



## **SOUND TRANSIT AUDIT AND REPORTING COMMITTEE MEETING**

### **Summary Minutes**

**December 11, 2014**

### **CALL TO ORDER**

The meeting was called to order at 9:35 a.m. by Committee Chair Larry Phillips, in the Ruth Fisher Boardroom, 401 South Jackson Street, Seattle, Washington.

### **ROLL CALL**

#### Chair

(P) *Larry Phillips, King County Council Chair*

#### Vice Chair

(P) *Dave Enslow, Sumner Mayor*

#### Committee Members

(P) *John Lovick, Snohomish County Executive*

(P) *Mike O'Brien, Seattle Councilmember*

(A) *Joe McDermott, King County Councilmember*

(P) *Josh Benaloh, Citizen Oversight Panel Chair*

(P) *Mary Moss, Lakewood Councilmember*

Ms. Katie Flores, Board Coordinator, announced that a quorum of the Committee was not present at roll call.

### **REPORT OF THE CHAIR**

Brian McCartan, Executive Director of Finance and Information Technology, reviewed the meeting agenda.

Chair Phillips noted that the approval minutes of the June 26, 2014 Audit and Reporting Committee meeting would be delayed until a quorum was present at the meeting

### **ANNUAL EXTERNAL REPORTING**

#### State Auditor's Office 2013 Annual Accountability Audit

Kelly Priestley, Director of Accounting, presented the report. The following areas of Sound Transit were examined during this audit period: financial condition, procurement (bidding/prevaling wage), payroll/personnel, the travel card program, and conflict of interest/ethics laws. The audit found that Sound Transit complied with applicable requirements, provided adequate safeguarding of public resources, complied with state laws and regulations and its own policies and procedures in the areas examined.

#### 2014 Financial and Federal Audit Plan (KPMG)

Ms. Priestley introduced Karissa Marker, Michael Ortman and Michael Hayhurst from KPMG. Ms. Marker introduced Mr. Hayhurst as the newest member of the KPMG audit team. Mr. Ortman will cover Ms. Marker's work during her maternity leave. The report has already been reviewed by management, and Ms. Marker directed the Committee to the full report in their meeting packets. Ms. Priestley noted that Boardmember packets include the responsibilities and communication requirements, the deliverables list, a new section on user consideration controls, and Appendix A which provides detail on the procedures.

### **FINANCIAL REPORTING**

Brian McCartan, Executive Director of Finance and Information Technology, provided the financial report.

#### 3rd Quarter Financial Report

All Agency revenues are exceeding budget. Tax revenues continue to outperform the budget and are forecast to be \$25 million ahead of budget this year. Transit operation expenditures are below budget, helped by fuel prices, and are projected to stay below for the remainder of the year. Ridership is stronger

than anticipated, and fare box recovery is exceeding forecast on all three modes. There is an unusual budget variance in capital expenditures that was noted in the September meeting – project spending has exceeded the 2014 year budget because of procurement and payments that occurred earlier than forecasted in the Northgate and University Link project plans. Board action will be sought to authorize projected budget overages for the year. The projects, while over budget for the year, continue to stay within the overall project budgets.

### 3rd Quarter Asset Liability Management Report

There are no significant changes in the Asset and Liability Report from last quarter. Interest earnings are tracking below budget because of an arbitrage payment to the IRS for interest earnings exceeding interest paid on tax-exempt bonds.

### 3rd Quarter Contract Reports

There were no significant issues to report.

(Boardmember Mike O'Brien and Dave Enslow arrived at this time; a quorum of the Committee was present)

### Risks of Construction Cost Inflation Presentation

Mr. McCartan and Shahnaz Ghazi, Senior Financial Budget Analyst, presented the report. A major risk of the construction program is cost inflation. Construction costs are affected by factors that include labor costs international commodity prices, construction activity, and the general state of the economy. The recession affected bids for Sound Transit construction contracts lowering them significantly. For contracts over \$200 thousand, Sound Transit awarded \$1.04 billion in construction contracts over the period 2008-2014, compared to the estimate of \$1.36 billion, a saving of \$315.6 million or 23%.

Ms. Ghazi gave a brief overview of the construction risk categories and how they were affected during the recession. Mr. McCartan, citing a report by the outside firm Parsons Brinckerhoff, noted the effects of the slow recovery in the construction industry. The ST2 forecast reflects the Parsons Brinckerhoff prediction of modestly growing construction costs through 2023, or the duration of the ST2 capital program. Despite the promising construction cost forecast there remain risks, which were taken into account in calculating the cost estimates and contingencies. In response to Boardmember questions Mr. McCartan noted also that most Sound Transit contracts specify that the construction cost risks are assumed by the contractor. If the agency were awarded the TIFIA loan, the Agency would be able to absorb a fairly serious recession and have the funds to deliver on the current projects.

## **BUSINESS ITEMS**

Chair Phillips noted that a quorum was now present, which Ms. Flores confirmed, and that the Committee could now vote on the approval of business items.

### Minutes of the June 26, 2014 Audit and Reporting Committee Meeting

**It was moved by Boardmember O'Brien, seconded by Boardmember Benaloh, and carried by unanimous vote that the minutes of the June 26, 2014 Audit and Reporting Committee Meeting Minutes be approved as presented.**

## **2015 PERFORMANCE AUDIT TOPIC SELECTION**

David Hammond, Internal Audit Director, delivered the presentation on the 2015 Performance Audit Topic Selection. He began by giving a brief review of the potential 2015 audit topics: QA/QC Efficiency and Effectiveness, Emergency Management Planning and Preparedness, Facility Maintenance, and Central Link Operating Costs.

When selecting audit topics, several criteria are considered: potential for cost savings, potential to improve performance and efficiency, potential to facilitate decision-making, potential to contribute to public accountability, and the potential to reduce agency risk.

The audit of QA/QC Efficiency and Effectiveness would have a large scope involving many participants, and a construction budget in the billions of dollars. This program operates under Federal Transit Administration regulations and standards, and is subject to the triannual review. There haven't been any issues identified in those reviews; however, there have been some quality issues as projects are delivered. For these reasons, the QA/QC Efficiency and Effectiveness audit is Mr. Hammond's recommended choice for the 2015 Performance Audit Topic.

The Emergency Management Planning and Preparedness budget is \$1.5 million, but the potential cost impacts of not being prepared for emergencies could be significant. This audit would be focused on potential long-term cost avoidance and cost prevention, rather than short-term cost reduction.

The Facility Maintenance 2015 budget is in development, but currently is forecast at \$7 million. Through the audit there would be a potential to impact larger budgets as well. Mr. Hammond noted that he doesn't believe that this is the ideal option at this time, as the scope and impact are smaller than other options. Additionally, there are already some audit activities scheduled for this department in 2015.

Central Link Operations is a \$60 million program, with costs primarily based on service levels. The audit would use peer benchmarking available through the National Transit Database. Mr. Hammond noted that this audit could impact the upcoming rollout of new service in 2016, and might be more effective when the Link Light Rail operating system matures.

Committee members noted that they would like to see the audit topics that are not chosen today on the list of potential 2016 audit topics. Boardmember Benaloh noted that he has a preference toward selecting the Emergency Management Planning and Preparedness topic because of the potential for lives to be saved as a result, however he also supports the selection of the QA/QC Efficiency and Effectiveness topic.

Chair Phillips offer a motion to select QA/QC Efficiency and Effectiveness as the topic for the 2015 Performance Audit.

**It was moved by Boardmember O'Brien, seconded by Boardmember Lovick, and carried by unanimous vote to select the QA/QC Efficiency and Effectiveness topic as the Performance Audit focus for 2015.**

## **INTERNAL AUDIT UPDATE**

### Third Quarter Internal Audit Update

#### Real Estate Acquisition Audit (Miller & Miller)

Mr. Hammond introduced Steve Miller from Miller & Miller, P.S., to present a briefing on the findings of the Miller & Miller Performance Audit of Sound Transit Real Property Activities Related to the University Link Extension. The audit was conducted under Government Auditing Standards, including internal control assessment requirements.

The audit objectives were to verify that real estate parcels and real estate rights were acquired within the timelines required by the University Link Extension plan; that the real estate and right-of-way acquisitions resulted in equitable values; and that the real estate and right-of-way acquisitions conformed to Sound Transit policies and procedures.

The conclusions of the audit were positive. Real property and related interests were acquired in an equitable and timely manner. Sound Transit complied with its own policies, which conformed to Federal requirements.

Mr. Miller expressed his appreciation of the Sound Transit Real Estate Division, whose staff provided appropriate responses to Miller & Miller recommendations included in the report. Mr. Hammond noted that there would be a follow-up on the results of the report in 2015.

#### 2014 Performance Audit Update

The 2014 Performance Audit is focused on the Sound Transit Public Safety Program.

#### Prior Recommendation Status

Mr. Hammond noted that Small & Attractive Assets, Travel, and Procurement will be audited annually.

#### Audits of Small & Attractive Assets (Follow Up)

Small & Attractive Assets are items that are not capitalized and tracked in the accounting system, but must still be recorded as Agency assets. Past audit recommendations for the Accounting & IT division have been to fully implement monitoring procedures directed by policy, record asset costs; and to require electronic submission of inventory, or alternatively reconsider the need for a database system. The result has been an increase in compliance.

#### U-250 Construction Cost Audit (Follow Up)

This was a contract compliance audit that evaluated the Agency GCCM practices. The recommendations have been closed; those included an audit of the timing of the costs incurred versus billed, and obtaining an electronic cost ledger on a project basis in order to facilitate contract close out audits.

#### ORCA Business Account Pricing

Shelli Applegate, Senior Internal Auditor, reported on the ORCA Business Account Pricing Audit. The ORCA business account program enables businesses and institutions to provide transit passes to their employees, customers, and students. The focus of the audit was to determine whether Sound Transit receives accurate revenue for service provided via the ORCA Business Account Program, and whether Sound Transit's oversight of the ORCA Business Accounts is efficient and effective. The recommendations were to consider the use of growth rates, expand the use of custom agreements, and improve pricing worksheet integrity. There will be a follow-up on the audit in 2015.

#### Internal Audits in progress

The internal audits in progress are:

- Performance Audit—Public Safety Program
- Performance Metrics—DECM
- Phase Gate
- IT Project Management
- Project Labor Accounting
- Non-Revenue Vehicle (Follow-up)
- Blanket Purchase Order (Follow-up)
- 2013 Performance Audit—Post-Award Contract Management (Follow-up)

#### **NEXT MEETING**

The 2015 schedule for Audit and Reporting Committee meetings is still being determined. The date and time will be announced once the final schedule is known.

**ADJOURN**

The meeting was adjourned at 11:11 a.m.

  
Larry Phillips  
Audit and Reporting Committee Chair

ATTEST:

  
Kathryn Flores  
Acting Board Administrator

APPROVED on March 19, 2015, KWF