

AUDIT COMMITTEE

Thursday, November 4, 2010
4:00 PM

PLEASE NOTE CHANGE IN MEETING ROOM LOCATION

East Wing, Lower Level Conference Room
County Government Center
70 West Hedding Street
San Jose, CA

AGENDA

CALL TO ORDER

1. ROLL CALL

2. PUBLIC PRESENTATIONS:

This portion of the agenda is reserved for persons desiring to address the Committee on any matter not on the agenda. Speakers are **limited to 2 minutes**. The law does not permit Committee action or extended discussion on any item not on the agenda except under special circumstances. If Committee action is requested, the matter can be placed on a subsequent agenda. All statements that require a response will be referred to staff for reply in writing.

3. ORDERS OF THE DAY

CONSENT AGENDA

- 4. Approve the Regular Meeting Minutes of September 2, 2010.**

REGULAR AGENDA

- 5. ACTION ITEM - Approve the 2011 Audit Committee Meeting Schedule.**
- 6. ACTION ITEM - Review and receive the audited Comprehensive Annual Financial Report for the Santa Clara Valley Transportation Authority, and the Santa Clara Valley Transportation Authority Amalgamated Transit Union Pension Plan Report for Fiscal Year 2010.**

7. ACTION ITEM - Review and receive the Audited Financial Report for Fiscal Year 2010 of the Santa Clara Valley Transportation Authority Retirees' Other Post Employment Benefits Trust (Trust).

OTHER ITEMS

8. INFORMATION ITEM - Receive the Auditor General's report on the SVRT Contract Compliance Internal Audit.
9. INFORMATION ITEM - Receive an update from Auditor General staff on the status of the audits in the current Internal Audit Work Plan.
10. Items of Concern and Referral to Administration.
11. Review Committee Work Plan. (Burns)
12. Committee Staff Report. (Burns)
13. Chairperson's Report. (Gage)
14. Determine Consent Agenda for the December 9, 2010 Board of Directors Meeting.
15. ANNOUNCEMENTS
16. ADJOURN

NOTE COMMITTEE MEMBERS: In order to establish a quorum for this meeting, members are asked to call the Board Secretary's Office at (408) 321-5680 or E-mail: bd.sec.polling@vta.org before 5:00 p.m. on the day prior to the meeting. Thank you for your cooperation.

In compliance with the Americans with Disabilities Act (ADA), those requiring accommodations or accessible media for this meeting should notify the Board Secretary's Office 48 hours prior to the meeting at (408) 321-5680 or e-mail: board.secretary@vta.org, (408) 321-2330 (TTY only). VTA's Homepage is located on the Web at: <http://www.vta.org/> or visit us on Facebook <http://www.facebook.org/scvta>.

Disclosure of Campaign Contributions to Board Members (Government Code Section 84308) In accordance with Government Code Section 84308, no VTA Board Member shall accept, solicit, or direct a contribution of more than \$250 from any party, or his or her agent, or from any participant, or his or her agent, while a proceeding involving a license, permit, or other entitlement for use is pending before the agency. Any Board Member who has received a contribution within the preceding 12 months in an amount of more than \$250 from a party or from any agent or participant shall disclose that fact on the record of the proceeding and shall not make, participate in making, or in any way

attempt to use his or her official position to influence the decision. A party to a proceeding before VTA shall disclose on the record of the proceeding any contribution in an amount of more than \$250 made within the preceding 12 months by the party, or his or her agent, to any Board Member. No party, or his or her agent, shall make a contribution of more than \$250 to any Board Member during the proceeding and for three months following the date a final decision is rendered by the agency in the proceeding. The foregoing statements are limited in their entirety by the provisions of Section 84308 and parties are urged to consult with their own legal counsel regarding the requirements of the law.

All reports for items on the open meeting agenda are available for review in the Board Secretary's Office, 3331 North First Street, San Jose, California, (408) 321-5680, the Monday, Tuesday, and Wednesday prior to the meeting. This information is available on VTA's website at <http://www.vta.org> and also at the meeting.

**NOTE: THE BOARD OF DIRECTORS MAY ACCEPT, REJECT OR MODIFY
ANY ACTION RECOMMENDED ON THIS AGENDA.**



Audit Committee

Thursday, September 2, 2010

MINUTES

CALL TO ORDER

The Regular Meeting of the Audit Committee was called to order at 4:03 p.m. by Chairperson Gage in Room 157, County Government Center, 70 West Hedding Street, San Jose, California.

1. ROLL CALL

Attendee Name	Title	Status
Don Gage	Chairperson	Present
Rose Herrera	Vice Chairperson	Present
Chuck Page	Member	Present
Nancy Pyle	Member	Present

A quorum was present.

2. PUBLIC PRESENTATIONS

There were no Public Presentations.

3. ORDERS OF THE DAY

There were no Orders of the Day.

CONSENT AGENDA

4. Minutes of June 3, 2010

M/S/C (Herrera/Pyle) to approve the Minutes of June 3, 2010.

NOTE: M/S/C MEANS MOTION SECONDED AND CARRIED AND, UNLESS OTHERWISE INDICATED, THE MOTION PASSED UNANIMOUSLY.

REGULAR AGENDA

5. Task Order Contract with Deloitte & Touche

Michael T. Burns, General Manager, provided background information on the contract with Deloitte and Touche noting the two-year contract included three additional one-year options with discretion on exercising the options resting with the Audit Committee. Mr. Burns stated staff recommends the extension of the contract through January 2012 to allow Deloitte to complete the remaining internal audits contained in the FY11 Internal Audit Work Plan.

M/S/C (Herrera/Page) to approve submitting a recommendation to the Board of Directors to Approve exercising the first one-year option to extend the task order contract with Deloitte & Touche, LLP for Auditor General services, for amount not to exceed \$175,000 as specified in the contract. Exercising this option will extend the contract term to January 8, 2012 and increase the maximum contract value to \$525,000.

6. SAP Governance Risk and Compliance Report

Greg Thomas, Auditor General, provided background information on Deloitte's audit on the access control of VTA's SAP financial system and the installation of the Governance Risk and Compliance (GRC) monitoring tool which reports on segregation of duties conflicts. He provided a presentation on the GRC Segregation of Duties Design Assessment Internal Audit highlighting the audit objective and scope and the summary results.

Mr. Thomas indicated three low risk observations were identified relating to VTA customized transaction codes, segregation of owners and approvers of rule sets, and monitoring of the segregation of design and access conflicts. He noted none of the issues were significant.

Chairperson Gage questioned if the tool was modified for VTA. Mr. Thomas indicated there were some specific customizations when installed but it was implemented as is.

Member Page questioned if there are experts in the utilization of the GRC tool and if recommendations are made as to who should be analyzing the reports.

Mr. Thomas noted the individual conducting the fieldwork of the audit has expertise in configuration and set up of the tool. Emily Kwan, Manager, Deloitte, stated higher level employees who are able to evaluate whether the users and conflicts are appropriate should analyze the reports. Mr. Thomas added they will verify who is reviewing reports and confirm they are appropriate.

Member Herrera commented she is impressed with process rules and access controls of the GRC tool and is pleased VTA is ahead of the game and focused on prevention.

On order of Chairperson Gage and there being no objection, the Committee received the Auditor General's report on the SAP Governance Risk & Compliance (GRC)

Segregation of Duties and Sensitive Access Controls Internal Audit.

7. Scope of Work for Annual Financial Audit Services

Leonard Danna, Partner, Vavrinek, Trine, Day and Co., LLP (VTD), provided a presentation on the audit plan for year end June 30, 2010, highlighting the following: 1) Scope of Changes for 2009-2010; 2) 2009-2010 Fee analysis; 3) Significant new accounting pronouncements; 4) Timetable: interim, final, and completion; 5) Interim work completed to date; and, 6) Final audit work. Mr. Danna added there were no significant changes in audit scope for the current year but noted management requested a review of controls in place against fictitious employees and employee vacation payout.

On order of Chairperson Gage and there being no objection, the Committee reviewed the Scope of Work for Annual Financial Audit Services.

8. Contract with Vavrinek, Trine, Day and Co.

Joseph Smith, Chief Financial Officer, provided background information on the Contract with Vavrinek, Trine, Day and Co., LLC (VTD) which expires at the end of the present fiscal year. A Request for Proposal was issued and after completion of evaluations and interviews, staff recommended the retention of VTD. He noted they had the lowest cost, their past performance of duties was done with objectiveness, and deliverables were received on time. VTD also specializes in governmental accounting and was instrumental with VTA receiving a financial accounting certificate of excellence.

M/S/C (Herrera/Pyle) to authorize the General Manager to execute a contract with Vavrinek, Trine, Day and Co. to provide financial and compliance audit services to Santa Clara Valley Transportation Authority (VTA) for three years starting July 1, 2011 at a cost of \$375,000 and two additional one-year extensions at a cost of \$125,000 for each year. The total value of the contract for the five year period ending June 30, 2016 is \$625,000.

9. Internal Audit Workplan

Greg Thomas, Auditor General, provided a presentation on the status of the internal Audit Work Plan highlighting, the proposed timeline and reporting of internal activities, and the Silicon Valley Rapid Transit Project (SVRT) Contract Compliance Internal Audit. He noted the fieldwork of the evaluation and assessment of the contract between Hatch-Mott McDonald/Bechtel is nearly complete and an update will be provided at next Audit Committee Meeting.

On order of Chairperson Gage and there being no objection, the Committee received an update from Auditor General staff on the status of the audits in the current Internal Audit Work Plan.

OTHER ITEMS

10. Items of Concern and Referral to Administration

There were no Items of Concern and Referral to Administration.

11. Committee Work Plan

Mr. Burns noted several important items are scheduled for the November Agenda including review of the Comprehensive Annual Financial Report (CAFR) and ATU Pension Plan report, Contract Compliance Audit, and approving the Committee schedule for 2011.

Member Page requested the CAFR and Pension plan be distributed as soon as possible to give the Committee time to review.

On order of Chairperson Gage and there being no objection, the Committee reviewed and accepted the Committee Work Plan.

12. Committee Staff Report

There was no Committee Staff report.

13. Chairperson's Report

Chairperson Gage noted the Board adopted the Auditor General's recommended FY11 Internal Audit Workplan which continues the previous strategy of including both compliance and management audits. The first audit is scheduled to be received at the November meeting.

Chairperson Gage announced his final meeting as Chairperson and a member of the Committee will be in November. He stated he looks forward to receiving the results of the SVRT Compliance Audit at that meeting. He thanked the Committee for their role in helping the Board fulfill its obligations for safeguarding VTA's financial integrity.

14. Determine Consent Agenda for the October 7, 2010 Board Meeting

CONSENT: Item # 6, SAP Governance Risk & Compliance (GRC) Segregation of Duties and Sensitive Access Controls Internal Audit; and,

Item #8, Authorize the General Manager to execute a contract with Vavrinek, Trine, Day and Co. to provide financial and compliance audit services to Santa Clara Valley Transportation Authority (VTA) for three years starting July 1, 2011 at a cost of \$375,000 and two additional one-year extensions at a cost of \$125,000 for each year. The total value of the contract for the five year period ending June 30, 2016 is \$625,000.

REGULAR: None

15. Announcements

There were no Announcements.

16. Adjournment

On order of Chairperson Gage and there being no objection, the meeting was adjourned at 4:47 p.m.

Respectfully submitted,

Menominee L. McCarter, Board Assistant
VTA Office of the Board Secretary



Date: October 20, 2010
 Current Meeting: November 4, 2010
 Board Meeting: N/A

BOARD MEMORANDUM

TO: Santa Clara Valley Transportation Authority
 Audit Committee

THROUGH: General Manager, Michael T. Burns

FROM: Board Secretary, Sandra Weymouth

SUBJECT: 2011 Audit Committee Meeting Schedule

Policy-Related Action: No

Government Code Section 84308 Applies: No

ACTION ITEM

RECOMMENDATION:

Approve the 2011 Audit Committee Meeting Schedule.

BACKGROUND:

The VTA Board of Directors Audit Committee generally meets quarterly on the first Thursday of the month prior to the Board of Directors meeting. The following meeting dates are proposed for 2011. The Audit Committee meets at the County Government Center, 70 West Hedding Street, Room 157, at 4:00 p.m., or as otherwise posted.

Thursday, February 3, 2011	4:00 p.m.
Thursday, May 5, 2011	4:00 p.m.
Thursday, August 4, 2011	4:00 p.m.
Thursday, November 3, 2011	4:00 p.m.

FISCAL IMPACT:

There is no Fiscal Impact.

Prepared by: Tracene Y. Crenshaw
 Memo No. 2385



Date: October 25, 2010
 Current Meeting: November 4, 2010
 Board Meeting: December 9, 2010

BOARD MEMORANDUM

TO: Santa Clara Valley Transportation Authority
 Audit Committee

THROUGH: General Manager, Michael T. Burns

FROM: Chief Financial Officer, Joseph T. Smith

SUBJECT: Fiscal Year 2010 Comprehensive Annual Financial Report for the Santa Clara Valley Transportation Authority, and the Santa Clara Valley Transportation Authority Amalgamated Transit Union Pension Plan Report

Policy-Related Action: No

Government Code Section 84308 Applies: No

ACTION ITEM

RECOMMENDATION:

Review and receive the audited Comprehensive Annual Financial Report for the Santa Clara Valley Transportation Authority, and the Santa Clara Valley Transportation Authority Amalgamated Transit Union Pension Plan Report for Fiscal Year 2010.

BACKGROUND:

Pursuant to state law and the Administrative Code of the Santa Clara Valley Transportation Authority (VTA), Vavrinek, Trine, Day & Company, LLP (VTD), a Certified Public Accounting Firm, conducted an audit of VTA finances for the fiscal year ended June 30, 2010 (FY 2010). The auditors are required by audit standards to obtain reasonable assurance about whether the financial statements are free of material misstatement as well as assess whether the accounting principles used and estimates made by management are reasonable. Audited financial statements are required to be submitted to the State Controller, Metropolitan Transportation Commission, Federal and State agencies, and other parties such as the bondholders and financial rating agencies.

DISCUSSION:

Audit Results

VTD rendered a “clean” or unqualified opinion on VTA’s financial statements. The audit report states that VTA’s Comprehensive Annual Financial Report (CAFR) presents fairly, in all material respects, the respective financial position of the business-type activity, the governmental activities, each major fund, and the aggregate remaining fund information of VTA as of June 30, 2010, as well as the respective changes in financial position and cash flows. There were no material weaknesses noted in the internal controls over financial reporting and operations. The Independent Auditor’s opinion addressed to the Board is on pages 2-1 and 2-2 of the CAFR.

Auditor’s Management Letter

In planning and performing the audit of VTA’s financial statements, VTD considered VTA’s internal control system and procedures. Based on their consideration, they issued the Memorandum of Internal Controls or Management Letter addressed to the Board. This type of memo typically includes any audit findings or observations and recommendations to address the issue(s).

An audit finding denotes a serious violation of internal control procedures, such as a control deficiency, a significant deficiency or a material weakness, which must be addressed by the management. A control deficiency exists when the design or operation of control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects VTA’s ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the VTA’s financial statements that is more than inconsequential will not be prevented or detected by the entity’s internal control. A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the VTA’s internal control. An observation reflects recommended improvements to existing internal controls or procedures. There were no audit findings as a result of the FY2010 audit.

Audited Financial Statements

VTA uses the fund accounting system for financial reporting to ensure and demonstrate compliance with finance-related legal requirements. A fund is a grouping of related accounts that is used to maintain control over resources that have been segregated for specific activities or objectives. VTA’s funds can be divided into three categories: proprietary, governmental, and fiduciary.

The financial statements, related footnotes, and Management Discussion and Analysis as presented in the CAFR were prepared in accordance with the reporting requirements recommended by the Government Finance Officers Association (GFOA).

The GFOA awarded a Certificate of Achievement for Excellence in Financial Reporting to VTA for its CAFR for the fiscal year ended June 30, 2009. This was the 14th consecutive year that VTA achieved this coveted award. The award provides affirmation that VTA's Comprehensive Annual Financial Reports are consistently prepared in accordance with generally accepted accounting principles and applicable legal requirements.

The CAFR reports the results of operations for:

- Proprietary Funds
 - § VTA Enterprise - Transit Operating, 1996 Measure B Transit Rail Program; 2000 Measure A Transit Improvement Program
 - § Internal Service Fund - Workers' Compensation; General Liability; Compensated Absences
- Governmental Funds
 - § Special Revenue Fund - Congestion Management Program (CMP)
 - § Capital Projects Funds - Congestion Management & Highway Program; 1996 Measure B Highway Program
- Fiduciary Funds
 - § Trust Funds - VTA Amalgamated Transit Union (ATU) Pension Plan; ATU Spousal Medical and Retiree Vision/Dental Fund; Retirees' Other Post Employment Benefits (OPEB) Trust
 - § Agency Funds - Bay Area Air Quality Management District; 1996 Measure B Ancillary Program

Financial Highlights

Proprietary Funds

The Proprietary Funds account for activities that are reported using the full accrual basis of accounting. VTA maintains two types of proprietary funds: Enterprise Funds and Internal Service Funds.

Enterprise Funds

Enterprise Funds are used to account for functions of VTA that are principally supported by user charges, sales tax and intergovernmental revenues. There are three types of activities that fall under this category: VTA Transit Operating, 1996 Measure B Transit Rail Program, and 2000 Measure A Transit Improvement Program.

Statement of Revenues, Expenses, and Changes in Fund Net Assets

A Comparative Statement of Revenues, Expenses, and Changes in Fund Net Assets is included

on page 2-85 of the CAFR. For FY2010, operating revenues (mainly from transit service fares and advertisement income) were \$38.8 million, up \$391 thousand (1%) compared to FY2009. Fares from transit services increased \$673 thousand (1.9%) from the prior fiscal year mainly due to higher fare rates introduced during the fiscal year. VTA's largest revenue source for operating and capital funding, the 1976 Half-Cent Sales Tax and 2000 Measure A Half-Cent Sales Tax, were \$2.4 million (1.7%) and \$2.0 million (1.5%) higher, respectively, compared to FY2009, reflecting a small turnaround of taxable sales activity in the Santa Clara County. Operating grants consist mainly of Federal Section 5307 Urbanized Formula Grants, federal planning grants, State Transit Development Act (TDA) and other state and federal assistance grants (including new federal grant under the American Recovery and Reinvestment Act) were \$12.0 million (10.4%) higher than the prior fiscal year mainly due to an increase in Federal Section 5307 grant receipts.

Total operating expenses in FY2010 were \$6.5 million or 1.8% lower than FY2009 as VTA implemented various cost control measures in response to declining revenues. Labor costs were only \$389 thousand higher compared to the prior year as VTA implemented furlough programs for various employee categories and froze hiring of vacant positions. The non-labor expense categories that experienced significant variances in FY2010 include Services (\$4.4 million), Casualty and Liability Insurance (\$1.1 million), Purchased Transportation (\$3.7 million), Leases and Rentals (\$1.3 million) and Cost Allocated to Capital and Other Programs (\$5.6 million) resulting in an overall decrease in operating expenses compared to FY2009. For the non-operating expenses, the major change was in the Capital Contributions to/on-behalf of Other Agencies which increased \$39.1 million in FY2010. Interest expenses increased \$8.9 million mainly a result of reclassification of bond interest capitalized in prior years to interest expense in the Measure A Transit Improvement Fund.

Total Enterprise Fund net assets were \$2.8 billion, an increase of \$70.6 million over the FY2009 net assets. Of the total net asset increase, \$95.4 million was related the 2000 Measure A Transit Improvement Program Fund. VTA Transit Fund's net assets declined \$6.5 million in FY2010 mainly due to lower TDA and STA grant revenues. VTA accounts for the 2000 Measure A Transit Improvement Program as part of its Enterprise Fund. Even though the 2000 Measure A program revenues and related capital expenses are reported as part of Enterprise Fund financial statements, they are restricted for capital programs and operating activities included in the 2000 Measure A ordinance.

Reserves

As of June 30, 2010, VTA Transit Fund reports a total operating reserve balance of \$51.9 million. The VTA Board has established an operating reserve goal of 15% of the final operating budget at June 30 in the VTA Transit Enterprise Fund to meet emergency needs that cannot be funded from any other source. This is meant to ensure that funds are available in the event of unanticipated revenue shortfalls or if unavoidable expenditures may be required. As of June 30, 2010, the reported operating reserve balance is at 15% of the FY2010 final operating budget.

In addition to operating reserve balance, the Enterprise Fund also has a restricted and unrestricted reserve balance of \$547.0 million. Restricted funds are intended for specific purposes, bound by legally contracted agreements, Board policies, or ballot measure provision as approved by county voters. Of this amount, \$324.4 million represents local share of approved

capital funding that VTA must provide toward Board-approved capital projects, in the VTA Transit fund, Measure A Transit Improvement fund and Measure B Transit fund. The remaining amount is restricted or designated for debt service payments (\$16.9 million), debt reduction fund (\$53.2 million), SWAP/lease collateral (\$114.2), retention payment (\$3.9 million) and Inventory, Prepaid Expenses, and Issuance Costs (\$34.4 million). Details of the reserve balances are shown in the Financial Section of CAFR, page 2-24.

Budgetary Comparison

As shown on the Budgetary Comparison Schedule for the VTA Transit Fund (pages 2-87 & 2-88), the FY2010 actual results for revenues were unfavorable compared to both the Adopted and Final Budget. However, total operating and other expenses were below both the Adopted and Final Budget. VTA was originally projecting a net budgetary deficit of approximately \$3.8 million. Subsequently, the budgetary forecast was revised which showed a surplus of \$3.9 million. Based on the FY2010 actual results, VTA Enterprise Fund reported a budget surplus of \$16.3 million, a \$12.4 million favorable variance when compared to the Final Budget.

Internal Service Funds

Internal Service Funds are set up to account for services to other funds, departments or to other governments on a cost-reimbursement basis. General Liability, Workers' Compensation, and Compensated Absences programs are accounted for in the Internal Service Funds.

The Statement of Revenues, Expenses and Changes in Fund Net Assets (page 2-25) report an increase in net assets of \$3.1 million primarily due to higher contributions made to the funds than the claim payments made during the fiscal year (\$1.3 million). In addition, the investment earnings and other income of \$1.8 million contributed to the remaining increase in net assets. As reflected in the Statement of Fund Net Assets, page 2-24, Internal Service Fund column, total net assets amounted to \$18.5 million.

Governmental Funds

Governmental funds are reported using the modified accrual basis of accounting. This means that revenues are recognized in the accounting period in which they become "measurable and available." VTA's Governmental Funds are divided in two categories: Special Revenue Funds and Capital Projects Funds.

Special Revenue Funds are set up to account for revenues from specific taxes or other earmarked revenue sources which, by law, are designated to finance particular activities of government. The Congestion Management Program falls under the Special Revenue Fund category.

Capital Projects Funds are set up to account for resources used for acquisition or construction of major capital assets by a governmental unit. VTA reports the Congestion Management and Highway Program, and 1996 Measure B Highway Program under the Capital Projects Funds category.

Congestion Management Program (CMP)

The CMP Special Revenue Fund is used to account for the congestion management, planning, and programming and development services within the geographic boundaries of Santa Clara

County. The Statement of Revenues, Expenses and Changes in Fund Balances (page 2-29) reports a \$235 thousand increase in fund balance due to revenues exceeding expenditures in the current fiscal year. Total fund revenues, which mainly include member assessment and grants, were \$4.5 million in FY2010; \$184 thousand higher than the prior year due primarily to an increase in federal operating assistance grants. Total expenses were \$4.3 million, a decrease of \$1.5 million due mainly to lower VTA labor and overhead costs, and professional services. The CMP fund balance was \$287 thousand at the end of FY2010.

Congestion Management & Highway Program (CM&HP)

CM&HP Capital Projects Fund is used to account for the acquisition of capital assets and construction of highway projects administered on behalf of state and other local governments (other than those accounted for in the Measure B Highway Capital Projects Fund). The CM&HP administers highway projects on behalf of other agencies.

As reflected on page 2-29, the CM&HP expended approximately \$19.9 million on project costs during FY2010. The primary expenditures were for US101 Improvements (Embarcadero Road - SR85), Silicon Valley Express Lanes (SR237/I-880 Express Connectors), and I-880 HOV Widening (SR237-US101) projects. The bulk of the funding for these three projects came from federal grants and Measure A Swap funds. In total, CM&HP received approximately \$19.9 million in FY2010; comprised of \$5.3 million from federal grants, \$1.4 million from state grants, \$9.5 million from Measure A Swap funds, and \$3.7 million from other sources.

Measure B Highway Program

Measure B Highway Program Capital Projects Fund is used to account for acquisition of capital assets or construction of 1996 Measure B Highway projects. The Measure B Highway projects consist primarily of widening highways and improvements that become the property of the State.

As shown on page 2-29, VTA expended approximately \$2.4 million during FY2010 for Measure B Highway projects. Of this amount, \$2.2 million was contributed by Measure B Highway Fund and the remainder was received from 1996 Measure B Swap fund sources.

Fiduciary Funds

The Fiduciary Funds are used to account for assets held by VTA as a trustee (in a trust fund) and as an agent for others (in an agency fund). These assets cannot be used to support VTA's programs. VTA's Fiduciary Funds consist of trust and agency funds. The trust funds include the VTA ATU Pension Plan, ATU Spousal Medical and Retiree Vision/Dental Fund, and the Retirees' Other Post Employment Benefits (OPEB) Trust. The VTA ATU Pension Plan Report is discussed on page 8 of this report. Bay Area Air Quality Management District and the Measure B Ancillary Programs are reported as agency funds.

Retirees' Other Post Employment Benefits (OPEB) Trust

The Retirees' Other Post Employment Benefits (OPEB) Trust was established by VTA to implement the GASB Statement Number 45 in FY2008. In prior fiscal years, VTA reported the retiree medical program as part of its Internal Service Funds. The Combining Statement of Changes in Fiduciary Net Assets (page 2-90) shows a total increase of \$19.4 million to the Trust in the current fiscal year. It includes the actuarially determined Annual Required Contribution of

\$14.2 million from VTA to the Trust. Investment earnings were \$12.7 million due primarily to mark-to-market investment gains of \$10.1 million on the Trust investments as of June 30, 2010. Total expenses of the Trust, which mainly include the retiree medical premium payments were \$7.5 million. As of June 30, 2010, total net assets held in the OPEB Trust totaled \$119.7 million. As required by GASB, VTA has also published a separate financial report for the OPEB Trust.

ATU Spousal Medical and Retiree Vision/Dental Funds

These funds account for the ATU Spousal Medical Program, which is a medical insurance benefit for eligible pensioners' spouses, and the ATU Retiree Vision/Dental Program, which is a vision and dental benefit for eligible pensioners. Both benefits are funded through employee contributions.

As shown on the Combining Statement of Changes in Fiduciary Net Assets for Retiree Trust Funds (page 2-91), total employee contributions to Spousal Medical and Vision/Dental were approximately \$910 thousand and \$325 thousand, respectively. Total benefit payments made on behalf of ATU Spousal Medical Fund totaled \$1.2 million for FY2010. Total changes in net assets show an increase of \$1.4 million for both funds. Total net assets were \$7.6 million for Spousal Medical and \$4.4 million for Vision/Dental.

Bay Area Air Quality Management District (BAAQMD)

The BAAQMD Agency Fund accounts for the activities that relate to the Transportation Fund for Clean Air (TFCA) Program. The TFCA is generated by a \$4 surcharge on vehicle registrations in the county. The BAAQMD administers these funds in the nine-county Bay Area. Funds are available for allocation to alternative fuels, arterial management, bicycle, and trip-reduction projects that reduce vehicle emissions. Assets in the BAAQMD fund are held by VTA in a custodial capacity; therefore, they are reported in the Agency Fund. As of June 30, 2010, BAAQMD's total assets were approximately \$3.3 million, as reflected on page 2-92.

Measure B Ancillary Program

The Measure B Ancillary Program was established to administer the 1996 Measure B funds. During FY2010, VTA received and expended County contributions for Ancillary Program projects such as highway and intersection improvements, signal synchronization, and bikeway paths. The County contribution represents funding received and passed on to other governments, commonly referred to as "pass-through" grants. As of June 30, 2010, the total assets of this program were \$2.2 million (page 2-92).

AMALGAMATED TRANSIT UNION (ATU) PENSION PLAN REPORT

The Santa Clara Valley Transportation Authority ATU Pension Plan Fund reports on the activities of the pension benefit plan covering VTA employees represented by the Amalgamated Transit Union (ATU). The ATU Pension Plan is 100% funded by VTA's contribution.

Audit Results

VTD rendered a "clean" or unqualified opinion on the ATU Pension Plan Report, a component unit report of VTA's CAFR. The audit report states that it presents fairly, in all material respects, the activities of the ATU Pension Plan for the year ended June 30, 2010, in conformity the accounting principles generally accepted in the United States of America. The Independent Auditor's opinion addressed to the Board is on page 1 of the component unit report.

Financial Highlights

As shown on the Statement of Changes in the Plan Net Assets of ATU Pension Plan Report (page 6), net assets increased \$34.6 million for the year ended June 30, 2010. The major factor for the increase was \$38.9 million in net investment earnings during the fiscal year including mark-to-market valuation gains of \$27.3 million. VTA contributions to the Plan were \$17.9 million and the benefit payments to retirees and administration expenses were \$22.3 million during FY2010. As of June 30, 2010, net assets amounted to \$317.4 million. Report details are shown on pages 5 & 6 of the ATU Pension Plan component unit report.

These financial statements can be viewed online at <http://www.vta.org/inside/investor/index.html>. A hard copy may be requested by writing to Santa Clara Valley Transportation Authority, Fiscal Resources Division, 3331 North First Street, San Jose, CA 95134-1927.

FISCAL IMPACT:

There is no fiscal impact as a result of this action.

Reviewed and verified by: Grace Ragni, Fiscal Resources Manager

Reviewed and verified by: Ali Hudda, Deputy Director of Accounting

Prepared by: Tony S. Sandhu, Financial Accounting Manager
Memo No. 2382

[Click here to view the Fiscal Year 2010 Comprehensive Annual Financial Report](#)

[Click here to view the VTA Amalgamated Transit Union Pension Plan Report](#)



Date: October 19, 2010
 Current Meeting: November 4, 2010
 Board Meeting: December 9, 2010

BOARD MEMORANDUM

TO: Santa Clara Valley Transportation Authority
 Audit Committee

THROUGH: General Manager, Michael T. Burns

FROM: Chief Financial Officer, Joseph T. Smith

SUBJECT: Audited Santa Clara Valley Transportation Authority Retirees' Other Post
 Employment Benefits (OPEB) Trust Financial Report for Fiscal Year 2010

Policy-Related Action: No

Government Code Section 84308 Applies: No

ACTION ITEM

RECOMMENDATION:

Review and receive the Audited Financial Report for Fiscal Year 2010 of the Santa Clara Valley Transportation Authority Retirees' Other Post Employment Benefits Trust (Trust).

BACKGROUND:

Pursuant to the provisions of the Trust, Vavrinek, Trine, Day & Company, LLP (VTD), a Certified Public Accounting Firm, conducted an audit of the Trust's finances for the fiscal year ended June 30, 2010 (FY2010). The auditors are required by audit standards to obtain reasonable assurance about whether the financial statements are free of material misstatement as well as assess whether the accounting principles used and estimates made by management are reasonable.

The Trust was established by VTA Board of Directors in May 2008 to comply with the accounting pronouncement promulgated by the Government Accounting Standards Board (GASB) - the accounting standard making body for the state and local governments, and special districts such as VTA. The Trust financial statements report on the activities of the retiree medical benefit program for Santa Clara Valley Transportation Authority employees who meet certain age and service criteria and retire directly from VTA. The Trust is 100% funded by VTA's contributions.

DISCUSSION:**Audit Results**

VTD rendered a “clean” or unqualified opinion on the Trust Financial Report, a component unit of VTA’s Consolidated Annual Financial Report (CAFR). The audit report states that it presents fairly, in all material respects, the activities of the Trust for the year ended June 30, 2010, in conformity with the accounting principles generally accepted in the United States of America. The Independent Auditor’s opinion addressed to the Board is on page 1 of the Audited Financial Report.

Financial Highlights

The Statement of Changes in Trust Net Assets (page 6) shows a total increase of \$19.4 million in Trust net assets for the year ended June 30, 2010. It includes the actuarially-determined Annual Required Contribution amount of \$14.2 million from VTA to the Trust. Net investment income was \$12.7 million due primarily to mark-to-market investment gains of \$10.1 million on the Trust investments as of June 30, 2010. Total expenses of the Trust, which mainly include the retiree medical premium payments, were \$7.4 million. As of June 30, 2010, total net assets held by the Trust totaled \$119.7 million. Report details are shown on pages 5 & 6 of the Audited Financial Report.

These financial statements can be viewed online at <http://www.vta.org/inside/investor/index.html>. A hard copy may be requested by writing to Santa Clara Valley Transportation Authority, Fiscal Resources Division, 3331 North First Street, San Jose, CA 95134-1927.

FISCAL IMPACT:

There is no fiscal impact as a result of this action.

Reviewed and Verified by: Grace Ragni, Fiscal Resources Manager

Reviewed and Verified by: Ali Hudda, Deputy Director of Accounting

Prepared by: Tony S. Sandhu, Financial Accounting Manager
Memo No. 2383

[Click here to view Audited Financial Report for Fiscal Year 2010 of the Santa Clara Valley Transportation Authority Retirees' Other Post Employment Benefits Trust \(Trust\).](#)



Date: October 22, 2010
Current Meeting: November 4, 2010
Board Meeting: December 9, 2010

BOARD MEMORANDUM

TO: Santa Clara Valley Transportation Authority
Audit Committee

THROUGH: General Manager, Michael T. Burns

FROM: Auditor General, Greg Thomas

SUBJECT: SVRT Contract Compliance Internal Audit

FOR INFORMATION ONLY

BACKGROUND:

The VTA Board of Directors in January 2009 approved the contract with Deloitte & Touche, LLP (D&T) to provide Auditor General and internal audit services to VTA.

In August 2010, the Board approved the FY11 Internal Audit Work Plan recommended by the Auditor General. That same month, Deloitte & Touche, LLP, in its capacity as VTA's Internal Audit, initiated the second item identified in this plan: Silicon Valley Rapid Transit (SVRT) Project Contract Compliance. The audit was performed in accordance with the Standards for Consulting Services issued by the American Institute for Certified Public Accountants.

DISCUSSION:

The Silicon Valley Rapid Transit (SVRT) project, now known as the Bay Area Rapid Transit (BART) Silicon Valley Project, is a 16-mile extension of the existing BART system to San Jose, Milpitas and Santa Clara, which will be delivered through a phased approach. The first phase, the Berryessa Extension, is a 10-mile, two-station extension beginning in Fremont at the future BART Warm Springs Station and proceeding through Milpitas, the location of the first station, and going to the Berryessa area of north San José, at the second station. VTA continues the design and engineering for the second 6-mile phase of the project that includes a 5.1 mile-long subway tunnel through downtown San Jose, and ends at grade in Santa Clara near the Caltrain Station. Construction on the second phase of the project will commence as additional funding is secured

The joint venture of Hatch Mott McDonald (HMM) and Bechtel is under contract to VTA to provide consultant design, engineering and project management services on the SVRT Project. The contract's effective date was February 9, 2004. Through May 2010, expenditure commitments on this contract have been approximately \$124 million.

The purpose of this internal audit was to conduct a contract compliance audit of the HMM/Bechtel contract to gain an understanding of how this contract is currently being managed, and identify areas for improvement in its organization, deliverables, milestones, and cost reporting. The audit focused exclusively on the Berryessa Extension phase.

Internal Audit completed its review and the results of this audit are presented in Auditor General Report No. 2010-02 (see Attachment B). This report describes in detail the objectives established for this audit, its scope, and the approach used by the internal audit team. The report presents the internal audit team's observations, the risk rating associated with each observation as well as an overall risk rating to the VTA organization, and the Auditor General's recommendation for addressing each observation. The report also includes VTA management's response to each observation, and the steps that have or will be taken to address the Auditor General's recommendations. Attachment A summarizes the audit's objectives and scope, the internal audit team's observations and recommendations, and VTA management's response.

An overall risk rating of Medium was issued, based on four individual observations rated Medium and six rated Low. No high risk issues were identified. However, the large size, complexity and financial magnitude of the SVRT project was factored into both the individual and overall risk ratings, and this factor helped to push the overall risk rating from Low to Medium. VTA agreed with these findings, and all recommendations will be targeted for implementation by June 30, 2011.

Recommendations for improvement contained in this report are presented for the consideration of VTA management, which is solely responsible for the effective implementation of any corrective action plans.

Prepared By: Greg Thomas, Auditor General
Memo No. 2711



Santa Clara Valley Transportation Authority

Audit Committee Meeting, Agenda Item No. 8

‘SVRT Program Contract Compliance Internal Audit

November 4, 2010

Auditor General’s Office

Greg Thomas, Principal

Denise Martini, Director

Michael Kling, Senior Manager

Marius Anelauskas, Senior Associate

SVRT Program Contract Compliance Internal Audit

Audit Objectives & Scope

Objectives		
<ul style="list-style-type: none"> Evaluate contract compliance related to Contract organization, deliverables and milestones; Evaluate whether consultant team was reporting deliverables and cost information in accordance with the Contract requirements; Identify potential areas of improvement in managing and monitoring the services provided under the Contract. 		
Scope		
<ul style="list-style-type: none"> HMM / Bechtel Original Contract HMM / Bechtel Contract Amendments HMM / Bechtel Contract Invoices) Monthly Cost Reports 	<ul style="list-style-type: none"> HMM / Bechtel Contract Work Directives Monthly Work Directive Cost Reports Quarterly FTA Updates Various SVRT Policies and Procedures 	<ul style="list-style-type: none"> Invoice Review and Processing SDBE Requirements Contract Amendment Processing Monthly Reporting Process

Observations	Recommendations	Mgmt. Response
1. Contract Amendments <i>(Risk Rating: Low)*</i>		
<p>Amendments to the Contract were signed by VTA after the effective date, as specified within the Amendment.</p>	<p>Although funds are approved by the VTA Board of Directors prior to expenditure, Management should ensure appropriate documentation of approval in the administration of funds.</p>	<p>VTA concurs. Management will be committing additional contract management and project management resources to the SVRT Program, and will do so by June 2011. These additional resources will review the contract amendment processes and establish clear guidelines with project staff to assure timely execution of contract amendments.</p>

* See Appendix on Page 5 for risk rating definitions and Overall Risk Rating resulting from work performed.

SVRT Program Contract Compliance Internal Audit

Observations	Recommendations	Mgmt. Response
<p>2a. Invoices <i>(Risk Rating: Medium)*</i></p>		
<p>No formal policy observed relating to signature requirements for Contract Attest and Contract Administration. Identified instances where Contract Attest approved invoices without Contract Administration Approval.</p>	<p>Management should finalize the updated procedure for the internal review of invoices, and include definition of roles, responsibilities, and signature requirements of Contract Administration and Contract Attest functions.</p>	<p>VTA concurs. The existing procedures are being updated to reflect the recommendations made in the SVRT Soft Cost Audit and will be finalized by November 30, 2010. The current forms, including the invoice approval sheet, are also being updated and will be finalized by November 30, 2010.</p>
<p>2b. Invoices <i>(Risk Rating: Low)*</i></p>		
<p>Identified invoices where payments were made past the due date of 30 days.</p>	<p>Management should assess invoice approval process, and identify opportunities to streamline this process. Furthermore, Management should consider establishing a tracking methodology to flag invoices approaching Contract due dates.</p>	<p>VTA concurs and has implemented all of the recommendations. The invoice approval process has been streamlined and turnaround times for various levels of invoice approvals have been established. A tracking mechanism has been implemented.</p>
<p>3. Labor Rates <i>(Risk Rating: Medium)*</i></p>		
<p>Observed one year during which annual consultant rate increases were higher than those specified within the Contract. Higher rates are allowed as exceptions under the Contract; however, rate increases were higher for 30 out of 33 personnel.</p>	<p>Management should consider adherence to the established labor rate escalation guidelines as specified within the Contract.</p>	<p>VTA concurs with the recommendation. VTA contracts allow exceptions to the limitation on rate adjustments upon review and consideration by VTA. In 2009, VTA instituted a policy of allowing zero consultant rates increases with only limited exceptions on a case by case basis. The date examined for this audit was for a period prior to implementation of this policy.</p>

SVRT Program Contract Compliance Internal Audit

Observations	Recommendations	Mgmt. Response
4a. Work Directives (WD) – Monthly Reports <i>(Risk Rating: Low)*</i>		
Identified discrepancies between invoice amounts and the WD monthly reports of costs incurred to date. Noted descriptive reporting in December 2009 and January 2010 included substantially less detail than specified in the VTA policies/requirements.	<ul style="list-style-type: none"> •Management should consider making it clear costs reported in WD Monthly Report are not actual costs but an estimate/forecast. •Management should verify descriptions of progress for each month are sufficient to understand prior month’s work in order to make any necessary adjustments. 	VTA concurs. The regular reporting for WD’s will be adjusted to clarify forecast versus actual statements of cost info. Also, monthly progress descriptions will be reviewed and modified as necessary to help ensure sufficient levels of detail and clarity. Recommendations will be completed by March 2011.
4b. Work Directives (WD) – Budgets <i>(Risk Rating: Low)*</i>		
Noted one instance where final WD value was above established value.	Management should consider implementing strategies to keep expenditures within estimated amounts stated in WD. Management should also consider developing a requirement for exceptions, which would describe the need to include appropriate documentation of approval within the WD amendment or close-out documentation.	VTA concurs. Management will investigate strategies to keep expenditures within estimated amounts in WD. Current procedures will also be modified so necessary exceptions are documented in WD amendment or close-out documentation. Recommendations will be completed by March 2011.
5. Deliverables <i>(Risk Rating: Low)*</i>		
Identified instances where WD deliverables were not clearly delineated in the WD forms, which include a “Deliverables” section. In particular, it was noted that one WD that did not specify deliverables within the “Deliverables” section, although WD suggested specific requirements.	Management should consider requiring additional detail within WDs to establish clear WD deliverables. In addition, Management should consider formally using some type of roadmap or matrix to track all major deliverables that are prepared as part of the Contract to allow for transparency as well as a paper trail for work that is being completed by the consultant team.	VTA concurs. Management will adjust the work directive process to incorporate close-out and reconciliation documentation of actual costs and the completion of work. This will be completed by June 2011.

SVRT Program Contract Compliance Internal Audit

Observations	Recommendations	Mgmt. Response
<p>6. SVRT Program/Project Roles and Responsibilities <i>(Risk Rating: Low)*</i></p>		
<p>Noted open SVRT Berryessa Extension Project Director position. At the time of analysis, the Deputy Director SVRT Program was filling the open position as the SVRT Berryessa Extension Project “Acting” Project Director. As a result, he was working in two roles simultaneously.</p>	<p>Management should consider filling open position as soon as possible. If the open position is filled by an employee under the existing Contract, VTA Management should structure project admin. process such that any adjustments to Contract or scope of work are subject to review or approval by a VTA management employee at same level or above the Contract employee.</p>	<p>VTA concurs. This position was filled effective September 7, 2010.</p>
<p>7. Subconsultants <i>(Risk Rating: Medium)*</i></p>		
<p>Noted instances where subconsultants included in invoices were not included in list of subconsultants specified in Contract or current amendment at time of invoice. Additionally, although no debarred or suspended vendors were observed, certifications were not kept on file.</p>	<p>Management should consider establishing a formal process for tracking status of suspension / debarment certifications. Additionally, Management should consider performing periodic evaluations of subconsultants billed to invoices against the approved subconsultant list.</p>	<p>VTA concurs. VTA will consider enhancing contract language that defines the responsibility of the Prime as it relates to suspension/debarment certification. Management will also assess the best method to ensure contract compliance. Both of these efforts will be completed by June 2011.</p>
<p>8. Certificates of Insurance <i>(Risk Rating: Medium)*</i></p>		
<p>Several instances were noted where subconsultant insurance coverage was below Contract or did not include all insurance types. An organized filing system was not observed for tracking the necessary documentation to support the insurance requirements of the subconsultants.</p>	<p>Management should consider establishing a policy to perform periodic evaluations of insurance for prime consultants as well as subconsultants. Furthermore, Management should consider using a tracking sheet, matrix and filing process to track compliance or exceptions and certificates for various insurance types for the prime and subconsultants.</p>	<p>VTA will review the current process of tracking the receipt of insurance certificates for prime consultants and ensure that continuing insurance coverage is reported. This effort will be completed by December 31, 2010. VTA’s contractual relationship is with the prime contractor and the insurance clause in the contract requires them to carry adequate coverage for all contingencies including subcontractor contingencies.</p>

AUDITOR GENERAL REPORT No. 2010-02

TO: Chair Audit Committee, Don Gage
Santa Clara Valley Transportation Authority

THROUGH: General Manager, Michael Burns

FROM: Auditor General

DATE: October 18, 2010

SUBJECT: Silicon Valley Rapid Transit Program – Hatch Mott McDonald (“HMM”) /
Bechtel Contract Compliance Internal Audit

Enclosed is our report for the Silicon Valley Rapid Transit Program HMM / Bechtel Contract Compliance Internal Audit.

Our internal audit was performed in accordance with the terms of our engagement letter between Santa Clara Valley Transportation Authority and Deloitte & Touche LLP for Auditor General Services, Contract No. S09022 dated January 9, 2009, and in accordance with the Standards for Consulting Services issued by the American Institute of Certified Public Accountants. This report is intended solely for the information and use of Management and the Audit Committee of the Santa Clara Valley Transportation Authority (VTA) and is not intended to be used by anyone other than these specified parties. Recommendations for improvement are presented for Management’s consideration. Management is responsible for the effective implementation of corrective action plans.

Please contact Greg Thomas, Principal, in the VTA Auditor General’s office, if you have any questions.

This report is intended solely for the information and internal use of Santa Clara Valley Transportation Authority, and should not be used or relied upon by any other person or entity.

AUDITOR GENERAL REPORT No. 2010-02

Silicon Valley Rapid Transit Program Contract Compliance Audit

October 18, 2010

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This report is intended solely for the information and internal use of Santa Clara Valley Transportation Authority, and should not be used or relied upon by any other person or entity.

I. EXECUTIVE SUMMARY

The Santa Clara Valley Transportation Authority's ("VTA") Silicon Valley Rapid Transit ("SVRT" or "SVRT Program") Project is a 16-mile extension of the Bay Area Rapid Transit District system ("BART") from a future Warm Springs station in Fremont to the cities of San Jose, Milpitas and Santa Clara in Santa Clara County.

Internal Audit (IA) performed a contract compliance internal audit of SVRT's HMM / Bechtel Joint Venture consultant contract (Contract # S03099) (the "Contract") with the following objectives:

- ❖ Evaluate and assess contract compliance related to Contract organization, deliverables and milestones;
- ❖ Evaluate and assess whether the consultant team was reporting deliverables and cost information in accordance with the Contract requirements; and
- ❖ Identify potential areas of improvement in managing and monitoring the services provided under the Contract.

The contract compliance internal audit work focused on the SVRT Program's Silicon Valley Berryessa Extension Project ("Berryessa Extension" or "Berryessa Extension Project"), which is a portion of the 16-mile extension of the SVRT Project that is currently in progress. At the time of our work, the Berryessa Extension Project was in the midst of preparing for entry into the FTA New Starts Final Design phase.

Based on the internal audit work performed, controls designed to help ensure effective contract management processes, such as proper approval and monitoring, need strengthening. Our overall assessment of the relative risk related to the identified control weaknesses is Medium. The Medium rating, which represents an estimated level of risk exposure to the VTA organization, was developed by evaluating ten different observations individually and collectively and then taking into account the large size, complexity and financial magnitude of the SVRT project. The Medium rating is based upon four individual observations rated Medium and six individual observations rated Low. No high risk issues were identified. VTA agreed with these findings, and all recommendations will be targeted for implementation by June 30, 2011.

Based on our Contract compliance internal audit work, observations were identified related to contract amendments, invoices, labor rates, work directives, deliverables, SVRT Program/Project Roles and Responsibilities, subconsultants, and certificates of insurance. Some of the key observations include the following:

- ❖ **Contract Amendments**
 - Effective Date - We identified several instances where amendments to the Contract were signed by VTA after the effective date as specified within the amendment.
- ❖ **Invoices**
 - Review Process – There was no formal VTA policy observed for how VTA personnel review and approve Contract invoices.
 - Timing of Invoice Approval Process - For several of the invoices that were evaluated, payments were made past the due date of 30 days.

❖ **Labor Rates**

- Escalation/Adjustments – An instance was identified where a group of rate increases were higher than the rates specified within the Contract.

❖ **Subconsultants**

- Small / Disadvantaged Business Enterprise (“S/DBE”) Certification Tracking – No formal process was observed to track S/DBE certificates, or any changes in S/DBE status among subconsultants during the project.
- Debarment and Suspension – No formal process was observed to track the certification of debarment and suspension of subconsultants from HMM / Bechtel per Contract requirements.

❖ **Certificates of Insurance**

- Subconsultant Insurance – Several instances were noted where coverage was below the amount required by Contract. Additionally, the proof of insurance observed did not include all insurance types.

More detailed observations and recommendations are provided in the main body of the report.

II. BACKGROUND

The Santa Clara Valley Transportation Authority’s (“VTA”) Silicon Valley Rapid Transit (“SVRT” or “SVRT Program”) Project comprises a 16-mile extension of the Bay Area Rapid Transit District system (“BART”) from a future Warm Springs station in Fremont to the cities of San Jose, Milpitas and Santa Clara in Santa Clara County, CA. The full SVRT Project (“Project”) comprises six stations from Fremont through Milpitas and downtown San Jose and into the City of Santa Clara, CA near the San Jose International Airport. Roughly five miles of the alignment will be underground in a twin bored tunnel.

The Contract’s effective date was February 9, 2004. Through May 31, 2010, contracted commitments for expenditures on the Contract totaled approximately \$124.0 million. These costs include approximately \$51.2 million for 35 percent-complete tunnel design and program management phase, \$43.3 million for 65 percent-complete tunnel design and program management phase, \$10.0 million for program management through December 2009, and an additional \$19.5 million for program management through March 2011.

The contract compliance internal audit work focused on the SVRT Program’s Silicon Valley Berryessa Extension Project (“Berryessa Extension” or “Berryessa Extension Project”), which is the portion of the entire 16-mile extension of the SVRT Project that is currently in progress. At the time of our work, the Berryessa Extension Project was in the midst of preparing for entry into the FTA New Starts Final Design phase. Specifically, this internal audit included an evaluation and assessment of contract compliance related to Contract organization, deliverables and milestones; an evaluation and assessment of whether the consultant team was reporting deliverables and cost information in accordance with the Contract requirements; and identification of potential areas of improvement in managing and monitoring the services provided under the Contract.

III. OBJECTIVE, SCOPE & APPROACH

A. Objective

The objectives of the Contract compliance internal audit of the HMM / Bechtel Contract were to:

- ❖ Evaluate and assess Contract compliance related to
 - how the Contract is organized,
 - whether deliverables are provided by HMM / Bechtel per the Contract, and
 - how the Contract is administered by VTA;
- ❖ Evaluate and assess whether the HMM / Bechtel consultant team was reporting deliverables and cost information in accordance with the Contract requirements; and
- ❖ Identify potential areas of improvement for VTA in managing and monitoring the services provided under the Contract.

B. Scope

The analysis included an assessment of HMM / Bechtel's compliance with the Contract and VTA's administration of the Contract. We evaluated the Contract information and documentation, Contract amendments, VTA policies and procedures, Contract cost information and Contract deliverables.

C. Approach

The approach to fieldwork, conducted in August 2010, included the following:

- ❖ Read and analyzed relevant SVRT project documents and policies and procedures.
- ❖ Conducted interviews and follow-up discussions with VTA and consultant personnel who are involved in either managing the consultant work or providing the services to VTA to gain an understanding of the Contract and the work associated with the Contract.
- ❖ Conducted interviews and follow-up discussions with VTA and consultant personnel to gain an understanding of the VTA Contract compliance policies and procedures used to manage performance of the Contract.
- ❖ Evaluated and assessed Contract compliance attributes to determine if they were consistent with Contract requirements.
- ❖ Read and analyzed cost data from October 2009 through May 2010 and other project documents related to the Contract from March 2003 through May 2010.
- ❖ Developed observations and recommendations for improvement and discussed observations with VTA Management prior to issuing report.

IV. RATINGS

Risk ratings have been assigned to each observation to provide VTA Management with a better understanding of the risk and potential impact of each observation. In addition, an Overall Risk Rating has been provided herein to help Management understand the overall risk and impacts of the observations. For this report, the risk ratings take into consideration the magnitude of the immense size, complexity and financial commitments of the SVRT Program and its Berryessa Extension component.

The VTA risk rating definitions are:

- ❖ High – Significant control weakness presents a high likelihood of the event occurring potentially exposing VTA to significant financial loss, unauthorized access to key data, business or service interruption, and/or an impact to the VTA brand or public perception. This control weakness should be addressed promptly. If not addressed or corrected, it could expose VTA to significant financial or other loss, or otherwise significantly impair its reputation.
- ❖ Medium – Significant control weakness presents a possibility the event will occur potentially exposing VTA to moderate levels of financial loss, short term disruption to operations, short term impact to VTA brand or public perception and/or not making full use of human or system resources. This control weakness should be addressed in the near term.
- ❖ Low – Control weakness, if corrected or mitigated, will further strengthen the system of internal control. Likelihood of occurrence and impact if the event did occur are rated as low.
- ❖ Other Opportunities (No Rating) – Opportunity to improve efficiency or profitability of operations, but does not indicate an internal control weakness.

The risk ratings resulting from the work performed are provided to help Management understand the relative risk and potential impact of the observations.

Overall Risk Rating

Our overall assessment of the relative risk related to the identified control weaknesses is Medium.

Overall Risk Rating: Medium

The Medium rating, which represents an estimated level of risk exposure to the VTA organization, was developed by evaluating ten different observations individually and collectively and then taking into account the large size, complexity and financial magnitude of the SVRT project. The Medium rating is based upon four individual observations rated Medium and six individual observations rated Low. No high risk issues were identified.

V. RESULTS:

The following sections summarize the internal audit observations, each individual area's risk rating, recommendations from the Auditor General's office, and Management's responses. The results of our field work have been reported and are delineated below in the sections entitled Contract Amendments, Invoices, Labor Rates, Work Directives, Deliverables, SVRT Program/Project Roles and Responsibilities, Subconsultants, and Certificates of Insurance.

1. Contract Amendments

An evaluation of the Contract amendments was conducted to assess consistency in approval methodology, timing, and board approval of funds allocated through Contract amendments. We evaluated the Contract, as well as 29 amendments to the Contract, and noted the following with respect to the effective date of the Contract Amendments:

- a. **Effective Date** - We noted 16 cases (55% of Amendments) where the Amendments to the Contract were signed by VTA after the effective date, as specified within the Amendment. Per discussion with client personnel, late signatures may have occurred

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because final negotiations to the Amendments may have occurred after the required start date of the work associated with each of the Amendments. Additionally, according to VTA personnel, approval by the VTA Board of Directors was received prior to the effective dates of any Amendments which authorized specific contract funding or provisions. In one case, we noted an Amendment that was dated several months after the specified effective date, thus retroactively implementing changes to the Contract.

Recommendation:

Management should verify that Contract amendments are appropriately signed prior to the effective date of each Contract amendment. Although funds are approved by the VTA Board of Directors prior to expenditure, Management should ensure appropriate documentation of approval in the administration of funds. Additionally, VTA management should evaluate the practice of establishing Contract amendments which amend Contract terms retroactively. Formal policies should be developed to help ensure timely acceptance of Contract amendments.

Risk Rating: Low

Management Response:

VTA concurs. Management will be committing additional contract management and project management resources to the SVRT Program, and will do so by June 2011. These additional resources will review the contract amendment processes and establish clear guidelines with project staff to assure timely execution of contract amendments.

2. Invoices

An evaluation of the invoices from October 2009 – May 2010 was conducted to identify Contract and policy compliance, including invoice review and certification, payment timing, and backup documentation. We noted the following with respect to the review process and payment timing:

- a. **Review Process** – The existing VTA procedure for how VTA personnel review Contract invoices is out-of-date and not fully comprehensive. It is currently undergoing revision and augmentation. The following summarizes our understanding of how Contract Attest and Contract Admin work together to review Contract invoices-:
 - i. There is a summary level draft process in place for invoice review, currently being evaluated and updated by VTA.
 - ii. Contract Attest determines any issues relating to invoice backup documentation, and identifies any necessary short payment.
 - iii. Contract Administration works with HMM / Bechtel and Contract Attest to facilitate delivery of necessary documentation for full or partial invoice payment. No formalized process was observed in this area.
 - iv. There was no formal policy observed relating to signature requirements for Contract Attest and Contract Administration. Of nine invoices evaluated, six instances were identified where Contract Attest approved the invoice without Contract Administration Approval. Two instances were identified where Contract Administration approved the invoice without Contract Attest Approval. The invoice approval sheet does not include signature areas for both Contract Attest and Contract Administration.

Recommendation:

Management should consider finalizing the updated procedure for the internal review of invoices. This procedure should include definition of roles, responsibilities, and signature requirements of Contract Administration and Contract Attest functions. Furthermore, Management should re-evaluate the current format of the invoice approval sheets, and create separate signature areas for Contract Attest and Contract Administration

Risk Rating: Medium

Management Response:

VTA concurs. The existing procedures are being updated to reflect the recommendations made in the SVRT Soft Cost Audit and will be finalized by November 30, 2010. The current forms, including the invoice approval sheet, are also being updated and will be finalized by November 30, 2010.

- b. **Timing of Invoice Approval Process** - In six out of the eight invoices that were evaluated, payments were made past the due date of 30 days. We noted the following:
- i. On average, the late invoices were paid 6.7 days past the 30 days specified by Contract.
 - ii. On average, the time from approval by Contract Attest / Contract Administration until approval by VTA Project Controls was 20.8 days
 - iii. Following VTA Project Controls approval, invoices were signed by VTA Berryessa Extension PM within an average of two days.

Recommendation:

Management should assess the invoice approval process, and identify opportunities to streamline this process. Furthermore, Management should consider establishing a tracking methodology to flag invoices that are approaching the due dates as established by the Contract.

Risk Rating: Low

Management Response:

VTA concurs and has implemented all of the recommendations. The invoice approval process has been streamlined and turnaround times for various levels of invoice approvals have been established. A tracking mechanism has been implemented to help ensure that the invoice approval process is completed in a timely manner and exceptions identified and flagged for escalation.

3. Labor Rates

An evaluation of the labor rate escalation, dated April 30, 2008 and December 31, 2007 for Bechtel and HMM, respectively, was conducted to determine the compliance of labor rate escalation with requirements set forth in the Contract. We noted the following:

- a. **Escalation/Adjustments** – We tested the labor rate adjustments for April 30, 2008 for the Bechtel consultants and for December 31, 2007 for the HMM consultants. The

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Bechtel rate increases were within the Contract allowances. HMM rate increases were higher than those specified within the Contract. The rate increases ranged from 1.04% to 11.76% with an average rate increase of 6.1%, compared to the rate increase allowed by Contract of 4.84%. For non-promoted personnel, the average rate increase was 5.4%. Higher rates are allowed as exceptions under the Contract; however, rate increases for 30 out of 33 personnel, including 25 non-promotion personnel shown on the HMM rate sheet, exceeded the Contract allowances. The fiscal impact of the adjustments was not calculated as part of this analysis.

Recommendation:

Management should consider adherence to the established labor rate escalation guidelines as specified within the Contract. Additionally, for cases where an exception from the specified labor escalation rate is executed, Management should consider including a memorandum to file documenting reasons for the exception(s).

Risk Rating: Medium

Management Response:

VTA concurs with the recommendation. VTA contracts allow exceptions to the limitation on rate adjustments upon review and consideration by VTA. It should be noted that in 2009, VTA instituted a policy of allowing zero consultant rates increases with only limited exceptions on a case by case basis. The data examined by this audit report are for a period occurring before this policy was instituted.

The Bechtel consultants represent approximately half of the total direct labor component for this HMM/Bechtel joint-venture contract, and the audit findings indicate that this component was within the contract allowances. The HMM consultant requested exceptions to the contract allowances were based on employment classification changes (promotions) and recognition of new professional credentials. In other cases, specific rationale provided by HMM was reviewed and considered for approval by VTA management. The 5.4% indicated in the audit observations relates only to the HMM personnel. When evaluated across both Bechtel and HMM, the aggregate rate increase is significantly lower, being within one-half of one percent of the contract allowance.

In all cases, exceptions are evaluated and approved using managerial discretion when rate adjustments are determined to be in VTA's best interest. However, it is agreed that the rationale supporting VTA approval of the rate changes could have been more specifically documented.

The Contracts Department will update its procedures manual to help ensure that as part of the amendment process, documentation is included in the contract file memorializing the approval by both Project Management and Contracts Management regarding all rate escalations, including the exceptions. These changes will be implemented by June 2011.

4. Work Directives

An analysis of the Work Directives (“WD”) and associated reporting and budgeting requirements was conducted to assess compliance with the Contract. The WD methodology and the process for managing SVRT deliverables were revised last year, based on Auditor General recommendations intended to improve soft cost management. Although additional enhancements are suggested below, the new WD methodology has improved the effectiveness of soft cost management. The Work Directive methodology is a new process that has been put into place, and although there are several opportunities for improvement noted below, it has been beneficial to the project team.

We observed the following with respect to the monthly reports and budgets:

a. Monthly Report

- i. Invoice Amounts – Of the three WD monthly reports sampled, there were two instances noted where there was a discrepancy between invoice amounts and the WD monthly reports of costs incurred to date. In discussions with the SVRT Project team, we were informed that this is because, the WD monthly report includes an estimate of costs incurred as it is used as a tool to make decisions about needed work, not to report actual cost information.
- ii. Progress Descriptions – We evaluated the WD Monthly Reports for December 2009, January 2010 and May 2010, which were required to be in compliance with P0501-D300-INS-CONT-001, “Work Directive Process and Format” and P0501-D300-PRO-PC-330, “Work Directives Monthly Progress Reporting.”, We noted that descriptive reporting in December 2009 and January 2010 included substantially less descriptive detail than specified in the requirements noted above.

Recommendation:

Management should consider making it clear that the costs reported in the WD Monthly Report are not actual costs but an estimate or forecast of that month’s costs to complete the described activities. In addition, Management should verify that the descriptions of progress for each month should meet the WD requirements and are sufficient to understand the prior month’s work in order to make any necessary adjustments in work activities or staffing.

Risk Rating: Low

Management Response:

VTA concurs. The regular reporting for Work Directives will be adjusted to clarify the forecast versus actual statements of cost information. Also, monthly progress descriptions will be reviewed and modified as necessary to help ensure sufficient levels of detail and clarity. Both of these changes will be implemented by March 2011.

- b. **Budgets** – Out of the seven completed WDs that were evaluated, we noted that in one instance (WD-103), the final value was above the approved value. The WD was authorized for \$3,196,000, but the final spend was \$3,272,446, an addition of \$76,446 at the time of closeout. The other completed WDs we tested were closed out below approved values.

Recommendation:

Management should consider implementing strategies to keep expenditures within the estimated amounts stated in the Word Directive. Management should also consider developing a requirement for exceptions, which would describe the need to include appropriate documentation of approval within the WD amendment or close-out documentation.

Risk Rating: Low

Management Response:

VTA concurs. It should be noted that Work Directives are management tools operating within explicit contract Task Order limitations, and are used to evaluate progress and overall costs as the work progresses. Although there are no explicit Contract requirements that prohibit Word Directives from being exceeded, Management will investigate potential strategies to keep expenditures within the estimated amounts stated in the Work Directive. Also, current procedures will be modified so that necessary exceptions are documented in the WD amendment or close-out documentation. Both these recommendations will be completed by March 2011.

5. Deliverables

An analysis of the deliverables associated with the original Contract, as well as individual Work Directives, was conducted to verify compliance with the scope of deliverables specified within the Contract. We observed the following with respect to Contract deliverables, WD deliverables and deliverable roadmaps:

- a. **Contract Deliverables** – All deliverables tested were located. Several deliverables were in “Draft” or “In Progress” status as the SVRT Project team was in the process of preparing various types of documentation for submittal and subsequent acceptance into the FTA New Starts Final Design phase.
- b. **Work Directive Deliverables** – Deliverables for each of the WDs were not always clearly delineated in the WD forms, which include a “Deliverables” section. In particular, we noted that WD108-111 did not specify deliverables within the “Deliverables” section, although the WD descriptions suggested specific reporting requirements. Additionally, we tested six deliverables as required in WD106 and confirmed the existence of each of the six deliverables.
- c. **Deliverable Roadmap** – The SVRT project team has developed an informal Deliverables Roadmap or matrix of the documentation that is being prepared to be submitted to the FTA in order to apply for approval to enter into FTA “New Starts Final Design” phase. This Roadmap is being used by the SVRT Project team to track the deliverables that need to be submitted to FTA.

Recommendation:

Management should consider requiring additional detail within the WDs to establish clear deliverables for each WD. Although several of the WDs evaluated are considered “Level of

Effort” project components, there are certain written deliverables associated with this “Level of Effort” work that could be specified and tracked by VTA management. In addition, Management should consider formally using some type of roadmap or matrix to track all of the major deliverables that are prepared as part of the HMM / Bechtel contract to allow for transparency as well as a paper trail for the work that is being completed by the consultant team.

Risk Rating: Low

Management Response:

VTA concurs. Management will adjust the work directive process to incorporate close-out and reconciliation documentation of actual costs and the completion of work. This will be completed by June 2011.

6. SVRT Program/Project Roles and Responsibilities

An analysis of the SVRT Program organizational charts was conducted to understand the roles, responsibilities and lines of authority and reporting that occurs between VTA and the HMM / Bechtel Contract team. We observed the following with respect to an open Project Director Position for the SVRT Berryessa Extension Project:

- a. **Open SVRT Berryessa Extension Project Director Position** – There is currently an open SVRT Berryessa Extension Project Director position. At present, the Deputy Director SVRT Program has been filling the open position as the SVRT Berryessa Extension Project “Acting” Project Director. As a result, he has been working in two roles. Based on discussions with VTA Management, a Project Director is anticipated to be placed in the open position in the near future. VTA Management is currently considering filling the Project Director position with an employee under the existing Contract.

Recommendation:

Management should consider filling the open Project Director Position for the SVRT Berryessa Extension Project as soon as possible. If the Open Position is filled by an employee under the existing Contract, VTA Management should structure the project administration process such that any adjustments to the Contract or scope of work are subject to review or approval by a VTA management employee at the same level or above the contract employee within the organizational structure.

Risk Rating: Low

Management Response:

VTA concurs. This position was filled effective September 7, 2010.

7. Subconsultants

An analysis of the administrative requirements associated with the subcontractors utilized by HMM / Bechtel was performed to assess compliance with the Contract. As the Project moves further into the design and construction phases, and additional subconsultants are used, the importance of administrative management of subconsultants should continue to be emphasized.

We observed the following with respect to approved subconsultants and debarment and suspension:

- a. **List of Approved Subconsultants** – Within the eight invoices tested, we noted three instances where the subconsultants included within the invoices were not included in the list of subconsultants specified in the Contract or current amendment at the time of the invoice.
- b. **Debarment and Suspension**
 - i. We randomly selected 10 subconsultants and checked company names against the national prohibited vendor database. No exceptions were noted.
 - ii. We requested certification of debarment and suspension of subconsultants from HMM / Bechtel, per Contract requirements. Although no debarred or suspended vendors were observed, certifications were not kept on file by HMM / Bechtel.

Recommendation:

Management should consider establishing a formal process for tracking status of suspension / debarment certifications. Additionally, Management should consider performing periodic evaluations of subconsultants billed to invoices against the approved subconsultant list, to help ensure Contract compliance.

Risk Rating: Medium

Management Response:

VTA concurs. VTA will consider enhancing contract language that defines the responsibility of the Prime as it relates to suspension/debarment certification. Management will also assess the best method to ensure contract compliance. Both of these efforts will be completed by June 2011.

8. Certificates of Insurance

An analysis of the insurance requirements of the Contract and associated documentation was performed to assess compliance of HMM / Bechtel and their subconsultants. As the Project moves further into the design and construction phases, the importance of compliance with insurance requirements should continue to be emphasized. We noted the following with respect to HMM / Bechtel insurance and subconsultant insurance:

- a. **HMM / Bechtel Insurance** – We observed evidence of insurance required by Contract for HMM / Bechtel. However, we did not observe a process to retain the necessary documentation that describes the insurance coverage of the prime consultant.
- b. **Subconsultant Insurance** – We sampled 17 subconsultants to assess proof of insurance. Several instances were noted where coverage was below the amount required by Contract. Additionally, the proof of insurance observed did not include all insurance types. We did not observe an organized filing system for tracking the necessary documentation to support the insurance requirements of the subconsultants.

Recommendation:

Management should consider establishing a policy to perform periodic evaluations of insurance for prime consultants as well as subconsultants. Furthermore, Management should consider using a tracking sheet, matrix and filing process to track compliance requirements and certificates for various insurance types for the prime and subconsultants. Additionally Management should consider establishing a process for approval of exceptions to the insurance requirements for subconsultants as well as a tracking sheet or matrix to track compliance requirements for various insurance types for subconsultants that the prime consultant could develop and maintain on a periodic basis. VTA Management and HMM / Bechtel should work closely together to develop specific roles and responsibilities for tracking of documentation, and approval of exceptions.

Risk Rating: Medium

Management Response:

VTA will review the current process of tracking the receipt of insurance certificates for prime consultants and ensure that continuing insurance coverage is reported. This effort will be completed by December 31, 2010. VTA's contractual relationship is with the prime contractor and the insurance clause in the contract requires them to carry adequate coverage for all contingencies including subcontractor contingencies.



Date: October 19, 2010
Current Meeting: November 4, 2010
Board Meeting: N/A

BOARD MEMORANDUM

TO: Santa Clara Valley Transportation Authority
Audit Committee

THROUGH: General Manager, Michael T. Burns

FROM: Auditor General, Greg Thomas

SUBJECT: Review Status of Internal Audit Work Plan

FOR INFORMATION ONLY

VTA's Auditor General is responsible for developing and recommending the Annual Internal Audit Plan, assigning and managing the audit resources required to conduct each internal audit, and providing audit results and progress reports to the Audit Committee.

To keep the members informed, staff from Deloitte & Touche, LLP, the independent auditing firm providing Auditor General services to VTA, will provide reports at each Audit Committee meeting on the current status of the internal audit work plan and its component audits.

Prepared By: Greg Thomas, Auditor General
Memo No. 1896



Santa Clara Valley Transportation Authority

Audit Committee Meeting, Item No. 9

FY2011 Internal Audit Work Plan

November 4, 2010

Auditor General's Office

Greg Thomas, Principal

Farah Faruqui, Partner

Denise Martini, Director

Sandra Koning, Manager

Internal Audit Plan for FY2011

Audit Project	Description	Timing *	Type of Audit	Risk Area
SVRT Contract Compliance <i>(completed)</i>	Conduct an assessment of the contract between Hatch-Mott MacDonald/Bechtel and VTA; evaluate how the contracts are organized and if there are clear deliverables and milestones enforced.	Q2 FY2011	Compliance Audit/ Value-Add Audit	SVRT
Investment Control Design Assessment	Evaluate the existing Investment controls by performing a design assessment on the adequacy and appropriateness of management's key controls.	Q3 FY2011	Annual Compliance Requirement	Fiscal Controls
IT Security <i>(deferred from prior year)</i>	Assess the security of the VTA network and external facing applications.	Q4 FY2011	IT Audit	Network
Follow Up Assessment	Evaluate and assess VTA management's progress on implementing management responses to audit observations.	Varies	Follow Up	N/A

* Q = quarter, a three-month period of the fiscal year. Q1 is July – September, Q2 is October – December, Q3 is January – March, and Q4 is April – June.

Revised Timeline & Reporting of Internal Audit (IA) Activities

Internal Audit Project	FY2010					FY2011											
	Feb	Mar	Apr	May	Jun	July	Aug	Sept	Oct	Nov	Dec	Jan	Feb	Mar	Apr	May	Jun
FY11 Internal Audit Plan Refresh		completed →			AC mtg												
SAP Segregation of Duties (SOD)				completed →				AC mtg									
IT Security													→			AC mtg *	
SVRT Contract Compliance							completed →			AC mtg							
Investment Control Design Assessment										→			AC mtg *				
FY12 Internal Audit Plan Refresh													→			AC mtg *	

■ Completed
 ■ Planned
 ■ Rescheduled

* Reflects proposed 2011 Audit Committee meeting schedule.

This report is intended solely for the information and use of management and the Audit Committee of the Santa Clara Valley Transportation Authority and is not intended to be used by anyone other than these specified parties.