

SUBJECT: Requirements for audits of state agencies and contracts

COMMITTEE: State Affairs — committee substitute recommended

VOTE: 5 ayes — Swinford, Miller, Gattis, B. Cook, Farrar

0 nays

4 absent — J. Keffer, Martinez Fischer, Villarreal, Wong

WITNESSES: None

BACKGROUND: In order for a state agency, or corporation dedicated to the benefit of a state agency, to employ a private auditor, the agency or corporation must:

- be authorized to do so by law or through a delegation of authority from the state auditor;
- submit the scope of the proposed audit to the state auditor for review and comment; and
- procure the services of the private auditor through a competitive selection process.

Government Code, ch. 2262 relates to contract management. Sec. 2262.003 requires state agencies to include in each of their contracts a provision that the state auditor may conduct an audit or investigation of any contractor or subcontractor receiving state funds. Acceptance of state funds under the contract acts as acceptance of the state auditor's authority. The chapter does not apply to public institutions of higher education nor to contracts of the Texas Department of Transportation (TxDOT) that relate to highway construction or engineering.

DIGEST: CSHB 905 would require a state agency or corporation to have a delegation of authority from the state auditor in order to contract with a private auditor.

The bill would require state contracts to include a provision that an entity that was audited or investigated by the state auditor would have to provide the auditor with access to any information the auditor deemed necessary to

evaluate the entity's performance under the contract or subcontract, determine the state's rights or remedies under the contract or evaluate whether the entity had acted in the best interest of the state. This provision, and current audit provisions in Government Code, sec. 2262.003, would apply to institutions of higher education and TxDOT.

The bill would take immediate effect if finally passed by a two-thirds record vote of the membership of each house. Otherwise, it would take effect September 1, 2005, and would apply only to a contract entered into, amended, extended, or renewed on or after that date.

**SUPPORTERS
SAY:**

CSHB 905 would clarify that all state agencies must have the approval of the State Auditor's Office prior to hiring a private auditor. Under current law, an agency that plans to use a private auditor must submit the scope of the proposed audit to the state auditor for review and comment - a requirement that would be meaningless unless the state auditor had the authority to withhold approval of the audit. Yet despite this requirement to obtain state auditor approval, many agencies have undertaken audits with private auditors, including contract management audits, without first receiving this approval. In some cases, poor contract management has cost the state millions of dollars.

Clarifying that all agencies first must receive the permission of the State Auditor's Office would improve the integrity of the process used to procure external audits, improve management of the state's audit resources, facilitate coordination of audits, and lessen the impact of multiple audits on state agencies. Ensuring that the State Auditor's Office had a complete picture of audits being performed on state agencies and their contractors also would enable the state auditor to require private auditors to provide access to their working papers, if deemed necessary, and ensure that the audit was conducted properly and met the needs of the state.

Similarly, requiring entities audited or investigated by the state auditor to provide the auditor with access to any information the auditor deemed necessary would ensure that the state auditor had all the information necessary to determine whether a vendor had acted in the state's best interest. Although this authority already is implicit, recent developments in other states indicate that it is necessary to make this authority explicit. Some states have encountered problems in which vendors with financial arrangements with certain manufacturers influenced state purchasing

decisions to the detriment of the state. These vendors then claimed that these financial arrangements were proprietary information that could not be disclosed without harming their competitiveness. Giving explicit authority to the state auditor to access all necessary information would protect the state from these situations and possible litigation.

The bill would not compromise businesses' proprietary information because the State Auditor's Office has strict procedures for conducting audits and safeguarding working papers. Audit working papers are exempt from open records requirements under state statute, and anyone who violates the open records act and releases proprietary information is subject to criminal penalties. Moreover, the bill would not change the state auditor's access to information because this authority is granted implicitly under current law.

The bill would extend provisions in current statute on the state auditor's authority to conduct audits of contractors to institutions of higher education and TxDOT because it is essential to ensure good contract management at these entities, which deal with large amounts of taxpayer dollars.

**OPPONENTS
SAY:**

The broad language in the bill could give the state auditor carte blanche to rifle through the files of a company that worked with the state. Audits ought to be tied to more specific, empirical concerns and the documents or information necessary to investigate those concerns. Giving the state auditor total access to a company's files could result in the disclosure of proprietary information that then could damage the company's competitive position. The bill should include provisions to ensure that this sensitive information was protected properly.

CSHB 905 could make the process of hiring a private auditor less efficient by adding an additional layer of approval and bureaucracy. State agencies that have delegated authority to hire private auditors are capable of determining what their audit needs are.

NOTES:

The committee substitute added the requirement that a state agency or corporation have received delegated authority from the state auditor in order to employ a private auditor. The substitute also specifies that the

provisions of the bill would apply only to a contract that was entered into, amended, extended, or renewed on or after the bill's effective date.