Annual Audit Plan Report
Fiscal Year 2022

Prepared By:

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Chief Audit Officer

Approved By:

Port Commission, and
Audit Committee of the Port Commission

To: Port Commission of the Port of Houston Authority, and
              Audit Committee of the Port Commission

Date: October 25, 2021

Subject: Annual Audit Plan Report – Fiscal Year 2022

Dear Commissioners:

I am pleased to submit to you the Fiscal Year 2022 Audit Plan Report. The basis of this year's Annual Audit Plan ("Audit Plan") was an Annual Risk Assessment ("ARA") performed by the Internal Audit Department as required by the applicable professional auditing standards (the ARA report is submitted under separately). Additional consideration is given to input from the Audit Committee, Executive Director, Chief Officers, and department directors. This document serves as a key reference and guide to perform the audit responsibilities in an efficient and effective manner. To enhance our effectiveness, our approach is balanced by conducting the audits using in-house staff, and where appropriate, by outsourcing some projects requiring certain technical or specialized skills.

This Audit Plan includes performance, compliance/contract, policies and procedures compliance consultative reviews and unannounced audits. The plan also provides for follow-up procedures and special projects. Data analytics and continuous auditing techniques are utilized where practical.

Updates will be provided to the Audit Committee of the Port Commission at least twice a year to review the status and progress of executing the Audit Plan and to discuss other pertinent audit issues.

Respectfully submitted,

/s/ Maxine N. Buckles
Chief Audit Officer

cc: R. Guenther, Executive Director
        T. Heidt, Chief Operating Officer
        T. Finley, Chief Financial Officer

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BACKGROUND AND AUTHORITY

The Internal Audit Department ("IAD") provides independent, objective assurance and consulting services designed to add value and improve the operations of the Port of Houston Authority ("Port Authority"). Attribute Standard 1000 of the International Standards for the Professional Practice of Internal Auditing as issued by the Institute of Internal Auditors ("IIA") requires that the IAD *"… be responsible and accountable for the Internal Audit function using a systematic, disciplined approach to evaluate and improve the effectiveness of governance, risk management and controls processes, and incorporate a Code of ethics of the IIA by adopting an Internal Audit Charter"*. Audit results are issued, to the Audit Committee of the Port Commission ("Audit Committee") and Port Authority Management.

AUDIT DEPARTMENT ORGANIZATION

The Internal Audit function is overseen by the Audit Committee of the Port Commission, as required by statute. In September 2021, IAD was reorganized to administratively report to the Chief Financial Officer, a change from the previous role held by the Executive Director.

During FY2021, the IAD had a total headcount of 5, consisting of one Chief Audit Officer, two audit managers, one internal auditor, and an administrative assistant. No headcount increases are planned for fiscal year 2022. However, the IAD will engage, as appropriate, certain third-party resources to conduct specialized auditing and supplement internal resources. As we receive additional training, certifications, and experience, we will continue to increase our ability to provide enhanced and value-added services.

APPROACH AND METHODOLOGY

The IAD adheres to: 1) the International Standards for the Professional Practice of Internal Auditing as issued by the Institute of Internal Auditors (IIA – known as the "Red Book"), and 2) the Government Auditing Standards ("GAS" – commonly referred to as the "Yellow Book") as promulgated by the Government Accountability Office ("GAO"). To assure compliance with these professional standards, the IAD is required to undergo a peer review every 5 years, the first of which was completed during FY2018.

The Annual Audit Plan is a flexible commitment to perform engagements in accordance with the responsibility and authority noted in the Port of Houston Authority Internal Audit Charter. The Audit Plan, which is approved by the Audit Committee, serves as a working document that considers items such as the Annual Risk Assessment ("ARA"), input from the Audit Committee, Department Management, and results from previous audits where applicable. Due to the continual requests for audit services, the increasing demand for non-audit services, and the required testing for planned activities, the Audit Plan will be monitored and revised as necessary throughout the year.

The professional standards noted previously require that the Audit Plan be rooted in risk-based methodology. In FY 2021, the IAD updated the ARA and utilized an electronic risk assessment tool to gather annual updates to departmental risks and controls. This process should provide for incorporation of ongoing changes to the risks and controls database.

Evaluating the various factors provides the IAD with indicators for project prioritization and scope. We then identify the available resources to determine the volume of activity to include in our plan (see Audit Resource Allocation section below).

AUDIT RESOURCE ALLOCATION

The Audit Plan prioritizes the IAD's limited staffing resources and budgeted funds based on the previously referenced risk assessment supplemented by management input. Auditable areas with higher risk profile ratings, management concerns, and regulatory requirements will be prioritized during the year.

The number of planned projects is based on consideration and an evaluation of:
- Current IAD headcount
- The existence or absence of established procedures (written and/or informal)
- Engagement manpower requirements
- Other types of ongoing audits, analyses and reviews performed by other Port Authority areas
- Unplanned requests from the Audit Committee, Executive Director, Chief Financial Officer, or Port Authority Management

USE OF EXTERNAL CONSULTANTS

For projects that involve circumstances where: 1) the use of experts/specialists is required; 2) the independence of the Internal Audit Department as an organization is impaired; or 3) there is the potential for significant political sensitivity, the Chief Audit Officer may elect to use external consultants. NOTE: An estimated amount is included in the annual budget for the use of these types of resources.

AUDIT PROGRAMS

Following the Audit Committee's recommendation and the Port Commission's approval of the Audit Plan, specific audit programs will be developed for each audit activity for fiscal year ending December 31, 2022. The audit programs will be designed with consideration of business processes, compliance and other requirements, performance considerations, management input, and specialized skills in order to meet the specific audit objectives of each project. Audit programs, workpapers and reports will be prepared in accordance with:

- The Institute of Internal Auditor's International Standards for the Practice of Internal Auditing ("Red Book")
- Government Auditing Standards ("Yellow Book")
- Relevant standards issued by the American Institute of Certified Public Accountants

STATUS AND UPDATES TO THE ANNUAL AUDIT PLAN

The specific projects conducted throughout the year will support the guidance provided in the Audit Plan. The nature, extent and timing of audit activities may vary as a result of changes in operations, organizational structure, competing resource priorities and management needs.

The IAD will also provide any assistance to the Audit Committee, Executive Director, and Chief Financial Officer with special projects when requested (assuming the available resources exist and depending on the context and priority of the assignment as it relates to risk, exposure, fraud, waste and/or abuse). These special projects will normally be performed in addition to planned audit work. If the assistance requires the use of external consultants, additional funds may need to be provided by the appropriate departments and/or the Audit Committee. Executing the Audit Plan involves an update and status process that is performed regularly among the IAD, management and the Audit Committee.

ANTICIPATED BENEFITS OF AUDIT ACTIVITIES
- Compliance
- Improved Accountability
- Improved Risk Management and Internal Controls
- Improved Financial and Operational Reporting
- Improved Efficiency
- Cost Savings

FISCAL YEAR 2022 PLANNED ACTIVITIES (FOCUS AREAS)

The following summaries highlight areas of probable projects for the FY 2022 Annual Audit Plan which is subject to modification based on the needs of the organization. The audit process, while often tracked in a linear fashion, is truly dynamic and reacts to evidence, impact, and magnitude of discovery occurring during the entire engagement process. As such, the following project areas are considered a starting point from which to execute the Audit Plan and will provide a level of transparency and accountability for meeting goals and objectives.

COMPLIANCE AND/OR CONTRACT AUDITS

A compliance audit is a comprehensive review of an organization's adherence to regulatory guidelines. Independent accounting, security or IT consultants evaluate the strength and thoroughness of compliance preparations. Auditors may review polices, user access controls and risk management procedures over the course of a compliance audit. Planned audit areas include:

COMPLIANCE - CONSTRUCTION

DESCRIPTION: For the calendar years 2019 and 2020 the Port Authority has invested approximately $ 115.6 million and $ 228.9 million, respectively, in construction projects. Expenditures in this category represented approximately 99% of net cash used in capital financing activities during both calendar years 2019 and 2020. During 2021 a major ship channel expansion project was launched. As of September 30, 2021, the Port Authority expended approximately $124 million on construction projects. IAD will review, these expenditures, on a test basis, for compliance with the Port Authority's agreements and established policies and procedures.

COMPLIANCE - U.S. FOREIGN TRADE ZONE ("FTZ")

DESCRIPTION: FTZs are designated areas where the U.S. government considers foreign merchandise trade outside U.S. Customs territory. Merchandise may be transported into an FTZ without formal customs entry, import quotas and other import restrictions. Duties and excise taxes are not assessed until the merchandise enters U.S. commerce. Currently the Port Authority manages FTZ #84, which includes many privately owned and port-owned sites located throughout Houston and Harris County, Texas. For the calendar years 2019 and 2020, the Port Authority collected FTZ related revenues totaling $452 thousand and $551 thousand, respectively. As of September 30, 2021, the Port Authority has billed $ 370 thousand in FTZ related revenues. The IAD will review compliance with the U.S. Department of Commerce requirements for managing an FTZ.

COMPLIANCE- OFFICE OF FOREIGN ASSETS CONTROL ("OFAC")

DESCRIPTION: The Port Authority periodically hosts non-US delegations (or visitors) and participates in industry developmental activities with non-US entities. Foreign participants are screened via the Department of Treasury's Specially Designated Nationals ("SDN") list review prior to visiting the Authority's facilities. The IAD will review the OFAC process and procedures and will audit compliance with the requirements of the OFAC policy.

COMPLIANCE - CONTRACTS OTHER THAN CONSTRUCTION

DESCRIPTION: The Port Authority routinely engages third parties to perform a variety of services. As this area has not received a recent detailed process review or audit, IAD will review, these expenditures, on a test basis, for compliance with the Port Authority's agreements and established procedures.

COMPLIANCE - OTHER POSTEMPLOYMENT BENEFITS ("OPEB") TRUST

DESCRIPTION: In addition to retirement benefits, the Port Authority provides certain post-employment health and welfare benefits ("OPEB") to eligible retired employees and their dependents. In February 2015, the Port Authority established a new, stand-alone trust for the OPEB Plan with Compass Bank as trustee. In July 2015, the Commission approved a revised funding policy. On December 31, 2019 and 2020, there were 319 retirees who were eligible for these benefits. For the calendar years 2019 and 2020, the Port Authority assets held in

trust for OPEB were approximately $82.3 million and $95.1 million, respectively. IAD will review OPEB activities for compliance with applicable policies and procedures.

COMPLIANCE – ENVIRONMENTAL INTERNATIONAL STANDARDS ORGANZIATION ("ISO") 14001

DESCRIPTION: The Port Authority is ISO 14001 certified which requires external periodic audits to verify continued conformance with the ISO 14001 standards. Currently, Det Norske Veritas ("DNV GL") is the external audit firm engaged by the Port Authority to perform the 2022 ISO 14001 compliance audit. IAD will partner with the Environmental Affairs Department and DNV GL to support the recertification process through both internal and external reviews and audits.

COMPLIANCE- INVESTMENTS

DESCRIPTION: The Port Authority made investments in the Local Government Investment Cooperative ("LOGIC"), Texas Cooperative Liquid Assets Securities System Trust ("Texas CLASS") and the Texas Local Government Investment Pool ("TexPool Prime"), which are subject to the Texas Public Funds Investment Act, Chapter 2256, Texas Government Code ("PFIA). On December 31, 2019 and 2020, the Authority had invested $310.6 million and $219.6 million, respectively. IAD will review the compliance with the Texas Government Code reporting requirements and the Authority's Investment Policy.

PROCESS REVIEWS

PROCESS REVIEW – OPERATIONS MAINTENANCE

DESCRIPTION: During FY2020, the Port Authority expended approximately $21.7 million in purchases associated with the acquisition of operations maintenance equipment, supplies and services. As of September 30, 2021, the Port Authority has expended approximately $16.3 million in operations maintenance equipment, supplies and services, which included $2.2 million related to Covid-19 response. The Port Authority has maintenance processes that vary by department and location. IAD served in a consultative role in the 2019/2020 Maintenance Operations Controls Consulting Project and will continue to monitor and review the implementation of the process and control improvement recommendations provided.

PROCESS REVIEW – IT PROCUREMENTS

DESCRIPTION: During FY2020, the Port Authority expended approximately $4.9 million in purchases associated with the acquisition of IT-related equipment, supplies and services. As of September 30, 2021, the Port Authority has expended approximately $1.7 million in IT related equipment and supplies. The IAD will review, document and walkthrough several key business processes to evaluate compliance with procurement and other policies and assess tracking and control of high value items within IT Systems.

CYBER SECURITY

DESCRIPTION: Cyber security continues to be identified as a high-risk area for the Port Authority, which is consistent with most organizations. During 2020, the Information Technology Department's ("IT") response to the Covid-19 pandemic included implementation of systems and communications tools to facilitate access for telecommuters and stakeholders attending virtual meetings. These activities highlighted risks associated with a remote workforce and employees utilizing personal devices to connect with Port Authority systems. During 2021, IT, with the support of the Training and Development Department, implemented the fifth year of Cyber Security Awareness Training.   IAD will continue to work in collaboration with the IT and other departments as needed to ensure that the Port Authority mitigates risks in this area.

MAJOR SYSTEM APPLICATIONS REVIEWS/MONITORING

DESCRIPTION: IAD will review IT governance processes and perform user access reviews of the Port Authority's major system applications. Monitoring includes procedures to assess the effectiveness of IT internal

controls, adequacy of segregation of duties, system access and user access is appropriate for employees and compatible with assigned job duties. Application performance accuracy testing and any other procedure considered necessary to improve efficiency of the Port Authority's system applications may also be performed

SAP CONCUR

DESCRIPTION: In April 2021, the Accounts Payable department deployed SAP Concur, an automated expense management software system. This system improves various payables functions such as electronically capturing invoice and receipt details, streamlining the payment process to vendors and employees, and enhances and simplifies the reporting process. IAD will review the post implementation process, adequacy of segregation of duties, and user access to validate that SAP Concur control processes are operating effectively.

PROCESS REVIEW – GENERAL CARGO REVENUES

DESCRIPTION: During FY 2020, the Port Authority generated $ 54.8 million in revenue associated with general cargo at its terminals, which is approximately 15.1% of total operating revenue. As of August 31, 2021, the Port Authority Turning Basin Terminals general cargo revenues were approximately $39.3 million, or 14% of total operating revenues. A significant number of these transactions rely on manual processes. IAD will review a selection of general cargo customers to identify key business processes, confirm/verify reported volumes, test for approvals, billing, payment, and contract compliance (focus on "major customers" and "high risk customers").

SPECIAL PROJECTS & ON-GOING MONITORING

SAFETY AND SECURITY

DESCRIPTION: The Port Authority owns and operates public facilities in the Houston Ship Channel region. The safety and security of Port Authority people and assets is an important mission for the Port Authority. Port police, fire and safety personnel continually execute strict processes and procedures in compliance with a facility security plan ("FSP") filed with the US Coast Guard ("USCG") to mitigate these risks, including engagement of 24-hour security details provided by Allied Universal. Several external audits conducted by the USCG, US Customs and Border Protection and professional consultants, as well as internal audits lead by Port Authority facility security officers are performed to ensure compliance with the FSP. The IAD receives routine updates related to safety and security audit activities, and will work in collaboration with safety, security and other departments as needed to ensure that the Port Authority mitigates risks in this area.

RISK MANAGEMENT

DESCRIPTION: Risk management continues to be an area of focus for the Port Authority. Periodically, the Risk Management department engages with external resources to review and evaluate the claims handling practices of the Port Authority's third-party administrator. In addition, an annual insurance coverage audit is planned to assist with identifying potential gaps in insurance coverage. It is anticipated that these or similar efforts will be utilized to optimize costs while mitigating risks to the Port Authority. IAD will continue to work in collaboration with Risk Management as needed.

ANNUAL RISK ASSESSMENT ("ARA")

DESCRIPTION: Each year the IAD develops the Audit Plan based upon risks (primarily business, financial and operational). Professional auditing standards (IIA and GAS) require that audit resources be allocated to projects supported by a continuous risk assessment methodology. Risk assessments will be performed as needed on a recurring basis to ensure a systematic review of risks and potential risks to the Port Authority.

REGULATORY COMPLIANCE

DESCRIPTION: The Port Authority is subject to several regulatory requirements. The Legal department monitors the multitude of regulatory requirements to which the Port Authority must comply. IAD will continue to work in collaboration with Legal as needed to ensure potential compliance gaps are identified and appropriately

addressed.

FOLLOW-UP PROCEDURES

DESCRIPTION: As issues are identified while conducting audits/engagements, they are documented and reported accordingly. To help initiate change and continued improvement, our follow-up procedures will effectively monitor progress on implementation of management responses to our recommendations. IAD will communicate with responsible management at regular intervals to monitor progress on implementation of corrective actions. These communications will be documented and published accordingly. Additionally, a sample of items will be tested on a periodic basis, depending on the magnitude, impact, and estimated cost-benefit.

QUALITY ASSURANCE PROCEDURES

DESCRIPTION: Professional standards require that the audit function have a system of quality control/assurance in place to ensure all necessary elements are in place and operating effectively. Each audit is reviewed by a professional staff member not directly assigned to the audit. The goal is to verify that sufficient, appropriate evidence is gathered and documented to adequately support conclusions based on procedures that are designed to test relevant audit objectives (this includes consideration of fraud, professional judgment, competency, and supervision).

FRAUD HOTLINE/REPORTING

DESCRIPTION: The IAD provides two primary vehicles for reporting fraud, waste and/or abuse: (1) A Fraud Hotline answered by EthicsPoint, a subsidiary of Navex Global, a third-party hired by the Authority to independently gather and report fraud and/or misconduct to the IAD and (2) links to report fraud available from both the Port Authority SharePoint Homepage and EthicsPoint website. The IAD also provides auditing support based on requests from the Port Security and/or other authorities. Each reported concern must be addressed. This may require performing substantive procedures, such as an audit, or may be referred to an outside agency or department for follow-up. The initial contact, work performed, conclusions and/or referral are documented to support disposition of the reported issues. In some instances, this may also require subsequent follow-up or monitoring to adequately resolve.

DATA ANALYTICS & CONTINUOUS MONITORING

MONITORING REVIEW – Promotion & Development ("P&D") Fund

DESCRIPTION: During FY2020, the Port Authority disbursed approximately $3.6 million, or 0.9% of gross operating revenues, on P&D activities. As of August 31, 2021, the Port Authority incurred approximately $2.5 million, or 0.8% of gross operating revenues, in P&D activities. The IAD will monitor the authority's compliance with statutory requirements governing use of the P&D fund, pursuant to Section 5007.219(a), Texas Special District Laws Code.

DATA ANALYTICS

DESCRIPTION: IAD utilizes data analytics to gain a better understanding of monetary, transactional, and other numerical data and compares that data to internal and/or external criteria to assess reasonableness. Professional and industry tools and techniques are applied to support a systematic and standard approach for data reliability and consistency. Data analytics are included in audit and review reports, where practical, to communicate results.

BEST PRACTICES

DESCRIPTION: The IAD maintains awareness of significant Port Authority transactions and events as well as significant events which occur external to the Port Authority. This is accomplished by attending professional conferences and seminars, internal meetings and by participating in various roundtable events. Financial transactions are periodically reviewed to detect anomalies. Special monitoring reviews or audits may be generated as a result of these activities.

UNANNOUNCED AUDITS

DESCRIPTION: The IAD may perform audits on an unannounced basis during the year. These may include:
- Payroll
- Purchase Orders
- Charge Card Purchases
- Petty Cash