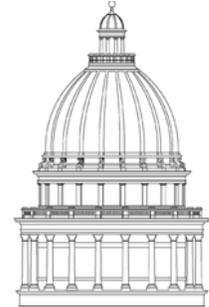


Office of
LEGISLATIVE AUDITOR GENERAL
State of Utah

**REPORT NUMBER ILR 2010-D
July 2010**



A Limited Review of UDOT's Controls Over Right-of-Way Property Management

Our office was asked to validate the accuracy and depth of a Utah Department of Transportation (UDOT) Right-of-Way (ROW) Property Management Section employee disciplinary case and determine if proper action was taken. We evaluated two UDOT internal audits, employee reviews, and discussed concerns with individuals. We agree with the findings from the two internal audits and believe that UDOT corrective actions are adequate. Furthermore, UDOT has created new policies and improved oversight over the ROW process.

Late last year, allegations concerning a UDOT employee's undisclosed conflict of interest were reported to UDOT's Internal Audit Division. A UDOT internal audit confirmed the allegations, and the audit findings were presented to UDOT management. Recent media interest has brought the audit results and additional employee reviews to the public's attention. Specific findings included the following:

- A UDOT employee allowed family members to rent a UDOT ROW property while the utilities for the house were subsidized with Utah taxpayer dollars.
- Family members in UDOT homes were compensated to maintain the properties.

In 2009, conflict of interest allegations were reported to UDOT's Internal Audit Division.

During 2009, UDOT's auditors conducted two internal audits of the ROW Section; the first audit released in August was a general review of the Section's internal controls, policies and procedures, documentation and areas of responsibility. Three months later, UDOT released a second audit which reviewed the conflict of interest actions by a UDOT employee.

Internal Audit and Subsequent Employee Reviews Identified Conflicts of Interest

UDOT was notified of a potential UDOT employee conflict of interest by the property management consultant that supervises UDOT's ROW properties. ROW properties are houses and parcels of land bought by UDOT before the expansion of a road or corridor. UDOT rents out the ROW properties while plans, funding, and approval for the expansion are finalized. A formal audit request was submitted by the ROW director to UDOT's Internal Audit Division. Once completed, the conflict of interest audit identified one ROW property management agent who violated multiple administrative rules and UDOT policies. The audit identified three instances where the ROW agent had a conflict of interest:

A UDOT ROW agent hired related parties to work on ROW property.

- The ROW agent hired her husband's stepdaughter and spouse (A&S) to work on UDOT vacant corridor properties. During fiscal years 2009-2010, A&S was contracted to repair 19 out of 20 houses and the total amount paid to A&S during that time was \$102,970.
- The ROW agent hired a son-in-law to perform maintenance yard work on ROW properties and complete pre-bid inspections. During fiscal years 2009-2010, the ROW agent approved work invoices totaling \$3,276.
- The ROW agent hired a former real estate partner to complete pre-bid inspections of ROW properties. The partner received \$500 for this work.

The opportunity cost for repairs and additional expenses for ROW houses was over \$100,000.

Due to the events in the first example, UDOT was unable to rent the ROW properties in need of repair. Since only one contractor was working on multiple houses, some of UDOT's ROW houses sat dormant, and the estimated lost revenue and additional expenses was

over \$100,000. Furthermore, the agent approved all repair invoices without management oversight.

Agent Failed to Disclose Conflict of Interest to UDOT Supervisors

These conflict of interest situations involved a family member of the ROW agent, a relative of her husband, and a former partner. We believe the ROW agent should have disclosed to management these conflict of interest before work was started on UDOT properties. UDOT documents state that the ROW agent's supervisor was not notified of these conflicts of interest until the facts were exposed throughout the course of the internal audit.

In December 2007, before the improper actions took place, the ROW agent signed a UDOT Conflict of Interest Declaration to verify that her activities did not constitute a conflict of interest. By signing the document, the ROW agent acknowledged the rules and penalties, and further demonstrated the need to:

- Disclose information acquired by reason of Department position, that could result in personal or another's private gain or benefit.
- Refrain from using, or attempting to use, Department position to secure special privileges or exemptions for self or others.

The ROW agent clearly violated these provisions by providing work, non-competitively, to a family member and friends. Additional violations of UDOT policy were cited in UDOT's audit and are discussed below.

ROW Agent Violated UDOT Policies

We agree with the findings of the internal audit which claim that the ROW agent violated UDOT's Rules of Conduct and Code of Ethics. Citing UDOT Policy 05C-30, the ROW agent failed to comply with the following provisions:

- (1) Conduct themselves in a manner that is above reproach;

ROW agent signed Conflict of Interest Declaration before improper actions took place.

Internal audit cites multiple violations of rules and policies by the ROW agent.

(2) Be honest in all work settings...

(4) Not knowingly alter, falsify or omit necessary information when required or requested by the Department to keep records, make measurements or calculate quantity...

(6) Abide by all civil or criminal laws, regulations, State administrative rules governing their work or professional activities, work place rules, policies and procedures of the Department. The Department will not condone the activities of employees who achieve results through violation of law or unethical business dealings...

(19) Not be wantonly careless or negligent in the performance of their duties...

With reference to conflicts of interest, UDOT policies direct UDOT employees to comply with the following requirements:

(1) Not use their state position or any influence, power, authority or confidential information ... for private gain, and

(3) Not engage in business such as selling goods, materials or services to the Department or contractors or consultants working for the State where there may exist a potential conflict of interest.

All of these violations are cited in the internal audit. As UDOT proceeded with disciplinary actions against the agent, additional violations by the ROW agent and the agent's immediate supervisor, the ROW lead agent, were identified.

Employee Reviews Identified Additional Problems with ROW Agents

In December 2009, an Intent to Terminate Notice was presented to the ROW agent. After the ROW agent appealed the decision and presented additional information that merited further investigation by the internal audit division, UDOT conducted a disciplinary hearing for the ROW agent in January 2010. During this hearing, two further infractions of UDOT policy by the ROW agent were revealed. In addition, the ROW agent's supervisor, or lead agent, was found to be storing personal supplies on UDOT property without payment.

Discipline hearings revealed additional conflict of interest violations by UDOT employees.

ROW Agent Split Work Orders and Rented Property for Less than Fair Market Value. UDOT management identified five occasions when the ROW agent multiplied projects on ROW houses to keep all project bids under \$1,000. According to UDOT officials, all projects under \$1,000 do not need to go through the bid process; as a result, the ROW Agent was allowed to dictate who would complete each project. Further inquiry revealed that the ROW agent supplied materials from a UDOT storage unit to A&S. A&S underbid competitors and was awarded 19 out of 20 contracts because they did not need to charge for materials for repair projects over \$1,000.

ROW agent split work orders to keep repair bids under \$1,000 and supplied materials for repairs.

In addition, UDOT found that the ROW agent was renting two ROW properties to related parties for less than fair market value. To amplify this infringement, UDOT paid for the utilities in one of the properties; such payments did not occur in any other ROW property. Figures 1.1 and 1.2 displays our analysis of the rent per square foot for the rental homes of the agent’s daughter and husband’s stepdaughter. The figures also show rent per square foot for comparable properties.

Figure 1.1 Rent per Square Foot of ROW Agent’s Daughter’s Property. This property was leased in April 2009, and the ROW agent determined that UDOT would cover the cost of utilities. The first rent reflects the actual rent per square foot. When the payment of utilities is included, the actual rent per month dropped to \$166. Comparable properties are UDOT ROW homes located near the rental.

Property	Rent per month	Property Square Foot	Rent per Square Foot
Daughter's property before utilities	\$ 500	3,700	\$ 0.14
Daughter's property - utilities covered by UDOT	\$ 166	3,700	\$ 0.04
Previous tenants	\$ 2,500	3,700	\$ 0.68
Lowest comparable property	\$ 1,590	5,700	\$ 0.28
Highest comparable property	\$ 1,100	2,700	\$ 0.41

Our analysis of the rents shows that the agent’s daughter was renting well below the fair market value of the four other comparable properties even before the cost of utilities was included in the calculation. Furthermore, UDOT learned that the ROW agent

ROW agent approved below fair market value rent to related parties.

evicted tenants who were paying \$2,500 a month plus utilities in the same property in order to accommodate her daughter.

Figure 1.2 Rent per Square Foot of ROW Property for Agent’s Husband’s Stepdaughter. Out of 49 properties, the ROW agent’s relative paid the lowest rent per square foot. The lowest and highest comparable properties are included in the table.

Property	Rent per Month	Property Square Foot	Rent per Square Foot
Husband’s stepdaughter's property	\$ 400	3,700	\$ 0.11
Lowest comparable property	\$ 1,000	6,100	\$ 0.16
Highest comparable property	\$ 1,220	1,970	\$ 0.62

The rent per square foot for all 48 comparable properties was greater than \$0.11, which was the amount paid by the ROW agent’s relative. The cost for the lowest comparable property was \$0.16 per square foot.

In addition, UDOT officials discovered that the length of the rent contract was favorable for the ROW agent’s relative. UDOT usually limits the term of rent contracts to one year, but the term for this particular contract was five years, beginning August 2008. The contract essentially locked in below fair market value rent payments for five years, whereas the majority of comparable property rents increase each year.

The Intent to Terminate Notice was amended to include the additional charges identified in the employee reviews and disciplinary hearing. Shortly after the amended notice was presented to the agent, which she appealed a second time, the ROW agent resigned. According to UDOT management, the ROW agent would have been terminated had she not resigned.

ROW Lead Agent Was Reprimanded for Not Disclosing Use of UDOT Property. When UDOT was conducting the ROW agent’s employee review, her supervisor was found to be using UDOT property without payment. The UDOT lead agent had been storing personal items in the garage of a ROW property for two years, and the estimated fair value of usage was \$600. Although the employee

ROW agent approved a five year rent contract for a relative.

Another UDOT employee was found using ROW property without payment.

paid the amount in arrears, the individual was officially reprimanded for not disclosing the use of the property and was relieved of all supervisor duties.

ROW Division Has Created Additional Checks and Balances to Supervise Employees

UDOT management has addressed a number of concerns as a result of the audits and employee reviews. Adjustments in ROW training, conflict of interest disclosure, contract oversight and approval, the procurement process, and record keeping are intended to address the liability issues discussed in this letter.

Checks and Balances Existed Before Audits, but Internal Policy Has Improved. Before the misuse of UDOT property occurred, UDOT had conflict of interest checks and balances in place. To address employee misinterpretation of what constitutes a conflict of interest, UDOT currently requires all staff to receive training on Procurement Rules and the ROW process. In addition, every ROW employee and consultant is required to sign the Conflict of Interest Disclosure Statement. Unfortunately, the disclosure statements are not renewed each year. We recommend Conflict of Interest Disclosure Statements be renewed and signed each year by UDOT ROW staff and consultants.

As mentioned earlier, some of the major infractions of the ROW agent involved relatives renting UDOT ROW properties. Past UDOT policy did not discourage renting ROW properties to UDOT relatives, but the policy has been updated to address potential conflicts of interest. UDOT's Internal Policy 6.1.1 now includes the following rule:

To avoid conflicts of interest, an employee of UDOT shall not approve or recommend a lease for a friend, relative, or immediate family member, including the employee himself or herself, without having the senior group leader's review and written approval of the transaction. If approved by the senior group leader, the lease must be for fair market value for the premise.

We recommend that UDOT ROW staff and consultants sign a disclosure statement every year.

UDOT has updated their internal policy to prevent conflicts of interest.

Additional Signatures Needed for Project Approvals, and ROW Engineer Should Provide Greater Oversight. One weakness exploited by the ROW agent in UDOT's procurement process was the approval of bids and repairs by only one employee. Because no one else was required to approve the bids and repairs, the ROW agent was able to act independently of management or peer approval. UDOT has since adjusted their bid and repair forms to include two signatures.

UDOT has also recently added the position of a ROW engineer to oversee all ROW agents. The engineer's tasks are to ensure conformity with UDOT requirements as well as to implement and provide continuous improvement to the ROW team's processes and operations.

UDOT has Reinforced Property Management Consultants' Role. Before the ROW agent assumed the role of delegating repair work under \$1,000, the property management consultant was responsible for all minor repairs. Within Attachment B of the original contract between UDOT and the consultant, the following language clarifies this role:

2.3 Repair Work: Minor repairs will be made within forty-eight (48) hours in accordance with *Utah Code*. Minor repairs are repairs with a replacement cost of \$1,000 or less. The Contractor will make all such repairs without prior approval from the State.

Minor repairs on UDOT ROW properties were delayed because the ROW agent delegated most repair projects to a single individual, resulting in lost rent revenues. UDOT has since reinforced their process to funnel all repair duties for ROW properties to the independent property management consultant. Furthermore, the consultant is responsible to perform all bid solicitation according to state procurement guidelines as outlined in the existing contract.

UDOT Will Randomly Audit Lease Files to Ensure Proper Rent Rates. UDOT will require the contracted property management consultant to maintain all lease files online. UDOT will then audit a minimum of three files at random each month to ensure that properties are being leased for fair market value. UDOT believes that the action items mentioned above should address the problems identified in the audits and employee reviews.

A ROW engineer will oversee all UDOT ROW agents.

All repair work under \$1,000 will be managed by the property management consultant.

The effect of the ROW agent's actions was lost rent revenue from ROW rental properties and questionable repair costs and quality. We believe that proper supervision did not exist between the supervisors and the ROW agent, which led to unendorsed decisions. We were unable to verify that ROW agent performance plans and reviews occurred for the fiscal year 2009 and the first eight months of fiscal year 2010. The performance plans and reviews are important management tools for overseeing employees and ensuring that they are properly completing the tasks assigned to them. We recommend the UDOT ROW Division carry out and document annual employee performance plans and reviews.

In conclusion, the ROW process has been modified to protect against future conflict of interest violations, and the additional checks and balances created should address the problems mentioned in this audit. We believe that UDOT handled the employee infringements properly and should carry out the following recommendations:

Recommendations

1. We recommend Conflict of Interest Disclosure Statements be renewed and signed each year by UDOT ROW staff and consultants.
2. We recommend that UDOT ensure that UDOT ROW employee performance plans and reviews occur each year and that proper documentation of the reviews is retained.

We were unable to verify that performance plans and reviews occurred in fiscal year 2009 and the first part of fiscal year 2010.

We recommend the UDOT ROW Section carry out and document annual employee performance plans and reviews.

Agency Response



State of Utah

GARY R. HERBERT
Governor

GREG BELL
Lieutenant Governor

DEPARTMENT OF TRANSPORTATION

JOHN R. NJORD, P.E.
Executive Director

CARLOS M. BRACERAS, P.E.
Deputy Director

July 13, 2010

John M. Schaff, CIA
Auditor General
Office of the Legislative Auditor General
W315 Utah State Capitol Complex
Salt Lake City, UT 84114

Re: Report No. ILR 2010-D; A Limited Review of UDOT's Controls Over Right-of-Way Property Management

Dear Mr. Schaff:

The Utah Department of Transportation's Right of Way Division (ROW) is pleased to provide the following response to the Auditor General's July 2010 audit of the ROW Division. We pride ourselves in taking the right actions for the right reasons. UDOT strongly supports the use of audits as an important tool to improve state government.

Recommendation No. 1: We recommend Conflict of Interest Disclosure Statements be renewed and signed each year by UDOT ROW staff and consultants.

Response: ROW agrees with this recommendation.

UDOT agrees with and has already implemented the auditors' recommendation to obtain annual renewals of the signed Conflict of Interest Disclosure Statements. We understand the importance of avoiding conflicts of interest in the course of carrying out public works. The process now states that each July, all internal ROW employees and external consultants must sign a current Conflict of Interest Disclosure Statement, which will be kept on file. This will provide ROW with the opportunity to remind all parties of the responsibility to remain free of conflicts of interest on a regular basis.

Recommendation No. 2: We recommend that UDOT ROW employee performance plans and reviews occur each year and that proper documentation of the reviews is retained.

UDOT agrees with the auditors' recommendation to ensure performance reviews are completed and retained for every Right of Way employee. The FY2010 Performance Reviews for every employee in the Right of Way Division have been completed, with originals sent to DHRM, and a copy retained locally for reference and as a backup. In FY2011, all Performance Plans and Reviews will be in the DHRM's new online system.



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CONCLUSION

UDOT and the ROW Division appreciate the effort put forth by David Apple and Tim Osterstock in conducting this audit. The staff exhibited the highest level of professionalism and due care in the performance of their duties. The audit was invaluable in identifying areas of our business where opportunities existed for improvement. We will be better able to manage real properties under state ownership because of it.

Sincerely,

A handwritten signature in blue ink, appearing to read "Lyle D. McMillan".

Lyle D. McMillan
Director, Right of Way and Property Development