan noted that the Audit and Reporting Committee provides an independent review of the Agency's operations. The existing Audit and Reporting Charter, Resolution No. R2001-03 and a new proposed charter was included in Committee members' packets.

The proposed charter covers three key areas: review of financial reporting, debt and investments and contracts; receiving and informing audits and ensuring follow-up; and reviewing internal controls. It removes some of the background text and Sound Transit staff responsibilities. Instead, the charter focuses on the duties of the committee: the committee's role in reviewing financial statements and reports; the specific audits; internal control procedures; and the committee composition and meeting structure. The charter will be brought to the next Audit and Reporting Committee for further discussion and possible action.

Mr. McCartan reviewed a proposed agenda for future meetings that would include sections on audit review, financial reporting, and internal controls. Chair Conlin suggested a possible addition to the agenda where a particular item could be reviewed in more detail at each meeting.

Boardmember Enslow asked if the auditor will have a line of communication with the Audit and Reporting Chair; Mr. McCartan confirmed that is the case, and that relationship is included in the proposed charter. Committee member Wiesner noted that the new charter does not include an obligation for the auditor to report to the COP; instead the COP member who is present at the ARC meeting would relay information to the COP. Boardmember Butler asked whether a risk assessment function could be in the charter or part of an annual work program. Brian McCartan noted that Sound Transit would like to develop an internal risk

assessment for selecting performance audit topics that would be kept current. David Hammond, Interim Internal Audit Manager updated the committee on the 2010-2011 Audit Work program, it is currently in review then will be brought to a future ARC meeting.

Review of Proposed 2010 Performance Audit Topics

Under ST2, a performance audit will be conducted annually either by Sound Transit or the State. In years that the State will not be performing an audit, Sound Transit will conduct a performance audit. The internal audit function at Sound Transit will allow the Agency to look at efficiencies and ways to improve best business practices. In 2010, the State is not performing a performance audit, so the Committee reviewed a list of Proposed 2010 Performance Audit Topics that was developed by using the State Auditor's Office's (SAO) risk assessment of Sound Transit, and by interviewing Sound Transit management. The list represents topic areas that could be completed in 2010 within existing budget resources. An updated list was distributed to the Committee that included additional information on whether it matched with the SAO's risk assessment.

Mr. McCartan reviewed the list of topics, including procurement of information technology (IT) services and systems, ridership data collection and fare collection, Central Link light rail inventory control and preventative maintenance, utilizing economic price adjustments in contract clauses for materials and labor, and facilities management or partner agency rolling stock maintenance.

Boardmember Butler asked if the list was in priority order; Ms. Earl responded that the list is prioritized in her view, with procurement of IT services and systems her highest priority. Boardmember Butler also asked if the Citizen Oversight Panel made a recommendation. Mr. Wiesner responded that the COP used the SAO risk assessment as part of the COP retreat; the COP placed ridership data collection and fare collection at the top of the list. Chair Conlin noted that there was strong interest in both procurement of IT and ridership data collection and fare collection. He asked that procurement of IT be done for 2010 with the intent that it makes an audit on ridership data collection and fare collection easier in the future. Mr. McCartan also noted that the Board would have a future discussion on the Research and Technology fund.

Overview of 1st Quarter Financial Results & Reports

Mr. McCartan provided follow-up information on questions from the last meeting; there was a question about a contract with Milrail, Inc. He explained that the contractor was the only provider for the rail lubricator needed for Central Link and the scope was increased once work began because the problem was larger than originally thought.

Mr. McCartan noted that the financial reports cover the 1st Quarter of 2010. He reviewed some items of note; the farebox revenue is significantly below budget at 77%. Ridership is weaker than anticipated on Central Link and Sounder. The ORCA system is also being reviewed to check the allocations and see if there are any problems in that area. Ms. Earl noted that a campaign has been started on Sounder to inform riders about tapping on and tapping off when riding Sounder.

Capital expenditures for light rail were at 95% of budget for 2009, but the first quarter of 2010 is at 194% of budget because of two contracts for University Link for tunneling, mobilization happened sooner than anticipated. The project is above budget for the first quarter, but well within the lifetime budget for the project.

There were no changes to the stop light indicators in the Asset Liability Report.

Next Meeting

September 16, 2010
Ruth Fisher Boardroom

Adjourn

The meeting was adjourned at 1:01 p.m.

APPROVED ON December 16, 2010.



Richard Conlin
Audit and Reporting Committee Chair

ATTEST:



Katie Flores
Board Coordinator