



Office of the Washington State Auditor
Pat McCarthy

Accountability Audit Report
Pend Oreille County Public Hospital
District No. 1
(Newport Hospital and Health Services)

For the period January 1, 2017 through December 31, 2018

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**Office of the Washington State Auditor
Pat McCarthy**

September 3, 2020

Board of Commissioners
Newport Hospital and Health Services
Newport, Washington

Report on Accountability

Thank you for the opportunity to work with you to promote accountability, integrity and openness in government. The Office of the Washington State Auditor takes seriously our role of providing state and local governments with assurance and accountability as the independent auditor of public accounts. In this way, we strive to help government work better, cost less, deliver higher value and earn greater public trust.

Independent audits provide essential accountability and transparency for District operations. This information is valuable to management, the governing body and public stakeholders when assessing the government's stewardship of public resources.

Attached is our independent audit report on the District's compliance with applicable requirements and safeguarding of public resources for the areas we examined. We appreciate the opportunity to work with your staff and we value your cooperation during the audit.

Sincerely,

Pat McCarthy
State Auditor
Olympia, WA

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AUDIT RESULTS

Results in brief

This report describes the overall results and conclusions for the areas we examined.

As referenced above, we identified areas in which the District could make improvements. These recommendations are included with our report as a finding.

In keeping with general auditing practices, we do not examine every transaction, activity, policy, internal control, or area. As a result, no information is provided on the areas that were not examined.

About the audit

This report contains the results of our independent accountability audit of Newport Hospital and Health Services from January 1, 2017 through December 31, 2018.

Management is responsible for ensuring compliance and adequate safeguarding of public resources from fraud, loss or abuse. This includes the design, implementation and maintenance of internal controls relevant to these objectives.

This audit was conducted under the authority of RCW 43.09.260, which requires the Office of the State Auditor to examine the financial affairs of all local governments. Our audit involved obtaining evidence about the District's uses of public resources, compliance with state laws and regulations and its own policies and procedures, and internal controls over such matters. The procedures performed were based on our assessment of risks in the areas we examined.

Based on our risk assessment for the years ended December 31, 2018 and 2017, the areas examined were those representing the highest risk of fraud, loss, abuse, or noncompliance. We examined the following areas during this audit period:

- Accounts payable – general disbursements, contract payments, and electronic funds transfers
- Compliance with maintenance contracts
- Contract compliance – cash receipting and deposit timeliness

SCHEDULE OF AUDIT FINDINGS AND RESPONSES

2018-001 The Hospital District's internal controls over contracts, conflict of interest, and disbursements were not adequate to safeguard public resources, resulting in overpayments.

Background

Pend Oreille County Public Hospital District No. 1 employs about 340 people and provides rural health care services as well as long-term care with assisted living facilities. In fiscal year 2018, the District reported about \$12 million in non-payroll expenditures.

State law prohibits municipal officers from having a beneficial interest in a contract. The law defines beneficial interest as a financial interest in a contract to which the government or agency is a party, if an official participates in awarding the contract or is responsible for the contract because of the office he or she holds. The District is responsible for establishing internal control processes over contracting sufficient to comply with state law and ensure the District receives the benefits of the agreement.

In November 2017, the District hired a new Maintenance Manager whose responsibilities included planning, organizing, supervising, coordinating and controlling plant operations and maintenance functions. The Maintenance Manager submitted a letter of resignation on November 29, 2018, and left employment with the District shortly after.

Description of Condition

In December 2019, during the initial planning of our audit, District staff identified concerns with contracts made by the former Maintenance Manager.

Our audit subsequently determined that in January 2018, the District signed a service contract with a maintenance management company based in Florida at the Maintenance Manager's recommendation. The agreement stated that the company would conduct quarterly maintenance inspections to service the District's HVAC equipment according to manufacturer specification for \$42,965 a year, including applicable taxes.

In February 2018, the Maintenance Manager submitted a purchase order for \$14,431 payable to the maintenance management company. As part of the approval process, the District's purchasing department reviewed the transaction and determined that as this was for capital equipment and was missing the approval of the Chief Financial Officer for the expense. The District reviewed the Facility

Department's budget-to-actual expenditures and found the Department had exceeded its annual budget in the first two months of the year. The Department's largest expenses were payments to the maintenance management company. This led the District to investigate further.

The District found that from December 20, 2017, through February 28, 2018, the District was invoiced for and made payments to the maintenance management company totaling \$170,070, which exceeded the contracted amount of \$42,965 a year. Our audit found that while the District had policies requiring varying levels of approval for expenses based on dollar amount, the Maintenance Manager did not seek the required approvals, and the Purchasing Department processed the payments despite the missing approvals. We found that 34 of 43 maintenance management company invoices lacked the required Director approval and seven lacked the required CEO approval.

The District also discovered that the Maintenance Manager had previously worked for the maintenance management company as its Vice President from December 2011 to December 2015. The District requires that employees complete a conflict of interest disclosure form annually, but the Maintenance Manager never completed the conflict of interest form, which might have disclosed his previous employment with this company.

Additionally, the maintenance management company had contracted with seven local subcontractors whose combined invoices amounted to \$100,299 of the total maintenance costs. The maintenance management company used the invoices it received from the subcontractors and applied its own fees to collect a higher amount than the actual cost of the work.

Cause of Condition

The District failed to follow its established process for reviewing and approving purchase orders to ensure that appropriate approvals were obtained prior to paying the vendors invoices. The District also lacked proper oversight on contracts to ensure the vendor was only providing services approved by the contract. Further, the District failed to follow its own procedures by not ensuring that the Maintenance Manager completed a conflict of interest form.

Effect of Condition

We identified questionable payments of about \$38,336 that the District paid for the maintenance management company's markup over invoices billed by seven unapproved subcontractors. We identified an additional \$31,434 in questionable

payments to the company for services we could not determine the company provided to the District, due to the unsupported invoices.

Additionally, the District did not comply with state Code of Ethics for Municipal Officers laws when the Maintenance Manager, who was previously employed by the maintenance management company, encouraged the District to contract with the maintenance management company for a quarterly maintenance service contract.

Recommendations

We recommend the District follow its established controls over disbursements and improve contract monitoring. The District should ensure that invoices are supported, appear reasonable for the services provided and contain the proper approvals before payment. Further, the District should adequately monitor contracts to ensure vendors provide services in accordance with the contract, only bill for services provided and do not exceed the contracted dollar amount.

We also recommend that the District follow its own conflict of interest policies and procedures, to ensure all employees complete the conflict of interest form, and reference any identified conflicts of interest before awarding contracts.

District's Response

The District understands the Finding and Description of Condition stated by the State Auditor's Office (SAO). The District's procurement processes are designed to require the signature of the appropriate level of manager/director prior to issuing and receiving a purchase order. The District acknowledges internal policies were not adhered to and the purchase orders were issued without the proper level of authority or the proper backup to support the service provided under a contractual arrangement. The District also acknowledges the failure to obtain a completed Annual Conflict of Interest Disclosure form from the Maintenance Manager.

Prior to receiving this report the District implemented new safeguards to help eliminate the conditions noted in this report. As an immediate response to the condition, a recap of existing District policy "Purchase Orders Budgets and Manager's Responsibility" was circulated to appropriate parties in the District immediately following the violation of policy. Purchasing, AP and accounting staff have received instruction to deny any request for purchase orders or payments when the proper signing authority has not been obtained. Completion of the Annual Conflict of Interest Disclosure has been realigned to occur as part of the orientation process and monitoring of annual completion has been moved to the HR

Department. The District has provided ongoing education regarding procurement law for public works, including clarification that contracts are required to cover any agency (or sub-contractor) performing work on District premises. The contracts must include a scope of work and defined contract amount for the service to be provided; all aspects of public works requirements must be followed to maintain compliance. The District has committed to provide ongoing external education in the area of procurement. During his first month of employment, the most recently hired Plant Manager attended a full-day workshop provided by MRSC to provide an overview of the requirements necessary in performing procurement and public works contracting responsibilities. The District will continue to utilize the resource material and training classes provided by MRSC to provide ongoing training.

Auditor's Remarks

The Maintenance Manager initiated questionable contract payments of about \$38,336 without adequate oversight by the District. We reaffirm our finding and will review the District's corrective action during the next audit.

Applicable Laws and Regulations

RCW 42.23.030 - Interest in contacts prohibited

Budgeting Accounting and Reporting System (BARS) manual – Accounting Principles and Controls, Internal Control

RELATED REPORTS

Financial

A financial statement audit was performed by a firm of certified public accountants. That firm's report is available on our website, <http://portal.sao.wa.gov/ReportSearch>.

INFORMATION ABOUT THE DISTRICT

Pend Oreille County Public Hospital District No. 1 owns and operates several healthcare facilities in Pend Oreille County. The District operates Newport Hospital and Health Services, a licensed 24-bed hospital; Newport Community Hospital Long-Term Care Unit, a 50-bed facility; Newport Health Center, a provider-based rural health clinic (previously operating in two locations as Family Health Center Newport and Family Medicine Newport), opening in August 2016, and River Mountain Village, a 45-unit assisted living facility.

An elected, five-member Board of Commissioners governs the District. Commissioners serve staggered, six-year terms. The Board appoints management to oversee the District's daily operations as well as its 343 employees. For fiscal years 2017 and 2018, the District operated on an annual budget of approximately \$36 and \$37.7 million.

Contact information related to this report	
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Information current as of report publish date.

Audit history

You can find current and past audit reports for Newport Hospital and Health Services at <http://portal.sao.wa.gov/ReportSearch>.

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.

We work with our audit clients and citizens to achieve our vision of government that works for citizens, by helping governments work better, cost less, deliver higher value, and earn greater public trust.

In fulfilling our mission to hold state and local governments accountable for the use of public resources, we also hold ourselves accountable by continually improving our audit quality and operational efficiency and developing highly engaged and committed employees.

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.

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 as well as [fraud](#), state [whistleblower](#) and [citizen hotline](#) investigations.

The results of our work are widely distributed through a variety of reports, which are available on our [website](#) and through our free, electronic [subscription](#) service.

We take our role as partners in accountability seriously, and provide training and technical assistance to governments, and have an extensive quality assurance program.

Contact information for the State Auditor's Office	
Public Records requests	PublicRecords@sao.wa.gov
Main telephone	(564) 999-0950
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