PERFORMANCE AUDIT:

PORT AUTHORITY OF ALLEGHENY COUNTY

JULY 1, 2002, THROUGH AUGUST 22, 2007

DECEMBER 2007

JACK WAGNER, AUDITOR GENERAL

PENNSYLVANIA DEPARTMENT OF THE AUDITOR GENERAL

December 3, 2007

Mr. Stephen G. Bland, CEO
Port Authority of Allegheny County
Heinz 57 Center
345 Sixth Avenue
Pittsburgh, PA 15222-2527

Dear Mr. Bland:

Enclosed is our performance audit of the Port Authority of Allegheny County for the period of July 1, 2002, through June 30, 2006, with updated information through August 22, 2007. The Second Class County Port Authority Act requires that we conduct a performance audit of the Port Authority at least once every four years, and we completed the audit in accordance with generally accepted government auditing standards as issued by the Comptroller General of the United States.

The most significant finding in this report, Finding One, concerns the Port Authority's governance. Specifically, we report that the Commonwealth contributes more than 55 percent of the operating revenues to the Port Authority but has no representation on the Port Authority's board of directors. Instead, as you know, the nine board members are all appointed by one local official, the chief executive of Allegheny County. This arrangement—which does not result in a structure of checks and balances inherent in a more diversely appointed board—will have to be corrected through a legislative change. We are recommending such a change, and we call for your active support of it.

In Finding Two, we report that the Port Authority contributed to its own fiscal crisis by committing $15.5 million to rent prime downtown office space unnecessarily. The $15.5 million includes $7.7 million to renovate the new space in the downtown Heinz Center and $7.8 million to enter into a 10-year lease for that prime new space. What makes this commitment of funds so irresponsible is that the Port Authority moved into this new leased space after having just spent $4.7 million to renovate space that it owns—and was already using—in nearby Manchester. Furthermore, while 40 percent of that owned space in Manchester now remains vacant, the Port Authority still is not using all the new leased space downtown. As a result, the Port Authority is using taxpayer dollars to lease empty prime space when it has empty but usable owned space.

In Finding Three, we describe how the Port Authority gave excessive benefits to top executives, other staff, and retirees. The excess benefits include generous pension arrangements, excessive vacation and sick time, and additional compensation for the former CEO. The Port Authority also extended excessive vacation and sick time, generous pension arrangements, and other allowances to other members of management and staff. No matter who has been the recipient, these excessive benefits have been paid for by state, federal, and county taxpayers and by fares from riders. In addition, the excessive benefits related to the pension plans have significantly decreased the funding levels of those plans, thereby impacting the future pension benefits of employees who have not yet retired.

In Finding Four, we found that the Port Authority ineffectively planned, budgeted, and/or implemented three of its most prominent capital projects undertaken during the last decade. We note that, even with the elimination of crucial design components of the projects, the Port Authority overstated its overall ridership estimates and, at the same time, understated either project costs or completion dates.

In Finding Five, we report a successful aspect of the Port Authority's performance, specifically the success of the Port Authority in generating advertising revenues with its own in-house advertising sales staff.

These five findings are discussed in detail in the enclosed report. Please note that we have already conveyed most of Findings One, Two, and Three to you via three interim reports we released earlier this year (January 30, March 2, and March 22). Subsequently, in a letter to us dated March 30, 2007, the Port Authority responded positively to many of the issues we raised, and we discuss that response in the report. We also include the Port Authority's most recent response dated November 30.

As provided by the government auditing standards under which the audit was conducted, we will follow up on our findings and recommendations to determine whether significant findings and recommendations are being addressed. Accordingly, we will contact you to follow up on these matters within the next 12 to 24 months.

Sincerely,

JACK WAGNER
Auditor General

Enclosure

Distribution: Chairman and Board of Directors, Port Authority of Allegheny County

cc: The Honorable Edward G. Rendell, Governor of Pennsylvania
The Honorable Joseph B. Scarnati, III, President Pro Tempore, Pennsylvania Senate
The Honorable Dennis M. O'Brien, Speaker, Pennsylvania House of Representatives
Members of the Allegheny County Delegation, Pennsylvania Senate
Members of the Allegheny County Delegation, Pennsylvania House of Representatives
The Honorable Dan Onorato, Allegheny County Chief Executive
President and Members, Allegheny County Council

Pennsylvania Department of the Auditor General
Jack Wagner, Auditor General
December 2007

Table of Contents

Table of Contents

Performance Audit:
Port Authority of Allegheny County

Pennsylvania Department of the Auditor General
Jack Wagner, Auditor General
December 2007

Pennsylvania Department of the Auditor General
Jack Wagner, Auditor General
December 2007

Results in Brief

The Port Authority of Allegheny County should undergo a change in its governing structure so that the largest financial contributor, the Commonwealth of Pennsylvania, is represented by seats on the nine-member board of directors. Requiring legislative action by the Pennsylvania General Assembly, this change in governance is the most significant factor that will lead to permanent reform at the Port Authority.

In this performance audit report, we discuss the governance issue as well as other significant issues of the financially troubled Port Authority covering the period of July 1, 2002, through June 30, 2006, with certain information updated through August 22, 2007. We are required to conduct this audit by the Second Class County Port Authority Act, and we have completed our work under generally accepted government auditing standards issued by the Comptroller General of the United States.

Included in our report are 5 findings and 13 related recommendations, as well as an update of audit findings from our prior audit of the Port Authority released in July 2003. In addition, beginning on page 69, we have included the Port Authority's full written response dated November 30, 2007.

Port Authority operation and finances

As the second largest metropolitan transit agency in the Commonwealth of Pennsylvania and the 21st largest transit operation in the country, the Port Authority serves an area of 730 square miles, including the City of Pittsburgh, all of Allegheny County, and limited portions of Armstrong, Beaver, Washington, and Westmoreland counties.

As of January 2006, the Port Authority had 3,035 employees, of which 89.8 percent were represented by a collective bargaining unit. The nine board members are appointed by a single person, the Allegheny County Chief Executive, and confirmed by the Allegheny County Council.

 Performance Audit:
Port Authority of Allegheny County

Pennsylvania Department of the Auditor General
Jack Wagner, Auditor General
December 2007

The board members hire a chief executive officer who is responsible for the daily operation of the Port Authority, reports to the board, and is aided by members of senior staff.

For the fiscal year ended June 30, 2005, the Port Authority's total income was $309.2 million, most of which came from government grants and subsidies (county, state, and federal) and fares from riders. State government—i.e., Pennsylvania taxpayers—contributed $169.4 million of this total, which was significantly more than the amounts contributed by either the Allegheny County government, the federal government, or the riders. In fact, the $169.4 million contributed by the state is more than all the other contributions combined.

Findings and recommendations

1. **No state representation on governing board (pages 10–18)**
   The governing body of the financially troubled Port Authority of Allegheny County has included local but no state appointees even though state taxpayers provide the most money to keep the Port Authority operating.

   A legislative change is needed to address this finding, and the Port Authority as well as Allegheny County government should lobby for such a change to make the Port Authority more accountable to its largest contributor, the Commonwealth of Pennsylvania. We recommend that the Governor and the General Assembly should each appoint two Allegheny County residents to the Port Authority's nine-member board, thereby giving the Commonwealth four board seats in total.

   The county's chief executive should continue to appoint the remaining five board members but should ensure that at least one represents downtown businesses and another represents riders with disabilities.

---

2. **Unnecessary, expensive, and unused office space (pages 19–25)**
   The Port Authority was not accountable to taxpayers and, in fact, contributed to its own fiscal crisis by committing $15.5 million to rent prime downtown office space unnecessarily.

   This finding is made even more significant because the Port Authority is leasing prime downtown office space while, at the same time, owning a useable headquarters building nearby that is 50 percent vacant. We recommend that the Port Authority should return to the building it owns and sublet the expensive downtown space. In its response, the Port Authority notes it is considering the related cost of such actions, but it fails to address our recommendation not to renew or renegotiate the downtown lease when it expires in 2010.

3. **Top management that did not lead by example (pages 26–39)**
   The Port Authority gave excessive benefits to top executives, other staff, and retirees. Among these benefits were bonuses, liberal vacation and health care policies, early retirements, generous pensions, and various other advantages unusual for public employees. We issued interim reports to the Port Authority about these matters earlier in 2007, but top officials there have expressed disappointment that we limited our audit focus to management without extending our focus to union employees. We maintain, however, that it is critical for management to lead by example and, in so doing, can set prudent standards that lead to union negotiations that are fiscally responsible.

4. **Poor planning or implementation of capital projects (pages 40–55)**
   The Port Authority poorly planned or poorly implemented three of its most significant capital projects undertaken

during the past ten years. Regarding the West Busway/Wabash High-Occupancy-Vehicle project, the Port Authority should evaluate alternative solutions to the underutilization and excessive operating costs of the Wabash tunnel. Regarding the South Hills Village parking garage (associated with the Light Rail Transit System project), the Port Authority spent more than the federal government agreed to fund and should avoid this type of overspending in future projects. Regarding the poor planning and subsequent cost overruns for the North Shore Connector project, the Port Authority should carefully plan and budget the remainder of the project to ensure timely completion without additional cost overruns.

5. **Good revenues from sales of advertising by in-house staff (pages 56-57)**
   We report a positive finding about increased revenues from the sale of advertising space by the Port Authority's in-house sales staff.

Status of findings from prior audit

In determining the status of findings from our prior performance audit of the Port Authority for the period of July 1, 2000, through September 30, 2002, we found one unresolved issue related to computer equipment. Specifically, the Port Authority did not implement our recommendation that called for more accurate recording of the acquisition, transfer, and disposal of equipment.

Introduction and Background

In 1956, the Second Class County Port Authority Act (Act) created the Port Authority of Allegheny County (Port Authority) and gave it responsibility for planning and developing port facilities to serve the Pittsburgh area. In 1959, the Pennsylvania General Assembly amended the Act to permit the Port Authority to acquire privately owned transit facilities and to own and operate a public system of mass transit. The Port Authority began operations on March 1, 1964, when it assumed control of and consolidated the Pittsburgh Railways Company and 32 independent bus and inclined plane companies.[1]

The Port Authority is the second largest metropolitan transit agency in the Commonwealth of Pennsylvania, and the 21st largest transit operation in the country. The service area consists of 730 square miles, including the City of Pittsburgh, all of Allegheny County, and limited portions of Armstrong, Beaver, Washington, and Westmoreland counties.

The Port Authority's mission statement is "To deliver outstanding transportation services which connect people to life." Its corresponding vision statement is "To become America's premier public transportation company." [2]

As of January 2006, the Port Authority had 3,035 employees, of which 89.8 percent were represented by a collective bargaining unit.[3] A 9-member board of directors governs the Port Authority's operations, and all 9 members are appointed by a single person, the Allegheny County Chief Executive, and confirmed by the Allegheny County Council. The board members hire a chief executive officer who is responsible for the daily operation of the Port Authority and who reports to the

[1] "History of the Port Authority," Port Authority of Allegheny County Web site. Accessed June 18, 2007, at http://www.portauthority.org/PAAC/CompanyInfo/GeneralStatistics/History/tabid/55/Default.aspx.
[2] "Mission and Vision Statements," Port Authority of Allegheny County Web site. Accessed June 12, 2007, at http://www.portauthority.org/PAAC/CompanyInfo/GeneralStatistics/VisionandMission/tabid/78/Default.aspx.
[3] *Transit Agency Operational Audit, Port Authority of Allegheny County*, Pennsylvania Transportation Funding and Reform Commission, Final Report–Technical Appendix, Final Copy–January 2007. Page 3, "Introduction." Accessed online at ftp://ftp.dot.state.pa.us/public/pdf/TFRCReport/PAACFullReport.pdf on June 12, 2007.

board. The chief executive officer is aided by senior staff members who, for the period of our audit, represented the following seven divisions: office of the chief of staff, transit operations, engineering and construction, finance, marketing and communications, human resources, and information technology.[4] See Appendix C for the Port Authority's organization chart.

As of June 12, 2007, according to Port Authority officials, the Port Authority's fleet consisted of 905 buses, 83 light rail vehicles, 75 small transit vehicles, and 2 incline cars, all of which operated on 213 bus and rail routes and the Monongahela Incline.[5] During the fiscal year ended June 30, 2006, ridership totaled 69.9 million persons.[6] Ridership had been declining an average of almost 1 percent each year over the last decade until the fiscal year ended June 30, 2005, when it increased 1.7 percent following the completion of bus and light rail projects.[7] For the fiscal year ended June 30, 2006, ridership increased again, this time by 1.8 percent.[8] See Appendix A for ridership statistics for the fiscal years ended June 30, 2003, through June 30, 2006.

[4] "2007 Operating and Capital Improvement Budgets: Divisional Introduction," Port Authority of Allegheny County Web site. Accessed May 8, 2007, at http://www.portauthority.org/PAAC/Portals/0/2007BudgetFiles/departments/DivisionalIntroduction.pdf . The Port Authority announced in a press release dated March 5, 2007, that it planned to reduce the number of assistant general managers from eight to five as part of its cost-cutting measures. The impact on the Port Authority's organizational structure by these cuts was not disclosed. See the Web site at http://www.portauthority.org/PAAC/News/NewsRoom/PressReleases/tabid/278/Default.aspx.

[5] Information provided by Port Authority officials at exit meeting with Department of the Auditor General on November 21, 2007. As of July 1, 2007, the number of buses dropped to 878.

[6] Port Authority Financial Statements for the fiscal year ended June 30, 2006.

[7] Page 3, "Finance" section, *Transit Agency Operational Audit, Port Authority of Allegheny County*, Pennsylvania Transportation Funding and Reform Commission, Final Report–Technical Appendix, Final Copy–January 2007. Accessed June 12, 2007, at ftp://ftp.dot.state.pa.us/public/pdf/TFRCReport/PAACFullReport.pdf.

[8] Passenger data obtained from the Port Authority's financial statements.

Funding

For the fiscal year ended June 30, 2005, the most recent year for which detailed comparable financial data was available, the Port Authority's total income was $309.2 million, most of which came from government grants and subsidies (county, state, and federal) and fares from riders. State government—i.e., Pennsylvania taxpayers—contributed $169.4 million of this total, [9] which was significantly more than the amounts contributed by either the Allegheny County government, the federal government, or the riders.

Financial position of the Port Authority

For the fiscal year ended June 30, 2005, the expenses for transit operations were $304.9 million, yielding a transit operations surplus of $4.3 million when compared to the income of $309.2 million. The $4.3 million surplus was then combined with other Port Authority income from investments and other sources[10] and offset against expenses from capital activity and depreciation[11] to produce a net loss of $13 million for the fiscal year ended June 30, 2005. The net loss brought the Port Authority's accumulated deficit to over $66.6 million, a deficit that had begun prior to 2002.

Analysis of data extracted from the Port Authority's accounting records for the four fiscal years ending with June 30, 2006, shows that the expenses most affecting the financial problems related to operating activity of the Port Authority include a $35.2 million increase in fringe benefits for active and retired employees, a $10.9 million increase in fuel and lubrication

[9] National Transit Database, Federal Transit Administration. Available at http://www.ntdprogram.gov. View date: March 5, 2007.
[10] Other sources of funding include approximately $12 million in income from investments, and approximately $152 million in grants for construction projects and debt service. In 2005, the federal government provided about 72.3 percent of these capital grants; the state provided about 24.2 percent of the grants with the requirement that the Allegheny County government provide the remaining 3.5 percent.
[11] Capital activity costs include approximately $28 million to pay the interest on debt, $88 million for depreciation, and approximately $65 million to offset the increases in capital assets, net of related debt.

costs, and a $5.8 million increase in salaries—including the salary of the former CEO and his "sellback" of accumulated sick leave.

Also over the last four fiscal years ending with June 30, 2006, the increases in capital activity that most affected the financial position of the Port Authority include a $9.9 million increase per year in bond interest expense, a $9.6 million increase per year in bond payments, and a net increase of $75.2 million in capital assets.

Objectives, Scope, and Methodology

The Department of the Auditor General conducted this performance audit in order to provide an independent assessment of selected operations of the Port Authority of Allegheny County. The Second Class County Port Authority Act requires the Department of the Auditor General to conduct a performance audit of the Port Authority at least once every four years.[12] We conducted our work according to generally accepted government auditing standards as issued by the Comptroller General of the United States.

Objectives

The major objectives covered by the audit were a review of selected contracts, leases, and major capital projects; a review of operating revenues and expenses, including pension and other employee benefits; and an update on the status of prior audit findings. The specific audit objectives follow:

- To assess the benefits provided by the short- and long-term Port Authority contracts and to determine whether the contracts furthered the Port Authority's intended mission.

- To assess the operational impact of major capital projects, either completed or in progress as of March 31, 2007.

- To identify significant cost increases in operating expenses at the Port Authority, including employee benefits, and to recommend changes to help defray the impact of these cost increases.

- To identify the impact of operating revenues and recommend ways to maximize those revenues.

- To assess the impact of the Deferred Retirement Option Plan (D.R.O.P.) pension plan provisions and other pension plan benefits adopted by the Port Authority for selected non-represented employees.

[12] 55 P.S. § 553.2(a)(2).

- We also planned to follow up on the implementation of the recommendations made during our prior audit of the Port Authority (released in July 2003) in the areas of the bus maintenance work order system, the establishment of effective controls over fixed assets, computer equipment and the motor fleet, and in controlling maintenance overtime.

Scope

The primary scope period of the audit was for the fiscal years from 2003 through 2006, a four-year period authorized by the enabling legislation. The four-year period started on July 1, 2002, and extended through June 30, 2006. Our analysis of certain contracts, projects, costs, benefits, and revenues noted that relevant Port Authority activity continued after June 30, 2006. As a result, our inquiry and analysis continued through August 2007, an extension of time considered necessary to allow for a more accurate reporting of identified issues, to allow management to respond effectively to findings, and when feasible, to take into account Port Authority management's corrective actions. The individual report findings specify if an extension of time was necessary.

Methodology

We performed the following procedures to accomplish our audit objectives.

We interviewed and/or met with key Port Authority personnel, including its chief executive officer, chief financial officer, controllers, manager of real estate services, director of accounting, assistant general manager of human resources, assistant general manager of engineering and construction, assistant general manager of marketing and communications, chief technology officer, director of planning, lead transit planner, senior grants administrator, and the manager of benefits administration.

To analyze Port Authority governance arrangements, we reviewed the Port Authority's enabling legislation, the Pennsylvania Transportation Funding and Reform Commission's Final Report, dated November 2006,[13] and publications from The Allegheny Institute for Public Policy.[14]

For our analysis of the Heinz Building lease, we reviewed two separate internal studies of office space requirements and usage conducted by the Port Authority in March 1999 and February 2007. We analyzed the original Heinz Building office lease agreement, as well as the associated amendment, between 623 Smithfield Associates, Ltd., and the Port Authority. We also examined the office lease agreements between the Port Authority and its various tenants at the Port Authority's Manchester building, including the Dick Corporation and DMJM/GANNETT. Finally, we reviewed the lease agreement, as well as its renewals and amendments, between the Port Authority and the Pittsburgh Trust for Cultural Resources for additional building space owned by the Port Authority.

For our analysis of the Deferred Retirement Option Plan and other benefits for employees not represented by a union, we reviewed the Port Authority's financial statements for the three fiscal years ended June 30, 2004, through June 30, 2006; the minutes of the February 22, 2002, meeting of the Port Authority board of directors where the D.R.O.P. was authorized; and the applicable retirement and disability allowance plans for employees not represented by a union. We also examined the pension account summaries, the payroll and employment histories, and the records of any prior public service purchases for the 44 D.R.O.P. participants. Additionally, we reviewed the annual actuarial cost studies prepared by the Port Authority's pension plan consultant for the plan years ended December 31, 2000, through 2005. We reviewed the collective bargaining agreements between the

[13] *Investing in Our Future: Addressing Pennsylvania's Transportation Funding Crisis,* Pennsylvania Transportation Funding and Reform Commission, Final Report, November 2006, Chapter Three – "Transit Operational Audits,"
[14] "Port Authority Governance Needs to be Reformed," *Policy Brief – An electronic publication of The Allegheny Institute for Public Policy,* March 1, 2007, Volume 7, Number 9.

Port Authority and Local Union 29 of the International Brotherhood of Electrical Workers, AFLCIO, effective May 1, 2003, to April 30, 2006, and May 1, 2006, to April 30, 2009. Finally, we analyzed the Port Authority's retirement and disability allowance plan for employees represented by Local 85 of the Amalgamated Transit Union effective December 1, 1997, and we also examined the November 19, 2005, memorandum of agreement between the Port Authority and Local 85 of the Amalgamated Transit Union.

We evaluated the Port Authority's management of three major capital projects: the West Busway/Wabash high-occupancy-vehicle project, the Stage II Light Rail Transit (LRT)/South Hills Village Park & Ride project, and the North Shore Connector project. For this analysis, we reviewed the original project proposals, impact studies, cost projections, revenue estimates, needs analyses, community input, ridership statistics, and other available data used to justify the projects. We also compared original project justifications to actual costs and other intended or unintended results.

For our analysis of operating expenses and operating revenues, we reviewed recorded data obtained from the Federal Transit Administration and the Port Authority's accounting records. We subjected accounts with significant changes to additional inquiry and analysis.

For the status of prior audit recommendations, we performed tests as part of, or in conjunction with, the current audit and interviewed appropriate Port Authority personnel regarding the specific prior audit findings and recommendations. We noted the changes made to resolve the findings, the adoption of the prior audit's recommendations, or the establishment of other corrective actions in the areas of the bus maintenance work order system and the controls over fixed assets and computer equipment, the motor fleet, and maintenance overtime.

Findings and Recommendations

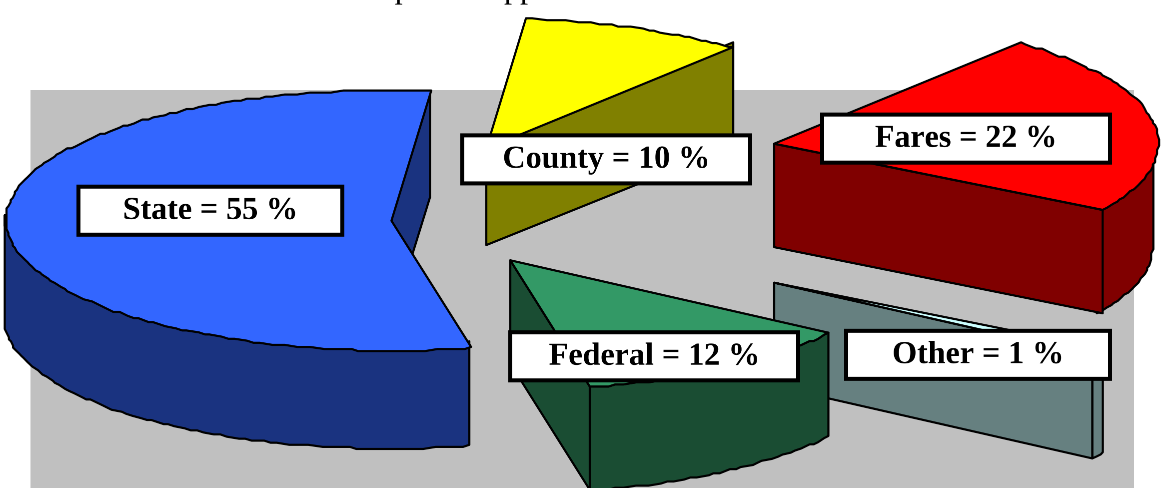
As the result of our audit work, we identified 5 findings and have made 13 related recommendations, all of which we present in this report. We expect that the Port Authority will address our recommendations diligently as it continues its operations, and we acknowledge that the Port Authority has already discussed publicly a number of proposed changes. This report will help us to facilitate follow-up so that we can determine and report subsequently (1) what corrective actions the Port Authority has taken and (2) how effective any such corrective actions have been.

Finding One

The governing body of the financially troubled Port Authority of Allegheny County has included local but no state appointees even though state taxpayers provide the most money to keep the Port Authority operating.

The Port Authority has suffered from serious financial and image difficulties over our audit period. Service cuts have been made in an attempt to reduce the operating deficit, and more cuts and/or fare increases have been discussed. No matter how necessary, such actions can be devastating to riders, the Pittsburgh business community, Allegheny County citizens, and Port Authority employees.

But the effects of Port Authority operations do not stop at Allegheny County's borders: Taxpayers from across the state have been providing most of the funds to operate the Port Authority for many years. For example, for the fiscal year ended June 30, 2005, the state contributed 55 percent toward the Port Authority's operating revenues of $309.2 million. At the same time, the Port Authority covered only 23 percent from fares and other revenues; Allegheny County government gave 10 percent; and the federal government contributed 12 percent. Yet as the largest contributor to Port Authority operations, the state made no specific appointees to the board.



Who pays to operate the Port Authority?

This chart uses data from the Federal Transit Administration for the fiscal year ended June 30, 2005.

For the fiscal year ended June 30, 2006, we determined that the Commonwealth's contribution was more than 59 percent ($183.5 million) of the operating revenues, and that the county's contribution had dropped to 7.9 percent ($24.6 million).[15]

1. A change in the governing structure is the most significant factor that will lead to permanent reform.

The fact that the Port Authority is not represented by the largest contributor to its operations becomes even more significant for two reasons:

- First, because a single official from Allegheny County appoints all nine Port Authority board members who make major decisions, such decisions might not reflect viewpoints as diverse and balanced as the viewpoints of members appointed by different sources.
- Second, there is a greater risk that a board appointed by a single local source will tend to exercise its powers in ways that miss the larger picture of the Port Authority's effect on—and accountability to—the state as a whole.

In short, the board's current appointment process does not result in a structure of checks and balances that are inherent in a more diverse structure of governance.

The importance of the governance structure cannot be overstated. It is the single most critical factor on which all future reform and oversight of the Port Authority are based. Because of this importance, the governing structure of the Port Authority must be changed to include permanent representation by the state on behalf of state taxpayers. This change must be made legislatively.

[15] We based these figures on our analysis of the Port Authority's June 30, 2006, financial statements and grant arrangements.

Changes in the board structure have not been made despite our calling for them in March 2007

In March 2007, we called on the Port Authority's board and management, as well as on the Pennsylvania Governor and various legislators, to change the Port Authority's structure of board appointments. Our recommendation was part of our interim reporting about the Port Authority's liberal use of funds to give excessive benefits, bonuses, and other considerations to Port Authority executives, other management and employees, and retirees.[16]

The March 2007 interim reporting was preceded by two other interim communications to the Port Authority management and board:

- On January 30, 2007, we reported about the Port Authority's unnecessary expenditure of $15.5 million to lease prime Pittsburgh office space for its executives and other staff while still owning an entire useable office building nearby for which the Port Authority had just spent $4.7 million in renovations and furnishings.

- On March 2, 2007, we reported how Port Authority management was benefiting from liberal and excessive benefits—particularly pension and retirement benefits that included, for example, the Deferred Retirement Option Plan—while, at the same time, there were operating deficits as well as a 30 percent shortfall in the management pension fund itself.

[16] On March 22, 2007, we wrote to the management of the Port Authority, with copies sent to the board of directors. Also copied were Pennsylvania's Governor, the President Pro Tempore of the Senate, the Speaker of the House, Allegheny County Senate and House members, Allegheny County Council members, and the Allegheny County Chief Executive. Our correspondence was developed in accordance with generally accepted government auditing standards that provide for interim reporting—that is, prior to completion of an audit report—when matters need immediate attention and correction. Earlier, on January 30 and March 2, 2007, we reported on other matters according to those same interim reporting standards; those other matters, which we will discuss later in this report, also provided evidence on which to base our finding about governance.

Following our interim reporting, the Port Authority did initiate changes in its operations, including giving up or scaling back some of the benefits for top management. Still, the Port Authority had already been severely damaged as the result of years of persistent excess. Not only did Port Authority management over the years fail to set an example of prudence or moderation, but the board also failed to change management's misguided direction. For example, if the Port Authority management received generous benefits, it was predictable that the unions representing the Port Authority would also receive some generous benefits, and vice versa.

The Allegheny County government provided little help in redirecting the Port Authority or in implementing checks and balances. This absence of oversight was allowed to go on for decades even though the county—in addition to appointing the board—contributed annually to the Port Authority's budget. It was not until 2007 that the county controller's office began an audit of the Port Authority. [17]

It is not clear why the county did not act sooner but, when combined with the disproportionate funding provided by the state, the county's inaction is all the more reason why the Port Authority must have state representation. **As long as state taxpayers are footing most of the bill, the state must be able to appoint representatives to the Port Authority's board.** Accountability to state taxpayers simply does not exist under the present arrangement.

2. The Auditor General is not alone in calling for a change in governance.

Others besides the Department of the Auditor General have called for a change in governance structure, including the Transportation Funding and Reform Commission, the

[17] Jim Ritchie, "County Controller to audit Port Authority," *Tribune-Review*, Pittsburgh, April 2, 2007.

Allegheny Institute for Public Policy, various legislators, and even the media. An analysis follows.

The Transportation Funding and Reform Commission has called for change. Created in February 2005 by executive order of the Governor, the Transportation Funding and Reform Commission was charged with conducting detailed studies and making recommendations about public transportation, highways, and bridges in Pennsylvania.[18] Regarding public transportation, the Commission conducted transit audits of seven transit agencies—including the Port Authority of Allegheny County—that represent more than 93 percent of the state's transit ridership. In all seven of those transit agency audits, the Commission found the following:

- There is an unbalanced relationship between state and local transit funding, governance, and decision-making.
- The vast majority of funding is provided by the state, but the vast majority of transit boards are wholly appointed by local officials.
- While the locally appointed boards make decisions that directly impact the level of state funding required to run the transit agencies, the boards' decisions may not match state policies, goals, or interests.

The Commission acknowledged that the state has historically taken a limited role in transit oversight despite its high level of financial contribution. However, the Commission also asserted that this minimal approach should be replaced with greater oversight by the state and

[18] The Commission's head, the current Secretary of the Department of Transportation, retired from the Port Authority in 1996 with 17 years of service. According to the Commonwealth of Pennsylvania's Web site at http://www.governor.state.pa.us/governor/cwp/view.asp?A=1112&Q=437818, the Secretary had served as the Port Authority's director of planning and business development and, later, as director of planning, engineering and construction.

greater accountability by local governments and the transit agencies themselves.[19]

The Commission's decision to call for change was likely also influenced by its analysis of the striking differences in the governance structure of peer transit agencies in other states. For example, in making specific comparisons of the Port Authority of Allegheny County with its peer transit agencies, the Commission found that other sampled agencies did not allow a single official to have the virtually unrestrained power to appoint every governing board member.[20] Following are some examples to show how the governance structure is set in comparable transit agencies elsewhere:

- In Denver, Colorado, <u>the public elects</u> a 15-member board of directors to the regional transit agency.
- In Minneapolis, Minnesota, <u>the Minnesota governor appoints</u> the 17 members to the region's largest transit operation, and <u>the Senate confirms</u> those members.
- In Cleveland, Ohio, <u>various designated officials appoint</u> (for example, mayors, council members, municipal managers, and county commissioners, according to jurisdiction) the 10 members to govern the transit authority.[21]

For the Port Authority of Allegheny County specifically, the Commission raised a serious "question of balance" based on the ability of a single elected official to direct all

---

[19] *Investing in Our Future: Addressing Pennsylvania's Transportation Funding Crisis,* Pennsylvania Transportation Funding and Reform Commission, Final Report, November 2006, Chapter Three – "Transit Operational Audits," pages 32-33.
[20] According to the Port Authority's enabling legislation, one of the appointed board members must be a member of county council. But the choice of *which* county council member is left to the appointing official, the county executive. <u>See</u> 55 P.S § 556.
[21] *Transit Agency Operational Audit [of the] Port Authority of Allegheny County*, Commonwealth of Pennsylvania, Transportation Funding and Reform Commission, Final Report, Technical Appendix, January 2007, "Governance" section, page 9.

board member appointments. The Commission asked how two structures of governance should best be balanced: a structure that benefits from policies and decisions made by board members all appointed by the same official [i.e., the existing structure] *versus* a [different] governing structure that benefits from "a robust diversity of views and opinions."[22] While the Commission did not answer its own question, the fact that the issue was raised so directly draws clear attention to the extreme imbalance that exists at the Port Authority now.

The Allegheny Institute for Public Policy has called for change. At the Allegheny Institute for Public Policy, change in the Port Authority's governance has been a recurring theme. In March 2007, for example, the Institute published a policy brief calling for governance reform and, as support for its position, cited the governance approaches of ten transit systems from across the United States.[23] <u>Of those transit agencies receiving a significant amount of revenues from the state, the Port Authority was the only one that had no state appointees on its board</u>. In July 2007, the Institute raised the issue again: "As long as the state is going to provide the bulk of operating funds for the Authority, there needs to be some oversight on behalf of state taxpayers."[24]

Legislators have called for change. With the passage of the state's 2007-08 budget that allots even more state taxpayer dollars to the Port Authority, various legislators have noted the absence of state representation on the Port Authority's board. As a result, legislation has been introduced in the General Assembly regarding this governance issue.

---

[22] *Transit Agency Operational Audit [of the] Port Authority of Allegheny County,* page 10.
[23] "Port Authority Governance Needs to be Reformed," *Policy Brief – An electronic publication of The Allegheny Institute for Public Policy*, March 1, 2007, Volume 7, Number 9.
[24] "Legislature Has Unfinished Port Authority Business," *Policy Brief – An electronic publication of The Allegheny Institute for Public Policy,* July 26, 2007, Volume 7, Number 39.

Summary of Finding One

In summary, the many problems that have existed for decades at the financially troubled Port Authority of Allegheny County are directly related to the appointment process of board members by one elected official. This extreme imbalance must be addressed so that accountability and leadership come from the largest funding source—which in this case is state government.

<u>Recommendation</u>

1. The Port Authority of Allegheny County, the Governor of Pennsylvania, and state legislators should agree to a legislative change to amend the Port Authority's governance structure as follows:

- The Governor should make two appointments to the Port Authority's nine-member board. Both appointees should be residents of Allegheny County.

- The General Assembly should also appoint two Allegheny County residents to the board, including one appointment by the President Pro Tempore of the Senate, and one by the Speaker of the House of Representatives. Both appointees should be residents of Allegheny County and should not hold elected office.

- The county's chief executive should continue to appoint the other five board members, including one who serves on the Allegheny County Council as currently mandated by law. Of the remaining four appointees, the county's chief executive should ensure that at least one represents downtown businesses and another represents riders with disabilities.

<u>Summary of the Port Authority's Response to Finding One</u>
followed by, *in italic type*,
<u>Department of the Auditor General's Evaluation of the Port Authority's Response</u>

In its response, the Port Authority notes that the process for appointing board members is not controlled by Port Authority board or staff but is instead determined by state law, specifically the Second Class County Port Authority Act.

➔ *Through state taxpayers, the Commonwealth of Pennsylvania is the major contributor to the Port Authority's operations—or, in effect, the "majority owner" of the Port Authority. Therefore, it is imperative for the Commonwealth to have seats on the board so that the state's interests are represented. We have already noted that a legislative change is required to change the Port Authority's governing structure. It is especially important, however, for Port Authority officials to be as vocal in lobbying for this change in governance as they are in lobbying the Commonwealth for even more financial assistance.*

Finding Two

The Port Authority was not accountable to taxpayers and, in fact, contributed to its own fiscal crisis by committing $15.5 million to rent prime downtown office space unnecessarily.

In 2000, the Port Authority decided to spend a minimum of $15.5 million over ten years for two floors of premium office space in downtown Pittsburgh. The new headquarters space is used by Port Authority executives and other staff and also by the board for its meetings.

This matter is significant for the following reasons:

1. **The Port Authority spent millions of dollars unnecessarily while a budget crisis was looming.** The Port Authority signed the ten-year lease for $7.8 million in 2000 and also paid $7.7 million to renovate and furnish the new space prior to moving in. At the time, although the Port Authority had balanced its budget, it was doing so with increasing difficulty based on unstable funding streams and rising costs (e.g., for fuel, utilities, and employee benefits). In fact, on April 1, 2001, about 6 months after the Port Authority completed its move downtown, it raised fares for the first time in 10 years.

2. **The Port Authority made riders pay more.** Contrary to the recommendation we made to Port Authority management during our audit work, the Port Authority did not terminate its expensive lease arrangements even though, by its own admission, senior management has been discussing a move out of the new space since March 2005. As of the date of this report, the Port Authority continues to pay the excessive and unnecessary rents while charging riders higher fares, making service cuts, and continuing to lobby for more money from the state.

3. **The Port Authority moved out of a useable headquarters that it already owns.** The Port Authority already owns a headquarters building on Beaver Avenue in nearby Manchester that was formerly used by much of the

staff, including the executive staff, and could be used by them again. In fact, the Port Authority spent $4.7 million to refurbish the Manchester building in 1997 just three years before signing the new lease downtown. The Port Authority has tried unsuccessfully for several years to sell or lease the Manchester building.

4. **The Port Authority is leasing more space than it uses.** Not only is the Port Authority failing to headquarter itself at the useable building it already owns on Beaver Avenue, but it also is paying for wasted space at the leased headquarters downtown. In February 2007, during our on-site audit work at the leased headquarters downtown, our audit team observed that approximately 2 out of every 10 work stations were vacant; the Port Authority's review in that same month put the number at 1 vacant work station out of every 4. Regardless, there were 230 employees who originally moved downtown in 2000, and there were at least 26 fewer employees in the downtown headquarters as of March 2007.[25] Also in March 2007, the Port Authority announced that further staff reductions would be made.

[25] March 30, 2007. Letter from Stephen G. Bland, Chief Executive Officer, Port Authority of Allegheny County, to Jack Wagner, Pennsylvania Auditor General.

Overall, the Port Authority has been paying for wasted space ever since its original move to downtown when it cited the need for more space.[26] Our own analysis, below, shows that the projected need was overstated.

Space available to Port Authority as of October 2000 compared to its own projected need of 77,720 square feet

Location	Square feet	Status in Oct. 2000
Manchester *entire building*	55,500	already owned
Heinz Center *third floor*	46,997	leased July 2000
Heinz Center *fifth floor*	23,578	leased October 2000

⇓

126,075
square feet was available
to meet need of 77,720 square feet

Auditors' Conclusion:

The total available space of 126,075 square feet was 38 percent more—or 48,355 more square feet—than the need projected by the Port Authority for its move downtown. Announced staff reductions in 2007 should mean that even less space is now necessary.

[26] In *History of the Port Authority* on the Port Authority's Web site, the move is reported as follows: "Citing the need for more space, Port Authority moved its corporate headquarters from its location in Manchester to the former Gimbels Building on Sixth Avenue in Downtown Pittsburgh in August 2000. The Manchester office then became headquarters to Port Authority's training and technology functions. The IT Division and the Training Department, which were previously spread out at several locations throughout Port Authority, moved to Manchester." The *History of the Port Authority* was accessed online throughout our audit work, most recently on August 7, 2007, at the following Web address: http://www.portauthority.org/PAAC/CompanyInfo/GeneralStatistics/History/tabid/55/Default.aspx.

The preceding four items were previously reported to the Port Authority

We previously reported the major components of this finding to the Port Authority on January 30, 2007, during the course of our audit work.[27] In a response dated March 30, 2007, the Port Authority said it was [still] evaluating the possible relocation back to the building in Manchester:

> *A complete cost assessment to rehabilitate and relocate back to the Manchester facility had been prepared by the engineering and construction division and was shared with the State Auditor General's office prior to publication of their preliminary finding. This assessment identified $4.43 million in costs to rehabilitate the facility and move the staff back to Manchester. Serious consideration is being given to the possibility of this move and has been part of senior management discussions and analysis since March 2005. Consideration is also being given to the costs to terminate the Heinz 57 Center lease or sublet the space, as well as other less costly alternatives to moving back to Manchester. It should be noted that a sudden move would result in the immediate loss of a portion of the $7.7 million in costs incurred in moving downtown without realizing the full benefit from these expenditures. Port Authority would also incur substantial current costs in fulfilling the remaining obligations under the terms of the lease. An additional cost consideration is potential reimbursement of*

[27] Standard 8.40 of *Government Auditing Standards,* 2003 revision, issued by the Comptroller General of the United States, says the following: "During the audit, the auditors should consider interim reporting of significant matters to appropriate entity officials. Such communication, which may be oral or written, is not a substitute for a final report, but it does alert officials to matters needing immediate attention and permits them to take corrective action before the final report is completed."

> *federal and state funding that was provided for capital improvements to move into the Heinz 57 Center. As of 2/28/07, the amounts of those reimbursements are calculated at over $5.1 million.*[28]

In February 2007, the Port Authority also noted it would be difficult to sublet its downtown space.[29] However, at least two Pittsburgh media outlets indicated within the prior year that one candidate might be a likely tenant. Specifically, the *Pittsburgh Business Times* reported in March 2006 that the H.J. Heinz Company already leased 270,000 square feet at the Heinz Center but "had run out of space" in that building and was looking elsewhere for more space.[30] Similarly, the *Tribune-Review* reported in June 2006 that the Heinz Company was looking for more space but that the existing vacant space at the Heinz Center was not enough to accommodate the company.[31]

On August 22, 2007, we spoke with the Port Authority's controller to ask whether the Port Authority had plans to renew the lease. At that time, the controller said he was not aware of any Port Authority actions to renew the lease, which terminates on June 30, 2010. The controller also noted that the Port Authority had recently completed the transfer of some of its key computer personnel from the owned building in Manchester to the leased space in the Heinz Center in order to make room to refurbish the Manchester building.

[28] March 30, 2007. Letter from Stephen G. Bland, Chief Executive Officer, Port Authority of Allegheny County, to Jack Wagner, Pennsylvania Auditor General.
[29] February 2, 2007. "Port Authority urged to move to less-expensive office space," by Joe Grata, *Pittsburgh Post-Gazette*. Mr. Grata quoted Port Authority spokesman Bob Grove, who spoke of paying for the remaining term of the Heinz Center lease "unless we could find someone to sublet to. Given the Downtown office vacancy rates, we're not sure that's very likely." This article was last accessed on August 6, 2007, online at http://www.post-gazette.com/pg/07033/758868-147.stm.
[30] March 3, 2006. "H.J. Heinz in talks to put logo on Dominion Tower, sources say," by Robert Sandler, *Pittsburgh Business Times*. This article was last accessed on August 2, 2007, online at http://pittsburgh.bizjournals.com/pittsburgh/stories/2006/03/06/story3.html.
[31] June 4, 2006. "Major companies consider downtown locations," by Ron DaParman, *Tribune-Review*, Pittsburgh. Accessed August 7, 2007, online at http://www.pittsburghlive.com/x/pittsburghtrib/business/realestate/s_456176.html.

Summary of Finding Two

The Port Authority showed poor judgment when, in 2000, it moved more than 200 employees, including executives, from the Manchester headquarters that it still owns to leased space in the Heinz Center downtown. The cost of a 10-year lease, plus renovations, and furnishings, will total a minimum of $15.5 million by the time the lease expires in 2010. Three years prior to its move, the Port Authority had already spent $4.7 million to renovate the Manchester headquarters. The reason cited for moving was a need for more space, but the move actually resulted in the Port Authority's having access to as much as 38 percent more space than it said it needed.

Recommendations

2. The Port Authority should under no circumstances renew or renegotiate a lease to remain at the Heinz Center.

3. The Port Authority should take action to sublet the space at the Heinz Center or terminate the lease, and should return to the former headquarters building in Manchester, which the Port Authority already owns.

Summary of the Port Authority's Response to Finding Two
followed by, *in italic type,*
Department of the Auditor General's Evaluation of the Port Authority's Response

In its response, the Port Authority says it is conducting a cost-benefit analysis related to rehabilitating the Manchester building, and also related to moving costs and future maintenance costs. The Port Authority's response also notes that the lease for the downtown Heinz Center expires in 2010 and that "immediate action to exit that lease would not be financially prudent, as Port Authority would still be responsible to fulfill its rental agreement."

➔ *The Port Authority's response fails to address our recommendation that under no circumstances should the lease for the Heinz Center be renewed or renegotiated when the lease expires. Nor does the response acknowledge that the Heinz Center lease continues to cost taxpayers and riders more than $900,000 a year for empty offices. Taxpayer dollars and rider fares should not be subject to such waste.*

Finding Three

The Port Authority gave excessive benefits to top executives, other staff, and retirees.

Whether using money from its operating budget or its separate pension funds, the Port Authority showed poor judgment by needlessly spending taxpayer dollars to award excessive benefits to top executives, other staff, and retirees.

This finding is made more significant by the fact that the Port Authority's actions occurred during—and just prior to—the present fiscal crisis. It is reasonable for taxpayers to expect that a taxpayer-funded organization entrusted with public resources should always work more for the public good and less for individual gain, and should do so with even greater sensitivity during times of financial belt-tightening. In this particular case, whether or not a fiscal crisis existed or was pending, the Port Authority was ill-advised to spend as it has done.

This finding is comprised of numerous sub-parts, most of which have already been communicated to the Port Authority through our interim reporting during the course of our audit work.

1. **The Port Authority used taxpayer dollars and riders' fares to give excessive benefits and other considerations to the former CEO.**

    - **The Port Authority "reimbursed" the former CEO $306,746—which is almost 70 percent more than he paid—to pave the way for his retirement at age 50 with a full pension.** The board of the Port Authority agreed to reimburse the former CEO for paying the Port Authority $181,530 to get credit for his 20 years and 10 months of prior employment there. Although buy-backs of prior employment are not necessarily unusual, the former CEO's buy-back was rare for two reasons:

- ⇨ First, while some government entities allow employees to use their own money to buy back prior years of military service, for example, and then apply those years toward their retirement, the Port Authority's policy allowed the former CEO to buy back <u>any</u> former public service and credit it toward his retirement. This rare and generous policy allowed the former CEO to retire at age 50 with full pension and retirement benefits.

- ⇨ Second, and even more significant, not only did the Port Authority permit the generous buy-back, but it also <u>gave</u> him the money to do so. Specifically, the Port Authority **reimbursed the former CEO 100 percent of the amount he paid** ($181,530), **plus almost 70 percent more** to cover interest that he missed by using his own money in the first place ($18,557) and also to cover his projected income taxes ($106,659) so that he would still net the entire $181,530 that he had originally paid. The total reimbursement to the former CEO amounted to $306,746.

- **The Port Authority paid the former CEO $270,000 in extra compensation beyond his salary.** In addition to his salary that began as $145,000 in 1997 and grew to $195,000 by 2005, the CEO also received $30,000 in deferred compensation or annuity payments for each of those nine years.

- **The Port Authority paid the former CEO $106,202 in total for giving up some of his already-generous vacation time.** Each year, the former CEO was given 6 weeks of vacation time, a generous benefit made even more lucrative because he treated it like a bonus. Specifically, not only did the former CEO get more vacation time than many other public servants, but he also got **cash back** each year for not using all that time. Accordingly, at his request, the Port Authority paid the former CEO the amounts shown in the next table.

Taxpayers paid when the former CEO decided to sell some of his 6 weeks of vacation time back to the Port Authority to get the cash instead.	
April 2000	$ 8,220
December 2000	12,115
November 2001	12,404
January 2003	12,404
February 2004	12,693
January 2005	12,981
September 2005	35,385
Total	**$106,202**

- **The Port Authority paid the former CEO $380,214 in one lump sum, plus an annual salary, for continuing to work after retiring early**. Under the administration of the former CEO, a Deferred Retirement Option Plan (known as D.R.O.P.) was begun that allowed the CEO and 43 other top managers to keep working after "retiring." Not only did the D.R.O.P. participants continue to earn their generous salaries, but they also became eligible to get a substantial lump sum when they actually left the Port Authority later. Although the D.R.O.P. program had been billed as a cost savings measure to help the solvency of the management pension fund, which had been underfunded since January 2001, it is not clear if or to what extent any such savings were achieved. On the other hand, the former CEO received a payment of $380,214 from the Port Authority's pension fund when he actually left the Port Authority in September 2005.

2. **The Port Authority used operating funds—provided by state, federal, and county tax dollars, and by riders' fares—to grant top executives disproportionate benefits and other considerations.**

   - **The Port Authority continued to follow a policy that awarded excessive vacation time to other top executives and then allowed them to sell some of it back every year and/or carry some of it forward.** These options are more liberal than the choices offered to most other non-union employees at the Port Authority, who could cash in unused vacation time only when they retired or resigned. In the past three years, the Port Authority paid $336,027 to top executives and other non-union employees for unused vacation time. The present CEO of the Port Authority collected $6,923 for selling back vacation time after being on the job for only six months. He received this money on December 31, 2006, around the same time that he announced potential service cuts and told the public that the Port Authority would have to live within its means. Also in 2006, there were 15 other executives who received lump sums totaling $118,494 for unused vacation time, ranging from a low of $1,033 to a high of $26,047. In 2005, 18 non-union employees (not including the former CEO) received $93,008; in 2004, 11 such employees (again, not including the former CEO) received $56,544.

   - **The Port Authority used a total of $80,000 from taxpayers and riders to fund relocation allowances for two executives.** The Port Authority provided relocation allowances to two employees upon their hiring, including the current CEO, who received $45,000 in June 2006 for a move from Albany, New York, to Pittsburgh. In addition, an operations officer received $35,000 in April 2005 when he relocated from Seattle, Washington. These amounts were paid in lump sums, with employment and withholding taxes then subtracted, at the time both employees started work.

We found no documentation of a relocation policy that spelled out why moving expenses would be paid, who would be entitled to receive them, or how any such amounts would be calculated. We also found no evidence that the Port Authority requested receipts or other itemized documentation of actual moving expenses. In short, these relocation allowances were treated more like bonuses than like moving expense reimbursements.

3. **The Port Authority offered its non-union employees and retirees a generous pension plan and other benefits at the expense of the taxpayers of Allegheny County and the Commonwealth of Pennsylvania.**

   - **Pension plan provisions allowed non-union employees to retire in their 40s with a full monthly pension.** Despite being underfunded, the non-represented pension plan continued to permit employees with only 25 years of service—regardless of age—to retire without any reduction in retirement benefits.[32] While we acknowledge that the Port Authority issued a new pension plan revision on January 1, 2007, and amended this provision to restrict retirement eligibility to age 55 and 25 years of service, the clause applies only to employees hired after December 1, 2005.[33] Furthermore, even those employees with 25 years of service can receive full pension benefits simply by working until age 55, which is 10 years younger than the plan's normal retirement age of 65.[34] Under the provisions governing current employees, a related actuarial valuation report indicated

[32] Port Authority of Allegheny County Retirement and Disability Allowance Plan for Employees Not Represented by a Union, as amended and restated effective as of January 24, 2003, and January 1, 2007, Section 8.3.
[33] Ibid. Section 8.2.
[34] Port Authority of Allegheny County Retirement and Disability Allowance Plan for Employees Not Represented by a Union, as amended and restated effective as of January 24, 2003, and January 1, 2007, Section 7.1.

that 26 plan participants—or 8.8 percent of the 308 plan participants—had 20 to 24 years of service, and that 26 of the 27 were under the age of 55.[35] These 26 employees are thus nearing retirement eligibility and will be qualifying for a lifetime pension benefit.

- **In 1998, the Port Authority reduced the time from 10 years to 5 years for employees not represented by a union to vest, while still requiring union employees to have 10 years of service to vest.** Prior to June 1, 1998, an employee was required to work ten years with the Port Authority before becoming eligible to vest in the pension plan. Effective June 1, 1998, the Port Authority reduced the vesting period for employees not represented by a union to five years via a plan amendment. According to the most recent actuarial valuation report,[36] ten employees have vested benefits and will collect them in the future in an amount projected to be $453,162. In addition, 215 of 308 active plan participants, or approximately 70 percent, have reached the five-year vesting level. If the provision had remained at ten years, the 215 vested members would have been reduced to 141 vested members, a difference of 74 members.

- **The Port Authority allowed its employees not represented by a union to reach their 25-year retirement mark by counting an unlimited number of years from jobs they held elsewhere.** This attractive buy-back provision, which is rare for public service employees in Pennsylvania, placed these employees in an elite status and, at the same time, contributed to the financial crisis. Port Authority employees who are members of the pension plan for employees not represented by a union can count their prior work years from virtually any public employer,

[35] Actuarial Valuation Report as of January 1, 2005, for the Plan Year Ending December 31, 2005, as compiled by Mercer Human Resource Consulting.
[36] Ibid.

including those in other states, to reach the 25-year retirement mark at the Port Authority.[37] This provision became effective on June 1, 1998. This practice goes well beyond the typical buy-back provisions that the Department of the Auditor General sees in its audits of thousands of pension plans reviewed each year by its Bureau of Municipal Pension Audits, most of which allow only buy-backs for military service. Although participants of the Port Authority's Amalgamated Transit Union (ATU) Local 85 Plan can also purchase service time, that time is limited only to 1.5 to 4 years of military service time. The Port Authority's International Brotherhood of Electrical Workers (IBEW) Local 29 Plan does not permit the buy-back of any service time.

- **The Port Authority allowed employees not represented by a union to accrue unlimited sick leave in a way that represents three generous gifts in one.** First, employees not represented by a union already enjoy having no limits on sick leave they accrue while employed. Second, the accrued Port Authority sick leave provides another extra because it can count toward the 25 years of service needed to reach full retirement.[38] Finally, if the employee chooses to use sick time toward the time requirement for reaching full retirement, then sick leave reduces the amount of buy-back time needed for Port Authority employees to qualify for pension benefits. Based on our review of the 44 D.R.O.P. members, 43 had at least one year of accrued sick leave credited to the service time and included in their pension calculation. Nineteen of the 44 D.R.O.P. members, including the former CEO, had less than the 25 years of service time needed to qualify for the plan; but, after including their accrued sick

[37] Port Authority of Allegheny County Retirement and Disability Allowance Plan for Employees Not Represented by a Union, as amended and restated effective as of January 24, 2003, and January 1, 2007, Section 6.
[38] Ibid. Section 2.8.

leave, these employees were able to meet the 25-year minimum.

- **The Port Authority paid for post-retirement healthcare benefits for retirees until qualification for Medicare benefits at age 65.** These benefits consist of medical, hospital, prescription, and dental and vision coverage, as well as Medicare Part B premium reimbursements.[39] The Port Authority has included provisions in the plan to require the retirees to pay a portion of the health care costs.[40] The Port Authority further amended the plan in 2006 to require retirees to pay a percentage of their pension toward the medical premiums.[41] Although this legacy benefit does not impact the underfunded pension fund, it does impact the Port Authority's seriously deficient operating fund. As of June 30, 2006, the Port Authority reported that the post-retirement benefits cost $25,827,092. The payment of these benefits reduces funds available that otherwise could be allocated towards ongoing Port Authority operations. Although the Port Authority has amended the plan to require retirees to contribute a percentage of their pension toward the health care premiums, continued availability of this coverage will remain a critical component of the Port Authority's legacy costs.

- **The Port Authority added an extra $500 to every monthly pension payment for all early retirees until they reach the age of 62.** This extra payment is yet another example of a benefit that is rare among pension plans, and it has cost the Port Authority's pension fund millions of dollars that should never have been expended. It is inexplicable that the Port Authority continues to tap into the already-decreasing pension

[39] Port Authority of Allegheny County Retirement and Disability Allowance Plan for Employees Not Represented by a Union, as amended and restated effective as of January 24, 2003, and January 1, 2007, Sections 12.2 and 12.3.
[40] Ibid. Section 12.8.
[41] Ibid.

fund by giving all retirees a supplement of $500 a month, or $6,000 a year, until they turn 62. The Port Authority's decision-making about this bonus tells a story of continued excess: (a) management awarded itself this supplement in 1993, starting at $300; (b) raised the supplement to $500 in 1998; and (c) made no move to stop awarding the bonus when the pension fund began to show a deficit in 2001. Considering that management already had more generous pension benefits than most public employees in general, this bonus plan never should have started in the first place. Of the 44 employees who elected to enroll in the D.R.O.P. retirement plan, 42 were under the age of 62 and received the additional $500 monthly Supplemental Benefit amount. This provision resulted in an increased potential payout amount of $2,491,500 from the Port Authority's pension fund until these identified retirees reach the age of 62. Included in this potential payout is $72,000 for the former CEO.

We previously reported the major components of this finding to the Port Authority in separate communications on March 2 and March 22, 2007. In a response dated March 30, 2007, the Port Authority proposed various changes to its non-represented employees' compensation and benefits package as cost savings initiatives.[42] The proposed changes communicated by the Port Authority are acknowledged in italics following our recommendations that begin on the next page.

Summary of Finding Three

The Port Authority gave excessive benefits to the former CEO, other top executives, non-union employees, and retirees. The

[42] The Port Authority included the same cost saving initiatives in a press release dated March 5, 2007. Refer to http://www.portauthority.org/PAAC/News/NewsRoom/PressReleases/tabid/278/mid/465/newsid465/214/Default.aspx. Accessed November 1, 2007.

management retirement benefits and other considerations were contrary to the Port Authority's charge to provide quality services at a reasonable cost. In short, the Port Authority's employee benefits have not reflected the necessary accountability to the taxpayers of Allegheny County and the Commonwealth of Pennsylvania. However, in a response to us dated March 30, 2007, the current CEO of the Port Authority communicated that changes were being implemented and that such changes would address various recommendations we have made. We acknowledge these proposed changes and report the Port Authority's proposals below as they were communicated to us. At the same time, we note that we will need to follow up with subsequent audit work to determine the actual changes made, as well as their extent and effect.

Recommendations

4. The Port Authority should take significant steps to address the ever-rising cost of health care for Port Authority management retirees, thereby reducing the demand on its already excessive operating expenses. *The Port Authority communicated to us on March 30, 2007, that it was addressing this recommendation. See the italicized bullets that follow these recommendations.*

5. The Port Authority should restore the pension vesting period to ten years for new management hires. *The Port Authority communicated to us on March 30, 2007, that it was addressing this recommendation. See the italicized bullets that follow these recommendations.*

6. The Port Authority should restrict the buy-back provisions in the pension plan for non-represented employees by allowing only purchases for prior military service. *The Port Authority communicated to us on March 30, 2007, that it was addressing this recommendation. See the italicized bullets that follow these recommendations.*

7. The Port Authority should amend the pension plan for employees not represented by a union to limit or eliminate the amount of sick leave that can be used to calculate the service years for pension benefits. *The Port Authority communicated to us on March 30, 2007, that it was addressing this recommendation. See the italicized bullets that follow these recommendations.*

8. The Port Authority should eliminate the $500 supplemental pension benefit. *The Port Authority communicated to us on March 30, 2007, that it was addressing this recommendation. See the italicized bullets that follow these recommendations.*

9. Port Authority management should review existing spending policies and practices and bring them more in line with prudent fiscal measures. For example, we recognize that the use of a moving allowance can be an effective recruiting tool. However, in order to present a position of fiscal restraint and financial responsibility, these expenses should be properly documented, and only reasonable expenses should be reimbursed. *Although the Port Authority's response of March 30, 2007, did address proposed changes in spending policies and practices, it did not address the moving allowances.*

Changes announced by the Port Authority in its response dated March 30, 2007 [43]

- *Those retiring after July 1, 2007 will no longer be eligible for post retirement healthcare. Such retirees will become eligible to receive a $500 per month stipend for up to five (5) years; but only during the period of retirement from age 60 to 65, or until Medicare eligible, whichever comes first. (This measure is an attempt to address the rising costs of healthcare which is a legacy cost that grows at a rate that*

[43] March 30, 2007. Letter from Stephen G. Bland, Chief Executive Officer, Port Authority of Allegheny County, to Jack Wagner, Pennsylvania Auditor General.

is 4.5 times the rate of inflation.) [Note from the Department of the Auditor General: This measure is related to our recommendation 4.]

- *Eliminate the $500 monthly supplement. The $500 supplement originated during the collective bargaining process with ATU local 85. It was provided to non-represented employees to remove any barriers from an employee transferring into a non-represented position.* [Note from the Department of the Auditor General: This measure is related to our recommendation 8.]

- *DROP participants may remain active employees for no more than five years, but no later than July 1, 2007. This in effect is a termination of the DROP plan as of July 1, 2007. The DROP plan was offered on a one-time basis in 2002 for the purpose of succession planning. The DROP was available to all non-represented plan members, including non-management employees, who were eligible to retire from the plan at that time. For pension purposes, those who elected the DROP were treated the same as if they had retired on the election date. That is, the pension benefit for each was frozen, and no increase was granted for additional service or compensation with the Port Authority. At the time this plan was implemented, it was estimated by the actuarial firm that the Port Authority's Non-Represented Employee Pension Plan could experience a modest cost savings for each employee who elected into the DROP plan rather than retiring from employment.* [Note from the Department of the Auditor General: In our March 2, 2007, interim report to the Port Authority, we communicated that the Port Authority should eliminate future special incentives such as the D.R.O.P.]

- *The following adjustments have been proposed to non-represented employees' healthcare benefits as follows: All Non-Represented Employees – Increase healthcare contribution to 2% of base salary, effective July 1, 2007 and to 3% of base salary, effective July 1, 2008.* [Note from the Department of the Auditor General: These adjustments are related to our recommendation 4.]

- *The vesting period for the non-represented employee pension plan will change from 5 years to 10 years. The cost savings from this change has been described by our actuaries as negligible. However, this change will now reflect the same vesting period that is present in the represented employees' pension plans.* [Note from the Department of the Auditor General: This measure is related to our recommendation 5.]

- *Eliminate the option to purchase prior public service; only military time will be eligible for such buy-backs. Currently, the years of service purchased back by the various employee groups is as follows: ATU 1309 years, 3 months; Non-represented 324 years, 9 months; IBEW 21 years, 5 months.* [Note from the Department of the Auditor General: This measure is related to our recommendation 6.]

- *Eliminate the crediting of unused sick leave toward continuous service for retirement.* [Note from the Department of the Auditor General: This measure is related to our recommendation 7.]

<u>Summary of the Port Authority's Updated Response to Finding Three</u>

followed by, *in italic type*,

<u>Department of the Auditor General's Evaluation of the Port Authority's Updated Response</u>

In its updated response dated November 30, 2007, the Port Authority states that Finding Three "addresses a topic over which the current Board has no control." The Port Authority's response also discusses its "broad series of cost-savings initiatives" announced as the result of our earlier interim report about these matters. The Port Authority's response emphasizes that—"due to current collective bargaining agreements"—

certain cost-saving actions do not pertain to union employees but only to management employees and the Port Authority Police. The cost-savings actions include, for example, increased healthcare contributions by employees, frozen senior management position salaries, elimination of lifetime healthcare for employees retiring after June 30, 2007, and elimination of the $500 monthly pension supplement.

➔ *The response by the Port Authority mirrors the concerns expressed to us orally by Port Authority management officials who expressed disappointment that our audit findings focused on management officials and not on union employees. We continue, however, to assert our position that management should lead by example, thereby setting prudent standards and helping to make union negotiations fiscally responsible.*

Finding Four

The Port Authority poorly planned or poorly implemented three of its most significant capital projects undertaken during the past ten years.

In recent years, the Port Authority either completed or embarked on at least three major public transportation projects under its $1 billion Major Capital Investment Program.[44] The three major projects discussed here include the following:

- The opening of the West Busway in September 2000 and the associated Wabash Tunnel in December 2004.
- The opening of the Stage II Light Rail Transit in June 2004 and the associated South Hills parking garage in May 2005.
- The start of construction for the North Shore Connector project in late 2006.

Although the federal government agreed to provide 60.5 to 80 percent of the funding for the three projects, the Port Authority either spent or planned to spend Commonwealth monies for the bulk of the remaining project costs. In fact, the original Full Funding Grant Agreements with the Federal Transit Administration, or FTA, estimated that the Commonwealth would contribute approximately $187 million in total for the three projects.

Despite the fact that the Port Authority benefited from the generous federal and state funding sources, it poorly planned or poorly implemented the three projects. The cause of this poor planning and/or poor implementation is not clear, but the effect is very clear: specifically, the Port Authority increased spending significantly from its own capital or operating budgets when it could not afford to do so. In addition, because it failed to anticipate and/or to control all project costs, the Port Authority also abandoned important design and service

[44] http://www.portauthority.org/PAAC/News/CapitalProjects/tabid/229/Default.aspx. Accessed on November 3, 2007.

components and reduced ridership estimates for the West Busway project. Finally, the Port Authority deferred important design components for the North Shore Connector project.

The narrative that follows includes a discussion of the projects just described.

West Busway/Wabash High-Occupancy-Vehicle Project

In October 1994, the Port Authority entered into what is known as a Full Funding Grant Agreement with the FTA to construct a busway from the Borough of Carnegie to downtown Pittsburgh. The agreement established an overall budget of $326.8 million, funded 80 percent with federal monies and 20 percent with Commonwealth monies. There was no local match from Allegheny County.

The October 1994 agreement anticipated that the project would be substantially completed and opened for operation on or before June 30, 1998. The original approved design included the following components:

- an interchange for buses with the Parkway West in Carnegie.

- an exclusive roadway for buses along a mostly abandoned railroad corridor from Carnegie to the Corliss section of the City of Pittsburgh and then alongside a Consolidated Rail Corporation (CONRAIL) freight line to Station Square. At Station Square, the roadway would connect to a new high-occupancy-vehicle bridge across the Monongahela River into downtown Pittsburgh.

- a reversible high-occupancy-vehicle facility through a refurbished Wabash Tunnel through Mount Washington that would also connect to the new high-occupancy-vehicle bridge into downtown Pittsburgh.

The Port Authority opened the West Busway in September 2000 and the Wabash Tunnel in December 2004. In November 2006, the Port Authority estimated that the final project costs would total approximately $275 million, or about $46.8 million under the revised budget.

Although the actual costs were less than the revised projections, the reduction in project costs was not proportionate to the greater reduction in project benefits. Specifically, due to the poor planning and the poor implementation, the project was completed late, was completed with reduced ridership estimates and—most significant of all—was completed without two important components: the Monongahela River Bridge and the CONRAIL shelf.

The details of this poor planning and poor implementation follow:

- **The Port Authority did not adequately plan for all contingencies to the West Busway/Wabash high-occupancy-vehicle (HOV) project.** Subsequent to the execution of the Full Funding Grant Agreement, the Port Authority increased the estimated overall cost of the original West Busway/Wabash HOV project to $515 million, or $188.2 million greater than the approved funding.

- **The Port Authority attributed the bulk of this cost increase to two project components: the new Monongahela River Bridge and the section of the busway along the CONRAIL line.** In April 1994, the Port Authority estimated construction costs for the CONRAIL shelf and the Monongahela River Bridge to be $34 million and $26 million, respectively. Additionally, the design, construction management, and project administration for these two components of the project were estimated to be $20 million.[45] The Port Authority

[45] Federal Transit Administration and Port Authority of Allegheny County, "Phase 1: Airport Busway/Wabash HOV Final Environmental Impact Statement," April 1994.

faulted the property acquisition and relocation costs of the Gateway Clipper Fleet (a tour boat operation), a lack of consensus on the alignment of the Monongahela River Bridge, and the increased costs associated with a second-track addition by CONRAIL as the reasons for the increased project costs.

- **When the Port Authority removed the Monongahela River Bridge and the section of the busway along the CONRAIL line from the project in 1997, instead of the project being reduced by $80 million, it was reduced by only $5 million.** Furthermore, removing both the Monongahela bridge and the CONRAIL line busway from the project eliminated a direct route form the Western suburbs into downtown Pittsburgh, thereby directly and negatively impacting service and projected ridership as well.[46] The overall budget for the project now totaled $321.8 million, largely unchanged from the original $326.8 million budget. In June 1997, the Port Authority submitted a recovery plan to the FTA with this change. According to the revised agreement, the busway would conclude at the Corliss section of the city. Buses would then travel along Carson Street and cross an existing bridge to downtown Pittsburgh. The Wabash Tunnel would also be refurbished and used as a reversible high-occupancy-vehicle lane with ramps to Carson Street.

- **Even though the Port Authority reduced the amount of construction effort needed by eliminating two parts of the project, it still extended the amount of time necessary to complete the project by at least three years.** The recovery plan extended the target operation date for the Parkway West to Carson Street portion of the project to December 31, 2001, and the target completion date of the

[46] The average daily ridership had been projected to increase by 16,500 by the year 2010, according to the Federal Transit Administration and Port Authority of Allegheny County's "Phase 1: Airport Busway/Wabash HOV Final Environmental Impact Statement," April 1994. However, the projection was lowered to 10,000 following the reduction in the project's scale, according to the Port Authority of Allegheny County's "Phase 1 Airport Busway/Wabash HOV Facility Final Environmental Assessment and Section 106 and 4(f) Evaluation," September 1998.

Wabash Tunnel to Carson Street portion of the project to December 31, 2002.

- **After plans to build the new Monongahela River Bridge were abandoned, the Port Authority still refurbished the underutilized Wabash Tunnel and significantly increased operating costs.** In September 1998, the Port Authority estimated that the elimination of the Monongahela River crossing would reduce anticipated peak-hour high-occupancy-vehicle (HOV) volumes through the Wabash Tunnel from 350 vehicles each hour to 200 vehicles each hour.[47] Nevertheless, the Port Authority continued the Wabash Tunnel refurbishment project. The original West Busway/Wabash HOV project included the use of the tunnel and a new Monongahela River Bridge to carry Port Authority buses and other high-occupancy vehicles. The revised agreement eliminated the Monongahela River Bridge and authorized a ramp from the Wabash Tunnel to Carson Street. In December 2004, the Port Authority completed the Wabash HOV facility at an estimated cost of $29.2 million.

- **It is unclear why the Port Authority continued to refurbish the Wabash Tunnel since Port Authority vehicles did not normally use this tunnel.** Since December 27, 2004, the tunnel has operated as a one-way reversible facility that accommodates vehicles with two or more passengers inbound during the morning peak hours and outbound during the evening peak hours. The tunnel has permitted unrestricted access outbound during weekends. Port Authority revenue vehicles have not used the Wabash Tunnel as part of daily operations. Port Authority buses have used the Wabash Tunnel only for detours and special operations.

- **Since December 2004, the Wabash Tunnel has been underutilized even by non-Port Authority vehicles.** The

[47] Port Authority of Allegheny County, "Phase 1 Airport Busway/ Wabash HOV Facility Final Environmental Assessment and Section 106 and 4(f) Evaluation," September 1998.

Port Authority's own traffic counts for the week from April 18 to 24, 2006, disclosed that an average of 498 vehicles traveled the tunnel on weekdays (when usage is restricted to high-occupancy vehicles) and that 961 vehicles traveled the tunnel during the weekend (when usage is not restricted to high-occupancy vehicles).

- **In January 2007, the Port Authority entered into a one-year contract to pay $575,000 from its operating budget for the maintenance and operation of the tunnel.** Prior to January 13, 2007, the Port Authority paid $780,000 annually for the daily operation and maintenance of the Wabash Tunnel with the capital funds provided by the Full Funding Grant Agreement.

- **If the Port Authority closes the Wabash Tunnel prior to the end of the tunnel's useful life, the FTA will seek reimbursement for a large share of the tunnel's remaining value.** At its meeting on October 27, 2006, the Port Authority's Board of Directors acknowledged concerns regarding the Wabash Tunnel's "low traffic, nonuse of revenue vehicles (buses), and cost impact to the operating budget."[48] The board directed Port Authority management to develop an exit strategy within two months. In a letter to the FTA dated October 31, 2006, the Port Authority proposed two alternatives: the transfer of ownership to the Pennsylvania Department of Transportation (PennDOT) or the closing of the facility. In early December 2006, the FTA responded that if the Port Authority closed the Wabash Tunnel prior to the end of the tunnel's useful life, the Port Authority must reimburse the FTA its proportionate share (80 percent) of the tunnel's remaining value. The FTA also indicated that it was not opposed to the exploration of alternative uses for the facility.

- **The Port Authority estimated that operating the facility outbound only would cost approximately $300,000**

[48] Source: Port Authority's October 31, 2006, letter to the Federal Transit Administration.

annually from the operating budget. On February 20, 2007, the Port Authority met with representatives of Allegheny County, PennDOT, and the Southwestern Pennsylvania Commission to discuss opportunities to reduce or eliminate Port Authority operating costs for the Wabash facility. Port Authority representatives agreed to develop a cost estimate for operating and maintaining the tunnel with Port Authority personnel, while PennDOT representatives agreed to investigate the potential for sharing operating costs for monitoring and incident response management. Allegheny County agreed to develop and implement additional signs to enhance public awareness and improve usage of the facility. As of the end of our on-site audit work in March 2007, the Port Authority had not conducted a follow-up meeting or adopted any measures to mitigate the Wabash Tunnel operating costs.

**Light Rail Transit
System, Stage II**

In January 2001, the Port Authority entered into a Full Funding Grant Agreement with the Federal Transit Administration to modernize the Port Authority's light rail transit system (LRT) for $386.5 million. According to the grant agreement, the federal government would provide $234 million (60.54 percent), the Commonwealth would furnish $48.7 million (12.60 percent), and Allegheny County would fund $9.8 million (2.54 percent). Additionally, the proceeds from bonds issued by the Port Authority would provide $94 million (24.32 percent).[49] The agreement specified that the modernized LRT must be operational by June 2, 2004.

The major components of the project included rebuilding the Overbrook Trolley Line and portions of the Library Line, as well as purchasing 28 new light rail vehicles. The project also entailed the expansion and modernization of the Port

[49] The Port Authority pays for the annual debt service for these bonds with funds from the Commonwealth's Public Transportation Assistance Fund (PTAF).

Authority's operations control center, the replacement of 9 stations, the construction of 1 new station, and the construction of 3 park-and-ride lots. One of the park-and-ride lots would encompass the South Hills Village parking garage.

According to the Full Funding Grant Agreement, the Stage II Light Rail Transit Project would add approximately 2,200 parking spaces via three new park-and-ride facilities. The 1,522 spaces associated with the first five floors of the South Hills Village parking garage plus the 430 spaces at the new Library park-and-ride facility and the 230 spaces at the new Washington Junction facility satisfied the grant agreement's requirements.

In April 2001, a few months after the Full Funding Grant Agreement was signed, consultants hired by the Port Authority counted a maximum of 1,234 vehicles parked at 1,441 available spaces at the Port Authority's outdoor lot at the South Hills rail station and at adjacent spaces leased from the South Hills Village Mall. In October 2001, the consultants projected that the Port Authority would require 1,940 spaces at the South Hills Village site by 2005 and 2,540 spaces by 2015 in order to accommodate anticipated LRT patrons.[50]

In its January 2007 monitoring report, the FTA indicated that the Port Authority had substantially completed the Stage II LRT Priority Project for an anticipated total of $386 million.[51] The Port Authority opened its Stage II LRT in June 2004 and the South Hills Village parking garage in May 2005.

Ultimately, the Port Authority unnecessarily built the two uppermost levels of the South Hills Village parking garage and spent $4 million in excess of the Full Funding Grant Agreement. There was far less usage of the South Hills Village garage than the Port Authority had anticipated, and the result was an increase in the Port Authority's operating deficit.

---

[50] GAEC, DE Leuw, Cather/URS Greiner/CDM, "Stage II Light Rail Transit Program: South Hills Village Park & Ride Program Costs and Patron Flow Analysis," October 19, 2001.

[51] Federal Transit Administration, "Project Management Oversight Program: Stage II LRT Priority Project," January 2007.

Following are details of errors in planning associated with this project:

- **The Port Authority's decision to add the two unnecessary stories to the garage was made based on what management officials believed was good planning because they could not have been able to add parking spaces to a five-story garage for a comparable cost in the future.** In 2003, the Port Authority solicited bids for the construction of a parking structure with five, six, or seven stories. According to management officials, the Port Authority decided to build a seven-story garage due to the economies of scale noted in the individual bids. The bids indicated that the addition of two floors increased the number of spaces by 691 and the overall cost by approximately $4 million.

- **The number of new parking spaces provided by the seven floors at the South Hills Village garage exceeded the Port Authority's commitment specified in the Full Funding Grant Agreement.** Nevertheless, the Port Authority built two extra garage floors. The Port Authority opened the South Hills Village parking garage in May 2005 at a cost of approximately $31.9 million. The Port Authority constructed the seven-story garage on the lower portion of its own outdoor lot that had previously provided 1,060 parking spaces. The construction increased the number of available Port Authority parking spaces at the South Hills Village site by 1,744 for a total of 2,804 spaces. As of March 2007, the seven-story garage consisted of 2,213 indoor spaces, while the remainder of the outdoor lot provided 591 spaces.

- **Since the seven-story parking structure furnished a greater number of spaces than the number required by the Full Funding Grant Agreement, the Port Authority could not use grant agreement funds to pay for the construction of the two uppermost floors.** Thus, the Port Authority spent $4 million in funds from its issuance of major capital bonds in order to build two extra garage floors. Although past practice was to pay the debt service for these capital bonds from the Commonwealth's Public Transportation Assistance Fund (PTAF), this funding source is nearly exhausted and may not be available over the entire useful life of the garage.

- **Since the South Hills Village garage opened in May 2005, patron usage has been significantly lower than anticipated.** According to garage personnel, the garage has been nearly 75 percent empty most days since its opening. In fact, the Port Authority has now closed the same two uppermost floors that it had originally opted to build. The Port Authority's occupancy records for the thirteen weeks from December 11, 2006, to March 9, 2007, disclosed that an average of 459 vehicles parked at the garage each weekday, while an average of 404 vehicles parked at the outdoor lot each weekday. Accordingly, total weekday usage of the South Hills Village site averaged 863 vehicles.[52] In other words, approximately 1,000 fewer vehicles parked at the site on weekdays during the thirteen weeks in 2006-07 than the total estimates cited by the Port Authority in 2001.

- **Moreover, during the 13 weeks in 2006-07 cited above, about 400 fewer vehicles parked at the South Hills Village site on weekdays than the total number of vehicles parked at the preexisting lots in April 2001.** While patrons park at the outdoor lot for free, the Port Authority charges a fee of $1 for garage patrons with a monthly pass and $2 for single-day garage usage.

- **The reduced occupancy of the garage occurred in part because Port Authority management changed the conditions for garage usage.** The 2001 garage usage projections were based on the assumption that garage parking would be free. Additionally, the Port Authority built free park-and-ride facilities in Library (430 spaces)

[52] Vehicle counts for the outdoor lot were provided as of 10 a.m. each weekday. As of December 12, 2006, the Port Authority's garage operator recorded vehicle counts for the entire day.

and Bethel Park (286 spaces). It is clear that, when the Port Authority projected the number of garage users, it did not adequately assess both the impact of free parking in the lot immediately adjacent to the South Hills Village garage and the effect of free parking elsewhere along the LRT system. Ultimately, decisions by the Port Authority undermined its own earlier estimates of parking garage usage.

- **Due to its low usage levels, the South Hills Village parking garage incurred a deficit of $163,470 from May 2005 (when it opened) to December 2006.** For that 20-month period, revenue totaled only $224,858, which consisted of $180,208 from general patron parking and $44,650 from a lease with the Bethel Park Giant Eagle grocery store for employee parking spaces. On the other hand, operating costs totaled $388,328, which included electricity costs of $112,658 and contracted costs of $275,670 for garage operation and management. The following table illustrates the South Hills Village garage revenues and expenses from May 2005 through December 2006:

South Hills Village Garage Revenues and Expenses

Revenue sources:	
General patron parking	$ 180,208
Giant Eagle leases	44,650
Total	224,858
Less expenses:	
Management contract	275,670
Electricity	112,658
Total	388,328
Operating deficit	**$(163,470)**

At the close of most of our on-site audit work in March 2007, Port Authority management officials indicated they were actively seeking developers for the land adjacent to the South

Hills Village parking garage where the 591 free spaces are located. By leasing this land, management hoped to earn revenue for the Port Authority and induce customers now using the free lot to use the garage instead.

Subsequent Event:

In a press release dated September 28, 2007, the Port Authority announced that its board of directors approved a long-term lease of the upper park-and-ride lot to an outside developer at a rate of $131,500 annually for 99 years.[53]

North Shore Connector Project[54]

In the late 1990s, the City of Pittsburgh developed a plan to revitalize its downtown area. In 1997, the City and the Southwestern Pennsylvania Commission conducted studies of a rapid transit link between downtown Pittsburgh and the rapidly developing North Shore. In 1999, the Port Authority assumed responsibility for the project when it began the North Shore Connector Draft Environmental Impact Statement.

The Port Authority's original North Shore Connector design included two extensions of its existing 25-mile LRT system as follows:

(1) a 1.2-mile extension from the Gateway Subway Station in Downtown Pittsburgh to the Carnegie Science Center in the North Shore via twin bored tunnels under the Allegheny River.

[53] "Press Releases," Port Authority of Allegheny County Web site. Accessed November 6, 2007, at http://www.portauthority.org/PAAC/News/NewsRoom/PressReleases/tabid/278/mid/465/newsid465/373/Default.aspx.

[54] Significant public controversy has existed with regard to the Port Authority's choice to tunnel under the Allegheny River versus choosing other alternative designs to extend mass transit to the North Side of Pittsburgh. This report does not evaluate the political and governmental decision-making process associated with either the final choice or its alternatives.

(2) a 0.3-mile underground extension from the Steel Plaza Subway Station in Downtown Pittsburgh to the new David L. Lawrence Convention Center in the northeast end of the central business district.

The project initially involved the construction of two new stations on the North Shore and a new station at the Convention Center, the replacement of the station at Gateway Center, and the acquisition of four new light rail transit vehicles. In April 2005, the Port Authority estimated that the original project would cost $393 million.

Ultimately, the Port Authority prepared unrealistic cost estimates and, consequently, deferred important design components of the North Shore Connector project and reduced the projections of ridership.

Details of the poor planning and poor implementation of this project follow:

- **The Port Authority reviewed its April 2005 cost estimates and discovered that the original cost estimates were wrong**. In mid-2005, the FTA directed the Port Authority to solicit bids for the construction of the twin tunnels under the Allegheny River. Three firms responded. The lowest of the three bids was **<u>24 percent higher</u>** than the engineer's previous estimate. As a result, the Port Authority reviewed the entire project cost and determined that it was no longer possible to build the originally proposed North Shore Connector for $393 million. According to the North Shore Connector environmental report prepared by the Port Authority and the FTA in December 2005, the following factors contributed to the increased project cost: "a greater than forecasted inflation rate, skyrocketing increases in the cost of concrete, steel and fuel, and overall cost escalation due to project delay."[55]

[55] Federal Transit Administration and Port Authority of Allegheny County, "North Shore Connector Environmental Report on Proposed Project Revision," December 2005.

- **In December 2005, the Port Authority proposed that it defer the design and construction of the Convention Center line and station, as well as the acquisition of four new light rail vehicles; this revision reduced the anticipated average weekday ridership from 15,800 to 14,300 in the year 2025.** In April 2005, Port Authority management had estimated the total cost of the deferment to be approximately $85 million, which included about $72 million for the Convention Center line and station and approximately $13 million for the new light rail vehicles. The proposed deferment should have brought the project cost down to $308 million.

- Although the Port Authority deferred three elements of the North Shore Connector's original design and reduced the ridership estimates, the October 2006 Full Funding Grant Agreement significantly increased the overall project budget by $127 million. The revised overall budget totaled $435 million, which represents an increase of $127 million, or 41 percent, over the $308 million originally estimated for the remaining components of the initial North Shore Connector project. According to the grant agreement, the federal government would provide $348 million (80 percent), the Commonwealth would furnish $72.5 million (16.67 percent), and Allegheny County would fund $14.5 million (3.33 percent). Project construction began in late 2006. The agreement anticipated that the revised project would be open to operation on or before June 30, 2011.

Summary of Finding Four

The Port Authority ineffectively planned, budgeted, and/or implemented three of its most prominent capital projects undertaken during the last decade. The Port Authority eliminated two crucial design components of the West Busway/Wabash HOV project and reduced ridership estimates by 6,500 riders for an average weekday. The Port Authority significantly increased operating costs for the Wabash Tunnel by $575,000 per year, even though it does not use the tunnel for Port Authority vehicles; it also overestimated the use of the tunnel by non-Port Authority vehicles. The Port Authority unnecessarily built two levels of the South Hills parking garage, incurring $4 million additional debt and ultimately increasing its operating deficit by $163,470 for the 20 months ended December 31, 2006. Finally, the Port Authority eliminated the design and construction of the Convention Center line and station for the North Shore Connector project, thereby also eliminating a vital connection to the new David L. Lawrence Convention Center. The savings affiliated with this elimination have subsidized the dramatically rising costs to tunnel under the river and, at the same time, have camouflaged the actual amount of those rising costs.

Recommendations

10. The Port Authority must significantly improve any requests for capital project approval and funding from the state and federal government. Specifically, the Port Authority must be more precise in the preparation of the plan design, estimate of costs, projections of riders, and identification of all contingencies and ramifications prior to submission of requests to ensure that realistic designs, costs, benefits, and timelines are employed.

11. The Port Authority should immediately and thoroughly evaluate alternative solutions to the underutilization and excessive operating costs of the Wabash Tunnel. The analysis should consider the following options: (a) completing the project as originally designed, (b) exploring public/private partnerships to operate the tunnel and thereby reduce the cost to the Port Authority, (c) using the tunnel for Port Authority buses where practical, and (d) exploring permanent one-directional use of the tunnel. Management should then promptly take the appropriate steps to implement its identified solution.

12. The Port Authority should not exceed the stipulations of its Full Funding Grant Agreements for future capital projects.

At the same time, the Port Authority should take into account the impact of incurring additional debt on operating funds, particularly at a time when the Port Authority is operating at a deficit.

13. The Port Authority should carefully plan and budget the remainder of the North Shore Connector project to ensure the timely completion of all fundamental project components without additional cost overruns.

<u>Summary of the Port Authority's Response to Finding Four</u>

followed by, *in italic type*,

<u>Department of the Auditor General's Evaluation of the Port Authority's Response</u>

The Port Authority's response states that the Port Authority "follows all aspects of the federally-prescribed planning process for capital projects." The response also notes that the Port Authority will take over operation and maintenance of the Wabash Tunnel beginning January 1, 2008, and that it has been looking for ways to increase usage. Finally, the Port Authority notes that it is continuing to promote use of the South Hills Village garage.

➔ *Although the Port Authority's response discusses compliance with the federally prescribed planning process, our finding and recommendations instead addressed the <u>quality</u> of the plans and the related decisions that resulted in a severe understatement of project costs and inaccurate estimates related to ridership and usage.*

We also note that the Port Authority's response fails to mention and/or acknowledge the significant cost overruns for the North Shore Connector project, which is still in progress and has an estimated completion date of 2011.

Finding Five

The Port Authority has increased its revenue from the sale of advertising space since the sale of advertising was taken over by Port Authority staff.

A major component of other revenue sources at the Port Authority has been the money generated from selling advertising space on Port Authority vehicles, particularly the bus fleet. Prior to 2004, the Port Authority used an outside advertising agency to sell ads on the bus fleet vehicles. But the advertising agency's sales performance began to level off, and the Port Authority was unable to reach an equitable agreement with the advertising agency to continue its work. Therefore, the Port Authority dropped the agency and established an in-house advertising sales staff.

In its first fiscal year of operating an internal advertising department, the Port Authority's advertising revenue was $677,082. In the fiscal year ended June 30, 2005, however, with the use of advertising commissions totaling $14,826 paid to the staff as an incentive, the Port Authority increased its advertising revenue by $277,106, or 41 percent, to $954,188.

By March 15, 2007, the advertising revenue had reached more than $2.4 million and, in fact, surpassed the amounts raised when the advertising function was performed externally. As a result of these positive developments, we are not recommending any changes at this time.

<u>Summary of the Port Authority's Response to Finding Five</u>
followed by*, in italic type,*
<u>Department of the Auditor General's Evaluation of the Port Authority's Response</u>

The Port Authority acknowledges this positive finding but, at the same time, notes that the Port Authority "cannot realistically expect to attract large, single advertising contracts each year."

➔ *We acknowledge the Port Authority's realistic notation that increases in advertising revenues may not be so dramatic each year.*

Status of Findings from Prior Audit

As reported in the Objectives and Methodology section of this report, the Department of the Auditor General conducted a prior performance audit of the Port Authority of Allegheny County. The audit covered the period from July 1, 2000, through September 30, 2002, and the report was released in July 2003.

Objectives and findings of the prior audit; status of findings during the current audit period.

The prior audit consisted of five objectives, which we list below with a summary of the accompanying findings and a status for the current audit period:

1. **Prior objective**:
   Determine whether the Port Authority complies with Federal Transit Administration (FTA) and Port Authority policies and procedures established to safeguard fixed assets.

   Prior related finding:
   The Port Authority's control over its equipment inventory was deficient. The 2001 biennial inventory of equipment conducted by the Port Authority from August 2001 to November 2001 disclosed that the Port Authority could not physically locate 466 computer equipment items valued at greater than $875,000. As of September 2002, Port Authority personnel had not filed any disposal, transfer, or missing item reports for those items.

   The Port Authority also did not document the acquisition costs for 112 of the 414 computer equipment items on its August 2002 central inventory list. Testing of 36 of the 414 items revealed that 12 could not be located and 3 items were found at locations other than those recorded on the computerized inventory listing.

Status of this prior finding:
Our current audit found that the Port Authority did not implement the prior report's recommendation to enforce its policies and procedures regarding fixed assets. In the prior audit, we had recommended that Port Authority personnel accurately record the acquisition, transfer, retirement, and disposal of all equipment. We also recommended that Port Authority personnel report missing equipment to the Transit Police. During the current audit, our audit team originally tested 40 assets listed on the master computer inventory log and could not locate 6 items. We therefore conducted an additional review and determined that four of the six items were retired but not removed from the listing. The audit team's review of the computer asset records maintained by 15 of the 50 asset custodians found that 3 asset custodians could not provide records. A comparison of the remaining 12 asset listings to the master inventory log noted discrepancies involving 201 of the 554 listed assets.

We have concluded that this prior finding was not resolved.

Response by the Port Authority to this Status Update

followed by, *in italics*,

Department of the Auditor General's Evaluation of the Port Authority's Response

The Port Authority's response notes that it has now addressed this prior finding by establishing specific new policies and procedures.

➔ *We acknowledge the response by the Port Authority that it has recently implemented effective controls over its computer inventory and will verify these efforts during our next audit.*

---

2. Prior objective:
Determine whether Port Authority employees follow the policies and procedures for non-revenue vehicles and assess the adequacy of relevant management controls.

Prior related findings:
The prior audit reported that the Port Authority did not maintain adequate control over its non-revenue vehicles. Employees who used non-revenue vehicles did not always prepare the required vehicle use documents, while the documents that were prepared often contained inaccuracies. Division directors did not take action to correct missing or inaccurate mileage logs. Moreover, the assignment of one non-revenue vehicle for use on a 24-hour per day basis was not supported by the written justification of the division director. Finally, the Payroll Department did not adjust the wages of two of the sampled Port Authority employees who had used non-revenue vehicles for commuting purposes.

Status of these prior findings:
The current audit found that the Port Authority complied with the recommendations of the prior report. The Port Authority revised its non-revenue vehicle policy in May 2003, as well as implemented and most recently revised an automated vehicle mileage tracking system in November 2002 and September 2006, respectively. Since May 2003, the Port Authority assigned quality assurance personnel to each division to ensure the consistent and accurate submission of use logs for each non-revenue vehicle.

Our analysis of use logs for 31 of 292 non-revenue vehicles from July 2005 through June 2006 found that Port Authority personnel accurately and completely reported mileage data for all 31 vehicles for each of the twelve reviewed months. Additionally, the department head, division director, and chief executive officer approved written justifications for all 17 vehicles assigned to employees on a 24-hour basis as of October 1, 2006.

The Payroll Department adjusted the wages for the 50 Port Authority employees who used non-revenue vehicles for commuting purposes from July 1, 2005, through June 30, 2006. Finally, the Port Authority's Internal Audit Department conducted reviews of the non-revenue vehicle fleet for the 2003, 2004, and 2005 calendar years.

3. Prior Objective:
Determine whether the Port Authority purchases goods and services in compliance with federal and state laws and with its own policies.

Prior related finding:
The Port Authority complied with procurement laws, regulations and policies.

4. Prior Objective:
Assess the Port Authority's progress in developing an effective work order system for bus maintenance.

Prior related finding:
Prior audits disclosed that the Port Authority had not developed a comprehensive centralized work order system for bus maintenance that tracks employee output, material usage, and productivity. On December 18, 2000, the Port Authority awarded a $3.9 million contract for the implementation, training, and maintenance of an automated work order system. The Port Authority suspended work under this agreement on February 9, 2001, and ultimately terminated the contract effective April 22, 2001. We concluded that the Port Authority failed to document research and

properly plan the work order system project, resulting in unnecessary expenditures of approximately $561,000. The Port Authority paid the contractor a settlement fee of $250,000, and staffing costs for preparation and preliminary implementation of the contract were about $311,000.

Status of this prior finding:
The current audit disclosed that the Port Authority has developed and implemented a work order system for the maintenance of its rail, bus and non-revenue vehicles. The 40 sampled work orders documented priority levels, maintenance work descriptions, request dates, completion dates, the employees that performed the tasks, labor hours, any applicable overtime hours, and supervisory approvals. Additionally, the system maintained accessible work histories for all Port Authority vehicles. Interviews of maintenance personnel indicated that the current work order system has improved the efficiency of vehicle maintenance operations. Accordingly, we concluded that the Port Authority has complied with the prior recommendations to develop and implement a work order system.

5. Prior objective:
Assess managerial controls over bus maintenance overtime.

Prior related finding:
The prior audit reported that the Port Authority had not established adequate management controls over bus maintenance overtime. The eight maintenance facilities did not consistently document overtime approval and justification or report monthly overtime totals and budget variances. Furthermore, the Port Authority had not developed a work order system that identified overtime associated with specific maintenance projects.

Status of this prior finding:
The current audit found that the Port Authority complied with the prior report's recommendation to establish management controls over bus maintenance overtime. The Port Authority's bus maintenance overtime expenditures decreased from $3.7 million for the fiscal year ended June 30, 2003, to $3.0 million for the fiscal year ended June 30, 2006.

The Port Authority established controls over bus maintenance overtime through both its budgeting process and payroll system. The Port Authority required directors and managers to review and justify budget variances, including overtime, with the Chief Operations Officer monthly and with the Chief Financial Officer and Chief Executive Officer quarterly. At the time of these reviews, management adjusted budgeted overtime as necessary. The payroll system provided additional controls, because supervisors electronically "signed off" on the overtime entered into the system. Additionally, the Port Authority established and implemented a work order system that became fully integrated in all its maintenance shops as of December 31, 2005. This system allowed the Port Authority to anticipate the overtime to be incurred by maintenance projects. Although the Port Authority had not developed a comprehensive written overtime policy as of March 2007, it did establish management controls over bus maintenance overtime.

Appendix A Ridership Statistics: Port Authority of Allegheny County

Port Authority of Allegheny County
ridership statistics for fiscal years June 30, 2003,
through June 30, 2006[56]

Transit Service	2003	2004	2005	2006	Change
Bus, Light Rail & Incline	52,412,18	50,642,195	51,721,037	53,048,033	1.2%
Contract Services	6,708,539	6,778,941	6,894,646	7,146,929	6.5%
Senior Citizens	6,720,460	6,433,264	6,424,107	6,128,850	(8.8)%
ACCESS	1,852,149	1,822,580	1,772,956	1,757,959	(5.1)%
Free Ridership	2,083,336	1,842,598	1,845,262	1,830,371	(12.1)%
Total	69,776,665	67,519,578	68,658,008	69,912,142	0.2%

[56] Source: Passenger data obtained from the Port Authority Financial Statements dated June 30, 2003, through June 30, 2006.

Appendix B Operating Revenues and Expenses

Table B-1
Operating Revenue Sources[57]

	2002	Percent	2003	Percent
Fare Revenue	$64,252,645	24.1%	$ 69,380,506	25.3%
Other Revenue	3,199,705	1.2	3,175,546	1.2%
Subsidies:				
Federal	27,079,804	10.2	32,809,554	12.0%
State	145,954,768	54.7	143,331,383	52.2%
County	26,178,148	9.8	25,856,803	9.4%
Total	$266,665,070	100.0%	$274,553,792	100.0%

Table B-2
Operating Revenue Sources[58]

	2004	Percent	2005	Percent
Fare Revenue	$ 70,192,384	24.3%	$69,242,026	22.4%
Other Revenue	1,629,125	0.6	2,741,375	0.9
Subsidies:				
Federal	38,259,051	13.2	38,338,390	12.4
State	151,488,782	52.4	169,391,759	54.8
County	27,439,826	9.5	29,522,239	9.5
Total	$289,009,168	100.0%	$309,235,789	100.0%

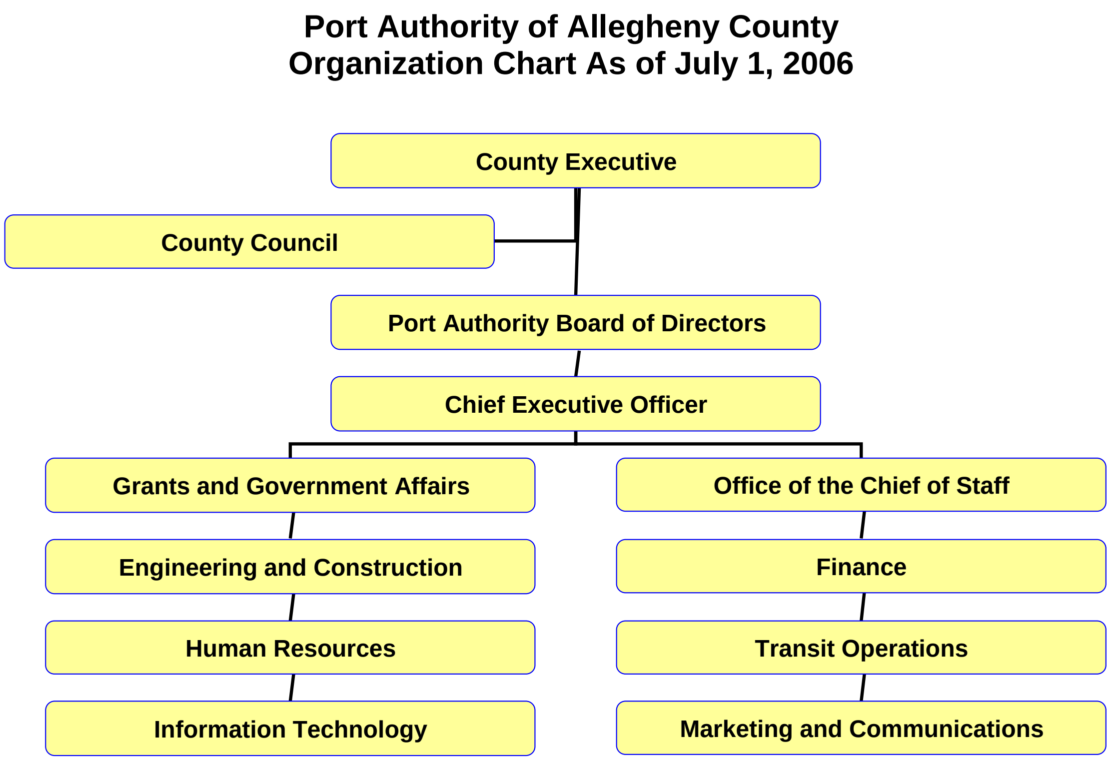
[57] Source: National Transit Database, Federal Transit Administration. http://www.ntdprogram.gov 3/5/2007. The Web site did not include 2006 data.
[58] Ibid.

Table B-3
Operating Expenses[59]

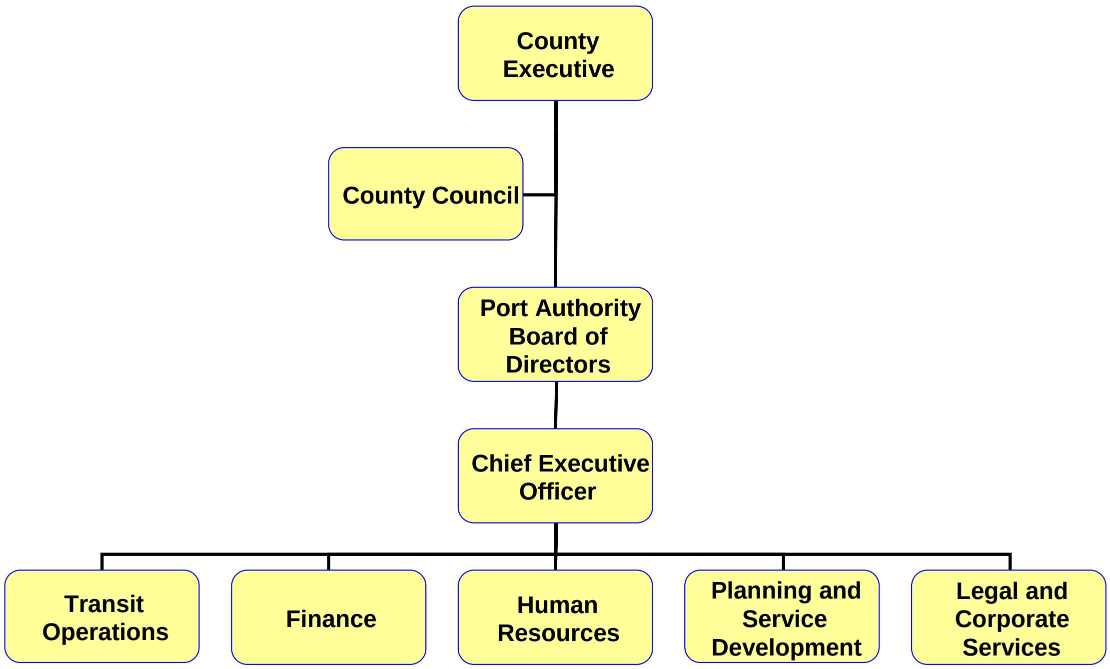
	2002	2003	2004	2005
Operators' Wages	$ 64,622,834	$ 61,951,246	$ 65,384,871	$ 65,051,998
Other Salaries & Wages	71,365,074	69,629,849	72,387,988	73,050,463
Fringe Benefits	67,885,385	67,642,157	71,633,756	84,589,342
Services	5,649,830	7,297,344	6,395,828	8,441,214
Materials and Supplies				
Fuel and Lube	9,775,144	7,979,523	9,527,229	14,124,518
Tires and Other	18,561,660	17,145,618	16,917,764	15,760,759
Utilities	6,604,259	5,934,401	6,055,653	6,911,699
Casualty and Liability	1,605,131	(278,334)	1,899,962	2,896,081
Purchased Transportation				
In Report	452,683	422,613	451,033	460,880
Filing Separate Report	29,602,045	29,105,920	29,738,548	30,437,275
Other Expenses	2,417,745	5,749,889	4,981,999	3,185,476
Expense Transfers	(7,608,230)	0	0	0
Total	$270,933,560	$272,580,226	$285,374,631	$304,909,705

[59] Source: National Transit Database, Federal Transit Administration. http://www.ntdprogram.gov 3/5/2007. The Web site did not include 2006 data.

Appendix C Port Authority Organization Charts



Port Authority of Allegheny County
Organization Chart As of July 1, 2007



Response from the Port Authority of Allegheny County

Port Authority
connecting people to life

November 30, 2007

The Honorable Jack Wagner
Auditor General
Commonwealth of Pennsylvania
229 Finance Building
Harrisburg, PA 17120

Dear Mr. Wagner:

The purpose of this letter is to document our response to the findings noted in your Performance Audit of the Port Authority of Allegheny County for the period July 1, 2002 to August 22, 2007, report dated November 2007. Findings two and three were previously addressed in our responses to you interim findings letters but will be updated in this letter.

Finding One: "The governing body of the financially troubled Port Authority of Allegheny County has included local but no state appointees even though state taxpayers provide the most money to keep the Port Authority operating."

Management Response:

> The appointment of Port Authority Board Members is outside of the authority and control of the Board and staff. The process for appointing members of the Board of Directors is determined by state law (Second Class County Port Authority Act).

Finding Two: "The Port Authority was not accountable to taxpayers and, in fact, contributed to its own financial crisis by committing $15.5 million to rent prime downtown office space unnecessarily."

Management Response:

> Port Authority staff is conducting a cost-benefit analysis that includes the estimated cost of the rehabilitation of the Manchester building, as well as the moving costs and future maintenance costs. Our lease at the Heinz 57 Center

expires in 2010, and immediate action to exit that lease would not be financially prudent, as Port Authority would still be responsible to fulfill its rental agreement.

Finding three: "The Port Authority gave excessive benefits to top executives, other staff, and retirees."

Management Response:

This addresses a topic over which the current Board has no control. Prior to the first audit report issued by State Auditor General Wagner earlier this year, Port Authority announced it was instituting a broad series of cost-savings initiatives to address the Pennsylvania Transportation Funding and Reform Commission's call for business reforms at the state's transit agencies. Due to current collective bargaining agreements, the following actions only affect management employees and the Port Authority Police:

- Accelerated the departure of employees in a Deferred Retirement Option Program
- Eliminated "lifetime healthcare" for those retiring after June 30, 2007
- changed the "buy-back" of previous employment time to only military years of service and instituted 10-year vesting period
- Eliminated a $500 monthly pension supplement
- Increased employees' healthcare contributions to 2 percent of annual salary in Fiscal Year 2008 and 3 percent in FY 2009
- Fiscal Year 2008 salaries frozen
- The CEO's salary frozen through June 2009 (amounting to a three-year freeze) and elimination of his deferred compensation contribution by the Authority
- All senior management position salaries frozen through June 2008 (amounting to a two-year freeze) and elimination of their deferred compensation contribution by the Authority
- Eliminated use of accrued of sick leave toward pension service
- Reduced the number of senior managers from eight to five

Port Authority also eliminated 370 budgeted positions, including 50 administrative positions, and instituted 203 layoffs by June 30, 2007.

The Authority will realize more than $11 million in savings in Fiscal Year 2008 alone as a result of the wage freezes, layoffs and changes to employee pensions and benefits.

We assume that the recommendation on Page 33 refers to healthcare costs for represented employees, which can only be addressed through collective bargaining.

Port Authority is prohibited by state law from changing the benefits given to current retirees.

Port Authority management and Board continue to address financial issues over which they have control. For instance, CEO Steve Bland eliminated use of a personal vehicle assigned to him; voluntarily took a three-year wage freeze; eliminated his deferred compensation; and reduced his vacation time.

Finding Four: "The Port Authority poorly planned or poorly implemented three of its most significant capital projects undertaken during the past ten years."

Management Response:

Port Authority follows all aspects of the federally-prescribed planning process for capital projects, which includes extensive public input, federal oversight and years of study, planning, design and engineering. (See attached chart)

Port Authority announced at its November 16, 2007 Operations and Consumer Relations Committee meeting that it will be taking over operation and maintenance of the Wabash Tunnel beginning January 1, 2008. We continue to look for ways to increase usage of the facility.

Port Authority continues to promote use of the South Hills Village garage. For example, the Port Authority is promoting use of the garage, as the free upper lot directly adjacent to the garage will close on December 1 – eliminating free parking for about 600 customers. In addition, the Authority previously entered into a revenue-generating lease agreement with Giant Eagle for 250 spaces.

Finding five: The Port Authority has increased its revenue from the sale of advertising space since the sale of advertising was taken over by Port Authority staff."

Management Response:

The increased advertising revenues are part of our continuing efforts to generate new revenues. While we continue to work to meet or exceed recent revenue levels, it should be noted that Port Authority cannot realistically expect to attract large, single advertising contracts each year.

Prior Audit Finding One: The Port Authority's control over its equipment inventory was deficient.

Management Response:

The Port Authority has addressed this prior audit finding with the establishment of specific policies and procedures. There has been ongoing training of fixed asset custodians and better communication between the fixed asset accountant and the fixed asset custodians. For most of fixed assets inventory, all of the problems have been corrected. The State Auditor General's report focuses on a specific subset of fixed assets, the computer inventory. The Port Authority acknowledges that there were lapses in the execution of the asset policy and procedures as it relates to computers. There have been a significant number of personnel changes in the IT group. Many of the former custodians and management of IT have left the Port Authority.

As a result of the reorganization of the Port Authority that occurred on July 1, 2007, IT personnel now report to the Chief Financial Officer. The policies and procedures that were designed to establish accountability and control for computer equipment will be enforced more rigorously as these custodians are now under the direction of the CFO and are part of the finance department.

We appreciate the inclusion of some positive findings in the report by the State Auditor General as noted below in our resolution of prior audit findings. We will monitor these items and make sure that we continue to remain in compliance.

Port Authority complied with procurement laws, regulations and policies.
Port Authority complied with recommendations of the prior audit regarding control over its non-revenue vehicles.
Port Authority complied with prior recommendations to develop and implement a work order system.
Port Authority established controls over bus maintenance overtime through both its budgeting process and payroll system.

If you have any questions or comments on the above responses, please contact me at 412-566-5311.

Sincerely,

Stephen G. Bland

Stephen G. Bland
Chief Executive Officer

Audit Report Distribution List

This report was distributed to the following individuals upon its release:

Commonwealth of Pennsylvania:

The Honorable Edward G. Rendell
Governor

The Honorable Robin L. Wiessmann
State Treasurer
Commonwealth of Pennsylvania

The Honorable Allen D. Biehler, P.E.
Secretary
Pennsylvania Department of Transportation

The Honorable Joseph B. Scarnati, III
President Pro Tempore
Senate of Pennsylvania

The Honorable Dennis M. O'Brien
Speaker of the House
Pennsylvania House of Representatives

The Honorable Roger A. Madigan
Chair
Senate Transportation Committee
Senate of Pennsylvania

The Honorable J. Barry Stout
Minority Chair
Senate Transportation Committee
Senate of Pennsylvania

Members of the Allegheny County Delegation
Senate of Pennsylvania

The Honorable Joseph F. Markosek
Chairman
House Transportation Committee
Pennsylvania House of Representatives

The Honorable Richard A. Geist
Minority Chairman
House Transportation Committee
Pennsylvania House of Representatives

Members of the Allegheny County Delegation
Pennsylvania House of Representatives

Timothy A. Guss
Comptroller
Pennsylvania Department of Transportation

Audit Report Distribution List, continued

Allegheny County:

Dan Onorato
Allegheny County Chief Executive

Chairman and Members
Allegheny County Council

Mark Patrick Flaherty
Allegheny County Controller

United States Department of Transportation:

Federal Transit Administration
James S. Simpson
Administrator

Port Authority of Allegheny County:

Mr. Stephen G. Bland
Chief Executive Officer

Chairman and Members
Board of Directors

David A. Gramc, CPA
Controller