

OVERVIEW

VILLAGE

SAFE

WATER

PROGRAM,

2/2/06

STATE OF ALASKA

DEPT. OF ENVIRONMENTAL CONSERVATION

DIVISION OF WATER
DIRECTOR'S OFFICE

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March 3, 2006

The Honorable Paul Seaton
Chair, House State Affairs Committee
House of Representatives
Alaska State Capitol, Room 102
Juneau, AK 99801-1182

RE: Questions from the House State Affairs Committee

Dear Representative Seaton:

Thank you for the opportunity to provide a Village Safe Water (VSW) Program overview to the House State Affairs Committee in early February. I apologize for my delay in getting back to the Committee. Committee members asked a couple questions, paraphrased below, that we offered to respond to in writing.

The Legislative Budget and Audit Committee completed a January 9, 2004 audit of selected projects in the Village Safe Water Program. One audit finding was excessive wages for "on-site managers", or what DEC calls Project Superintendents. The audit included a recommendation to pay such workers a salary rather than an hourly wage. What has DEC done to control Project Superintendent wages?

State labor laws require that Project Superintendents receive an hourly wage, rather than a salary. They are entitled to hourly pay for each hour worked. Additionally, State law entitles workers who spend more than 20% of their weekly hours performing "hands on" types of work to overtime pay for hours worked in excess of eight in a workday or 40 in a workweek. All Project Superintendents meet this standard, and are therefore eligible for overtime pay.

The Department has resolved this audit issue by putting new policies into effect two years ago. In March of 2004, three new program procedures (enclosed) were established dealing with compensation for Project Superintendents, construction crew work schedules, and nepotism to help guard against another instance of the compensation situation revealed by the audit. Wage rates, per diem rates, and hours per workweek are all limited by these policies, and nepotism is prohibited.

In addition to Project Superintendents, other program staff including engineers, accountants, and administrative staff are included in payroll processing to help ensure compliance with these new policies. A review conducted after last construction season also verified compliance.

The January 9, 2004 audit recommended that the Village Safe Water program be transferred to the Department of Transportation. Why hasn't that transfer occurred?

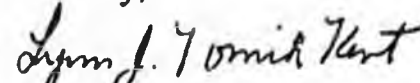
As mentioned in my oral testimony, the Department has resolved the audit issues that may have lead to this recommendation by the auditors.

The Department responded to this issue in a letter to Legislative Budget and Audit on February 5, 2004, sharing the Department's position that the VSW program would be better served in DEC rather than in the Department of Transportation. It is my understanding that at that time, the Department believed that such a move would be detrimental to program management and efficiency since the VSW program operates side-by-side with DEC's other financial and technical assistance programs such as the Municipal Water, Sewer and Solid Waste Matching Grant program, the operations assistance program, and the two low-interest loan programs. The programs share staff, a management and administrative support structure, and the same objectives and technical focus. VSW also works closely with the drinking water and wastewater regulatory programs at DEC to ensure that constructed facilities will meet the regulatory requirements.

In addition, the Department of Transportation responded to the recommendation in a letter dated December 4, 2003 to Legislative Budget and Audit, stating that the focus of the programs in Department of Transportation is competitive public works construction projects rather than the VSW program of grants to communities. It was the Department of Transportation's belief that these two very different programs would not easily lend themselves to consolidation within the Department of Transportation.

Please let me know if the committee has any additional questions regarding the Village Safe Water Program.

Sincerely,


Lynn J. Tomich Kent
Director

Enclosure: Policies and Procedures – Superintendent Compensation Policy
Policies and Procedures – Project Labor Oversight
Policies and Procedures – Nepotism on Force Account Projects

Superintendent Compensation

STATE OF ALASKA DEPARTMENT OF ENVIRONMENTAL CONSERVATION POLICIES AND PROCEDURES MANUAL	P&P Title: Superintendent Compensation Policy
	Effective: March 24, 2004
Issued By: Dan Easton, Director <i>Dan Easton</i> Division of Water	Department Contact is: Facilities Program Manager

PURPOSE:

To establish a policy which defines the maximum allowable wages, hours, and per diem for superintendents working on force account projects managed by the Village Safe Water program. This policy applies to all VSW force account projects where the project superintendent is an employee of the grantee.

BACKGROUND:

The Village Safe Water (VSW) program authorizes grantees to construct projects using their own labor and equipment. The option of constructing projects by force account is left to the grantee and typically requires the community to hire an on-site superintendent. VSW must give prior approval to all employment contracts between grantees and superintendents. VSW assists grantees in ensuring fair and equitable compensation for superintendents while safeguarding project funds from excesses in employment agreements. Since public funds are used to pay superintendents, it is necessary to establish certain cost controls relevant to superintendent employment contracts.

ANALYSIS:

This policy contains several cost containment components. In order to set reasonable cost controls, the department reviewed similar controls and operating procedures adopted by other agencies and organizations. To determine the maximum allowable VSW superintendent wage rate, a review was conducted of the Department of Transportation and Public Facilities (DOTPF) and the Alaska Native Tribal Health Consortium (ANTHC) wage rates for construction superintendents and Davis Bacon wages for comparable positions. The department concluded that a maximum pay rate of \$48.50 is comparable to these other pay rates. In order to determine the maximum allowable lodging and meal rates for superintendents, the rates defined in the Alaska State Administrative Manual and State/Union contracts were examined and comparable rates adopted. The maximum allowable hours that may be worked by superintendents was derived by balancing cost and safety concerns with short construction season realities. This restriction is similar to that employed by DOTPF.

POLICY:

- The maximum wage rate allowed for VSW project superintendents is \$48.50 per hour (including benefits, if any) for up to 40 hours a week. Any work performed beyond a 40 hour work week will be considered overtime and will be payable at time and a half.
- Any cost of benefits beyond workman's compensation, social security, and unemployment insurance must be deducted from the maximum wage rate described above.
- The maximum hours a superintendent may work is 72 hours a week during construction periods and 40 hours a week during non-construction periods. This limit is cumulative and applies whether the superintendent is managing one or more projects.
- On-site lodging expenses (cost of staying in the grantee community), if any, are limited to actual costs.
- On-site meal allowances (cost of food while staying in the grantee community), if any, may not exceed \$30.00 per day.
- Off-site lodging expenses (cost of staying in a location away from the grantee community for short term project related work), if any, are limited to actual costs.
- Off-site meal allowances (cost of food while staying in a location away from the grantee community for short term project related work), if any, may not exceed \$42.00 per day.
- In instances when the grantee provides meals and/or lodging, the Superintendent is not entitled to per diem or allowance for the meals and/or lodging.

IMPLEMENTATION:

This policy will be reviewed periodically to determine the need for updates. This policy shall apply to all superintendent employment contracts on projects managed by VSW. It shall be implemented upon its effective date.

Any contracts currently in existence that contain cost provisions that exceed those defined in this policy shall be renegotiated to within the limits of this policy within 60 days of the effective date of this directive.

Exceptions to this policy will only be allowed with the prior written approval of the Division Director.

The policy is not intended to prescribe wage rates, lodging costs, or meal allowances. It is only intended to set an upper limit on these costs. Actual wage rates should be commensurate with the experience of the superintendent and the complexity of the project. The maximum pay rate should only be given to highly experienced superintendents working on highly complex projects.

PROCESS:

- When filling out a VSW Grant Offer Request Form for construction projects which will use a force account labor force and where the grantee will hire an on-site superintendent/foreman, VSW engineers will indicate that a special grant condition applies.
- Upon receipt of a Grant Offer Request Form which indicates this special grant condition is applicable, the grants administrator will ensure the following grant condition is contained in the Grant Offer and a copy of this field directive is attached to the Grant Offer: *The grantee agrees to comply with the established VSW Field Directive - Superintendent Compensation (copy attached).*
- The VSW project engineer will remind grantees that are about to negotiate employment agreements with superintendents about the cost control requirements established by this field directive.
- Prior to approving an employment agreement between a grantee and an on-site superintendent, the VSW project engineer will ensure that provisions contained in the agreement are within the limits established under this directive.
- If a superintendent employment agreement does not conform to this directive, the VSW engineer will notify the grantee of the unallowable costs.

Grant Agreements and Superintendent Contracts Signed Prior to the Effective Date of this Directive:

- Grant agreements that (1) were signed prior to the effective date of this directive and (2) are for force account projects employing a superintendent will be amended to contain the following condition: *The grantee agrees to comply with the established VSW Field Directive - Superintendent Compensation (copy attached).*
- Superintendent employment agreements that (1) are in effect on the date of this directive and (2) are not in compliance with this directive must be renegotiated to conform to the policies contained in this directive before the 2004 construction season begins. The VSW project engineer will notify the grantee and the superintendent of this requirement.

Project Labor Oversight

STATE OF ALASKA DEPARTMENT OF ENVIRONMENTAL CONSERVATION POLICIES AND PROCEDURES MANUAL	P&P Title: Project Labor Oversight
	Effective: March 31, 2004
Issued By: <i>Dan Easton</i> Dan Easton, Director Division of Water	Department Contact is: Facilities Program Manager

PURPOSE:

To define the Village Safe Water (VSW) program's policy regarding oversight of project labor and overtime on VSW force account projects. This policy applies to all VSW force account projects where the project superintendent is an employee of the grantee.

BACKGROUND:

VSW engineers are responsible for ensuring that hours worked by construction crews and superintendents on force account projects are within established limits and are commensurate with project size and complexity. At the onset of a force account project, standard working hours will be established for the construction crew and superintendent. VSW engineers will monitor and manage project labor costs and overtime charges by reviewing Daily Project Status Reports and bi-weekly Summary Time Reports prepared by the project superintendent. This directive re-emphasizes several current VSW force account oversight practices and further defines procedures for monitoring project labor costs.

POLICY:

All project labor costs will be managed and monitored by VSW engineers to ensure that overtime hours worked by superintendents and construction crews are consistent with labor forecasts established at the onset of a project based upon project size and complexity.

IMPLEMENTATION:

- When filling out a VSW Grant Offer Request Form for construction projects which will use a force account labor force and where the grantee will hire an on-site superintendent, the VSW engineer will indicate that a special grant condition applies.
- Upon receipt of a Grant Offer Request Form which indicates this special grant condition is applicable, the grants administrator will ensure the following grant condition is contained in the Grant Offer: *"The grantee agrees to abide by the limits established for working hours in conformance with the VSW field directive for Project Labor Oversight."*

- Prior to construction, the VSW engineer will coordinate with the project superintendent to establish labor forecasts consistent with the size and complexity of the project. Special attention will be given to crew size and the number of overtime hours to be worked by the construction crew and superintendent. Labor forecasts may not exceed 60 hours per week for the construction crew and 72 hours per week for superintendents during construction periods and 40 hours a week during non-construction periods (see also VSW Field Directive- Superintendent Compensation).
- If the project superintendent anticipates the need to deviate from established labor forecasts, he/she must contact the VSW project engineer for prior approval. In an emergency situation where the VSW engineer can not be contacted and it is necessary to deviate from established labor forecasts, the project superintendent must leave messages for the VSW engineer via phone, fax and/or email on the course of action being taken. The project superintendent must document the event and coordinate with the VSW engineer at the earliest possible time thereafter.
- The project superintendent will submit Project Status Reports on a daily basis and Summary Time Reports at the end of each pay period to the VSW project engineer. The Summary Time Reports must include daily and weekly summaries of the construction crew and superintendent that worked on the project and the number of overtime hours worked by the construction crew and superintendent.
- The VSW engineer will review Summary Time Reports at the end of each pay period to ensure the project is adhering to VSW approved labor forecasts.
- If a Summary Time Report deviates from labor forecasts, the VSW engineer will promptly contact the project superintendent to determine the reason for such inconsistencies and take corrective action as necessary. Corrective action can take the form of a written notification and warning to potential dismissal of the project superintendent for violation of this field directive.

EXCEPTIONS:

Significant planned deviations to this policy will only be allowed with the prior written approval of the Division Director.

Nepotism Policy on Force Account Projects

STATE OF ALASKA DEPARTMENT OF ENVIRONMENTAL CONSERVATION POLICIES AND PROCEDURES MANUAL	P&P Title: Nepotism on Force Account Projects
	Effective: March 24, 2004
Issued By: <i>Dan Easton</i> Dan Easton, Director Division of Water	Department Contact is: Facilities Program Manager

PURPOSE:

To define the Village Safe Water (VSW) program's policy regarding the hiring and/or supervising of relatives on VSW force account projects. This policy applies to all VSW force account projects.

BACKGROUND:

Communities often construct VSW projects using force account methods. This may include the community hiring a superintendent to manage on-site work and the community hiring their own labor force. Currently there is no policy in place regarding nepotism on VSW force account projects. Although there has only been one documented case of nepotism in the history of the VSW program, a policy is needed to prevent potential occurrences of nepotism in the future.

POLICY:

It is the policy of the VSW program to eliminate actual or potential conflicts of interest, favoritism, and/or weaknesses in internal controls caused by the employment of related persons. Grantees and superintendents on projects managed by VSW may not cause to be hired nor supervise any individual on the VSW project that is related by blood or marriage, within and including the first degree of kindred (husband, wife, son, daughter, father, mother, sister, brother).

IMPLEMENTATION:

- When filling out a VSW Grant Offer Request Form for construction projects which will use a force account labor force and/or where the grantee will hire an on-site superintendent, VSW engineers will indicate that a special grant condition relating to nepotism applies.
- Upon receipt of a Grant Offer Request Form which indicates this special grant condition is applicable, the grants administrator will ensure that the following condition is contained in the Grant Offer and a copy of this field directive is attached to the Grant Offer: *"The grantee agrees to comply with the established VSW Field Directive - Nepotism on Force Account Projects (copy attached)."*
- VSW engineers will ensure all superintendent employee contracts contain the following clause: *"the superintendent may not hire nor supervise any relative on the VSW project that is related by blood or marriage, within and including the first degree of kindred (husband, wife, son, daughter, father, mother, sister, brother)."*

LOWELL POINT COMMUNITY COUNCIL

February 2, 2006

Representative Paul Seaton
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Homer, AK 99603
907-465-3472 facsimile

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Seward, AK 99664
Phone: 907-362-3701
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Subject: House Concurrent Resolution 28

Dear Paul Seaton,

Since we were not given the opportunity to speak again during the teleconference this morning, there are a few items that we, the Lowell Point Community Council, would like to clarify about our Village Safe Water project. There was some misinformation given out this morning.

It became obvious this morning that our community has gotten caught in the middle of many changes that are happening with the Village Safe Water program. Our community has sought the VSW grant to help with some serious health issues that are in our community. We applied for the grant for five years before we were finally approved by the legislature in 2004. Since then we have made no progress towards construction and now VSW is making us use a portion of our construction grant to fund further feasibility studies because of new rules in 2005. We have had a feasibility study done that was funded by and approved by the VSW Program, the Governor and the legislature.

Lowell Point is a unique oceanfront community that is on the road system and close to a small town, Seward. We have many year round homes that are both owner-occupied and rentals, an apartment building with 11 units and some vacation homes. We also have a State Park, a resort area that is very busy in the summer, a fire department, and several other businesses including lodges, bed and breakfasts and a boatyard/marine construction business. We have huge numbers of visitors in the summer and we maintain a good size population during the winter. The AKDOT has listed Lowell Point Road as the second most traveled road in the Seward area, second only to the main highway into town. We also have the City of Seward's waste water treatment lagoon in our community, though we currently cannot hook into it.

It would seem that we should be able to simply drive water wells and install septic systems to prevent any health hazards at Lowell Point but it is not this simple. Our community water source is an unconfined aquifer that allows mixing with the ocean and the groundwater. This unconfined aquifer leaves us very vulnerable to any kind of groundwater contamination.

- a. Due to saltwater intrusion, a large portion of the community cannot get freshwater despite the depth of their water wells. These residents use rainwater catchment systems or haul water for their homes. The homes that can get fresh water from their wells are vulnerable to any groundwater contamination in the area.
- b. The water table at Lowell Point is very high so septic systems are very expensive to install. While there are a few very nice homes on Lowell Point there are many more small homes that cannot afford to install septic systems and they are using outhouses or honey bucket systems for their septic needs. This waste is filtering directly into our aquifer and there is a very large potential for health hazards.
- c. The existing Seward Wastewater Treatment Plant is another past and potential future health hazard. In 1986 the lining of the lagoon was torn and leaked a large amount of its contents into our groundwater and our aquifer. Several wells on Lowell Point were found to be contaminated after this incident. This kind of incident could happen again.

- d. Water samples taken during the feasibility study by engineers and VSW indicated elevated and high levels of nitrates where the unconfined aquifer drains out at low tide. In addition, large algae blooms have been seen many times in these same areas.
- e. Lowell Point has a State Park area that has summertime caretakers and outdoor bathrooms. These bathrooms are used by many thousands of visitors in the summer and winter and are potential contaminators of our aquifer.
- f. There is a resort area on Lowell Point that brings hundreds of people to Lowell Point each day during the summer. There are tent and RV camping sites that are full all summer long. These sites can have from 250-400 campers in them at any time. There is a public restroom area that is potentially significantly contaminating the groundwater.

This morning the VSW referred to the cost per home of the system as being around \$95,000 per home for the sewer system and \$200,000 per home for the sewer and water systems. This calculation was based on their determination of there being only 30 year round homes on Lowell Point. We disagree with this determination for several reasons.

- a. VSW has sent out four different surveys to the Community Council and the property owners to come to this determination. These surveys are not standard surveys and each time we are asked for similar information just phrased in different ways. The first two surveys were sent to the LPCC to list which properties were lived in year round. Our calculations came up with over 50 homes that were lived in year round. Then the VSW has sent out two different surveys to the actual property owners asking them to specify which days they were absent in the past three years from their property. The survey is so difficult and detailed that many people have not filled them out and have therefore been excluded. The rules that the VSW is using to determine year round resident are extremely strict and we would challenge anyone to pass their "resident" test. Despite their claims that they are working with us, we feel that they are going out of their way to stop our project with their new "rules."
- b. The VSW will not consider homes as year round homes unless they are lived in by the property owner or have had the same renter in the house for at least three years. There are quite a few homes on Lowell Point that are rented out year round or in the winter. These homes are not considered even though they have people living in them year round.
- c. There is an 11 unit apartment building that houses many people year round. These apartment units are not considered since they are rentals. This building is one of the most significant users of water and producers of waste in the area. The apartment building is owned by a nearby fish processing plant and they often also have a temporary bunkhouse on site during the summer to house their employees.
- d. The VSW is not including businesses in their evaluation, which is valid since the Village Safe Water project does not fund businesses. However, they should take into consideration that most, if not all, of these businesses would pay to hook into the system when it is built. Plus most of these businesses either rent out the premises in the winter or they have a temporary residence on site for employees.
- e. There are currently three new homes that are being built in the area and there is a large demand for more housing in the area. There is a huge potential for future homes to be built here and these future residents will significantly worsen the public safety issues if there is no public sewer system in the area.
- f. Lowell Point does have some seasonal aspects. There are over 62 cabins or homes in the area. The fact that not all of these homes are lived in year round should not be the main concern. Our concern and I believe the concern of the Village Safe Water program is to eliminate current or potential health hazards in Alaska. During the summer all of the buildings are occupied and there are huge numbers of other visitors. This is when we have actual and potential health and safety hazards. Just because some of the houses or buildings may not have someone in them year round does not eliminate the increased potential of having a huge health and safety problem while everyone is here during the summer.

We do not believe that this kind of cost per unit has been evaluated in all of the areas that have been funded by Village Safe Water. We would guess that many of the communities in remote areas with 25 people in them have cost significantly more per household than ours.

We have somehow gotten caught in the middle of some regulation changes at VSW. Our project has been studied, recommended and approved for funding. Due to the regulation changes that happened after our grant was approved, our project has been stopped and we have to start over with the feasibility study. We do not think that this is right.

We sincerely hope that you can see how important our Village Safe Water project is for our community. There are many residents that cannot get fresh water in their homes and we are extremely vulnerable to many different health hazards year round and especially during the summer.

Please call with any questions or suggestions for getting our project back on track. Thank you for your time.

Sincerely,


Jim McCracken
President
Lowell Point Community Council

Cc. Representative James Elkins
Representative Berta Gardner
Representative Carl Gatto
Representative Max Gruenberg Jr.
Representative Bob Lynn
Representative Jay Ramras

200 communities

Sustainability

2005 fiscal year
completed



1) Sustainability
Consistent review guidelines signed

2) local capacity

3) business plan

4)

Access to existing facilities

Occupancy of homes - 30 homes
capital cost

Project Accounting
↑ internal controls

New federal OS requirements

Legislative Intent

Included in SFY 2006 Capital Budget for Village Safe Water Program

It is the intent of the Legislature:

- I. That the Department of Environmental Conservation (DEC) will establish guidelines for deciding whether proposed project costs are reasonable and whether proposed projects are sustainable; ensure that projects are limited to systems that are reasonable and sustainable; and exercise final decision authority as to project costs and the types and extent of projects to be constructed.
- II. That DEC will exercise project accounting control by assigning accounting personnel specifically to program accounting functions and by developing an account reporting system that is capable of providing up-to-date accounting information to engineers and managers.
- III. That DEC will encourage development of local ordinances that enhance the establishment and collection of user fees which are adequate to pay for the sustained operation of facilities constructed by the program.
- IV. That DEC will work with the Regulatory Commission of Alaska to encourage local management of projects constructed by the program in compliance with standards established by the Commission.

History of Rural Utility Business Advisor (RUBA) program History of Use and Development of Capacity Indicators

The RUBA program began using indicators of community capacity in 1991 when the RUBA program began working with the Dept. of Environmental Conservation, Village Safe Water (VSW) Program. At that time, VSW provided funding to the RUBA Program to assist in developing management capacity in select communities. The indicators were at that time primarily used as a method for the program to report progress of effort back to VSW.

As the program grew, the indicators went through several variations. By 1998 when the program funding was changed from a RSA with DEC to a direct grant from EPA, the indicators underwent substantial revision. At this time, the indicators were being primarily used as a communication tool with the community and to prioritize technical assistance. The indicators took the form of a report card where each indicator was given a "Inadequate", "Meets Minimum Requirements", or "Exceeds Minimum Requirements". They continued to be used to report status of communities to agencies including the EPA.

In April of 2002 the reporting format was substantially changed to the system that is now in use. The indicators were grouped into two categories - Essential Indicators and Sustainable Indicators. *Essential Indicators* were those issues that through the programs experience working with rural utilities were identified as being critical for the utility to continue to function in the short term (6-18 months). *Sustainable Indicators* were those issues that if not addressed would likely create a financial or managerial strain on the utility and cause substantial problems in the long term (1-5 years).

In July of 2004 the Village Safe Water program began requiring as a special grant condition that entities receiving a capital construction grant request that a management assessment be completed and that the utility meet all the *essential* capacity indicators.

In April of 2006 there were two additional essential capacity indicators added to the assessment.

- The utility is current paying all water/wastewater electric bills.
- The utility has on hand a year's adequate fuel supply or it has a financial plan to purchase an adequate supply.

These were added in response to several instances that occurred in the winter of 2004-2005 that threatened rural piped systems. These indicators would assure that these two issues would be examined and not be missed in the assessment.

Capacity Indicators Currently Used by the Rural Utility Business Advisor (RUBA) Program

Utility Finance Indicators

Essential Indicators

- | Yes | No | |
|--------------------------|--------------------------|--|
| <input type="checkbox"/> | <input type="checkbox"/> | All revenue and expenses for the utility are listed in the utility budget. |
| <input type="checkbox"/> | <input type="checkbox"/> | The utility has adopted a balanced realistic budget. |
| <input type="checkbox"/> | <input type="checkbox"/> | Monthly financial reports are prepared and submitted to the policy making body. |
| <input type="checkbox"/> | <input type="checkbox"/> | The utility is current paying all water/wastewater electric bills. |
| <input type="checkbox"/> | <input type="checkbox"/> | The utility has on hand a year's adequate fuel supply or it has a financial plan to purchase an adequate supply. |
| <input type="checkbox"/> | <input type="checkbox"/> | The utility is receiving revenues (user fees or other sources) sufficient to cover operating expenses. |

Sustainable Indicators

- | | | |
|--------------------------|--------------------------|---|
| <input type="checkbox"/> | <input type="checkbox"/> | The utility is receiving revenues (user fees or other sources) sufficient to cover operating expenses and Repair & Replacement (R&R) costs. |
| <input type="checkbox"/> | <input type="checkbox"/> | YTD revenues are at a level equal to or above those budgeted. |
| <input type="checkbox"/> | <input type="checkbox"/> | YTD expenditures are at a level equal to or below those budgeted. |
| <input type="checkbox"/> | <input type="checkbox"/> | A monthly manager's report is prepared. |
| <input type="checkbox"/> | <input type="checkbox"/> | Budget amendments are completed and adopted as necessary. |

Accounting Systems Indicators

Essential Indicators

- | Yes | No | |
|--------------------------|--------------------------|---|
| <input type="checkbox"/> | <input type="checkbox"/> | The utility has adopted a collection policy and actively follows it. |
| <input type="checkbox"/> | <input type="checkbox"/> | The utility bills customers on a regular basis. |
| <input type="checkbox"/> | <input type="checkbox"/> | An accounts receivable system is in place which tracks customers and reports past due accounts and amounts. |
| <input type="checkbox"/> | <input type="checkbox"/> | An accounts payable system is in place. |
| <input type="checkbox"/> | <input type="checkbox"/> | The payroll system correctly calculates payroll and keeps records. |
| <input type="checkbox"/> | <input type="checkbox"/> | A cash receipt system is in place that records incoming money and what it was for. |
| <input type="checkbox"/> | <input type="checkbox"/> | The utility has a cash disbursement system that records how money was spent. |

Sustainable Indicators

- | | | |
|--------------------------|--------------------------|---|
| <input type="checkbox"/> | <input type="checkbox"/> | A chart of accounts is used that identifies categories in a reasonable, usable manner. |
| <input type="checkbox"/> | <input type="checkbox"/> | Monthly bank reconciliations have been completed for all utility accounts. |
| <input type="checkbox"/> | <input type="checkbox"/> | The utility has a purchasing system that requires approval prior to purchase, and the approval process compares proposed purchases to budgeted amounts. |

Payroll Tax Indicators

Essential Indicators

- | Yes | No | NA | |
|--------------------------|--------------------------|--------------------------|--|
| <input type="checkbox"/> | <input type="checkbox"/> | | The utility has a system to accurately calculate, track, and report payroll tax liabilities. |
| <input type="checkbox"/> | <input type="checkbox"/> | | The utility is current on filing federal and state tax reports. |
| <input type="checkbox"/> | <input type="checkbox"/> | | The utility is current on making federal and state tax deposits. |
| <input type="checkbox"/> | <input type="checkbox"/> | <input type="checkbox"/> | If there are any past tax liabilities, a repayment agreement has been signed and repayments are current. |

Personnel System Indicators

Essential Indicators

- | | | |
|--------------------------|--------------------------|---|
| Yes | No | |
| <input type="checkbox"/> | <input type="checkbox"/> | The utility has a posted workers compensation insurance policy in effect. |
-

Sustainable Indicators

- | | | |
|--------------------------|--------------------------|---|
| <input type="checkbox"/> | <input type="checkbox"/> | The utility has adopted and uses a Personnel Policy, which has been reviewed by an attorney, AML, or DCCED for topics and language. |
| <input type="checkbox"/> | <input type="checkbox"/> | The utility has adequate written job descriptions for all positions. |
| <input type="checkbox"/> | <input type="checkbox"/> | The utility has adopted and follows a written personnel evaluation process that ties the job description to the evaluation. |
| <input type="checkbox"/> | <input type="checkbox"/> | The utility has an adequate written hiring process. |
| <input type="checkbox"/> | <input type="checkbox"/> | The utility has personnel folders on every employee that contain at least: 1-9, Job Application and Letter of Acceptance. |
| <input type="checkbox"/> | <input type="checkbox"/> | The utility has a probationary period for new hires that includes orientation, job-training/oversight, and evaluations. |
| <input type="checkbox"/> | <input type="checkbox"/> | The utility provides training opportunities to staff as needed and available. |

Organizational Management Indicators

Essential Indicators

- | | | |
|--------------------------|--------------------------|--|
| Yes | No | |
| <input type="checkbox"/> | <input type="checkbox"/> | The entity that owns the utility is known and the entity that will operate the utility is set. |
| <input type="checkbox"/> | <input type="checkbox"/> | The policy making body is active in policy making of the utility. |
| <input type="checkbox"/> | <input type="checkbox"/> | The policy making body enforces utility policy. |
| <input type="checkbox"/> | <input type="checkbox"/> | The utility has an adequately trained manager. |
| <input type="checkbox"/> | <input type="checkbox"/> | The utility has an adequately trained bookkeeper. |
| <input type="checkbox"/> | <input type="checkbox"/> | The utility has an adequately trained operator(s). |
| <input type="checkbox"/> | <input type="checkbox"/> | The utility has adopted the necessary ordinances (or rules and regulations) necessary to give it the authority to operate. |
-

Sustainable Indicators

- | | | |
|--------------------------|--------------------------|--|
| <input type="checkbox"/> | <input type="checkbox"/> | The utility has adopted an organizational chart that reflects the current structure. |
| <input type="checkbox"/> | <input type="checkbox"/> | The policy making body meets as required. |
| <input type="checkbox"/> | <input type="checkbox"/> | The utility complies with the open meeting act for all meetings. |

Operation of Utility Indicators

Essential Indicators

- | | | |
|--------------------------|--------------------------|---|
| Yes | No | |
| <input type="checkbox"/> | <input type="checkbox"/> | The utility operator(s) are actively working towards necessary certification. |
| <input type="checkbox"/> | <input type="checkbox"/> | The utility has a preventative maintenance plan developed for the existing sanitation facilities. |
-

Sustainable Indicators

- | | | |
|--------------------------|--------------------------|---|
| <input type="checkbox"/> | <input type="checkbox"/> | The manager receives a monthly O&M report from the utility operator and routinely "spot checks" the facilities to see that the maintenance items are being completed. |
| <input type="checkbox"/> | <input type="checkbox"/> | The utility has a safety manual and holds safety meetings. |
| <input type="checkbox"/> | <input type="checkbox"/> | Utility facilities have not suffered any major problems/outages due to management issues that are still unresolved. |
| <input type="checkbox"/> | <input type="checkbox"/> | The utility is operating at the level of service that was proposed. |
| <input type="checkbox"/> | <input type="checkbox"/> | The operator provides status reports to the manager on a routine basis. |
| <input type="checkbox"/> | <input type="checkbox"/> | The utility has completed and distributed its <u>Consumer Confidence Report</u> (CCR). |
| <input type="checkbox"/> | <input type="checkbox"/> | The utility meets all required regulations (is not on the <u>Significant Non-Compliance</u> (SNC) list). |
| <input type="checkbox"/> | <input type="checkbox"/> | The utility maintains an inventory control list. |
| <input type="checkbox"/> | <input type="checkbox"/> | The utility maintains a critical spare parts list. |



Frank H. Murkowski
GOVERNOR

STATE OF ALASKA
OFFICE OF THE GOVERNOR
JUNEAU

January 28, 2005

ADMINISTRATIVE ORDER NO. 224

I, Frank H. Murkowski, Governor of the State of Alaska, under the authority of art. III, secs. 1 and 24, of the Alaska Constitution, order all departments of the executive branch, under the direction of the Office of the Governor, to ensure that certain future capital projects funded by the State of Alaska meet, to the extent consistent with federal and state law, the State of Alaska's sustainability standards as outlined in this Order.

BACKGROUND AND PURPOSE

The purpose of this Administrative Order is to provide a framework for cooperation that enhances collaboration between the State of Alaska and the Denali Commission by providing a common definition of sustainability. Infrastructure needs in Alaska, especially in rural areas, are enormous compared to available funding. As a result, it is imperative that every dollar investment be done in a way that will maximize the sustainable long-term benefits to Alaskans.

The Denali Commission Act of 1998, as amended (Division C, Title III, P.L. 105-277), states that the purposes of the Denali Commission are to:

1. deliver the services of the federal government in the most cost-effective manner practicable by reducing administrative and overhead costs;
2. provide job training and other economic development services in rural communities, particularly distressed communities; and
3. promote rural development and provide power generation and transmission facilities.

The program areas of the Denali Commission to which the state's collaboration will apply are:

- Energy projects
- Health facilities
- Solid waste projects
- Training
- Washeterias
- Multi-use facilities
- Solid Waste projects

- Elder and teacher housing
- Domestic violence facilities
- Economic development

The Denali Commission Act recognizes that these purposes can only be accomplished through a collaborative, coordinated effort by the State of Alaska and federal agencies. To this end, the federal and state co-chairs, State of Alaska department commissioners, and the University of Alaska president signed a Memorandum of Understanding (MOU) dated July 2003 with the Denali Commission and various federal agencies that conduct business in the State of Alaska. The MOU outlines points of understanding that facilitate the collaboration and coordination necessary for achievement of the purposes of the Denali Commission and related missions of agencies who are parties to that MOU.

The points of understanding outlined in the MOU include recognition of the following:

1. Sustainability
Minimizing life cycle costs when investing in public infrastructure projects is an essential "first step" in achieving sustainability.

2. Regional Strategies
Systematic planning and coordination on a local, regional, and statewide basis are necessary to achieve the most effective results from investments in infrastructure, economic development, and training.

- a. Community Plans

A single community strategic plan should be sufficient to identify and establish the priorities of each rural community.

- b. Sharing Information

The power of sharing information increases efficiencies and decreases duplication of services by state and federal agencies.

- c. Economic Development

Sound economic development facilitates growth of self-sufficient communities, and the coordination of activities will stimulate economic growth.

- d. Workforce Development (Vocational and Technical Training)

Workforce development is a critical component to building sustainable public infrastructure and self-sufficient communities in Alaska.

Guidelines To Achieve Sustainability

This Administrative Order incorporates a sustainability policy and guidelines that further align State of Alaska infrastructure planning and funding for those capital projects that fall within the Denali Commission's program areas.

In executing this Administrative Order, all departments of the executive branch under the direction of the Office of the Governor shall use the following definition of sustainability and the investment guidelines in this Order to guide the funding of state capital investments that fall within the Denali Commission's program areas.

Sustainability, by definition, includes all costs associated with management, operation and maintenance, renewal, and replacement (after the design life has been achieved) necessary to maintain an acceptable level of service.

- Users Support Costs

The high cost of infrastructure in some areas of Alaska may make it infeasible for the total cost to be borne by local users. However, to the extent possible, user rates and fees should be assessed to cover all costs necessary to maintain sustainability.

- Lowest Cost Possible

All practical steps should be taken to reduce the cost of sustainable infrastructure. This includes simplification of projects; standardization of infrastructure; combining utilities; regionalization of utility management structures; bulk purchase of fuel; and; training and development of management personnel.

- Business Plan Required

A sound business plan must be in place for each project. Sound business planning is key to ensuring that infrastructure projects will be operated and maintained. A business plan shall include demonstration of how all costs necessary to assure a sustainable project or level of service will be achieved.

INVESTMENT GUIDELINES

All departments of the executive branch under the direction of the Office of the Governor shall consider all available information regarding each of the factors outlined below, and any other relevant information, in making investment decisions. In cases in which sustainability of an investment is questionable, the State of Alaska, either directly or through its partners, will work with project proponents in an effort to find workable solutions to ensure that a project is sustainable.

To this end, it is incumbent that requestors provide relevant information that may not otherwise be available and to actively develop workable solutions. Solutions may involve a smaller-scale project, mobile facilities, and multi-community or regional management approaches. If no workable sustainable solution is apparent, the State of Alaska or its

partners may suggest alternative means to access critical services.

The following guidelines should be followed when considering funding a capital project with State of Alaska funding:

- Local governments to assume responsibility

Existence of a state-chartered government increases the probability that basic infrastructure and services funded by the State of Alaska will be sustained over the long term. The State of Alaska recognizes that other regional organizations share both responsibility and capacity to contribute to sustainability. A project's consistency with a regionally approved plan will be a strong factor in support of a project.

- Good faith

The long-term sustainability of State of Alaska investments is highly dependent on the good faith of the investment recipient. In evaluating potential investment, priority will be given to recipients that have historically demonstrated good faith in making and keeping financial commitments. Previous demonstrations of bad faith, particularly with previous state or federal investments, or failure to pay taxes, may preclude additional investments.

- Proximity and access to existing services and facilities

In determining the need for a new facility, a careful evaluation of existing access to services or facilities must be presented. Where the needs of two or more communities in close proximity to one another can be adequately and more cost-effectively served by a single facility, that option would be selected over separate facilities for each community.

- Renovation a priority over new construction

Renovation or expansion of existing facilities will be favored over new construction when it can adequately meet community needs at significantly lower life-cycle costs.

- Infrastructure sized to meet needs

Infrastructure will be sized to meet needs that can reasonably be projected over the design life of the project. If population is increasing, appropriate excess capacity will be provided to accommodate growth. Decreasing population may result in a smaller facility than the current population would dictate.

- Affordability

Project evaluation will include the project proponent's capacity to afford the life-cycle costs associated with sustaining proposed services and facilities.

- Unit cost

Unit cost of construction varies widely across the state for a number of reasons, including the technology employed and design utilized. High unit costs tend to work counter to project sustainability. Some of the variables impacting unit cost (such as project location and soil conditions) are not controllable, but many others are. Every reasonable effort will be made to control unit costs by working with investment recipients to ensure that the most appropriate technology and designs are applied.

- Absence of imminent environmental threat

New facilities will be protected against imminent environmental threats, such as flooding and erosion, consistent with Administrative Order No. 175.

- Needs of existing communities have priority

Priority will be given to the infrastructure needs of existing communities before consideration of proposals to create new communities, unless there is a congressionally directed relocation of an existing community.

This Order takes effect immediately.

DATED at Juneau, Alaska, this 28th day of January, 2005.

/s/Frank H. Murkowski
Governor

WWW.GOV.STATE.AK.US

Administrative Orders 201-present | Contact the Governor | Webmaster | State of Alaska

MEMORANDUM

State of Alaska

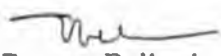
Department of Environmental Conservation
Office of the Commissioner

TO: James F. Clark
Chief of Staff
Office of the Governor

DATE: April 26, 2004

FILE NO: G:\COMM\WP\2004\VSW Audit Clark.doc

PHONE NO: 465-5065

FROM: 
Ernesta Ballard
Commissioner

SUBJECT: Village Safe Water Audit

I appreciate your patience concerning the Legislative Budget & Audit report on DEC's Village Safe Water program (VSW). While the audit's quality is poor, we addressed it seriously and have learned several lessons. The following is information on our response to the audit.

First, though imperfect, the VSW administrative structure is fundamentally sound. In the past, it was not uncommon for the State to make direct grants to communities where a check was issued and the State had no further involvement. The VSW program makes grants to communities, but the grants are co-managed by DEC and communities, with bookkeeping provided by a private CPA firm. This system keeps track of the funds and ensures that they are used for intended purposes. It involves the community as owner, but the State retains essential controls regarding the grant purpose.

Second, the audit revealed a few issues warranting corrective action. Here is what we have done and are doing to improve management:

- We have moved the program manager position from Juneau to Anchorage to place it closer to the engineers and the day-to-day operations. This involved laying off the previous Juneau-based program manager (who found a job with DOT/PF). Recruitment for the Anchorage-based position is nearly complete.
- We are in the process of reclassifying a position to add contracting support. Some of the problems identified by the audit stem from having the engineers prepare their own contracts for construction services. This new position will provide the engineers with the contracting help they need according to the audit and our own observations. That position will be established in the next few months.
- We have effected three new program procedures dealing with nepotism, compensation for project superintendents, and construction crew work schedules to help guard against a repeat of the \$200,000+ compensation situation revealed by the audit.

Last, an essential point overlooked by the audit is the VSW's relationship to its surrounding programs. The VSW operates side-by-side with DEC's other financial assistance programs, such as

The Honorable James F. Clark

2

April 26, 2004

the Municipal Water, Sewer and Solid Waste Matching Grant program and our two low-interest loan programs. The four programs share staff, a management and administrative support structure, and the same objectives and technical focus. The Village Safe Water program is most efficiently located in DEC. There is no need to relocate the program to DOT/PF.

Please let me know if you would like further detail.

STATE OF ALASKA

DEPT. OF ENVIRONMENTAL CONSERVATION
OFFICE OF THE COMMISSIONER

FRANK H. MURKOWSKI, GOVERNOR
410 Willoughby Ave., Ste 303
Juneau, AK 99801-1795
PHONE: (907) 465-5065
FAX: (907) 465-5070
<http://www.state.ak.us/dec/>

June 23, 2004

The Honorable Ralph Samuels, Chair
Legislative Budget and Audit Committee
716 W. 4th Avenue
Anchorage, Alaska 99501-2133

Dear Representative Samuels:

In your February 26, 2004 letter you requested that prior to the end of the fiscal year, I provide members of the Legislative Budget and Audit Committee (LB&A) with an update on the Department of Environmental Conservation's (DEC) progress in implementing commitments we made in our response to a LB&A audit entitled "Department of Environmental Conservation, Village Safe Water (VSW), Selected Projects." Our commitments are highlighted in italics below and are followed by a brief description of our progress.

"The audit revealed that the VSW program continues to have serious problems with 1099 and I-9 form procedures. Some of the problem stems from confusion over whether responsibility lies with the VSW engineer or the CPA firm. This situation will be corrected through a combination of employee training and amending the CPA firm contract before the next construction season (by May 1 of this year)."

VSW staff received training regarding required Internal Revenue Service (IRS) and U.S. Immigration and Naturalization Service (INS) forms and procedures on June 8, 2004. Refresher training will be provided annually. The VSW contract for accounting and bookkeeping services was amended to clarify IRS and INS reporting responsibilities on May 20, 2004.

"In two, and perhaps three cases, the program did not exhibit sufficient control over superintendent compensation (including salary, travel and housing arrangements). While paying superintendents a salary is not the answer, the program clearly needs to establish better limits on superintendent compensation."

DEC completed new guidance is being prepared and will be in effect before the construction season (by May 1 of this year). New guidance establishing limits on superintendent compensation and allowable overtime with an effective date of March 24, 2004 (see enclosure A). In addition, new guidance regarding oversight of project labor and overtime on VSW force account projects was completed with an effective date of March 31, 2004 (see enclosure B).

"The audit accurately revealed a single incident of nepotism that should not have been tolerated. A new policy is being prepared and will be in effect before the construction season (by May 1 of this

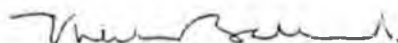
year). " DEC completed new guidance relating to nepotism on force account projects with an effective date March 24, 2004 (see enclosure C).

"Finally, we do not dispute that the VSW engineers could benefit from better procurement and contracting support. The program intends to reclassify an existing position to create a contracting officer position in the VSW program before the end of the current fiscal year."

We are reclassifying an existing position to create a procurement specialist position. A Position Description has been prepared (see enclosure D) and will be submitted to Human Resources staff in the Department of Administration within the next two weeks for approval to recruit.

If you have any questions, please let me know or, you may contact Dan Easton, DEC's Director of the Division of Water at 465-5135.

Sincerely,



Ernesta Ballard
Commissioner

cc: The Honorable Gene Therriault, Legislative Budget and Audit Committee
The Honorable Ben Stevens, Legislative Budget and Audit Committee
The Honorable Con Bunde, Legislative Budget and Audit Committee
The Honorable Gary Wilken, Legislative Budget and Audit Committee
The Honorable Lyman Hoffman, Legislative Budget and Audit Committee
The Honorable Lyda Green, Legislative Budget and Audit Committee
The Honorable Mike Chenault, Legislative Budget and Audit Committee
The Honorable Mike Hawker, Legislative Budget and Audit Committee
The Honorable Vic Kohring, Legislative Budget and Audit Committee
The Honorable Beth Kerttula, Legislative Budget and Audit Committee
The Honorable Reggie Joule, Legislative Budget and Audit Committee
Mike Maher, Director, Division of Information & Administrative Services, DEC
Dan Easton, Director, Division of Water, DEC.

Superintendent Compensation

STATE OF ALASKA DEPARTMENT OF ENVIRONMENTAL CONSERVATION POLICIES AND PROCEDURES MANUAL	P&P Title: Superintendent Compensation Policy
	Effective: March 24, 2004
Issued By: Dan Easton, Director <i>Dan Easton</i> Division of Water	Department Contact is: Facilities Program Manager

PURPOSE:

To establish a policy which defines the maximum allowable wages, hours, and per diem for superintendents working on force account projects managed by the Village Safe Water program. This policy applies to all VSW force account projects where the project superintendent is an employee of the grantee.

BACKGROUND:

The Village Safe Water (VSW) program authorizes grantees to construct projects using their own labor and equipment. The option of constructing projects by force account is left to the grantee and typically requires the community to hire an on-site superintendent. VSW must give prior approval to all employment contracts between grantees and superintendents. VSW assists grantees in ensuring fair and equitable compensation for superintendents while safeguarding project funds from excesses in employment agreements. Since public funds are used to pay superintendents, it is necessary to establish certain cost controls relevant to superintendent employment contracts.

ANALYSIS:

This policy contains several cost containment components. In order to set reasonable cost controls, the department reviewed similar controls and operating procedures adopted by other agencies and organizations. To determine the maximum allowable VSW superintendent wage rate, a review was conducted of the Department of Transportation and Public Facilities (DOTPF) and the Alaska Native Tribal Health Consortium (ANTHC) wage rates for construction superintendents and Davis Bacon wages for comparable positions. The department concluded that a maximum pay rate of \$48.50 is comparable to these other pay rates. In order to determine the maximum allowable lodging and meal rates for superintendents, the rates defined in the Alaska State Administrative Manual and State/Union contracts were examined and comparable rates adopted. The maximum allowable hours that may be worked by superintendents was derived by balancing cost and safety concerns with short construction season realities. This restriction is similar to that employed by DOTPF.

POLICY:

- The maximum wage rate allowed for VSW project superintendents is \$48.50 per hour (including benefits, if any) for up to 40 hours a week. Any work performed beyond a 40 hour work week will be considered overtime and will be payable at time and a half.
- Any cost of benefits beyond workman's compensation, social security, and unemployment insurance must be deducted from the maximum wage rate described above.
- The maximum hours a superintendent may work is 72 hours a week during construction periods and 40 hours a week during non-construction periods. This limit is cumulative and applies whether the superintendent is managing one or more projects.
- On-site lodging expenses (cost of staying in the grantee community), if any, are limited to actual costs.
- On-site meal allowances (cost of food while staying in the grantee community), if any, may not exceed \$30.00 per day.
- Off-site lodging expenses (cost of staying in a location away from the grantee community for short term project related work), if any, are limited to actual costs.
- Off-site meal allowances (cost of food while staying in a location away from the grantee community for short term project related work), if any, may not exceed \$42.00 per day.
- In instances when the grantee provides meals and/or lodging, the Superintendent is not entitled to per diem or allowance for the meals and/or lodging.

IMPLEMENTATION:

This policy will be reviewed periodically to determine the need for updates. This policy shall apply to all superintendent employment contracts on projects managed by VSW. It shall be implemented upon its effective date.

Any contracts currently in existence that contain cost provisions that exceed those defined in this policy shall be renegotiated to within the limits of this policy within 60 days of the effective date of this directive.

Exceptions to this policy will only be allowed with the prior written approval of the Division Director.

The policy is not intended to prescribe wage rates, lodging costs, or meal allowances. It is only intended to set an upper limit on these costs. Actual wage rates should be commensurate with the experience of the superintendent and the complexity of the project. The maximum pay rate should only be given to highly experienced superintendents working on highly complex projects.

PROCESS:

- When filling out a VSW Grant Offer Request Form for construction projects which will use a force account labor force and where the grantee will hire an on-site superintendent/foreman, VSW engineers will indicate that a special grant condition applies.
- Upon receipt of a Grant Offer Request Form which indicates this special grant condition is applicable, the grants administrator will ensure the following grant condition is contained in the Grant Offer and a copy of this field directive is attached to the Grant Offer: *The grantee agrees to comply with the established VSW Field Directive - Superintendent Compensation (copy attached).*
- The VSW project engineer will remind grantees that are about to negotiate employment agreements with superintendents about the cost control requirements established by this field directive.
- Prior to approving an employment agreement between a grantee and an on-site superintendent, the VSW project engineer will ensure that provisions contained in the agreement are within the limits established under this directive.
- If a superintendent employment agreement does not conform to this directive, the VSW engineer will notify the grantee of the unallowable costs.

Grant Agreements and Superintendent Contracts Signed Prior to the Effective Date of this Directive:

- Grant agreements that (1) were signed prior to the effective date of this directive and (2) are for force account projects employing a superintendent will be amended to contain the following condition: *The grantee agrees to comply with the established VSW Field Directive - Superintendent Compensation (copy attached).*
- Superintendent employment agreements that (1) are in effect on the date of this directive and (2) are not in compliance with this directive must be renegotiated to conform to the policies contained in this directive before the 2004 construction season begins. The VSW project engineer will notify the grantee and the superintendent of this requirement.

Project Labor Oversight

STATE OF ALASKA DEPARTMENT OF ENVIRONMENTAL CONSERVATION POLICIES AND PROCEDURES MANUAL	P&P Title: Project Labor Oversight
	Effective: March 31, 2004.
Issued By: <i>Don Easton</i> Dan Easton, Director Division of Water	Department Contact is: Facilities Program Manager

PURPOSE:

To define the Village Safe Water (VSW) program's policy regarding oversight of project labor and overtime on VSW force account projects. This policy applies to all VSW force account projects where the project superintendent is an employee of the grantee.

BACKGROUND:

VSW engineers are responsible for ensuring that hours worked by construction crews and superintendents on force account projects are within established limits and are commensurate with project size and complexity. At the onset of a force account project, standard working hours will be established for the construction crew and superintendent. VSW engineers will monitor and manage project labor costs and overtime charges by reviewing Daily Project Status Reports and bi-weekly Summary Time Reports prepared by the project superintendent. This directive re-emphasizes several current VSW force account oversight practices and further defines procedures for monitoring project labor costs.

POLICY:

All project labor costs will be managed and monitored by VSW engineers to ensure that overtime hours worked by superintendents and construction crews are consistent with labor forecasts established at the onset of a project based upon project size and complexity.

IMPLEMENTATION:

- When filling out a VSW Grant Offer Request Form for construction projects which will use a force account labor force and where the grantee will hire an on-site superintendent, the VSW engineer will indicate that a special grant condition applies.
- Upon receipt of a Grant Offer Request Form which indicates this special grant condition is applicable, the grants administrator will ensure the following grant condition is contained in the Grant Offer: *"The grantee agrees to abide by the limits established for working hours in conformance with the VSW field directive for Project Labor Oversight."*

- Prior to construction, the VSW engineer will coordinate with the project superintendent to establish labor forecasts consistent with the size and complexity of the project. Special attention will be given to crew size and the number of overtime hours to be worked by the construction crew and superintendent. Labor forecasts may not exceed 60 hours per week for the construction crew and 72 hours per week for superintendents during construction periods and 40 hours a week during non-construction periods (see also VSW Field Directive- Superintendent Compensation).
- If the project superintendent anticipates the need to deviate from established labor forecasts, he/she must contact the VSW project engineer for prior approval. In an emergency situation where the VSW engineer can not be contacted and it is necessary to deviate from established labor forecasts, the project superintendent must leave messages for the VSW engineer via phone, fax and/or email on the course of action being taken. The project superintendent must document the event and coordinate with the VSW engineer at the earliest possible time thereafter.
- The project superintendent will submit Project Status Reports on a daily basis and Summary Time Reports at the end of each pay period to the VSW project engineer. The Summary Time Reports must include daily and weekly summaries of the construction crew and superintendent that worked on the project and the number of overtime hours worked by the construction crew and superintendent.
- The VSW engineer will review Summary Time Reports at the end of each pay period to ensure the project is adhering to VSW approved labor forecasts.
- If a Summary Time Report deviates from labor forecasts, the VSW engineer will promptly contact the project superintendent to determine the reason for such inconsistencies and take corrective action as necessary. Corrective action can take the form of a written notification and warning to potential dismissal of the project superintendent for violation of this field directive.

EXCEPTIONS:

Significant planned deviations to this policy will only be allowed with the prior written approval of the Division Director.

Nepotism Policy on Force Account Projects

STATE OF ALASKA DEPARTMENT OF ENVIRONMENTAL CONSERVATION POLICIES AND PROCEDURES MANUAL	P&P Title: Nepotism on Force Account Projects
	Effective: March 24, 2004
Issued By: <i>Dan Easton</i> Dan Easton, Director Division of Water	Department Contact is: Facilities Program Manager

PURPOSE:

To define the Village Safe Water (VSW) program's policy regarding the hiring and/or supervising of relatives on VSW force account projects. This policy applies to all VSW force account projects.

BACKGROUND:

Communities often construct VSW projects using force account methods. This may include the community hiring a superintendent to manage on-site work and the community hiring their own labor force. Currently there is no policy in place regarding nepotism on VSW force account projects. Although there has only been one documented case of nepotism in the history of the VSW program, a policy is needed to prevent potential occurrences of nepotism in the future.

POLICY:

It is the policy of the VSW program to eliminate actual or potential conflicts of interest, favoritism, and/or weaknesses in internal controls caused by the employment of related persons. Grantees and superintendents on projects managed by VSW may not cause to be hired nor supervise any individual on the VSW project that is related by blood or marriage, within and including the first degree of kindred (husband, wife, son, daughter, father, mother, sister, brother).

IMPLEMENTATION:

- When filling out a VSW Grant Offer Request Form for construction projects which will use a force account labor force and/or where the grantee will hire an on-site superintendent, VSW engineers will indicate that a special grant condition relating to nepotism applies.
- Upon receipt of a Grant Offer Request Form which indicates this special grant condition is applicable, the grants administrator will ensure that the following condition is contained in the Grant Offer and a copy of this field directive is attached to the Grant Offer: *"The grantee agrees to comply with the established VSW Field Directive - Nepotism on Force Account Projects (copy attached)."*
- VSW engineers will ensure all superintendent employee contracts contain the following clause: *"the superintendent may not hire nor supervise any relative on the VSW project that is related by blood or marriage, within and including the first degree of kindred (husband, wife, son, daughter, father, mother, sister, brother)."*



STATE OF ALASKA POSITION DESCRIPTION

POSITION CONTROL
NUMBER (PCN)
18-7131
(Six Digits)

To the Employee/Supervisor:

This form provides a complete and accurate description of functions assigned to this position. It is primarily used to classify the position and as a basis for establishing selection criteria for refilling the position. Extra sheets of paper may be attached if more space is needed.

Please use black ink or type.

1. Name (last, first, middle) Vacant	2. Current Job Class Title Environmental Conservation Manger II
3. Department Environmental Conservation	4. Division Water
5. Region/Section/Unit Administration Section	6. Work Phone: Fax: E-mail Address:
7. Work Address (Street/City) 555 Cordova Street, 4 th Floor Anchorage, AK 99501	8. Name/Title of Supervisor Thomas V. Cherian, Administrative Manger IV PCN:18-7047 Work Phone: (907) 465-5137
Position Status Code: <input checked="" type="checkbox"/> Full Time = FACL <input type="checkbox"/> Part Time = PACL <input type="checkbox"/> Seasonal = SACL <input type="checkbox"/>	

9. Requested Action:
<input type="checkbox"/> Updated PDQ <input checked="" type="checkbox"/> New Position <input type="checkbox"/> Flexible Staffing
<input type="checkbox"/> Reclassification to: Procurement Specialist IV
Other _____
Reason for Request: Meet federal and state requirements
10. Organization Code: 48531 18-88-01-01
Delegated <input type="checkbox"/> Nondelegated <input type="checkbox"/>

FOR PERSONNEL USE ONLY

Final Classification Action

Class Title	Code	Range	FLSA	BU	Position Type	Loc. Code
Approved by	Review Date		Effective Date		Input Date	

DUTIES AND RESPONSIBILITIES

List all duties of the position in the format described below:

Examples of Good and Poor Duty Statements

- | | | |
|---|-------------------------------------|---|
| <p>Poor Statement</p> <ul style="list-style-type: none"> ◆ Assist in handling correspondence. ◆ I administer all nutritional programs in the district. | <p>Should be written as:</p> | <p>Good Statement</p> <ul style="list-style-type: none"> ◆ Receive, open, time stamp, and route incoming mail. ◆ I plan and schedule field visits for nutritionists within the district; review individual nutrition plans for adequacy and for conformance with program guidelines; maintain activity and statistical records; meet with other health administrators within the district to help coordinate services. |
|---|-------------------------------------|---|

Define Essential and Marginal Duties

Supervisors must determine essential and marginal functions/duties of the position. Essential functions are the fundamental duties of the position. Marginal functions are those duties that could reasonably be assigned to another position. A duty may be considered an essential function for several reasons, including but not limited to:

- ◆ the function may be essential because it is the reason the position exists;
- ◆ the function may be essential because of the limited number of employees available who could perform the function; and/or
- ◆ the function may be essential because it is highly specialized and requires specific expertise or ability.

For example, an essential function of a Mail Clerk Carrier is mail delivery which typically requires lifting/carrying heavy containers. The Mail Clerk Carrier is also assigned to cover office telephones during the noon hour. The telephone reception task is a marginal function as it can be assigned to another position.

The supervisor must mark each duty/function as essential (E) or marginal (M).

Rate the importance of each duty:

Rating of Importance

Not all duties should be rated as "most important."

- 1. = Most Important
- 2. = Very Important
- 3. = Moderately Important
- 4. = Somewhat Important
- 5. = Least Important

Calculate Percentage of Time for Each Duty

Determine the percentage of time spent on each duty by thinking of the job in a time block of a week. Estimate how much time is spent performing each duty. For example, if you spend one day each week processing applications, divide the time spent on the duty by the time block: 1 day divided by 5 days equals 20 percent. Similarly, 5 hours/week divided by 37.5=13 percent. The total time spent on duties must equal 100 percent. If the work changes seasonally, prepare two sections of #13, e.g., one for the summer season and one for winter.

12. In one or two sentences, state the main purpose of the position.

The Procurement Specialist IV is responsible for administering and managing the procurement program for the Division of Water, with distinct responsibility for procurement within the Village Safe Water Program. The scope of complexity includes regular and recurring formal procurement of engineering and construction management services, construction materials, and transportation services throughout Alaska.

13. List all duties of the position. Begin with the most important duty. List duties in a decreasing order of importance with the least important duty last. Describe each task in detail (see previous page). List the percentage of time spent at each duty and rate the importance of each duty (see previous page).

*The supervisor must define each duty/function as essential (E) or marginal (M).

Essential = E

Marginal = M

Importance = IMP

Percent of Time = %/T

*E/	IM	%/	DUTIES/FUNCTIONS/TASKS
			<p><u>General Information</u></p> <p>The Procurement Specialist IV manages advanced level work, including supervising and directing all engineering and construction related contracts for the Division of Water, and in particular the Village Safe Water (VSW) Program. The VSW program presently administers over \$80 million of state and federal water, sewer, and solid waste construction funding annually. Projects funding levels range between \$100,000 and \$3 million, with the majority being over \$1 million. The majority of contract transactions range between \$100,000 and \$750,000, of which over one hundred may in active status (between solicitation and close out) at any one time, with several hundred occurring over the course of a year.</p>
E	1	5	<p><u>Compliance with Federal Regulations</u></p> <p>The Procurement Specialist IV establishes accounting control procedures for procurement, and maintains and develops the VSW Procurement Manual, a unique set of standards authorized by separate federal review, which meets or exceeds those procurement standards referenced in 40 CFR 31 (EPA Uniform Administrative Requirements for Grants and Cooperative Agreements to state and local governments). VSW contracts and procurement are also subject to the provisions of the existing MOU between US Department of Agriculture and the ADEC.</p>

*E/	IM	%I	DUTIES/FUNCTIONS/TASKS
E	1	15	<p><u>Consultant & Trainer</u></p> <p>The Procurement Specialist IV is expected to be the in-house expert on all construction contracts and acquisitions, providing guidance and assistance to the Division Director, Section and Program Managers, Project Engineers, federal program and grant managers, and contract staff.</p> <p>The Procurement Specialist IV is provides training to those individuals on a scheduled and as-needed basis. Analyze and provide technical feasibility analysis on projects.</p>
E	1	40	<p><u>Procurement and Contract Administration</u></p> <p>The Procurement Specialist IV is responsible for managing and administering all the Division's construction contracts and acquisitions. This includes preparing Professional Services Contract Approval Request (PASCAR), Request For Proposals (RFP), overseeing proposal evaluation committees, pre-proposal conferences, and Requests for Alternate Procurement documents if necessary. The Procurement Specialist IV is expected to have thorough knowledge of applicable statutes, regulations, and other legal authority applicable to establish grants and contracts.</p>
E	2	10	<p><u>Compliance Monitor</u></p> <p>This Procurement Specialist IV monitors, reviews, and audits data from contractors and AKSAS to ensure that all payments are made in accordance with applicable State laws and regulations governing procurement. This position also ensures that Federal Program requirements, and in particular those procurement standards referenced in 40 CFR 31 (EPA Uniform Administrative Requirements for Grants and Cooperative Agreements to state and local governments), are satisfied and the appropriate audit trail is available for review.</p> <p>The Procurement Specialist IV serves as the central contact for the VSW Program for completion of the Annual Single Audit of federal grant funds.</p>
E	2	5	<p><u>Resolution of Disputes</u></p> <p>The Procurement Specialist IV is expected to review construction related protests, claims, appeals, prepare findings of fact, and advise the senior management on resolutions.</p>
M	3	5	<p><u>Contracts Closure</u></p> <p>Responsible for working with state and federal program mangers, DIAS staff and contract staff to ensure the successful completion of the projects. Responsible for ensuring that the contractors and the state meet all necessary contract terms and conditions to meet both federal and state.</p> <p>Responsible for review all contracts for year-end close out, extending if necessary or establishing new contracts.</p>
E	2	10	<p><u>Supervision of Procurement Staff</u></p> <p>Manage the work of procurement staff who independently perform formal procurements; assign projects, provide options or recommendations to resolve issues, review proposals or contracts, and approve procurements.</p>

*E/	IM	%/	DUTIES/FUNCTIONS/TASKS
E	2	5	<p><u>Division Contracts</u></p> <p>Responsible for providing technical guidance to the Director and Program Mangers on Division contracts for services relating to program operation. Represent the Division in negotiation with contractors and other related parties on contracts. Such contracts include, but are not limited to accounting services (totaling between \$100,000 and \$200,000 per year), data system development (over \$200,000 per year), technical writing and graphic design, and records management related services.</p> <p>With specific regard to the VSW Program contracts for accounting services, the Procurement Specialist IV is responsible for ensuring that all services meet the requirements under standards established by the American Institute of Certified Public Accountants and Government Auditing Standards, issued by the Comptroller General of the United States.</p>
M	4	5	<p><u>Other Duties</u></p> <p>Perform other duties as assigned</p>

PHYSICAL REQUIREMENTS AND POTENTIAL HAZARDS

14. The following identify the physical demands and potential hazards typically encountered by this position. The information is necessary in part to ensure compliance with the Americans with Disabilities Act and the OSHA Bloodborne Pathogens Standards. Your responses should reflect physical demands or exposure to hazards which can be *reasonably anticipated and an expectation of the job*.

Mark the box with the rating that best matches the requirement of this position according to the following scale:

NA: Not applicable, not required of this position

NE: Requirement is present, but is *not* essential to the position. (For example, a receptionist encounters aggressive/angry people, but this is not an essential assignment.)

O: Occasional up to 33 percent of the time *and* essential to the position. (For example, a lifeguard swims only occasionally, but it is essential that a lifeguard be able to swim; or a correctional officer must deal with aggressive/angry people.)

F: Frequent over 33 percent of the time.

PHYSICAL REQUIREMENTS AND POTENTIAL HAZARDS	NA	NE	O	F
Sitting				X
Walking			X	
Standing			X	
Running	X			
Bending or twisting			X	
Squatting or kneeling			X	
Reaching above shoulder level			X	
Climbing (e.g., ladders)		X		
Driving cars, light duty trucks		X		
Driving heavy duty vehicles	X			
Using foot controls to operate equipment (e.g., not driving a car)	X			
Repetitive motion of hands/fingers				X
Grasping with hand, gripping				X
Lifting/carrying 10-25 pounds			X	
Lifting/carrying 26-50 pounds		X		
Lifting/carrying more than 50 pounds	X			
Pushing/Pulling				X
Work in/exposure to inclement weather	X			
Work in/exposure to cold water	X			
Exposure to dust, chemicals or fumes	X			
Work/live in remote field site	X			
Use of hazardous equipment (e.g., guns, chainsaws, explosives) guns, chainsaws, explosives)	X			

Swimming, scuba diving	X			
Work at heights (e.g., towers, poles)	X			
Exposure to infection, germs, or contagious diseases	X			
Exposure to blood, body fluid, or materials potentially contaminated by blood or body	X			
Exposure to needles or sharp implements	X			
Use of hot equipment (e.g., kitchen ovens and lab equipment)	X			
Exposure to electrical current (not outlets)	X			
Seeing objects at a distance	X			
Seeing objects peripherally	X			
Seeing close work (e.g., typed print)				X
Distinguishing colors				X
Hearing conversations or sounds				X
Hearing via radio or telephone				X
Communicating through speech				X
Communicating by writing/reading				X
Distinguishing odors by smell	X			
Distinguishing tastes	X			
Exposure to wild/dangerous animals	X			
Exposure to insect bites or stings	X			
Work/travel in boat/small aircraft	X			
Exposure to aggressive/angry people (e.g., correctional institutions, law			X	
Restraining/grappling with people (e.g., correctional institutions, law	X			
Other:				
Other:				

Items checked above must be consistent with tasks listed in #13. Provide further explanation if needed.

Are there any other physical or mental requirements of this position that have not been addressed above?

None

15. List machinery, tools, equipment, instruments, vehicles, computer hardware/software, etc., used in performing this job.

Must be proficient in the use of personal computer, networked computer systems, and the internet. Working knowledge of MS Word, Excel, and PowerPoint.

16. List the laws, rules, regulations, standards, codes, or other regulatory guides you regularly use in performing your work. Examples are statutes, federal regulations, professional standards, building codes, trade practices, and procedure manuals:

- EPA Uniform Administrative Requirements for Grants and Cooperative Agreements to state and local governments (40 CFR 31),
- MOU between the US Department of Agriculture – Rural Development and the ADEC.

- MOU between the US EPA and the ADEC.
- American Institute of Certified Public Accountants and Government Auditing Standards, issued by the Comptroller General of the United States.
- All applicable Ethics Act provisions and Conflict of Interest policies
- VSW Procurement and meet the requirements under standards established by the American Institute of Certified Public Accountants and Government Auditing Standards, issued by the Comptroller General of the United States.
- Procedures Manual,
- VSW Superintendent Manual,
- USDA Rural Development regulations,
- Alaska Native Tribal Health Consortium Department Operating Guidelines,
- State of Alaska administrative codes and procedures.

17. List actions you take or decisions you make on a regular basis without higher level approval:

- Negotiate contract conditions, develop procedures, forms, and Negotiate, develop, and manage contracts;
- Expert consultant to Director and the managers on contract development, management, and related issues;
- Division Procurement Officer for construction contracts who routinely provides technical supervision to program managers.

18. List other critical requirements of the job (e.g., skills in writing, negotiating, communications, etc.):

- Knowledge of professional procurement codes, procedures and practical application in public administration and financial management;
- Familiarity with governmental budgeting and reporting principles and practice;
- Comprehensive listening skills and the ability to communicate to mixed audiences at various comprehension levels or in a culturally appropriate manner.
- Must possess acute business acumen, sound judgment, reliable character, reputation, and ethics and be able to arrive at sound decisions regarding contractual matters.
- Strong verbal communication and writing skills.

19. Employee's comments--Note any other aspects of the job not covered:

20. **Employee Certification.** I certify that the above statements are accurate and complete to the best of my knowledge.

Signed _____ Date _____

THE FOLLOWING SECTIONS MUST BE COMPLETED BY THE SUPERVISOR AND/OR THE DIVISION DIRECTOR OR DESIGNEE.

21. Review Sections 1-19 for accuracy and completeness. Note any additions or exceptions below:

SUPERVISORY RESPONSES SHOULD BE CONSISTENT WITH THE ORGANIZATION CHART AND INFORMATION PROVIDED IN SECTIONS 12, 13, AND 17.

22. **SUPERVISORY RESPONSIBILITIES.** Complete this section if the position is responsible for supervising other positions.

Level Definition of Authority

- 1. = Employee effectively takes action.
- 2. = Employee discusses decision with me and then takes action.
- 3. = Employee presents recommendations to me, I make decision and direct employee to take action.
- 4. = No authority.

Rate position's level of authority according to the above definitions.

List Positions Directly Supervised	Rate Level of Authority					
	Appoint	Promote	Transfer	Take Disciplinary Action	Discharge	Settle Grievances
PCNs						

23. List the most important purpose, service, or product expected of this position.

Establishing procurement control procedures for VSW Program (which administers over \$80 million in construction project funds annually) and ensuring compliance with federal regulations.

24. List specific or specialized training, education, experience and/or skills needed to perform the duties of this position.

- Thorough and demonstrated knowledge of contract law, procurement principles, methods, and techniques, regulations, practices, property accountability, solicitation, award and administration of major contracts, and protest and disputes resolution, with special emphasis on contracts associated with federal assistance funding.
- Extensive knowledge of current contract and bidding developments and case decisions.
- Demonstrated ability to render comprehensive contract management advisory opinions, recommendations, and guidance.
- Expert knowledge of contractual claims analysis and investigative techniques to research entitlement principles, prepare studies and serve as a consultant in the application of a variety of claims settlement, negotiation, and resolution regarding contractual issues.
- Working knowledge of federal and state policies and directives governing contracting, procurement, and property management administration for grants or other assistance funds.

25. List licenses, certifications, registrations, physical or other standards required by state or federal law or regulation. Please cite the specific law or regulation.

26. List other positions you supervise that perform work similar to this position.

PCN	JOB CLASS TITLE

27. Attach a current dated organization chart for the unit/section that shows the PCNs, job class titles, and locations of positions.

28. Supervisor Certification. I certify that the above statements are accurate and complete to the best of my knowledge.

Signed [Signature] Date 6/25/04

29. Division Director (or designee) Certification. I certify that the above statements are accurate and complete to the best of my knowledge.

Signed [Signature] Date 6/25/04

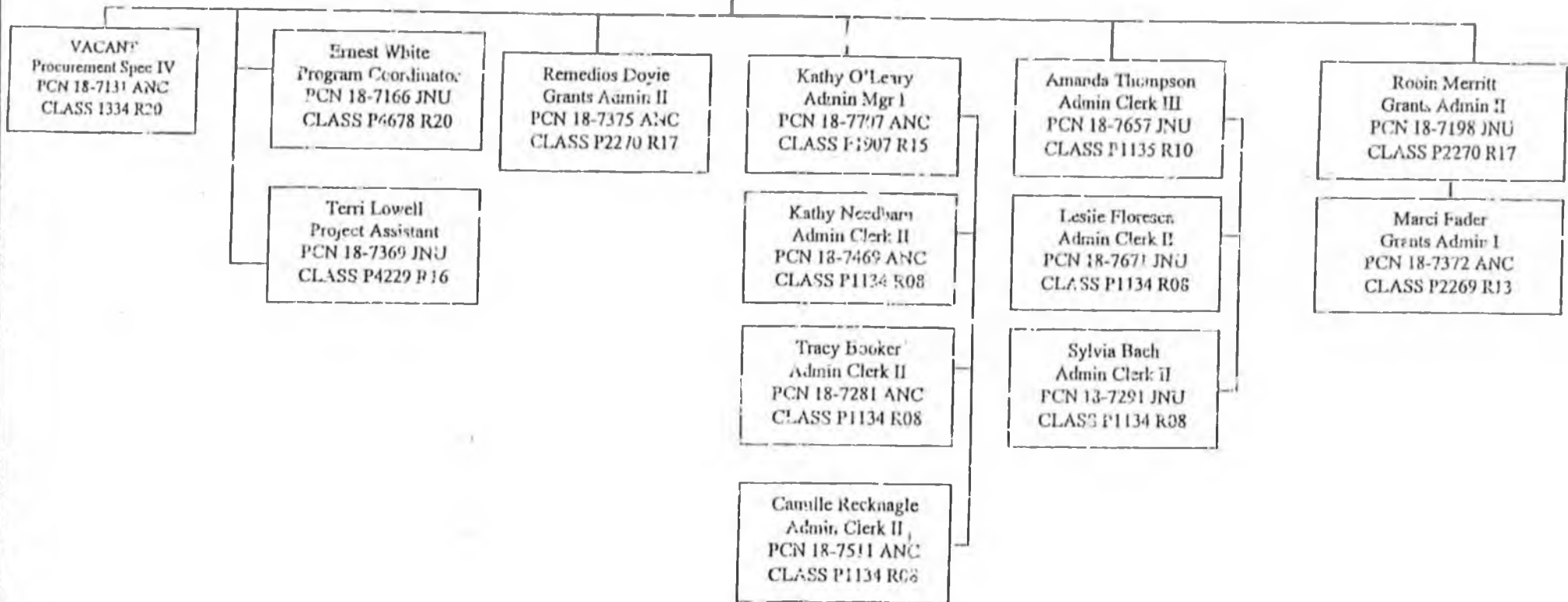
30. Human Resources Manager or Department Certification.

Signed _____ Date _____

STATE OF ALASKA
DEPARTMENT OF ENVIRONMENTAL
CONSERVATION
DIVISION OF WATER

ADMINISTRATIVE UNIT

Submitted by: Don Easton
Dan Easton, Director
Effective 05-26-04



STATE OF ALASKA

FRANK H. MURKOWSKI, GOVERNOR

DEPARTMENT OF ENVIRONMENTAL CONSERVATION

410 Willoughby Ave., Ste 303

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OFFICE OF THE COMMISSIONER

September 7, 2004

Pat Davidson
Legislative Auditor
Division of Legislative Audit
Legislative Budget and Audit Committee
Alaska State Legislature

Dear Ms. Davidson:

RE: Statewide Single Audit for Fiscal Year Ending, June 30, 2003, Department of Environmental Conservation (DEC)

We have reviewed the findings and recommendations in the above referenced report, and appreciate this opportunity to respond. The report provides DEC with a good opportunity to review our current procedures and we believe the information in this letter will help to clarify a number of issues, and inform you about our intended actions. We have responded to the recommendations included in the report and offer our suggestions and solutions.

Recommendation No. 32

The Department of Environmental Conservation (DEC) Finance Officer and Village Safe Water (VSW) Program Manager should work with the State's cash manager to establish VSW disbursement procedures which maximize conservation of the State's general fund (GF).

This recommendation centers on the prescribed practice of advancing project funding to either the VSW accounting firm or the Alaska Native Tribal Health Consortium (ANTHC). We will review our policies and procedures and look at ways to improve our cash management practices regarding the advancement of funding for VSW projects.

While it is true that VSW procedures for advances were originally established over a decade ago, it is not accurate to say that communication technology has significantly reduced the handicap of construction activities and associated requests for project funding in rural Alaska. If anything, the handicap has grown larger because of the complexities entailed with managing multiple state and federal sources of project funding, which was not the case a decade ago.

Contrary to your recommendation, there is a great deal more required in making an advance than the transfer and receipt of funding, which admittedly requires little time. In particular, each request for a transfer of funds requires that the VSW Program Manager and Grant Manager each confirm that a



number of grant requirements are being met. These grant requirements have been established to ensure program compliance with the multiple federal funding sources, and to promote continued safe, sustainable operation of rural sanitation facilities. For example, the VSW Program Manager works closely with the Manager for the Department of Community and Economic Development's Rural Utility Business Advisor (RUBA) program in reviewing requests for most advances. The RUBA program provides information about Essential Capacity Indicators (ECIs) for every community that receives a VSW grant, and notifies VSW about concerns. Requests for funding advances may be denied if ECIs are not being adequately addressed by the grantee.

Because of the attention and time required to adequately review each request for a funding advance, and the continuing demands of rural construction management in Alaska, we do not agree with your recommendation to advance funds on a semimonthly basis. This is because of the increased risk associated with the advancement of funds for projects where sustainability is in question.

We acknowledge that in most cases there is no need to provide advances for an entire construction season, and that the VSW procedures need to be reviewed, and revised to reflect a consistent process entailing more frequent advances. It is our intent at this time to review this process in attempt to identify ways to that may reduce the period of time for which advances are now issued.

Recommendation No. 33

The DEC Finance Officer and the VSW Program Manager should revise the accounting procedures for VSW grants administered by the ANTHC to allow proper financial statement presentation in the State's Comprehensive Annual Financial Report.

The Department supports this recommendation and will work with ANTHC to develop a yearend report which reflects actual expenditures of VSW funding and actual balances remaining.

Recommendation No. 34

The DEC Finance Officer should implement procedures to ensure personal services expenditures charged to the EPA Infrastructure Grants comply with federal cost principles.

The Department supports this recommendation. Steps are being taken to ensure that those employees funded 100% by a federal grant will complete bi-annual certifications. Additionally, for those funded by multiply funding sources, actual hours worked on a particular project will be reflected on the employee timesheet.

Recommendation No. 35


The VSW Program Manager should work with project engineers to strengthen internal controls over the VSW procurement process.

The Department supports this recommendation. The Division of Water has created a procurement specialist position to support the VSW program to provide the kind of support and guidance needed

to strengthen both internal controls and provide training and oversight for project engineers and superintendents. We share your interest in achieving practices which are fully consistent with procurement policies.

Thank you for providing this opportunity to comment on your findings and recommendations. If you have any questions or need additional information regarding the audit response, please contact Gary Zepp at (907) 465-5289.

Sincerely,



Ernesta Ballard
Commissioner

Enclosure

cc: Mike Maher, Director, Division of Administrative Services/ADEC
Dan Easton, Director, Division of Water/ADEC

Personal Services Cost

Payroll through: 12/31/2005 % of Year: 50.00%

Village Safe Water

PCN	Name	YTD Expense	Projected Exp	Total Cost	Authorization	% of Auth Expensed	% of Auth Remain
187070	Greg MaGee	\$52,359.58	\$62,540.01	\$114,899.59			
187127	Vacant		\$42,051.71	\$42,051.71			
187198	Robin Merritt	\$44,530.81	\$51,908.28	\$96,439.09			
187281	Tracy Booker	\$23,166.45	\$26,503.30	\$49,669.75			
187284	Doug Poage	\$55,771.50	\$54,911.96	\$120,683.46			
187285	Lynn Marino	\$53,541.56	\$62,344.01	\$115,885.57			
187291	Sylvia Bach	\$25,486.20	\$29,174.36	\$54,660.56			
187315	Jim Patterson	\$59,029.20	\$68,823.11	\$127,852.31			
187370	Debra Addie	\$48,489.80	\$57,536.34	\$106,026.14			
187371	Vacant		\$47,336.72	\$47,336.72			
187372	Marcie Fader	\$38,899.29	\$37,407.67	\$76,306.96			
187386	Tim Law	\$49,932.32	\$58,132.23	\$108,064.55			
187392	Roger Burleigh	\$51,621.44	\$58,132.23	\$109,753.67			
187411	Marie Steele	\$41,287.01	\$50,186.67	\$91,473.68			
187469	Rosemary Ritter			\$0.00			
187469	Vivian Terrell	\$11,712.34	\$28,451.36	\$40,163.70			
187510	Raymond O'Neill	\$41,478.23	\$50,186.67	\$91,664.90			
187629	George Wilson	\$52,127.63	\$60,713.22	\$112,845.85			
187642	Ken Hunt	\$9,071.47	\$0.00	\$9,071.47			
187642	Vacant		\$47,336.72	\$47,336.72			
187661	Lon Tefler	\$48,525.40	\$56,571.15	\$105,097.55			
18N611	Vacant		\$29,840.25	\$29,840.25			
18N612	Vacant		\$29,840.25	\$29,840.25			
18N772	Vacant		\$29,840.25	\$29,840.25			
18N869	Lyudmila Umans	\$8,067.35	\$23,891.26	\$31,958.61			
	Charge to Other Programs	(\$481,238.01)	(\$531,444.87)	(\$1,012,682.88)			
	Charges from Other Programs	\$163,429.05	\$36,428.93	\$199,857.98			
	Grand Total:	\$397,289.62	\$573,648.79	\$975,938.41	\$1,666,100.00	24%	76%

STATE OF ALASKA

FRANK H. MURKOWSKI, GOVERNOR

DEPT. OF ENVIRONMENTAL CONSERVATION OFFICE OF THE COMMISSIONER

410 Willoughby Ave., Ste 303
Juneau, AK 99801-1795
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<http://www.state.ak.us/dec/>

April 15, 2005

Reese Jensen
Senior Auditor
Division of Legislative Audit
Legislative Budget and Audit Committee
Alaska State Legislature

Dear Mr. Jensen:

RE: Management Letter No. 1, FY 04 Statewide Single Audit, Department of Environmental Conservation (DEC)

We have reviewed the findings and recommendations in the above referenced report, and appreciate this opportunity to respond. The report provides DEC with a good opportunity to review our current procedures and we believe the information in this letter will help to clarify a number of issues, and inform you about our intended actions. We have responded to the recommendations included in the report and offer our suggestions and solutions.

Recommendation No. 1

The DEC finance officer should implement procedures to ensure personal services expenditures charged to the EPA infrastructure grants comply with federal cost principles.

The Department supports this recommendation, and has implemented processes to ensure the requirements of OMB Circular A-87 are met. Those employees solely dedicated to a particular federal grant are required to complete bi-annual certifications. Additionally, for those employees whose salaries are chargeable to more than one cost objective, actual hours worked on each cost objective are reflected on the employee timesheet.

Recommendation No. 2

The VSW program manager should work with project engineers to strength internal controls over the VSW procurement process.

The Department supports this recommendation, and hired a Procurement Specialist III in September 2004 to support the VSW program. This position is solely dedicated to the VSW

program, and is supervised by the Division of Information and Administrative Service to ensure appropriate segregation of duties and authorities. The incumbent has been working to strengthen internal controls and to provide appropriate oversight and guidance for VSW procurement practices.

Recommendation No. 3

The DEC finance officer and Division of Water facility programs manager should implement procedures to ensure compliance with EPA grant requirements for small and disadvantaged business utilization.

The Department supports this recommendation. The VSW Procurement Specialist is working to update bid documents and agreements to include Minority Business Enterprise/Women's Business Enterprise (MBE/WBE) "fair share" objectives, and to require reporting of actual MBE/WBE procurements.

Recommendation No. 4

The DEC finance officer and Division of Water facility programs manager should improve oversight of funds passed through to ANTHC.

The Department disagrees with this recommendation, in that the Indian Health Service (IHS), a federal agency, not the Department, is responsible for oversight of the Alaska Native Tribal Health Consortium (ANTHC). The IHS contracts with the ANTHC to manage IHS projects, and is the cognizant federal agency for the ANTHC. All agreements related to IHS projects funded by EPA and USDA monies granted to the state are between the Department and the IHS. The ANTHC is not a party, and is in no way a subrecipient of the Department subject to its oversight. As questions frequently arise due to the unique nature of the relationship between the Department, the IHS, and the ANTHC, a legal review is underway to confirm relationships and responsibilities to the satisfaction of all interested parties, and put the matter to rest.

Thank you for providing this opportunity to comment on your findings and recommendations. If you have any questions or need additional information regarding the audit response, please contact Joanna McDowell at (907) 465-5289.

Sincerely,



Kurt Fredriksson
Commissioner

cc: Mike Maher, Director, Division of Information and Administrative Services, DEC
Dan Easton, Director, Division of Water, DEC

Bcc: Joanna McDowell, Finance Officer, Division of Information and Administrative Services,
DEC
Bill Griffith, Facility Programs Manager, Division of Water, DEC

For DEC
Hearing

January 9, 2004

Members of the Legislative Budget
and Audit Committee:

In accordance with the provisions of Title 24 of the Alaska Statutes, the attached report is submitted for your review.

DEPARTMENT OF ENVIRONMENTAL CONSERVATION
VILLAGE SAFE WATER PROGRAM
SELECTED PROJECTS

November 19, 2003

Audit Control Number

18-30028-04

We reviewed the Department of Environmental Conservation spending practices in the construction of water and sewer systems through the Village Safe Water program. We found that the procedures over spending lacked some normal business safeguards and that this small program did not have the necessary business support. We recommend transferring this program to the Department of Transportation and Public Facilities, where this support is readily available.

The audit was conducted in accordance with generally accepted government audit standards. Fieldwork procedures utilized in the course of developing the findings and discussion presented in this report are discussed in the Objectives, Scope, and Methodology section.

Pat Davidson, CPA
Legislative Auditor

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OBJECTIVES, SCOPE, AND METHODOLOGY

In accordance with Title 24 of the Alaska Statutes and a special request by the Legislative Budget and Audit Committee, we conducted an audit of the Village Safe Water Program (VSW) administered by the Department of Environmental Conservation (DEC).

Objectives

The objectives of the audit were as follows:

- To evaluate DEC oversight over engineering firm billings.
- To evaluate DEC oversight over project payrolls.
- To evaluate DEC purchasing practices in project communities.

Scope and Methodology

The audit request asked us for a review of DEC spending practices in the construction of water and sewer systems through the VSW program. To enhance our understanding of the audit request, we were provided examples of possible waste on particular projects.

Our audits are conducted under standards issued by Congress, known as the *Government Audit Standards*. These standards direct us to assess the ability of program processes to accomplish program objectives, meet legal requirements, and control waste, fraud, and abuse.¹ These standards also encourage us to "make recommendations for actions to correct problems identified during the audit and to improve programs and operations."²

The VSW program had 35 projects with active construction during the 2002 construction season. We reviewed selected aspects of 20 of these projects. Each of the 20 projects was located in a different community.

Fieldwork for the audit included the following:

- Review of statutes, regulations, ordinances, grant agreements, contracts, and written policies and procedures.

¹ *Government Audit Standards* (2003) §§ 2.09-2.11, 7.12-7.13, 7.17-7.25. For the purpose of the *Government Audit Standards*, "abuse" is defined to occur when "conduct of a government program or entity falls far short of behavior that is expected to be reasonable and necessary business practices by a prudent person." *Government Audit Standards* (2003) § 7.25.

² *Government Audit Standards* (2003) §§ 8.28-8.29.

- Interviews with state and federal agencies.³
- Review of project files.
- Review of records of project accounting, payroll, personnel, and expenditures.
- Review of prior evaluations, studies, and audits of the VSW program by various entities.

³ In addition to past and present DEC personnel, we interviewed employees of the following: U.S. Environmental Protection Agency, U.S. Department of Agriculture, Denali Commission, State Department of Community and Economic Development, State Department of Transportation and Public Facilities, Alaska Industrial Development and Export Authority, State Department of Labor and Workforce Development, Internal Revenue Service, U.S. Citizenship and Immigration Service, and local tax officials.

ORGANIZATION AND FUNCTION

In 1970, the Village Safe Water Act established under Alaska Statute 46.07 created the Village Safe Water (VSW) program. The Act established "a program designed to provide safe water and hygienic sewage disposal facilities in villages in the state." An eligible "village" is defined as "an unincorporated community that ~~has a population of less than 1,000 people~~ ~~with a population of less than 1,000 people~~, a second class city, or a first class city with no more than 600 residents."⁴

The VSW program was originally administered by the State Department of Health and Welfare but was later transferred to the Department of Environmental Conservation (DEC). The program is currently administered as a separate section within the DEC Division of Facility Construction and Operation.

All of VSW's field engineers and its grants administrator are stationed in its Anchorage office. The field engineering staff consists of eight engineers, three engineering associates, one engineering assistant and one graduate intern. The VSW program manager and a planner work out of DEC's Juneau office.

The majority of VSW's funding is through federal grants from the U.S. Environmental Protection Agency and the U.S. Department of Agriculture. The balance is Alaska legislative appropriations for capital budgets from state funds.

For FY 04, the program has a project budget of \$81 million. DEC engineers are directly administering 43% of this budget while 57% is being forwarded to the Alaska Native Tribal Health Consortium.

For most VSW projects, the community provides the workforce. This is termed a "force account" arrangement in the public construction field. DEC engineers may directly oversee a project or may delegate day-to-day oversight to a construction management firm.

~~Once the State has appropriated funds for a specific project, those funds technically belong to the State of Alaska. However, DEC has hired an Anchorage CPA firm to manage a bank account that holds the grant funds "in trust" for each project community. The CPA firm issues checks for project expenditures, as directed by DEC.~~

⁴ AS 46.07.080(2).

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BACKGROUND INFORMATION

Project Selection

The Village Safe Water (VSW) enabling statute (AS 46.07) authorizes the program to construct water and sewer systems in the state's "villages." The statute defines a "village" as "an *unincorporated community that has between 25 and 600 people residing within a two-mile radius, a second class city, or a first class city with not more than 600 residents.*"⁵ Though the Department of Environmental Conservation (DEC) has a tradition of constructing projects in communities in bush Alaska, that is, communities off the road system, the statute is silent as to any priority among eligible locations.

In fact, statutes, regulations, and federal grant conditions are all silent as to DEC's selection criteria when applicant requests exceed available funds. However, DEC has developed a ranking system to prioritize requests, which is publicly described on its homepage.⁶

DEC has separate ranking processes for projects in the planning and construction phases. In each process, applications receive weighted points in specific categories (see Exhibit 1). Scoring and ranking is conducted by the VSW program management in Juneau, rather than by the Anchorage-based engineers that supervise completion of the selected projects.

EXHIBIT 1
PLANNING SCORING CATEGORIES
Plan information Community development status Council resolution
CONSTRUCTION SCORING CATEGORIES
Public health and environmental threats Project development status Other funds Operation and maintenance capabilities Project coordination Economic feasibility

Project Construction

Alaska Statute 46.07.040 authorizes VSW "to provide for the construction by contract or through grants to public agencies or private nonprofit organizations, or otherwise." The statute further provides that "workers from the village in which the facility is being constructed shall be utilized to the maximum extent feasible."

Under the VSW enabling statute, DEC has several options to construct a project. First, DEC may contract for construction by a contractor using the traditional competitive bidding process of AS 36.30. Second, DEC may transfer funding to the Alaska Native Tribal Health

⁵ AS 46.07.080(2).

⁶ See www.state.ak.us/dec/dfco.

Consortium, with construction under consortium procedures. Third, DEC can arrange for the community to provide its own construction workforce. Workers under the latter "force account" arrangement are technically employees of the local government or a local organization. However, DEC still oversees the project and pays all the bills.

VSW projects are funded from three sources: (1) grants from the U.S. Environmental Protection Agency; (2) grants from the U.S. Department of Agriculture; and (3) state capital project funds. Federal grantors leave the method of construction to DEC's discretion, so long as there is compliance with federal grant conditions and regulations. Federal grantors have agreed that the written procedures in DEC's manual for the VSW program are an acceptable approach to the federal requirements.

REPORT CONCLUSIONS

The audit request asked us for a review of Department of Environmental Conservation (DEC) spending practices in the construction of water and sewer systems through the Village Safe Water (VSW) program. To enhance our understanding of the audit request, we were provided examples of possible waste on particular projects.

The concerns reflected in the audit request were well-founded. As we detail below, DEC procedures for spending lack some normal business safeguards that the public has a right to expect for construction projects.

In essence, approximately \$35 million⁷ in public construction is being monitored by a dozen engineers⁸ buried within a regulatory agency. Though well-meaning and exemplary in dedication, these DEC employees suffer from a lack of the usual business support services that enable other state engineers to focus on engineering. In short, there is a mismatch between their professional training and the tasks that consume much of their time.

Our recommended solution is to transfer VSW construction to the Department of Transportation and Public Facilities (DOTPF) with its support services, economies of scale, training opportunities, career paths, and business discipline (see Recommendation No. 1).

~~A common trend in our findings is the considerable ambiguity that the program has~~
assumed in accountability for how project funds are actually spent. This is not surprising given that awarded funds are kept by DEC "in trust" for the recipients and jointly controlled by various parties with procedures that fluctuate considerably in practice.

While local hire is desirable, a community's capacity to assume substantial control needs to be carefully evaluated on a case-by-case basis rather than presumed as the norm. When such delegation and transfer of project responsibility is truly deemed feasible, oversight and accountability need to be documented by agreement in no uncertain terms.

Our detailed conclusions follow.

⁷ The VSW program has an FY 04 capital budget of \$81 million. The VSW engineers are administering \$35 million of these projects while \$46 million has been transferred to the Alaska Native Tribal Health Consortium.

⁸ The 11 DEC engineers who work directly with VSW communities are stationed in Anchorage. They had an office supervisor during the 2002 construction season, but that position is now vacant. The program manager is in Juneau.

Unskilled oversight of construction management firms and other engineers allows waste

DEC commonly contracts with engineering firms to monitor day-to-day spending and perform other tasks, such as design work, on VSW projects. Information provided with the audit request relayed concerns about billing practices under 24 of these contracts, with those contracts involving 22 different communities.⁹ Construction management, that is, the critical delegated control over VSW spending, was the subject of 11 of the contracts in question.

In larger agencies, the drafting of construction management contracts can be entrusted to experienced contracting officers whose business savvy protects the public from exploitive billing. However,

[REDACTED]

Exhibit 2 shows the various deficiencies that were spread among the 24 contracts we reviewed. The disparity in business negotiating skills indeed leaves the state open to exploitive billing.

Most VSW engineers recognize that they are not contract experts and would welcome professional help in ensuring communities get fair value for project money. In Recommendation No. 1, we propose a reorganization in which these well-meaning engineers will get the business support they need so they can refocus on engineering.

EXHIBIT 2

CONTRACTS ALLOWED WASTEFUL SPENDING

- Missing standard contract terms. Travel time, overtime, and holiday pay not addressed in most contracts.
- Lack of standardization between contracts. Labor rates and contract fees varied considerably between contracts.
- Contractors dictate rates and fees with little scrutiny by engineers.
- Contractors inflate pricing on pass through expenses.
- Questionable services and rental charges were allowed.
- Missing fee schedules in contract files.
- Contractors dictate contract changes.
- Uncertainty of cumulative dollars authorized and spent under amended contracts.
- Billings did not agree with contract terms.
- Engineers unaware of federal grant requirements.
- VSW skills are outmatched by contractor's business savvy.

⁹ We note that one of these communities had a 2000 census population of only 22 persons and, per the state demographer, an estimated 2002 population of only 2 persons. This reflects the need for VSW to carefully prioritize its allocation of limited project funding. Recent media coverage highlighted generalized federal concern about grants for public works projects in the State's "phantom" villages." See Liz Ruskin, "Stevens vows to examine funding," *Anchorage Daily News*, October 23, 2003, pp. A-1, A-10.

DEC management insists that the billing provisions in question are simply the accepted norm for private engineering firms. Based on our discussions with state and federal agencies,¹⁰ we disagree.

Unskilled oversight of on-site managers allows waste

A minority¹¹ of projects are directly managed by a DEC engineer rather than by a construction management firm. While DEC oversees the project and pays all the bills, the community provides its own workforce to build the facility. This is termed a "force account" arrangement in the public construction field.

a. Overpaid on-site managers

Communities with such force account projects hire an on-site manager with the concurrence of DEC's engineer.¹² This manager is not from the community and may or may not be a resident of Alaska. DEC's engineer drafts the employment contract, under which the manager is technically a "temporary employee," rather than a contractor, and this employee works for the community, rather than DEC.

We have reviewed the compensation of the three highest-paid on-site managers during the 2002 construction season (see Exhibit 3). While DEC defends these wages, we find them excessive and wasteful. This practice offends today's public expectations for small DEC projects.

Our concerns about DEC's skills at oversight are detailed in Recommendation No. 2.

EXHIBIT 3			
THREE HIGHEST PAID ON-SITE MANAGERS			
2002 CONSTRUCTION SEASON			
<u>Gross wages</u>	<u>Per diem</u>	<u>Other direct*</u>	<u>Total</u>
\$197,078	\$5,712	\$3,200	\$205,990
\$184,918	\$4,662	\$7,700	\$197,280
\$134,758	\$8,892	—	\$143,650

* Other direct = payments made directly to manager's personal business

¹⁰ We consulted contracting specialists at DOTPF, the Denali Commission, and the Alaska Industrial Development and Export Authority. Clear, consistent billing terms that protect the state are no novelty. DOTPF has training academy courses that teach contracting skills. A veteran Public Health Service engineer at the Denali Commission also noted the availability of valuable training from the federal government.

¹¹ Out of 35 VSW projects with actual construction during the 2002 season, 22 were conducted through a construction management firm, 11 had an on-site manager who reported directly to DEC's engineer, one used both a construction management firm and an on-site manager, and one was simply run by a general contractor.

¹² DEC refers to this on-site manager as a "superintendent" in the employment contract.

b. Problems with safeguards over crew payrolls

The on-site manager supervises the local force account crew. We found DEC's loose controls over crew payrolls to fall short of normal business safeguards. Those loose controls are symptomatic of the overall ambiguity as to whether DEC or the community is accountable for how project funds are spent.

While we did not find any fraudulently-issued paychecks, such neglect of payroll safeguards is an opportunity for fraud to occur and not be detected (see Recommendation No. 3).

We do not fault the on-site manager for DEC's failure to appreciate a risk that could jeopardize public confidence. However, the shortcoming once again shows a mismatch between the professional skill set of public engineers and the business savvy needed to protect public spending.

c. Unskilled purchasing

The audit request expressed concern about purchasing practices in project communities. Given the on-site manager's broad discretion over purchasing and hiring in a community,¹³ we reviewed the application of DEC-prescribed spending procedures at three projects administered by an on-site manager.

We found problems with DEC's oversight procedures that show a lack of business skills in areas such as purchasing, risk management, and compliance with tax laws. Some of these problems simply waste public money,¹⁴ while some others discussed below invite confrontations with regulators such as the Internal Revenue Service (IRS), federal immigration authorities, and the Alaska Department of Labor and Workforce Development.

We noted particular expenditures that were wasteful,¹⁵ or at least questionable, in view of an inadequate explanation from the DEC engineer.

¹³ Some VSW engineers allow the on-site manager to choose the source for any purchase up to \$5,000 without the engineer's preapproval. At least one engineer allows the on-site manager to choose the source up to \$25,000 without preapproval. Comparison shopping is required between \$5,000 and \$50,000. Purchases over \$50,000 require competitive bidding. The on-site manager also awards jobs, sets pay rates, and rents local equipment.

¹⁴ For instance, one on-site manager ordered insurance for a rental of heavy equipment. He neglected to cancel the insurance policy at the end of the five-month rental period, resulting in a \$5,000 overpayment for an unnecessary coverage extending over 22 months. The automatically-renewing coverage would presumably still be in force today if we had not alerted DEC's engineer.

¹⁵ For instance, local ordinances exempted project purchases from the local sales taxes, which could total 5%. However, we noticed a variety of purchases in which the on-site manager did not attempt to claim the exemption. DEC approved payment even though the bills or receipts clearly included the local tax.

For example, we were unable to evaluate the pricing of some tools and office supplies, such as those in Exhibit 4. The DEC engineer lacked personal familiarity with these purchases, having entrusted them to the on-site manager. Sometimes this delegation occurred when the engineer signed open purchase orders that authorized general charging at local stores. When the engineer sought explanations for Legislative Audit, the on-site manager summarily responded with generalities such as "tools and safety equipment" and "tools that are necessary for water and sewer projects."

We recognize the value contributed to an area's economy by purchases of common hand tools and office supplies at local convenience outlets. However, we also expect that a skilled purchasing agent could negotiate bulk purchases of such items that would service numerous projects.¹⁶ Such business economies of scale are an unrealistic expectation, though, by DEC's unsupported VSW engineers.

d. Wasteful duplication of bookkeeping efforts

While DEC lacks adequate safeguards over what the money is used for, up to five different bookkeeping systems concurrently track how much is left. This redundant bookkeeping is wasteful.

Overall disbursements of grant funds are, as usual, tracked by DEC's administration through the state accounting system. However, DEC also pays an Anchorage Certified Public Accounting (CPA) firm \$159,000 a year to maintain the computerized books and separate bank accounts needed for VSW projects. The funds in each bank account are considered to be held "in trust" for the community, with the CPA firm issuing checks to vendors and force account employees as DEC authorizes.

DEC engineers have online access to the cash basis books that the CPA firm keeps for each project, which are basically check registers. However, most engineers are hesitant to fully utilize this system due to both their limited accounting background and the system's inability to reflect pending, unpaid purchases.¹⁷ Engineers thus create their own spreadsheets of

EXHIBIT 4	
UNEXPLAINED HIGH COSTS FOR COMMON HAND TOOLS AND SUPPLIES	
	<u>Cost</u>
Claw hammer	\$25
Hacksaw frame	\$29
Bolt cutter	\$140
Pliers	\$23
Wrench	\$89
Wrench	\$65
Wrench	\$56
Wrench	\$31
Grease gun	\$27
60-watt light bulb	\$2
Executive stapler	\$12
Tape refill	\$21
Post-it notes	\$11
Wastebasket	\$11

¹⁶ For instance, large hardware chains now sell over the internet.

¹⁷ Depending upon accounting background, users think of unpaid purchases as warranting an encumbrance, account payable, reserve, or some other deduction from committed funds. Regardless of terminology, a cash basis checkbook does not reflect items ordered or wages earned until the check is actually cut. There is an ever-present risk of spending over budget unless one adopts a practical solution.

pending expenses and resort to creative solutions, such as the preplanned holding of a \$60,000 check for several months. These spreadsheets in effect constitute a redundant, unofficial set of books that are not tied in to the state accounting system or to the subsidiary system operated by the CPA contractor.

The contract that DEC drafts for on-site managers requires that managers also track spending commitments under their project budgets. One on-site manager employed his spouse to act as an on-site bookkeeper (see Exhibit 6 on page 21), and purchased a \$2,700 computer system out of project funds. Like DEC's engineers, these front-line managers could conceivably use on-line access to the CPA firm's system. However, their immediate needs require that they, too, rely on their own self-designed spreadsheets to track expenses under an unofficial system.

Yet another unofficial system, tracking by the community itself, may exist at some sites. For instance, \$1,700 of a project's money was used to send an officer of a community council to Anchorage for a two-day QuickBooks course.¹⁸

All of this redundancy shows both waste and, once again, the lack of business support that diverts DEC from focusing its engineering talents on the communities' important technical problems.

Noncompliance with tax and payroll laws invites enforcement

The lack of support also surfaces in noncompliance with various tax and payroll laws routinely expected of most small businesses. Some of this noncompliance presents the possibility of enforcement actions, as well as the obvious erosion of confidence in the program by public cynicism over double standards.

DEC engineers were apparently unaware that longstanding federal tax laws require Form 1099 reporting of some payments to vendors that exceed \$600. Only one Form 1099 was filed for all of the VSW projects administered by DEC during the 2002 tax year.¹⁹ This is not a new issue²⁰ and, despite the potential for IRS penalties, DEC apparently lacks the business infrastructure to solve this problem.

¹⁸ This \$1,700 included the employee's project wages of \$660 for two 10-hour days, with overtime. Such QuickBooks training could have been obtained far more economically from the local college (\$102) or even on-site from the state's rural utility business advisor at no charge.

¹⁹ We checked three projects for completion of Form 1099 and found at least 15 vendors for which that reporting was required in 2002. However, the contract CPA firm failed to file any 1099 forms for these projects.

²⁰ DEC arranged for a private auditor to review VSW procedures back in 2001, with the auditor reporting to DEC that the necessary 1099s were not being issued.

State law provides penalties for employers that circumvent workers compensation coverage. One on-site manager initiated a recharacterization of his uninsured work. He wrote DEC: "If insurance for [this project] is not in place, and you don't want to run this through payroll, you can issue me a P.O. [purchase order] for consulting services to cover the time . . ." After being paid for one pay period of "consulting services," he worked the next month as an employee but still without workers compensation coverage.

A similar issue arose when another on-site manager was paid wages as an employee while sizeable additional payments were paid directly to his private business. Among these additional payments was \$4,662 in per diem and \$7,700 designated as a reimbursement for health insurance premiums. Whatever reason for this arrangement,²¹ the split once again blurred the important distinction between employee and consulting contractor.

State wage and hour laws forbid hourly workers from performing the same job as both an employee and a volunteer. While one on-site manager consistently claimed very long days on his timesheets (see Recommendation No. 2), he asserts that there have been many additional hours for which he has not charged the VSW program.²² Such confused boundaries invite wage claim disputes with costly penalties.²³

Long-standing federal law requires every employer to complete Form I-9 after verifying an employee's identity and citizenship status. The contracts for on-site managers make this an explicit part of their duties. Nevertheless, when a federal agent inspected the forms for three projects, the agent found errors of varying significance on every form. In fact, we noted that no Form I-9 was even provided by the manager for 11 employees on these projects.²⁴

²¹ For instance, we note that DEC did not report the \$7,700 as taxable income on the manager's W-2 form. DEC should ensure that this treatment meets IRS standards. The IRS government liaison can assist DEC in this regard.

²² On July 2, 2003, the on-site manager wrote DEC: "I have given hundreds of hours of mine and [spouse's] time without charging . . ." On July 11, 2003, he wrote DEC: "over the last ten years, [spouse] and I have given pro bono thousands of hours to various VSW projects." [Emphasis added.] He now indicates to DEC that he is continuing to work on the project free of charge, well after DEC shut the project down for exhausted funding. We have not attempted to evaluate whether such statements are accurate or hyperbole; they simply reinforce our position in Recommendation No. 2 that employees like this belong on a salary.

The same manager has also volunteered cash payments that further complicate the boundaries of his employment relationship. After a history of \$6,700 in equipment thefts at one site, he wrote that he was "personally offering a \$1,000.00 cash reward in this matter." When the DEC engineer ordered work to stop for exhausted funding, the on-site manager declined and promised that he would personally pay for any overruns, implicitly agreeing to act as a sort of guarantor.

²³ DEC can clarify such status questions by requesting an opinion letter from the Department of Labor and Workforce Development. Also, we recommend that DEC obtain advice from the Department of Law concerning the risk of continuing apparent authority to bind the state and continuing liability for workplace injuries.

²⁴ Contracts for the on-site managers also require them to obtain the usual IRS Form W-4 from every employee. Forms for six employees were incomplete on the three projects.

DEC must ensure that its on-site managers appreciate the need for careful attention to payroll tax laws. Though on-site managers technically work for the communities, we think the IRS may treat DEC as a "responsible person" for the purpose of assessing penalties.

Finally, we note that recent federal regulations clarify the IRS intent to evaluate the reasonableness of compensation that nonprofit corporations pay influential employees. Total compensation packages over \$90,000, while not automatically unreasonable, are subject to IRS review. Excessive compensation is subject to heavy penalty taxes. To the extent that the VSW program expands its awards to community councils organized as nonprofit corporations, this is another area of tax compliance that necessitates specialized business support.

Better monitoring needed for safeguards over outside employment

Some DEC employees are assigned considerable autonomous discretion on VSW projects. Given the scope of discretion, the Executive Branch Ethics Act contemplates that DEC management will carefully screen outside employment for any conflicts of interest.²⁵ Such conflicts might include significant business ties with vendors and contractors, or activities in which DEC employees must juggle loyalties to the state and private customers. In Recommendation Nos. 4 and 5, we address the need for clear rules and specific action on this and other ethical matters pertinent to this program.

This need to protect the public from potential conflicts of interest again reflects the value of specialized support skills.

The move to projects in recent road system subdivisions reflects changing priorities

VSW's enabling statute only defines eligibility as "villages" that are either incorporated cities with up to 600 people or unincorporated settlements with 25 to 600 people within a two-mile radius. Program funding for the 2002 construction season expectedly emphasized the installation of basic water and sewer in remote "bush" communities off the road system. Out of the 73 VSW projects directly administered by DEC in 2002, 85% were in locations off the road system with either formal incorporation as a city or a long-standing history before statehood.

Nine projects were funded for communities on the road system that lacked formal status as a unit of local government. While six of these locations have long traditions of prestatehood settlement, two others²⁶ present the fundamental issue of program expansion into recent subdivisions. VSW leadership needs to openly consider this issue before straying further from the implicit public assumptions for the program.

²⁵ See AS 39.52.160, 39.52.170, 39.52.140, 39.52.120.

²⁶ Nikolaevsk, Voznesenka.

There is no question that the two communities in question have had hepatitis cases that, at the time,²⁷ might conceivably have been prevented through better water treatment. However, these two communities are neither impoverished, nor isolated, nor long-standing historical settlements. Each project involves only around 50 homes. Like many poststatehood arrivals, extended families came up from the Lower 48 and platted their own subdivisions in unincorporated areas²⁸ along the road system. They have prospered over the years and installed private communal utilities that now need upgrading.

The VSW program was never intended to displace the usual funding mechanisms for improvements in modern subdivisions on the road system. However, instead of paying special assessments to a developer, homeowner association, or local government, the residents at these two locations incorporated their homeowner association as a community council. They then asked DEC to pay for subdivision infrastructure, even down to the level of fire hydrants or new septic tanks. While this is certainly legal, it presents a fundamental question of priorities for scarce financial resources.

Questionable purchasing presumes unlimited future funding

During 2002, DEC awarded \$1.7 million to one of these subdivisions²⁹ for a well, a water tank, and a 20 x 40-foot building with a treatment system. However, at this point, that subdivision expects further funding because the tank, building, and bank account are all empty.

Construction of the structures, with landscaping, was completed before the project ever found a workable source of water, or even decided upon a treatment method. Seven wells were drilled, including the region's deepest of 680 feet, without finding one that consistently delivered the quantity and quality of water needed by the community.³⁰

Recommendation No. 5 discusses some issues on renting, fixing, and furnishing a house provided to the on-site manager to serve as living quarters and an office. Other questionable

²⁷ While vaccination is certainly a personal choice for residents of these communities, we note that hepatitis is now preventable by a vaccine routinely administered to the public.

²⁸ These two subdivisions lie within the boundaries of the Kenai Peninsula Borough, but not within an incorporated city.

²⁹ Voznesenka.

³⁰ DEC's engineer expressed to us his disappointment at the progress in finding water. Also, a dispute apparently developed between the on-site manager and a consultant over the technical aspects of the drilling process. Nevertheless, after seven unsuccessful wells, DEC's engineer still did not recognize the need to evaluate this situation for potential claims involving contractor error. DEC's small group of engineers lacks adequate business support in this important aspect of contract monitoring.

priorities were purchases such as a \$33,000 pickup truck, signage costing \$3,100,³¹ and a \$4,000 archeological study.³²

This type of questionable spending implicitly treats DEC funding as a general purpose, discretionary block grant, rather than funding that is to be narrowly-focused on a specific health-related facility. It also reflects an implicit strategy that, once you drive that first stake, the legislature will never leave a project unfinished and always provide more money.

In our Auditor's Comments section, we discuss the need to reassess the tradition of full funding and suggest requiring meaningful in-kind contributions by capable communities.

³¹ This signage consisted of (1) various construction warning signs for \$2,046, (2) three metal signs advertising the local water utility for \$384, (3) two water utility decals for a vehicle for \$190, and (4) six magnetic water utility signs for \$568 that will presumably allow private vehicle owners to assert that they are operating their vehicles on utility-related business. Warning signs are an obvious candidate for multi-project economies of scale, while the other items exemplify unchecked waste given the stage of the project.

³² Though no archeological sites had ever been discovered near the construction site, DEC indicates that the Department of Natural Resources ordered a study for purposes of the Federal Historic Preservation Act. The on-site manager then hired a local college teacher to conduct an immediate study for \$4,000. The teacher conducted two days of field work, looked at nine "shovel tests," and wrote a four-page report indicating that nothing had been found. Once again, the state would have benefited from specialized skills in negotiating the price, as well as the real need for a full study in the first place.

FINDINGS AND RECOMMENDATIONS

Recommendation No. 1

The governor should, by executive order, place the Village Safe Water program within the public facilities section of the Department of Transportation and Public Facility.

We recommend that the governor, by executive order,³³ place the Village Safe Water (VSW) program within the public facilities section of the Department of Transportation and Public Facility (DOTPF).³⁴ The program will benefit from DOTPF's support services, economies of scale, training opportunities, career paths, and business discipline.³⁵

Our observations on the personal limits of engineers in the Department of Environmental Conservation (DEC) are not intended as attacks on their conscientiousness. Their deficiencies in oversight are not due to any lack of integrity, dedication, or engineering talent. All of the DEC engineers in this program exhibit an exemplary level of commitment to enhancing the quality of life for rural communities.

Their strengths and enthusiasm lie in their familiarity with arctic technology and their social skills in working with the residents of bush Alaska. The six most senior VSW engineers have a total of 100 years of experience in constructing rural water and sewer facilities. Unfortunately, there is a mismatch between these special talents and the morass of nonengineering administrative tasks that consume their day.

In a larger organization, such tasks would be routinely assigned to others with specialized business skills such as purchasing, accounting, risk management, environmental coordination, legal review, internal auditing, and quality control.

Two DEC engineers estimate that they spend only ten percent of their time on the actual engineering tasks needed to help their communities.

³³ See Alaska Constitution art. III, sec. 23.

³⁴ While our audit was, of course, conducted at the request of the legislature, our recommendation is certainly consistent with the governor's recent Administrative Order No. 202 that encourages "*recommendations for consolidation and reorganization of departments, divisions, and duties and any other recommendation to promote sound and efficient administration.*"

³⁵ We recognize that DOTPF traditionally administers its projects through competitive bidding by commercial contractors. However, statutes that govern DOTPF procurement appear sufficiently flexible to allow a force account arrangement when feasible. See AS 35.15.010 (in-house work permissible "*when it appears to be in the best interests of the state*"); AS 44.33.300 (governor may waive competitive bidding for work in impoverished community done by government entity or nonprofit).

Forcing DEC engineers to wear all these hats places them in an untenable, no-win posture few would envy. On one hand, they are to be zealous advocates for a community, deftly maneuver it through bureaucratic red tape, and do whatever it takes to get the job done. On the other hand, they are expected to police the community's use of public money. When the need arises, we expect them to apply traditional business discipline in making realistic choices that may be locally unpopular.

DEC, expectedly, defends the status quo, mainly asserting that DEC engineers have ready access to the DEC regulators who issue the necessary permits for water and sewer projects. We question, though, whether that relationship is really an advantage instead of another weakness in the current placement.

The public expects DEC to function as an impartial regulator. Public confidence in this function is threatened, not enhanced, when a regulated developer shares the same organizational identity and the same physical offices. Environmental compliance is a costly requirement for private developers, and there is an inherent issue of comparative fairness for the latter permittees who cannot simply visit another floor to expedite their applications.

However, the main reason to reassign VSW construction is DEC's lack of the necessary business infrastructure to safeguard spending from abuse. We believe that a better home for this program is DOTPF's public facilities section.

VSW engineers will benefit from the business discipline, support services, training opportunities, and career paths³⁶ found at DOTPF. However, in giving VSW a better placement, DOTPF should consider keeping the current work group intact, given its cohesive nature, bush skills, initiative, and culture of dedicated advocacy.

Recommendation No. 2

The state should mandate that on-site managers be paid with a salary rather than on an open-ended hourly basis.

The on-site manager on VSW projects is not an engineer and is labeled by DEC as the project's "superintendent." Nevertheless, under the contract traditionally prescribed by DEC, the position oversees on-site construction with the broad discretion and authority characteristic of a high-level manager. Despite this managerial status, compensation under the contract has been on an uncapped, self-reported, hourly basis, with the potential for copious overtime pay, rather than a fixed salary.

³⁶ Despite the talents of DEC engineers assigned to the VSW program, the size and unique classifications of their work group foreclose meaningful opportunities for internal advancement. DOTPF, on the other hand, offers a full career path of engineer positions up through Engineer V.

Though not a permanent resident, an on-site manager can become quite popular within the community. VSW procedures³⁷ do not encourage a community to monitor a manager's ongoing compensation. Nevertheless, we consider such extraordinary wages to be a waste of project funding and another symptom of the ambiguity as to whether DEC or the community is accountable.

The normal business solution is hardly novel: pay these managers with a competitive fixed salary for full-time, temporary employment judged under specific performance milestones. We recommend that the drafting and oversight of such contracts be transferred to professional procurement staff with the expertise, experience, and personal skills to comfortably police this type of abuse.

Once again, this oversight problem is symptomatic of the human limits faced by VSW engineers. Business waste results from DEC's unrealistic expectation that each of these well-meaning engineers be a jack-of-all-trades in a specialized world where economies of scale save money.

a. Excessive wages for on-site managers

During the 2002 construction season, this pay arrangement resulted in an extraordinary level of gross wages for some of these on-site managers (see Exhibit 3 on page 9). Such wages obviously exceeded the compensation of every engineer directly employed by the state.

DEC engineers, who drafted these contracts, have offered us a variety of justifications for the high compensation of their on-site managers: (1) they do a lot of work; (2) communities like them; (3) they endure bush living hardships; (4) they would not like the reduced pay of a salary; (5) good ones cost at least \$100,000; (6) they are denied the state benefit package; (7) some technically work for nonprofits rather than true cities; and (8) communities lack incentives to control manager pay levels.³⁸

³⁷ The community usually contributes none of its own money to the project. All expenses, including the wages of the on-site manager, are usually paid by DEC out of state and federal funds, with an apparent local assumption that more funding will be available next year if the project runs short. Further, the on-site manager has considerable discretion over residents' cash flow as the manager awards jobs, sets pay rates, rents local equipment, and buys everything from used furniture to stump removal services.

³⁸ DEC's limited control was apparent when its engineer directed one community to reduce the number of workdays specified in its employment agreement with the on-site manager. The community declined and continued its previous arrangement. DEC's ambiguous authority was also apparent when the same community leadership asked the engineer, "Can you be fired?"

b. Perks can further enhance high wages

DEC can authorize payments for significant perks for on-site managers. Exhibit 5 shows the overall package of just under \$225,000 enjoyed by the highest-paid manager for a construction season reflecting less than two-thirds of a full work year. If projected for full-year employment, this pay rate would translate to an annual compensation of \$356,000.

DEC permitted this on-site manager a variety of fringe benefits as he juggled three projects at three locations during a single construction season. Approximately \$5,700 was provided as "per diem" for his meals. Up to \$3,000 in gas appears³⁹ to have been provided for daily commutes between his home and the two jobs on the road system.

For days when the manager did not commute, DEC rented him a two-story, 3-bedroom, sauna-equipped home/office at one of his road system projects. This rental was renovated, painted, and furnished for him at DEC expense, including such items as two TV/VCRs and a \$2,700 computer system.

While such perks are not unusual in private corporations, Recommendation No. 5 addresses our concerns within the context of public employment.

Finally, while not included in Exhibit 5, the manager's accompanying spouse was paid to work on two of his projects, frequently during the same workweek (see Exhibit 5).

EXHIBIT 5	
VILLAGE SAFE WATER PAYMENTS FOR THE HIGHEST-PAID ON-SITE MANAGER	
CALENDAR YEAR 2002 (63% FTE)	
Manager's gross wages	\$197,078
Fee for "consulting services"	3,200
Per diem	5,712
Gasoline	3,165
Rental house	6,500
Utilities for house	952
Furnishings for house	4,946
Indemnification for site thefts	<u>2,700</u>
<i>Total for 63% of full year</i>	<u>\$224,253</u>
<i>Projected payment for full year</i>	<u>\$355,957</u>

³⁹ The two projects were, respectively, 194 and 141 round-trip road miles from the manager's home. DEC engineers made no effort to discover or control the manager's commuting habits or use of over \$3,000 in auto gas reimbursement. However, we conclude that the gas reimbursement was largely used for personal commuting given the compact job sites, limited need for distant errands, and the timing of the gas purchases. For instance, in August 2002, the manager purchased sufficient gas for 30 potential round-trips (194 miles each) between the most distant project and his home.

c. Overtime origins of excessive wages

The high wages are a function of hourly pay arrangements with uncapped overtime. Exhibit 6 shows the weekly hours claimed by the highest-paid of DEC's on-site managers, including ten consecutive weeks in which he juggled both a bush project⁴⁰ and one of two projects on the road system in the Kenai Peninsula Borough. Between the two projects, he consistently claimed exactly 110 hours for each of those ten consecutive weeks.

Exhibit 7, shown on page 22, is another perspective on time reporting by the highest-paid manager. He claimed 94 workdays of over 14 hours a day, with 37 of those days exceeding 16 hours a day. We even noted one day in which he claimed the full 24 hours, followed by a 16-hour day.

Though this on-site manager's overtime rate is a significant one at \$67.50 per hour, his timesheets simply record his total hours for the day. There is no indication as to when work actually began and ended, the precision of recording time in fractional hours, any minimum call-outs, travel time, standby time, or even whether meal breaks and commuting occurred on or off the clock.⁴¹

DEC's written procedures, DEC engineers, and the contracts themselves were all silent on such costly nuances of overtime for these hourly employees. DEC engineers

EXHIBIT 6				
WEEKLY HOURS CLAIMED BY VSW'S HIGHEST PAID ON-SITE MANAGER AND HIS SPOUSE				
2002 CONSTRUCTION SEASON				
Week	On-site Manager		Spouse	
	No. of Projects	Hours	No. of Projects	Hours
1	2	52		
2	2	62		
3	3	66		
4	3	82		
5	2	104	1	40
6	2	102	1	40
7	2	92	1	40
8	2	112	1	40
9	2	108	1	40
10	2	112	1	40
11	2	108	1	60
12	2	108	1	60
13	2	108	1	50
14	2	92	1	60
15	2	108	1	60
16	2	108	2	96
17	2	110	2	96
18	2	110	2	96
19	2	110	2	96
20	2	110	2	96
21	2	110	2	96
22	2	110	2	96
23	2	110	2	90
24	2	110	2	90
25	2	110	2	90
26	2	110	2	90
27	1	24	1	24
28	2	84	1	48
29	2	76	1	48
30	1	44	1	32
31	1	68	1	48
32	1	32	1	32

Shading indicates a week in which time was claimed for both a remote bush project and at least one project on the road system.

⁴⁰ Nulato

⁴¹ Paying an on-site manager for commuting time would constitute a "portal to portal" employment agreement, not a customary arrangement for public employees.

unapologetically indicated that they simply left it to the discretion of the on-site manager to claim time as he deemed appropriate.

Given the continued FY 04 funding for some of this work, these problems may well continue without direct intervention.

d. Missing DEC oversight

Existing DEC oversight procedures were only sporadically applied by DEC engineers. DEC's written procedures prescribe that timesheets for force account employees, including on-site managers, will be sent to DEC for review. But in most cases, this simply does not happen.⁴²

Rather, individual employee timesheets are presumably kept by on-site managers, who directly fax only a summary to the contract CPA firm that cuts the paychecks. During our audit, DEC could not immediately produce individual timesheets for the past season's work on the three projects that we selected for payroll review. Those timesheets had never been reviewed by DEC engineers and had to be retrieved from the manager's home in another city.⁴³

DEC procedures require the completion of daily activity reports by on-site managers, a standard practice in the construction industry. DEC engineers could ideally compare managers' time claims to these routine reports, as well as to the engineers' own observations during site visits. However, for two of the projects, busy engineers only had time for brief visits once or twice a month, and daily activity reports often lacked sufficient detail for meaningful monitoring of exactly who did what on a given day. On the third project, there were no engineer site visits during 2002, and the on-site manager simply decided not to complete any daily field reports.⁴⁴

EXHIBIT 7		
14-PLUS HOUR WORKDAYS CLAIMED BY VSW'S HIGHEST PAID ON-SITE MANAGER AND HIS SPOUSE		
2002 CONSTRUCTION SEASON		
	<i>On-site Manager</i>	<i>Spouse</i>
Days over 14 hours	94	40
Days over 16 hours	37	-0-
Days over 18 hours	3	-0-

⁴² In fact, one DEC engineer candidly told us that he would not know what to look for if the timesheets were sent to him for review. Another told us that he simply would not have time to review them.

⁴³ Though DEC and its on-site manager cooperated with our request, it was clear from the logistical hurdles that DEC seldom, if ever, attempts to inspect such timesheets for legitimacy, accuracy, or even existence. However, such oversight is an important business safeguard given the traditional risks we discuss in Recommendation No. 3.

⁴⁴ Though DEC asserts there was only limited activity at this project during 2002, we note that the on-site manager received approximately \$21,000 in gross wages for work done at that site. Also, his spouse grossed approximately \$5,500 in wages at this project during 2002.

Difficulties in effectively monitoring this manager were further compounded in 2003. DEC placed the oversight for each of his three projects with a different DEC engineer. When we noted the obvious benefits of consolidated monitoring, one engineer feared that DEC's choice of manager would then override the engineers' personal choices as to which projects they prefer as assignments.

Recommendation No. 3

The VSW program should institute traditional business safeguards to protect the integrity of force account payrolls.

A common form of construction site corruption is "ghost employees," that is, fictitious workers' paychecks that are cashed by someone in a position to manipulate the system. One national authority on loss prevention warns:⁴⁵

This scheme is especially prevalent among construction companies and other businesses that hire short-term, temporary employees who work 'out in the field.' It is also not uncommon for owners of small closely-held businesses to add their children or other relatives to the payroll as "ghosts."

The traditional business safeguard is to assign the key stages in a construction payroll to different people that serve as a cross-check on each other. In other words, particularly at a remote site, the same individual simply should not (1) complete the initial hiring paperwork, (2) set the pay rates, (3) approve the hours on daily timesheets, (4) store timesheets and personnel files, (5) complete the daily activity reports, and (6) physically hand out the paychecks.

DEC's ambiguous written procedures theoretically insist upon some oversight. However, most DEC engineers now appear to leave the whole payroll process from start to finish to the unreviewed discretion of the on-site manager. While we did not discover any "ghost employees," we are surprised that DEC fails to appreciate the risk and surprised that on-site managers would allow DEC to place them in a position so vulnerable to suspicion.

For the three projects in which we reviewed 2002 payrolls, hiring was left to the discretion of the on-site manager, including the setting of pay rates. However, DEC procedures still required that every employee sign a written employment agreement to avoid later disputes over pay, status, benefits, and conditions of employment. Between the three projects, the on-site manager failed to provide DEC with the required agreements for 35 employees, including his own spouse. On five of the agreements provided to DEC, the position or pay rate was simply left blank.

⁴⁵ W. Steve Albrecht et al., *Guide to Fraud Investigations*, 3rd ed., (Fort Worth, Texas: PPC, 1999), sec. 508.3. Also see Joseph T. Wells, *Occupational Fraud and Abuse* (Austin, Texas: Obsidian Pub., 1997), chapter 8.

The usual practice was for the contract CPA to express mail employee checks directly to the on-site manager's home, which was distant from the project community. This may have seemed practical at the time given the manager's frequent commuting, and we found no evidence that the checks were not properly distributed to the payees.

Nevertheless, this scenario placed the manager in an unacceptable position when coupled with his private custody of the individual timesheets and the other factors we discuss above. A skeptical business world simply assumes a higher risk of ghost employees when a payroll process, from hiring to paycheck distribution, is dominated by one person in a remote setting. This basic shortcoming is another symptom of the over-delegation that can result when engineers lack the business support services found in larger organizations.

Recommendation No. 4

DEC's designated ethics supervisor should, with comprehensive assistance from the Department of Administration, determine the extent of any conflicts of interest among employees and establish clear boundaries.

Some DEC employees are assigned considerable autonomous discretion on VSW projects. Given the scope of discretion, the Executive Branch Ethics Act contemplates that DEC management will carefully screen outside employment for any conflicts of interest.⁴⁶

Obviously, outside employment should not compromise DEC's needs as a public employer with a limited staff. Conflicts from outside employment may impair employees' eligibility for particular assignments or their impartiality in selecting particular contractors and vendors.

We recommend that DEC's designated ethics supervisor obtain comprehensive assistance from the human resource professionals with the Department of Administration (DOA). In view of DEC management's uncertainty in this matter, a specialist from DOA should interview employees to ascertain the specific nature of any outside employment and to assist them in complying with the ethics act disclosure requirements in a meaningful manner. DOA should then assist the designated ethics supervisor in issuing clear boundaries for outside employment.

As we discuss in Recommendation No. 1, the longer term solution for this and other shortcomings in business infrastructure is to relocate the VSW program within DOTPF's public facilities section.

⁴⁶ We have discussed particular concerns with DEC management. However, due to the confidentiality of ethics act disclosures, this report does not attempt to cite any particular example.

Recommendation No. 5

For force account projects, the VSW program should adopt regulations setting basic business standards for potential conflicts of interest, transactions with project employees, and nepotism.

Our discussions earlier in this report detail the considerable discretion that on-site managers have in local spending on force account projects. The concept sounds positive in the abstract, with DEC scaling down a cumbersome purchasing bureaucracy to fit local realities. Cash is brought into a local economy and stays there, as longtime residents get hired and sell the project anything available.

However, in the zeal to "just get things done," DEC has left on-site managers in an unregulated void when it comes to some basic business safeguards that the public has a right to expect. More specifically, these managers are simply left to set their own boundaries when it comes to potential conflicts of interest, transactions with employees, and nepotism.

Such a standard-less void, by default, invites questionable practices that may eventually cross the line into misconduct. While managers' choices may not technically violate existing laws,⁴⁷ anecdotes that disappoint public expectations can jeopardize statewide confidence in the program as irreparably as any lawsuit. Development of consistent rules will once again benefit from specialized business expertise outside of the engineering field. Pertinent concepts from the state's ethics act and procurement code will, of course, be a good starting point for the drafting of specific rules that fit the context of these projects.

Our discussions in this report include examples where the same individuals have multiple roles on a project, such as community officers, employees, vendors, and beneficiaries. While such "self dealing" may be a reality and not inherently wrong, VSW projects need standards for scrutinizing the necessity and pricing of such transactions between related parties.⁴⁸

Clear standards regarding nepotism are another needed business safeguard. Employment for an on-site manager's accompanying spouse occurred at two projects in our review, including the frequent 90-hour weeks detailed in Exhibit 6 on page 21. Contrary to DEC's requirements for all force account employees, her employment was not reduced to a written agreement as to position, pay rate, and terms. Rather, her husband-manager set her pay rate, approved her timesheets, and assigned her duties as an "office clerk" or "bookkeeper" as he

⁴⁷ Neither on-site managers nor nonprofit community councils appear to be covered by the Executive Branch Ethics Act.

⁴⁸ For instance, DEC paid a community vice-president wages of \$19,185 as well as additional payments of \$3,600 to his private business for building equipment shelters. DEC paid an unallocated lump sum of \$2,000 to another force account employee in a bulk purchase of items ranging from mosquito repellent to chain saws to hand tools to lubricants to a mud pump.

An employee at another project received \$31,419 in wages and over \$45,000 for the rental of his construction vehicles. We also noted that the project was charged \$1,700 more than the quoted price for this vehicle use.

deemed necessary. Her timesheets, like that of the other employees, were kept in the couple's home and never reviewed by the DEC engineer.

Another troublesome situation concerns an on-site manager's personal purchase of a home rented at DEC expense. With the community president as landlord, DEC entered into a one-year oral lease of a two-story, three-bedroom, sauna-equipped house intended to serve as the manager's home/office. At the beginning of the tenancy, repairs were made at DEC expense including plumbing and painting.⁴⁹ The on-site manager put the utilities in his own name.

Ten days before the end of the year-long tenancy, DEC approved payment of a bill for \$9,000 in back rent. On the last day of the tenancy, the on-site manager signed a contract to personally purchase the home. While the home was later appraised for \$10,000 more than the purchase price, we note that five years ago, before DEC's plumbing and painting work, the assessed value for the purpose of property taxes was \$31,000 higher than the purchase price. We further note that the sales contract is silent as to any rent due between the end of DEC's lease and the closing date for the manager's personal purchase.

When DEC inquired about this transaction, the on-site manager responded that he (1) had sold his condo in Arizona, (2) had decided to stay in Alaska, (3) was purchasing this house "for the sake of the project,"⁵⁰ (4) was doing DEC a favor since it would not have to move its equipment and furnishings, (5) was allowing the community continued use of the office and shop in return for an eventual charitable tax deduction,⁵¹ and (6) was currently completing an application for further DEC funding. He also indicated that the community president and he may sue the state for defamation and implying a conflict of interest by inquiring about the transaction.

⁴⁹ DEC records were not adequate to distinguish employee time and materials for the house repairs from work on the project itself. However, there appear to have been repairs, painting, and plumbing work done on the house, with much of this work concentrated within the nine-day period between May 25 and June 14, 2002.

⁵⁰ We recommend that DEC obtain advice from the Department of Law concerning the need to negate any inference that this real estate was purchased on behalf of the state and to negate state liability for any eventual defaults or injuries.

⁵¹ While the on-site manager suggested the availability of this tax deduction, we note that a homeowner association may not qualify as a charity under Internal Revenue Code § 501(c)(3).

AUDITOR'S COMMENTS

The Village Safe Water program could require meaningful in-kind contributions by capable communities.

Though there have been some exceptions over the years, the usual assumption of the Village Safe Water (VSW) program is that communities invest none of their own funds or property. Under the force account arrangement used by the Department of Environmental Conservation (DEC), the community gets a facility along with paychecks for the local crew that builds it. DEC asserts that the use of force account labor, a business plan, and a local operator fosters a sense of community "ownership" in the completed project.

In some cases, an available workforce is all that can be expected. However, state funding is increasingly strained and federal funding increasingly expects local responsibility, commitment, and sustainability.⁵³ Communities could be encouraged to expect VSW assistance as a startup partnership, rather than a perpetual entitlement.⁵⁴

There will certainly be legitimate cases in which a community truly has nothing tangible to contribute. However, Exhibit 8 lists examples of local in-kind contributions

EXHIBIT 8 POTENTIAL COMMUNITY COMMITMENT (IN-KIND CONTRIBUTIONS) BY BENEFICIARIES OF VSW PROJECTS
Land for treatment building and water tank ⁵²
Use of vacant building for construction office
Use of cars and trucks
Use of construction equipment
Use of hand tools
Lodging for on-site manager and visiting specialty contractors
Community landscaping, gardening, and cleanup at construction site

⁵² For example, community leaders at one project had considerable land in the area, but we found no discussion of potential land donations or trades for the project site. Rather, DEC without question agreed to pay \$40,000 to purchase the nearby site of choice from someone outside of the community.

⁵³ See our prior audit of rural energy programs at the *Alaska Industrial Development and Export Authority*, July 12, 2001, Audit No. 08-30006-01.

⁵⁴ We are not the first to question whether the beneficiaries of VSW projects should be expected, when able, to make a tangible contribution to their project's construction. In 1999, a federal inspector general reviewed the use of rural development grants from the U.S. Department of Agriculture. The inspector general's report states:

Regarding the equipment rental charges, we believe the intent of 7 CFR 1780, Subpart B, Section 1780.49(e) is to prohibit grant recipients from benefiting financially from the use of their own equipment when that use could have been donated to the project reducing the amount of grant funds actually needed. (However, we do believe that RUS [Rural Utilities Service] should continue to reimburse grantees for their incidental costs associated with the use of the equipment such as those expenditures incurred for oil, fuel, and maintenance.)

that the public has a right to expect in other cases. In other words, as the program moves into more capable communities, DEC should not presume that the program needs to fund every element of the project.

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February 17, 2004

Ms. Pat Davidson
Legislative Auditor
Legislative Audit Division
P.O. Box 11300
Juneau, AK 99811-3300

Preliminary Audit Report
Village Safe Water Program, Selected Projects, November 19, 2003.

Dear Ms. Davidson:

We appreciate the opportunity to respond to the subject preliminary audit report. Overall the report remains a disappointment, not because it does not reveal significant need for improvement in some areas – it does, but because it contains so many other poorly informed or inaccurate analyses and findings. We offer our comments with the intent of helping focus the final report on meaningful analyses and more valuable findings. Detailed comments are enclosed. General comments follow.

The audit did not use the well-established body of construction management practices as the standard for reviewing Village Safe Water (VSW) construction management procedures. Instead, the preliminary report relies on vague notions of “normal business safeguards” or “business savvy” as audit standards. Time and again the preliminary report finds fault with practices that are, in fact, well-established, effective norms in the construction management field.

The preliminary audit report still misunderstands, ignores or misrepresents the basic structure for the VSW program. For example, the VSW program often uses a CPA firm to hold and disburse project funds for payroll and procurement. Disbursements must be authorized by both the community and the VSW engineer. This arrangement is effective at involving the community as project owner while maintaining state control over expenditures. The process has been copied by most other state and federal agencies that are funding force account projects in rural Alaska. The draft audit report concludes only that the process creates “ambiguity.” Either the auditors miss the importance of state control over project spending or they do not understand the process.

The preliminary audit report, like the management letter, contains unsupported allegations. For example, Exhibit 2 claims examples of “wasteful spending” in a number of areas with no specifics, alleging only that “contractors dictate changes” or “contractors dictate rates and fees with little scrutiny by engineers.” The report lacks discussion of the specific basis for these conclusions. Absent specifics, the report does not provide information that we can use to examine our processes or to otherwise respond to the allegations.

The audit report, again like the management letter, speculates about what might happen despite the evidence that no problems have ever been experienced. The lengthy discussion of "ghost employees" is a good example. The discussion on program employee conflicts of interest and ethics falls into this category as well. We acknowledge that the audit appropriately examines control systems and the potential for problems, as well as actual instances of problems. In some cases however, the analysis goes well beyond reasonable characterization of the potential for wrongdoing, essentially assuming that criminal activity is inevitable.

The audit relies on one or two rare situations to rationalize sweeping organizational changes. It fails to suggest other options for correcting perceived inadequacies, and instead leaps to a conclusion that the VSW program would be better off within the Alaska Department of Transportation and Public Facilities (DOTPF). The final report should indicate whether the auditors were asked to look at reorganizing VSW within DOTPF, or whether they arrived at that conclusion on their own.

Many of the report's conclusions stand out as groundless:

- There is no basis for faulting DEC procedures to guard against employee conflict of interest due to outside employment (Recommendation No. 4). The agency employs the same Ethics Act procedures as other agencies. The audit revealed no conflicts of interest or other Ethics Act violations. A thorough review by a Department of Administration official found no violations.
- The VSW program's timesheet procedures reflect construction management norms (see Recommendation No. 3). Despite the preliminary audit report's discussion of "ghost employees" it found no evidence of this ever occurring and program practices simply reflect industry norms. Either industry norms should be used as a basis for evaluating VSW practices, or all discussion of this issue eliminated from the report. The program should not be faulted because the auditors are unfamiliar with construction management practices.
- The audit's finding that there is wasteful duplication of bookkeeping efforts is a result of the auditors' unfamiliarity with the complexities of construction management. The suggestion that one set of books could be used is overly simplistic and unrealistic. Including this discussion in the report dilutes the more substantive findings.
- The recommendation that superintendents be paid a salary (Recommendation No. 2) is extraordinarily ill-conceived. The industry norm is to pay superintendents on an hourly basis to accommodate the variability in construction project work schedules. Paying a salary would waste state funds by paying for time that is not actually worked.

The "Auditor's Comments" that communities should contribute to the projects where possible amounts to an endorsement of existing Village Safe Water procedures.

Finally, there is merit in some of the report's conclusions:

- The audit revealed that the VSW program continues to have serious problems with 1099 and I-9 form procedures. Some of the problem stems from confusion over whether responsibility lies with the VSW engineer or the CPA firm. This situation will be corrected through a combination of employee training and amending the CPA firm contract before the next construction season (by May 1 of this year).
- In two, and perhaps three cases, the program did not exhibit sufficient control over superintendent compensation (including salary, travel and housing arrangements). While paying superintendents a salary is not the answer, the program clearly needs to establish better limits on superintendent compensation. New guidance is being prepared and will be in effect before the construction season (by May 1 of this year).
- The audit accurately revealed a single incident of nepotism that should not have been tolerated. A new policy is being prepared and will be in effect before the construction season (by May 1 of this year).
- Finally, we do not dispute that the VSW engineers could benefit from better procurement and contracting support. The program intends to reclassify an existing position to create a contracting officer position in the Village Safe Water program before the end of the current fiscal year.

Again, we appreciate the opportunity to comment.

Sincerely,

Ernesta Ballard
Commissioner

enclosure

Alaska Department of Environmental Conservation
Preliminary Audit Report Comments
Village Safe Water Program, Selected Projects, November 19, 2003

Findings and Recommendations

Recommendation No. 1: The Governor should, by executive order, place the Village Safe Water program within the public facilities section of the Department of Transportation and Public Facilities.

We strongly disagree with this recommendation. The audit analysis, centered mainly on a single atypical Village Safe Water (VSW) project, is insufficient basis for recommending such a sweeping organizational change, and ignores all of the reasons why the program is housed in the Department of Environmental Conservation (DEC) in the first place.

For example, the recommendation ignores the relationship between the VSW program and the other DEC water and sewer assistance programs: the Municipal Water, Sewerage and Solid Waste Matching Grant (MMG) program, the Drinking Water Loan State Revolving Loan (DWSRF) program, the Clean Water State Revolving Loan (CWSRF) program, and the Remote Maintenance Worker (RMW) program. MMG program staff administer VSW program funds in some communities. VSW and RMW staff work side-by-side in many villages. Loans made through the CWSRF and DWSRF programs are often paired with grants from the MMG program. These programs are all intrinsically linked and having them in a single organization unit produces immense efficiency, affords some flexibility in assigning agency resources, and provides for continuity and a high level of service to client communities. As far as we can tell from the preliminary audit report, the relation of the VSW program to these other DEC assistance programs was never considered.

The recommendation also ignores the efficiency of having the drinking water and wastewater assistance program, including the VSW program, housed in the same agency as the drinking water and wastewater regulatory programs. The assistance and regulatory programs share the same uniquely DEC mission. Assistance and regulatory program staff share the same areas of expertise. Regulatory staff and VSW program staff work hand-in-hand with communities bringing expertise in both the regulatory standards and the means by which they can be achieved.

Finally, the VSW program differs substantially from the DOTPF programs. With an occasional exception, DOTPF does not use a force account process. DOTPF programs do not share the DEC and VSW program mission to protect health and the environment. DOTPF and DEC staffs do not share similar expertise.

Implementing this recommendation would prove tremendously inefficient and wasteful. There are far more effective means to achieve better contracting support for VSW engineers than to place the program within DOTPF.

Recommendation No 2: The state should mandate that on-site managers be paid with a salary; rather than on an open-ended hourly basis.

We disagree with this recommendation. Paying on-site managers or superintendents on an hourly basis is a prudent practice and an industry norm. Rural construction projects frequently experience slow periods where minor work items need to be completed but where a full-time superintendent is not necessary. It would be a waste of public funds to pay an individual for a forty hour workweek, when only ten hours were worked.

We examined VSW program superintendent compensation more broadly than the narrowly-focused audit. For the 2002 construction season, the range of regular-hour wages paid to VSW superintendents varied from \$17.50/hour to \$47.50 per hour. The average wage rate was \$35.03 per hour. This compares to the average \$36-\$38 per hour DOTPF pays project superintendents, although DOTPF project superintendents typically receive a State benefit package when VSW superintendents do not.

To deal with the audit's isolated case of a superintendent working on more than one active project at a time, and to otherwise curtail the potential for inordinate compensation due to the cumulative effect of overtime, housing or travel-related payments, we will issue program guidance before the beginning of this coming construction season (before May 1) on superintendent compensation, including per diem and housing allowances.

Recommendation No. 3: The VSW program should institute traditional business safeguards to protect the integrity of force account payrolls.

We disagree with this recommendation. The VSW force account payroll process is spelled out in guidance and works as follows: (1) the community and the VSW engineer set the pay rates based upon prevailing rates in the area; (2) the project superintendent completes the initial hiring paperwork; (3) the superintendent approves daily time sheets and sends a summary to the VSW project engineer and the contract CPA firm; (4) the contract CPA firm mails the pay checks to the superintendent or, in some cases, to the community; and (5) the superintendent distributes the checks and stores the timesheets and personnel files. This process is certainly adequate and reflects industry norms.

The superintendent's job is to review each employee's timesheet for accuracy based on their records of employee hours. The VSW engineers cannot confirm employee hours since they are not on-site and have no knowledge of who worked what hours. Yes, a superintendent could embark on the felony criminal offense of creating "ghost employees." We trust that the criminal justice system provides some disincentive for criminal behavior. We also believe that the voluntary annual financial audits contracted by the program are a reasonable measure to protect against "ghost employees."

Recommendation No. 4: DEC's designated ethics supervisor should, with comprehensive assistance from the Department of Administration, determine the extent of any conflicts of interest among employees and establish clear boundaries.

We disagree with this recommendation. Nothing in the audit suggested evidence of actual conflicts of interest, nor did the audit offer evidence that VSW engineers would be more vulnerable to conflicts of interest than any other state engineering employees.

Nevertheless, we requested that a Department of Administration Senior Resources Management Consultant complete a review of all VSW engineers with respect to ethics disclosures. No evidence of Ethics Act Violations or conflict of interest was found.

Of the 11 VSW employees, only one had been engaged in outside employment on a project wholly unrelated to his responsibilities as a VSW engineer. The review found "no evidence of an Ethics Violation nor . . . any conflicts of interest regarding VSW employees and outside employment or consulting."

Recommendation No. 5: For force account projects, the VSW program should adopt regulations setting basic business standards for potential conflicts of interest, transactions with project employees, and nepotism.

We agree with this recommendation in part. We agree that the nepotism incident revealed by the audit, though isolated, should have been prohibited by program guidance. We also agree that rules governing conflicts of interest would be a valuable addition to the body of Village Safe Water guidance. We will issue programmatic guidance on both nepotism and conflicts of interest before the beginning of next construction season (by May 1 of this year).

We disagree that there is a need for additional rules pertaining to transactions with employees. All purchases are subject to the Village Safe Water procurement procedures, including purchases from persons who happen to be project employees. The combination of the existing Village Safe Water procurement code and a new conflict of interest policy will be sufficient control over transactions with employees.

ADDITIONAL COMMENTS AND RESPONSES

In addition to our responses to the specific Findings and Recommendations discussed above, we offer the following comments on the rest of the preliminary audit report.

Objectives, Scope and Methodology.

Page 1, first paragraph, first sentence: "*.. we conducted an audit of the Village Safe Water program (VSW) administered by the Department of Environmental Conservation (DEC).*" Although the audit claims to have reviewed 20 projects, it truly investigated only three projects all supervised by the same superintendent. Of the three projects investigated, the audit focused on a single project. We believe the audit falls well short of a program audit and is better categorized as a project audit.

Organization and Function

Page 3, sixth paragraph: "*DEC engineers may directly oversee a project or may delegate day-to-day oversight to a construction management firm.*" DEC does not delegate oversight. It may contract with a construction management firm to provide construction management services.

Page 3, seventh paragraph, second sentence: "*However, DEC retains an Anchorage CPA firm to manage a bank account that holds the grant funds 'in trust' for each project community.*" This alludes to a fiduciary relationship on the part of DEC. Grant funds are not held "in trust" for each project community. They are held by a CPA firm as a matter of program operating procedures.

Page 3, seventh paragraph, third sentence: "*The CPA firm issues checks for project expenditures, as directed by DEC.*" Disbursements are made upon approval of both DEC and the community.

Background Information

Page 5, third paragraph, third sentence: "*Scoring and ranking is conducted by the VSW program management in Juneau, rather than by the Anchorage-based engineers that supervise completion of the selected projects*". This is incorrect. Project scoring and ranking is conducted by a three-member team representing VSW, the Alaska Department of Community and Economic Development, and the U. S. Environmental Protection Agency.

Page 6, first paragraph, last sentence: "*However, DEC still oversees the project and pays all the bills.*" Bills are paid using funds granted to the community. Disbursements require the approval of both DEC and the community.

Report Conclusions

Page 7, second paragraph, first sentence: "*The concerns reflected in the audit request were well-founded.*" We suspect this overstates the audit findings. Perhaps the auditors could claim that some of the concerns were well-founded.

Page 7, second paragraph, second sentence: "*As detailed below, DEC procedures for spending lack some normal business safeguards that the public has a right to expect for construction projects.*" This overstates the audit findings.

Page 7, third paragraph, first sentence: "*. . . public construction is being monitored by a dozen engineers buried within a regulatory agency.*" The Village Safe Water program is a DEC program organized with other drinking water and wastewater assistance programs under the agency's Division of Facility Construction and Operation. The engineers aren't *buried* within a regulatory agency.

Page 7, third paragraph, second sentence: "*. . . these DEC employees suffer from a lack of the usual business support services that enable other state engineers to focus on engineering.*" We agree that VSW engineers, like most public and private engineers, could benefit from better procurement and contracting support. The program will reclassify an existing position to create a contracting officer position in the VSW program before the end of the current fiscal year.

Page 7, fourth paragraph: "*Our recommended solution is to transfer VSW construction to the Department of Transportation and Public Facilities (DOTPF) with its support services, economies of scale, training opportunities, career paths, and business discipline (see Recommendation No. 1).*" This is a bad idea for reasons discussed elsewhere. Engineer career paths within DEC are excellent and equal or exceed those in other agencies. We are interested in the basis for the auditors' comparison of DOTPF and DEC economies of scale, training opportunities, career paths, and business discipline. Where do DEC training opportunities and career paths fall short of DOTPF's? What was used to compare economies of scale?

Page 7, fifth paragraph, first sentence: "*A common thread in our findings is the considerable ambiguity that the program has tolerated in accountability for how project funds are actually spent.*" This statement is vague. What is meant by the term "ambiguity" in this context?

Page 7, fifth paragraph, second sentence: "*This is not surprising given that awarded funds are kept by DEC "in trust" for the recipients and jointly controlled by various parties with procedures that fluctuate considerably in practice.*" Funds are held by a CPA firm to allow for strict control over expenditures and reporting. Funds are not controlled by various parties. Funds are dispersed upon approval of the community and VSW. Procedures are spelled out in various guidance documents. Procedures vary to the extent needed to make sense under the variety of construction situations we encounter.

Page 7, sixth paragraph, first sentence: "*. . . a community's capacity to assume substantial control needs to be carefully evaluated on a case-by-case basis rather than presumed as the norm.*"

It is unclear what is meant by this sentence. If this suggests that the State should simply build the facilities for the communities with no community participation whatsoever, we strongly disagree.

Page 7, sixth paragraph, second sentence: "... oversight and accountability need to be documented by agreement in no uncertain terms." What does this mean?

Page 8, "Unskilled oversight of construction management firms and other engineers allows waste." This entire section lacks backup and support for conclusions. Many of the conclusions stem from the auditors' lack of understanding of the VSW procedures.

Page 8, "Exhibit 2: Contracts Allowed Wasteful Spending." This exhibit lists allegations without offering any idea of the basis for such assertions. For example, the exhibit states that contractors inflate pricing on pass through expenses. What is the basis for this conclusion? Where is it discussed elsewhere in the report? Was this a widespread phenomenon, or was it just one project? Elsewhere the exhibit simply restates vague, subjective observations such as "VSW skills are outmatched by contractor's business savvy." Including unsupported allegations gives the appearance of bias.

Page 8, second paragraph, second and third sentence: "However, engineers in DEC are left to draft their own contracts. The result is a loose, haphazard assortment of provisions invented as the need arises, with pricing and billing terms largely dictated by seasoned contractors." VSW contracts for engineering, design, and construction management are competitively bid with a not-to-exceed price. Pricing and billing terms are not dictated by contractors and contract provisions are not haphazard. Contracts follow the procedures contained in the "Securing Professional Services" section of the VSW procedures manual.

Page 8, fourth paragraph, second sentence: "In Recommendation No. 1, we propose a reorganization in which these well-meaning engineers will get the business support they need so they can refocus on engineering." We believe our proposal to reclassify an existing VSW position to create a contracting officer position in the VSW program is the optimal solution to the need for increased business support.

Page 8, footnote 9: "We note that one of these communities had a 2000 census population of only 22 persons and, per the state demographer, and estimated 2002 population of only 3 persons." The community in question is Ivanof Bay. At the time the VSW landfill study grant was awarded to Ivanof Bay, the 2000 census was not available. According to the 1990 census, Ivanof Bay had a population of 35. The estimated population in the VSW grant application (2000) was 40. Therefore, by statute, Ivanof Bay was eligible to receive a VSW grant.

Page 9, footnote 11: "Out of 35 VSW projects with actual construction during the 2002 season, 22 were conducted through a construction management firm, 11 had an on-site manager who reported directly to DEC's engineer, one used both a construction management firm and an on-site manager, and one was simply run by a general contractor." No VSW construction project was "simply run by a general contractor". There was a general contractor carrying out construction work in Bethel, but the project was administered by an engineering firm with oversight by City staff and a VSW engineer.

Page 9, first paragraph, second sentence: "*Based on our discussions with state and federal agencies,¹⁰ we disagree.*" Footnote 10 indicates that the auditors consulted "contracting specialists" at DOTPF, the Denali Commission, and the Alaska Industrial Development and Export Authority. We mean no disrespect, but the VSW program has far more experience running construction projects in rural Alaska than the Denali Commission or the Alaska Industrial Development and Export Authority.

Page 9, second paragraph, second sentence: "*While DEC oversees the project and pays all the bills . . .*" This oversimplifies the program disbursement process as discussed previously.

Page 9, third paragraph, second sentence: "*This manager is not from the community and may or may not be a resident of Alaska.*" We are not aware of VSW superintendents that are not Alaska residents and question the basis for the statement.

Page 9, fourth paragraph, second and third sentences: "*We have reviewed the compensation for the three highest-paid on-site managers during the 2002 construction season. While DEC defends these wages, we find them excessive and wasteful.*" We agree these wages are high and do not defend them. A new policy regarding superintendent compensation is being prepared and will be in effect before the construction season (May 1 of this year).

Page 10, first paragraph, second sentence: "*We found DEC's loose controls over crew payrolls to fall short of normal business safeguards.*" The Village Safe Water payroll controls are the industry norm for construction projects.

Page 10, first paragraph, third sentence: "*Those loose controls are symptomatic of the overall ambiguity as to whether DEC or the community is accountable for how project funds are spent.*" There is no ambiguity. Both DEC and the community are responsible.

Page 10, second paragraph: "*While we did not find any fraudulently-issued paychecks, such neglect of payroll safeguards is an opportunity for fraud to occur and not be detected (see Recommendation No. 3).*" The payroll safeguards employed by the Village Safe Water program are the industry norm. Payroll fraud is a criminal offense. This statement suggests that the auditors were unfamiliar with construction management practices.

Page 10, third paragraph, second sentence: "*However, the shortcoming once again shows a mismatch between the professional skill set of public engineers and the business savvy needed to protect public spending.*" We disagree with the conclusion and the use of the vague concept of "business savvy" as an audit standard.

Page 10, fourth paragraph, second sentence: "*Given the on-site manager's broad discretion over purchasing . . .*" Superintendent purchasing is circumscribed by VSW program guidance.

Page 10, fifth paragraph, first sentence: "*DEC's oversight procedures . . . show a lack of business skills in areas such as purchasing, risk management, and compliance with tax laws.*" The reference to "risk management" is unclear. What "risk management" problems were found?

Page 10, fifth paragraph, second sentence: "*Some of these problems simply waste public money . . .*" We find it odd to characterize something as a "simple waste of public money."

Page 10, footnote 13, second sentence: "*At least one engineer allows the on-site manager to choose the source up to \$25,000 without preapproval.*" The VSW Standard Procurement Policy, dated March 1, 1999 states that for items costing \$5,000 or less, the minimum procurement action is discretionary competition. For items costing from \$5,001 to \$50,000, the minimum procurement action is written quotes or proposals from at least three firms. For items costing \$50,001 or more, the minimum procurement action is sealed bids or proposals, with notice requesting bids placed in a newspaper of general circulation for a minimum of four days at least 14 days before bids or proposals are due. Prior to 1999, VSW procedures allowed superintendents to procure goods or services costing \$25,000 or less (in accordance with the VSW procurement rules) without pre-approval of the VSW project engineer. In the isolated case cited, a superintendent's contract had been renewed without updating to the new procurement process. The superintendent in this case never exercised the outdated \$25,000-or-less delegated procurement provision.

Page 10, footnote 15: "*For instance, local ordinances exempted project purchases from local sales taxes, which could total 5%. However, we noticed a variety of purchases in which the on-site manager did not attempt to claim the exemption. DEC approved payment even though the bills or receipts clearly included the local tax.*" Although this was clearly an oversight on the part of the Voznesenka superintendent and the project engineer, we believe this statement suggests that this was a frequent occurrence resulting in the loss of sizable sums. In fact, the purchases which included the local tax were for photo processing and minor office supplies.

Page 11, *Exhibit 4: Unexplained High Costs for Common Hand Tools and Supplies*. This Exhibit serves to demonstrate the auditors' basic unfamiliarity with the rural Alaska environment. The Exhibit also does not indicate quantities, so it is impossible to tell whether an \$11 purchase of "Post-It Notes" refers to single note or an entire case of notes.

Page 11, second paragraph, second and third sentences: "*However, we also expect that a skilled purchasing agent could negotiate bulk purchases of such items that would service numerous projects. Such business economies of scale are an unrealistic expectation, though, by DEC's unsupported engineers.*" This shows a lack of understanding of the basic statutory structure for the VSW program. We have neither the authority nor means to aggregate funding sources for bulk purchases.

Page 11, third paragraph, first and second sentences: "*. . . up to five different bookkeeping systems concurrently track how much money is left. This redundant bookkeeping is wasteful.*" Each bookkeeping system serves a unique purpose. This finding is a result of the auditors' unfamiliarity with the complexities of construction management. The suggestion that one set of books could be used is overly simplistic and unrealistic.

Page 12, second paragraph, second sentence: "*One on-site manager employed his spouse to act as an on-site bookkeeper, and purchased a \$2,700 computer system out of project funds.*" The

purchase of a computer at the start of a project using project funds is common practice. The computer is needed to establish an effective office at the construction site. Upon completion of the project, the computer is left with the community to assist them in utility management. We see nothing wrong with this practice.

Page 12, second paragraph: *"Yet another unofficial system, tracking by the community itself, may exist at some sites. For instance, \$1,700 of a project's money was used to send an officer of a community council to Anchorage for a two-day QuickBooks course."* This was the Vozeneska project. This training was not related to construction cost tracking. This training was for the purpose of increasing the community's utility management capability.

Page 12, fifth paragraph, first sentence: *"DEC engineers were apparently unaware that longstanding federal tax laws require Form 1099 reporting of some payments to vendors that exceed \$600."* We agree VSW continues to have serious problems with 1099 and I-9 form procedures. Some of the problem stems from confusion over whether responsibility lies with the VSW engineer or the CPA firm. This situation will be corrected through a combination of employee training and amending the CPA firm contract before next construction season (by May 1 of this year).

Page 13, second paragraph, first and second sentences: *"A similar issue arose when another on-site manager was paid wages as an employee while sizeable additional payments were paid directly to his private business. Among these additional payments was \$4,662 in per diem and \$7,700 designated as a reimbursement for health insurance premiums."* Health insurance and per diem costs were part of the superintendent's employment contract with the grantee (the City).

Page 14, second and third paragraphs: These paragraphs discuss the need for better monitoring and safeguards over outside employment. As stated earlier, a Department of Administration Senior Resources Management Consultant completed a review of all VSW employees with respect to ethics disclosures and found no evidence of Ethics Violations or any conflicts of interest regarding VSW employees and outside employment or consulting. In fact, only one of the 11 VSW engineers had any outside employment at all, and that single, small project posed no Ethics Act concern whatsoever.

Page 14, fifth paragraph: *"Nine projects were funded for communities on the road system that lacked formal status as a unit of local government. While six of these locations have long traditions of pre-statehood settlement, two others (Vozeneska and Nikolaevsk) present the fundamental issue of program expansion into recent subdivisions. VSW leadership needs to openly consider this issue before straying further from the implicit public assumptions for the program."* We believe that legitimate public assumptions for the program stem directly from statute. The definition of "village" is found at AS 46.07.080. For VSW purposes, a village includes "an unincorporated community that has between 25 and 600 people residing within a two-mile radius, a second class city, or a first class city with not more than 600 residents." The Legislature clearly intended to make roadside communities eligible for the program. There are numerous examples of statutes that distinguish between remote communities and roadside communities. The Village Safe Water Act is not one of them. We do not agree with the audit

report's suggestion that we abandon the statutory definition of eligibility for the auditors' notion that roadside communities should be ineligible.

Page 15, second paragraph, first sentence: *"The VSW program was never intended to displace the usual funding mechanisms for improvements in modern subdivisions on the road system."* The program was intended to serve roadside communities. By its very nature, the Village Safe Water program subsidizes the development of community water and sewer systems. The capital costs of essentially all water and sewer infrastructure in the U.S. have been subsidized by federal or state programs to some extent. The intent of the Village Safe Water program is clearly expressed in statute.

Page 15, fourth paragraph, second sentence: *"Seven wells were drilled, including the region's deepest of 680 feet, without finding one that consistently delivered the quantity and quality of water needed by the community."* This was the Voznesenka project. A total of seven wells were drilled in the community. Five are producing varying quantities of water. Taken together, these wells will provide an adequate supply of water for the community. Well drilling is not an exact science and a well driller cannot, nor should reasonably be expected to guarantee that each well will provide a significant supply of water.

Page 15, fifth paragraph, second sentence: *"Other questionable priorities were purchases such as a \$33,000 pickup truck, signage costing \$3,100 and a \$4,000 archaeological survey."* These costs are associated with the Voznesenka project. The truck cost \$30,288 and is not a pickup truck, but a utility truck registered to the Voznesenka Community Council. The \$3,100 for signage was a prudent use of project funds. An archeological survey was required by the Department of Natural Resources (DNR), Office of History and Archeology. The archeologist selected is on the DNR approved list of archeologists. The archeology costs are in line with standard rates.

Page 16, second paragraph, first sentence: *"This type of questionable spending implicitly treats DEC funding as a general purpose, discretionary block grant, rather than funding that is to be narrowly-focused on a specific health related facility."* There is no basis for suggesting that VSW project funds are being treated as a general purpose, discretionary block grant. The audit report, as far as we can tell, unearthed no costs that were not directly related to the projects.

Page 16, first paragraph, second sentence: *"It also reflects an implicit strategy that, once you drive that first stake, the legislature will never leave a project unfinished and always provide more money."* Projects are phased to the extent possible to provide a responsible end point when each grant is completed. There is no presumption of the inevitability of continued funding as suggested.

Page 16, third paragraph: *"In our Auditor's Comments section, we discuss the need to reassess the tradition of full funding and suggest requiring meaningful in-kind contributions by capable communities."* This comment is an endorsement of existing VSW policy.

Page 16, footnote 32: *"Though no archeological sites had ever been discovered near the construction site, DEC indicates that the Department of Natural Resources ordered a study for the purposes of the Federal Historic Preservation Act. The on-site manager then hired a local college*

teacher to conduct an immediate study for \$4,000. The teacher conducted two days of field work, looked at nine "shovel tests" and wrote a four page report indicating that nothing had been found. Once again, the state would have benefited from specialized skills in negotiating the prices, as well as the real need for a full study in the first place." We contacted the Department of Natural Resources, Office of History and Archaeology. The reason they recommended an archeological survey was because very few surveys had been completed in the area and it was believed that the area could have archaeological significance. The survey was conducted by the head of the anthropology program at the University's Kenai Peninsula College. We believe the cost of the survey is comparable to the cost of similar surveys in similar situations. Of additional note, the auditors seemingly fail to realize the importance of surveys and that it is much more cost effective to conduct surveys in advance of construction than to contend with archaeological issues during construction. We believe that most persons familiar with construction, the cost of archaeological surveys, and potential impacts of archaeological issues arising during construction would deem the \$4,000 money well spent.

Findings and Recommendations

Page 17, third paragraph, second and third sentences: *"The six most senior VSW engineers have a total of 100 years of experience in constructing rural water and sewer facilities. Unfortunately, there is a mismatch between these special talents and the morass of non-engineering administrative tasks that consume their day."* The second sentence overstates the situation. Some degree of non-engineering work is commonplace for engineers in the public sector.

Page 17, fifth paragraph: *"Two DEC engineers estimate that they spend only ten percent of their time on the actual engineering tasks needed to help their communities."* This statement lacks specificity in its use of the term "actual engineering tasks." Again, we suggest that the vast majority of public sector engineers spend the majority of their time on activities that they do not consider "actual engineering tasks." The audit report statement is not particularly illuminating and only suggests that VSW engineers are no different in how they view their jobs than other public sector engineers.

Page 18, first paragraph, first sentence: *"Forcing DEC engineers to wear all these hats places them in an untenable, no-win posture few would envy."* We agree that VSW engineers wear a variety of hats. Although the audit report suggests that this is undesirable, it is a reality of being a public engineer doing business in rural Alaska. We do not believe VSW engineers are placed in "an untenable, no win posture". And apparently the VSW engineers themselves do not think their positions are undesirable, as the program has experienced very little turnover.

Page 18, second paragraph: *"DEC, expectedly, defends the status quo, mainly asserting that DEC engineers have ready access to the DEC regulators who issue the necessary permits for water and sewer projects. We question, though, whether that relationship is really an advantage instead of another weakness in the current placement."* All VSW projects undergo the same regulatory processing as all other drinking water or wastewater projects. VSW projects do not receive preferential or expedited treatment.

Page 18, third paragraph, first and second sentences: *"The public expects DEC to function as an impartial regulator. Public confidence in this function is threatened, not enhanced, when a regulated developer shares the same organizational identity and the same physical office."*

Again, we take exception to any allegation that VSW projects receive preferential or expedited treatment during the permitting process. DEC functions as an impartial regulator. We do not share the audit report's view that public confidence has been eroded, and point out that the public also expects state programs to operate efficiently. From an efficiency standpoint, the VSW program is optimally housed within DEC.

Page 18, fourth paragraph, first sentence: *"However, the main reason to reassign VSW construction is DEC's lack of the necessary business infrastructure to safeguard spending from abuse."* We disagree for reasons stated previously.

Page 18, fifth paragraph, first sentence: *"VSW engineers will benefit from the business discipline, support services, training opportunities, and career paths found at DOTPF."* We disagree. We also doubt that DOTPF could support the VSW program without additional personnel and financial resources.

Page 18, paragraph six, third sentence: *"Despite this managerial status, compensation under the contract has been on an uncapped, self-reported, hourly basis, with the potential for copious overtime pay, rather than a fixed salary."* We indicated previously our agreement with this characterization of an isolated case.

Page 18, footnote 36: *"Despite the talents of DEC engineers assigned to the VSW program, the size and unique classifications of their work group foreclose meaningful opportunities for internal advancement. DOTPF, on the other hand, offers a full career path of engineer positions up through Engineer V."* The five-step career path available to VSW engineers begins with the VSW Engineering Assistant job classification and continues with VSW Engineering Associate, VSW Engineer I, VSW Engineer II, and VSW Engineer III.

Page 19, first paragraph, first and second sentences: *"Although not a permanent resident, an on-site manager can become quite popular with the community. VSW procedures do not encourage a community to monitor a manager's compensation."* This statement constitutes a gross generalization.

Page 19, second paragraph: *"The normal business solution is hardly novel: pay these managers with a competitive fixed salary for full-time, temporary employment judged under specific performance milestones."* This solution is certainly novel in the construction management field. Its novelty as a construction management practice stems from the widely-recognized fact that paying construction superintendents a salary will waste funds paying for time that is not actually worked. The audit report suggests the wrong solution.

Page 19, fourth paragraph, first sentence: *"During the 2002 construction season, this pay arrangement resulted in an extraordinary level of gross income for some of these on-site managers (see Exhibit 3 on page 9)."* This reference and Exhibit 3 pertain to only the three highest paid VSW superintendents. We examined VSW program superintendent wages more

broadly than the narrowly-focused audit. For the 2002 construction season, the range of regular-hour wages paid to VSW superintendents varied from \$17.50/hour to \$47.50 per hour. The average wage rate was \$35.03 per hour. This compares to the average \$36-\$38 per hour DOTPF pays project superintendents, although DOTPF project superintendents typically receive a State benefit package when VSW project superintendents do not. However, we agree that there were two, and perhaps three cases in which the program did not exhibit sufficient control over superintendent compensation.

Page 19, footnote 37: *"The community usually contributes none of its own money to the project. Communities are prohibited by statute from contributing to the cost of construction.*

Page 19, footnote 38: *"DEC's limited control was apparent when its engineer directed one community to reduce the number of workdays specified in its employment agreement with the on-site manager. The community declined and continued its previous arrangement. DEC's ambiguous authority was also apparent when the same community leadership asked the engineer, 'Can you be fired?'"* The example does not demonstrate ambiguous authority. What it does demonstrate is that the VSW program engineers exhibit control over project spending. That the communities do not always appreciate the continuing level of cost and expenditure control is not surprising.

Page 21, first paragraph, first sentence: *"The high wages are a function of hourly pay arrangements with uncapped overtime."* Based on information discussed previously, we do not agree that VSW hourly superintendent wages exceed norms.

Page 21, fourth paragraph: *"DEC's written procedures, DEC engineers, and the contracts themselves were all silent on such costly nuances of overtime for these hourly employees. DEC engineers unapologetically indicated that they simply left it to the discretion of the on-site manager to claim time as he deemed appropriate."* Again, we agree with the need to control overtime to guard against recurrence of the isolated incidents discussed in the report. New guidance regarding superintendent compensation is being prepared and will be in effect before the construction season (May 1 of this year).

Page 22, Exhibit 7 *"14-Plus Hour Workdays Claimed by VSW's Highest Paid On-Site Manager and His Spouse"* and Page 21, Exhibit 6 *"Weekly Hours Claimed By VSW's Highest Paid On-Site Manager and His Spouse."* (At this point in the report, we cannot help but wonder how many different ways a single audit report can cite the same information on overtime and bring up the same single nepotism case. What purpose does the repetition serve?) Once again, we agree with the need to better control overtime and to prohibit nepotism. Guidance to address superintendent overtime and nepotism issues is being prepared and will be in effect prior to the construction season (May 1 of this year).

Page 22, first paragraph: *"Given the continued FY04 funding for some of this work, these problems may well continue without direct intervention."* These problems will be addressed via guidance that is being prepared and will be in effect prior to the construction season (May 1 of this year).

Page 22, fourth paragraph, last sentence: *"On the third project, there were no engineer site visits during 2002, and the on-site manager simply decided not to complete any daily field reports."*

The third project referred to was a project in Nulato. There were no engineer site visits because there was not enough work activity to justify the time and cost of such visits. By not completing daily field reports, the superintendent violated procedures contained in the VSW Superintendent's Manual, which state that Daily Field Reports are to be completed. Progress on the very limited field work was summarized, however, in Pay Period Progress Reports. This was the same superintendent that was working on the Voznesenka and Nikolaevsk projects. In addition to the summary reports, the superintendent verbally apprised the VSW engineer of status and progress.

Page 22, footnote 42: *"In fact, one DEC engineer candidly told us that he would not know what to look for if the timesheets were sent to him review. Another told us that he simply would not have time to review them."* The VSW engineers have no basis for reviewing individual timesheets as they are not on site. Individual timesheet review and preparation of timesheet summaries is the job of the project superintendent on VSW and other construction projects.

Page 22, footnote 43: *"Though DEC and its on-site manager cooperated with our request, it was clear from the logistical hurdles that DEC seldom, if ever, attempts to inspect such timesheets for legitimacy, accuracy or even existence. However, such oversight is an important business safeguard given the traditional risks we discuss in Recommendation No. 3."* The VSW program's timesheet procedures reflect construction management norms. The DEC engineers do not review individual timesheets, nor should they.

Page 22, footnote 44: *"Though DEC asserts there was only limited activity at this project during 2002, we note that the on-site manager received approximately \$21,000 in gross wages for work done at that site. Also, his spouse grossed approximately \$5,500 in wages at this project during 2002. The superintendent oversaw the following project activities during 2002: construction of diversion berms in the wetland discharge area; repairs to the sewage lagoon; and construction of a concrete silt and effluent discharge pipe."*

Page 23, second paragraph: *"A common form of construction site corruption is "ghost employees", that is, fictitious workers' paychecks that are cashed by someone in a position to manipulate the system."* The VSW program's timesheet procedures reflect construction management norms. Despite the preliminary audit report's discussion of "ghost employees" it found no evidence of this ever occurring and program practices simply reflect industry norms. Either industry norms should be used as a basis for evaluating VSW practices, or all discussion of this issue eliminated from the report.

Page 23, fourth paragraph, first and second sentences: *"The traditional business safeguard is to assign the key stages in a construction payroll to different people that serve as a cross check on each other. In other words, particularly at a remote site, the same individual simply should not (1) complete the initial hiring paperwork, (2) set the pay rates, (3) approve the hours on daily time sheet, (4) store timesheets and personnel files, (5) complete daily activity reports, and (6) physically hand out the paychecks."* "Traditional business safeguards" should not be substituted for the more appropriate standard of construction management norms. Of additional note: VSW superintendents do not set pay rates.

Page 23, fifth paragraph, first and second sentences: *"DEC's ambiguous written procedures theoretically insist upon some oversight. However, most DEC engineers now appear to leave the whole payroll process from start to finish to the unreviewed discretion of the on-site manager."* Timesheet summaries are submitted by superintendents and are reviewed by VSW. The VSW program's timesheet procedures reflect construction management norms.

Page 23, fifth paragraph, third and fourth sentences: *"While we did not discover any "ghost employees," we are surprised that DEC fails to appreciate the risk and surprised that on-site managers would allow DEC to place them in a position so vulnerable to suspicion."* As stated elsewhere, the VSW program's timesheet procedures reflect construction management norms. Despite the preliminary audit report's discussion of "ghost employees" it found no evidence of this ever occurring and program practices simply reflect industry norms. Either industry norms should be used as a basis for evaluating VSW practices, or all discussion of this issue eliminated from the report.

Page 23, paragraph six, third sentence: *"Between the three projects, the on-site manager failed to provide DEC with the required agreements for 35 employees, including his spouse."* The three projects referenced were the Voznesenka, Nikolaevsk and Nulato projects. Each of these projects had the same superintendent. Following the discovery of the missing agreements by the auditor, we reviewed the files for these projects and the proper employment forms are now in place. Again the audit brings up the single case of nepotism.

Page 24, second paragraph: *"Nevertheless, this scenario placed the manager in an unacceptable position when coupled with his private custody of the individual timesheets and the other factors we discuss above. A skeptical business world simply assumes a higher risk of ghost employees when a payroll process, from hiring to paycheck distribution, is dominated by one person in a remote setting. This basic shortcoming is another symptom of the over-delegation that can result when engineers lack the business support services found in larger organizations."* We reiterate: the VSW program's timesheet procedures reflect construction management norms. Despite the preliminary audit report's discussion of "ghost employees" it found no evidence of this ever occurring and program practices simply reflect industry norms. Either industry norms should be used as a basis for evaluating VSW practices, or all discussion of this issue eliminated from the report.

Page 24, paragraph 6: *"As we discuss in Recommendation No. 1, the longer term solution for this and other shortcomings in business infrastructure is to relocate the VSW program within DOTPF's public facilities section."* We disagree for reasons stated elsewhere in this response.

Page 24, footnote 46: *"We have discussed particular concerns with DEC management. However, due to confidentiality of ethics act disclosures, this report does not attempt to cite any particular example."* The report could not "cite any particular example" because none existed, not because of confidentiality concerns. The audit revealed no conflicts of interest or other Ethics Act violations. A review by a Department of Administration official found no violations.

Page 25, second paragraph: *However, in the zeal "just to get things done", DEC has left on-site managers in an unregulated void when it comes to some basic business safeguards that the public has a right to expect. We disagree with the characterization of the VSW process as unbounded "zeal 'just to get things done.'"* For the most part, the VSW program guidance contains sufficient instruction to guide program activities.

Page 25, fifth paragraph, first sentence: *"Clear standards regarding nepotism are another needed business safeguard. The audit accurately revealed an incident of nepotism that should never have been tolerated. A new policy on nepotism is being prepared and will be in effect before the construction season (by May 1 of this year).*

Page 26, paragraph one, first sentence: *"Another troublesome situation concerns an on-site manager's personal purchase of a home rented at DEC expense."* This statement is in regards to the Voznesenka project. This statement is simply untrue. The superintendent did not purchase the rental home.

Page 26, paragraph one, third sentence: *"At the beginning of the tenancy, repairs were made at DEC expense including plumbing and painting."* This is correct and we agree that it was a questionable judgment. The audit report, however, should point out that the improvements were necessary, at least in part, to allow the residence to serve as crew quarters. The report's implication that the work was simply a matter of improving the home for the personal comfort of the superintendent should be amended to reflect the complete picture.

Page 26, third paragraph: *"When DEC inquired about this transaction, the on-site manager responded that he (1) had sold his condo in Arizona, (2) had decided to stay in Alaska, (3) was purchasing this house for the sake of the project, (4) was doing DEC a favor since it would not have to move its equipment and furnishings, (5) was allowing the community continued use of the office and shop in return for an eventual charitable tax deduction, and (6) was currently completing an application for further DEC funding. He also indicated that the community president and he may sue the state for defamation and implying a conflict of interest by inquiring about the transactions."* The audit report should indicate that the superintendent did not purchase the home.

3132 CHANNEL DRIVE
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OFFICE OF THE COMMISSIONER

February 5, 2004

Ms. Pat Davidson, Auditor In-Charge
Division of Legislative Audit
PO Box 113300
Juneau, AK 99811-3300

Dear Ms. Davidson:

I appreciate the opportunity to respond to Legislative Audit's preliminary report concerning the Village Safe Water (VSW) Program, Selected Projects. As I stated in my response to the management letter of the same program, my review of the audit is based on the Department of Transportation's program of competitive public works construction projects rather than the Village Safe Water program of grants to communities. As such, these are two very different programs.

The Department participates with the Department of Environmental Conservation (DEC) in many of the VSW projects by designing the road or boardwalk that becomes part of the project. However, we typically will do a Memorandum of Agreement (MOA) with an entity such as the Bureau of Indian Affairs (BIA) or the Alaska Native Tribal Health Consortium (ANTHC) for construction.

Adding \$100 million a year to our normal program, such as last year's bond package did, was an additive increase, and has taxed our resources, but to add an entirely new type of program, such as VSW, would require additional personnel and resources.

The Department of Transportation will gladly assist the Department of Environmental Conservation and the Village Safe Water Program in any way DEC desires, including making our business and contracting support services and training programs available to the VSW Engineers.

Sincerely,

Mike Barton
Commissioner

February 13, 2004

Members of the Legislative Budget
and Audit Committee

We have reviewed the response to our preliminary audit on the Department of Environmental Conservation (DEC), Village Safe Water (VSW) Program. Nothing contained in the response gives us cause to reconsider our findings, recommendations, or conclusions.

DEC's response indicates a willingness to address some of the management control weaknesses discussed in the report and have included estimated implementation dates for improved controls over tax reporting issues, superintendent compensation, and nepotism. DEC also recognizes the need to improve procurement and contracting support for the VSW program. However, the response also listed a number of objections to other management control weaknesses discussed in the report. Most of these objections can be grouped into five general categories which are discussed below.

Appropriate audit criteria

DEC asserts "standard construction management practices" were not used as the criteria for evaluating this program. This audit compared VSW practices to those required of it by: 1) the Environmental Protection Agency (EPA); 2) the U.S. Department of Agriculture (USDA); 3) VSW procedure manuals; and 4) standard procurement and accounting controls. We do not agree with DEC that the program should be allowed to ignore EPA, USDA, and VSW requirements. Even if some of the construction industry follows looser procedures, VSW must adhere to the procedures established by its program and by its public entity status.

All audit findings discussed with department staff

DEC's response states we did not provide information that the department needed to examine its processes or to respond to the audit report. This is untrue. We obtained most of our audit evidence from DEC staff and discussed all significant factual finding with at least two DEC staff members. This is done in the normal course of all of our audits. Further, Government

Audit Standards require reports to be clear and concise, as lengthy, highly-detailed reports are not effective in communicating with the public.

Ambiguous responsibility for project funds

DEC's response takes exception to our use of the term "in trust" and says "grant funds are not held 'in trust' for each project community." In direct contrast, the VSW procedure manual, which sets the ground rules by agreement with the federal funding agencies, includes a letter from EPA that states, in part:

According to the [VSW] manual and confirming discussions with [named employees] of VSW, the state's "grant offer" to the village stipulates that a VSW engineer will represent the village in all technical matters related to the . . . project, and is the sole person to approve invoices and timesheets for payment. . .

Basically the village does not control the grant funds and is not accountable to the state for expenditures, and is therefore not a true "subgrantee. . ."

According to our regional [EPA] counsel, the true relationship that exists between the state and the villages during the course of these projects is in the nature of a trust where control of the project funds actually rests with the state for the benefit of the villages. Upon completion of a project, title to the facilities then passes from the state to the villages, completing the trust. [emphasis added]

Further, an attorney general memorandum of advice¹ directed to DEC states the following:

The accounting firm is a trustee acting on behalf of the villages and is procured by [DEC]. . . The accounting firm maintains a check register, writes payroll and pays vendors for deliverables of the project which have been approved by DEC's VSW engineer. . . Under its trusteeship, an accounting firm may maintain several villages' accounts. . . [emphasis added]

Such an oversight status obviously carries important fiduciary responsibilities.

Lack of perceived need for improved spending controls

Each example of questionable purchasing was reviewed with the individuals that approved them for DEC. As necessary, we conducted a further review with the employee's supervisor. For instance, we clearly state that DEC's engineer was unable to obtain an adequate justification for the prices of the items shown in Exhibit 4 on page 11 of the audit report. We

¹ Department of Law memorandum 663-97-0368 (Feb. 3, 1998), pp. 2, 3.

reviewed the documentation with the engineer in each instance, who in turn had the opportunity to review it with the on-site manager. The point was that the documentation should have supported the pricing at inception and it certainly should have supported it after these additional steps.

DEC's response downplays the waste from unnecessary payments of sales tax. From the pattern we observed with a variety of vendors, not just isolated "minor office supplies" as indicated in the response, opportunities to economize were simply neglected.

Similarly, there is an attempt to deflect concerns regarding the \$1,700 expense-paid trip for basic computer training that was available for \$102 from the local college or from the State itself at no charge. The point was, of course, not to refute the need for the training itself, rather to point out the wasteful excess expenditure.

Finally, DEC's response also suggests that the seven wells drilled for a 55-home project function as some sort of coordinated network. However, DEC records instead show a frustrating geophysical search for water that should have been resolved long before the funds were all dissipated into the numerous lesser priorities we list in the report. The DEC engineer currently states that there may be some upcoming feasibility work to determine if two of the seven wells can be linked or if a new water source will be need to be found.

Minimized need for timesheet reviews

Some of the neglected procedures are specified in the VSW procedure manual itself. While DEC's response cites "industry norms" in a generic fashion, references to its own prescribed rules are markedly absent. This highlights a problem since the VSW procedure manual serves as the program's ground rules by agreement with the federal funding agencies.

For instance, DEC dismisses the need for VSW engineers to approve the timesheets signed by force account employees and the on-site managers that may be paid over \$100,000 a year. Though the VSW manual has accumulated some ambiguities over the years, it still contains definite instructions for these timesheets to be forwarded to the assigned DEC engineer for approval.²

Despite the manual's guidance, DEC's response states that "[t]imesheet summaries are submitted by superintendents and are reviewed by VSW" [emphasis added]. This reflects a discrepancy between what the engineers do in practice and what DEC management expects to be done.

² For instance, Section I of the manual states that "The Village Safe Water Project Engineer must approve all invoices and timesheets for payment by [the contract CPA firm]." DEC's proposed redraft of the manual states, "The Village Safe Water Engineer responsible for a project must stamp and approve all invoices and timesheets for that project." DEC's supplementary manual for on-site managers states, "Original timesheets will be forwarded to the Project Engineer along with the pay period construction progress report . . ."

In the projects selected for our detailed review of payroll procedures, the assigned engineers indicated that they reviewed neither individuals' timesheets nor summaries of timesheets. In interviews of other DEC engineers, we discovered that even reviews of the summaries were actually the exception rather than the rule.

Oversight of potential conflicts of interest

Our report cited an on-site manager's plans to personally purchase the home that DEC had improved and rented for his project duties. The seller was the president of the community that owns the VSW project. DEC's response simply states that "*the superintendent did not purchase the home.*"

Information regarding this planned purchase was reported to us by three DEC engineers and supplemented by records they supplied. The records clearly showed that DEC approved the back rent and that the on-site manager intended to occupy the home in a personal capacity at the end of the lease, settled on a formal closing date for the purchase, obtained a survey and an appraisal of the property in preparation for purchase, received an estimate of closing costs from a lender, and intended to proceed with the purchase.

We appreciate the information that this purchase may have been modified or cancelled. Nevertheless, the fact remains that this type of situation was allowed to progress. This incident illustrates the need for DEC to articulate clear expectations for both its own employees and those employed by project communities.

Similarly, DEC insists that it has now reviewed the Executive Branch Ethics Act with its own employees and satisfied itself as to their conformance. Our review of past disclosures and management's approach to them showed a substantial need for improvement in DEC's procedures to prevent violations. We appreciate the commissioner's assurance that this issue has been thoroughly addressed.

In summary, we reaffirm the findings and conclusions presented in the report.

Pat Davidson, CPA
Legislative Auditor