



**CEO's Response to the Report of the Special Investigatory Committee
December 9, 2008**

Former US Attorney Michael McKay recently completed a ten-month investigation into areas identified as potentially vulnerable to fraud by a 2007 performance audit. His report contains eight recommendations, which the Port will implement immediately. This response plan outlines how the Port will respond to each of Mr. McKay's recommendations.

Recommendation A: Implement a robust Compliance Program

- The CEO has directed a newly-formed team to develop workplace responsibility awareness and training program for the six policies that serve as the Port's compliance program: employee ethics, consultant ethics, fraud, anti-harassment, appropriate use of information technology and whistleblower protection. These policies will be aggressively promoted throughout the Port to ensure that all staff members understand their responsibility for ensuring that Port policies are followed in every area. The program will include communication, formal and informal training, ongoing policy development, and, in response to the report's recommendation, special emphasis on compliance.

Deliberate communication and training will continually reinforce a culture that reflects basic integrity, common sense and good citizenship in the workplace and in the community. Ongoing policy development will ensure that policies are continually refined, improved and integrated and that employees are aware of and understand existing policies. The CEO has asked for a report from the team by February 15.

- On December 8, 2008, the CEO released an updated, strengthened whistleblower policy. Although the Port has had such a policy in place since 1997, the updated version clarifies which matters should be reported, clearly lists appropriate people to approach with concerns, and defines the retaliatory actions that are forbidden under the policy. In general, the updated policy is easier to understand and follow.

The CEO noted with concern that throughout his report, Mr. McKay provides several examples where Port staff failed to come forward to report ongoing practices that violate policy or law. The Port has invested significant time, dollars and energy over the past several months revising, reorganizing and improving our contracting and procurement processes. The CEO believes it is critical that Port employees feel invested in improving the organization and feel safe to speak out when they see actions that raise suspicion. A strong whistleblower policy is crucial to creating that safe environment

- The Port has taken several other recent actions in the area of ethics and workplace responsibility:
 - The Port Commission adopted a revised Ethics Code for Commissioners (Resolution 3583) in September, 2007, and the CEO subsequently revised the Port’s parallel Policy for Employees.
 - The Port implemented a new Ethics Policy for Consultants.
 - The Port adopted a new Fraud Awareness Policy and implemented a confidential Fraud Hotline, accessible to the public and to employees.

Recommendations A.1: Strengthen several areas of Ethics Policy

Recommendation A.1.a: Prohibit use or disclosure of information not available to the general public and acquired by reason of Port employment to the detriment of the Port.

Recommendation A.1.b: Include a reporting requirement for all financial interests held by employees in entities doing business with the port (include documentation of the disclosure, review by the supervisor, and enforcement of any recusal adopted as a result of the financial interest).

Recommendation A.1.c: Include a reporting requirement for all potential conflicts of interest, financial or otherwise, of an employee who is in a position to influence the selection, non-selection, or conduct of business between the Port and any entity.

The Port will immediately implement each of these suggested additional changes in our Ethics Code and Policy. All three make good sense. The first - prohibiting use or disclosure of information not available to the general public – can be implemented quickly. The other two, which address reporting and recording certain financial interests and potential conflicts of interest may take longer to develop, but work will begin immediately.

Recommendation A.2: Increase the role of the Port legal department in the compliance program—at the development, implementation, training and oversight levels

Mr. McKay also suggests increasing the role of the Port legal department in all levels of a compliance program, including development, implementation, training and oversight. The Port’s Legal Department is playing a major role in the development phase of a workplace responsibility program and will continue to have a high level of involvement and responsibility in all future phases, as well as primary responsibilities in the program compliance and policy development areas.

Recommendation A.3: Increase the role of the Ethics Board in the compliance program.

The suggestion to increase the role of the Port’s independent Ethics Board is excellent. The Ethics Board currently consists of five outside members, appointed by the Commission for three year terms. The scope of the Board’s duties and responsibilities is set out in the Commission Ethics Code, Resolution No. 3583 and has not changed in many years. The Commission has indicated they will evaluate this recommendation, creating an appropriate additional role for the Ethics Board and revising and updating its Resolution accordingly.

Recommendation A.4: Incorporate initial and ongoing employee training into the compliance program.

Training a workforce of 1600 employees is not a simple or inexpensive task, but the Port fully agrees that policies such as fraud awareness, ethics and anti-harassment need regular communication and training to be fully effective. The planned workplace responsibility awareness program will feature formal initial and reinforcement training.

In November, Port staff members were notified that they were required to complete an on-line anti-harassment training module by December 31. New hires will receive the full course; all other employees will be given a follow-up course every 18 months. This model of mandatory initial and reinforcement training will be evaluated for use with other policies such as ethics and fraud awareness. The CEO has asked staff to prepare a proposed formal training plan for his review by February 15.

Other training programs, such as lunch training sessions, will be used while more formal training is being constructed.

A complete remodel of the Port's internal website is already underway. The new design features easier employee access to policies as well as any accompanying materials.

Recommendation B: Ensure all procurement processes comport with Port policy and State and Federal law.

Recommendation B.1: Implement a mechanism to ensure that all procurement processed comport with Port policy, as well as state and federal law.

In response to the State Performance Audit, the Port established a Central Procurement Office (CPO) which has been fully functional for several months and has placed early emphasis on quality control and staff training. The CPO is responsible for providing guidance and oversight of the procurement process to ensure that Port policies and procedures comply with applicable federal and state laws. Relevant state laws and policies are used to establish and revise explicit procedures; then, Port staff members are trained to follow the procedures so that only those trained to do so have contracting responsibilities. In addition, the Port is implementing quality control procedures to check that procedures are being followed, and has begun using the organization's internal audit department and other resources for independent quality assurance.

Recommendation B.2: Review procurement processes with respect to both state and federal law.

The CPO is currently considering three fundamental process improvements and changes:

- The CPO will review all applicable state procurement laws to ensure that the Port is complying with those requirements, and will establish any additional necessary policies and/or procedures. The CPO will draft or revise applicable policies and procedures and practice guidelines as necessary.

- Clarify Port practices for communications with third parties during the procurement process. In the future, for service agreements over \$200,000 and all construction procurements, all communication must be directed through CPO staff during the procurement process through contract execution. However, a Port project manager may conduct negotiations directly with the consultant after the Port has selected the most qualified firm and notified all bidders of the decision. CPO staff members, as professional procurement staff, should manage any such communication to ensure compliance with federal and state laws and to maintain a fair and transparent competitive process. The CPO will provide additional training and direction so that Port staff members understand the limitations placed on discussions and communication with potential bidders, subcontractors, suppliers, consultants and vendors.
- Improve how procurement requests are submitted to the CPO for service agreements, construction, and goods and services. Currently, no overall central system exists, although a unified system is in place for construction and goods and services.

In addition, the CPO will work with requesting departments to identify all federal and grant dollar requirements and review the documents to be certain that those requirements are contained in the procurement and contract documents.

Recommendation B.2.a: Professional Service Agreements (PSAs) – ensuring the Port is in compliance with the conditions applied to grant dollars.

The Port is implementing a revised policy on service agreements that provides for CPO oversight and more explicit definitions of the categories of service agreements and procedures for each category. The policy will replace existing policies. This training will begin in January/February 2009.

With respect to the procurement of professional and personal services, the Port has implemented requirements as to when the Port Commission is informed of advertisements and, in many cases, the Port will obtain Commission approval prior to contract execution. The Port Commission will be notified of all amendments to service agreements when the amendment(s), either singly or cumulatively, exceeds fifty percent of the original contract value.

The Port has notified and is working with FAA representatives to ensure that any questions regarding grant funding on the major 2004 and 2006 Embankment Contracts are identified and addressed.

Recommendation B.2.b: Small Works Roster Program – ensuring the Port is in compliance with the conditions applied to grant dollars.

The Port conducted classes for Port Construction Services personnel regarding proper Small Works contracting procedures on March 20, 2008. Topics included:

- Revised procedures for tracking small works expenditures against budget
- Work requests and authorizations
- Cost limitation language for contracts
- Contract work authorization estimate and tracking sheet

The CEO has directed that additional training must occur by the end of January 2009 for the Port Construction Services and Central Procurement Office staff members who award or administer these contracts. This additional training will address:

- Procedures for soliciting bids from the roster and for public advertising;
- Procedures for enrolling new contractors on the roster and for updating the roster information;
- Procedures for contacting contractors by e-mail and making corrections to addresses;
- Document tracking and resending of information when applicable;
- Rules for structuring Small Works contracts with respect to the \$200,000 limit.

Since Fall 2006, the Port has been advertising Small Works contracts to all registered contractors on the Small Works Roster as well as posting each advertisement on the Port's small works public website and on a wall display located in the PCS office.

In May of 2008, Interim Capital Development Director Dwayne Lee discovered through an internal review that Small Works Roster contracts were being broken into smaller contracts to fit within the \$200,000 statutory limit. Mr. McKay included that in his report. The Port does not condone that practice. Mr. Lee provided guidelines on Small Works Roster in July 2008, including the following:

- Requiring a justification memo be placed in the file describing Port Construction Services participation and setting forth the reason for using a Small Works contract for any Small Works contract that is part of a larger project costing more than \$200,000;
- Listing appropriate circumstances when a Small Works contract or contracts may be structured at less than \$200,000, even if it is part of a larger work effort;
- Requiring review by the Central Procurement Office and the Capital Development Division of such justification memos.

Over the past few weeks, the Capital Development Division Director reviewed the list of Small Works contracts awarded in 2008 to confirm that improper "contract splitting" is not still occurring. He did not find any evidence of improperly split contracts awarded since May 2008. There are legitimate circumstances when structuring project work into Small Works contracts of less than \$200,000 is legal and appropriate, so there may be some confusion even within PCS about when such a practice is allowed. Training will emphasize those distinctions.

Recommendation B.2.c: Major Construction – ensuring the Port is in compliance with the conditions applied to grant dollars.

The Port provided timely notification and a complete copy of the McKay findings to the FAA. The Port intends to fully cooperate with any follow up reviews, or other actions the FAA may require.

Recommendation B.3: Senior Port leadership, in conjunction with Port legal department, conduct a detailed review of all procurement aspects at the Port to ensure policies and procedures are in compliance with state and federal law.

Review and revision of Port contracting procedures is underway. The CPO is currently working on revisions to Port policies and procedures regarding the procurement of personal and professional

services. The Port will adopt and implement those provisions by February 2009. Training on the new policies and on Resolution 3605 will begin concurrently with implementation. The CPO is also beginning to consider revisions and new policies, procedures, and/or practice guidelines for goods and services, major construction and the small works roster, as well as other purchasing and procurement activities in the coming year.

Recommendation B.4: Consider amending Port policies to clarify that the Engineer's Estimate against which contractor bids are compared is the Engineer's Estimate that is required under state law to be prepared prior to the advertisement for bids in major construction contracts for public works. Engineer's Estimate should be preserved intact and not altered after the advertisement is published, unless a formal addendum is also published.

The Port will develop a policy and publish procedures no later than the end of January 2009 clarifying when and how the Engineer's Estimate is compiled, how it must be protected as "procurement-sensitive information," how bids are evaluated against the estimate and what steps must be taken if the apparent low bid exceeds the estimate by more than 10%.

Recommendation B.5: Upon completion of review and updating on policies and procedures, all Port employees and consultants who are responsible for procurement tasks should receive comprehensive training on both the laws and the policies pertaining to their duties.

Extensive training has already occurred including:

- Training on the areas of responsibility for all change orders and change order documentation, as well as roles and responsibilities within the new review process and contract schedule enforcement.
- Revised construction and contract management processes training was conducted by Engineering and Central Procurement Office staff.

PCS staff was notified via email and trainings were held on expected compliance with new procedures, especially in comparing expenditures to budgeted limits.

Training on contracting for consultant services was initially provided to two groups, and will be scheduled subsequently for all other appropriate individuals.

In addition, the CPO plans to establish and conduct a program of ongoing training for all Port staff responsible for procurement and contract administration tasks. Eventually, the CPO envisions implementing two training programs: (1) a certification program for CPO staff and (2) a certification program for any Port staff involved in any procurement actions or responsible for performing certain contract administration duties.

- The CPO Staff certification program would be similar to the Federal government warranted contracting officer program. CPO staff would attend a series of federal classes that warranted contracting officers are required to complete and other classes that we determine appropriate.
- For the Port staff certification program, CPO would develop a series of in-house training courses. Port staff members would be required to complete the training prior to participating in procurement tasks and/or certain contract administration tasks.

These certification programs require substantial investment of time and money. In the meantime, given time and financial constraints, the CPO will develop training sessions on the new policies and procedures as they are developed, Resolution 3605, and source selection evaluation. The CPO currently plans to implement the first training on the new policy and procedure for service agreements and Resolution 3605 in January/February 2009. Likewise we hope to implement training on source selection evaluation in January/February 2009.

Recommendation C: Increase legal department involvement in the procurement process.

Recommendation C.1: Increase involvement of legal department at all levels of the procurement process in order to contribute to more transparent Port procurement activities and more limited opportunities for circumvention of procedural safeguards.

The Legal Department regularly consults with the CPO and the Capital Development Division on matters of policy development, interpretation of standards, regulations, Port policy documents and statutes and to ensure that standard practices, procedures and documents comply with applicable law. Exceptions to internal CPO and Capital Development Division practices and procedures are regularly coordinated with the Legal Department. Management of the Procurement and Legal Departments are engaged in on-going discussions to identify additional, more formal and more frequent consultation processes.

Recommendation C.2: All procurement actions should receive legal review.

The Legal Department is regularly involved with capital project development and procurement decisions as projects progress through planning to completion. However, legal review of procurement decisions and documents must take into account the Central Procurement Office and Capital Development Division role in the review, training and enforcement of procurement procedures, as well as their specialized expertise. The Legal Department and the CPO and Capital Development Division are currently working to implement practices that will assure appropriate legal review without creating duplicative or unnecessary review levels.

Recommendation D: Ensure legal department involvement is appropriately documented, i.e. maintain a record of actions reviewed, inquiries made, and/or legal advice provided.

The Legal Department has prepared a set of draft guidelines for documenting and distributing legal advice that will be finalized and published by December 31, 2008. In summary, the guidelines will distinguish between discussions involving straightforward procedural issues that carry minimal legal risk from more complex issues that include an element of material risk. Written record will be made for matters involving material legal risk, or that in the judgment of the attorney should be recorded.

The Legal Department attorneys frequently attend planning and strategy meetings where legal risk is not the subject, but where they may make an observation about a potential legal issue that could arise. If in the judgment of the attorney a material legal issue has been raised or appears to have been overlooked, a written opinion typically will be issued.

Recommendation E: Centralize procurement document management system.

Recommendation E.1: Consider implementing a centralized procurement documents management system.

In early 2009, the Central Procurement Office will determine an appropriate document management system for both hard copies and electronic files. Currently multiple systems are used for small works, major construction, service agreements and goods and services. Funding is provided in the 2009 budget to establish a centralized filing system, and CPO staff members are currently exploring options.

Protocols and procedures need to be established for matters such as where the official files are maintained, who has responsibility to maintain the documents/files and ensure all documents are in the file, how we handle and manage electronic files, what has to be maintained in hard copy, and what controls are needed for managing use of the files.

Developing protocols is not a simple matter: Port staff members are located in many different buildings and there are legitimate reasons why some files must be maintained at different locations. CEO Yoshitani has instructed the CPO staff to make this goal a priority in early 2009.

Recommendation E.2: Evaluate the current contract file management system and consider a more centralized, accessible system.

See above responses.

Recommendation F: Standardize project manual provisions used in major construction projects.

The Port recognizes the value of a central, consistent, explicit set of standard instructions and common contract provisions to guide the many staff members involved in forming and administering construction contracts. Creating one falls to the newly-formed Capital Development Division which includes project managers, contract specialists and construction managers. A computer-based system would be readily available, standardized for all users and easily updated. Establishing such a system requires identifying applicable laws, policies and best practices, ensuring that procedures meet the needs of the Port's wide variety of construction types, locations and customers and compiling a large quantity of information. Once the manual is written and posted, the Capital Development Division will train staff on its use, follow up to ensure compliance and periodically review for updates.

Recommendation G: Include an enforceable audit provision in all contracts that survives termination of the contract.

Contract provisions for construction (both major construction and small works) and service agreements need to be reviewed and updated or revised. An appropriate audit provision and duty to cooperate provision will be included in the terms. This is another goal of the CPO, but a time frame for beginning and completing this goal is not yet established. As an interim measure, the Port will include an audit provision as a supplemental condition in all small works procurements initiated after January 1, 2009.

Recommendation H: Consider appropriate personnel action.

In reviewing the report findings and deciding upon discipline, the CEO considered the severity of the finding and the extent of involvement. A higher level of expectation exists for leadership. Each and every manager has a responsibility to spot potential fraud and take action to stop it, no matter who is directing that fraud, including the CEO.

Mr. McKay identified two employees that he deemed worthy of particular emphasis when I reviewed appropriate discipline for fraud. He did not make specific recommendations of action, but rather highlighted two employees who were directly involved in the majority of actions that met the test of fraud.

The CEO immediately reviewed the associated material and initiated action against these two employees. When confronted, John Rothnie, Project Manager for the Third Runway project and Larry McFadden, General Manager of Port Construction Services, chose to resign.

Different levels of discipline have been given to those associated with the commission memo outlining the contract for TTI.

Ray Rawe, Chief Engineer, will receive a three week suspension without pay because he had knowledge of the memo and was in a position to identify the misrepresentation but did not do so.

Three senior managers have received one week's suspension without pay for their failure to mention the contingent nature of the contract adjustment: David Soike, Deputy Managing Director, Aviation; Paul Powell, Manager, Contract Services; and Robert Riley, Director, Aviation Capital Improvement Program.

Finally, the CEO will place letters of reprimand in the personnel files of Linda Strout, Deputy CEO; Mark Reis, Managing Director, Aviation; and Craig Watson, General Counsel. Given their positions of authority and the importance of the issue, the CEO believes that they should have been engaged in reviewing the commission memo and ensuring it was accurate.

If new information comes out from the Department of Justice investigation or other regular audits, I will consider further disciplinary action. There are still a few details to follow up on in the McKay report; these disciplinary actions represent the majority of the issues.