



## STATE OF WASHINGTON

November 25, 2019

The Honorable Jay Inslee  
Governor of Washington  
P.O. Box 40002  
Olympia, WA 98504-0002

Members of the Washington State Legislature  
Legislative Building  
Olympia, WA 98504-0600

Dear Governor Inslee and Members of the Legislature:

State law (RCW 39.26.220<sup>1</sup>) requires the State Auditor and Attorney General to annually give the Governor and the policy and fiscal committees of the Legislature a collaborative report on state agency contract audit and investigative findings, enforcement actions, and status of the state agency resolution.

This letter serves as our report of findings and actions taken on audits issued in fiscal year 2019, which spanned from July 1, 2018, through June 30, 2019.

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<sup>1</sup> <https://app.leg.wa.gov/RCW/default.aspx?cite=39.26.220>

## **STATE AUDITOR'S OFFICE**

### ***Performance Audits***

The Washington State Auditor's Office (Office) issued one performance audit report in fiscal year 2019 that dealt with contract-related issues.

#### **Contract Assurances for Vendor-Hosted State Information Technology Applications<sup>2</sup>**

On December 13, 2018, our Office issued a performance audit report that examined the adequacy of the security provisions included in contracts for vendor-hosted IT applications. We looked at seven contracts from five state agencies to assess how they ensure their vendors safeguard the applications and the data they hold. The audit's key findings included:

- Most of the contracts required vendors to comply with the state's general IT security standards, but only one required compliance with the agency's specific standards.
- Agencies could improve their monitoring practices by more consistently following leading practices, including more effectively using risk assessments, being more specific with compliance requirements, and more actively monitoring and verifying compliance.
- The Department of Enterprise Services (DES) could help agencies by including specific IT guidance in its contracting policies and procedures.

To address these key findings, we made several recommendations to DES to improve the guidance it provides to state agencies that contract for IT services. We also made recommendations to the Office of the Chief Information Officer (OCIO) to provide clearer guidance to agencies on how their vendors should comply with state security standards. Finally, we issued guidance to all state agencies to help them comply with state law and follow leading practices as they develop their contracts and monitor their vendors' performance.

### ***Fraud and Whistleblower Audits***

During fiscal year 2019, our Office issued two fraud reports that contained findings related to contracting issues.

#### **Department of Social and Health Services<sup>3</sup>**

On September 27, 2018, our Office issued a fraud-related audit report on the Department of Social and Health Services (DSHS) Developmental Disabilities Administration (DDA) program. This audit resulted from DSHS notifying our Office of four separate instances when it believed there was illegal activity involving client funds and DDA contracted supported-living providers. The contracted supported-living providers act as representative payees for DSHS clients who oversee all financial matters.

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<sup>2</sup> <https://portal.sao.wa.gov/ReportSearch/Home/ViewReportFile?arn=1022707&isFinding=false&sp=false>

<sup>3</sup> <https://portal.sao.wa.gov/ReportSearch/Home/ViewReportFile?arn=1022311&isFinding=false&sp=false>



After reviewing DSHS's investigations, we determined that \$19,639 of client funds was misappropriated from four contracted supported-living providers between April 2, 2015, and February 6, 2018. Although the misappropriations were a result of the contracted providers, DSHS is ultimately responsible for internal controls over the monitoring of contractors to protect its clients.

We recommended DSHS strengthen its internal controls over the monitoring of contractors by ensuring reconciliations of client funds are performed and then are reviewed by a secondary party, increasing frequency of client fund reviews, and ensuring that purchases made with client funds are supported with backup records.

DSHS created the following plan of resolution:

- Develop and offer a training that focuses on safeguards to prevent financial exploitation and theft
- Develop a CARE provider bulletin for all providers related to safe money management
- Provide optional templates that providers may use in creating Individual Financial Plans
- Continue tracking loss of client funds by supported contractors and ensure reimbursement occurs to each client
- Within staffing resources available, continue the review of client funds managed by the residential agencies and verify compliance with Washington Administrative Code 388-101D, which pertains to management of client funds

#### Office of the Attorney General<sup>4</sup>

The Office of the Attorney General (AGO) notified our Office regarding the potential loss of public funds by a nonprofit organization called the Washington Coalition of Crime Victim Advocates (Coalition). The Coalition had a grant agreement with the AGO to fund training, certification and technical assistance for crime victim service center advocates. Our Office investigated the Coalition and on April 29, 2019, issued a fraud report regarding the AGO. Invoices submitted for reimbursement by the Coalition to the AGO totaling \$199,978 were for expenses not incurred by the Coalition. Of these invoices, \$14,716 had been deleted in the Coalition's accounting records, and \$7,637 was a result of overbilled invoices.

We recommended the AGO continue to improve internal controls over grant agreement contracts, with specific guidance to:

- Obtain supporting payment documentation to compare with invoice records received to validate invoice information and billed amounts for services
- Ensure grant agreement deliverables and terms are met before distributing state administered grant funds

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<sup>4</sup> <https://portal.sao.wa.gov/ReportSearch/Home/ViewReportFile?arn=1023721&isFinding=false&sp=false>

The AGO recovered \$50,316 from the Coalition in August 2017. We also recommended that the AGO attempt to recover the remaining misappropriated \$149,662 and related investigation costs of \$23,517.05.

The AGO responded by explaining it immediately stopped making payments to the Coalition as soon as it suspected the fraud. The AGO stated it is doing everything in its power to recover the misused grant funds, and is committed to recovering all of the misappropriated public money. On March 5, 2019, the AGO referred this matter to law enforcement.

### *Compliance and Accountability Audits*

During fiscal year 2019, our Office issued four compliance and accountability audit reports that contained findings related to contracting issues.

#### Eastern Washington State Historical Society<sup>5</sup>

On July 12, 2018, our Office issued an accountability audit report on the Eastern Washington State Historical Society, known to the public as the Northwest Museum of Arts and Culture (Museum).

In this audit, we found that the Museum did not follow required state procurement laws while searching for vendors to help carry out its mission of engaging people in the appreciation of arts and culture. State law requires the Museum to solicit bids through a competitive process for any purchase of goods and services exceeding \$10,000 (excluding sales tax). The Department of Enterprise Services (DES) gave the Museum delegated authority of up to \$50,000 for purchases of goods and services, provided that the Museum follows state procurement laws.

We examined seven contracts that took effect during fiscal year 2017 and found the Museum paid five vendors \$187,145 without having contracts in place. One of these vendors received \$84,362, which exceeds the delegated procurement authority. The Museum also established two contracts that were not competitively procured, and did not post contracts into the state's contract database or state vendor registration and bid notification system. The Museum also did not adequately monitor these contracts, resulting in unsupported expenses for goods and services totaling \$23,226.

We recommended that the Museum strengthen its internal controls related to contracting by designating a contract manager to coordinate and oversee procurement and contract activities, track all active contracts, and ensure staff complete required contract training courses.

The Museum concurred with the audit findings and stated it will take the following steps to strengthen its compliance with state procurement and contract policies:

- Appoint a contract manager and more effectively monitor contracts
- Create a monitoring system that tracks employee training
- Establish internal policies and procedures relating to contracting

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<sup>5</sup> <https://portal.sao.wa.gov/ReportSearch/Home/ViewReportFile?arn=1021710&isFinding=false&sp=false>



Department of Ecology<sup>6</sup>

On July 19, 2018, our Office issued an accountability audit report on the Department of Ecology (Ecology) that contained a finding related to its internal controls over fee collections for the vehicle emission testing program that is administered by a contracted vendor, Applus.

We found that Ecology was verifying the amount of fee revenue deposited into the state's accounting system matched the amount shown on the invoices. However, it was not reconciling the supporting records to the invoices to ensure the fee revenue was accurate. We also found the vendor took invalid deductions the contract did not allow, totaling \$1,376.

We recommended Ecology:

- Improve its process for reviewing vendor invoices by reconciling supporting records to invoices to ensure it has collected all fee revenue
- Ensure staff responsible for performing the review understand a contract's terms and conditions
- Recover improper deductions made by the vendor

In its response, Ecology stated it will begin verifying supporting records for emissions testing invoices as part of its reconciliation process and ensuring the monthly vendor report is for the same period as weekly invoices. Ecology also stated it will work with the vendor and Department of Enterprise Services (DES) to determine which deductions the contract allows.

Department of Social and Health Services<sup>7</sup>

On August 23, 2018, our Office issued an accountability audit report on the Department of Social and Health Services (DSHS). This report contained a finding regarding its inability to ensure it properly accounted for and adequately supported payments made to its contracted vendor for payroll services. The audit found that:

- The contracted vendor for payroll services over-requested \$987,088 in wages, benefits, and payroll taxes during calendar year 2017. Of that amount, over \$750,000 was attributable to Federal Insurance Contribution Act (FICA) refunds and adjustments.
- Uncashed checks totaling \$376,726 were over 180 days old as of December 31, 2017. Of that amount, \$210,966 was funded by Medicaid and had not been returned to the grantor.
- In some instances, individual providers, taxing authorities, and union trusts were overpaid. DSHS has established a list of potentially overpaid claims, but the IPOne electronic payment system has been unable to process overpayment adjustments since implementation.
- The vendor did not file all required State Unemployment Tax Act (SUTA) returns or pay unemployment taxes on behalf of DSHS.

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<sup>6</sup> <https://portal.sao.wa.gov/ReportSearch/Home/ViewReportFile?arn=1021796&isFinding=false&sp=false>

<sup>7</sup> <https://portal.sao.wa.gov/ReportSearch/Home/ViewReportFile?arn=1021987&isFinding=false&sp=false>

We recommended DSHS:

- Request the vendor refund its \$987,088 overpayment
- Consult with its federal grantor about whether it must repay the federal portion of the uncashed checks
- Continue to work with the vendor to obtain information needed to properly reconcile and account for public funds, and to implement system modifications
- Ensure the vendor files SUTA returns and pays unemployment taxes for individual providers

In resolution, DSHS worked with the vendor to recover \$847,591 in FICA refunds. DSHS will now request payment reconciliation information directly from the taxing entities and trusts, because the vendor could not provide adequate information. The vendor stated it hoped to have an automated financial reconciliation report developed by the second quarter of 2019. DSHS is also working with the vendor to create a process to return the funding of uncashed checks back to them and the federal portion to Medicaid. Last, DSHS is working with the vendor to ensure it receives the information needed to reconcile all payments made to the vendor, all SUTA returns are filed, and payments are made for unemployment taxes.

#### Traffic Safety Commission<sup>8</sup>

On September 20, 2018, our Office issued an accountability audit report on the Traffic Safety Commission (Commission) that contained a finding related to a lack of internal controls over contract monitoring.

During fiscal years 2015-2018, the Commission spent \$8,942,520 on contracts to help perform its mission of keeping Washington roads safe, including trainings and outreach to reduce traffic injuries and fatalities. The audit tested eight of these contracts and found five instances when payment amounts in the general ledger of the Agency Financial Reporting System (AFRS) did not match those recorded in the contract sub-ledger, totaling \$457,000. The testing also found a contract amendment of \$65,000 that did not go through the competitive solicitation process.

We recommended that the Commission:

- Regularly reconcile AFRS, supporting records, and the contract invoice sub-ledger to ensure effective project management
- Develop a process for updating written policies and procedures to ensure they align with current state law, and implement controls to monitor changes to state law. Further, the Commission should have program managers train through the Department of Enterprise Services.

The Commission acknowledged there was no reconciliation between payments in AFRS for vendor contracts and the sub-ledgers maintained by the Finance Director. The Commission stated the Fiscal Analyst 5 now will perform this reconciliation and have it reviewed by the Office Assistant 3, who will report discrepancies to the Finance Director. The Commission also agreed to implement changes to prevent procurement violations, such as the \$65,000 contract amendment.

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<sup>8</sup> <https://portal.sao.wa.gov/ReportSearch/Home/ViewReportFile?arn=1022086&isFinding=false&sp=false>



### ***Financial and Federal Audits***

During fiscal year 2019, our Office issued one financial and federal audit report that contained findings related to contracting issues.

#### Washington State Fruit Commission<sup>9</sup>

On December 27, 2018, our Office issued a financial and federal audit report on the Washington State Fruit Commission (Commission) that determined it had inadequate internal controls in place to ensure compliance with federal procurement requirements.

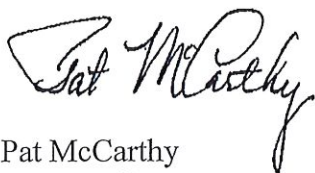
This finding resulted directly from the Commission not having records to support that a \$150,000 contract for advertising was procured through competitive proposals, and did not have a request for proposals that indicated the scope of work or the criteria for which the vendor would have been evaluated.

We recommended the Commission establish internal controls to ensure it procures vendor contracts following federal requirements. The Commission responded by agreeing to implement a process in which a request for proposals will be formally advertised when a contract exceeds \$100,000.

### **ATTORNEY GENERAL'S OFFICE**

The State Auditor's Office issued no audit or investigative findings related to contracting that required referrals to the Office of the Attorney General for enforcement.

Sincerely,



Pat McCarthy  
State Auditor



Bob Ferguson  
Attorney General

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<sup>9</sup> <https://portal.sao.wa.gov/ReportSearch/Home/ViewReportFile?arn=1022916&isFinding=false&sp=false>