



Washington State Auditor's Office

Troy Kelley

Independence • Respect • Integrity

2013 Annual Report

March 26, 2014

Message from State Auditor Troy Kelley:

In my first year in office as Washington State Auditor we have built a solid senior management team committed to our mission of holding state and local government accountable for the use of public resources. Guiding us toward our vision of “government that works for citizens” are our organizational values of independence, respect, and integrity.

We hold ourselves accountable for our use of public resources as well, using Lean principles to streamline our administrative and audit processes and efficiently managing data, using it to measure and improve our performance.

It has been an exciting, challenging first year, as we have built the team, ethic and expectations for the years ahead. State and local governments provide essential services and opportunities for individuals, families, organizations and businesses across Washington. Public trust is built on the knowledge that government is operating as efficiently, openly and successfully as possible. I understand and respect the essential role our Office plays in providing that knowledge to the public.

Troy Kelley,



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2013 – A year of leadership and innovation

The State Auditor’s Office is responsible for auditing all units of government in Washington, which puts us in a unique position to not only see where financial, compliance, or performance problems exist, but also to provide recommendations, training, and guidance to help government officials fix these problems.

In 2013, the Washington State Auditor’s Office completed the first year under the leadership of the state’s 10th State Auditor, Troy Kelley, the first new state auditor in 20 years. Kelley, a former Washington state legislator, took office in January 2013.

The year that followed was marked by realignment and role changes aligned with Auditor Kelley’s individual philosophy of transparency and a listening, cooperative, relationship-based audit process that encourages improvement. It has been a time of reflection and fine-tuning in a Lean-driven environment focused on making better government the bottom line.

Auditor Kelley led the agency to development of a new vision: “Government that works for citizens,” in pursuing its mission of holding state and local government accountable for the use of public resources.

To build toward that vision and accomplish that mission, the State Auditor’s Office has laid out some [strategic goals](#). We want to help governments work better, cost less and deliver high value, so they can earn greater public trust. To succeed, we need to improve our own audit quality and operational efficiency, and develop highly engaged and committed employees in our agency.

A team of widely experienced veteran staff members and leaders have been joined by an inspired, motivated new group of professionals who come to us from college, the private sector and other state and local government agencies. It’s a combination of expertise, depth and enthusiasm that will set the standard for continued team building across the agency. They are supported by solid training, sound mentoring and commitment to making a difference in their community and their state.

Auditor Kelley, an attorney and officer in the National Guard, has made it clear that it is not enough to simply audit governments. The agency needs to use what it learns in audits of governments to help them improve, helping them find solutions and emulate best practices.

We do more than audit; we make a difference.

With all that in mind, in 2013 Auditor Kelley and his executive team:

- Used Lean strategies across the agency to improve efficiency and reduce costs
- Expanded the [Local Government Performance Center](#)
- Secured passage of legislation returning full subpoena authority for the agency
- Established a notification protocol to allow local officials ample time to incorporate any audit rate changes in their budget process
- Refined the online filing process for local governments
- Increased the number of performance audits conducted
- Increased the agency’s legislative presence
- Improved timeliness of [Whistleblower](#) investigations
- Reorganized the [Fraud](#) program
- Improved the [Citizen Hotline](#) process
- Redesigned the agency [website](#), adding social media presence to expand transparency and accessibility

Local Government

The Washington State Auditor’s Office takes very seriously our statutory responsibility to examine the financial affairs of all local governments statewide. There are more than 2,284 individual local governments located statewide, covering 36 government types including; cities, counties, school districts, ports, fire districts, public utility districts, and many more. In 2013, our Office conducted 2,095 audits of local government. The number of reports released by audit type is as follows:

Number of reports released by audit type	
Accountability	1,196
Financial and Federal	461
Financial	398
Special	21
Investigations	14
Federal Program	5
Total	2,095

Top areas of audit concern for local governments

We are using the broad issues and patterns identified in our audits to develop resources to help all levels of government work better and smarter. The top areas of concern identified by our audits of local government in 2013 were:

- *Lack of internal controls over accounting and financial reporting*
- *Lack of internal controls over cash receipting and expenditures*

The lack of internal controls accounted for approximately 39 percent of all significant audit issues reported by the State Auditor’s Office. As a result we compiled a self-assessment checklist for local governments (available on our [Local Government Performance Center Resource Page](#)) to assess their own internal control environment for accounting and financial reporting. Additional resources provide guidance in placing controls where weaknesses are perceived.

- *Declining financial condition*

In the last few years, local governments have faced a daunting economic environment. Since we released the first financial condition audit summary to highlight local government financial distress in November 2012, problems continue to persist. In response we have begun work on tools to help local government officials assess their government’s condition so that they can respond to financial threats as early as possible. (See our Local Government Performance Center Resource Page.)

- *Non- compliance with federal grants*

Many local governments struggle with ensuring compliance with the many requirements that accompanying receiving federal grants. Our website has guidance for local governments on the basics of federal grant management including links to helpful checklists, best practices and federal guidance links. Additionally, each year the State Auditor’s Office partners with the Washington Finance Officers Association to provide six classes on the basics of grant management; explaining what grants are all about and giving an overview of general grant requirements along with identifying common areas of audit concern.

- *Procurement, bid and prevailing wage*

The laws governing bidding can be quite complicated. On our Local Government Performance Center Resource Page we have provided a tool that provides a broad overview of the basics of bid law. In addition, each year the State Auditor’s Office partners with Labor and Industries to provide classes around the state focused on educating state and local employees on procurement, bid law and prevailing wage requirements.

Audits of School District Alternative Learning Experience Programs

In 2011, the Legislature passed ESHB 2065 requiring school districts that purchase services or activities for students in ALE programs must provide services or activities “substantially similar” to those available to students in their regular schools. During 2013, we conducted an audit to:

- Determine compliance with new “substantially similar” spending requirements
- Assess how well districts complied with enrollment reporting requirements

Our audit questioned more than \$1.5 million of the \$3.6 million spent by the 12 districts tested for “substantially similar” spending requirements. Additionally, for the 10 districts tested for enrollment reporting we found an average error rate of 45 percent. Find details of our audit results and recommendations in a separate report on the [Schools page of our website](#).

Local government financial reporting system

By statute all local governments are required to report their revenues and expenditures to us within 150 days after their fiscal year end. For the last 10 years, our Office has made this data available on our website in the Local Government Finance Reporting System. We strive to publish this data well before the Legislative Session begins to make it available to all interested parties. As part of the effort to publish the data quicker, we developed an online report filing system for local governments to submit this financial information to us.

Online filing is not required for local governments, however we strongly encourage

2013 filing statistics	Reports filed online	Reports filed offline	Non-filers	Total
The number of local governments	1,008	468	422	1,909

it. It makes filing easier, quicker and ensures required schedules are filed using the latest versions. In 2014 we are under taking significant outreach to encourage all local governments to file online, with the goal of having all local governments filing online by fiscal year 2015.

Local Government Performance Center

It is exciting to be able to help governments through the work we do, not just point out the problems we find. The Local Government Performance Center was established to do just that.

The Center helps local governments solve problems, reduce costs and improve the value of their services to citizens by offering resources such as training, tools and technical assistance. For example, after an intensive analysis of its process through the Center's Lean Academy, Whatcom County reduced the time it takes to issue a single-family home building permit from 31 days to nine.

We are also using the broad issues and patterns identified in fraud investigations to inform/develop training through the Local Government Performance Center.

Shared broadly, this information and training can help local governments reduce costs, improve results and continue to earn greater public trust. Over time, we hope to be able to help more local governments more quickly and more economically than with individual audits.

In 2013, about 2,300 local government leaders and staff took part in training. Of those who attended the training, 90 percent shared positive evaluations and almost all said the training would help improve efficiency or reduce costs. We also reached more than 800 people through more general presentations at local government conferences in 2013.

Visit the Center on our website at: www.sao.wa.gov/local/Pages/LGPC.aspx

State Government

Comprehensive Annual Financial Report (CAFR)

We completed the 2013 CAFR audit, which covered the year ended June 30, 2013 and issued our “unqualified” opinion on the report in November. The “unqualified” opinion means that in our professional judgment these financial statements fairly present the state’s financial position.

Each year, following this audit, we also publish a CAFR Summary, which is a five- to 10-page document that serves as a “snapshot” of the state’s financial position, including revenues, expenditures, cash balances, and debt. The summary points out highlights of the lengthy financial statements. It also highlights some of the financial challenges facing the state including the unfunded liabilities associated with workers compensation supplemental pension COLA’s, state pension systems, post-employment benefits, and the Guaranteed Education Tuition Program.

The 2013 CAFR Summary can be found [here](#).

Statewide Single Audit (Federal Compliance Audit) 2013

Through this process, we audit to determine whether state agencies comply with federal grant requirements in spending the large amounts of federal dollars they receive. By the State Auditor’s Office conducting this audit, we are able to avoid duplication of efforts (and costs) between federal and state auditors.

We conducted the 2012 Single Audit for the State and provided our audit opinions as well as audit findings and questioned costs to the Office of Financial Management in March 2013 so they could meet their March 31, 2013 reporting deadline; and we are currently completing the 2013 audit.

We did report some significant deficiencies in internal controls and compliance; we issued 63 federal audit findings, a significant increase from the prior year; and we questioned \$4 million in federal expenditures.

We also issued a 16-page Single Audit Summary in 2013 to present the highlights from the federal compliance audit. [This summary](#) provides a reader with a high level statistics and key conclusions from our Single Audit.

Accountability Audits 2013

We performed an audit of credit card use by state universities. This audit examined whether state universities had effective internal controls on the use of state-issued credit cards. While in most cases internal controls were in place and credit cards were used for allowable purchases, we found that cards were used to make more than \$225,000 in purchases prohibited by state policies for alcohol, gifts and other items.

We performed an audit of tuition waivers awarded by colleges and universities. This audit was performed to determine if students receiving tuition waivers met eligibility criteria and to verify colleges and universities awarded waivers to students that did not exceed the maximum levels established by state law and policy. We found that while tuition waivers were awarded to eligible students for amounts that were within the maximum levels, we estimate colleges and universities awarded \$71.7 million in tuition waivers with inadequate documentation to support either initial or on-going student eligibility.

For 2014, we will be doing audits of local funds under the control of state agencies. Local funds are monies that are under a state agency’s control but are not deposited with the State Treasurer.

Energy

Approved by voters in 2006, the Energy Independence Act, also known as Initiative 937, requires electric utility companies in the state to invest in renewable energy sources and energy conservation programs. The Act applies to all electric utilities that serve more than 25,000 customers in the state. Of the 17 qualifying utilities, we have authority to audit 12 municipal utilities.

We have issued all but two of the compliance reports for the 2010-2011 conservation and the 2012 renewable energy compliance periods. Specific to the reports already issued, all utilities were in compliance with both their conservation and renewable energy targets. We expect to complete the two remaining audits during the first quarter of 2014.

Results of these audits are available online on the [Energy](#) page of our website.

Performance Audit

The Performance Audit division's work includes a blend of long-term audits of major state programs, as well as shorter-term evaluations designed to give policymakers options with which to meet the state's challenges. They also reflect our goal of helping governments work better and cost less, while delivering higher value and earning greater public trust.

Performance audits released in 2013:

- [Washington State Ferries: Vessel Construction Costs](#)
 - We found it costs more to build a ferry when Washington State Ferries is the purchaser, for two primary reasons.
- [Enhancing Background Checks in Washington](#)
 - Washington could improve safety of children and vulnerable adults by retaining fingerprints and implementing an automated background check service.
- [Creating a 21st-century Financial Management System](#)
 - Washington's current financial management system, which administers multi-billion-dollar budgets, is not meeting the state's needs.
- [Washington's Tolling Program: Lessons Learned from Project Delays](#)
 - Lessons learned from the State Department of Transportation's State Route 520 tolling project, which experienced delays in implementation.
- [Developmental Disabilities in Washington, Increasing Access and Equality](#)
 - Of approximately 35,000 people who are eligible and have applied for state developmental disabilities services, 12,000 receive full services, 7,800 receive only partial or limited services, and 15,000 receive no services.
- [Developmental Disabilities Administration: Improving payment systems](#)
 - \$11 million in questionable payments, \$5.5 million in unauthorized payments, safety concerns over caregiver background checks.
- [Regulatory Reform: Improving Permit Timeliness](#)
 - State agencies could shorten the time it takes to submit, review and make decisions on business permit applications through simple improvements.

Since we issued our first performance audit in 2007, governments report they saved nearly \$1 billion as a result of implementing our recommendations. Over our standard four-year tracking period, agencies reported implementing about 84 percent of our issued recommendations, resulting in almost \$780 million of actual savings. We expect additional savings as governments adopt our ongoing performance audit recommendations.

Special Investigations

In the first three months of his term, State Auditor Kelley secured legislation from his former colleagues that returned full subpoena power to our Office. The State Auditor's Office renewed subpoena power is a significant tool in allowing us to reduce the cost and improve the timeliness of our investigations.

The State Auditor's Office conducts three types of investigations:

Fraud

In 2013, we reported on 59 investigations of misappropriation from local and state governments totaling \$1,021,759. (See chart below for display of this total misappropriation by category)

Misappropriation type	Value
Cash receipting	\$183,750
Payments	\$375,213
Payroll	\$414,730
Other	\$48,066
Total	\$1,021,759

One of our largest investigations was at a water district where we found \$352,641 of misappropriations through various schemes.

Our Office also performs an extensive amount of educational outreach by providing presentations and trainings throughout the state at government accounting and auditing professional association conferences. This training utilizes the results of our investigations as case studies to show how fraud risk increases due to the lack of oversight by management and strong policies, procedures and proper internal controls. In addition, we are using the broad issues and patterns identified in our investigations to develop additional resources through our Local Government Performance Center to help all levels of government work better and smarter.

Citizen Hotline

The Washington State Auditor's Office operates a hotline for citizens and government employees to report assertions of government fraud, waste and abuse. It is also a place to report government efficiency or outstanding achievement.

In 2013, we received 433 hotline reports and opened investigations into 418 of them.

Hotline submissions are typically received through SAO's website. However, if individuals want to leave a voice message about their concern, they can call our toll-free hotline at 1-866-902-3900.

Whistleblower Program

Enacted by the Washington State Legislature, the Whistleblower Act provides an avenue for state employees to report suspected improper governmental action.

Of the 146 assertions received in 2013, we opened cases on 18 of them.

Of the 18 cases we opened in 2013, we issued reports on 15 of them. In eight cases we found reasonable cause to believe an employee had engaged in improper government action.

Quality Assurance

It's reasonable to ask "Who audits the auditor?"

We are committed to continuously improving how efficiently we carry out our business, and hold ourselves to highest standards of quality in the audit work we do. We do it because it's right, and because we know Washington citizens expect no less of us.

Our Office is subject to external peer reviews every three years to ensure our audits satisfy government auditing standards. The peer reviews are conducted by the National State Auditors Association (NSAA) with the National Association of State Auditors, Comptrollers and Treasurers (NASACT).

SAO received a "clean opinion" on its [2013 external peer review](#). The reviewers concluded the Office had a well-designed quality control system, and applicable audit policies and standards were complied with in almost all cases. SAO does so many different types of audits across so many different teams that it takes a concerted effort by everyone involved to maintain such a high standard of quality.

We are also audited by the Washington State Office of Financial Management.

We are also audited every two years by an independent public accountant under contract with the Office of Financial Management (OFM). This Cabinet-level agency provides information, fiscal services and policy support to the Governor, Legislature and state agencies. Such audits generally focus on our administrative operations.

Like all state agencies, we are required to report on how we plan to resolve any audit issues, and the Director of Financial Management issues an annual report on the audit resolution status. These reports are available to the public on the OFM website at www.ofm.wa.gov.

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