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Combatting Corruption and Racketeering: A Successful New Strategy for Reforming Public Contracting in New York City's Construction Industry

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INTRODUCTION

The theme of the presentation I make to you this morning is in one respect starkly different, and perhaps at variance, with the traditional view of corruption and organized crime experts on control strategies. Most criminologists have focussed on the control of corruption and organized crime racketeering as a law enforcement challenge. They have called for the design of strategies to be executed by police, prosecutors and the courts. I, on the other hand, believe that so long as government places sole responsibility in the law enforcement community to protect society from the cancer of organized crime, government will surely fail. The courts, the police and prosecutors, acting alone, simply do not have the power to block the myriad opportunities for organized crime's successful exploitation of legitimate and illegitimate industries. Nor do they have the means to reduce the incentives for individuals and businesses to reach out for the illegitimate services which organized crime syndicates can provide.

I say this not as a detractor of police and, prosecutors, or of the performance of

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the judiciary in meting out sufficiently severe prison sentences. To the contrary, I have been fortunate to have worked in and with the finest federal, state and local prosecutorial and investigative offices operating in New York City. In the past ten years these offices have produced some extraordinary, indeed historic, prosecutions. Life time incarceration of the most important bosses of the city's Cosa Nostra crime families has been achieved; criminal monopolies have been broken up; powerful labor racketeers, business executives and political leaders have been sent to jail. The resulting media coverage of these successful prosecutions has often given the impression that the organized crime groups are on the run. But the impression is illusory.

As important as these prosecutions have been, they have by no means succeeded in significantly controlling the domination and/or influence of organized crime in many of New York City's legitimate and illegitimate industries. New crime bosses have emerged; different organized crime monopolies are being formed; another set of mobsters is taking the reins in unions where labor racketeers have been purged through criminal convictions; companies convicted of frauds and other economic crimes have reappeared like chameleons under new names with different corporate composition.

It is thus apparent that more need be done -- that the law enforcement initiatives of the past have not, by themselves, been enough. I submit that this a principally because in certain industries *the opportunities* to engage in racketeering are so many and *the incentives* to reach out for the services of racketeers are so great that criminal sanctions alone cannot possibly constitute a sufficient deterrence. A truly comprehensive corruption and racketeering control strategy must therefore look beyond prosecutions and incarcerations to a plan for changing those

structural and economic industry characteristics that generate motivation and opportunity to act corruptly. While criminal investigations and prosecutions will always play a critical role in identifying the particular industry traits that generate corruption, law enforcement can only play a limited role in forcing reform of these characteristics.

Because such reforms often require altering the most fundamental ways in which an industry conducts its business, meaningful change can be exceedingly difficult to achieve. In many instances, it will require modification of the practices and procedures long followed by the major institutions which comprise the particular industry. While implementation of such institutional reform can be imposed through legislation, regulation or judicial decree, it stands far better chance of success if voluntarily adopted by the institutions affected.

This morning I would like to discuss one approach which has recently been adopted in New York City to bring about such institutional reform in a large niche of our construction industry. The vehicle for that reform has been creation within a major construction agency of a new kind of office with powers, resources and roles never before consolidated in or made available to a stand alone crime-control office. This office is known as the Office of Inspector General, and it has been given the mandate to protect a 4.3 billion dollar (or 7.3 billion guilders) New York City construction program from victimization by organized crime groups, criminal monopolies and cartels, fraud, corruption, bribery, extortion, racketeering and the many other crimes so endemic to the City's construction industry.

By describing why this office was created, how it is structured, the powers it possesses or has access to, what roles it plays and some of its successes, I hope that I might provide you with a perspective on how control of corruption and racketeering can be

accomplished through means and institutional reform not exclusively within the realm of law enforcement.

Why the Office Was Created

In April 1988, a report was released by the New York State Organized Crime Task Force that documented in frightening detail an incontrovertible fact. New York City's largest industry - the construction industry - was then, as it had been for the past century, dominated by corruption and racketeering. The report provided a fascinating analysis of why this particular industry has been so susceptible to racketeering and corruption and it described how organized crime syndicates had so successfully exploited this susceptibility. The picture painted was a depressing one -- an industry victimized by bid rigging, price fixing, illegal cartellization among contractors and suppliers, labor racketeering, bribery, extortion and frauds.

One of the sectors of the construction industry where corruption, racketeering, fraud, waste and abuse had wreaked particularly tragic consequences had been in the City's school construction program. New York's school system is enormous and is dependent on an equally enormous infrastructure. It serves one million students, employs a staff of over 100,000 and is comprised of over 1,000 facilities or buildings. Its annual operating budget is close to 7 billion dollars, larger than that of many countries in the world. In the past several decades, however, billions of dollars have been wasted on a school construction program which has left the educational infrastructure in a deplorable state -- bathrooms, closets and gymnasiums converted into makeshift, overcrowded classrooms; deteriorating roofs, windows and walls leaking and collapsing; dangerous and inadequate heating and electrical systems (many schools still being heated with coal fired furnaces); and a severe shortage of almost every type of school

facility.

In response to this crisis condition, the New York State Legislature created a new, independent School Construction Authority (SCA) and charged it with reconstructing the entire educational infrastructure. The Authority was given an initial five year budget of 4.3 billion dollars (or 7.3 billion guilders) and sweeping powers to expedite the design, site acquisition and construction processes.

While the SCA appeared to many as an extraordinarily bold step toward the reconstruction of our deteriorated school facilities, to others it represented an agency extremely vulnerable to exploitation by all sorts of criminals -- Cosa Nostra mobsters, labor racketeers, cartels of contractors and suppliers, corrupt inspectors, etc.

The Trustees of the new Authority had no illusions about this vulnerability, and in the Spring of 1989 invited me to a discussion of how I might design a mechanism to protect the Authority from the endemic criminality which so infects the construction industry. At that time I was directing a strike force of close to 100 prosecutors, investigators, accountants, analysts and support personnel focussed exclusively on prosecuting corruption and racketeering in the City's construction industry. It was exciting work and we were making some very significant cases. I was thus not enthusiastic about the prospect of leaving the world of law enforcement with its powerful investigative and prosecutorial tools, to enter into a construction bureaucracy destined to grow to close to 1,000 people.

But the trustees spelled out a challenge that was impossible to reject. They pointed out, "You have been part of an investigative initiative focussed on construction industry racketeering which has been more comprehensive, intensive and sustained than any before it.

That initiative has developed an extensive intelligence base spelling out who the criminals are, how they are organized, how they operate and whom they victimized. But," they pointed out, "you have nonetheless concluded in the Report issued by the Organized Crime Task Force that the industry's systemic corruption and racketeering can never be controlled by law enforcement alone. You have called for institutional reform of those structural characteristics of the industry which generate motivations, ability and opportunity to act corruptly. Here then is our challenge -- we are willing to put our money where your mouth has been. Design a strategy and mechanism to protect this Authority and to support institutional reform. If you conclude that it can't be done, then much of your writings can only be judged as academic theorizing and glib thoughts that are never likely to be implemented."

Once the challenge was framed in these words, it was impossible to reject. And so commenced endless discussions and debate on how to design a non-law enforcement office which could realistically hope to keep a \$4.3 billion construction budget from getting into the hands of the crooks and racketeers who are so pervasive in this industry. The office we designed is known as the Office of the Inspector General (IG) of the New York City School Construction Authority (SCA).

In designing this new office we immediately recognized certain principles which would have to be reflected in whatever structure we put together. Some of these included the following:

- 1) While not statutorily (nor could it constitutionally be) a law enforcement agency, the IG could not succeed without the strong support of law enforcement. Only law enforcement has the investigative tools to really determine who is doing what to whom and how (e.g., wiretaps, grand juries, informants generated through promises of immunity or lenient prosecutorial exposure, search warrants, and sting operations). Anti-crime

commissions and regulatory agencies which have lacked these powerful tools have generally failed in effective crime control, as much from a lack of current, detailed information as from a lack of sufficient punitive powers to generate true deterrence. Thus, a means for integrating law enforcement agencies into the IG operations would have to be found. In this way, law enforcement could operate as the engine which would drive reform.

- 2) The IG must have a state-of-the-art intelligence operation. In the business of crime control, information is a sin qua non. Intelligence must not only be aggressively collected and constantly expanded and updated, it must also be organized so as to be immediately retrievable and simultaneously useable by multiple disciplines -- investigators, accountants, analysts, prosecutors, civil attorneys, etc. Above all, the intelligence must be institutionalized and not, as is so often the case, in the heads or files of "experts" of "specialists" in the office. Thus, the IG would have to be dependent on an advanced computer operation managed by a highly trained Management Information Services Unit.
- 3) One of the IG's principal goals would have to be deterrence of corrupt activity. Its operations would have to generate a perception and a reality that wrongdoing would be detected and would result in significant punishment -- prosecutions, civil law suits and/or administrative sanctions (ranging from the withholding of construction progress payments to debarment from future work).
- 4) Another equally important goal would have to be to block opportunities and reduce incentives to act corruptly. Thus, its structure must include experts in loss prevention analysis, public administration theory and management methodology. And it must be empowered to assure that institutional reform measures be adopted by the SCA.
- 5) The IG could not succeed unless the SCA itself were prepared to accept in some instances a short term diminution in speed, efficiency and cost savings in order to assure that operations are conducted lawfully and ethically. One of the factors which has always driven corruption and racketeering in this industry is that "time is money". By cutting corners, bending rules or paying bribes to avoid compliance with time consuming requirements, money could be saved, profits increased and projects delivered more quickly. Management at the SCA would have to be forced to resist the temptation "to get the job done at whatever cost or means."
- 6) Finally, the IG as an office would have to be so positioned within the SCA that it could play a major policy role in shaping the SCA

organizational structure, as well as its daily construction operations. Thus the IG would have to have a defined *internal* role within the SCA. On the other hand, the IG must simultaneously be capable of maintaining some degree of autonomy. Some of the IG's actions or recommendations might not be well received by the SCA; the IG would therefore have to be protected from inappropriate retaliation or co-opting by the SCA.

With these principles in mind, we turned to (1) defining a mission statement for the IG; (2) designing a methodology for accomplishment of that mission; and (3) structuring an office to implement that methodology. The mission statement we settled on is the following:

Mission

The mission of the IG is to protect the SCA from victimization by racketeering, fraudulent schemes, wasteful practices and all manner of crimes perpetrated by those doing business with, as well as those employed by, the SCA -- e.g., billing for services or supplies not delivered; bribery and extortion in the inspectional services; bid rigging, price fixing, illegal cartelization among contractors or suppliers; labor racketeering by union officials and corporate officers; no-show employee payrolls; sham minority group extortions. By reducing corruption, fraud and racketeering, and by supporting civil suits for the recovery of monies that have been lost, the IG will save the SCA money. It should further serve the objective of attracting greater private sector participation in the SCA's construction programs.

We designed the methodology to accomplish this mission as follows:

Methodology

The IG's efforts will follow a two-pronged approach: *deterrence* and *opportunity blocking*. Deterrence is to be accomplished by creating both a perception and reality in the construction community of a substantial likelihood that crimes, frauds, and wrongdoing perpetrated against the SCA will be both detected and punished. The mechanisms of detection and punishment must be creative and multi-faceted. Thus, investigations will employ sophisticated auditing, surveillances, undercover operations and stings as well as traditional law enforcement techniques. The IG will additionally develop a network of individuals (both in the construction industry and within the SCA itself) who will provide

information to the IG about criminality impacting on the SCA. Investigations must not be merely reactive to complaints; rather they must pro-actively scrutinize areas of operations previously identified as prone to corruption or criminal exploitation. In order to be "pro-active," investigative initiatives must be informed by a comprehensive intelligence base and guided by sophisticated analysis of corruption and crime problems affecting the SCA. Likewise, deterrence must be based upon a wide range of sanctions including use of such civil remedies as forfeiture, treble damages, restitution and injunctive relief as well as criminal fines and incarceration. Sanctions must also include significant punitive administrative actions to be taken by the SCA against those proven to have victimized it (e.g., debarment from future contracts).

Experience has shown that deterrence by itself will not be sufficient to control the kind of systemic criminality that threatens the SCA's mission. Therefore, the IG will work with the operating units of the SCA to design systems, strategies, practices and procedures which reduce opportunities and incentives to engage in criminal and fraudulent schemes. However, the IG will approach its institution building task sensitive to the impact that recommended organizational or systems reform might have on the SCA's ability to build schools efficiently and expeditiously. It will avoid the pitfalls of some previous anti-corruption efforts which have imposed systems, procedures and multiple layers of oversight that have inadvertently contributed to organizational paralysis and dysfunctional conflict, thereby ironically increasing incentives for corrupt payments to expedite the process.

In order to implement this methodology, we designed a structure of multiple units, each with defined responsibilities, but highly dependent on each other to accomplish their respective tasks. The structure we designed is as follows:

Structure

The IG has three component parts: an operations division, a counsel's office and an administrative support team. (See chart attached hereto.)

Operations. Operations is comprised of an *Investigations Bureau* and a *Policy and Analysis Bureau*. These two units combine the tools and expertise of five discrete disciplines -- legal, investigative, analytic, accounting and engineering -- in order to accomplish the IG's mission of deterrence and opportunity blocking.

The principal subdivisions of the *Policy and Analysis Bureau* are the Intelligence Unit and the Research and Analysis Unit.

Intelligence: The IG cannot succeed without a steady flow of information about the actors and organizations with whom the SCA is in contact. Comprehensive information about vendors, contractors, and types of fraud and criminality affecting the SCA must be collected in order to plan investigative strategies and to design the opportunity blocking systems which support the IG's primary mission. Therefore, the Intelligence Unit will have three responsibilities: 1) to obtain information from a wide array of sources both within and without the IG's office; 2) to oversee an aggressive field associate program; and 3) to manage the storage and retrieval of intelligence information.

Research and Analysis: This unit will utilize the information generated by the Intelligence Unit and by the Field Investigations and Criminal Investigations and Prosecutions Units to prepare two types of analytic reports: 1) strategic assessments of patterns of criminal activity that impinge upon the operations of SCA; and 2) systems analyses that identify practices and procedures within SCA operations that create incentives and opportunities for corruption. The strategic assessments will be used by field operations in planning and implementing investigations; the systems analyses will be used to design more effective regulations, practices, and procedures for SCA. Research and Analysis will further be responsible for drafting recommendations and IG position papers for submission to the President and the Board of Trustees.

The *Investigations Bureau* is comprised of the Field Investigations Unit and the Criminal Investigations and Prosecution Unit.

Field Investigations: This unit will be staffed by attorneys, investigators, accountants and engineering/design audit experts, assisted by tactical analysts from the Research and Analysis Unit. The unit will investigate complaints that come into the SCA, as well as initiate its own audits and investigations based upon reports from the Intelligence Unit and on strategic assessments from the Research and Analysis Unit. It will be responsible for conducting investigations of entire projects, specific contracts, and categories of construction activities believed to be corruption-prone. Information generated by its investigations will be transmitted to the Intelligence and Research and Analysis Units. Research and Analysis will in turn prepare strategic assessments identifying patterns of criminality in particular trades or operations affecting the SCA. These assessments will be used to direct future investigations to be undertaken by the Field Investigations Unit. Where criminal prosecutions might result from an investigation, the Field Investigations Unit will work with and support the Criminal Investigations and Prosecution Unit.

Criminal Investigations and Prosecutions: This unit will be comprised of personnel detailed from three law enforcement agencies -- the New York State Organized Crime Task Force, the New York County District Attorney's Office, and the New York State Police. This unit brings to the IG law enforcement tools traditionally unavailable to administrative agencies and IG offices. This law enforcement presence will bolster deterrence and generate critical information for the IG.

The Operations Division will be supported by (and will in turn support) the Counsel's

Office. This office will function as follows:

Counsel. The IG's Office operates in a comprehensive and complex web of specialized civil and criminal laws. Therefore it requires full-time counsel to advise it on the multitude of civil, criminal and regulatory legal issues the IG confronts on a daily basis.

Counsel will also play the critical role of chief civil enforcement specialist and strategist. S/he will review all investigative initiatives to determine whether civil or administrative remedies would be appropriate -- e.g., civil OCCA and RICO, forfeiture, anti-trust, and injunctive actions. Where appropriate, counsel will co-ordinate liaison with the SCA general counsel as well as with various federal, state, and local agencies that are responsible for bringing such specialized actions.

Counsel will review all recommendations and position papers prepared by Research and Analysis. Where recommendations involve proposals to modify existing procedures or contract provisions, counsel will work with Research and Analysis in the drafting of such recommendations.

Finally, supporting the whole IG is an Administrative Support Service team, which will function as follows:

Administrative Support. Support Services will have two principle responsibilities: security and administration. Security includes plant security, motor pool, background checks, internal investigations of the IG office, subpoena control, safekeeping of evidence and maintenance of technical equipment. Administrative responsibilities include finances, purchasing, budgeting, support staff supervision, office procedures and related matters.

How the Inspector General relates to the School Construction Authority

The traditional relationship of an IG to the agency it is designed to protect is that of an outside entity, independent from the operations it is charged with investigating. How else, it is

argued, can the inspector general assure that its investigations and ability to criticize the subject agency's operations will not be compromised by manipulation of budgets, personnel policies and allocation of resources? What commissioner or agency CEO, it is asked, will not seek to emasculate an office whose investigations and reports might embarrass his or her agency? Conversely, how much independence and initiative can an IG be expected to demonstrate when his salary enhancements and promotional opportunities are in the hands of the very people he is supposed to be investigating? Thus, the standard model for inspectors general in New York City is as an independent agency with no structural role or reporting responsibilities inside the agency over which it has oversight responsibilities.

This model, however much it might advance an IG's investigative independence, seriously undercuts the IG's ability to influence policy and procedures within the subject agency. If acting as an outside, independent agency, the inspector general must often rely on the threat of embarrassment through critical published reports or leaks to the media in order to generate reform of the agency's policies and procedures. Actual use, or threatened use, of such leverage necessarily results in an adversarial relationship between the inspector general and the subject agency. Recommended reforms are rarely well received when proposed by an adversary.

Thus, we faced a dilemma in structuring the relationship of the SCA to its Inspector General. If we were to succeed in controlling racketeering and corruption through institutional reform then the IG would have to play a role as a senior policy maker within the SCA. How, then, could it protect itself from being co-opted or how could it effectively carry out its covert investigations?

The answer we arrived at tilted in favor of institutional integration but provided important

safeguards. The IG was designated a senior vice-president of the SCA, reporting directly to and working closely with the President/CEO. The IG attends every cabinet meeting and is involved in the formulation of all policies and procedures. As I shall describe later, no contractor may bid on an SCA construction project unless the firm has previously been approved by the IG and no contract can be awarded unless first signed off on by the IG.

However, to protect its independence, the IG office is physically located in a different part of New York City than the SCA headquarters. And most importantly, the IG not only reports to the President/CEO but also to the Board of Trustees which appoints the President/CEO. This dual reporting gives to the IG a role that is simultaneously both internal and external to the SCA. In our short history, I am pleased to say that there has been no lack of support and cooperation from the President/CEO for either our investigations or recommendations for institutional reform.

Snapshot of investigative planning and execution and the multiple remedial results made possible

Perhaps the best way to illustrate how the many units described above interact is to describe a hypothetical initiative undertaken by the IG office and the variety of remedial actions thereby made possible. As you will see, the success of the IG in accomplishing its mission is dependent on each unit being supported by, and in turn supporting, every other unit.

Let us suppose that we have reason to believe that the roofing industry in New York City is mob controlled and engages in multiple forms of criminality. Such belief could have arisen from an indictment of some industry members, from allegations determined to be credible or from information gained from unrelated investigations. With over 1,000 buildings in the school

inventory and plans to construct many new ones, it is clear that the SCA is a major source of income for the roofing trade and would stand to lose millions if victimized by rampant criminality in this industry.

The first thing we would do would be to direct a strategic analyst from the Research and Analysis Unit to prepare an assessment of the patterns of corruption and racketeering in the roofing industry throughout the city. That analyst would start by requesting from the Intelligence Unit all information relating to the local roofing trade. The analyst would also conduct its own research of the issue (and feed the results of his or her research back to the Intelligence Unit).

Intelligence will have a computerized base of information drawn from such sources as federal, state and local indictments, investigative reports, newspaper articles, books, periodicals, and legislative and commission reports that would be analyzed and digested. Informants from the Field Associates program, as well as law enforcement investigators and prosecutors, would be interviewed. Companies identified as having mob connections, criminal histories or suspicious associations would be subjected to corporate background analyses to identify affiliations with other companies and sources of capitalization. Computer runs of Board of Education contracting files would be requested in order to identify what roofers had participated in the school building program over the past several years and who their suppliers were.

Based on this information and more, the strategic analyst would prepare a report presenting an assessment of how the roofing industry had been infected by past criminality and how the SCA might be vulnerable. Let us suppose a cartel of roofing contractors had been identified in one indictment. Certain frauds in the underperforming on contracts had been

exposed in another investigation. An informant described how invoices could be falsified to defraud the Authority. Certain Cosa Nostra connections with various companies could be established or suspected. All of this information would be set forth in the strategic analyst's criminal assessment.

This assessment would then be forwarded to the Investigation Bureau. An investigative team would be assigned to develop and execute an investigative plan. The team might be comprised of two investigators (interviews and surveillances), an engineering auditor (field inspections of current roofing projects), an accountant (analysis of books and records), and a tactical or investigative analyst. The investigative plan would draw on the criminal assessment to set forth an investigative strategy for determining whether SCA's roofing contractors are engaging in any of the patterns of conduct identified in the criminal assessment. As the investigations proceed, reports would be generated daily by each member of the team, and these reports would be fed to the Intelligence Unit which, through its computerized network linking it with all units in the office, would make the information immediately available to the rest of the organization.

As the investigation proceeds, other units and disciplines would become involved. The law enforcement personnel in the Criminal Investigations and Prosecutions Unit would pursue criminal leads utilizing such investigative tools as wire taps, subpoenas, grand juries, etc. Where appropriate and legally permissible, they could feed information back to the Intelligence Unit. As wrongdoing (criminal or otherwise) is identified, the systems analyst would review the investigative findings to determine whether SCA policies and procedures could or should be reformed to block opportunities to engage in such wrongdoing (e.g., a different approach to job

site inspections, invoice auditing, contractor or supplier selection). The Counsel would review the investigative findings to determine whether civil relief might be available (e.g., contract actions, forfeiture of contractor assets, treble damage civil racketeering suits, injunctive relief).

At the conclusion of the investigation, it is therefore possible that a number of different deterrent and opportunity blocking strategies might have been made possible -- indictments and civil lawsuits against certain individuals and companies; debarment of contracting firms from future work; and recommendations for reform of SCA internal policies and procedures.

The foregoing is, of course, only one of many ways in which the IG may initiate investigations. An IG Hot-Line telephone number is prominently displayed at hundreds of construction sites urging the public to report allegations of wrongdoing. Other investigations may be initiated by the law enforcement personnel assigned to the Criminal Investigations and Prosecutions Unit. By virtue of their integration into the IG office, police officers can utilize their informants and undercover operatives to further their investigations into labor racketeering, official corruption and corporate frauds. The IG can also sponsor undercover companies to bid on SCA construction work, and place undercover operatives in the Authority where they can pose as inspectors, engineers or managers and approach construction company personnel who are targets of investigations.

As a result of these investigations and the many varied kinds of sanctions they make possible, deterrence of criminal conduct can be substantial. As importantly, the need for institutional reform can be documented and revisions of policies and procedures imposed so as to block opportunities to criminally victimize the SCA.

Another effective tool in attacking racketeering companies lies in the power of the IG to

direct the SCA to refuse to do business with any company that it deems to be lacking in "a reputation for honesty and integrity". By virtue of that simple phrase, the IG can accomplish more in a few days to cripple a mob controlled company than a criminal investigation can do in a year. By refusing to do business with a company, we are not only cutting off a part of the mobs "legitimate" livelihood, we are also preventing it from engaging in the many illicit activities it would have pursued on SCA projects.

In recognition of the powerful economic tool we possess, the SCA has instituted a prequalification procedure in which the Office of the Inspector General plays a key role. No firm can do business with the SCA without first having passed a prequalification review by the Inspector General.

Based upon our experience with organized crime and the construction industry, we have developed a comprehensive questionnaire that not only allows us to identify corrupt companies, but helps us to ferret out the alter egos, successor companies and dummy corporations that frequently enable organized crime figures to remain in business even after exposure or criminal conviction.

The prequalification process frequently involves all the various components of our office. Because some organized crime figures can be highly sophisticated in hiding the true ownership and control of a company, we often have to marshal the talents of our intelligence specialists, research analysts, criminal investigators and accountants to track down leads and verify information which would lead us to conclude that the company should not be permitted to bid for SCA contracts. Some of these prequalification reviews have generated criminal investigations and some significant prosecutions.

It is our experience that no matter how adept a group is at constructing a corporate veil, it is often in the area of finances that the veil is finally lifted. Invariably, it is only when one examines bank accounts or the personal indemnifications that insure or bond a company, that one finally begins to see who truly owns or controls a firm.

In our first year and a half of operation we have been highly successful in penetrating these corporate veils and debarring companies for a period of up to five years. The effect of these sanctions are compounded as other public agencies, based on our findings, also bar these companies from government work. We are now in the process of expanding the prequalification process to include subcontractors and vendor/suppliers as well. By extending prequalification to these latter groups we also prevent corrupt companies and individuals from earning our money indirectly, as well as directly.

QUANTIFYING OUR ACCOMPLISHMENTS

Because the IG office has only been fully operational for just over a year and a half (and fully staffed for much less than that), it is difficult to quantify many of its accomplishments. One reason is that many of our investigations (and the prosecutions, civil suits and recommendations for institutional reform which will result therefrom) are still at a stage where need for confidentiality precludes public disclosure and discussion. Nevertheless there are still some impressive results which can be reported.

Prosecutions

Some of the prosecutions we have generated or to which we have made substantial

contributions include the following:

Two indictments and convictions of individuals running "boiler room" operations in New York City and California that generated counterfeit surety bonds. Because surety bonds protect the owner against default by its contractors, the SCA and numerous other agencies had been put at great financial risk by the submission of these phony bonds. An IG analytic task force is preparing a report based on the investigative findings to recommend reform of bonding practices.

One indictment of a contractor for submitting fraudulent bills to the SCA and another indictment of a vendor for defrauding the United States Army Corps of Engineers and the SCA in a \$1.6 million phony billing scheme.

Conviction of a contractor for attempting to bribe an SCA employee.

Conviction of the "Godfather" of the Greek Organized Crime Family in New York City and several of his associates for concealing the mobster's hidden interest on a prequalification application submitted to the SCA. The Godfather, whom many in the city's Greek community considered untouchable, is serving a one year jail sentence.

The anticipated indictment in the very near future of a contractor who defrauded the SCA by more than \$500,000. The underlying investigation was structured not only to develop evidence of crimes but also to identify assets which the SCA will seize in a civil suit that will parallel the criminal prosecution.

While prosecutions such as these and the many others that will surely follow serve a valuable deterrent role, they do little on their own to reduce the myriad opportunities that construction contractors and vendors have used to defraud public agencies such as the SCA. As stated earlier, this protection can only be brought about through institutional reform of the practices and procedures by which the SCA conducts its business.

Institutional Reforms

(1) *Prequalification of Contractors.* Perhaps the most immediately beneficial reform generated by the IG was adoption of the extraordinarily rigorous prequalification process referred to above. Throughout the world where contracts are awarded through competitive bidding, most public agencies do not scrutinize the moral worth and performance capability of their potential contractors until after bids are submitted. Only then is the one company with the lowest bid subjected to such scrutiny. Reviewing a company's moral worth at this late point in the contracting process presents several problems. First, there is generally inadequate time to do an in depth analysis of the firm, its principals and other affiliated companies. Construction firms are extraordinarily adept at operating like chameleons -- disappearing one day only to reappear the next with different names, principals, addresses, etc. It is therefore extremely important although time consuming to conduct an adequate background investigation, especially of those corrupt firms who have gone to great lengths to conceal their hidden owners and unethical past dealings. Secondly, there is a strong possibility that if an agency rejects a company that has submitted the lowest competitive bid, that company will sue the agency and possibly delay award of the contract to any other company for many months -- a potentially disastrous occurrence to an agency with a need to move its contract forward immediately. Finally, if the pool of contractors submitting bids contains a corrupt or racketeer influenced company, other reputable and honest companies may not submit bids as a result of threats or perception of a violent retaliation.

The IG therefore designed a process which required prequalification of all contractors -- no company may even seek to do work with the SCA or submit a bid unless it has first been

found qualified to do business. One of the criteria for prequalification is that the company have a reputation for and a record of law-abiding and ethical conduct. As described above, the IG scrutinizes each company's financial history, the background of its owners, officers and all affiliated companies. To date the IG has conducted over 2000 background evaluations in connection with prequalification and contract approvals. Over 60 firms have been debarred, many of whom had ties to organized crime or were alter egos of firms with prior legal or debarment problems. (See attached newspaper articles.)

(2) *Advisories and Certifications.* Any debarment recommended by the IG must be sustainable in a court of law in the event of legal challenge. Consequently, there are occasions where there may be circumstantial evidence about the fitness of a firm but insufficient evidence to sustain a debarment in the event of judicial review.

In such instances we may issue an Advisory to the SCA whereby we caution the appropriate personnel closely to supervise the firm in the event it is awarded a contract. Because of our background review, the Advisory can pinpoint particular areas where project managers should be on guard for corrupt activity.

In other instances where we are concerned about a company's past behavior or possible associations, we may ask the applicant to complete a sworn Certification in which the principals either pledge to refrain from certain types of behavior or vow that they will have no involvement with specific individuals or companies. To date, we have issued over a dozen Advisories and two dozen Certifications. In one instance where a firm was found to have violated a Certification promise not to permit a corrupt individual to have any involvement with the firm, we terminated the firm's contract and saved hundreds of thousands of dollars by

claiming the firm had fraudulently induced the SCA to enter into the contract.

(3) *The Independent Auditing Firm.* A dilemma we sometimes face in prequalification reviews is whether or not a firm should be punished for the acts of one individual, especially where the firm has since severed all connections with that person.

A case in point involved the E. W. Howell Company, a major construction firm in the New York area. Howell had several SCA contracts, and was about to be awarded an additional \$32 million project, when the IG learned that they were the subject of a pending criminal investigation. Our own investigation disclosed the strong possibility that two former principals of Howell might shortly be indicted for fraud in connection with a five year old construction project.

Under SCA standards we could have caused Howell to be debarred from future work and terminated from their two existing SCA contracts. We recognized, however, that the suspect employees had left the firm, that new owners were in place and that the new owners, anxious to "turn a new leaf," had cleaned house and adopted rules for a more tightly run operation.

Moreover, we recognized that if Howell were to be disqualified from the pending contract, the SCA would have had to spend an additional \$2.5 million by awarding that contract to the next lowest bidder, and might have been forced to terminate Howell's two other contracts.

In an effort to be fair to the new owners, but at the same time mindful that the company had benefitted from corrupt activities in the past, the OIG fashioned an historic and novel solution (see attached briefing paper) whereby the contract was awarded to Howell under the following conditions:

- Howell was required to adopt a strict Code of Business Ethics, and agreed to extensive training of all Howell staff on both the new Code and related ethical

issues.

- Howell designed and implemented a comprehensive Corruption Prevention Program to prevent any criminal or unethical conduct from occurring on SCA jobs.
- Howell was required to retain the services of an Investigative Auditing Firm (IAF) at Howell's expense, to monitor and enforce Howell's adherence to the Code of Ethics and to the Corruption Prevention Program. Howell was further required to provide the IAF access to all of Howell's books, records and operations. The IAF is to report all findings to the IG.

The agreement provides the SCA with an unprecedented measure of protection. We can monitor, via the internal perspective of the IAF, this contractor's compliance with strict standards of ethics. And the company, not the taxpayer, foots the bill. Moreover the agreement represents an important step in the direction charted by the SCA trustees, its President/CEO and the Inspector General by shifting the primary responsibility for preventing and detecting corruption and racketeering from law enforcement to private industry. The bottom line is simple: Howell must, at its own expense, hire an investigating/auditing firm that will detect and report any corrupt activity to the IG.

If Howell fails to live up to its agreement, the SCA may bar the company from bidding on future contracts and rescind any or all existing contracts with the company. Interestingly, when the indictments were unsealed two weeks ago, the E.W. Howell Company, as a corporate entity, was not named as a defendant. One of the principal reasons publicly cited by the prosecutors for not naming Howell as a defendant was the firm's willingness to adopt the IAF agreement in its dealings with the SCA.

(4) *Procedural Reforms.* As one would expect with a billion dollar a year program, SCA operations are governed by a detailed and lengthy Policies and Procedures manual. Every

procedure is scrutinized by the Research and Analysis Unit from a loss prevention perspective. Furthermore, every allegation of corruption and every investigative finding is analyzed to determine if further modification of procedures or adoption of new ones are warranted. As a result of this process, the Research and Analysis has concluded over 15 studies which have produced recommendations that have saved or in the future will save millions of dollars.

Recognition of the OIG's Efforts

We are beginning to receive indications that the approach and organizational philosophy of the IG is being recognized as a model for possible replication elsewhere. We have been receiving an increasing number of inquiries from public agencies, legislative groups, academicians and news reporters seeking information on our prequalification and other procedures and approaches.

Law enforcement groups have also begun to recognize the value of working with such a uniquely positioned office. We are now working on significant criminal investigations with federal, state and local law enforcement agencies. Because we combine elements of law enforcement with administrative responsibilities, we can provide these agencies access to information that few prosecutors could easily obtain. For example, through the prequalification process we can compel an individual or firm to release information that no law enforcement body could ever obtain through voluntary release. Moreover, prosecutors are discovering that we are in a singular position of being able to assist undercover companies in getting prequalified. Several prosecutors have approached us about assisting an undercover company obtain work from the SCA.

One of the most significant endorsements of the IG's efforts came from the John F. Kennedy School of Government at Harvard University. The Kennedy School obtained a grant from the United States Justice Department, National Institute of Justice, to study the Office of the Inspector General so as to determine if the office represents a model for combatting corruption that should be replicated on a national level.

In describing the Office of the Inspector General, the grant proposal states that "the Office of the Inspector General represents a significant departure from prior models of inspectors general such as those found at the Federal level; indeed the consolidation of power, resources and roles comprising this agency may never before have been made available in a similar constellation to a stand-alone crime control office." The Kennedy School has particularly singled out the blending of traditional law enforcement procedures with research and analytical tools "as a significant new effort to prevent and control organized crime through a variety of non-traditional remedies and reforms."

* * *

In conclusion, the Office of the Inspector General for the New York City School Construction Authority gives us the opportunity to combat criminal activity using both traditional and non-traditional methods. In addition to standard criminal investigations, we have the power to sue individuals and companies civilly to recover monetary damages and we can prevent them from doing work with the SCA under any corporate name or form. Moreover, by being directly involved in the policy making mechanisms of the Authority, we can influence how the SCA does business and thus further block opportunities to engage in corrupt activity.

While protecting the SCA from victimization by the unscrupulous elements in the construction industry is our primary goal, there are other benefits to be derived from any success that we may achieve. It is a common knowledge that many of the more reputable and ethical construction companies in New York have in the past refused to bid on government work because of their distaste for all the corruption and organized crime influences that have historically been associated with government contracting. One of our successes in the first year has been that, as we have begun to weed out the criminals and corrupt companies, we have sent a message to the industry that has not gone unnoticed. Slowly, major construction companies that have never bid on public work before have begun to bid SCA projects. If our efforts convince more of these companies to join the SCA family we will improve the quality of public construction immeasurably while generating serious competition to the cartels (some of which are mob controlled) which have long dominated aspects of school construction.

Most of the staff of the IG office have a background in law enforcement. In the end, the real excitement and rewards of working this office lie in the fact that we can through administrative steps, informed and supported by law enforcement initiatives, do so much more to penalize and prevent corruption and racketeering than we were able to do when working exclusively in law enforcement agencies.

OFFICE OF THE INSPECTOR GENERAL ORGANIZATION PLAN

