



Office of the Washington State Auditor
Pat McCarthy

Accountability Audit Report

Fort Worden Public Development Authority

For the period January 1, 2018 through December 31, 2020

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

December 27, 2021

Board of Directors
Fort Worden Public Development Authority
Port Townsend, 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 Authority 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 Authority'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,

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, Authority 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 Authority could make improvements. These recommendations are included with our report as findings.

We also noted certain matters related to disbursements and leave usage that we communicated to Authority management and the Board of Directors in a letter dated December 23, 2021. We appreciate the Authority's commitment to resolving those matters.

Additionally, as noted under the Related Reports – Special Investigations section of this report, certain matters were examined and reported as part of a separate engagement.

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 Fort Worden Public Development Authority from January 1, 2018 through December 31, 2020.

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 Authority'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.

Based on our risk assessment for the years ended December 31, 2020, 2019 and 2018, the areas examined were those representing the highest risk of fraud, loss, abuse, or noncompliance. We examined the following areas during this audit period:

- Annual report filing – timeliness and completeness
- Financial condition
- Accounts payable – general disbursements, credit cards, travel expenditures and employee reimbursements
- Payroll – gross wages, leave balances and accruals and leave cash outs
- Accounts receivable – billing, collection and refund of deposits for hospitality reservations
- Transactions with the Fort Worden Foundation

SCHEDULE OF AUDIT FINDINGS AND RESPONSES

Fort Worden Public Development Authority January 1, 2018 through December 31, 2020

2020-001 The Authority's internal controls over filing annual financial reports were inadequate for ensuring compliance with state reporting requirements.

Background

The Board of Directors, the public and others rely on the information included in the financial statements and reports to make decisions. Authority management is responsible for designing, implementing and maintaining internal controls that provide reasonable assurance financial reporting is reliable.

State law (RCW 43.09.230) requires the Authority to submit annual financial reports to our Office within 150 days after the end of each fiscal year. The annual financial reports include financial statements, supporting schedules and notes to the financial statements.

Description of Condition

The Authority did not adequately monitor its operations to ensure it filed its 2018, 2019 and 2020 annual reports with our Office in a timely manner. The Authority filed its 2018, 2019 and 2020 annual reports with our Office 743, 372 and 155 days late, respectively.

Cause of Condition

The Authority experienced turnover in key accounting and other staff positions, as well as staffing reductions starting in 2020. Prior audits found financial statements were unreliable. This required significant effort from new staff to correct prior errors, resulting in the Authority preparing and submitting late annual reports to our Office.

Effect of Condition

Filing financial reports late hinders public transparency, as well as our Office's efforts to compile statistical financial information for the Legislature and others. Late filings also prevent our Office from auditing the Authority's financial

statements, which prevents the public and other interested parties from obtaining timely and accurate information about the Authority's fiscal operations. Additionally, without timely access to financial reports, the Board and management cannot effectively monitor or make appropriate financial decisions regarding the Authority's operations.

Recommendation

We recommend the Authority establish and follow internal controls for ensuring it submits accurate, complete and timely financial reports in accordance with state law.

Authority's Response

We concur with this Finding and the recommendation. We cannot speak for the previous administration reasons for the late filings. Our efforts have been to catch up with required filings and have successfully filed for 2018, 2019 and 2020. We see no need to change internal procedures other than to enforce what is already in place to timely file future reports.

We want to thank the Audit Team for their support in helping address and correct the false 2018 filing.

Auditor's Remarks

We appreciate the Authority's commitment to resolve this finding and thank the Authority for its cooperation and assistance during the audit. We will review the corrective action taken during our next regular audit.

Applicable Laws and Regulations

RCW 43.09.230, Local government accounting, Annual reports

The *Budgeting, Accounting, and Reporting System* (BARS) manual, Chapter 3, Accounting Principles and Internal Control

The *Budgeting, Accounting, and Reporting System* (BARS) manual, Chapter 4, Reporting Principles and Requirements

SCHEDULE OF AUDIT FINDINGS AND RESPONSES

Fort Worden Public Development Authority January 1, 2018 through December 31, 2020

2020-002 The Authority's financial condition puts it at risk of not being able to meet financial obligations.

Background

State law (RCW 35.21.730-755) allows cities and counties to create public development authorities, which are public corporations that perform duties to improve local government administration and efficiency. The specific purpose of an Authority is defined by its charter and the ordinance or resolution that created it. The City of Port Townsend created the Fort Worden Public Development Authority to enhance the Fort Worden State Park and implement a Lifelong Learning Center there. The Authority's main revenue source comes from fees for management and operation of visitor and hospitality services within the 90-acre main campus.

Description of Condition

As noted in finding 2020-001 of this report, the Authority only recently filed its 2018 and 2019 financial statements, and did not file its 2020 financial statements until our audit was almost complete. We analyzed the Authority's financial condition for fiscal years 2018 and 2019 based on unaudited financial information, and we found the following:

- As of fiscal year end 2019, the Authority only had enough cash to operate for an estimated 22 days. This indicates the Authority's resources for properly responding to emergencies, including unexpected revenue losses and spending increases, may be inadequate. We further noted that 67 percent of reported 2019 ending cash and investments was restricted to certain uses. Removing restricted cash dropped the estimated cash balance sufficiency down to just seven days.
- Operating margin, which is the difference between operating revenues and expenses, was negative 26.2 percent for 2019. A negative operating margin indicates the Authority may be spending more money than it is generating. As such, the Authority will need to increase revenues and/or decrease spending to remain sustainable.

- Estimated ending cash and investments decreased \$687,499 from fiscal year end 2018 to 2019. Much of the decline was attributed to a \$3.1 million increase in operating expenses during that period.

The Authority's financial condition suffered further declines in 2020. In response to the COVID-19 pandemic, Washington's Governor ordered precautionary measures to slow the spread of the virus. These measures included canceling public events, limiting public gatherings, and restricting travel and non-essential activities. Since the Authority's main revenue sources are from tourist and hospitality services, these restrictions had a severe financial effect on the Authority, which was already struggling. We analyzed the Authority's bank statements, and we determined cash further declined about \$379,857 during 2020. Additionally, the Authority's former Chief Operations and Finance Officer used funds set aside to pay for capital projects to cover operating expenses. As a result, the Authority did not have enough funds to pay its contractors. The Authority had \$880,778 in unpaid construction invoices as of the end of 2020, and it could not apply for grant reimbursement until after it paid the invoices.

COVID-19 restrictions started to lift in 2021 and the Authority took steps to address its financial condition. The Authority's bank statements indicate ending cash increased \$316,956 from January to July 2021. The Authority also paid its outstanding construction invoices.

Additionally, the Authority had an estimated \$3.2 million in outstanding revenue bonds at the end of 2019. Payment for these bonds became difficult because of the Authority's declining financial condition. The Authority refunded this debt in September 2021, deferring payments to 2023.

The Authority has recently taken other significant steps to address lost revenues and manage cash flows. These steps include changing its leadership, organizational restructuring and renegotiating its contract with the Washington State Parks and Recreation Commission.

Cause of Condition

The Authority experienced turnover in key accounting and other staff positions, as well as staffing reductions starting in 2020. Prior audits found financial statements were unreliable. This required significant effort from new staff to correct prior errors, resulting in delayed financial reports to the Board of Directors. Without timely and reliable financial information, management and the Board of Directors cannot effectively monitor and make appropriate financial decisions to ensure the Authority can maintain operations.

The Authority's revenues were also significantly reduced throughout 2020 because of the state's restrictions in response to the COVID-19 pandemic.

Effect of Condition

The Authority's financial condition puts it at risk of not being able to meet financial obligations, continue enhancing Fort Worden State Park, and providing services at the park, as its charter establishes.

Recommendation

Although the Authority has recently taken significant steps to improve its financial condition, we recommend management and the Board of Directors continue monitoring and evaluating the Authority's financial activities to ensure it follows its financial plan and achieves the desired results. We also recommend revising the plan as needed to resolve the Authority's cash flow and sustainability issues. Finally, we recommend the Authority ensure accurate and timely financial information is available to inform the Board's decisions.

Authority's Response

We acknowledge and agree with this Finding and will continue to progress to improve the condition of the Authority. A review of what has been accomplished might help set the stage for this response. The Authority has made significant progress, yet there remain some critical parts to complete. We have attempted below to list what has been accomplished and what remains:

Several matters have been closed out and have been put into place that will allow us to progress forward on toward full recovery of the Authority's weakened financial condition. Many of these steps are outlined below and may not represent fully all the actions taken:

- *Timely approved 2021 Budget*
- *Implemented key staff transitions*
- *Implemented City Code revisions*
- *Implemented Board transition*
- *Completion of Makers Square*
- *Completion of KTPZ Capital Investment in Makers Square*
- *Completion of the Historic Tax Credits*
- *Acquired bridge financing to close project payables*

- *Obtained appropriation of Makers Square Grant for \$712,000 in continued project investments*
- *Reconciliation of financials from 2015 to 2020*
- *Filing of Past Due Annual Reports for 2018, 2019 and 2020*
- *Maintained operations through 2021 summer season*
- *Finalized refinancing of outstanding loans for Glamping and Energy*
- *Implemented reorganization measures*
- *Drafted new partner relations terms*
 - *Drafted implementing documents i.e. Lease, Lease Assignment, Operating Agreement, Rental Agreement*
- *Executed Hospitality Concession Agreement*
- *Executed Amendment #4 to the Master Lease with State Parks*
- *Completed all submittals requested by the State Auditor's Office as a part of the Accountability Audit and Fraud Investigation*
- *Responded to a record high amount of public records requests*
- *Brought all past due accounts payables to current status*
- *Developed a financial forecasting and budget tool*

We may have omitted a few others, but this past year and half has been very focused on responding to the internal and external impacts associated with a variety of forces that continue to present an existential threat to the PDA and the Fort.

There are yet some remaining matters that will be addressed in 2021. Action will allow the PDA to continue progress on its final measures to secure the future of the PDA:

- *Seating members of the Board to assist the Executive Director with two Task Force assignments*
 - *Future modifications to improve Hospitality Services*
 - *Implementing new future partner relations terms*
- *Seating members of the Board to a Finance and Audit Committee to assume the following initial tasks:*
 - *Review 2021 financial close out*
 - *Review of SAO Accountability Audit Findings*
 - *Develop and recommend 2022 Annual Budget*
 - *Develop 2022 Capital Improvement Plan:*
 - *Implement next phase of Makers Square Site Development using state grant*
 - *Implement next phase of Work Force Housing Bldg. 203 Project using County Funds*

- *Implement completion of Glamping using Restoration Bond proceeds*
- *Approval of Property Management Agreement with Fort Worden Foundation*
- *Approval of County Grant Debt Security Agreement*

The last two bullets are key to allow the PDA to close the Restoration Bond. This bond is key to addressing the financial condition of the PDA. It will restore critical capital and operating cash necessary to survival of the PDA. It will also establish two credit lines to support operational cash flows and debt reserves.

Auditor's Remarks

We thank the Authority for its response and appreciate the steps the Authority is taking to improve its financial condition. We will review the corrective action taken during our next audit. We are grateful for the Authority's cooperation and assistance during the audit process.

Applicable Laws and Regulations

RCW 43.09.200, Local government accounting, Uniform system of accounting

The *Budgeting, Accounting and Reporting System* (BARS) manual, Chapter 3, Accounting Principles and Internal Control

RELATED REPORTS

Special investigations

The State Auditor's Office issued a report on a misappropriation of public funds at the Authority. That report is available on our website, <http://portal.sao.wa.gov/ReportSearch>.

INFORMATION ABOUT THE AUTHORITY

The Washington State Parks & Recreation Commission (Washington State Parks), recognizing Fort Worden’s unique setting and historic attributes, adopted the 2008 Fort Worden Facility Use and Development Plan to transform the fort into a financially self-sustaining Lifelong Learning Center.

The Fort Worden Lifelong Learning Center Public Development Authority (PDA) was created by the City of Port Townsend on September 19, 2011 to provide an independent legal entity to work in a partnership with State Parks to manage, promote, develop, secure funding, and enhance Fort Worden State Park. In November 2013, the PDA entered into a Master Lease with Washington State Parks to operate and manage the properties located within the 90-acre main campus of Fort Worden State Park. The Authority develops the necessary agreements and partnerships for the use, operation, management, and renovation of state-owned facilities and properties within Fort Worden, as well as manages and operates visitor and hospitality services within the campus area.

The Authority is governed by an 11-member Board of Directors who are appointed by the City of Port Townsend. The Board appoints an Executive Director to oversee the Authority’s daily operations and staff. The Authority reported operating and capital expenditures of \$3.2 million, \$10.8 million and \$6.7 million in 2020, 2019 and 2018, respectively.

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 the Fort Worden Public Development Authority 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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