

TEXAS DEPARTMENT OF HOUSING AND COMMUNITY AFFAIRS

AUDIT COMMITTEE MEETING

4:00 p.m.
Tuesday, November 9, 2010

Room 116
TDHCA Headquarters
211 East 11th
Austin, Texas

MEMBERS PRESENT:

GLORIA RAY, Chair
TOM GANN
LOWELL KEIG

STAFF PRESENT:

MICHAEL GERBER, Executive Director

AGENDA

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PROCEEDINGS

MS. RAY: Well, the computer says it is exactly 4:00 p.m. And with that, the Chair calls the Audit Committee of the Texas Department of Housing and Community Affairs, November 9 meeting 2010, to order. The Chair, Gloria Ray, present. Tom Gann?

MR. GANN: Present.

MS. RAY: Lowell Keig?

MR. KEIG: Present.

MS. RAY: We have a quorum. We have 100 percent of our committee members available. And as is customary, with the Audit Committee meeting, the Chair would like to recognize that --

I don't have any witness affirmation forms in front of me. Are there any witness affirmation forms?

(No response.)

MS. RAY: There are not affirmation forms. Is there anyone that wishes to make public comment at this time and to fill out an affirmation form?

(No response.)

MS. RAY: Hearing none, let the record show that we have no public discussion at this time. The Chair recognizes Sandy Donoho, the Director of Internal Audit to begin the presentations as called for in the report items.

MS. DONOHO: Thank you. Item 1 is presentation, discussion and possible approval of the Audit Committee meeting minutes for

July 28, 2010. The Audit Committee minutes are in your Board book.

Are there any questions regarding the minutes?

(No response.)

MS. DONOHO: Staff recommends approval of the minutes.

MR. GANN: Move to approve.

MR. KEIG: Second.

MS. RAY: It has been moved and seconded to approve the minutes of the July 28, 2010 Audit Committee. Is there any discussion?

(No response.)

MS. RAY: All those in favor, please say aye.

(A chorus of ayes.)

MS. RAY: Those opposed, no.

(No response.)

MS. RAY: The ayes have it. And we can go to Item 2.

MS. DONOHO: Okay. Item 2 is presentation, discussion and possible action on the proposed Internal Audit plan. The Internal Audit work plan is required by the Texas Internal Auditing Act, which is the statute that governs the Internal Audit functions.

The plan outlines the work that Internal Audit will undertake in the coming year. It is based on a complex and lengthy agency-wide risk assessment that is done by the Internal Audit staff. It includes interviews of staff, surveys, research into statutes, federal regulations, and review of program information.

Looking at the draft plan in your Board book, we have two

carryover audits on the plan from last year. The largest is an audit of the neighborhood stabilization program. And we are currently working on that audit.

We delayed the start of that project in order to allow management time to get the NSP funds committed by the September 3 deadline. We are in field work, and we hope to have that one done by Christmas.

The other carryover project is an audit of IT governance that is required by our audit standards. We have completed this audit. Management has a draft report, and we are waiting on their responses. So we hope to have that to you in the next week or two.

There are four new audits on the plan. We scaled back a bit this year because of our anticipated workload in the area of management assistance and special projects. The four new audits that we are proposing cover our highest risk areas: weatherization, disaster recovery, TCAP and exchange.

We also have a number of special projects and other tasks that are required either by state law or by our auditing standards. And those are at the bottom part of the plan.

These include a quality assurance self assessment, which is our self assessment of whether we comply with our audit standards; a revision of our audit charter and our Board resolutions, which is now an annual requirement; an update of our policies and procedures; as well as ongoing tasks that include coordinating with our external audit partners, following up on

prior audit issues, monitoring ARRA funds, and handling our fraud hotline and other fraud complaints.

One of the most exciting additions to our plan is an update in the configuration of our TeamMate software, which is a software we use to document our audits. Because of some hardware changes on the server end that I won't bore you with, we will be able to access some additional features with this software that will ultimately result in some efficiencies for us, and best of all, we will be able to provide you with much better, more timely information about our audits, and about the Department's risk assessments.

For example, instead of keeping a separate database for our prior audit issues, and that long report that is really hard to read, we will automatically be able to generate that data from our working papers. And we can send emails automatically to the division directors to get their responses. They can enter directly into the software their responses and the timeline. It will give you information including aging reports on those prior audit issues and some pie charts, graphs, things like that that will give you more of a visual picture of where we are with prior audit issues.

There are other improvements to our annual risk assessment process that will involve the whole agency, our customer satisfaction survey process, our audit level timekeeping, and many other things that we now do manually.

Are there any questions regarding the proposed Audit Plan?

(No response.)

MS. DONOHO: Okay. Staff recommends approval of the

draft 2011 Audit Plan.

MS. RAY: Before we move for the approval, for the benefit of those of us that are, and the others that may not be aware, the entire Audit Committee had an opportunity to submit items that they thought were appropriate for the Audit Plan, as well as each member of the TDHCA Board had an opportunity to contribute to the building of the Audit Plan. So if there is no discussion on the Audit Plan, the Chair would recognize or receive a motion to accept the Audit Plan.

MR. GANN: I so move.

MR. KEIG: And do we have to recommend it to the full Board for approval as well? Or do we just approve it as a committee?

MS. RAY: We approve it in committee and it will be ratified by the Board, as I understand it.

MR. KEIG: So it will have the Roberts Rules of Order on that. So seconded.

MS. RAY: It has been moved and seconded to approve the draft 2010 Audit Plan.

All those in favor, please say aye.

(A chorus of ayes.)

MS. RAY: All those opposed, no.

(No response.)

MS. RAY: The ayes have it. Ms. Donoho.

MS. DONOHO: Okay. Item 3 is presentation and discussion of recent Internal Audit reports. We have two reports since our last Audit

Committee meeting.

The first one was internal audit of accounting operations. We performed a reconciliation of the Uniform Statewide Accounting System, which is used as the Comptroller's system to the combined balance sheets for HOME and Housing Trust Fund.

For fiscal year 2008 and 2009, we tested transactions, several hundred transactions, to ensure that they were properly authorized, that they were applied to the correct funding source, and that they were approved by management. We found that accounting operations generally has controls in place to ensure that financial transactions are handled correctly.

We did find two of 288 transactions, which was 1 percent that lacked supporting documentation, and one contract that was set up for less than the amount of the contract award. We recommended that accounting operations maintain the authorization documentation from the division that originated, and to implement a review step for the awards set up, and amendment processes.

The division management reports that both of these recommendations have already been implemented. Our objectives on this item were to determine if federal funds are drawn down in accordance with federal regulations, the Department's policies, and terms and conditions of the federal award and if financial transactions are performed in accordance with program rules, federal regulations, state rules and regulations, and generally accepted government accounting principles. So overall, you know, we only had those two little findings. I think they are doing a good job there.

MS. RAY: Yes. That speaks volumes, I think, to our accounting operations. Does accounting operations wish to make a comment on that audit at this time?

MR. GERBER: Ms. Chair, I don't know if the Board has had the pleasure of meeting David Cervantes and Esther Ku who are leaders in that division and ensure that we get the kinds of results that you see in the audit today.

So, any comments that you all would like to make?

MR. CERVANTES: No comments, other than to introduce Ms. Ku, who is the manager for accounting operations, and she is the one that deserves most of the credit for this, for the work in this.

MS. RAY: Ms. Ku, welcome to the Audit Committee meeting. We all know David.

(Simultaneous discussion.)

MS. RAY: But we haven't had an opportunity to meet you. And we are so glad to have you here. And I think it speaks volumes of your level of professionalism that you would have absolutely less than 1 percent.

(Simultaneous discussion.)

MS. RAY: To real numbers, but even less than that. They are really kind of small. We thank you for your professionalism. And we don't have to take action on that, do we? We just want to thank you for your professionalism.

And thank you, David.

MR. CERVANTES: Thank you.

MS. RAY: You really keep us looking good.

MS. DONOHO: Are there any other questions on this report?

MS. RAY: No.

MS. DONOHO: Okay.

MS. RAY: Moving on.

MS. DONOHO: The next one is the internal audit of construction quality in the Disaster Recovery Division. First the good news: the majority of homeowners that we contacted -- we called some homeowners who received homes from the Disaster Recovery Program -- they reported that they were pleased with the quality of their homes and with the professionalism of their builders.

We conducted a telephone survey of homeowners who received new homes, or whose homes were repaired as a part of that program. When we asked them how happy they were with the quality of construction, 56 of the 66 homeowners -- so about 85 percent rated their happiness as four or five on a scale of one to five.

The ACS contractor for Round Two has made some efforts to improve their oversight of the construction process during the course of the contract with the Department. However, we didn't feel like they were providing sufficient active ongoing oversight of the construction management process, which is a requirement of their contract.

They delegated construction management to Shaw Environmental, which is their subcontractor. Shaw provides damage assessments for existing homes, inspections of reconstruction and

rehabilitation. They also serve as a general contractor for rehabilitation of homes.

The Shaw staff reviewed inspection reports; they determined that all of the inspections are complete, and that the supporting documentation is present. We looked at a random statistical sample of 100 completed homes to determine whether that was true, whether the files had all of the documentation and all of the approvals. We found 19 of those 100 files did not contain the inspection documentation, all of the required inspection documentation.

And this is important because the payments to the builders are tied to the inspection process and without ensuring that the inspections are appropriately documented, there is a risk that a builder could receive payment for work that was not completed correctly, or that the program could be vulnerable if the homes are left uncompleted.

We felt like ACS should ensure that all of the inspection documents and requirements are satisfied and that the documentation is completed before the final inspection is accepted. They also hired -- ACS hired a construction manager to conduct inspections of the construction sites. But he doesn't document the results of his work.

Without documenting it, it is impossible to tell how much oversight he is actually providing. We recommended that ACS require that the inspections be documented. Also, the process used by ACS to track homeowner complaints doesn't include regular monitoring or effective aging of the complaints.

We recommended that ACS improve the complaint process to ensure that the homeowners' complaints are resolved on a timely basis. The other problem that we had is that Shaw is responsible for inspecting homes and is also the general contractor for rehabilitation projects. What that means is that they are inspecting their own work.

We recommended that ACS ensure that Shaw segregates these duties so that the same employee isn't assigning contractors, approving inspections, and authorizing payments.

Are there any questions about this audit report?

MR. KEIG: Yes. Okay. When you say that there's no recommendations on page 2 of 2, do you mean there's no recommendations for this committee to take action at this meeting, on this report, or the other reports? Is that --

MS. DONOHO: Right.

MR. KEIG: That is why we have none? Okay.

MS. DONOHO: Right. Yes.

MR. KEIG: As far as the -- just a second here. To your knowledge at this point, has ACS done anything to strengthen the process for capturing and tracking the complaints and ensure that the complaints are resolved in a timely manner?

MS. RAY: Mike, if you don't mind, could the disaster recovery staff respond to these questions.

MR. GERBER: Absolutely.

MR. KEIG: That is fine with me.

MS. RAY: It is kind of looking behind the scene. You guys are here because disaster recovery is probably the hottest item that we have to deal with, particularly as Board members.

And we do get telephone calls and emails, all of them dealing with disgruntled, dissatisfied, unhappy clients, and low income Texans. Still, and it goes on here so I would kind of like to hear from some of you all. MS. CRAWFORD: Sure. Well, at the stage that we are in this contract, to implement some overarching controls and to redo their complaint system wasn't required. We did ask them to continue to provide additional efforts in that they have a project manager that reviews that.

We do believe that those were great suggestions and had we had them a little earlier on, I think we definitely would have taken that effort a little bit further but we do discuss the complaints with them. And we did note the weaknesses that Internal Audit brought forth. We have about 52 days left on the contract though.

MR. KEIG: We had five months at the time that this report was issued. Right?

MS. CRAWFORD: Yes, sir.

MR. KEIG: And so, why did we just decide that this was a nice thing to suggest, but we just weren't going to do it?

MS. CRAWFORD: Well, I don't think that we ignored that suggestion at all.

MR. KEIG: Is it required by the contract for them to have a complaint process that tracks like this?

MS. CRAWFORD: No, sir.

MR. KEIG: Okay. Has ACS done anything to have Shaw segregate the duties, so that the same person who is doing this is not inspecting that?

MS. CRAWFORD: Right. The controls were separated and they reviewed them, and felt that there is not the same person. It is the same organization. But it is not the same staff overseeing the same -- their own work. Now, from an entity standpoint, that is correct.

MS. RAY: Well, I would like to kind of take this conversation a step further. I realize that ACS is winding down, and the money is just about spent. We are not going to get much amendment out of it anyway. But I do -- would like for us to talk about it a little bit, the lessons learned.

We have learned internally so that when we move on -- and there will always be disaster here in Texas. We are just now ramping up and dealing with issues associated with Ike and there will be other disasters.

The lessons that we have learned, so that when we put the contracts together in the future, that we put the controls on the front end of the contract, based on the lessons that we have learned here so that we can better serve the low income Texans.

MS. CRAWFORD: Absolutely. Point taken. And I think that that is the major discussion that we had with Sandy and her group, as soon as they issued the report. Which was -- there was some concern about taking the contractor off of production to repair some things that were very important, yes.

But were we going to get the value out of that? We have

already begun using the lessons learned from this report, and our oversight of the Ike contract, subcontractors, subrecipients.

MR. HAMBY: Well, I think there's two other important things to consider.

MS. RAY: Yes, Kevin?

MR. HAMBY: It is that -- I'm sorry. Kevin Hamby. One of the things that is important that is not included in Ms. Donoho comments is that we also have our own monitoring staff that goes out and does a review of the houses that have been constructed or repaired.

And quite honestly, throughout the entire contracting process, the whole issue of rehabilitated homes has been difficult because of the work involved and the amount of expense involved, and who is going to serve as general contractor and whether or not they can get people to be a general contractor on a rehab home or whether they were going to serve in that capacity.

So we were discussing that throughout the process. And we asked ACS early on. And I don't know to the extent that they did it. They probably didn't do it sufficiently, to make sure that they had a review process.

As a matter of fact, they had asked to do some of the teardowns; Shaw had asked to do some of the teardowns of homes. And we said, I think that there is a conflict of interest there and you can't do that because Shaw can't be in the business of tearing down the homes, and verifying all of the work that is done at the same time, being that contractor.

And so I think ACS was at least sensitive to the subject,

although they probably didn't adequately put a system in place. As a matter of fact, we have a monitor going out next week that is going to inspect some 51 homes. And so we do go through the process of making sure the homes are completed. And we have our documentation.

I think Ms. Donoho is right. We should get better documentation inside the old track system. And I think that is being done. That is being looked at. And certainly, one of the things we are requiring is, as we move forward in Ike, is how the subrecipients actually work for the programs.

MR. KEIG: I guess that was my next question was, how are our internal audits coming out? Did we not see what internal -- I shouldn't say internal audit, or internal inspections, as opposed to what Internal Audit did. Did we not see these issues? What -- I think, were we looking for different things, or what?

MR. HAMBY: Well, we were looking at homes and how they were completed and our monitors that were going out. To give you an example, we would go out, and we would determine that a ladder was left out, or we see some systemic problem, and so we would work with the builders at that point to correct that systemic problem.

That doesn't mean all of the past houses, but all of the future houses. And so we just completed our sample. We did not inspect all 2,600 homes. But due to our sampling, whenever we would see anything that would have a repeat pattern, then our monitoring team would get with the builders, and say, you need to fix this in any home you have already done. And you

also need to make sure that you don't do it anymore.

So we had an immediate impact, if there was any problem that we detected that occurred in more than one or two homes. We had issues with flashing on ceilings. We had issues with ladders to go in the attics. And they corrected those.

You know, we also have people who don't completely -- sometimes we get complaints. We had a whole series of complaints about people who thought their air conditioners were too small for their house.

But the way the homes were built, they were built with such high insulation factors, that if they had a larger air conditioner in the house, they would have had mold issues. Because it would have caused the air conditioner not to kick on quickly enough and not to dry the air in the house. So it would create a mold problem.

And so there's some of that education factor. So any complaint we get, we follow up on it. If we see it in a couple of different houses, then we start looking for it. And we fix that problem, and require the contractors to go back and fix this.

MR. GANN: Do you see any disparity in quality inside the city versus outside of the city?

MR. HAMBY: I don't believe so. We are using the same builders in a lot of cases. So it is --

MR. GANN: Some of them have different kinds of inspections going on at different times, too.

MS. CRAWFORD: But I think yes, for county inspections versus city or none, from that respect. That is why we have an inspection process put into place with Shaw. So they had to go out and inspect.

And then we also had our inspectors go out. Tricia's group going out and reviewing, looking at those as well to ensure that the quality and the appropriateness was there in the building.

MR. HAMBY: Then we also now have an outside vendor that also does it, like this.

MS. RAY: Do we have that level of inspection. Because many a municipality, or a city, invariably has stringent rules and regulations to impose than the county. So we have to be aware of that to make it as equal as we possibly can.

MR. HAMBY: And then of course, there is always whatever the highest inspection standard was. Some cities had a higher demand. And they had to meet the higher one. And then a county that didn't have as high a structure -- we would do that.

MS. RAY: I live in a county that tees me off sometimes.

MR. KEIG: After the report, did Shaw quit paying the contractors until they had got the inspection documentation in place?

MS. CRAWFORD: What I will say about that is, it wasn't that it didn't necessarily exist. It wasn't in the place that the internal auditors were looking. Which I agree, that is where it should be.

But that doesn't mean that it -- we couldn't find it if we were testing draws and looking for all of the appropriate documentation. We were

always able to obtain this. Again, I agree that it should be timely in the world track system. But sometimes, it didn't get uploaded. And a couple of times, we found that they had the wrong documents on the wrong home.

MR. KEIG: Why didn't we put that in our management response then? It wasn't that it wasn't there, that it wasn't filed or it was missing, or something like that. I mean, I come in the world of health care and documentation is everything.

And if we had something, and it happened to be in the wrong place in the file, that was really there, I mean, we point it out in our management response. So I am just wondering -- I am hearing this after I read the report. Well, it is really not 19 percent. It is something less than that because of the documentation was elsewhere.

MS. DONOHO: It was not present. And if you recall the last Audit Committee meeting, we talked about the followup on KPMG's work last year, on the statewide audit where they tested draws and looked to see if documentation was in the files. And it was not.

And then Curtis and I went out and did some of that work. And you know, in those cases, we looked, not only in world track, but I went down to ACS in San Antonio and looked at their hard copy files.

And some of that documentation was still not present. It is the same type of documentation. It is the inspection documents, the city inspection, the occupancy certificates, those kinds of things that are supposed to be present in the file before the builder can be paid, before the draw is paid. So it is the same sort of documentation.

So Kelly's assertion that it existed somewhere out there, or in the universe, is probably true but it was not in the file. And they are basing their payments to those builders on that documentation. So if they don't have it, how are they paying the builder? That is the point.

MR. KEIG: Right. And I guess what I am concerned about is, I am not hearing that they took corrective action to fix this issue after the audit report came out. We don't know today if they are still paying contractors that may not have all of the documentation present.

MS. CRAWFORD: Well, when we test, we go out and test still. And so what I am saying, not to minimize Ms. Donoho's staff's work. I agree with the finding that it should be present. So that is why we didn't argue that finding; it should be.

MR. GERBER: So have we gone back and looked at the 19 percent specifically, based on the audit just to see if the documents are --

MS. CRAWFORD: No. But we are going out next week. And we will include that.

MR. GERBER: So we will report back to the Audit Committee.

MS. CRAWFORD: Absolutely.

MR. GERBER: Next month, about those specific 19 percent and we will also make sure that the procedures, I know we talked to them about this audit, after it happened to go and make sure that the tightening that we did several months ago, is in fact being maintained.

Because no one should get paid without having the documentation in the file. Because HUD is going to find that to be something

that is ultimately going to be ineligible. And we will have a repayment issue. So we will address that.

MS. DONOHO: I also believe that KPMG is testing that again. Or was it Deloitte?

MS. CRAWFORD: We didn't have any --
(Simultaneous discussion.)

MS. DONOHO: Okay. Then probably not. Okay. I wasn't sure. You know, okay.

MS. RAY: It is probably one of the more spirited conversations associated with some of our audit findings, and rightfully so. Disaster recovery is certainly as important as anything that you can do. It is important that we do what we are supposed to do, take care of the low income citizens.

How heart-wrenching it must be to lose everything they have and just have to start all over. So Sandy, if you would, make an action item that we will revisit this at the next Audit Committee meeting.

MS. DONOHO: Okay.

MS. RAY: Let's see. Where do we stand on this case?

MS. DONOHO: Okay.

MS. RAY: So Mr. Gann, do you have anything else that you would like to share?

MR. GANN: No, none other.

MS. RAY: Mr. Keig?

MR. KEIG: No. Just one comment is, we have to keep in mind that the buck stops with us.

MS. RAY: Absolutely.

MR. KEIG: And that we can hire contractors. But we have to inspect what we expect. And taxpayers hold us responsible for, you know, proper use of funds and documentation and that sort of thing regardless of whether a sub or a sub-sub or somebody else does the work.

MS. RAY: Yes. One comment I would like to make to you, Kelly -- Kelly, you are deeply involved. You have been involved with this whole process. The writing of the contract, the awarding of the contract. And once you got kicked in the teeth.

But I am always amazed at your level of knowledge down to the detail level. You are not an ordinary gumshoe.

(Simultaneous discussion.)

MS. RAY: This is a term that just deals with the legalese. You really get down to the nitty gritty and you are very well informed on the details of the program. I appreciate it. We appreciate it very much, your expertise and your view, the depth and so forth.

MR. GANN: I will second that.

MR. KEIG: Your compliments are now covered for the month of November.

(Simultaneous discussion.)

MS. RAY: What do you call people that are lawyer rate on their job? But we do appreciate your level of expertise. Ms. Donoho, where do we go from here?

MS. DONOHO: Item four, which is a follow up discussion on

the ACS HUD LIT contract. So it may be the Kevin Hamby show again. If you remember the last Audit Committee meeting, HUD OIG had issued a report on an audit of the contract between the Department and the ACS for the Round Two Hurricane Rita.

Some of the things that they recommended required a revision of the contract in order to address their concerns. So the last Audit Committee meeting, we talked about an update of this action item for an update this time on the efforts to revise the contract. So Kevin is here to talk about that.

MS. RAY: Do a little soft-shoe.

MR. HAMBY: As you recall from our last meeting, the issue was that we had some wrong items in our contract. We had some repayments that HUD had asked for. And we also had some issues that would impact the future audits on draws and other issues.

And so we set about the process of trying, again, near the end of a five year contract, a three and a half year contract. And we renegotiated the contract from the beginning. And Mr. Keig pointed out at the time that he wasn't sure how you convince somebody to do so. It is not necessarily in their financial interest.

So we looked at it. And again, we tried to make it in their financial interest. We looked at how they approached what they were doing. And didn't find it. Probably underpaid a little bit. But a lot of the funds had been mischaracterized.

And so we were able to renegotiate that part of it. But we also

looked at the scope of services. That was the 3.1 and more closely reflected what the actual work that was being done was being done. And then what we ended up determining was, that we had treated this as we had thought all along, as a firm fixed price contract. And that would change the support documentation that was required.

So one of the ways that we encouraged ACS to play with us was, that we said, you are either going to have to supply all of the documentation that we have now requested for you for the past three years, or you are going to have to redo this firm fixed price contract. And after looking at the amount of work it would take to go back and recover all of the support documentation, it sort of became agreeable to us that this was a firm fixed price contract.

I believe, they haven't taken it yet. But we had a reimbursement of \$210,000, which they didn't really want to give us back. They didn't want to cut a check for it. So we put out a memo to them, that we were going to take \$210,000 out of one of their draws, that was present. And I think that was done. That took care of all the issues.

From our reporting standards, it would have caused a conflict. And so we took that money, and we resolved that issue. We believe the amendment, we are now down to parsing a few words.

But largely, amendment 4.1 is completed. They have the final copy of it. And so we are now hoping that that should be done pretty quickly. Because we have gone back and forth for several months on the big issues and now we are down to small issues that we think can be resolved.

And so we are hopeful that all of those issues will be done sometimes before Thanksgiving. And that would impact the way that they audit. They look at the audits in the future. Because the documentation that would be necessary.

And as we like to point out frequently, and even the HUD program people like to point out frequently, we have 2,600 pieces of evidence that we have been managing this contract pretty well, and that they are sitting out there. And so it is a way to -- we think we are going to be line.

And we talked to the program staff. They have accepted our responses. The HUD program staff, they accepted our responses, and are comfortable with the items that we have moved forward.

MS. RAY: HUD is --

MR. HAMBY: Well, comfortable that they are going to be --

MR. GERBER: HUD program staff. Not the IG. And so there is still a --

MR. HAMBY: Not the OIG.

MR. GERBER: And they are the ones.

MR. HAMBY: They are the ones that would actually be in charge of getting --

MS. RAY: Mr. Keig?

MR. KEIG: Yes. It is not necessarily an Audit Committee comment. But I assume that the final payment won't be made until we get the amendment back?

MR. HAMBY: Oh, it will be long before that. Because we

actually had another, we needed to actually administer about another five to \$7 million that she will be addressing to the Board tomorrow. We are going to gather up other funds that are all the efficiencies or just Board for the reason wants to spend in other areas.

And then bring them all together and try to serve another 50 residents of the area, somewhere near 50 residents in the area. And we are going to ask ACS to hold over to administer those. Because they already have the applications, and they have the infrastructure in place to do so.

So we anticipate getting that done in the first week of December. Because it is going to impact mid-January. So we don't anticipate that it will be a problem.

MR. GANN: You know, all of this to me, it just seems like it is part of this tremendous learning curve we have had to go through with all of these things that we have had to deal with the last two years basically, it seems like. And this is -- you know, we didn't know what kind of animal we had out there.

Neither one of these last two subdivisions you are talking about, whether it needed a fence or a cave to take care of all of that. It think it is coming out it is going to be a cave.

But you all have done a good job. And I know this is part of our learning curve. And we do need to learn it well. And I think you all --

MR. HAMBY: I think it is interesting and important to note that if you talk to HUD now, with our Ike and Dolly, they have adopted more of a Texas model than they have adopted Louisiana and Mississippi models. And

so you know, nationwide, they are following of our rebuilding communities, as opposed to handing out checks.

In fact, they won't even let you have a compensation program with Ike and Dolly funds. And so it is --

MR. GERBER: And they have certainly had their issue, in the soft process improvement. And yes, we want to perfect how we handle record keeping. But I think that just the fact that the type of contract is being changed at this point, yes. Is reflected, that even HUD, and HUD programs -- we have been joined at the hip with them.

You know, I think it indicative that even HUD doesn't know what kind of an animal this is. And over time, they have become more sophisticated. And we have had to adapt. And they have as well.

And but I think we can say with fairly real confidence, I mean, this is a program that is really the standard for how reconstruction gets done. It is not perfect by a long shot. But at the end of the day, we will have 2,700, 2,600 houses that we can point to, that are going to hold up well, and we feel good about.

They are not large houses. They are not the best houses in the world. But they are a decent house for low income Texans to recover with. And we feel proud about what we have accomplished.

MR. HAMBY: Desmond Simon says that 85 percent of the people who move into them, like them. That is probably better than other homebuilders have.

(Simultaneous discussion.)

MR. GANN: You still have to worry about the complaints.

MR. HAMBY: We are going to have some complaints. But I mean, it is from that standpoint -- we had some mistakes. We just had some language issues that had to be fixed. And that is what we thought they were. And that is what we still think they are.

MS. RAY: Well, having been involved with this program from the beginning -- maybe not from the actual occurrence of Rita, but certainly from the morning of the contract, I am very pleased with the work that you did, and that the legal staff did to move us to where we are right now.

I am very pleased with it. Even though maybe OIG might not be as pleased as we are. But I think we had a good strong contract, a very efficient contract. I think ACS has served us well, considering where we were before we got that contract. We have come a long way. But we always must understand, there is always opportunity for improvement.

And I don't know if anybody else was listening to Kevin as he was going through his discussion on how he had ACS to make some decision. Did anybody else think he sounded like the Godfather of legalese? We kind of made us a deal they couldn't refuse. That is what it sounded like to me.

MR. HAMBY: I am hoping from experience no one else was listening.

(Simultaneous discussion.)

MS. RAY: I know how hard you worked on disaster recovery since the inception of the program. And I think that we are a better agency. And Texas is better because of the hard lesson that we learned with Rita.

And we move into rebuilding homes that Ike.

And we are sorry it has taken us as long to get to where we are with Ike. We should have been further down the road. But that is not our the department's fault.

But hopefully, we will implement the lessons that we have learned from Rita and Ike will be even better than Rita it has been a long hard road, and it makes me feel so good to see those brand new homes down there, how strong and sturdy they are. And only time will tell whether they will be able to stand another Rita or another Ike, or something that is untoward to happen.

MS. CRAWFORD: They will withstand another Rita.

MS. RAY: We will see.

(Simultaneous discussion.)

MR. GERBER: But it does naturally raise a significant issue that is going to come up actually, as we go through Sunset Review. The first item that they dealt with was how does the State approach disaster recovery planning at the state level.

And one of the choices that has been made by state leadership now for Hurricane Ike is that the state won't be in charge of monitoring. We won't contract with an ACS. We will turn dollars over to 18 subrecipients. And they will contract individually with corporations or others of their choosing to go and do this work.

MS. RAY: I think that is a bad mistake.

MR. GERBER: We have had a lot of conversations about it.

And I think that one of the things that we are going to have to be prepared to do is to based on our experience, is to take back some of those programs and administer them at the state level if we need to.

MS. RAY: I must agree. That is exactly what is going to happen. Unfortunately, the time that it is going to take to get us to that point, where we are going to have to take them back, the people are not going to be served.

And that is just a little bit in my craw about the Ike recovery situation. Because the objective must always be to serve the people, not to serve the subrecipients down there. And that is unfortunate that we are -- we are getting to learn that lesson well as a State.

I am off my soapbox. We don't need to take action on this, do we?

MS. DONOHO: No.

MS. RAY: Okay. No action required on that. Okay. As we are moving into Item 5, if there are no objections from the committee, because of issues that we are going to be dealing with, with some reports that came in subsequent to us posting the agenda, if there are no objections, I would like to move Item 5 down the agenda, behind Item 8.

MR. GANN: I have no objection.

MR. KEIG: I am okay with that.

MS. RAY: Mr. Keig, you are okay with that? Okay. Then that is what we will do, and move into Item 6.

MS. DONOHO: Okay. Item Number 6 is presentation and

discussion of the status of external audits. There are six external audits on the list for 2011 fiscal year that are either planned, underway, or were recently completed, and in which reports are pending. These include the usual look at the Department's financial records by Deloitte, our annual review of federal funds by KPMG.

A HUD audit of disaster recovery, HUD OIG is looking at disaster recovery again. A review of the tax credit exchange program by treasury that has already happened. And an upcoming quarterly monitoring visit by DOE. I believe they will be here next week.

And there is a change to the table in your Board book. We received the report from the September DOE monitoring a few days ago, and we will discuss that under Item Number 7. There are hard copies here if anybody needs one, since it wasn't in the Board book.

Also not listed is an eighth audit we were recently notified of, a HUD review of Section 8 rent reasonableness that is coming up in December. In addition to the external audits pending for 2011, the Department has still not received reports for the following external audits from 2010.

There is an HHS review of the Low Income Home Energy Assistance Program, LIHEAP. Your Board book mistakenly says HUD, but it is HHS. There is a HUD review of Davis Bacon compliance. We received a draft report. Response were submitted back to HUD November 1. And they haven't issued their file yet on that.

There is a HUD review of the disaster recovery program. This was a July 2009 monitoring visit. The draft report was received in March

2010. Responses were submitted back to HUD in June, and they have not issued a file report.

So whenever I start worrying about internal audit keeping up with their time schedule, I think about this audit, and it makes me feel a whole lot better. Are there any questions on the status of external audits?

(No response.)

MS. RAY: There are no questions. We can move forward to item 7.

MS. DONOHO: Okay. Item 7 is presentation and discussion of recent external audit reports. HUD recently did a monitoring of the Neighborhood Stabilization Program, NSP. Overall, HUD concluded that the state's program was very well managed, and the department staff were knowledgeable about NSP requirements.

The deadline for obligating the NSP funds was September 3, 2010. HUD indicated that the Department had fully obligated its NSP funds by the deadline. They reviewed the policies and procedures for the NSP program and stated that they were very comprehensive. And if followed, should ensure that the activities meet the program requirements.

Their testing found no instances of ineligible properties. They didn't identify any findings. However, they had one significant concern with respect to projects proposed by two subrecipients.

They identified several instances where thorough property inspections were not conducted, and work specifications and cost estimates were not developed. Without doing that, they felt like the State can't assure

compliance with property standards, procurement requirements, and the reasonableness of cost determinations. They recommended the reviews of property inspections and cost estimates contain sufficient attention to detail.

As mentioned earlier, when we talked about the audit plan in Item Number 2, Internal Audit is currently performing an audit of the NSP program, in spite of HUDs recent review. The reason for this is because the federal monitors monitor primarily for the program's compliance with federal rules and regulations.

Internal Audit looks more specifically at a program based on both state and federal regulations, the Department's rules, the program's policies and procedures, as well as considering best practices and the potential for efficiencies and process improvements in the program. So that is why our program may get a clean bill of health from federal monitors, and still have findings from internal audit.

So I wanted to make that clear, that just because the federal monitors think the program is functioning well, based on the standards that they monitor against, there is a difference between monitoring and auditing, and a difference between the standards that they use, and the more broader standards that Internal Audit would use for criterial for an audit. Are there any questions regarding the NSP monitoring report?

(No response.)

MS. DONOHO: Okay. DOE performed a financial monitoring of the Weatherization Assistance Program. This was a desk audit for the

2010 financial review. They had no findings.

They found that the Department is in compliance with all policies, procedures and guidance related to financial management of the Weatherization Program's ARRA grant. Are there any questions on --

(No response.)

MS. DONOHO: Are there any questions on that report?

MS. RAY: None whatsoever.

MS. DONOHO: Okay. DOE has been performing quarterly monitoring on the Weatherization Assistance Program. They were here in June.

They conducted a monitoring visit to review the records maintained by the Department, look at the award file, check performance measure data, and look at production and expenditures. They didn't have any findings, but they identified nine concerns.

They had concerns about vacancies for crucial positions at the Department such as program offices and monitors not being filled. They felt like there was a disconnect between the program officers in the field, and the physical staff who released funds to subgrantees.

They pointed out that the process that we currently use may not be adequate to control wasteful spending. They stated that they believe the threat of deobligation to these subrecipients was not a sufficient deterrent to ensure that the quality and volume of production would be where they thought it needed to be. They recommended that the Department consider not releasing funds to poorly performing subrecipients until the Department staff

has inspected the work.

They talked about the energy audits used to determine weatherization measures. And that those weren't consistent and may result in less cost effective measures being performed. They indicated as a recommendation to the Department and the subgrantees needed to perform better audits. This was an issue that the GAO also brought up in their review last spring.

Some subgrantees use a priority list, instead of an energy audit. But not all of the measures on the list are implemented completely or correctly, according to DOE. They recommended that the Department increase its efforts to ensure that the priority list is used correctly.

They also suggested that a more comprehensive method of conducting the energy audits for multifamily units was needed. They suggested that the Department contract with engineering firms with energy efficiency experience in order to perform those audits.

They mentioned that the weatherization field guide was not implemented by subgrantees, and that we should require the subgrantees and their contractors to follow the field guide. They had concerns about the \$6,500 limit on weatherization activities. Because it should be according to DOE, an average cost across all units statewide, and not a per home limit.

MS. RAY: Before you go any further?

MS. DONOHO: Okay.

MS. RAY: What do they mean by that? Exactly what does that mean?

MS. DONOHO: Well, I believe the Department was suggesting that you know, there was a \$6,500 limit per home on weatherization.

MS. RAY: Right.

MS. DONOHO: And their feeling was, that it is an average statewide across all homes that are weatherized. So my home may cost \$10,000 and your home may cost four, 13,000, or I am sorry. But 3,000. But if it averages out to \$6,500, then we are good.

MS. RAY: I am glad it is something like that.

(Simultaneous discussion.)

MS. BOSTON: Well, and the way that Texas has always done it was, that we made it a hard cap. We have always told our subrecipients that it is a hard cap, and that we were assured of not exceeding. But we had always told them that if you ever have an exception come ask, and we will give you a waiver.

MS. RAY: Yes.

MS. BOSTON: So until ARRA -- keep in mind that the program cap was \$3,000.

MR. DeYOUNG: \$3,055.

MS. BOSTON: Per unit. And so with that half, it would have been very easy for them to exceed consistently. So by just giving them the hard cap, when we switched to ARRA, we didn't change that requirement. But they can get a waiver of fee if they need to.

We actually tend to be having the opposite problem, which is

their costs aren't high enough. So we aren't seeing much where they could have exceeded but for that cap.

MR. GANN: Well, it is extra effort, if they succeed, just to come back and get the waiver. That is the trouble if you are trying to do X number of jobs out there. And if you do in half of them even, it is just of lot of extra time. That is not what they are interested in doing. I can see the problem.

But I understand the cap. I think the cap is a good goal to hit for. But it looks like to me that they are complaining to us that we didn't spend enough money on each house.

MS. BOSTON: They are. And that is really so. I mean, that is something that we have been striving for the whole time. You know, the subrecipients, because the program historically had been closer to that 3,000 limit. For them to wrap their mind around how to get up to \$6,500.

They are also used to leveraging with our LIHEAP funds, which is the other program funds that we get from Health and Human Services. So they are used to certain weatherization measures in a home, they are used to dealing with LIHEAP. And so to kind of change their thinking and switch to WAP when they still are getting LIHEAP, you know, it is just -- it is more part of their everyday way of operating.

So we have been working with them. And this actually addresses several of the fundings, that we have been working with the subrecipients on a whole house assessment, which was both a DOE finding that we needed to switch to this. It is also probably the best way to increase

the cost per unit.

You all appeared to, as the full Board approved it as a draft rule several months ago. And it being adopted at this meeting tomorrow as a final rule. To make sure that that is really put into effect down at subrecipient level, where not only it has become part of our monitoring instrument, but we also are going to disallow costs when we find units who haven't used the whole house assessment method.

So we feel like -- and we have been working with the network to make sure that they understand that that includes we have vamped up the training opportunities for them to make sure that the training they needed for our whole house assessment is in place. That -- some of the subrecipients will still be doing priority lists.

But we are kind of moving away from that. Because it doesn't give them enough costs per unit. So it is still approved by DOE for them to view either the priority list, or the energy audit. But the expectation now is that they go in, they do an assessment of the unit, and then based on that assessment, they will decide does the priority list make enough sense, because enough of the measures that we needed to do were already on the priority list? Or do we need to do the audit, the energy audit tool.

So that other measures will pop up. So I think that will address not only increasing the costs per unit, but also several of the other concerns that DOE had. And when I am talking about, I am talking about both the August report, as well as the newer report that I think Ms. Donoho had provided.

MS. DONOHO: Yes. But we haven't talked about that yet.

MS. BOSTON: Yes. Because they also released a newer report. So some of the things from the first report aren't mentioned anymore, which we at the staff level will see as -- they must be pretty okay with it, if they aren't continuing them. Deloitte had actually stated that we resolved something. But things relating to costs per unit actually are carried through the newest report. And we have talked to them about the steps we are taking. And they feel comfortable. They hadn't make additional suggestions of what else they could do besides everything that we have told them of in the process of doing and adopting.

MR. KEIG: Are we going to give them a formal comprehensive plan or responses to how TDHCA will address their concerns expressed in this report, and any procedures that will be put in place to monitor them?

MS. BOSTON: We are. And how are we going to ask them, if we can do -- because we have both reports, and haven't responded, because I'll acknowledge we're late on responding to this one, we're probably going to see if we can give them one response that is comprehensive to both because a lot of it is iterative and redundant.

MS. RAY: I like your plan much better. And I also would be hiring someone, and let you all figure it out. I mean, a lot of people don't realize what a big state Texas is. The smaller states might not have some of the challenges that we have, because we are so big. And because we are so big, we are so divergent.

Because we are so big, we have got different climate concerns

all over the state. And one rule doesn't fit all. And you can -- I don't see anyway that you can control your costs by not having some form of cap. With a plan for over -- spending more.

(Simultaneous discussion.)

MS. RAY: Why don't you talk about that kind?

MS. BOSTON: Yes.

MS. RAY: Because everybody says, oh, well, why don't we just spend \$2,000 and somebody did the small stuff. It would be more trouble than we were before. But I thank you for that explanation but that didn't make any sense at all to me.

MS. DONOHO: There was one more concern I had that I wanted to mentioned. They said that they found deficiencies in some of the files, so that they reviewed and that the Department should provide a check list to ensure that the files contain all of the necessary documentation. Is there anything else on this report? Any other questions?

MR. KEIG: They didn't give us a deadline. But are we shooting for, before the end of the year, or something like that.

MS. BOSTON: For the response. Before -- before Thanksgiving.

MR. KEIG: Oh, That is correct.

MS. BOSTON: We have been -- I have been nagging staff a little bit. I think it I supposed to be on my desk tomorrow.

MS. RAY: And we are going to be talking a little more about weatherization as we move forward. Later items, a lot of them, Mr. Gann

mentioned that he didn't know whether we needed a fence or a cave. And another item that they are talking about. Because disaster recovery, this weatherization is going to be really, a really big case. A really big deal.

MS. BOSTON: We are going to make sure that you always have good things to talk about in audit committee until ARRA is over.

MS. RAY: Okay. Thank you.

MS. DONOHO: The next report was the September onsite monitoring of the WAP program, the weatherization. This is the one that wasn't in your Board materials because we got it last Friday. But because it is related to what we have been talking about, we sent out copies. And there are some here on the end of the table, if anybody would like one. Okay.

VOICE: We have put them, posted them on the laptops.

(Simultaneous discussion.)

MS. DONOHO: Okay. This visit, they reviewed administrative financial and programmatic aspects of log. And they visited one subgrantee agency. They had two findings and five concerns. Overall, they have noted that our program at TDHCA has a capacity and the ability to produce set levels, syndicated to our state plan.

However, they had several areas of concern, and the two findings. They have a list of six subgrantees that they identified as at-risk agencies due to either not producing at the contracted levels, or having what they call a lack of organization or financial controls in their programs.

According to them, these six represent 16 percent of the subgrantee network. So 16 percent of the subgrantee network, according to

them, is at risk. They pointed out that the Department has spent 25.5 percent of the grant funds for the entire grant as of the report date.

And the ARRA funding period is at its halfway point. And then they pointed out that 6,500 unit cost. The fee per average was lower than that. They stated that the Department needs to have an approved audit tool in place. Okay.

MS. RAY: Before we go any further -- that number is significant in housing.

MR. GERBER: It is and it's closer to 35 percent. In fact, the Secretary of Energy sent out a press releases announcing that we hit the 30 percent.

MS. RAY: Who would have thought it? I would have thought it complimentary.

MS. DONOHO: DOE mentioned that the Department needs to have an approved audit tool in place, and to ensure that it's used correctly when assessing units which is what Brooke was talking about earlier. They requested that we provide them with a written schedule to identify the milestones necessary to achieve this, and to continue training subgrantees on the proper use of the NEAT audit, which was one of the audit tools. They pointed out that we needed to ensure that energy audit analysis -- they looked at all allowable measures and rank them appropriately.

And that the majority of the client files they reviewed demonstrated an improper use of the audit tool. They found the subgrantee that they visited paid a contractor for a window that was not installed. They

considered this payment to be fraudulent.

And they used the word fraudulent, because the program reimbursed the contractor for expenses on a measure that was not installed in the home. They stated that the Department should include documents. The subgrantee should include documentation that all client files have been notified of the hazards associated with lead safe renovation and mold.

They pointed out that though the Department should provide closer monitoring of subgrantees to ensure that the energy audits are done appropriately, measures are performed as required, and costs were charged correctly. Their big statement, they said DOE considers the oversight of the subgrantee with respect to their contractors to be lax.

On the plus side, and there is a plus side, they pointed out that the Department as a whole, and I am assuming the way they worded this, that they are talking TDHCA -- not the subgrantee level, appears to have sound financial policies and procedures in place that provide sufficient checks and balances against fraud, waste and abuse, that the policy council position they noted is vacant and the previous monitoring visit was billed and that we have been submitting reports on time after missing one previously.

Are there any questions on this report?

MS. RAY: I don't have any questions, but I do have a comment for management. Both Brooke, and Mike. You know, this particular program is one of the thing that we have on our 2011 audit plan.

I am very concerned. Because so much -- it is so -- the ramp is so steep for the subrecipients out there to accomplish. And I think we have

seen this since the orientation of the program. I would like to see us, that ought to be one of the first ones out of the box.

Because I think we are going to continue to see, see back from the Department of Energy, as well as HUD on this program. I am so concerned about the -- when you are dealing with that much money, there is going to be much -- exponential opportunity for abuse of this program, and for fraud.

One little window not being installed, I am not too concerned about that. But I am concerned about the opportunity for all at the subrecipient level. And based on some conversations I have had, even at the peer levels across the state.

And we are going to have to be so very vigilant. I really want us to think about, seriously -- my request to direct anything that you do is that we need to seriously think about a way that we can overcome the appearance of any conflict of interest within our Department when it comes to monitoring, auditing and inspecting this program. The auditors from on high are going to be all over us. And we need to have a strong plan in place to make it, to show our interest in appropriate management because it is going to be a killer.

And it is going to make us look real bad when the snakes start crawling out from under the rocks, as they will when you have this much money out there to be expended particularly when we are not even hitting the six point, the \$6,500 mark.

And we know we have got to spend some more money. And people are going to be there in all kinds of ways. We just -- you really need to

give that some serious thought in terms of our department.

Because this is going to hurt us worse than the disaster recovery program, I think. Because there is just so much money out there. And people do all kinds of things, and they think they can get by with it. So I am off my soapbox on that one. But I just really want you to --

MS. BOSTON: I would say that there definitely are instances of fraud, waste and abuse. I think we have some good controls in place, not necessarily that that prevents it from happening. Because I don't know that we can always do that.

But we have good processes in place for making sure our subrecipients understand what it is and what it looks like, and how to share that with us, when they believe it is happening. How their employees can pass it up to us. We have a process put in place for our employees, if they believe, if they are seeing something either here, or at a subrecipient.

It can be done. And Sandy has actually helped us some on trying to make sure that our SOPs and guidance that we have given out, both internally, as well as to our subrecipients have good strong processes in place for that. You know, we are seeing stuff coming up.

And I think the other thing that -- probably there is probably one word. But I feel good about it. We are taking immediate action every time we have become aware of something, whether that is shutting them down immediately, freezing activity, getting our monitors out there.

I mean we have just had these crews who immediately get out there and inspect that they need to inspect. Sandy has gone on some of

them when it's come up. You know, her team has actually been very wonderful in terms of helping us, so when we get any referrals from the assayer's office or, you know, concerns of complaints. So we are taking steps.

And then additionally, we are working on some issue, on some recommendations internally with Mike, on some additional steps that we can take to continue to try and mitigate and -- I agree with you. It has a lot of potential for problems. But at the same time, I think, not to be falsely optimistic. But I think most of the subrecipients are doing -- are doing right by the program. They may have issues that they don't realize that they are doing something wrong. And that is why we are able to catch that during monitoring. I think in most cases they aren't purposely being fraudulent. And so finding the ones who are is you know, priority one. And then making sure -- that on the last, that we have them trained well, under the era of continual TA.

I think one of the only other things I would say is, you know, our issue in this case is compounded a little bit, because we can't just give the money to someone else. So when we have a problem like Institute for Rural Development, IRD, when that wasn't working out, that network of 44 providers is approved by DOE. As you probably recall, we had tried to expand that network in the past.

So when we do go after an entity and we freeze them either temporarily or permanently, it is going to have -- you are going to touch on the program's progress. And you know, I would rather see us spend 90 percent

of the funds, and have it spent well and know that it was 10 percent got left on the table, because we had to slow things down to make it clean.

And I am not saying -- we are going to leave 10 percent on the table. But you know, there is an intersection there, that there will be a point at which if enough things have to slow down or cease or be frozen temporarily, production cannot continue at the rate that it has been going.

MS. RAY: I do appreciate your approach. And I can appreciate the difficulty whether I'm never going to be a way to prevent fraud, waste and abuse. The only thing I'm saying is that we must have a strong process in place at the Department level to address it when it happens. And it has to be an efficient process. Because otherwise, you are kind of chasing your tail.

You know you get here. You get a telephone call; you run at it. You deal with that. Well, the next thing you know, you have got another one on the other side and that sort of thing. So we have got to build a system process so that we are not chasing our tail.

And we have a strong plan for addressing it, this fraud, waste and abuse. And we will talk more about this Executive Session and some of the things that I kind of think about in my head. Not to belabor this issue at this particular point of the discussion but this one is going to bite us if we are not really careful.

MR. GANN: I had one more question. I have seen checklists come by a couple of times here in the last few minutes. Are they physical checklists or is there a sheet of paper in that file where they can check off and

see, make sure, that that is supposed to be in the file.

Because I am thinking from the bottom side. I am not talking about it from our side. We still need to check every file for every item. But those people on the bottom side have a little help in making sure that everything is in the file?

MS. BOSTON: Yes. We give them very comprehensive training and checklists and tools. And when we either with DOE or when we go out for monitoring, and we identify that they may not be following it accurately, or it seems like maybe someone there doesn't realize there's list. You know, we immediately correct that and make that a finding on our monitoring report.

MR. GANN: Good.

MS. BOSTON: Do you want to add anything?

MR. DeYOUNG: Yes. The requirements for any client file are contained in the Texas Administrative Code --

MR. GANN: Okay.

MR. DeYOUNG: -- and it is codified so that they --

MR. GANN: I mean, a simplistic form is really what I am talking about. Okay.

MR. GERBER: We want every employee who touches the program to know clearly what they are doing, because they are also being paid with a federal grant. And so there is that need to document exactly what that is, so they can appropriate compensate those employees and that Agency.

I would just add to the discussion, you know, to some extent,

we do find out about these through the hotline. We find out about them through reports --

MS. RAY: Those came up.

MR. GERBER: Which it was a great idea of mine. By Sandy. And you know, we have doubled the number of inspections that are required by this program. Only 5 percent of them are required by DOE. We didn't feel comfortable with that.

We are shooting for as high as 12 percent when we get there. We are now hovering around ten, but we are trying to buck that up a little bit if we can. We're also, as Brooke alluded to, trying to do some things, kind of set the tone at the top.

But to make sure that that is understood by everyone who touches these program dollars. And so make sure that every employee of even the most remote subrecipient agency understands what the expectations are for the program. And what the expectations are, that ethical behavior and their proper ethical management of the program.

And so we have got several ideas that we are sort of batting about now, about making sure that agencies -- in many cases, as you have noted Ms. Ray, this is more money than many of them have ever seen in their lives. And some have collapsed under it.

The agency in Abilene decided to collapse rather than to try to sort through their problems. We have had similar problems, I just will identify for you. Agencies, for example, in Laredo. Both the City of Laredo and Webb County, which has been --

MS. RAY: Why don't we do this in Executive Session and talk about this.

MR. GERBER: Sure. But one of the -- we don't want to single the agencies out. You know, you run into issues about setting tone, and setting in place a process that even if you wanted to move dollars, how do you go about moving them?

And so deobligation is going to be a real issue that we are going to deal with over the next several weeks. And there will be several agencies that we will talk about in more specific terms. But we are leaving that thread out. And I think DOE understates it in their model report because we are going to use it as a tool, and I think it is going to send a shock wave to the system.

And frankly, for those agencies that are performing well, they understand what that means, and they understand, I think the pressure on them. And I think there is going to be a lot of effort to help provide some peer to peer support.

One of the big requests that we got from the association representing these agencies is us doing more investment and trying to provide peer to peer counseling and help to get the other agencies up to that level of performance that we all expect.

MS. RAY: Some of the fallout that I have seen across the -- in taking this road, is kind of sad. Some of our strongest professionals have fallen out as a result of this.

MR. GERBER: It has been very tough.

MS. RAY: And it is a sad thing to see. So with that, we will just move on to the next item.

MS. DONOHO: Okay. If that is it for that one. Item 8 is the prior audit issues. We have 64 current prior audit issues down from 118.

There were 15 issues that were previously recorded as implemented that we verified and closed during this period. There were 33 issues previously reported as implemented, that we are waiting on further information in order to clear those?

There are four issues that were recently reported as found as implemented. And we will verify and close these as time allows. There were twelve issues reported as pending or action delayed, as soon as they are reported as implemented, we will clear those as well. We didn't have any issues reported as not implemented.

There is one issue which is number 141. And this relates to separating weatherization monitoring from technical assistance. It was previously reported as management as implemented.

At this point, we will report to change it to no action intended, based on managements assertion that they are still considering what they are going to do about that one. I think we are saving that discussion for the next item.

So are there any questions about the status of prior audit issues?

MR. KEIG: Yes. On the 33 issues previously reported, they have not yet been able to verify. Did I understand you to say that you have

requested out for information to verify and they have not responded yet?

MS. DONOHO: No. When we get the issues in, and they report them as implemented, then we look at them. And we put them on our plates. So that when we have time between audits and stuff, we can clear them.

In a lot of cases, that requires us to go out and pull some samples and test. Or it requires us to go out and ask for some additional supporting documentation. So those 33 are in that category.

They are ones that we have on our plate. And we will probably have to go back to the divisions and say you know, we need this or that to make sure that they have been implemented. The management has reported them as implemented.

MR. KEIG: I know some are going to take longer than others. But if you got 15 done since the last meeting, is that about a quarter ago? Do you think it might take two quarters to knock out those 33?

MS. DONOHO: Maybe less.

MR. KEIG: Okay.

MS. DONOHO: It just depends on the workload and staffing level and that sort of thing.

MR. KEIG: Do you feel like you have adequate resources to attack those?

MS. DONOHO: Yes.

MR. KEIG: On what you consider a timely basis?

MS. DONOHO: Yes.

MR. KEIG: Okay.

MS. DONOHO: Yes.

MS. RAY: Let me ask you this, that was a very good point, Mr. Keig. When we first started this all-inclusive process of our audit committee, and I really do like this process, Mr. Keig, very much, I think we all learned a lot. And I think it makes us much stronger as an agency. We had some problems with this issue, with this item, about the status of the prior audit issues. I want to commend you on a much improved process.

I want you to share some information with us on where we have gone since we started that, and where we are right now. That shows us how effective your staff has been in moving us along. We had some serious heartburn about this area about audit committee reporting with these audit issues.

MS. DONOHO: Well, when I first took over as an internal audit director a little over three years ago, I inherited 457 prior audit issues that went back over a ten year period. And so we worked really hard to clear and close those issues. The 118 that we have had since then have been audits that were either internal audit or external audits done in that three year time frame.

And as we have cleared them, they have dropped off, so that we are down to 64, down -- that number continuously changes because more issues are added as we do audits or external audits happen. And as we cleared them, because once they have been reported to you, as implemented, they drop off your list. And then we clear them and they go away.

MS. RAY: Well, we understand it is not a static number.

MS. DONOHO: Right.

MS. RAY: That is a whole lot better than 457.

MS. DONOHO: Right. And Mr. Keig's heartburn that a couple of ones before is because we have always just reported the number. And we haven't reported which divisions they were in.

And so based on that conversation, my staff has been breaking them out into you know, these are the issue numbers, so that you can find them in your report and this is the division that they come from, and that sort of thing. So I think that we made some progress on that.

MR. KEIG: Yes. There is no level of detail that --

MS. DONOHO: Right. And I have never had anybody ask that level of detail before. And so we kind of quit providing it. And you prompted us into being more diligent about providing that level of detail.

I think when we make the changes to the audit software that we use, we will be able to provide you with a much more useful report on prior audit issues, that will give you some idea of how long each issue has been hanging out there, and what its current status are. And we will be able to prioritize them as well, so that we can clear the most important ones first. Right.

MS. RAY: You sound excited about your new software.

MS. DONOHO: I am.

MS. RAY: I truly believe that a picture is always better than a thousand words. And by using charts and graphs in a visual way of looking at

our business and trends, we as management can have a much better feel for the direction that we are taking, as opposed to just a lot of words and a lot of numbers that don't mean anything.

MS. DONOHO: Well, and it requires you to flip through and find issue 112 or whatever, which is, I know, a hassle. The thing that I am most looking forward to is that I won't have to nag all of the division directors to give me the responses on the status of their prior audit issues.

I can send them -- generate an automatic email and they can go in and enter those themselves, and it will cut way down on that process.

(Simultaneous discussion.)

MS. RAY: Thank you very much.

MS. DONOHO: Are there any other questions on the status of prior audit issues?

MR. GERBER: With all of these state budget cuts, can we still afford that software?

(Simultaneous discussion.)

MS. DONOHO: We have had it for several years, and it is extremely useful.

MS. RAY: Okay. Do we want to go back to Item Number 5? Or have we beat that horse to death already, as we have gone completely --

MS. DONOHO: It is up to you.

MS. RAY: It is up to you, Ms. Internal Audit Director.

MS. DONOHO: The only thing I wanted to mention, what we had on Item 5 is a follow up and discussion on the WAP programs monitoring

process. This is related to our April 2010 Internal Audit report where we identified some issues related to monitoring and technical assistance functions of WAP. In July, you all asked that we look at those, that management look at those issues and report back to the Audit Committee on what they have been doing.

I did want to mention that the seven prior audit issues from our April 2010 report, two of them, which are the Davis Bacon policies and procedures. And considering the population of homes completed at the end of the year when they put together their monitoring, list of homes to monitor. Those two were reported as implemented.

The other recommendations, through year end process, and then one was reported as implemented. But that is the monitoring one that we are moving back to no action intended.

MS. RAY: And we talked about that.

MS. DONOHO: Right. So I think management is here to talk about this issue, or answer any questions you might have.

MR. KEIG: I wanted to hearken back to -- another previous comment was, looking -- giving input from Internal Audit on SOPs, I just want to make sure that we do have the proper degree of separation of controls, where we are not drafting the SOPs that we are later going to have to audit. Because you can't audit something you created.

MS. DONOHO: Right. That is exactly right. Internal Audit has been asked to comment on them. And generally, we comment on them in terms of internal controls because our other standards allow us to comment

on internal controls in existing processes. Primarily, you see that in IT. But you also see it in things like development of policies and procedures. For example, they asked me to look at the fraud policy and procedures for the weatherization program.

I looked at the policy. And there were a couple of ways to commit fraud, waste and abuse that they might consider. And so what I did was, have you thought about this, have you thought about that? That is not you need to put it in here or whatever.

MR. KEIG: Right. So you are not drafting it.

MS. RAY: You are not in any case writing the standard operating procedures.

MS. DONOHO: Except my own.

MS. RAY: I meant, for any other Department.

MS. DONOHO: Well, no. Of course not.

MS. RAY: That would be inappropriate.

MS. DONOHO: The other thing that they had on that draft policy and procedure was a sign off by Internal Audit. And I made that clear to them that I was not going to sign off on their policies and procedures. And they needed to remove that from their draft, because that is not a responsibility of Internal Audit. So yes, we are very careful when we --

MR. KEIG: You understand, we aren't just being mean.

MS. DONOHO: Right.

(Simultaneous discussion.)

MS. DONOHO: I think the staff around here will tell you, my

own staff as well as management, that we spent a lot of time thinking about our auditor independence and how our work is impacted by that. And we are very careful not to violate that independence.

MR. KEIG: You all realize, she made me read a whole book of this stuff.

(Simultaneous discussion.)

MS. RAY: He asked for another book.

MS. DONOHO: He asked for a new book.

MS. RAY: Okay. Mr. Gann, do you have any further comments?

MR. GANN: No.

MS. RAY: Mr. Keig, do you have any further comments?

MR. KEIG: No, ma'am.

MS. RAY: Mr. Gerber. Does management have any further comments before we move into Executive Session?

MR. GERBER: No, ma'am.

MS. RAY: At 5:22 p.m., the Audit Committee of the Governing Board of the Texas Department of Housing and Community Affairs is going into Executive Session as provided for in Texas Government Code Chapter 551 and Texas Government Code Section 2306.039(c).

(Whereupon, the Committee recessed into Executive Session at 5:22 p.m.)

MS. RAY: Thank you very much for being present. Thank you very much for your input. At 4:00 p.m., the Audit Committee concluding

its Executive Session and reconvened in open session. No action was taken in Executive Session. The meeting is adjourned.

(Whereupon, at 6:05 p.m., the meeting was concluded.)

CERTIFICATE

IN RE: TDHCA Audit Committee

LOCATION: Austin, Texas

DATE: November 9, 2010

I do hereby certify that the foregoing pages, numbers 1 through 60, 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.

11/17/2010
(Transcriber) (Date)

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