

Schedule of Audit Findings

Port of Seattle
King County
September 16, 2005

1. The Port cannot demonstrate the appropriateness of certain expenditures, made inappropriate expenditures and paid vendors in advance of receiving services.

Description of Condition

Credit card charges totaling \$95,050 are unsupported and two employees who made charges on these cards were investigated by the Port's Police Department for misappropriating public assets: The Port's Aviation Maintenance Department charged \$1,676,833 to Port credit cards in 2004, about 39 percent of the Port's total annual credit card charges. In fall 2004, the Port's internal auditor reviewed these charges, noting \$233,469 in unsupported expenses charged to a card that supports the Air Cargo shops. After the audit ended, the Aviation Maintenance Department produced invoices supporting some of these charges. However, documentation for \$95,050 in expenses still was not available by the time the internal auditor issued her report in March 2005. Without invoices supporting these charges, the Port cannot demonstrate they were for a valid public purpose or that goods and services were received by the Port.

During 2004, the Port's Police Department investigated two employees working in the Aviation and Maintenance Department and referred those investigations onto the King County Prosecuting Attorneys Office:

- One employee purchased approximately \$1,200 in water pressure equipment using the Port's credit card and sold the items to other employees. This employee reimbursed the Port for these items. Charges have not been filed against this employee.
- A second employee misappropriated approximately \$10,000 in Port supplies and equipment for his personal use. This employee purchased some of these items using the Port's credit card. The Port recovered these supplies and equipment or obtained reimbursement from the employee, who no longer works for the Port. The former employee pled guilty to charges brought against him and was convicted.

The Port was not reimbursed \$300,000 it paid to sponsor an international sporting event that was cancelled: The Port contributed \$300,000 to the Seattle Organizing Committee for the Pacific Rim Sports Summit. The Port's Executive Director, who sat on the Board of this Committee, approved \$50,000 of this amount. The Port paid that \$50,000 in June 2004 and \$250,000 in January 2005. The expenses were initially classified as "other contractual services" even though no contract or agreement to provide services to the Port was in place. The Port later reclassified the \$250,000 to its trade development expense account. The event was cancelled in April 2005. The Port did not receive a refund, nor did it have a contract with the organization stating the amount it could expect to recover if the event was cancelled. The Port indicates it has made efforts to collect these amounts but lacks documentation to demonstrate those efforts. Moreover, the Port paid for unspecified services that it never received.

Expenditures totaling \$18,500 are not within the Port's authority to make and are gifts of public funds: In 2004, the Port of Seattle made three payments that appear to be gifts of public funds and do not appear to be for a valid public purpose. We found no documentation demonstrating the public purpose of these expenditures or showing what services the Port

received for those payments. Article 8, Section 7 of the Washington State Constitution prohibits gifts of public funds.

The Port donated \$500 to the Seattle Art Museum in memory of a former Port Commissioner that passed away: The Port did not receive any goods or service in return for this expenditure.

The Port made two contributions totaling \$18,000 to the Housing Partnership, also known as the King County Housing Alliance: This organization sent a letter to the Port seeking a contribution. Our scan of Port e-mails indicate that a Port Commissioner, who serves on the Housing Partnership's Board of Directors, was making inquiries of Port staff as to why the contribution had not been made as of January 30, 2004. The Port states these are appropriate expenditures because they help the "poor and infirm," as referenced in Article 8, Section 7 of the State Constitution.

The Alliance's Web site describes the organization as an advocate for affordable housing that provides workshops and publishes a newsletter described as a "policy journal." The organization does not provide housing.

Other local governments have the authority to provide services such as education, health and housing which are beneficial to the poor. However such services are outside of those authorized by the Legislature for Washington State ports.

The Port lacks documentation to demonstrate how \$13,000 coded to the promotional hosting, trade development and community relations accounts promotes the Port's business, promotes its trade and industrial development, or promotes its properties, utilities and facilities: In 2004, the Port spent \$1.5 million on promotional hosting, trade development and community relations expenditures. We examined 20 vouchers supporting a selection of expenditures coded to these expense accounts and found the following:

The Port contributed \$2,000 to the Salmon Homecoming Alliance and coded the cost to its community relations account. The records supporting the expense state the Port will benefit by educating the public about salmon restoration. However, the Port does not have authority to educate the public about salmon. The records do not demonstrate what the Port received in exchange for this contribution. Nor do the records explain how this cost provides for the proper promotion, advertising, improvement and development of such port properties, utilities and facilities.

The Port contributed \$2,000 to the National Wildlife Federation to sponsor the Tukwila Habitat Fair and coded the cost to the trade development account. Port records do not demonstrate how this expenditure fosters continued or increased trade or tourism in the region or use of the Port's facilities, programs and/or services.

The Port paid Seattle School District \$5,000 and coded the cost to its promotional hosting account. Port records indicate the payment was a sponsorship of a World Basketball Invitational Tournament hosted by Seattle School District and the benefit was to promote positive community relations. The Port's records do not demonstrate how this expenditure promotes the Port's business, trade and industrial development nor does the documentation explain what the Port received for this payment. The Washington State Auditor's *Budgeting, Accounting and Reporting Manual* for Ports states: "promotional hosting must be explicitly related to promoting trade and industrial development"

The Port contributed \$1,000 to the Bellevue Schools Foundation 2004 "Spring for Schools Luncheon" and \$3,000 to the Bellevue Boys and Girl's club. These expenditures were coded to the trade development expense account. Port records do not demonstrate how these payments "foster trade or tourism in the region or make use of the Port's facilities, programs and/or services," as described in the Port's policy on trade development expenditures. The Port stated

the contributions were made to assist underprivileged children. Other local governments have the authority to provide services such as education, health and housing which are beneficial to the poor. However such services are outside of those authorized by the Legislature for Washington State ports.

The Port paid \$49,208 to artists in advance of services rendered: In October 2004, the Port made advance payments to four artists for signing a contract to provide works of art for the newly renovated airport. These payments totaled \$49,208. The Port stated these payments provided the artists with money to pay for materials to begin their work, because artists "typically do not have available funds." The contract with each artist states payments will be made upon issuance of the contract, then upon 50 percent completion, then upon 100 percent completion of the fabrication and the balance when installation occurs. At the time the payments were made, no services had been received by the Port or provided by artists.

The Port spent \$10,000 for a community relations event that excluded the community: The Port of Seattle opened its new Concourse "A" facilities at Seattle-Tacoma International Airport in June 2004. Opening celebrations included an invitation-only event attended by state and local government officials, airport business executives and airport vendors. Those attending were in positions to influence or control decisions regarding trade or development for the Port. The \$10,000 paid for a musical performance by a brass ensemble from the Seattle Symphony.

Although the general public was not invited to this event, the Port charged this expenditure to its community relations account. Community relations expenditures are directed toward the general public and are undertaken to increase public knowledge about the Port and its role as a port district. This invitation-only event was not intended to inform or educate the general public about the Port, its role or its facilities, programs or services. According to the Port's records this expenditure was made to, "improve relations with surrounding governments and local/national and state business leaders." This purpose seems inconsistent with the Port's definition of a community relations expenditure.

Cause of Condition

The Port sometimes assists other organizations in the community or otherwise participates in community events in ways that are outside of its authority.

Effect of Condition

When Port revenues are used for unallowable purposes, taxpayers do not receive the full intended benefit of those revenues.

Recommendation

We recommend the Port:

- Require its employees who make purchases using Port credit cards to maintain records that clearly demonstrate the appropriateness of those purchases and the goods and services received.
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- Examine expenditures in greater detail before approving them for payment. We also recommend the Port not make expenditures without ensuring those expenditures do not violate state constitutional restrictions against gifting public funds.
- Manage its risk when making expenditures for the purpose of promotion by entering into contracts that specify the services the Port will receive. We also recommend the Port seek recovery of the public resources it contributed to the international sporting event, possibly including legal actions or the use of a collection agency.

- Carefully assess the nature of its promotional hosting and trade development expenditures to ensure they are authorized Port expenditures under state law and Port policy.
- Discontinue paying vendors before services have been rendered.
- Maintain all documentation necessary to support its expenditures.

Port's Response

"Credit card charges totaling \$95,050 were unsupported and two employees who made charges on these cards were investigated by the Port's Police Department for misappropriating public assets . . ."

- *Port policy requires retention of documentation to support all procurement made with credit cards. The Port Internal Auditor proactively tests compliance in operating divisions to various Port policies, which identified the challenges experienced with receipt retention at the Aviation Maintenance operations. Aviation Maintenance took immediate steps and located many of the missing records, although some were ultimately not found. Moreover, Aviation Maintenance immediately instituted controls to ensure that records supporting all procurement credit card purchases are retained and readily available.*

Use of public funds

- *The position of the State Auditor's Office represents a major shift in policy. For decades, the Port has selectively reinvested small portions of its gross income back into the community that it serves and from which it draws its support. These expenditures are no different (but much smaller in magnitude) than those undertaken by other municipal entities within the same community. The Port has continuously understood that it is granted the power and authority to make these investments by virtue of Article VIII, Section 7 of the Washington State Constitution. Indeed, the Washington State Supreme Court -- in a case challenging the Port's authority to make other expenditures under the same Constitutional provision -- stated expressly: [Article VIII, Section 7] specifies the purposes for which public money or property may be given away--the necessary support of the poor and infirm. State ex rel. O'Connell v. Port of Seattle, 65 Wn.2d 801, 804, 399 P.2d 623, 625 (1965). Although the Port acknowledges that these expenses do not fall squarely within any authority expressly granted by Title 53 of the Revised Code of Washington, the Port has never understood -- and the State Auditor's Office has never indicated -- that the provisions of Title 53 do not imply, or actually operate to limit, the power stated by the Supreme Court in the O'Connell decision.*
- *In reference to the payment made to the Seattle Organizing Committee (SOC) for the Pacific Rim Sport Summit, further clarification is provided that the SOC has no assets but has filed a claim against the United States Organizing Committee. The parties have agreed to mediation of the claim. It is unclear whether the Port will stand as a sponsor, as distinguished from a creditor. The Port intends to send a letter to the attorney handling the SOC claim, providing notice that the Port is an interested party in the recovery.*
- *In reference to the specific payments noted in the findings, we suggest further dialog to facilitate better understanding as to the purpose of the expenditures and their relationship to Port business. As examples:*
 - *The payment to the Seattle Public School District for the World Basketball Invitational Tournament was made to support the hosting of an international basketball tournament of Chinese amateur players. The tournament has been*

hosted throughout the world at different sites. The tournament brought amateur players, their coaches, families and supporters from around the world with the majority from China. The tournament and associated activities occurred over several days increasing economic activity in the Port district through air and ground transportation, hotel accommodations, restaurants and the entertainment industry. The sponsorship was important for international tourism promotion and building important trade relationships with China, an emerging trade partner to the Port of Seattle.

- *On the payment made to the Seattle Symphony for the SeaTac Airport Concourse A Grand Opening, those invited and in attendance were in positions to influence or control decisions regarding trade or development for the Port. Therefore, the expenditures were appropriately for the support of an event tied to the promotion of trade and development.*

“\$49,208 was paid to artists in advance of services rendered . . .” (reference to four artists commissioned to provide works of art for the Airport renovation.)

- *Artists were commissioned to provide works of art related to the renovations of SeaTac Airport. Monies were advanced to the artists to pay for materials to cover their cash flow needs. The commissioned works of art were completed and delivered to the Port.*

General recommendation - “Maintain all documentation necessary to support its expenditures.”

- *Port policy requires the retention of documentation to support all expenditures. Administrative protocols are in place to facilitate review for compliance. Any incidence of departures from this policy will be immediately addressed.*

Auditor’s Remarks

The Port indicates our audit report finding is a “major shift in policy”. However, in a March 2003 letter to Port Commissioners, our Office made the following recommendations:

. . . We noted the Port had not clearly demonstrated how several [community relations] expenditures promoted tourism, or promoted, advertised, improved, or developed Port properties, utilities and facilities.

Many of these expenditures involved donations, typically through sponsorships or attendance at fund-raising events, to foundations or associations for local school districts, universities and other community organizations.

We recommend the Port revise its policy to require documentation for all its community relations expenditures that clearly demonstrates how the expenditures promoted tourism, or promoted, advertised, improved, or developed Port properties, utilities and facilities. This policy should further require central monitoring over these expenditures to ensure that the Port is receiving and demonstrating the promotion of tourism, or the promotion, advertisement, improvement, or development of Port properties, utilities and facilities.

Our recommendations mirrored RCW 53.08.160, 53.08.255, and RCW 53.36.130, which are listed below.

Also, the Port appears to argue that *State ex rel. O’Connell v. Port of Seattle*, 65 Wn.2d 801, 804, 399 P.2d 623, 625 (1965) authorizes the Port to selectively [reinvest] small portions of its gross income back into the community that it serves and from which it draws its support.

However, that case focused on the narrower question of whether the Port of Seattle may spend money on promotional hosting, as authorized by Amendment 45 to the State Constitution and RCW 53.36.130. We are not challenging the Port's authority to spend money on promotional hosting.

Ports, as municipal corporations, are limited in their powers to those necessarily or fairly implied in powers expressly granted, and those essential to the declared purposes of ports. Port of Seattle v. Washington Utilities and Transportation Commission, 92 Wn. 2d 789, 794 -95, 597 P.2d 383 (1979) Port expenditures must remain within the powers expressly or impliedly granted to ports in statute.

We thank the Port for the assistance we received during the audit.

Applicable Laws and Regulations

The Port's Community Relations Policy states:

Community Relations expenditures are typically directed toward the general public. Community Relations expenditures are not generally undertaken with the intention of fostering continued or increased use of the Port's facilities, programs and/or services. Instead, Community Relations expenditures are undertaken to increase public knowledge about and/or support for the Port, its role in the port district or its facilities, programs and/or services.

The Port's Trade Development Policy states:

Trade Development expenditures are costs and expenses incurred by the Port to promote trade or tourism in the region or to advertise, promote or increase awareness of Port facilities, programs or services. Trade Development expenditures are focused towards persons who may, either directly or indirectly, foster trade or tourism in the region or make use of the Port's facilities, programs and/or services. Trade Development expenditures are undertaken with the specific intention of fostering continued or increased trade or tourism in the region or use of the Port's facilities, programs and/or services. Although the causal link between a particular Trade Development expenditure and any continued or increased trade, tourism and/or use of Port facilities, programs or services may be indirect or difficult to establish, expenditures for Trade Development are undertaken only when it is estimated that the potential business benefit outweighs the cost . . .

The Port's Community Relations and Trade Development Policies are in part based on RCW 53.08.160, which reads:

RCW 53.08.160 Studies, investigations, surveys--Promotion of facilities.

All port districts organized under the provisions of this act shall be, and they are hereby, authorized and empowered to . . . make such expenditures as are necessary . . . for the proper promotion, advertising, improvement and development of such port properties, utilities and facilities . . .

RCW 53.08.255 discusses how Ports may spend monies to advertise and distribute information to attract visitors and encourage tourism

Any port district . . . has power to expend moneys and conduct promotion of resources and facilities in the district or general area by advertising, publicizing, or otherwise distributing information to attract visitors and encourage tourist expansion.

The Port's Promotional Hosting Policy reads:

What are the acceptable purposes for promotional hosting?

The Port Commission has identified the approved objects of promotional hosting to be:

Marketing an individual or organization on the use, continued use or increased use of Port services, facilities or properties.

Persuading individuals or organizations to donate, supply or sell to the Port on the best available terms;

Persuading individuals or an organization to purchase, lease or contract from or with the Port on terms most favorable to the Port; or

Persuading individuals or an organization to assist the Port in fostering the increased use of its services and facilities by improving transportation schedules, adding to existing transportation services and facilities, adjusting rates, improving navigation, and generally increasing and improving the scope and efficiency of Port operations.

Thus, promotional hosting is generally undertaken to develop business or foster goodwill between a customer, supplier or trade partner (whether current or potential) and the Port . . .

RCW 53.36.130 Expenditures for industrial development, trade promotion, or promotional hosting--Source and amount of funds.

Funds for promotional hosting expenditures shall be expended only from gross operating revenues and shall not exceed one percent thereof upon the first two million five hundred thousand dollars of such gross operating revenues, one-half of one percent upon the next two million five hundred thousand dollars of such gross operating revenues, and one-fourth of one percent on the excess over five million dollars of such operating revenues: PROVIDED, HOWEVER, That in no case shall these limitations restrict a port district to less than twenty-five hundred dollars per year from any funds available to the port.

RCW 53.36.150 Expenditures for industrial development, trade promotion, or promotional hosting--Duties of state auditor.

The state auditor shall, as provided in chapter 43.09 RCW:

(1) Audit expenditures made pursuant to RCW 53.36.120 through 53.36.150; and

(2) Promulgate appropriate rules and definitions as a part of the uniform system of accounts for port districts to carry out the intent of RCW 53.36.120 through 53.36.150: PROVIDED, that such accounts shall continue to include "gross operating revenues" which shall be exclusive of revenues derived from any property tax levy except as provided in RCW 53.36.130.

The Washington State Auditor's Budgeting, Accounting and Reporting Manual for Ports contains the following rules for promotional hosting.

Promotional hosting means furnishing customary meals, refreshments, lodging, transportation or any combination of those items in connection with: business meetings, social gatherings, and ceremonies honoring persons or events, relating to the authorized business promotional activities of the port. Hosting may also include reasonable and customary entertainment, and souvenirs of nominal value, all incidental to such events.

Promotional hosting must be explicitly related to promoting trade and industrial development . . .

RCW 42.24.080 - Municipal corporations and political subdivisions--Claims against for contractual purposes--Auditing and payment--Forms--Authentication and certification.

All claims presented against any county, city, district or other municipal corporation or political subdivision by persons furnishing materials, rendering services or performing labor, or for any other contractual purpose, shall be audited, before payment, by an auditing officer elected or appointed pursuant to statute or, in the absence of statute, an appropriate charter provision, ordinance or resolution of the municipal corporation or political subdivision. Such claims shall be prepared for audit and payment on a form and in the manner prescribed by the state auditor. The form shall provide for the authentication and certification by such auditing officer that the materials have been furnished, the services rendered or the labor performed as described, and that the claim is a just, due and unpaid obligation against the municipal corporation or political subdivision; and no claim shall be paid without such authentication and certification

Article VIII, Section 7 of the Constitution of the State of Washington states:

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.