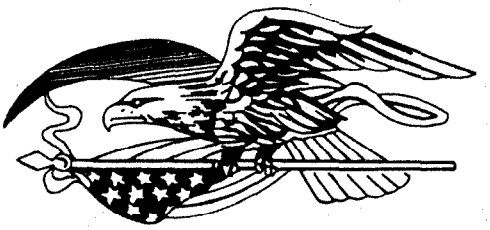
United States General Accounting Office

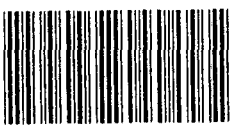
GAO

Office of Special Investigations

SPECIAL REPORT



FTA New York Mas Transit Grants:
False Statements to FTA Grantes/Grantee
Violations of Contracting Policy



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GAO

United States
General Accounting Office
Washington, D.C. 20548

Office of Special Investigations

B-245557

September 10, 1992

Congressional Recipients

This report presents the results of our investigation, about which you were advised in a January 1992[1] report. That January report concluded that the Long Island Railroad (LIRR), a Federal Transit Administration (FTA)[2] grantee, misused federal funds because it lacked effective financial, technical, and other management systems to ensure compliance with federal requirements. The report also noted that FTA's Region II (headquartered in New York) was slow to detect and correct serious and long-standing procurement and quality assurance deficiencies on the Holban/Hillside Maintenance Facility, a $393 million LIRR construction project that received $176.4 million of its funding from FTA. In addition, a 1990 audit report by the New York State Comptroller's Office criticized the project, stating that LIRR had no assurance that millions of dollars in costs were fair and reasonable. The Committees and Members of Congress that asked to receive the results of GAO's FTA reviews are listed at the end of this letter.

On the bases of GAO's earlier review and the New York State Comptroller's report, we initiated an investigation to determine if fraud had contributed to the misuse of federal funds on the Holban/Hillside project. Specifically, we investigated (1) the Minority Business Enterprise (MBE) program of North Star/Tern Star, the largest prime contractor (prime) on the project, and (2) two contract change orders, totaling approximately $2 million, that LIRR approved for the same contractor.

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[1]Mass Transit Grants: Noncompliance and Misspent Funds by Two Grantees in UMTA's New York Region (GAO/RCED-92-38, Jan. 23, 1992).

[2]Before the December 18, 1991, enactment of the Intermodal Surface Transportation Efficiency Act of 1991 (P.L. 102-240), FTA was known as the Urban Mass Transportation Administration.

RESULTS IN BRIEF

On the Holban/Hillside project, we found that the prime made false statements to New York State's Metropolitan Transportation Authority (MTA) and LIRR regarding the involvement of MBE subcontractors in the project, for the purpose of causing LIRR to award it the contract. (See app. II.) Those false statements concerned the substantive function of the MBEs on the project and the dollar amounts of the MBE subcontracts for the project.

Federal and state MBE regulations require prime contractors to use minority- and women-owned businesses as subcontractors that serve a substantive, or "commercially useful[,] function." (49 C.F.R. § 23.47(d)(1) (1991)) The prime's representation, in its contract bid, of MBE participation and its overstated MBE subcontract values caused LIRR to grant it two prime contracts although two other contractors had submitted lower bids. However, the largest MBE subcontractor was controlled by the prime rather than the MBE's owner and, therefore, did not serve a commercially useful function on the project. The prime's president subsequently told us that the MBE had brought nothing to the project, other than its minority status, and that the purpose of including it in the bid was to demonstrate to LIRR that the prime met MBE requirements. In addition, the schedule that the prime submitted to LIRR after the contract was awarded, listing all MBEs on the contract, misrepresented MBE participation on the project: It continued to overstate the dollar amounts of actual MBE subcontracts and listed an MBE that had neither bid nor performed any work on the project. Senior officials of the prime later admitted that the subcontract values had been overstated to meet MBE dollar-amount requirements. The prime's president told us that the government forces him to use "charlatan" MBEs because a sufficient number of MBEs are not available to perform on large construction projects.

In addition, the Federal Bureau of Investigation (FBI) and the U.S. Department of Transportation, Office of Inspector General, have opened investigations for possible fraud on the basis of the MBE information discussed in this report. In turn, the FBI and Transportation's Office of Inspector General presented the matter to the U.S. Attorney's Office for the Eastern District of New York, which also agreed to investigate the allegations for possible fraud violations.

As a second matter of import during our investigation, we also determined that two change orders--amendments to the

contract to correct a deficiency or ambiguity in the contract--violated LIRR's written change order procedures and lacked appropriate supporting documentation. (See app. III.) The two change orders totaled $1,993,000. LIRR's Director of Contracts and Purchasing, whose authorizing signature was required for all change orders, initially refused to sign for the two because they had been negotiated without his knowledge, in violation of LIRR procedures. He also stated his belief that by approving the change orders, LIRR was "buying performance"--or paying more than the contracted price to ensure completion of the project. LIRR's president subsequently ordered him to sign for both.

In addition, LIRR's Internal Audit Department refused to render an opinion in a report as to the reasonableness of the larger claim--$1,500,000--because it was "unauditable" and "not based on verifiable data/calculations." Less than 2 months after LIRR made the last payment on these change orders and before the project was completed, LIRR removed the prime from the project for material breaches of contract resulting from nonperformance.

METHODOLOGY

We performed our investigation between July 1991 and April 1992. We interviewed current and former personnel from the New York State Comptroller's Office; MTA; LIRR; Parsons Brinkerhoff/Morrison Knudsen (PB/MK), the project's construction manager; North Star/Tern Star; and several of the prime's minority subcontractors. We also reviewed New York State Comptroller, LIRR, and other audit reports; federal and MTA regulations and procedures governing the MBE program; LIRR regulations for the issuance/approval of change orders; and documents related to the MBE activities and change orders on the Holban/Hillside project discussed in this report.

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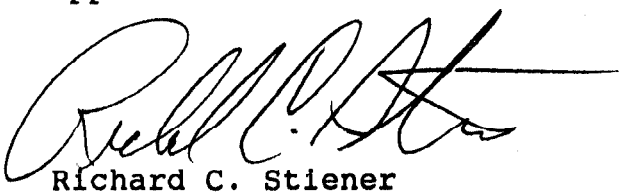
We will send copies of this report to the Secretary of Transportation; the Administrator, FTA; and the Director, FTA Region II. Copies will be sent to others upon request. If you have questions concerning this report, please call

me, at (202) 272-5500, or Robert Hast, Assistant Director for Investigations, GAO New York Regional Office, at (212) 264-0982. Major contributors to this report are listed in appendix IV.



Richard C. Stiener
Director

List of Recipients

The Honorable John Glenn, Chairman
Committee on Governmental Affairs
United States Senate

The Honorable Donald W. Riegle, Jr., Chairman
Committee on Banking, Housing, and Urban Affairs
United States Senate

The Honorable Alan Cranston, Chairman
Subcommittee on Housing and Urban Affairs
Committee on Banking, Housing, and Urban Affairs
United States Senate

The Honorable Barbara Boxer, Chair
Government Activities and Transportation Subcommittee
Committee on Government Operations
House of Representatives

The Honorable Cardiss Collins
House of Representatives

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Abbreviations

FBI	Federal Bureau of Investigation
FTA	Federal Transit Administration
GAO	General Accounting Office
LIRR	Long Island Railroad
MBE	minority business enterprise
MTA	Metropolitan Transportation Authority
OSI	Office of Special Investigations
PB/MK	Parsons Brinkerhoff/Morrison Knudsen
UMTA	Urban Mass Transportation Administration

BACKGROUND

The Holban/Hillside Maintenance Facility project was completed in 1991, over 3 years behind schedule. Project costs increased from $171 million to $393 million, which included $176.4 million in FTA funds. FTA gives its grantees, such as LIRR, primary responsibility for the appropriate use of federal mass transit funds but retains oversight responsibilities. Citing problems at the Holban/Hillside project, FTA stopped funding all LIRR capital projects in 1989. It reinstated funding in 1991 after LIRR implemented management improvements.

CONTRACTS FOR THE HOLBAN/HILLSIDE PROJECT

The LIRR is a wholly owned subsidiary of MTA, a New York State agency that has oversight responsibilities for five other New York City area transportation authorities. On September 5, 1984, LIRR awarded prime contract 5153 to North Star/Tern Star, a joint venture, to construct the Under Car Cleaning/Wheel Truing Shop at the Holban/Hillside Maintenance Facility for $14,460,000. On July 10, 1985, LIRR also awarded prime contract 5128 to North Star/Tern Star to construct the Car Repair Shop at Holban/Hillside for $79,635,310.

Although the prime's bids exceeded the low bids on the two contracts by over $1 million--$400,000 and $618,310, respectively--LIRR awarded the contracts to the prime because the bids of the otherwise qualified low bidders did not meet federal and state MBE requirements for publicly funded construction projects. Federal regulations required recipients of FTA funding, such as MTA, to award 10 percent of all federally funded contract dollars to eligible MBEs. MTA's Board of Directors, with FTA agreement, required MTA to award 20 percent of all contract dollars to minority-owned businesses and 5 percent to women-owned businesses, regardless of funding source.

Prior to awarding these two contracts, LIRR contracted with Parsons Brinkerhoff/Morrison Knudsen (PB/MK) to be the project's construction manager. As manager, PB/MK's duties included monitoring MBE program compliance, reviewing change order requests, and participating in change order negotiations.

MINORITY BUSINESS ENTERPRISE PROGRAM

The Congress created the MBE program[3] to increase opportunities for minority-owned businesses to participate in and benefit from federally funded contracts. Both federal and MTA

[3]Small Business Act, 15 U.S.C. §§ 631, 637 (1988).

regulations require that minorities or women own at least 51 percent of their businesses to qualify for the program. They also require that MBEs be controlled by their owners and that they serve a "commercially useful function" on a construction project, that is, they exercise independent control over their sections of a project. (49 C.F.R. § 23.47(d)(1))

MTA's Affirmative Action Department reviews all prospective MBEs to verify authenticity of ownership and ability to perform. At the time of a prime contractor's original bid, MTA requires that the prime contractor and the proposed MBEs sign and submit an intention-to-subcontract form. No later than 90 days after a prime contract is awarded, MTA also requires a written subcontractual agreement between a prime contractor and any MBE appearing on the MBE schedule. MTA then requires contractors to submit monthly schedules containing the dollar value of MBE subcontracts.

An April 1991 report by New York State's Office of the State Comptroller, Selected Contracting Practices Relating to Construction of the LIRR's Holban/Hillside Maintenance Facility, identified problems with the use of MBEs by the prime on contracts 5128 and 5153. According to the report, although the prime was awarded the contracts because its bids met MBE requirements, the prime had not met the requirements when LIRR placed it in default, removing it from the project: Specifically, it had not met MTA's minority-owned business requirements on contract 5128 or the women-owned business requirements on contract 5153. The New York State report concluded that because the prime was not the low bidder, LIRR had paid $1 million more than was appropriate by awarding the two contracts to a contractor that subsequently failed to meet its indicated MBE requirements.[4]

[4]We did not assess the validity of this conclusion.

FALSE STATEMENTS BY PRIME CONTRACTOR INVOLVING MBE PROGRAM

We found that the prime made false statements to MTA and LIRR in its contract bids and schedules, concerning MBE involvement in the project. The prime exerted fundamental control over some of the MBE subcontractors included in its bids and schedules, in violation of federal and MTA regulations. It also overstated the dollar amounts of its MBE subcontracts and included an MBE in its schedule of participating MBEs although the MBE had neither bid nor worked on the project. A discussion follows of four MBE subcontractors involved with the prime on the project. Two of the MBE subcontractors performed excavation and concrete work; the third, steel-erection work. The fourth was an MBE subcontractor in concrete but never worked for the prime on the project.

SOME MBES SERVED NO COMMERCIALLY USEFUL FUNCTION

The prime violated MBE program--federal and MTA--regulations by using MBEs that exercised little control, or served no commercially useful function, over their own sections of the project. For example, on contract 5128 a senior official of the prime told us that the prime exercised complete control over an excavation and concrete MBE subcontractor that had the largest MBE subcontract of the project: It supervised the MBE's operations, ordered its materials and labor, and advanced its payroll and material costs to it. According to a PB/MK safety inspector who worked at the project site, no difference existed between the prime and this MBE subcontractor.

According to a project manager of the prime, the prime assigned one of its employees to the MBE to oversee its operations and kept him on the MBE's payroll. We reviewed payroll records submitted by both the prime and the MBE and confirmed that this individual had alternated employment between the prime and the MBE. The project manager also told us that the prime billed work it controlled through the MBE to make it appear (to MTA) that (1) the MBE had done the work and (2) the prime was meeting its MBE requirements. According to a non-MBE subcontractor to the prime, his verbal subcontract agreement was with the prime. However, the written subcontract he later received was with the MBE, of whom he had never heard. A New York City Transit Authority audit report on the MBE, dated November 2, 1987, determined that the MBE had no independent control of its operations.

Officials of the prime told us that the MBE's president lacked the technical expertise to run a construction company or to oversee an $11.3-million subcontract. The subcontract was to perform excavation and concrete work for the project's foundation. The officials also stated that the president had been a former laborer for the prime and had no special trade experience or knowledge. To

illustrate, during his deposition for annual MBE recertification by the MTA, the MBE's president was asked to specify the type of equipment needed to perform the subcontract. His reply was "mostly shovels." He stated that the prime would bring the heavy equipment "to start the initial digging." He continued, "I have never been in machinery in my life." The MBE's president also acknowledged during his deposition that he did not know how to read blue prints and needed help from the prime's project manager in preparing his bid for the subcontract.

The excavation and concrete MBE was awarded the subcontract even though it owned no major construction equipment and had no full-time employees on its payroll. According to a project manager of the prime, the prime ordered all of the MBE's labor from the local union hall. As a further example of the MBE's lack of independent control, most of the MBE's employees--as our review of its and the prime's payroll records confirmed--continued to work on the project for the prime when the MBE was removed from the job for alleged unlawful job-related activities. The prime also informed PB/MK of its intention to use the MBE's personnel after the MBE was removed.

Our attempts to interview the MBE's president were unsuccessful. When we questioned the prime's president, he acknowledged that the MBE had brought nothing to the job other than its minority status and that the purpose of the MBE's existence was to meet MBE requirements.

Further, the prime alternated employees between its payroll and the payrolls of the excavation and concrete MBE and a second MBE subcontractor that also performed excavation and concrete work. This occurred despite a precontract warning from a senior LIRR official who learned that the prime had done so on a previous public project. For example, payroll records of the second MBE reveal that some employees appeared on the prime's payroll and those of the first and second MBEs. The second MBE was removed from the project because it had been suspended from New York State's Department of Transportation program for minority-owned businesses for, among other reasons, alternating personnel with the prime on another public project. Additionally, a woman-owned MBE subcontractor that worked in steel erection for the prime was suspended or denied certification from four New York agencies, including MTA. The MTA concluded that the woman-owned steel-erection MBE "performed no commercially useful function and . . . its activity resembled that of a broker which performs in name only while relinquishing essential control to others."

To obtain his point of view, we interviewed the prime's vice president who signed the contract and prepared MBE schedules. According to the vice president, completing the job was the prime's

responsibility; and it could not rely on the MBEs to complete the work. Furthermore, according to the vice president, he maintained tight control of the MBEs on the job site because he himself was financially liable.

OVERSTATED VALUES OF MBE SUBCONTRACTS AND ERRONEOUS INCLUSION OF ONE MBE

Senior officials of the prime admitted to us that the prime had overstated the dollar amounts of its MBE subcontracts to meet the MBE dollar-amount requirements. For example, for contract 5128 the prime represented, on an MTA-required monthly schedule, that it had an $11.3 million subcontract with the first excavation and concrete MBE. However, in a deposition given for annual MBE recertification, that MBE's president reported that his subcontract was for $2 million. In addition, the prime represented that it had a $4.4-million subcontract for steel erection with the previously mentioned woman-owned MBE, just over the minimum 5 percent of the original contract needed for contract award eligibility. During her deposition to MTA, however, the president of the steel-erection MBE stated that her subcontract with the prime was probably for $3.5 million. A schedule, which the prime submitted to LIRR and MTA at the time of the MBE's deposition, reported a total subcontract amount with the steel-erection MBE for $3.25 million. When we interviewed this MBE's president, she could not recall the contract amount.

In another instance on contract 5128, the prime submitted a document to LIRR that, according to a senior LIRR official, represented that a $2 million subcontract existed between the prime and a fourth MBE that worked in concrete. When we interviewed this MBE's president, he stated that he had initially allowed the prime to use his name for bidding the prime contract. However, once LIRR awarded the prime contract, he never bid on the Holban/Hillside project, he told the prime's vice president that he had no intention of bidding on it, and he did not work on it. Furthermore, without entering into a written subcontract with the concrete MBE within MTA's required 90 days, the prime continued to list it as a participating MBE subcontractor.

When confronted with these discrepancies, the prime's president told us that we (GAO) were "naive" and that the government forces him to use "charlatan" MBEs because a sufficient number of legitimate MBEs capable of performing major contract work do not exist.

INVESTIGATIONS RESULTING FROM GAO'S WORK

We presented the previously discussed information on MBEs and the prime to the FBI and the U.S. Department of Transportation,

Office of Inspector General. They have opened their own investigations concerning possible fraud with respect to these MBE practices. The two agencies have also presented the matter to the U.S. Attorney's Office for the Eastern District of New York, which has agreed to investigate the allegations for possible fraud violations.

LIRR CHANGE ORDER PROCEDURES WERE VIOLATED AND LIRR PAYMENTS WERE MADE CONTRARY TO RECOMMENDATIONS

LIRR approved and paid the two change orders we investigated--totaling approximately $2 million. However, LIRR's approval of the change orders violated established LIRR procedures concerning payment negotiation and documentation/claim support. According to LIRR's "Purchases and Materials Manual," a claim for additional costs processed as a change order must be accompanied by a proposal that includes documentation to prove that such costs will be incurred. On a claim "in excess of $10,000-20,000," LIRR's contract administrator and PB/MK must participate together in the negotiations involving the amount and reasonableness of the claim and ultimate change order. The manual also requires that written minutes of the negotiations be prepared. In addition, MTA's "All Agency Procurement Guidelines" states that LIRR is required to obtain approval from MTA's Board of Directors on change orders for $250,000 or more or for 15 percent or more of the total contract price.

Although not required to follow staff and PB/MK recommendations, LIRR's president ordered that the two change orders be paid, against recommendations not to do so: LIRR's Director of Contracts and Purchasing, its chief contract administrator, recommended against paying either change order; LIRR's General Counsel and Director of Audits recommended against paying the larger one, for $1,500,000; and senior PB/MK officials recommended against full payment of either one. On December 9, 1987, 2 months after making the final payment on the change orders, LIRR placed the prime in default, removing it from the project.

PREVIOUS CRITICISM OF LIRR AND CONTRACTOR HANDLING OF CHANGE ORDERS

An October 1990 audit report by New York State's Office of the State Comptroller--LIRR Abused the Change Order Process During Construction of the Holban/Hillside Maintenance Facility--identified many change orders as lacking evidence of proper support, such as cost estimates or negotiation minutes. According to the audit report, "[W]ithout a documented cost estimate or evidence of negotiation," there is "no assurance that the costs paid for these change orders were fair and reasonable." The report specifically identified the two change orders, totaling $1,993,000, that we investigated, saying they "lacked support and were of questionable validity." The Office of the State Comptroller also recommended "that the propriety of these [two] payments should be investigated by the appropriate State and/or Federal investigative bodies."

When we began our investigation, we inquired of local and federal law enforcement agencies with jurisdiction and determined

that no investigations had been opened on the two change orders. However, in 1989, before the state comptroller's report, the New York State Attorney General's Office obtained a 49-count indictment against the prime for submitting fraudulent change orders to LIRR. According to the indictment, the prime had submitted at least $225,000 in false change orders to LIRR. A New York Supreme Court dismissed the indictment because LIRR had failed to establish the prime's intent to commit larceny. (People v. North Star Contracting Corp., 205 N.Y.L.J. 21 (1991)) The court found that for about 2 years the prime had openly and routinely submitted lump sum estimates in connection with change orders and that LIRR's acceptance of the estimates ratified the prime's lump sum interpretation of the contract.

VIOLATION OF NEGOTIATION PROCEDURES AND LACK OF DOCUMENTATION/WRITTEN CLAIM

LIRR's approval of the change orders violated established LIRR procedures as stated in LIRR's "Purchases and Materials Manual" in that (1) the required personnel were neither informed of nor present at the negotiations on the change orders, (2) both change orders lacked appropriate documentation, and (3) the second change order was not based on a written claim.

Absence of Required Negotiation Participants

In July 1986, the prime submitted a written claim to LIRR for payment of "Owner-Caused Schedule & Cost Impacts," amounting to $5,918,271 on contract 5153, in support of the first change order. This claim alleged that because of LIRR-caused problems, the prime had incurred the additional costs and project completion had been postponed by 11 months. The claim was thus allegedly for work already completed rather than for proposed work, as required by LIRR's manual. The LIRR forwarded the claim to PB/MK for evaluation. In a December 9, 1986, memorandum to LIRR, PB/MK's project manager disagreed with most of the claim and advised LIRR to pay no more than $250,000.

In January 1987, however, according to a senior LIRR official, LIRR's then newly appointed Chief of Capital Construction negotiated the claim, and ultimately both change orders, with the prime's president: the first for $1,500,000 and the second for $493,000. According to high-ranking LIRR and PB/MK officials, the Chief excluded senior LIRR and PB/MK personnel required by LIRR procedures from the change order negotiations. According to LIRR's Director of Contracts and Purchasing (chief contract administrator for LIRR) at the time of the project, negotiations for both change orders were held without his participation, violating LIRR procedures.

When informed of the above statements, the former Chief of Capital Construction told us that (1) PB/MK was responsible for establishing the negotiated figures, (2) the Director of Contracts and Purchasing's supervisor had been involved, (3) the $1,500,000 was negotiated several months later than stated, and (4) his negotiations were under the direction of LIRR's president. Our review of documents and interviews with appropriate officials contradicted his version of the first three events. However, LIRR's president confirmed that the Chief of Capital Construction had performed the negotiations at his direction.

Lack of Required Documentation/Written Claim

On January 28, 1987, LIRR's Capital Construction Department recommended that a $250,000 payment be made on the claim for the first change order. The prime's invoice, dated February 6, 1987, referred to the change order for the claim as "Special Payment Contract 5153" but had no further information about the purpose of the invoice. The LIRR authorized the $250,000 payment on February 20, 1987, and paid it on March 11, 1987. LIRR contract records state that it was the first of two payments on the $1,500,000 change order, with the balance paid October 7, 1987.

LIRR authorized and paid the second change order for $493,000 on contract 5128 on the same dates as the initial payment on the first change order--February 20 and March 11, 1987, respectively. The prime's invoice for this change order was dated February 6, 1987, as was the invoice for the first change order. The invoice cited the second change order as a "Special Payment Contract 5128" but, as with the first change order, had no further information.

In addition, counter to LIRR procedures the second change order had no written claim, and thus no proposal with documentation, associated with it. LIRR and PB/MK records and our interviews support this absence of a claim. According to LIRR documents, the change order was "given toward anticipated claims" against LIRR. One former high-ranking LIRR official stated that it is "highly unusual to pay for anticipated claims." He was also surprised that LIRR would pay change orders with no support, which is against LIRR procedures.

CHANGE ORDERS PAID DESPITE LIRR AND PB/MK OBJECTIONS

After the January 1987 change order negotiations, the then LIRR Director of Contracts and Purchasing, whose authorizing signature was required for all change orders, initially changed the draft LIRR authorization letters for the two change orders to address his concerns about the change orders' appropriateness. The letters, as he changed them, stated that the payments were to provide the prime with "interim funds to assure the timely

completion and prosecution of the work." He believed LIRR was "buying performance" with the payments--or paying above the contracted price to ensure the project's completion. However, the prime refused to accept the changes to the letters, according to the Director, because it "had an agreement with [LIRR's Chief of Capital Construction]."

The Director told us that he then refused to sign the two authorization letters--for the initial $250,000 payment on the first change order and for the $493,000 payment for the second change order--because the letters did not accurately represent the payments' purpose. When he refused, according to the Director, LIRR's president ordered him to sign, which he did, "against [his] better judgement." However, LIRR's president, not the Director, signed the final documentation on the $1,250,000 balance of the claim on contract 5153.

According to a high-ranking LIRR official, a member of MTA's Board of Directors had questions about the $1,500,000 negotiated settlement for the first change order and asked LIRR's General Counsel to review the claim. On September 10, 1987, LIRR's General Counsel issued a memorandum stating that LIRR had liability in some areas of the claim but that determining the claim's value was impossible because the claim was based on "unauditable" amounts. According to a senior LIRR official, LIRR's General Counsel also personally recommended to LIRR's president that the claim not be paid.

On September 16, 1987, also in response to the MTA board member's inquiry about the $1,500,000 settlement, LIRR's Internal Audit Department reported on the claim to LIRR's Chief of Capital Construction. The report states: "[T]he proposed $1,500,000 settlement amount is not based on verifiable data/calculations"; and the claim's largest components appear to be "intangible, non-quantifiable factors. . . . Therefore we are unable to render an opinion regarding the reasonableness of the proposed settlement amount." In addition, LIRR's Director of Audits recommended personally to LIRR's president that the claim not be paid.

Previously, on September 10, 1987, LIRR requested MTA's Board of Directors to approve the entire $1,500,000 payment, citing the contract as being 97 percent complete. Following the MTA Board of Directors' approval, LIRR paid the balance of $1,250,000 on October 7, 1987. According to the MTA board member who previously questioned the $1,500,000 negotiated settlement, he had not been told that LIRR had violated its internal procedures, when the board approved the final payment. The board member stated that if he and the board had known of the violations, the board would have sent the matter to counsel for review before voting to approve.

With regard to the second change order, according to a senior PB/MK official, PB/MK "objected to the [$493,000] payment and refused" to take any responsibility for it. He stated that some senior LIRR officials also objected to the payment and refused to sign. LIRR paid it on March 11, 1987. The records that we reviewed at LIRR and PB/MK were inadequate to determine if the $493,000 change order had been presented to the MTA Board of Directors for its approval.

When we interviewed the then president of LIRR, he acknowledged that he had ordered the Director of Contracts and Purchasing to sign, despite the Director's objections and in violation of LIRR's contracting procedures. He also acknowledged authorizing the change orders' payment, against the personal recommendations of LIRR's General Counsel and Director of Audits, in hopes that this would "purchase" the prime's completion of contract 5153. He said he intended to place the prime in default on contract 5128 upon completion of 5153.

LIRR REMOVAL OF PRIME FROM THE PROJECT

On December 9, 1987, LIRR placed the prime in default for material breaches of contract involving nonperformance and other matters, removing it from the project. The former Chief of Capital Construction told us that the prime never performed the work stipulated in the negotiated settlement for the larger change order. Shortly after the final payment of $1,250,000 was made, the prime's president "came back asking for more money." According to the Chief, the prime's president told him that if more money was not paid, he (the prime's president) would stop work on the entire project, using his control over the project's trade union employees. This, according to the Chief, is what ultimately led to the prime's sudden default. The prime's president, when we confronted him with the Chief's statement, said "this was partially true" but that the money was owed him.

APPENDIX IV

MAJOR CONTRIBUTORS TO THIS REPORT

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