BEFORE THE

TEXAS DEPARTMENT OF HOUSING AND COMMUNITY AFFAIRS

AUDIT COMMITTEE MEETING )

Capitol Extension
Room E1.012
1400 Congress Avenue
Austin, Texas

Thursday,
June 13, 2002

The above-entitled committee came on for meeting, pursuant to notice, at 8:45 a.m.

BOARD MEMBERS:

VIDAL GONZALEZ, Chairman
ELIZABETH ANDERSON, Member
SHADRICK BOGANY, Member

STAFF:

EDWINA CARRINGTON, Executive Director
DAVID GAINES
BILL DALLY

I N D E X

P R O C E E D I N G S

MR. GONZALEZ: I will call the meeting to order. This is the audit committee meeting and it's a committee that will solicit public comment at the beginning of the meeting and provide for public comment on each agenda item. We do have one witness affirmation form from our auditors, Mr. George Scott, and we'll call on David Gaines.

Excuse me. Let me go ahead and entertain a motion to approve our minutes dated January 17, 2002. Are there any additions or corrections to the minutes?

MS. ANDERSON: I move adoption of the minutes.

MR. BOGANY: Second.

MR. GONZALEZ: We have a motion by Beth, second by Shad. All those in favor, say aye.

(A chorus of ayes.)

MR. GONZALEZ: All opposed?

(No response.)

MR. GONZALEZ: Motion carries. And also we do have a quorum and all board members are present.

Okay, David.

MR. GAINES: Thought I better do this first; there's nothing worse than a dry auditor.

MS. ANDERSON: Have you been rehearsing that line?

(General laughter.)

MR. GAINES: Good morning, committee, Ms. Carrington, Chair. Today we have our audit committee meeting and that's behind Tab 8 in your board book. The first action we have and the only action item relates to amendments to the 2002 audit plan, and what you see in front of you is the original plan -- I'm sorry -- this is behind Tab 7, excuse me -- what you see in front of you is the original audit plan with the proposed updates or amendments to the plan in bold italics.

There are two projects that are being proposed for deletion or dropping off the audit plan. A summary of the first project is listed at the top of page 1 and the second project is about mid-page on page 2. These projects are being proposed for deletion for several reasons. First off, the initially perceived risks associated with these projects that resulted in them being proposed don't appear valid based on some preliminary procedures and further consideration. Additionally, the internal auditing division doesn't have the available hours to do it that it originally planned on last fall. And finally, we have had a budget overage on one of our projects that has cost us more time than we had originally expected.

And I'll be glad to go into details on any of these explanations or provide a summary of the projects I'm proposing to delete if you'd like.

I'm also proposing an amendment to the audit plan to reclassify an audit that was originally an audit of the project management tools that were being used in the development of the central database project, reclassify that from an audit to an advisory services project. I started serving as chair off the committee, a nonvoting chair of the central database steering committee at the request of management in October of 2001, and it was that same month I proposed this audit and it was accepted by the board as a project.

As a result of Comptroller General of the United States and the head of the General Accounting Office in January 2002 announcing significant changes in the auditor independence requirements under government auditing standards, I've concluded that serving in both capacities would conflict with the newly established standards. This issue was discussed with the steering committee at our March 2002 meeting and management requested at that time that I continue serving in my role as chair of the committee. Management just believed they'd receive greater value for my services in providing real-time advice and facilitating this effort, real-time direction as opposed to periodic audit reports, and I basically agreed in that respect, and so I'm proposing that that be reclassified to an advisory services project.

In that respect, it should be noted that there are certain safeguards that need to be in place when the auditor is providing non-audit services, and these include: establishing a written agreement with management and the documentation should include an understanding of the services to be provided; management's responsibility for the substantive outcomes of the work; management establishing and monitoring the performance of the non-audit services and ensure that it meets management's objectives; management making decisions that involve management functions related to the audit services and accepting full responsibility for such decisions; and then finally, evaluating the adequacy of the services performed and any findings that result.

Now, if this reclassification is accepted by the board and the plan amended accordingly, that agreement will need to be developed and I'll see that it's done, of course.

The remaining items on the audit plan are either projects in progress or ongoing projects with the exception of the last project listed on page 3, and here I'm proposing that the internal auditing division facilitate a controlled self-assessment program for the department by developing methodology and providing guidance and direction.  This program would basically be owned by management and is a proactive review to ensure processes, systems, and activities are controlled and executed in a manner that supports and achieves the business objectives.

The controlled self-assessment program envisioned:  would provide checklists of critical steps necessary to achieve effective procedures and controls; include management in developing action plans to fix identified gaps between what the current state is and what the current state is desired to be and would require management to prioritize these gaps; allow management to measure and therefore hopefully be proactive in managing controls over the operations; allow management to periodically measure progress; and it will drive operational ownership and involvement in an understanding of controls by management.

Initially I thought this would be an ongoing program with periodic reports, it will start out slowly, probably with one of the smaller program areas or functional areas to be used as a prototype, and then once management is happy with the program and the approach we're taking, then we can institute it throughout the remaining operations of the department.  I see this as an ongoing program.

Any questions relating to the amendment to the plan?

MS. ANDERSON: Mr. Chairman, if I may, I'd like to ask Ms. Carrington a question about this last item.

MR. GONZALEZ: Sure.

MS. ANDERSON: Ms. Carrington, I know that the board in its full meeting will consider conceptual organizational changes for the agency, and in your preliminary planning for those changes is Mr. Gaines assisting you in assuring that as we think through those changes we think through the associated processes and controls and so forth that would be needed in the new organization?

MS. CARRINGTON: Yes, Ms. Anderson, Mr. Gaines has been involved. Matter of fact, he was the first meeting I had on the first day when I went to work at TDHCA and David has been involved throughout all of our discussions on our reorganization.

MS. ANDERSON: Great.

MR. GONZALEZ: Any other questions? I guess we're prepared to approve the amended Fiscal Year 2002 Audit Plan.

MR. BOGANY: So moved.

MR. GONZALEZ: Motion by Shad.

MS. ANDERSON: I would like to second the motion but I also have an amendment to the motion, so can I do both those things?

MR. GONZALEZ: Go ahead.

MS. ANDERSON: I second it.

MR. GONZALEZ: Second the motion.

MS. ANDERSON: And then, Mr. Chairman, I would propose an amendment to the motion, and while I believe the controlled self-assessment is a very good idea and indicative of the agency's desire for sound management practices across our programs and the functional areas, I would just amend the motion to say that we would not initiate that project until the plan of reorganization is implemented which it's my understanding that that implementation would be substantially complete by about the end of this year, and so I would amend the motion that the controlled self-assessment portion of the plan not be initiated until sometime in calendar year 2003 so we're not trying to do controlled self-assessment while we're in the midst of moving functions and so forth around in the agency.

MR. GONZALEZ: Shad, do you have a problem with that amendment?

MR. BOGANY: Accept it.

MR. GONZALEZ: Then we'll entertain -- we'll vote on the amended motion. All those in favor?

(A chorus of ayes.)

MR. GONZALEZ: All opposed?

(No response.)

MR. GONZALEZ: Motion carries unanimous.

MR. GAINES: Thank you. The next item on the agenda is a report from Deloitte & Touche relating to its opinion audit for the period ending August 31, 2001. George Scott, the managing partner with Deloitte & Touche is here with us today and I'll turn the presentation over to him.

MR. GONZALEZ: Welcome, Mr. Scott.

MR. SCOTT: Good morning. As a part of the audit of the financial statements of the department, we also review and evaluate the internal control environment that is in operation during that period. As a part of that, of any audit, we also issue what we call, A Report to Management, at the end. In that report we have identified that we identified no situation that we believe is a material weakness in the control environment of the organization; however, we do have some comments that we believe could improve the financial reporting process of the department, and I thought I'd run through those with you just briefly.

Our first one addresses the accounting for the

Texas Housing Trust Fund. Currently, the activity for that process of originating loans is accounted for in two different areas so it's very difficult to see the program as a whole: The funding is in one fund and the actual loans, the actual funding of the loans themselves are in another fund, so it's very difficult to follow that from one transaction to another, so we would encourage you to at least look at is there a way to bring that together in one activity so a reviewer of the financial statements could see that in one place.

In the down payment assistance loan program area there appears to be a disconnect between the accounting function and the loan processing group, mainly in the area -- obviously the loans are handled appropriately; however, accounting does not always get the information when the loans are completed, so revenue associated with those loans is not actually recognized on a timely basis in some instances, and so again, the two databases -- and you'll see that later on -- the issue of separate databases creates a problem in the efficiency and the timeliness of certain accounting processes.

As far as recording accounts payable, the practice of the department has been to actually after the end of the year only account for those transactions that occur 30 days after year-end. Obviously, when you're in a full accrual situation, as you incur liabilities, some of those liabilities occur after 30 days, so again, the cutoff issue, especially with the new GASB 34 reporting requirements where you go to a pure full accrual presentation, we encourage the department to look at a process to not only do the first 30 days -- which you're already doing -- but also look beyond that because there are liabilities that occur which pertain to the prior year.

In the information reporting area, as I've already alluded to in a couple of cases already, there are separate databases which are used throughout the department, makes it difficult in many cases in the accounting process; there are multiple manual transactions which are recorded because of the different and varying databases. The organization has been going through an implementation of PeopleSoft since 1997 and obviously with the completion of that and other improvements that you have planned, many of these issues should be resolved, but currently it continues to be a potential weakness in the control environment because of the separate databases and the difficulty of getting information from one department to another in some cases.

And finally, this is really not an observation as far as the control environment but it is a very significant change in how the department will report its results, and that will occur actually at the end of this fiscal year. It’s referred to as the new reporting model or GASB 34, it completely changes how governments report their financial activity to more of a commercial model with a management discussion and analysis as part of the report, similar to the SEC -- if you’re familiar with the SEC reporting environment.

It will state in that report whether the organization is better or worse off financially than it was the year before; essentially you’ll lead to that conclusion. However, it will also report on a full accrual basis and the information as you have in multiple funds will be all condensed into one presentation where it will look very similar to a commercial organization, but you’ll also provide information of the funds too in the report.

In fact, you have both situations, so your report is actually going to be longer, more information, hopefully with the MD&A will pull all the information together where a reader can understand the true financial condition of the organization. But again, it changes the way you gather information, changes the processes of financial reporting, so there are costs involved internally as it pulls that information together, so again, it’s another situation where you will be reviewing your processes to make sure that those processes ensure appropriate financial reporting.

With that, I’ll be happy to answer any questions you might have.

MR. GONZALEZ: So are you saying that if we had a centrally managed database, that would eliminate those two issues that you brought up?

MR. SCOTT: The inefficiency part, absolutely, and integrated management.

MR. GONZALEZ: Any other questions? David, any responses?

MR. GAINES: Not in regards to this report.

MR. SCOTT: Thank you very much.

MR. GONZALEZ: Thank you.

David, do you have some other?

MR. GAINES: Yes. There’s a second report item on the agenda, and this relates to the report on federal compliance and controls over compliance relating to the State’s federal single audit for the fiscal year ending August 31, 2001. It’s located immediately after the Deloitte & Touche report, and the report was issued in February 2002 by KPMG who is contracted with the State Auditor’s Office to perform the single audit work for the State as a whole. The information in your board book relates only to that portion of the report that applies to Texas Department of Housing and Community Affairs.

The first several pages of the report, identified as pages 2 through 8, is really just a high-level overview with the generic audit language and a high-level summary of the audit results, and I'll paraphrase this portion of the report as I discuss the detailed audit issues that follow this section, and those begin immediately after page 8 and it's identified and starts with page 123, so this is quite a lengthy report, and again, I've just pulled out the portions relating to TDHCA.

In summary, the audit was to determine compliance with the types of requirements described in the U.S. Office of Management Budget Circular A-133 Compliance Supplement that are applicable to major federal programs. And the report goes on to say that the responsibility of compliance is with management while expressing an opinion on such compliance is the responsibility of the auditors.

The report discusses that the audit was conducted in accordance with Generally Accepted Auditing Standards for this type of audit except in certain circumstances when the auditors were unable to satisfy themselves by audit procedures or by obtaining sufficient documentation that certain compliance requirements were met. One of the exceptions identified in the report was that the auditors were not able to satisfy themselves that the department has fulfilled its subrecipient monitoring compliance requirements relating to the HOME Program. This finding is located on page 123 which is immediately following the summary information of your handout and it relates to lack of documentation supporting the soft costs incurred by the HOME Program subrecipients.

The auditors’ test work identified $29,000 in questioned costs and since there was no documentation associated with this cost category, the estimated questioned costs relating to that circumstance is $2.3 million. The auditors recommended that the HOME Program management ensure that the required documentation is received and supports the related the costs for document for draw-down purchases and that it’s allowed and considered as an ongoing part of the subrecipient monitoring function. Our management agrees with the recommendation and referred to procedures that it implemented with the 2001 HOME awards that were released and awarded in the spring of 2002.

A related concern, and because of this finding and a similar audit finding in the previous report, HUD issued a letter to the department dated April of this year, April 22, that states that the department must review all subrecipient draws for project-related soft costs for the 1999, 2000, and 2001 fiscal years to ensure that all draws are adequately supported, and if not, reimburse HUD from non-federal funds. And a response to this letter from HUD is pending at this point.

MS. ANDERSON: You mean we're preparing a letter of response, or we sent it and HUD is pending?

MR. GAINES: I believe our response is pending.

The auditors also report that the State has complied in all material respects with applicable requirements except for certain compliance requirements that were not met. Among the exceptions noted by the auditors throughout the State was noncompliance relating to the Low Income Home Energy Assistance Program and Weatherization Assistance Program of the department. This finding is located on page 127 of the report and relates to one of the department's subrecipients that had some embezzlement problems and it included some of the departments' energy assistance and weatherization funds. The amounts in question range from $171,000 to $212,000, depending on which auditor or monitor report you're referring to, and KPMG recommended the department establish the amounts of the department, issue a management decision, and demand repayment.

The department basically responded that they would conduct a field visit to make this determination, and upon trying to arrange such a field visit the department was informed that it would be a waste of time because the associated related records were not available, they were being held by other authorities in connection with the embezzlement investigations. At that time the department issued a demand letter and I understand the status of that is that the letter is with the subrecipient’s legal counsel who is supposed to be contacting our legal counsel to decide how to best proceed.

Are there any questions relating to this particular issue?

(No response.)

MR. GAINES: The department is also specifically mentioned, among other agencies, that it had some reportable conditions, and reportable conditions are matters that have come to the auditors’ attention relating to significant deficiencies in the design or operation of internal controls over compliance that could adversely affect the State’s ability, and in this case the department’s ability, to administer federal programs in accordance with applicable requirements. They identified three reportable conditions relating to the HOME subrecipient monitoring function.

The first one related to soft costs and that was the issue we just identified. The second finding is on page 124 of your report that states that TDHCA does not have adequate internal controls in place for monitoring subrecipient programs, and provided a listing of bullets there describing the weaknesses that they noted. You might scan through those bullets.

One bullet in particular I wanted to just touch on real quick was the sixth bullet and it mentioned the compliance division closed 185 contracts during the year. This comment was in error and that's why I wanted to bring it up specifically. We informed the auditors at the time of the report draft that it was in error; however, for whatever reasons it did make it to the report. Recent discussions with the audit partner in charge of the project confirmed that the inclusion of the comment was in error, and while it's in error, the underlying condition expressed by the bullet is that only 49 contracts were monitored of the open contracts during Fiscal Year 2001 and that these contracts represented approximately 12 percent of the total pass-through expenditures for the year and 20 percent of the total contracts for the year. So apparently they were expressing that as a concern thinking those percentages were too small.

The auditors also referred to the department's practice of monitoring contracts once the draw has exceeded 75 percent. They expressed this is a concern and I'll touch on that again momentarily in their recommendation.

The last bullet that they listed, and I just want to touch on it real quick, relates to the lack of a fully operational risk assessment program, and I'm just bringing that up again because this continues to be an issue that the department has been struggling with for an extended period of time now.

The auditors recommended that we strengthen our controls over subrecipient monitoring during the contract period by developing and documenting a departmentwide monitoring program and accounting for each contract or grant from inception through closeout. The report mentioned the contracts should be monitored before 75 percent of the contract dollars are spent and they mentioned technical assistance specifically should be considered part of the function and feed into the risk assessment process.

There's other activities going on besides just construction inspection, and while they felt like the 75 percent was late, they also mentioned outside the report that that in itself is not as much of a great concern as not having other monitoring activities leading up to that

75 percent. So there's a lot of other things that should be happening leading up to that, and that's also expressed some concern about waiting that late because at that point it's a little late to do much if you have significant problems.

The third finding is on 126 of the report, and this finding relates to a problem noted relating to tracking on-site monitoring visits. The compliance division acknowledged the problem associated with their information systems and responded that it's in the testing phase of a multi-family compliance tracking system that will address this issue.

Any questions relating to the KPMG report?

MR. BOGANY: I have one.

MR. GAINES: Yes, sir.

MR. BOGANY: In the possible reorganization and things that we're going to vote on today, are these corrections, Ms. Carrington, a part of that?

MS. CARRINGTON: Much of the restructuring is reflective of the comments and recommendations that we saw in the Sunset Advisory Commission report, Senate Bill 322, and also audits from the State Auditor's Office, along with our external auditors.

MR. BOGANY: Okay, thank you.

MS. ANDERSON: I don't have any questions.

MR. GAINES: The next report item then is the status of prior audit issues, so just flip back a couple more pages and you have an 11-page table starting there, if you'll get that in front of you. These are basically just outstanding audit issues that have not previously been reported by management to you as implemented or otherwise resolved. As management reports implementation or other disposition, they'll be reported to you and then dropped off future reports; however, they'll be kept on the database tracking system until at some point they're independently verified as implemented or disposed by either internal audit or other external auditors.

There are currently 29 issues on the database being reported to you as outstanding; 19 of these issues relate to three recently released reports, so we're down to about ten older issue that we're still dealing with. The issues reported by George Scott just previously are not included in this report and they'll be added for future reporting.

There are a few issues I've planned for specific discussion but if you happen to have questions on any of them, please let me know. I was going to concentrate on a discussion of issues relating to the HUD report and these are issues 253 through 260 on pages 5 and 6 of your report. I wanted to just touch on these because of the potential significant impact it could have on the resources of the department and on the HOME Program.

The overriding issue throughout this report and these audit issues is that the department is not providing adequate monitoring and oversight of properties acquired under several of the HOME Program activities. That was HUD's conclusion based on the review of one of our subrecipients. There were several specific concerns identified in the report and as part of their required corrective actions, instructed the department to investigate all related files going back to the 1998 program year. Of course this is the significant resources of the department I was referring to in the HOME Program. In instances where those couldn't be resolved the corrective action would include reimbursing HUD with non-federal funds.

Management has expressed concerns regarding the nature and scope of HUD's review and is in general disagreement with some of the criteria used by HUD in measuring the department against and the way HUD projected the exceptions it noted to the total population. The department is also in agreement with corrective action calling for investigating all projects back to 1998. In this respect the department has met with HUD officials on one occasion to try to arrive at an acceptable action plan to move forward.

The compliance division has recently completed a review of the sample items tested by HUD as well as additional sample items to try to either confirm or negate the results that HUD came to the table with and reported. Currently that report is in the final stages of preparation and it will be routed to executive for their consideration in the near future, I believe just within the next week or two, prior to being routed to HUD stating our conclusions and proposed actions to move forward.

These issues as well as the KPMG report and Deloitte & Touche report were the only audit issues I was going to specifically discuss at this time. Some of the older outstanding issues relate to cross-divisional initiatives, and I think that's where we've had the hardest time in moving forward when it affects multiple divisions. At this point I'm almost thinking these are efforts that need to be incorporated and factored into the reorganization, and that's primarily why I'm not touching on those at this point.

MR. BOGANY: I have a question.

MR. GONZALEZ: Yes.

MR. BOGANY: Ms. Carrington, on these HUD issues, how far are we from clearing these up? I know there have been some other things on the radar screen, but how far are we from tackling these issues?

MS. CARRINGTON: We are working on them; it is one of the items within the agency that has very high priority. I will not tell you that we are going to resolve these issues in a short period of time, I will tell you that we are working on them, they're very serious for us. We know that we're probably going to have one more audit report that is probably going to be fairly critical of what's been going on in the HOME Program, but we have been having regular meetings with staff addressing these issues, but it's going to be a while.

MR. BOGANY: So we're looking maybe a year from now correcting these issues?

MS. CARRINGTON: I'm looking at David and Ruth

MR. DALLY: Bill Dally, chief financial officer for the department.

One of the issues is -- and the reason she's saying that even the next audit report by KPMG, they came out and did their fieldwork just the last month or two, and they need to go back to files that have expenditures and things and so the things that we put in the 2001, those contracts did not have enough activity for them to test, so what they're going to be do is they're going to be testing the old stuff and they'll still say we've still got these issues, but when they come back and do their fieldwork this fall, they will look at some of the new stuff and make comment that they have or have not seen a correction. But it will take time.

But this thing was issued in February, the KPMG report, and so we're already halfway through this current fiscal year when they come back, and we set up to -- when the comments are coming up, it's almost a year earlier and so we can make corrections in how we do a future cycle, but until that cycle really matures and they can come in and test those expenditures, it's a while before they really confirm, okay, you've corrected it, so that's why there's a bit of a lag in time.

MS. CARRINGTON: We have put processes in place over the last six to nine months that improve what's going on in the HOME Program but it is going to take a while for us to see the results of those improved processes.

MS. ANDERSON: Mr. Chairman, may I make a comment?

MR. GONZALEZ: Yes, Beth.

MS. ANDERSON: A lot of these audits certainly predate a lot of us in the room, including the four people sitting up here, but you know, I think it's interesting that as far back as June of '99 our own internal audit department in an internal audit gave us early warning about these problems, and not a lot of productivity spent now in figuring out why everybody ignored them, you know, right after the early warning and in subsequent years.

But to me, I just want to sort of make a statement to the management and the staff of the agency that speaking as one member of this committee that I take these findings very seriously, and I, furthermore, expect that the legislature takes these findings very seriously, and so it's an element of restoring the credibility of this agency that we're all working so hard to restore. And my expectation is that as we reorganize and as we select people to run important functional and programmatic elements of this agency that the people we select will have a commitment to David and to the auditors to working expeditiously to clear findings.

And I understand that when you've got problems, they're going to, you know, but then I'm going to kind of hold you to what you just said, then in the 2000 cycle when we start to see those audits in a year or so that we won't be seeing the same problems and that the people selected for leadership in this agency will have a commitment to make audit findings not the last thing -- you know, we all have too much on our plates but to me to let these things just slip year after year after year is not the level of performance that any of us expect of ourselves.

So we have an opportunity now both with very strong new management and with a reorganization plan to strengthen the way we operate to make this part of the process of being more effective going forward. I just have an expectation that we'll do that sooner rather than later.

MR. GONZALEZ: Good point.

MR. GAINES: The final report item on the agenda is the status of internal and external audits, and so if you'll turn past the prior audit issue schedule. You'll note that the statewide audit is already back in progress, and that's what Bill was just referring to. KPMG is again contracting with the State Auditor's Office to conduct this work, they're currently on site, the project is underway.

The State Auditor's Office also has several other projects in its plans. The first is a review of the implementation of the Sunset recommendations. The SAO's current plans are to begin their review in the first or second week of July with the intent of reviewing areas that the department considers complete. The project duration is estimated to be three to four weeks and the plans include Sunset staff coming back later in the year to conclude the areas of review not addressed by the State Auditor's Office.

The next SAO project includes plans to review the funding and expenditure transactions of the Community Service Block Grant and Energy Assistance Program to ensure the funds are disbursed in alignment with the state outcome measures and available funds are maximized to support state service delivery. The review also considered the service delivery methods and procedures for the Section 8 Program to determine if the department has feasible action plans to address the increasing demands for Section 8 services and to resolve federal noncompliance issues.

This project is also currently in process. Just yesterday the respective program areas provided me the initial information requests from the State Auditor’s Office that they’ll be using as a basis to develop an understanding and to identify associated risks. This project is estimated to be five to six months in duration.

MR. BOGANY: David, can I ask you a question?

MR. GAINES: Yes, sir.

MR. BOGANY: And this is just a point of information, I’m just understanding the audit. Does KPMG when they go through this audit, do they make recommendations for us or is their job just to find where the issues are with no recommendations and that’s left up to staff to correct it, or do they actually say, Hey, this is how you can solve this problem if you do this and this?

MR. GAINES: The answer is recommendations come with the auditors' reports in most cases. The audit I most recently spoke of will be done by the State Auditor's Office, and it's the single audit, the first audit I referred to, that's done by KPMG, and either way they'll identify conditions, exceptions to compliance, internal control weaknesses, they'll point those out, and then make recommendations.

MR. BOGANY: On how to cure those issues.

MR. GAINES: Right, and oftentimes management knows the recommendation and it's not unusual to solicit input from management on how to best address this issue.

MR. BOGANY: And then once they make a recommendation, then it's upon us to go ahead and act on what they've recommended?

MR. GAINES: I would say, for all practical purposes, yes. I think theoretically, not necessarily, we can argue cost benefit. It's not going to be looked upon very favorably by other oversight agencies if that's the case. If it's an instance of compliance with laws and regulations, I'd say even theoretically we have to do it and you have to be in compliance with the laws and regulations. Good business practices, internal control considerations, I kind of put those in the category of up for discussion, but it's also in the best interest of the department to accommodate them.

MR. BOGANY: And the reason I ask this question, I know that if you follow the guidelines that HUD lays out and says these are the guidelines that must be followed to get these monies, like for example, weatherization and all this other stuff, but when you take that and go to the real world and see how it applies to the people that are out there using it, it's sometimes not on the same -- it's like two magnets put together and it just doesn't match.

And so how much flexibility. I want to use this as an example. I know in Houston we have one program with the city that works extremely well because the city says, Hey, this is how it's going to work and this is how it needs to work to work, and then the county over here follows every rule possibly that HUD has and they send their money back every year. And so I'm wondering when we take these recommendations, Ms. Carrington or the staff, do you guys have a way to say this is how it's going to work over here, and does HUD give you enough guidelines to work between those guidelines or following strict guidelines? Am I making sense?

MR. GAINES: Yes, and I think I can answer and you can tell me if I understood your question. There's many ways to skin a cat usually and in that respect HUD has the requirements, you have to follow them or they’re going to question the costs. One of the things I’ve noted in the past relating to the department is you can negotiate with the funding sources on how to best accomplish your objectives, and in the past, according to management that was in place at the time -- and that’s currently causing us some problems -- they had agreements with HUD to do this or that but the agreements weren’t put in writing, and I believe what happens is, you know, three years later you come up with a new HUD monitor or new federal person, and of course, in that respect I’ve just really encouraged if you need to negotiate and come to alternative approaches and if HUD agrees, get it in writing, because otherwise it’s worth the paper it’s written on.

MR. BOGANY: All right, thank you.

MR. GONZALEZ: Any other questions?

MR. GAINES: The final project currently planned by the State Auditor’s Office is a performance measure certification audit to assess the accuracy of the Fiscal Year 2001 performance measurement data that’s reported to the LBB and the adequacy of the related control systems surrounding the reporting of that data, the accumulation of that data. This review is expected to begin in mid-July to last approximately four weeks.

And turning back to my notes just then, I skipped the project just previous to that, a recently completed investigation that the SAO completed in March 2002 relating to a former employee that misrepresented the information with the intent of benefitting from one of the department's programs, and that was just a project that they've recently released.

The second page of the handout is the status of various internal audit projects.  The first project relates to the central database project that we just discussed in the amendment to the audit plan that's being reclassified.  We are currently in the reporting process and the review of controls on the Low Income Housing Tax Credit project deliverables, and although a report release date in June, I'm really expecting at this point it's going to be late July, early August for assorted reasons.

We're in the final reporting phase on the payroll audit; we have an exit conference planned with the appropriate management personnel tomorrow; we're requesting responses and we expect those within a week, at which time we'll sit down with executive and go over the report, management's responses with the intent of releasing that report the following week.

MS. ANDERSON:  May I ask a question?  With regard to the payroll audit, who is the accountable person that's responsible for preparing these answers that you say are due back to you in about a week?

MR. GAINES: We direct those to the operations management responsible for the conditions being noted, and of course their goal is to provide a response that's acceptable to executive.

MS. ANDERSON: But are there multiple names? I'd like to understand who in the agency -- I mean, this is an example, here is a chance.

MR. GAINES: Right. In this particular instance we do have several audit issues and they'll be directed to the director of Human Resources and the chief financial officer, depending on which issue falls in which area.

MS. ANDERSON: Okay, noted. Thanks.

MR. GAINES: Are there any questions related to the status of audits?

MR. BOGANY: Got your work cut out for you.

MS. ANDERSON: Good report, David.

MR. GONZALEZ: Good presentation.

MR. GAINES: Thank you.

MR. GONZALEZ: That should conclude the report. Do any of you have any additional comments or anything at this point?

MS. ANDERSON: No.

MR. BOGANY: No.

MR. GONZALEZ: If not, we'll entertain a motion to adjourn.

MR. BOGANY: So moved.

MS. ANDERSON: Second.

MR. GONZALEZ: All those in favor?

(A chorus of ayes.)

MR. GONZALEZ: All opposed?

(No response.)

MR. GONZALEZ: Motion carries. The audit committee meeting is adjourned.

(Whereupon, at 9:35 a.m., the meeting was concluded.)

C E R T I F I C A T E

MEETING OF: TDHCA Audit Committee

LOCATION: Audtin, Texas

DATE: June 13, 2002

I do hereby certify that the foregoing pages, numbers 1 through 36, inclusive, are the true, accurate, and complete transcript prepared from the verbal recording made by electronic recording by Penny Bynum before the Texas Department of Housing and Community Affairs.

06/25/02

(Transcriber) (Date)

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