

A Performance Audit

Port Authority of Allegheny County

*For the period July 1, 2007 through December 31, 2012
Issued March 2014*

COMMONWEALTH OF PENNSYLVANIA

EUGENE A. DEPASQUALE - AUDITOR GENERAL

DEPARTMENT OF THE AUDITOR GENERAL





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EUGENE A. DePASQUALE
AUDITOR GENERAL

March 24, 2014

Ms. Ellen McLean
Chief Executive Officer
Port Authority of Allegheny County
Heinz 57 Center
345 Sixth Avenue, Third Floor
Pittsburgh, PA 15222

Dear Ms. McLean:

This report contains the results of the Department of the Auditor General's performance audit of the Port Authority of Allegheny County. The Second Class County Port Authority Act requires that we conduct a performance audit of the Port Authority at least once every four years, and this report covers the period from July 1, 2007, through December 31, 2012. We completed the audit in accordance with generally accepted government auditing standards as issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

The audit objectives focused on the following areas: (1) capital projects funding, including, but not limited to, the issuance of bonds and debt service payments; (2) governance structure, including but not limited to, the board composition; (3) contract procurement and monitoring processes; and (4) review of service routes, planning, and scheduling process. We also conducted an analysis of Port Authority's revenue and expenditures and determined the status of the implementation of the recommendations presented in our report dated December 3, 2007.

We found that Port Authority made significant improvements in its operations since our previous audit. Most notably, the agency took several actions to address the rising pension and post-employment health care costs, and we discuss those actions in the two observations in this report. On another positive note, we found that the Port Authority appropriately used its Public Transportation Assistance Fund allocations to pay debt obligations.

We also found that the Port Authority had to make changes to its service routes during our audit period. We reviewed the planning and evaluation process for the changes and determined that the Port Authority implemented the changes after an extensive system-wide review and analysis of all service routes. We also found that the Port Authority provided several opportunities for public input before the final decisions were made.

While we were encouraged to see the positive steps taken by the Port Authority, the audit revealed areas for improvement in the agency's procurement process. Specifically, we found that the Port Authority did not consistently comply with requirements regarding debarment and suspension of contractors and subcontractors. We also found a sole source contract that was not properly approved, and another contract that was not properly advertised. In addition, we found some instances where the Port Authority made questionable decisions when procuring some goods and services, and other instances where the agency's failure to adequately prepare bid proposals resulted in large change orders that significantly increased the costs of the contracts.

Finally, we found several deficiencies related to the Port Authority's relocation policy. We noted \$4,300 of expenses that were paid twice; two instances where the agency's failure to adhere to its relocation policy cost it nearly \$5,000; and one employee was reimbursed more than \$28,000 for relocation costs.

We made ten recommendations in this report to address the issues we identified. Implementation of these recommendations is critical to ensuring that the Port Authority adheres to all required procurement policies and procedures and eliminates unnecessary contract expenses and/or the potential for fraud, waste, and abuse.

We want to thank Port Authority officials and staff for the cooperation extended to the audit team throughout the engagement.

Sincerely,



Eugene A. DePasquale
Auditor General

cc: Chairman and Board of Directors, Port Authority of Allegheny County

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**Executive
Summary**

The Second Class County Port Authority Act requires the Department of the Auditor General to conduct a performance audit of the Port Authority of Allegheny County (Port Authority) at least once every four years.¹ This audit covered the period of July 1, 2007, through December 31, 2012, unless noted otherwise. (Additional information on the audit scope, as well as the audit objectives and methodology can be found in Appendix A.)

During this audit we found that the Port Authority has taken several actions in the last few years to increase revenues, reduce expenses, and improve its effectiveness and efficiency in operations. Specifically, we note the following in this report:

- The Port Authority has taken numerous actions to address its pension obligations, which resulted in the 2012 pension contribution payment being 34 percent lower in 2012 than in the prior year. (See *Observation One* beginning on page 39.)
- The Port Authority reduced post-employment health care benefits for new employees in an effort to reduce the costs associated with those benefits; for example, new hires in the ATU bargaining unit receive a maximum of three years health care at retirement, effective August 2012. (See *Observation Two* beginning on page 46.)
- The Port Authority effectively planned and implemented its 2010 and 2011 changes to service routes and solicited and incorporated public input when making changes to service routes. (See *Finding Five* beginning on page 31.)
- The Port Authority appropriately used annual Public Transportation Assistance Fund allocations to pay debt obligations. (See *Finding Six* beginning on page 35.)
- The Port Authority implemented the recommendations made in our December 2007 performance audit; in this report, we focused on the changes the Port Authority made to eliminate excessive benefits. (See the *Status of Findings from Prior Report* beginning on page 50.)

¹ See Chapter 17 (relating to Second Class County Port Authorities) of Title 55 (Navigation) of the Pennsylvania Statutes, 55 P.S. § 553.2(a)(1).

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While we are pleased to report on the positive actions taken by the Port Authority, we also identified some procurement process issues and have made several recommendations for improvement. The dollar value of the issues identified may not be material, however, the implementation of our recommendations is critical to ensure that the Port Authority follows all required policies and procedures for procuring goods and services and eliminates unnecessary contract expenses and/or the potential for fraud, waste, and abuse. With regard to procurement, we found the following:

- The Port Authority did not implement FTA recommendations and did not comply with its own procurement requirements, including those related to subcontractor debarment and suspension certification, subcontractor lobbying certification, sole source approval, and public advertisement when awarding some of its contracts. (See *Finding One* beginning on page 6.)
- The Port Authority made questionable decisions regarding some contracts, including automatic extensions without price comparisons and inadequate communication among departments before renewing contracts. (See *Finding Two* beginning on page 14.)
- The Port Authority failed to adequately prepare contract bid proposals for two contracts, leading to change orders that significantly increased the cost of each contract and possibly resulted in other vendors not submitting bids. (See *Finding Three* beginning on page 21.)

Additionally, during this audit we found that the Port Authority implemented a relocation policy in November 2007 in response to one of the recommendations made in our December 2007 audit. However, we found the following issues related to that policy:

- The Port Authority paid relocation expenses of more than \$28,000 to one employee and failed to properly adhere to its relocation policy for two other employees, which cost the Port Authority nearly \$5,000. (See *Finding Four* beginning on page 25.)

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In its written response to the audit, Port Authority acknowledged the issues we found. Agency officials stated that the Port Authority would take action to implement our recommendations. (See page 73 for the Port Authority's entire response.) We will follow up with the Port Authority in our next quadrennial performance audit to determine the extent to which the Port Authority actually implemented our recommendations.

In the meantime, we are encouraged to see the improvements the Port Authority made over the past five years. With its pledge to implement the recommendations made in this report, the Port Authority continues to take positive steps in moving the agency forward.

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**Introduction
and
Background**

In 1956, the act known as the “Second Class County Port Authority Act”² (Act) required the establishment of the Port Authority of Allegheny County (Port Authority). One of the primary intentions of the Act in establishing the Port Authority was to improve and develop the port districts along the rivers within Allegheny County.

The Pennsylvania General Assembly amended the Act in 1959 to allow the Port Authority to acquire privately-owned transit facilities and to own and operate a public system of mass transit. The Port Authority began its mass transit operations on March 1, 1964, with the consolidation of 33 private transit carriers.

The Port Authority, which is the second largest public transportation system in the state, provides transportation services within the City of Pittsburgh, all of Allegheny County, and into portions of neighboring Beaver and Westmoreland counties.

The Port Authority’s transit network includes fixed route bus service, a light rail system, and the Monongahela and Duquesne Inclines. The Port Authority also provides ACCESS, which is a coordinated, shared-ride paratransit system offering door-to-door, advanced reservation transportation for elderly and handicapped persons. See Appendix B for ridership statistics of the Port Authority.

The Port Authority served approximately 63.9 million passengers in 2013.

Organization Structure

The Port Authority is governed by a board of directors (“board”). Historically, the board was statutorily comprised of not more than nine members, all appointed by the county executive of Allegheny County. On July 18, 2013, the governor approved Act 72 of 2013, which changed the governing board’s structure, effective immediately.

The board’s composition was changed to be comprised of 11 members, 6 of whom are appointed by the county executive of Allegheny County. Two of these six members must come from a recommended list of candidates supplied by the following

² 55 P.S. § 551 *et seq.*

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organizations: The Allegheny Conference, the Southwestern Pennsylvania Commission, the Committee for Accessible Transportation, and councils of government that have constituent members in the county. Further, these two appointees are subject to confirmation by a majority vote of the members of the Allegheny County council.

The Governor and the legislative leaders from each of the four caucuses appoint the remaining five board members. The Governor's appointee must be a Pennsylvania resident, while all of the other appointees must be residents of Allegheny County and are required to have expertise or substantial experience in budgeting, finance, economic development, transportation, or mass transit operations.

The board of directors governs the Port Authority's operations. Further, the board of directors hires a chief executive officer who is responsible for the daily management of the Port Authority and who reports to the board. On February 1, 2013, the former chief executive officer was voted out of his position, and the chief financial officer assumed the position of interim chief executive officer. On January 24, 2014, the board of directors voted to hire the interim chief executive officer as chief executive officer with a three-year contract effective February 1, 2014.

The chief executive officer is currently aided by seven senior staff members who oversee the following divisions: transit operations, finance, planning and development, communications, legal and corporate services, human resources, and engineering and technical support. (See *Appendix C* for an organization chart of the Port Authority.)

Over 2,400 people work at the Port Authority.

As of June 30, 2013, the Port Authority had 2,406 employees, of which 91.1 percent were represented by a collective bargaining unit.

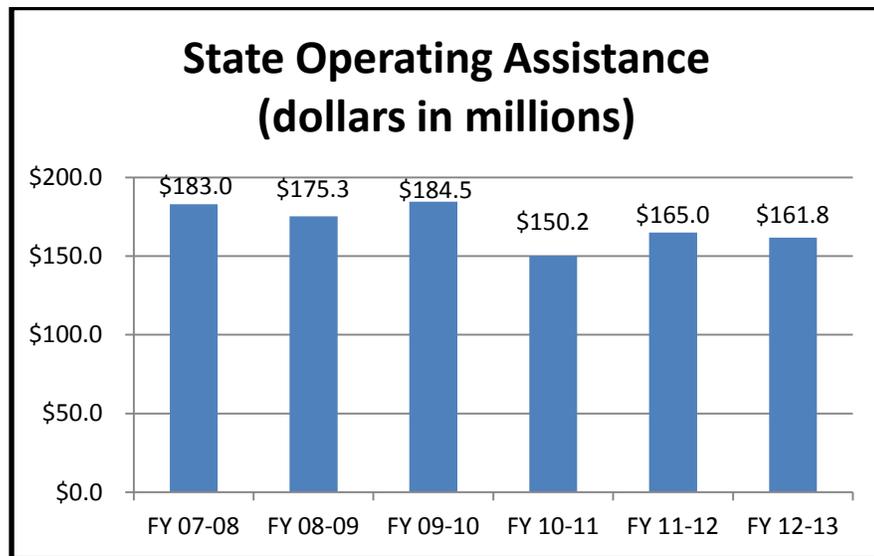
Funding and Financial Position

Revenues. For the fiscal year ended June 30, 2013, the most recent year for which detailed comparable financial data was available, the Port Authority's operating revenues amounted to \$104.2 million. The majority of this revenue was passenger

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fares. The Port Authority increased fares to a \$2.50 base fare, which is one of the highest in the nation, effective July 1, 2012.

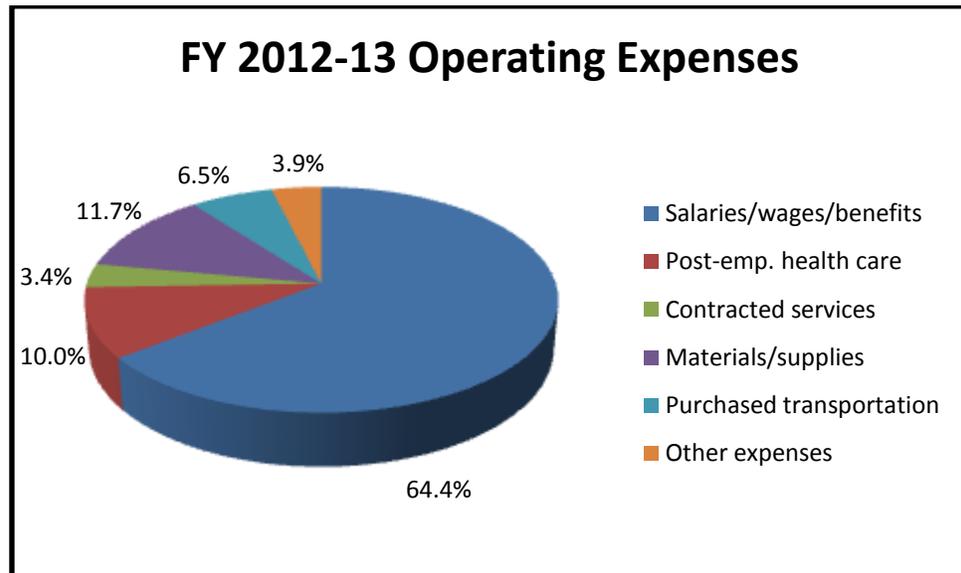
The Port Authority also received federal, state, and county operating subsidies and grants. For the fiscal year ended June 30, 2013, the Port Authority received \$161.8 million in state operating assistance. Historically, the state has contributed the largest portion of funding to the Port Authority. The following table shows the amount of state operating assistance provided to the Port Authority since fiscal year 2007-08³:



Expenses. During fiscal year 2012-13, operating expenses (excluding depreciation) amounted to \$386.8 million. Together, wages, salaries, and employee benefits amounted to \$249.3 million, or 64.4 percent, of total operating expenses (see the following chart). During fiscal year 2012-13, the Port Authority had a contractual wage freeze for employees represented by a union, which resulted in salary and wage expenses being lower than those of the prior fiscal year by approximately \$200,000. Other operating expenses include materials and supplies, purchased services, utilities, and ACCESS services.

³ State operating assistance to the Port Authority declined in fiscal year 2010-11 because the state anticipated tolling Interstate 80 and then allocating some of those toll revenues to the Port Authority. However, tolling for Interstate 80 was never authorized, and the state did not have other money available to allocate to the Port Authority.

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Port Authority's total expenses exceeded all revenue sources by \$75.7 million in FY 2012-13.

Even with all operating and non-operating revenues combined, the Port Authority completed the fiscal year ended June 30, 2013, with expenses exceeding revenues by \$75.7 million. (See *Appendix D* for a statement on the Port Authority's revenues, expenditures, and changes in net position for the fiscal years ended June 30, 2012, and 2013.)

Additional State Operating Assistance. As a result of the new labor agreement that the Port Authority and the ATU reached on August 8, 2012, the state promised the Port Authority a \$30 million operating supplement for each of the four years of the new labor agreement (FY 2012-13 through FY 2015-16).

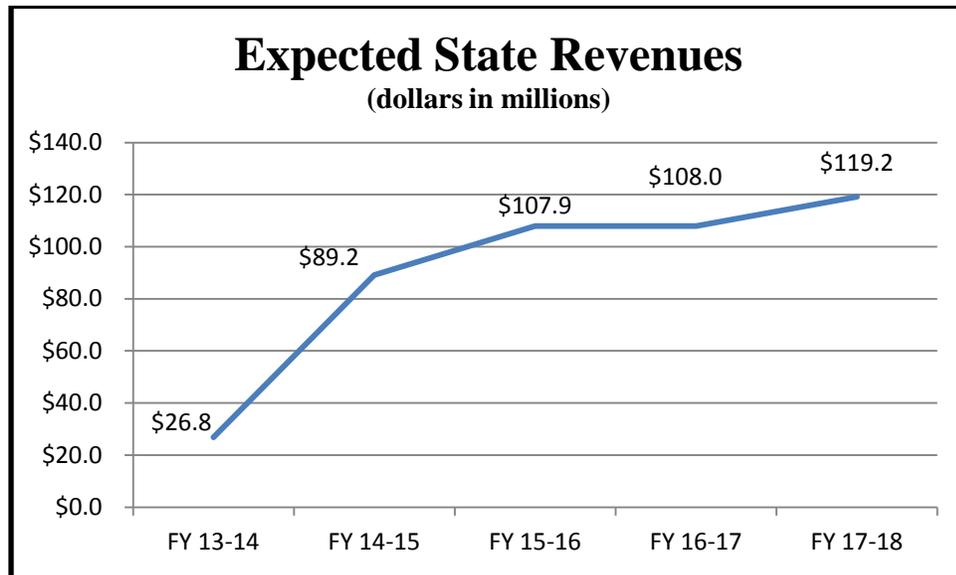
An October 2, 2012, letter from the Pennsylvania Department of Transportation (PennDOT) to the Port Authority stated "as part of PennDOT's participation in the Port Authority's recent labor negotiations and settlement, we agreed to provide an additional \$30 million annually for the life of the labor contract. It is understood that if the Commonwealth is unable to meet that obligation, the labor contract will be voided, returning to previous contract terms, and PAAC [Port Authority] will have to cut service to balance its budget."

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The Port Authority received the promised additional \$30 million in state funding in fiscal year 2012-13, and plans to do so for the next three fiscal years.

2013 comprehensive transportation funding package brings new revenues to the Port Authority

On November 25, 2013, a statewide transportation funding package (Act 89 of 2013), was signed into law. This legislation provides new revenues for roads, bridges, multimodal transportation, and mass transit, including the Port Authority. It is expected that the Port Authority will receive \$451 million from fiscal year 2013-14 through fiscal year 2017-18 in new revenues, broken down as follows:



According to Port Authority officials, with the addition of these new revenues, the Port Authority expects that it can move away from its financial crises and operating deficits and that it won't have to make additional service reductions in the foreseeable future. Further, with these new revenues, the Port Authority expects that it will be able to address capital projects designed to enhance services.

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Finding One → **The Port Authority did not comply with its own procurement requirements and did not implement FTA recommendations when awarding contracts.**

Key Points:

The Port Authority did not implement audit recommendations of the Federal Transit Administration (FTA) and did not comply with its own requirements including the following when procuring contracts:

- subcontractor debarment and suspension certification requirements
- subcontractor lobbying certification requirements
- sole source approval requirements
- public advertisement requirements

Summary

The Port Authority awarded nearly 900 contracts with a value greater than \$10,000 between July 1, 2007, and December 31, 2012, to purchase materials, goods, supplies, and services. The total combined value of these 900 contracts was

\$1.375 billion. The following table summarizes the contracts by type, number and total value:

Contract Type	Number	Total Value
Parts and materials	768	\$482.7 million
Professional services	68	\$428.6 million
Construction	38	\$464.0 million

We selected 46 contracts⁴ for a detailed review to assess whether Port Authority procurements were necessary, economical, transparent, and in compliance with applicable Port Authority policies and federal regulations.

We found that the Port Authority did not implement FTA debarment and suspension audit recommendations to ensure that three contractors were not debarred, suspended, or otherwise prohibited from entering into federally funded contracts. Further, the Port Authority did not comply with its own procurement requirements to ensure that 50 subcontractors were not debarred, suspended, or otherwise prohibited from entering into such contracts. The Port Authority also did not comply with its own procedures to ensure that 10

⁴ These 46 contracts were comprised of 22 parts and materials contracts, 15 professional services contracts, and 9 construction contracts. The Port Authority paid these contractors a total of \$33.1 million.

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subcontractors used by contractors it hired met all lobbying requirements for the proper use of federal funds. In addition, the Port Authority failed to follow its own requirements related to bid advertising for one contract and failed to adhere to all approval requirements when awarding another contract using the sole source procurement method.

The Port Authority's compliance with all applicable laws, regulations, policies, internal procedures, and any other requirements related to procurement and contracting is crucial to ensuring that the Port Authority is consistent in its procurement practices and takes appropriate action to eliminate the potential for fraud, waste, and abuse of its contracting monies.

Audit Results**The Port Authority did not implement debarment and suspension audit recommendations of the Federal Transit Administration when entering into contracts with three vendors.**

The U.S. Department of Transportation (USDOT) prohibits transit agencies, including the Port Authority, from awarding contracts to any party that is debarred, suspended, or otherwise excluded from participating in any program, including any procurement activity, which receives federal funds.⁵

According to the USDOT, a party may be suspended or debarred from participating in federally funded contracts for offenses such as fraud, antitrust violations, forgery, bribery, falsification of records, making false statements, making false claims, conspiracy, failure to comply with applicable environmental requirements, failure to pay the predetermined minimum wage, and other offenses indicating a lack of business integrity or business honesty that seriously and directly affects a person's or company's present responsibility.⁶

To comply with this federal requirement, the Port Authority obtained signed certifications from its prospective contractors that stated that the contractor and its principals were not presently debarred, suspended, proposed for debarment, or

⁵ See 49 C.F.R. § 18.35, as well as Executive Order 12549, issued February 18, 1986, and Executive Order 12689, issued August 16, 1989.

⁶ Refer to USDOT's summary of frequently asked questions regarding suspension and debarment at http://www.dot.gov/sites/dot.dev/files/docs/FAQ_11212012_0.pdf.

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declared ineligible for participation in Port Authority transactions by any department or agency of the federal government, the Commonwealth of Pennsylvania, or any other state.

However, the Federal Transit Administration (FTA) recommended an additional step that agencies, including the Port Authority, could take to ensure that no contract is awarded to a debarred or suspended entity. The FTA's guidance⁷ to recipients of federal assistance awarded by the FTA "strongly recommends" that agencies check the Excluded Parties List System (EPLS)—an electronic, web-based system that identifies those parties excluded from receiving federal contracts, certain subcontracts, and certain types of federal financial and non-financial assistance and benefits. The FTA also recommends that agencies check the EPLS even if they have collected a debarment and suspension certification from a prospective contractor.

In addition to this guidance, the FTA made specific recommendations to the Port Authority after it conducted a procurement system review of the Port Authority from March 27 to April 1, 2011. The report noted that 12 of 44 procurement files did not include "any verification of checking the Excluded Parties List System (EPLS) prior to award" and then recommended that the Port Authority adopt procedures to ensure that it documents it has checked the EPLS for all contracts exceeding \$25,000.

In its response to this review, the Port Authority acknowledged that the files were missing proper documentation and stated that it will review contract documentation "on a periodic basis to ensure compliance with the most recent FTA requirements and guidance."

We found that within weeks of the release of the FTA's 2011 report, the Port Authority awarded three contracts—each valued greater than \$25,000—without checking the EPLS, or at least documenting that it checked the EPLS. The Port Authority had no explanations as to why there was no evidence of EPLS searches for these three contracts.

⁷ Circular FTA C 4220.1F.

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Even though the Port Authority obtained debarment/suspension certifications from these three contractors, we believe the Port Authority should have followed the FTA's recommendations and taken the additional step of checking the EPLS to reduce the risk of contracting with a debarred or suspended entity. The Port Authority should then have maintained documentation of those checks in the contract files.

Suspension and debarment actions are designed to protect the government from doing business with entities that have been prohibited from participating in federally funded contracts for offenses such as fraud, forgery, and bribery. When the Port Authority fails to check the EPLS, it is not properly using the EPLS as an effective tool designed to reduce the risk that the Port Authority would enter into a contract with such a business.

The Port Authority did not comply with subcontractor debarment and suspension requirements for 26 percent of the contracts we reviewed.

The USDOT requires transit agencies, including the Port Authority, to apply the same suspension and debarment requirements to subcontractors as they do to contractors. The Port Authority has adopted procedures and designed its contracts to meet the USDOT's suspension and debarment requirements for subcontractors.

According to its own procedures, the Port Authority must obtain from the contractor a signed suspension and debarment certification for each of its subcontractors. Further, standard language in the Port Authority's contracts expressly requires the contractor to provide to the Port Authority signed certifications from each subcontractor that the subcontractor and its principals are not presently debarred, suspended, proposed for debarment, declared ineligible, or voluntarily excluded from covered transactions by any federal department or agency.

In our review of the 46 contracts, we found that the Port Authority did not consistently comply with these requirements. Specifically, we found that 12 contracts, or 26 percent, did not include any signed certifications from the 50 associated subcontractors. Further, we found that the Port Authority's contract files did not include evidence that the Port Authority

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conducted a search for any of the above 50 subcontractors on the EPLS at the time of the award of the applicable subcontracts. The Port Authority had no explanations as to why certifications were not obtained or the EPLS was not checked.

The Port Authority must make every effort to ensure that suspended and debarred companies do not participate in the agency's contracts. The failure of Port Authority staff to obtain signed subcontractor certifications and to search the EPLS exposed the Port Authority to the risks of fraud, waste, and abuse—issues that are to be mitigated when all debarment and suspension tools are used properly.

The Port Authority did not comply with subcontractor lobbying certification requirements for more than 10 percent of the contracts we reviewed.

The Port Authority must meet requirements related to lobbying when awarding contracts over \$100,000. Specifically, federal law⁸ prohibits a recipient of a federal contract, grant, loan, or cooperative agreement from using appropriated funds “to pay any person for influencing or attempting to influence an officer or employee of any agency, a member of Congress, an officer or employee of Congress, or an employee of a member of Congress” in connection with any covered federal actions. Further, contractors and subcontractors with contracts and subcontracts in excess of \$100,000 are required to certify that they have not made any such prohibited payments.

The Port Authority has deliberately worded its contracts to obtain assurance that no party to its contracts (i.e., both prime contractors and subcontractors) misuses federal funds. The standard language in the Port Authority's contracts expressly requires the contractor to provide to the Port Authority signed certifications from each subcontractor with a subcontract in excess of \$100,000. The declarations must state that the subcontractor has not made, and will not make, any lobbying payment prohibited by federal law. The Port Authority's procurement manuals also require the Port Authority to obtain from the contractor a signed lobbying certification for each subcontractor with a subcontract in excess of \$100,000.

⁸ 31 U.S.C. §1352.

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In our review of the 46 contracts, we found that 5 contracts, or nearly 11 percent, did not include the required certifications from the 10 applicable subcontractors. The Port Authority had no explanations as to why these lobbying certifications were not obtained and in the files.

The Port Authority should make every effort to ensure that it does not participate in any way with the misuse of federal funds. Accordingly, the Port Authority should ensure that it complies with its own mandates to obtain signed subcontractor certifications from its contractors.

The Port Authority did not comply with its own sole source procurement procedures for a contract awarded in 2011.

Included in our review of 46 contracts were four contracts that were awarded using the sole source procurement method. We found that the Port Authority did not follow its sole source procurement requirements when awarding one of those contracts. In October 2011, the Port Authority used the sole source procurement method to enter into a two-year \$31,880 contract for the regular calibration and maintenance of an under-floor wheel lathe.⁹ We found that this contract was awarded without proper management approvals and signatures.

Specifically, we found that the employee who signed the contract was only authorized to approve purchases valued at \$10,000 or less. The contract file did not include evidence that the sole source procurement was reviewed or approved by the applicable management personnel required by the Port Authority's purchasing procedures manual. Further, the contract file did not include any evidence that the legal department reviewed and approved the contract.

We also found that the contract document itself was prepared by the vendor. However, according to the Port Authority contract manager, "oftentimes, sole source vendors are inflexible as to the terms of their standard contract, and the buyer has little in the way of leverage to modify terms. The calibration and maintenance of the truing machine is essential to operations, and could not be provided by other vendors." What made this procurement process troubling was that the

⁹ The Port Authority purchased the lathe in 2001 for approximately \$1.2 million.

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contract file did not include evidence that the Port Authority's legal staff reviewed this vendor-prepared contract to ensure that all of the clauses, representations, and certifications required by the Federal Transit Administration were incorporated.

While the dollar value of this one contract may not appear to be significant relative to the total contract dollars expended by the Port Authority, the deviations from established internal controls are certainly significant. Adherence to procurement requirements, especially when using the sole source method, is critical to ensuring that the contracts are allowable, necessary, and economical.

The Port Authority did not comply with its public advertisement requirement for an invitation to bid issued in 2010.

Our review of the 46 contracts included determining whether Port Authority properly advertised bid invitations. We found one instance where the Port Authority did not follow its policy and procedures regarding the public advertisement for sealed bids.

On October 11, 2010, the Port Authority first publicly advertised its invitation to bid a contract (with an estimated cost in excess of \$200,000 for one year) for the installation, maintenance, and removal of transit advertising. On October 29, 2010, or 18 days later, the Port Authority publicly opened the two bids it had received.

The Port Authority's applicable procurement manual requires the Port Authority to advertise bid invitations for contracts with an anticipated value in excess of \$100,000 at least 30 days before the opening of the sealed bids. The purpose of the policy is to allow bidders sufficient time to prepare bids before the date of bid opening. Port Authority procurement staff acknowledged that the agency did not follow its policy in this instance; however, they did not provide an explanation for the shorter advertising period.

Although the Port Authority awarded this contract to the lower of the two bidders, the Port Authority's failure to allow for the full 30 days notice may have limited the pool of bidders

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because other potential bidders may not have had sufficient time to prepare bids. As a result, the Port Authority may have missed the opportunity to achieve better pricing for this contract.

Recommendations

1. The Port Authority should follow the FTA's audit recommendations and published guidance to check the EPLS prior to awarding any and all contracts exceeding \$25,000 to ensure that it does not contract with any suspended or debarred entity. Furthermore, the Port Authority should maintain documentation of such checks in its contract files.
2. The Port Authority must comply with its own stated policies and procedures, as well as ensure that contractors comply with the terms of its own contracts, regarding subcontractor certifications about lobbying and suspension and debarment to ensure that the Port Authority does not participate in any way with the misuse of federal funds or with entities that pose a business risk to the agency.
3. In order to encourage full and open competition in its invitations for bids, the Port Authority must comply with its own 30-day public advertisement requirement, in order to allow vendors sufficient time to prepare bids before the bid opening date.
4. The Port Authority must comply with its own stated procedures and ensure that all sole source procurements receive the required management oversight and approval, as well as legal review and approval, before the contracts are awarded.

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Finding Two → **The Port Authority made questionable decisions regarding some of its contracts.*****Key Points:***

- The Port Authority paid over \$60,000 to a contractor for a fare policy that the agency has yet to adopt.
- The Port Authority automatically extended a contract for equipment cleaner despite test results showing the product performed poorly.
- The Port Authority automatically extended two service contracts without any price comparisons to ensure it was still receiving the service at the lowest possible price.

Summary

Our review of 46 contracts found instances in which the Port Authority did not take adequate and appropriate actions to ensure it prudently spent its funds on various contracts.

Specifically, we found three instances where the Port Authority

automatically extended the terms of the contracts without sufficiently or appropriately evaluating product performance or researching current competitor pricing before authorizing the extensions. In one case, we found that the Port Authority extended the contract for a product that did not work (and may have caused adverse health effects), and in two other instances, the Port Authority may have paid more than necessary for other products or services. We also found, in a fourth instance, that the Port Authority paid a contractor more than \$60,000 for a fare policy, and then did not adopt that policy.

While the examples we found were not of a large enough dollar value to solve the financially-strapped Port Authority's fiscal issues, the Port Authority should review all of its expenditures and take all necessary actions to ensure it spends its revenues in the most prudent manner possible.

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Audit Results**The Port Authority paid over \$60,000 to a contractor for a fare policy that the agency has yet to adopt.**

In 2010, the Port Authority awarded a contract, valued at \$91,865, to a consultant¹⁰ to accomplish two primary objectives: 1) review the fare policy drafted by the Port Authority's own employees and provide strategies for improvement, and 2) develop a new fare model. The contract allowed for, and the Port Authority exercised, the option to extend the term of the agreement for an additional two years. The first of the two one-year extensions also increased the maximum amount of the contract by \$46,988 for a total value of \$138,853.

The Port Authority ultimately paid the contractor a total of \$102,688 (\$60,859 for the fare policy task and \$41,829 for the fare model task). Although the contractor developed and recommended both a fare policy and fare model pursuant to the contract terms, the Port Authority has only utilized the fare model. The agency has not adopted a fare policy. The discussion that follows focuses on the portion of the contract related to the development of a fare policy.

The contractor's proposal estimated that 138 contractor hours and 36 subcontractor hours would be necessary to accomplish the contract's fare policy tasks. The Port Authority had already devoted considerable staff time and resources toward the development of a fare policy, so it was expected that the contractor would review and make recommendations to improve that policy.

However in 2011, when the Port Authority approved the first of two one-year extensions to the contract, 188 additional hours of work related to the fare policy were added to the contract because the Port Authority was planning to recommend to its board of directors a move to a flat fare, proof-of-payment system, which would remove the existing two zone system.

In accordance with the terms of the contract agreement, the contractor made a fare policy presentation to the board of directors on October 11, 2011. However, as of November 2013, or over two years later, the Port Authority had not adopted a fare policy.

¹⁰ The selected contractor was the top rated of three proposers.

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In September 2013, we asked Port Authority management why the Port Authority had not yet adopted a fare policy. They stated that the agency had not yet adopted the policy due, at least in part, to senior management discord about the direction the policy should take. They also stated that fare policy discussions were on hold until a new chief executive officer was hired. On January 24, 2014, the Port Authority board voted to hire the agency's then interim chief executive officer to the same permanent position effective February 1, 2014.

Since there has been no action on a fare policy in over two years, when the Port Authority ultimately resumes fare policy discussions with its new CEO, the October 2011 policy recommendation may no longer be relevant and may not be useful. One of the most basic and fundamental measurements of the necessity or economy of a contract is whether the agency used the end product created by the contracted services. In this case, the Port Authority did not, leading us to question the agency's decisions to spend over \$60,000 for this consulting service if there was discord about the policy's direction.

The Port Authority automatically extended a contract for equipment cleaner despite test results showing the product performed poorly.

The Port Authority competitively bid and awarded a contract for equipment cleaner to the lowest of six bidders. The original agreement, valued at \$11,375, went into effect on September 8, 2011, with two one-year options to extend. As early as June 2012, Port Authority staff noted that product use had dropped dramatically and scheduled a product performance test. Two employees separately tested the product on September 4, 2012. One of these employees found its performance to be unacceptable for four of six different criteria; the other employee found the product's performance to be unacceptable for three of the same six criteria. Both employees recommended that the product be rejected.

On September 4, 2012, the quality assurance specialist sent an email to several members of the purchasing department as well as to a facilities manager and a bus maintenance manager, informing them that the performance field test was conducted. Although the email indicated that another cleaner worked more efficiently, the email did not report that both employees who

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conducted the test rejected the product currently under contract.

On November 8, 2012, the Port Authority extended the contract for both optional years and increased the maximum value of the contract to \$33,750. According to Port Authority officials, the agency extended the contract on November 8, 2012, without checking the actual results of the field performance test.

Just a few weeks after renewing the contract—on November 30, 2012—Port Authority health and safety personnel informed management that some employees complained that the equipment cleaner under contract had a bad odor, irritated their throats, and did not work as well as the product formerly used by the agency. When faced with poor performance *and* potential health effects to its employees, the Port Authority terminated the contract and returned eight drums of product in January 2013. In June 2013, the Port Authority received a refund check for \$2,002.

We believe that if the employees responsible for extending the contract had checked the actual performance test results prior to developing the November 8 change order, the agency could have avoided the inappropriate contract extension.

In summary, the Port Authority should not have extended the contract and continued to use the product after its performance was deemed unacceptable. Further, the automatic extension of the contract for a deficient product delayed the search for a new product and prolonged the use of a deficient product that was potentially harmful to employees.

The Port Authority automatically extended two service contracts without any price comparisons to ensure that it was still receiving the service at the lowest possible price.

HVAC and refrigeration maintenance services. In 2009, the Port Authority competitively bid and awarded a one-year contract with two optional one-year extensions for HVAC and

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refrigeration maintenance services to the lowest bidder.¹¹ The original contract value was \$133,875.¹² In 2010, the Port Authority extended the contract for a second year even though the contractor's original bid did not offer the lowest price for year two.

The contractor's overall bid price for year two was \$20,470 greater than the overall price for year two offered by its closest competitor in the 2009 solicitation. In fact, the contractor's bid price for the second year represented a 25 percent increase over its bid price for the first year, while the closest competitor's price for the second year involved only a 6.8 percent increase.

The Port Authority used the contract for a third year at an overall price that exceeded the third-year bid price offered by the closest competitor in the 2009 solicitation by \$21,900. Port Authority officials could only provide us with a copy of a memorandum dated August 15, 2010, that stated that "a phone survey of various firms" revealed that the contractor's current hourly rate for regular maintenance for the second year of the contract was "consistent with current market prices." However, the memo did not identify the vendors or their specific prices, and Port Authority's contract file did not include any evidence of a phone survey. Furthermore, Port Authority staff did not conduct a cost analysis or prepare a change order for the third contract year.

With regard to the overall price increase of 25 percent from the first to the second year, we found that the Port Authority had a policy in place to discourage such large price increases. According to its policy,¹³ the "Port Authority shall not exercise a Contract Option if, as a result of the inclusion of the Contract Option, the Contractor would no longer be the low bid as compared to the other bids received for this Contract."

When the Port Authority exercised the first option year of the contract with this vendor, it violated its own policy. The sum of the prices for the first and second years of this contractor's bid exceeded that of its closest competitor in the solicitation by

¹¹ The bids of the two competitors were considered to be technically non-compliant because neither competitor responded to a letter sent by the Port Authority (after the bid opening) requesting additional information.

¹² The Port Authority ultimately paid this contractor \$150,720 for all three years of the contract.

¹³ Procedure number PM-160 in the Port Authority's manual for the procurement of parts and materials, effective date June 1, 2001.

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\$15,975. While this competitor was ultimately found to be technically non-compliant because it did not answer the Port Authority's request for additional information, we believe the Port Authority was still aware that a competitor that offered lower prices existed. As a result, the Port Authority should have issued a new request for bids after the first year of the contract to ensure it contracted with the vendor offering the lowest price.

Transit advertising services. In late 2010, the Port Authority competitively bid and awarded a contract for the installation, maintenance, and removal of transit advertising to the lower of two bidders. The original contract, valued at \$224,160, included the ability for the Port Authority to exercise up to three optional years of service. The contractor's bid did not involve any price increase for the second through fourth years. Prices from the only other bidder were higher than those of the contractor for each of the four years.

In January 2012, the board authorized a one-year extension valued at \$224,160, citing the fact that the optional year did not involve a price increase. In January 2013, the board authorized a \$448,320 extension of the contract for the third and fourth years, again citing the absence of a price increase.

The Port Authority's contract file did not contain any evidence that the Port Authority conducted any research (including via Internet or telephone) in either 2012 or 2013 to confirm that competitors did not offer current pricing lower than that of the selected contractor. The number of available vendors and/or pricing may have changed since the public bid opening in October 2010.

In fact, documentation in the contract file noted that one vendor was unable to participate in the 2010 solicitation due to other contractual commitments. Additionally, new firms may have entered the market since 2010. Further, because the selected contractor provided unit rates for its bid (e.g., \$23 for the installation and \$8 for the removal of a king-size advertisement), a relatively quick comparison to current competitor pricing may have been very easy to do. When paying nearly a quarter of a million dollars a year for a service, a quick price comparison would have been a very prudent exercise for the cash-strapped agency to ensure it paid the lowest price possible.

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Recommendations

5. The Port Authority must not automatically extend contracts that were originally awarded based on lowest bid without first conducting a price comparison to ensure extending the contract would be the most fiscally prudent decision. Further, the Port Authority must document such a comparison in the contract file.
6. The Port Authority must timely and appropriately respond to product performance tests in order to avoid the automatic extension of contracts for poorly performing products.
7. The Port Authority must carefully evaluate its needs before awarding any contract or contract extension to ensure that it only spends money on products that it will use, as well as products that do not potentially harm its employees.

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Finding Three → **The Port Authority failed to adequately prepare contract bid proposals for two contracts, which led to change orders that significantly increased the cost of each contract and possibly resulted in other vendors not submitting bids.**

Key Points:

- Increased an electrical construction contract’s value from \$1.0 million to \$1.7 million, or 70 percent, because the Port Authority’s preliminary plan did not include all needed components.
- Increased a general construction contract’s amount from \$841,215 to \$1,361,215, or nearly 62 percent, because the Port Authority’s original plan was to “do a lower level of expense job.”
- Increased the possibility that other vendors did not submit bids because the bid documents failed to contain the exact parameters of the needed work under the contracts.

Summary

In our review of 46 contracts, we found two instances in which the Port Authority had to increase the value of its contracts after the contracts were awarded, because the Port Authority did not adequately state its full needs in its request for bids documents.

With one of the contracts, the Port

Authority’s board of directors questioned staff on the reasons for the increased costs. Port Authority staff answered that the original bid documents were based on cheaper methods of doing work. With the other contract, we could not find evidence that all pertinent Port Authority staff, especially operations personnel, made onsite visits to determine project needs until after the contract was awarded.

In both situations, the Port Authority selected a vendor based on responses to the inadequate request for bids documents. However, if those bid documents had contained more accurate descriptions of needed work, it is possible that other vendors could have submitted bids and that the Port Authority could have selected a lower costing contract. It is also possible that the existing bidders would have submitted different bids due to the larger size of the project.

Further, in the instance where the contract had to be increased because the Port Authority’s original bid document requested a

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cheaper level of work, the Port Authority paid for work results that were not satisfactory, and subsequently had to pay the contractor for additional work to get the job done right. In other words, the cheaper route was more expensive.

Audit Results

The Port Authority failed to perform sufficient “due diligence” in preparing a request for bids for electrical work which ultimately led to a 70% increase in the contract cost.

In March 2012, the Port Authority awarded a \$1 million contract to a vendor for general electrical construction for upgrades and improvements to property and facilities owned and/or operated by the Port Authority. The deliverables included transformer replacement and/or repair, wiring, conduits, junction boxes, breakers, and cabinets.

The bid documents for the contract specifically described work associated with the fare collection equipment site preparation at stations and locations throughout Port Authority’s light rail and bus systems. However, in July 2012, the Port Authority executed a change order that increased the value of the contract by \$700,000, to a sum of \$1.7 million, because the original description of this work was based on a preliminary layout of equipment for fare collection and that layout was no longer adequate.

Subsequent to the bid, key Port Authority staff, including operations personnel, conducted site visits at each location. Based on these site visits, Port Authority officials determined that equipment needed to be relocated at several stations and some new equipment needed to be added. In addition, they identified a need to increase some of the planned conduit and wire sizes to meet voltage drops and code requirements.

Due to turnover with staff involved with the preliminary layout for this project, current Port Authority officials could not state for certain the extent to which operations staff conducted site visits prior to developing the request for bids documents, but believed there was “some involvement” of former operations staff in the preliminary layouts.

However, they also commented that the Port Authority may have been able to make the layout revisions prior to bidding the

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contract if the former project director had a clearer vision of the project and that the preliminary layout would have been “closer to reality” if operations staff had been involved at the beginning of the project.

While we found that the Port Authority did not have to pay this contractor for any “rework,” our concern is that the Port Authority should have recognized the need to relocate equipment prior to the preparation of the bid documents, and then it could have issued a request for bids (RFB) that reflected the more exact project parameters. With the issuance of a different RFB, the possibility exists that other bidders could have responded, offering a lower contract cost, or the existing bidders would have submitted different bids due to the larger size of the project.

Port Authority’s attempt at doing a lower expense job ultimately resulted in a change order that increased the contract value by 62% or more than \$500,000.

In 2009, Port Authority awarded a general construction contract to a vendor for storm water separation and paving improvements to a large parking lot owned by the Port Authority. The original contract value was \$841,215.

A change order signed on June 11, 2010, increased the contract amount by \$520,000, or nearly 62 percent, because the original work the Port Authority requested did not meet the agency’s needs. Specifically, and for the most part, the Port Authority hired the contractor to repave three portions of a large parking lot using “mill and overlay.” However, after completing one portion of the lot, Port Authority officials decided that full depth paving of all three portions of the parking lot was needed.¹⁴

When asked by a board member why the contract value needed to be increased, the former CEO responded by indicating that the Port Authority was trying to keep expenses down.¹⁵

¹⁴ \$60,000 of the \$520,000 change order was for storm drainage channel remediation, which ultimately was not performed.

¹⁵ At this same meeting, the former CEO responded that the Port Authority was aware of the need for this project to be completed for approximately three years.

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The decision to go with a less expensive plan ultimately cost the Port Authority additional money because the work on the first portion of the parking lot had to be done over. Further, because the Port Authority knew for over three years that the lot needed work, it is reasonable to expect that the Port Authority should have known the actual condition of the parking lot and the type of work truly needed to make the lot safe and usable.

Recommendation

8. The Port Authority should adequately plan needed work before issuing request for bids documents. Such planning must include conducting all necessary and thorough site visits, ensuring adequate competition among vendors, monitoring of projects on a regular basis, and considering the potential effects of cheaper methods of work.

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Finding Four → **The Port Authority paid excessive relocation expenses of more than \$28,000 to one employee and failed to properly adhere to its relocation policy for two other employees, which cost the Port Authority nearly \$5,000.**

Key Points:

- The Port Authority paid more than \$28,000 in excessive relocation expenses to a new employee hired in 2009.
- The Port Authority did not enforce a key provision of its relocation policy for two other employees, which cost the agency nearly \$5,000.
- The Port Authority did not accurately account for relocation expense reimbursements, which would have cost the Port Authority \$4,300 if we had not notified the agency of the error.

Summary

In response to our prior audit recommendation, Port Authority implemented a relocation policy in November 2007. The policy states that “in the interest of attracting high quality employees,” the Port Authority may provide expense reimbursements to newly-hired full-time permanent employees

when moving from more than 50 miles from Allegheny County. The policy outlines allowable expenses, including travel costs for the employee and family members, household moving costs, and temporary board and lodging.

During our audit period, the Port Authority reimbursed six employees a total of \$48,174 for relocation expenses. We reviewed these expenses and found that the Port Authority paid excessive relocation expenses to one employee and then reimbursed this employee twice for the same lodging expenses. Moreover, the Port Authority did not adequately enforce its relocation policy for two other employees, costing the cash-strapped agency thousands of dollars.

We found that the Port Authority paid more than \$28,000 for one employee’s relocation expenses and while that amount was within the overall maximum allowed per the policy, we believe that the Port Authority was excessively generous when you consider the financial struggles of the agency. While limiting those expenses would not solve the financial strains of the Port

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Authority, such prudence would go a long way to show the public, including Port Authority customers, that the agency was taking appropriate measures to be fiscally responsible with taxpayer dollars.

We also found that the Port Authority lost \$4,749 by not enforcing a key provision of its relocation policy and jeopardized \$4,300 by not properly accounting for the payment of certain relocation expenses. Again, these amounts would not have changed the Port Authority's financial position, but rather, these discrepancies demonstrate the importance of the Port Authority appropriately accounting for every dollar it spends.

Audit Results

The Port Authority paid more than \$28,000 in excessive relocation expenses to a new employee hired in 2009.

The Port Authority reimbursed one employee \$28,695 for her move from Boston to Allegheny County when she was hired in 2009. These reimbursements included the following expenses:

New Hire Meeting:	
Lodging	\$1,129
Airline	\$ 463
Rental car	\$ 440
Meals	\$ 97
Miscellaneous	\$ 138
Total meeting	\$2,267
Moving:	
Movers	\$5,793
Airline	\$ 563
Moving supplies	\$ 329
Meals	\$ 143
Total moving	\$6,828
Transitional Housing:	
Lodging (for 5 months)	\$15,065 ¹⁶
Rental car	\$ 4,241
Personal mileage	\$ 294
Total Transitional housing	\$19,600
Total Relocation Expense Reimbursement	\$28,695

¹⁶ This amount includes a \$4,300 duplicate payment for lodging expenses described later in the finding, as well as an unidentified \$15 fee for the lodging in October 2009.

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The Port Authority's relocation policy states that the overall maximum of all relocation expenses, including lodging, should not exceed \$35,000. In addition, the policy states that the monthly maximum for temporary board and lodging is \$2,000 and that these expenses should not be paid for more than 60 days, unless approved otherwise by the CEO. In this case, the former CEO exercised the option to approve additional expenses that went beyond the policy. Specifically, this employee received a letter of employment signed by the former CEO which stated that the Port Authority would reimburse a maximum of \$35,000 in relocation expenses to include up to *six months* of temporary lodging, which is more than the 60 days stated in the policy.

While the relocation expenses paid to this employee did not exceed the overall maximum stated in the policy and the employment letter, we still believe the expenses were excessive, especially when compared to the relocation expenses reimbursed to the other five employees, which ranged from \$1,579 to \$8,405.

For example, this employee chose temporary lodging at a corporate apartment complex less than half of a mile from the Port Authority's headquarters, which cost \$2,150 a month. Both the lodging cost per month and the length of time that lodging was provided exceeded the standard limits of the policy. Furthermore, even though this employee was residing less than half of a mile from the office, Port Authority also provided her with a rental car for four months after her hire, which cost the agency an additional \$4,241.

While the former CEO provided for generous relocation expense reimbursements in the employment letter, no other documentation existed to justify the necessity of such a high level of expenses. Current Port Authority officials stated that all relocation expense reimbursement arrangements and approvals were made by the former CEO; thus, they could not offer any explanations other than to state that it was within the former CEO's discretion to offer and approve any enhancements to the relocation policy. Further, current Port Authority officials pointed out the value of this employee to the agency due to her 30-plus years of experience in the transit industry.

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Nonetheless, Port Authority officials stated that “in light of the concern that the auditors have brought to current Port Authority management’s attention,” the Port Authority has amended its relocation policy to say that if total relocation expenses exceed \$20,000, and/or if any exceptions to the policy are going to be offered to a candidate, the CEO has to document the justifications for same in a memorandum and receive the written concurrence of the board chairperson before such expenses can be authorized, approved, or paid.

The Port Authority did not enforce a key provision of its relocation policy for two other employees, costing the Port Authority nearly \$5,000.

The Port Authority’s relocation policy requires that when employees who were paid for relocation expenses resign from the agency within two years of hire, those employees must return a portion of the relocation reimbursement to the Port Authority. The Port Authority failed to enforce this provision in two cases, costing the Port Authority \$4,749.

Specifically, the relocation policy says that if an employee leaves the Port Authority within one year of hire, the employee must reimburse the Port Authority 100 percent of the relocation expenses. If the employee leaves between one and two years of hire, then 50 percent of the relocation expenses must be returned to the Port Authority.

We found that of the six employees that the Port Authority reimbursed for relocation expenses during our audit period, four of them resigned from their posts. In two instances, the resignations were within two years of employment, which meant that these employees should have refunded some of their relocation expenses to the Port Authority.

One employee was paid \$2,575 for relocation expenses for his move from Ohio, but less than two months later, this person resigned. As a result, he should have paid back the full \$2,575 relocation expense to the Port Authority. When we asked Port Authority officials if they attempted to collect this money, they told us that the employment letter for this employee did not include a clause requiring the refund of relocation expense reimbursements in the event the employee voluntarily separated from the Port Authority before two years of

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employment. Therefore, Port Authority's human resources office did not even request a refund.

The other employee was paid \$4,347 for his move from Maryland. He resigned from the Port Authority less than two years after his hire, which meant that he should have reimbursed the Port Authority 50 percent of his payment, or \$2,174. In this case, language regarding a refund was included in the employment letter but again Port Authority's human resources staff did not request a refund from the employee.

In both cases, the relocation policy was in effect at the time of hire and resignation, and therefore, the Port Authority should have ensured that the appropriate language was included in all employment letters and it should have enforced the policy and collected a refund. The failure of Port Authority officials to enforce the agency's own policy resulted in a \$4,749 loss to the Port Authority.

The Port Authority did not accurately account for relocation expense reimbursements, which would have cost the Port Authority \$4,300 if we had not notified the agency of the error.

As we discussed earlier in this finding, the Port Authority reimbursed an employee \$2,150 a month for five months of temporary housing. However, we found that the Port Authority reimbursed this employee twice for two months' lodging, which resulted in an overpayment of \$4,300.

This overpayment went unnoticed by Port Authority officials for more than two years until we discovered the error and brought it to the attention of Port Authority officials. These officials then contacted the employee and requested reimbursement for the double payment. We confirmed that the employee paid back the \$4,300.

While we were pleased to see the repayment of this duplicate reimbursement, the Port Authority should ensure that it has adequate procedures in place to more closely review all expenses to prevent double payments of any invoice.

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Recommendations

9. The Port Authority must adhere to its relocation policy and only reimburse employees for expenses within the prescribed maximums of the policy. In those cases where it believes it is reasonable to exceed such maximums, justification for such an exception from both the CEO and the board should be documented in the Port Authority's files.

10. The Port Authority must enforce its relocation policy provision requiring a refund to the agency in the event of an employee's resignation within two years of hire. Also, the Port Authority must consistently ensure that it includes appropriate language that details the provisions of the relocation policy in all employment letters.

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Finding Five

The Port Authority effectively planned and implemented its 2010 and 2011 changes to service routes, and it solicited and incorporated public input when making changes to service routes.

Key Points:

- The 2010 system-wide overhaul was based on a transit development plan that was well-reasoned and that included public input.
- The 15% service route cuts in 2011 were well-reasoned, and the Port Authority solicited and incorporated public input on those changes.

Summary

Between July 1, 2007, and December 31, 2012, the Port Authority implemented two major changes to its service routes—a system-wide overhaul in 2010 and a 15 percent service reduction in March

2011. We found that in both cases the Port Authority effectively planned the route changes. We also found that the Port Authority solicited and incorporated public input on the route changes during the planning process.

In addition, we found that the Port Authority currently evaluates and adjusts its service routes on a quarterly basis. According to Port Authority officials, these evaluations take into consideration driver input and rider complaints. Three of the quarterly service route adjustments involve moving trips or run times and changing stop locations. The other quarterly adjustment—typically in September—involves more significant changes, such as eliminating a route for which there is a replacement, adding a route, or moving route responsibility from one Port Authority garage to another.

Audit Results

The 2010 system-wide overhaul was based on a transit development plan that was well-reasoned and that included public input.

In November 2006, the Pennsylvania Transportation Funding and Reform Commission recommended that each transit agency across the state engage an independent transit expert to complete a full network design analysis at least once every five years. As a result, the Port Authority entered into a contract in

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2007 with a consulting firm to revamp the service routes in its system and to create a transit development plan (TDP). The Port Authority's system had not been reviewed in about 50 years.

It took the Port Authority nearly two years to finalize and implement the TDP. The two-year process included the following steps:

- Interviews of 59 stakeholders representing 29 different community and business organizations
- Market analysis of population, employment, and income trends
- Peer analysis of nine comparable transit systems
- Route-by-route evaluation to determine the strengths and weaknesses of the existing system
- Public input on the route evaluations
- Development and analysis of three overall service concepts, each of which consisted of a variety of changes to each route
- Public input on the three service concepts
- Final recommendations on route changes

We found that the Port Authority and its contracted consultant provided a reasonable rationale for each proposed route change. The most common reasons given for changing routes were low ridership and duplicative or complicated routes. The proposed changes were developed to improve productivity, to provide fast and direct service, and to simplify the names and nature of routes.

We also found that the Port Authority held over 60 different events, providing numerous opportunities for the public to participate in the planning process. Public input was gathered at open house events, a public hearing, a "planning" bus that brought agency staff and materials to community festivals and shopping centers, as well as meetings with local governments, non-profit organizations, and environmental groups.

According to documents we obtained and reviewed, over 2,700 members of the general public, Amalgamated Transit Union employees, agency scheduling staff, and consultant staff provided input through petitions, e-mails, comment cards/forms, and the TDP hotline.

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After obtaining public input, final recommendations on service route changes were developed, and these recommendations included modifications based on public comment.

In October 2009, the Port Authority board adopted the TDP; and in April, June, and September 2010, the Port Authority implemented significant portions of the planned overhaul.

The Port Authority implemented 15 percent service route cuts in 2011 because of the budget deficit, but again the Port Authority appropriately solicited and incorporated public input on those changes.

The Port Authority's projected budget for fiscal year 2010-11 estimated an operating deficit of \$47 million.¹⁷ As a result, the Port Authority initially planned—and in November 2010, its board approved—a 35 percent service route reduction which was to go into effect in January 2011. There was considerable public outcry over the planned service route cuts especially since those cuts were coming on the heels of the 2010 service changes.

Port Authority officials worked with state officials to come up with a plan to address this deficit. In December 2010, Port Authority received an additional \$45 million in state operating assistance. The deficit reduction plan also included a fare increase that was implemented in January 2011. With the additional state operating assistance and increased fare revenues, Port Authority officials were able to reduce the planned 35 percent service route reductions to a 15 percent reduction. These cuts were then implemented in March 2011.

We found that the Port Authority adopted a policy in 1984 that requires the Port Authority to solicit and consider public comments (primarily through a public hearing) prior to instituting a fare increase or major reduction in service. This policy defines a major service reduction as “a 30% or more reduction in transit route miles or transit revenue vehicle miles of one route.” In addition to soliciting comments at a public hearing, the policy also states that the public must “be given

¹⁷ A major factor contributing to this planned operating shortfall was the federal government's rejection of Pennsylvania's plan to toll Interstate 80. Revenues from those tolls were planned for allocation to the state's mass transit agencies, among other uses.

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the opportunity to submit written comments directly to the Port Authority.”

Since the Port Authority planned to adopt a fare increase and initially anticipated a 35 percent service reduction in January 2011, it held a well-publicized public hearing on August 19, 2010, and a public comment period from July 28 to August 31, 2010. According to Port Authority documents, more than 2,800 individuals provided more than 8,000 comments addressing the fare and service proposals.

As we stated earlier, the Port Authority ultimately cut service routes by 15 percent in March 2011. We found that the Port Authority’s planning process for these service cuts complied with the 1984 policy and appeared to be well-reasoned.

The Port Authority ranked its existing routes primarily according to registered average ridership¹⁸ and then on the basis of number of passengers per total vehicle hours. After soliciting public input, the agency cut 29 routes, based on eliminating duplicative routes, those with low ridership, and those with low passenger numbers per vehicle hour. The Port Authority retained several routes considered to be the sole source of bus service for the specific geographic area.

While any service route cut will impact specific individuals, we concluded that Port Authority took appropriate measures to minimize the impact to its overall passenger population.

¹⁸ Registered average ridership refers to the total ridership on the fare box for the month divided by the number of weekdays in the month.

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Finding Six

The Port Authority appropriately used annual Public Transportation Assistance Fund allocations to pay debt obligations.

Key Points:

- The Port Authority received \$211.7 million in PTAF monies from FY 2007-08 through FY 2011-12.
- The Port Authority used annual PTAF allocations for debt service payments in accordance with program requirements.

Summary

The Public Transportation Assistance Fund (PTAF) was established in 1991 as a dedicated funding source to provide operating assistance to mass transit agencies.

The PTAF was funded through a fee on the sale of new tires, a motor vehicle rental fee, and a motor vehicle lease tax.

In 2007, the Pennsylvania General Assembly implemented a major restructuring of mass transit agency funding when it repealed and replaced the PTAF enabling legislation with a new transportation funding law, Act 44 of 2007.¹⁹ Act 44 folded the PTAF into a newly created fund known as the Public Transportation Trust Fund. Act 44 provided that this new fund would receive all of the revenues that used to be deposited in the PTAF and that mass transit agencies, including the Port Authority, would continue to receive annual allocations of those revenues (still commonly referred to as PTAF allocations).

However, Act 44 stipulated that transit entities with outstanding debt obligations that were secured by PTAF revenues prior to 2007 had to use their annual PTAF allocations to pay those debt service obligations. Any monies from the PTAF allocations that were remaining after the debt payments were made could be used for operating assistance.²⁰

¹⁹ Act 44 of 2007 repealed 74 Pa.C.S. § 1301 *et seq.*, on July 18, 2007, retroactively effective July 1, 2007.

²⁰ Act 46 of 2010 amended The Fiscal Code to allow mass transit agencies that issued refunding bonds to pay the debt service of bonds financed with PTAF revenues to also use the annual PTAF allocations to pay the debt service of those refunding bonds. *See* 72 P.S. § 1601-G, enacted July 6, 2010, retroactively effective July 1, 2010.

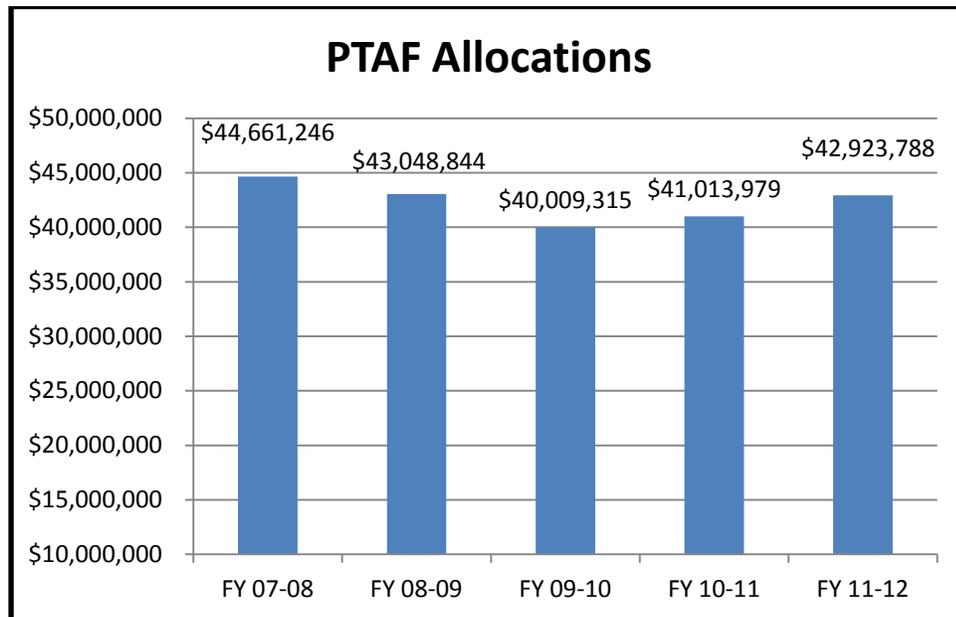
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Because the scope of our audit was July 1, 2007, through December 31, 2012, we examined the Port Authority’s use of PTAF allocations to ensure that those monies were used first for debt service, and then for operating assistance. We found that the Port Authority used its PTAF allocations properly during our audit period.

Audit Results

The Port Authority used annual PTAF allocations for debt service payments in accordance with program requirements.

During each of the fiscal years from July 1, 2007, through June 30, 2012, the Port Authority was allocated over \$40 million in PTAF monies, as shown below.



During that same time period, the Port Authority had the following four debt obligations. Three of these debt obligations were financed with PTAF revenues while the fourth debt obligation was related to refunding bonds that were issued to pay off debt financed with PTAF revenues. These four debt obligations were as follows:

- Subordinate Lien Special Revenue Transportation Bonds, Series of 1999. The proceeds from this bond sale were used to purchase buses and related equipment. These bonds fully matured in March 2009.

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- Special Revenue Transportation Bonds Refunding, Series of 2001. The proceeds from this bond sale were used to advance refund outstanding 1999 special revenue bonds.
- Special Revenue Transportation Bonds Refunding, Series of 2011. The proceeds from this bond sale were used to refund the 2001 series listed above, which were financed with PTAF revenues.
- Master Financing Agreement with Koch Financial dated March 28, 2003. The financing agreement was used to procure buses and bus parts between March 2003 and April 2007.

We reviewed the bank statements associated with these four debt obligations and found that the Port Authority used the PTAF allocations to make all of the required debt service payments. We also found that, as allowed by Act 44, the Port Authority used the PTAF allocations in excess of the required debt service payments for operating assistance. In other words, the Port Authority appropriately spent PTAF allocations during the fiscal years 2007-08 through 2011-12.

The following table shows the annual debt service payments made by Port Authority during our audit period:

Port Authority Debt service payments					
Debt obligation	FY 2007-08	FY 2008-09	FY 2009-10	FY 2010-11	FY 2011-12
Subordinate Bonds of 1999	\$12,572,405	\$12,576,655			
Special Revenue Bonds of 2001	\$13,635,075	\$13,636,875	\$19,750,832	\$19,749,706	
Refunding Bonds of 2011					\$22,083,917
Master Financing Agreement	\$16,902,469	\$16,902,469	\$16,902,469	\$16,902,469	\$16,902,469
Totals	\$43,109,949	\$43,115,999	\$36,653,301	\$36,652,175	\$38,986,386

Sources: Port Authority and U.S. Bank Trustee bank statements from July 1, 2007, through June 30, 2012.

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In examining the Port Authority's use of PTAF allocations, we also found that during fiscal year 1995-96, the Port Authority borrowed \$10.6 million from PTAF funds originally designated for capital purposes to use for operating expenses. Over a decade later, a February 28, 2008, letter from the Port Authority to the Pennsylvania Department of Transportation (PennDOT) stated that the Port Authority had not yet been able to pay back the borrowed amount because of operating cash shortfalls. As a result, there was an outstanding loan balance between the operating and PTAF capital accounts.

In December 2008, the Port Authority used unexpended supplemental operating assistance to repay the capital account loan. The Port Authority then used, with PennDOT's approval, the transferred \$10.6 million to purchase new buses.

This borrowing from the PTAF allocation appears to be an isolated incident, and as we stated earlier, the Port Authority properly used its PTAF allocations during our audit period.

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Observations

During our prior audit of the Port Authority, we found that the agency provided overly generous pension and health care benefits to its employees. We made several recommendations to address the issues associated with such generous benefits. As part of this current audit, we conducted procedures to determine if the Port Authority implemented our recommendations, and we are pleased to report that the Port Authority implemented the majority of our recommendations and reduced many of its employee benefits. The specifics of all of the changes that the Port Authority made are discussed in detail in the next section of this audit report (*Status of Findings from Prior Report*).

However, it is our observation that the Port Authority continues to make significant annual payments into its pension plans and for post-employment health care costs. In this section of the report, we present information on the annual payments the Port Authority made for these expense items each year of our audit period, as well as information on how benefit reductions impacted the payment amounts.

It is important to note that we did not audit the Port Authority's pension plans or its expenses related to post-employment health care costs. We did, however, review the Port Authority's annual *Single Audit* reports and its annual actuarial reports prepared for each of its three pension plans. We also interviewed the Port Authority's contracted actuary. The data presented in this section of the report is for informational purposes only, and we are not concluding on the financial status of the pension plans.

Observation One → The Port Authority has taken numerous actions to address its pension obligations; however, the generous benefits of the past continue to require significant payments from the Port Authority.

During the majority of our audit period, all full-time employees of the Port Authority were eligible to participate in one of three defined-benefit retirement and disability allowance plans. The three plans, which also provide post-employment health care benefits, are as follows:

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- Amalgamated Transit Union (ATU) Local 85 Plan
- International Brotherhood of Electrical Workers (IBEW) Local 29 Plan
- Plan for Employees Not Represented by a Union (NonRep)

As of January 1, 2012, the date of the most recent actuarial reports, the three plans combined had a total 5,817 active and retired participants. Of that number, 3,299, or 56.7 percent, were retired participants. Participation among the three plans is as follows:

	Active Participants	Retired Participants	% of Retired Participants
ATU Plan	2,179	2,769	56.0%
IBEW Plan	93	136	59.4%
NonRep Plan	246	394	61.6%
Total	2,518	3,299	56.7%

Effective September 1, 2011, no new employees were permitted to start participation in the NonRep Plan. Instead, they were enrolled in a defined-contribution plan. Current participants had the option to continue participation in the NonRep Plan or roll their current accumulated contributions to a Section 457 deferred compensation plan. This same change was made to the IBEW plan effective January 1, 2012.

These changes were just a few of the numerous amendments the Port Authority made in order to reduce its pension expenses.²¹ One of the more significant changes the Port Authority made was to its early retirement eligibility benefit.

In the past, the Port Authority permitted non-represented employees with only 25 years of service—regardless of age—to retire without any reduction in retirement benefits. This benefit proved to be quite costly considering that an employee could collect retirement benefits for 30 years or more.²²

²¹ For a more detailed discussion on historical benefits the Port Authority provided to employees along with recent reductions in those benefits, please see the section of this report titled *Status of Findings from Prior Report, Prior Finding 3*.

²² An employee who started employment with the Port Authority at age 18 could retire at age 43. The average life expectancy for a man living in the United States is 76 and for a woman is 81. Therefore, it is possible that a Port Authority retiree could collect pension benefits for well over 30 years.

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As a result, in fiscal year 2005-06, the Port Authority amended its early retirement eligibility requirement for new hires. Now, under all three pension plans, early retirement with full pension is available only to those persons who have 25 years of service and reach age 55.

Nonetheless, the Port Authority continues to have unfunded liabilities with its pension plans. As of January 1, 2012, the total unfunded liability of the three plans combined was \$153 million. Further, because the number of retired participants in the three plans surpasses the number of active members who make annual contributions into the plans, it will take decades for the Port Authority to reduce its total pension liability. In the meantime, the Port Authority continues to make a significant annual cash payment from its operating budget to its three pension funds.

The Port Authority paid \$19.4 million in 2012 into its three defined-benefit pension funds, a decrease of 34 percent over the \$29.5 million payment of the prior year.

The Port Authority's contracted actuary calculates an annual required contribution amount that the Port Authority should pay into each of the three retirement plans. This annual required contribution includes the amount needed for current year costs, as well as an amount for future payments.

According to the audited financial statements for each of the three pension plans, the Port Authority paid the full annual required contribution for each of its three pension plans for calendar years 2007 through 2012. The payments for each plan for those years are shown in the table that follows.

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Port Authority Annual required contributions to pension plans				
Calendar Year	Non-Rep Plan	ATU Plan	IBEW Plan	Three Plans Combined
2007	\$4,471,985	\$12,622,026	\$1,092,732	\$18,186,743
2008	\$3,687,745	\$9,908,915	\$381,249	\$13,977,909
2009	\$5,037,719	\$23,346,064	\$679,059	\$29,062,842
2010	\$4,734,816	\$17,480,911	\$477,378	\$22,693,105
2011	\$5,254,033	\$23,546,814	\$653,214	\$29,454,061
2012	\$4,674,158	\$13,984,742	\$774,764	\$19,433,664

Source: Independent auditor's reports prepared by MaherDuessel, Certified Public Accountants, for each of the three pension plans for the year ended December 31, 2012.

As this table shows, the Port Authority's pension contributions increased significantly in 2009, which was attributed primarily to the funds' investment assets experiencing losses with the 2008 financial market crash. In the years that followed, the annual contribution amount, as determined by the actuary, fluctuated to take into consideration the current conditions of the investment markets.

By 2012, the Port Authority's total pension contribution to these three plans decreased 34 percent over the 2011 year. This decline is primarily attributable to changes in the ATU plan as a result of a new bargaining agreement that went into effect in 2012. The changes that impacted the annual required contribution calculation included an increase in employee contributions from 5.5 percent to 10.5 percent, as well as a change in the asset valuation method. Specifically, the asset valuation method was changed from a five-year smoothing period to a ten-year smoothing period.

Even with these changes, the total 2012 pension payment of \$19.4 million represented over five percent of the agency's operating budget for FY 2012-13.

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Even with the pension benefit changes that the Port Authority implemented, all three of its pension plans were not fully funded as of January 1, 2012.

One of the most meaningful ways to show the Port Authority's pension liability is through the "funded ratio." This ratio compares a pension plan's actuarial value of assets to the actuarial accrued value of the liabilities. The annual trend of this ratio, when shown as a percentage, indicates whether a pension plan is getting financially stronger or weaker. Generally, the higher the percentage, the stronger the pension plan.

Funded ratios at or above 100 percent indicate that the pension plan can cover all payment obligations. Ratios below 100 percent show that a plan is unable to make payments or may be in jeopardy of not being able to make all required future payments. While no definitive standard exists for determining a "healthy" funded ratio, a 2007 Government Accountability Office report on government pension plans identified 80 percent and above as a marker for a healthy pension plan. Since the issuance of that report, that 80 percent threshold has become widely cited when discussing healthy funding ratios. Accordingly, we used the 80 percent as a benchmark when looking at the funded ratios of the Port Authority's three pension plans. The table below shows the funded ratio for the Port Authority's three pension plans for the past six years.

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Port Authority			
Funded ratio for each pension plan			
(Dollars in thousands)			
	Actuarial Value of Assets	Actuarial Accrued Liability	Funded Ratio
ATU Plan:			
01/01/07	\$706,909	\$754,026	93.8%
01/01/08	\$741,403	\$762,018	97.3%
01/01/09	\$624,449	\$774,856	80.6%
01/01/10	\$681,207	\$780,955	87.2%
01/01/11	\$660,428	\$801,542	82.4%
01/01/12	\$697,819	\$799,194	87.3%
Unfunded Liability as of 01/01/12:			\$101,375
IBEW Plan:			
01/01/07	\$20,798	\$23,774	87.5%
01/01/08	\$22,448	\$22,844	98.3%
01/01/09	\$18,565	\$23,613	78.6%
01/01/10	\$20,150	\$23,434	86.0%
01/01/11	\$19,236	\$24,031	80.0%
01/01/12	\$17,886	\$24,120	74.2%
Unfunded Liability as of 01/01/12:			\$6,234
NonRep Plan:			
01/01/07	\$68,634	\$107,269	64.0%
01/01/08	\$67,237	\$99,555	67.5%
01/01/09	\$57,197	\$100,652	56.8%
01/01/10	\$63,845	\$103,358	61.8%
01/01/11	\$63,616	\$107,279	59.3%
01/01/12	\$62,139	\$107,501	57.8%
Unfunded Liability as of 01/01/12:			\$45,362
Total Unfunded Liability, all 3 plans, as of 01/01/12:			\$152,971
Source: Independent auditor's report prepared by MaherDuessel, Certified Public Accountants, for each of the three pension plans for the year ended December 31, 2012.			

As this table shows, as of January 1, 2012, only the ATU pension plan's funded ratio is over the 80 percent benchmark for financial soundness. The table also shows that over the course of our audit period, each of the three plans' fiscal health was getting weaker as evidenced by the funded ratio as of

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January 1, 2012, being lower than the January 1, 2007, level for all three plans.²³

The NonRep pension plan is the most fiscally unsound with a funded ratio of only 57.8 percent as of January 1, 2012, which means that it is in a weaker financial condition and could be more likely to be unable to make payments in the future. As we stated earlier, the Port Authority has made its full required contribution to this plan over the past six years.

According to the Port Authority's actuary, the Port Authority implemented a new payment plan, beginning in 2013, to make annual required contributions at such a level that will allow the plan to be fully funded in 15 years. The 2013 annual required payment was estimated to be in the six to seven million dollar range. This new payment schedule assumes the plan's investments will earn at least a 7.25 percent rate of return after taking into consideration the fact that new employees are no longer permitted to enter this defined-benefit pension plan.

Along the same line, no new employees are permitted to join the IBEW defined-benefit plan. The Port Authority is aware that a new funding strategy may be necessary in order to sufficiently fund the plan, but the Port Authority cannot make any changes to the plan until a new bargaining agreement is negotiated.

²³ GASB Statement No. 68, *Accounting and Financial Reporting for Pensions*, establishes new accounting and financial reporting requirements for governments that provide employees with pensions. This change will require the Port Authority to record a "net pension liability" on its *Statement of Net Position* beginning in FY 2014-15. In essence, this net pension liability will represent the unfunded portion of pension funds. As of June 30, 2013, Port Authority management had not determined the impact that GASB 68 would have on its financial statements.

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Observation Two The Port Authority reduced post-employment health care benefits for new employees, but it will take years for this legacy cost to decrease since the Port Authority is obligated to pay current retirees for the generous benefits provided in the past.

In addition to providing a pension benefit, the Port Authority provides post-employment health care benefits to its retirees. Under all three retirement and disability allowance plans, post-employment health care benefits include medical, hospital, prescription, dental, and vision insurance coverage as well as Medicare Part B premium reimbursement.

The number of retirees in each of these plans as of January 1, 2012, the date of the most recent actuarial report, is as follows:

Retirement Plan	Number of Retirees
ATU Plan	2,769
IBEW Plan	136
NonRep Plan	394
Total	3,299

Benefit provisions for the ATU and IBEW Plans are established and amended through negotiations between the Port Authority and the respective union. The Port Authority's Board of Directors determines the benefits for persons in the NonRep Plan. During our audit period, the Port Authority changed the level of benefits provided in these three plans.²⁴

One of the more significant changes the Port Authority made was to reduce the length of time a retiree could receive post-employment health care benefits. With regard to the two union plans, as of July 1, 2012, new hires under the ATU Plan and, as of July 1, 2013, new hires under the IBEW Plan, were eligible for only three years of health care coverage at full retirement. Persons who were hired under those plans prior to those dates receive post-employment health care benefits for life.

²⁴ For a more detailed discussion on historical benefits the Port Authority provided to employees along with recent reductions in those benefits, please see the section of this report titled *Status of Findings from Prior Report, Prior Finding 3*.

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Even with these changes, the Port Authority continues to have significant annual expenses related to post-employment health care and will for years since it has to honor the agreements made with current retirees and continue to pay the generous benefits to those persons.

The Port Authority paid only for the current year costs for post-employment health care, which amounted to \$32.2 million in FY 2012-13, and opted not to make advance payments toward its future post-retirement health care costs.

Similar to the pension plans, the Port Authority's contracted actuary calculates an annual payment amount that the Port Authority should pay into each of its three post-retirement health care plans. This annual payment amount includes the amount needed for current year costs, as well as an amount for future payments.

However, unlike its pension benefits, the Port Authority did not make the full annual payment for its post-employment health care benefits during our audit period. Instead, the Port Authority made the minimal payment each year to fund only the current portion of the health care expenses for retirees.²⁵ According to Port Authority officials, the agency had not been in a strong enough financial position to make larger contributions.

The following table shows the total amount that the Port Authority paid for the current portion of its three post-employment health care plans each year since fiscal year 2007-08 and the percentage that those payments were to the annual required payment amount calculated by the actuary.

²⁵ Paying only the current portion of the annual payment amount is known as a "pay-as-you-go" contribution, and it is a common practice among governmental entities with regard to post-employment health care benefit plans. The Port Authority and other governmental entities are not required to make cash contributions to fund future payments.

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Port Authority Post-employment health care payments made and annual payment amounts ATU, IBEW, and NonRep Plans Combined			
Fiscal Year	Payment made (current expense only)	Annual payment amount (includes future payments) ^{1/}	Percent of annual payment amount paid by the Port Authority
2007-08	\$26,717,462	\$68,872,315	39%
2008-09	\$31,124,023	\$49,939,098	62%
2009-10	\$32,591,679	\$66,380,799	49%
2010-11	\$35,246,722	\$67,823,356	52%
2011-12	\$34,393,445	\$69,603,574	49%
2012-13	\$32,242,883	\$71,058,684	45%
<p>^{1/} The annual payment amounts are adjusted each year by the actuary to account for the ongoing obligation the Port Authority has accumulated because it does not fully contribute to the plan. The annual payment amount is adjusted for interest on that obligation and past under-contributions to arrive at the final amount shown here that should be contributed to fully fund the post-employment health care plans.</p> <p>Source: Port Authority of Allegheny County, Single Audit reports for the fiscal years ended June 30, 2008, through June 30, 2013, completed by MaherDuessel, Certified Public Accountants.</p>			

As shown on the table above, in fiscal year 2012-13, the Port Authority paid \$32.2 million for post-employment health care costs, which was only 45 percent of the \$71.1 million annual payment amount calculated by the actuary. This \$32.2 million payment, which paid only for the current year's post-employment health care expenses, represents 8.3 percent of the Port Authority's operating budget for fiscal year 2012-13. If the Port Authority had made the full \$71.1 million payment, it would have equated to 18.4 percent of the operating budget.

The Port Authority's accrued liability for post-employment health care costs amounted to \$240.7 million in fiscal year 2012-13, a 19 percent increase over the prior year level.

Each year that the Port Authority does not make the full annual payment for its post-employment health care plans, it reports an "OPEB expense" (other post-employment benefits) on its financial statements. This OPEB expense is the difference between the annual payment amount as determined by the Port

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Authority's actuary and the amount Port Authority actually contributed to its health care plans.

For fiscal year 2012-13, the Port Authority recorded a \$38.8 million OPEB expense on its *Statement of Revenues, Expenses, and Changes in Net Position*. Because OPEB expense must be recorded as an operating expense, the unfunded portion of the annual payment amount decreased the Port Authority's net worth.

Further, because the Port Authority did not fully contribute to each of its post-employment health care plans for years, the OPEB expense amount continues to grow each year. This accumulating cost is recorded each year on the Port Authority's *Statement of Net Position* as a liability, which in turn impacts the Port Authority's financial position.

As of June 30, 2013, the amount of the accumulated post-employment health care contributions that were not paid amounted to \$240.7 million, which was a 19 percent increase over the \$201.9 million level of the prior year.

This "OPEB expense" shows that the Port Authority has significant demands on its cash flows related to this benefit. Further, Port Authority's long-term liabilities for post-employment health care benefits remain a critical issue for the Port Authority's financial condition. Carrying these obligations is a real concern for the Port Authority, because the Port Authority wants to keep its commitment to retirees to pay promised benefits; however, it is getting more difficult each year to do so.

In addition, the liabilities related to these legacy costs are a real concern for the Port Authority because bond rating agencies, such as Standard & Poor's, view liabilities for post-employment health care benefits as debt-like in nature and take this obligation into consideration when rating bonds. Mitigating the concern over bond ratings is the fact that Port Authority officials told us the agency is in "maintenance mode" and has no plans to begin any new capital projects that would require the issuance of bonds.

We believe that the Port Authority should research its options in order to make advance payments toward its future post-retirement health care costs.

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Status of Findings from Prior Report

Released in December 2007, our previous quadrennial performance audit of the Port Authority covered the period July 1, 2002, through June 30, 2006, and resulted in five findings. Finding 5 was positive and thus had no recommendations. In response to the remaining four findings (Findings 1, 2, 3, and 4), we made 13 recommendations for improving the Port Authority's operations.

Generally accepted government auditing standards require auditors to evaluate whether the audited entity has taken appropriate corrective action to address findings and recommendations from previous engagements that are significant to the current audit objectives.²⁶

As part of our current audit, to determine whether the Port Authority implemented our December 2007 recommendations, we performed the following:

- Reviewed our prior audit report and corresponding working papers
- Interviewed pertinent Port Authority employees
- Obtained and analyzed the Port Authority's responses to our written requests for information
- Reviewed relevant Port Authority policies and procedures
- Conducted Internet research related to Port Authority's governance
- Examined and analyzed Port Authority documents and records

The scope of our review and audit work focused on the current audit period, July 1, 2007, through December 31, 2012, but we also considered all corrective actions taken by the Port Authority through December 31, 2013. The results of our work are presented in this section.

²⁶ Section 6.36, *Government Auditing Standards*, 2011 Revision, issued by the Comptroller General of the United States, United States Government Accountability Office, Washington, D.C.

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Prior Finding 1 **The governing body of the financially troubled Port Authority of Allegheny County has included local but no state appointees even though state taxpayers provide the most money to keep the Port Authority operating.**

Prior Finding: We reported that even though the state provided the largest portion of funding to the Port Authority, state officials did not appoint any members to the governing board (also known as the board of directors). Instead, the county executive of Allegheny County appointed all nine members to the board in accordance with the Second Class County Port Authority Act.

We emphasized that it was important for state officials to appoint members to the governing board so that the board could have a set of checks and balances in place that is inherent in a more diverse structure of governance. In addition, we stated that the Port Authority's governing board needed to include permanent representation by the state on behalf of state taxpayers, especially when the state was providing significant revenues to the financially troubled agency.

We concluded that the many problems that have existed for decades at the financially troubled Port Authority were directly related to the appointment process of board members by one elected official.

Recommendations: We recommended that the Governor and the General Assembly should each appoint two Allegheny County residents to the Port Authority's nine-member board, thereby giving the commonwealth four board seats in total. We also recommended that the county's chief executive should continue to appoint the remaining five board members but should ensure that at least one member represents downtown businesses and another represents riders with disabilities.

Port Authority's Response: Port Authority's management responded that the process for appointing board members is not controlled by the Port Authority's board or staff but is instead determined by the Second Class County Port Authority Act.

Status as of this Audit: During our current audit, Port Authority officials reiterated that the board's composition is

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determined by law. Therefore, the county executive continued to appoint all nine members to the board.

The current county executive, who was sworn into office on January 3, 2012, went beyond simply appointing board members by requesting undated signed resignation letters from each new board appointee. The county executive requested these letters from Port Authority board members, as well as from other county appointments, as a means to extend his control over legally independent boards and authorities.

In essence, those persons who signed these letters turned their votes over to the county executive; otherwise, they risked being forced out. One county council member said the letters “amount to a seizure of power by the county executive.”²⁷

Specific to the Port Authority, by February 1, 2013, the county executive had appointed four new members to the Port Authority’s governing board and obtained undated signed resignation letters from at least three of them. Those same four members voted to oust the Port Authority’s chief executive officer from his position after he refused to resign when the county executive asked him to do so. The fifth board member who also voted to oust the chief executive officer was subsequently named board chairman. The newly-named board chairman signed one of these letters, but the former chairman did not.

After criticism from county council members, among others, the county executive agreed on April 2, 2013, to destroy all the undated signed resignation letters he had obtained, including those for five Port Authority board members.

The use of these letters by the county executive underscores the importance of our prior recommendation that state officials must appoint members to the Port Authority’s governing board.

Certain members of our General Assembly responded to the controversy over these letters by introducing a bill to change how the Port Authority board appointments are made, and on

²⁷ Andrew McGill, “Undated resignation letters questioned at Allegheny County Council meeting,” *Pittsburgh Post-Gazette*, March 20, 2013.

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July 18, 2013, the Governor signed legislation that restructured the Port Authority's governing board.²⁸

This legislation changes the board size from 9 members to 11 members and limits the Allegheny County executive's appointment to only 6 members. The Governor and the legislative leaders from each of the four caucuses appoint the remaining five members. The Governor's appointee must be a Pennsylvania resident, while all of the other appointees must be residents of Allegheny County.

This legislation also requires two of the six members named by the county executive to come from a recommended list of candidates supplied by the following organizations: The Allegheny Conference, the Southwestern Pennsylvania Commission, the Committee for Accessible Transportation, and councils of government that have constituent members in the county. These two appointees are subject to confirmation by a majority vote of the members of the Allegheny County council.

This new legislation also provides checks and balances by placing rules on board actions related to adopting bylaws; appointing a chief executive officer; authorizing bonds, other borrowing, and leasing; and approving contracts over five million dollars. The legislation provides that these actions must be tabled upon motion and seconded by two of the four board members appointed by members of the General Assembly who are not of the same party affiliation as the county executive.

This legislation, which went into effect on July 18, 2013, does not prevent a former board member from being reappointed to the new 11-member board. As a result, six members from the former nine-member board were reappointed to the new board by the county executive.

With the enactment of this legislation and the changes it brings to the Port Authority's governing board, we consider our prior recommendations related to governance to be implemented.

²⁸ Act 72 of 2013, immediately effective, which amended Chapter 17 (relating to Second Class County Port Authorities) of Title 55 (Navigation) of the Pennsylvania Statutes, known as the Second Class County Port Authority Act. *See also* 55 P.S. § 556.

Port Authority of Allegheny County**Prior Finding 2**

The Port Authority was not accountable to taxpayers and, in fact, contributed to its own fiscal crisis by committing \$15.5 million to rent prime downtown office space unnecessarily.

Prior Finding: In 2000, the Port Authority signed a 10-year lease for \$7.8 million to rent two floors of the Heinz Center. The Port Authority also paid \$7.7 million to renovate and furnish the new space prior to moving in.

We noted that the Port Authority already owned a headquarters building in Manchester. The Port Authority did not sell that Manchester building but instead allowed some employees to continue to work out of it. The Port Authority spent \$4.7 million to refurbish the Manchester building in 1997, just three years before signing the new lease downtown.

While the Port Authority said it moved to the Heinz Center because it needed more space, we found that the Port Authority actually leased more space than it needed at the Heinz Center. At the time of the 2000 lease, a budget crisis was looming for the Port Authority. Less than a year after the Port Authority completed its move, it raised fares for the first time in 10 years

Recommendations: We recommended that the Port Authority should not renew or renegotiate the Heinz Center lease. We also recommended that Port Authority should take action to sublet the space at the Heinz Center or terminate the lease, and that it should return to the former headquarters building in Manchester, which the Port Authority already owns.

Port Authority's Response: In 2007, the Port Authority's management stated that staff was conducting a cost-benefit analysis regarding its headquarters site. The analysis included the estimated cost of rehabilitating the Manchester building, future maintenance costs of the Manchester building, and moving costs if the Port Authority moved from downtown back to the Manchester building. Management stated that the lease at the Heinz Center expired in 2010, and exiting the lease early would not be financially prudent since the Port Authority would still be responsible for fulfilling its rental agreement.

Status as of this Audit: Port Authority officials stated in a 2009 letter to the Department of the Auditor General that the

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agency had completed an in-depth engineering evaluation of the condition of the Manchester facility. The results of that evaluation showed that the Manchester building had major structural and health-related deficiencies, and the estimated repair costs amounted to \$20.6 million.

Using the results of that engineering evaluation, Port Authority officials conducted a financial analysis considering the following three options:

1. Completely renovate the Manchester building and vacate the Heinz Center.
2. Continue to lease office space at the Heinz Center and demolish part of the Manchester building.
3. Continue to lease office space at the Heinz Center and “mothball” the Manchester office tower.

This analysis revealed that it was most advantageous, from a cost perspective, for the Port Authority to continue to lease office space at the Heinz Center and to demolish part of the Manchester building.

On June 26, 2009, the Port Authority board authorized an extension on the Heinz Center lease for another 10 years at a total cost of \$10.6 million. On September 28, 2012, the board authorized the Port Authority to enter into contracts with various vendors for the demolition of part of the Manchester building.

As of September 30, 2013, the Port Authority had budgeted over \$9.4 million for this demolition. The scheduled date of completion for the demolition is April 2014.

As a result of our work, it was evident that the Port Authority did not implement our prior recommendations. However, we consider this issue to be resolved, since the Port Authority conducted an in-depth engineering evaluation and an extensive financial analysis in order to select the most cost-beneficial option related to these two buildings.

Because our primary concern was, and continues to be, accountability to taxpayers and the use of their dollars, the Port Authority must complete its demolition project on time and on budget. Further, the Port Authority must continually evaluate the costs associated with both leasing the Heinz Center offices

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and maintaining the remaining space of the Manchester building to ensure costs remain prudent and any unnecessary building costs are not passed on to Port Authority riders and taxpayers.

Prior Finding 3 The Port Authority gave excessive benefits to top executives, other staff, and retirees.

Prior Finding: We reported that the Port Authority showed poor judgment by spending taxpayer dollars to award excessive benefits to top executives, other staff, and retirees. We noted that the Port Authority awarded the excessive benefits prior to and during its fiscal crisis.

We reported that the Port Authority paid over \$1 million in benefits to its former chief executive officer that included reimbursement for his buy-back of prior service with the Port Authority, deferred compensation, sell-back of unused vacation time, and retirement benefits.

We also reported that the Port Authority provided excessive benefits to its top executives including awarding them extensive vacation time and then allowing them to sell some of it back each year for cash. Further, the Port Authority paid \$80,000 for the relocation expenses of two executives it hired.

Our prior report also discussed the excessive benefits the Port Authority granted to non-represented employees. The Port Authority's pension plan permitted non-union employees with only 25 years of service—regardless of age—to retire without any reduction in retirement benefits. Employees vested in this plan after only five years of employment.

This plan was revised on January 1, 2007, to restrict retirement eligibility to age 55 and 25 years of service for employees hired after December 1, 2005. However, the Port Authority allowed employees to buy back unlimited service from any public employer, including those in other states, and to count unused sick leave toward the 25-year threshold for full retirement.

Finally, we reported that the Port Authority provided overly generous benefits to its retirees which included providing post-

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retirement health care benefits for retirees until they qualified for Medicare at age 65 and paying all early retirees an extra \$500 a month until they reached the age of 62.

Recommendations: We made six recommendations related to this finding. Three of our recommendations related to the pension plan that the Port Authority had in place for non-represented employees. Specifically, we recommended that the vesting period should be changed from 5 years to 10 years, that unused sick time should not be counted towards the 25-year service threshold, and that only prior military service should be allowed to be bought back.

We made two recommendations related to retirees' benefits. We recommended that the Port Authority reduce the health care costs for management retirees and that it eliminate the monthly \$500 pension supplement it paid to early retirees.

The final recommendation we made called on the Port Authority to review its existing spending policies and practices and bring them more in line with prudent fiscal measures, including the practice of providing moving allowances.

Port Authority's Response: Port Authority management agreed with each of our recommendations and began to address them during 2007. Each of those actions is discussed in the "Status as of this Audit" section that follows.

Status as of this Audit: The Port Authority made several changes regarding employee benefits since our prior audit. The Port Authority addressed each of our recommendations, and it took additional actions to reduce employee costs. These changes included:

Chief Executive Officer

- Froze the base salary of \$180,000 until July 2009 when it was raised to \$185,000. Froze that new base salary through February 2013 when the chief executive officer departed.
- Discontinued the annual deferred compensation contribution effective July 1, 2007.
- Limited fringe benefits to the same benefits provided to other management staff effective January 1, 2008.

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Top Executives

- Froze salaries through June 30, 2008.
- Eliminated deferred compensation contributions effective July 1, 2007.
- Reduced the number of senior managers from eight to six.
- Implemented a relocation reimbursement policy on November 28, 2007. The policy requires receipts in order for the Port Authority to provide reimbursements. (See Finding Four for the concerns we had with relocation expenses paid by the Port Authority during our current audit period.)

Management Pension Plan (includes CEO and senior staff)

- Changed the vesting period from 5 years to 10 years effective July 1, 2007.
- Eliminated the option to purchase prior public service except for qualified military service effective July 1, 2007.
- Eliminated the crediting of unused sick leave toward continuous service for retirement purposes effective July 1, 2007.
- Changed the retirement plan effective September 1, 2011, so that all employees hired beginning that date were placed in a defined-contribution pension plan.
- Changed the employee contribution rate for non-union employees and transit police officers remaining in the defined-benefit pension plan from 4.5% of compensation to 10.5% effective October 1, 2012.

Other Management Changes

- Terminated the Deferred Retirement Option Plan (DROP) effective July 1, 2007.
- Increased health care contribution rate to 2% of base salary effective July 1, 2007, and to 3% of base salary effective July 1, 2008. The rate remained at 3% through December 31, 2012.
- Froze salaries in fiscal years 2008 (July 1, 2007, through June 30, 2008), 2011, 2012, and 2013. A 3% salary increase was granted in both fiscal years 2009 and 2010.

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- Froze wages for Port Authority's transit police from August 2009 through November 2011.

Non-Represented Retirees

- Eliminated post-retirement health care for those persons retiring after June 30, 2007.
 - For participants with at least 10 years of continuous service, the Port Authority began to provide a \$500 monthly supplement for up to five years during the period of retirement from age 60 to age 65 or until Medicare eligible, whichever occurs first.
- Eliminated the \$500 monthly pension supplement for early retirees effective July 1, 2007.

Union Staff

- Increased ATU Local 85 health care contribution rate from 1% to 2% of base wages effective January 1, 2009, and to 3% of base wages effective January 1, 2011.
- Changed IBEW retirement plan to a defined-contribution plan effective January 1, 2012, for all new hires.
- Adopted a new union agreement with ATU Local 85 effective from July 1, 2012, through June 30, 2016. This agreement includes the following:
 - Wage freeze until July 1, 2014.
 - Employee contribution to the defined-benefit pension plan was raised from 5.5% to 10.5% as of August 26, 2012.
 - Employees hired after July 1, 2012, will be eligible for up to a maximum of three years of retiree medical coverage.

In addition to the above-listed changes, the Port Authority eliminated 370 budgeted positions and instituted at least 203 layoffs by June 30, 2007. In March 2011, the Port Authority eliminated another 261 positions. While the Port Authority did not make these changes in direct response to our recommendations, these staff cuts reduced the Port Authority's expenses related to benefits.

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While the Port Authority took numerous actions to reduce the excessive benefits provided to staff by implementing each of our recommendations, legacy costs, which included retirement benefits and post-retirement health care payments, continued to impact the Port Authority's financial condition. (See Observations One and Two for more information.)

Prior Finding 4 The Port Authority poorly planned or poorly implemented three of its most significant capital projects undertaken during the past ten years.

Prior Finding: The Port Authority either completed or started at least three major public transportation projects under its \$1 billion Major Capital Investment Program during our prior audit period. The three major projects included the following:

- The opening of the West Busway in September 2000 and the associated Wabash Tunnel in December 2004.
- The opening of the Stage II Light Rail Transit in June 2004 and the associated South Hills Village parking garage in May 2005.
- The start of construction for the North Shore Connector project in late 2006.

We reported that the Port Authority poorly planned or poorly implemented these three projects, which resulted in increased spending from the Port Authority's capital and operating budgets when the Port Authority could not afford such spending.

Specific to the West Busway/Wabash Tunnel project, we reported that even though the Port Authority removed two crucial project design components, the Port Authority still extended the project completion timeline by at least three years. We also reported that the Port Authority entered into a one-year contract to pay \$575,000 for the maintenance and operation of the tunnel from its operating budget. In addition, we reported that the Wabash Tunnel traffic volume had not met estimates, and the Port Authority itself did not use the tunnel for its own revenue-generating vehicles.

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With regard to the Stage II Light Rail Transit project, our work focused on the South Hills Village parking garage. We reported that the Port Authority unnecessarily built two levels in that garage, incurring \$4 million additional debt.

Regarding the North Shore Connector project, we reported that the Port Authority deferred the acquisition of four new light rail vehicles, and it eliminated the design and construction of the Convention Center line and station. The savings affiliated with these eliminations subsidized the rising costs to tunnel under the river, and at the same time, camouflaged the actual amount of the project's rising costs.

Recommendations: On a broad scale, we recommended that the Port Authority must significantly improve any requests for capital project approval and funding from the state and federal government. We also recommended that the Port Authority should not exceed the stipulations of its Full Funding Grant Agreements for future capital projects. At the same time, the Port Authority should take into account the impact of incurring additional debt on operating funds, particularly at a time when the Port Authority is operating at a deficit.

Specific to the Wabash Tunnel project, we recommended that the Port Authority should immediately and thoroughly evaluate alternative solutions to the underuse and excessive operating costs of the Wabash Tunnel and promptly take the appropriate steps to implement its identified solution.

With regard to the North Shore Connector project, we recommended that the Port Authority should carefully plan and budget the remainder of the North Shore Connector project to ensure the timely completion of all fundamental project components without additional cost overruns.

We did not make any recommendations specific to the Stage II Light Rail Transit project and the associated South Hills Village parking garage.

Port Authority's Response: Port Authority management responded that the Port Authority follows all aspects of the federally-prescribed planning process for capital projects, which includes extensive public input, federal oversight, and years of study, planning, design, and engineering.

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Port Authority management also stated that the Port Authority would be taking over operation and maintenance of the Wabash Tunnel beginning January 1, 2008, and management would be looking for ways to increase usage of the tunnel.

Further, Port Authority officials stated that Port Authority continues to promote the use of the South Hills Village garage. In addition, Port Authority entered into a revenue-generating lease agreement with Giant Eagle for 250 spaces.

The Port Authority's response did not specifically mention the North Shore Connector project.

Status as of this Audit: With regard to our recommendation related to the Wabash Tunnel, the Port Authority took over operations and maintenance of the tunnel on January 1, 2008, as planned. According to Port Authority officials, the annual operating and maintenance costs for the tunnel amount to approximately \$134,000, which includes nearly \$27,000 for the transit police force.

These annual operating costs are significantly lower than the one-year maintenance contract of \$575,000 that the Port Authority put in place during our prior audit. As a result, the Port Authority reports that it is saving about \$441,000 annually in its operating budget by operating and maintaining the Wabash Tunnel with its own employees.

To help offset the operating and maintenance costs of the Wabash Tunnel, the Port Authority entered into a two-year agreement effective January 1, 2010, to lease the Wabash surface parking lot. The Port Authority extended the lease agreement through December 31, 2013. Annual lease revenue was \$158,875 in 2012, and it is expected to amount to \$162,847 in 2013.

With regard to usage of the Wabash Tunnel, the Port Authority did not use any of its revenue-generating vehicles in the tunnel for regularly scheduled service during our current audit period. Port Authority officials stated that it does not make sense for the Port Authority to deviate its South Hills bus routes off the West Busway to travel through the Wabash Tunnel.

Usage of the tunnel by non-Port Authority vehicles has not reached planned levels. However, the Port Authority is not in a

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position to close the tunnel for underuse because if it were to close the tunnel prior to the end of its useful life, the Port Authority would have to reimburse the federal government for a portion of the remaining value of the tunnel.

Based on the results of our audit work, we have concluded that the Port Authority implemented our recommendation to take action to reduce the operating costs of the Wabash Tunnel. While usage has not met expectations, the Port Authority has found a solution to generate enough revenues to cover the tunnel's operating expenses. We would encourage the Port Authority to continually search for opportunities to minimize the costs of tunnel operations while finding ways to maximize tunnel usage.

With regard to the North Shore Connector project, Port Authority officials completed the construction of the two tunnels under the Allegheny River in March 2012. The Port Authority's budget for that project was \$435 million. However, final project costs amounted to \$517 million. In order to finance this \$82 million cost overrun, the Port Authority used \$63.5 million in federal funds and \$15.2 million in additional discretionary state funds, with the remainder coming from Allegheny County and miscellaneous grant programs.

During our current audit, Port Authority officials stated that the Port Authority does not plan to accomplish the deferred aspects of the North Shore Connector project. If the Port Authority were to decide to complete this project, we would recommend that the Port Authority more carefully plan and budget the project to ensure timely completion and to avoid cost overruns.

With regard to our broad recommendations related to capital project approvals and exceeding Full Funding Grant Agreements, Port Authority officials stated that the Port Authority has not started any new capital projects, and in fact, the agency has moved from system expansion to system preservation and improvement. As a result, the Port Authority did not have the opportunity to implement these recommendations during our current audit period.

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Appendix A**Objectives,
Scope, and
Methodology**

The Department of the Auditor General conducted this performance audit in order to provide an independent assessment of specific operations of the Port Authority of Allegheny County. We conducted this audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

Objectives

Our performance audit objectives were as follows:

- To assess capital projects funding, including but not limited to the issuance of bonds and debt service payments. Audit work focused on the Port Authority's receipt and use of Pennsylvania Transportation Assistance Fund monies.
- To determine the Port Authority's board of directors' governance structure, including but not limited to the board composition. Our audit work included following up on the implementation of the recommendations made related to governance during our prior audit of the Port Authority (released December 2007).
- To evaluate the Port Authority's contract procurement and monitoring processes.
- To review the Port Authority's service routes planning and scheduling process. Audit work focused on service route changes made in April, June, and September 2010 and March 2011.

In addition to the four objectives, we planned to conduct an analysis of the Port Authority's revenues and expenditures. In analyzing the Port Authority's expenditures, we planned to review expenses related to retirement and post-employment health care benefits.

In addition to governance, we also planned to follow up on the implementation of the other recommendations made during our prior audit of the Port Authority, which included the areas of

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office leases; excessive benefits to top executives, other staff, and retirees; and poorly planned and implemented capital projects.

Scope

This audit report presents information for the period of July 1, 2007, through December 31, 2012, unless otherwise indicated.

Port Authority of Allegheny County management is responsible for establishing and maintaining effective internal controls to provide reasonable assurance that the Port Authority is in compliance with applicable laws, regulations, contracts, grant agreements, and administrative policies and procedures. In conducting our audit, we obtained an understanding of the Port Authority's internal controls, including any information systems controls, as they relate to those requirements and that we considered to be significant within the context of our audit objectives. We assessed whether those controls were properly designed and implemented. Any deficiencies in internal control that were identified during the conduct of our audit and determined to be significant within the context of our audit objectives are included in this report.

Methodology

To address our four audit objectives, we performed the following procedures:

Pennsylvania Transportation Assistance Fund:

- Interviewed the director of grants and capital programs.
- Obtained and reviewed the Port Authority's Single Audits for the fiscal years ended June 30, 2008, through June 30, 2013, as well as the audit report prepared by Arthur Andersen for the fiscal year ended June 30, 1996.
- Obtained and analyzed Pennsylvania legislation regarding transportation funding, including Act 26 of 1991, Act 44 of 2007, and Act 46 of 2010.
- Obtained and reviewed the official statements, including the debt service schedules, for the bond series issued in 1999, 2001, and 2011.

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- Obtained and reviewed the debt service schedule for the Master Financing Agreement (formerly the Koch agreement) for the procurement of buses.
- Obtained and reviewed letters from the Pennsylvania Department of Transportation (PennDOT) to the Port Authority documenting PTAF payments made to the Port Authority for the fiscal years ended June 30, 2008, through 2012.
- Obtained and analyzed Port Authority and U. S. Bank Trustee bank statements associated with the agency's debt obligations from July 1, 2007, through December 31, 2012.

Governance:

- Reviewed the Port Authority's enabling legislation, as well as Act 72 of 2013, which amended the Second Class County Port Authority Act upon its enactment on July 18, 2013.
- Obtained and reviewed various media articles discussing the county executive of Allegheny County's request for undated signed resignation letters from the Port Authority's board members and other county officials.
- Discussed the undated signed resignation letters with the two former chairmen of the Port Authority's governing board during the period from July 1, 2008, through September 27, 2013.

Contract Procurement and Monitoring:

- Interviewed procurement management personnel (including the director of purchasing and materials management and three contract managers) and staff from the accounting department to obtain an overview of the procurement process.
- Obtained and reviewed summaries of the Port Authority's stock item purchase process, Request for Bid (RFB) process, and Request for Proposal (RFP) process prepared by the agency's director of internal audits.

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- Obtained and reviewed Port Authority policies and procedures related to procurement, including manuals regarding the solicitation and administration of contracts for professional services, construction, and parts and materials as well as policy statements regarding bid protests, disadvantaged business enterprises, and purchasing approvals.
- Reviewed federal laws, regulations, and executive orders related to the procurement and administration of contracts.
- Reviewed the Federal Transit Administration (FTA) Circular 4220.1F, *Third Party Contracting Guidance*, issued November 1, 2008, and revised April 14, 2009, July 1, 2010, February 15, 2011, and March 18, 2013.
- Reviewed the FTA's July 2011 report of its review of the Port Authority's procurement system conducted from March 27 to April 1, 2011.
- To evaluate the validity and reliability of the Port Authority's three computer-generated lists of contracts valued over \$10,000 and executed between July 1, 2007, and December 31, 2012, we conducted the following procedures:
 - Compared the board-approved contracts found in the board meeting minutes from January 1, 2010, to December 31, 2012, to the Port Authority's three contract lists.
 - Obtained a list by vendor for the expenditure line item called "purchased services" in the Statement of Revenues, Expenses, and Changes in Net Position in the Port Authority's Single Audits for each fiscal year from July 1, 2010, through June 30, 2012, in order to determine if the vendors included in the Single Audit were the same vendors included on the contract lists.
 - Interviewed Port Authority's director of information technology services regarding our review of the FTA's January 7, 2011, report of its financial management oversight review of the Port Authority for the period from November 1, 2009, through October 31, 2010.

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- Obtained and reviewed 40 contract files (which included documents associated with 46 individual contracts) for detailed testing.
- Obtained and evaluated detailed information about the solicitation, administration, and monitoring of the 46 individual contracts from the following Port Authority personnel: the director of purchasing and materials management, three contract managers, the interim chief financial officer, the assistant general manager of engineering and technical support, the director of technical support and capital programs, the assistant director of capital programs, and the DBE contract compliance officer.

Service Routes:

- Interviewed the director of service planning and evaluation.
- Obtained and reviewed Port Authority policy regarding the public hearing process for fare increases and major service reductions.
- Obtained and reviewed reports prepared by the Port Authority's transit service consultant in order to create the agency's transit development plan (TDP), including summaries of the stakeholder interviews, market analysis, peer analysis, route-by-route evaluations, service concepts, and public involvement program.
- Analyzed the TDP's service concepts and recommendations to determine whether the Port Authority and its consultant provided a rationale for each proposed route change.
- Obtained and reviewed a Port Authority executive summary of the public process, materials available at the September 15, 2009, public hearing, and public comments associated with the TDP.
- Obtained and reviewed TDP documents presented to the Port Authority board's planning and development committee on October 21, 2009, and to the entire board on October 23, 2009. The documents included, in part, the board resolution adopting the TDP, an overview summary of public participation during the Port Authority's formal

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comment period, final TDP recommendations and changes following the public comment period, a service coverage map, and the general framework for TDP implementation.

- Obtained and analyzed statistics used to cut service routes in March 2011 to determine the basis for these cuts, such as duplicative routes and low ridership.
- Obtained and reviewed a Port Authority executive summary of the public process, materials available at the August 19, 2010, public hearing, and public comments associated with the proposed 2011 fare increase and service reduction.
- Examined summaries of the Port Authority's quarterly service changes implemented between July 1, 2007, and December 31, 2012.

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Appendix B Ridership Statistics of the Port Authority of Allegheny County

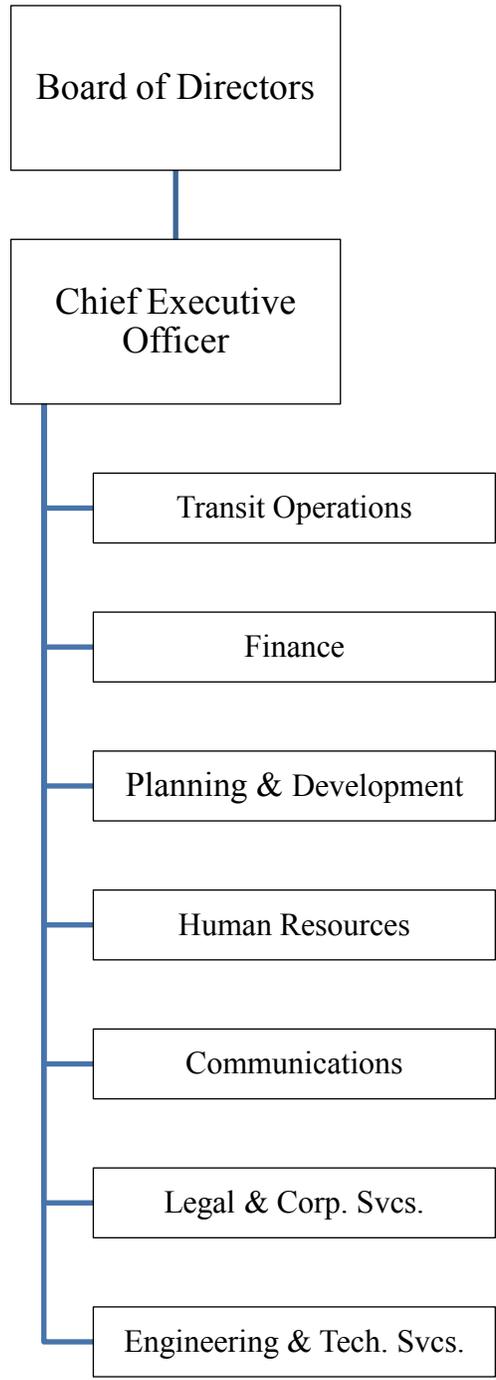
Port Authority of Allegheny County Ridership Statistics FY 2007-08 through FY 2012-13 ²⁹						
Transit Service	Fiscal Year 2007-08	Fiscal Year 2008-09	Fiscal Year 2009-10	Fiscal Year 2010-11	Fiscal Year 2011-12	Fiscal Year 2012-13
Bus, Light Rail, Incline	50,685,856	51,143,088	49,395,535	47,179,095	49,771,724	47,327,079
Contract Services	7,085,301	7,484,010	7,068,430	7,423,470	7,410,453	7,542,272
Senior Citizens	5,970,729	6,147,990	5,818,655	5,325,842	5,042,824	4,895,348
ACCESS	1,693,648	1,699,537	1,651,372	1,722,354	1,769,543	1,716,098
Free Ridership	1,842,570	1,756,092	1,752,589	1,692,126	1,869,312	2,377,168
Total Ridership	67,278,104	68,230,717	65,686,581	63,342,887	65,863,856	63,857,965

²⁹ Developed by Department of the Auditor General staff from data obtained from the Port Authority's Single Audit reports for the fiscal years ended June 30, 2008, through June 30, 2013

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Appendix C

Organization Chart of the Port Authority of Allegheny County



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Appendix D**Statements of Revenues, Expenses, and Changes in Net Position, Fiscal Years 2011-12 and 2012-13, of the Port Authority of Allegheny County³⁰**

	<u>FY 2012-13</u>	<u>FY 2011-12</u>
Operating Revenues:		
Passenger fares	\$89,761,603	\$86,817,780
State shared ride program	12,374,391	11,900,227
Advertising	1,541,524	1,458,982
Miscellaneous income	<u>537,730</u>	<u>1,237,454</u>
Total operating revenues	<u>\$104,215,248</u>	<u>\$101,414,443</u>
Operating Expenses:		
Salaries and wages	\$134,122,043	\$134,319,383
Fringe benefits	115,173,736	127,874,411
OPEB expense, net	38,815,801	35,210,129
Services	13,134,626	10,040,841
Materials and supplies	45,338,931	46,739,749
Purchased transportation	25,154,899	26,184,443
Other expenses	15,084,728	16,920,183
Depreciation	<u>118,525,155</u>	<u>107,340,363</u>
Total operating expenses	<u>\$505,349,919</u>	<u>\$504,629,502</u>
Operating Loss	<u>(\$401,134,671)</u>	<u>(\$403,215,059)</u>
Non-Operating Revenues (Expenses)		
Capital funds used for		
Operating Assistance	\$ 52,928,770	\$ 69,590,302
State operating grants	161,756,198	165,037,154
Local govt. operating grants	30,518,699	27,668,700
Interest expense	(14,072,466)	(14,934,382)
Capital Grant Funding	<u>94,329,345</u>	<u>139,116,306</u>
Total non-operating revenue	<u>\$325,460,546</u>	<u>\$386,478,080</u>
Change in Net Position	(\$75,674,125)	(\$16,736,979)
Total net position, beginning, restated	<u>\$1,085,778,110</u>	<u>\$1,102,515,089</u>
Total net position, ending	<u>\$1,010,103,985</u>	<u>\$1,085,778,110</u>

³⁰ Developed by Department of the Auditor General staff from the Port Authority's Single Audit report for the fiscal year ended June 30, 2013.

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**Response from
Port Authority
of Allegheny
County**

The following pages contain the Port Authority of Allegheny County's entire response to this audit report. The Port Authority responded to each subsection within Findings One through Four. After each of the Port Authority's responses, we have inserted our evaluation of the Port Authority's responses. The Port Authority did not provide responses to Findings Five and Six or to the two observations contained in the report.

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**PORT AUTHORITY OF ALLEGHENY COUNTY'S RESPONSE TO DRAFT
REPORT OF THE PENNSYLVANIA DEPARTMENT OF THE AUDITOR
GENERAL****Introduction**

On January 31, 2014 Port Authority of Allegheny County (PAAC) was provided with a draft report of the Pennsylvania Department of the Auditor General, Bureau of Special Performance Audits (SAG) regarding SAG's on-site Performance Audit of PAAC that began in March, 2013 and concluded in December, 2013. Subsequently, following submission of initial comments that PAAC provided to the draft report on February 14, 2014 and an exit conference that occurred between PAAC and SAG personnel on February 19, 2014, SAG provided PAAC with updated versions of certain portions of the draft report. PAAC has been directed to provide its final comments in response to the draft report, as amended, by February 24, 2014. In compliance with this directive, PAAC submits the following response to the draft report, with respect to findings one through four that set forth corrective recommendations. PAAC wants to initially acknowledge and thank SAG personnel for making adjustments to certain portions of the report in response to PAAC's initial comments submitted on February 14.

Today's Port Authority

PAAC certainly appreciates SAG's acknowledgement of PAAC's efforts that resulted in the favorable comments set forth in findings five and six and wishes to underscore the significant advances made since the 2007 SAG audit and recognized in the Observations portion of the report. On virtually every financial front, PAAC is not the same transit agency of years past. PAAC today is a much leaner operation that provides a quality public transportation system -- bus, rail, incline and paratransit -- for the benefit of the residents, corporate employers, and local businesses in Allegheny County as well as those of our surrounding counties. PAAC has made some very significant changes in the last few years. Most notably:

- We have increased operating revenue;
- We have cut more than \$45 million in expenses by reducing our workforce by 21%;
- We have contained costs and improved efficiency;
- We have fixed our pension problem; and
- With the cooperation of our largest labor union, ATU Local 85, we have changed retiree health benefits in a way that permanently reduces PAAC's legacy cost obligations.

It is on legacy cost reduction that PAAC has outpaced any other public entity in Pennsylvania and many across the country. On its pension obligation, PAAC has closed the defined benefit plan to all new non-represented, IBEW, and police employees and

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increased cost sharing for all remaining participants. Today participants in all defined benefit plans contribute 10.5% of salary, reducing the annual cost to the agency. New employees in the non-represented, IBEW and police workforce participate in a defined contribution plan, thereby capping the PAAC's long-term obligation to these employees.

In addition, PAAC has greatly reduced the escalating cost of retiree medical promises. In 2007, retiree healthcare for non-represented and police employees was eliminated without regard to years of service. Over three collective bargaining agreements, ATU Local #85 and IBEW employees have made significant concessions on eligibility and increased cost sharing resulting in reductions in long-term liabilities. As of August 2012, new hires in the ATU bargaining unit receive a maximum of three years healthcare at retirement. Going forward, management will continue to search for ways to reduce healthcare costs for our active employees particularly in light of the added fees and taxes contemplated under the new Affordable Care Act.

Management Responses to SAG Findings

FINDING ONE: The Port Authority did not comply with its own procurement requirements and did not implement FTA recommendations when awarding contracts

PAAC Response: While specific responses to the individual components of this finding are set forth below, it is initially noted that PAAC must respectfully disagree with this overall finding, as to the breadth of its conclusion. As SAG is aware, FTA conducts frequent file reviews of grant recipients, such as PAAC, to assure compliance with federal regulations. Indeed, Port Authority is amongst the largest FTA grant recipients in the Commonwealth, and is amongst the top fifty FTA grant recipients in the country. As a result and as it should, FTA has higher expectations of PAAC than it does for smaller grant recipients. It is, in fact, PAAC's diligence in complying with FTA guidelines that has made PAAC successful in acquiring FTA funding for a multitude of capital projects that would otherwise have gone unfunded, to the detriment of the region.

The FTA Review referenced in Finding One occurred in March, 2011. The FTA Procurement System Review (PSR) is one of the most, if not the most, thorough and comprehensive procurement-focused assessments conducted by FTA and its assigned reviewers, and it is typically reserved for FTA's larger grant recipients. The PSR consists of six system-wide procurement elements, as well as fifty-four individual procurement elements. Of those components, FTA expressed concerns as to only one of the system-wide elements, and twelve of the fifty-four individual procurement elements. The issues set forth regarding those concerns were relatively minor and easily resolved. All findings were officially closed within eight months following the completion of the PSR. We were advised that PAAC compared well to other FTA grant recipients who have undergone a PSR. Of course, and since purchasing controls and procedures can always

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be subject to further improvements and efficiencies, PAAC continues efforts to improve efficiency and minimize leakage in its procurement operations.

It is for this reason that PAAC believes SAG's conclusion as set forth in Finding One is overbroad. To state a more accurate summation in the converse, PAAC is in compliance with the overwhelming majority of procurement system requirements, while there remain some system protocols where occasional deviations have been observed and require further consideration and attention.

1. The Port Authority did not implement debarment and suspension audit recommendations of the Federal Transit Administration when entering into contracts with three vendors.

PAAC Response: Because the report does not identify the specific contracts with purported deficiencies, it is unclear exactly which files are referenced in this statement, such that it is difficult to confirm what circumstances existed as to each respective file, and the specific time frames when they occurred. In any event, as SAG accurately notes, the FTA did not conclude that PAAC permitted debarred or suspended contractors or subcontractors to work on PAAC projects, or even that PAAC was not checking the EPLS list as to contractors prior to bid award. Rather, the FTA noted that certain files lacked documentation that EPLS was checked prior to award. PAAC thereafter worked to improve file documentation.

SAG asserts that PAAC failed to *document* that EPLS checks occurred in three contracts. SAG asserts that these failures occurred "within weeks" of the FTA's 2011 report. SAG further concludes that EPLS documentation deficiencies occurred even though PAAC stated it would review contract documentation "on a periodic basis to ensure compliance with the most recent FTA requirements and guidance."

An FTA draft report was disseminated June 7, 2011. PAAC did respond to the FTA draft report in late June, 2011. From the receipt of FTA's draft report and over the course of several months thereafter, PAAC utilized its best efforts to address FTA's recommendations as promptly and as effectively as possible. Any suggestion that PAAC was indifferent or unduly inattentive towards FTA's recommendations because PAAC did not assess, review, improve and implement revised protocols within a three week period is unfair. As noted above, all issues identified in the PSR were successfully resolved to FTA's complete satisfaction in December, 2011.

Notwithstanding the foregoing and in response to the underlying concern raised by SAG, it should be noted that PAAC has previously revised its file checklist to require the assigned contract specialist to confirm that an EPLS check was performed and documented in the subject Purchasing file. This practice continues today, and has been reemphasized following receipt of SAG's report, and should adequately address any perceived concerns raised by SAG.

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Auditor General's Evaluation of PAAC's Response

The Port Authority acknowledges that there were deviations from established procurement protocols, and we are pleased to note that our audit has prompted the Port Authority to reemphasize to its relevant staff the importance of following protocols, including the EPLS check and the necessity to document that the check was performed.

The three contracts referenced in this finding had notice-to-proceed dates of August 15, 2011; August 31, 2011; and September 8, 2011. Since the Port Authority received and responded to the FTA's report in June 2011 and the Port Authority stated that the issues presented in the FTA's procurement system review were "easily resolved," it is reasonable to expect that the FTA recommendations would have been implemented within that six to ten week time frame. Further, Port Authority stated that it previously revised its file checklist to require the contract specialist to confirm that the EPLS check was performed, yet the files for all three contracts did not contain the checklist. We reiterate our recommendation that the Port Authority should ensure that the EPLS check is performed and documented prior to awarding contracts that exceed \$25,000.

2. *The Port Authority did not comply with subcontractor debarment and suspension requirements for 26 percent of the contracts we reviewed.*

PAAC Response: PAAC cannot confirm the accuracy of the percentages set forth in this conclusion because SAG's report does not specifically identify the 26 percent of contracts that purportedly did not comply with subcontractor debarment and suspension requirements. Notwithstanding same and in a good faith effort to respond to the concern raised by SAG, PAAC acknowledges that it continues to wrestle with establishing the best system to achieve compliance with FTA requirements regarding debarment status of subcontractors. Many contractors are unable to identify all subcontractors prior to contract award, or there is a need to substitute a new subcontractor for previously identified subcontractors. This is not an unusual event in construction. Of course, the potential for oversights in documentation increase once construction activities begin.

Fortunately and recognizing these challenges, FTA provides several options for meeting requirements regarding subcontractor debarment. As set forth in 2 C.F.R. § 180.300, acceptable practices for verifying lower tier transactions include (1) checking the EPLS, (2) collecting a certification, or (3) establishing that a debarment certification clause is set forth within the subcontract. Any of these three options comply with FTA guidelines.

In fact, Port Authority's construction contract terms and conditions meet FTA requirements independent of obtaining subcontractor certificates. In PAAC's

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construction contract Terms and Conditions (T's and C's) utilized during this time frame addressed in this audit (and currently), Section 2, Article 2.4 requires that the contractor/bidder not enter into any "lower tier covered transactions" with a "person" who is debarred, suspended, etc., and further required the bidder/contractor to include the provisions of the Article in all lower tiered covered transactions. It also allows the bidder to decide the method to determine whether the person involved in a lower tiered transaction was debarred. In Section 500, Article 1.13.B, the contractor is required to include Section 200, Article 2.4 in each "subcontract." Thus, the T's and C's believed to be in use during the relevant time frame already meet FTA requirements as to subcontractor verification, regardless of whether the physical certificates from the subcontractor are ultimately collected and maintained in the subject purchasing file.

Further revisions to PAAC's construction contract T & C's are being rolled out currently. In its new format, subcontractor certifications will not be collected by PAAC. Instead, contractors will be required to submit "Form K" to all pay estimate submittals. Form K will require that the contractor identify each subcontractor, and certify that each subcontractor's debarment status has been met.

It is also noteworthy that, to the best of PAAC's knowledge, information and belief, no federally debarred or suspended contractor or subcontractor has ever worked on a PAAC project.

Auditor General's Evaluation of PAAC's Response

In its response to this finding, the Port Authority essentially acknowledges that it has experienced problems with ensuring compliance with FTA requirements regarding the debarment status of subcontractors. While the Port Authority's response addresses federal requirements, the response is silent on the key point made in our finding. Specifically, our finding notes that the Port Authority did not comply with its own procedures or enforce its own contract terms regarding suspension and debarment.

Further, the Port Authority refers to Section 0500, Article 1.13.B of its standard solicitation for construction contracts but does not quote the provision that is directly and specifically applicable, which is Section 0500, Article 1.13.A. That section explicitly requires the contractor to provide the Port Authority a signed debarment /suspension certification from each subcontractor.

The Port Authority also noted that it is implementing revisions to its construction contract terms and conditions. The revised contracts will no longer require the agency to collect the debarment certifications. In light of these revisions, we recommend that Port Authority revisit its internal policies and procedures to ensure that the contract language aligns with internal policies.

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Finally, contrary to the Port Authority's statement that it is unaware of the noncompliant contracts referenced in the report, during our audit fieldwork Port Authority staff provided us with written responses to each of our inquiries that identified the 50 subcontractors referenced in the report. The documentation provided to us stated that the agency was unable to locate the required subcontractor certifications.

3. *The Port Authority did not comply with subcontractor lobbying certification requirements for more than 10 percent of the contracts we reviewed.*

PAAC Response: As noted above, PAAC would need to be provided with the identity of the specific contracts and subcontractors referenced in this statement to confirm the accuracy of SAG's 10 percent statement. Notwithstanding the foregoing and in a good faith effort to respond to this finding, PAAC initially notes that SAG personnel are aware that lobbying certificate requirements only apply to contracts or subcontracts over \$100,000 in value. PAAC would further need to confirm that the entities referenced in SAG's statement are in fact "Subcontractors," and not "Suppliers." Section 500, Article 1.13.C of the T's and C's believed to have been in use during the relevant time frame of the audit required that the lobbying certificate be signed by each "Subcontractor" and makes no mention of "Suppliers" (in the T's and C's, there is a defined term for both Subcontractors and Suppliers). Accordingly, there is no requirement for the contractors to supply lobbying certificates for any Suppliers as that term is defined in the T's and C's. Nothing in the FTA guidelines is contrary to this practice. The federal "New Restrictions on Lobbying" are set forth in 49 C.F.R. Part 20. In discussing what is required of a "person" (which would include a contractor) who receives a "subcontract" from a "person" who has a federal contract or grant, Section 20.110 provides that such person is required to file a lobbying disclosure form if the contract or subcontract, at any tier, exceeds \$100,000 and the forms are required to be forwarded from tier to tier until received by the grant recipient. As indicated, this section specifically mentions "subcontracts." When federal regulations intend to reference both subcontractors and suppliers, it is typical that the guidelines would identify both in PAAC's long experience with federal procurement laws and regulations. Subcontractors and suppliers are not one of the same.

Notwithstanding the above and in a good faith effort to address the concern raised by SAG, PAAC is rededicating itself to the task of improving upon its 90% compliance rating as to subcontractor lobbying certificates (again, assuming that all 10% of the subcontractors referenced by SAG were in fact subcontractors, and not suppliers.) The necessity of compliance is being reinforced with relevant personnel across all relevant departments.

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Auditor General's Evaluation of PAAC's Response

We are encouraged that, as a result of our audit, the Port Authority is reinforcing the necessity for compliance across all relevant departments. We must note, however, that each of the 10 entities that we discuss in our finding was indeed a subcontractor and not a supplier. PAAC procurement and engineering staff identified and/or confirmed the identities of the applicable subcontractors and the suppliers related to the contracts under review.

4. *The Port Authority did not comply with its own sole source procurement procedures for a contract awarded in 2011.*

PAAC Response: SAG's reference is identified in its report as the sole source procurement for calibration and maintenance of an under-floor wheel lathe. It is claimed that the contract was awarded without proper management approval and signatures. As SAG is aware from its review of the file and from PAAC's response to SAG's Information Request No. 11, proper management approval was given, as the sole source justification memo was copied to PAAC's then AGM of Engineering, who thus had awareness of and ultimate authority to authorize this sole source procurement. It is acknowledged, however, that the PAAC representative who actually signed the contract did not have adequate limits of authority to sign this agreement. This event was an aberration, as reflected by the fact that such an incident was identified in only one sole source event. That does not change the fact that the service was necessary, the agreement was appropriate and the senior manager who had authority to authorize same was aware of and approved this procurement proceeding. PAAC required this service to maintain the equipment within proper operating tolerances, and had entered into previous agreements for the same service with the same vendor. The previous agreement for this service was executed by PAAC's then Director of Rail Operations, who acted within her designated limits of authority to do so. Even to date, the referenced vendor remains the only qualified provider of this service. Current protocols do require that all proposed sole source agreements be referred to the Director of Purchasing and PAAC Legal Department for review to ensure compliance and proper file documentation and agreement form before any sole source procurement is finalized.

Auditor General's Evaluation of PAAC's Response

In its response to this finding, the Port Authority acknowledges that the agency representative who signed the contract in question did not have "adequate limits of authority" to sign the agreement on behalf of the Port Authority. Although we are pleased that the Port Authority concurs with this particular assessment, we respectfully disagree with other statements in the agency's response.

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The Port Authority states that proper approval was given for this contract because the assistant general manager was “copied” on the sole source justification memorandum. While we were able to confirm that the assistant general manager was copied on the memo, we did not find any evidence that the manager actually approved the contract. Being copied on a memo can indicate awareness or knowledge of a contract but does not indicate approval of the contract. More important is the fact that the contract file also did not include any e-mails or other communications that noted approval of the procurement by any management level employee required by policy to approve contracts or anyone from the legal department. As we stated in our finding, this lack of approval is a significant deviation from established internal control procedures.

Finally, the Port Authority states that “current” protocols require all proposed sole source agreements be referred to the agency’s legal department for review. The statement implies that past protocols did not require such a referral. However, our review of three other sole source contract files found that all three contracts included evidence of a legal department review. Each of these three contracts had notice to proceed dates prior to the contract referenced in this finding leading us to conclude that legal review and approval has always been the protocol. We reiterate our recommendation that the Port Authority should ensure compliance with all established protocols.

5. The Port Authority did not comply with its public advertisement requirement for an invitation to bid issued in 2010.

PAAC Response: This SAG finding references a transit advertising installation procurement. It is opined that, because bids were opened eighteen days after the solicitation was issued, as opposed to thirty days as per PAAC’s standard protocols, that PAAC may have limited the pool of potential bidders because bidders may not have had sufficient time to prepare bids.

Initially, it is noted that PAAC’s thirty day self-imposed requirement is above and beyond the requirements of state law. Section 559.1(a) of the Second Class County Port Authority Act sets forth the advertising requirements for bid solicitation, which can legally be accomplished in a period of time of less than two weeks:

- (a) All contracts or purchases in excess of ten thousand dollars (\$10,000) shall be in writing and, except those hereinafter mentioned, shall not be made except with and from the lowest responsible bidder meeting specifications, after due notice in at least one newspaper of general circulation, published or circulating in the county at least three (3) times, at intervals of not less than three (3) days where daily newspapers of general

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circulation are employed for such publication, or in case weekly newspapers are employed, then the notice shall be published once a week for two (2) successive weeks. **The first advertisement shall be published not less than ten (10) days prior to the date fixed for the opening of bids.** (emphasis added).

It is further noted that this procurement was a “rebid” of an immediately preceding solicitation. The solicitation was reissued, in part, for the purpose of determining whether PAAC could enlarge the pool of potential bidders, while at the same time achieving a timely award to meet PAAC’s pressing need for this service as it relates to advertising sales (an important non-fare related revenue generator for PAAC). Under the circumstances presented, PAAC believes this procurement was properly advertised and afforded ample opportunity for additional parties to submit bids. Notwithstanding the aforementioned and in a good faith effort to address SAG’s concern, PAAC stands by, and intends to enforce consistently, its thirty day protocol going forward, as it has largely done successfully in the past.

Auditor General’s Evaluation of PAAC’s Response

We are pleased that the Port Authority expressed its intent to enforce the 30-day advertising requirement in the future. We noted this deviation from established procedures because the estimated value of the contract was \$200,000, which significantly exceeded the \$100,000 threshold required in the Port Authority’s procurement manual. The Port Authority established policies and procedures to ensure that contracts are allowable, necessary, and economical. Therefore, we continue to recommend that the Port Authority should ensure that its employees consistently adhere to established policies and procedures.

FINDING TWO: The Port Authority made questionable decisions regarding some of its contracts.

1. *The Port Authority paid over \$60,000 to a contractor for a fare policy that the agency has yet to adopt.*

PAAC Response: While PAAC has admittedly not yet adopted a new fare policy, PAAC did acquire valuable information from the contractor regarding developing and potentially implementing a new fare policy or components of a new fare policy. The contractor was considered one of the foremost experts on public transportation fare policy and fare modeling. The contractor was able to present to the Authority a clear summary of other fare policy’s from agencies across the country. Notwithstanding

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the above, PAAC does not delegate its decision making authority to contractors. A contractor's recommendations are considered by senior management and PAAC's Board (based upon recommendations made by management) who make the ultimate decision to accept, reject, or modify the recommendations for ultimate implementation. Delays in implementation decisions do not render the contractor's services to be useless or wasted from PAAC's perspective.

Rather, many of the recommendations of the contractor are still under consideration, but have simply been delayed due to a number of organizational factors. PAAC has been in the midst of total transformation of its fare collection system moving from a "flash pass" system to a Smartcard based system in incremental and deliberate phases. Until this installation is fully completed and all of PAAC's existing "flash pass" products are fully converted to Smartcard-based technology, PAAC believes it would be premature and unduly confusing to its riders if it began making wholesale changes to its fare policy.

The recent changes to the leadership structure at PAAC have also delayed the timeline on making improvements to the Authority's fare policy. The appointment of a new CEO and a new PAAC Board (changes that have occurred over the past year) will give the organization the continuity necessary to hold further discussions on changes in fare policy and time same to complement PAAC's ongoing Smartcard fare collection system conversion. The groundwork for these discussions will come directly from the work product prepared by the fare policy contractor and knowledge gained by PAAC management via engaging same.

Auditor General's Evaluation of PAAC's Response

In its response, the Port Authority acknowledges that it has not adopted a fare policy since the contractor's presentation to the board of directors in October 2011. Again, as stated in our audit report, the Port Authority cites organizational factors and changes in leadership as reasons for the delay in policy implementation. However, while the Port Authority remains confident that the nearly 2 ½ year-old recommendations are useful, we are concerned that the recommendations may no longer be relevant and that the Port Authority may have to spend more time or more money to obtain up-to-date information.

- 2. The Port Authority automatically extended a contract for equipment cleaner despite test results showing the product performed poorly.***

PAAC Response: PAAC respectfully disagrees with SAG's observation that it "automatically" extended the contract. The referenced contract was entered into on September 8, 2011, with an option to extend for two additional years. The product of the lowest responsive, responsible bidder was determined to be compliant with

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specifications set forth in the solicitation, prior to bid award. Subsequently, performance issues with the product began to surface. Performance testing occurred, and while the User Group advised following the testing that the product did not perform as well as another product, no recommendations were made to modify the specifications, and the actual performance test results were not provided at that time. Subsequently, the User Group requested that the Procurement Department exercise the option to extend. Pricing of the option years was determined to be fair and reasonable. The option was exercised in early November, 2012. On November 30, the Procurement Department was first advised that the product's performance was unacceptable, and was further alerted to potential health concerns (said potential health concerns were raised by one employee at one of the two operating locations then utilizing the product, but were never established or confirmed due to PAAC's subsequent termination of the contract for this product). Upon receipt of these complaints, the Purchasing Department promptly cancelled the contract and secured a refund for unused product that had been purchased. While it would have been preferable had the User Group advised the Purchasing Department of issues concerning the cleaner prior to contract extension, this was not an "automatic" extension as suggested by SAG. Rather, the Purchasing Department extended the contract based upon (1) pricing, and (2) a recommendation from the end user group. Fortunately and due to strong and favorable termination language provided in its agreement, PAAC successfully terminated the contract and achieved a refund for the unused product that it returned. PAAC believes that this incident was a result of less than desirable communication between departments. In effort to reduce the potential for such events going forward and in a good faith effort to address the concern raised by SAG, PAAC has implemented a revised Bid Review Form. The revision to this form serves to assure acceptance by: (1) the Legal Department—to confirm legal bid compliance; (2) Technical Support—to confirm compliance as to specifications; and (3) the User Department—to assure satisfaction with performance. If any of these departments raises concerns, the Procurement Department conducts further investigation, and when required, the various departments conference regarding the best solution. Additionally, the Procurement Department will request copies of any performance testing documentation for its procurement files, when advised that such testing will or has occurred, and will verify whether a product "passed" or "failed" a performance test with the User Group/technical expert for the subject product.

It should be further noted that the safety and well-being of Port Authority's employees is and will always be one of the agency's highest priorities and concerns. Accordingly, before any cleaning agent or other chemical is utilized in Port Authority's day-to-day operations (including the equipment cleaner at issue), Port Authority's System Safety Department reviews all chemical Material Safety Data Sheets relative to the chemical's composition and proper uses. The purpose of this review is to ensure the general safety of the product and to ensure that any special instructions or precautions that have to be followed when utilizing the product are clearly communicated and understood by relevant personnel. Of course, if a complaint about the safety of a product being utilized is brought to Port Authority

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management's attention once the product is introduced into the workplace, that product would be subject to further scrutiny to ensure its continued use would not present a hazard in the workplace. In the instant case, however, the need for additional investigation or scrutiny from a health/safety perspective became moot because Port Authority was already in the process of terminating the equipment cleaner contract for poor performance when the one complaint raising health concerns relative to use of same was received by Port Authority management.

Auditor General's Evaluation of PAAC's Response

In its response, the Port Authority takes responsibility for "the less than desirable communications between departments" and then offers good faith solutions to the weakness identified by our audit. The revisions to the agency's bid review form, the requirement for bid acceptance by three key groups of employees, and the requirement to communicate both the existence and results of performance tests to the procurement department are certainly steps in the right direction.

While we acknowledge the Port Authority's efforts to correct the above-mentioned communication issues, we find it necessary to provide clarification regarding some of the agency's other remarks. We were not provided with any evidence to support the Port Authority's statement that the user group requested that the procurement department exercise the option to extend the contract for the equipment cleaner. Further, documentation in the contract file indicates that Port Authority health and safety personnel informed management that more than one employee complained about the cleaning product's odor and propensity to cause throat irritation.

Finally, the evidence in the contract file does not support the Port Authority's closing statement that the Port Authority was already in the process of terminating the equipment cleaner contract for poor performance when Port Authority management received a complaint about health concerns. The Port Authority actually acknowledges that fact when it stated earlier in its response that the procurement department was notified of the product's poor performance and potential health concern and "upon receipt of these complaints, the contract was cancelled."

- 3. The Port Authority automatically extended two service contracts without any price comparisons to ensure that it was still receiving the service at the lowest possible price.***

PAAC Response: SAG's finding in this regard identifies the two contracts at issue as (1) HVAC and refrigeration maintenance services, and (2) transit advertising services. PAAC does not concur that contract extensions were "automatic," but PAAC agrees that more substantive file documentation justifying exercise of option years could be generated and maintained on a going forward basis.

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HVAC and refrigeration services. This contract consisted of a one year agreement with two one year options. SAG claims that that this contract was extended for a second year in 2010, even though the original bid did not offer the lowest price for year two. Specifically, SAG notes that the contractor's overall price for year two was \$20,470 higher for year two than the contractor's closest competitor, when bids were opened in 2009. SAG further notes that the contractor's price for a third year was \$21,900 higher than pricing offered by a competitor, when bids were received in 2009.

It is initially noted that the competitor pricing referenced in SAG's response is not an appropriate comparison, as these competitor bids were established to be non-responsive. The failure of these competitors to respond to PAAC's request for further information necessary to evaluate their respective bids is not a mere "technicality," as SAG states. To the contrary, it is an essential requirement under state and federal law for an agency to establish a bidder's ability to meet basic contract specifications. Absent meeting this initial threshold, there can be no comparison of pricing because it cannot be established that all competitors are bidding on the same criteria. The reference by SAG to a purported violation of PM-160 is without merit, because the reference to comparison bids can only be applied as to technically and legally responsive bids.

As noted in SAG's draft report, PAAC Assistant Manager of Facilities (as representative of the User Group and project manager for this contract) submitted a memo to the procurement department advising of his phone survey efforts and the results of same. This phone survey established that the pricing offered by the current contractor remained less than market rates, as market rates existed at the time the option was evaluated. PAAC does agree that the documentation provided by PAAC personnel would have been improved had it identified the respondents to the phone survey, but such is not tantamount to classifying the contract extension as "automatic," nor is more detailed information required by state law or our internal policies. In light of SAG's concerns, however, Purchasing personnel will ensure such information is included in future user group documentation/justifications for extending contracts.

Transit Advertising Services. This contract consisted of a one year term with three additional one year options. As SAG notes in its report, the pricing for these services did not increase for years two through four. Historically, PAAC has experienced difficulty finding any other vendor to bid these services, and the only other bid from a responsive bidder who responded to the initial solicitation was substantially higher than the contractor's pricing. In a memorandum dated January 4, 2012 from Port Authority's Director of Advertising Sales (as representative of the User Group and as project manager for this contract), it is noted that the contractor's pricing was determined to be fair and reasonable. PAAC again agrees that the justification memo could have been more comprehensive, but the extension was not "automatic," nor is more detailed information required by state law or our internal policies. Again,

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however, and in light of the concern raised by SAG, Purchasing personnel will ensure such information is included in future user group documentation/justifications for extending contracts.

Auditor General's Evaluation of PAAC's Response

In its response, the Port Authority offers that more substantive file documentation justifying the exercise of option years could be generated and maintained going forward. We agree that if the Port Authority generates and maintains more substantive documentation in its procurement files, the agency's ability to ensure compliance with established policies and procedures will improve.

With respect to the contract for HVAC and refrigeration services, evidence in the contract file indicated that Port Authority procurement personnel were aware that a competitor offered significantly lower prices for the first optional year. Further, our interview of relevant procurement personnel revealed that Port Authority staff did not conduct any cost analysis or prepare a change order for the second optional year. In the absence of a change order, the board of directors did not vote to authorize the second contract extension valued over \$100,000.

Regarding the transit advertising contract, the documentation in the contract file repeatedly cited the absence of a price increase with the current vendor but made no mention of any price comparison with any other vendor. The Port Authority stated that it experienced difficulty locating other potential vendors, yet documentation in the contract file noted that one other vendor was unable to participate in the 2010 solicitation due to other contractual commitments. Therefore, Port Authority was aware of at least one alternative vendor, and it should have contacted that vendor for a price comparison prior to the 2012 or the 2013 contract extensions.

In summary, we are pleased that the Port Authority intends to improve its procurement records, and we are hopeful that the above reiteration of our concerns prompts the Port Authority to conduct cost analyses and adequate price comparisons before it extends contracts in the future.

FINDING THREE: The Port Authority failed to adequately prepare contract bid proposals for two contracts, which led to change orders that significantly increased the cost of each contract and possibly resulted in other vendors not submitting bids.

PAAC Response: Initially, it is noted that PAAC respectfully disputes the conclusions (1) that bid solicitations were inadequately prepared, and (2) that the perceived "failures" resulted in increased costs. These conclusions are based upon an analysis that suggests that any "add on" to a scope of work necessarily wastes money and efforts. There exist valid reasons for change orders that add value to the services

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provided, and do not necessarily duplicate efforts. Changes in circumstances (such as bids coming in well under the engineer's estimate or project budget) also occur that render what may previously have been an unrealistic option now feasible and responsibly and validly subject to modification via change order.

1. ***The Port Authority failed to perform sufficient "due diligence" in preparing a request for bids for electrical work which ultimately led to a 70% increase in the contract cost.***

PAAC Response: SAG acknowledges in its report that "Port Authority did not have to pay this contractor for any rework," yet the highlighted statement in this portion of the report for this finding certainly implies that PAAC's perceived insufficient "due diligence" in preparing the bid documents resulted in a waste of funds in the hundreds of thousands of dollars, and thus may be misleading to those who will review the published report. As indicated in PAAC's response to SAG Information Request E-15, improvements were developed following the preliminary layout upon which the original specifications were based. Potential improvements in design can be a continuing process in projects of this magnitude and are not uncommon or unusual.

Auditor General's Evaluation of PAAC's Response

While we agree with the Port Authority that design improvements related to a large project such as this are not uncommon or unusual, we remain concerned that, in this instance, Port Authority may have been able to avoid such a large change order if operations staff had been significantly involved at the beginning of the project. Specifically, if operations staff had been significantly involved in the planning process prior to bid development instead of after the bid documents were issued, the bid documents would have reflected actual project parameters, and the Port Authority could have avoided issuing a \$700,000 change order. As stated in the finding, if the Port Authority had issued a request for bids that reflected the actual project parameters, the possibility exists that other bidders may have responded, offering a lower total contract cost, or the existing bidders may have submitted different bids due to the larger size of the project.

2. ***Port Authority's attempt at doing a lower expense job ultimately resulted in a change order that increased the contract value by 62% or more than \$500,000.***

PAAC Response: This finding pertains to a 2009 procurement for storm water separation and pavement improvements to a large park and ride lot. As SAG acknowledges repeatedly in its report and as well-known publicly over the past several years, PAAC experienced significant operating and capital budget constraints

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in the time frame of this procurement. To highlight that PAAC “originally ‘opted’ to take the ‘cheaper’ route” implies that PAAC had vast resources from which it could perform more extensive improvements when the project was originally bid, and then simply elected not to do so. PAAC respectfully asserts that this is a misrepresentation of the circumstances and considerations that went into the preparation of the original plans for the contract at issue. Budgetary considerations led PAAC to initially make a decision to mill and overlay in certain areas. At that time, PAAC's state of good repair backlog was very high and the availability of capital funds was limited. In order to make other much-needed capital improvements, it was decided that the budget could not be increased to accommodate full-depth paving throughout the site based on the engineer's estimate. Upon receipt of favorable bids well under the budget and engineer's estimate, and after the first small portion of mill and overlay proved inadequate, it was determined PAAC could incorporate the full-depth paving within the project budget without adversely impacting other components of PAAC's state of good repair capital program. Only a small portion of the lot was reconstructed as full depth replacement. While the reconstructed area could have been left in that state, its service life would have been significantly less than full replacement, thus warranting full replacement so that wearing would be uniform throughout the entire site. Most of the cost expended with the change would have been incurred even had it been included in the bid documents, and PAAC took advantage of favorable bids received in response to the original project design.

Auditor General's Evaluation of PAAC's Response

We stand by our conclusion that the Port Authority did not properly prepare bid proposals. Statements made by the Port Authority in its response support this conclusion. Specifically, the Port Authority acknowledges that the mill and overlay method of repairing the parking lot proved to be inadequate. In addition, the Port Authority stated that the favorable bids were well under the budget and the engineer's estimate indicating to us that the estimates may not have been adequately prepared. While we appreciate the Port Authority's efforts to be budget-conscious, we continue to recommend that the Port Authority adequately plan needed projects. The Port Authority should ensure it does not sacrifice quality in anticipation of cost savings.

FINDING FOUR: The Port Authority paid excessive relocation expenses of more than \$28,000 to one employee and failed to properly adhere to its relocation policy for two other employees, which cost the Port Authority nearly \$5000.

PAAC Response: It is initially noted that the provision of employee relocation packages is a rare occurrence at PAAC. SAG's report acknowledges that, over the entire performance audit period from 2007 through 2012, only \$48,174 has been expended by

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PAAC to provide relocation to new employees. No relocation packages were offered to any PAAC new hires in calendar years 2012 or 2013.

1. ***The Port Authority paid more than \$28,000 in excessive relocation expenses to a new employee hired in 2009.***

PAAC Response: This finding references the hire of an individual to fill a senior management-level position responsible for overseeing service planning and scheduling functions (functions that become particularly critical in times of financial difficulty when hard decisions had to be made to provide the best transit service possible for the community with particularly limited financial resources). The individual hired to fill this position in 2009 had significant service planning, scheduling and policy experience from more than 30 years of service in the public transit industry. As SAG is aware, the payment of relocation expenses to this individual was well within the limits of PAAC's then-existing relocation policy. SAG does not contend that the payment of relocation expenses to this individual violated any state or federal law, or any internal PAAC policy.

Notwithstanding the above and in light of the concern that SAG brought to current Port Authority management's attention, Port Authority has amended its current Relocation Policy to provide that if total relocation expenses are to exceed \$20,000 and/or if any exceptions to the Policy are going to be offered to a candidate, the Chief Executive Officer (or his or her designee) will document the justifications for same in a memorandum and receive the written concurrence of the Chairperson of Port Authority's Board before same can be authorized, approved or paid. This amendment to PAAC's relocation policy was adopted and administratively implemented by PAAC while SAG personnel were still on site completing their performance audit activities.

Auditor General's Evaluation of PAAC's Response

We are encouraged that, as a result of our audit, the Port Authority has taken measures to introduce transparency to the approval process for relocation expense reimbursements. However, due to the Port Authority's ongoing financial struggles, we recommend that the Port Authority carefully consider reimbursing any relocation expenses that exceed \$20,000.

2. ***The Port Authority did not enforce a key provision of its relocation policy for two other employees, costing the Port Authority nearly \$5000.***

Port Authority of Allegheny County

PAAC Response: PAAC agrees that it failed to pursue recovery of relocation expenses for two employees, who left PAAC within two years of hire. In order to address this oversight on a going forward basis, PAAC has now revised its resignation form so as to specifically require a review of an employee's service history and relocation benefits provided upon resignation, in order to assure identification of recovery opportunities. The form will now be circulated directly to the Director of Employment and Development, as well as the Manager of Payroll, who have responsibilities related to recovery of such benefits. These managers will also work with PAAC's Legal Department, as necessary, to ensure such expenses are recovered in a timely manner.

Auditor General's Evaluation of PAAC's Response

We acknowledge the Port Authority's agreement with our finding and support the agency's procedural revisions designed to achieve appropriate and timely recovery of relocation benefits from employees who have resigned.

3. *The Port Authority did not accurately account for relocation expense reimbursements, which would have cost the Port Authority \$4,300 if we had not notified the agency of the error.*

PAAC Response: PAAC confirms the accuracy of this finding, and appreciates SAG's efforts to bring this oversight to PAAC's attention so that it could be promptly corrected.

Auditor General's Evaluation of PAAC's Response

No response is necessary.

Port Authority of Allegheny County

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