

Joint Transportation Committee

Management and Support Operating Costs Final Report

Washington State Department of Transportation Ferries Division
Financing Study II



Prepared For:

Joint Transportation Committee
Washington State Legislature

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Joint Transportation Committee

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Executive Summary

The 2007 Legislature directed the Joint Transportation Committee (JTC) to review the Washington State Department of Transportation (WSDOT) Ferries Division (Ferries) operating administrative costs (ESHB 1094 §205(1)(b)(iii)).

This report will:

- Inform Ferries long-range planning and associated farebox recovery projections.
- Provide information critical to the long-term financing studies currently being conducted, at the direction of the legislature, by the JTC and the Washington State Transportation Commission (WSTC) (ESHB 1094 § 206(2) & § 205 (1)(c)(ii)).
- Inform future Ferries fare policies.

A. Scope of Report

The Legislature directed this review of Ferries operating administrative costs. Ferries designates these costs as “management and support costs” for the operating program. These costs when added to terminal and vessel operating and maintenance costs are included in Ferries’ farebox recovery calculation.¹ This report utilizes Ferries’ “management and support costs” designation within the farebox recovery model to examine operating administrative costs. This report:

- Identifies components of management and support costs;
- Evaluates and makes recommendations on the reasonableness and management of those costs; and
- Discusses options for inclusion of operating administrative costs within “management and support costs” for purposes of calculating farebox recovery.

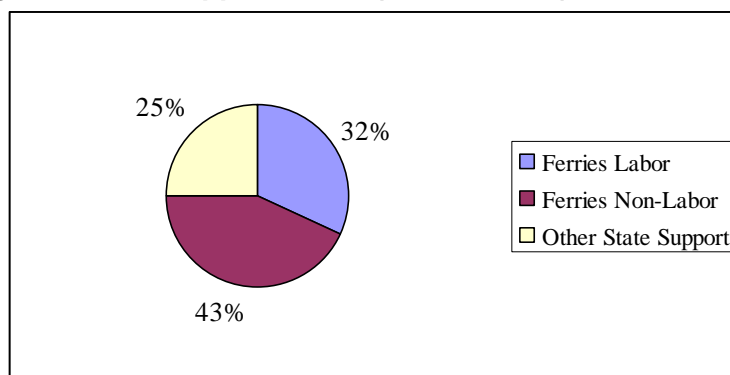
In FY 2006, management and support costs included in the farebox recovery calculation included both management and support costs incurred directly by Ferries, and a pro-rated portion of management and support costs incurred by WSDOT.

The total management and support costs for the 2005-07 biennium reviewed in this report were \$68.4 million and included:

- Ferries labor – \$21.8 million;
- Ferries non-labor expenses – \$29.5 million; and
- Other state support – \$17.1 million.

¹ Farebox recovery shows the percentage of Ferries’ operating costs recovered by revenues from the farebox and other non-tax sources of income (i.e., concessions).

Management and Support Costs (\$68.4 million), 2005-07 Biennium



Sources. The consultants reviewed the 2005-07 biennium organization chart, FY 2006 draft route statements that show farebox recovery, financial reports produced by Ferries, and information provided by the Office of Financial Management (OFM) and Ferries on the marine insurance program.

B. Direct Management and Support Costs

Ferries management and support costs (Ferries labor and Ferries non-labor costs in the chart above) in the 2005-07 biennium totaled \$51.3 million or 75 percent of all management and support costs included in the farebox recovery calculation. Of this \$51.3 million, \$21.8 million was for labor and \$29.5 million for non-labor costs.

Labor Management and Support Costs (\$21.8 million): Ferries has a total staff of 1,629 full-time equivalent (FTE) positions of which 1,309 (80 percent) are direct vessel, terminal, and maintenance staff. The other 320 staff (20 percent) are at headquarters, of which 149 are operating budget management and support staff (included as Ferries labor costs in the calculation of farebox recovery) and 30 are in the WSDOT information technology budget (included as “other state support” in the calculation of farebox recovery). The remaining 141 headquarter positions are budgeted in the capital budget and are not included in the calculation of farebox recovery.²

The 149 FTE operating budget positions are 10 percent of the total FTEs in the operating budget and 9 percent of total operating labor costs.

Consultant Observation: The consultants believe that having 10 percent of total operating FTEs in management and support is an acceptable level of administrative staffing. This level of staff is within a normal range of administrative staffing and is warranted by the extent and complexity of Ferries’ operating environment.³

² The capital positions are discussed in the *Capital Program Staffing and Administration, WSDOT Ferries Division Financing Study II, Final Report* April 2008.

³ The *Washington State Ferries Financing Study Final Report*, January 2007, provides a review of the labor, community outreach and complexities involved in operating the nation’s largest ferry service.

Non-Labor Management and Support Costs (\$29.5 million for 2005-07 biennium): The largest non-labor expenses are insurance, rents/leases, services, merchant discount fees/bank charges, and management and organizational expenses.

- ***Insurance (\$9.2 million⁴):*** Ferries is not included in the State of Washington’s self-insurance program. Ferries carries its own marine insurance for commercial property and liability coverage for terminals and vessels, for a total premium of \$9.7 million in the 2005-07 biennium (\$0.5 million is paid by WSDOT and included in the “Other State Support” category in farebox recovery calculations). The policy has a \$1 million deductible and includes a \$225 million excess protection and indemnity insurance.

Ferries has collected \$10.2 million in insurance claims since 1990, with the largest recovery being \$3 million paid in 2002 on property damage from the operation of passenger-only ferry service in Rich Passage. Ferries has had some misunderstandings of the coverage that have been clarified and may result in additional claims.

Recommendation 1: OFM, WSDOT and Ferries should review the marine insurance program to determine whether it is cost-effective versus being self-insured, including the Ferries terminal property, hull and machinery, war risk, and liability coverages.

Recommendation 2: If OFM, WSDOT and Ferries conclude that it is cost-effective to continue to retain commercial insurance, the coverages and deductibles should be reviewed. Consideration should be given to optional deductible limits above the current \$1 million.

Recommendation 3: Ferries should ensure that it has a full understanding of the coverages provided if it continues to procure commercial insurance. Ferries should also ensure that, as it implements the administrative cost allocation requirements of ESHB 2358, consideration is given to the insurer’s requirements to distinguish direct labor from administrative overhead costs that are allocated to capital projects. This will facilitate Ferries’ claims management.

- ***Rent and Leases (\$4.4 million):*** Major expenses are \$2.4 million in rent for the Ferries headquarters space in Seattle, \$0.8 million for warehouse rent in Seattle; and \$0.5 million for rent of meeting rooms and other temporary facilities.
- ***Services (\$3.7 million):*** Major expenses are \$1.1 million for temporary employment services and \$1.0 million for services rendered by other state agencies (\$1.0 million), with the remainder for a variety of miscellaneous services such as participation in the on-call, oil-response program, and human resources services.

⁴ Total insurance costs included in farebox recovery are \$17.3 million including costs included in Other State Support – or 25 percent of all management and support costs.

Recommendation 4: Ferries, WSDOT and OFM should review Ferries' temporary employment expenditures and determine which, if any, of the temporary positions should be created as permanent positions, with particular attention to those used to meet new workload requirements.

- *Merchant Fees/Bank Charges (\$2.6 million):* Ferries expended \$2.5 million on merchant discount fees (fees charged by credit card companies to Ferries when customers pay by credit card). This represents 0.9 percent of farebox revenues of \$283.7 million. Ferries accepts both Discover and American Express, which have higher fees than Visa and MasterCard. Visa and MasterCard were 90 percent of all credit card transactions during the biennium.

Recommendation 5: Ferries should consider accepting only Visa and MasterCard, which have lower merchant discount fees.

- *Management and Organizational Expenses (\$1.8 million):* Management and organizational expenses are consultant expenses including revenue forecasting, terminal and vessel design services, development of an annual report, establishment of new revenue controls, development of an electronic fare system policy and procedures manual, and coordination of non-farebox revenues, such as concessions. Ferries uses an on-site consultant, who served in this capacity for longer than a year, for promotion of concession facilities.

Recommendation 6: Ferries should review its use of long-term on-site consultants.

C. WSDOT Management and Support (Other State Support) Allocated from WSDOT

The category in the farebox recovery calculation identified as “other state support” is charges from WSDOT, some of which are passed to WSDOT by other state agencies. WSDOT’s total charges for the 2005-07 biennium calculation of farebox recovery were \$17.5 million or 25 percent of all management and support costs included in farebox recovery.

There are three ways in which WSDOT expenses included in the calculation of farebox recovery were handled in the 2005-07 biennium:

- 1) Charging Motor Vehicle Account expenses to the Puget Sound Ferry Operations Account (\$9.7 million in the 2005-07 biennium);
- 2) Absorbing the costs within the Motor Vehicle Account and not charging the costs to the Puget Sound Ferry Operations Account (\$7.5 million);
- 3) Charging WSDOT expenses to the Ferries Operating budget (\$0.3 million) (Program X).⁵

⁵ Administrative expenses charged to the Ferries operating budget are expended in the Puget Sound Ferry Operations Account as part of Ferries' operating budget. Other WSDOT expenses charged to the Puget Joint Transportation Committee

WSDOT also incurred \$1.4 million in expenses in support of the electronic fare system that were not accounted for in farebox recovery.

WSDOT Policy: Inter-Fund Charges and Charges to Ferries Budget: WSDOT does not have a clear policy, and the legislature has not provided policy guidance, on which Motor Vehicle Account expenses to charge to the Puget Sound Ferry Operations Account nor on which WSDOT expenses to bill directly to the Ferries operating budget.

In some cases WSDOT services that benefit Ferries are charged to the Puget Sound Ferry Operations Account, in some to Ferries operating budget, and in others to the Motor Vehicle Account. In some cases the Motor Vehicle Account absorbs the costs, but in other cases the Motor Vehicle Account charges the Puget Sound Ferry Operations Account for expenses. Historically the legislature has transferred Motor Vehicle Account money to the Puget Sound Ferry Operations Account beyond the statutorily required amount, resulting in a circular movement of funds when the Motor Vehicle Account charges the Puget Sound Ferry Operations Account.

Recommendation 7: The legislature and WSDOT should develop a consistent policy on expenses to be charged from the Motor Vehicle Account to the Puget Sound Ferry Operations Account. The policy should specifically address whether administrative indirect charges, such as WSDOT Executive Management, are to be charged to the Ferry Operations Account.

Recommendation 8: If the policy is to include Motor Vehicle Account administrative indirect expenses in charges to the Puget Sound Ferry Operations Account, such charges should be distinguished from costs incurred in the direct delivery of ferry services.

Recommendation 9: The legislature and WSDOT should develop a consistent policy on expenses to be charged directly to the Ferries operating budget.

WSDOT Executive Management Charges: WSDOT charged the Puget Sound Ferry Operations Account \$1.6 million for executive management services in the 2005-07 biennium, including a \$0.9 million charge for services from the Management and Support (S1) program, which includes the Secretary of Transportation and other WSDOT executive staff, charges for an Office of Equal Opportunity (OEO) officer, and charges for two tort claims investigators in the WSDOT Risk Management Office in the Risk Management (S2) program.

Recommendation 10: WSDOT should not charge the Puget Sound Ferry Operations Account for S1 Executive Management if such charges are not made to other transportation related accounts. If WSDOT does continue to charge S1

Sound Ferry Operations Account are shown as separate WSDOT charges in the Fund, but are not included in the Ferries operating budget.

expenditures to the Ferry Operations Account, the charges should be periodically reviewed and updated.

Recommendation 11: WSDOT should review the consistency of its practice in charging for OEO officers. The Ferries Executive Management budget should not be charged for the expense of an OEO officer unless other WSDOT budgets are also charged for such expenses.

WSDOT Information Technology Charges: The Puget Sound Ferry Operations Account was charged \$8.4 million in the 2005-07 biennium for WSDOT information technology services, of which \$0.2 million was for information technology administration. In the 2007-09 biennium, WSDOT is not charging to the Puget Sound Ferry Operations Account for such services. The remaining \$8.2 million in charges was to support the information technology 30 FTEs included in Ferries' headquarters organization chart and to provide Ferries information technology services. WSDOT will continue to charge Ferries for these services in the 2007-09 biennium.

Recommendation 12: WSDOT should continue the practice adopted in the 2007-09 biennium of not charging sub-program C1 Information Technology Administration expenses to the Puget Sound Ferry Operations Account.

Recommendation 13: WSDOT should make a determination of whether Information Technology (Program C) expenses should continue to be charged to the Puget Sound Ferry Operations Account, as part of its policy review of charges from the Motor Vehicle Account to the Puget Sound Ferry Operations Account.

WSDOT Other Government Charges: In the 2005-07 biennium, expenditures from WSDOT Program U – Charges from Other Agencies included in Ferries farebox recovery calculation totaled \$6.6 million. These charges include: costs incurred by the Attorney General in defending Ferries' tort claims, Ferries excess insurance premium, and Ferries claims payments. Prior to the 2003-05 biennium, these expenses were paid from the Puget Sound Ferry Operations Account. These charges all relate to Ferry insurance and risk management, bringing the total insurance related costs in the farebox recovery calculation to \$17.3 million or 25 percent of all management and support costs.

Recommendation 14: Ferries should not include risk management administration fees in its calculation of farebox recovery because the charge is no longer allocated between WSDOT and Ferries.

Recommendation 15: In addition to reviewing the Marine Insurance Program, WSDOT, OFM, and Ferries should review the range of costs incurred by the State in providing insurance, risk management services, and claims defense to determine what, if any, costs could be reduced.

D. Management Communication and Oversight

Farebox recovery is a key indicator in setting ferry fares and is often used to compare Ferries' performance to that of other transit agencies. It is, therefore, important that the legislature and the public have a clear understanding of what is included and excluded as costs in the farebox recovery calculation.

Expenses in Farebox Recovery: A key policy question is which expenses to include and exclude in farebox recovery. Alternatives for costs to be included range from counting only operating costs included in Ferries' operating budget (Program X) to counting all costs incurred by the State in delivering ferry services, which would include costs not presently part of Ferries' farebox recovery calculation, such as the Marine Employees Commission and security provided by the Washington State Patrol. The legislature has directed Ferries to exclude security related costs, but WSDOT's information technology charges included in farebox recovery include their costs in support of the security plan.

Recommendation 16: Ferries and the legislature should develop a policy on what costs are to be included in farebox recovery. The consultants recommend that all costs charged to the Puget Sound Ferries Operations Account be included in farebox recovery, as this methodology would tie most directly to the level of fares needed to meet the legislatively adopted 16-year financial plan.

Recommendation 17: The legislature should clarify its intent in excluding security costs from the calculation of farebox recovery so that WSDOT expenses can be properly included or excluded based on that direction.

Legislative Oversight Communication: Ferries has provided different information on management and support costs in response to legislative inquiries, which makes it more difficult for the legislature to understand these costs. Ferries has historically calculated farebox recovery on an annual basis, which does not align with the State's biennial budget periods.

Recommendation 18: In order to provide consistent communication with the legislature, Ferries should use a uniform definition of Ferries management and support costs based on costs included in the calculation of farebox recovery.

Recommendation 19: Ferries should provide a biennium farebox recovery calculation to align with the State's budget periods.

The chart below presents the recommendations in this report and WSDOT's responses which are incorporated in the body of the report.

List of Recommendations

Area	Recommendation	WSDOT Response
Ferries Non-Labor Management and Support Costs	1. OFM, WSDOT and Ferries should review the marine insurance program to determine whether it is cost-effective versus being self-insured, including the Ferries terminal property, hull and machinery, war risk, and liability coverages.	Concur
	2. If OFM, WSDOT and Ferries conclude that it is cost-effective to continue to retain commercial insurance, the coverages and deductibles should be reviewed. Consideration should be given to optional deductible limits above the current \$1 million.	Concur
	3. Ferries should ensure that it has a full understanding of the coverages provided if it continues to procure commercial insurance. Ferries should also ensure that, as it implements the administrative cost allocation requirements of ESHB 2358, consideration is given to the insurer's requirements to distinguish direct labor from administrative overhead costs that are allocated to capital projects. This will facilitate Ferries' claims management.	Concur
	4. Ferries, WSDOT, and OFM should review Ferries' temporary employment expenditures and determine which, if any, of the temporary positions should be created as permanent positions, with particular attention to those used to meet new workload requirements.	Concur
	5. Ferries should consider accepting only Visa and MasterCard, which have lower merchant discount fees.	Concur
	6. Ferries should review its use of long-term on-site consultants.	Concur
WSDOT Management and Support (Other State Support)	7. The legislature and WSDOT should develop a consistent policy on expenses to be charged from the Motor Vehicle Account to the Puget Sound Ferry Operations Account. The policy should specifically address whether administrative indirect charges, such as WSDOT Executive Management, are to be charged to the Ferry Operations Account.	Concur
	8. If the policy is to include Motor Vehicle Account administrative indirect expenses in charges to the Puget Sound Ferry Operations Account, such charges should be distinguished from costs incurred in the direct delivery of ferry services.	Concur
	9. The legislature and WSDOT should develop a consistent policy on expenses to be charged directly to the Ferries operating budget.	Concur
	10. WSDOT should not charge the Puget Sound Ferry Operations Account for S1 Executive Management if such charges are not made to other transportation related accounts. If WSDOT does continue to charge S1 expenditures to the Ferry Operations Account, the charges should be periodically reviewed and updated.	Concur

Area	Recommendation	WSDOT Response
	11. WSDOT should review the consistency of its practice in charging for Office of Equal Opportunity (OEO) officers. The Ferries Executive Management budget should not be charged for the expense of an OEO officer unless other WSDOT budgets are also charged for such expenses.	The Department will review and make changes if warranted.
	12. WSDOT should continue the practice adopted in the 2007-09 biennium of not charging sub-program C1 Information Technology Administration expenses to the Puget Sound Ferry Operations Account.	Concur
	13. WSDOT should make a determination of whether Information Technology (Program C) expenses should continue to be charged to the Puget Sound Ferry Operations Account, as part of its policy review of charges from the Motor Vehicle Account to the Puget Sound Ferry Operations Account.	Concur
	14. Ferries should not include risk management administration fees in its calculation of farebox recovery because the charge is no longer allocated between WSDOT and Ferries.	The Department will work with OFM and the legislature to determine appropriate farebox recovery calculation.
	15. In addition to reviewing the Marine Insurance Program, WSDOT, OFM, and Ferries should review the range of costs incurred by the State in providing insurance, risk management services and claims defense to determine what, if any, costs could be reduced.	Concur
Management Communication and Oversight	16. Ferries and the legislature should develop a policy on what costs are to be included in farebox recovery. The consultants recommend that all costs charged to the Puget Sound Ferries Operations Account be included in farebox recovery, as this methodology would tie most directly to the level of fares needed to meet the legislatively adopted 16-year financial plan.	Concur
	17. The legislature should clarify its intent in excluding security costs from the calculation of farebox recovery so that WSDOT expenses can be properly included or excluded based on that direction.	The Department will work with OFM and the legislature to determine appropriate farebox recovery calculation.
	18. In order to provide consistent communication with the legislature, Ferries should use a uniform definition of Ferries management and support costs based on costs included in the calculation of farebox recovery.	Concur
	19. Ferries should provide a biennium farebox recovery calculation to align with the State's budget periods.	Concur

Section I. Purpose and Scope of Review

A. Purpose

The 2007 Legislature directed the Joint Transportation Committee (JTC) to review the Washington State Department of Transportation (WSDOT) Ferries Division (Ferries) operating administrative costs (ESHB 1094 §205(1)(b)(iii)).

Farebox recovery measures the percentage of Ferries' operating costs that are recovered by the farebox and other direct income sources (i.e., concessions). The calculation of farebox recovery includes a category of expense identified as management and support which, in response to the legislative direction to review Ferries administrative costs, is the focus of this study.

This report provides information on Ferries' management and support expenses that will inform development of a revised Ferries Long-Range Plan and associated farebox recovery projections, as required by ESHB 2358. In addition, this report provides information critical to the long-term financing studies currently being conducted, at the direction of the legislature, by the JTC and the Washington State Transportation Commission (WSTC) (ESHB 1094 § 206(2) & § 205 (1)(c)(ii)). This study will also help inform future Ferries fare policies.

B. Scope of Report

The Ferries' budget is divided into an operating program, which maintains and operates the vessels and terminals, and a capital program, which preserves and improves the vessels and terminals. This report looks only at the operating program and specifically at those charges identified in Ferries' farebox recovery model as management and support.

This report:

- Identifies components of management and support costs;
- Evaluates and makes recommendations on the reasonableness and management of those costs; and
- Discusses options for inclusion of operating administrative costs within "management and support costs" for purposes of calculating farebox recovery.

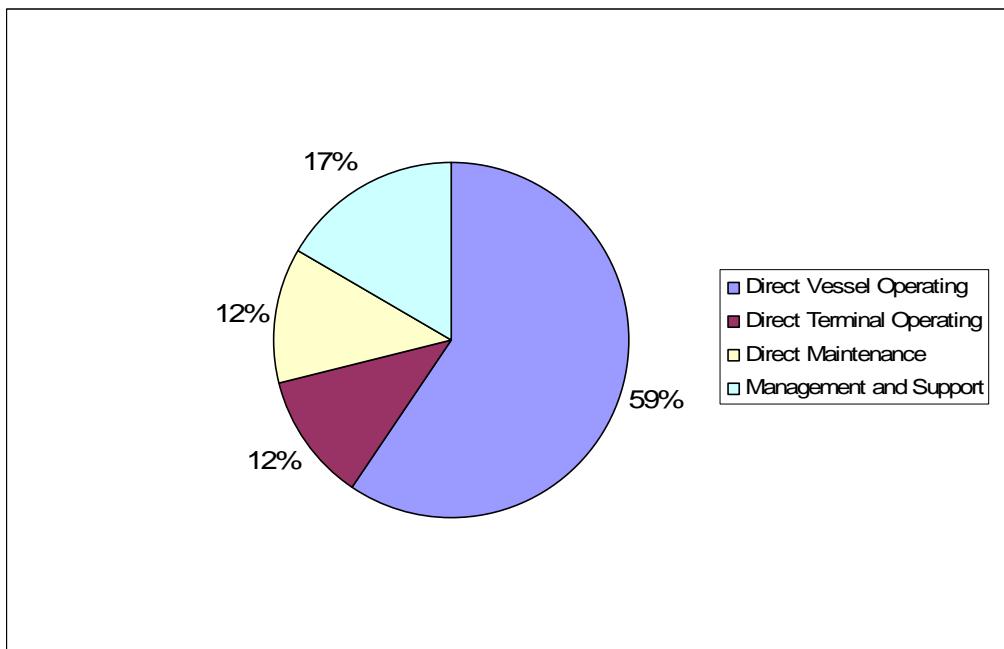
C. Farebox Recovery

Farebox recovery shows the percentage of Ferries operating costs that are recovered by revenues from the farebox and other non-tax sources of income (i.e., concessions). By legislative direction, security costs are not included in the calculation of farebox recovery

(ESHB 1094 §225(6)). In FY 2006, farebox recovery was at 74 percent,⁶ with \$0.2 million in Ferries' security costs excluded from the calculation.

Operating costs of \$191.4 million were included in the calculation of FY 2006 farebox recovery. Costs included were direct terminal expenses (\$22.5 million), direct vessel expenses (\$113.6 million), direct maintenance expenses (\$23.4 million), and management and support expenses (\$31.9 million). This report looks at management and support expenses, which in FY 2006 were 17 percent of all costs included in the farebox recovery calculation, as shown in the figure below.

**Figure 1
Farebox Recovery Costs, FY 06**

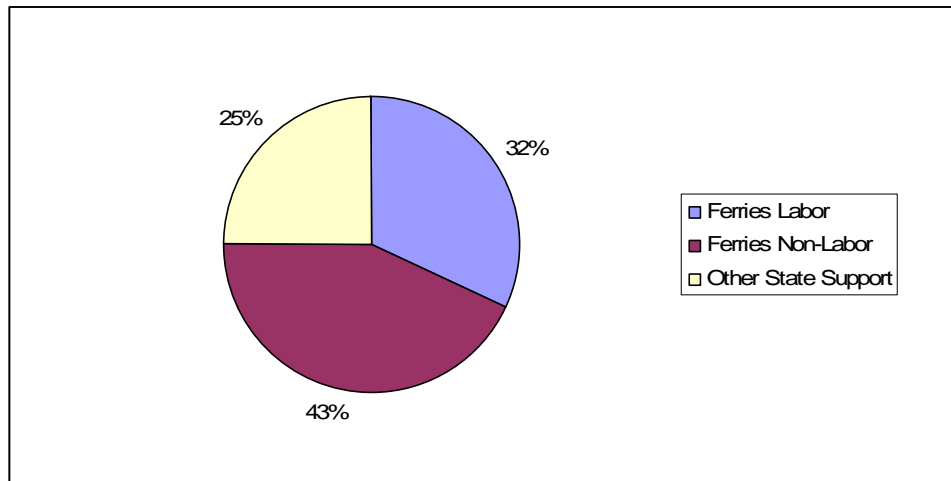


D. 2005-07 Biennium Management and Support Expenses

Management and support expenses in the farebox recovery model include Ferries labor, Ferries non-labor expenses, and other state support. Total management and support expenses for the 2005-07 biennium were \$68.4 million, of which 32 percent (\$21.8 million) was for Ferries labor, 43 percent (\$29.5 million) for Ferries non-labor expenses, and 25 percent (\$17.1 million) for other state support.

⁶ For more information on farebox recovery see *Washington State Ferries Financing Study Final Report, Appendix E. Operating Budget Review*, January 2007. Farebox recovery has not yet been calculated for FY 2007.

Figure 2
Management and Support Costs (\$68.4 million), 2005-07 Biennium



E. Sources and Methods

The consultants used data from the most recent full biennium – 2005-07.

Ferries has cooperated fully in the development of this report. The 2005-07 biennium information that the consultants analyzed for this report was provided by Ferries' finance and human resources systems.

The reports Ferries provided and that consultants used included:

- 2005-07 biennium organization chart;
- FY 06 draft route statements;
- Administrative expenditure and budget data;
- Authorized administrative positions by biennium;
- Administrative expenses for X3 (Operations Management and Support) and X7 (Maintenance Management and Support); and
- X (Operating) program non-labor expenses by subprogram.

In addition, the consultants reviewed the 2007 Marine Insurance Market Specifications and the 2007 Marine Insurance Renewal Proposal.

The consultants also interviewed Ferries, WSDOT, and Office of Financial Management (OFM) staff, and used information received in developing three prior reports: (i) *Washington State Ferries Financing Study Final Report*, January 2007, Appendix E. *Operating Budget Review*; (ii) *Auto-Passenger Vessel Preservation and Replacement Final Report of WSDOT Ferries Division Financing Study II*, January 2008; and (iii) *Capitol Program Staffing and Administration Cost Final Report of WSDOT Ferries Division Financing Study II*, April 2008.

Section II. Ferries Management and Support Costs

This section reviews Ferries labor and non-labor management and support costs in the 2005-07 biennium. Ferries labor and non-labor expenses are 75 percent of all management and support costs included in the farebox recovery calculation. The other 25 percent are categorized as other state support and are reviewed in Section III of this report.

This sections finds that the Ferries management and support staffing is a reasonable percentage of overall Ferries' operating staff (10 percent). The section includes recommendations that would potentially reduce non-labor costs by reviewing the marine insurance program and improving Ferries' claims management, reviewing the use of temporary employees, and reducing merchant discount fees.

A. Overview

Ferries management and support costs for the 2005-07 biennium totaled \$51.3 million, of which \$21.8 (43 percent) was labor costs and \$29.5 million (57 percent) was non-labor costs. Ferries management and support expenditures were in four sub-programs of the Ferries operating budget: Operations Management and Support, Maintenance Management and Support, Finance and Administration, and Executive Management.

Table 1
Ferries' Management and Support Expenses, 2005-07 Biennium
(\$ millions)

Budget Sub-Program	FTE	\$ Labor	\$ Non-Labor	\$ Total
X3 Operations Management and Support	61.00	8.7	12.6	21.3
X7 Maintenance Management and Support	28.00	5.3	2.9	8.2
X8 Finance and Administration	33.00	4.2	9.8	14
X9 Executive Management	27.25	3.6	4.2	7.8
Total	149.25	21.8	29.5	51.3
Percent of Total		43%	57%	

B. Management and Support Labor

1. Staffing Overview

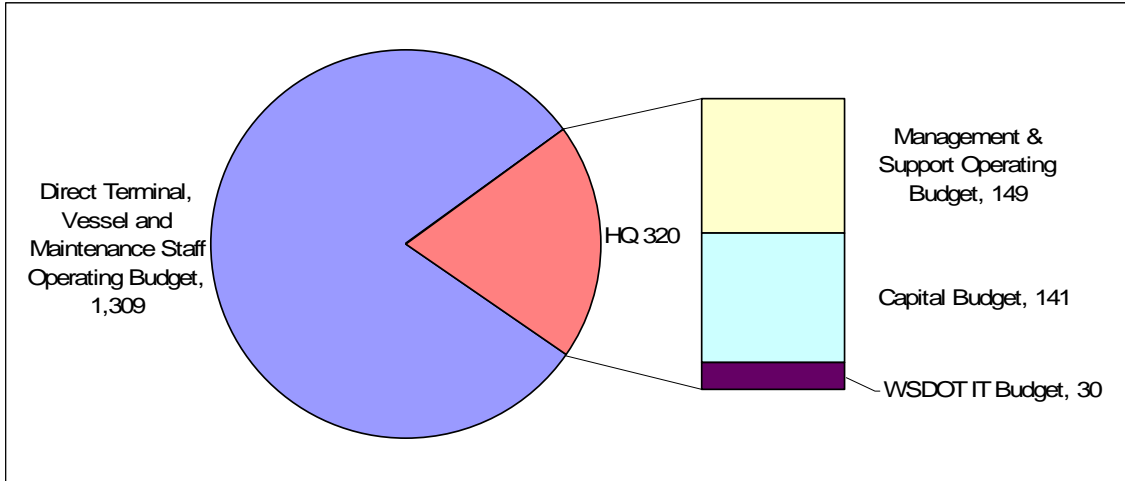
This review is based on the 2005-07 Ferries organization chart. Ferries has a total staff of 1,629 full-time equivalent (FTE) positions of which 1,309 (80 percent) are direct vessel, terminal, and maintenance staff and are included in the farebox recovery calculations. The other 320 staff (20 percent) are at headquarters, of which 149⁷ are operating budget

⁷ One of the 149 positions, the Office of Equal Opportunity Officer, is funded by Ferries but reports to WSDOT. The position is not counted by Ferries as a Ferries' position in their organization chart.

management and support staff, 30 are in the WSDOT information technology budget, and 141 are budgeted in the capital budget.⁸

The 149 management and support positions in the operating budget are the focus of this section.

**Figure 3
Ferries FTEs, 2005-07 Biennium**



2. Management and Support Staff as a Percentage of Total Operating Staff

As shown in the table below, the 149 management and support operating budget FTEs are 10 percent of the total FTEs in the operating budget and represent 9 percent (\$21.8 million) of total operating budget labor costs of \$230.1 million in the 2005-07 biennium. Labor expense of \$21.8 million includes charges from capital staff to the operating budget of \$1.2 million.⁹

⁸ See *Capital Staffing and Administration Final Report of WSDOT Ferries Division Financing Study II*, April 2008, for more information on capital staff.

⁹ See *Capital Program Staffing and Administration, WSDOT Ferries Division Financing Study II, Final Report*, April 2008, p. 20, for further explanation of these charges. Capital staff charges to the operating budget are also reviewed in the *Capital Program Staffing and Administration Appendix* which details these expenses by section.

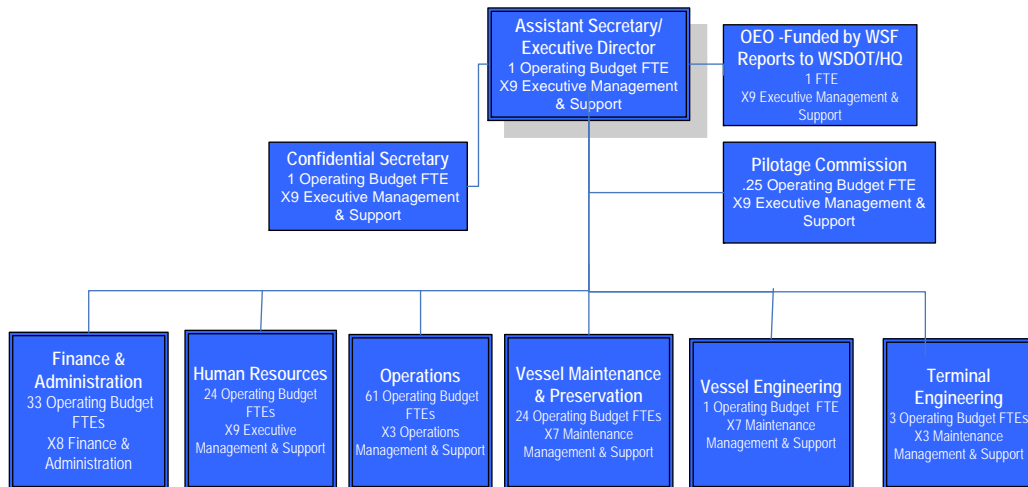
Table 2
Operating Budget Management & Support Staff/Total Operating Budget Staff,
2005-07 Biennium
(\$ millions)

	Budget Sub-Program #	FTE	% FTE	\$ Labor	% Labor
Operations Management and Support	X3	61.00	4%	8.7	4%
Maintenance Management and Support	X7	28.00	2%	5.3	2%
Finance and Administration	X8	33.00	2%	4.2	2%
Executive Management	X9	27.25	2%	3.6	2%
Sub-total Management & Support		149.25	10%	21.8	9%
Vessel & Terminal Maintenance & Operations	X1,2,4,6	1,308.75	90%	208.3	91%
Total		1,458.00		230.1	

3. Management and Support Staff: Organization Chart

The table above shows the number of FTE positions within each budget sub-program. The organization chart below shows the distribution of the management and support positions among the Ferries' divisions.

Figure 4
Management and Support Organization Chart, 2005-07 Biennium



4. Consultant Observations: Ferries Management and Support Labor

The consultants believe that having 10 percent of total operating FTEs in management and support is an acceptable level of administrative staffing. This level of staff is within a normal range of administrative staffing and is warranted by the extent and complexity of Ferries' operating environment. As reviewed in the *Washington State Ferries Financing Final Report*, January 2007, Ferries operation and consequent administrative staffing requirements are affected by labor agreements, required community involvement and outreach in policy development and fare setting, and by the operation of the nation's largest ferry service.

C. Management and Support Non-Labor Costs

1. Non-Labor Cost Overview

Ferries non-labor management and support costs in the 2005-07 biennium were \$29.5 million (37 percent) of total non-labor, non-fuel cost of \$79.5 million in the 2005-07 biennium.

Table 3
Non-Labor, Non-Fuel Cost, 2005-07 Biennium
(\$ millions)

	Budget Sub-Program #	\$	%
Operations Management and Support	X3	12.6	16%
Maintenance Management and Support	X7	2.8	4%
Finance and Administration	X8	9.9	12%
Executive Management	X9	4.2	5%
Sub-Total Management and Support		29.5	37%
Vessel & Terminal Maintenance & Operations	X1,2,4,6	50.0	63%
Total		79.5	

2. Management and Support Non-Labor Costs: Major Expenses

As shown in the table below, 75 percent of the \$29.5 million in management and support non-labor costs in the 2005-07 biennium were for insurance, rent and leases, services (i.e., temporary services, services from other state agencies and physical examinations), merchant discount fees (i.e., fees on credit card transactions) and bank fees, and management and organizational expenses.

The remaining 25 percent of management and support non-labor costs is for a range of expenses from printing, communications, and Attorney General expenses to training and personnel services.

Table 4
Management and Support Non-Labor Costs, 2005-07 Biennium
(\$ millions)

Budget Item	X3	X7	X8	X9	\$ Total	%
	\$ Operations M&S	\$ Maintenance M&S	\$ Finance & Admin	\$ Exec. Mgmt.		
Insurance	9.2				9.2	31%
Rent & Leases	0.1	0.6	3.7		4.4	15%
Services: Temporary, Other State Agencies, Physicals	1.0	0.2	0.8	1.7	3.7	13%
Merchant Discount Fees/Bank Charges			2.6		2.6	9%
Management and Organizational	0.7	0.6	0.3	0.2	1.8	7%
Printing, Books	0.5	0.1	0.7		1.3	4%
Communications	0.2	0.2	0.7		1.1	4%
Payments to Attorney General				0.9	0.9	3%

Budget Item	X3	X7	X8	X9	\$ Total	%
	\$ Operations M&S	\$ Maintenance M&S	\$ Finance & Admin	\$ Exec. Mgmt.		
Supplies & Materials	0.4	0.1		0.2	0.7	2%
Utilities		0.6			0.6	2%
Training & Employee Recognition				0.3	0.3	1%
Equipment - IT & Non-Inventoried	0.1	0.1	0.1	0.1	0.4	1%
Info Technology Services			0.3		0.3	1%
Payments to OEO				0.3	0.3	1%
Advertising	0.2				0.2	1%
General Repairs/Office Machine Maintenance			0.1	0.1	0.2	1%
Transportation Equipment Fund Equipment Rental	0.1	0.1			0.2	1%
Facilities & Services			0.2		0.2	1%
Lodging			0.1		0.1	0%
Outside Repairs, Equip Rental		0.1			0.1	0%
Personnel Services				0.1	0.1	0%
OSC Services				0.1	0.1	0%
Miscellaneous Other Expenses	0.1	0.1	0.3	0.2	0.7	2%
Total	12.6	2.8	9.9	4.2	29.5	

3. Insurance: Findings and Recommendations

a. Marine Insurance Program

Ferries has a marine insurance program that provides coverage for its vessels and terminals. When the State instituted a self-insurance program in FY 1991, a decision was made by the state's Risk Management Advisory Committee and the OFM Risk Management Division to exclude Ferries from the self-insurance program given the unique nature of the risks associated with the provision of ferry service. At the time of this decision, Ferries had a marine insurance program that was continued and is similar to the existing coverage.¹⁰

Ferries' marine insurance program is bid every five years by OFM's Risk Management Division and is subject to annual renewals. Ferries' staff participate in the policy reviews and renewals but are not directly responsible for procuring the coverage. Ferries is responsible for making the business decision on coverages to be provided, including deductibles and other features of the program.

b. Marine Insurance Program Premiums and Coverages

In the 2005-07 biennium, the total premiums were \$9.7 million, of which \$9.2 million was paid by the Ferries' operating budget and \$0.5 million of which was paid by WSDOT (see discussion in Section III on WSDOT insurance charges).

Coverages provided and the biennium premiums are shown in the table below.

¹⁰ Interviews with OFM Risk Management staff indicate that this decision was consistent with overall State policy at the time not to self-insure unique risks where commercial insurance was available.

Table 5
Marine Insurance Program Premium, 2005-07 Biennium
(\$ millions)

Insurance	\$ Premium	% of Premium
Terminals		
Terminal Liability	0.9	
Terminal Property	2.7	
Sub-total Terminals	3.6	37%
Vessels		
Hull & Machinery (\$25 million P&I*)	5.6	
Excess P& I (\$225 million additional coverage)**	0.5	
Sub-total Vessels	6.1	63%
Total Premium	9.7	
* P&I = Protection & Indemnity		
** Premium paid by WSDOT Program U		

- *Vessels:* In the 2005-07 biennium the marine insurance program covered 29 vessels which included 24 auto-passenger ferries, four passenger-only ferries, and a vessel operated by WSDOT North Central Region where State Route 21 crosses the Columbia River. The total insured value of the vessels was \$832 million in FY 2007.
 - *Hull and machinery insurance:* Covers damages to a vessel up to the insured limit for each vessel. The insured limit has been set at 50 percent of the replacement value of the auto-passenger vessels and 100 percent of the replacement value of the passenger-only vessels.
 - *Protection and indemnity insurance:* Covers third party liabilities, such as passenger injuries, up to \$250 million per occurrence.
- *Terminals:* In the 2005-07 biennium, the marine insurance program covered docks, quays, and shoreside facilities at Ferries' 20 terminals and its Eagle Harbor Maintenance and Repair Facility.
 - *Property damage:* Covers property damage to terminals. The total insured value of the terminals and Eagle Harbor was \$354 million in FY 07, which is 100 percent of the estimated replacement value. Coverage is provided for facilities owned by Ferries and for those that are leased (five terminals).
 - *Terminal operators liability:* Covers third party liabilities (i.e., for accidents and injuries) occurring at the terminals or at Eagle Harbor.
 - *Limits:* In the event of earthquake, the terminal policy has a limit not to exceed \$50 million in any one location, subject to a single limit of \$50 million as the result of terminal losses due to earthquake.
- *Deductible:* Ferries' deductible is \$1 million per accident (except passenger-only vessels limits, which are \$250,000), with all coverages combined in the deductible amount. For example, if a terminal is damaged by a vessel, the \$1 million deductible applies to all property, vessel, and third party claims against the policy. For hull and machinery and protection and indemnity coverage, the policy

- provides a stop loss of \$3.5 million for the aggregate of all losses, after which Ferries would have a deductible of \$25,000 per accident or occurrence.
- *War Risk*¹¹: Coverage includes war risk solely on selected vessels.¹² Vessels selected for war risk coverage are those operating on the international route and in the central Puget Sound.
 - *Oil Pollution*: Ferries is self-insured for water pollution liability and has not included this risk in its marine insurance program due to cost.
 - *Marine Engineering Fee*: The insurer rebates to Ferries some of the premium to pay for safety and security expenses. In the 2005-07 biennium, the amount rebated was approximately \$0.5 million.

c. Claims Experience

Since 1990, Ferries, as shown in the table below, has collected \$10.2 million in insurance claims. The 2007 Marine Insurance Market Specifications used to solicit proposals for insurance includes separate lists of vessel hull and machinery losses over \$25,000 and of terminal damage losses over \$25,000. A copy of the two lists is included in Appendix A.

Since 1990, Ferries has collected \$0.4 million in claims from its vessel hull and machinery coverage out of total vessel losses of \$4.5 million. During this same period Ferries has collected \$5.5 million in claims from its terminal policy out of total terminal losses of \$11.3 million.

In addition to these claims, since 1990 Ferries has collected on three protection and indemnity claims: \$1.2 million paid in 2000 on a crew injury case alleging permanent injury resulting from a slip/fall from a ladder; \$3.0 million paid in 2002 on the “wave wake” cases involving property damage allegedly relating to operation of the passenger-only ferries in Rich Passage; and a recently settled \$0.1 million claim from a crew injury alleging exposure to toxic chemicals.

Table 6
Marine Insurance Claims Receipts, 1990-2007
(\$ millions)

Coverage	\$
Terminal Coverage	5.5
Protection & Indemnity Coverage	4.3
Vessel Coverage	0.4
Total	10.2

Interviews with Ferries staff indicate that there has been some confusion regarding coverage where Ferries’ negligence is involved. It has been clarified that the coverage is no-fault and is in effect if negligence on the part of Ferries is involved. Ferries staff indicate that this clarification may result in filing additional claims for previously incurred losses.

¹¹ War risk includes acts of terrorism.

¹² Thirteen of Ferries’ vessels are included in the war risk coverage. Appendix B includes a list of the vessels covered by the war risk coverage.

d. Recommendations

The marine insurance program should be reviewed to determine its cost-effectiveness as compared to being self-insured. In particular, OFM Risk Management and Ferries should review:

- *Self-Insurance:* Whether Ferries should put a portion or all of its risk into the State’s self-insurance program. For example, it may be possible for the state to self-insure up to a catastrophic level, beyond which an insurance policy would be in effect. OFM indicates that an actuarial study would be needed to assess whether being self-insured would be a more cost beneficial approach to insuring some or all of Ferries’ risk.
- *Terminal Property Coverage:* The continued need for terminal property coverage should be reviewed in light of the change in terminal structures to concrete and steel versus wood, with consequent reductions in risk of property damage.
- *Machinery and Hull Coverage:* Whether it is cost effective to maintain hull and machinery coverage on boats that are in a non-active status most of the year and on older vessels. For all vessels, given the relatively low claims activity, the cost-effectiveness of continuing machinery and hull coverage should be reviewed.
- *War Risk Coverage:* Only 13 of Ferries’ 24 auto-passenger vessels (20 now that the Steel Electrics have been retired) have war risk coverage. Should this coverage be extended to other vessels?
- *Deductible:* The \$1 million deductible has been in effect since at least FY 1991. OFM and Ferries should review whether it would be cost-effective to increase the deductible or acquire only catastrophic coverage. The State’s general and auto insurance has, for example, a \$10 million deductible.

Recommendation 1: OFM, WSDOT and Ferries should review the marine insurance program to determine whether it is cost-effective versus being self-insured, including the Ferries terminal property, hull and machinery, war risk, and liability coverages.

WSDOT Response: We concur with the recommendation.

Recommendation 2: If OFM, WSDOT and Ferries conclude that it is cost-effective to continue to retain commercial insurance, the coverages and deductibles should be reviewed. Consideration should be given to optional deductible limits above the current \$1 million.

WSDOT Response: We concur with the recommendation.

Ferries’ claims management has been affected by misunderstandings regarding coverage under the policy. It is also affected by the fact that the insurer wants to know only the direct costs of repairs, excluding overhead charges. This means that on occasion Ferries has had difficulty collecting from the insurer because it cannot distinguish the direct costs

of staff versus administrative staff charges. Implementation of the requirements of ESHB 2358 to separately identify administrative charges to projects will help with that aspect of claims management.¹³

Recommendation 3: Ferries should ensure that it has a full understanding of the coverages provided if it continues to procure commercial insurance. Ferries should also ensure that, as it implements the administrative cost allocation requirements of ESHB 2358, consideration is given to the insurer’s requirements to distinguish direct labor from administrative overhead costs that are allocated to capital projects. This will facilitate Ferries’ claims management.

WSDOT Response: We concur with the recommendation. Our Risk Management Department will work with Ferries Division and OFM to ensure full understanding of the coverages provided. Working with OFM we will ensure the distinction between direct labor and administrative overhead as required by ESHB 2358.

4. Rent and Leases: Findings and Recommendations

In the 2005-07 biennium, Ferries’ operating budget paid \$4.4 million in rent and leases, and the capital budget paid \$3.1 million.

Ninety-six (96) percent of operating budget rent and lease expenditures are for property leases, with 4 percent resulting from copier and other equipment leases.

Table 7
Rent and Leases Expenditures, 2005-07 Biennium
(\$ millions)

	X3	X7	X8	X9	Total	
	\$ Operations M&S	\$ Maintenance M&S	\$ Finance & Admin	\$ Exec. Mgmt.	\$	%
Rent & Leases - Property/Ferries Division		0.5	3.2		3.7	84%
Rent & Leases - All Other Property			0.5		0.5	11%
Rent & Leases - Copy Machines	0.1				0.1	2%
TEF* Equipment Rental		0.1			0.1	2%
Total	0.1	0.60	3.70		4.4	

*Transportation Equipment Fund

a. Ferries Division Rent and Leases

The major expenses for rent and leases are for three facilities: headquarters offices at 2901 3rd Ave. in Seattle, the Seattle warehouse, and the north region training facility. Biennium lease payments are outlined below along with the \$0.3 million in move-in expenses incurred when headquarters was moved to the 2901 3rd Ave. building. Rent for the 2901 3rd Ave. headquarters is also paid by the capital budget, with the cost allocation

¹³ See *Capital Staff and Administration Cost Report, WSDOT Ferries Division Financing Study II, Final Report*, April 2008, for further information on the distribution of administrative work order charges.

between the operating and capital budgets based on the space used by capital and operating budget supported divisions.

Table 8
Leases and Rents, 2005-07 Biennium
(\$ millions)

Leases	\$	\$ Capital Budget	\$ Total
2901 3rd Ave. - Headquarters	2.4	3.0	5.4
Seattle Warehouse	0.8	0	0.8
NRO Training Facility	0.2	0	0.2
Total Lease Costs	3.4	3.0	6.4
<i>One time move-in expense</i>	<i>0.3</i>		<i>.3</i>
Total Costs	3.7	3.0	6.7

b. Rent and Leases All Other Properties

In the 2005-07 biennium, Ferries spent \$500,000 on other leases, which were primarily rental of rooms for outreach, meetings and conferences. This amount also includes expenses for leasing parking in the headquarters building.

5. Services: Findings and Recommendations

In the 2005-07 biennium, the operating budget paid \$3.7 million for services, of which 76 percent was for temporary employment services (\$1.1 million including information technology support and temporary services), services rendered by other state agencies (\$1.0 million) and for miscellaneous other services (\$0.7 million). The remaining 25 percent of expenses were for Ferries' commute trip reduction program, drug testing and physical examinations for employees, janitorial and cleaning services, and services rendered by other governments.

Table 9
Services Expenditures, 2005-07 Biennium
(\$ million)

	X3 \$ Operations M&S	X7 \$ Maintenance M&S	X8 \$ Finance & Admin	X9 \$ Exec. Mgmt.	\$ Total	%
Temporary Services	0.3	0.1	0.3	0.4	1.1	30%
Services Rendered by Other State Agencies	0.2		-0.1	0.9	1.0	27%
Other Services	0.4		0.2	0.1	0.7	19%
Commute Trip Reduction*			0.3		0.3	8%
Drug Testing				0.2	0.2	6%
Information Tech Support	0.1				0.1	3%
Physical Exams				0.1	0.1	3%
Services Rendered by Other Governments		0.1			0.1	3%
Janitorial & Cleaning Services			0.1		0.1	3%
Total	1.0	0.2	0.8	1.7	3.7	

*Includes payments under 631020 for commute trip reduction

a. Temporary Employment Services

In the 2005-07 biennium, Ferries budgeted \$0.4 million for management and support temporary employment services but spent nearly three times that amount (\$1.1 million). Most temporary employees filled vacancies, met temporary peak workloads as with the move to the new headquarters building, and provided vacation relief. In five cases, new workloads were added to Ferries during the biennium, and temporary employees were used to fill these positions.

Table 10
Temporary Employment Assignments, 2005-07 Biennium
(\$ millions)

Division	Budget	Total \$	Assignment	Reason	
				Vacancy/ Relief/Temp. Peak	Workload Change
Operations M&S	X3	0.3	Dispatch		MEC* dispatch decision
			Regional Operations	Yes	
			Port Engineers	Yes	
			Document Control	Yes	
			Customer Information	Yes	
Maintenance M&S	X7	0.1	Eagle Harbor	Yes	
Finance & Administration	X8	0.3	Finance	Yes	Credit card reconciliation
			Accounting	Yes	
			Admin. Services	Yes	
			Budget	Yes	
Executive Management	X9	0.4	Human Resources	Yes	Jones Act, Labor & Industry Claims Recruitment - deck, engine & terminal New payroll system
			Risk Management		
			HR Services		
			Payroll		
			Payroll	Yes	
			Training	Yes	
Total		1.1			

* Marine Employment Commission

Recommendation 4: Ferries, WSDOT, and OFM should review Ferries' temporary employment expenditures and determine which, if any, of the temporary positions should be created as permanent positions, with particular attention to those used to meet new workload requirements.

WSDOT Response: We concur with the recommendation. All current temporary positions are under review and we will propose changes where appropriate as part of the FY2009 budget.

b. Services Rendered by Other State Agencies

In the 2005-07 biennium, Ferries paid \$1.0 million for services rendered by other state agencies. These charges were for:

- *Ferries' share of the State's new human resources system and ongoing payroll services* (\$0.4 million).
- *OFM labor relations staff* (\$0.3 million).¹⁴
- *Risk management charges* from the Washington State Employment Security Department for Unemployment Insurance Claims by former Ferries employees (\$0.3 million).
- *Risk Management Administration Account Fund 546 charges* for the insurance broker fee for the marine insurance program and related OFM charges for claims administration, commercial insurance, and loss prevention services (\$0.1 million).

c. Other Services

In the 2005-07 biennium, Ferries spent \$0.7 million on other services. These services include:

- *On-call, oil spill response program* participation in the Director of Operations budget (\$0.3 million).
- *Contracted headquarters move*, a one time cost (\$0.1 million).
- *Human resources labor relations, background checks, and training video production* (\$0.1 million).
- *Miscellaneous services* (\$0.2 million).

6. Merchant Discount Fees and Bank Charges: Findings and Recommendations

In the 2005-07 biennium, Ferries expended \$2.5 million on merchant discount fees (i.e., fees charged to Ferries when customers pay by credit card), which represents 0.9 percent of farebox revenues.

Ferries accepts Visa, MasterCard, Discover, and American Express. Of the \$2.5 million in merchant discount fees, Ferries paid \$2.3 million to Bank of America for Visa and MasterCard fees, \$0.2 million to American Express, and \$22,000 to the Discover Network.

American Express charges Ferries 2.02 percent and Discover 1.73 percent. MasterCard charges 1.55 percent and \$.10 per transaction. Visa charges are between 1.55 percent and 1.85 percent, and \$.04 per transaction. Other state agencies, for example State Parks and the Department of Licensing, accept only Visa and MasterCard because of the lower

¹⁴ ESHB 3178 passed in the 2006 legislative session transferred authority to the governor, rather than WSDOT, to negotiate marine employee labor agreements. For further discussion of Ferries' labor agreements see *Ferry Financing Study Final Report, January 2007: Appendix B. Legislative Concerns and Directions*, pp. 20-24.

discount rates. Related transit agencies, including Kitsap Transit and METRO, also only accept Visa and MasterCard.

Recommendation 5: Ferries should consider accepting only Visa and MasterCard, which have lower merchant discount fees.

WSDOT Response: We concur with the recommendation and are in process of minimizing customer impact of no longer accepting American Express and Discover until after summer 2008 sailing schedule. We anticipate implementation prior to September 2008.

7. Management and Organizational: Findings and Recommendations

In the 2005-07 biennium, Ferries spent \$1.8 million on management and organizational consultant expenses. Major expenses include revenue forecasting (\$0.3 million); terminal structural, mechanical, and electrical consulting (\$0.3 million); coordination and promotion of non-farebox revenues, such as concessions (\$0.3 million); development of an annual report and outreach (\$0.2 million); establishment of new revenue controls (\$0.1 million); and development of an electronic fare system policy and procedures manual (\$0.1 million).

Some of these consultants¹⁵ are on-site consultants, including the temporary employment agency staff used to promote products and coordinate with operations on such promotions, which are designed to encourage traffic at terminals and increase non-farebox revenues. This long-term on-site consultant has been with Ferries on this project for one year or longer. Similar to the recommendation included in the *Capital Program Staffing and Administration WSDOT Ferries Division Financing Study Final Report*, April 2008, Ferries should review the use of long-term on-site consultants.

¹⁵ The terminal engineering consultants are the same on-site consultants addressed in the *Capital Program Staffing and Administration WSDOT Ferries Division Financing Study Final Report*, April 2008.

Table 11
Management and Organizational Expenses, 2005-07 Biennium
(\$ millions)

Division	Budget	\$	Section	Services
Operations M&S	X3	0.2	Customer Information	Outreach/annual report
		0.2	Director of Operations	Product/promotions development & operations coord.
		0.1	Regional Operations	Product/promotions development & operations coord.
		0.1	Operations Revenue Control	Set up variance program/investigate revenue loss
		0.1	Operations Revenue Control	Electronic fare system policy & procedures manual
		0.7	Sub-total Operations M&S	
Maintenance M&S	X7	0.3	Terminal Maintenance	Structural, mechanical and electrical consulting
		0.1	Materials Management	Business process consultant
		0.1	Vessel Engineering	Vessel design
		0.1	Misc.	Training services, safety systems
		0.6	Sub-total Maintenance M&S	
Finance & Admin. Executive Management	X8	0.3	Planning	Revenue forecasting
	X9	0.2	Risk Management	Jones Act third party administrator
Total		1.8		

Recommendation 6: Ferries should review its use of long-term on-site consultants.

WSDOT Response: We concur with the recommendation and will compare costs and available expertise to propose changes to consultants where appropriate for the FY2009 budget. We are no longer using two consultants in the Ferries Operations Department because their projects were completed during the 05/07 biennium.

Section III. WSDOT Management and Support

This section reviews the WSDOT management and support costs included in Ferries' calculation of farebox recovery. These WSDOT costs include charges for executive management, human resources, Office of Equal Opportunity (OEO) staffing, information technology, and services from other governments for insurance and risk management. Some of these WSDOT expenses are charged to the Puget Sound Ferry Operations Account and some to other non-Ferries accounts.

This section includes recommendations on policy clarifications regarding costs charged from the Motor Vehicle Account to the Puget Sound Ferries Operations Account and from WSDOT directly to Ferries budget. It also recommends reviews of WSDOT ferry related expenses and charges, and the separation of WSDOT indirect and direct costs, if indirect costs are charged to Ferries.

This section notes that with WSDOT costs included, 25 percent of management and support costs in farebox recovery are for insurance related expenses.

A. Overview

1. WSDOT Costs Included in Farebox Recovery

WSDOT management and support costs included in Ferries' calculation of farebox recovery for the 2005-07 biennium totaled \$17.5 million.

There are three ways in which WSDOT expenses included in the farebox recovery calculation were handled in the 2005-07 biennium:

- 1) Charging Motor Vehicle Account expenses to the Puget Sound Ferry Operations Account (\$9.7 million in the 2005-07 biennium);
- 2) Absorbing the costs within the Motor Vehicle Account and not charging the costs to the Puget Sound Ferry Operations Account (\$7.5 million);
- 3) Charging WSDOT expenses to the Ferries Operating budget (\$0.3 million) (Program X).¹⁶

¹⁶ Administrative expenses charged to the Ferries operating budget are expended in the Puget Sound Ferry Operations Account as part of Ferries' operating budget. Other WSDOT expenses charged to the Puget Sound Ferry Operations Account are shown as separate WSDOT charges in the Fund, but are not included in the Ferries operating budget.

Table 12
WSDOT Management and Support, 2005-07 Biennium
(\$ millions)

Budget Sub-Program	\$	Account Charged	%
S1 WSDOT Executive Management	1.1	Puget Sound Ferry Operations***	
S2 WSDOT Risk Management Officer	0.2	Puget Sound Ferry Operations***	
C1 Program Administration - WSDOT IT	0.2	Puget Sound Ferry Operations***	
C2 Field Services Support - WSDOT IT	8.2	Puget Sound Ferry Operations***	
<i>Sub-total Motor Vehicle Account Charges to Puget Sound Ferry Operations Acct.</i>			
	9.7		55%
U6 Charges from Other Agencies			
Ferries Tort Claims Defense	2.4	Motor Vehicle Account	
Ferries Excess Insurance*	0.5	Motor Vehicle Account	
Ferries Claims Payments	3.7	Motor Vehicle Account	
Risk Management Administration Fee**	0.9	Motor Vehicle Account	
<i>Sub-total Charges from Other Agencies</i>			
	7.5		43%
<i>Sub-total Charges from Other Agencies in Farebox Recovery</i>			
	17.2		
X9 Payment to WSDOT for OEO Officer	0.3	Puget Sound Ferry Operations****	2%
Total	17.5		
*Payment for Excess P&I Insurance - see Table 5 Marine Insurance Program Premium			
** Included by Ferries in the FY06 farebox recovery calculation. WSDOT indicates that there is no separate charge for Ferries risk management administration fee. The charge should not have been included in calculating farebox recovery.			
*** Expenses originated in the Motor Vehicle Account and were then charged by the Motor Vehicle Account to the Puget Sound Ferries Operating Account.			
**** Charged directly to the Puget Sound Ferry Operations Account through the Ferries operating budget.			

2. WSDOT Costs Excluded from Farebox Recovery

In addition to the costs included in farebox recovery, WSDOT also spent \$1.4 million in the 2005-07 biennium in support of the electronic fare system in its Information Technology Project (C4) budget. These expenses were not recognized in the calculation of farebox recovery in the biennium nor were they charged to the electronic fare system capital project in the Ferries capital budget.

In the 2007-09 biennium, WSDOT will charge ongoing support costs for the electronic fare system (\$1.6 million) to the Puget Sound Ferry Operations Account through its Information Technology Field Services (C2) budget.

3. WSDOT Policy: Inter-Fund Charges and Charges to Ferries Budget

WSDOT does not have a clear policy, and the legislature has not provided policy guidance, on which Motor Vehicle Account expenses to charge to the Puget Sound Ferry Operations Account nor on which WSDOT expenses to bill directly to the Ferries operating budget.

In some cases WSDOT services that benefit Ferries are charged to the Puget Sound Ferry Operations Account, in some to Ferries operating budget and in other cases to the Motor Vehicle Account. In some cases the Motor Vehicle Account absorbs the costs, but in

other cases the Motor Vehicle Account charges the Puget Sound Ferry Operations Account for expenses.

Historically the Motor Vehicle Account has transferred money to the Puget Sound Ferry Operations Account beyond the statutorily required amount, resulting in a circular movement of funds when the Motor Vehicle Account charges the Puget Sound Ferry Operations Account.

WSDOT should distinguish between indirect charges (such as C1 Information Technology Program Administration Expenses and S1 WSDOT Executive Management) and costs incurred in direct support of Ferries when charging expenses to Ferries. This will provide greater oversight of direct costs associated with the delivery of ferry services.

Recommendation 7: The legislature and WSDOT should develop a consistent policy on expenses to be charged from the Motor Vehicle Account to the Puget Sound Ferry Operations Account. The policy should specifically address whether administrative indirect charges, such as WSDOT Executive Management, are to be charged to the Ferry Operations Account.

WSDOT Response: We concur with the recommendation and we expect to address this policy with OFM as we develop our 09/11 budget. Additionally, OFM intends to address this in the next round of budget instructions.

Recommendation 8: If the policy is to include Motor Vehicle Account administrative indirect expenses in charges to the Puget Sound Ferry Operations Account, such charges should be distinguished from costs incurred in the direct delivery of ferry services.

WSDOT Response: We concur with the recommendation and OFM intends to address this in the next round of budget instructions.

There has also been a lack of clarity about which expenses should be paid directly by the Ferries operating budget (Program X). For example, a portion of the Marine Insurance Program is paid by WSDOT with the remainder budgeted in the Ferries operating budget.

Recommendation 9: The legislature and WSDOT should develop a consistent policy on expenses to be charged directly to the Ferries operating budget.

WSDOT Response: We concur with the recommendation and look forward to working with OFM and the legislature to develop this policy. Additionally, OFM intends to address this in the next round of budget instructions.

B. WSDOT Executive Management

As shown in the table above, WSDOT's Management and Support Program (S) had two sub-programs that charged to the Puget Sound Ferry Operations Account: S1 Executive Management and Support, and S2 Risk Management. Total expense to the Puget Sound Ferry Operations Account was \$1.3 million in the 2005-07 biennium.

1. Executive Management Sub-Program S1

The S1 sub-program includes the Secretary of Transportation, Engineering and Regional Operations, Chief of Staff, Communications and Public Involvement, Governmental Liaison, Audit Office and Office of Equal Opportunity. The S1 sub-program charged \$1.1 million to the Puget Sound Ferry Operations Account in the 2005-07 biennium. The same amount has been charged each biennium since 1997-98, when WSDOT had a policy of billing other funds. Since the late 1990s, WSDOT has not billed any fund other than the Puget Sound Ferry Operations Account for S1 expenses.

In addition to the charges from Sub-Program S1, Ferries paid \$0.3 million in the biennium to WSDOT for an OEO officer position reporting to WSDOT. WSDOT does not charge other funds for OEO officer expense.

Recommendation 10: WSDOT should not charge the Puget Sound Ferry Operations Account for S1 Executive Management if such charges are not made to other transportation related accounts. If WSDOT does continue to charge S1 expenditures to the Ferry Operations Account, the charges should be periodically reviewed and updated.

WSDOT Response: We concur with the recommendation and we expect to address this policy with OFM as we develop our 09/11 budget. Additionally, OFM intends to address this in the next round of budget instructions.

Recommendation 11: WSDOT should review the consistency of its practice in charging for OEO officers. The Ferries Executive Management budget should not be charged for the expense of an OEO officer unless other WSDOT budgets are also charged for such expenses.

WSDOT Response: We will review the practice of charging OEO Officers to Ferries and will make changes if warranted for the 09/11 budget.

2. Executive Management Sub-Program S2

The S2 sub-program includes the Assistant Secretary for Finance and Administration, Accounting Services, Human Resources, Administrative Services, Risk Management and the Budget Office. In the 2005-07 biennium, the S2 sub-program charged \$0.2 million to the Puget Sound Ferry Operations Account for expenses of two torts investigators for Ferries claims that reported to the WSDOT Risk Management Manager.

C. WSDOT Information Technology

As shown in the table above, in the 2005-07 biennium two sub-programs of WSDOT Program C charged the Puget Sound Ferry Operations Account: Program C1 Information Technology Administration and C2 Field Services Support. Total charges were \$8.4 million in the biennium.

1. Information Technology Administration Sub-Program C1

In the 2005-07 biennium, sub-program C1 Information Technology Administration charged \$0.2 million to the Puget Sound Ferry Operations Account. In the 2007-09 biennium, WSDOT ceased charging C1 expenses to the Puget Sound Ferry Operations Account and does not expect to pursue such charges in the future. WSDOT does not charge other funds for Sub-Program C1 expenditures.

Recommendation 12: WSDOT should continue the practice adopted in the 2007-09 biennium of not charging sub-program C1 Information Technology Administration expenses to the Puget Sound Ferry Operations Account.

WSDOT Response: We concur with the recommendation.

2. Information Technology Field Services Sub-Program C2

WSDOT Program C2 information technology charged \$8.2 million to the Puget Sound Ferry Operations Account in the 2005-07 biennium. The staff and budget for information technology charged to the Puget Sound Ferry Operations Account are managed by the WSDOT Information Technology Division. Staff in the Ferries information technology section are physically located at Ferries headquarters.

Table 13
WSDOT Information Technology, 2005-07 Biennium
(\$ millions)

	\$	%
Salaries & Wages	3.6	44%
Asset Purchases	1.4	17%
Repairs, Alterations & Maintenance	1.2	15%
Communications	0.8	10%
Personal Services Contracts	0.5	6%
Purchase Service	0.4	5%
Supplies	0.2	2%
Miscellaneous Expenses	0.1	1%
Total	8.2	

1. Information Technology Staff

The Puget Sound Ferry Operations Account was charged \$3.6 million in the 2005-07 biennium for 30 Information Technology positions included in Figure 3, representing 44 percent of all information technology charges to the Puget Sound Ferry Operations Account.

2. Information Technology Services to Ferries

The information technology section provided help desk, infrastructure and ongoing technology support to Ferries. In the 2005-07 biennium, the section spent \$0.8 million of its \$8.2 million expenditure in support of the Ferries' security plan.

3. Information Technology Field Services Charges to other Funds

Program C has appropriations in four funds in addition to the Motor Vehicle Account. Funds charged for field services support are the Puget Sound Ferry Operations Account and the Multimodal Account. Project specific charges are included in the Transportation Partnership Act and the Nickel Accounts.

Recommendation 13: WSDOT should make a determination of whether Information Technology (Program C) expenses should continue to be charged to the Puget Sound Ferry Operations Account, as part of its policy review of charges from the Motor Vehicle Account to the Puget Sound Ferry Operations Account.

WSDOT Response: We concur with the recommendation and will analyze all Information Technology charges to determine if they directly support ferry operations. We believe expenditures such as the AOSS (dispatch system), vessel wireless system, Electronic Fare System (EFS) are directly related to ferry operations and should continue to be charged to the Puget Sound Ferry Operations Account.

D. WSDOT Other Government Charges

In the 2005-07 biennium, expenditures from WSDOT Program U Charges from Other Agencies that were attributable to Ferries include: costs incurred by the Attorney General in defending Ferries' claims, Ferries excess insurance premium, and Ferries claims payments.¹⁷ As shown in Table 12, expenses for these three charges in the 2005-07 biennium totaled \$6.6 million. Prior to the 2003-05 biennium, these expenses were paid from the Puget Sound Ferry Operations Account.

1. Risk Management Fees

In addition to these charges, Ferries shows a risk management administration fee in its farebox recovery model. Total charges in the biennium are estimated at \$0.9 million. WSDOT states that prior to the 2003-05 biennium, WSDOT charged the Puget Sound Ferry Operations Account a portion of charges paid by the department for the operation of the OFM Risk Management Office (25 percent). Beginning in the 2003-05 biennium, all Ferries related payments have been made from the Motor Vehicle Account and no portion of this charge from the OFM Risk Management Office has been identified as Ferries' share (WSDOT Response to Consultant Questions, March 2008). It appears that this expense should not be included in the calculation of farebox recovery.

¹⁷ This expense is identified in farebox recovery and WSDOT financial records as Ferries self-insurance premium. However, Ferries is not part of the State's self-insurance program and the charges are actually claims paid by the self-insurance program fund that are then subsequently reimbursed by WSDOT from the Motor Vehicle Account.

Recommendation 14: Ferries should not include risk management administration fees in its calculation of farebox recovery because the charge is no longer allocated between WSDOT and Ferries.

WSDOT Response: We will work with OFM and the 2009 legislature to determine an appropriate farebox recovery calculation.

2. Total Insurance Related Expenses

As discussed in Section II, Ferries directly incurred \$9.7 million in insurance premium costs and other state agency risk management related charges. These costs are in addition to the \$7.5 million in Ferries’ related expenses in WSDOT Program U and \$0.2 million in WSDOT Program S2 for risk management staff. In the 2005-07 biennium, insurance and claims expenses totaled \$17.3 million or 25 percent of all management and support costs.

Table 14
Insurance Related Expenses, 2005-07 Biennium
(\$ millions)

Insurance Related Expenses	\$
Marine Insurance Program Premium *	9.7
Ferries Tort Claims Payments	3.7
Ferries Tort Claims Defense	2.4
Risk Management Administration Fee**	0.9
Ferries Risk Management Charges from OFM	0.3
WSDOT Sub Program S2 Charges for 2 Tort Claims Investigators	0.2
Ferries Payments to Fund 546 for Broker Fee	0.1
Total	17.3
Total Management & Support Costs	68.4
% Insurance Related	25%
* \$9.2 million paid by Ferries budget, \$0.5 million by WSDOT	
** Ferries includes, WSDOT does not	

Recommendation 15: In addition to reviewing the Marine Insurance Program, WSDOT, OFM, and Ferries should review the range of costs incurred by the State in providing insurance, risk management services, and claims defense to determine what, if any, costs could be reduced.

WSDOT Response: We concur with the recommendation and will work with Risk Management and OFM to review what Ferries Division costs, if any, can be reduced during the 09/11 biennium.

Section IV.

Management Communication and Oversight

This section reviews and makes recommendations on how Ferries calculates and communicates to the legislature information on management and support costs and farebox recovery.

A. Management and Support Costs in Farebox Recovery: Findings and Recommendations

Farebox recovery is a key indicator in setting ferry fares and is often used to compare Ferries' performance to that of other transit agencies. It is, therefore, important that the legislature and the public have a clear understanding of what is included and excluded as costs in the farebox recovery calculation.

The legislature has provided some policy direction regarding farebox recovery:

- ESHB 1094 §225(6) states that farebox recovery should exclude security costs.
- ESHB 2358 states that, in developing fare and pricing policy proposals, Ferries must “recognize that each travel shed is unique, and might not have the same farebox recovery rate and the same pricing policies” ((ESHB 2358 §5(2)(a)).
- ESHB 2358 also states that fares should “generate the amount of revenue required by the biennial transportation budget” which is measured in part by farebox recovery (ESHB 2358 §5(2) (d)).

1. Policy on Costs to Include in Farebox Recovery

The key policy question is which expenses to include in farebox recovery. Should the costs be:

1. Only operating costs included in Ferries' budget (Program X)? This option would be a measure of Ferries' ability to control costs.
2. Operating costs included in Ferries budget and WSDOT operating costs, whether or not charged to the Puget Sound Ferries Operations Account? This is how farebox recovery expenses are currently calculated (with the exclusions discussed in Section III).
3. Operating costs charged to the Puget Sound Ferries Operations Account, which includes the Ferries budget (Program X), certain WSDOT expenses (Programs C and S), and the Marine Employees Commission? This option would make farebox recovery directly relate to the fares revenue assumed in the legislative budget and associated 16-year financial plan for the Puget Sound Ferries Operations Account.
4. All operating costs incurred by the State in delivering ferry services, which would include expenses incurred by the Washington State Patrol? This option would provide a more complete view of total costs.

The table below shows the different ways of calculating farebox recovery and the impact on systemwide recovery rates under the different calculation methods in FY 2006. The options range from 3 percent more to 3 percent less farebox recovery, depending on the costs included.

**Table 15
Alternative Farebox Recovery Calculation Approaches**

Alternative Farebox Recovery Calculation Approaches	FY 06 Farebox Recovery Rate	Change from Current Calculation
1. Ferries Budget*	76.4%	2.8%
2. Current (Ferries Budget* + WSDOT (Programs C, S, U))	73.6%	
3. All Expenses in the Puget Sound Ferries Operations Account (Ferries* budget, WSDOT Programs C&S, MEC)	74.5%	0.9%
4. All State Expenses in Delivery of Ferry Service (Ferries, WSDOT, MEC, State Patrol)	70.3%	-3.3%

* Excluding security costs

Recommendation 16: Ferries and the legislature should develop a policy on what costs are to be included in farebox recovery. The consultants recommend that all costs charged to the Puget Sound Ferries Operations Account be included in farebox recovery, as this methodology would tie most directly to the level of fares needed to meet the legislatively adopted 16-year financial plan.

WSDOT Response: We will work with OFM, the Governor's Office, and the legislature during the 2009 session, to determine an appropriate farebox recovery calculation. Depending upon input we receive, the outcome may have several options; whether farebox recovery calculations are within OFM budget instructions, legislation, Commission policy or WAC rule.

2. Policy on Costs to be Excluded from Farebox Recovery Calculations

The legislature has directed Ferries to exclude security costs from its calculation of farebox recovery. Ferries has therefore not included the cost of two positions in the Operations Division. WSDOT expenses included in the calculation of farebox recovery have included expenses incurred by WSDOT Information Technology in the development of the security plan.

Recommendation 17: The legislature should clarify its intent in excluding security costs from the calculation of farebox recovery so that WSDOT expenses can be properly included or excluded based on that direction.

WSDOT Response: We will work with OFM and the 2009 legislature to determine an appropriate farebox recovery calculation.

B. Legislative Oversight Communication

In communicating with the legislature, Ferries should use a consistent definition of management and support costs. For example, for the *Washington State Ferries Financing Study Final Report*, January 2007, Ferries provided information on management and

support costs including only the costs for Executive Management and Finance, and Administration budget subprograms. This is different from the way in which management and support costs are calculated for farebox recovery purposes, which includes all Ferries' headquarters staff.

Recommendation 18: In order to provide consistent communication with the legislature, Ferries should use a uniform definition of Ferries management and support costs based on costs included in the calculation of farebox recovery.

WSDOT Response: We concur with the recommendation and will work with OFM to develop a proposed definition of Ferries Management and Support. We will work with 2009 legislature to ensure mutual understanding and acceptance of Ferries Management and Support costs.

Ferries should also consider providing farebox recovery on a biennium basis to align with the state budgeting periods.

Recommendation 19. Ferries should provide a biennium farebox recovery calculation to align with the State's budget periods.

WSDOT Response: We concur with the recommendation and will provide a fiscal year and biennial farebox recovery calculation for the 07/09 biennium.

Appendix A. Marine Insurance Program Claims Experience

**Table A1.
Hull and Machinery Losses over \$25,000
1990-2006**

Incident	\$ Loss	Date
Storm Damage		December 17-18, 1990
M.V. Kalama	\$9,431	
M.V. Elwha	\$1,378,695	
<i>Total</i>	<i>\$1,388,126</i>	
Deductible	\$1,000,000	
Paid by Underwriters	\$388,126	
Buoy Collision		
M.V. Skagit	\$31,000	January 29, 1991
Propeller Damage		
M.V. Kittitas	\$100,000	February 5, 1991
Vessel Collision		
M.V. Sealth/M.V. Kitsap	\$70,000	September 6, 1991
Propeller Damage		
M.V. Spokane	\$54,821	April 16, 1993
Propeller Damage		
M.V. Walla Walla	\$50,301	May 17, 1993
Hard Landing		
M.V. Issaquah	\$26,644	October 31, 1994
Hard Landing		
M.V. Nisqually	\$47,000	May 23, 1995
Rudder Damage		
M.V. Kitsap	\$480,000	September 18, 1996
Storm Damage		
M.V. Quinault	\$52,047	March 3, 1999
Hard Landing		
M.V. Elwha	\$45,758	September 8, 1999
Grounding		
M.V. Wenatchee	\$182,064	July 2, 2000
Grounding		
M.V. Sealth	\$562,441	May 29, 2001
Propeller Damage		
M.V. Yakima	\$51,379	July 22, 2003
Rudder Damage		
M.V. Evergreen State	\$90,141	August 4, 2003
Grounding		
M.V. Sealth	\$273,392	December 24, 2004
Hard Landing		
M.V. Klickitat	\$137,099	October 25, 2005
Driver Motor Damage		

Incident	\$ Loss	Date
M.V. Klickitat (estimate)	\$135,000	November 29, 2005
Propeller Damage		
M.V. Yakima	\$52,713	March 31, 2006
Driver Motor Damage		
M.V. Elwha (estimate)*	\$656,000	April 7, 2006
Total Claims	\$4,485,926	
Total Paid by Underwriters	\$388,126	9%
<i>Ferries' Responsibility</i>	<i>\$4,097,800</i>	
* Final costs were \$2.3 million, some of which may be eligible for a claim. Ferries is reviewing.		

Source: 2007 Marine Insurance Market Specifications

Table A2.
Terminal Damages over \$25,000
1990-2003

Incident	\$ Loss	Date of Loss
Orcas Island	\$401,425	June 28, 1990
M.V. Chelan hard landing		
<i>Deductible</i>	<i>\$250,000</i>	
Paid by Underwriters	\$151,425	
Storm Damage	\$1,144,910	December 18, 1990
Vashon	\$268,645	
Lopez Island	\$845,308	
Eagle Harbor	\$1,369	
Anacortes	\$13,445	
Mukilteo	\$16,143	
<i>Deductible</i>	<i>\$250,000</i>	
Paid by Underwriters	\$894,910	
Vashon Island	\$60,159	September 17, 1993
M.V. Quinault hard landing		
Faultleroy	\$769,012	September 22, 1993
M.V. Klahowya hard landing		
Anacortes	\$458,230	January 19, 1994
M.V. Elwha hard landing		
Lopez Island	\$284,000	May 23, 1995
M.V. Nisqually hard landing		
Mukilteo	\$36,233	September 4, 1996
M.V. Cathlamet hard landing		

Incident	\$ Loss	Date of Loss
Seattle - Slip 2	\$2,892,793	June 12, 1998
M.V. Sealth hard landing <i>Deductible</i>	\$1,000,000	
Paid by Underwriters	\$1,892,793	
Clinton	\$52,992	August 6, 1998
M.V. Cathlamet hard landing		
Orcas Island	\$3,578,439	September 8, 1999
M.V. Elwha hard landing <i>Deductible</i>	\$1,000,000	
Paid by Underwriters	\$2,578,439	
Port Townsend	\$45,398	December 14, 2000
Storm Damage		
6.8 Earthquake	\$42,106	February 28, 2001
Bremerton	\$3,210	
Seattle (estimate)	\$10,000	
Vashon	\$28,896	
Kingston (estimate)	\$1,539,159	June 9, 2001
Transfer Span collapse	Not insurable per underwriters	
Southworth	\$37,796	November 30, 2003
M.V. Issaquah hard landing		
Total Claims	\$11,289,660	
Paid by Underwriters	\$5,517,567	49%
<i>Ferries' Responsibility</i>	<i>\$5,772,093</i>	

Appendix B. Vessels Covered by War Risk Hull and Machinery Insurance

**Table B1.
Vessels Covered by War Risk Hull and Machinery Insurance
2007 Marine Insurance Program**

Vessels	War Risk Coverage
<i>Steel Electric Class 1920s*</i>	
Illahée	No
Klickitat	No
Nisqually	No
Quinault	No
<i>Misc. 1940s</i>	
Rhododendron	No
<i>Evergreen State Class 1950s</i>	
Evergreen State	No
Klahowya	Yes
Tillikum	Yes
<i>Super Class 1960s</i>	
Elwha	Yes
Hyak	Yes
Kaleetan	No
Yakima	No
<i>Misc. 1960s</i>	
Hiyu	No
<i>Jumbo Mark I Class 1970s</i>	
Spokane	Yes
Walla Walla	Yes
<i>Issaquah Class 1980s</i>	
Cathlamet	Yes
Chelan	No
Issaquah	Yes
Kitsap	Yes
Kittitas	Yes
Sealth	No
<i>Jumbo Mark II Class 1990s</i>	
Puyallup	Yes
Tacoma	Yes
Wenatchee	Yes
Total No	11
Total Yes	13
* Vessels retired from service Nov. 2007	

Source: 2007 Marine Insurance Market Specifications