



Office of the Washington State Auditor
Pat McCarthy

Fraud Investigation Report

Department of Revenue

For the investigation period October 5, 2020 through November 3, 2023

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Office of the Washington State Auditor Pat McCarthy

May 23, 2024

Director Drew Shirk
Department of Revenue
Olympia, Washington

Report on Fraud Investigation

Attached is the official report on a misappropriation at the Department of Revenue. On September 26, 2023, the Department notified the Office of the Washington State Auditor of a potential loss of public funds. This notification was submitted to us under the provisions of state law (RCW 43.09.185).

Our investigation was performed under the authority of state law (RCW 43.09.290) and included procedures we considered necessary under the circumstances.

If you are a member of the media and have questions about this report, please contact Director of Communications Kathleen Cooper at (564) 999-0800. Otherwise, please contact Special Investigations Program Manager Stephanie Sullivan at (360) 688-0858.

Pat McCarthy, State Auditor
Olympia, WA

cc: Sarah Saavedra, Internal Audit Manager

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FRAUD INVESTIGATION REPORT

Background and Investigation Results

On September 26, 2023, the Department notified our Office regarding a potential loss of public funds, as required by state law (RCW 43.09.185).

In July 2022, the Department found that an out-of-state Revenue Auditor altered documents for internet service reimbursements and monthly special allowance. The employee altered the service address on the documents to make it appear that she was working in an area with a higher monthly special allowance.

Out-of-state Revenue Auditors audit businesses outside Washington that are required to report tax revenues to the state. These positions are based outside Washington in order to decrease auditors' travel costs, allow auditors to perform on-site audits, and increase auditors' knowledge of tax laws and systems for their assigned regions. Since these employees are based out of state, the Department is authorized under RCW 82.01.070 to offer a monthly special allowance, internet service reimbursements, and other items to help them maintain a home office and defray the extra costs related to out-of-state services.

The Department investigated and determined the Revenue Auditor was overpaid \$4,000 in monthly allowances and \$1,569.40 in internet service reimbursements between January 1, 2022, and August 1, 2023. The Department reduced the total loss amount by \$1,300.55 for reimbursements the Revenue Auditor was eligible for, but did not claim, from September 1, 2023, through November 1, 2023. The Department determined the total loss was \$4,268.85.

We reviewed the Department's investigation, which found the following:

- The Revenue Auditor was hired on October 5, 2020, and was living in North Carolina. The Department required her to move to Illinois for the position but did not confirm that she moved. The Revenue Auditor changed her permanent address with the Department from North Carolina to Illinois in September 2021. Three months later, the Revenue Auditor changed her mailing address to a home in South Carolina.
- In January 2022, the Revenue Auditor began submitting internet service bills for reimbursement that listed an Illinois address. In the summer of 2023, the Revenue Auditor's regular manager was on vacation, and another manager reviewed the reimbursement requests. This acting manager told Department officials in August that he believed the Revenue Auditor was altering her internet service bills by using a PDF-editing tool to move text boxes and obscure the original South Carolina service address, internet service provider, date and amount.
- Between January 2022 and August 2023, the Department processed and paid out reimbursements for 20 altered internet service bills. Each payment was \$78.47, resulting in \$1,569.40 being reimbursed based on altered documentation.

- In addition, the Revenue Auditor collected a higher monthly allowance between January 2022 and August 2023 because Illinois allowances are \$200 more than allowances for South Carolina. This resulted in the Revenue Auditor collecting \$4,000 more than was allowed.
- The Department determined that the Revenue Auditor was eligible for \$1,300.55 in monthly allowances and other expenses for which she had not requested reimbursement, so the Department reduced its loss calculation by \$1,300.55. The Department calculated a total loss of \$4,268.85.
- On August 29 and September 6, 2023, the Department interviewed the Revenue Auditor. During the interview, she acknowledged altering her internet bills to make it appear that she was residing in a different state, but said she was unaware these alterations would result in a higher reimbursement rate.

We agree with the Department's conclusions except for its decision to reduce the loss by an amount the Revenue Auditor may have been eligible for but did not claim. To determine whether any additional losses occurred, we performed additional investigative procedures over the time frame of the Revenue Auditor's entire employment with the Department. We found:

- From May 2021 to October 2023, the Revenue Auditor worked from South Carolina. We confirmed this using virtual private network traffic and IP login locations. Between May 2021 and December 2021, the Revenue Auditor was reimbursed at North Carolina's monthly allowance rate, which was \$200 a month more than South Carolina. The Department paid \$1,600 more than the employee's appropriate monthly allowance.
- From November 2020 through December 2021, the Revenue Auditor submitted internet service bills for reimbursement that we could not determine were altered or original copies. Therefore, we question the full amount – \$980.36 – the Revenue Auditor claimed for internet reimbursement.

In total, we identified misappropriation of \$5,600 in monthly special allowances and \$2,549.76 in questioned costs for internet service reimbursements.

Control Weaknesses

The Department's internal controls were inadequate for safeguarding public resources. We found the following weaknesses allowed the misappropriation and questionable payments to occur:

- The Department lacked policies and procedures specific to the payment of out-of-state auditor monthly allowances and reimbursements.
- The Department's Audit Division did not sufficiently supervise and oversee out-of-state employees to verify their work locations and the appropriateness of their reimbursement documents.

Recommendations

We recommend the Department strengthen its internal controls related to out-of-state employee reimbursements and monthly allowances. Specifically, the Department should develop policies and procedures and implement processes to verify out-of-state employees' work locations.

We will refer this case to the Washington State Executive Ethics Board for any further action it determines is necessary.

We also recommend the Department seek recovery of the misappropriated \$5,600, questionable amounts as appropriate, and related investigation costs of \$7,350 from the former Revenue Auditor and/or its insurance bonding company, as appropriate. Any compromise or settlement of this claim by the Department must be approved in writing by the Attorney General and State Auditor as directed by state law (RCW 43.09.330). Assistant Attorney General Matt Kernutt is the contact person for the Attorney General's Office and can be reached at (360) 586-0740 or Matthew.Kernutt@atg.wa.gov. The contact for the Office of the Washington State Auditor is Brandi Pritchard, Assistant Director of Local Audit and Special Investigations, who can be reached at (509) 726-1886 or Brandi.Pritchard@sao.wa.gov.

Department's Response

We appreciate the continued partnership with the State Auditor's Office. The Department of Revenue takes misappropriation seriously.

When the Department originally identified the issue, we immediately notified the State Auditor's Office of the suspected loss following RCW 43.09.185.

Following the notification, the Department performed an investigation. Once the investigation was completed, we provided the results to the State Auditor's Office. The Department prepared to take disciplinary action; however, the employee resigned prior to the action being taken.

The Audit Division has addressed the findings of the internal investigation. Since the internal investigation was completed, the Audit Division wrote policies and procedures specific to the payment of out-of-state auditor special allowances and reimbursements and updated training manuals for supervisors.

This event occurred during the COVID-19 pandemic. The pandemic made it difficult to travel and supervisors were not allowed to physically inspect the employee's location as had been previous practice.

To address the lack of sufficient supervision and oversight over out-of-state employees, post-pandemic, supervisors are required to verify work locations physically in-person within 6 months of employment, and annually thereafter.

The Department is also exploring other address verification processes.

To address the appropriateness of reimbursement documents, the Department is exploring additional supervisory training regarding how to verify the authenticity of documents.

The Department is seeking guidance from the Attorney General's Office on restitution options.

Auditor's Remarks

We thank Department officials and personnel for their assistance and cooperation during the investigation. We will follow up on the Department's internal controls during the next audit.

ABOUT THE STATE AUDITOR'S OFFICE

The State Auditor's Office is established in the Washington State Constitution and is part of the executive branch of state government. The State Auditor is elected by the people of Washington and serves four-year terms.

We work with state agencies, local governments and the public to achieve our vision of increasing trust in government by helping governments work better and deliver higher value.

In fulfilling our mission to provide citizens with independent and transparent examinations of how state and local governments use public funds, we hold ourselves to those same standards by continually improving our audit quality and operational efficiency, and by developing highly engaged and committed employees.

As an agency, the State Auditor's Office has the independence necessary to objectively perform audits, attestation engagements and investigations. Our work is designed to comply with professional standards as well as to satisfy the requirements of federal, state and local laws. The Office also has an extensive quality control program and undergoes regular external peer review to ensure our work meets the highest possible standards of accuracy, objectivity and clarity.

Our audits look at financial information and compliance with federal, state and local laws for all local governments, including schools, and all state agencies, including institutions of higher education. In addition, we conduct performance audits and cybersecurity audits of state agencies and local governments, as well as state whistleblower, fraud and citizen hotline investigations.

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