



**Office of the Washington State Auditor**  
**Pat McCarthy**

**Accountability Audit Report**  
**Port of Seattle**  
**King County**

**For the period January 1, 2015 through December 31, 2015**

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**Office of the Washington State Auditor  
Pat McCarthy**

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Port Commission  
Port of Seattle  
Seattle, Washington

**Report on Accountability**

Thank you for the opportunity to work with you to promote accountability, integrity and openness in government. The State Auditor’s Office takes seriously our role of providing state and local governments with assurance and accountability as the independent auditor of public accounts. In this way, we strive to help government work better, cost less, deliver higher value and earn greater public trust.

Independent audits provide essential accountability and transparency for Port operations. This information is valuable to management, the governing body and public stakeholders when assessing the government’s stewardship of public resources.

The attached comprises our report on the Port’s compliance and safeguarding of public resources. Our independent audit report describes the overall results and conclusions for areas we examined. We appreciate the opportunity to work with your staff and we value your cooperation during the audit.

Sincerely,

Pat McCarthy  
State Auditor  
Olympia, WA

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## AUDIT SUMMARY

### Results in brief

In most areas we audited, Port operations complied with applicable requirements and provided adequate safeguarding of public resources. The Port also complied with state laws and regulations and its own policies and procedures in most areas we examined.

However, we identified areas in which the Port could make improvements.

We recommended the Port establish policies to ensure extra compensation payments are based on performance standards or goals, as required by the state Constitution and conduct additional legal review to determine if any further actions, such as repayment, are necessary or required by state law.

These recommendations were included in our report as a finding.

### About the audit

This report contains the results of our independent accountability audit of the Port of Seattle from January 1, 2015 through December 31, 2015.

Management is responsible for ensuring compliance and adequate safeguarding of public resources from fraud, loss or abuse. This includes the design, implementation and maintenance of internal controls relevant to these objectives.

Our audit involved performing procedures to obtain evidence about the Port's uses of public resources, compliance with state laws and regulations and its own policies and procedures, and internal controls over such matters.

In keeping with general auditing practices, we do not examine every transaction, activity or area. Instead, the areas examined were those representing the highest risk of fraud, loss, abuse, or noncompliance. The following areas were examined during this audit period:

- One-time payment to exempt workforce
- Cash receipting at the Bell Harbor and Shilshole Bay Marinas
- Fleet fuel and maintenance card program
- Promotional hosting expenditures
- Procurement (bidding/prevaling wage/change orders)
- Police department overtime

## SCHEDULE OF AUDIT FINDINGS AND RESPONSES

### **2015-001 The Port paid extra compensation to employees that did not comply with the state Constitution.**

#### *Background*

In September 2014, the Port hired a new Chief Executive Officer (CEO). During 2015, under the leadership of the new CEO, the Port experienced significant operational, personnel and administrative changes, including an almost entirely new executive leadership team.

In November 2015, the Port announced that the required work week of a non-represented employee would change from 37.5 hours to 40 hours, to bring the Port more closely in line with industry standards. Under the new 40-hour work week, those Port employees who were paid on an hourly basis would work and earn about 7 percent more each year. However, since the Port based the pay of salaried employees on market averages and the job they performed, rather than a set amount of hours, the pay of salaried employees would not change.

On December 8, 2015, Port Management and the Port Commission authorized a one-time special payment to all non-represented, salaried employees consisting of 7 percent of the employee's annual salary as of December 13, 2015.

Non-represented and salaried employees could be eligible to receive the payment if they worked full-time with a schedule of either 37.5 or 40 hours per week, or part time, or were still in their probationary period. Eligibility also required the employee to meet all of the following conditions:

- Began work at the Port on or before December 13, 2015.
- Be active, not terminated, on December 31, 2015, the date the payment was made.
- In a regular or temporary position lasting more than six months.

A non-represented, salaried employee was not eligible to receive the payment if he or she:

- Was temporarily hired to work six months or less.
- Worked their last day as a Port employee during 2015.

- Informed the Port that their expected employment end date would occur before February 1, 2016.

The one-time payment given to non-represented, salaried employees was not contingent on rendering future services, not based upon past hours worked, not tied to job performance, and was not a salary increase. Also, employees were not obligated to return the one-time payment upon termination of employment.

***Description of Condition***

On December 31, 2015, 642 non-represented employees received a one-time special payment, equal to 7 percent of annual salary, that ranged in amounts from \$3,850 to \$24,500 for a total expense to the Port of \$4,782,796. The payment amount distribution is shown in the following table:

<b>Amount of Payment</b>	<b>No. of Employees</b>
Less than \$5,000	43
\$5,000 - \$9,999	537
\$10,000 - \$14,999	55
\$15,000 - \$19,999	6
More than \$20,000	1
<b>Total</b>	<b>642</b>

**Authorization of payment:** The Port Commission at the December 8, 2015, open public meeting under Resolution Number 3712 authorized the one-time payment. During the meeting, details were not presented such as the number of employees and positions who were to receive the payment, including employees already working 40 hours per week, and the total amount of the payment.

**Reason for payment:** Resolution Number 3712 stated the reason for the payment in Section II, Part D, Number 10 as: “. . . One-time Special Pay: Consistent with the Port’s Total Rewards Program, and particularly with respect to supporting a high-performing organization that enables the Port to attract and retain the most qualified high-performing employees, and in response to the newly adopted 40 hour work week, all eligible salaried employees will, on December 31, 2015, receive a one-time payment consisting of 7 percent of the employee’s annual compensation amount. This section II D.10 shall expire on December 31, 2016 . . .” The payment

was made to improve employee morale and to support a high-performing organization that enabled the Port to attract and retain the most qualified high-performing employees in response to the newly adopted 40-hour work week.

**Change to 40-hour work week:** Resolution Number 3712 shifted the Port to a standard 40-hour work week. However, employees who were already working a 40-hour work week were eligible to receive the payment; we found that 26 employees were already working a 40-hour work week prior to the change and received a total one-time payment of \$227,029.

**Retroactive increase in annual pay:** The calculation of the one-time payment for each salaried non-represented employee was based on the employee's annual compensation as of December 13, 2015. We found that after the one-time payment was made to employees on December 31, 2015, the annual compensation amounts for six employees were retroactively increased in January 2016 as a result of promotions, completion of probation or other pay increase reasons, and their one-time payment amounts were recalculated. The retroactive increases in annual compensation were not in line with the procedures set forth to determine payment amounts to employees, which resulted in each of them receiving an amount above what was originally determined by a total of \$1,120. During the audit, the Port was seeking repayment from the six employees.

**Ineligible employees:** Port employees who resigned or retired before December 31, 2015, were ineligible to receive the one-time payment. We found two employees whose last day worked occurred on October 30, 2015, and December 11, 2015, respectively, which made them ineligible to receive the payment. The total one-time payment to the two former employees was \$16,570. During the audit, the Port was seeking repayment from the two former employees.

### *Cause of Condition*

The method in which the Port executed this one-time payment constitutes extra compensation not allowed by the state Constitution. The Port did not establish performance standards or goals that exceeded normal employment requirements prior to the payment of the extra compensation as required by the state Constitution.

### ***Effect of Condition***

The Port violated the state Constitution, and 642 employees received extra compensation to which they were not entitled. In addition, this compensation might not be recoverable by the Port.

### ***Recommendation***

We recommend the Port establish policies to ensure extra compensation payments are based on performance standards or goals as required by the state Constitution.

We also recommend the Port conduct additional legal review to determine if any further actions, such as repayment, are necessary or required by state law.

### ***Port's Response***

*We thank the Washington State Auditor's Office (SAO) for your thorough accountability audit of the Port of Seattle. The Port respects the finding of the SAO and will implement the recommendations to refine policies as necessary and conduct additional legal review.*

*We respectfully offer the following for consideration:*

#### ***Business Rationale and Benefit Achieved***

*The Port of Seattle recognizes that a high-performing organization is vital to fulfilling our commitments to deliver on the Century Agenda including adding 100,000 jobs over 25 years, reducing our environmental footprint, and promoting more equitable growth.*

*Beginning in 2014 and continuing through 2015, the Port introduced significant operational and personnel changes including large-scale organizational restructuring, changing the required work week of non-represented employees from 37.5 hours to 40, bringing in new leadership across multiple departments, and discussing new pay and benefit programs. During this time, the Port also announced the formation of the Northwest Seaport Alliance, a joint operating agreement with the Port of Tacoma, requiring significant organizational changes.*

*By November 2015, these changes resulted in employees expressing concerns about overall job security, uncompensated mandatory work hours, administrative changes resulting in reduced overall pay, and employee morale. Human Resources received approximately 150 emails along these lines. The Port also considered the strength of our highly-competitive regional job market and the risk of losing talent. In response to employee concerns, the Port determined that a one-time payment, versus more costly permanent wage increases, was the best option to achieve*



*our business rationale of retaining our highly-skilled and experienced workforce while limiting the financial impact.*

*The stated cause leading to the audit finding is the “method in which the Port executed the one-time payment.” Clarification was obtained during the course of the audit from the SAO that had the one-time extra compensation been paid in installments, or if promises had been made by employees to stay in their job for a period of time, there would not have been an audit finding.*

*The Port achieved the intended business outcome of retaining our dedicated employee talent pool. Consideration was received in return for the one-time extra compensation. Despite significant employee concerns expressed in the waning months of 2015, the Port achieved a 96% retention rate in 2016. We believe the one-time payment contributed to the overall retention rate.<sup>1</sup>*

### **Legal Review**

*The Port’s principle for determining compensation is grounded in the Washington State Constitution. Under Washington state law, Port districts have broad authority to set compensation for employees.*

*The one-time payment was carefully tailored to meet constitutional requirements as understood by Port counsel. The Port intentionally identified the lump-sum payment as forward-looking, timed to address employees’ concerns and the Port’s business goal of retaining high-performing employees. As discussed above, the Port had clear business interests in making this one-time payment and, from the Port’s perspective, achieved the stated intent. State law and Port policy together establish and delegate authority for the implementation of Commission actions to the CEO.*

### **Going Forward**

*The Port respects the SAO’s recommendations. The Port is conducting additional legal review to determine if further actions are required by state law.*

*The Port will comprehensively review all policies and procedures related to extra compensation payments including benchmarking ourselves against local government practices. Finally, the Port of Seattle Commission plans to take a number of measures to ensure greater overall transparency between the executive office and the Commission going forward.*

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<sup>1</sup> *Of the 640 employees receiving the one-time compensation, only 29 left the Port voluntarily during 2016 for reasons other than retirement. This represents 4.3% of the total number of employees who received the payment and the total amount paid to these employees was \$190,230*

### ***Auditor's Remarks***

The State Auditor's Office is appreciative of the Port's response, including the background provided on the business rationale for approving the one-time payment. The Office also appreciates the steps the Port is taking to review their policies and procedures related to compensation and conducting additional legal review.

We thank the Port's staff and management for their cooperation and assistance during the audit. We will follow up on the Port's implementation of our recommendations during our next audit.

### ***Applicable Laws and Regulations***

Washington State Constitution – Article II Legislative Department – Section 25 Extra Compensation Prohibited.

The legislature shall never grant any extra compensation to any public officer, agent, employee, servant, or contractor, after the services shall have been rendered, or the contract entered into, nor shall the compensation of any public officer be increased or diminished during his term of office. Nothing in this section shall be deemed to prevent increases in pensions after such pensions shall have been granted.

Washington State Constitution – Article VIII State, County, and Municipal Indebtedness – Section 7 Credit Not to Be Loaned.

No county, city, town or other municipal corporation shall hereafter give any money, or property, or loan its money, or credit to or in aid of any individual, association, company or corporation, except for the necessary support of the poor and infirm, or become directly or indirectly the owner of any stock in or bonds of any association, company or corporation.

## RELATED REPORTS

### **Financial**

A financial statement audit was performed by a firm of certified public accountants. That firm's report is available from the Port of Seattle. The firm reported a significant deficiency in internal controls over financial reporting regarding the Port's ancillary revenue operating system. The deficiency is in the design of the internal controls necessary to adequately address system reliability, process controls and data security in the ancillary revenue operating system.

### **Federal grant programs**

A firm of certified public accountants evaluated internal controls and tested compliance with the federal program requirements, as applicable, for the Port's major federal programs. That firm's report is available from the Port of Seattle.

## INFORMATION ABOUT THE PORT

The Port is a municipal corporation of the State of Washington (the “state”), organized on September 5, 1911, under the state statute RCW 53.04.010 et seq. In 1942, the local government in King County selected the Port to operate the Seattle-Tacoma International Airport (the “Airport”).

Port policies are established by a five-member Commission elected at-large by the voters of the County for four-year terms. The Commission appoints the Chief Executive Officer, who oversees daily operations for the organization. Through resolutions and directives, the Commission sets policy for the Port. These policies are then implemented by the Chief Executive Officer and his executive staff.

The Port is comprised of three operating divisions: Aviation, which manages all operations at the Airport, including landside operations such as parking garage; Seaport, which manages maritime cargo and cruise passenger marine terminals as well as industrial property connected with maritime businesses; and Real Estate, which manages recreational and commercial moorage facilities, leases commercial and industrial properties and plans and facilitates the development of selected real estate assets.

A number of corporate service departments are structured under Corporate, which provides high quality and cost-effective professional and technical services to the operating divisions and supports the overall goals of the Port. Capital Development houses departments responsible for engineering, project management and construction functions. Other port-wide departments include Accounting and Financial Reporting, Business Intelligence, Commission Office, Executive, Environmental and Sustainability, Finance and Budget, Human Resource, Information and Communications Technology, Labor Relations, Legal Public Affairs, Police, Emergency Management and Risk Management.

For 2015, the Port had total operating revenues of \$558.9 million, which represents a 4.6 percent increase from 2014. Total operating expenses increased from \$306.3 million in 2014 to \$317.8 million in 2015. The Port’s net operating income before depreciation increased \$12.9 million from 2014 to 2015. The Port employed 1,779 employees in 2015.

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*Information current as of report publish date.*

### **Audit history**

You can find current and past audit reports for the Port of Seattle at <http://portal.sao.wa.gov/ReportSearch>.

## ABOUT THE STATE AUDITOR'S OFFICE

The State Auditor's Office is established in the state's Constitution and is part of the executive branch of state government. The State Auditor is elected by the citizens of Washington and serves four-year terms.

We work with our audit clients and citizens to achieve our vision of government that works for citizens, by helping governments work better, cost less, deliver higher value, and earn greater public trust.

In fulfilling our mission to hold state and local governments accountable for the use of public resources, we also hold ourselves accountable by continually improving our audit quality and operational efficiency and developing highly engaged and committed employees.

As an elected agency, the State Auditor's Office has the independence necessary to objectively perform audits and investigations. Our audits are designed to comply with professional standards as well as to satisfy the requirements of federal, state, and local laws.

Our audits look at financial information and compliance with state, federal and local laws on the part of all local governments, including schools, and all state agencies, including institutions of higher education. In addition, we conduct performance audits of state agencies and local governments as well as [fraud](#), state [whistleblower](#) and [citizen hotline](#) investigations.

The results of our work are widely distributed through a variety of reports, which are available on our [website](#) and through our free, electronic [subscription](#) service.

We take our role as partners in accountability seriously, and provide training and technical assistance to governments, and have an extensive quality assurance program.

<b>Contact information for the State Auditor's Office</b>	
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<b>Main telephone</b>	(360) 902-0370
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