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An audio of the meeting proceedings and meeting materials are available on the Port of Seattle web site - <http://www.portseattle.org/about/organization/commission/commission.shtml>

NOTES FOR AUDIT COMMITTEE SPECIAL MEETING DECEMBER 7, 2010

The Port of Seattle Commission Audit Committee met in a special meeting at 8:30 a.m., Tuesday, December 7, 2010 in the Commission Chambers at Pier 69, 2711 Alaskan Way, Seattle, WA. Committee members Albro, Tarleton and Miller were present, as well as CEO Tay Yoshitani and Joyce Kirangi, Port Internal Audit Manager.

SPECIAL ORDER OF BUSINESS: PRESENTATION OF AWARD FOR PUBLIC SERVICE

Commissioner Tarleton gave outgoing volunteer public member Steve Miller a plaque in recognition of his outstanding contribution to the work of the Audit Committee. Other members of the Committee and CEO Tay Yoshitani joined in thanking Mr. Miller for his three years of service on the Audit Committee.

CALL TO ORDER

The committee special meeting was called to order at 9:00 a.m. by Commissioner Gael Tarleton.

SPECIAL ORDER OF BUSINESS: RECOGNITION OF SERVICE

The Audit Committee recognized Records Supervisor Donna Wynn for her service as minute taker and staffing the Audit Committee and also her service to the Port of Seattle Commission.

APPROVAL OF MINUTES

The minutes from the September and October Audit Committee meetings were approved. Committee member Albro made the motion for approval.

Preliminary Discussion of 2011 Internal Audit Work Plan

Committee Chair Tarleton decided to put the discussion of the 2011 Internal Audit Work Plan as the Committee's first order of business. Internal Audit Director Joyce Kirangi turned the presentation over to Jack Hutchinson, Senior Audit Manager, to lead the presentation of progress

through the 2010 Internal Audit Work Plan. Mr. Hutchinson went through the process for developing the year-long work plan, including quantitative and qualitative issues in the year before. Internal Audit will work from Port-wide level on down to departments. Internal Audit (IA) combined the quantitative and qualitative issues, to see what the Port is facing in terms of different kinds of risk.

Reviewing 2010, there were 18 exited audits. Commissioner Tarleton asked how many were carry-overs, and Jack Hutchinson stated 4 from 2009 were carried over, which meant 14 of the audits were completed in 2010. They also completed a number of special projects, including, for example on PCI compliance work. Currently five audits are in the wrap-up stage, including public parking department, Republic Parking, concession audit, which the Real Estate Division is handling, and crane rentals, which were held off due to State Auditor's Office (SAO) work in that area. Commissioner Tarleton stated she was asking because she was looking at totals for years past, in order to see the trend in capacity, and that the Committee should be conscious of this in planning the 2011 work plan. Ms. Kirangi agreed that using prior history as baseline is useful. Commissioner Albro stated that a certain amount of carry-over items from year to year is acceptable. This allows shuffling of work, and is not a negative sign per se. Commissioner Tarleton stated that going into 2011, it's a good idea to have a three-year retrospective.

Jack Hutchinson went through the last three years of audits listed in the PowerPoint presentation. He noted the large amount of time spent in Aviation Division, due to the high number of concessions. There were 19 audits in Aviation, almost all lease and concession. There was also review of procurement processes in Capital Development Division(CDD), but partly due to SAO performance in 2007, which resulted in the creation of CDD, they wanted some time to pass and see what issues coming up. Commissioner Tarleton noted that considering 80% of operating revenue comes out of the airport, and 20% out of the seaport so that relative level of risk appropriate. Jack Hutchinson. also went through percentages by Division so far. He reviewed the agreement to do systems audit, which included accounts receivables and billing this year, and payables the year before that. Commissioner Albro asked how closely percentages agree with allocation of labor hours? Jack Hutchinson replied that were not exactly the same, since not all audits take the same time, that the complexity of individual audits vary greatly. The process for doing these is well-defined at this point. Capital Development audit was only 3% of all audits, but a tremendous amount of time, they were very complex, with many different aspects, 15-18% of time spent. Commissioner Albro asked if this could be done ongoing, and Ms.Kirangi agreed that they had a robust data base to do that. Steve Miller asked how close time spent on audits came to our long-range goals. Commissioner Tarleton wanted to know this as well, and noted that we should be gaining efficiency. She noted that we're not just measuring quantitatively, but what performance metrics looks like, and how performance measures work. Mr. Hutchinson. assured the AC that IA is capturing some of that information. He also mentioned a new computer system that will track resource use.

Mr. Hutchinson. went through the preliminary numbers for 2011, requesting input from Committee, Ms. Kirangi noted the process for deciding audit plan is when Senior Management requests audits. IA is lowering those numbers from last year that year. Commissioner Albro noted how easy it was to get overly focused on work plan, don't see some emerging issues. Wants to see dependencies on external organizations, including those we rely on for various services, including municipal

organizations and consultants, reliance on organizations that cease to exist. Mention now that we want to broaden perspective.

Miller noted we had more identified needs that we had time for. A couple of those that were dropped were hard to let go, and he hoped they would not let go again. All present agreed it would be good to take notice of proactively affected lease audits as they come forward. Joyce Kirangi agreed, saying she would not drop the same items again.

Tarleton requested a review of strategic plan, and the need to dig deep in one or two areas that are new for us. She wanted to IA to identify areas that cut across the organization, like security or procurement. She requested from CEO Yoshitani that management requests be given a lot of weight. Joyce K. stated she would do so. CEO Yoshitani noted that Joyce Kirangi always asked what areas need audits. He noted also that measuring our performance in the whole organization, will uncover areas where we are not measuring as well, and we can ask help from IA in these areas.

Interviews for 2011 Audit Committee Public Member

Tarleton noted same questions asked all candidates, process would be very open and last 15-20 minutes for each interviewee. Each interview at a time, others would step out.

The first interview: Christina Gehrke. She gave her name and residence (Kirkland, WA.)

Ms. Gehrke made an opening statement about why she wanted the job. She noted she is always looking for ways to give back to the community, and gave several examples. She thought this opportunity fit her qualifications very well.

Commissioner Albro wanted to know what she saw as challenges in the internal audit function. Ms. Gehrke said it was important to have sufficient resources, especially in risk management, and also be able to look beyond historical record to look ahead what are risks coming down, figure out what those risks. Commissioner Albro asked further about marshalling resources, and Ms. Gehrke said she would even borrow resources from other groups, hire additional staff, and work with senior management.

Mr. Yoshitani also thanked her for applying, wanted to know if she could manage the time commitment, given her full-time job. Ms. Gehrke noted she was very organized in looking at materials, and time management. Commissioner Tarleton also noted that flow of work and need were uncertain, does employer support her participation. Ms. Gehrke noted her management was supportive of people taking part in outside boards.

Commissioner Tarleton noted the strength of her resume, as one consideration is expertise, as most Commissioners don't have it that much. Her role is that of expert, working with others in management. She asked Ms. Gehrke how her experience will lead her to lend that expertise. Ms. Gehrke noted that in her job she had to help understand changes in FASBY and other regulations, and to keep abreast of internal audit changes. This was also part of her role as educator in teaching future auditors.

Mr. Miller: requested more information about her experience with GASBY. Ms. Gehrke stated an example of helping Native American organizations prepare audits for various funds. She also mentioned work with the Yellowbook standards, and other Federal standards. She mentioned how she looked at different reporting standards, and helped organizations to understand them.

Commissioner Albro asked about her experience with Enterprise Risk Management (ERM). Ms. Gehrke said at her job she helped organize an ERM for financial, operational and credit risk groups. She went through her experience with controls for operational risk. She noted every organization had different kinds of risk. She noted the Port had lots of bonds, and concessions at airport as examples of risk.

Commissioner Tarleton asked if she had any previous work with organizations that had business with the Port, and whether she wished to make a final statement. Ms. Gehrke replied she had no prior work with the Port, noted she had work with Jack Hutchinson. She also thought her background does suggest she can add value for the organization.

The second interview: Mr. Kariuke Nderu. Residence in Issaquah, WA.

Opening statement: I work in Seattle, and am excited about this opportunity, which is a very complex field, especially in assessing the work of IA. Usually the public is not left with much besides a lot of information. My value is giving a meaning to what is being said, like assessing when things are going well.

CEO Yoshitani notes his background, and experience with a public entity. He asked Mr. Nderu what is the structure and relationship to the board. Mr. Nderu noted he reports to CEO, CFO, and reports to the board. Added that it is difficult for the board to know what day-to-day work is. He notes that the kind of structure he works with was recommended by the Organization of Internal Auditors, but it can fail. The risk is that sometimes the reporting structure can fail to work.

Commissioner Albro noted what challenges he sees in an Audit Committee. What would guide your approach? Mr. Nderu replied that the biggest risk is misunderstanding how to measure risk. This is a very tricky field, there are many nuances to what risk are, and it can be complicated, since the auditor has interest in keeping the board happy, the board wants to keep the constituents happy, so sometimes the elephant in the room can be evaded.

His example of risk is that at the POS, the business of the Port is to transport. The possible risk to revenue is perhaps 80%. What is this based on? Maybe this year is 50%, and we should be able to talk about specifically.

Mr. Miller asked if he has knowledge of GASBY, other government audit standards? Mr. Nderu replied he reviews CAFR for many cities for GFOA. He also reviews financial statement for Seattle schools. Experience gives you the of understanding the story that the financial statements is trying to say.

Commissioner Tarleton asked about the time commitment of monthly meetings in public. She also wanted to know why do you think you can be representative for people. Mr. Nderu replies that his

exposure to audits gives him a perspective and that he also has created internal audit functions. He believe that from the public's point of view, he would not be an employee at the port, but the "3rd eye". He thought about commitment, something to be said about people volunteering in high-stress area. He can make time.

In his closing statement, his closing thought is that there is internal audit discussion, which is technical, and human discussion, which I have experience in as well.

The third interview: Mr. Ty Watanabe. Residence in Redmond, WA

Opening statement: He noted that he had a lot of experience with private sector audits, but no prior public experience.

Experience: External audits in financial and quasi-governmental audit (housing services) GAP, GAS, but limited in government procedures. He mentioned setting up internal audit function, including ERM, global risk procedures, risk appetite, governance risk and compliance.

CEO Yoshitani noted he did not mention a lot of public institutional experience in auditing. How did he feel this was a difference? Mr. Watanabe replied that the environment is entirely different. He noted his technical side, governmental side is weakest, and that he would rely on your financial people for expertise.

Commissioner Albro asked what challenges there were for the port in internal audit, allocating resources, work plan. Mr. Watanabe felt that the ERM is great at understanding what risk exists that needs to be addressed with limited resources. He would continue work with ERM, and see how it reflects in the internal audit plan.

Commissioner Tarleton asked a two-fold question: why is your experience helpful in representing public, and do you have the time for this work?

Mr. Watanabe replied it would be honestly difficult to answer truthfully, as he did not know how much time this group takes. He thought there might some Push/pull between the time spent with the Internal Auditor and the Audit Committee. He needed flexibility if there are side meetings, but every meeting is fine. He also feels he is ordinary middle class person who has the knowledge hones in private industry.

Mr. Miller asked if he had any conflict of interest, any prior work with Port? Mr. Nderu mentioned No, but that he has submitted an application to be an auditor with ST.

In his closing statement, Mr. Watanabe noted his contribution is developing ERM frameworks, incorporating aspects of audit function, and financial background at KPMG. And he had a strong financial reporting and governance perspective.

Commissioner Tarleton thanked Tom Barnard for organizing the slate of candidates. Commissioner Abro questioned Mr. Miller about his time commitment? Mr. Miller replied he spent lots of time in

first year, but that won't reoccur. His prep time is half an hour on reports, 10 minutes on minutes, overall it is a manageable commitment.

Lease and Concession Audits: Sodexho America, LLC, and Smarte Carte Inc,

Ms. Kirangi reported she was closing two lease audits, and there were not a lot of issues with either.

The first was Sodexho, a vending machine concession. Ms. Kirangi went through revenue figures on PowerPoint. She said that the audit is a clean audit, according to usual terms of compliance with regulations and laws, terms and conditions of the lease. There is one issue of untimely payment, and the assessment of financial charge for late payment. Audits in 2008-2009 were late in some instances. This is old period, when we looked at the new 2010 audits, it is no longer an issue. 2010 payment history for this concessionaire is clean.

Commissioner Tarleton asked: What do you attribute this to? Ms. Kirangi said that management practice change in accounting department in 2010.

Deanna Zachrisson added that both accounting had stepped up its monitoring practice, but also Sodexho has had trouble with its business in 2008-09. There were changes in their accounting staff, and we have helped them.

Commissioner Albro asked what percent of monthly payments were late?

Ms. Kirangi, referenced that data on page 7 of report,

Commissioner Albro noted then that about half the time they were late. Average number of days late? Jack Hutchinson said they did not calculate, but time schedule for MAG payments is quite specific, payment is understood without notification. He also noted that the timeline can be difficult to comply, because concessionaire has to close their books to calculate what is owed. This can be challenging.

Commissioner Albro asked whether it was a big or small company? The answer was that it makes an excess of \$1M a year. He then asked about the strategy for collection of fees, and that was explained later.

Mr. Miller asked about whether there was a loss of funds, as in the recent SAO finding. Ms. Kirangi noted that this is not an issue here, and the concessionaire was bonded.

One other issue raised JK: also communicated to management on issue of vending machine in admin building, first right to operate goes to Department of the Services for the Blind. You need to contact them, and work this out.

Smartcarte lease audit: Clean report, no issues.

Commissioner Albro: Made a statement that in his opinion is no need to forgive any late payments, and the POS should be uniform in enforcing that. There should be zero tolerance for late payments for concessionaires, and there is no reason for us in public sector to accept it. Commissioner Tarleton supports it, noting concessions have bonding and surety payments as well.

It was also noted that the concessionaires Concessions International and Borders have been billed on those late fees noted earlier this year.

Update on Concession payment issue

Caluza: Status of Management Receivables and Accounting Financial Reporting. Pertinent facts: The Port bills \$42M monthly, about \$500M yearly.

Aging of those is indication of how well collecting of money it is owed.

\$6.3 m \$5.3 are current. Situation not a problem.

\$200k of 31-60 days.

\$27K, 6-0-90,

\$6K over 90.

Late fees has been a concern, and we received a clarification in 2009. We received resources to address. We issued Late fees of \$200k, collected \$190K, the rest are in disputes, or collection enforcement through surety and bonding. One tenant in default.

Zero tolerance: Been aligned with that since we have had resources of all late fees.

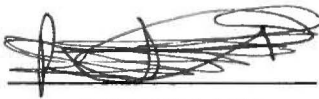
Commissioner Albro: Two different situations 1) no warning of slow pay or no pay, 2) alerting there is a problem.

Rudy Caluza notes that there is pro-active management.

ADJOURNMENT

There being no further business, the meeting was adjourned at 11:00 a.m.

(A digital recording of the meeting is available on the Port's website.)



ROB HOLLAND

SECRETARY

