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COMMONWEALTH OF PENNSYLVANIA

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**A SPECIAL INVESTIGATION OF THE  
PENNSYLVANIA DEPARTMENT OF COMMUNITY AND  
ECONOMIC DEVELOPMENT,**

*Contract with the Pennsylvania State Association of Township Supervisors*

**December 2010**

**JACK WAGNER, AUDITOR GENERAL**  
**PENNSYLVANIA DEPARTMENT OF THE AUDITOR GENERAL**

December 7, 2010

The Honorable Edward G. Rendell  
Governor  
Commonwealth of Pennsylvania  
225 Main Capitol Building  
Harrisburg, Pennsylvania 17120

Dear Governor Rendell:

This report contains the results of the Department of the Auditor General's special investigation of the Pennsylvania Department of the Community and Economic Development ("DCED"), specifically, Contract No. 4000008729 with the Pennsylvania State Association of Township Supervisors ("PSATS") for training services. The investigation was initiated after the Department of the Auditor General received an allegation that PSATS was overbilling the Commonwealth for services provided.

Our investigation was hindered by PSATS' failure to promptly provide complete and accurate information to the investigators. Although it is formally organized as an unincorporated non-profit association, PSATS is, in fact, a large business enterprise and, as such, should be able to provide original records and other basic information to support its invoices to the Commonwealth. Accordingly, we are constrained to draw the adverse inference that its failure to provide all of the original records requested and complete and accurate information on a timely basis was done purposely to prevent our investigation from uncovering problems with PSATS' billings to the Commonwealth. We were also hindered by the lack of detail provided on PSATS' invoices to DCED, in that the format of the invoices does not lend itself to being substantiated.

Despite these obstacles, our investigation found the following:

- The now-former Executive Director of PSATS received compensation averaging \$407,608 per year in calendar years 2004 through 2008, which is excessive when compared to others in similar positions and which may be in violation of federal and state laws restricting the use of the net earnings of a nonprofit organization.
- DCED employees who were responsible for implementing and administering the training services program, and who were also responsible for evaluating

the competitive proposals submitted in 2005 for a new training services contract that was ultimately awarded to PSATS, had accepted meals, hotel lodging, and conference expenses from PSATS in the amount of \$2,716.69, including eleven meals during the time the competitive proposals were being evaluated, in violation of state gift and travel rules and possibly in violation of the Public Official and Employee Ethics Act.

- PSATS used a method to bill for reimbursement of the payroll costs for its employees' time in which all employees in a particular category were billed at the same rate, rather than billing for the actual rate for each employee, resulting in potential overcharges to the Commonwealth. Attempts to verify that the Commonwealth was not being overcharged were thwarted by PSATS' persistent failure or refusal to produce original payroll records -- conduct which supports an inference that it was done purposely to prevent us from determining the magnitude of the overcharges to the Commonwealth resulting from PSATS' method of billing.
- DCED permitted PSATS to add surcharges of 9% for "overhead" costs and 8% for "administrative" costs to pass-through billings for goods and services provided by third-party vendors and contractors, resulting in PSATS receiving reimbursement in excess of its actual indirect costs with respect to those billings, in violation of the contract. Our analysis indicates that, for every 100 invoices submitted to the Commonwealth, PSATS would receive approximately \$569,000 of excess compensation solely from the 17% surcharge on the cost of goods and services provided by third-party vendors and contractors.
- PSATS failed to provide an adequate explanation of the composition of the 9% surcharge that it added to all billings to cover "overhead costs" and the 8% surcharge to cover "administrative costs," making it impossible to determine whether such surcharges were in excess of actual overhead and administrative costs incurred in providing the services described in the contract.
- DCED permitted PSATS to bill for the aggregate costs of all training classes provided in a particular time period, rather than require PSATS to itemize the costs for each individual training class, thereby making it impossible to determine, from the information provided, whether PSATS gave proper credit for all registration fees actually collected from attendees of the training classes. With respect to two programs that we analyzed, we found that PSATS did not credit the Commonwealth for \$44,594 in registration fees collected.
- DCED has not established guidelines on eligible costs to be reimbursed under the contract. Consequently, DCED reimbursed PSATS for excessive and unreasonable costs relating to food provided at training seminars, meals from local restaurants, and training at historic inns and resorts. During the fiscal

year ended June 30, 2007, the more egregious of these expenses cost the Commonwealth approximately \$20,000.

The findings and recommendations presented in this report are intended to not only provide guidance to DCED when drafting and entering into future contracts for training services, but also to assist DCED in its monitoring of the current contract with PSATS and to serve as a basis for DCED to withhold future payments to PSATS until such time as PSATS provides the information necessary to prove that it has not overbilled the Commonwealth. If PSATS fails to provide such information, we would then recommend that DCED institute proceedings to debar PSATS from future Commonwealth contracts. It is unacceptable that an entity such as PSATS, which essentially owes its very existence to an act of the General Assembly and which receives a majority of its revenue from the Commonwealth, cannot or will not provide information to substantiate its invoices to the Commonwealth.

As already stated, we are particularly concerned about the amount of salary paid to PSATS' now-former Executive Director. Given the nature of PSATS as a nonprofit, quasi-public organization largely funded by tax dollars – both those raised at the local level and paid to PSATS as dues by its member townships, and those raised at the state level and paid to PSATS for services rendered – we find the amount to be excessive. A more reasonable amount of compensation would impose a lower burden on PSATS' member townships and reduce their costs accordingly.

Note that our investigation was neither designed nor intended to be a detailed study of every system, procedure, or transaction at PSATS. Accordingly, the findings and recommendations presented in this report pertain only to matters found during the investigation. We urge DCED to implement all of the recommendations made in this report. The Department of the Auditor General will follow-up at the appropriate time to determine whether our recommendations have been implemented.

We are also providing copies of this report to the Pennsylvania Office of Attorney General, State Ethics Commission, Pennsylvania Treasury Department, Pennsylvania Department of Revenue, and the Internal Revenue Service, as well as the other Commonwealth agencies, in addition to DCED, with previous or current contracts with PSATS, including the Department of Environmental Protection, Department of Labor and Industry, and the Department of Transportation, for their review and any further action that they deem appropriate.

This report is a public document, which contains both DCED's response to the report and our counterresponse to DCED, and its distribution is not limited. Additional copies can be obtained through the Department of the Auditor General's website, [www.auditorgen.state.pa.us](http://www.auditorgen.state.pa.us).

Sincerely,  
/S/

**JACK WAGNER**  
Auditor General

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## EXECUTIVE SUMMARY

FINDINGS	RECOMMENDATIONS
<p><b><u>FINDING I:</u></b>  DCED employees who were responsible for implementing and administering the training services program, and who were also responsible for evaluating the competitive proposals submitted in 2005 for a new training services contract that was ultimately awarded to PSATS, had accepted meals, hotel lodging, and conference expenses from PSATS in the amount of \$2,716.69, including eleven meals during the time the competitive proposals were being evaluated, in violation of state gift and travel rules and possibly in violation of the Public Official and Employee Ethics Act.</p>	<p>We recommend that DCED:</p> <ul style="list-style-type: none"> <li>• Require employees to arrange to meet with PSATS at a time other than mealtime. If it is necessary for employees to meet over a meal period or to attend the PSATS annual meeting, we recommend that DCED employees follow the Commonwealth’s travel and gift rules and pay for their own expenses and submit the expenses to DCED for reimbursement;</li> <li>• Require employees who must for a legitimate reason attend a meeting at a luxury resort to obtain accommodations elsewhere at a cost within the limits allowable for Commonwealth employees; and</li> <li>• Ensure that employees comply with the Governor’s Code of Conduct, the Commonwealth Travel Procedures Manual, and the Ethics Act.</li> </ul>
<p><b><u>FINDING II:</u></b>  PSATS used a method to bill for reimbursement of the payroll costs for its employees’ time in which all employees in a particular category were billed at the same rate, rather than billing for the actual rate for each employee, resulting in potential overcharges to the Commonwealth. Attempts to verify that the Commonwealth was not being</p>	<p>We recommend that DCED:</p> <ul style="list-style-type: none"> <li>• Require PSATS to produce to DCED’s Comptroller for verification the names of the employees, the payroll records, and the original time-keeping records for all PSATS employees whose time was devoted to the contract. The Comptroller should analyze the records to</li> </ul>

<p>overcharged were thwarted by PSATS' persistent failure or refusal to produce original payroll records -- conduct which supports an inference that it was done purposely to prevent us from determining the magnitude of the overcharges to the Commonwealth resulting from PSATS' method of billing.</p>	<p>determine the actual costs incurred by PSATS in providing the services described in the contract, reconcile such actual costs to invoices submitted by PSATS, and take action to recover any overcharges;</p> <ul style="list-style-type: none"> <li>• Monitor future invoices to ensure that PSATS is not billing the same employee's costs to multiple training programs or to contracts with other agencies;</li> <li>• Amend its contract with PSATS to define with specificity the manner in which an employee's annual salary and fringe benefits may be converted to an hourly rate for the purpose of billing for reimbursement of the costs incurred in providing the services described in the contract; and</li> <li>• Periodically verify the accuracy of the payroll charges being submitted for payment by comparing the invoices to PSATS' actual payroll documents and to PSATS' original time-keeping records.</li> </ul>
<p><b><u>FINDING III:</u></b> DCED permitted PSATS to add surcharges of 9% for "overhead" costs and 8% for "administrative" costs to pass-through billings for goods and services provided by third-party vendors and contractors, resulting in PSATS receiving reimbursement in excess of its actual indirect costs with respect to those billings, in violation of the contract. Our analysis indicates that, for every 100 invoices submitted to the Commonwealth, PSATS would receive approximately \$569,000 of excess compensation solely from the 17%</p>	<p>We recommend that DCED:</p> <ul style="list-style-type: none"> <li>• Recoup from PSATS the 17% surcharge that PSATS applied to services provided by third-party vendors, and</li> <li>• Develop guidelines for allowable costs that address the conditions identified in this report and require that all future contracts entered into by DCED include the guidelines. If DCED is unable or unwilling to develop its own standards, then we</li> </ul>



<p>surcharge on the cost of goods and services provided by third-party vendors and contractors.</p>	<p>recommend that it adopt regulations similar to those developed by the federal government. DCED should ensure that all employees responsible for approving invoices for payment are familiar with the applicable guidelines.</p>
<p><b><u>FINDING IV:</u></b>  PSATS failed to provide an adequate explanation of the composition of the 9% surcharge that it added to all billings to cover “overhead costs” and the 8% surcharge to cover “administrative costs,” making it impossible to determine whether such surcharges were in excess of actual overhead and administrative costs incurred in providing the services described in the contract.</p>	<p>We recommend that DCED:</p> <ul style="list-style-type: none"> <li>• Obtain an understanding of the fees that it was charged and attempt to recoup from PSATS any sums billed that were in excess of actual costs incurred in providing the services described in the contract; and</li> <li>• Draft future Requests for Proposals and contracts to require prospective vendors to document cost factors for administration and overhead in order to preclude the contractor from charging for costs in excess of the actual costs incurred in providing the services under the contract.</li> </ul>
<p><b><u>FINDING V:</u></b>  The now-former Executive Director of PSATS received compensation averaging \$407,608 per year in calendar years 2004 through 2008, which is excessive when compared to others in similar positions and which may be in violation of federal and state laws restricting the use of the net earnings of a nonprofit organization.</p>	<p>We recommend that DCED draft future Requests for Proposals and contracts with nonprofit organizations to require prospective vendors to document the amount of compensation paid to top management employees and certify that the amount is reasonable and in compliance with state and federal law.</p>
<p><b><u>FINDING VI:</u></b>  DCED permitted PSATS to bill for the aggregate costs of all training classes provided in a particular time period, rather than require PSATS to itemize the costs for each individual training class, thereby making it impossible to determine from the</p>	<p>We recommend that DCED:</p> <ul style="list-style-type: none"> <li>• Require PSATS to reformat its invoices to show the costs and the registration fees collected for each individual class, as the contract requires. This could be</li> </ul>

<p>information provided whether PSATS gave proper credit for all registration fees actually collected from attendees of the training classes. With respect to two programs that we analyzed, we found PSATS did not credit the Commonwealth for \$44,594 in registration fees collected.</p>	<p>accomplished by insisting that PSATS submit invoices that conform to the Cost and Price Analysis section of PSATS' response to the RFP;</p> <ul style="list-style-type: none"> <li>• Require PSATS to produce to DCED's Comptroller records of the registration fees collected for each individual class, so that DCED's Comptroller can determine whether proper credit was given for such fees, and take action to recover any overcharges; and</li> <li>• Examine the original records that the contract requires PSATS to keep and maintain in order to verify that the Commonwealth is receiving the proper credit on the invoices PSATS submits for registration fees collected from attendees of the classes.</li> </ul>
<p><b><u>FINDING VII:</u></b> DCED has not established guidelines on eligible costs to be reimbursed under the contract. Consequently, DCED reimbursed PSATS for excessive and unreasonable costs relating to food provided at training seminars, meals from local restaurants, and training at historic inns and resorts. During the fiscal year ended June 30, 2007, the more egregious of these expenses cost the Commonwealth approximately \$20,000.</p>	<p>We recommend that DCED:</p> <ul style="list-style-type: none"> <li>• Review the invoices in detail and obtain an explanation for any questionable or poorly documented expense prior to approving the invoices for payment;</li> <li>• Require PSATS to periodically review the locations where trainings are held to ensure that the costs incurred for facility charges (including meals) is competitive and cost efficient;</li> <li>• Institute measures that define what costs are appropriate to be submitted to the Commonwealth for payment; and</li> <li>• In the absence of creating its own</li> </ul>

	guideline, require PSATS to follow OMB Circular A-122, the federal guideline for nonprofit organizations.
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We are also providing copies of this report to the Pennsylvania Office of Attorney General, State Ethics Commission, Pennsylvania Treasury Department, Pennsylvania Department of Revenue, and the Internal Revenue Service, as well as the other Commonwealth agencies, in addition to DCED, with previous or current contracts with PSATS, including the Department of Environmental Protection, Department of Labor and Industry, and the Department of Transportation, for their review and any further action that they deem appropriate.

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## INTRODUCTION AND BACKGROUND

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The Pennsylvania Department of Community and Economic Development (“DCED”) was created by an act of the General Assembly in 1996 to consolidate the functions of the former Department of Commerce and the former Department of Community Affairs. DCED’s mission is to foster opportunities for businesses and communities to succeed and thrive in a global economy, thereby enabling Pennsylvanians to achieve a superior quality of life. The statute that created DCED transferred to DCED the function of the former Department of Community Affairs to provide, monitor, and coordinate municipal training designed to meet the comprehensive education needs of local government.<sup>1</sup>

The Pennsylvania State Association of Township Supervisors (“PSATS”) is a nonprofit association organized and operating under Section 501(c)(4) of the Internal Revenue Code. It was originally formed in 1921 pursuant to the authorization of an act of the General Assembly that is the predecessor of Section 1402(a) of the Second Class Township Code.<sup>2</sup> Among its purposes and powers are the following:

- to “hold annual meetings . . . to discuss questions and subjects pertaining to the duties of elected and appointed township officials and the improvement of township government;”<sup>3</sup> and
- to “adopt and amend bylaws” to “govern the qualification of delegates, election of officers, their designation, qualifications and duties, payment of dues and other organizational matters” and to “function under the bylaws to advance the interest of township government.”<sup>4</sup>

The statute expressly authorizes townships to appropriate money to pay dues to PSATS and to pay the expenses of sending officials to attend PSATS meetings. At the present time, more than 1,450 townships in the Commonwealth, represented by over 10,000 elected officials, are members of PSATS.<sup>5</sup> PSATS is governed by a 13-member Board of Directors elected from its member townships, and is headquartered in a 24,000-square foot building<sup>6</sup> in Hampden Township, Cumberland County.

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<sup>1</sup> Act of June 27, 1996, P.L. 403, No. 58, § 301(a)(3) (The Community and Economic Development Enhancement Act).

<sup>2</sup> Act of May 1, 1933, P.L. 103, No. 69, § 1402(a), as amended, 53 P.S. § 66402(a) (The Second Class Township Code). This act incorporated the provisions of the Act of May 5, 1921, P.L. 397, No. 189, §§ 1 to 3, as amended, which was the first state law authorizing the formation of a State Association of Township Supervisors.

<sup>3</sup> 53 P.S. § 66402(b).

<sup>4</sup> *Id.* § 66402(c).

<sup>5</sup> PSATS, “Mission and Background,” [www.psats.org/about\\_mission.html](http://www.psats.org/about_mission.html), last accessed on Nov. 1, 2010.

<sup>6</sup> This does not include the recent addition of classroom space estimated to be an additional 10,000 to 15,000 square feet.

In 1996, DCED's Center for Local Governments, pursuant to its mandate to provide training to local governments, awarded a contract to PSATS to provide training programs for local government officials. According to a DCED official, the Local Government Training Program is designed to provide affordable training opportunities to local government officials in a full range of disciplines, including municipal finance, administration, tax collection, police, fire, public works, land use planning, code enforcement, and environmental issues. PSATS provided training services under that contract and subsequent renewals and extensions from 1996 until 2005.

In 2005, in anticipation of the expiration of its contract with PSATS, DCED issued a request for proposals ("RFP") for a new contract to provide training services. PSATS was one of two entities that responded to the RFP. Based upon DCED's evaluation of the competing proposals, the contract, No. 4000008729, was awarded to PSATS in late 2005, with an effective date of January 1, 2006.

At the time that this contract was executed, the Commonwealth allocated \$3.9 million over the term of the contract – a five-and-a-half-year period (January 2006-June 2011) – for services to be provided under this contract. However, within the first 14 months of the contract, DCED amended the contract on three occasions expanding the scope of work to be provided and increasing total contract amount to \$5.6 million.<sup>7</sup> The amendments resulted, in part, from other Commonwealth agencies and other offices within DCED "piggy-backing" on the contract through Memoranda of Understanding<sup>8</sup> with DCED or Service Purchase Contracts<sup>9</sup> routed through DCED. The amendments expanded the training services to be provided by PSATS to include:

- Pennsylvania Department of Environmental Protection ("DEP"), Sewage Enforcement Officers program;
- DEP, Pennsylvania Brownfields 2006 conference;
- Pennsylvania Department of Labor and Industry, PennSERVE program;
- Pennsylvania Department of Transportation ("PennDOT") in various subject areas specified by PennDOT;
- DCED, Office of Community Development, in subject areas to be specified by the Office of Community Development; and
- DCED, Center for Local Governments, Floodplain Management Program.

A key feature of this contract, which is especially pertinent to this investigation, is that the contract only permits PSATS to be reimbursed for its *actual costs* incurred in providing the training services. The contract provides, in pertinent part:

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<sup>7</sup> As of September 13, 2010, the 2006-2011 contract has been amended a total of 14 times, and the total contract amount has been increased to \$12,062,104, an average of over \$2.4 million per year.

<sup>8</sup> A Memorandum of Understanding is an interagency agreement as defined under the Commonwealth Attorneys Act, which allows cooperative arrangements between executive agencies. Sections 501 and 502 of the Administrative Code of 1929, as amended (71 P.S. §§ 181 and 182), require Commonwealth departments and agencies to coordinate their work and activities with other Commonwealth departments and agencies.

<sup>9</sup> A Service Purchase Contract is a standard form contract used by agencies of the Commonwealth to procure services from approved outside vendors.

The Consultant [PSATS] may be *reimbursed for the costs incurred* in providing the services described in this Contract up to the total amount available under this Contract. *All such costs*, including services contributed by the Consultant or others and charged to the project account, *shall be supported by properly executed vouchers or other records indicating in proper detail the nature and propriety of the charge.*<sup>10</sup>

In March 2007, the Department of the Auditor General (“Department”) received an allegation from a confidential informant that PSATS was overcharging DCED for the training services that it was providing under the contract by using several techniques to either overstate its costs or otherwise manipulate the factors in the formula that determines the compensation it was to receive.

The allegations were assigned to this Department’s Office of Special Investigations (“OSI”) for investigation. OSI’s investigation included interviews of DCED’s management personnel, program employees, and chief counsel. Several staff employees of PSATS were also interviewed, including the Executive Director.<sup>11</sup> However, the scope of the interviews was limited, because the presence of PSATS’ legal counsel in many of the interviews may have inhibited the employees from speaking freely. We also contacted the current and former auditors hired by PSATS and were provided limited access to the auditors’ electronic work papers.

We also reviewed documents submitted to DCED by PSATS as part of the normal billing procedure, such as invoices and supporting documentation. However, in order to verify the personnel costs billed under the contract, we needed information that only PSATS could provide. Our requests for payroll data for every employee being billed to Commonwealth contracts went unanswered for extended periods of time. When the data was finally provided to us, we were unable to use it to verify personnel costs charged under the DCED contract, because several weaknesses and deficiencies were found in the data and because PSATS, despite our requests, did not provide *original* supporting documentation. Consequently, we were unable to determine with precision the monetary effect of the problems identified with payroll.

For financial data, we relied on the Internal Revenue Service Form 990 (“Return of Organization Exempt from Income Tax”) filed by PSATS for the years 2006 through 2008, and on PSATS’ audited financial statements for 2005. These data are summarized in Table 1.

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<sup>10</sup> Contract, Article V, Section 2(b) (emphasis added).

<sup>11</sup> The executive director of PSATS during the time period covered by this report retired from PSATS effective December 31, 2009, and a new executive director assumed the position effective January 1, 2010. Throughout this report, the term “Executive Director” refers only to the now-former executive director who retired effective December 31, 2009.

**Table 1**  
**PSATS' Revenue from Government Grants and Contracts,**  
**Calendar Years 2005-2008**

<b>Calendar Year</b>	<b>Revenue from Government Sources</b>	<b>Total Revenue</b>	<b>Percentage of Total Revenue from Government Sources</b>
2005	\$ 3,595,222	\$ 7,049,686	51 %
2006	\$ 4,625,609	\$ 8,785,838	53 %
2007	\$ 6,179,502	\$10,074,603	61 %
2008*	\$ 4,212,098	\$ 8,173,403	52 %
<b>TOTALS</b>	<b>\$18,612,431</b>	<b>\$34,083,530</b>	<b>54.6%</b>

*\*The period under investigation was 2005-2007. The financial data for 2008 has recently been published and is the most current financial data publicly available.*

The financial information set forth in Table 1 shows that government grants and contracts provided more than half of PSATS' income in each of the years 2005 through 2008 and 54.6% of PSATS' income for the four-year period as a whole.

While PSATS was generally responsive to our requests for information other than payroll, we must note that, throughout our investigation, PSATS persistently failed to produce, or significantly delayed access to, the original time-keeping records that must be examined to verify that PSATS' charges to DCED were in accordance with the terms and conditions of the contract. While feigning cooperation, PSATS actually provided only incomplete, incorrect, or unsupported payroll information. As a result, we were unable to verify that PSATS did not overbill for the services of its employees under the contract.

Because the records that we requested could have confirmed that PSATS was properly billing only for reimbursement of its actual payroll costs, we are constrained to draw an adverse inference from PSATS' persistent failure or refusal to provide all of the original records requested and complete and accurate information on a timely basis. Accordingly, we conclude that it was done purposely by PSATS to impede or prevent our investigation from uncovering problems with PSATS' billings to the Commonwealth and, more particularly, to prevent us from determining the magnitude of the overcharges resulting from the system that PSATS used for billing payroll costs.

Our investigation resulted in the seven findings presented in this report. According to DCED, as of September 2010, PSATS is still utilizing the same method to invoice the Commonwealth as it did during our investigation. We urge DCED to implement all of our recommendations, and we urge other Commonwealth agencies to consider the findings and recommendations in this report with regard to their contacts with PSATS. The Department of the Auditor General will follow-up at the appropriate time to determine whether our recommendations have been implemented.

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## FINDINGS AND RECOMMENDATIONS

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**FINDING I:** DCED employees who were responsible for implementing and administering the training services program, and who were also responsible for evaluating the competitive proposals submitted in 2005 for a new training services contract that was ultimately awarded to PSATS, had accepted meals, hotel lodging, and conference expenses from PSATS in the amount of \$2,716.69, including eleven meals during the time the competitive proposals were being evaluated, in violation of state gift and travel rules and possibly in violation of the Public Official and Employee Ethics Act.

PSATS provided OSI with a list of expenses that it paid on behalf of Commonwealth employees between January 13, 2005, and October 30, 2007. Our review of these expenses, which is summarized in Table 2, found that, between 2004 and 2006, PSATS paid for meals and conference expenses totaling \$2,716.69 for five of the six DCED employees who were responsible for evaluating and selecting the winning proposal for a new contract to provide training services in December 2005. Eleven of the meals, costing \$121.60, were during the period when the proposals were being evaluated and the contract was being negotiated, including a lunch on the same day that PSATS submitted its proposal.

**Table 2**  
***Meals and Expenses Provided to DCED Employees by PSATS,  
 Calendar Years 2004-2006***

	Evaluator 1	Evaluator 2	Evaluator 3	Evaluator 4	Evaluator 5	Total
Meals provided during proposal review period	\$ 8.50	\$ 13.00	\$ 8.60	\$ 48.30	\$ 43.20	\$ 121.60
Meals provided at times other than proposal review period	25.00	89.40	44.70	206.50	99.20	464.80
Conference Expenses	0	0	0	704.20	1,426.09	\$2,130.29
<b>TOTALS</b>	<b>\$ 33.50</b>	<b>\$102.40</b>	<b>\$53.30</b>	<b>\$ 959.00</b>	<b>\$1,568.49</b>	<b>\$ 2,716.69</b>

*Source: Information provided by PSATS and by Nemaquin Woodlands Resort.*



Commonwealth employees who were directly responsible for administering the contract attended the three-day PSATS annual board meetings at Nemacolin Woodlands Resort (“Nemacolin”) in Fayette County.<sup>12</sup> The expenses of \$2,130 incurred by these individuals for attending the board meetings were included in the total meeting expenses, approximately \$189,366, billed to and paid by PSATS.

We interviewed the DCED Project Coordinator for the contract, and she stated that she attended this meeting three times – in 2006, in 2004, and one other time prior to 2004 – and that she attended at the request of her supervisor to provide a briefing on the training program and on one occasion to talk about the DCED website. Records provided by Nemacolin confirm a two-night stay in both 2004 and 2006 and that the expenses were billed to PSATS.

The DCED Project Manager for the contract also attended the 2004 meeting, and records from Nemacolin confirm that his expenses for a two-night stay were paid by PSATS. Neither the Project Coordinator nor the Project Manager submitted requests for reimbursement of travel expenses to DCED related to these trips. Both employees told OSI that their trips to the luxury resort were approved by DCED management.

The DCED Supervisor told OSI that he recalls that the employees attended training in 2006. He stated that travel expenses should have been submitted through DCED if the employees stayed overnight. He also stated that he was unaware of PSATS paying for their stay. He does not recall who attended in 2004.

### **Laws and Policies that Prohibit Activities by Commonwealth Employees**

Section 1103 of The Public Official and Employees Ethics Act (“Ethics Act”), titled “Restricted Activities,”<sup>13</sup> provides, in pertinent part:

- (a) No public official or public employee shall engage in conduct that constitutes a conflict of interest.<sup>14</sup>

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<sup>12</sup> For calendar years 2004 through 2006, PSATS incurred at least \$189,366 in expenses related to these annual trips, which included meeting rooms, room charges, food and beverage costs (including alcohol), wine tastings, and fees for the golf course, shooting range, and horse stables.

<sup>13</sup> Act of October 15, 1998, P.L. 729, No. 93, § 1103, as amended, 65 Pa.C.S. § 1103.

<sup>14</sup> “Conflict” or “Conflict of interest” is defined in Section 1102 of the act as follows:

Use by a public official or public employee of the authority of his office or employment or any confidential information received through his holding public office or employment for the private pecuniary benefit of himself, a member of his immediate family, or a business with which he or a member of his immediate family is associated. The term does not include an action having a de minimis economic impact or which affects to the same degree a class consisting of the general public or a subclass consisting of an industry, occupation, or other group which includes the public official or public employee, a member of his immediate family or a business with which he or a member of his immediate family is associated.

\* \* \*

- (c) No public official, public employee or nominee or candidate for public office shall solicit or accept anything of monetary value including a gift, loan, political contribution, reward, or promise of future employment based on any understanding that public official, public employee or nominee that that the vote, official action, or judgment of the public office would be influenced thereby.

In addition, the *Governor's Code of Conduct*<sup>15</sup> provides, in pertinent part:

**§ 7.153. Gifts and favors.**

- (a) No employe[e], appointee or official in the Executive Branch of the Commonwealth may solicit or accept for the personal use of himself or another, a gift, gratuity, favor, entertainment, loan or other thing of monetary value from a person who:

- (1) Is seeking to obtain business from or has financial relations with the Commonwealth.

- (2) Conducts operations or activities that are regulated by the Commonwealth.

\* \* \*

- (4) Has interests that may be substantially affected by the performance or nonperformance of the official duty of the employe[e].

- (b) The only exceptions are limited to the following instances:

\* \* \*

- (5) Receipts of bona fide reimbursement for actual expenses for travel and such other necessary subsistence as is compatible with other restrictions set forth in this part and for which no Commonwealth payment or reimbursement is made. *However, an employe[e] may not be reimbursed , and payment may not made on his behalf, for excessive personal living expenses, gifts, entertainment or other personal benefits nor may an employe[e] be reimbursed by a person for travel on official business under Commonwealth orders. [emphasis added]*

Finally, Management Directive 230.10 Amended, *Travel and Subsistence Allowances*,<sup>16</sup> provides, in pertinent part:

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<sup>15</sup> *Code of Conduct for Appointed Officials and State Employees*, 1 Pa. Code Subchapter K, §§ 7.151 through 7.159 (“RESTRICTED ACTIVITIES: CONFLICTS OF INTEREST”).

\* \* \*

03.i All persons who incur expenses while traveling on official Commonwealth Business are to be reimbursed in accordance with this directive. To preclude the possibility of financial benefit, expense reimbursements received from any other source such as the federal government, a private business, an individual or other third party shall be remitted to BCPO [Bureau of Commonwealth Payroll Operations] immediately upon receipt. Checks received are not to be cashed but must be endorsed payable to the Commonwealth of Pennsylvania.<sup>17</sup>

\* \* \*

### **11.e(2) Luncheon or Dinner Meetings**

\* \* \*

Employees on official business attending luncheon or dinner meetings not sponsored by the Commonwealth are entitled to receive reimbursement for actual costs incurred. . . . Luncheon or dinner meetings must meet the following criteria:

- The luncheon or dinner meeting is planned in advance, must include persons who are not employed by the Commonwealth, and must be approved by an agency head or designated deputy agency head.
- The meal must be an integral part of the meeting.
- The meal must be served at the same establishment that hosts the meeting.
- The purpose of the meeting must be to discuss business and the nature of the business must be stated on the [travel expense report].

### **Conclusions and Recommendations:**

Our investigation found that several DCED employees who were responsible for implementing and administering the DCED training services program, and who were also responsible for evaluating the competitive proposals submitted in 2005 for the new training services contract that was ultimately awarded to PSATS, had accepted meals, hotel lodging, and conference expenses from PSATS in the amount of \$2,716.69, including eleven meals costing \$121.60 during the time the competitive proposals were being evaluated. This conduct is in violation of the Governor's Code of Conduct and the

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<sup>16</sup> Governor's Office, Management Directive 230.10 Amended, *Travel and Subsistence Allowances*, dated December 28, 2005; Governor's Office, Management Directive 230.10 Amended, *Travel and Subsistence Allowances*, dated February 15, 2007.

<sup>17</sup> PSATS paid the expenses incurred by the DCED employees attending PSATS' annual conference directly to the vendor. It did not send reimbursement checks to the employees.

Commonwealth Travel Procedures Manual and may also be in violation of the Ethics Act.

While DCED employees who are responsible for administering DCED's training program may need to meet with PSATS employees, and may even need to attend PSATS' annual board retreat, it is not appropriate for PSATS to pay for the related expenses. Government employees must maintain objectivity and independence in their duties, both in appearance and in reality. Accepting meals and stays at luxury resorts at the expense of a vendor compromises that objectivity and independence and prevents the government employees from discharging their duties without bias towards a particular vendor.

We recommend that DCED:

- Require employees to arrange to meet with PSATS at a time other than mealtime. If it is necessary for employees to meet over a meal period or to attend the PSATS annual meeting, we recommend that DCED employees follow the Commonwealth's travel and gift rules and pay for their own expenses and submit the expenses to DCED for reimbursement;
- Require employees who must for a legitimate reason attend a meeting at a luxury resort to obtain accommodations elsewhere at a cost within the limits allowable for Commonwealth employees; and
- Ensure that employees comply with the Governor's Code of Conduct, the Commonwealth Travel Procedures Manual, and the Ethics Act.

We are also referring this report to the State Ethics Commission and the other Commonwealth agencies, in addition to DCED, with previous or current contracts with PSATS, including the Department of Environmental Protection, Department of Labor and Industry, and the Department of Transportation, for their review and whatever further action they may deem appropriate.

**FINDING II: PSATS used a method to bill for reimbursement of the payroll costs for its employees' time in which all employees in a particular category were billed at the same rate, rather than billing for the actual rate for each employee, resulting in potential overcharges to the Commonwealth. Attempts to verify that the Commonwealth was not being overcharged were thwarted by PSATS' persistent failure or refusal to produce original payroll records -- conduct which supports an inference that it was done purposely to prevent us from determining the magnitude of the overcharges to the Commonwealth resulting from PSATS' method of billing.**

OSI received an allegation that PSATS was overbilling DCED for training services provided under the DCED contract by charging more than actual payroll costs incurred. To test this allegation, we attempted to reconcile the payroll records of PSATS to the invoices PSATS submitted to DCED for the fiscal year ended June 30, 2007.

In response to our request for payroll information, PSATS provided a chart that we have reproduced as Table 4. The underlying information, which is set forth in Table 5, shows that, due to its method for billing for reimbursement of its payroll costs, PSATS could have overbilled DCED for payroll costs by as much as \$89,632 in the fiscal year ended June 30, 2007.

Our attempt to verify whether or not PSATS actually overbilled its payroll costs was thwarted because of numerous weaknesses and deficiencies in the information provided by PSATS and by DCED. The weaknesses and deficiencies included the fact that DCED failed to require PSATS to produce detailed information about its payroll, the fact that PSATS failed to retain its original time-keeping records, and the fact that PSATS contended that the method it selected for billing hourly rates is solely within its own discretion.

The following is a more detailed summary of the relevant facts and the sequence of events.

The pertinent provision of the contract is as follows:

The Consultant [PSATS] may be *reimbursed for the costs incurred* in providing the services described in this Contract up to the total amount available under this Contract. *All such costs*, including services contributed by the Consultant or others and charged to the project account, *shall be supported by properly executed vouchers*

*or other records indicating in proper detail the nature and propriety of the charge.*<sup>18</sup>

Under a plain-meaning interpretation of this provision, compliance would entail the use of time-keeping records routinely kept by organizations to prepare payroll. However, PSATS did not bill actual payroll rates for its employees. Rather, PSATS explained that it assigned its employees to various categories in a classification system and billed DCED a single rate for all employees in a particular category. As a result, DCED was not being billed for reimbursement of the actual payroll costs incurred by PSATS for each of its employees who devoted time to the contract.

PSATS contended that its method was permissible under the terms of the contract. We do not agree with such an interpretation of the contract. Moreover, PSATS' failure to retain its original time-keeping records not only made it impossible to verify the employee hours devoted to the contract, but also made it impossible to determine the variance, if any, between actual payroll costs and payroll costs billed pursuant to PSATS' method of billing the same rate for all employees in a particular category.

The invoices that PSATS submitted to DCED consisted of a cover page, on which the expenses were summarized by cost categories,<sup>19</sup> and documentation to support each cost category. We have reproduced in Table 3 an excerpt of an invoice submitted to DCED in February 2007 for an "Auditors" training course. The supporting documentation, titled "DCED General Contract Totals Summary," lists the service or type of work provided ("Administrative," "Fiscal," and "Production"), the rate per hour, the hours worked, and the amount charged for each PSATS employee. The following analysis focuses on the "Administrative" category, but the weakness and deficiencies apply generally to all categories.

**Table 3**  
*Excerpt of PSATS' Documentation Supporting  
Invoice for Reimbursement of Costs Incurred under the Contract*

**DCED General Contract Totals Summary**  
*For Month Ended February 2007*

<i>Course Name</i>	<i>Work Type</i>	<i>Rate/Hour</i>	<i>Hours</i>	<i>Amount</i>
<i>Auditors</i>				
	Administrative	\$32.50	0.75	\$24.38
	Fiscal	\$48.25	0.50	\$24.13
	Production	\$40.00	2.50	\$100.00
	<i>Totals for Auditors</i>		3.75	\$148.51

<sup>18</sup> Contract, Article V, Section 2(b) (emphasis added).

<sup>19</sup> The cost categories, which were set forth in the proposal submitted by PSATS in response to the RFP, were "Faculty," "Travel," "Facility," "Production," "Administration," and "Fees."

We found the following weaknesses and deficiencies based on information that PSATS and DCED provided:

1. The invoices that PSATS submitted to DCED do not include the names of the individual PSATS employees who worked on the training program. Instead, as illustrated in Table 3, PSATS identified the individuals only by category or job function, such as “Administrative,” “Fiscal,” and “Production.”

DCED should have required PSATS to bill the Commonwealth for actual personnel costs by employee, as the contract requires. This would have provided DCED with information that could be substantiated with verifiable supporting documentation, such as employee payroll rate information and time-keeping records. This weakness created the opportunity for PSATS to overbill payroll rates and hours and to double-bill different training programs or different contracts for the same employees’ time.

2. PSATS overstated the actual hourly rates for many of its employees who worked on the contract.

PSATS initially told us that its employees work 35 hours per week, which, by our calculations, must equate to 1,820 hours available to work per year.<sup>20</sup> However, PSATS also told us that it uses 1,550 hours per year to convert annual salaries to an hourly payroll rate. This has the effect of increasing the hourly rates charged to the Commonwealth. For example, an Administrative employee earning \$28,275 annually would have an hourly rate of \$15.53 using 1,820 hours per year, as opposed to an hourly rate of \$18.24 using 1,550 hours per year, or \$2.71 more per hour.

When asked to explain why it used 1,550 hours per year rather than 1,820 hours, PSATS replied through its attorney that an employee who works 100% on the contract is billed using the 1,820 hours per year factor, but that an employee who is not fully assigned to the contract is billed using the 1,550 hours per year factor due to a “partial loss of efficiency and productivity.”

Although this explanation serves to reconcile to some degree the apparent discrepancies in the hourly rates charged by PSATS, it offers no reassurance that PSATS is being reimbursed only for its actual costs. The hourly rate for an employee should be the same regardless of whether the employee works full time on the contract. Any incidental “loss of efficiency and productivity” by employees working less than full time on the contract should be covered by the 17% surcharge that PSATS added to

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<sup>20</sup> 52 weeks per year x 35 hours per week = 1,820 hours per year.

its invoices for “administrative and overhead fees,” as discussed in Finding III.<sup>21</sup>

3. PSATS failed or refused to provide original time-keeping records to establish the hours that each of its employees worked on all Commonwealth contracts.<sup>22</sup>

PSATS’ Assistant Director of Management Services initially told us that employees’ time is recorded on a Microsoft Access database, a fact that was confirmed by a sample document that PSATS provided. However, when we asked PSATS to produce the time records in their original form (i.e., the Microsoft Access database) for all employees with time charged to any Commonwealth contract, we were informed through PSATS’ attorney that the “initial time-keeping records are not retained.” Instead, PSATS provided us with an Excel spreadsheet showing a summary of its employees’ time that was billed to the Commonwealth. It was further explained that a PSATS employee entered the data from the Microsoft Access database into the Excel spreadsheet to calculate the hours to be billed to the Commonwealth.

PSATS’ failure to retain the original time-keeping records is not only a departure from fundamental bookkeeping practices, but is also a violation of the Audit Provisions section of the contract, which provides, in pertinent part:<sup>23</sup>

- The Consultant agrees to maintain records which will support the prices charged and costs incurred for this Contract.
- The Consultant shall preserve books, documents, and records that relate to costs or pricing data for the Contract for a period of three (3) years from date of final payment.

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<sup>21</sup> We would also point out that calculating the hourly billing rate based on 1,550 hours per year would result in an overcharge to Commonwealth for any employee who works more than 1,550 hours on the contract in any actual year. To illustrate, if an Administrative employee who earns \$28,275 per year actually works 1,600 hours on the contract in one year, and PSATS bills the Commonwealth \$18.24 per hour (based on 1,550 hours per year), PSATS would receive \$29,184, or \$908 more than the annual salary it actually pays to the employee. Based on information supplied by PSATS, the Commonwealth was billed for six employees who logged more than 1,550 hours in 2006, and for four employees who logged more than 1,550 hours in 2007.

<sup>22</sup> Because PSATS has multiple contracts with different Commonwealth agencies, one of our objectives was to confirm that no employee’s time was double-billed, i.e., that the same employee’s time was not billed to more than one agency. To verify this, we requested payroll registers and time and attendance records for all employees whose time was billed to *any* Commonwealth contract, not just the DCED contract. However, we were unable to complete this objective because PSATS did not retain the original time-keeping records for its employees.

<sup>23</sup> Contract, Article IX, Audit Provisions.



- The Consultant shall give full and free access to all records to the Commonwealth and/or their authorized representatives.

The invoices submitted to DCED for reimbursement of payroll costs incurred by PSATS in providing the services described in the contract cannot be verified without access to the original records showing the actual hours worked by each employee. An Excel spreadsheet is not an original record and is not an acceptable substitute.

4. PSATS billed for its employees' time by job category, not by each employee's actual hourly rates, resulting in overcharges and undercharges to the Commonwealth.

PSATS' Assistant Director of Management Services explained:

- PSATS does not bill DCED based on each employee's actual salary or wage rate.
- PSATS classifies its employees into a number of categories and bills DCED a single rate for all employees in a particular category.
- PSATS has billed DCED using this categorical method since 1996, when PSATS was first awarded the training contract.
- The billing rate for a category is based on the salary range of the employees in that particular category.

Table 4 is a reproduction of a table supplied by PSATS (with employees' names deleted) to illustrate how PSATS established the hourly rate for each employee who worked on the contract.

**Table 4**  
***PSATS Hourly Rate Comparison to Contract Rate,  
Fiscal Year Ended June 30, 2007***

<b>Employee Classification</b>	<b>2006 Salary</b>	<b>No. of Hours</b>	<b>Hourly Rate w/o Benefits</b>	<b>Benefits (42%)</b>	<b>Hourly Rate w/ Benefits</b>	<b>Contract Rate</b>
<b>SEO Program Manager*</b>	44,300	1,050	42.19	17.72	59.91	\$63.50
<b>PennDOT Development</b>	48,000	1,550	30.97	13.01	43.97	\$40.00
<b>Program Manager</b>	44,000	1,550	28.39	11.92	40.31	\$40.00
<b>Program Manager</b>	48,250	1,550	31.13	13.07	44.20	\$40.00
<b>Program Manager</b>	37,000	1,550	23.87	10.03	33.90	\$40.00
<b>Program Manager</b>	40,000	1,550	25.81	10.84	36.65	\$40.00
<b>Production-SEO</b>	41,000	1,550	26.45	11.11	37.56	\$36.50

<b>Employee Classification</b>	<b>2006 Salary</b>	<b>No. of Hours</b>	<b>Hourly Rate w/o Benefits</b>	<b>Benefits (42%)</b>	<b>Hourly Rate w/ Benefits</b>	<b>Contract Rate</b>
<b>Curriculum Dev. Manager</b>	45,000	1,550	29.03	12.19	41.23	\$40.50
<b>PCCA Training Specialist*</b>	42,000	1,550	27.10	11.38	38.48	\$38.50
<b>PCCA Administrative Assistant</b>	27,000	1,550	17.42	7.32	24.74	\$27.50
<b>Administrative #1</b>	22,000	1,550	14.19	5.96	20.15	\$32.50
<b>Administrative #2</b>	28,000	1,550	18.06	7.59	25.65	\$32.50
<b>Administrative #3</b>	24,500	1,550	15.81	6.64	22.45	\$32.50
<b>Administrative #4</b>	27,250	1,550	17.58	7.38	24.96	\$32.50
<b>Administrative #5</b>	28,500	1,550	18.39	7.72	26.11	\$32.50
<b>Administrative #6</b>	28,000	1,550	18.06	7.59	25.65	\$32.50
<b>Administrative #7</b>	36,000	1,550	23.23	9.75	32.98	\$32.50
<b>Administrative #8</b>	28,275	1,550	18.24	7.66	25.90	\$32.50
<b>Administrative #9</b>	34,750	1,550	22.42	9.42	31.84	\$32.50
<b>Administrative #10</b>	30,250	1,550	19.52	8.20	27.71	\$32.50
<b>Administrative #11</b>	27,000	1,550	17.42	7.32	24.74	\$32.50
<b>Fiscal</b>	78,000	1,550	50.32	21.14	71.46	\$48.25
<b>Fiscal</b>	53,000	1,550	34.19	14.36	48.55	\$48.25
<b>Fiscal</b>	47,500	1,550	30.65	12.87	43.52	\$48.25
<b>Fiscal</b>	32,000	1,550	20.65	8.67	29.32	\$48.25
<b>Technical Support</b>	52,750	1,550	34.03	14.29	48.33	\$58.00
<b>Technical Support</b>	74,300	1,550	47.94	20.13	68.07	\$58.00
<b>PSATS Management</b>						\$95.25
<b>Contract Management</b>	88,000	1,550	56.77	23.85	80.62	\$80.00
<b>Training Course Developer</b>	27,000	480	56.25	-	56.25	\$55.00
<b>Development Senior Advisor</b>	32,750	619	52.91	-	52.91	\$51.50
<b>Development Senior Advisor</b>	55,000	1,092	50.37	21.15	71.52	\$51.50
<b>Mailing Staff</b>						\$24.75

\*SEO is Sewage Enforcement Officer; PCCA is Pennsylvania Construction Codes Academy.

To illustrate PSATS' explanation of its method of billing by job category, Table 4 shows that the hourly rate with benefits for all eleven employees categorized as "Administrative" is \$32.50 per hour. However, the actual payroll cost for these eleven employees ranges from \$20.15 per hour to \$32.98 per hour (an average rate of \$26.19 per hour), and ten of the eleven employees had actual hourly rates below the rate assigned to the category.

5. Table 4, which was provided to us by PSATS, contains the following weaknesses:
  - The table lists estimated salaries rather than actual salaries. Based on actual salary data subsequently provided, the salaries in the table are incorrect.
  - Of the eleven Administrative employees listed in the table with a 2006 salary, three employees (#2, #3, and #6) were not hired until 2007.
  - The table does not include all PSATS employees billed to the DCED contract. For example, the table does not include two part-time PSATS employees who were billed by PSATS at a flat rate of \$7,000 each (totaling \$14,000) per month.
  - Based on the contract, the PSATS Management employee listed at a contract rate of \$95.25 (the Executive Director) is "in kind" and therefore should not have been billed and should not be included in the table.<sup>24</sup>
  - PSATS used calendar year salaries and compared it to the fiscal year billing rate.
  - Four employees' "No. of Hours" used to determine the hourly rate are less than the 1,550 hours.
6. Our calculation of the potential effect of PSATS billing the Commonwealth by job category rather than actual hourly rates is set forth in Table 5, which illustrates that PSATS may have overbilled the Commonwealth by as much as \$89,632 in the fiscal year ended June 30, 2007. The inconsistencies in the data provided by PSATS and the lack of original time-keeping records prevented us from calculating the effect with greater accuracy.

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<sup>24</sup> The PSATS contract's cost proposal specifies that "certain PSATS senior staff . . . will be offered in-kind and without expense to the Center."

**Table 5**  
**Potential Overcharges Due to PSATS' Billing Methods,**  
**Fiscal Year Ended June 30, 2007**

<b>Employee Classification</b>	<b>Hourly Rate w/ Benefits</b>	<b>Contract Rate</b>	<b>Over (Under) Charge per hour</b>	<b>Potential Over/Under Charge</b>
<b>SEO Program Manager</b>	59.91	\$63.50	3.59	\$ 3,769.50
<b>PennDOT Development</b>	43.97	\$40.00	(3.97)	\$ (6,153.50)
<b>Program Manager</b>	40.31	\$40.00	(0.31)	\$ (480.50)
<b>Program Manager</b>	44.20	\$40.00	(4.20)	\$ (6,510.00)
<b>Program Manager</b>	33.90	\$40.00	6.10	\$ 9,455.00
<b>Program Manager</b>	36.65	\$40.00	3.35	\$ 5,192.50
<b>Production – SEO</b>	37.56	\$36.50	(1.06)	\$ (1,643.00)
<b>Curriculum Dev. Manager</b>	41.23	\$40.50	(0.73)	\$ (1,131.50)
<b>PCCA Training Specialist</b>	38.48	\$38.50	0.02	\$ 31.00
<b>PCCA Administrative Assistant</b>	24.74	\$27.50	2.76	\$ 4,278.00
<b>Administrative #1</b>	20.15	\$32.50	12.35	\$ 19,142.50
<b>Administrative #2</b>	25.65	\$32.50	6.85	\$ 10,617.50
<b>Administrative #3</b>	22.45	\$32.50	10.05	\$ 15,577.50
<b>Administrative #4</b>	24.96	\$32.50	7.54	\$ 11,687.00
<b>Administrative #5</b>	26.11	\$32.50	6.39	\$ 9,904.50
<b>Administrative #6</b>	25.65	\$32.50	6.85	\$ 10,617.50
<b>Administrative #7</b>	32.98	\$32.50	(0.48)	\$ (744.00)
<b>Administrative #8</b>	25.90	\$32.50	6.60	\$ 10,230.00
<b>Administrative #9</b>	31.84	\$32.50	.66	\$ 1,023.00
<b>Administrative #10</b>	27.71	\$32.50	4.79	\$ 7,424.50
<b>Administrative #11</b>	24.74	\$32.50	7.76	\$ 12,028.00
<b>Fiscal</b>	71.46	\$48.25	(23.21)	\$ (35,975.50)
<b>Fiscal</b>	48.55	\$48.25	(0.30)	\$ (465.00)

<b>Employee Classification</b>	<b>Hourly Rate w/ Benefits</b>	<b>Contract Rate</b>	<b>Over (Under) Charge per hour.</b>	<b>Potential Over/Under Charge</b>
<b>Fiscal</b>	43.52	\$48.25	4.73	\$ 7,331.50
<b>Fiscal</b>	29.32	\$48.25	18.93	\$ 29,341.50
<b>Technical Support</b>	48.33	\$58.00	9.67	\$ 14,988.50
<b>Technical Support</b>	68.07	\$58.00	(10.07)	\$ (15,608.50)
<b>PSATS Management</b>		\$95.25		
<b>Contract Management</b>	80.62	\$80.00	(0.62)	\$ (961.00)
<b>Training Course Developer</b>	56.25	\$55.00	(1.25)	\$ (600.00)
<b>Development – Senior Advisor</b>	52.91	\$51.50	(1.41)	\$ (872.79)
<b>Development – Senior Advisor</b>	71.52	\$51.50	(20.02)	\$ (21,861.84)
<b>Mailing Staff</b>		\$24.75		
<b>Net Overcharge</b>				<b>\$89,632.37</b>

When asked to explain the apparent discrepancies produced by the “Contract Rates,” PSATS replied through its attorney as follows:

The contract does not specify the manner in which PSATS shall calculate the hourly rates it charges for the labor of PSATS personnel engaged in performing the contract. The contract does not identify or direct any specific correlation between the PSATS salaries of the employees involved and the hourly rates charged for their time in performing the contract, nor does it provide any guidelines or requirement for the calculation of hourly rates. Accordingly, the development of hourly rates for purposes of contract billings and the utilization of individuals’ annual salaries as a factor in developing such hourly rates is a matter wholly internal to PSATS and solely within its decisional province.

**Conclusions and Recommendations:**

Despite the contract provision that PSATS was only to be “reimbursed for the costs incurred in providing the services described in this Contract,” rather than charging actual payroll costs, PSATS assigned each of its employees to a category based on job classification and charged a single hourly rate for all employees in a particular category. Our analysis of the available data, which is summarized in Table 5, demonstrates that the potential overcharges to the Commonwealth could have been as much as \$89,632 in the fiscal year ended June 30, 2007.

Although the contract clearly permits only reimbursement for actual costs incurred in providing the services described in the contract, DCED was lax in the drafting of the RFP and in the drafting of the contract with PSATS by failing to define with specificity the manner in which an employee's compensation and fringe benefits may be converted to an hourly rate for billing purposes. PSATS took advantage of the lack of specificity to implement a system for billing payroll costs that may have resulted in substantial overcharges. Indeed, PSATS contends that the method by which it arrives at the rates it charges "is a matter wholly internal to PSATS and solely within its decisional province."

DCED was also lax in its monitoring of the rates that it was being charged for PSATS employees whose time was being billed under the contract, by failing to verify that billings were supported by original time-keeping records. If DCED had been more vigilant in examining PSATS' invoices, it would have been afforded an opportunity to challenge the questionable methods used by PSATS to bill for reimbursement of its payroll costs and the highly suspicious failure by PSATS to retain its original time-keeping records -- records which are required to be kept under the audit provisions of the contract and without which the billings for reimbursement of payroll costs cannot be verified.

We further note that, throughout our investigation, PSATS persistently failed to produce, or significantly delayed access to, the original payroll records that we asked to examine, which are records that must be examined to verify that PSATS' charges to DCED were in accordance with the terms and conditions of the contract. While feigning cooperation, PSATS actually provided only incomplete, incorrect, or unsupported payroll information. As a result, we were unable to verify that PSATS did not overbill for the services of its employees under the contract.

Because the records we requested could have confirmed that PSATS was properly billing only for reimbursement of its actual payroll costs, we are constrained to draw an adverse inference from PSATS' persistent failure or refusal to provide all of the original records requested and complete and accurate information on a timely basis. Accordingly, we conclude that it was done purposely by PSATS to impede or prevent our investigation from uncovering problems with PSATS' billings to the Commonwealth and, more particularly, to prevent us from determining the magnitude of the overcharges resulting from the system that PSATS used for billing payroll costs.

We recommend that DCED:

- Require PSATS to produce to DCED's Comptroller for verification the names of the employees, the payroll records, and the original time-keeping records for all PSATS employees whose time was devoted to the contract. The Comptroller should analyze the records to determine the actual costs incurred by PSATS in providing the services described in the contract, reconcile such actual costs to invoices submitted by PSATS, and take action to recover any overcharges;

- Monitor future invoices to ensure that PSATS is not billing the same employee's costs to multiple training programs or to contracts with other Commonwealth agencies;
- Amend its contract with PSATS to define with specificity the manner in which an employee's annual salary and fringe benefits may be converted to an hourly rate for the purpose of billing for reimbursement of the costs incurred in providing the services described in the contract; and
- Periodically verify the accuracy of the payroll charges being submitted for payment by comparing the invoices to PSATS' actual payroll documents and to PSATS' original time-keeping records.

We are also providing copies of this report to the Pennsylvania Office of Attorney General, the Pennsylvania Treasury Department and the other Commonwealth agencies, in addition to DCED, with previous or current contracts with PSATS, including the Department of Environmental Protection, Department of Labor and Industry, and the Department of Transportation, for their review and whatever further action they may deem appropriate.

**FINDING III: DCED permitted PSATS to add surcharges of 9% for “overhead” costs and 8% for “administrative” costs to pass-through billings for goods and services provided by third-party vendors and contractors, resulting in PSATS receiving reimbursement in excess of its actual indirect costs with respect to those billings, in violation of the contract. Our analysis indicates that, for every 100 invoices submitted to the Commonwealth, PSATS would receive approximately \$569,000 of excess compensation solely from the 17% surcharge on the cost of goods and services provided by third-party vendors and contractors.**

PSATS primarily fulfills the requirements of the DCED contract by securing goods and services from third-party vendors and contractors. The indirect costs incurred by PSATS with respect to these transactions are minimal (e.g., Internet, telephone, and accounting) and should be recouped by applying the 9% surcharge for “overhead” and the 8% surcharge for “administrative” to the time that PSATS’ employees spent on obtaining and reviewing the goods and services.<sup>25</sup> By also applying the combined 17% surcharge to the cost of the goods and services obtained from third-party vendors and contractors, PSATS is billing an unreasonable and excessive amount for its indirect costs.

For example, PSATS coordinated the 2006 Pennsylvania Department of Environmental Protection Brownfields Conference held in Harrisburg. The original invoices submitted by third parties for this two-day conference, as is shown in Table 6, totaled \$41,924. PSATS provided nothing more than the “Administrative services” item in the table costing \$9,157. PSATS obtained all other goods, services, and materials for this conference from outside vendors and contractors at a cost of \$32,767.

Had PSATS charged the 17% overhead and administrative surcharge only with respect to its own staff time (the “Administrative services” item in the table), it would have received a \$1,557 reimbursement, which is a reasonable reflection of the indirect costs incurred in presenting the conference. Instead, PSATS also applied the 17% surcharge to the \$32,767 paid to third parties and received a total of \$7,128 for “overhead and administrative” costs, which is more than 4½ times as much as would have been reasonable.

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<sup>25</sup> Indirect costs represent the costs to an organization that are not easily identifiable to a particular grant, contract, or project. Indirect costs are generally classified as overhead/facilities (i.e., rent, utilities, building maintenance) and administrative (i.e., human resources, accounting, and executive office). Cost allocation plans or indirect cost rates are used to charge indirect costs to particular grants, contracts, and projects.



**Table 6**  
*Costs Charged by PSATS for DEP's 2006 Brownfields Conference*

<b>Expense</b>	<b>Invoice Amount</b>	<b>17% surcharge added by PSATS</b>	<b>Total amount billed by PSATS</b>
Hotel catering (provided by vendor)	\$20,703	\$3,520	\$24,223
Brochures and materials (provided by vendor)	\$10,908	\$1,854	\$12,762
Speaker gifts (50 large Hershey Candy Bars) (provided by vendor)	\$1,156	\$197	\$1,353
Administrative services (provided by PSATS)	\$9,157	\$1,557	\$10,714
<b>TOTALS</b>	<b>\$41,924</b>	<b>\$7,128</b>	<b>\$49,052</b>

PSATS submits over 100 invoices to the Commonwealth every year for training programs. Our analysis of nine randomly selected invoices is set forth in Table 7. Each of the selected invoices included pass-through charges for goods and services provided by third-party vendors and contractors, and, in each case, PSATS applied the 17% surcharge to the pass-through payments made to these third parties. The average surcharge billed to and paid by the Commonwealth with respect to services provided by third parties was \$5,690 per invoice (\$51,208.59 divided by 9).<sup>26</sup>

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<sup>26</sup> The unreasonableness of these surcharges is illustrated by the fact that PSATS may have added the 17% surcharge to invoices submitted by DCED charging for the time of DCED employees who taught courses presented by PSATS. A DCED official stated during an interview with OSI that two DCED employees conducted the Manufactured Homes Inspection course for PSATS and that DCED billed PSATS for their services. If DCED did, in fact, bill PSATS, then, pursuant to its billing procedures, PSATS would have paid DCED as a third-party vendor and then billed DCED for reimbursement of that cost, adding the customary 17% surcharge – leading to the absurd result of DCED paying PSATS a 17% surcharge for processing DCED's invoice for DCED's own employees' time.

**Table 7**  
**Analysis of 17% Surcharges on Pass-Through Payments to Third Parties**

Invoice	<u>1</u> Cost of services provided by third parties	<u>2</u> Costs of services provided by PSATS	<u>3</u> Totals cost of services provided (column 1 + column 2)	<u>4</u> 17% surcharge if charged on total costs (column 3)	<u>5</u> 17% surcharge if charged only on PSATS' costs (column 2)	<u>6</u> Excessive charges by PSATS (difference between columns 4 and 5)
CET Invoice 379*	\$57,819.70	\$17,574.26	\$75,393.96	\$12,816.97	\$2,987.62	\$9,829.35
CET Invoice 389	\$68,998.63	\$21,994.81	\$90,993.44	\$15,468.88	\$3,739.12	\$11,729.77
CET Invoice 408	\$45,162.95	\$17,232.41	\$62,395.36	\$10,607.21	\$2,929.51	\$7,677.70
SEO Invoice 377	\$42,369.61	\$34,283.14	\$76,652.75	\$13,030.97	\$5,828.13	\$7,202.83
SEO Invoice 386	\$33,494.66	\$33,417.97	\$66,912.63	\$11,375.15	\$5,681.05	\$5,694.09
SEO Invoice 396	\$18,257.61	\$52,529.00	\$70,786.61	\$12,033.72	\$8,929.93	\$3,103.79
DCED Invoice 13	\$13,622.95	\$8,193.33	\$21,816.28	\$3,708.77	\$1,392.87	\$2,315.90
DCED Invoice 14	\$7,674.44	\$4,953.83	\$12,628.27	\$2,146.81	\$842.15	\$1,304.65
DCED Invoice 20	\$13,826.47	\$7,881.78	\$21,708.25	\$3,690.40	\$1,339.90	\$2,350.50
<b>TOTALS</b>	<b>\$301,227.02</b>	<b>\$198,060.53</b>	<b>\$499,287.55</b>	<b>\$84,878.88</b>	<b>\$33,670.29</b>	<b>\$51,208.59</b>

\* CET is the Codes Enforcement Training Program.

**Conclusions and Recommendations:**

Goods and services provided by third-party vendors and contractors have a minimal impact on the indirect costs incurred by an organization. It is appropriate to recover these costs by charging an indirect cost rate to the time spent by employees relating to these services.

PSATS' practice of applying its 17% surcharge for overhead and administrative costs on the pass-through payments for goods and services obtained from third-party vendors and contractors results in an excessively high reimbursement for indirect costs. Based on our analysis of a sample of invoices selected randomly from the invoices submitted by PSATS, the average amount billed to and paid by the Commonwealth was \$5,690 per invoice.<sup>27</sup> At that rate, for every 100 invoices submitted to the Commonwealth, PSATS would receive excess compensation of approximately \$569,000 solely from the 17% surcharge on the cost of goods and services provided by third parties.

<sup>27</sup> See Table 7 and footnote 26.

DCED was not being fiscally prudent when it permitted PSATS to apply its 17% administration and overhead surcharge to amounts paid to third-party vendors and contractors. Applying this surcharge to the cost of services provided by others is unreasonable and violates the Contract provision that PSATS be “reimbursed for the costs incurred in providing the services described in this Contract...”<sup>28</sup>

We recommend that DCED:

- Recoup from PSATS the 17% surcharge that PSATS applied to services provided by third-party vendors and contractors, and
- Develop guidelines for allowable costs that address the conditions identified in this report and require that all future contracts entered into by DCED include the guidelines. If DCED is unable or unwilling to develop its own standards, then we recommend that it adopt regulations similar to those developed by the federal government.<sup>29</sup> DCED should ensure that all employees responsible for approving invoices for payment are familiar with the applicable guidelines.

We are also providing copies of this report to the Pennsylvania Office of Attorney General, Pennsylvania Treasury Department and the other Commonwealth agencies, in addition to DCED, with previous or current contracts with PSATS, including the Department of Environmental Protection, Department of Labor and Industry, and the Department of Transportation, for their review and whatever further action they may deem appropriate.

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<sup>28</sup> Contract, Article V, Section 2(b) (emphasis added).

<sup>29</sup> The federal government’s Office of Management and Budget (“OMB”) has established guidelines for reasonableness of costs in Section A of Attachment A of OMB Circular A-122, titled *Cost Principles for Non-Profit Organizations*, which provides as follows:

[A cost is deemed to be reasonable if,] in its nature or amount, it does not exceed that which would be incurred by a prudent person under the circumstances prevailing at the time the decision was made to incur the costs. The question of the reasonableness of specific costs must be scrutinized with particular care in connection with organizations or separate divisions thereof which receive the preponderance of their support from awards made by Federal agencies. In determining reasonableness of a given cost, consideration shall be given to:

a. Whether the cost is of a type generally recognized as ordinary and necessary for the operation of the organization or the performance of the award.

b. The restraints or requirements imposed by such factors as generally accepted sound business practices, arm’s length bargaining, Federal and State laws and regulations, and terms and conditions of the award.

c. Whether the individuals concerned acted with prudence in the circumstances, considering their responsibilities to the organization, its members, employees, and clients, the public at large, and the Federal government.

d. Significant deviations from the established practices of the organization which may unjustifiably increase the award costs.

**FINDING IV: PSATS failed to provide an adequate explanation of the composition of the 9% surcharge that it added to all billings to cover “overhead costs” and the 8% surcharge to cover “administrative costs,” making it impossible to determine whether such surcharges were in excess of actual overhead and administrative costs incurred in providing the services described in the contract.**

One of the allegations received by OSI was that PSATS, by charging excessive fees for overhead or administration costs, or both (as discussed in Finding III), was, in effect, including a “profit” factor in its billings under the contract in contravention of the contract provision limiting PSATS to being “reimbursed for the costs incurred in providing the services described in this Contract” and also in contravention of PSATS’ status as a non-profit organization.

In the Cost and Price Analysis presented to DCED as part of its proposal, PSATS included the following definition of “fees:”

Fees: These costs are factored at a rate of .09 for overhead and .08 administrative. Overhead fees include the operational cost of the PSATS professional and administrative resources dedicated to the training program. *Administrative fees represent the cost of the delivery of services under the provisions of the RFP to the Center by PSATS.* [Emphasis added]

The practice of classifying some costs as overhead and others as administrative is standard business practice. However, our attempts to determine what specific costs are included in “administrative fees” were unsuccessful because PSATS would not, or could not, explain the composition of these charges. Despite our repeated inquiries to PSATS and DCED for the meaning of the term “cost of the delivery of services under the provisions of the RFP” and for the specific expenses included in the overhead and administrative cost factors, we were never able to elicit a clear explanation as to what the two “fees” represent.

The various explanations provided by PSATS and DCED are listed below, followed by our comments.

- When OSI initially asked PSATS to explain what the 9% overhead fee and the 8% administrative fee represent, PSATS officials told OSI that it did not need to explain because the amounts were approved by DCED.

OSI comment: The contract provides that PSATS is to be “reimbursed for the costs incurred in providing the services described in this Contract....”

Although DCED approved the fees, PSATS must still explain what the fees represent and the specific costs being reimbursed.

- When OSI made further inquiry into the composition of these costs, PSATS informed OSI that its former independent auditor calculated the rates, but that PSATS could not obtain a copy of the analysis. PSATS, through its attorney, indicated that PSATS had contacted the former independent auditor and that he had retained no work papers. PSATS' attorney later stated that PSATS did not know the auditor's current whereabouts.

OSI comment: OSI located and interviewed PSATS' former independent auditor, who stated that he did not calculate the 9% overhead rate or the 8% administrative rate. Although he may have given PSATS suggestions on what to include, he stated that it would be against professional standards for him to actually calculate the rate for PSATS.

- When OSI once again asked for an explanation of the fees, PSATS, through its attorney, responded as follows:

PSATS is a non-profit organization, and the charge referred to cannot be characterized as "profit." There is no individual or entity which "profits" from the contract. If an alternative label for the 8% charge were sought, it could more accurately be characterized as an element of overhead than any other designation. . . . In developing its proposal for the contract, PSATS carried through this internal dichotomy and separated the amounts it proposed to charge on account of overhead into two components in accordance with its customary practice. While the rationale for the separate categorization might be questioned, the appropriateness of the total charge is not questionable. As the accountant's analysis for the year 2006 shows, the 9% and 8% charges are considerably less than the actual costs incurred by PSATS in conducting its operations. Moreover, [PSATS] would respectfully suggest that the cost of unbilled facilities and services employed to support the contract is self-evidently greater than the amounts charged.

OSI comment: The accountant's analysis referred to in the above response refers to a document created by PSATS' current auditors using data from 2006. It does not document the rates charged during the period under review. OSI was unable to verify the information presented in the indirect cost calculation because PSATS did not give us free and unfettered access to the work papers supporting its financial statements and this indirect cost calculation.

- OSI interviewed the former DCED contract administrator who was on the RFP review and selection committee when the contract was awarded. She

was aware of the 9% overhead fee and the 8% administrative fee in the cost proposal, but she could not explain what the numbers represented. She stated that she had never really analyzed the specific cost categories included in PSATS' cost proposal. She did recall someone (apparently at PSATS) stating that the 8% administrative fee was the fee for training. She did not recall anyone saying that the fees were profit.

OSI comment: Although the DCED employee did not recall anyone referring to the 8% administrative fee as “profit,” the statement that it is the fee for training suggests that it is, in fact, revenue in excess of the costs, which is, in effect, “profit.” Actual costs incurred for training would have been billed to the contract as a direct expense.

- OSI interviewed the DCED manager who supervised the former contract administrator. The DCED manager stated the following with regard to the Cost and Price Analysis submitted by PSATS as part of its proposal:
  - Fees included “indirect costs” such as overhead and related management fees, including building and utility costs.
  - Because PSATS is a non-profit organization, there is no profit motive, and this 17% fee would not include profit.
  - When PSATS' proposal was reviewed and the 17% fee was addressed, it was determined to be reasonable, given that the federal government uses 17% as a benchmark.
  - However, the supervisor was unaware of how PSATS came up with this percentage.

OSI comment: DCED should not assume that a contractor would not try to obtain revenue in excess of costs just because it calls itself a non-profit organization. DCED should have asked how the two fees were calculated in order to ensure that it would not be reimbursing PSATS for costs in excess of the actual cost of providing the services described in the contract.

### **Conclusions and Recommendations:**

PSATS' classification of indirect costs into overhead and administrative fees is consistent with standard business practices. However, it would also be a standard business practice for PSATS to retain records to document the composition of such indirect costs and the basis used to allocate the costs among the various programs. PSATS has failed to produce such documentation.

The DCED contract provides that PSATS is to be “reimbursed for the costs incurred in providing the services described in this Contract...” Although PSATS certainly had overhead expense, it would not or could not provide an adequate explanation of how it arrived at 9% as the factor that would reimburse that expense. Moreover, because PSATS would not or could not provide an adequate explanation of the

composition of the 8% administrative fee, and because administrative expenses were billed as direct costs on the invoices, it appears that the 8% administrative fee may be an artificial factor created by PSATS for the purpose of obtaining compensation in excess of its actual costs incurred in providing the services described in the contract.

We recommend that DCED:

- Obtain an understanding of the fees that it was charged and attempt to recoup from PSATS any sums billed that were in excess of actual costs incurred in providing the services described in the contract; and
- Draft future Requests for Proposals and contracts to require prospective vendors to document cost factors for administration and overhead in order to preclude the contractor from charging for costs in excess of the actual costs incurred in providing the services under the contract.

We are also providing copies of this report to the Pennsylvania Office of Attorney General, Pennsylvania Treasury Department and the other Commonwealth agencies, in addition to DCED, with previous or current contracts with PSATS, including the Department of Environmental Protection, Department of Labor and Industry, and the Department of Transportation, for their review and whatever further action they may deem appropriate.

**FINDING V: The now-former Executive Director of PSATS received compensation averaging \$407,608 per year in calendar years 2004 through 2008, which is excessive when compared to others in similar positions and which may be in violation of federal and state laws restricting the use of the net earnings of a nonprofit organization.**

In response to an allegation that the Executive Director of PSATS<sup>30</sup> was receiving a percentage of the revenue from all contracts awarded to PSATS, we first determined whether the allegation was true. When interviewed, the Executive Director admitted to OSI that he received an incentive or commission from PSATS equal to 1.9% of the contracts awarded to PSATS, but he added that the payment came from PSATS’ general fund and that his time was not billed to the Commonwealth.

We then researched the Internal Revenue Service Form 990 “Return of Organization Exempt from Income Tax” filed by PSATS for the years 2004 through 2008 in order to determine how much the Executive Director received in total compensation and how much the next highest paid PSATS employee received for those years. The information obtained from these returns is set forth in Table 8.

**Table 8**  
***Executive Director’s Salary Compared with the Next Highest Paid PSATS Employee, Calendar Years 2004-2008<sup>31</sup>***

<b>Calendar Year</b>	<b>Salary</b>	<b>Deferred Compensation</b>	<b>Executive Director’s Total Compensation</b>	<b>Next Highest Paid Employee</b>
2008	\$482,017	\$79,257	\$561,274	\$204,823
2007	400,681	35,897	436,578	150,703
2006	371,210	38,843	410,053	147,359
2005	313,696	38,333	352,029	140,137
2004	261,082	17,024	278,106	113,441
<b>TOTALS</b>	<b>\$1,828,686</b>	<b>\$209,354</b>	<b>\$ 2,038,040</b>	<b>\$756,463</b>

The information in Table 8 shows that the Executive Director received total compensation from PSATS for the five-year period 2004-2008 of \$2,038,040, or an average of \$407,608 per year. It further shows that the Executive Director received nearly triple the compensation of the next highest paid PSATS employee during the five-year period.

<sup>30</sup> See footnote 11.

<sup>31</sup> PSATS’ IRS Form 990 return for calendar year 2009 has not yet been published as of the date of this report.



We next researched the compensation paid to the executive directors of township associations in other states, the results of which are set forth in Table 9, and the compensation paid to executive directors of organizations of a similar nature in the Harrisburg area, the results of which are set forth in Table 10.

**Table 9**  
*Salaries of Executive Directors of Other State Township Associations,  
Calendar Years 2004-2008*

<b>Calendar Year</b>	<b>PSATS</b>	<b>Texas Municipal League<sup>32</sup></b>	<b>Michigan Township Associations<sup>33</sup></b>	<b>Ohio Township Association<sup>34</sup></b>	<b>Township Officials of Illinois<sup>35</sup></b>
2008	\$561,274	\$275,474	\$209,061	\$70,631	\$98,720
2007	436,578	281,200	208,722	119,673	106,717
2006	410,053	268,474	177,281	113,750	99,843
2005	352,029	255,274	157,702	NPA	95,430
2004	278,106	241,156	152,715	NPA	88,691

*\*Source: IRS 990 Tax Forms; NPA means Not Publicly Available.*

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<sup>32</sup> The Texas Municipal League has three separate entities: the Municipal League (with six internal departments), Intergovernmental Risk Pool, and Intergovernmental Employee Benefit Program. The Municipal League represents 1,067 member cities.

<sup>33</sup> The Michigan Townships Association is the largest local government association in Michigan with more than 1,200 townships as members. The Michigan Townships Association lobbies on behalf of its members and provides various educational programs, annual conferences, and various publications including a magazine.

<sup>34</sup> The Ohio Township Association is dedicated to promoting and preserving township government in Ohio through lobbying efforts and education forums. It maintains the Ohio Township Administrators Network, the Coalition of Large Ohio Urban Townships, and the Law Directors' Group. Its active members are trustees and fiscal officers from Ohio's 1,308 townships, and it also has more than 4,000 associate members.

<sup>35</sup> The Township Officials of Illinois serves as the clearinghouse of information for Illinois townships. It publishes a monthly magazine, provides education programs, and sponsors a risk management program. It represents 99% of the state's 1,432 townships.

**Table 10**  
**Salaries of Executive Directors of Comparable Non-Profit Agencies in Pennsylvania,**  
**Calendar Years 2004-2008**

<b>Calendar Year</b>	<b>PSATS</b>	<b>PA Institute of Certified Public Accountants<sup>36</sup></b>	<b>Pennsylvania School Boards Association<sup>37</sup></b>	<b>Pennsylvania League of Cities and Municipalities<sup>38</sup></b>
2008	\$561,274	\$326,436	\$216,376	\$233,479
2007	436,578	292,345	191,823	186,712
2006	410,053	235,518	183,934	185,034
2005	352,029	220,089	177,288	181,272
2004	278,107	191,000	159,967	177,866

\*Source: IRS 990 Tax Forms.

These comparisons reveal that not only did the Executive Director of PSATS receive nearly triple the compensation of the next highest paid PSATS employee, but he also received considerably more compensation than the amounts paid to the executive directors of other organizations of similar nature in Pennsylvania and other states.

Both federal<sup>39</sup> and state<sup>40</sup> laws prohibit the net earnings of a non-profit organization from being used to benefit members, officers or directors of the organization. The net earnings may only be used to advance the organization's mission.

An employee receiving compensation in an amount greater than would be reasonable under the circumstances is considered to be receiving an excess benefit in violation of federal and state law. We believe it is relevant in this regard that the compensation package of the Executive Director for each of the years under review in

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<sup>36</sup>The Pennsylvania Institute of Certified Public Accountants (PICPA) is a professional association of more than 19,000 certified public accountants. Headquartered in Philadelphia, it has offices in Harrisburg and Pittsburgh, and 11 geographical chapters. It also oversees the PICPA Foundation for Education and Research.

<sup>37</sup> The Pennsylvania School Boards Association's mission is to promote excellence in school board governance through leadership, service and advocacy for public education. The Association serves approximately 4,500 school directors across Pennsylvania's 500 school districts.

<sup>38</sup> The Pennsylvania League of Cities and Municipalities ("PLCM") represents Pennsylvania's cities, townships, towns, boroughs, and home rule communities that all share PLCM's municipal policy interests. PLCM's services include legislative advocacy, publications, inquiry and research, education and training certification programs, consulting-based programs, and group insurance trusts.

<sup>39</sup> 26 C.F.R. Ch. 1 § 53.4958-4(a)(1). In general, an excess benefit transaction means any transaction in which an economic benefit is provided by an applicable tax-exempt organization directly or indirectly to or for the use of any disqualified person, such as the organization's President or Executive Director, and the value of the economic benefit provided exceeds the value of the consideration. See 26 CFR Ch. 1 §53.4958(f)(1) for the definition of a disqualified person.

<sup>40</sup> 15 Pa.C.S. §5545. A nonprofit corporation that charges a fee for service may make an incidental profit. Accordingly, "[a]ll such incidental profits shall be applied to the maintenance and operation of the lawful activities of the corporation, and in no case shall be divided or distributed in any manner whatsoever among the members, director, or officers of the corporation."

this report included an incentive or bonus payment equal to 1.9% of gross revenues from all contract business, including but not limited to the contract with DCED.<sup>41</sup>

The Executive Director contended that the 1.9% incentive payment that he received was paid from PSATS' general fund and that his time was not billed to the Commonwealth contract. However, although his time may not have been billed to the Commonwealth directly, the 17% surcharge for overhead and administrative expenses provided an ample source of excess revenue to fund the payments. As stated in Finding IV, we were never able to obtain a clear explanation from PSATS for the 9% surcharge for overhead costs or the 8% surcharge administrative costs, and, as we stated in Finding III, this combined 17% surcharge on pass-through billings from third-party vendors and contractors generated revenue for PSATS that was clearly in excess of its actual costs incurred.

### **Conclusion and Recommendations:**

The compensation paid to the Executive Director of PSATS during the years 2004 through 2008, averaging \$407,608 per year, is excessive and unreasonable when compared to the next highest paid employee within PSATS and when compared to organizations of comparable size and mission, and may be in violation of state and federal laws restricting the use of the net earnings of a nonprofit organization.

We recommend that DCED draft future Requests for Proposals and contracts with nonprofit organizations to require prospective vendors to document the amount of compensation paid to top management employees and certify that the amount is reasonable and in compliance with state and federal law.

In addition, copies of this report will be forwarded to the Internal Revenue Service, the Pennsylvania Department of Revenue, and the Pennsylvania Office of Attorney General for their review and whatever further action they may deem appropriate. We are also providing copies of this report to the Pennsylvania Treasury Department and the other Commonwealth agencies, in addition to DCED, with previous or current contracts with PSATS, including the Department of Environmental Protection, Department of Labor and Industry, and the Department of Transportation, for their review and whatever further action they may deem appropriate.

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<sup>41</sup> This is also relevant to Finding IV, which was based on an allegation that PSATS was being operated to generate revenues so far in excess of costs that it was functionally operating as a profit-making enterprise. Paying its former Executive Director an incentive or bonus equal to 1.9% of the gross revenue from all contract business is indicative that, for a supposedly nonprofit entity, PSATS was inordinately preoccupied with generating ever-increasing revenues.

**FINDING VI: DCED permitted PSATS to bill for the aggregate costs of all training classes provided in a particular time period, rather than require PSATS to itemize the costs for each individual training class, thereby making it impossible to determine from the information provided whether PSATS gave proper credit for all registration fees actually collected from attendees of the training classes. With respect to two programs that we analyzed, we found PSATS did not credit the Commonwealth for \$44,594 in registration fees collected.**

Among the allegations received by OSI was that PSATS was obtaining more money than permitted under the contract by underreporting the amount of registration fees actually collected. The Cost and Price Analysis section of the RFP, which was incorporated into the contract, required an itemization for each proposed training class of (1) the costs to be incurred in six different cost categories<sup>42</sup> and (2) the estimated registration fees to be collected. The last column in the Cost and Price Analysis is net cost, indicating that registration fees collected are to be used to offset or reduce the costs submitted to DCED for reimbursement.

In an attempt to verify that the Commonwealth was being credited with the proper amount of registration fees collected by PSATS, we asked PSATS to produce records that would show the registration fees collected for each individual class during the fiscal year ended June 30, 2007.<sup>43</sup> In response to our request, PSATS produced a list of registration fees collected for each individual class. We then compared the information on the list to the total amount of registration fees that PSATS deducted from invoices submitted, during the fiscal year, to DCED for classes that DCED identified in its RFP as the “Core Municipal Training Programs.”<sup>44</sup>

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<sup>42</sup> The cost categories were “faculty,” “travel,” “facility,” “production,” “administration,” and “other expenses.”

<sup>43</sup> Article IX of the contract sets forth the record-keeping requirements:

- The Consultant [PSATS] agrees to maintain records which will support the prices charged and costs incurred for this Contract.
- The Consultant shall preserve books, documents, and records that relate to costs or pricing data for the Contract for a period of three (3) years from date of final payment.
- The Consultant shall give full and free access to all records to the Commonwealth and/or their authorized representatives.

<sup>44</sup>The RFP identified three categories of training (1) the core municipal training programs (finance, management, economic development, etc.), (2) tax collector training and qualification program, and (3) the Pennsylvania Uniform Construction Code. Each invoice submitted by PSATS represents only one training category.

Our analysis of the Core Municipal Training Programs, shown in Table 11, shows that, between September 6, 2006, and June 12, 2007, PSATS collected \$100,571 from attendees of the classes, but gave proper credit on invoices for only \$31,530, leaving a net deficiency of \$69,041 due and owing to DCED. In most of the invoices, PSATS underreported the registration fees collected. However, in two invoices, PSATS reported more registration fees than it actually collected. Because the invoices did not reflect the registration fees collected for each individual class, we were unable to determine the cause of the discrepancies on each invoice.

**Table 11**  
***Analysis of Registration Fees PSATS Collected and Remitted***  
***For the Core Municipal Training Programs,***  
***Fiscal Year Ended June 30, 2007***

<b>Invoice Date</b>	<b>Fees Collected</b>	<b>Fees Remitted</b>	<b>Fees Due to (from) DCED</b>
September 6, 2006	\$ 5,630	\$ 8,110	(\$ 2,480)
October 4, 2006	3,460	0	3,460
November 9, 2006	6,625	0	6,625
November 9, 2006	7,175	5,930	1,245
December 8, 2006	4,085	1,825	2,260
December 8, 2006	7,760	0	7,760
January 10, 2007	3,270	0	3,270
January 10, 2007	9,925	0	9,925
February 12, 2007	1,240	0	1,240
March 7, 2007	5,687	40	5,647
March 7, 2007	0	600	(600)
March 9, 2007	8,175	0	8,175
April 10, 2007	9,739	4,450	5,289
May 10, 2007	3,510	0	3,510
June 13, 2007	16,700	10,575	6,125
June 13, 2007	7,590	0	7,590
<b>TOTALS</b>	<b>\$ 100,571</b>	<b>\$ 31,530</b>	<b>\$ 69,041</b>

After discovering that PSATS did not reduce its invoices for the Core Municipal Training Programs by the total amount of registration fees collected, we analyzed the registration fees remitted by PSATS for another program specified in the contract between DCED and PSATS.

For the second program analyzed, shown in Table 12, PSATS remitted \$24,447 more than the amount required. Between July 18, 2006, and July 10, 2007, PSATS collected \$465,356 from attendees of the Code Enforcement Officers program, but gave credit on the invoices for \$489,802, or \$24,447 too much. Again, we were unable to determine the exact cause of the discrepancies due to the lack of detail in the invoices.

**Table 12**  
***Analysis of Registration Fees PSATS Collected and Remitted***  
***Code Enforcement Officers Program,***  
***Fiscal Year Ended June 30, 2007***

<b>Invoice Date</b>	<b>Fees Collected</b>	<b>Fees Remitted</b>	<b>Fees Due to (from) DCED</b>
July 18, 2006	\$ 9,735	\$ 8,020	\$ 1,715
September 6, 2006	1,050	62,455	(61,405)
October 4, 2006	25,912	48,087	(22,175)
November 13, 2006	25,170	43,581	(18,411)
December 8, 2006	40,407	36,180	4,227
January 10, 2007	49,725	38,935	10,790
February 15, 2007	20,045	75,615	(55,570)
March 13, 2007	45,840	55,635	(9,795)
April 10, 2007	56,270	38,827	17,442
May 10, 2007	17,645	32,885	(15,240)
June 12, 2007	106,110	17,930	88,180
July 10, 2007	67,447	31,652	35,795
<b>TOTALS</b>	<b>\$465,356</b>	<b>\$489,802</b>	<b>(\$24,447)</b>

**Conclusion and Recommendation:**

DCED allowed PSATS to bill for the aggregate costs of all training classes provided in a time period, rather than the costs for each individual class, and then to reduce the total amount billed by giving credit for registration fees collected from attendees of the classes. Because the invoices do not show detailed costs for each individual class, it is not possible to analyze the costs for each class or to verify that proper credit for the registration fees collected for each class was given. This afforded PSATS the opportunity to obtain more compensation than it was entitled to receive under the terms of the contract by underreporting registration fees collected from attendees of the classes.

With respect to two programs that we analyzed (the Core Municipal Training Program and the Code Enforcement Officers Program), we found that, on every invoice, PSATS failed to offset the correct amount of registration fees collected. Considering the two programs combined, PSATS collected total registration fees of \$565,927, but gave credit for only \$521,332, resulting in a net deficiency of \$44,594.

We recommend that DCED:

- Require PSATS to reformat its invoices to show the costs and the registration fees collected for each individual class, as the contract requires. This could be accomplished by insisting that PSATS submit invoices that conform to the Cost and Price Analysis section of PSATS' response to the RFP;

- Require PSATS to produce to DCED's Comptroller records of the registration fees collected for each individual class, so that DCED's Comptroller can determine whether proper credit was given for such fees, and take action to recover any overcharges; and
- Examine the original records that the contract requires PSATS to keep and maintain in order to verify that the Commonwealth is receiving the proper credit on the invoices PSATS submits for registration fees collected from attendees of the classes.

We are also providing copies of this report to the Pennsylvania Office of Attorney General, the Pennsylvania Treasury Department and the other Commonwealth agencies, in addition to DCED, with previous or current contracts with PSATS, including the Department of Environmental Protection, Department of Labor and Industry, and the Department of Transportation, for their review and whatever further action they may deem appropriate.

**FINDING VII: DCED has not established guidelines on eligible costs to be reimbursed under the contract. Consequently, DCED reimbursed PSATS for excessive and unreasonable costs relating to food provided at training seminars, meals from local restaurants, and training at historic inns and resorts. During the fiscal year ended June 30, 2007, the more egregious of these expenses cost the Commonwealth approximately \$20,000.**

A fiscally prudent government agency will establish guidelines on what constitutes eligible costs to be reimbursed under a government-sponsored program. The benchmark on which most costs are judged is reasonableness – the amount of money that a prudent person would spend at the time the expense was incurred.<sup>45</sup> When expenses are paid with tax dollars, care also needs to be given to the appearance of the costs incurred.

We reviewed invoices submitted by PSATS during the fiscal year ended June 30, 2007 for DCED’s core courses, the Sewage Enforcement Officer program, and the Code Enforcement Trainings for reasonableness. We found that DCED consistently reimbursed PSATS for excessive or unreasonable costs. Some of the more egregious instances are listed below. The costs are represented at the invoice amount and the invoice amount plus the 17% charged by PSATS for overhead and administrative fees. The Commonwealth reimbursed PSATS at the “invoice plus 17 percent” amount.

### **Food and Beverages**

Our review of expenses found that PSATS provided breakfast, lunch, and break snacks and beverages at most training sessions. Providing a continental breakfast is a customary expense that we did not question except in the most egregious circumstances. We do, however, question the need for the Commonwealth to pay for both lunch and break snacks/beverages. The costs in Table 13 are not an inclusive list of all costs paid by DCED for lunches and snacks. It represents only some of the more questionable costs.

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<sup>45</sup> See footnote 29 for the federal government’s Office of Management and Budget (“OMB”) Circular A-122, titled *Cost Principles for Non-Profit Organizations* regarding reasonableness of costs.



**Table 13**  
**Questionable Food and Beverage Invoices Submitted by PSATS,**  
**Fiscal Year Ended June 30, 2007**

Expense Item	Invoice Amount (rounded)	Amount with 17% overhead/administrative surcharge applied (rounded)
Annual Convention <sup>46</sup> <ul style="list-style-type: none"> <li>• 37 deli buffet meals @ \$27.62 each</li> <li>• 44 “Milk and Cookie Breaks” @ \$7.50 each</li> <li>• 50 danish and muffins @ \$2.75 each</li> <li>• 15 croissants @ \$2.00 each</li> </ul>	\$7,823	\$9,153
Beer and wine - Brownfields Convention	419	490
Banquet for 15 (Pocono Inn) @ \$28.80 each	432	505
Water for 37 people (purchased by PSATS) @ \$9.08 per person	336	393
3 dozen cookies @ \$30 per dozen	90	105
2 dozen cookies @ \$17.50 per dozen	35	41
50 lunches (training related) @ \$17.64 each	882	1,032
42 lunches (training related) @ \$14.73 each	619	724
35 lunches (training related) @ \$16.94 each	593	694
35 lunches (training related) @ \$14.65 each	513	600
29 lunches (training related) @ \$17.48 each	507	593
28 lunches (training related) @ \$16.82 each	471	551
25 lunches (training related) @ \$16.92 each	423	495
25 lunches (training related) @ \$26.16 each	654	765
20 lunches (training related) @ \$23.10 each	462	540
2 day seminar in Clarks Summit, PA	2,200	2,574
<b>TOTALS</b>	<b>\$16,459</b>	<b>\$19,257</b>

As shown in Table 14, when invoicing the Sewage Enforcement Officer Program, PSATS requested reimbursement for restaurant charges in the Harrisburg area. There was no indication that the expenses were necessary for the training program.

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<sup>46</sup> The items listed are only a few of the questionable charges in connection with this event.

**Table 14**  
**Restaurant Charges for Harrisburg Area Restaurants**  
**Charged to the Sewage Enforcement Officer Program,**  
**Fiscal Year Ended June 30, 2007**

Restaurant	Invoice Amount (rounded)	Amount with 17% applied (rounded)
Al's Pizza, Enola	\$ 35	\$ 41
Al's Pizza, Enola	29	34
Al's Pizza, Enola	27	32
Al's Pizza, Enola	16	19
Applebee's, Harrisburg – Program meeting	28	32
Bricco, Harrisburg	34	40
Cafe Fresco, Harrisburg	10	11
City Bar & Grill, Harrisburg - Meeting with DEP	30	35
Isaac's, Mechanicsburg	54	64
LA Pizza, Harrisburg	27	32
Neato Burrito, Harrisburg	6	7
Outback, Mechanicsburg	50	59
Papa John's, Mechanicsburg – “lunch for everyone”	97	113
Red Robin, Hershey	24	29
Red Robin, Hershey – Staff meeting	32	38
Roly Poly, Enola	54	64
Roly Poly, Enola – Lunch meeting	55	64
Ruby Tuesday, Mechanicsburg - Meeting	39	45
Ruby Tuesdays –Harrisburg - Meeting with DEP	35	41
Ruby Tuesdays, Harrisburg – Meeting with DEP	40	47
Simply Turkey	8	9
Starbucks, Harrisburg	2	2
<b>TOTALS</b>	<b>\$734</b>	<b>\$858</b>

**Historic Inns and Resorts**

PSATS employees told us that they do not solicit competitive bidding for training venues unless there is a reason to move from an established venue. Although other venues with training facilities were located in the same vicinity, trainings were held at two venues that were historic inns or resorts more appropriate for personal vacations than taxpayer-paid conferences.

- The first, an inn and resort located in Greensburg, Westmoreland County, includes such amenities as a “superbly stocked Scotch Bar,” a AAA-, Three Diamond-, and Wine Spectator Award-Winning Restaurant, and beautifully landscaped grounds including a lily pond and Victorian gazebos.

- The second, an historic hotel located in Bethlehem, Northampton County, was recently restored to “its original 1922 grandeur,” according to its promotional material, and offers 128 beautifully appointed guest rooms, including 24 luxurious suites. The hotel offers an award-winning restaurant with a sommelier on staff.

### **Conclusion and Recommendations:**

The training courses offered by PSATS are funded by a combination of Commonwealth funds under the contract and local funds paid by the individual municipalities to send their officials and employees to the training courses. Because all of the costs are paid with public funds, PSATS has the responsibility to keep the costs to a minimum, and DCED, as the contract administrator, has the responsibility to ensure that the costs incurred by PSATS are reasonable and necessary for the performance of the contract.

We found that PSATS charged the Commonwealth for staff lunches in the Harrisburg area, and held training at venues based on past experience without obtaining price quotes from other venues. Moreover, PSATS held training at historic inns and resorts more appropriate for personal vacations than taxpayer-paid conferences. We also found that PSATS billed for extravagant and excessive food and beverage expenses in connection with many of the training programs and conferences.<sup>47</sup>

Finally, we found that PSATS applied a 17% surcharge to these excessive and unreasonable billings, purportedly to cover its administration and overhead costs. After applying the 17% surcharge, during the fiscal year ended June 30, 2007, the sampling of expenses that are set forth in Tables 13 and 14 cost the Commonwealth in excess of \$20,000.

We recommend that DCED:

- Review the invoices in detail and obtain an explanation for any questionable or poorly documented expense prior to approving the invoices for payment;
- Require PSATS to periodically review the locations where trainings are held to ensure that the costs incurred for facility charges (including meals) is competitive and cost efficient;
- Institute measures that define what costs are appropriate to be submitted to the Commonwealth for payment; and
- In the absence of creating its own guideline, require PSATS to follow OMB Circular A-122, the federal guideline for nonprofit organizations.

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<sup>47</sup> Reducing or eliminating meals is one way to keep costs to a minimum without affecting the quality of the training provided.

We are also providing copies of this report to the Pennsylvania Office of Attorney General, the Pennsylvania Treasury Department and the other Commonwealth agencies, in addition to DCED, with previous or current contracts with PSATS, including the Department of Environmental Protection, Department of Labor and Industry, and the Department of Transportation, for their review and whatever further action they may deem appropriate.

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## DCED'S RESPONSE TO DRAFT REPORT

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COMMONWEALTH OF PENNSYLVANIA  
DEPARTMENT OF COMMUNITY AND ECONOMIC DEVELOPMENT  
HARRISBURG, PA 17120

OFFICE OF SECRETARY

November 19, 2010

Mr. Jeffrey H. Gribb  
Director  
Department of Auditor General  
Office of Special Investigations  
327 Finance Building  
Harrisburg, PA 17120

**Re: Special Investigation of Contract with PSATS for Training Services**

Dear Mr. Gribb:

The Department of Community and Economic Development is in receipt of the draft report of the special investigation involving the training services administered through a contractual agreement with the Pennsylvania State Association of Township Supervisors ("PSATS") and appreciates the opportunity to respond to the findings.

Act 58 of 1996 established, within the Department of Community and Economic Development (the "Department" or "DCED"), the Center for Local Government Services (the "Center") to serve as the link between the Commonwealth and local governments. In addition to other duties, the Center is responsible for coordinating state program resources and providing training for local government officials.

In 2005 when the Department initiated an RFP for training consultant services, it wanted to fulfill the requirements of the aforementioned Act by accomplishing several goals: to provide a consistent training program for all classes of local government officials, to work collaboratively with key stakeholders, and to work collaboratively with other state agencies that have a need to provide training to the 40,000 plus local government officials. Two proposals were submitted and reviewed by the Department. PSATS submitted the only proposal which had the capacity to deliver the services required by the contract. Additionally, they established a partnership agreement with the five other major local government associations. Based on a thorough review of the proposals, the PSATS proposal was able to fulfill the requirements of the RFP and the contract was awarded to them.

Since the inception of the training contract, the Department has provided for coordination, monitoring, and oversight of the contractual activities through the Training Manager's position. Throughout the evolution of the outsourced training programs and activities, we have continually implemented modifications to improve the delivery of programs while maintaining due diligence in protection of the Commonwealth's funds.



Following contract execution and through our internal contract monitoring, DCED found instances where process documentation was weak and implemented policies to strengthen and clarify various contract provisions, including accountability, reporting, and to prohibit any questionable activity. In January 2008, Center staff met with PSATS to discuss the invoicing, equipment acquisition and disposition, the use of registration fees and reporting. Subsequent to this meeting the Department issued Training Program Guidelines that were officially adopted and included as a binding part of the PSATS contract in December 2008. These Guidelines provided for greater accountability concerning all of these issues. Additionally, DCED recovered from PSATS, unaccounted for or undocumented registration fees in the amount of \$49,336.53, covering July 1, 2006 to the present. A copy of these guidelines is enclosed.

In response to the findings identified in your report, DCED submits the following response:

Finding I: During the course of conducting official business on an established contract DCED attended meetings and conferences conducted by PSATS. In some instances these meetings covered a significant portion of the day and lunch was provided in order to work more efficiently. It was necessary and proper for DCED employees to participate in these programs to keep one of our key constituent organizations apprised of legislative and regulatory matters affecting its membership. The expenses for these employees, in hindsight, would have been more appropriately paid directly by DCED rather than through the contract with PSATS. There was, however, no conflict inherent in participation by DCED employees who may have also participated in the selection process. The Governor's Center has a limited number of staff and it is therefore difficult if not impossible to segregate those who participate in contract review and those that participate in conferences related thereto. DCED is committed to adhering to the requirements of the State Ethics Act, Commonwealth travel procedures, and the Governor's Code of Conduct, and has already so apprised its staff.

Finding II: DCED promptly provided all requested information under its control to the Auditor General's Office of Special Investigation. These records attest to the fact that the reimbursement methods for invoices submitted under the subject contract were consistent with the contract and based upon commonly used structures, including classification-based reimbursement for wages and benefits. DCED will incorporate modifications to its training contract reimbursement terms to implement suggestions made in this Finding.

Finding III: The contract with PSATS provided for a 17% overhead/administrative cost and did not specify items that were to be excluded. In the development of a new contract DCED will provide specificity on those items that are eligible for the overhead/administrative charge and those items that are not.

Mr. Jeffrey H. Gribb  
November 19, 2010  
Page 3

Finding IV: The adequacy of PSATS explanations to the Auditor General's inquiries is a judgment made by the Auditor General and is not a matter for response by DCED.

Finding V: Compensation for PSATS officials is not a matter within the purview of DCED and therefore no response is made.

Finding VI: DCED Training Program Guidelines require mandatory reporting requirements of registration fees. Additionally, DCED recovered, \$49,336.53 from PSATS for undocumented and unaccountable registration fees from July 1, 2006 to the present.

Finding VII: Through the Training Program Guidelines, DCED has required PSATS to follow Commonwealth policies on travel and meal reimbursement rates. Additionally, they are required to find the most cost effective but suitable facilities to conduct Commonwealth training programs. Consistent with this Finding, DCED will more closely monitor training site selections to meet these requirements.

The Department appreciates the efforts of the Auditor General's office of Special Investigations to help strengthen the training program and has or intends to implement a significant number of modifications to training contracts and procedures to improve its efforts to provide the most cost effective program.

Sincerely,

A handwritten signature in black ink, appearing to read "Austin J. Burke". The signature is fluid and cursive, with a long horizontal stroke extending to the right.

Austin J. Burke  
Secretary

## Training Program Guidelines

- A. Purpose
- B. Background
- C. Workflow
- D. Financial/Budget
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**A. Purpose**

The purpose of these guidelines is to provide administrative procedures for the handling of the PA Local Government Training Partnership (LGTP) contract in order to provide greater accountability and to demonstrate compliance.

**B. Background**

The core mission of the Department of Community and Economic Development's (DCED), Governor's Center for Local Government Services (GCLGS) and hereafter referred to as "the Center" is to provide a full range of technical and financial services to local governments to increase their capacity to provide vital programs and efficient and effective services to their residents. Our local government training initiative is at the center of this capacity building objective.

The Center trains local government officials through the LGTP. The training is provided under contract with the Pennsylvania State Association of Township Supervisors (PSATS) and hereafter referred to as "Contractor," through a partnership agreement with the six major local government associations: The County Commissioners Association of PA, the PA State Association of Boroughs, the PA League of Cities and Municipalities, the PA State Association of Township Commissioners, the PA State Association of Township Supervisors, and the PA Municipal Authorities Association hereafter referred to as "Partners."

Additionally, DCED developed a Memorandum of Understanding (MOU) to establish a partnering relationship with other state agencies having an identified need and desire to provide training through the LGTP. As necessary, the contract is amended to include additional funds for training activities as identified in a Letter of Understanding (LOU) developed by each partner from other state agencies. Under the current MOU, DCED is partnered with the following state agencies: The Department of Environmental Protection, the Pennsylvania Department of Transportation, the Pennsylvania Emergency Management Agency, Labor & Industry, the Rural Development Council, the Department of General Services, the Department of Conservation and Natural Resources, the Department of General Services, and the Department of Agriculture.

Courses are designed to keep municipal officials current on new laws and legislative requirements and enhance their abilities to govern more effectively. The courses are delivered from disciplines including:

- Community & Economic Development
- Environmental
- Finance
- Local Government Administration
- Planning/Land Use
- Public Safety
- Recreation
- Tax Collection

- Uniform Construction Code

The courses are offered throughout the Commonwealth of Pennsylvania.

**C. Workflow**

The training contract is managed by the Center's Training Coordinator. The Training Coordinator is the first point of contact on all correspondence regarding training initiatives. The Contractor will receive a written notice to proceed with planning for the general contract and other related DCED courses immediately after the enactment of a state budget.

**D. Financial/Budget**

**1. Course Costs**

The Contractor will develop a proposed budget based on the courses determined by the Center to be delivered during each fiscal year. The budget will include anticipated registration fees based on the number of individuals registering for each course (see Registration Fees). The budget used for the development and delivery of the LGTP courses will be coordinated through and approved by the Center's Training Coordinator. The final approved budget will be submitted to the Center's Training Coordinator.

**2. Registration Fees**

The Contractor will charge registration fees for all courses using the fees listed below unless otherwise agreed to in writing between the Contractor and the Center:

- A. Full day course with snacks/soda/coffee and lunch \$80; without lunch \$50.
- B. Evening/Half day course with snacks/soda/coffee but no lunch \$50.
- C. Webinars are \$50.

Fees will be reviewed annually.

The handling and disposition of registration fees will be in accordance with the contract as follows:

- a. Contractor will account to the Center for all registration fees collected in a format that relates the fees to the program funding source.
- b. Contractor will continue to utilize such fees in support of the programs from which they are generated as proposed and accepted in the Price and Cost Analysis submitted with the original bid for contract services.

- c. Whenever an annual budgeted amount has been or is anticipated to be expended before the end of a program year and/or before all approved programs have been completed, Contractor will submit to the Center, for approval, a revised budget to include any unexpended registration fees.
- d. In addition, the Contractor may develop and submit to the Center, for review and approval, a proposal to utilize the unexpended registration fees for additional training activities. The additional training activities may be scheduled for the ensuing program year if, in the judgment of the Contractor and the Center, there is insufficient time remaining in the current year. In such an event the supporting registration fees shall be treated as dedicated to and encumbered by the obligation of such additional activities. If the additional training activities are not completed in the time provided for, the registration fees will become unencumbered and retained by the Center.
- e. The Center may request the Contractor to develop a budget for proposed training activities utilizing all unencumbered registration fees as deemed necessary.

### **3. Invoicing**

Invoices should be submitted to the Center's Training Coordinator once a month, as reasonably possible in accordance with the Reporting Requirements. It may be necessary for the Contractor to submit an invoice early; this shall be coordinated with the Center's Training Coordinator. Additionally, a monthly financial Cost Close-Out report by course will be provided to the Center for all related training courses. The Center's Training Coordinator will provide such documentation to all Program Managers.

Invoices must be mailed to: The Department of Community and Economic Development, 24DCED, PO Box 69181, Harrisburg, PA 17106 and must contain the following information:

- a. Location Code: 24DCED, Invoice Date, Invoice Number, and Gross/Total Amount placed in the top third of invoice cover.
- b. Documentation to support all costs incurred for the development and/or delivery of the training.
- c. They must relate to the budget categories in the fully executed contract provided to the Contractor.
- d. The Contractor must submit one completed copy of all DCED training invoices and one completed copy for all other state agencies.

- e. The invoice cover sheet should also contain the following information: Name, address and federal identification number of Contractor, state vendor number, electronic single application contract #, contract period, date of request, appropriation number, amount of request, and courses covered under each request. Also included on the cover sheet should be a total for each major budget category and the registration revenues deducted from the total cost. The backup documentation for each major expense category should have a cover sheet with a calculator tape of costs that match all expenses that follow. Lastly, the Contractor should indicate the bank information for payment deposits.
- f. Invoice billing for agencies covered under the MOU, should be submitted to the agency's Program Coordinator for approval and to the Center for payment.

#### 4. Equipment

All materials, including office furniture and equipment, purchased by Contractor with Commonwealth funds or generated by the Contractor in performance of this Contract shall be the property of the Commonwealth and upon termination or expiration of this Contract shall be delivered as soon as practicable to DCED. Contractor shall implement needed repairs and maintenance for all such materials in its possession. DCED shall bear the cost of all such repairs and maintenance. The Contractor shall maintain a property inventory with DCED identification tags provided by the Commonwealth, that identifies all property or equipment with a unit acquisition cost of \$500 or more, and all other equipment listed below purchased in whole or in part with Commonwealth funds. Such materials shall be referred to as "inventoried items."

##### Equipment Under \$500

Power Tools

Computers and Computer Accessories

Audio/Video Equipment

All equipment must be used to support the delivery of services outlined in the contract, MOU, LOU, or any other official document related to the contract that authorizes the purchase of such equipment.

If it becomes necessary to dispose of any inventoried items prior to the expiration of its prescribed useful life because it has become inoperable, outdated, or no longer needed, the Contractor shall first request and obtain in writing approval of the same from the Center. The Department retains the right to keep the property.



Contractor must update the inventory list as purchases, disposals and transfers are made throughout the contract period and shall submit a current list to the DCED at the end of each fiscal year and at the end of the contract period and at such other times as the DCED may reasonably request.

The Contractor must record the date, authorization, delivery location and recipient of all inventoried items which, subsequent to purchase, delivered to an entity or individual pursuant to a written authorization by DCED. Contractor shall have no responsibility with respect to any such items following such authorized delivery and signature of receipt.

#### **E. Marketing**

The Contractor will develop a marketing plan using best practices, to determine an appropriate and most economical way for providing notification to all municipalities of available training and all future training provided through the Partnership. The Contractor shall use brochures, websites, fax alerts, mailings, county conventions, county meetings, publications, and/or any other mechanism determined to be feasible and within reason.

##### **1. Brochures**

Brochures are developed by the Contractor in concert with the Center staff. However, all brochure formats shall be electronically sent to the Center's Training Coordinator for final review prior to them being sent to the printer. The brochures will be reviewed and/or revised as necessary in coordination with the DCED's Program Managers and/or staff and returned to the Contractor with approval to produce for distribution.

The brochures will be designed in the following manner:

- A. All brochures shall be clear, concise, and easy to read. They must follow a consistent format.
- B. All brochures shall contain logos and/or the names of all cosponsoring organizations.
- C. The Center's full name and logo and the Partnership's full name and logo shall appear on all brochures funded by the Department.
- D. Programs funded by the Land Use Planning and Technical Assistance Program, shall indicate the availability of on-site training courses. On-site training courses are a specialized method of course delivery where the entity requesting the training is responsible for organizing the logistics of the course.
- E. The following statement shall appear on the brochures for all DCED funded courses: "*This program is presented in*

*cooperation with the Governor's Center for Local Government Services with funds from the annual appropriation from the General Assembly to the Department of Community and Economic Development. Trainees are admitted without regard to race, color, age, sex, religion, political affiliation, national origin or disability."*

- F. The following statement shall appear on all PENNDOT funded courses: *"This program is presented by the (name of co-sponsoring organization) in cooperation with the Governor's Center for Local Government Services with funds from PENNDOT and the Federal Highway Administration. Trainees are admitted without regard to race, color, age, sex, religion, political affiliation, national origin or disability."*

The Contractor shall provide 100 finished brochures to the Center concurrently as they are mailed to the public. The Center's Training Coordinator will forward brochures as needed to the DCED Regional Offices.

Brochures must be mailed no later than six weeks prior to the date of the first class.

## **2. Website**

The Contractor will maintain the LGTP website which will include information about courses being offered, dates, locations, and how to register. The course information will remain on the website until the course is completed. Course information will be moved to the Completed Courses section of the website after the last course within a given series is complete.

The website will contain the branding for the training program which includes a logo and the various colors to coordinate with a particular training series. The website must also contain all future LGTP courses to be delivered during the current fiscal year. A link to the Partnership training website should be included on the web page of all existing Partners and vice-a-versa.

A section of the website shall contain "how-to" information for professionals interested in becoming instructors for the Center's LGTP program (see Instructors).

## **F. Courses**

### **1. Course Materials**

All material provided to course attendees will reference the Department of Community and Economic Development and the Center's Local Government Training Partnership. The contractor will provide to the Center's Training Coordinator, one copy of all new and revised finalized course materials/handouts prior to the first training session for all courses during each fiscal year. Course handout material shall be the same for all classes delivered in a specific subject area regardless of a change in the instructors. Additional handouts not included in the course material must first be approved by the Center.

Course materials shall be updated through the coordination of approved instructors, the Center's Training Coordinator, and other DCED staff as applicable.

**2. Development**

All DCED course development activity shall be coordinated through the Center's Training Coordinator unless prior approval was given to the Contractor to enter into a subcontract agreement with another individual or entity to develop the course.

Course curriculum shall be updated through the coordination of approved instructors, the Center's Training Coordinator, and other DCED staff as applicable.

**3. Delivery**

Courses shall be delivered in an open enrollment format where individuals may register and attend courses previously scheduled by the Center. Municipalities may also request onsite delivery of courses. When delivered onsite, the municipality is responsible for costs associated with development and/or delivery unless otherwise specified by the Center. The Contractor shall develop web-based courses in coordination with requests by the Center.

**4. Locations**

LGTP courses must be offered across the Commonwealth. The Contractor must exhaust all efforts to find the least expensive but reasonable location for all trainings that will meet the needs of the course.

**5. Registration/Cancellations**

The Center's Training Coordinator in coordination with the Contractor will determine whether to cancel and/or reschedule any LGTP course based on attendee registration or other circumstances. The Contractor will provide regular registration information as follows:

- a. A weekly Current Course Registration update should be sent electronically to the Center's Training Coordinator for all currently advertised courses.
- b. A monthly A-Z Registration report will be sent to the Center's Training Coordinator for all courses provided during the current fiscal year.
- c. The Contractor will notify all registered attendees by phone, fax, and/or email if a course is cancelled; and post such changes on the training website.

In the event of a weather related/last minute cancellation, all registered attendees must be notified by phone as soon as the determination is made to cancel the course.

#### **6. Instructors**

Course instructors must be professionals with expertise in the field they intend to teach, be an experienced presenter, and have knowledge of local government. They must be approved by the Center to represent DCED at trainings. New instructors must receive an orientation of the Center by the Center's Training Coordinator or other designee prior to teaching and receive peer support set up by the Contractor during their initial training sessions, unless otherwise specified.

Current instructors representing the Center will forfeit their "grandfather" status if inactive for two or more years. After a two-year inactivity period, they must reapply to the Center to be an instructor. The Contractor shall maintain an active roster of instructors.

Instructors will be compensated with a flat rate of \$300/half day and \$450/full day for instruction, travel, and preparation time for the scheduled course delivery date. Course development time is \$35 per hour. Increased compensation for specialized course development and instruction may be requested by the Contractor if warranted and approved in writing by the Center. All travel expenses will be reimbursed in accordance with the Management Directive: Travel and Subsistence Allowances 230.10 Amended.

Professionals interested in becoming an instructor for LGTP must submit an original letter of interest and resume to the Center's Training Coordinator and one copy to the Contractor. Use of the Center's staff to instruct courses under the Partnership will be coordinated through the Center's Training Coordinator.

#### **G. Meetings**



There are several meetings held during the fiscal year in which the Contractor will have a major role. The meetings include the bi-weekly training meetings with Center staff, course development meetings, Partners meetings, and mid-year and year-end training partnership meetings. Other meetings may be scheduled as necessary.

The Contractor will participate in bi-weekly meetings with the Center staff to review program logistics, training issues, new developments, and the coordination of training related activities.

The Contractor will participate in meetings, as needed with the Partners to assist with the coordination, development and delivery of courses to be offered through the LGTP.

#### **H. Reporting**

The Contractor is responsible for providing the following reports to the Center's Training Coordinator:

- A. Financial Reports: Active Contracts, Costs Close-Out by course, and Registration Fees.
- B. Program Reports: A-Z Report, Current Course Registrations, and LOU Activity.
- C. Equipment Report (see Equipment Policy)
- D. Summary Reports: Mid-year and Year-end Reports

The Active Contracts report is a budget showing all funding streams included in the contract and expenses incurred to date. The Costs Close-Out is a report listing all budgeted funding per course, expenses, remaining program funds, and revenues. The registration fee report shows the amount collected by program based on the number registered and the fee amount per course.

The A-Z report is a listing of all courses and the registrants for the current fiscal year. The Current Course Registrations report is a listing of all currently advertised courses and the number of people registered to date. The LOU Activity is a monthly report of all work done on the contract by program.

The financial reports are due by the 15<sup>th</sup> of every month. The A-Z Report and the LOU Activity reports are due by the 15<sup>th</sup> of every month. The Equipment Report is due at the end of every fiscal year. The Current Course Registrations report is due by Friday of each week.

The Contractor will provide two summary reports for the training program each fiscal year; a mid-year report and a year-end report. The reports will provide an accounting of all activity occurring for the respective periods. The reports will contain a summary of all courses offered and all cancelled courses. It will include dates, locations, course titles, number of attendees, and a summary of training

evaluations for each course. Additionally, for all cancelled courses, an explanation for why the course was cancelled and the number of registered attendees per course. The year-end report must contain a summary comparison of attendance per course for the same or similar courses in the current reporting year in comparison to each of the previous contract years.

## **I. Partners**

### **1. Submitting Proposals**

Proposals must be submitted to the Contractor and copied to the Center's Training Coordinator by the date set by the Center during each fiscal year.

### **2. Review and Approval Process**

Proposals will be reviewed by the Center staff and the Contractor to determine feasibility and need. The Contractor will provide notification to the Partners of approved or unapproved courses as soon as practically possible following budget enactment.

### **3. For All Approved Courses**

The Contractor shall enter into a subcontract agreement approved by the Center to administer and implement said courses. Said agreement shall incorporate provisions of these guidelines.

Revised 4/22/2009

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## THE DEPARTMENT OF THE AUDITOR GENERAL'S COMMENTS ON THE RESPONSE OF DCED TO DRAFT REPORT

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The Department of Community and Economic Development's response to the draft report is encouraging to the extent that DCED has acknowledged that the Pennsylvania State Association of Township Supervisors has taken advantage of a very loosely written contract to obtain compensation in excess of its actual costs in providing the services described in the contract. It is also encouraging that DCED has already taken some limited steps to tighten up the terms of the contract to improve PSATS' accountability and has expressed an intention to consider some of our recommendations in the drafting of future contracts. Because taxpayer dollars are involved, DCED must take a stronger leadership position with regard to all contracts with PSATS.

However, on balance, we are disappointed in DCED's failure to follow our recommendations to demand from PSATS an accounting for questionable billings in the past and to take action to recover any overcharges that may be discovered in that process. We certainly commend DCED for adopting new "Training Program Guidelines"<sup>48</sup> and for recovering \$49,336.53 from PSATS representing unaccounted for or undocumented registration fees, but DCED's efforts to date do not go nearly far enough.

More particularly, we are disappointed that DCED has made no commitment to follow our recommendations to pursue recovery of potential overcharges cited in Finding II (relating to excessive hourly rates PSATS charged for its employees who worked on the contract), Finding III (relating to PSATS adding excessive surcharges of 9% for overhead costs and 8% for administrative costs to pass-through billings from third-party vendors and subcontractors), and Finding IV (relating to the failure of PSATS to document that such surcharges accurately reflect PSATS' actual overhead and administrative costs).

We are also disappointed in the off-hand manner in which DCED has evaded responding to two of our findings, Finding IV and Finding V. The clear import of Finding IV is that PSATS was unable to demonstrate that the percentage factors it used to bill for its overhead and administrative costs bore any relationship to its actual costs. We recommended that DCED should demand proof that the percentage factors reflect PSATS' actual costs and to recoup from PSATS any sums billed that were in excess of actual costs incurred by PSATS in providing the services described in the contract. To flippantly state, "The adequacy of PSATS['] explanations to the Auditor General's

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<sup>48</sup> The "Training Program Guidelines" appended to DCED's response, which were incorporated into the contract after the period covered by this investigation, cover a multitude of program issues that were not spelled out in the original contract. Included therein are guidelines that partially address the deficiencies identified in Finding VI, in that they require PSATS to more accurately account for registration fees collected, and Finding VII, in that they require PSATS to find "the least expensive but reasonable" training sites and require the cost of meals to be borne by the course attendees rather than DCED.

inquiries is a judgment made by the Auditor General and is not a matter for response by DCED” completely evades the important issues raised in the finding and recommendation.

We are also disappointed in the failure by DCED to address the excessive compensation received by PSATS’ former Executive Director described in Finding V. We do not agree that the compensation paid to PSATS officials “is not a matter within the purview of DCED” when the compensation is so far out of line in comparison with similar nonprofit organizations that its legality under federal and state law governing the use of the net earnings of a nonprofit organization is called into question. Such matters are brought within the purview of a state agency pursuant to the standard contract clauses requiring organizations that enter into contracts with the Commonwealth to comply with all federal, state, and local laws.<sup>49</sup> Furthermore, PSATS is not just an ordinary business entity. Rather, it is an organization that owes its very existence to a statute enacted by the General Assembly of this Commonwealth, and it is supposed to be operating on a non-profit basis for the benefit of its member townships and township officials. Finally, it is clear that, were it not for the enormous revenues generated by the contract with DCED, there would not have been funds available to pay exorbitant compensation averaging \$407,608 per year to the former Executive Director of PSATS.

Even in those instances in which DCED has expressed an intention to follow our recommendations, we find its assurances to be vague and indefinite, without specific dates for implementation. We sincerely hope that DCED follows all of our recommendations, both with respect to reforming the current contract and recovering past overcharges and with respect to awarding any future contracts. By doing so, DCED will ensure that no more Commonwealth funds are wasted paying excessive billings under this contract. In any event, the Department of the Auditor General will follow up at the appropriate time to determine whether all of our recommendations have been implemented.

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<sup>49</sup> The pertinent provisions of the contract are as follows:

12. (b) The Consultant shall maintain the highest standards of integrity in the performance of this Contract and shall take no action in violation of state or federal laws, regulations or other requirements that govern contracting with the Commonwealth.

13. Compliance With Law. The Consultant shall comply with all applicable federal and state laws and regulations and local ordinances in the performance of the Contract.

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## **DISTRIBUTION LIST**

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