TEXAS DEPARTMENT OF HOUSING AND COMMUNITY AFFAIRS

AUDIT COMMITTEE MEETING

TDHCA Headquarters
221 East 11th Street
Room 116
Austin, Texas

Thursday,
September 15, 2011
7:30 a.m.

COMMITTEE MEMBERS:

TOM GANN, Chair
LOWELL KEIG, Member

STAFF:

TIMOTHY K. IRVINE, Interim Executive Director

I N D E X

P R O C E E D I N G S

MR. GANN: We'll call this meeting to order of the Audit Committee of the Texas Department of Housing and Community Affairs on September 15, 2011, 7:30 a.m., and we're meeting at 221 East 11th Street in Room 116.

I'll call the roll at this time and certify our quorum. Ms. Bingham?

(No response.)

MR. GANN: Tom Gann here.

Mr. Keig?

MR. KEIG: Here.

MR. GANN: We do have a quorum.

We also have a period for public comments. Do we have any public comment at this time?

(No response.)

MR. GANN: Sandy Donoho, you're up next, but I understand we have a new member. Would you introduce him to us and tell us a little about him.

MS. DONOHO: Yes. This is Matt Embry. He's the newest addition to Internal Audit. He's a certified fraud examiner, he came to us from the Weatherization Assistance Program where he was a monitor. What that means is according to our auditor independent standards is that he won't be auditing a lot of the programs that he used to here. We're happy to have him and he's jumped right in and he's doing a great job.

MR. GANN: Thank you for being here, Matt.

I think I'll just turn it over to you at this time, Sandy.

MS. DONOHO: Item 1 is Presentation discussion and possible approval of the Audit Committee minutes for May 5, 2011. The Audit Committee minutes for May 5, 2011 are in your board book. Are there any questions on those minutes? Staff recommends approval of the minutes.

MR. GANN: I'll take a motion.

MR. KEIG: So moved.

MR. IRVINE: I'll second. All those in favor say aye.

(A chorus of ayes.)

MR. GANN: Any opposed?

(No response.)

MR. GANN: There are none.

MS. DONOHO: Item 2 is Presentation, discussion and possible approval of the Internal Audit Work Plan. As you know, the Internal Audit Work Plan is required by the Texas Internal Auditing Act which is the statute that governs the state's internal audit functions.

The plan outlines the work that Internal Audit will undertake in the coming fiscal year. The plan is based on a complex and lengthy agency-wide risk assessment that includes interviews of major staff, surveys of all of directors and managers, research into statutes and federal regulations, and review of a very large amount of program information. The board has had a chance to review the draft plan, and you as the Audit Committee members have had a chance to review the full risk assessment and the documents that are attached to that.

We have eight new audits on the plan this year. Four of these, which are the Neighborhood Stabilization Program followup, the HHSP Program, the HOME Multifamily and Loan Processing, are larger audits. This year we decided to add four smaller audits of very specific areas and do a combination of larger and smaller audits so that we can maximize hour audit efforts with the staff that we have by performing these smaller audits when we have downtime and we're waiting for documents or responses and things like that.

We have a number of special projects and other tasks that are either required by state or by our auditing standards. These projects are on our plan every year and some of them occur periodically. The annual ones include a quality assurance self-assessment which is a self-assessment of whether or not our working papers comply with auditing standards. We annually review our charter and our board resolutions, and you'll see those in January. We do an update of our policies and procedures. There's a December 2011 implementation of the GAO auditing standards, so we'll need to revise our policies and procedures to comply with the newer standards, as well as some ongoing tasks that include coordinating with external auditors, following up on prior audit issues, handling calls from our Fraud Hotline, as well as other fraud complaints. Also, we'll be preparing for our 2012 peer review next year.

Are there any questions regarding the proposed 2012 Audit Plan?

MR. KEIG: No.

MR. GANN: Staff recommends approval of the 2012 Audit Plan.

MR. KEIG: I move we approve the Audit Plan.

MR. GANN: A motion has been made and I will second. All those in favor say aye.

(A chorus of ayes.)

MR. GANN: Any opposed?

(No response.)

MR. GANN: There are none.

Ms. Donoho, I'd better recognize our chairman, I know he's in the room. J. Paul Oxer, appreciate you being here today.

MR. OXER: Good morning, all. Yes, sir, Mr. Chairman.

MS. DONOHO: Item 3 is Presentation and discussion of recent internal audit reports. We've released two internal audit reports since our last meeting and these two reports were the last two audits on our plan from last fiscal year.

The first one is an internal review of the Disaster Recovery Program and we released this report in June. It was on our plan to do an audit of this area, but because the Disaster Recovery Program was reassigned to the General Land Office, we weren't able to complete our audit as required by the plan, but we didn't really want the planning work that we did to go to waste, so we developed a report based on our getting an understanding of the program during the audit planning phase. I wanted to mention this report even though we no longer have that program primarily because it took a great deal of staff time to research and prepare the report. We provided this report as a baseline to the General Land Office as they move forward in administering that program.

The report contains self-reported information taken from program staff. It was provided for informational purposes. It was not an audit and is not considered an audit report. It consequently was not conducted in accordance with auditing standards and we made that perfectly clear in the report.

Are there any questions on this report?

(No response.)

MS. DONOHO: Okay. Then the next one is an internal audit report on the Tax Credit Exchange Program. We released that August 4.

The department is on track and it has a plan to ensure that the Tax Credit Exchange Program funds are disbursed and that the developments are placed in service by Treasury's deadline of December 31, 2011, however, in order to meet this deadline the department may have to modify some of the internal controls which were set up to help ensure that the funds are only used for costs that were incurred for the program and that are eligible costs. The controls include cost certification, final inspection and withholding payment of developer fees.

The department has options if developments are not completed or placed in service by the deadline set by Treasury. The options include denying a developer the right to participate in other programs, to recapture expended funds, replacement of the developer, general partner or anybody else providing services to the developer, foreclosure is another option, or some combination of the above. So because these options are available, we felt that the risk of a property not being placed in service by the deadline was significantly reduced. That's good news as long as management and the board are okay with the fact that some of these internal controls may have to be modified in order to move the deadlines.

In addition, we looked at 38 draws and two of them included an incurred cost which totaled $111,521. These included estimated bank payments and anticipated costs. We also identified $3,617 in our sample that were expenses paid for donations, late fees, gifts, food and party supplies. Although these expenses are not specifically prohibited under the contracts, we felt like the department should ensure that the draws are only paid for incurred costs and that future contracts should identify and implement restrictions on expense types in order to ensure that the funds are spent on activities that support the mission of the program. I think even though the $3,617 out of the sample was not a lot of money, some of those expenses I think just don't look good.

Twelve of the 38 draws we looked at included inadequate support for $4.2 million in expenses. That's not necessarily that the money wasn't allowed for those programs or wasn't spent correctly, but the support was not there in those documents that we reviewed. Of the 38 we tested there were six draws that were missing one or more of the required items on the draw checklist. I think this is a function of the draw checklist not being specific when there are exceptions to the rules. And so we suggested that the department clarify the draw checklist to more clearly communicate what's expected.

Also, the department does not require properties to include specific information on their third party inspection reports. As a result, there's a big difference in the variety of third party inspection reports that come in, and various stakeholders rely on those reports to determine the progress of the development. Because of that, I think it may limit the usefulness of the reports if they're all kind of different and don't tell you consistently the same things like how much of the development is completed or any potential issues or photos of the development, that sort of thing. So we felt like the department needed to communicate to the third party inspectors what they wanted to see in those reports so that there might be some increased consistency.

Are there any questions on this report.

MR. KEIG: On the first bullet point about the donations, late fees, gifts, food and party supplies, does FARs not apply to this type of contract, the allowable expenses?

MS. DONOHO: I don't think so.

MR. KEIG: But by analogy, I know FARs, penalties and that sort of thing, those are not allowed. I'm especially having trouble with late fees being allowed under this contract, but if thee's nothing in the contract and you're saying the FARs on allowable expenses don't apply, there's no recourse here. Is that my understanding?

MS. DONOHO: Right. And that's why our recommendation was limited to the next time we do these types of contracts we need to consider those things.

MR. KEIG: Putting that in the contract.

MS. DONOHO: Right. Because those things could be avoided.

MR. KEIG: Is that something that management is considering, along with legal and future contracting?

MR. IRVINE: Sure. We're always taking these processes as a way to improve and tighten up contracts and the processes. But on these specific expenditures, Teresa Shell, who administers the Exchange Program, might provide a little explanation and clarification.

MR. GANN: Good morning.

MS. SHELL: As it specifically relates to the incurred expenses, there were two that were significant costs. One was for prepaid interest that was being held in escrow accounts by one particular developer, and we did fund that, however, when it was pointed out to us that those funds were actually just sitting in escrow, I had the developer go ahead and pay those interest expenses. And there may be a point in time where that note is prepaid early so then there would be a reimbursement back to the property, so that would show up in the final accounting of that property.

The other item was for a management contract for like six months in advance, and it was for a transaction that has a developer that is very inexperienced, so the management entity, who is very well respected, took the approach that he was going to set up a plan and charged him for the entire amount. So I deemed that to be appropriate given the developer and the development and the issues that we've had with this transaction thus far. The management company is still in place and those fees have still been assessed.

As far as the donation, that was for an item that was donated to a constable's office. That item has been reimbursed back to the development by the developer, and they thought it was something that was a good idea but perhaps it was not.

The items for token gifts and party foods and balloons and those things, they were grand openings and groundbreaking, and traditionally those would be acceptable expenses. I can see where they would be questionable and I appreciate that being pointed out to us. Within the draw review process we have been questioning all the way down to $2 receipts because some of the draws they just submit their receipts, whether it be from Home Depot or WalMart or whatever it is, so we have them document those.

MR. KEIG: And how about late fees?

MS. SHELL: Late fees? There were some items that were paid for tax assessments for property taxes whereby they didn't pay their taxes on time and they were assessed a late fee. I don't think that's a good idea, however, we didn't have any prohibition for paying it, and it was a reimbursement for the expenditure.

MR. KEIG: Didn't we have at least some type of general clause in the contract that said expenses must be reasonable, some kind of reasonableness language?

MS. SHELL: Yes, sir.

MR. KEIG: I mean, that's the only one that really gives me a lot of heartburn is paying for their late fees.

MS. SHELL: Understood. The contract itself, to my knowledge, does not have any prohibitions on expenditures, however, obviously there is an additional test.

MR. KEIG: Are we going to have any type of look-back after we close this program out to spot check or a random sample or something like that to see whether there are other expenses that we might question and go back with recourse against that party?

MS. SHELL: I think that through our review process as it stands today, a lot of the sample that was taken for the audit were transactions and draws that were early on in the process prior to our setting out a standard and then typing up that standard. We held a webinar training and then we posted those trainings on the web in downloadable power points, and then I posted additional guidance to provide specific do not expend these types of items and this is not a good idea, keep it within a reasonable component.

MR. KEIG: If we're modifying internal controls but we've got some stop gap measures which reduce or mitigate the risks because we're trying to meet a deadline, then at least in my opinion it makes some sense to do some type -- and it's not necessarily an audit because she's already done an audit, her department, but some type of look back to see: Well, okay, we got this done, let's go back and take a random sample and see if there's any more costs that need to be recouped.

Education is great, and I believe in front-end education but there are some people that all the educating in the world isn't going to make a difference because they're going to push the envelope.

MS. SHELL: Understood.

MR. KEIG: Just something to consider in terms of managing the project and trying to save money -- or not save money but make sure we're spending money how we're supposed to.

MS. SHELL: Exactly. From a fiduciary standpoint and from just a common sense standpoint.

MR. KEIG: I don't have any other questions.

MR. GANN: And all good questions, good answers too.

MR. KEIG: Thanks.

MR. IRVINE: And we will go back and look at those types of contractual issues, not just in the Exchange contracts but in all of our contracts.

MS. DONOHO: I think from an auditor perspective, $3,617 in draws is not a material amount. We were just looking at it in terms of should we really be spending money designated for low income housing on these activities, and that's a question that we wanted to ask.

Item 4, Presentation and discussion of the status of external audits. Looking at the table in your board book, there were 16 external audits, reviews or monitoring visits for fiscal year 2011. That's, as far as I know, the most so far, certainly the most since I've been here. Thirteen of those are complete and the reports were released. We'll be talking about four of them under item 5, and we've talked about the other ones in past meetings we've had.

One is complete but the report has not been released. That was a Department of Homeland security's audit of the FEMA alternative housing pilot project which was part of the Disaster Recovery Program. At this point I would be surprised if we actually saw that, that will probably go to GLO.

Two of these are complete but no report is anticipated. These include HUD monitoring and technical assistance visit on a Section 8 pilot project and a Treasury review of the Tax Credit Exchange Program.

In fiscal year 2012 there are currently three external audits underway. These include the annual statewide audit by KPMG which is part of the state's annual financial process, the audits of the department's financial statements by the State Auditor's Office this year -- previously it was done by Deloitte -- and a HUD OIG review of the Neighborhood Stabilization Program which is also currently underway. We are providing support to all of these groups of auditors also.

Are there any questions on the status of external audits?

MR. KEIG: No.

MR. GANN: I don't have any questions. I'd probably like to make a comment, though, that the office did receive a letter from the Governor's Office stating that we had some prior audit issues and to make sure that we take care of all these that are coming out of the statewide audit, and also to ensure that any findings that are in the current year are properly addressed, so I just want to put that in the record.

MS. DONOHO: And we'll talk more about the prior audit issues on another agenda item.

Item 5 is Presentation and discussion of recent external audit reports. There were four external audit, monitoring or technical systems reports released recently, or between now and our last Audit Committee meeting.

The first one is a DOE monitoring report of the Weatherization Assistance Program. DOE has been coming quarterly so we have two of these we'll talk about. This first one was sent to us on June 28. They conducted an on-site monitoring visit to two of our sub-recipients, the Dallas Health and Human Services and the City of Fort Worth. They identified five findings and three concerns.

And the first finding was that an oven and gas range were replaced but they felt like the cost should be disallowed because the test results didn't support the replacement of these appliances under the health and safety standards. There were client files in Dallas that indicated that they were mixing ARRA grant funds and using it to pay for the same measures in the same home that they were also using DOE grant funds, and that's not allowable, it's a violation of DOE's guidance.

They had a concern that the department didn't issue a final financial and performance report for program years 2009 to 2010. That caused the reporting system to accumulate amounts for two years and resulted in inaccurate reports in the system. The final report was subsequently issued but they wanted us to correct the reports for 2011 and 2012 based on that report being submitted.

They also had lead safety forms and mold forms missing from client files in Dallas. Assessments and inspections were poorly done by Dallas agency personnel or their contractors, they were missing measures, missed opportunities. They had numerous issues with unit inspections for both of these sub-recipients. They included poor air sealing, no blankets or pipe wraps on hot water heaters, missing documentation for historic preservation, missing insulation, extensive sheetrock repair.

They also had a finding that the NEAT audit software was not being used correctly. This affects the identification of work that's done in a unit when they go out and do the assessment and it tells them what weatherization measures they need to put in place. They also had a concern about lack of a formal requirement to use the Texas Field Guide, and that affects the consistency of the work that's done if they're not following the field guide.

In addition, they also discussed the 13 under-performing sub-recipients that we have and the department's plans for managing these sub-recipients to ensure that the ARRA funds were spent.

Are there any questions on this report?

MR. KEIG: How are the 13 distributed across the state?

MS. DONOHO: I think management would like to respond to that one.

MR. DeYOUNG: Mike DeYoung, director of the Community Affairs programs.

The 13 under-performing sub-recipients are --

MR. KEIG: Is that going to be on Table 1, Carrollton, Fort Worth?

MR. DeYOUNG: Yes, in the report.

MR. KEIG: Dallas, Carrollton, Fort Worth. So it's all up in DFW but it seems like they went out west too, didn't they?

MS. DONOHO: The next report is the West Texas

MR. KEIG: Right. So my question is I seem to recall we did some education on the front-end for this, we even hired a contractor or something, but we did some education for the people that were going to go out in the field and do the work, and the Davis-Bacon Act and all kinds of stuff.

MR. DeYOUNG: Yes. We have a training academy that we've used to train and ramp up all the sub-recipients, and they can send staff and actually contractors to that training academy.

MR. KEIG: And is the training academy done regionally?

MR. DeYOUNG: The training academy has classes held at regional sites that subcontractors, sub-recipient staff can go to as well as TDHCA staff. We also have the ability to go directly to an agency that is experiencing difficulty in any aspect of the Weatherization Program.

MR. KEIG: So did the folks in DFW get the same training as the people out in West Texas?

MR. DeYOUNG: Yes.

MR. KEIG: And West Texas seemed to have a whole lot less issues going on than DFW, just my impression from these reports. Is that a fair assessment, or is there something else involved there that's skewing that?

MR. DeYOUNG: The team that was involved in the Dallas-Fort Worth assessment was different from the team from DOE that was involved in the West Texas assessment.

MR. KEIG: All right. What types of actions are we taking to try to get some of these issues corrected, especially up in the Dallas-Fort Worth Metroplex?

MR. DeYOUNG: Each time we have a monitoring report from DOE or a TDHCA monitoring, the findings that we discover or even concerns are entered into a database, and as we look for training opportunities that feeds into the direction that we take with the training academy or with our on-staff trainers that we have at TDHCA. If we feel like it's limited to a single sub-recipient and it's a very narrow focus, say the NEAT audit, one of the findings is improper use of the NEAT audit, our staff would go up and we would conduct a one day or one-and-a-half day very targeted training based on the DOE finding. Whether it was improper measurements of insulation or when they're actually inputting data into the audit they're not making accurate assessments of the building, we would try and focus on those individual items.

From a bigger perspective, if we see that this is being repeated over at Fort Worth and at the City of Dallas and Arlington, we would call all four together and say: Look, we need to have a day where everybody brings their assessors in or their auditors in and let's sit down and talk about how this audit works, how the interaction of the audit and the information that we gathered during the assessment affects the outcome from the audit because that's what determines what work will be done in the household.

And some of these findings which you see here result from improper assessment, some work right before the audit that probably wasn't done to the level that we want, and so you don't have a hot water heater being wrapped because it probably wasn't inputted into the audit and it's just a simple input, but in many instances they weren't doing that. And we know it because we can look at that audit and say did that water heater rank, it's a $5 piece of material, it should rank every time, but if it's not in there we know they didn't assess it or they didn't get it inputted, so then we go back to their paperwork during the assessment and see was this even written up in the document, did they think about water heater wrap, and if they didn't then that's a training issue, whoever is doing the audit isn't doing that completely.

MR. KEIG: Do you have enough resources to try to take care of these issues?

MR. DeYOUNG: Yes, we do.

MR. KEIG: Did you want to say something?

MR. IRVINE: I would just say that the key to this, and this was hammered pretty hard by Bob Adams and the DOE folks when they were in here recently, and that is when you identify the problem, whether it's identified through audit, inspection, whatever, the agency itself needed to prioritize not only how it's going to get whatever didn't get done fixed but how it's going to change its systems and train its people to ensure that those things don't recur.

The real objective here is that the weatherization team goes to the house once, and this back-and-forth stuff about we went out and we did a really good job, somebody found some problems and we went back and fixed it up some more is really slowing the program, and I think it's something that really does raise eyebrows with DOE and it's something our team is very, very focused on.

Our training academy, ACS is the third party provider for that, they've been great, but these, quite honestly, are hands-on issues that involve TA from our team. Now, I think that it also links to a larger, more systemic kind of issue and that is we've got some folks that just aren't getting it, and we are dealing with those kinds of issues in other ways.

MR. GANN: It seems like to me, though, this is elementary, the one we're talking about is elementary where you wrap a pipe, and it seems like we've got too much government involved, frankly, to be honest with you, but those guys that are on the bottom line, all you have to do is have one man change up and come down and they're just trying to follow what's above them. But we need to have a paragraph in there saying: Hey, if you see something as a contractor or subcontractor or worker that you know is not supposed to be that way, then bring it up. Because that's stuff that should be elementary and they should be going back themselves and checking it before it ever got to us. And maybe a paragraph to say that, you know: If you see something wrong and you're a handyman, speak up.

MR. DeYOUNG: Lean forward.

MR. GANN: Yes. Because this stuff is typical for construction because you can change one man in a five-man crew and if he's the one wrapping the pipe and he doesn't care, that's the way it works. Just a paragraph is all you're talking about.

No more questions?

MR. KEIG: No more questions.

MS. DONOHO: The next report is another DOE monitoring report of the Weatherization Assistance Program. This one came out on September 1. DOE conducted on-site monitoring visits at three sub-recipients. These are the West Texas ones: the City of Lubbock, West Texas Opportunities in Lamesa, and Texas and South Plains Community Action Agency in Levelland. They didn't identify any findings during this monitoring visit.

They had one concern and some issues that they felt like required corrective action. Their concern had to do with procurement training for West Texas Opportunities and South Plains Community Action Agency. They said that the prices submitted by bidders for materials and labor were used as a negotiating tool to provide pricing by preferred contractors rather than accepting the lowest bid. They recommended that the department provide additional procurement training for these sub-recipients. The corrective action that they required was to address several technical problems noted in the units that they inspected. Again, we're talking about water heater tank wrapping, pipe insulation, water heater venting.

They also noted that the prioritization was based on time spent on a waiting list at two sub-recipients which was not an allowable practice and they also felt like the inspections were poorly done in all of the units that they visited. As a result of the inspections being poorly done, measures were missed or were not corrected prior to them being reported as completed units.

Are there any questions on this report?

MR. GANN: I don't have any.

MR. KEIG: No.

MS. DONOHO: The next one is Section 8 Management Assessment Program, our CNAP certification. The CNAP is something they do every year. The CNAP review rates the department's Section 8 program on 15 program educators identified in the Code of Federal Regulations and it provides an overall score for the department. The department scored 85 percent which is considered standard; 90 percent would have gotten us a high performers rating.

The department had one area in which it scored zero which was lease-up. There was also another zero on the report in your list but that one was a deep concentration bonus, it's optional and we don't use it here at the department.

So as a result of the lease-up score, the department reports they have purged the waiting lists for nine local operator areas and reopened the lists in two areas that have sufficient housing stock, so hopefully that will fix that problem.

Are there any questions on this report?

MR. KEIG: One.

MS. DONOHO: The next report is the HUD monitoring report on the Homelessness Prevention and Rapid Rehousing Program, HPRP. That one was released August 16.

HUD examined the department's implementation of the HPRP program including activities, policies and procedures, program process, eligible activities and oversight of sub-recipients. They concluded that the program was well managed, staff was knowledgeable regarding the program requirements. They didn't have any instances identified of ineligible activities, they didn't identify any findings.

They had one significant concern which was that the department completed monitoring on all 58 of the sub-recipients, they identified 19 of these sub-recipients for full monitoring visits, however, only nine had been monitored as of the date of the review and only five of the monitoring reports were sent out. The agency's standard operating procedures require that monitoring reports be sent out within 45 days of the monitoring visit. The first three reports out of the five exceeded the 45-day deadline by an average of 71 days, the last two took two weeks longer than the 45 days. HUD recommended management review this requirement and make adjustments to the monitoring review time.

I'd also like to mention here that Internal Audit identified this issue in our last audit of the Community Services Block Grant programs as well which was in 2009, I believe.

Are there any questions about this report?

MR. KEIG: Just for management, what are we doing to address that concern?

MR. DeYOUNG: The timeliness issue, we're working with staff to get the reports out quicker. The reality is that we were starting up a new program with new staff who are new to TDHCA, we didn't have a template for monitoring these, we tried to modify some of the existing monitoring reports format to fit this new program from the Federal Government. The first three reports took a dramatically long time since we had individuals who had never drafted a monitoring report working in new regulations, a lot of back and forth between the project manager and the monitor assigned to the agency.

The deadline of 45 days, as Sandy mentioned, is a self-inflicted -- for lack of a better term -- deadline. We could make it 60 days, I'd like to keep it at 45 because I think that's responsive to the sub-recipients. If we find something, I want to notify them as quickly as possible.

I think over the last month we've been able to work within that time frame. We're on target to get all the reports out now within 45 days. Is there a possibility still that we could exceed the 45 days? Yes, because again we're dealing with new sub-recipients, new regulations. So every effort is being made to meet that 45-day deadline, we've worked very closely with our monitoring staff to try and alleviate a lot of the back and forth, trying to get a more friendly format for the reports, so that we should be able to meet the 45 days. I would really not want to entertain extending that deadline to 60 days, I think it's more important that we get them the corrective action and our concerns so that they can start immediately on resolution of those issues.

MR. GANN: I think we all realize what was going on a couple of years ago and we were all busy and adding new personnel right and left, huge increases. And Sandy, I appreciate you and your group for picking up these kinds of -- they're not little things but these kinds of things and bringing them to our attention even two years ago. But we need to continue to work on it and start achieving some of that too, so good luck on that too.

MR. IRVINE: And while it may be untypical of some of the new things that will emerge, it's a one-time thing.

MR. GANN: And overall I noticed we got good high marks on it, so great. I don't have any other comments.

MR. KEIG: Me either.

MS. DONOHO: Item 6 I have been looking forward to all day, Presentation and discussion of the status of prior audit issues. The reason I've been looking forward to this is as I've mentioned several times, when I came to TDHCA four years ago I inherited 457 prior audit issues and those dated back almost ten years. We have followed up and cleared all of those issues as well as the issues from 59 internal and external audit reports that had findings over the past four years. This is work that we do outside of our planned audits and I'm very grateful to my staff who worked very hard this summer to clear these issues. We have a few that are still outstanding but it's just a handful.

Of the 64 that we had last time, 24 were reported previously as implemented, we verified and closed those. There were 24 reported by management as implemented and those are on the attached list, so we have nine from Community Services and 15 from the Neighborhood Stabilization

Program that are reported as implemented. There are six issues that are in the process of implementation, two from Community Affairs and four from the Neighborhood Stabilization Program. So those 30 are what we have that we're working on now waiting on responses. The other 24 are ones that we need to clear.

The 15 from the Neighborhood Stabilization Program, we have on our audit plan for this coming year a followup of the Neighborhood Stabilization Program so we didn't clear those 15 because we're waiting to do that during our followup audit. So really we just have nine from Community Affairs. Some of those, as Mr. Keig pointed out, are a little old and that's because we clear issues based on where the issue came from, how important we think the issue is, what documentation or work we have to do to support it. So the nine that we have outstanding we have some documentation that we recently received from Community Affairs and we're going to get those cleared pretty quick here. But our backlog is gone so that's the very good news.

There are ten issues that we transferred to the General Land Office with the Disaster Recovery Program. We also shared our tracking database with them so that they could go forward on attempting to clear those.

MR. KEIG: Did we give them a copy of that non-audit report?

MS. DONOHO: I'm sorry?

MR. KEIG: The non-audit report, did we give that to the General Land Office as well?

MS. DONOHO: Yes, absolutely.

MR. GANN: They had to be appreciative of that.

MS. DONOHO: I hope so. I think that it gave them a starting place, you know, here's the history of this program, here's the numbers as of a month before of how many houses had been built and that sort of thing, so I think it at least documented that for them. And then the ten prior audit issues I'm sure they weren't nearly as excited to get.

But anyway, the good news is that we've cleared all of them with the exception of the 19 NSP issues that we'll clear during our followup audit and the Community Affairs issues that we're working on now.

Part of the reason that we pushed to finish this, besides the fact that it's taken a long time is because we're getting ready to switch to a new database. Essentially we're going to use our software that we use to do our audits to track these, so I think the repots that you see on these for future Audit Committee meetings will be clearer and a little easier to understand than in the past.

Are there any questions regarding prior audit issues?

MR. KEIG: No.

MS. DONOHO: Item 7 is Presentation and discussion of the status of the Fraud Hotline and fraud complaints. In fiscal year 2011 Internal Audit handled 91 fraud complaints, so this in addition to our audit work. Even if they don't relate to what the department does, it still takes our time to refer the complainant to the appropriate authority, to refer the complaint to program staff, or to follow up on the complaint ourselves. Even if we don't take the lead in investigating it, we still do some initial work up front on all of these.

Of the 91 that we received, 60 were calls from our hotline, 12 of them related to the department's programs, the other 48 were not related to the department's programs, so those were people where we referred them to the local housing authority or to another state agency depending upon the nature of the complaint.

The 12 that were related to department's programs and staff, five were from Weatherization or CF, two from Neighborhood Stabilization Program, two from Disaster Recovery, two from Multifamily, one from Manufactured Housing. Of the 12, four were related to eligibility for programs, one theft, two fraud, one waste, one kickback, just kind of a wide range, two were employee things, one was a rule violation. Nine of the 12 we referred to programs, two were referred to our oversight agencies -- that includes the State Auditor's Office, the Attorney General's Office, HUD OIG, DOE OIG, HHS OIG, FBI, depending on the complaint -- one of them was handled internally.

There were 31 complaints that we received from other sources: there were ten from Weatherization, seven from Disaster Recovery -- so the good news hopefully that number will drop next year since we no longer have Disaster Recovery -- seven from Tax Credits, two from CSBG, two from HOME, two Section 8 and one Manufactured Housing.

Nineteen of the 31 complaints that we had that didn't come in on the hotline came from TDHCA staff. I think the good news about that is that our efforts to get the word out to staff about how to deal with complaints of fraud, waste or abuse seem to be working, and I was really excited to see that when we put these numbers together because we've made an effort to put up signs in the break room, management has sent out emails to all the staff about how to handle fraud, waste and abuse complaints. I think that process is working.

The news that's not so exciting is that only one of these came from our sub-recipients and our sub-recipient network, and I know that Michael DeYoung and his group have put together fraud, waste and abuse training for their sub-recipient network and so those people have had that training but they're not referring complaints to the department. So Tim and I have talked about management and Internal Audit working together to try to get the word out to the sub-recipients about the fraud, waste and abuse hotline and about complaint handling, and hopefully that will increase.

MR. IRVINE: And I think that the sub-recipient challenge is a matter of creating an environment where they understand that reporting fraud, waste and abuse is not tripping the guillotine, it's starting a curative and aggressive beneficial process. I think that Sandy has just been great on these ones that we've identified internally and we've all come together to work through them and figure out how to handle them. In one major instance of a misapplication of a whole lot of government money in a local sub-recipient, they self-reported and I'm pleased to say they were aggressively on top of the situation, bringing in new people, new policies, new procedures, new controls, fixing the problem both retrospectively and prospectively, and we worked with them. And I think that in doing that we communicated we like people that identify problems and fix them. So the problem, I guess, in getting out that word is people aren't going to stand on the rooftops and talk about their fraud experiences.

MS. DONOHO: So the 31 that we received that weren't on our hotline, 15 of them we referred to program staff. When they're referred to program staff, generally it's because they're not really fraud, waste or abuse, they're just other problems, a rule violation or some questionable activity that's probably not fraud as far as we can determine.

As you are probably aware, we have a statute that requires us, once we have achieved a reasonable belief that fraud has occurred, to refer that to the State Auditor's Office, so on every complaint that we get we make a written referral to them. And then we also refer them to the appropriate oversight. Once that happens we really don't know what happens with those cases, so for the 31 that we have, 12 of them were referred to our oversight agencies and four of them we found no evidence that anything wrong has happened. So on those 12 unless they come back and tell us that somebody got indicted or something happened with those cases, we really don't know what happens.

MR. KEIG: Are we supposed to take like administrative corrective action before we refer it to them, or is that part of the referral process, you work out what they tell you, go fix this but we're going to look further into this?

MS. DONOHO: If it's something that relates to a program it may be that we do something here at the department but we still make the referral.

MR. KEIG: It seems we have to stop the bleeding because we don't know what they're going to do after we refer it to them. And I don't know if you've had any specific situations where it's been an issue, but if we identify say $100,000 that needs to be returned to the department, do we go ahead and take steps to do that, or are we just referring it on to SAO?

MR. IRVINE: We take it really on a case-by-case basis. As soon as these issues are identified, we convene a group of Sandy, our program people, our legal or our public relations people, we all kind of close ranks. Typically one of the first actions on a contact is if you've got something that really indicates that they just don't have systemic adequate controls and would want to present a risk of more loss, we shut the program down.

Now, as for recouping those costs, generally these are small, broke nonprofits and it's not going to be a high recovery opportunity, but we do coordinate and protect those rights. We bring in the OAG's bankruptcy division to advise us on those issues. We have not really been looking at the administrative penalty matter because, frankly, like I said, there's no money there and the biggest objective is to lock it down and protect against future loss.

MS. DONOHO: And those are processes that don't really involve Internal Audit because those are management decisions: how do you handle the sub-recipient, are you going to recoup any money, that sort of thing. That's not within our purview in Internal Audit so once we've done what we needed to do to determine that yes, this is a valid case, then management decides how they're going to handle it from there.

The ones that we refer to the program staff are generally not fraud. For example, there may be a complaint regarding landlord-tenant relations at a Tax Credit property and we may talk with Patricia about that and then the next time her staff goes out to monitor they might look at those files into that issue or make a trip out there. But if we don't feel like there's that level of fraud that we've identified that needs to be referred and that sort of thing, the case ends. So that's why it's difficult to tell you how they were all resolved because the ones that we believe are fraud go to somebody else outside the agency and then we don't know what happens with them.

I guess that's all that I have for fraud, waste and abuse. Are there any questions on this item?

MR. KEIG: No.

MR. GANN: No.

MS. DONOHO: That concludes the agenda items.

MR. OXER: Mr. Chairman, I have a question.

MR. GANN: Okay.

MR. OXER: I know there's no followup on that but is there a way to do an after action report just to check back on those?

MS. DONOHO: The ones that we refer to the external?

MR. OXER: The ones that you have substantial cause to believe there is actually fraud, waste and abuse.

MS. DONOHO: It depends on where the referral goes and who handles it. For example, I have some Disaster Recovery cases that I worked on -- and we also continue to work on these cases if we're asked to -- I had some Disaster Recovery cases that I worked on with HUD OIG and it took about two years for one of those cases to be indicted.

MR. OXER: You can run but you can't hide.

MS. DONOHO: Right. In that case they did come back and say we have an indictment on this person and they were arrested yesterday, and so we're informed to that level. But sometimes it takes years for these cases.

MR. OXER: I think it would be something to be worth pursuing to be able to, frankly, the way they say in West Texas, put a few notches in our pistol so let's make sure that anybody who's going to try this knows we're going to come after them.

MS. DONOHO: And I think that we're always pleased to see us make the news because it makes it clear that the agency has a policy of not tolerating abuse of our funds.

MR. GANN: Mr. Chairman, we appreciate your comments, and this is the open public comment section, would you mind signing one for us.

(General laughter.)

MR. OXER: More than happy to.

MR. GANN: Thank you, sir, we appreciate it.

I think that concludes our agenda items. And Matt, we're glad to see you onboard. Get on that other side as soon as you can, that stuff you can't touch right now, because I know you're an expert at it.

That concludes our agenda.

MR. KEIG: Do we need to move to adjourn?

MR. GANN: No, we don't have to, we just adjourn. Thank you so much. We are adjourned.

(Whereupon, at 8:25 a.m., the meeting was concluded.)

C E R T I F I C A T E

MEETING OF: Audit Committee

LOCATION: Austin, Texas

DATE: September 15, 2011

I do hereby certify that the foregoing pages, numbers 1 through 35, inclusive, are the true, accurate, and complete transcript prepared from the verbal recording made by electronic recording by Nancy H. King before the Texas Department of Housing & Community Affairs.

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(Transcriber) (Date)

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