

Washington State Auditor's Office
Accountability Audit Report

City of Seattle
King County

Report Date
June 22, 2009

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WASHINGTON
BRIAN SONNTAG
STATE AUDITOR



**Washington State Auditor
Brian Sonntag**

July 6, 2009

Council
City of Seattle
Seattle, Washington

Report on Accountability

We appreciate the opportunity to work in cooperation with your City 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 City 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
June 22, 2009**

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Audit Summary

**City of Seattle
King County
June 22, 2009**

ABOUT THE AUDIT

This report contains the results of our independent accountability audit of the City of Seattle for July 1, 2007, through June 30, 2008.

We evaluated internal controls and performed audit procedures on the activities of the City. We also determined whether the City 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:

- Ability to meet current and future financial and operational obligations
- Statutory authority for programs or actions
- Use of restricted funds
- Investments and deposits
- Safeguarding of public resources
- Procurement requirements
- Conflict of interest
- Open public records and open public meetings laws

RESULTS

In most areas, the City 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 City should improve its internal controls over purchasing and contracting.

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

Related Reports

**City of Seattle
King County
June 22, 2009**

FINANCIAL

Our opinion on the City's 2007 financial statements and compliance with federal grant program requirements is provided in a separate report, which includes the City's financial statements. We reported a significant deficiency in internal controls over financial reporting regarding City Light's accounting for inventory and unbilled receivables.

FEDERAL GRANT PROGRAMS

We evaluated internal controls and tested compliance with the federal program requirements, as applicable, for the City's major federal programs, which are listed in the Federal Summary section of the 2007 financial statement and single audit report. That report includes one finding regarding weaknesses in internal controls over federal grant reporting requirements and one finding regarding internal controls over compliance with federal suspension and debarment requirements.

That report is available on our Web site at www.sao.wa.gov.

Description of the City

**City of Seattle
King County
June 22, 2009**

ABOUT THE CITY

The City of Seattle is the largest city in King County and the state, with a population of approximately 586,200 citizens.

The City has a mayor-council form of government with nine elected Council Members, an elected Mayor and an elected City Attorney. Seattle's charter vests legislative authority in the Mayor and Council. The Mayor is the chief executive officer of the City and is responsible for the enforcement of the City's laws and contracts and directing subordinate City officers. The Council establishes City policy through enactment of ordinances (laws) and adoption of resolutions.

The City's budget for 2008 was \$3.51 billion, including \$926 million for the general fund. It has approximately 11,000 employees and provides a full range of services including water, drainage and wastewater, solid waste, electric power, police, municipal court, fire, emergency medical, parks and recreation (including four golf courses), planning and economic development, and municipal libraries.

ELECTED OFFICIALS

These officials served during the audit period:

Mayor
Council:

Greg Nickels
Richard Conlin
Tim Burgess
Sally J. Clark
Jan Drago
Jean Godden
Bruce Harrell
Nick Licata
Richard J. McIver
Tom Rasmussen
Thomas A. Carr

City Attorney

APPOINTED OFFICIALS

Director of Finance

Dwight Dively

CITY CONTACT INFORMATION

Address: City of Seattle
700 5th Avenue, Suite 4300
P.O. Box 94669
Seattle, WA 98124-4669

Phone: (206) 684-2489

Web site: www.seattle.gov

AUDIT HISTORY

We audit the City annually. The past five accountability audits have reported three findings. Our 2004 audit contained a finding related to misappropriation of public funds and our 2007 audit reported inappropriate use of restricted funds. These findings have been resolved.

Schedule of Audit Findings and Responses

City of Seattle King County July 1, 2007 through June 30, 2008

1. The City should improve its internal controls over contracting and purchasing compliance.

Background

The City of Seattle's Department of Executive Administration (DEA) is responsible for ensuring City compliance with procurement, purchasing and contracting requirements. The DEA Purchasing Division is responsible for ensuring City compliance with procurement, purchasing and contracting of goods and services. The DEA Contracting Services Division is responsible for procurement and contracting of public works and consultant contracts.

The Seattle Public Library is independent of DEA control, but is subject to the authority of its Board of Trustees, which is appointed by the Mayor and confirmed by the City Council.

Description of Condition

We identified instances of noncompliance with procurement and contracting requirements.

Purchases

We tested 43 purchases of which 13 were from Seattle Public Utilities. We found the following instances where Seattle Public Utilities did not comply with City purchasing requirements:

- A blanket contract for water meters that expired on December 31, 2006, was still being used in January 2009. The vendor was paid over \$500,000 since the contract expired.
- One vendor was paid \$108,000 for printed materials with no contract in place. These purchases were not competitively procured as required by the Seattle Municipal Code.
- An \$186,945 purchase of materials for Spokane Street viaduct utility relocation project was made in late 2007. In March 2008, payment for this purchase was split into six smaller transactions to conceal noncompliance with purchase documentation requirements and to avoid detection by the existing internal controls. We identified other issues related to this purchase that we communicated to City management.

Public Works

We examined nine public works projects totaling \$15.1 million. Our audit focused on projects that did not appear on the Contracting Services' list of public works projects in order to determine if procedures for ensuring compliance with public works project requirements are working.

During our discussions with Contracting Services we identified weaknesses in the public works process and found one project that bypassed Contracting Services' procedures. No system is in place to ensure all public works projects are reported to Contracting Services. The following instance of noncompliance confirms that Contracting Services' reliance on project managers to self-report is not working.

- A Seattle Public Utilities project manager who arranged the installation of an equipment storage building did not follow public works procedures. Contracting Services was not notified of the project, which cost \$177,110. This work was not competitively procured as required by state law.

Further, Contracting Services has no procedures in place to ensure change orders to public works contracts are used properly.

- A Fleets and Facilities Department's renovation project at City Hall was inappropriately expanded through a change order to include work unrelated to the original project. The change orders increased the cost of the project from \$138,258 to a final \$402,557.

We found additional issues at the Seattle Public Library. We examined three Library projects totaling \$6.3 million. For all three examined public works projects Library management did not verify the contractors were licensed or registered and had industrial insurance coverage prior to contracting with them. For one of the three projects, the Library paid seven of 15 subcontractors before receiving Statements of Intent to Pay Prevailing Wages. We also found the Library paid 14 of 74 subcontractors whose statements did not include required pay rates or registration numbers.

We note the Library is governed by its Board of Trustees, so it is not required to use Contracting Services. In the absence of that requirement, the Library itself should have systems in place to ensure compliance with state contracting laws.

Cause of Condition

Purchasing

Seattle Public Utilities and Purchasing Services did not sufficiently coordinate its efforts to ensure timely renewal or rebidding of blanket contracts, and did not have sufficient controls to detect payments made without appropriate contracts.

Additionally, Seattle Public Utilities management overrode existing internal controls over purchasing due to the perceived urgency of the Spokane Street viaduct utility relocation project.

Public Works

Contracting Services does not have procedures that will identify potential violations of state law and City policy regarding purchases and contracts.

Library employees were not aware of all public works contracting requirements. Further, Contracting Services was not consulted on these compliance issues.

Effect of Condition

A \$177,110 public works project was completed and paid for without a contract or competitive procurement and another contract was inappropriately amended through change orders, resulting in the competitive procurement process being bypassed.

Procurement laws exist to ensure a fair and impartial process that gives all interested parties an opportunity to bid for public works projects. By not ensuring this process is followed, the City may not be getting the best price for projects.

The City places itself at risk of liabilities for unpaid or underpaid wages and cost increases due to lack of written contracts or due to poor quality work performed by unqualified contractors.

Recommendation

We recommend:

- The City provides additional and continuous purchasing and contracting training to all involved with public works contracting.
- Library contracts follow Contracting Services' procedures.
- Contracting Services establish internal controls to identify projects at other departments/divisions/offices that are bypassing established procedures.

City's Response

The City of Seattle is committed to operating in compliance with applicable laws and regulations as well as established policies and procedures with regard to purchasing and contracting. We appreciate the opportunity to respond to these issues and describe our actions to address them.

The City concurs with the finding that the cited purchases from three vendors did not comply with required competitive bidding. To ensure compliance, the City will strengthen its internal controls, develop exception monitoring tools, and provide continual training to employees involved in purchasing activities. It is important to note that our subsequent review confirmed that the purchases were actually paid at competitive prices and therefore did not result in financial loss to the City.

The City concurs with the finding that one public works project did not comply with contracting requirements. The department that managed the project has a Capital Projects Group (CPG) that closely oversees public works activities. However, the project

was not submitted to the CPG and so some procurement procedures were not followed. The City will provide continual training on policies and procedures to staff involved in public works procurement and payment activities, and will develop financial reports and analysis tools to help managers detect violations so any issues can be addressed in a timely manner.

The City believes that use of a change order issued to a contractor who was already working on-site in space adjacent to Seattle Channel offices was appropriate. The change order permanently fixed a cooling problem in Seattle Channel, protected the sensitive and expensive electronic equipment from immediate jeopardy, and avoided the risk of additional costs to the City. The City appreciates and will implement the auditor's recommendation to develop procedures to detect material change orders so they can be evaluated and any issues can be promptly addressed.

The City concurs with the finding that verification activities regarding license or registration and industrial insurance coverage of certain Seattle Public Library (the Library) contractors were not documented. The City also concurs that some payments to subcontractors were made prior to receipt of their Statement of Intent to Pay Prevailing Wages. It is important to note that the subject vendors had been used by the Library within the past year and they had been properly verified to be licensed and registered, and had industrial insurance coverage in place. Subsequent review also confirmed compliance with prevailing wage requirements. The Library is taking steps to update their contracting procedures and to provide continual training to staff involved in contracting activities. It should be noted that the Library is governed by a board of trustees appointed by the Mayor and confirmed by the Council. The trustees have distinct legal authority to administer contracts, but the City appreciates the auditor's recommendation that the Library should utilize the City's central contract administration capabilities and will make such resources available as needed.

Auditor's Remarks

The City was very helpful during our investigation and we appreciate its commitment to strengthening its policies and procedures. We are committed to providing any help we can to ensure strong control systems are in place.

Applicable Laws and Regulations

The Seattle Municipal Code (SMC) regulates City purchasing of supplies, materials, equipment, and services and requires competitive bidding. SMC 20.60.106 provides in part:

- A. Except in emergencies provided for in this subchapter, all expenditures for supplies, materials, equipment, and services within the purview of this subchapter the estimated cost of which is in excess of Thirty Thousand Dollars (\$30,000) per requisition shall be made on written contract entered into upon the basis of competitive bids and are subject to the preferences provided by SMC Section 20.60.210. Notices inviting sealed competitive bids shall be published at least once in the City official newspaper, and at least five (5) calendar days must intervene between the date of the last publication and the final date for submitting the bids; provided, that purchases of patented or proprietary items available from a single source, or purchases or contracts for services

within the purview of this subchapter where competitive bidding is deemed impracticable by the Director, shall be exempt from the competitive bidding requirements of the section; provided, further, that the purchase of supplies, materials, and equipment to be resold by the using agency may be negotiated for by the Director when, in his or her judgment, the lowest and best price can be obtained by such negotiation.

The bid threshold had increased from \$30,000 to \$42,000 as of 2008. SMC 20.60.140 provides for escalation of bid dollar limits and provides in part:

A. As of January 1, 1997, all monetary amounts specified in Sections 20.60.106 and 20.60.110 shall be annually adjusted hereafter by the Director, consistent with the formula described in SMC Section 20.50.120 for adjustment of the consultant selection threshold, so that the thresholds for competitive bidding for purchases and the consultant selection threshold are maintained at the same amount.

RCW 35.22.620 limits the amount of public works construction that can be performed by City employees. It provides authority for cities to bid public works, requires bidding for all public work exceeding certain limits, and states in part:

(1) As used in this section, the term "public works" means as defined in RCW 39.04.010.

(2) A first-class city may have public works performed by contract pursuant to public notice and call for competitive bids. As limited by subsection (3) of this section, a first-class city may have public works performed by city employees in any annual or biennial budget period equal to a dollar value not exceeding ten percent of the public works construction budget, including any amount in a supplemental public works construction budget, over the budget period. The amount of public works that a first class city has a county perform for it under RCW 35.77.020 shall be included within this ten percent limitation. . . .

Whenever a first-class city has had public works performed in any budget period up to the maximum permitted amount for that budget period, all remaining public works within that budget period shall be done by contract pursuant to public notice and call for competitive bids.

RCW 39.06 requires that contractors be licensed and registered and it provides:

RCW 39.06.010 Contracts with unregistered or unlicensed contractors and with other violators prohibited.

No agency of the state or any of its political subdivisions may execute a contract:

(1) With any contractor who is not registered or licensed as may be required by the laws of this state other than contractors on highway projects who have been prequalified as required by RCW 47.28.070, with the department of transportation to

perform highway construction, reconstruction, or maintenance; or . . .

(3) For two years from the date that a violation is finally determined, with any person or entity who has been determined by the respective administering agency to have violated RCW 50.12.070(1)(b), 51.16.070(1)(b), or *82.32.070(1)(b). During this two-year period, the person or entity may not be permitted to bid, or have a bid considered, on any public works contract.

RCW 39.06.020 Verification of subcontractor responsibility criteria.

A public works contractor must verify responsibility criteria for each first tier subcontractor, and a subcontractor of any tier that hires other subcontractors must verify responsibility criteria for each of its subcontractors. Verification shall include that each subcontractor, at the time of subcontract execution, meets the responsibility criteria listed in RCW 39.04.350(1) and possesses an electrical contractor license, if required by chapter 19.28 RCW, or an elevator contractor license, if required by chapter 70.87 RCW. This verification requirement, as well as the responsibility criteria, must be included in every public works contract and subcontract of every tier.

RCW 39.04.350 requires that bidders have industrial insurance and states in part:

Bidder responsibility criteria — Supplemental criteria.

(1) Before award of a public works contract, a bidder must meet the following responsibility criteria to be considered a responsible bidder and qualified to be awarded a public works project. The bidder must:

(a) At the time of bid submittal, have a certificate of registration in compliance with chapter 18.27 RCW;

(b) Have a current state unified business identifier number;

(c) If applicable, have industrial insurance coverage for the bidder's employees working in Washington as required in Title 51 RCW; an employment security department number as required in Title 50 RCW; and a state excise tax registration number as required in Title 82 RCW;

RCW 39.12.040 regulates prevailing wage compliance and it states in part:

Statement of intent to pay prevailing wages, affidavit of wages paid — Alternative procedure.

- (1) Except as provided in subsection (2) of this section, before payment is made by or on behalf of the state, or any county, municipality, or political subdivision created by its laws, of any sum or sums due on account of a public works contract, it shall be the duty of the officer or person charged with the custody and disbursement of public funds to require the contractor and each and every subcontractor from the contractor or a subcontractor to submit to such officer a "Statement of Intent to Pay Prevailing Wages". For a contract in excess of ten thousand dollars, the statement of intent to pay prevailing wages shall include:
 - (2) (a) The contractor's registration certificate number; and
 - (3) (b) The prevailing rate of wage for each classification of workers entitled to prevailing wages under RCW 39.12.020 and the estimated number of workers in each classification.

Each statement of intent to pay prevailing wages must be approved by the industrial statistician of the department of labor and industries before it is submitted to said officer. Unless otherwise authorized by the department of labor and industries, each voucher claim submitted by a contractor for payment on a project estimate shall state that the prevailing wages have been paid in accordance with the prefiled statement or statements of intent to pay prevailing wages on file with the public agency.

Status of Prior Audit Findings

**City of Seattle
King County
June 22, 2009**

The status of findings contained in the prior years' audit reports of the City of Seattle is provided below:

- 1. The City of Seattle did not comply with state law governing the use of Real Estate Excise Tax proceeds.**

Report No. 74973, dated June 30, 2008

Background

We disagreed with the City's use of \$3,188,702 of Real Estate Excise Tax 2 proceeds for projects related to construction of fire station and to create or extend trails.

Status

The issue has been resolved. The City responded by transferring the costs to a different, less restrictive funding source.



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.

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