TEXAS DEPARTMENT OF HOUSING AND COMMUNITY AFFAIRS

AUDIT COMMITTEE MEETING

9:10 a.m.
Thursday,
April 26, 2001

Waller Creek Office Building
Room 437
507 Sabine
Austin, Texas

MEMBERS:
C. KENT CONINE
JAMES DAROSS

STAFF PRESENT:
DAISY STINER, Executive Director
DAVID GAINES, Director of Internal Audit
BILL DALLY, Chief Financial Officer
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PROCEEDINGS

MR. CONINE: Let's call the Audit Committee meeting of the Texas Department of Housing and Community Affairs to order April 26, 2001, at about 9:10. I'll call the roll this morning. Kent Conine, chair, is here.

Jim Daross?

MR. DAROSS: Here.

MR. CONINE: Marsha Williams?

(No response.)

MR. CONINE: Absent. We've got two. I believe that's a quorum.

I have -- anybody else for public comment? I have two witness affirmation forms. Anybody else who would like to address the Audit Committee?

(No response.)

MR. CONINE: I'm sure the two that I have will be done at the appropriate time so we'll hold off on that.

Action items -- the presentation, discussion, and possible approval of minutes of our January 26 meeting.

MR. DAROSS: Move the minutes be approved.

MR. CONINE: Motion for approval. I guess I can second that. All approved, say aye.

MR. DAROSS: Aye.
MR. CONINE: All opposed?

(No response.)

MR. CONINE: Motion passes.

Tab 2, presentation, discussion, and possible approval of amendments to the fiscal year 2001 audit plan.

Mr. David Gaines.

MR. GAINES: It's David Gaines, director of internal audit. Good morning, chair.

MR. CONINE: Good morning.

MR. GAINES: Mr. Daross, Ms. Stiner.

MS. STINER: Good morning.

MR. GAINES: We have a lot of information to cover today, and to try to make that somewhat bearable I thought we might throw in a little bit of wit, and so if it pleases the committee --

MR. CONINE: We're in trouble already.

MR. GAINES: -- if it pleases the committee we'll just make this presentation half information and half-wit.

(General laughter.)

MR. GAINES: Before we go to the first action item I'd like to suggest to the committee to allow Mike O'Brien and the board of external auditors to present their reports.

MR. CONINE: Okay.
That will allow them to move on to other things if they have other engagements this morning. In that case I'll introduce Mike O'Brien of KPMG.

MR. CONINE: Good morning, Mr. O'Brien.

MR. O'BRIEN: Good morning. I'm Mike O'Brien with KPMG. Also with me here this morning is Rick Mendoza, who also was part of the audit team. His firm was.

As listed on your agenda, there's five items. Really the revenue bond enterprise items are subsets of the overall department, so may I suggest let's concentrate on the report to the governing board, general purpose financial statements, and then the general purpose financial statements because that includes the information for the revenue bond enterprise fund.

So you should have a report labeled Report to the Audit Committee, Texas Department of Housing and Community Affairs.

MR. CONINE: Hang on just a second. (Perusing documents.)

MR. O'BRIEN: Not the one that says Revenue bond enterprise fund.

MR. CONINE: All right.

MR. O'BRIEN: Just to go over again, as we do
every year, our responsibility as independent auditors is to audit the financial statements of the department, and we're talking about the annual financial report that is issued by the department. The report is prepared by management of the department and we audit the financial statements and express an opinion.

We've done it. We've expressed our opinion which is an unqualified or clean opinion. That's what you want to have on your financial statements. When we do an audit we're auditing the financial statements. We're not auditing the system of internal controls surrounding the financial statements.

We do have a responsibility to review the major transaction cycles, the material internal controls with respect to financial reporting, which we have done. We don't have any material weaknesses in the internal controls. We have issued a management letter with some recommendations and those are simply that. They're recommendations.

They're not what we call material weakness items. They're not anything that the committee needs to take action on. They're really for information to the committee.

There are many other controls that we don't look at, and that's why you have David Gaines and an
internal audit group, because there are controls out there that don't deal with financial reporting but definitely impact the operations of the department.

In the financial statements this year there weren't any new accounting principles adopted. There weren't any changes in existing accounting principles. There were no significant or unusual transactions to point out. There weren't any changes in the accounting for some of the estimated items like loan losses and real estate owned and amortization of deferred commitment fees. Those are all basically the same as they've been in the past.

Continuing on page 2 of that report in the middle of the page, Significant audit adjustments -- we did have an audit adjustment this year, and this is something we've been going back and forth on for a while dealing with the down payment assistance program and the allowance -- the amount of the allowance for loan loss.

After working through that and dealing with management we felt the allowance needed to be reduced by about $1.8 million. We felt like it was overly conservative, so what we did was take a look at the delinquency history of the entire loan portfolio and apply that same sort of percentage to these down payment assistance loans.

You don't have a lot of history on how those
will pay off, because a lot of those loans don't pay off until the loan is --

    MR. CONINE: Due upon sale or refinance.

    MR. O'BRIEN: Right.

    MR. CONINE: But what you're saying is that we have now by virtue of this audit increased our loss reserve or decreased our loss reserve?

    MR. O'BRIEN: Well, if you compare it to last year the loss reserve is increased, but it's not -- the final amount is not increased as much as the preliminary statements show. We reduced it by $1.8 million.

    MR. CONINE: Now --

    MR. O'BRIEN: There's an adequate allowance, in our opinion, on the balance sheet.

    MR. CONINE: And obviously you said very few of those to base some certain percentage on. Do you remember roughly how many that have been repaid or have been -- what percentage that are out there that you base that -- is it 5 percent or 20 percent have come back?

    MR. O'BRIEN: What we did was take the statistics for the overall first lien portfolio and applied it to the down payment portfolio, but I don't remember the exact -- the regular loans --

    MR. CONINE: That's kind of apples and oranges, isn't it?
MR. O'BRIEN: They're attached to the same property.

MR. CONINE: Okay.

Help us, Bill.

MR. DALLY: Bill Dally, chief financial officer. We have -- I think it's somewhere in the neighborhood of probably 10 percent of those have actually paid back, but in some instances those things are forgiven. It's only if the property owner were to sell that property fairly rapidly and then due upon sale we would get return of those funds, and those have been the type we've gotten back, if they actually stay there in the home then those things are really forgiven.

MS. STINER: Mr. Chair.

MR. CONINE: Yes.

MS. STINER: Bill, he's asking about the portfolio. Is this the portfolio of whole loan that the Countrywide portfolio that he used as a baseline for that projection?

MR. DALLY: We used our experience with the first lien to look at the delinquencies there, and then we did add a factor of about 40 percent I believe to that, and that was negotiated. I kept saying, No, without a lot of experience I'm erring on the side of conservatism, and they still felt we were over-accrued or had too high an
estimate on that allowance that more or less we're going
to repay, so I said, Okay.

MR. CONINE: This may not be the place to ask
this question, but regarding the down payment assistance
funds that we've distributed in years past that we have
out on the street, like you say, 10 percent of them may
have been paid back, some of them may have been forgiven,
others are still sitting there. Is there a readily
available report I could go grab and look at and see over
the last ten years or nine years the program's been in
existence where we are in that whole process?

Our theory was loan it out, it will come back,
we can use it later on, and I'm curious where we're
heading with that.

MR. DALLY: Our loan servicing group -- yes,
they can pull a report. I don't have one with me today,
but yes, we can get you something --

MR. CONINE: Because I'd like to see a synopsis
on where we are on that thing just to see. I was at
another meeting earlier this week and the subject came up,
so I'll kind of like to see it.

Okay. Go ahead.

MR. O'BRIEN: Obviously this is an estimation
process, and as new information comes in every year you
can expect the allowance to be increased if needed, or
decreased, if needed based upon current information. But as of year-end we're comfortable if there's an adequate allowance on the balance sheet.

MR. CONINE: Okay.

MR. O'BRIEN: There's a new item this year called Summary of uncorrected misstatements, what we always called audit differences. In other words, when we do an audit not everything we find gets adjusted for, because there's a lot of immaterial amounts that -- maybe they're not technically correct but they don't really materially affect the financial statements.

This year because of changes in the auditing standards we have to formally report those, and we've got a schedule attached to this document that gives you the amounts, and you can see they're clearly immaterial or all balance sheet presentation items dealing with really unreported accruals or amounts payable to subrecipients, mainly because we have a lot longer time after year-end to look at what actually comes in than the management does when they close the books out, because we look at actual history for a couple more months and take the actual amount versus their estimates.

So you can see on a percentage basis they're all listed 1 percent of the totals.

There weren't any disputes or disagreements
with management. We received from them full cooperation as usual.

Any questions on any of those items? If not --

MR. CONINE: Mr. Daross?

(No response.)

MR. DAROSS: No questions.

MR. CONINE: I don't think I have any further.

MR. O'BRIEN: Okay. I'll just point out in the general purpose financial statement booklet, which I'm sure you've gotten a copy of in the past --

MR. CONINE: Yes.

MR. O'BRIEN: -- our opinion is in the front, right at the beginning, and it's an unqualified or clean opinion. It goes to the financial statements and the footnotes in this document.

Then on the management letter, which is the one labeled Letter on internal control and accounting procedures --

MR. CONINE: Time out. (Perusing documents.)

There it is.

MR. O'BRIEN: In auditor's terms these are not considered material weaknesses, which would be items that would be significant enough to cause a material misstatement in the financial statements. These are simply recommendations that we bring forward to management
for consideration, and we just go over them with you for information.

And really the only one I want to go over again is the first one, GASB statement 34. We have a big change up coming in accounting and disclosure requirements for all governmental entities. We talked about it a little bit last year. I just want to bring it up again this year, because it's now going to be implemented at the beginning of the next fiscal year.

There's going to be a lot of changes in the format, the basis of accounting for the governmental funds, that sort of thing, and there will probably be quite a bit of work on the part of the staff to get ready for that.

And the rest of the items are -- have all been taken care of by management or are in the process of being taken care of, and I won't go over all the details. I'll be happy to answer questions if you have any.

MR. CONINE: I might ask Mr. Dally if I might, on this new wonderful world coming, how that's going to affect your daily life, you and staff?

MR. DALLY: We are going to classes and training and we'll be working in concert with the comptroller. The comptroller ultimately has the responsibility for the financial reporting of the entire
state, and so they set out a subset of rules to us as agencies to pull these things together.

One of the major things of GASB 34 that will not affect us but will affect most governmental agencies is the -- they are finally going to put infrastructure: streets, bridges, and those kinds of things in their books, put a valuation on them so that people can evaluate their condition.

For us, our front financial statements will change. The activities, the revenues and expenses should -- you should see a little closer correlation of cost and stuff, and it's been the criticism that sometimes these transfers and things in funds -- it was not easy for outside readers to tell how each activity was doing on governmental. The other thing is government is moving to what they call more of a full accrual basis. We're going to put assets on and we're going to depreciate them.

Now, for purposes of our enterprise funds we have always done that, so half of our shop has really been operating under accrual basis, so it's just bringing in those assets and those things that are -- we've been paying for out of general revenue in our federal funds, essentially.

There will be a lot more work for staff because the look of these financial statements will significantly
change come next year.

MR. CONINE: But to summarize, you're ahead of the curve right now in your opinion, getting ready for it, or are you behind the curve?

MR. DALLY: I think we're fine. I hesitate because my focus has been over at the Hill the last few months. We're going to gather up and redouble our efforts this summer once the session's out and stuff and give the staff a look at this, but I think we'll move along --

MR. CONINE: This kicks in September 1, I understand. Is that what this memo tells me?

MR. DALLY: Yes.

MR. CONINE: So we'll get a chance to revisit this issue again or at least --

MR. DALLY: Yes.

MR. CONINE: -- make sure we do before September 1, some time this summer?

MR. DALLY: That's right.

MR. CONINE: Okay. Thank you.

MR. DALLY: That concludes my report unless there are other questions.

MR. CONINE: Any other questions, Mr. Daross?

MR. DAROSS: No.

MR. CONINE: Ms. Stiner, do you have anything to add?
MS. STINER: No, sir.

MR. CONINE: Good report.

MR. DALLY: Thank you.

MR. CONINE: Glad to have another good one. We appreciate your efforts.

Mr. Gaines?

MR. GAINES: The next agenda item is Proposed amendments to the fiscal year 2001 audit plan. That's behind tab 2. There are several changes I'm proposing to the plan.

First off, I'd like to point out about halfway down the page I'm adding an audit to single-family lien procedures, and the purpose of this audit is to assess whether the department's programs have adequate procedures in place to assure that lien restrictions filed on single family properties are properly filed to protect the department's interest.

There's been interest expressed by certain directors in the past regarding this project, and you may recall members of the committee had expressed interest in this as well. So that's a project we would like to add.

MR. CONINE: Okay.

MR. GAINES: And there's several projects that I'm proposing to drop for reasons I'll discuss in a moment, but those reasons are in addition to basically...
just not having enough time.

    The original available audit hours we budgeted under the original plan have not materialized. We had a staff vacancy for two months longer than originally expected. We're currently experiencing some maternity leave and we're expecting that to go on for ten weeks.

    Additionally we also spend more time than originally expected with external auditors, including Sunset, and attending oversight committees at the legislature, and the software audit that we'll be presenting to you later this morning also went over budget for reasons we believe were out of our control at that time, and so for those reasons I'm proposing dropping the internet security audit.

    Also on that particular audit the technical expertise I was planning to come on staff with us never materialized, and I just don't believe we have the expertise in house to try to conduct that audit.

    I will say in my discussions with the information services director since he's come on board, he's noted considerable vulnerabilities to the system, and he's mentioned -- he's been working with the staff to resolve those and correct those weaknesses, and I believe the most recent update I had with them they're pretty well satisfied with where they're at at this point.
I'm proposing dropping the Section 8 audit because HUD has requested that we have a program-specific audit by independent auditors to review the department's compliance with the Section 8 financial management requirements, and the department's chief financial officer is currently in discussions with the external auditors to have that audit conducted by the end of this fiscal year, August 31.

MR. CONINE: So that one's going to be done but by somebody else?

MR. GAINES: Yes, sir.

MR. CONINE: Okay.

MR. GAINES: The next project -- it's not really an audit. It's these quarterly performance measurement reports. I'm proposing dropping those from the audit plan.

In the past we've done those. These reviews have been primarily cursory in nature, reviewing for conciseness, clarity, the reasonableness of management's explanations. While we'll be glad to continue doing this in the future on an as-requested basis, I believe for the most part they've become so routine they aren't adding any real value at this time, so I'd like management to express to me that they're interested in that and we'll be glad to continue it, because they are not very long for each
quarterly review we did.

And finally, we're requesting the payroll audit, and the reasons behind that are nothing more than time constraints.

Are there any questions relating to this in particular?

MR. DAROSS: Well, generally speaking, I find it disturbing that you're having to drop some of the audits. The internal audit is an essential function the agency needs to have, and I understand that you've got personnel issues on two different fronts.

Have you been getting applicants for the position that's vacant?

MR. GAINES: That position has been filled, and it's also that position that is out on maternity leave.

MR. DAROSS: Well, if you don't have the people, you don't have the people.

MR. GAINES: And this is for the plan for this fiscal year ending August 31, so to the extent that any of these projects resurface in this year's audit planning process, which we try to do on a risk basis, then we can include those in the plan for the coming fiscal year of course, course.

If there's a continued need or a demonstration of need for the internet security audit that's something
that we could consider contracting out for if we don't have the in-house expertise, as we would do with any project where we didn't believe we had the expertise.

MR. CONINE: Is there a report the Audit Committee could get on our new IS portion relative to the subject matter of internet security rather than a full-blown audit report?

MR. GAINES: Is there a report that you could --

MR. CONINE: That he could generate.

MR. GAINES: I believe -- and maybe I should allow him to respond to that as opposed to say what I believe, but I'll be glad to mention what I believe. I believe he's in the audience.

MR. CONINE: Maybe management would furnish us a report at our next meeting just to -- I'm just trying to find some -- so we can get some material feedback but maybe not a full-blown internal audit but at least a report from one who has just recently come on board.

MS. STINER: Yes, sir. He's already highlighted some of those issues. We'd be glad to roll that into a high-level summary report of those particular security issues.

Sid, I don't guess you'll be violating any trade secrets by telling us what you're doing to address
them? Please answer that. I don't know how public we want to make those, but we certainly could provide that to members of the committee.

MR. STRUSS: My name is Sid Struss. I'm director of information systems.

We are already currently preparing for a modified security audit as David was talking about -- can cost upwards from an outside contractor in the neighborhood of about 60- to $70,000. What we have done is worked with Department of Information Resources and done a preliminary security audit of our entire agency, which means what do various staff members think what security is and so forth.

That audit is completed, and they did that of every state agency to determine what state agencies do -- does DIR or these outside auditors really need to audit?

We scored very high points here, which means that we are not going to have a visit of that nature, so we're not really on the high list of a concern. So what we have done is our own inside security audit, and we're already doing the necessary steps to tighten up on all aspects of security, so should a security audit be done of our agency we'll pass with flying colors.

MR. CONINE: It strikes me, Mr. Daross, as having someone new coming in almost like an audit in and
of itself, and maybe if you could furnish us with a copy of the one that was recently completed maybe that's all we'll need to take a look at.

MR. STRUSS: We sure will.

MR. CONINE: Thank you.

Are you looking for an action item for us to amend your audit plan this year? Is that what needs to happen?

MR. GAINES: That would be a possibility, acceptance of amended plan. Alternatively, I could report deviations from the plan with my annual report to the LBB and State Auditor's Office.

MR. CONINE: And from what I'm looking at everything's being pushed back either a couple of months specifically or just are still ongoing, and that's what you feel currently with the staff levels you have and workload that some of it you're shedding, some of it you're not, but you can deliver those at these new dates?

MR. GAINES: That's what we're currently planning on. What's remaining in the plan is two audits. One of them we -- the single-family liens procedures we should really just be getting started on, so we're planning towards the end of this fiscal year for that.

And then the other one that's been pushed back to August 31 is the community services monitoring function
that the auditor who is currently on maternity leave has been performing, and I believe she's expected back in June sometime, so I was going to push that back and allow for that.

MR. CONINE: One of the things I really wanted to get done this year was that payroll audit. I hate to see it fall by the wayside, and just for my two cents if there's any way to cram that thing in I'd love to see you get that done.

MR. GAINES: We'll cram to the extent we can.

MR. CONINE: Any other questions or comment from you, Mr. Daross?

Do you want to move that we accept his report and amended plan?

MR. DAROSS: Sure. I move that we accept the amended audit plan and we recommend to the full board that the amended audit plan be adopted.

MR. CONINE: I'll second that.

All in favor, say aye.

(A chorus of ayes.)

MR. CONINE: All opposed?

(No response.)

MR. CONINE: All right.

MR. GAINES: The next item on the agenda is the software license audit I was just referring to, and I'd
like to turn that discussion over to Sam Ramsey, the lead
auditor on that project.

MR. CONINE: Good morning, Mr. Ramsey.

MR. RAMSEY: Good morning. For the record, my
name's Sam Ramsey. I'm internal audit manager for TDHCA.

Good morning, everyone.

MS. STINER: Good morning, Mr. Ramsey.

MR. RAMSEY: This morning I'd like to give an
overview of the software license and software management
controls audit we just recently completed and hopefully
answer any questions you may have after I finish going
over it.

Before I get started, I'd just like to say I'm
trying to get over the lingering effects of a cold, so if
I start coughing or my voice starts to go, I'm not trying
to wiggle out of any kind of touchy audit issues or
anything.

MR. CONINE: We'll get you some water if you
need some.

MR. RAMSEY: Okay.

This audit was a scheduled review in our FY
2000 audit plan. You may note that if you have that
available. But before we get started, does anybody need a
copy of the audit report?

MR. CONINE: I've got one.
MR. RAMSEY: Overall -- I'll just get into the audit objectives.

Our purpose was to determine the department's compliance with House Bill 1895, which essentially calls for a software audit every two years by the department to make a determination whether the agency is paying for a license for software or software maintenance costs that he was not using or does not need. Also, the legislation had a requirement that all state agencies and universities obtain available software through a commodity list developed and maintained by the Department of Information Resources.

If they chose not to do that they had to obtain waiver from DIR to make a purchase.

In addition, our review included a review of controls of the adequacy of purchased [phonetic] software. In other words, basically how we manage software in the agency. So that was our primary objectives for the audit. Any questions along those lines?

(No response.)

MR. RAMSEY: Pretty much I'm just going to go over the executive summary of our reports and touch on those, and if you have any questions feel free to jump in as I go along.

With regard to the legislative requirements of
House Bill 1895, we felt the department may not have identified all possible software-related cost savings associated with the software packages that the department did not need or are no longer using. By that I mean we basically felt the process could have been a little more thorough as far as how they went about trying to determine that.

Secondly, we noted that any -- House Bill 1895 requirements and LBB instructions as far as that requirement called for any particular cost savings to be reported to the LBB, and we noted that even though we did identify some cost savings none were reported to the LBB.

And as to this point the department is still in the process of doing the necessary actions it needs to to address any unnecessary software expenses that have been incurred that we no longer need or use.

With regard to the management of the department's software, overall we noted a lack of adequate internal controls in place to ensure that software programs installed on its computers -- or our computers are licensed and authorized, and that all purchased software programs licenses are properly accounted for and safeguarded. I might note that management was in general agreement with our findings, and as indicated on the report corrective action was either being taken or in
progress on what was being planned.

I'd like to note that during the latter stages of our fieldwork ISD or Information Services Division had begun undertaking work to develop a database to start managing the software aspects of the agency.

Is there any questions or comments along those -- as to what I've just gone over?

MR. CONINE: Probably a lot of comment. I guess my first question is in your opinion how did we get in this mess?

MR. RAMSEY: Overall I guess we just basically haven't managed our software very closely in the past.

MR. CONINE: Is it a personnel issue, specific personnel, or a turnover issue in that department or is it -- what would you --

MR. RAMSEY: How would I characterize it?

MR. CONINE: Yes.

MR. RAMSEY: It's just something that we've purchased software and not really given it the attention that we should have. It's just -- the situation seemed to end up being the way it was, or is. Lack of policy and procedures too, but in talking with -- working with the ISD staff right now, Sid, Curtis, and so forth, they've undertaken a lot of what needs to be done right now to get things in shape as they need to be or should be.
MR. CONINE: And how long has Mr. Curtis been on board?

MR. HOWE: I'm Curtis Howe.

MR. CONINE: Hello.

MR. HOWE: I've been on board since November of 2000.

MR. CONINE: Okay.

MR. RAMSEY: This audit got started about that time.

MS. STINER: Mr. Chair, may I just --

MR. CONINE: Yes.

MS. STINER: -- add a comment too that may help clarify how we got to this point?

Traditionally each director has their own budget, and there was no central control over purchases of software like there was of no hardware, so you had a lot of different purchases going out from individual basis based on what the director felt they needed in terms of software. But I think what you've heard explained this morning is that we're moving into a more centralized inventorying of software, and I suspect included in that plan by IS will be some kind of checks and balances on what individual staffers can install on their own computers.

So it's a task that the new IS director has
undertaken, and we've talked about it extensively how you
control the installation of software and avoid any illegal
use of licenses in the department. But as I said,
traditionally that as been an individual procurement
request from the various divisions.

So I think part of the plan that Mr. Struss has
talked to me about is that all requests now for computer
hardware and software will be at least coordinated through
that office or the committee that's been established for
those purposes.

MR. RAMSEY: Along those lines, that's more or
less the up front aspect of it. Previously we've had an
informal process where when any software requisition was
made it was forwarded to the ISD director, but that
process was fairly informal.

More or less our issue with the software
management is more or less, once it's actually purchased,
tracking it, making sure that we have licenses and so
forth that will support whatever is installed on our
machines, and doing periodic audits just to ensure that
nothing unauthorized is being used on the machines,
because that would subject us to copyright infringement
penalties, and that's what we've been at risk for.

MR. CONINE: I guess what about the requirement
to report to the LBB cost savings or whatever we're
supposed to from a statutory -- I guess from a statutory
respect that were not reported? Is that something that we
just found out that we were supposed to be doing, or
something we knew about but we just didn't do?

MR. RAMSEY: Well, it's just something that
didn't occur. Basically the House Bill 1895 is
legislation that calls that each agency perform an audit
evory two years and to make an assessment of software that
we don't need or use. The LBB came up with some
instructions last July that modified that requirement and
the fact -- all they wanted to see was FY 2000 purchases
and they also wanted to see any cost savings, which is
also part of the legislative requirement.

But we actually performed two House Bill 1895
audits last year, one in August of 2000 and another in
December of 2000, and the August of 2000 audit did not
identify any cost savings at the time. And the second
audit that was done in December did identify some cost
savings, but that was resubmitted back in the first part
of February with the amended BOP [phonetic], and the
savings just were omitted.

MS. STINER: Mr. Chair, not to prolong the
discussion, but Sid Struss is in the audience.

Sid, do you want to comment since the
discussion is about this? Will you come forward and just
share with the committee the status of --

MR. STRUSS: I think a lot of your questions that you had at the very beginning, was it personnel issues or not living up to the statutory regulations and so forth -- one of the -- when I came on board -- I came on board right before Curtis did, which was September, and House Bill 1895 is a relatively new bill that was passed, and it was really to help agencies -- they buy software and they would keep going, and they would forget the fact that they bought a certain software and it would be sitting out on their servers, but yet they weren't using it, but they were turning in maintenance fees, which we were doing here.

Our maintenance fees are for everything that we have, software and hardware and so forth, is a substantial high number.

When I came on board I did my own audit. I'm not an auditor, but my own feasibility study -- and I realized that I've never seen a maintenance fee as high as the maintenance fees we were paying here. So I had gotten with our director, David Gaines, to say I think we ought to take a look at this House bill and you guys confirm, what are we missing here? What are we supposed to be doing to make sure that we live up to all the requirements that we're supposed to do?
And Sam's done a very good job as far as finding what we have been missing in this agency that we need to do.

We also did find and discover -- I think Curtis may verify the exact number, but I believe it was some $40,000 that we immediately just wiped off the list in maintenance fees that we have been paying for software that we have not even been using. It was for applications that were on the servers that we weren't using. So this whole software -- this whole deal is really good because it does help agencies save money if they go in and perform what they're supposed to.

We've done everything now. We do report to the LBB what they need to find out. We take care of all those aspects. I think we're pretty much on board with responding to all the issues that were brought out on the audit.

MR. CONINE: Any other questions?

(No response.)

MR. CONINE: That's good to hear. Thank you.

MR. STRUSS: You're welcome.

MR. RAMSEY: Any other questions, comments?

(No response.)

MR. RAMSEY: I'd like to point out that typically -- not typically but in the past we've had a
difficult time getting timely responses and so forth during the course of our audits. I just want to mention that working with Sid and Curtis and his staff, they've been very timely and helpful in getting everything we need.

MR. CONINE: The target dates in here for their implementation of your recommendations are -- we can put those on the schedule, David, and make sure that we follow up?

MR. RAMSEY: We will track those.

MR. CONINE: Hit those targets. Okay. Thank you for that report.

MR. RAMSEY: Thank you.

MR. GAINES: Speaking of tracking audit issues, the next agenda item is the status of prior audit issues.

There are currently 53 outstanding audit issues on the tracking system, and management has reported significant progress in addressing these issues. Management's recently reported that approximately 70 percent or 37 of the 53 items have been implemented.

MR. CONINE: Good.

MR. GAINES: There's eleven that are in the process of implementation. One is classified as partially implemented; no further action is intended.

We have three issues for which the action has
been delayed, and there's one issue for which no action is intended.

MR. CONINE: I didn't follow the math, but I assume that adds up to 53.

MR. GAINES: The last time I checked. And I'm not real sure exactly how you'd like to go through these, and to what level and degree, if you have any particular questions --

MR. CONINE: Run through that scenario once more. There's 37 completed.

MR. GAINES: We have eleven that are in process of implementation.

MR. CONINE: That their scheduled dates are not -- their scheduled completion dates have not occurred yet?

MR. GAINES: Of those eleven I believe there's seven where the target dates have been pushed back. We haven't met the most recent target date but we have had seven of those that were pushed back, and three of them the target dates have not yet arrived.

MR. CONINE: Okay.

MR. GAINES: That just adds up to ten. I'm not sure where the eleventh one falls. I'll have to look at my notes.

And then there's one --
MR. CONINE: There's 37 and eleven.

MR. GAINES: One of the -- the eleventh item one of the target dates has expired.

MR. CONINE: Okay.

MR. GAINES: So those are the eleven in progress.

There's one that's partially implemented with no further action intended.

MR. CONINE: Okay.

MR. GAINES: And I looked at what was done in that respect and that was reasonable.

MR. CONINE: All right.

MR. GAINES: There's three where the action has been delayed. Two of those were basically pending action by HUD on those, and one of them looks to me like it's a resource constraint. That's why it's been delayed. And then there's no action intended on one of the audit issues and looking at management's explanation for that in agreement with them that action's not necessary considering the change in circumstances.

MR. CONINE: What's your pleasure, Mr. Daross, this morning? Do you have any thoughts?

MR. DAROSS: The only one of these items that I have a real concern about I think everyone on the board does, and that's the subrecipient monitoring process.
That's apparently coming along and is on target.

MR. GAINES: There's several issues here. One of them I do specifically want to touch on is classified as implemented, and this is the HUD-OIG audit on subrecipient administrative cost, and you may recall there was one -- there's basically two sides: our in-house administrative costs which we previously resolved, and then our administrative costs relating to subrecipients, and that was a two-part issue also.

There was this cost associated with the 19 subrecipients that were tested by OIG, and we've resolved that with HUD, and then the other half was okay for all those subs included in our original sample that we never tested, we want you to provide support for those. And I believe the last time we were discussing this management and the committee were concerned that might relate to all subrecipients going back to the beginning of time.

We got an opinion from HUD that, no, those are just the subs within the original sample, and they just tested 19 of the original sample. There was an additional 40. So management went back and accumulated the support for those additional 40, submitted that to HUD in late March, and we're waiting on HUD's response or acceptance or rejection of that support.

MR. DAROSS: So that July 31 date is just to
wait for HUD's response?

    MR. GAINES: Well, we might be talking about
different audit issues. I believe this particular audit
issue the target date was April 1 of 2001, so if you're
referring to the particular audit issue I do have
summaries of these in front --

    MR. DAROSS: Maybe I'm looking at the wrong
one. On the first page reference number 136, the bottom
of that page.

    MR. GAINES: Issue 136. (Perusing documents.)
Okay. That is another subrecipient monitoring issue as I
was saying. There was several. This particular issue
relates to the recommendation that the department develop
a system to identify, capture, and exchange relevant
monitoring information in a form and time frame that will
allow department employees to effectively perform their
monitoring responsibilities.

    Management in their status updates refers to
the development of a departmentwide database as reasons
for the delays. However, I believe this particular issue
relates primarily to just identifying the information
necessary for monitoring and risk assessment purposes and
making it available.

    I believe the department can proceed with this
regardless of the status of the departmentwide database.
In fact, some of the program areas have in regard to the risk assessment. The compliance division has implemented risk assessment process and is currently using that for the HOME and CDBG programs. Energy assistance has developed and is using the risk assessment model and is using it for their selection of subrecipients to monitor.

I believe the status of the other areas is that the community services division is evaluating the risk assessment process and their status has been indicated that they're evaluating the process to be used and that they're working with IS to accumulate that information.

I don't think this is an IS question oftentimes, because first off you've got to identify what information you need, and once you do that it may or may not be automated at this point. Based on some of the monitoring files I've reviewed in some of the other program areas a lot of this information has not been automated, so it's not so much an IS question.

But IS is looking at -- community services is looking at that and working with IS to accumulate the information.

And in the Housing Trust Fund and Section 8 programs this is still in the future. They're evaluating what they should be doing and trying to figure out where the information comes from to move forward. In Section
8's case I believe there's no significant monitoring function to begin with, so they're going to have to, of course, establish a function in order to deal with this kind of issue.

MR. CONINE: So next time we see this report are the 37 that have been completed going to fall off the report?

MR. GAINES: Yes, sir. Once management reports them as implemented I'll take them off the reporting system. I'll continue to track them in our database until which time either internal audit or external audit independently assesses an implemented status, at which time I'll drop them completely off the database. That's how we've operated.

Some of these issues we may never get around to. As we follow up we'll of course prioritize and try to look at what we think to be the greatest risk. The external auditors are responsible for following up with their prior audit issues to the extent they relate to audit objectives that they're pursuing. And so oftentimes if I realize the external auditors are coming back I'll just wait on them to follow up on their issues.

MR. CONINE: Ms. Stiner, any comment from management side to the process here and how we're moving along from your perspective?
MS. STINER: Thank you, Mr. Chair.

From the perspective of management we are moving along on this fairly well. We discussed whether or not the central database is central to having a system that works. It's been my position that it is. I respectfully disagree with David on that account. But it doesn't mean that we can't have an interim system that works, so we've encouraged all the program areas to move toward an interim system until the central database is available for centralized reporting and tracking, so it will have a model that everybody can buy into and use.

But given that the interim progress is going along fairly well.

MR. CONINE: Given that, I think -- I don't think I have the appetite to delve into too many of these issues today. I think --

MR. GAINES: I think we've just touched on the more significant ones.

MR. CONINE: Yes. I think I'll save the in-depth examination of where we are for the next go-round at our next meeting, and let management have more time to get some more of these issues maybe resolved and get it down from 53 down to something a little more palatable.

MR. GAINES: As I say, significant progress has been made of the 53. Thirty-seven that will be dropping
off --

MR. CONINE: That's good to hear.


MS. STINER: What does that leave, 16? My math is a little fuzzy. Sixteen. Right?

MR. CONINE: Sixteen. You're right.

MS. STINER: Good.

MR. GAINES: The final agenda item is the summary status of internal-external audits that is probably right at the back of your handout.

MR. CONINE: Okay.

MR. GAINES: You'll note that the State Auditor's Office has completed their projects. The most recent project completed was the Fiscal Year 2000 statewide federal single audit.

In connection with this audit the SAO followed up on prior audit issues relating to this agency in connection with that audit, and in this respect the SAO gave the department credit for taking corrective action on three of the prior audit issues, and there was one other prior audit issue which relates -- it's a repeat finding for this year, and it relates to a material weakness finding reporting on the HOME subrecipient monitoring function last year.

Of course, this time frame was September 1,
1999 and 2000 -- August of 2000, and so to the extent we were not able to take corrective action early in that year that would result in a repeat comment as it has, and the prior comment management has responded to as being pretty much implemented at this point, so I believe that issue's pretty well taken care of.

MR. CONINE: Okay.

MR. GAINES: And I was going to say that concludes my presentation. I know there's other audits there, and for some reason I'm turning to my summary and I don't have it in front of me. I know there's an HHS audit there that has been -- I believe the status of planned report release date at this point is unknown.

As recently as yesterday we talked to -- management talked to the HHS personnel and the status continues to be unknown. It's a matter of getting around to it and finishing it up.

There's a payroll -- or claims audit by the comptroller's office that's been completed and we're awaiting on that report.

MR. CONINE: This says "unknown" on here or reporting an unknown, but you're saying it's been completed?

MR. GAINES: Yes. Well, we believe the audit has been completed. They're in the reporting phase, so I
guess the audit's not completed until the report's out. I believe -- we were talking with management recently. They believe the check's in the mail.

MR. CONINE: Okay.

MR. GAINES: Is that right?

MR. DALLY: Yes.

MR. GAINES: So we need to trace that audit down. It presumably is in the mail, and we're in the process of getting more aggressive on trying to find that. I will just point out during that exit conference the results were fairly successful, as that's one of these audits we need to be doing this with.

MR. CONINE: Okay.

MR. GAINES: We'll do that as soon as we get that in hand.

MR. CONINE: And you had "software audit" on here, which we just heard about.

MR. GAINES: That's the one we just presented.

MR. CONINE: And the CDBG subrecipient monitoring --

MR. GAINES: Yes. That's the audit that we've extended the target date on that until August, pursuant to the amendment to the audit plan we were discussing earlier.

MR. CONINE: Any other comments, Mr. Daross?
MR. DAROSS: No.

MR. CONINE: Any other comment, Ms. Stiner, from you?

MS. STINER: No, sir.

MR. CONINE: A nice report.

MR. GAINES: No other comments from me. Thank you.

MR. CONINE: We'll just keep on keeping on and have another meeting here in a couple of months.

MR. GAINES: Yes, sir. Thank you.

MR. CONINE: If there's no other comments the Audit Committee stands adjourned.

(Whereupon, at 10:05 a.m., the meeting was adjourned.)
CERTIFICATE

MEETING OF:    TDHCA Audit Committee
LOCATION:      Austin, Texas
DATE:          April 26, 2001

I do hereby certify that the foregoing pages, numbers 1 through 45, 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.

05/01/01
(Transcriber) (Date)

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