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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>

APPROVED AMENDED MINUTES
AUDIT COMMITTEE SPECIAL MEETING April 5, 2011
(Revision to staff in attendance and date of minutes approved)

The Port of Seattle Commission Audit Committee met in a special meeting at 9:00 a.m., Tuesday, April 5, 2011, in the Commission Chambers at Pier 69, 2711 Alaskan Way, Seattle, WA. Committee members Commissioner Albro, Holland and Gehrke were present, as well as Dan Thomas, Chief Financial Officer, Joyce Kirangi, Port Internal Audit Manager, and Commission Staff Tom Barnard.

CALL TO ORDER

The committee special meeting was called to order at 9:02 a.m. by Commissioner Albro.

[Review of the Port Capital Improvement Program](#)

Joyce Kirangi introduced the presentation, made note it was not part of work plan in 2011, but the one in 2010. She noted that this was part of the follow-up to 2007 SAO audit, which covered capital development. In responding to that audit, management made many improvements, and had IA review the changes. IA spent time looking at controls, processes, strategies, that CDD put together to manage projects. Jack Hutchinson then took over for the rest of the presentation.

Jack Hutchinson described context for the policies and procedures that CPO and CDD came up with, which was not in existence prior to SAO 2007 Performance. Prior to this, the tasks of project management were dispersed into three divisions: Airport, Seaport, and Corporate. Current FTEs for the CDD division include 200 FTEs, and the division manages procurement at an average amount of \$300 M, including allocated costs, and fully loaded costs. He also described training process of over 1000 employees of new procedures, which continue. He noted changes in service agreements, and the drop in Category I service agreements (< \$50K), whose preponderance were noted by the 2007 SAO Performance Audit. He noted management work in the Small Works Department, another areas noted in the SAO Performance Audit, which lowered the number of contractors getting multiple contracts. Also outlined were efforts by CDD to develop indicators to measure performance by the division. These were viewed as just beginning, but moving in the right direction.

Finally, audit staff noted certain features of this audit report which will be included in further reports, including an expanded methodology section and management response section.

Mr. Hutchinson noted that the audit was clean and had not any individual findings; there were a couple of issues brought to management's attention. One was vague language associated with Change Orders on some contracts, which made it difficult to see whose responsibility project changes were – the contractor or the Port. (In those cases, it was noted in Management's response letter that this was part of prior procedures associated with Change Orders.) The other was whether the number of Change Orders was correct, and whether they had been consciously split to lower the cost. The level of Change Orders being lower would remove a level of direct Commission approval, though this was not done consciously. This was another issue raised by the SAO Performance Audit.

Finally, he noted the ongoing work to update the Small Works Contracting database. He described the system as it exists, and weaknesses in being alerted for contracting opportunities. This could result in contractors being excluded, and the lack of an audit trail to note that. Management has been aware of this, and is implementing a new system in mid-2011.

Commissioner Albro suggested discussion be broken up into 1) audit issues, 2) management letter issues, and 3) small works issues.

Ms. Gehrke and the Committee discussed how far along CDD efforts were at measuring performance. Mr. Hutchinson noted that measures did exist; were moving in the right direction, and more importantly, do reflect primary risks of division, which they do. Project soft costs and project cost growth were given as examples of measurement that they are doing. The audit did not feel its role was to do a comparison with other entities. Discussion ensued around how well performance could be assessed at this time, when measures were relatively new. The Quarterly Capital Development Report one of the reforms came out of the SAO report was also mentioned as a new measure for gauging how well projects are managed overall. Mechanisms are in place that includes goals as well as measurements. The process used to measure still evolving at a conceptual level, not yet solid and robust.

The training program by CPO was also noted and commended by the Committee. One question is whether the burden of all regulations worth the benefit, and the balance between the new regulations and efficient procurement for projects. Ralph Graves noted that the initial goal had been to build a program that complies with state law and best practices, and not bring projects to standstill. We believe that can do that at a lower cost, but it can be done more efficiently, for example by using LEAN procedures. Training effort for both CPO and others will bear fruit.

The Committee also discussed the causes for the reduction in small works contracts and the drop in Category I. CDD explained the concept of IDIQ contracts and how this affected the level of contracts and opportunities for small business. CDD show the IDIQ service agreements that replace the Category I contracts. Small firms can still bid for these. State law has this as an objective. And they are using SCS roster, and work with Office of Social Responsibility. The

Committee commended CDD and CPO for embracing findings of SAO Audit, foster culture of compliance, and embrace change.

The discussion then moved on to the issues mentioned in the Management letter and Change Orders. These were not findings and were minor isolated issues. These included vague language in a couple of Change Orders that made it unclear whose responsibility changes were – the contractor or the Port. Procedures for disclosing site conditions were reviewed by CDD. Secondly, and connected to this, was the possible splitting of Change Orders, which affected the level of Commission review, and was an issue called out in the SAO report. Third was the general weakness in the current roster system, which would allow some contractors to be left out of the solicitation process. It was noted that a new roster system was coming into place in mid-2011.

Lease and Compliance Audit of Thrifty Car Rental for 2008-9:

It was noted that this was the last of ten rental car audits leases. It was noted that the revenue model of 10% gross percentage in this lease was described as a common rate. The audit made sure that what was reported in revenue was correct and matched internal company records. They also measured that the CFC revenue came in correctly. There were two issues. One involved a CFC not collected correctly, and the Port was asking for reimbursement. The other issue involved overpayment of the concession fee based on location of Thrifty outlets. One location was over paying by \$87K. In both cases, the issue will be resolved shortly.

Approval of Minutes of February 1, 2011, Audit Committee meeting:

Minutes were approved. It was noted that the format was tending towards a verbatim reading of the audit, and it would be better to modify it towards a summary format. Mr. White is also taking over the task from staff member Mr. Barnard.

Preliminary discussion of Long-Range Goals and Objectives:

The Committee noted the necessity to do an on-going evaluation of the Committee's and the Internal Audit effectiveness, and comparing against best practices, and lines up with our Charter, and the resources necessary to accomplish the task.

Committee Staff reviewed the history of the Long-Range Goals and Objectives document, and how it reflects the changing focus of the Audit Committee and the IA depending on who is heading the Committee. There are problems of continuity with this, and a more rational system of the developing work. The Charter was also out of compliance with IIA standards. The Risk Assessment Plan that the Internal Audit work plan is based on was reviewed, and the underlying risks associated with it. That would provide a long-term (3 year) guide for the long-term goals and objectives, and the level of resources available to the Internal Audit Department, and use an external audit assessment as a way of measuring the work of the Internal Audit.

General discussion ensued on these issues – what the direction of the Audit Committee should be, what type of audits should be done, based on outside entities being responsible for 80% of our revenue, and how to define the type of audits that are done. The necessity to define specific expertise based on core areas, and how to measure progress in areas was discussed as well, and its connection to the ERM efforts. The challenge of different perspective of individual committee members was noted, and the necessity of everyone being in agreement, and of the committee's

work not be politicized. The correct relationship of resources to the reach of the Committee was noted, and the ability to refine the mission was mentioned. Finally, the key starting point of the Charter and the necessity of common language of defining audits were stressed, and the IA Department promised work on this front. The matching of work of the Internal Audit to the risk presented was important. Because the lease revenue is important, and the organization was built based on addressing that, the auditing is much better. Therefore, is the same level of risk present? Much better controls exist, less revenue is being collected. Should the function stay the same, and the focuses of the Audit Committee stay the same? Has the internal audit become part of the internal controls, and is that appropriate?

Rudy Caluza, Director of Accounting and Financial Reporting also commented on the importance of the Internal Audit and the Audit Committee. The function of the Internal Audit is spread thin, and the exposure of the Port towards revenue risk is still important, and the function of Internal Audit in this area should not be lessened.

The importance of providing oversight was noted, and the good use of Internal Audit is more vital of that than individual acts of oversight by the Commission. The perception of oversight should not be confused with effective oversight itself.

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

Approved, as amended, on June 7, 2011.