

Washington State Auditor's Office
Accountability Audit Report

Port of Seattle
King County

Report Date
November 2, 2010

Report No. 1004616

Issue Date
December 13, 2010



WASHINGTON
BRIAN SONNTAG
STATE AUDITOR



**Washington State Auditor
Brian Sonntag**

December 13, 2010

Board of Commissioners
Port of Seattle
Seattle, Washington

Report on Accountability

We appreciate the opportunity to work in cooperation with your Port to promote accountability, integrity and openness in government. The State Auditor's Office takes seriously our role to advocate for government accountability and transparency and to promote positive change.

Please find attached our report on the Port of Seattle's accountability and compliance with state laws and regulations and its own policies and procedures. Thank you for working with us to ensure the efficient and effective use of public resources.

Sincerely,

BRIAN SONNTAG, CGFM
STATE AUDITOR

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King County
November 2, 2010**

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Audit Summary

**Port of Seattle
King County
November 2, 2010**

ABOUT THE AUDIT

This report contains the results of our independent accountability audit of the Port of Seattle from January 1, 2009 through December 31, 2009.

We evaluated internal controls and performed audit procedures on the activities of the Port. We also determined whether the Port complied with state laws and regulations and its own policies and procedures.

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 noncompliance, misappropriation or misuse. The following areas were examined during this audit period:

- Procurement
- Disbursements
- Conflict of interest
- Insurance
- Revenue and receivables
- Contract compliance
- Loss reporting

RESULTS

In most areas, the Port complied with state laws and regulations and its own policies and procedures.

However, we identified a condition significant enough to report as a finding:

- The Port did not adequately monitor management contracts with third parties.

We also noted certain matters that we communicated to Port management. We appreciate the Port's commitment to resolving those matters.

Related Reports

**Port of Seattle
King County
November 2, 2010**

FINANCIAL

An audit of the Port's financial statements and compliance with federal program requirements was performed by a firm of certified public accountants. That firm's reports are available from the Port.

PERFORMANCE AUDITS

Initiative 900, approved by voters in 2005, gives the State Auditor's Office the authority to conduct independent performance audits of state and local government entities. Performance audits may include objective analysis on ways to improve program performance and operations, reduce costs and identify best practices.

We issued the Port of Seattle Real Estate Management and Select Programs performance audit report in December 2010 that is available on our Web site.

Description of the Port

Port of Seattle King County November 2, 2010

ABOUT THE PORT

The Port of Seattle was established in 1911 when King County voters approved its formation to manage properties along the Seattle waterfront. In 1941 the Legislature broadened the authority of port districts to operate airports. Approximately one year later, local governments in King County selected the Port to operate Seattle-Tacoma International Airport.

King County voters elect five Port Commissioners who serve four-year terms. Commissioners establish policy for the Port and appoint a Chief Executive Officer who oversees Port employees and programs. In 2009 the Port employed 1,575 employees.

The Port is comprised of three operating divisions. The Aviation Division serves the predominant air travel needs of a five-county area. The Seaport Division focuses primarily on containerized cargo and passenger marine terminals as well as industrial property connected with maritime businesses. The Real Estate Division manages moorage facilities, leases commercial and industrial buildings/properties and plans and facilitates the development of selected real estate assets.

Most of the Port's funding comes from bond proceeds, a local tax levy, passenger facility charges, customer facility charges, grants, interest from investments, income from leases and revenue collected from customers and the public for parking and other services the Port provides.

The Board of Commissioners approves an operating budget annually. Actual operating revenue totaled \$449 million in 2009 while operating expenses totaled \$246 million.

The Port uses revenue bonds and other sources to finance construction at the airport. General obligation bonds, lease revenue and local property taxes help fund the seaport and real estate construction programs. In 2009 the Port collected \$73.5 million in property taxes.

The capital budget for 2009 was \$676 million and the capital improvement program for 2009-2014 is \$2.1 billion.

ELECTED OFFICIALS

These officials served during the audit period:

Board of Commissioners:

Bill Bryant
John Creighton
Gael Tarleton
Lloyd Hara
Patricia Davis

Note: Tom Albro and Rob Holland replaced Patricia Davis and Lloyd Hara in January 2010.

APPOINTED OFFICIALS

Chief Executive Officer
Chief of Staff
Chief Financial and Administrative Officer
General Counsel
Managing Director, Seaport
Managing Director, Aviation
Managing Director, Real Estate
Managing Director, Capital Development

Tay Yoshitani
Kurt Beckett
Dan Thomas
Craig Watson
Charles Sheldon
Mark Reis
Joe McWilliams
Ralph Graves

PORT CONTACT INFORMATION

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Phone: (206) 728-3000

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AUDIT HISTORY

The last accountability audit was performed in 2009 covering the years 2006, 2007 and 2008.

Schedule of Audit Findings and Responses

**Port of Seattle
King County
November 2, 2010**

1. The Port did not adequately monitor management contracts with third parties.

Background

The Port contracts with outside parties to manage four properties: the Portside Café, Bell Harbor International Conference Center, World Trade Center – West and World Trade Center – Seattle. Revenues from these four properties were approximately \$9 million in 2009. Bell Harbor is the largest property, with revenue of \$6.6 million. The management companies are reimbursed for expenses incurred on behalf of the Port.

Port management requested an internal audit of the Portside Café prior to issuing a request for proposal for a new management contract. The audit period was from January 1, 2008 through December 31, 2009. That audit revealed several conditions that we are reporting. As part of our audit, we reviewed the other management agreements to determine if similar conditions are present.

Description of Condition

Portside Café

The internal audit found:

- Recurring operating losses. Since 2006, the Café has lost an average of \$150,000 annually. The operating agreement for the Café stipulated that it should break even.
- The management company did not conduct inventories during the audit period. Consequently, the internal auditor could not ascertain the true cost of goods sold, spoilage or loss.
- More than \$73,550 in unallowable expenses was paid to the management company. The largest was \$46,642 in salary and benefit overpayments to the management company. The salary and benefits were calculated and billed to the Port using an estimate rather than the actual costs causing the overpayment. An estimated percentage of salaries, rather than actual costs, was used to calculate the amounts.

As soon as the Port suspected the contractor was reimbursed in excess of actual costs, the losses should have been reported immediately to our Office in accordance with state law (RCW 43.09.185).

As a result of the audit, the Port's Chief Executive Officer closed the Portside Café in April 2010.

Bell Harbor and World Trade Center – Seattle

State law (RCW 43.09.240) requires receipts to be deposited within 24 hours. The Port sweeps money into a Port account out of an account used by the management company that operates Port facilities. However, the management company makes deposits only on Monday, Wednesday and Friday, which means Port funds are not deposited into the Port's account daily.

Cause of Condition

The Port did not have internal controls sufficient to ensure the management companies complied with state law and that expenses were for valid business purposes. The Port also did not adequately monitor to ensure compliance with the terms of the management agreements.

The Port relied on attendance by representatives of our Office at a meeting after the internal audit was complete to be sufficient notification of known or suspected losses. However, staff from our Office was not present at the meeting, at which the internal audit results were discussed. In addition, the law requires reporting to occur when the Port first suspects a loss.

Effect of Condition

By not immediately reporting all known or suspected losses or other illegal activity, the Port is not complying with the law. Moreover, by not complying with the law, full accountability and transparency is not provided to taxpayers who pay for Port operations.

By not adequately enforcing the terms of the management agreement, the Port spent more public funds than it was legally required to do. Further, the Port was deprived the use of these funds for public purposes.

Inadequate internal control over cash handling by Port contractors increases the risk that a loss or misappropriation of public funds may occur and not be detected in a timely manner, if at all.

Recommendation

We recommend the Port:

- Immediately report all known or suspected losses or other illegal activity to the State Auditor, as required by state law.
- Seek recovery of unallowable expenses from the café management company.
- Improve monitoring of the management companies to ensure compliance with the terms of the management agreement.
- Ensure management companies deposit funds in accordance with state law.

Port's Response

Immediately report all known or suspected losses or other illegal activity to the State Auditor, as required by state law.

The Port believes that existing policies and procedures address the auditor's recommendation as detailed below.

Additionally, the Port is accountable and transparent in reporting of losses. This is handled by means of the State Auditor's Loss Reporting Website, Audit Committee in public session and/or discussions with Port management. The instance brought forward by the SAO from review of the Port of Seattle Internal Audit Report on the Portside Café is an anomaly in that Port staff did not consider this type of agreement to fall within the context of the RCW. It was not procedurally submitted to the SAO as with all other self-reported losses but it was discussed in the Audit Committee during public session.

In 2009, the Port developed a Workplace Responsibility Program, a collaborative effort among the Workplace Responsibility Office, Human Resource & Development Information Technology, Internal Audit, Labor Relations, Risk Management and the Legal Department to implement a comprehensive ethics and workplace compliance program. In 2010, the Workplace Responsibility Office was established to provide overall leadership and coordination of the Workplace Responsibility Program. The WR Office guides, supports and reinforces efforts to successfully advance the Port's mission, while upholding the highest standards of business conduct, ethics and workplace behavior. This is reflected in the Code of Conduct/Workplace Responsibility Handbook representing the Port's core values and is a collection of 14 policies that set forth fundamental expectations regarding business and workplace conduct. These Code policies include CC-5 Fraud Awareness and Prevention and CC-6 Loss Prevention.

The specific purposes of CC-5 and CC-6 are:

- To ensure proper stewardship over public funds and assets, and provide timely and proper handling of any known losses or suspected fraudulent activity involving those funds and assets. To comply with RCW 43.09.185, that requires State agencies and local governments to immediately report any known or suspected loss of public funds or assets to the State Auditor's Office (SAO)*
- To establish clear expectations and ensure consistent and timely action by the Port*
- To ensure that losses are minimized; investigations and audits are not hampered; and bond claims are not jeopardized.*

The Workplace Responsibility Office is currently coordinating efforts among the Internal Audit department, Legal, Risk Management, ICT and the POS Police department to clarify, communicate and train on the reporting requirements and to streamline and refine current information-sharing protocols.

Currently, the Internal Audit department receives a list of all reported losses from the POS Police department monthly, as well as a report of all damages and/or losses to port properties from the Risk Management department

Existing policies and procedures address the auditor's recommendation but in an effort to further improve those procedures, the Port has adopted a standard form for reporting employee losses and it is used by Human Resources, Legal and Labor Relations ensuring that information is reported uniformly.

Seek recovery of unallowable expenses from the café management company

The recovery of unallowable expenses referenced in the audit performed by the Port of Seattle's Internal Audit Department is currently under legal review. The Port will be assessing the expected costs to recover against the actual recovery itself.

Improve monitoring of the management companies to ensure compliance with the terms of the management agreement.

The terms of the agreements are monitored by the staff managing those agreements. Additionally, the Internal Audit Department audits the third party agreements for compliance. However, the Port will review existing processes and procedures to determine if they need to be enhanced to mitigate risk.

Ensure that management companies deposit funds in accordance with state law

Effective September 21, 2010 Bell Harbor International Conference Center and World Trade Center Seattle have daily Loomis pick-ups to ensure adherence to state law.

Auditor's Remarks

We thank the Port for its cooperation and assistance during the audit and look forward to reviewing the Port's corrective action during our next audit.

Applicable Laws and Regulations

RCW 43.09.185, Loss of public funds--Illegal activity--Report to state auditor's office, states, in its entirety:

State agencies and local governments shall immediately report to the state auditor's office known or suspected loss of public funds or assets or other illegal activity.

RCW 43.09.200 states in part:

The state auditor shall formulate, prescribe, and install a system of accounting and reporting for all local governments, which shall be uniform for every public institution, and every public office, and every public account of the same class.

The system shall exhibit true accounts and detailed statements of funds collected, received and expended for account of the public for any purpose whatever, and by all public officers, employees, or other persons. The accounts shall show the receipt, use, and disposition of all public property, and the income, if any, derived there from; all sources of public income, and the amounts due and received from every source; all receipts, vouchers, and other documents kept, or required to be kept,

necessary to isolate the validity of every transaction; all statements and reports made or required to be made, for the internal administration of the office to which they pertain; and all reports published or required to be published , for the information of the people regarding any and all details of the financial administration of public affairs.

RCW 43.09.240 states in part:

Every public officer and employee, whose duty it is to collect or receive payments due or for the use of the public shall deposit such moneys collected or received by him or her with the treasurer of the local government once every twenty-four hours.

RCW 43.09.260, Local government accounting--Examination of local governments--Reports--Action by attorney general, states:

It shall be unlawful for any local government or the responsible head thereof, to make a settlement or compromise of any claim arising out of such malfeasance, misfeasance, or nonfeasance, or any action commenced therefore, or for any court to enter upon any compromise or settlement of such action, without the written approval and consent of the attorney general and the state auditor.



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.

Our mission is to work in cooperation with our audit clients and citizens as an advocate for government accountability. 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.

The State Auditor's Office employees are located around the state to deliver our services effectively and efficiently.

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 and fraud, whistleblower and citizen hotline investigations.

The results of our work are widely distributed through a variety of reports, which are available on our Web site and through our free, electronic subscription service. We continue to refine our reporting efforts to ensure the results of our audits are useful and understandable.

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

State Auditor
Chief of Staff
Deputy Chief of Staff
Chief Policy Advisor
Director of Audit
Director of Special Investigations
Director for Legal Affairs
Director of Quality Assurance
Local Government Liaison
Communications Director
Public Records Officer
Main number
Toll-free Citizen Hotline

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