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July 1, 2009

The Honorable Brian Sonntag, CGFM
Washington State Auditor
Washington State Auditor's Office
Washington State Capitol Campus
P.O. Box 40021
Olympia, Washington 98504-0021

Re: Performance Audit Report, Port of Seattle Construction Management, Report No. 100008 - Annual Report

Dear Auditor Sonntag:

The Port of Seattle Commission is pleased to report on the status of our response to the performance audit conducted in 2007, and to provide you with our second and final annual report.

Since submitting the 2008 annual report, the port has completed work in the following areas:

- Delegation of Authority
- Fraud risk assessment
- Construction management practices
- Contract administration practices
- Centralized project controls

Through these reforms, we believe the Port of Seattle has achieved the objectives you established in your audit report.

Delegation of Authority

In our first annual report of July 1, 2008, we reported on the work of a commission subcommittee led by Commissioners Patricia Davis and Gael Tarleton. At that time, the subcommittee had proposed a new resolution, No. 3605, to replace the previous delegation of authority. On August 26, 2008, the commission unanimously adopted the new resolution. Resolution No. 3605 changes the way the port conducts business, increases commission oversight of all capital projects and procurements, eliminates project-wide authorizations, and requires a three-stage commission approval process for all capital projects over \$200,000.

In addition, Resolution No. 3605 must be reviewed within eighteen months by the commission. On April 21, 2009, the commission was briefed on both the implementation of the resolution and

on proposed adjustments needed to clarify its intent. A thorough review process involving port commissioners, senior management and staff will be undertaken prior to late summer 2009. The commission considers this resolution integral to the ongoing improvement of business practices and culture at the Port. As such, it is a living document that requires regular review and revision in order to be effective.

Fraud Risk Assessment

As previously reported, on January 22, 2008, the commission authorized a Special Investigative Committee to conduct a thorough internal investigation based on the audit recommendations. On December 3, 2008, the Special Investigative Committee issued its final report (the McKay Report). The report was reviewed with the commission in public session on December 9, 2008.

The investigation identified ten findings of civil fraud and eight recommendations for organizational improvement. The investigation identified areas in which policies or laws were violated but fraud was not established, and also identified areas in which neither violations of law nor fraud were established or where the conclusions of the state audit were not substantiated by fact. In response to the findings and recommendations of the McKay Report, the chief executive officer has taken disciplinary action and implemented reforms that will be completed by the end of 2009.

One of the reforms being implemented by the port is a comprehensive workplace responsibility program. The program will incorporate various port policies (including employee ethics, fraud awareness and prevention, whistleblower reporting procedures, anti-harassment and other related policies) into one comprehensive, sustainable program. The program will emphasize training and a heightened awareness of the importance of these compliance issues for port employees.

The compliance program is built upon a new statement of values and code of conduct. It includes robust, regular training, thorough communication with staff, and structured accountability for reporting of alleged violations, prompt and fair investigation, and consistent and appropriate discipline.

Construction Management Practices

In response to the SAO Audit, there have been concrete changes in three areas of construction management: change order estimates, contract schedule requirements, and small works contracting practices.

The port conducted a review of change order estimates prepared by contractors and internal port staff prior to request for approval. The SAO had been concerned by occurrences where estimates by staff matched contractor estimates. The following steps were taken:

- The Internal Audit Manager conducted an audit of change order markups and recovered \$3,285 of overpayments to contractors, and the Construction Management and Contract Administration departments recovered an additional \$8,896. These results were reviewed with senior management and the Audit Committee.

- New standard operating procedures for generating change order estimates have been written and staff has been trained on change order estimating, negotiations and documentation.
- Change orders now undergo a further independent review by contract administration and construction management before being accepted.

Significant efforts were made to enforce contract schedule requirements.

- All current projects were reviewed for contractual schedule compliance, and non-compliant contracts were issued notification letters requesting submission of the required documentation.
- A team was established to benchmark other government agency practices and policies relating to schedule and schedule compliance. Although port procedures were generally similar to other agencies, a number of “best practices” were adopted. Among them is a requirement that a contractor’s monthly pay request include an updated construction schedule that is then checked to ensure the contractor will complete the contract on time.

Changes have been made to the port’s small works contracting practices to improve the tracking of expenditures, and training was held for all construction managers and contract administrators within Port Construction Services on the revised procedures. In addition, the Central Procurement Office now manages all small works contracting.

Contract Administration Practices

Since establishing the Central Procurement Office, the port has taken action on an additional 13 SAO recommendations related to contracting and contracts administration. We have completed numerous reviews, including:

- Reviews of contract invoices
- Reviews of service agreements for proper competition
- Reviews to check for federal grant violations
- Reviews of service agreements for compliance with current laws and policy

Additionally, a new procurement policy for personal and professional consulting services (CPO-1) was implemented on January 31, 2009. This policy clarifies the competitive process for service agreement procedures; establishes a clearer delegation of responsibility for service directives; clarifies requirements for legal review of service agreements; and improves procedures for small works contracting. The port held 13 full-day training classes for CPO-1 and trained 354 port employees on procurement categories, acquisition planning, contract administration and Resolution No. 3605.

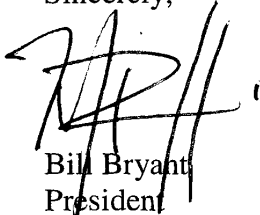
Centralized Project Controls

A team of department representatives undertook a comprehensive evaluation of the Seaport Project Office Tracking System (SPOTS), the Port Aviation Cost Trend (PACT) system, and the Project Management Information System (PMIS), an application used by Port Construction Services. They identified gaps in systems capabilities, sought ways to improve the efficiency of the existing applications, and established requirements for a new enterprise-wide system to

replace SPOTS and PACT. This evaluation was reviewed by the port's ICT Governance Board. On April 21, 2009, the port commission authorized funding for the acquisition of an enterprise project cost management System.

In closing, the 2007 performance audit provided the port commission and the chief executive officer with an opportunity to enhance the effectiveness of port systems and safeguard public resources. The port will continue to review our operations and seek out the practices of other government agencies to ensure that the port has developed and implemented the "best practices" for capital project delivery.

Sincerely,

A handwritten signature in black ink, appearing to be 'Bill Bryant', written over the printed name.

Bill Bryant
President
Port of Seattle Commission