Office of the New York State Comptroller



DIVISION OF STATE GOVERNMENT ACCOUNTABILITY

Port Authority of New York and New Jersey

Contracts for Personal and Miscellaneous Services

Report 2009-S-54

Thomas P. DiNapoli

This page is left intentionally blank.

Table of Contents

Authority Letter
Executive Summary7
Introduction
Background9
Audit Scope and Methodology11
Authority12
Reporting Requirements12
Contributors to the Report12
Audit Findings and Recommendations
Contract Justification
Call-In Agreements
Service Contracts14
WTC Service Contracts15
Contract Authorization16
Reassessment of Service Contracts17
Recommendations
Exhibit A22
Agency Comments
State Comptroller's Comments

This page is left intentionally blank.

State of New York Office of the State Comptroller

Division of State Government Accountability

July 19, 2011

Mr. David Samson Chairman Port Authority of New York and New Jersey 225 Park Avenue South New York, NY 10003-1604

Dear Mr. Samson:

The Office of the State Comptroller is committed to helping State agencies, public authorities and local government agencies manage government resources efficiently and effectively and, by so doing, providing accountability for tax dollars spent to support government operations. The Comptroller oversees the fiscal affairs of State agencies, public authorities and local government agencies, as well as their compliance with relevant statutes and their observance of good business practices. This fiscal oversight is accomplished, in part, through our audits, which identify opportunities for improving operations. Audits can also identify strategies for reducing costs and strengthening controls that are intended to safeguard assets.

Following is a report of our audit of *Contracts for Personal and Miscellaneous Services*. The audit was performed pursuant to the State Comptroller's authority as set forth in Section 7071 of McKinney's Unconsolidated Laws of New York.

This audit's results and recommendations are resources for you to use in effectively managing your operations and in meeting the expectations of taxpayers. If you have any questions about this report, please feel free to contact us.

Respectfully submitted,

Office of the State Comptroller Division of State Government Accountability

This page is left intentionally blank.



State of New York Office of the State Comptroller EXECUTIVE SUMMARY

Audit Objectives

One objective of our audit was to determine whether the Port Authority of New York and New Jersey (Port Authority) justified the need to contract for personal and miscellaneous services. Another objective was to determine whether the Port Authority periodically reassessed personal and miscellaneous services contracts to identify what work could be deferred, eliminated, or reduced to save funds.

Audit Results - Summary

The Port Authority obtains personal and miscellaneous services through two types of agreements: Service Contracts and Call-In Agreements. Service Contracts are usually for routine service functions such as cleaning, maintenance and repairs, and waste management, as well as project-related services such as construction management. Call-In Agreements cover temporary staffing services and professional, technical and advisory services, etc. According to available records, the Port Authority had 1,858 Service Contracts and Call-In Agreements valued at \$4.38 billion in effect during the period April 1, 2006 through July 30, 2009.

We found that the Port Authority generally did not have documentation to justify the need for new or renewed contracts for personal and miscellaneous services. For example, we reviewed a sample of 75 Service Contracts and Agreements with a total value of \$1.3 billion and found that the Port Authority lacked written support for the need for 57 of these contracts valued at \$1.18 billion. The primary reason for this is that the Port Authority did not require the departments seeking contract services to document their need for contracting for these services.

In addition, the Port Authority did not provide documentation to support that it periodically reassessed all of its contracts for personal and miscellaneous services. Therefore, the Port Authority may be missing opportunities to further reduce costs and save funds. If the Port Authority attained a 10-percent reduction in just the contracts we sampled, the Port Authority could realize savings of \$22 million each year.

Port Authority officials stated their business model is to outsource certain non-core functions, which they indicate allows them to focus on mission-critical objectives and achieve cost savings. The business model does not require the departments requesting these contracts to perform and document an assessment that would establish that outsourcing is the best approach to

accomplish the task. In this regard, it should be noted that the Port Authority has imposed strict caps on the number of its staff, with a goal of zero growth in personnel. As a result, even when analysis shows it is cost-effective to hire additional staff in order to bring contract work in-house, such initiatives are not permitted; and departments are expected to use contract services to obtain the staffing they need to meet the demands of their work.

The contract personnel are an additional aspect of the work force of the Port Authority, but are not disclosed in the count of personnel necessary to accomplish the Port Authority's work. Therefore, we recommend that the Port Authority demonstrate the true amount of resources needed to operate Port Authority facilities by publicly disclosing the number and cost of individuals it employs under contracts and agreements.

Our report contains five recommendations for improving the Port Authority's efforts to attain savings through justification and reassessment of its contracts for personal and miscellaneous services.

This report, dated July 19, 2011, is available on our website at: http://www.osc.state.ny.us. Add or update your mailing list address by contacting us at: (518) 474-3271 or Office of the State Comptroller Division of State Government Accountability 110 State Street, 11th Floor Albany, NY 12236

Introduction

Background

The Port Authority of New York and New Jersey (Port Authority) was established on April 30, 1921 under a clause of the United States Constitution permitting compacts between states. Its area of jurisdiction is called the Port District, a bi-state region generally within 25 miles of the Statue of Liberty. The Port Authority's mandate is to promote and protect the commerce of the bi-state port and to undertake port and regional improvements not likely to be financed by private enterprise or to be attempted by either state alone. It manages a network of aviation, ground transportation infrastructure, and seaport facilities organized in the following five departments: Aviation; Tunnels, Bridges & Terminals; Port Commerce; Port Authority Trans-Hudson (PATH); and Real Estate & Development. In 2010, the Port Authority employed a staff of 6,977. The Port Authority is also the owner of the World Trade Center (WTC), and is responsible for the construction and development of the Transportation Hub, the Freedom Tower (1 WTC), and WTC retail space.

The Port Authority obtains personal and miscellaneous services through two types of agreements: Service Contracts and Call-In Agreements. Service Contracts are usually used for routine service functions such as cleaning, maintenance, and repairs; waste management, as well as project-related services such as construction management; etc. Call-In Agreements cover temporary staffing services and professional, technical and advisory services, etc. According to available records, the Port Authority had 1,858 Service Contracts and Call-In Agreements in effect during the period April 1, 2006 through July 30, 2009 as follows:

Contracts Covering	Number	Amount	Total
Service Contracts:			
World Trade Center Projects	39	\$ 326,978,537	
Cleaning	64	199,987,223	
E-Z Pass	5	133,502,740	
Information Technology	185	176,356,953	
Security	29	453,901,304	
Facility Operation and Maintenance	15	261,475,802	
Maintenance Services	346	258,562,419	
Miscellaneous	510	1,862,711,324	
Sub-total - Service Contracts	1,193		\$ 3,673,476,302
Call-In Agreements:			
World Trade Center Projects	2	\$ 257,094,476	
Technology	15	4,923,469	
Human Resources	10	250,000	
Law	21	1,960,322	
Engineering	542	370,392,515	
Aviation	16	6,782,970	
Real Estate	40	45,222,717	
Other	19	18,103,602	
Sub-total – Call-In Agreements	665		704,730,072
Total	1,858		\$ 4,378,206,374

The Port Authority authorizes contracts through various means. Some contracts require board approval (Board Items). However, authorization for most Service Contracts and Call-In Agreements is delegated to the Executive Director, Department Director or other staff. Authorization for contracts and agreements over \$1.5 million is obtained by Memorandum of Justification (MJ). MJs are provided to the Board at its meeting, and unless the Board objects, are returned to the designated approver for signature. Authorization for contracts and agreements of \$1.5 million or less is obtained by Memorandum of Authorization (MA), which is signed by the designee and does not go to the Board. The MA or MJ includes the scope of work, estimated cost, and the selection process to be followed, and is prepared after the decision to contract for services.

Port Authority executive management issues annual budget memoranda, which since 2007 have expressed a policy of cost containment and "fiscal discipline" regarding operating expenses, with moderate increases of 1.1 percent in 2007, 0.9 percent in 2008, and no increase in 2009, by keeping its staffing levels flat. The Port Authority reports that its 2010 budget provided for 6,977 authorized positions, the lowest staffing level in 40 years. According to information provided by the Port Authority, about 75 percent of the 1,858 contracts and agreements were awarded using a competitive process (See Exhibit A).

Audit Scope and Methodology

One objective of our audit was to determine whether the Port Authority of New York and New Jersey justified the need to contract for personal and miscellaneous services, or for their continued use. Another objective was to determine whether the Port Authority periodically reassessed personal and miscellaneous services contracts to identify what work could be deferred, eliminated, or reduced to save funds. For the purpose of our audit, personal and miscellaneous services contracts are those in which the majority of the costs associated with the contracts are for services and labor. We did not include contracts for commodities or capital construction work. Our audit included contracts in effect at any time between April 1, 2006 and July 31, 2009, and our field work was performed between September 2009 and June 2010.

To achieve our objectives, we interviewed Port Authority personnel and reviewed contracts, Procurement Guidelines, and other supporting documentation provided by the Port Authority. We selected a judgmental sample of 75 of the 1,858 contracts active during our audit period (30 Service Contracts, 26 Call-In Agreements, and 19 contracts to provide WTC-related services) with a total value of \$1.38 billion. The contracts we selected were for engineering, architectural, design, construction management, janitorial, security-related, and other miscellaneous services. The value of each contract exceeded \$50,000. To obtain documentation that would justify the outsourcing of these 75 functions, we held 41 meetings with 71 department officials whom Port Authority officials designated as the correct sources of information regarding the sampled contracts.

We conducted our performance 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.

In addition to being the State Auditor, the Comptroller performs certain other constitutionally and statutorily mandated duties as the chief fiscal officer of New York State. These include operating the State's accounting system; preparing the State's financial statements; and approving State contracts, refunds, and other payments. In addition, the Comptroller appoints members to certain boards, commissions and public authorities, some of whom have minority voting rights. These duties may be considered management functions for purposes of evaluating organizational independence under generally accepted government

	auditing standards. In our opinion, these functions do not affect our ability to conduct independent audits of program performance.			
Authority	This audit was performed pursuant to the State Comptroller's authority as set forth in Section 7071 of McKinney's Unconsolidated Laws of New York.			
Reporting Requirements	A draft copy of this report was provided to Port Authority officials for their review and comment. Their comments were considered in preparing this final report, and are attached in their entirety to the end of this report. We have also added State Comptroller's Comments to address part of the Port Authority's response.			
	Within 90 days of the final release of this report, we request that the Chairman of the Port Authority of New York and New Jersey report to the State Comptroller, advising what steps were taken to implement the recommendations contained herein, and where recommendations were not implemented, the reasons why.			
Contributors to the Report	Major contributors to this report include Carmen Maldonado, Robert Mehrhoff, Erica Zawrotniak, Alina Mattie, and Altagracia Rodriguez.			

Audit Findings and Recommendations

We reviewed 75 contracts valued at \$ 1.3 billion and found that the Contract **Justification** Port Authority did not justify with documentation the need for 57 of these contracts valued at \$1.18 billion. Instead, Port Authority officials provided verbal explanations such as the lack of necessary in-house skills and the temporary nature of work as justification for contracting. Port Authority officials also stated that their business model is to outsource certain non-core functions in order to focus on mission-critical objectives and achieve cost savings. However, officials also stated that they do not require the departments requesting contracts to perform an assessment that would determine the best approach to accomplish the task. (We note that the Metropolitan Transportation Authority's All Agency Guidelines For Procurement of Services require that its constituent agency, prior to preparing a contract submission to the Board, document its determination that outsourcing is preferable because of factors such as timing, costs, workload analysis, qualifications, or nature of the services to be rendered.) In addition, the Port Authority has imposed strict caps on the number of its staff, with a goal of zero growth in personnel. As a result, even when analysis shows it is cost-effective to hire additional staff in order to bring contract work in-house, such initiatives are not permitted; and departments are expected to use contract services to obtain the staffing they need to meet the demands of their work. Call-In Department officials did not justify the need for 25 of 26 sampled Call-Agreements In Agreements we reviewed. The total value of these 25 agreements was \$98.9 million. One contract, for \$4.5 million, was initially justified. Officials initially indicated that MA and MJ documents would discuss the need to contract for services. However, they did not provide an MA or MJ or any other documents that address the need for 6 of the 25 contracts. Moreover, when we reviewed the 19 documents that were provided, we found they did not support the basis for the decision to contract out. Port Authority officials told us they use Call-In Agreements on an "as needed" basis when additional staff is needed, specific types of expertise not available in-house are required, or when unforeseeable temporary circumstances create a need for services on short notice. However, we found that much of the Call-In work was pre-planned and not short-term. In fact, the departments were using Call-In Agreements to supplement their staffs on an ongoing basis. For example, in one department, the cost of the consultants increased 39.5 percent from \$78 million in 2006 to \$106 million in 2009.

Consultants working for the Engineering Department, the largest user of the Call-In program, perform various duties including design, inspections, quality assurance testing, construction management services, and topographic services. Although Department officials told us they might not use all of the \$85 million authorized for its five-year program agreements (2006-10), we found that they had spent \$54 million in the first four years and planned to spend another \$25 million in 2010, exhausting almost all of the funding.

Other departments used Call-In Agreements to supplement their staff on a continuing basis. The Real Estate & Development Department issued a contract for advisory services related to the new WTC at a cost of \$36 million for a three-year period (2008-11), with two extension years at additional cost. The consultant provided real estate advisory services such as developing business plans, negotiating support, security, and retail facility design oversight. Although the Port Authority already has a real estate department, we saw no analysis of the department's ability to do any of this work itself with existing or additional in-house resources.

ServiceDepartment officials did not justify the need for 25 of the 30 ServiceContractsContracts we sampled. We reviewed the documents that were provided
for these contracts and we found they did not support the basis for the
decision to contract out. The value of the 25 contracts was \$785.1 million.
The other five valued at \$4.4 million were justified.

Port Authority Bus Terminal officials informed us that Port Authority management did not require them to substantiate the need for a 6-year cleaning contract costing \$27.5 million. The officials pointed out that Port Authority staff cleaned the bus terminal prior to 1980, but an assessment that year indicated that outsourcing this type of work would be less expensive. Since then, the Port Authority has adopted a practice of outsourcing its cleaning, janitorial, waste management, customer services, and maintenance and repair work without asking for a new assessment. We question whether the Port Authority should base its decision about continued outsourcing on a 30-year-old analysis, as underlying assumptions may change significantly over time.

In another instance, the Port Authority contracted for security guard service at multiple facilities at a cost of \$134.2 million for four years. This contract consolidated separate contracts for several facilities, as recommended by a consultant. However, no analysis was performed to determine whether this service should have been outsourced.

We also noted changes in Port Authority policy that impacted the cost of certain Service Contracts. In 2007 the Port Authority changed its policy

Office of the New York State Comptroller

for non-trade labor services, requiring changes in health, wages, and other supplemental benefits contractors must offer. Two recent outsourcing contract awards showed significant cost increases: Cleaning services for PATH Journal Square station and facilities increased 21 percent over the previous year, due to higher wages and benefit rates; and unarmed uniformed security guard services at multiple Port Authority facilities increased about 47 percent over the prior contracts. (For the security contract, about half of the increase resulted from additional positions necessary to meet security requirements.)

The Port Authority has also entered into a 3-year contract, valued at \$1.2 million, described as Electrical Maintenance Services at various facilities in New York City. Essentially, this contractor provides an electrician to change light bulbs and ballasts. No support has been provided that would indicate whether this contract was more cost-effective than employing Port Authority staff in these tasks.

WTC ServiceThe Port Authority is the owner of the World Trade Center (WTC) site.ContractsIt has assumed a direct development role for certain parts of the Center,
including construction of the Freedom Tower, Transportation Hub,
PATH station, and retail space. The Port Authority took over some of this
work from the private developer of the site, including existing contracts,
and has entered into new Service Contracts for other work related to the
WTC.

The Port Authority provided a listing of 41 contracts for services worth \$584 million related to the WTC in effect during the period April 1, 2006 through July 30, 2009. We sampled 19 WTC Contracts with a reported value of \$387.3 million.

Port Authority officials informed us that several of the contracts we sampled related to the 2006 agreement to the transfer of certain components of the WTC from the private developer to the Port Authority. Ten sampled contracts, totaling \$240.8 million, were taken over from the WTC's private developer by Board action. Two agreements, totaling \$22.0 million, reimburse the private developer of the WTC for the cost of services related to design of parking and retail space at the WTC site. Since the Port Authority did not make the initial choice to seek these contracts. Although we requested supporting documentation for the decision to assume responsibility for these portions of the WTC development, these documents were not provided.

For the remaining seven contracts totaling \$294.5 million, the Port Authority did not justify the decision to contract for services. Department

officials provided authorizing documents for six of the seven contracts: MJs for four contracts, a Board item for one contract, and a combination of MJs and Board items related to one contract. Officials told us these documents were sufficient to support their requests for outsourcing. For one contract with a value of \$500,000, we were not provided with documentation of authorization (MA signed by the designated approver) to enter into a contract.

We found that the MJ documents do not justify the need to contract for personal or miscellaneous services. Board items do not justify need; they only approve the action of contracting. The officials provided explanations, but did not provide documentation substantiating the need to outsource the seven sampled contracts totaling \$294.5 million that have been issued for the WTC.

While there are times when outside consultants must be hired, a documented analysis delineating the rationale for the decision to contract for services is important, even in these cases. Such documentation is important to fully support that the Port Authority's conclusions are correct and that opportunities and options for cost savings have been fully considered.

Contract Authorization The Port Authority does not require the department requesting contract services to document the basis for the decision to contract out. Generally, department officials provided an MA or MJ, which they believe is sufficient to support their request to outsource a service. However, these documents are prepared to support award of a contract, and generally do not provide the basis for the decision to contract out. Most officials provided verbal explanations but no documentation. Other officials provided documents that did not pertain to the initial decision to enter into the contract.

Some Department officials told us that, even if cost analyses indicate the addition of in-house staff would be cost-effective, requests to do so would most likely be turned down. For example, we were told that Management and Budget Department (MBD) denied a request to hire 2 temporary Maintenance Group Supervisors and 20 temporary General Maintainers for snow removal and other ground maintenance tasks at JFK Airport to replace contractors at a cost savings. Another official informed us that certain information technology work could be done in-house at a lesser cost than by a contractor. This request was also denied. At the closing conference for this audit, MBD officials indicated that the mandate to keep staffing levels flat would restrict additional hiring, even if proven cost-effective. As a result, departments continue to need to rely on

contract services for obtaining the staff necessary to meet its operating needs.

It is apparent that the use of contractors to perform several operations at the Port Authority is in line with management's model to use its employees for core services. As a result, the Port Authority extensively relies on them for essential services. We noted that several of the contacts are for multiple years and not periodically evaluated because the services are part of the daily operations at the Port Authority - e.g., snow removal, cleaning terminals, security, engineering, and construction management.

For example, the Engineering Department's staffing costs in 2009 were \$91 million and the cost of the consultants was \$106 million. We also noted that the Engineering Construction Management Division's staff of 153 employees was supplemented by 133 contractor employees. Although Engineering's Call-In program has been in place for the past 25 years, a cost analysis is still not prepared that compares the annual costs of outsourcing a task with the costs of hiring additional staff. Another example is the Law Department, where temporary staffing has been used to supplement its paralegal and litigation support staff for the past 17 years.

In another instance, the Port Authority contracted for security guard service at multiple facilities at a cost of \$134.2 million for four years. This contract consolidated separate contracts for several facilities; however, there was no information to support the decision to outsource these security services.

Therefore, to accurately report on the costs of operating the Port Authority, contract personnel should be considered a shadow work force of the Port Authority. We recommend that the Port Authority demonstrate the true amount of resources needed to operate its facilities by publicly disclosing the number and cost of individuals it employs under contracts and agreements.

Reassessment of The Port Authority does not periodically review all of the Service **Service Contracts** Contracts it is using to identify work that could be deferred, eliminated, or reduced to save funds.

Officials indicated that, as part of the annual budget process, Department officials may seek cuts or cost savings in various aspects of their operations, including contract services, to meet the overall goal of zero growth in expenses and staffing. The Management and Budget Department (MBD) reviews budget requests from the various departments and offices. Once the budget is adopted, MBD continually assesses the overall financial

and operating results of all Departments and offices compared to the approved budget. MBD does not require Departments to reassess every contract.

Although MBD officials informed us that they do not normally reassess the need for existing contract services, they did undertake several budget-related initiatives during 2009 at the direction of the Executive Director. For example, one initiative identified opportunities to reduce the Aviation Department's contract services by about \$15.7 million (including reductions to janitorial services, customer services, and ground transportation).

MBD officials provided a June 2009 document that indicates an agencywide goal to reduce consultant use by 40 percent and a memo that indicates Departments must reduce their 2010 budget request for consultants by 50 percent of the reduced 2009 budget. However, we noted the Engineering Department's 2010 budget for architectural/engineering services was \$133.4 million, only \$6.4 million (or 4.6 percent) less than the prior year. Port Authority officials told us that the June 2009 directive did not apply to the Engineering Department; however, the directive noted no such exception.

For 3 of the 26 sampled Call-In Agreements, MAs/MJs indicate they are subject to annual requests for funding. However, no request for funding was made in the subsequent contract years. In response to a preliminary finding, Port Authority officials informed us that funding is addressed through the budget process, and there is no formal revision of the MA/MJ or documentation of annual funding approvals for specific contracts that have previously been authorized. We believe the annual budget request provides an opportunity to reassess the need for such funding and services based on current circumstances.

In the same response, Port Authority officials advised that MBD implemented a new process for requesting consultant contracts in the first quarter of 2010. Departments are allowed the use of consultant contracts only for high-priority projects and would have to ensure that all available internal resources are fully utilized before any request for such contracts is submitted. In addition, MBD approval would be required before work orders are awarded under Call-In Agreements.

The Port Authority does not reassess all of its contracts for personal and miscellaneous services. Therefore, it may be missing opportunities to further reduce costs and save funds. If it attained a 10-percent reduction only in the contracts we sampled, the Port Authority could realize savings of \$22 million each year.

Office of the New York State Comptroller

Recommendations 1. Require department officials to document, prior to preparing the Memorandum of Justification, Memorandum of Authorization or Board Item, that outsourcing is more beneficial to the Port Authority because of factors such as timing, costs, workload analysis, qualifications, or the nature of the services to be rendered.

(Port Authority officials replied to our draft audit report that the Port Authority has several corporate practices and processes in place governing the procurement of outside services. They also indicated they have implemented certain enhancements that resulted in a reduction of \$14 million in consultant services costs. With regard to other service contracts, as recommended, they will be implementing additional procedures designed to enhance controls.)

<u>Auditor's Comments</u>: Our report reflects the 2010 enhancement referred to on page 1 of the Port Authority's response. The only new information is that they reduced consultant service costs.

2. Justify the current practice of holding staff size at a fixed level and obtaining needed services through Service Contracts or agreements, stating why it is in the best interest of the Port Authority and the public it serves.

(Port Authority officials replied to our draft report that they do not have a practice of maintaining staff at a fixed level while obtaining services through contracts or agreements. Instead they have a business model designed to optimize the use of permanent and contract resources which provides maximum flexibility and the ability to respond to changing priorities. They added that flexibility of the model has allowed them to address new business initiatives such as the acquisition of Stewart International Airport and the redevelopment of the World Trade Center through the redeployment of existing resources.)

<u>Auditor's Comments</u>: While many labels can be used to describe the manner in which the Port Authority operates, the message was clear that staff levels would be maintained. For example, one document in the 2010 Budget package states "Last year, the Port Authority introduced a zero-growth operating budget and kept the agency's headcount flat. This year, the agency will go even further, implementing the agency's second straight zero-growth operating budget and cutting authorized positions down to the lowest level in 40 years." Another budget planning document dated in early 2009 states "Zero percent growth in annual operating expenses and staffing levels." Thus managers did not seek to evaluate whether the work that had to be performed should be done by changing the number of Port employees or by obtaining contract services. Regarding Stewart International Airport, we did not see evidence to support the statement that resources were redeployed. Information providedshowsthereareonlyninePortAuthorityemployeesatStewart, but there is a five-year \$59.6 million operation and maintenance contract with an outside vendor. As for the redevelopment of the WTC, according to the contract information provided during the audit, the Port Authority has two contracts totaling \$22 million which they told us is for the redevelopment of the WTC.

Thus, the Port Authority needs to demonstrate the "maximum flexibility" resulting from the use of contract services while the number of employees is constant or reduced is in the best interest of the public it serves.

3. Demonstrate the true amount of resources needed to operate Port Authority facilities by publicly disclosing the number and cost of individuals it employs under contracts and agreements.

(Port Authority officials replied to our draft report that the recommendation as presented is not an opportunity to enhance their practices, but instead indicates that they are intentionally concealing information. They added that from a transparency standpoint, all Requests for Proposals, bid solicitations, Board actions, and contracts over \$25,000 are posted on award to the Port Authority's web site and are fully disclosed to the public. Likewise, their annual budgets and financial statements are on the web site.)

<u>Auditor's Comments</u>: While the Port Authority's financial statements disclose costs, the true impact in terms of the number of persons it takes to run the Port Authority's operations is not disclosed. We do not maintain that the Port Authority "intentionally conceals" this information. However, we believe that the public has a right to know how many people it takes to provide the services the Port provides. We view this as an opportunity for the Port Authority to demonstrate to the public the full extent of its impact on the job market by reporting the number of "non-core" employees engaged through its contracts for services.

4. Develop uniform written guidelines for entering into all Service Contracts and agreements that clearly delineate required steps, analyses, and documentation to support the decision to outsource, and specify the retention period.

(Port Authority officials replied they will prepare supporting documents for all service contracts that will demonstrate the benefits of outsourcing is consistent with existing guidelines and procedures.)

<u>Auditor's Comments</u>: We are pleased that Port Authority officials plan to document the benefits of outsourcing, however, it is not clear that this will address the recommendation if it is done within the "existing guidelines and procedures." During the audit, the Port Authority did not have any written guidelines or procedures.

5. Instruct managers to periodically reassess all Service Contracts and Call-In Agreements to identify opportunities to defer, reduce, or eliminate contract costs. Document the reassessment.

(Port Authority officials replied to our report they continually reassess the services being provided under the various service and call-in contracts, and provided the auditors with documentation for a number of specific examples of reassessments. They added that the reassessment could be better documented and that they implement additional procedures to enhance current controls, and will update the existing guidelines accordingly.)

<u>Auditor's Comments</u>: We did receive some documentation regarding reassessments which is reflected in our report. However, there is no requirement that managers periodically reassess all Service Contract and Call-In Agreements, as a result, it generally was not done. Many of the contracts are multiple-years and should be revisited.

Exhibit A

CONTRACTS/AGREEMENTS IN EFFECT APRIL 2006 THROUGH JULY 2009							
Award Process	Number of Contracts/ Agreements	Percentage	Current Contract Amount (\$ in millions)	Percentage of Total Contract Amount			
Competitive:							
-RFP	179	9.64	\$2,916.3	66.61			
-Competitive (other)	1,178	63.40	\$763.6	17.44			
-MBWE/SBA	44	2.37	\$21.4	0.49			
Non-Competitive:							
- Negotiated Sole/Single Source	181	9.74	\$133.5	3.05			
-Government Contracts	252	13.56	\$100.8	2.30			
Other	24	1.29	\$442.6	10.11			
Totals	1,858	100.00	\$4,378.2	100.00			

Agency Comments

THE PORT AUTHORITY OF NY& NJ

Michael G. Fabiano Chief Financial Officer

May 27, 2011

Carmen Maldonado Audit Director Division of State Government Accountability 123 William Street – 21st Floor New York, NY 10038

Re: Draft Audit Report 2009-S-54

Dear Ms. Maldonado:

Thank you for the opportunity to respond to your draft audit report covering the review of The Port Authority of New York and New Jersey's Contracts for Personal and Miscellaneous Services. We appreciate the efforts that you and your staff have taken to assess the controls established by the Port Authority relative to our use of contracts for personal and miscellaneous services. We welcome any input, which can further enhance our business processes, strengthen our controls or reduce our costs in furtherance of our goal to safeguard assets.

As detailed in our response to your recommendations, the Port Authority has employed a business model for the last twenty years designed to optimize the use of permanent and contract resources, and to provide the agency with the maximum flexibility to respond effectively to changing priorities resulting from shifts in business strategies, technologies, and/or changes in economic conditions. Overall, we believe the business model has served our stakeholders well and continues to allow us to be good stewards of the assets and mission entrusted to the Authority. We are also dedicated to continuous improvements of our processes and controls.

As you will note, we request that certain statements and comments in the draft report be updated and clarified so as to reflect more accurately the current reality. These requests for clarification stem from various reasons, including the fact that the audit covered a period that ended two years ago before certain enhancements were implemented, the possibility that additional information may alter the analysis, and to acknowledge where there are differences of opinion. After reviewing our suggestions for clarification, we welcome the opportunity to discuss any remaining areas where we disagree to help ensure the assessment is as accurate as is possible, which is in the interest of all of our stakeholders.

* See State Comptroller's Comments, page 29.

225 Park Avenue South, 15th Floor New York, NY 10003 T: 212 435 7738

Division of State Government Accountability

* Comment 1



-2-

If you have any questions or require additional information, please contact Andrew Levine, Assistant Director, Audit Department, at 201-216-6048.

Sincerely,

m. Faliano

Michael Fabiano Chief Financial Officer

Attachment

cc: Hon. David Samson, Chairman, PANYNJ
Hon. David S. Steiner, Chairman of the Audit Committee, PANYNJ
Christopher O. Ward, Executive Director, PANYNJ
Bill Baroni, Deputy Executive Director, PANYNJ

Recommendation 1. Require department officials to document, prior to preparing the Memorandum of Justification, Memorandum of Authorization or Board Item, that outsourcing is more beneficial to the Port Authority because of factors such as timing, costs, workload analysis, qualifications, or the nature of the services to be rendered.

Significant corporate practices and processes are in place governing the procurement of outside services which provide a highly effective level of control, accountability and transparency with respect to the approval of individual contracts and awards. Nevertheless, we agree that the supporting documentation can be improved and will implement the necessary actions to enhance our processes. As part of our internal drive to find areas for improvement and cost savings, we identified consultant contracts as an area for improvement and implemented changes in 2009, and we now have a two-year experience with those process enhancements, which we believe are effective in addressing some of the concerns you raise.

The process for seeking approval of the award of contracts is extremely rigorous. Following the development of the business justification for the recommended course of action by the requesting department, a comprehensive organizational review of all requests for service contracts and agreements is conducted by the Management & Budget, Law and Procurement Departments, the Office of the Secretary and other affected departments. Presentations to both senior executive staff and the Board are then required to demonstrate the need and value of the requested contracts, with departments being required to provide extensive justification regarding, amongst other things, the rationale for the requested service and whether the service represents the best value for the agency.

In addition, we further enhanced our processes covering the use of contract services, specifically as they relate to consultant contracts, for purposes of improving control and accountability over the use of consultants. As part of the 2010 Budget process (which began in 2009 after the period you were auditing), a number of additional agency controls related to requests for consultant services were put in place. Departments requesting the use of consultant services are now required to link the consultant contract to a high-priority, mission critical project, and demonstrate that internal resources are not available or do not possess the requisite skill sets needed to perform the required work in order for the consultant to be approved. As a result of those actions, consultant service costs were reduced by \$14 million in the 2010 Budget compared to 2009.

With regard to other service contracts, we will, as recommended, be implementing additional procedures designed to enhance our current controls and to more clearly demonstrate the benefits of outsourcing such services. We intend to base our approach on the enhancements we made to the process around consultant services.

Recommendation 2. Justify the current practice of holding staff size at a fixed level and obtaining needed services through Service Contracts or agreements, stating why it is in the best interest of the Port Authority and the public it serves.

The Port Authority does not have a practice of maintaining staff at a fixed level while obtaining needed services through contracts or agreements. Instead, the Authority employs a business model designed to optimize the use of permanent and contract resources, and provide the agency with the maximum flexibility to effectively respond to changing priorities resulting from shifts in business strategies, technologies, and/or changes in economic conditions. The business model we employ has been in place since the early 1980s. Executive management made a strategic business decision, at that time, to outsource certain non-core functions such as security guards, janitorial and landscaping services in order to better focus the agency on mission-critical objectives. This decision has served the agency and the region extremely well.

The effectiveness of the model has been demonstrated over the years through our ability to fulfill our mission and meet our regional obligations. In recent years, we have made significant reductions to our permanent workforce which is presently at its lowest level in 40 years. These reductions, in conjunction with other cuts, have allowed us to maintain a zero-growth operating budget for the last 3 years and have been integral to our ability to meet the significant financial requirements of our capital plan. At the same time, the flexibility of our model has allowed us to effectively address new business initiatives, such as the acquisition of Stewart International Airport and the redevelopment of the World Trade Center site, through the redeployment of existing resources.

Likewise, we have also been able to adjust our use of contract services in line with changes in activity levels at our facilities stemming from current economic conditions. As activity levels have fallen, we have reduced the use of service contracts, as appropriate, and, as a result, saved approximately \$46 million in 2010 compared to the prior year.

As such, we believe our business model provides us with the needed capability and flexibility to manage and balance our resource requirements, on both the internal staffing and contract services sides, thereby effectively addressing changes in strategies and business conditions.

Recommendation 3. Demonstrate the true amount of resources needed to operate Port Authority facilities by publicly disclosing the number and cost of individuals it employs under contracts and agreements.

The Port Authority adheres to strong corporate governance practices and strives to be transparent and fully accountable to the public we serve. Because of our commitment to these principles, it was extremely difficult to separate what we believed to be a possible inaccurate implication because of the way this recommendation was presented -- that the Port Authority was intentionally concealing information -- from an opportunity to enhance our practices.

From a transparency standpoint, all Requests for Proposals, bid solicitations, Board actions, and contracts over \$25,000 are posted on award to the Port Authority's web site and are fully disclosed to the public. Likewise, our annual budgets and financial statements, which include information related to staffing levels and contract service costs, are also fully disclosed to the public on our web site. For example, in our 2010 Financial Statements posted on our website, the first two line items under operating expenses are "Employee compensation, including benefits", and "contract services." The amounts are then listed as well as a comparison to the previous year. The 2010 financials clearly demonstrate that overall costs of operations between the two categories went down slightly from 2009 to 2010, consistent with the flexibility offered by our business model and the ability to adjust contract services when warranted.

Facility operating results, which reflect the full cost of operating our facilities including staffing and contract service costs, are fully disclosed in our financial statements. The financial statements also provide information on Port Authority staffing levels and contract service costs for the last ten years. Further, we believe that disclosing contract expenditures as we currently do more accurately reflects the true cost of managing our operations given that many of our contracts are performance based and do not require a specific number of contracted staffing levels.

As demonstrated above, we attempt to depict accurately the amount of resources needed to effectively and efficiently operate the Port Authority. We welcome specific recommendations as to how we might enhance our disclosure, but we reject any implication that we have concealed information from our stakeholders against principles to which we are committed. Therefore, we respectfully request that either this recommendation is expanded to include acknowledgement of our current disclosure and specific opportunities for enhancement or that this recommendation be removed from the report.

Recommendation 4. Develop uniform written guidelines for entering into all Service Contracts and agreements that clearly delineate required steps, analyses, and documentation to support the decision to outsource, and specify the retention period.

As noted in our response to Recommendation 1 above, supporting documentation will be prepared for all Service Contracts that will clearly demonstrate the benefits of outsourcing contracts into our existing guidelines and procedures.

* See State Comptroller's Comments, page 29.

Division of State Government Accountability

* Comment 2 **Recommendation 5.** Instruct managers to periodically reassess all Service Contracts and Call-In Agreements to identify opportunities to defer, reduce, or eliminate contract costs. Document the reassessment.

Consistent with the agency's budgetary and financial controls, it is standard Port Authority practice to continually reassess the services being provided under our various service and call-in contracts, and, during the course of the audit, we provided your staff with documentation supporting a number of specific examples of reassessments by staff that resulted in cost savings for the Authority. We recognize, however, that this continual reassessment could be better documented and the controls can be enhanced to ensure the principles are being followed. Therefore, as noted in our response to Recommendation 1 above, we will document the reassessment process as it currently exists, implement additional procedures to enhance our current controls and update the existing guidelines accordingly.

4

State Comptroller's Comments

- 1. The response indicates there is a need to update and clarify certain statements in the report to reflect more accurately the current reality. Port Authority officials claim this is due to the fact that the audit covered a time period before certain enhancements were implemented. However, the only enhancement which was part of the 2010 Budget Process is in our draft report. This is due to the fact that we include all information received during the field work and all documents received through the closing conference held on August 12, 2010. We also note that the contracts were selected from the most recent listing when the request was made at the opening conference on July 22, 2009.
- 2. Rather than the negative view of the recommendation taken by the Port Authority, we view this as an opportunity for the Port Authority to demonstrate to the public the full extent of its impact on the economy of the area by revealing the number of "non-core" positions it directly sponsors through its contracts for services. In addition, we note that State Law requires annual reporting by employment category of the number of persons employed under service contracts for consulting services to the State Comptroller's Office & Department of Civil Service, with annual reporting to the public under the Procurement Stewardship Act. This enhances transparency.