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September 17, 2015

Michael Garner
Chief Diversity Officer
Metropolitan Transportation Authority
Department of Diversity and Civil Rights
2 Broadway, 16th Floor
New York, NY 10004

**Re: DDCR Certification Unit Operation
MTA/OIG #2015-09**

Dear Mr. Garner:

The Office of the MTA Inspector General (OIG) has recently completed two reviews of the operations of the Compliance Unit of the Department of Diversity and Civil Rights (DDCR). The first focused on DDCR's monitoring tasks that have the potential to detect and deter fraud and other serious contractor violations. The second reviewed the accuracy and completeness of DDCR's reports, both to the MTA Board and to the Federal Transit Administration (FTA) regarding payment information as to on-going federally funded contracts during fiscal year 2013. These reports contained findings and recommendations all of which were accepted by DDCR.

In this third report, OIG examines the operations of DDCR's Certification Unit which is responsible for determining a firm's eligibility to participate in the Disadvantaged Business Enterprise (DBE) program.

As you know, in order to first obtain and then retain DBE status, an applicant must demonstrate that it is a member of a socially and economically disadvantaged group; demonstrate corporate independence and control of a firm; meet personal net worth standards; and operate within gross receipt thresholds. The firm and its owner(s) must meet these standards during the initial certification and, subsequently, when reexamined on an annual basis.

As Metropolitan Transportation Authority is one of four agencies in the New York State Unified Certification Program (NYSUCP)¹ DDCR must comply with federal regulations as set out in 49 CFR Part 26 which have been incorporated in NYSUCP standard operating procedures. In this audit OIG staff examined the completeness of initial certification processes and the subsequent annual reviews that are required for a DBE firm to retain its status.

¹ The following four agencies constitute the NYSUCP: Metropolitan Transportation Authority, NY Department of Transportation, Niagara Frontier Transportation Authority, and the Port Authority of NY/NJ. The group developed standard operating procedures for the NYSUCP, based on federal rule 49 CFR Part 26.

OIG found that most elements of the initial certification process were performed in accordance with NYSUCP guidelines. However, subsequent annual reviews were not always performed, and some financial determinations were insufficient.

Annual Reviews

According to NYSUCP procedures, the annual review process should take about two to three months. It begins 30 days prior to a firm's anniversary date on which it was first certified, when the Unified Certification Program (UCP) Partner initiates a request for the firm's annual submission materials. The process ends when the UCP Partner either issues a letter to the DBE affirming its continued participation, or removes it from the program. If a firm is unresponsive to requests for submission materials, the Certifying Partner "shall" initiate decertification within 30 days from the date that the annual submission was due.

In conducting its audit, OIG found that DDCR does not have a formal system in place to precisely determine whether all required annual reviews are completed each year. While the Assistant Director, Certification Unit, acknowledged that conducting initial eligibility reviews are the Unit's priority, she admitted that she does not track how often her unit completes the required annual reviews of the documents submitted by certified DBE firms. She acknowledged, too, that not all of the required reviews are completed, estimating that about 25 percent were not performed. An analysis of the certified DBE firms listed in NYSUCP's online directory BizNet² for 2013 revealed that approximately 30 percent did not have annual submission review dates posted for that year.³

To determine DDCR's compliance with the required steps of the annual review process, OIG reviewed a sample of 22 firms that, according to BizNet, did not undergo required annual submission reviews. We determined that from 2000 through 2014, the 22 firms should have collectively provided 183 annual submissions for review by DDCR which should have thus issued for this period 183 DBE Certification Annual Review Notice letters attesting to these firms' continued eligibility.

A detailed review of the 183 files revealed that 47 percent of the firms either did not submit any documents or their submissions were incomplete. Another 27 percent submitted all required documents, but there was no indication that any review had been completed by DDCR. Only 22 percent of the sampled files contained all required documents, as well as the Annual Review Notice letters issued by DDCR affirming continued eligibility after review.

A DDCR manager acknowledged that she occasionally skipped conducting annual reviews, allowing owners "the benefit of the doubt" when they did not submit annual review documents.

² BizNet is NYSUCP's public directory that lists all firms certified as DBE certified contractors. DDCR is required to access BizNet and enter the date each time it completes an annual review.

³ This 30 percent figure may not be precise because BizNet data is not always kept current.

This approach was shared by the Assistant Director and by other managers who explained that because a great deal of effort and resources are expended initially certifying firms, staff does its best to retain program participants. While OIG recognizes the effort DDCR makes to enroll firms in the program, the requirements, both under federal and NYSUCP's rules, cannot be ignored. DDCR needs to establish a deadline for receiving documents after which a firm is either removed from the program or the manager must explain, in writing to the Assistant Director, why an extension should be granted.

Financial Review Process

There are two financial standards that both the DBE firm and its owner must initially meet and continue to meet each year to maintain its status as a certified DBE firm. These are the gross receipts threshold for the firm itself and the owner's personal net worth ceiling. The gross receipts or "size standard" is based on the U.S. Small Business Administration's (SBA) definition of a small business.⁴ Firms must fall within the parameters SBA sets for each industry specialty code. In addition, federal regulations require that a firm's annual gross receipts are not to exceed allowable limits when averaged over a three year period. Prior to 2011, the applicable limit was set at \$20.41 million, with the current limit set at \$22.41 million. Gross receipts are inclusive of all receipts from "affiliated businesses", as defined by SBA rules. As set by Federal Regulations, the personal net worth of the qualifying owner could not exceed \$750,000 prior to 2011⁵, with the current ceiling set at \$1,320,000.⁶

During the initial DBE eligibility determination, DDCR collects both business and individual tax returns. Once a firm has achieved initial DBE certification, the owner must submit updated documentation to DDCR annually in order for the agency to determine whether the firm continues to meet program criteria.⁷ DDCR has the right to request additional information and documentation such as bank statements or loan documents to assist in the determination and verification of financial information.

OIG reviewed the financial analyses that DDCR performed initially and for each subsequent year for the 22 firms in its sample to test whether DDCR complied with these requirements. In preparation for this review, OIG auditors underwent 14 hours of DBE certification training sponsored by the U.S. Department of Transportation.

OIG observed that, in some cases, DDCR conducted full and rigorous reviews of financial records. For example, an applicant firm that had been approved by a New Jersey UCP also

⁴ See *Table of Small Business Size Standards Matched to North American Industry Classification System* at https://www.sba.gov/sites/default/files/files/Size_Standards_Table.pdf

⁵ Federal Register / Vol. 76, No. 19 / Friday, January 28, 2011 pg 5083

⁶ See 49 CFR §26.67 (2)(i)

⁷ See *New York State Unified Certification Standards: Standard Operating Procedures*, "Notice of Annual Submission Requirements," pp 38-39.

applied for NY certification. DDCR expanded the certification review of the original NJ UCP Partner and found that the owner was employed full time elsewhere, preventing him from devoting the time needed to exercise independent and effective management of the firm, thus disqualifying him from program participation under the federal "business control" standard. The firm's application was thus rejected. However, in other cases, a more extensive review was required than was carried out.

OIG reviewed the financial analyses performed on ten certified firms, both at the time of initial certification and subsequent annual review. While most of these financial packages were located, some could not be found, and in others, DDCR did not collect adequate supporting documentation. By failing to request all supporting financial information, accurate personal net worth figures could not always be determined.

Federal Rules also state that all affiliate income, without regard to magnitude, must be included in an applicant firm's total income. OIG found that in some cases the financial information for affiliated companies was not requested and analyzed by DDCR, thus failing to provide in some cases a basis for an accurate total income figure.

Skyline Software

The Compliance Unit of DDCR is charged with monitoring the performance of DBE contractors on MTA projects, including obtaining and verifying payments from prime contractors to their DBE subcontractors. This information is recorded and tracked using a customized software package called Skyline. If a DBE has worked on an MTA contract, this payment data can be used by the Certification Unit to verify the gross receipts submitted by the DBE as part of its annual review process. However, at present, Certification staff does not utilize the Skyline system.

OIG is informed that within the next year, DDCR is moving to join the NYSUCP state-wide web based system known as B2G. This system will centrally maintain payment to DBE firms by all four members of NYSUCP, and will contain additional information that the Certification Unit staff will review each year. The Certification Unit should also utilize this system once it is in place, and must use the data to verify information reported regarding MTA certified DBEs.

The Affidavit of No Change Form

In July 2014 the U.S. Department of Transportation (DOT) eliminated the requirement for DBE firms to annually submit Personal Net Worth Statements and personal tax returns. Instead, they are only required to submit an "Affidavit of No Change" form. The program now relies on the affidavit form itself to detect changes in owners' financial conditions that may affect program eligibility. Each certifying agency creates its own form, with some more comprehensive than others. We observed that DDCR's form states the corporate receipt threshold, but does not state

the personal net worth limit currently defined as \$1.32M. This personal net worth threshold should be specified as well.

In addition, federal regulations⁸ identify four categories, “ownership”, “control”, “size”, and “disadvantaged status”, regarding which firms must notify their certifying agency of any changes within 30 days of their occurrences. DDCR’s affidavit addresses the first two. However, it does not mandate the 30-day notification period for changes in business “size” and “disadvantaged status”. A revision of the form to include the aforementioned would both comply with Federal Regulations, and improve DDCR’s ability to hold the owner accountable for failing to report relevant information.

RECOMMENDATIONS

In order to fully comply with federal mandates and to ensure that its operations carry out program goals, OIG recommends that DDCR:

1. Develop a tracking system that enables the DDCR Assistant Director to monitor the completion of annual reviews by managers, and note those firms that have not been completed within 60 days of the firm’s anniversary date.
2. Ensure that completion dates for annual reviews are entered in BizNet.
3. Establish a deadline for receiving annual submission documents after which, if not received, a firm is either removed from the program or the manager explains in writing to the DDCR Assistant Director why an extension is being given.
4. Provide additional financial analysis training to DDCR managers such as U.S. DOT’s DBE/ACDBE Certification Training.
5. Ensure that all affiliate income is included in the gross receipts calculation of DBE firms.
6. Fully utilize the SKYLINE system and B2G when it becomes available to enable managers to verify gross receipts reported by DBE firms.
7. Update the “Affidavit of No Change” form to specify personal net worth limits and expand 30-day notification categories to include size and disadvantaged status.

⁸ See 49 CFR Part 26.83

Agency Response

In his response, the MTA Chief Diversity Officer noted that as follow-up to our report DDCR promptly began implementing all our recommendations. Specifically, the department has:

- *Developed a tracking system to enable DDCR certification managers to monitor completion of annual reviews;*
- *Entered completion dates of annual reviews in BizNet; and*
- *Initiated decertification proceedings that have resulted in the removal of over 40 DBE firms for failure to submit annual Affidavit of No Change forms.*

The department has also taken measures to enhance staff skills by facilitating access to financial analysis training provided by the USDOT, reinforced inclusion of affiliate information in all gross receipt calculations, and introduced direct access to Lexis/Nexis for use by certification managers.

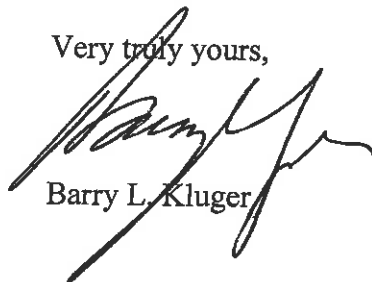
Further, DDCR has updated the Affidavit of No Change form to include the personal net worth threshold and extended the 30-day notification requirement to cover changes in size and disadvantage status. The department intends to recommend that the remaining three NYUCP agencies adopt these changes in their respective forms as well.

Finally, DDCR is in the process of migrating to the NYS B2G system.

We appreciate your personal and proactive attention to the issues we raised, as well as the courtesy and cooperation afforded to us at all times by you and your staff.

Should you have any questions regarding this final report, please contact me or Executive Deputy Inspector General Elizabeth Keating at (212) 878-0022.

Very truly yours,



Barry L. Kluger