

Special Review

**Department of Transportation
State Highway Administration**

A Senior Management Employee Appeared to Have Solicited Funds from Firms
Doing Business with SHA

A Former Senior Management Employee was Hired by a Firm and was Directly
Involved in an SHA Contract which this Employee Helped to Procure

Bid Evaluation Processes were not Adequately Documented and Certain Contract
Funds were Improperly Used

June 2011



OFFICE OF LEGISLATIVE AUDITS
DEPARTMENT OF LEGISLATIVE SERVICES
MARYLAND GENERAL ASSEMBLY

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Karl S. Aro
Executive Director

DEPARTMENT OF LEGISLATIVE SERVICES
OFFICE OF LEGISLATIVE AUDITS
MARYLAND GENERAL ASSEMBLY

Bruce A. Myers, CPA
Legislative Auditor

June 24, 2011

Delegate Guy J. Guzzone, Co-Chair, Joint Audit Committee
Senator James C. Rosapepe, Co-Chair, Joint Audit Committee
Members of Joint Audit Committee
Annapolis, Maryland

Ladies and Gentlemen:

We conducted a review of allegations received through our fraud, waste, and abuse hotline regarding possible conflicts of interest involving several senior State Highway Administration (SHA) management employees responsible for certain construction-related contracts.

Our review disclosed that one employee appeared to have solicited funds from firms doing, or seeking to do, business with SHA potentially violating State Ethics Laws, a Governor's Executive Order, and SHA policies. In this regard, we further noted that this employee was directly involved in certain questionable transactions with these firms.

In addition, SHA did not ensure that these firms complied with State Ethics Laws and SHA policies regarding the hiring and subsequent involvement of former SHA employees on SHA contracts. This is significant because SHA employees were routinely hired by firms doing business with SHA. For example, a former senior management employee was hired by a firm doing business with SHA within 12 days of retiring from SHA. The employee had significant involvement in approving the scope, amount, and award of a \$16 million contract awarded to this firm and was subsequently involved in the contract in his capacity as an executive of the firm.

Our review also noted that SHA circumvented certain established bid evaluation processes for a procurement that resulted in the award of two \$16 million contracts. For example, there were significant disparities between technical evaluations that were not resolved and certain key components of the rating process were not documented as required. Finally, SHA solicited the cooperation of firms involved in the hotline allegations to redirect contract funds for unrelated

projects, and/or to conceal overspending on other contracts, thereby circumventing Board of Public Works oversight and approval. As a result, we have expanded our review at SHA of redirected contract funds and will be issuing the related report in the near future.

Respectfully submitted,

Bruce A. Myers, CPA
Legislative Auditor

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Scope, Objectives, and Methodology

We conducted a review of several allegations related to the State Highway Administration (SHA) that were received through our fraud hotline. The allegations related to possible conflicts of interest involving several senior SHA management employees responsible for certain construction-related contracts.

The purpose of our review was to determine whether the allegations we received were valid and to determine if the related activities violated State law, regulations, and policies. This review was performed in accordance with State Government Article, Section 2-1220 of the Annotated Code of Maryland.

Our review consisted of tests, analyses, observations, and discussions with SHA personnel and others, as we deemed necessary, to achieve our objectives. The results of our review of the allegations are identified in findings 1 and 2. Other issues that came to our attention during our review are identified in findings 3, 4, and 5. Our review did not constitute an audit conducted in accordance with generally accepted government auditing standards. Our review was conducted from July through December 2010.

The response from the Department of Transportation, on behalf of SHA, to our findings and recommendations is included as an appendix to this report. As prescribed in State Government Article, Section 2-1224 of the Annotated Code of Maryland, we will advise the Department regarding the results of our review of its response.

Background Information

Agency Responsibilities

The Transportation Article, Section 8-201 of the Annotated Code of Maryland, establishes the State Highway Administration (SHA) in the Maryland Department of Transportation. SHA is responsible for the planning, construction, improvement, maintenance, and operations of the State highway system. SHA operates numerous facilities throughout the State, including a headquarters in Baltimore City and seven district offices.

Background

SHA entered into multi-year contracts with engineering firms to provide both construction management and inspection services for SHA construction projects. Separate contracts are issued for each of the seven SHA district offices. According to SHA records, there were seventeen open contracts¹ as of December 31, 2010 with an original contract cost of \$146 million and a remaining balance of approximately \$64 million. SHA's Office of Construction (OOC) was responsible for developing the scope of these contracts on behalf of the district offices, and the Office of Procurement and Contracts (OPC) was responsible for conducting the actual procurements (such as issuing the requests for proposals and publishing the solicitations). Both units were responsible for independently evaluating and rating the related technical proposals, and then comparing their results. After purportedly resolving any significant discrepancies, the final rankings were submitted to an independent screening committee which made the final recommendation to SHA's Administrator for awarding the contract.



The hotline allegations we received pertained to several senior management employees involved with the OOC who participated in the procurement and subsequent administration of the aforementioned contracts. Although the procurement of these contracts involved several SHA units and the awards were ultimately approved by the SHA Administrator, the allegations indicated that

¹ Contracts span several years so certain jurisdictions had multiple contracts open at the same time.

certain senior employees had significant involvement in the scope of the contracts and the selection of the related firm(s).

Our review of the hotline allegations also included a review of the procurement of two \$16 million contracts for construction management and inspection services in one SHA district. The contracts were procured by one request for proposal with the award going to the two highest-ranked firms. We selected these two contracts for review because of the association of the related firms with the hotline allegations.

Based on our review, we identified a number of questionable matters as described in the findings which follow. Consequently, we referred these matters to the Criminal Division of the Office of Attorney General. SHA should consult with the Office of the Attorney General before taking any actions related to the findings contained in this report. A referral to the Criminal Division does not mean that a criminal act has actually occurred or that criminal charges will be filed.

Findings and Recommendations

Potential Violation of State Ethics Laws, Governor's Executive Order, and SHA Policies

Finding 1

A senior Office of Construction (OOC) management employee appeared to have solicited funds from firms doing, or seeking to do, business with SHA potentially violating State Ethics Laws, a Governor's Executive Order, and SHA policies.

Analysis

A senior OOC management employee appeared to have solicited funds from firms doing, or seeking to do, business with SHA potentially violating State Ethics Laws, a Governor's Executive Order, and SHA policies. Specifically, the employee was a partial owner of an out-of-state company that promoted certain sports activities. Our review of the company's website disclosed that seven firms that do business with SHA were listed as sponsors for a charity event being hosted by the company in April 2009.² These firms accounted for seven of the eight sponsors of the event, with sponsorships ranging from \$250 to \$2,500.

The employee's financial relationship with these firms is significant because five of these firms had ongoing contracts with SHA as of December 31, 2010, which were procured, in part, by this employee's unit (OOC). Two of these firms were each awarded a \$16 million contract (\$32 million in total) for construction management and inspection services, in October 2008 and December 2008, shortly before the aforementioned sporting event. The employee may have attempted to expedite the award of these two contracts. Specifically, during the procurement process, the employee sent an email to SHA headquarters procurement staff stating "...we need to get this contract out ASAP as it's LONG overdue...we want to get it resolved... ." In addition, as noted in the subsequent findings, our review of the procurement of these contracts and certain related contract activity identified several questionable transactions. For example, the employee facilitated payments to these firms for certain services that were not within the scope of the contracts (for examples, refer to finding 5). SHA management advised us that they were unaware of the employee's business relationship but that their subsequent inquiries disclosed that the employee may have solicited financial sponsorships from current and prospective SHA firms for other events in previous years.

² The business website indicated that similar events had been held since 1999 but sponsorship information was not readily available.

Senior management personnel at the State Ethics Commission advised us that the aforementioned conditions could violate a number of State Ethics Laws including Sections 15-501, 15-505, and 15-506 of the State Government Article of the Annotated Code of Maryland. For example, Section 15-505 states that an “official or employee may not knowingly accept anything of economic value, regardless of form, directly or indirectly, from an entity that the official or employee knows, or has reason to know, does or seeks to do any business of any kind, regardless of the amount, with the official’s or employee’s governmental unit.” Any final decision related to violations of the State Ethics Laws would ultimately be determined by the State Ethics Commission.

Finally, we noted that the employee’s business interest was not always disclosed on the annual Financial Disclosure Statements filed with the State Ethics Commission. Specifically, personal business interests were only disclosed on the employee’s calendar years 1999, 2004, 2008, and 2009 statements.³ The full disclosure of this business interest on the Financial Disclosure Statements for the specified time periods would not alleviate the need to comply with other laws and policies.

These conditions also appear to violate SHA’s ethics policies, which state that employees should not accept any gift, regardless of its value, from any person or entity that does business with the State and should conduct themselves in a manner that is free of the existence or perception of any corruption or other misconduct. The aforementioned condition also appeared to violate several provisions of the Governor’s Executive Order, issued in February 2007. Specifically, the Executive Order states, in part, that an employee shall not “solicit or accept any gift or other item of monetary value from any person or entity seeking official action from, doing business with, or conducting activities regulated by the employee’s agency, or whose interests may be substantially affected by the performance or nonperformance of the employee’s duties.” The Order further states that employees shall avoid any actions creating the appearance that they are violating applicable laws or the ethical standards. Finally, the Executive Order provides that violations of the aforementioned provisions are “grounds for employee disciplinary action, including termination from State employment.”

³ For all four years, the employee disclosed a partial ownership of the company but stated that no income had been received from this business.

Recommendation 1

We recommend that SHA

- a. take appropriate action regarding the aforementioned employee's apparent violation of State Ethics Laws, Governor's Executive Order, and SHA ethics policies;**
- b. ensure that employees comply with State Ethics Laws, the Governor's Executive Order, and SHA's ethics policies; and**
- c. refer the matter to the State Ethics Commission and obtain advice as to whether the employee needs to file amended Financial Disclosure Statements for years when the relationship was not disclosed.**

Finding 2

A former senior management employee was hired by a firm doing business with SHA within 12 days of retirement and subsequently worked on an SHA contract that, as an employee, this individual had helped to procure.

Analysis

A former senior SHA management employee started working for a firm doing construction management and inspection services for SHA⁴ within 12 days of retiring from SHA in December 2008. The employee was directly involved in SHA's procurement of the firm's contract and subsequently was directly involved in this contract as an executive of the firm. For example, while at SHA, the employee approved the decision to procure construction management and inspection services from outside firms. We were advised that the procurement that resulted in this \$16 million contract represented the first time SHA used an outside firm to provide construction management services instead of utilizing SHA staff, as in the past. This senior employee also approved the scope and award amount of the related contract. While this procurement was also approved by the employee's subordinates and the SHA Administrator, the employee had sufficient authority to significantly impact these other approvals. Within ten months of retiring from SHA, the employee approved the first two invoices on this contract, totaling \$96,896, in his capacity as an executive of the firm. In addition, in his role as an executive, the former employee agreed to SHA's request⁵ to submit bills under this contract for work performed for another district under another contract for which funds were depleted (as discussed in finding 5).

Senior management personnel at the State Ethics Commission advised us that the aforementioned conditions could violate Section 15-504(d) of the State

⁴ This firm received one of the two \$16 million contracts noted in finding 1 and is referenced in all of the other findings.

⁵ The request was made by the employee commented upon in finding 1 who was a subordinate to this former employee while employed at SHA.

Government Article of the Annotated Code of Maryland, which states that an official or employee is precluded from working on a contract if that official or employee participated significantly in the matter. Any final decision related to violations of the State Ethics Laws would ultimately be determined by the State Ethics Commission. This statute is also referenced in a Governor’s Executive Order.

Furthermore, the aforementioned condition may have violated SHA’s ethics policies and contract provisions. Specifically, SHA’s policies prohibit a former SHA employee from having a direct or indirect interest in an SHA consultant contract (for example, working on an SHA consultant services contract) for one year (referred to as limited duration) after the employee’s tenure with SHA. The policies further provide that employees who “participate significantly” in a contract as State employees (which we believe applies to this employee) are prohibited from having any direct or indirect interest in the contract (that is, for the duration of the contract regardless of the duration). Furthermore, the policies provide that this prohibition is imposed on the firm through the firm’s contract with SHA and is also imposed on former SHA employees by State Government Article 15-504(d) of the Annotated Code of Maryland.

Recommendation 2

We recommend that SHA

- a. take appropriate action regarding the aforementioned former employee’s continued involvement with this contract and refer the matter to the State Ethics Commission; and**
- b. ensure that employees comply with State Ethics Laws, Governor’s Executive Orders, and SHA policies.**

Finding 3

SHA did not ensure that firms doing business with SHA complied with State Ethics Laws and SHA policies regarding the hiring of former State employees.

Analysis

SHA did not ensure that firms doing business with SHA complied with State Ethics Laws and SHA policies regarding the hiring of former State employees. We were advised SHA employees were routinely hired by firms doing business with SHA but no attempts were made to identify these employees and/or to ensure that their employment was not violating State Ethics Laws and SHA policies. For example, our review of the bid proposal submitted by one firm⁶ disclosed that the

⁶ This firm received one of the \$16 million contracts noted in finding 1 and is referenced in all of the other findings.

firm actively promoted former SHA employees in its bid submission. Specifically, the bid submission stated that no learning curve would be needed because its staff included a former SHA Chief Engineer, District Engineers from three districts, Area Engineers from two districts, a District Traffic Engineer, and many SHA project engineers, construction inspectors, and design engineers. SHA did not attempt to identify the former employees to ensure they were not working on SHA contracts in violation of the aforementioned laws and policies.

We requested that SHA obtain the listing of former employees for both of the firms that were awarded the \$16 million contracts noted in finding 1. One firm refused to provide SHA with the listing but the aforementioned firm (discussed in the preceding paragraph) disclosed that 35 former SHA employees were employed by the firm as of September 2010 (including the employee in finding 2).

Our review of these 35 employees disclosed that, in addition to the individual referred to in finding 2, another individual was hired within nine months of retirement from SHA and was on the screening committee that was responsible for evaluating bid proposals for a contract that was awarded to the firm. SHA management advised us that these employment arrangements did not conflict with State laws and regulations or SHA policies (excepting the relationship in finding 2) as long as former employees were working on different projects (that is, other than those for which they were specifically involved in procuring). However, SHA had no way of knowing whether these firms were using former employees on its SHA contracts.

State law provides that a former official or employee may not assist or represent a party, other than the State, in a case, contract, or other specific matter for compensation if the matter involves State government and the former official or employee participated significantly in the matter as an official or employee. In addition, SHA policy prohibits a firm from hiring a former SHA employee to work on a matter in which the former SHA employee “participated significantly” as a State employee and prohibits a former SHA employee from having a direct or indirect interest in an SHA contract for one year after the former employee’s tenure with SHA.

Recommendation 3

We recommend that SHA

- a. periodically obtain a record of former SHA employees from those firms that provide contractual services for SHA; and**
- b. refer to these records during the invoice payment approval process to determine if the firms were in compliance with State laws, regulations, and SHA policies prohibiting former employees from working on**

contracts/projects for which they were involved with the related procurement.

Questionable Procurement Practices

Finding 4

SHA's procurement of two \$16 million contracts circumvented certain established independent bid evaluation processes and was not adequately documented.

Analysis

SHA's procurement of the aforementioned two \$16 million contracts for construction management and inspection services, awarded in October 2008 and December 2008, circumvented certain established independent bid evaluation processes and was not adequately documented. SHA consolidated the procurement of these contracts and issued awards to the two highest-rated firms. Our review of the evaluation processes involving these firms disclosed the following conditions:

- SHA's Office of Procurement and Contracts (OPC) did not perform a complete rating of the technical proposals as required. Specifically, OPC only evaluated and rated four of the fourteen categories used to rank the firms (scope of services, work plan, time distribution, and past performance) which accounted for less than 50 percent of the possible assignable points. In this regard, we noted that OPC did not evaluate the "key employee" category which was the highest-weighted category. According to senior SHA management, all of the categories had been rated by OPC in the past but, this practice had been discontinued. OPC management advised us that they normally would have performed the review of the category with the highest weight, but did not do so this for this contract to expedite the contract approval process. If OPC had rated the remaining ten categories, the final ratings of the firms could have been different which could have impacted the ultimate award of the contracts.
- SHA did not document how disparities in the evaluation of technical proposals by the Office of Construction (OOC) and the portion of the evaluation performed by OPC were resolved. In this regard, the OPC rated one of the winning firms sixth out of the ten firms who submitted a proposal, while OOC rated this firm second (a contract was awarded to the two highest ranked firms). This is significant because these large disparities could have impacted the ultimate award. The OPC employee who performed these evaluations advised us that the recommendation to award these contracts was

basically deferred to the OOC since OOC personnel were the ultimate users of the services being procured. (Also, as noted above, OPC had not completed the evaluation process.) As a result, the scores provided to the screening committee reflected the OOC ratings.

- SHA could not adequately document certain key components of the rating process. For example, although the OOC performed a rating of the key employees based on nine attributes, the individual rating forms were not always signed by the raters, there was no documentation to support changes to the forms, and the ratings on the individual forms did not always agree with the summary schedules. In addition, OOC did not prepare the required documentation to justify the key employee ratings. Specifically, although OOC rated the key staff in October 2006, the related narrative documentation was not prepared until April 2008, after the OOC and OPC recommendations had been submitted to the screening committee. In addition, there was no documentation of the OOC evaluation of a change in one of the firm's key staff in calendar year 2007. According to management employees from both the OOC and the OPC, the documentation should have been prepared in conjunction with the key staff category ratings to support the assigned ratings.
- SHA's independent contract approval process normally provided by the screening committee was compromised. Two of the four members who served on the committee for these contracts were not officially designated to serve on the screening committee and there was no documentation to substantiate that they were subsequently authorized to serve on the committee. In addition, these two members were OOC employees who had previously evaluated the proposals and rated the firms. As such, these two members reviewed their own evaluations in the capacity as screening committee members which, in effect, compromised the independent approval process. We were advised by SHA management that, although there was no written policy regarding the composition of the screening committee, the intent was for the committee and its members to be independent of other procurement-related groups. Finally, another committee member that retired from SHA was hired by one of the winning firms within nine months of leaving SHA (finding 3).

The aforementioned discrepancies raise significant concerns with the integrity of the contract awards considering the potential conflicts of interest noted in our preceding findings.⁷ Accordingly, there is a lack of assurance that the contracts were awarded to the two most qualified firms.

⁷ As previously mentioned, two employees involved in the contract procurement (commented upon in findings 1 and 2) had certain financial relationships with one of the firms awarded the contract. These individuals were directly involved in the procurement process and supervised employees who were directly involved in the procurement.

Recommendation 4

We recommend that SHA

- a. ensure that OPC evaluates all proposal categories,**
- b. document the resolution of rating variances between OPC and units requesting services,**
- c. ensure that bid evaluations and ratings are fully and adequately documented, and**
- d. establish a written policy regarding the composition of the screening committee and ensure that the committee's independence is maintained during the evaluation process.**

Improper Use of Contract Funds

Finding 5

SHA solicited the cooperation of two of the firms involved in the hotline allegation to redirect contract funds from the two aforementioned \$16 million contracts for unrelated projects, and/or to conceal overspending on other contracts, thereby circumventing Board of Public Works oversight and approval.

Analysis

SHA solicited the cooperation of two of the firms involved in the hotline allegation to redirect contract funds from the two aforementioned \$16 million contracts for unrelated projects, and/or to conceal overspending on other contracts, thereby circumventing Board of Public Works oversight and approval. SHA solicited the cooperation of these two firms through correspondence referred to as "extension of services" letters which requested the firms to provide services that were not within the defined scope of their BPW-approved contracts and instructed the firms how to submit their invoices to facilitate the payments. Specifically, we noted the following issues related to the senior SHA management employee discussed in Finding 1 and the aforementioned \$16 million contracts:

- The contracts were used to cover overspending on other contracts. For example, on January 21, 2009, this senior SHA management employee emailed another SHA management employee asking if it was possible to "rob some funds" from one of the contracts to pay approximately \$60,000 for services provided by this same firm under another contract in another district that had no funds available. In addition, on October 27, 2010, the senior SHA management employee sent a letter to a firm requesting its cooperation to use one of the contracts to provide inspection services in another district when the funding on a different contract with this firm was fully expended. In the letter,

the employee anticipated that up to \$400,000 would be used but stated that the total amount should not exceed \$800,000 and provided detailed instruction for how the bills for these non-contract services were to be prepared and submitted for payment. The request was subsequently accepted by the former SHA employee commented in finding 2 in this individual's role as an executive of this firm.

- Contracts were used for services that were not within the scope of the contract. For example, on November 6, 2008, the senior SHA management employee sent a letter to one firm requesting that it use funds from one contract (its \$16 million construction management and inspection services contract) to provide technical support, maintenance, and enhancements to the OOC's internal Management Construction Management System (MCMS). While SHA considered this scope modification as an "extension of our Supplemental Construction Inspection Contract," the firm indicated in its response that this request was not an extension of service, but an additional task and nevertheless agreed to the modification request.

SHA did not maintain records to account for the potential financial impact of these activities and could not readily provide us with the total amount improperly expended on these contracts. However, we were advised that, as of August 3, 2010, approximately \$1.5 million had been diverted from one of these contracts to cover certain over-expenditures on another contract for inspection work in another district. In addition, our review of two paid invoices (dated June 3, 2010 and October 14, 2010) submitted by one of the firms for one of these contracts disclosed that the majority of the invoiced amounts (71 percent of \$250,583 and 65 percent of \$274,505) related to projects that were not within the defined scope of the BPW-approved contract from which they were paid (that is, the projects did not relate to work in the district for which the contract had been approved).

SHA management advised us that there was no documentation to substantiate the \$16 million estimated cost submitted to and approved by BPW for each of the aforementioned contracts. In addition, we noted that several of the firms that agreed to use their contract funds to cover unrelated services were subsequently awarded additional contracts. These factors could help to enable the aforementioned practices to occur.

SHA's improper use of these contracts appears to violate State laws and regulations which require contract modifications that materially change the scope of a contract or change the amount of the contract, or any cost component of the contract, by more than \$50,000 to be submitted to BPW for approval. In addition, the aforementioned conditions may have federal implications since these contracts are funded in part with federal funds.

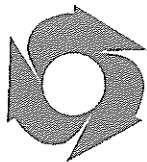
During our review we noted that the improper use of contract funds by OOC was not limited to the aforementioned firms and that senior SHA management was copied on certain correspondence sent to the cooperating firms. As a result, we are performing a special review of these activities and will be issuing the related report in the near future.

Recommendation 5

We recommend that SHA

- a. take appropriate corrective action regarding these matters,**
- b. develop procedures and controls to ensure contract funds are only used as authorized,**
- c. document the basis of contract amounts submitted to the BPW, and**
- d. obtain BPW approval for significant contract modifications.**

APPENDIX



Maryland Department of Transportation
The Secretary's Office

Martin O'Malley
Governor

Anthony G. Brown
Lt. Governor

Beverley K. Swaim-Staley
Secretary

Darrell B. Mobley
Deputy Secretary

June 23, 2011

Bruce A. Myers, CPA
Legislative Auditor
Office of Legislative Audits
Department of Legislative Services
Room 1202
301 West Preston Street
Baltimore MD 21201

Dear Mr. Myers:

Enclosed please find the Department's responses to the Legislative Auditor's Draft Special Review dated June 8, 2011, for the Maryland Department of Transportation (MDOT) – State Highway Administration (SHA). Additionally, an electronic version of this document has been sent to your office via email at response@ola.state.md.us (file name: SHAMyersDraftSpecialReview2011).

I want to assure you that the issues raised in your report are being taken seriously and are not acceptable practices. I also express my sincere appreciation to your staff for the assistance provided to me, as we have already begun the work to rectify these matters. As a result of Mr. Neil Pedersen's retirement effective June 30, 2011, I have designated Deputy Secretary Darrell B. Mobley to be the SHA Acting Administrator effective July 1, 2011.

If you or your staff has any questions or need additional information, please do not hesitate to contact Mr. Darrell B. Mobley, or myself. While at SHA, Mr. Mobley can be reached at 410-545-0400.

Sincerely,

A handwritten signature in black ink, appearing to read "Beverley K. Swaim-Staley".

Beverley K. Swaim-Staley
Secretary

Enclosure

cc: Ms. Lisa B. Conners, Director, Office of Finance, State Highway Administration
Mr. David L. Fleming, Chief Financial Officer, Maryland Department of Transportation
Ms. Cheryl R. B. Hill, Deputy Administrator for Administration, State Highway Administration
Mr. Joseph J. Lambdin, Director, Office of Audits, Maryland Department of Transportation
Mr. Darrell B. Mobley, Deputy Secretary, Maryland Department of Transportation
Ms. Sheri S. Sanford, Director, Office of Audits, State Highway Administration

**Maryland Department of Transportation
State Highway Administration
Special Review Responses
For the period covering July through December 2010**

Potential Violation of State Ethics Laws, Governor's Executive Order and SHA Policies

Finding 1

A senior Office of Construction (OOC) management employee appeared to have solicited funds from firms doing, or seeking to do, business with SHA, potentially violating State Ethics Laws, a Governor's Executive Order, and SHA policies.

Response 1:

- a. The Administration concurs with the auditors' recommendation. The employee to whom the auditor is referring to is no longer employed by SHA. This matter was referred to the State Ethics Commission by SHA on March 30, 2011.

- b. The Administration concurs with the auditors' recommendation. On March 7, 2011, SHA's Administrator issued a memorandum to SHA's senior management team reminding them of the May 2, 2011, deadline for filing the SEC's annual Financial Disclosure Statement (FDS) and requiring that they advise all appropriate staff of the deadline and their obligation to file. Employees are required to provide proof of filing to the SHA Office of Administration.

Periodically, SHA's Administrator issues a memorandum to all SHA employees regarding the State Ethics Laws, the Governor's Executive Order, and SHA's policy on gifts. The most recent memorandum was issued on April 18, 2011, which required employees to sign and date an acknowledgment form. The signed acknowledgment forms will be retained for future reference and audit. The importance of complying with the State Ethics Laws, the Governor's Executive Order, and SHA policies will continue to be discussed at SHA's Senior Management Team meetings. All employees will be informed that a failure to comply will result in disciplinary action, including termination, when warranted. The SEC has provided ethics training regarding the above-referenced law, Executive Order and policy to SHA's employees. The next training will be scheduled within sixty (60) days.

SHA's Administrator has appointed one of the Deputy Administrators as Ethics Coordinator for the SHA. Employees are encouraged to consult with the Ethics Coordinator concerning ethics questions or consult with the State Ethics Commission directly. In addition, SHA's Office of Audits has a fraud hotline where alleged ethics violations can be reported.

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- c. The Administration concurs with the auditors' recommendation and discussed with the State Ethics Commission the need for the former employee to file amended disclosure statements for years when the relationship was not disclosed. As mentioned above, this matter was formally referred to the State Ethics Commission on March 30, 2011, for follow-up.

Finding 2

A former senior management employee was hired by a firm doing business with SHA within 12 days of retirement and subsequently worked on an SHA contract that, as an employee, this individual had helped to procure.

Response 2:

- a. The Administration concurs with the auditors' recommendation. A letter dated April 6, 2011, was sent to the aforementioned former employee's consulting firm along with a copy of the Administrator's March 9, 2011, memorandum to all consulting firms doing business with SHA, reminding it that failure to comply could result in violations of the State Ethics Laws, Governor's Executive Order and SHA policies. The firm was also notified that this matter was referred to the State Ethics Commission. SHA's Office of Audits will be conducting random audits of invoices to confirm compliance with the State Ethics Laws and SHA's one year prohibition. A letter was sent to the aforementioned former employee's consulting firm on June 22, 2011, prohibiting the aforementioned former employee from working on this contract until further notice. In this letter, SHA requests the firm to conduct a comprehensive review of SHA contracts, for the period of January 1, 2009, to the present, to determine whether the aforementioned former employee or any other former SHA employees violated the terms of the General Conditions for Consulting Services Contracts and also determine whether any former SHA employees are involved in these contracts regardless of the date of the employees' termination of their employment with SHA.
- b. The Administration concurs with the auditors' recommendation. SHA respectfully directs your attention to its response to Finding 1 above and incorporates that response by reference here.

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Finding 3

SHA did not ensure that firms doing business with SHA complied with State Ethics Laws and SHA policies regarding the hiring of former State employees.

Response 3:

- a. The Administration concurs with the auditors' recommendation. SHA will require that all consulting firms submit on a quarterly basis a list of all former SHA employees who are employed by the firm. By June 30, 2011, an electronic mailbox will be established in order to facilitate the first quarterly reporting. The consulting firms will be required to certify these lists indicating that they are in "compliance with the General Conditions prohibiting a former SHA employee from working on any SHA contract for one year after leaving SHA and State Ethics Laws prohibiting work on a matter in which a former SHA employee participated significantly as a State employee, for an unlimited duration."

Failure to provide the above information could result in termination of the consultant services contract. In the future, this certification will be required for all solicitation documents as well. The firms will be directed to identify any potential ethics issues concerning its former SHA employees and seek an opinion from the State Ethics Commission regarding any potential conflicts of interest. This certification will be added to SHA's standard invoices for architectural and engineering services and solicitation documents and will be subject to periodic audit. These measures will be in place by December 31, 2011.

- b. The Administration concurs with the auditors' recommendation. Beginning August 1, 2011, SHA will require that contract managers perform a regular review during the invoice payment approval process to ensure that firms are complying with the restrictions indicated in the certification statement. SHA will direct the consulting firms to obtain an opinion from the State Ethics Commission regarding any potential conflicts of interest. SHA's Office of Audits will conduct periodic follow-up audits to ensure that the review by the contract managers is occurring. An advisory group comprised of SHA managers was formed in June 2011 and one of its tasks is to review the lists on a quarterly basis and identify, based on their knowledge of the former employees' involvement in the contract process at SHA, any former SHA employees who should not be working on SHA contracts.

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Questionable Procurement Practices

Finding 4

SHA's procurement of two \$16 million contracts circumvented certain established independent bid evaluation processes and was not adequately documented.

Response 4:

- a. The Administration concurs with the auditors' recommendation. The Department will assess the existing structure of the SHA Office of Procurement and Contracts. Processes were in place but not followed. The Department's Deputy Secretary will begin working with SHA as the Acting Administrator on July 1, 2011. Accordingly, the Deputy Secretary/Acting Administrator will determine whether additional personnel actions need to be made to ensure that policies and procedures will be followed, without fail, in the future. Further, the Office of Audits will have an increased role in reviewing the consultant firm selection process. By August 1, 2011, a plan will be in place concerning restructuring the Office of Procurement and Contracts.
- b. The Administration concurs with the auditors' recommendation. The Deputy Secretary/Acting Administrator will establish a work group to review the procedures and guidelines and determine the membership of the Consultant Screening Committee within sixty (60) days. We will re-evaluate the composition of the independent Consultant Screening Committee. The resolution of rating variances of the Office of Procurements and Contracts and units requesting services will be documented and retained.
- c. The Administration concurs with the auditors' recommendation. Effective August 31, 2011, a separate quality control review function will be established within the Office of Procurements and Contracts. This function will ensure that all technical evaluations and ratings are fully and adequately documented and retained in the selection file. The SHA's Office of Audits will conduct follow-up audits to ensure compliance.
- d. The Administration concurs with the auditors' recommendation. As a result of the efforts described in responses 4(a) and 4(b), SHA will establish a written policy regarding the composition of the Consultant Screening Committee and ensure that the Committee's independence is maintained during the evaluation process.

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Improper Use of Contract Funds

Finding 5

SHA solicited the cooperation of two of the firms involved in the hotline allegation to redirect contract funds from the two aforementioned \$16 million contracts for unrelated projects, and/or to conceal overspending on other contracts, thereby circumventing Board of Public Works oversight and approval.

Response 5:

- a. The Administration concurs with the auditors' recommendation. SHA has taken corrective actions concerning personnel who were the subject of OLA's findings. As mentioned previously, in June 2011, SHA organized an advisory group to review the procurement process and recommend process improvements. The Office of Finance will coordinate with the Office of Procurement and Contracts to implement additional adjustments to the financial management system that will strengthen internal controls and improve accountability. By September 30, 2011, the Office of Audits will be restructured to provide a more focused and effective oversight of the procurement process. Finally, additional mandatory training will be provided to procurement staff and contract managers by December 31, 2011.

With regard to the two aforementioned contracts, SHA will suspend awarding additional task orders until an internal assessment is completed. SHA is reviewing all task orders issued under these two contracts and to the extent practical any necessary corrective action will be taken including seeking retroactive BPW approval.

- b. The Administration concurs with the auditors' recommendation. As stated above, SHA's Administrator issued a memorandum dated March 9, 2011, to SHA's senior managers addressing the procurement and management of consultant contracts. The memorandum specifically discusses limiting the use of contracts that are awarded for a certain scope of services to only that scope of services unless a contract modification is approved by the BPW. The memorandum also instructed offices that if they have any tasks that are currently being performed outside the original scope of the contract, those tasks must have ended by March 31, 2011. SHA is currently performing a review of all active consultant contracts to determine that any such tasks have ended and that contract funds are used only as authorized. Any out of scope contract usage identified will be analyzed and appropriate corrective actions taken, including seeking retroactive BPW approval. This review will be completed by December 31, 2011. As these reviews are conducted, we are and will continue to cooperate fully with the Office of Legislative Auditors as they perform an expanded special review of improper use of consultant contract funds.

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To strengthen internal controls, SHA's Office of Finance will require a checklist that documents contract manager's certification of compliance with contract terms and conditions. This checklist will be a required document in the invoice payment process. SHA's Office of Audits will audit invoices on a random basis to ensure compliance with contract terms and conditions. This process, including necessary training, will be implemented by August 31, 2011.

- c. The Administration concurs with the auditors' recommendation and will develop procedures for documenting the basis for the dollar amount of contracts submitted to the BPW for approval consistent with what is anticipated to be the business need. Interim procedures will be in place by mid-July 2011. More comprehensive procedures will be developed and implemented as part of the effort referenced in response 5(d) below.
- d. The Administration concurs with the auditors' recommendation and will seek retroactive approval from the BPW for significant contract modifications. The Department will seek the advice of state procurement experts, including BPW staff, to conduct a systematic review of the overall procurement process at SHA to assure that a comprehensive corrective action plan is developed and implemented. We recognize that this may be a time consuming approach, but given the complexity of the procurement process, we believe this review is warranted. The resultant corrective measures will be in place by December 31, 2011.