



Office of the Washington State Auditor
Pat McCarthy

Accountability Audit Report

City of Spokane

For the period January 1, 2019 through December 31, 2019

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

April 19, 2021

Mayor and City Council
City of Spokane
Spokane, 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 City 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 City'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 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. In most of the areas we examined, City operations complied, in all material respects, with applicable state laws, regulations, and its own policies, and provided adequate controls over safeguarding of public resources.

As referenced above, we identified areas where the City 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 the City of Spokane from January 1, 2019 through December 31, 2019.

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 Washington State Auditor to examine the financial affairs of all local governments. Our audit involved obtaining evidence about the City's use 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.

The City contacted the State Auditor's Office in March 2020 requesting a special review of activities in the Community Housing and Human Services (CHHS) Department because of concerns Department staff raised. Specifically, the concerns related to the procurement of public works contracts, evaluation and award of sub-recipient agreements, potential conflicts of interest and inappropriate payments for contracted services.

Based on our risk assessment for the year ended December 31, 2019, the areas examined were those representing the highest risk of fraud, loss, abuse, or noncompliance. We examined the following areas during this audit period:

- CHHS Department – public works procurement, awarding of sub-recipient agreements, conflicts of interest, and compliance with contract payment terms

- Procurement – sole source exemptions, purchases and public works project change orders
- Utility billing – credit program eligibility and billing adjustments
- Accounts payable – fuel and travel credit card expenditures, employee travel reimbursements, and payroll and vendor electronic funds transfers
- Compliance with the allowable use of federal grant funds – Congestion Mitigation and Air Quality Program
- Police Department cash receipting – timeliness and completeness of deposits and use of fee schedules

SCHEDULE OF AUDIT FINDINGS AND RESPONSES

2019-001 The City's Community Housing and Human Services Department bypassed established internal controls regarding procurement of public works contracts, conflicts of interest, sub-recipient agreements, and contractor payments.

Background

The City's Community Housing and Human Services Department (Department) oversees services and community partnerships to support low to moderate income populations in Spokane. In fiscal year 2019, the Department operated on a \$9 million budget. The Department awards grant and local funds through agreements with sub-recipients that provide services to the community. The Department also manages properties and public works projects related to these services. The Department experienced turnover in the Department Director position three times from 2016 through 2019.

City Department directors are responsible for designing and following internal controls that provide reasonable assurance of compliance with state laws and City policies and of safeguarding public resources.

The City contacted the State Auditor's Office in March 2020, requesting a special review of activities in the Department because of concerns Department staff raised. Specifically, the concerns related to the procurement of public works contracts, evaluation and award of sub-recipient agreements, potential conflicts of interest and inappropriate payments for contracted services.

Description of Condition

Public works procurement

For public works projects, the City's purchasing policy requires informal competition using the small works roster when project costs are between \$10,000 and \$300,000.

Our audit found the Department did not comply with City policy and procedure for two public works contracts awarded in 2019. Specifically, for these public works contracts for flooring repairs of \$11,400 and \$13,300, the Department could not provide documentation to demonstrate it performed informal solicitations, as City policy requires.

Sub-recipient agreements

The Department does not have adopted policies or written procedures for awarding sub-recipient agreements for necessary services. The Department's informal practice is to solicit services from sub-recipients by posting a request for proposals (RFP) on the City's website and then performing risk assessments and evaluations of proposals received to select the most qualified sub-recipient.

We reviewed three sub-recipient agreements approved in 2019 of \$881,482, \$740,000 and \$495,841 for warming center and shelter operations. The Department could not provide evidence it followed its practice and solicited an RFP or performed a competitive bidding process for these agreements.

Conflict of interest

The City's Municipal Code and state law prohibit municipal officers or employees from participating in the making of contracts in which the officer or employee has a beneficial or personal interest, either directly or indirectly. The Municipal Code requires employees to notify supervisors or appointing authorities of potential conflicts of interest and for supervisors or appointing authorities to resolve and document the disposition of the potential conflicts of interest.

In our review of the three sub-recipient agreements noted above, we found two of the agreements awarded had an appearance of a conflict of interest, which may violate the City's Municipal Code and state law. Further, there was no documentation to evidence the Department or City resolved the potential conflicts of interest. Specifically, we noted:

- In November 2019, the Department recommended for award a \$740,000 agreement to a sub-recipient, despite the Department identifying the sub-recipient as "high risk" during a July 2019 selection process. According to the Pre-Award Applicant Risk Assessment Summary form, the sub-recipient was deemed high risk, in part, due to an unclear relationship with a charitable organization the sub-recipient identified as a partner. Additionally, according to Department staff, a City Council member participated in the July 2019 award process. The Public Disclosure Commission website shows that the founders of the charitable organization contributed to the City Council member's mayoral election campaign in 2019. Although the City did not award the July 2019 agreement to the sub-recipient, this relationship still existed at the time the Department recommended, and the City awarded, the November 2019 agreement to the high risk sub-recipient.

- The Department also recommended for award one sub-recipient agreement for \$495,841 in November 2019. According to Department staff, a Department Director responsible for the shelter and warming center programs participated in awarding the agreement and then left the City for employment with the sub-recipient. We noted the Department Director left the City in October 2019 before the City approved the agreement.

Gift of public funds

The Washington State Constitution, Article 8, Section 7 prohibits local governments from giving any money or credit to or in aid of any individual, association, company or corporation except for the necessary support of the poor and infirm. The Department awarded one consulting agency agreement of \$15,000 in 2017 to provide free housing legal clinics to citizens, and the agreement terms stated the “City will reimburse the consultant at actual cost for expenditures that are pre-approved by the City in writing and are necessary and directly applicable to the work required by this agreement . . .

The Department reimbursed the consulting agency for two mortgage payments and one car loan payment for one of the agency’s employees in 2017 totaling \$2,453, which are personal, non-business expenses. According to Department staff, a Department Director approved making the payments to the consulting agency as an alternative form of compensation for the employee’s service hours worked under the agreement, contrary to the express terms of the agreement.

Cause of Condition

According to the City, Department staff felt pressure and influence from Department directors, and those Department directors felt pressure and influence from a City Council member to approve projects, contracts, agreements and transactions that bypassed established internal controls, Department practices and the City’s adopted policies and procedures.

Effect of Condition

Public works procurement

Because the Department did not comply with the City’s purchasing policy and procedure, it cannot ensure it allowed for fair and equitable opportunities for contractors to submit quotes on public works projects and that it received the lowest responsible bidder for the projects.

Sub-recipient agreements

Without written policies and procedures, the Department cannot ensure employees follow a consistent and equitable process to evaluate, select and award agreements to the most qualified sub-recipients.

Conflict of interest

The City Council member and Department Director did not comply with the City's Municipal Code to notify supervisors or appointing authorities in writing when they identified the appearance of conflicts of interest. Therefore, there was no resolution and disposition of the potential conflicts before City employees and elected officials participated in awarding sub-recipient agreements. Any actual or potential conflicts of interest could violate the City's Municipal Code and state law.

Gifting of public funds

In 2017, the Department did not comply with agreement terms to reimburse the consulting agency for the actual cost of expenditures that are necessary and directly applicable to the work required by the agreement. The Department did not have any other documentation showing the City pre-approved these costs as allowable business expenses or that the consulting agency had performed the agreed upon services in accordance with the agreement terms for the amounts paid. Further, the Department's reimbursement to the consulting agency for personal expenses might be considered a gift of public funds and might violate the State Constitution.

Recommendations

The Department should follow its established internal controls and practices and comply with City policies and procedures. Specifically, the Department should:

- Follow the City's purchasing policy and procedure for the procurement of public works projects
- Establish written policies or procedures to ensure employees use a consistent and equitable process to evaluate, select and award agreements to sub-recipients
- Ensure employees and elected officials notify supervisors or appointing authorities in writing when they have actual or potential conflicts of interest and resolve and document the disposition of such conflicts of interest in accordance with the City's Municipal Code
- Communicate methods that allow employees to report improper actions or concerns

- Reimburse consultants for actual and appropriate business expenses and maintain documentation to demonstrate consultants perform necessary and applicable work in accordance with agreement terms

City's Response

The Community, Housing and Human Services Department (CHHS) of the City of Spokane appreciates the State Auditor's Office for its comprehensive and timely response to the request to evaluate the process and procedures related to public works procurement processes, conflicts of interest, sub-recipient agreements and the gifting of public funds. Though this work was initiated by the City of Spokane, your recommendations for how we can improve the delivery of services and provide appropriate oversight and accountability is appreciated and will guide departmental procedures moving forward. Thank you for the opportunity to respond to the audit recommendations. We acknowledge the findings and have developed a course of action that will ensure CHHS staff are fully educated and aware of the methods to report improper actions or raise concerns. This audit response specifically addresses the following areas:

1) Public Works Procurement

Within six months of the date indicated on this response letter, the CHHS department, in collaboration with other subject-matter expert department and disciplines for development, review, and implementation, will:

- *Establish protocol and implement a training program facilitated by the City's Purchasing department that addresses and aligns with specific sections of the City's adopted policies and procedures with the City's Procurement of Goods, Services and Works outlined in Spokane Municipal Code Title 07, Chapter 06. The training program will be designed in a manner that promotes proficiency and understanding of the established protocol.*
- *Collaborate with Human Resources and the Purchasing department to ensure that all staff have been provided training on Personnel Policies and Procedures regarding how to report fraud, waste, abuse and whistleblower protections.*
- *Include a training program in onboarding of future CHHS department employees facilitated by the City's Purchasing department that addresses and aligns with specific sections of the City's adopted policies and procedures with the City's Procurement of Goods, Services and Works outlined in Spokane Municipal Code Title 07, Chapter 06. The training program will be designed in a manner that promotes proficiency and understanding of the established protocol.*

- *Require current and future staff to participate in and acknowledge completion of training through and electronic training platform.*

Additionally, annually CHHS department leadership and employees will:

- *Review current or updated specific sections of the City's adopted policies and procedures with the City's Procurement of Goods, Services and Works outlined in Spokane Municipal Code Title 07, Chapter 06.*
- *Review current or updated Personnel policies and procedures regarding how to report fraud, waste, abuse and whistleblower protections.*

2.) Sub-recipient Agreements

Within six months of the date indicated on this response letter, the CHHS department, in collaboration with other subject-matter expert departments and disciplines for development, review, and implementation, will develop and implement written policies and procedures related to sub-recipient agreement selections based on funder requirements and established best practices that include a transparent process. These policies and procedures will:

- *Require employees to use a consistent and equitable process to evaluate, select and award agreements to sub-recipients.*
- *Require all selection committee members, including elected officials, to acknowledge with their signature having received and read conflict of interest policies and procedures. In addition to receiving and reading the policy, members should sign a form declaring any potential conflicts and fitness to participate in that specific award process. These documents will be retained as part of the RFP process.*
- *Ensure consultants are reimbursed for actual and appropriate business expenses and maintain documentation to demonstrate consultants perform necessary and applicable work in accordance with agreement terms. The program manager shall sign or electronically approve the payment for processing and review by a separate, independently managed department.*

3.) Conflict of Interest

Within six months of the date indicated on this response letter, the CHHS department employees and elected officials will:

- *Review the notification process and written documentation requirements for actual and potential conflicts of interest in accordance with specific sections Spokane Municipal Code.*
- *Review and acknowledge specific sections of The Washington State Constitution, Article 8, Section 7, Revised Code of Washington Law 42.23.030 and Spokane Municipal Code Title 01, Chapter 04A, Section 030*

addressing Code of Ethics and Prohibited Conduct, prohibited interest in contracts and credit not be loaned to states.

- *Sign a form indicating acknowledgement of reading aforementioned City municipal codes and understanding disposition of conflicts of interests. In addition to receiving and reading the policy, members should sign a form declaring any potential conflicts and fitness to participate in that specific award process. These documents will be retained as part of the RFP process.*

Additionally, future employees of the CHHS department and elected officials will:

- *Be informed of this process during the onboarding and training process.*
- *Provide ongoing education and review updated policies regarding conflict of interest.*

4.) Gifting of Public Funds

Within six months of the date indicated on this response letter, the CHHS department will:

- *Require current employees to attend and complete the Gifting of Public Funds training provided by Municipal Research and Services Center (MRSC) that references The Washington State Constitution, Article 8, Section 7 and Spokane Municipal Code Title 01, Chapter 04A, Section 030 addressing Code of Ethics and Prohibited Conduct. Following the training, employees will be required to sign a form acknowledging the training.*
- *Provide CHHS department specific training with a detailed process for CHHS leadership and staff members to use if an invoice or document is in question. The training program will be designed in a manner that promotes proficiency and understanding of the established protocol.*

Moving forward, employees of the CHHS department will:

- *Attend and complete the Gifting of Public Funds training provided by MRSC as part of the onboarding and training process.*
- *Require employees to stay proficient by participating in updated or refresher MRSC trainings or information regarding changes and best practices for use of public funds.*

Finally, as an overall measure, the City's Performance Audit team will be periodically engaged to review and identify other potential control gaps requiring attention and mitigation. That team will work with the CHHS Department and City Council to proactively strengthen any identified training and process needs. The City will also renew efforts to raise awareness of ways employees can raise

concerns to their supervisors, human resources, and/or anonymously through contracted resources as desired and appropriate.

We appreciate the State Auditors due diligence and thorough assessment of CHHS operations and the recommendations provided to guide policies and procedures moving forward.

Auditor's Remarks

We appreciate the City being proactive in identifying risks and bringing these concerns to our attention. The City was very helpful during our review and we appreciate its commitment to strengthening internal controls and its policies and procedures. We will continue to work with the City as it implements policies and procedures and are committed to providing any guidance or resources we can to help the City establish strong control systems. We will review the status of corrective action taken during our next audit.

Applicable Laws and Regulations

City Purchasing Policy, Section 5.3.4, Public Works, states:

All informal competition purchases in this category require the use of the Small Works Roster.

Purchases \$10,000 or less do not require competition.

Purchases over \$10,000 to \$300,000 require informal competition.

Purchases over \$300,000 require formal competition.

City Purchasing Policy, Section 5.2, Purchasing Code of Ethics, states in part:

Employees making procurements for the City shall conduct themselves in an ethical manner as follows:

They shall not participate in the selection, award or administration of a purchase if he or she has a real or apparent conflict of interest. Such a conflict of interest would arise when the employee or member of the employee's immediate family, his or her partner, or an organization which employs or is about to employ any of the parties indicated herein, has a financial or other interest in or a tangible personal benefit from a firm considered for contract.

They will behave with impartiality, fairness, openness, integrity, and professionalism in their dealings with suppliers.

City Municipal Code, Chapter 01.04A Code of Ethics, Section 01.04A.030 Prohibited Conduct, states in part:

The following shall constitute a violation of this Code of Ethics:

A. General Prohibition Against Conflicts of Interest.

In order to avoid becoming involved or implicated in a conflict of interest or impropriety, or an appearance of conflict of interest or impropriety, no current City officer or employee shall have an interest, financial or otherwise, direct or indirect, or engage in a business or transaction or professional activity, or incur an obligation of any nature, that might be seen as conflicting with the City officer or employee's proper discharge of his or her official duties, the conduct of official City business or as adverse to the interests of the City. Performance of a legally required duty by a City officer or employee shall not be considered a violation of the Code of Ethics.

1. Any employee who becomes aware that he or she might have a potential conflict of interest that arises in the course of his or her official duties shall notify in writing his or her supervisor or appointing authority of the potential conflict.
2. Upon receipt of such a notification, the supervisor or appointing authority shall take action to resolve the potential conflict of interest within a reasonable time, which may include, but is not limited to, designating an alternative employee to perform the duty that is involved in the potential conflict. The supervisor or appointing authority shall document the disposition of the potential conflict in writing in files maintained by the appointing authority. The supervisor or appointing authority may request an advisory opinion from the Ethics Commission before addressing and resolving of the potential conflict.

B. Personal Interests in Contracts Prohibited.

No City officer or employee shall participate in his or her capacity as a City officer or employee in the making of a

contract in which he or she has a personal interest, direct or indirect, or performs in regard to such a contract some function requiring the exercise of discretion on behalf of the City. Except, that this prohibition shall not apply where the City officer or employee has only a remote interest in the contract, and where the fact and extent of such interest is disclosed and noted in the official minutes or similar records of the City prior to formation of the contract, and thereafter the governing body authorizes, approves or ratifies the contract in good faith by a vote of its membership sufficient for the purpose without counting the vote or votes of the City officer(s) having the remote interest as defined below.

D. Personal Influence in Contract Selection Prohibited.

No City officer or employee shall influence the City's selection of, or its conduct of business with, a corporation, person or firm having or proposing to do business with the City if the City officer or employee has a personal interest in or with the corporation, person or firm, unless such interest is a remote interest and where the fact and extent of such interest is disclosed and noted in the official minutes or similar records of the City prior to formation of the contract, as defined in the preceding section. Provided, however, that no City officer or employee may receive anything of value from the City as a result of any contract to which the City shall be a party except for the City officer or employee's salary or lawful compensation.

RCW 42.23.030 – Interest in contracts prohibited, states in part:

No municipal officer shall be beneficially interested, directly or indirectly, in any contract which may be made by, through or under the supervision of such officer, in whole or in part, or which may be made for the benefit of his or her office, or accept, directly or indirectly, any compensation, gratuity or reward in connection with such contract from any other person beneficially interested therein.

Washington State Constitution, Article 8, Section 7 – Credit Not to Be Loaned states:

No county, city, town or other municipal corporation shall hereafter give any money, or property, or loan its money, or credit to or in aid of any individual, association, company or corporation, except for the necessary support of the poor and infirm, or become directly or indirectly the owner of any stock in or bonds of any association, company or corporation.

RELATED REPORTS

Financial

Our opinion on the City's financial statements and compliance with federal grant program requirements is provided in a separate report, which includes the City's financial statements. That report is available on our website, <http://portal.sao.wa.gov/ReportSearch>.

A financial statement audit over the City's pension trust fund, Spokane Employees' Retirement System, was performed by a firm of certified public accountants. That firm's report is available on our website, <http://portal.sao.wa.gov/ReportSearch>.

Federal grant programs

We evaluated internal controls and tested compliance with the federal program requirements, as applicable, for the City's major federal programs, which are listed in the Schedule of Findings and Questioned Costs section of the separate financial statement and single audit report. That report is available on our website, <http://portal.sao.wa.gov/ReportSearch>.

INFORMATION ABOUT THE CITY

The City of Spokane is the second largest city in the state with an estimated population of 222,000 residents. The City was incorporated in 1881 and adopted its first charter in 1910. The City provides police, fire, inspection, street, library, parks and recreation, traffic engineering, water, sewer, solid waste and general administrative services. In 2001, the City changed to a strong-mayor form of government.

An elected, seven-member Council and an independently elected Mayor govern the City. The Council appoints management to oversee the City's daily operations and its 2,100 employees. For fiscal year 2019, the City operated on an annual general fund budget of approximately \$183.6 million.

Contact information related to this report

Address:	City of Spokane 808 W. Spokane Falls Blvd. Spokane, WA 99201-3304
Contact:	Sally Stopher, Director of Grants, Contracts and Purchasing
Telephone:	509-625-6032
Website:	www.spokanecity.org

Information current as of report publish date.

Audit history

You can find current and past audit reports for the City of Spokane at <http://portal.sao.wa.gov/ReportSearch>.

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.

The results of our work are available to everyone through the more than 2,000 reports we publish each year on our website, www.sao.wa.gov. Additionally, we share regular news and other information via an email subscription service and social media channels.

We take our role as partners in accountability seriously. The Office provides training and technical assistance to governments both directly and through partnerships with other governmental support organizations.

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