

SOUND TRANSIT AUDIT AND REPORTING COMMITTEE MEETING
Summary Minutes
March 22, 2012

CALL TO ORDER

The meeting was called to order at 10:36 a.m. by Committee Chair Dave Enslow, in the Ruth Fisher Boardroom, 401 South Jackson Street, Seattle, Washington.

ROLL CALL

Chair
(P) *Dave Enslow, Sumner Mayor*

Vice Chair
(P) *Larry Phillips, King County Councilmember*

Committee Members

(P) *Fred Butler, Issaquah Deputy Council President* (A) *Mary Moss, Lakewood Councilmember*
(A) *Dow Constantine, King County Executive* (P) *Stuart Scheuerman, Citizen Oversight Panel Chair*
(P) *John Marchione, Redmond Mayor*

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

REPORT OF THE CHAIR

None.

CONSENT AGENDA

Minutes of the December 15, 2012 Audit and Reporting Committee Meeting

It was moved by Boardmember Marchione, seconded by Boardmember Butler, and carried by the unanimous vote of all members present that the minutes of the December 15, 2012 Audit and Reporting Committee be approved as presented.

EXTERNAL AUDITS

Status of the 2011 ORCA Audit and 2011 Financial and Federal Audit Entrance

The 2011 Financial and Federal Audit scope was presented at the last Audit and Reporting Committee meeting. The full audit scope is underway and is going smoothly.

Kelly Priestly, Controller, reviewed the 2011 Subarea Report rule updates and procedures. In 2010, Sound Transit began using a new methodology for the subarea report that established formal monitoring systems. The current process is easier and more transparent than the previous process and allows the report to be audited for accuracy. There are five new reporting rules for 2011. Under the new reporting rules, radio upgrades for ST Express will be allocated based on boardings/track miles, light rail noise abatement costs will be allocated based on location and Operations and Maintenance will be based on boardings/track miles. Revenues from operating grants will be allocated based on the project they are related to. There was one rule change for 2011, the bike locker program will be allocated based on the number of stations/project phase instead of the number of lockers/location. Some corrections were also made to cost allocations for the Sounder Yard and Shops, Layover and ST Express facilities, bus fleet replacement and

mobile communications. The corrections were needed because of errors in how the rules were applied in 2010. Annual data will be updated for current year information in order to calculate cost allocations for Sounder, ST Express and Link passenger fares and operations. Ms. Priestly noted that an appendix showing the rules used to allocate costs by subarea is included in Committee members' packets.

Ms. Priestly reviewed updates to the subarea report and agreed upon procedures for 2011. The new report is based on sources and uses and applies cost allocation rules at the audited financial statement level as opposed to having allocations within the detailed account level. This brings the report into closer alignment with financial policies. Two improvements were proposed by the ARC previously and are now included in the report. The report has more detail on reserve balances including showing original levels to add context. The bond interest expense will move to a cash basis to help bond holders see a number that corresponds to amortization schedules.

The agreed upon procedures remain unchanged since 2010. The 2010 report covered 2009 and 2010, the 2011 report will only cover 2011. Last year, the auditors reviewed every rule in the process, in 2011 auditors will only need to audit new rules and do testing on the existing cost allocation rules. The proposed procedures for the 2011 audit were included in the Committee members' packets. No changes were proposed to the procedures.

INTERNAL AUDIT UPDATE

David Hammond, Internal Audit Director, presented the internal audit update. A charter for the Internal Audit Division was developed in 2010; the charter included quarterly reports to the Audit and Reporting Committee as well as an annual statement that the Internal Audit function is free of any impairment. Mr. Hammond confirmed that the division is free of any impairment.

Moss Adams Performance Audit of Value Engineering Program

Mr. Hammond introduced Curtis Matthews, Allan Meyers, Don Stafford and Laurie Tish from Moss Adams, LLP, to review the performance audit conducted of Sound Transit's Value Engineering Practices. The completed audit was included in Committee members' packets. Mr. Matthews noted that value engineering is a process to identify areas for cost reduction that maintain or enhance achievement of essential functions. Mr. Stafford served as the subject matter expert on the audit and gave a history of value engineering. Value Engineering should lead to a reduction in Operations and Maintenance costs, improved performance and function of the system, and assures the public that costs are being managed well. On average, value engineering activities save \$12 for every one dollar spent.

The audit covered the period from September 2009 through September 2011. Mr. Matthews noted that the time period was specified in the request for proposals Sound Transit issued and represented a period where Sound Transit's value engineering program was evolving, and improving. Mr. Hammond noted that during that period the Design, Engineering and Construction Management Department was formed. The audit found that Sound Transit's performance is comparable to other transportation agencies.

The audit also identified near-term, mid-term and long-term areas for improvement. The audit recommended expanding the value engineering program to cover all projects, complying with industry best practices, creating a separate budget for value engineering based on .5-2% of the construction cost, and full time staffing for the value engineering program. The value engineering program should also include tracking and management to ensure outcomes are being achieved. Procurement for value engineering should be done separately from design work procurements.

Ron Lewis, Executive Project Director for East Link, provided comments on the audit. There is general agreement with most of the audit recommendations. Sound Transit will move forward with strengthening requirements, and the proposed documentation and separate value engineering budgets. Mr. Lewis noted that Don Davis, Executive Project Director North Link, is training for value engineering. Procurement of

value engineering services along with risk assessment services was an issue raised by the audit. Mr. Lewis stated that Sound Transit believes this practice promotes synergy and has served the agency well. Value engineering for North Link Project took place from October 2011 through February 2012 to prepare for the project baselining. The value engineering will be reflected in the budget with a savings of \$30-40 million, or 5% of the North Link Project budget.

Mr. Lewis also outlined how value engineering will be incorporated into Agency operations. An Operations Change Control Board has been established for project changes that affect operations. Operations staff also participates in the project Change Control Board meetings to ensure operations needs are being met.

Ms. Earl noted that a work plan will be developed to implement the recommendations and will report on the progress to the Committee in the fall. Mr. Matthews complimented Sound Transit on its value engineering program and its work to implement the recommendations.

State Performance Audit Update

Mr. Hammond noted that the State Auditor's office will do a performance audit of Sound Transit in 2012, so Sound Transit will not conduct a performance audit next year. A list of audit topics will be developed and presented to the Audit and Reporting Committee in September so that a topic can be selected at the December meeting for 2013. The State Auditor's office plans to issue its audit in July 2012 on how the Sound Transit and the Board support the Citizen Oversight Panel and respond to the Citizen Oversight Panel's work.

2011 Internal Audit Division Annual Report

A copy of the 2011 Internal Audit Division Annual Report was included in Committee members' packets. The Internal Audit Division completed 14 audits in 2011, and established internal procedures and protocols.

2012 Internal Audit Work plan

The work plan for 2012 was included in Committee members' packets and includes goals for 2012, audit focus for the year and a list of planned audit activities. In 2012, the Internal Audit Division will also follow up on management implementation of recommendations from prior audits and complete audits that began in 2011.

New Internal Audit Report: Medical Insurance Premium Payment Internal Controls

Mr. Hammond noted that the internal audit report on health benefit premiums was in Committee members' packets.

FINANCIAL REPORTING

4Q Asset Liability Management Report

Jim Block, Cash Investment Administrator, gave a presentation on the fourth quarter Asset Liability Management report.

There were no changes to the stoplight indicators. The federal government will keep the fed rate floating between 0 and 25 basis points through mid-2013. The state investment pool was at 13 basis points at the end of the fourth quarter and the King County investment pool was at 54 basis points. The investment portfolio is meeting all the benchmarks. As the economy strengthens, Sound Transit will prepare for a decrease in unrealized gains.

Overview of 4Q 2011 Financial Results and Reports

Pete Rogness, Budget Manager, gave a report on the fourth quarter 2011 Financial Results and Reports. Fourth quarter revenues are on budget at 100.05%. Sales tax was 2.6% below budget, Motor Vehicle Excise Tax was above the budget by \$3 million and fare revenues were above budget based on strong ridership in the fourth quarter. Miscellaneous revenues were up \$3.1 million due to the sale of the Lehman Brothers claim and vehicle lease revenues from Pierce Transit. Compared to last year, 2011 revenues are 4.2% ahead of tax revenues for 2010.

Total fare revenue was at 102% of the budget for transit operations. All departments are within budget, the largest under-run is salary and benefits at 11% below budget because of a 7.5% position vacancy rate. In 2011, 62 new positions were created, there were 61 vacancies at the end of the first quarter, 53 at the end of the second quarter, 44 at the end of the third quarter and 39 at the end of the fourth quarter. Ms. Earl noted that a 2% vacancy rate is assumed in the budget, the national average is 8-10%.

Capital expenditures for ST Express are at 98% of the annual budget. Mr. Rogness reviewed some of the items that affected the overall ST Express capital budget. Administrative costs were down \$1.6 million, the ST Express bus program was down \$1.3 million due to a change in scope. Right of way (ROW) costs were higher than the budget because of a schedule acceleration that affected ROW costs in Renton. There was a \$5 million payment to BNSF that was budgeted for 2011 that occurred in 2012.

Link is at 86% of the annual capital budget. North Link is on budget for design costs but ROW and Brooklyn station work has been delayed. East Link final design ROW acquisitions did not occur as scheduled in the budget.

Contract Reports

Contract reports covering contracts opened during the fourth quarter of 2011, sole source and propriety contracts opened in the fourth quarter, fourth quarter contracts under \$10,000, and all contracts over five years old were included in Committee members packets.

NEXT MEETING

June 28, 2012
10:30 a.m. to 12:30 p.m.
Ruth Fisher Boardroom

ADJOURN

The meeting was adjourned at 12:26 p.m.



Dave Enslow
Audit and Reporting Committee Chair

ATTEST:



Katie Flores
Board Coordinator

APPROVED on June 28, 2012, KWF.