

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

AGENDA

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P R O C E E D I N G S

1
2 MR. CONINE: Let's call the Audit Committee
3 meeting of the Texas Department of Housing and Community
4 Affairs to order April 26, 2001, at about 9:10.
5 I'll call the roll this morning. Kent Conine,
6 chair, is here.

7 Jim Daross?

8 MR. DAROSS: Here.

9 MR. CONINE: Marsha Williams?

10 (No response.)

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

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

16 (No response.)

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

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

22 MR. DAROSS: Move the minutes be approved.

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

25 MR. DAROSS: Aye.

1 MR. CONINE: All opposed?

2 (No response.)

3 MR. CONINE: Motion passes.

4 Tab 2, presentation, discussion, and possible
5 approval of amendments to the fiscal year 2001 audit plan.
6 Mr. David Gaines.

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

9 MR. CONINE: Good morning.

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

11 MS. STINER: Good morning.

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

16 MR. CONINE: We're in trouble already.

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

20 (General laughter.)

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

25 MR. CONINE: Okay.

1 MR. GAINES: That will allow them to move on to
2 other things if they have other engagements this morning.

3 In that case I'll introduce Mike O'Brien of
4 KPMG.

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

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

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

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

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

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

24 MR. CONINE: All right.

25 MR. O'BRIEN: Just to go over again, as we do

1 every year, our responsibility as independent auditors is
2 to audit the financial statements of the department, and
3 we're talking about the annual financial report that is
4 issued by the department. The report is prepared by
5 management of the department and we audit the financial
6 statements and express an opinion.

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

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

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

24 There are many other controls that we don't
25 look at, and that's why you have David Gaines and an

1 internal audit group, because there are controls out there
2 that don't deal with financial reporting but definitely
3 impact the operations of the department.

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

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

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

25 You don't have a lot of history on how those

1 will pay off, because a lot of those loans don't pay off
2 until the loan is --

3 MR. CONINE: Due upon sale or refinance.

4 MR. O'BRIEN: Right.

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

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

12 MR. CONINE: Now --

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

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

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

24 MR. CONINE: That's kind of apples and oranges,
25 isn't it?

1 MR. O'BRIEN: They're attached to the same
2 property.

3 MR. CONINE: Okay.

4 Help us, Bill.

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

14 MS. STINER: Mr. Chair.

15 MR. CONINE: Yes.

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

20 MR. DALLY: We used our experience with the
21 first lien to look at the delinquencies there, and then we
22 did add a factor of about 40 percent I believe to that,
23 and that was negotiated. I kept saying, No, without a lot
24 of experience I'm erring on the side of conservatism, and
25 they still felt we were over-accrued or had too high an

1 estimate on that allowance that more or less we're going
2 to repay, so I said, Okay.

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

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

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

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

22 Okay. Go ahead.

23 MR. O'BRIEN: Obviously this is an estimation
24 process, and as new information comes in every year you
25 can expect the allowance to be increased if needed, or

1 decreased, if needed based upon current information. But
2 as of year-end we're comfortable if there's an adequate
3 allowance on the balance sheet.

4 MR. CONINE: Okay.

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

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

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

25 There weren't any disputes or disagreements

1 with management. We received from them full cooperation
2 as usual.

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

4 MR. CONINE: Mr. Daross?

5 (No response.)

6 MR. DAROSS: No questions.

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

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

11 MR. CONINE: Yes.

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

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

19 MR. CONINE: Time out. (Perusing documents.)
20 There it is.

21 MR. O'BRIEN: In auditor's terms these are not
22 considered material weaknesses, which would be items that
23 would be significant enough to cause a material
24 misstatement in the financial statements. These are
25 simply recommendations that we bring forward to management

1 for consideration, and we just go over them with you for
2 information.

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

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

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

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

22 MR. DALLY: We are going to classes and
23 training and we'll be working in concert with the
24 comptroller. The comptroller ultimately has the
25 responsibility for the financial reporting of the entire

1 state, and so they set out a subset of rules to us as
2 agencies to pull these things together.

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

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

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

24 There will be a lot more work for staff because
25 the look of these financial statements will significantly

1 change come next year.

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

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

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

12 MR. DALLY: Yes.

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

15 MR. DALLY: Yes.

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

18 MR. DALLY: That's right.

19 MR. CONINE: Okay. Thank you.

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

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

23 MR. DAROSS: No.

24 MR. CONINE: Ms. Stiner, do you have anything
25 to add?

1 MS. STINER: No, sir.

2 MR. CONINE: Good report.

3 MR. DALLY: Thank you.

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

6 Mr. Gaines?

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

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

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

22 MR. CONINE: Okay.

23 MR. GAINES: And there's several projects that
24 I'm proposing to drop for reasons I'll discuss in a
25 moment, but those reasons are in addition to basically

1 just not having enough time.

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

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

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

19 I will say in my discussions with the
20 information services director since he's come on board,
21 he's noted considerable vulnerabilities to the system, and
22 he's mentioned -- he's been working with the staff to
23 resolve those and correct those weaknesses, and I believe
24 the most recent update I had with them they're pretty well
25 satisfied with where they're at at this point.

1 I'm proposing dropping the Section 8 audit
2 because HUD has requested that we have a program-specific
3 audit by independent auditors to review the department's
4 compliance with the Section 8 financial management
5 requirements, and the department's chief financial officer
6 is currently in discussions with the external auditors to
7 have that audit conducted by the end of this fiscal year,
8 August 31.

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

11 MR. GAINES: Yes, sir.

12 MR. CONINE: Okay.

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

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

1 quarterly review we did.

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

5 Are there any questions relating to this in
6 particular?

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

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

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

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

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

24 If there's a continued need or a demonstration
25 of need for the internet security audit that's something

1 that we could consider contracting out for if we don't
2 have the in-house expertise, as we would do with any
3 project where we didn't believe we had the expertise.

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

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

10 MR. CONINE: That he could generate.

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

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

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

24 Sid, I don't guess you'll be violating any
25 trade secrets by telling us what you're doing to address

1 them? Please answer that. I don't know how public we
2 want to make those, but we certainly could provide that to
3 members of the committee.

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

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

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

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

24 MR. CONINE: It strikes me, Mr. Daross, as
25 having someone new coming in almost like an audit in and

1 of itself, and maybe if you could furnish us with a copy
2 of the one that was recently completed maybe that's all
3 we'll need to take a look at.

4 MR. STRUSS: We sure will.

5 MR. CONINE: Thank you.

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

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

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

19 MR. GAINES: That's what we're currently
20 planning on. What's remaining in the plan is two audits.

21 One of them we -- the single-family liens procedures we
22 should really just be getting started on, so we're
23 planning towards the end of this fiscal year for that.

24 And then the other one that's been pushed back
25 to August 31 is the community services monitoring function

1 that the auditor who is currently on maternity leave has
2 been performing, and I believe she's expected back in June
3 sometime, so I was going to push that back and allow for
4 that.

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

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

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

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

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

18 MR. CONINE: I'll second that.

19 All in favor, say aye.

20 (A chorus of ayes.)

21 MR. CONINE: All opposed?

22 (No response.)

23 MR. CONINE: All right.

24 MR. GAINES: The next item on the agenda is the
25 software license audit I was just referring to, and I'd

1 like to turn that discussion over to Sam Ramsey, the lead
2 auditor on that project.

3 MR. CONINE: Good morning, Mr. Ramsey.

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

7 MS. STINER: Good morning, Mr. Ramsey.

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

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

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

20 MR. RAMSEY: Okay.

21 This audit was a scheduled review in our FY
22 2000 audit plan. You may note that if you have that
23 available. But before we get started, does anybody need a
24 copy of the audit report?

25 MR. CONINE: I've got one.

1 MR. RAMSEY: Overall -- I'll just get into the
2 audit objectives.

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

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

15 In addition, our review included a review of
16 controls of the adequacy of purchased [phonetic] software.

17 In other words, basically how we manage software in the
18 agency. So that was our primary objectives for the audit.

19 Any questions along those lines?

20 (No response.)

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

25 With regard to the legislative requirements of

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

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

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

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

1 progress on what was being planned.

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

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

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

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

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

16 MR. RAMSEY: How would I characterize it?

17 MR. CONINE: Yes.

18 MR. RAMSEY: It's just something that we've
19 purchased software and not really given it the attention
20 that we should have. It's just -- the situation seemed to
21 end up being the way it was, or is. Lack of policy and
22 procedures too, but in talking with -- working with the
23 ISD staff right now, Sid, Curtis, and so forth, they've
24 undertaken a lot of what needs to be done right now to get
25 things in shape as they need to be or should be.

1 MR. CONINE: And how long has Mr. Curtis been
2 on board?

3 MR. HOWE: I'm Curtis Howe.

4 MR. CONINE: Hello.

5 MR. HOWE: I've been on board since November of
6 2000.

7 MR. CONINE: Okay.

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

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

11 MR. CONINE: Yes.

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

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

25 So it's a task that the new IS director has

1 undertaken, and we've talked about it extensively how you
2 control the installation of software and avoid any illegal
3 use of licenses in the department. But as I said,
4 traditionally that has been an individual procurement
5 request from the various divisions.

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

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

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

24 MR. CONINE: I guess what about the requirement
25 to report to the LBB cost savings or whatever we're

1 supposed to from a statutory -- I guess from a statutory
2 respect that were not reported? Is that something that we
3 just found out that we were supposed to be doing, or
4 something we knew about but we just didn't do?

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

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

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

24 Sid, do you want to comment since the
25 discussion is about this? Will you come forward and just

1 share with the committee the status of --

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

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

17 When I came on board I did my own audit. I'm
18 not an auditor, but my own feasibility study -- and I
19 realized that I've never seen a maintenance fee as high as
20 the maintenance fees we were paying here. So I had gotten
21 with our director, David Gaines, to say I think we ought
22 to take a look at this House bill and you guys confirm,
23 what are we missing here? What are we supposed to be
24 doing to make sure that we live up to all the requirements
25 that we're supposed to do?

1 And Sam's done a very good job as far as
2 finding what we have been missing in this agency that we
3 need to do.

4 We also did find and discover -- I think Curtis
5 may verify the exact number, but I believe it was some
6 \$40,000 that we immediately just wiped off the list in
7 maintenance fees that we have been paying for software
8 that we have not even been using. It was for applications
9 that were on the servers that we weren't using. So this
10 whole software -- this whole deal is really good because
11 it does help agencies save money if they go in and perform
12 what they're supposed to.

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

18 MR. CONINE: Any other questions?

19 (No response.)

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

21 MR. STRUSS: You're welcome.

22 MR. RAMSEY: Any other questions, comments?

23 (No response.)

24 MR. RAMSEY: I'd like to point out that
25 typically -- not typically but in the past we've had a

1 difficult time getting timely responses and so forth
2 during the course of our audits. I just want to mention
3 that working with Sid and Curtis and his staff, they've
4 been very timely and helpful in getting everything we
5 need.

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

10 MR. RAMSEY: We will track those.

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

13 MR. RAMSEY: Thank you.

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

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

21 MR. CONINE: Good.

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

25 We have three issues for which the action has

1 been delayed, and there's one issue for which no action is
2 intended.

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

5 MR. GAINES: The last time I checked.

6 And I'm not real sure exactly how you'd like to
7 go through these, and to what level and degree, if you
8 have any particular questions --

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

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

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

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

21 MR. CONINE: Okay.

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

25 And then there's one --

1 MR. CONINE: There's 37 and eleven.

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

4 MR. CONINE: Okay.

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

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

9 MR. CONINE: Okay.

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

12 MR. CONINE: All right.

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

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

23 MR. DAROSS: The only one of these items that I
24 have a real concern about I think everyone on the board
25 does, and that's the subrecipient monitoring process.

1 That's apparently coming along and is on target.

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

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

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

25 MR. DAROSS: So that July 31 date is just to

1 wait for HUD's response?

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

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

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

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

24 I believe the department can proceed with this
25 regardless of the status of the departmentwide database.

1 In fact, some of the program areas have in regard to the
2 risk assessment. The compliance division has implemented
3 risk assessment process and is currently using that for
4 the HOME and CDBG programs. Energy assistance has
5 developed and is using the risk assessment model and is
6 using it for their selection of subrecipients to monitor.

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

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

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

22 And in the Housing Trust Fund and Section 8
23 programs this is still in the future. They're evaluating
24 what they should be doing and trying to figure out where
25 the information comes from to move forward. In Section

1 8's case I believe there's no significant monitoring
2 function to begin with, so they're going to have to, of
3 course, establish a function in order to deal with this
4 kind of issue.

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

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

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

23 MR. CONINE: Ms. Stiner, any comment from
24 management side to the process here and how we're moving
25 along from your perspective?

1 MS. STINER: Thank you, Mr. Chair.

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

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

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

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

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

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

1 off --

2 MR. CONINE: That's good to hear.

3 MR. GAINES: -- the future report. Okay.

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

6 MR. CONINE: Sixteen. You're right.

7 MS. STINER: Good.

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

11 MR. CONINE: Okay.

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

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

25 Of course, this time frame was September 1,

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

7 MR. CONINE: Okay.

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

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

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

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

24 MR. GAINES: Yes. Well, we believe the audit
25 has been completed. They're in the reporting phase, so I

1 guess the audit's not completed until the report's out.

2 I believe -- we were talking with management
3 recently. They believe the check's in the mail.

4 MR. CONINE: Okay.

5 MR. GAINES: Is that right?

6 MR. DALLY: Yes.

7 MR. GAINES: So we need to trace that audit
8 down. It presumably is in the mail, and we're in the
9 process of getting more aggressive on trying to find that.

10 I will just point out during that exit
11 conference the results were fairly successful, as that's
12 one of these audits we need to be doing this with.

13 MR. CONINE: Okay.

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

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

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

19 MR. CONINE: And the CDBG subrecipient
20 monitoring --

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

25 MR. CONINE: Any other comments, Mr. Daross?

1 MR. DAROSS: No.

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

4 MS. STINER: No, sir.

5 MR. CONINE: A nice report.

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

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

10 MR. GAINES: Yes, sir. Thank you.

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

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

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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.

(Transcriber) 05/01/01
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