



Washington State Auditor's Office

Independence • Respect • Integrity

Whistleblower Investigation Report Department of Transportation

Published July 30, 2015

Report No. 1014716





Washington State Auditor's Office

July 30, 2015

Lynn Peterson, Secretary
Department of Transportation

Report on Whistleblower Investigation

Attached is the official report on Whistleblower Case No. 15-004 at the Department of Transportation.

The State Auditor's Office received an assertion of improper governmental activity at the Agency. This assertion was submitted to us under the provisions of Chapter 42.40 of the Revised Code of Washington, the Whistleblower Act. We have investigated the assertion independently and objectively through interviews and by reviewing relevant documents. This report contains the result of our investigation.

Questions about this report should be directed to Whistleblower Manager Jim Brownell at (360) 725-5352.

Sincerely,

JAN M. JUTTE, CPA, CGFM
ACTING STATE AUDITOR
OLYMPIA, WA

cc: Steve McKerney, Director of Internal Audit
Governor Jay Inslee
Kate Reynolds, Executive Director, Executive Ethics Board
Jacque Hawkins-Jones, Investigator

WHISTLEBLOWER INVESTIGATION REPORT

Assertions and results

Our Office received a complaint asserting three Washington State Ferries employees mismanaged contracts within their divisions. Specifically, the complaint asserted: subject 1 allowed progress payments on a net 30 contract and allowed the vendor to begin work prior to being bonded; subject 2 authorized payments that were not covered under the contract; and subject 3 grossly mismanaged procurements when she failed to stop the behavior of subjects 1 and 2.

We found:

- Reasonable cause to believe subject 1 did not comply with state procurement law when she allowed a progress payment on a net 30 contract and allowed a vendor to begin work on a contract prior to being bonded.
- No reasonable cause to believe subject 2 and 3 grossly mismanaged contract procurements.

Background

Washington State Ferries (Ferries) is a division of the Washington State Department of Transportation. It features a 23 ferry fleet, carrying millions of passengers each year to 20 different ports of call. Because of the specialized maritime needs of Ferries it has its own purchasing and contracts departments. These departments must follow state contracting and purchasing laws.

About the Investigation

Our Office reviewed contracts, purchase orders, invoices and supporting documentation from August 1, 2013 to July 31, 2014. We also reviewed emails related to contracts and purchases.

Subject 1

The Ferries purchasing department (purchasing) procures goods and services, such as equipment, supplies, and vessel maintenance and repairs. Employees within purchasing are called buyers; each buyer has a monetary threshold for which they can approve a purchase; anything above that threshold must be approved by subject 1. Once a purchase order is signed by all the required parties, it moves on to the accounting department to process.

Our Office was provided a list of purchase orders over \$10,000, the highest monetary threshold for buyers; we selected 24 orders to review. We found one purchase order for nearly \$1.6 million allowed progress payments, which were unallowable in that particular type of contract. This purchase order was originally solicited as a request for quote (RFQ) for a net 30 contract, which obligates the Department to pay the full invoice 30 days after receipt or proof of the deliverable. There are no prepayments or progress payments in a net 30 contract.

Progress payments are allowed when the contractor has to expend large amounts of money to fulfill the order. While the product is in the manufacturing stage, the contractor sends an invoice to Ferries for portions of the contracted amount. According to a witness, the use of progress payments for purchase orders is allowable if Ferries includes that information when soliciting bids. Changing the payment schedule is a modification to the terms and conditions of the RFQ and would normally require the bid to be reopened. However, a witness said this was not necessary in this instance because Ferries had received only one bid for this contract.

According to witnesses, although the above-referenced purchase order was solicited as a net 30 contract, the vendor requested progress payments within its bid proposal. Purchasing accepted the terms because it was the only bid proposal submitted and Ferries had worked with the vendor in the past. The contract was signed February 3, 2014.

The accounting department questioned the payment after receiving the purchase order because the first piece of equipment had not been delivered, which is the standard in a net 30 contract. Subject 1 said that during the contracting process, purchasing thought it was in the best interest of Ferries to allow progress payments. Subject 1 said she sought advice from the Ferries legal department and subject 3 after accounting brought its concerns forward. When the RFQ terms changed to include progress payments, Ferries then was required by law to obtain a surety bond, in order to safeguard public resources. In the normal course of business a vendor would include the cost of a bond in its proposal, but in this instance, the vendor could not because the terms in the RFQ did not require one.

Subject 1 said the buyer made the decision not to re-bid because this vendor was the only bidder. She said securing the bond was the best way to address the issues accounting was having. She said this purchase order “slipped through the cracks” and in hindsight she realized the RFQ was done incorrectly, but everyone acted in good faith.

In August the vendor invoiced Ferries for the cost of the bond. Ferries then amended the contract to allow for the reimbursement to the vendor.

Because it was subject 1’s responsibility to ensure all purchasing laws and rules were followed, we found reasonable cause to believe she violated state law when she allowed progress payments on a net 30 contract. RCW 43.88.160(5)(e) states the [Department] cannot advance funds to a vendor before services “have been rendered or materials furnished.”

We also found the subject violated state law when she allowed the vendor to work for six months without a surety bond. RCW 39.08.010(1)(a) states the [Department] must require the vendor with whom it contracts to deliver a sufficient bond as surety.

Subject 2

The contract division is responsible for overseeing service contracts, such as advertising and training. Most contracts are monitored by a project manager who oversees and approves the services.

We reviewed two contracts for which subject 2 was the project manager. We found subject 2 authorized work to begin prior to the required documentation being in place and subsequently approved payment for these services.

Contract 1

Contract 1 is a media concession contract used for advertising purposes. Subject 2 authorized work to be performed by the vendor for contract 1 that exceeded the dollar amount of the original contract. We found two instances where services were authorized and performed prior to an amendment being executed and the vendor invoiced Ferries for these services. The subject both authorized the services and approved payments when there was no funding available. However, we found no payments were released until the correct documentation was in place.

Contract 2

Contract 2 provided a paging system for the entire fleet. Because the contract was so large the contract department drafted amendments as the services were to be performed throughout the fleet. Using this approach, the budget could be monitored more closely. On three occasions we found subject 2 authorized work to begin prior to amendments being finalized. Additionally, she approved payments for these services without all required documentation being in place.

As with contract 1, accounting questioned if invoices should be paid without proper documentation and withheld the payments until the documentation was provided.

Subject 2 said it was her job to work with the vendor and approve the work, depending on the contract. It was not her responsibility to complete the amendments. She became frustrated with the internal process because not everyone was completing their tasks and she voiced those concerns to subject 3. In fact, she grew so frustrated with the process that she resigned as project manager of contract 2.

We found subject 2 approved services and payments prior to amendments being in place. However, because the accounting department did not make the payments for the services, we did not find these actions rose to the level of gross mismanagement.

Subject 3

According to the complaint, subject 3 was aware of the subjects' failures to follow procurement laws and failed to intervene. We conducted interviews, reviewed emails and contract documents.

During an interview, subject 3 said she oversees purchasing, accounting and contracting and does not need to play a role in managing those departments. She said she provides support to the managers, but does not interfere with their duties

Subject 3 was not involved in the progress payments authorized by subject 1 and did not become aware of the issue until subject 1 approached her. Subject 3 discussed the situation with Ferries' legal advisor and, based on his recommendation, agreed with the decision to request the bond.

Subject 3 was informed by other Ferries employees of subject 2's approval of services and payments prior to amendments being finalized. Subject 3 instructed subject 2 to cease the behavior and attempted to expedite the amendment process with the contracting department.

We found no evidence to support the assertion that subject 3 knowingly allowed subject 1 and 2 to violate procurement laws. Therefore, we found no reasonable cause to believe subject 3 grossly mismanaged procurements.

Agency's Plan of Resolution

It is important to the Department that we appropriately and consistently adhere to all state laws and Department policies. We take our responsibility to the public seriously and endeavor to continually improve and maintain the public's trust.

While we understand that the investigation found reasonable cause to support assertion I, the Department will continue to review the investigation findings and implement corrective actions related to each assertion in the report. The Ferries Division has identified the following corrective actions:

- *The Department is totally committed to implementing well defined checks and balances to ensure full compliance with procurement laws and policies. In addition, Ferries Division management and key staff having responsibility for managing contracts and projects will participate in mandatory procurement and contract management training with the assistance of the Department.*
- *A detailed procedure has been put in place to address the findings from assertion I above. Specifics of the corrective action include:*
 - *Language has been added to the WSF Purchasing Desk Manual that requires contracts with progress payments obtain a surety bond.*

- *Instructions have been provided to the buyers and individuals responsible for approving purchase orders about the need for a surety bond when progress payments are a part of the contract.*
- *Request for Quote language has been added to procurement documents that states, "progress payments may be considered but will require a surety bond".*
- *The accountant will ensure surety bonds are on file for purchase orders prior to progress payments being submitted to the Accounting Department.*

State Auditor's Office Concluding Remarks

We thank Agency officials and personnel for their assistance and cooperation during the investigation.

WHISTLEBLOWER INVESTIGATION CRITERIA

We came to our determination in this investigation by evaluating the facts against the criteria below:

RCW 42.40.020, Definitions.

(4) "Gross mismanagement" means the exercise of management responsibilities in a manner grossly deviating from the standard of care or competence that a reasonable person would observe in the same situation.

RCW 43.88.160, Fiscal management – Powers and duties of officers and agencies.

(5) The treasurer shall:

(e) Perform such other duties as may be required by law or by regulations issued pursuant to this law.

It shall be unlawful for the treasurer to disburse public funds in the treasury except upon forms or by alternative means duly prescribed by the director of financial management. These forms or alternative means shall provide for authentication and certification by the agency head or the agency head's designee that the services have been rendered or the materials have been furnished; or, in the case of loans or grants, that the loans or grants are authorized by law; or, in the case of payments for periodic maintenance services to be performed on state owned equipment, that a written contract for such periodic maintenance services is currently in effect; and the treasurer shall not be liable under the treasurer's surety bond for erroneous or improper payments so made. When services are lawfully paid for in advance of full performance by any private individual or business entity other than equipment maintenance providers or as provided for by RCW 42.24.035, such individual or entity other than central stores rendering such services shall make a cash deposit or furnish surety bond coverage to the state as shall be fixed in an amount by law, or if not fixed by law, then in such amounts as shall be fixed by the director of the department of enterprise services but in no case shall such required cash deposit or surety bond be less than an amount which will fully indemnify the state against any and all losses on account of breach of promise to fully perform such services. No payments shall be made in advance for any equipment maintenance services to be performed more than twelve months after such payment except that institutions of higher education as defined in RCW 28B.10.016

may make payments in advance for equipment maintenance services to be performed up to sixty months after such payment. Any such bond so furnished shall be conditioned that the person, firm or corporation receiving the advance payment will apply it toward performance of the contract. The responsibility for recovery of erroneous or improper payments made under this section shall lie with the agency head or the agency head's designee in accordance with rules issued pursuant to this chapter. Nothing in this section shall be construed to permit a public body to advance funds to a private service provider pursuant to a grant or loan before services have been rendered or material furnished.

RCW 39.08.010, Bond required – Conditions – Retention of contract amount in lieu of bond.

(1)(a) Whenever any board, council, commission, trustees, or body acting for the state or any county or municipality or any public body must contract with any person or corporation to do any work for the state, county, or municipality, or other public body, city, town, or district, such board, council, commission, trustees, or body must require the person or persons with whom such contract is made to make, execute, and deliver to such board, council, commission, trustees, or body a good and sufficient bond, with a surety company as surety, conditioned that such person or persons must:

(i) Faithfully perform all the provisions of such contract;

(ii) Pay all laborers, mechanics, and subcontractors and material suppliers, and all persons who supply such person or persons, or subcontractors, with provisions and supplies for the carrying on of such work; and

(iii) Pay the taxes, increases, and penalties incurred on the project under Titles 50, 51, and 82 RCW on: (A) Projects referred to in RCW 60.28.011(1)(b); and/or (B) projects for which the bond is conditioned on the payment of such taxes, increases, and penalties.

RCW 39.08.100, Marine vessel construction – Security in lieu of bond.

On contracts for construction, maintenance, or repair of a marine vessel, the department of transportation or any county may permit, subject to specified format and conditions, the substitution of one or more of the following alternate forms of security in lieu of all or part of the bond:

Certified check, replacement bond, cashier's check, treasury bills, an irrevocable bank letter of credit, assignment of a savings account, or other liquid assets specifically approved by the secretary of transportation or county engineer, for their respective projects. The secretary of transportation or county engineer, respectively, shall predetermine and include in the special provisions of the bid package the amount of this alternative form of security or bond, or a combination of the two, on a case-by-case basis, in an amount adequate to protect one hundred percent of the state's or county's exposure to loss. Assets used as an alternative form of security shall not be used to secure the bond. By October 1, 1989, the department shall develop and adopt rules under chapter 34.05 RCW that establish the procedures for determining the state's exposure to loss on contracts for construction, maintenance, or repair of a marine vessel. Prior to awarding any contract limiting security to the county's exposure to loss, a county shall develop and adopt an ordinance that establishes the procedure for determining the county's exposure to loss on contracts for construction, maintenance, or repair of a marine vessel.