December 28, 2021

David S. Kim, Secretary
California State Transportation Agency
915 Capitol Mall, Suite 350-B
Sacramento, CA 95814

Dear Secretary David S. Kim,

In accordance with the State Leadership Accountability Act (Leadership Accountability), the High-Speed Rail Authority submits this report on the review of our internal control and monitoring systems for the biennial period ending December 31, 2021.

Should you have any questions please contact Pam Mizukami, Chief Deputy Director, at (916) 324-1541, pam.mizukami@hsr.ca.gov.

GOVERNANCE

Mission and Strategic Plan

Mission: To construct or build an electrified high-speed rail system that utilizes an alignment and technology capable of speeds of 200mph or greater, connecting California's diverse communities and improving mobility across the state.

Vision: Deliver a transformative high-speed rail system by building an organization that demonstrates leadership, collaboration, diversity, and strong stewardship of public funds.

Goals: To achieve our mission, the High-Speed Rail Authority's (Authority) strategic and workforce plans include specific goals and performance measures to track progress for each of the following areas:

- Safety: Ensure the safety and security of our construction workers, employees, and future customers/riders.
- Stewardship: Protection and conservation of public and environmental resources dedicated to California's High-Speed Rail project.
- Performance: Use of specific performance measures to track progress and support the development of a culture of progress and accountability.
- Transparency and Engagement: Publicizing plans, reports, etc. while also fostering two-way dialogue with stakeholders to provide information about program achievements, milestones, and challenges and seek meaningful feedback to enhance outreach and project delivery efforts.
- Diversity: Enhance and prioritize outreach and hiring practices that support a diverse workforce and development of a project that's representative of the State of California.
- Sustainability: Deliver a sustainable high-speed rail system for California that maximizes benefits to communities, protects resources and serves as a model for sustainable rail infrastructure.

Control Environment

Within the Authority, decisions are made through the governance process, which includes:

- Applying relevant statutes and regulations;
- Defined organizational roles and responsibilities;
- Individuals knowing and understanding their corresponding duties and authorities;
- Complementary internal processes and policies; and
- Employing comprehensive program and project leadership and management.

This effective governance structure achieves:

- The accomplishment of the Authority's mission and achieving its vision;
- Stewardship of public resources to create added value, and reduce cost and associated risk;
- Elimination of organizational and functional redundancy;
- Accountability by empowering individual and organizational entities; and
- Broad-based internal and external stakeholder engagement and communication.

Within the administrative jurisdiction of the California State Transportation Agency, the Authority operates with some policy and programmatic independence. The Authority is governed by an 11-member board appointed by the governor and the leaders of the Legislature.

To further guide the Authority in building and maintaining an effective control environment, the Authority's Chief Deputy Director approved a standard code of conduct policy that helps holds Authority leadership and general staff accountable for establishing an ethical climate in their work unit, by developing and adhering to internal controls and procedures. Subsequent policies and manuals have been developed to expand the applicability of the Authority's code of conduct.

Board of Directors

The Board of Directors (Board) was established in 2003 by California Public Utilities Code §185020 and is comprised of nine voting members and two non-voting ex-officio members. The Board oversees the planning, construction, and operation of the nation's first high-speed rail system.

Chief Executive Officer

The Chief Executive Officer (CEO) ensures that the Authority conducts itself in accordance with applicable federal and state laws, regulations, and the policies of the Board. The CEO also ensures the Authority complies with applicable grants. The CEO is accountable for all Authority activities, responsible for communication with the Board, organizing and providing direction to the Authority to accomplish its mission, and delegating authority, as needed, to accomplish the Authority's mission.

Authority Committee Structure

The Authority maintains a structure of six governance committees– the Executive Committee, Program Delivery Committee (PDC), Business Oversight Committee (BOC), Administrative Committee, Change Control Committee (CCC) and Enterprise Risk Committee (ERC). Each committee has its own purpose, organization, roles, and responsibilities as specified in each respective committee charter. These committees enable the Authority to have a strong governance structure with a streamlined system for decision-making and problem-resolution. The PDC, BOC, CCC, ERM and Administrative

Committee report directly to the Executive Committee. The Authority regularly reviews its committee structure and implements changes as necessary to ensure appropriate governance in line with the Authority's current operations.

Executive Committee

The Executive Committee is the senior governance committee. Members of the committee advise the CEO, who chairs the committee, on key agency decisions and recommendations to the Board. The Executive Committee makes executive, enterprise-wide policy decisions, provides overarching Authority strategy and priorities, resolves escalated disputes, and reviews agenda items for upcoming Board meetings.

Administrative Committee

The Administrative Committee provides guidance and oversight of human resources, information technology, communications, employee engagement, administrative functions, and facilities outside of Program Delivery. The Administrative Committee ensures effective and prudent administration and support to the entire Authority.

Business Oversight Committee

The BOC provides programmatic acquisition strategy, procurement governance, and commercial oversight. It acts as the Program Baseline configuration-management control board and approves all changes of scope, timeline, and budget to any program element within the Program Baseline. This committee ensures Program Baseline compliance with federal and state regulations and statutes and approves any program execution or fiscal request prior to presentation to the Board. The BOC escalates issues to the Executive Committee for resolution, as needed.

Program Delivery Committee

The PDC provides governance and oversight of the Authority's programmatic execution and performance. The PDC is accountable for all aspects of program development and delivery in accordance with the Program Baseline, including scope, schedule, and adherence to budget. This committee surveils the program opportunities and risk impacts to the Program Baseline, and advises the Board, the CEO, and the Executive Committee regarding Program execution and performance.

Enterprise Risk Committee (ERC)

The ERC is responsible for the overall oversight of the Enterprise Risk Management (ERM) program, the prioritization of risks, the review of sufficiency for risk responses, and ultimately reporting prioritized-enterprise risks to the Board. The ERC evaluates risks of the Authority and decides which are the highest threats and opportunities to be addressed and provides guidance or direction on taking action to mitigate those risks or take advantage of opportunities. In addition, the ERC reviews management risk responses and determines the sufficiency, adequacy, and completeness of them.

Change Control Committee

The Change Control Committee is responsible to oversee and to further improve the Authority's processing, decision-making, and documentation of Construction Package change orders (COs). The committee helps to ensure the consistency and timely evaluation of COs that are equal to or greater

than $1 million dollars in total value. The CCC will validate merit (based upon contract provisions, risks assessments, cost estimates and schedule analysis), sets Finding of Fact (FOF) and CO documentation standards, reviews FOFs and COs equal to or greater than $1 million for sufficiency and clarity and will make recommendations on approval/disapproval of COs.

Documenting the Control System

The Authority's success is contingent upon a clear understanding and implementation of roles and responsibilities at the organizational and individual levels. The Authority defines roles and responsibilities in the Program Management Plan, Responsibility Matrices, and the duty statements for all Authority staff. The functional organization chart and Concept of Operations describes the Authority's organization and integrates each organizational entity. In addition, each of the six governance committees document their outcomes through published meeting minutes, which are stored and accessible in the Authority's information storage systems.

To monitor overall performance and the adherence towards the Authority's mission and strategic objectives, executive-level management reports monthly are provided to the board of directors to communicate progress, risks, and opportunities to meet the subsequent goals of each office, program, or project. The Authority also regularly coordinates with, and reports to its State and Federal partners, as well as the public to build trust and partnership through transparency and early outreach.

Establishing and Maintaining a Competent Workforce

The Authority has established a Workforce and Succession Plan to maintain a competent workforce. Workforce and succession planning is a deliberate and systematic effort to guarantee leadership continuity at every level of the organization. The Workforce and Succession Plan provides the framework to address workforce gaps and business needs, which allows the Authority to strategically position the right people in the right roles at the right time to support continued successful delivery of the Program. This plan builds upon the Authority's current workforce management practices and identifies initiatives to improve the Authority's workforce management practices, including initiatives to improve the Authority's ability to recruit, hire, compensate, develop, engage, and retain exceptional talent.

Information and Communication

The Chief of Strategic Communications oversees the Authority's Strategic Communications Office which includes media relations, public records act requests, external affairs/stakeholder engagement, and special projects. The main responsibility is to proactively collect and communicate relevant, reliable information- both externally and internally- to inform decisions and enhance program efficiency.

The Media Relations Branch includes publications, daily media interaction, website updates and public records act requests. Social media content creation and amplification of key messages and news clips is managed by the Media Relations section in coordination with the Chief of Strategic Communications. As media inquiries come into the Authority statewide, our staff work with program and policy leads across the organization to ensure proper and accurate messaging is used.

The Strategic Communications team also works with the multimedia section for appropriate graphic and video support for specific projects, media, outreach, and social media efforts. The media section and the Office of Strategic Communications works directly with the Chief Information Officer's staff to update

the website and make necessary communications modifications. The Strategic Communications Office works closely with regional staff and the small business team to support with presentation material, staffing and overall set up for community meetings, working groups, procurement events, and environmental meetings.

The External Affairs team within the office of Strategic Communications is tasked with coordination and dissemination of information to regional, state, and national stakeholders in coordination with regional outreach leads. The External Affairs office in coordination with the Chief of Strategic Communications is also tasked with oversight of the student outreach and engagement effort "I Will Ride."

The Office of Strategic Communications is also tasked with managing numerous areas of internal communication including but not limited to:

- Updating the internal intranet portal "The Terminal." Staff is currently in the process of making necessary updates and ensuring that relevant fact sheets and data are current.
- Coordinating with Regional Directors and key senior staff to ensure that proper talking points and graphics are disseminated for use.
- Spearheading an internal database for organization of speaker's requests so all policy areas are coordinated and approved before speaking publicly to any groups.
- Monthly reports to the Authority from the Administrative Office to provide progress on key program initiatives, as well as internal, HSR initiatives.
- Monthly executive reports to the board of directors, allowing important program/project progress, risks, and opportunities across the Authority to be communicated down executive chains of command to their respective offices, branches, and committees.
- Working with policy staff on preparation for speaking engagements and Board presentations.
- Preparation of materials for the CEO's presentations to the Board of Directors and external partners.

Strategic Communications is also tasked with creation and dissemination of the following digital newsletters: bi-monthly internal newsletters, quarterly construction updates, small business newsletters, regional updates, and I Will Ride student engagement and outreach newsletters. These publications serve as a primary tool for dissemination of information both internally to staff as well as externally to press, stakeholders, the Legislature, and the public.

Finally, the Special Projects Branch responsibilities include drafting of the major reports statutorily required by the Legislature such as the Business Plan, the Project Update Report, and the Sustainability Report.

<u>Establishing Channels for Internal Reporting</u>

Besides having a strong quality management system, which will be discussed in the next section, the Authority has policies and procedures in place for employees to report inefficiencies and inappropriate actions to management (i.e., the standard code of conduct). As it relates to reporting inefficiencies, the Authority has also established a risk management office (RMO) and enterprise risk committee (ERC) to aggregate and report risk information collected through risk workshops, surveys, and other means.

Each functional group within the Authority owns its respective business risks and is responsible for the implementation of the necessary controls and risk response. Each functional group will report on risk

information through the RMO and the RMO will assess the adequacy of the risk assessment, the effectiveness of risk evaluation and response, and the sufficiency of risk reporting and monitoring.

MONITORING

The information included here discusses the entity-wide, continuous process to ensure internal control systems are working as intended. The role of the executive monitoring sponsor includes facilitating and verifying that the High-Speed Rail Authority monitoring practices are implemented and functioning. The responsibilities as the executive monitoring sponsor(s) have been given to:
Pam Mizukami, Chief Deputy Director.

The information included here discusses the entity-wide, continuous process to ensure internal control systems are working as intended. The role of the executive monitoring sponsor includes facilitating and verifying that the Authority's monitoring practices are implemented and functioning. This includes working with management who owns the risks to provide their current controls and ideas for future controls and response planning activities and evaluating if the controls are driving the performance outcomes or results intended. The responsibilities as the executive monitoring sponsor(s) have been given to Jamey Matalka, Director of Risk Management and Project Controls, and the Risk Management Office that he oversees.

It is important to note that management and RMO cannot be successful without a close partnership with Internal Audit. While management is chiefly responsible for developing and monitoring internal controls, RMOs partnership with Internal Audit is key to properly evaluate the effectiveness of internal controls and providing insights that can improve management of risk.

Quality Management System (QMS)

The Authority utilizes a Quality Management System (QMS), following International Organization for Standardization (ISO) quality standards, to ensure requirements and expectations are met in a manner that supports the continuous improvement of Authority processes. The Authority's quality program describes the requirements and process for identifying, documenting, and tracking quality and compliance-related concerns, non-conformances, and corrective action requests. It uses non-conformance reports (NCRs) to document and assign ownership of the non-conformance.

The Quality Management Team also monitors, tracks, and reports the status of these non-conformances through resolution in a centralized tracking system and elevates critical issues through the Authority's governance system. The QMS monitors the effectiveness of the risk management and internal control systems to include how management responds to vulnerabilities. QMS establishes and documents the organizational structure, responsibilities, procedures, processes, and resources needed to meet the Authority's quality policy and objectives described in the Quality Manual. Once the Authority resolves the non-conformance or vulnerability, the Quality Management Team will close the NCR and monitor that area for future non-conformances through annual audits.

The Quality Management Team will utilize periodic meetings within the Authority governance system to ensure that the Authority addresses potential issues, documents outcomes, and communicates this information through published meeting minutes.

RISK ASSESSMENT PROCESS

The following personnel were involved in the High-Speed Rail Authority risk assessment process: executive management, middle management, front line management, and staff.

The following methods were used to identify risks: brainstorming meetings, employee engagement surveys, other/prior risk assessments, external stakeholders, and performance metrics.

The following criteria were used to rank risks: likelihood of occurrence, potential impact to mission/goals/objectives, timing of potential event, and other.

The following personnel were involved in the High-Speed Rail Authority risk assessment process: Leadership and managers from 18 Offices and Branches, key consultants, and Executive management.

The following methods were used to identify risks: Issuance of a standard risk submission template with instructions and risk scoring criteria, brainstorming meetings, and workshops to complete the templates and an Executive workshop to review and validate the results.

The following criteria were used to rank risks: likelihood of occurrence, and potential impact to mission/goals/objectives, velocity of risk onset, and management's preparedness gap.

The Authority's Audit and (RMO) assisted executive management in performing an organization-wide risk assessment. The purpose of this risk assessment was to identify potential issues that might impede the Authority's progress in achieving its goals and mission.

The Audit Office and RMO held brainstorming sessions across the Authority to discuss the risk assessment process, highlight examples of the types of risks to identify and explanations of the risk rating criteria with each of the 18 Offices and Branches. The Offices and Branches then took the risk register template, completed it with their top 3-5 risks and submitted it back to the RMO, who aggregated the results to be reviewed at the Enterprise Risk Committee (ERC), which consists of members of the Authority's Executive management

Executive management evaluated the identified risks and provided input and discussion about the top risks, and what the Authority is currently doing to monitor and manage them. The ERC then voted on the top risks to validate which ones should remain as enterprise risks to the Authority. Of the identified risks the ones noted below will remain a focus for ongoing ERC reviews and programmatic risk monitoring by the RMO.

The RMOs objectives are to:

- Systematize the process by which the Authority responds to circumstances that could increase the cost or significantly delay or halt the Program,
- Increase transparency regarding challenges to project plans and objectives,
- Capture project opportunities,
- Satisfy legal and regulatory requirements and meet the needs and expectations of other
- stakeholders, and
- Rationalize allocation of resources including cost and schedule contingencies.

RISKS AND CONTROLS

Risk: Funding Uncertainty

As has been the case since the creation of the Authority, funding uncertainty continues to be a significant risk and an opportunity for the Authority. Moving into 2022 and beyond, the Authority could receive a significant amount of new federal funding and receive appropriations needed from the California Legislature. The Authority can also benefit through joint investments in shared corridors with other passenger rail operators, which could receive local or regional funding.

If the Authority receives new funding, it can continue and expand construction and reduce risks of insufficient cash and the resulting risks of project slow-downs and potentially employee layoffs.

Control: Effective management of funding-related issues.

- On-time submission of appropriate budget documents to the Department of Finance and to the California Legislature.
- Submission of quality applications for new federal funding and award of federal grants to support the project.
- Coordination with local and regional partners on joint investment opportunities.

Control: Effective communication with partners and stakeholders

The Authority will maintain consistent and timely communication and coordination with control agencies, the California Legislature, the federal government, local partners, and stakeholders regarding the status of the project and plans for continuing implementation. The CEO will also maintain strong connections and communications with various officials at the federal, state, and local levels.

Risk: Third-party Agreements

Interfaces / dependencies related to third parties (e.g., utility owners) pose substantial risk to the design and construction of the system. Risks include delays in program schedules, changes in scope to accommodate third party requirements, and additional budget to complete construction.

Control: Monitoring and Reviews

Regular program / leadership reviews (cost, schedule, issues management, assign responsibility in mitigation, etc.); re-baselining of cost and schedules as updates from third parties are made known; specialized and focused meetings and workshops; and third-party strike force created to address critical third-party concerns.

Control: Specialized Office/Department/Branch

The Program Delivery Office created a Utility Unit to help solve some stakeholder management issues; Infrastructure Delivery Branch and the Real Property Branch are currently working with utility owners to resolve issues impacting critical construction.

Control: Railroad agreements

Agreements in place with Railroads (that mostly act as memorandum of understandings). Currently in the process of pursuing improved agreements.

Control: Engagement

Increased stakeholder engagement has been implemented at all stages of project development.

Risk: Management of Change Orders

If the Authority does not effectively implement and adhere to newly established change order procedures then the program will experience delays and the DBs may file claims for additional compensation, resulting in funding gaps and schedule impacts.

Control: Change Control Committee

Establishment of the change control committee (CCC). See responsibilities and overview under the Control Environment section of this report.

Control: Key Performance Indicators (KPIs

KPIs have been established to support monitoring of contractor performance and change orders.

Control: Policies and Procedures

Established policies and procedures to provide governance and drive alignment of each project.

Control: Increased Staffing

New staff members to cover change order management and claims, and to support CCC initiatives and analysis.

Risk: Staffing Gaps

If the Authority is unable to efficiently fill established, vacant positions, then the Authority will be ill equipped to fulfill program requirements, meet objectives in a timely manner, comply with State and Federal mandates, and support its mission-critical activities.

Control: Ongoing and consistent management.

The Authority's HR team participates in early engagement with Authority staff on workload and staffing needs. The team works with staff to develop and justify needs for staffing increases and establishing appropriate positions to fully support the program's workload and needs. The team also participates in early engagement discussions with the department of finance (DOF) on staffing needs and maintains an ongoing dialogue to address staffing concerns while actively monitoring current resources and changes to resource needs.

Control: Form to Function

Continued Form to Function exercise to add new State positions where appropriate based on workload needs.

CONCLUSION

The High-Speed Rail Authority strives to reduce the risks inherent in our work and accepts the responsibility to continuously improve by addressing newly recognized risks and revising risk mitigation strategies as appropriate. I certify our internal control and monitoring systems are adequate to identify and address current and potential risks facing the organization.

Brian P. Kelly, Chief Executive Officer

CC: California Legislature [Senate (2), Assembly (1)]
    California State Auditor
    California State Library
    California State Controller
    Director of California Department of Finance
    Secretary of California Government Operations Agency