DOCUMENT RESUME

ED 428 519 EF 005 262

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TITLE	Building Clean. The Control of Crime, Corruption, and Racketeering in the Public Construction Markets of New York City. A Preliminary Assessment of Efforts Made by the Office of the Inspector General, New York City School Construction Authority.
INSTITUTION	Harvard Univ., Cambridge, MA. Kennedy School of Government.
SPONS AGENCY	Department of Justice, Washington, DC. National Inst. of Justice.
PUB DATE	1996-02-00
NOTE	146p.
CONTRACT	91-IJ-CX-0009
PUB TYPE	Reports - Descriptive (141)
EDRS PRICE	MF01/PC06 Plus Postage.
DESCRIPTORS	*Crime Prevention; Elementary Secondary Education; *Planning; *Public Schools; *School Construction
IDENTIFIERS	Evaluation Reports; *New York City School Construction Authority; New York (New York Metropolitan Area); *Racketeering

ABSTRACT

The Office of the Inspector General of the New York City School Construction Authority (SCA) is attempting to secure the School Construction Authority and its building program from crime, corruption, and racketeering. This report is a preliminary assessment of this effort. It sets forth for practitioners and theorists the strategy that guided the establishment and operations of the SCA Inspector General and the key issues of implementation it faced in seeking to accomplish its purposes. It discusses the goals and other measures of success by which the SCA Inspector General would hold itself to account, the strategies used, and the underlying assumptions it made about the world it faced; examines whether and how the SCA Inspector General enacted its theory in concrete operations; and determines the effectiveness of the SCA Inspector General which assessed the outcomes and outputs for which the Office was held accountable. Finally, the report suggests further ways and means to evaluate more completely the impacts of the Inspector General's efforts on SCA building metrics of price and performance; on the public construction markets in New York City, more broadly; and on organized crime in the city. (GR)

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BUILDING CLEAN

THE CONTROL OF CRIME, CORRUPTION, AND RACKETEERING IN THE PUBLIC CONSTRUCTION MARKETS OF NEW YORK CITY

A PRELIMINARY ASSESSMENT OF EFFORTS MADE BY THE OFFICE OF THE INSPECTOR GENERAL, NEW YORK CITY SCHOOL CONSTRUCTION AUTHORITY

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U.S. DEPARTMENT OF EDUCATION
EDUCATIONAL RESOURCES INFORMATION CENTER (ERIC)

February 1996

Final Report to the National Institute of Justice
Grant Number 91-IJ-CX-0009

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TAX ABATEMENTS FOR MOB CARTELS?

-- New York *Observer*, August 28, 1995

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I. INTRODUCTION[1]

In this publication, we report the preliminary assessment of the efforts of the Office of the Inspector General of the New York City School Construction Authority to secure the School Construction Authority (SCA) and its building program from crime, corruption and racketeering.

The operations of the SCA Inspector General comprised an opportunistic test of a complex strategy to combat organized crime and its control of legitimate industries and markets. But for the chance that developed in the late 1980s and early 1990s to rebuild New York City's schools, the idea of such an approach -- variously labeled "comprehensive," "multijurisdictional," and "market-based" -- would have been that: merely an idea. Instead, public builders and law enforcement agencies, concerned and intent to protect the SCA and its $4.3 billion capital program from crime and corruption, came together to attack organized crime at its sources, to reform the SCA's own procedures, and to "level the playing field" for legitimate firms in the hopes of inducing their return to the market and to the SCA's vendor pool.

Having seized that opportunity, our challenge is to discern what can be learned from their efforts. This preliminary assessment examines and analyzes the policies and practices of the SCA Inspector General as it attempted to put these important and innovative theories into operation. It also establishes the foundation for a more rigorous and formal outcome evaluation of the SCA's efforts in the future.

The Three Objectives of the Assessment

The principal, substantive aim of the assessment is to set forth for practitioners and theorists the strategy that guided the establishment and operations of the SCA Inspector General, and the key issues of implementation it faced in seeking to accomplish its purposes.

Our first task is to give an accurate account of the theory of action of the SCA Inspector General: the goals and other measures of success by which it would hold itself to account; the strategies it embraced to achieve its goals; and the underlying assumptions it made about the world it faced -- about the relationships among public construction, organized crime, and civil and criminal law enforcement in New York City -- that bound its strategies to its goals.

Our second task is to document in detail whether and how the SCA Inspector General enacted its theory in concrete operations. This includes describing its operational objectives, and the organization architecture it used to translate theory into practice: the

[1] The authors gratefully acknowledge the assistance of Harvey Simon in the preparation of this study.

procedures, structures and means it used to establish itself and to function; the authorities, skills and resources it acquired and used to accomplish its mission; and the priorities it set and the actions it took to realize its goals and objectives.

Third, our final task is to provide a preliminary consideration of the effectiveness of the SCA Inspector General. This objective includes taking stock of the outputs and outcomes for which the Office can be held to account. We suggest further ways and means to evaluate more completely the impacts of the Inspector General's efforts on SCA building metrics of price and performance; on the public construction markets in New York City, more broadly; and on organized crime in the city. This includes identifying the data that would be essential to gather to complete such an outcome evaluation.

II. THE OPERATING THEORY OF THE INSPECTOR GENERAL

Introduction

At the outset, it is useful to set out a clear idea of the theory that justifies, animates, and guides the SCA Inspector General. This establishes the basic frame to be used in evaluating the Office. In subsequent sections of this report, we explore the context leading up to the establishment of the Office, the ways in which the operational theory of the Inspector General was enacted in structures and operations, and the establishment of key working relationships within the Office, and between it and the wider law enforcement community. Finally, we present some preliminary judgments about what seems to have worked well, and how the enterprise as a whole could be more formally evaluated.

* * *

Society has long sought an effective response to the problem of organized crime. It has seemed outrageous that individuals who built organizations devoted to amassing wealth and political power by criminal means could effectively defy the law. It seemed urgent that society find some way to reduce the toll in corruption, crime and financial costs that organized crime imposed on the rest of society.

Finding an effective response has proven elusive. Until very recently, much of society's effort has focused on developing improved law enforcement methods to investigate and prosecute organized crime's leaders, soldiers and associates. Starting with the development of rackets bureaus in the 1930s, and proceeding through the formation of sophisticated organized crime intelligence units that became authorized to conduct wiretap surveillance, and armed with the special powers granted by the Racketeer Influenced and Corrupt Organization (RICO) statutes, the law enforcement community gradually improved its capacity to prosecute organized crime figures.[2] As a result, in many cities throughout the United States, organized crime figures have gone to prison, often for long periods of time.[3] Yet though many Mafia bosses and associates are dead or behind bars, recent reports of the mob's "demise" have also turned out to be premature.[4]

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[2] See discussion of rackets bureaus and RICO statutes *infra*, pp. 14-16.

[3] "With their main Mafia targets convicted or awaiting trial, Federal and state authorities in the metropolitan region are preparing a new campaign against the second tier of organized crime leaders in New York and New Jersey. In the last five years, most of the Mafia's bosses, underbosses, and acting bosses – John Gotti, Salvatore Gravano, Carmine Persico, Victor Orena, Alphonse D'Arco and Vittorio Amuso – have been imprisoned or have defected to become Government witnesses... 'The trend is that

In the 1980s, a cluster of new ideas emerged about how to deal with organized crime. Following a succession of highly-publicized revelations and inquiries concerning crime and corruption in construction in New York, then-Governor Mario M. Cuomo of New York directed the New York State Organized Crime Task Force (OCTF) to investigate racketeering in the New York City construction industry. In its findings and recommendations, OCTF developed a theory of organized crime control that referred alternately to the "comprehensive" model of organized crime control, and to the "multijurisdictional" approach. The first full statement of this theory was presented in the OCTF report.[5]

The Problem Of Racketeering, Crime And Corruption In The New York City Construction Markets

Even in the best of circumstances construction is a precarious enterprise. Weather conditions may wreak havoc with construction schedules. Materials needed for a particular stage of construction may be lost in road accidents, or arrive in damaged condition. Subcontractors may go out of business or perform below industry standards. Labor problems may disrupt the smooth flow of work and cause unexpected or costly delays.[6] Like other human endeavors, construction projects may also be sapped by the commonly-found forms of human incompetence and venality. Workers will fall short of perfection in mixing cement, or nailing 2x4's, or installing plumbing and wiring. The construction bosses and public inspectors who are supposed to guarantee the quality of the work may be overloaded or preoccupied. Some tools and materials will disappear from the site either by oversight, or because the workers needed them and thought no one would notice.

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there is no escape for mob bosses,' said Ronald Goldstock, the director of New York State's Organized Crime Task Force. 'The fate of anyone who assumes a leadership position in a Costa Nostra family is a life prison sentence or assassination by a rival.' " Selwyn Raab, "Prosecutors Shift Attack Against Mafia." New York *Times*, January 24, 1993.

[4] "Recurring rumors of the Mafia's decline have typically turned out to be greatly exaggerated. In many American cities, tales of mob control of unions and of entire industries, such as waste-removal and construction, are legion. Yet for years, too, prosecutors have trumpeted the arrest of organized crime bosses and the purging of mobsters from legitimate businesses...While the mob is reeling in some other cities, the remarkable resilience of organized crime in New York, home to the five strongest Mafia families, was abundantly dramatized by recent events..." Selwyn Raab, "Where the Mob Still Muscles In." New York *Times*, May 7, 1995.

[5] See, New York State Organized Crime Task Force. *Corruption and Racketeering in the New York City Construction Industry: Final Report to Governor Mario M. Cuomo from the New York State Organized Crime Task Force*. New York: New York University Press. 1990

[6] "[C]onstruction is a somewhat disorganized, disruptive, labor intensive and unpredictable process in the best circumstances...it requires thorough coordination from project inception to completion. In short, the central problem of public construction is coordination..." City of New York, Office of the Mayor, *Wicks Law Repeal - A Public Construction Necessity*, September, 1984. Cited in OCTF, *Final Report*, 1990.

For these reasons there is often a gap between the ideal and what is actually produced on construction projects. And that, in turn, may contribute to a widespread impression that construction is inherently hard to manage efficiently and cleanly, without having to engage in criminal activity and corruption to complete projects on time, on budget, and to accepted standards of quality.

By all accounts, however, the New York City construction industry suffered from far more than these ordinary problems. In its final report to the Governor, *Corruption and Racketeering in the New York City Construction Industry,* OCTF presented evidence that the industry was, in fact, riddled with crime and corruption. Whether the crime comprised the opportunistic theft of valuable supplies and equipment by lone individuals, or the systematic shakedowns of contractors by crews having connections to traditional mob syndicates, or, as in the pillaging of union pension funds and trusts, the ongoing criminal enterprises of the syndicates themselves, the fact was that crime plagued the city's construction industry. As such crimes often required the complicity of public officials, corruption in the regulation and administration of construction was also found to be rampant.

The Three Impacts Of Crime And Corruption In The New York City Construction Markets

As a problem affecting New York City's single largest industry, the issue of the crime and corruption in construction matters was one of great public importance. First, crime and corruption degraded industry *performance*, including price and quality. Second, it *implicated government institutions* in the corruption and waste that was rampant, particularly in public construction. Third, it *helped organized crime families to establish an extraordinary operating and financial base in New York.*

Price, Performance and Quality Impacts

Crime and corruption impacted the *performance* of the industry. In private industry, this impact principally manifested itself in increased costs. Sometimes the crime involved the wholesale theft of materials. Other times, organized crime groups rigged bids so that the lowest bid submitted for a job remained well above the real cost of doing the construction. Sophisticated racketeers who controlled labor unions, for example, also controlled the flow of materiel and supplies to construction sites. They could, and frequently did, use this leverage to raise the price of goods and services delivered, to force companies to pay more for "labor peace" even as the racketeers stole from the payroll and pension funds that were supposed to be delivered to workers.

The quality of major construction in the private sector was, however, not often in doubt: New York City's builders had produced some of the world's most magnificently engineered and rendered architecture. The New York City construction marketplace simply included in its prices the cost of organized crime influence and control of numerous of its aspects.

On the public side, by contrast, there was a significant impact not only on the cost of construction goods and services, but also on the times to completion and on the quality of the finished product. OCTF concluded in its *Final Report* that New York City public construction projects had become "multibillion dollar spending programs that hemorrhage money through fraud, waste and abuse." [7]

During the New York City Board of Education's reign over the school building in the city, delays were the rule.[8] With its cumbersome procedures and huge bureaucracies, it was quite possible that from design to completion a new school might take years. A

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[7] The OCTF *Final Report* asserted that "public construction projects are more vulnerable to fraud, waste and abuse than private construction projects because of the complex body of laws regulating the public construction process, the intense political pressure to begin and complete public works, and the severe administrative and personnel deficiencies in their administration. ...Many public contracting requirements and multilayer review procedures, originally instituted to assure fairness and prevent corruption, have instead resulted in less accountability and more corruption susceptibility." OCTF, *Final Report*, 1990, Pg. 251.

[8] Prior to the SCA, the Board of Education's Division of School Buildings had been responsible for designing and overseeing the construction of new buildings, as well as maintaining existing ones. The New York *Times* characterized the Board's construction procurement program, generally, as "a bureaucracy whose arcane regulations and complex web of divisions and bureaus opened the way for bid-rigging, bribery and the fabrication of evidence... 'It has loads of bureaus and lots of people with titles that don't match their jobs,' [one investigator] said. 'There were officials with very important sounding titles that didn't have much real power, and others with lowly titles but a lot of important responsibility. It was very hard to figure out.'" (Sam Dillon, "School Board's Maze a Factor in Scandal." New York *Times*, May 22, 1994.) The bureaucratic task of procurement seemed, in fact, to have a life and a logic all its own, but little to do with oversight of the finished product. Kevin Ford, the Inspector General's first General Counsel observed of the Board, "There was an awful lot of red tape on approvals, but no analysis of the work being done." (Kevin Ford, interview, 1992.)

single Manhattan high school, for example, had taken two decades to build, and seemed to reveal only the surface of a deep well of corruption, ineffectiveness and scandal:

> Intended to replace the famous High School for the Performing Arts, La Guardia High School was designed in 1969, the estimated cost being $9 million. Bid in 1972, it was begun in 1973. Construction was halted in 1974 and resumed in 1979. Completion was expected in 1982, at a cost of $39 million. By 1989, the project had cost $90 million, and major features of the school were still not completed, had failed, or had been abandoned. Several prosecutorial and investigative agencies [were] investigating this public construction debacle. [9]

Legitimate vendors fled the Board's vendor pool.[10] In their place, firms that were incompetent, or intent on defrauding the Board, or racketeer-influenced and controlled, or all three, came to dominate school construction. Buildings that were shoddy, long-delayed and high-priced became common. Thomas D. Thacher II, who in 1990 became the first Inspector General of the New York City School Construction Authority, reflected on the loss of high quality firms to the public construction marketplace:

> "The analysis we did showed that many clean contractors simply avoided public construction. Why? Because the playing field is almost never a level one. The low-bid system too often has government awarding contracts to the company who's prepared to cheat the best. Those who are prepared to cheat submit lowball bids and make up their profits later through underperformance and overbilling. Government has utterly failed to screen out these dirty, mobbed up companies from bidding on important public works projects.
>
> "In making up their loss later, they will have left a trail. But there's no institutional mechanism to examine that trail and to make them pay for their underperformance and overbilling. Short of being prosecuted, they can come back to play the next time, bidding on the next contract. Even if someone's performance has been terrible, the government rarely debars them. Typically, because the contractor was fully paid on the last contract, allowed to finish the job, and wasn't defaulted, the evidence to support a debarment is just not there. As a result, the bad contractors again and again get the contracts. Good contractors don't want to compete because they know bad contractors are going to low ball their bids, underperform, and overcharge."[11]

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[9] OCTF *Final Report*, 1991, pg. 141. See the *Report*, generally, pp. 135-263, for a detailed assessment of the issues and opportunities for reform of the construction industry in New York City.

[10] Thacher recalled that "when it was created, the SCA had two strikes against it. First, the bulk of contractors doing school work were at the low-end of the scale. Players who'd had to accommodate floats of months and an ineffectual bureaucracy managing the process. Quality players had fled and stayed in the private sector. The Board of Education was at the bottom of the list of good places to work, after the City, the Port Authority, and others. So, we had to purge them. But, second, we also had to attract new players. The recession in 1988 helped add players who'd never done public construction, let alone schools. E.g., Herber, HRH, Tischman. But we also had to eliminate bad players in order to attract new players to the game. These people didn't want to be seen at the same party. They were happy to have an Inspector General's office around." Thomas D. Thacher II, interview (1992).

[11] Thomas D. Thacher II, interview (1995).

Impacts on Government Operations and Public Perceptions

Second, the prevalence of crime and corruption in the New York City construction industry *seemed to implicate government institutions* in tolerating if not outright abetting the wastes, frauds and abuses being perpetrated upon the taxpayer. Many of the crimes committed within the industry were possible only through the corruption of public officials whose job it was to prevent such things from happening. Inspectors, hired to ensure that construction projects in both private and public sectors met stringent construction standards, were bribed to overlook shoddy construction.[12] Procurement officials, charged with the responsibility for contracting of public construction projects at the lowest possible cost, were bribed to provide information to corrupt firms about the specification to have been met, or the bids that were made by legitimate firms.[13]

Even with a succession of prosecutions, the problems giving rise to crime and corruption in the industry seemed to persist over generations. Government has appeared alternately as hostage and victim, as indifferent and resigned, or as complicitous and criminal. When confronted with the fact of crime and corruption in the industry, government's acquiescence or its outright denials have only seemed to implicate it further, for the public well-knew the score. Entire bureaucracies that were charged with securing the market on the public's behalf appeared at best helpless, undoubtedly inept, and at worst intimately implicated in criminal enterprises. With public construction so obviously plagued by performance issues of delay, poor quality and high prices, the corruption that it required and that accompanied it was as demoralizing as it was overt and enduring.

Impacts On Organized Crime

Third, the prevalence of crime and corruption *helped organized crime establish an extraordinary operating and financial base in New York,* and further emboldened racketeers and strengthened their hand. Firms sought a competitive advantage from cheating, and secured it by aligning themselves with organized crime. And criminal opportunities, no matter how small, might attract organized crime individuals or syndicates, seeking to exploit the moment for fast, one-time profits, or for a longer-term racketeering venture:

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[12] Over the years city newspapers reported frequent allegations and investigations of corruption in Board-managed facilities and programs. In 1986, for example, Brooklyn prosecutors indicted almost a quarter of the Board of Education's maintenance supervisors and inspectors on bribery charges in a scheme that District Attorney Elizabeth Holtzman reported had been going on for "nearly a decade and involved tens of millions of dollars." New York City Board of Education, Office of the Inspector General, *Division of School Buildings - A Review of Management Controls: Conclusions and Recommendations.* 1987. Cited in OCTF, *Final Report*, 1990.

[13] "Manipulation and fraud can infect contract letting, even in the face of apparent conformity with lowest-responsible bidding procedures. Corrupt officials can 'sell' inside information about in-house estimates or about other bidders and their bids. Design specifications can be drawn in such a way as to favor certain contractors." OCTF, *Final Report*, 1990.

> The large concentration of racketeers in New York City capable of exploiting the construction industry's racketeering susceptibility and potential, along with the instabilities and uncertainties created by the industry's fragility and fragmentation, create a need for a "rationalizing body." This body must be able to regulate the predatory activities of the racketeers and must have the influence necessary to bring coordination and predictability to the construction process. Organized crime syndicates can, and do, play both these roles. By controlling the activities of disparate groups of racketeers preying on the industry, syndicates can assure contractors that they will only have to pay off once for a specified result, that the amount to be paid will be "reasonable," and that "services" paid for will be delivered...This rationalizing function is not provided for altruistic reasons. [14]

The control of job sites, labor unions, construction firms, critical trades, and the flow of equipment and supplies provided the city's organized crime families with a steady stream of cash, wealth and power. Whether the criminal opportunities to make money were created by chance, or by firms intent on cheating to win -- by exploiting a weak procedure, a structural market inefficiency, a corrupt official, or lax oversight -- organized crime could, and, if it made good economic sense, *would*, take steps, ultimately, to control the opportunity for itself. For seizing control of these opportunities provided the rationalizing effect that was central to organized crime's strategy and power in the construction industry.

The Failure Of Market Forces, Regulation And Enforcement To Curb Crime And Corruption

Ordinarily, natural market pressures should have helped produce clean, high-performing markets, including those for public construction. After all, since many public customers presumably prefer to buy high-quality, low-priced construction from contractors who are not part of ongoing racketeering enterprises or prone to fraudulent schemes and other crimes, construction firms should arise offering such a product. Moreover, since construction firms have an interest in maintaining their reputations for quality construction and avoiding theft by their employees, competent firms should stand out and gain market share.

No doubt, these forces did exert some influence on the public construction marketplace, producing some submarkets of high-quality, honest work, and preventing organized crime from achieving dominance. The problem, rather, was that these mechanisms did not work powerfully enough throughout the marketplace. Even if honest firms withstand the "carrot and stick" tactics of bribery and extortion, honest firms remain vulnerable to unfair competition from firms that set much lower standards of performance, but that nonetheless escape the penalty for their shoddy work by being skilled in litigating

[14] OCTF, *Final Report*, 1990, Pg. 65.

change orders and contracts, escaping oversight, or corrupting inspection officials. In effect, firms that steal from public customers by giving less performance for the money maintain their competitive positions over honest firms by some combination of fraud, bribery, and extortion. Without external interventions, and relying instead solely on market forces, it turns out that *these* nefarious skills set the competitive standard in the marketplace, instead of the skills associated with building clean, at high standards of efficiency, price and performance.[15]

Unable to rely on market forces to develop corruption-free building and builders, the complex civil regulatory apparatus that had been built up to regulate public construction in New York City should have prevented the markets from performing poorly. Instead, this apparatus failed to reach deeply into the public construction marketplace or to improve its overall performance.[16] The methods for regulating construction could be easily corrupted, as could the methods designed to promote competitive procurement.[17] This has been particularly true when organized crime lurked in the background exploiting the greed and fears of the individuals whose job it was to buy, build, and inspect construction in New York City.

In sum, the Board's and the City's construction practices had, over time, not only failed to provide high quality, on time, low cost buildings. Their practices left the door of public construction open to crime, criminal schemes, and the systematic racketeering of organized crime. By all accounts, each of the five *La Cosa Nostra* families -- Gambino,

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[15] "Organizations competing for resources in the same environment but using different forms vary in their probability of being positively selected. Positively selected organizational forms are more *fit*, vis-à-vis that particular environment, than those not surviving... If a particular environment consists of a corrupt political machine opening the bidding on city contracts, then the 'fit' firm is the one most free with bribes and special favors." See, Howard E. Aldrich, *Organizations and Environments*. Englewood, NJ: Prentice Hall. 1975. Pp. 106-135.

[16] The public sector's own procedures created innumerable procedural and bureaucratic delays in completing projects, as well as sharply-felt political pressures to get projects done. Ultimately, agencies often worried less about criminals and contractors than about finishing long-delayed work. "In the public arena," Thacher observed, "voters evaluate the mayor or the governor on how fast construction projects are finished. As a Commissioner who's been appointed by the mayor or governor to build schools, roads, or sewage treatment plants, you're going to be evaluated first, on whether you build those items, and second, on whether there's been waste, fraud, or abuse." (Thomas D. Thacher II, interview, 1992). "Agency managers," the OCTF *Final Report* concluded, "may strain to define their problems as civil rather than criminal...if it is likely to slow down a construction project." OCTF, *Final Report*, 1990.

[17] New York State laws required public builders to award contracts to the lowest responsible bidder. Though the system reduced favoritism, it erected perverse new incentives for fraud. Vendors might fraudulently bid low to win, for example, all the while planning to pay their workers less than the legally required wage scale, or to bribe inspectors to ignore violations of costly contract specifications which they never intended to meet. The system also induced the excessive use of change orders and post-construction lawsuits to escalate costs. The practice was so widespread as to "make a mockery of the competitive bidding system." Indeed, the OCTF report found that "fraud, waste and abuse are so closely linked to the competitive bidding system that it is natural to ask whether that systems should be abolished altogether." For an excellent discussion of the impacts of lowest responsible bidder systems on quality in public procurement, generally, see Steven Kelman, *Procurement and Public Management: The Fear of Discretion and The Quality Of Government Performance*. Washington, DC: The AEI Press. 1990.

Genovese, Lucchese, Colombo and Bonanno -- was, by the late 1980s and early 1990s, firmly established in the New York City construction industry, corrupting officials, further degrading quality, and exacerbating the already-high costs of public and private construction. [18]

For brief moments, then, the public response to the problem of crime and corruption in public construction had been energetic in seeking either to reform limited aspects of its broken procurement, inspections, or regulatory machinery, on the one hand, or in attacking crime and organized crime acting in it on the other. The results, however, were imperfect, fleeting, and finally of little enduring consequence, either to the marketplace, or to organized crime's hold on it.

To law enforcement theorists and practitioners, the evidence was conclusive that law enforcement methods alone -- investigating and prosecuting individuals or syndicates of racketeers that were active in construction -- had failed, and would like continue to fail to reduce crime and corruption in that critical marketplace. "The courts, police and prosecutors, acting alone," Thacher wrote, "simply do not have the power to block the myriad opportunities for organized crime's successful exploitation" of the industry. "[T]he opportunities to engage in racketeering are so many and the incentives to reach out for the services of racketeers are so great that criminal sanctions alone cannot possibly constitute a sufficient deterrent."[19]

What was required was a comprehensive approach that considered the victim, the market and the predators as inextricably linked. To succeed, the approach required skills, authorities and resources deployed simultaneously to protect legitimate buyers and sellers, to repair broken market procedures, and to suppress organized crime.

Prior Strategic Innovation

The theme of law enforcement's limitations and its inability to deal effectively with the complex problems of corruption and organized crime in legitimate industries was an established one.

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[18] In spite of a succession of prosecutions over a period of seven decades, individual criminals, racketeers and syndicates came and went, and came again -- Robert Brindell in the 1920's, Tamany Hall, and more recently *La Cosa Nostra*. "Gleaming" prosecutions of individuals and syndicates, as Thacher characterized those in New York of the 1980s, simply seemed to leave the business open to the next wave of criminals eager to capitalize on the industry's structural weaknesses. "Even with the recent, stunning successes of prosecutors in targeting organized crime families," Thacher observed, "one cannot say that there has followed a diminution of racketeering." Thomas D. Thacher II, interview (1992).

[19] Thomas D. Thacher II, "Institutional Innovation in Controlling Organized Crime: Reflections on the Recent Integration of Law Enforcement Personnel with Industry Policy Makers in New York City School Construction." Presented to the Fifth International Anti-Corruption Conference, Amsterdam, March 11, 1992; reprinted in Cyrille Fijnaut and James Jacobs, eds., *Organized Crime and its Containment: A Transatlantic Initiative*, pp. 169-182.

Rackets Bureaus

During the 1920's and 1930's American prosecutors discovered the *technical* difficulties involved in investigating and prosecuting the complex conspiracies that were typical of racketeering enterprises. Unlike violent crime, the conspiracies might have few overt manifestations, and they proved resistant to the traditional gumshoe and trial lawyer approach of police and prosecutors at the time. [20]

As the power of organized criminal enterprises seemed to reach their zenith, the government initiated a new response: the rackets bureau. This model -- which teamed investigators, accountants, and prosecutors -- reflected an image of proactive investigators, using a variety of statutes to bring justice to bear on organized crime figures. It represented a radical improvement in the art of fighting organized crime that endures at the core of modern control efforts.[21]

The RICO Innovations

In the 1970s, important amendments to the rackets bureau model reflected the discovery that significant tactical challenges remained that went beyond the mere issues of

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[20] G. Robert Blakey, Ronald Goldstock, and Charles H. Rogovin. *Rackets Bureaus: Investigation and Prosecution of Organized Crime.* Washington, DC: Law Enforcement Assistance Administration, United States Department of Justice. 1978. The authors offer a useful account of the limitations of the traditional model of investigation and prosecution. "[T]he traditional role of the district attorney -- merely that of courtroom accuser -- was inadequate if the challenge of organized crime was to be met. What was needed...was proactive investigative and prosecutive work. Victims had to be sought out. The crimes committed by professional criminals had to be uncovered before they could be solved. Close police-prosecutor cooperation was essential from the beginning of an investigation if maximum and effective use were to be made of the special investigative tools peculiarly available to the prosecutor: the grand jury subpoena, immunity grants, wiretap orders, search warrants, etc. An integrated approach to each investigation and prosecution had to be undertaken. A careful effort had to be made to use all possible legal resources at every stage: investigation, grand jury presentation, preparation, trial, and appeal." Pp. xii-xiv.

[21] In 1931, a team of special agents from the Internal Revenue Service's Intelligence Unit was assigned to the United States Attorney for the Southern District of New York. The team came to New York on the heals of its first success, in Chicago, where its efforts had resulted in the conviction of Al Capone, the infamous organized crime boss, for failure to pay his income taxes. The IRS unit worked with United States Attorney George Z. Medalie, and his chief assistant, Thomas E. Dewey. Medalie took an aggressive approach to making cases: rather than waiting for cases to "be brought in on a platter," he combined the IRS investigators with the resources of the FBI, the Treasury Department's Intelligence service, the Secret Service, and other federal agencies. When Dewey later conducted a special rackets investigation in New York County (Manhattan) and subsequently was elected New York County District Attorney, he brought with him and expanded on that experience. He, too, rejected the then traditional role of the public prosecutor as one who presents to the court evidence brought to him by police (who had their own motives for not aggressively pursuing organized crime investigations) in favor or a sophisticated in-house team of investigative accountants. Thomas E. Dewey. *Twenty Against the Underworld.* New York: Doubleday and Company. Pg. 81

improved coordination for enhanced prosecution of individual mobsters. Failure, again, had become evident: mobsters were going to prison, yet mob control of legitimate industries continued. New leadership had emerged and taken hold of the criminal enterprises which, in spite of numerous prosecutions and incarcerations, had remained viable , ongoing and important as sources of mob wealth and power. Solving the purely technical matters of improved coordination for better case making had missed the target by a wide margin.[22]

The core problem, rather, appeared to be the enduring and intractable criminal enterprise itself, and the stranglehold that the mob had gained over important areas of legitimate economic life. To impact this required a shift in tactics. Federal and state RICO and forfeiture legislation put into prosecutors' hands a potent new mix of civil and criminal remedies, aimed not only at mob leadership, but also at the underlying economic enterprise. The goal was both to incapacitate mob leadership, and to weaken the financial and operating wherewithal of the racketeers.

RICO-driven prosecutions led, also, to the expansion of the traditional rackets bureau team to include accountants, analysts and other civilian experts, and to a widened conception of the role of the prosecutor. For with a new and more complex set of economic targets in their sights, prosecutors gathered about them specialists to make sense of the paper and money flows that constituted the financial infrastructure of the mob's criminal enterprises. A sophisticated investigative enterprise emerged that required prosecutors to exert more forceful leadership, and that tested their managerial skills. [23]

A Critical Reassessment

During the late 1980's law enforcement strategists stepped back from their operations to assess their handiwork. Something was amiss. For even with their new powers, with their teams financed and deployed, and with new civil and criminal prosecutions under way, there was mounting evidence that the problems of racketeer influence and control in some markets -- notably, construction, waste hauling, freight

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[22] See Jonathan Kwitny, *Vicious Circles*. New York, NY: W.W. Norton and Co., 1979.

[23] Prosecutors, it was proposed, could find even more ways to attack organized crime figures if they, too, became generally knowledgeable about the specific ways in which organized crime infiltrated legitimate businesses like the construction industry. They could use the records and legal powers of a variety of civilian regulatory agencies to develop leads and evidence to build cases against organized crime figures, and civil sanctions to punish them when criminal sanctions were unavailable. By using this information and legal authority, mobsters who were now relatively immune to prosecution would become vulnerable -- much as Al Capone became vulnerable when prosecutors realized they could investigate and prosecute him for tax evasion rather than for bootlegging or murder. See, for example, Ronald Goldstock, "The Prosecutor as Problem Solver," Occasional Paper, Center for Research in Crime and Justice, New York University School of Law, New York, 1991.

forwarding, produce markets -- were so profound that, in spite of everything, these markets remained firmly in organized crime's control. [24]

Strategists (among them the leadership of the New York State Organized Crime Task Force) came to the conclusion that prosecution and investigation alone would be unable to loosen the mob's grip on legitimate markets and industries. Without reform of the underlying *market* conditions that gave rise to racketeering opportunities, the markets themselves would remain as vulnerable and attractive as ever to anyone with the reputation or muscle to exploit their weakness. Law enforcement might succeed in attacking organized crime's leadership and its enterprises. Prosecutors could send whole branches and trees of organized crime families to prison. Without concurrent market reforms, however, the demand for the rationalizing services of racketeers would continue unabated, and with it the prospects for racketeer influence and control.

The Comprehensive Model

The "comprehensive" model received its first full statement in the OCTF *Final Report on Crime and Corruption in the New York City Construction Industry.* It acknowledged the important relationship between the business practices of individual firms, market relationships between buyers and sellers of goods and services, and the racketeering activities of gangsters.

The recommendations presented in that report went beyond the usual suggestions to improve the investigation and prosecution of individual organized crime figures. In a decisive break with traditional views about how best to fight organized crime, the OCTF strategy suggested that gaining an ever-increasing number of convictions against criminal defendants -- the prosecutor's traditional goal -- would not significantly and permanently reduce the level of racketeering and corruption in the New York City construction industry or elsewhere. The goal, it suggested, ought not simply to be to send mob leadership to prison, or to catch and hold corrupt government inspectors, or even only to attack particular criminal enterprises. The goal of government, rather, ought to be to reduce the "racketeering susceptibility and potential" of legitimate industries that were pressured or controlled by the mob. [25]

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[24] See, for example, Peter Reuter, *Racketeering in Legitimate Industries: A Study in the Economics of Intimidation.* Santa Monica, CA: The RAND Corporation, 1987, and Peter Reuter, "The Cartage Industry in New York," in Michael Tonry and Albert Reiss (eds.) *Beyond the Law: Crime in Complex Organizations.* Chicago, IL: University of Chicago Press, 1993. In 1986, the John F. Kennedy School of Government convened a series of national meetings with leading elected state and local prosecutors to explore the current state of prosecutor strategy. Prosecutors were concerned about their impact across a spectrum of activities, including organized crime control. See, Zachary Tumin, *"Summary of the Proceedings: Findings and Discoveries of the Harvard University Executive Session for State and Local Prosecutors (1986-1990)."* John F. Kennedy School of Government Program in Criminal Justice Policy and Management. 1990.

[25] OCTF, *Final Report*, 1990.

To achieve this goal, the strategists proposed, required that government, rather than relying on criminal investigations only to deter and incapacitate individual *offenders*, instead use its full array of civil, regulatory, and purchasing powers, also, to deter and incapacitate corrupt *firms*. The strategists reasoned that many corrupt or racketeer-influenced firms might be deterred as much by government refusing to do business with them, as by the more remote threat of prosecution, prison and monetary penalties for some of their officers.

The strategists thought, also, that the broad powers available to the government could be used to clean up the industry, and its relations with private and public developers. They envisioned government using a panoply of powers both to reduce the susceptibility of buyers and sellers to crime and corruption, and to alter the economic incentives that drew racketeers to the market in search of quick or enduring riches. The strategists observed, for example, that if city agencies refused to do business with corrupt or racketeer-influenced firms, not only would the city benefit by not having to pay the extra toll imposed by organized crime and the corruption it spawned, but non-corrupt firms would begin to reclaim a competitive industry that they had lost. This might gradually improve the performance of the industries that were reformed, and also weaken the power of organized criminal groups that depended on being able to corrupt the legitimate industry.

In effect, the idea was to use every scrap of power the government could muster to prevent organized crime from feeding off of ordinary economic activity. The approach emphasized comprehensive, simultaneous efforts by teams of professionals from many jurisdictions and sectors. They would use a wide range of civil and criminal authorities to at once attack organized crime leaders and enterprises, and to reform and repair market and regulatory functions whose weakness or total collapse beckoned organized crime to the trough. Strategists characterized these efforts as, in part, *deterrence-producing* and *opportunity-blocking.* [26]

Deterrence And Incapacitation Without Prosecution

The traditional law enforcement approach to controlling crime depends on the prosecution and incarceration of individual offenders. The notion is that such action not only deters other offenders, but also incapacitates the convicted offender. The net result is less crime than would occur in the absence of the prosecutions.

The comprehensive model was based, in part, on the thought that government could, in fact, produce strong deterrent effects by means other than individual prosecutions. OCTF strategists maintained that economic measures, such as city agencies refusing to do business with corrupt firms, could be at least as effective in deterring crime

[26] See Goldstock, "The Prosecutor as Problem Solver," 1991. Also see, Thacher, "Institutional Innovation in Controlling Organized Crime," 1992.

and corruption as criminal prosecution. "Businessmen may fear the loss of business more than the loss of liberty," the OCTF report contended.[27]

Similarly, the organized crime control strategists thought that corrupt firms could be "incapacitated" by means other than prosecution and conviction. Civil legal authorities might be used to force corrupt labor and corporate racketeers to disassociate themselves from firms they once lead or belonged to. Civil suits, brought under the RICO statutes, and based on information gathered from regulatory and purchasing agencies of the government, could be used to put corrupt companies and unions under court-appointed receivers, and compel not only the separation of corrupt individuals from positions of influence in the organizations, but also to help the organizations become less vulnerable to crime and organized crime influence.

Opportunity Blocking

The most radical of the ideas suggested in the OCTF approach, however, was that crime and organized crime could be reduced by a category of techniques described as "opportunity blocking." Opportunity blocking, according to one description, "seeks to change the social, economic, physical, or organizational environments, so that particular crimes become impossible, or at least very difficult to carry out."[28]

Generically, such techniques might include familiar crime fighting measures such as installing locked fare boxes on busses that the bus driver cannot open and requiring riders to use exact change. In the context of construction industry racketeering, agencies might carry out loss-prevention audits and security-conscious reforms of operating procedures; private firms might be required to retain private auditing firms to design and implement other administrative procedures and checks to prevent fraud in government contracting.

Promoting Industry Competition

Finally, strategists believed that an important way to eliminate organized crime influence and corruption in particular industries would be to improve competition in the industry. Specifically, they thought it would be important to find ways to reduce the competitive advantage that some kinds of organized crime-influenced firms seemed to have in seeking private and governmental contracts, and to increase the competitive advantage of legitimate firms. One way to do that would be to use government's regulatory powers to require firms in construction marketplaces, for example, to operate in ways that kept them free of corruption, or to use government buying power to advantage firms that could show that they were able to control crime and resist organized

[27] OCTF, *Final Report*, 1990.
[28] *Ibid.*

crime influence, as well as to build to competitive market standards of price and performance.

The Multijurisdictional Approach

The comprehensive model drew the "big picture" problem, and set the broad social goal to be reducing the "racketeering susceptibility and potential" of legitimate industries. To tackle such an illusive and massive problem, which was much larger than any single agency's own objectives, the comprehensive model required that government take a multijurisdictional approach. No longer could the "team" consist only of law enforcement personnel, even organized like rackets bureaus with their civilian professional and sworn enforcement staffs.

The multijurisdictional approach called for government to coordinate the actions of a "team," rather, that comprised the numerous public agencies and private interests arrayed around the market, each having an interest, purview, and a unique capability -- as well as some responsibility for the markets' current state. The aim of this co-ordination would be not only to increase the vulnerability of individual organized crime figures to effective criminal prosecution. Its aim, also, would be to use the powers of the private and public interests that dealt with the markets -- regulatory, administrative, and legal -- to reform the marketplace, make it less vulnerable and attractive to racketeers, and deter and incapacitate racketeers without, necessarily, prosecuting them directly. In effect, the strategy proposed to fight crime and organized crime in at-risk industries not simply by attacking the parasite, but by making the host specifically resistant to the parasite's attacks.

The Role of Law Enforcement

The comprehensive model and the multijurisdictional approach counted on law enforcement continuing to pursue its targets aggressively, attacking complex criminal conspiracies that were rampant in the industry. Law enforcement's role, however, included more than pure investigation and prosecution of racketeers. With its investigative powers and skills, law enforcement could acquire a unique view of the marketplace, one that included deep and quite specific knowledge of crimes, of schemes ongoing in the marketplace, and of the firms doing business there. A corresponding conception of the prosecutor as a "problem solver" emerged that seemed to capture what might be prosecutors' leadership role in these new initiatives. With that knowledge, market reformers could gain profound insight into how the market's structures were being attacked, where its vulnerabilities were, and which firms and individuals comprised the greatest risks to it. This was the key to unlocking highly effective industry and marketplace reforms, and a power that law enforcement uniquely possessed and could contribute.

When joined with administrative, civil, and regulatory initiatives, it was expected that the total effort -- the comprehensive model, and the multijurisdictional approach -- would both weaken organized crime, and strengthen key industries and markets, in the end reducing industries' "racketeering susceptibility and potential."[29]

The Opportunity to Innovate

The theory was an intriguing one, but like all theories, it required an operational test to see whether the general ideas could be developed into specific policies, operations and programs, and whether those new policies and programs would work. Fortunately, such an opportunity soon arose.

School Crisis

In the late 1980's, New York City experienced a deep crisis in the condition of its public school buildings and their fitness for students, teachers and education. For many years, the New York City Board of Education had failed either to maintain the city's public school buildings, or to build adequate new ones fast enough to meet demand. The facilities were vastly overcrowded, and physically decaying: a survey showed that over 85% of the school district's 1,000 buildings required major repairs, at a cost of billions of dollars. [30]

Yet burdened by decades of mismanagement, and thwarted by the City's and its own wasteful practices, it seemed unlikely that the New York City Board of Education could accomplish a building program of the scale required to resolve the current crisis.

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[29] For a discussion of "problem-oriented" tactics in the service of larger "institution building" strategies for prosecutors, see Zachary Tumin, *Findings and Proceedings,* 1990. For a discussion of the migration of tax and environmental agencies, generally, to problem-oriented strategies, see, also, Malcolm K. Sparrow, *Imposing Duties: Government's Changing Approach to Compliance*. Westport, CT: Praeger. 1994. Sparrow distinguishes importantly between "community policing" as a strategy, and "problem-oriented" policing as a tactic or technique to be used to achieve the larger purpose, only one of many tools community policing might use (see esp., Pp. Xx-xxi). See, also, Malcolm K. Sparrow, Mark H. Moore, and David M. Kennedy. *Beyond 911: A New Era for Policing*. Basic Books. 1990. Pp. 95-128. Also, Herman Goldstein, *Problem Oriented Policing*. New York: McGraw Hill. 1990.

[30] Nationally, a similar crisis in crumbling, overcrowded schools simmered and, in late 1995, made front page news. The New York *Times* reported that "[a]round the country, the nation's schoolchildren are attending schools that are falling apart, or are being jammed into classrooms that are sorely overcrowded... [T]he General Accounting Office [recently] cited $112 billion in pressing construction needs in the nation's existing schools, but found that states last year spent less than $3.5 billion on addressing them." Peter Applebome. "Record Cost Cited To Fix Or Rebuild Nation's Schools." The New York *Times*, December 26, 1995. Pg. 1.

The OCTF reports and others intensified concerns that the Board of Education would be unable to meet the demanding construction requirements. [31]

Faced with such crisis, then-Governor Mario Cuomo and the New York State Legislature established the SCA as an independent authority to oversee all new school construction and renovation in New York City, supplanting the Board of Education as the builder of record. The state streamlined procurement rules so that the new authority could build faster, cheaper, and more effectively, and provided the SCA with a $4.3 billion capital budget for its first five years of operations. [32]

With drafts of the OCTF report circulating, city and state officials also became deeply concerned that a new public construction authority, armed with expedited procurement procedures and a significant capital budget, might become the next easy mark for corruption and organized crime influence in the city. As a result of its special efforts, government might only end up enriching organized crime and investing in more shoddy buildings. The solution lay, it was thought, in arming the SCA with the special protection of an Inspector General whose job it would be to ensure that the SCA's operations remained substantially free of the economic and political costs associated with organized crime, crime and corruption.

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[31] In addition to OCTF's report, numerous other commissions, studies and reports had assessed the problems affecting procurement and contract administration in general and in public construction in particular. See, for example, the New York State Commission of Investigation, *Investigation of the Building and Construction Industry: Report of Conclusions and Recommendations.* 1985. Institute of Public Administration, *Contracting in New York City Government: Final Report and Recommendations.* New York City: 1987. See, also, New York State Commission on Government Integrity, *A Ship Without a Captain: The Contracting Process in New York City.* December, 1989. Also, The New York Building Congress, Inc., Public Construction Task Force. *Building New York City for the 21st Century.* 1990. And, New York City Charter Revision Commission, *How Does New York City Work? The Major Processes of City Government.* 1989.

[32] New York City School Construction Authority Act, ch. 738, 1988 N.Y. Laws 1525. The State gave the SCA the power to design, build, and rehabilitate all buildings for the New York City Board of Education, including acquiring real property. It established a three-member board of trustees to oversee the Authority and to select a president/CEO to run it. To expedite project approvals, the city's Mayor or two-thirds of its City Council would have but twenty days from SCA's submission of project plans to disapprove them. Otherwise, the plans "shall be deemed to be approved," and no further hearings or approvals would be permitted. All contracts in excess of $50,000 were to be awarded to the lowest responsible bidder. The SCA could, however, reject all bids when "it deem[ed] it in the public interest to do so." It required the SCA to establish "guidelines governing the qualifications of bidders," and limited bidding to those who prequalified based on past performance, current abilities, responsibility and reliability, "and other such factors as [the SCA] deems appropriate." The SCA was to establish "fair and equitable" procedures to resolve contract disputes. The State granted the SCA a five-year exemption from the Wicks law which, having required public builders at great cost and problems of coordination to hire multiple contractors on projects, had been the subject of much criticism. In the hopes of protecting the school construction funding stream from the vagaries of annual budget wars, the State provided that funding for the SCA was to be pursuant to five year budgets.

The Comprehensive Strategy Of The SCA Inspector General

In considering the design and functions of the Office of the Inspector General, strategists viewed previous regulatory and enforcement approaches as having failed because the relationships among the different aspects of the problem had not been fully grasped. Nor had a combined attack been launched that successfully combined all the many resources and authorities needed to block opportunities and detect and deter crime. Given the weakness of market forces and the prior failure of civil, regulatory, and enforcement initiatives to assure an open and competitive marketplace, or to secure public building programs from crime, corruption, and racketeering, the strategists sought a new approach for the Office of the Inspector General.

To address the problem of organized crime influence and control in the public construction markets, the Inspector General's and SCA's task appeared as two-fold. In the first instance it was to attack organized crime and corruption directly, to imprison mob leaders and associates, and disrupt the mob's day-to-day operations in the marketplace.

Second, and more broadly, it was to help level the playing field for qualified, high-performing firms, and induce their return to the public marketplace. The Inspector General's and SCA's objective, in this respect, was to deprive firms that cheated, during bidding or on the job, of their competitive advantage. To achieve this required that the SCA, with the Inspector General, secure or reform the SCA's machinery for procurement, contract administration, and project management so as to fortify itself against cheaters and cheating; to detect and punish those who tried to defraud it nonetheless; and to find ways to make past performance count resoundingly in future contract decisions, including uncovering poorly-performing firms and banishing them from its vendor pool.

Having attacked and contained the mob and corruption, and created a level playing field for qualified firms to compete on the basis of price and performance rather than on their ability to cheat and defraud, the theory predicted that natural market forces would more freely exert powerful and determinate influence on business practices. The result should be, over time, an efficient, high-performing industry able to sustain itself relatively free of crime or corruption.

The SCA Inspector General Model

The model of an organization that immediately captured the strategists' imagination was one that was attached to, and part of, the SCA itself. For in being attached to and part of the contracting agency, the office could use its position to influence the procurement, contract administration, and inspections practices of the parent organization, which was a significant purchaser and manager of goods and services in the public construction marketplace. It could also bring law enforcement powers credibly to bear on the problems and issues confronting the SCA in the form of high risk contractors,

schemes to defraud it, and the lurking presence of corruption in its midst and organized crime in its marketplace.

First, as an adjunct to the SCA, the office could use its own regulatory powers over contractors and its access to the industry to learn more about the firms that were operating in its markets. This would help the SCA to discern which among the many firms and individuals seeking to do business with it posed a substantial risk to it, and help the SCA to debar the high-risk contractors or otherwise control them.

Second, in being attached to and part of an important public buyer of construction services, the Inspector General could help the reforms-minded SCA bring its market muscle to bear to impact vendor selection and presence in the public construction marketplace more broadly. As contractors whom the SCA identified as high-risk were active in the wider public construction marketplace, the SCA could highlight their presence and reputation and stimulate a broader-band marketplace refusal to do business with them. In denying these individuals and firms access to public business opportunities, agencies and authorities could not only protect themselves, but would force high-risk firms from the public construction marketplace, and perhaps out of the industry altogether.

Third, the Inspector General might help develop reforms within the SCA that, if shared with other builders, could stimulate their wider use, perhaps encouraging legitimate firms to return to public construction faster, in greater numbers, and with more enduring effect. The SCA, for example, might highlight changes it made to bring its times-to-payment cycles more in line with private sector practice; or its efforts to redraw outdated bid specifications to reflect newly-available, lower cost materials and confer competitive advantage on the high-performance firms that used them. Moreover, by sharing the methods the Inspector General used to detect and punish cheaters in its midst, the SCA might encourage their wider adoption and make it further difficult for high-risk firms to compete in the public construction marketplace.

Fourth, the Inspector General could, through its window on the industry, use its own and other agencies' regulatory, civil and criminal enforcement powers to strengthen conventional enforcement efforts directed at ordinary crime, corruption, and organized crime groups. As law enforcement agencies became more effective in investigating and prosecuting racketeering and corruption directly impacting SCA operations, this, to would aid the SCA's near-term goal to buy and build clean, quickly and inexpensively. It would also help the SCA gain unique and detailed insights into the nature and identity of the threats it faced, learn with great specificity about any opportunities for crime and corruption that the SCA's own practices tolerated or stimulated, and aid it in flagging and debarring high-risk firms. Lastly, it would help the SCA leverage a broader clean-up of New York's construction market.

All of this, it was expected, would be achieved if the Inspector General, operating as an adjunct to the SCA, exploited that position to secure at least one major public builder from racketeering and corruption, and to permit new competitive industry

standards of price and performance to establish a toehold; to test and develop new "technologies" to prevent, detect and control crime and corruption; and to develop information and investigative opportunities to advance law enforcement efforts to attack crime and racketeering in the industry more broadly. These would have the intended longer-term impacts of securing a high-performing market that was more capable of regulating itself and required less "rationalizing" by organized crime. Further, in helping law enforcement agencies to attack organized crime and in blocking the mob's efforts to gain a spot at the SCA trough, the SCA Inspector General would help weaken organized crime itself.

A Clean Industry As An End And A Means

In sum, the Inspector General's strategy to protect the SCA and weaken organized crime in New York would be achieved both *directly* and *indirectly*. As a sophisticated regulatory agency positioned right in the middle of the construction industry, the Inspector General could *directly* help its law enforcement partners learn more about the overall character of the industry than their ordinary case-making activities permitted. It could provide an invaluable window onto the public construction marketplace from which law enforcement could gain information on the characteristics of the firms it suspected of being importantly linked to organized crime, and develop investigative opportunities quickly and at relatively low cost. Over time, law enforcement would become more effective in investigating and prosecuting racketeering and corruption in public construction.

Moreover, the Inspector General could use its own regulatory and civil enforcement powers, tied to a massive public construction program, to give a competitive advantage to firms in the industry that could and would build clean. This would have the *indirect* effect of weakening organized crime by denying business to firms it influenced or controlled, and setting a new and higher competitive standard based on price and performance. This, too, would advance the SCA's long-term interest to establish and secure a clean and competitive marketplace for public construction.

It is this complex combination of hypothesized effects that represents the innovative operational theory of the Office of the Inspector. What made the Inspector General strategy important and innovative was that it sought, simultaneously, to reform and improve public construction, both as an *end* to be pursued *by* attacking organized crime, and as a *means* to be used to *attack* organized crime. Attacking organized crime as a <u>means</u> to reform the industry would be important to bringing and keeping construction costs down, to improving overall price and performance in the marketplace, and to restoring to some degree of competitive vitality to the market. Cleaning up the market would be important as a <u>means</u> to deprive organized crime of its trough, and to weaken its financial and operating power.

The Study's Objectives And Three Evaluative Frames

The operational theory of the office and its organized crime control strategy articulated above implicitly establish three evaluative frames for this report.

The first and primary objective/evaluative frame would focus on the contribution that the Office of the Inspector General made, and the outcomes it helped to achieve, in its mission to keep the SCA's building program free of crime, corruption and racketeering. This would include efforts to reform SCA practices and procedures that left leave the SCA open to attack; to identify and screen out individuals and firms it had reason to believe sought seek to exploit the SCA building program, and to prevent the SCA from doing

business with them; to detect and root out crime, corruption and racketeering that nonetheless "crossed the moat," and, in partnership with law enforcement, to attack suspect firms to neutralize them. This evaluative frame would be unconcerned with wider, collateral effects on the industry or organized crime.

We would be concerned to discover, also, whether and how the Inspector General's crime control efforts impacted any broader efforts that the SCA may have made to build to competitive standards of price and performance. These would include, for example, direct effects of interventions by the Inspector General on procurement metrics such as times from bid to contract. They include, also, indirect effects of the Inspector General's interventions that were aimed, broadly at leveling the playing field for legitimate firms: finding and catching cheaters, making past performance count in contract award decisions, restoring the salience of competitive virtues of price and performance in market choice, and inducing legitimate firms to return to the SCA vendor pool and to compete for its business. This evaluative frame would look to outcomes for SCA building metrics such as price and performance to see what effect, if any, the Inspector General's interventions had, and by what means.

The second objective/evaluative frame would focus on the Office of the Inspector General's impact on the overall performance of the public construction enterprise in New York City. The aim would be to determine whether and how the Inspector General used its position to influence a restructuring of the public construction enterprise in New York generally. This would have resulted from its own efforts to ensure that the SCA could buy and build clean, the influence of that market power on broader industry standards, and the Inspector General's ability to strengthen conventional law enforcement efforts directed at ordinary crime, corruption, and organized crime occurring within public construction.

The third objective/evaluative frame focuses on the success of the operation of the Office of the Inspector General in weakening organized crime. That effect would be measured to some degree by the successes registered in the second evaluative frame that could be expected to deny organized crime a foothold in public construction. It also could be measured more directly by observing the extent to which the Inspector General was effective in supporting conventional law enforcement efforts against organized crime families, or in attacking crime, corruption, and organized crime influence in the specific projects funded by the SCA.

III. THE CHALLENGE TO THE INSPECTOR GENERAL: PROBLEMS OF PUBLIC CONSTRUCTION, REGULATION AND ENFORCEMENT AND THE BUREAUCRATIC APPROACH

Introduction

Organized crime strategists envisioned widening the state's attack on organized crime in general, and public construction in particular, to include the combined use of the state's regulatory authorities, its market muscle, and its purchasing power to "harden" the industry marketplaces to crime and racketeering. From their perspective, over and above prosecuting individual racketeers, their best chance to produce large, durable effects on organized crime and corruption lay in cleaning up the marketplace that spawned much of the illegal activity.

The Fragmented Response of Regulators, Enforcers, And Builders

The challenge confronting enforcement officials and regulators went beyond issues of procurement practice, contract administration, and construction management. For one, the size and scale of the public construction industry in New York City created an extraordinarily large moving target for regulators and law enforcement. It comprised hundreds, if not thousands of dispersed enterprises, over a hundred thousand workers, thousands of small and medium sized construction companies and materials supplier, hundreds of general contractors, hundreds of specialized subcontractors, and dozens of developers.

Moreover, racketeering and corruption were intimately woven into the basic structure and functions of the marketplace. Thacher characterized corruption and racketeering as "endemic and systemic" to it, as potentially part of every transaction for goods and services in the business.[33]

Third, these crimes were never clearly in view -- one could not go to a construction site and "see" extortion, bribery, theft, frauds, or collusive bidding and bid rigging. Even regular sounding business problems in construction could well be part of a fraud. Only by knowing where opportunities existed, who was proximate to them, and

[33] Thomas D. Thacher II, interview (1992).

when individuals might pursue and discuss them could "business problems" be recognized as part of a criminal conspiracy.[34]

Any solution would have to deal with these issues in a concerted fashion. Put this way, whatever approach might be taken would require *an market-wide focus that could impact the way business was conducted in all its many aspects.*

Yet the public response was itself highly fragmented, and marked by the following features:

- Constrained access to information about racketeering vulnerability and threat
- Substantial cultural and structural impediments to interagency coordination
- Little public accountability or internal agency pressures for dealing with the problem of industry-wide racketeering and corruption
- Bureaucratic strategies that focused on processing workloads rather than achieving broader social outcomes.

Constrained Access to Information About Racketeering Vulnerability and Threat

No one agency had the "big picture" view of the complex problem of racketeering and corruption in public construction, or easy access to such a comprehensive view. Agency boundaries impeded acquiring the information needed to establish such a view, and created a situation that organization theorists refer to as "information impactedness": no party could obtain accurate information from or about the other without great difficulty and cost.

For example, public builders who might want to build to competitive standards of price and performance, *and* build free of racketeering and corruption, would find the information they needed hard to acquire.[35] Meyer S. Frucher, whom Governor Mario Cuomo appointed as his designee to the SCA's Board of Trustees, had had extensive experience as a public builder in New York. As president and executive director of the Battery Park City Authority, developing the southern tip of Manhattan, Frucher had formally requested information from each of the city's law enforcement agencies concerning vendors that were in line to obtain contracts from the Authority. Most of the

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[34] *Ibid.*

[35] Organization theorists and economists refer to these hindrances as "transaction costs." For a detailed discussion of transaction cost economics and their impacts on organizations and markets, see, for example, Peter M. Blau and Marshall W. Meyer, *Bureaucracy in Modern Society.* New York: Random House, 1987. Pp. 170-180. See also Oliver E. Williamson, *Markets and Hierarchies: Analysis and Antitrust Implications.* New York: Free Press, 1975. Also, Oliver Williamson, "Organization Innovation: The Transaction Cost Approach." In *Entrepreneurship*, J. Ronen (ed). Lexington, MA: Heath. 1983. Pp. 101-134. And, Charles Perrow, *Complex Organizations: A Critical Essay.* New York: Random House. 1986. Pp. 236-247.

agencies he contacted failed to respond at all, or to share their information with him. To his great frustration and public embarrassment, the Battery Park City Authority ultimately found itself doing business with organized crime-involved construction firms, developers and unions.[36]

Frucher's situation was not unusual for a public builder in New York City. Although he decided which contractors would work on some of the city's most important public projects, he lacked the means to learn which among them had previous records of racketeering or posed substantial integrity risks. He possessed some knowledge of industry players and relationships, yet he lacked the information that he would need to substantiate a decision to exclude them from contracts. In effect, Frucher had little choice but to purchase services, knowingly or blindly, from secret cartels, and to submit to their price fixing and collusive bidding. And though his own contract administrators, engineers, and inspectors might have had detailed knowledge of standard industry practices, Frucher had little knowledge as to the structure of racketeer schemes, or which of his agency's procedures created opportunities for them to exploit. He ultimately had few defenses against his own employees' frauds and corruption.

In the construction business, *any* agency that sought to provide a more integrated response often discovered that it was critically short of some vitally-needed "strategic asset" required to do this, and terribly overstocked on others. These strategic assets might include resources, or authority, or a knowledge-base or skill. Without a good balance of assets in its "portfolio," and unable, except at great cost, to acquire those assets in which it was deficient, it was often difficult for an agency to make full use of the assets it did possess. As a result, agency potentials frequently went untapped, resources and authorities went unexpended, the full value of the public investment in them was rarely realized.

Prosecutors, for example, possessed the requisite technical legal skills and wielded unique powers to probe and prosecute criminal enterprises. With detailed information on the industry and its players, they could establish the probable cause needed to secure eavesdropping authority, to procure search warrants, to convene grand juries and confer immunity on informants, all to gain more detailed knowledge of the criminal conspiracies rampant in the industry. Yet prosecutors typically had little detailed knowledge of the construction industry, its relationships, or of where and when to look for frauds and other crimes. They were out of the loop and out of position, unable to acquire this information, except by fortuitous circumstance, or else at great cost. Limited, more often, to information exposing targets of opportunity that might come in, literally, over the transom, investigators and prosecutors could do little more than make a succession of isolated cases. Over time, these appeared to have achieved negligible and short-lived impacts on markets, leveraged little structural change, and failed to prevent the return of the next wave of racketeers to the industry trough.

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[36] Interview, Meyer S. Frucher (1990).

Organization Boundaries: Cultural Barriers to Coordination Among Agencies

The comprehensive model and the multijurisdictional approach required coordination across agencies. With good coordination, builders might build to competitive standards of price and performance, and at the same time build free of racketeer influence or control. Coordination among agencies and entities in the marketplace might produce the best social results of all -- to construct buildings quickly, at low cost, with good quality, and without mob involvement.

Coordination, however, required that the enforcement, regulatory and building agencies find ways to cooperate across the high and wide organization boundaries that separated them. Numerous of these agencies' objectives were in potential or actual conflict. Differences in their distinctive organizational norms, occupational cultures, and operating strategies could easily overwhelm any goals and values they might share.

Operationally, coordination would require agency heads from building and enforcement organizations to work together who ordinarily had little opportunity, interest, or positive past experiences in doing so. Agency heads might have entirely different views of the problem to be addressed -- whether, for example, to build quickly, or to build cleanly, free of corrupt or racketeer-influenced firms and individuals. They possessed vastly different professional objectives in the same arena -- the one to construct buildings, the other to imprison corrupt builders. They held strong and disparaging views of the other, including deep suspicions as to the integrity of builders who might be "in bed with the mob," and the motives of "headline grabbing" investigators and prosecutors. A builder's account of his success would not ordinarily include whether mob-influenced firms were among his contractors. A prosecutor or investigator's view of her success would not ordinarily include whether a building was actually built.

Under the best of circumstances, builders and enforcement organizations lacked much reason, desire or incentive to talk to each other, let alone coordinate their agencies toward some greater goal for all. Real structural and organization barriers, comprising diverse interests that could easily conflict, and vast differences in culture and strategy, made trust and cooperation difficult to achieve.[37]

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[37] The issue of boundaries among organizations is as much an issue *within* the law enforcement enterprise, as *between* it and public construction or procurement agencies. "The criminal justice system can be characterized as an 'industry' with a 'long-linked' technology. That is, it consists of a sequence of serially interdependent organizations whose combined efforts result in various products. ...[E]ach organization in an industry must establish some niche, some boundaries around that total effort for which that organization takes initiative... In the criminal justice industry the domains of the component organizations appear at first glance to be clearly defined and well established. Police do the policing; the prosecutors do the prosecuting; and the judges do the judging. But appearances can be deceptive..." See, William F. McDonald, "The Prosecutor's Domain." in *The Prosecutor*, William F. McDonald, (ed). Beverly Hills: Sage Publications. 1979.

Structural Barriers

Structurally, no single agency could easily track the fluid problem of corruption and racketeering as it moved across agency boundaries; nor were there strong pressures or easily-seized opportunities to integrate functions so as to gain greater perspective and control. Public builders, for example, did not feel responsible for making sure contractors who bid on their jobs were clean. They neither took very seriously the idea of finding out who from among their vendor pools was "mobbed up," or of avoiding doing business with such firms even when their mob status became obvious. Policing the business was law enforcement's job; getting buildings up was the builders'. These tasks were organized and treated as if they were quite separate.[38]

Nor did agency boundaries permit much forward integration: agencies easily avoided much responsibility for the downstream impacts of their prior decisions. Procurement specialists, for example, had no responsibility for downstream project management, or inspections and quality control. Their principal task was to run a fair procurement process, to find the lowest responsible bidder, and award the contract. In making their contract award decisions, low cost far outweighed past performance.

The Artificially Low Cost of Failure

In the construction business, the ability of the contractor to deliver on time and on budget is crucial to the central task of coordination. Any uncertainty in this regard adds to a project's total time and final costs. Indeed, economists regard uncertainty in the flow or quality of an organization's raw materials -- including, for example, the capabilities of its contractors -- as an important transaction cost impacting industry economies.

When faced with such uncertainties private firms, especially, seek ways to minimize them. They may shop competitively among suppliers on the basis of price and performance, for example, or expand their own operations backwards into the production chain to control more of its critical inputs. When, in the construction industry, the uncertainty is as significant as a contractor's ability to perform on time and on budget, the high cost of failure ordinarily propels a private builder to seek out and contract with proven performers.[39]

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[38] New York *Newsday*, for example, reported that "the rush to repair the crippled World Trade Center has benefited at least four firms that have had affiliations with organized crime figures or relatives of imprisoned godfather John Gotti... 'We faced a terrific emergency and hired people we think were the best to do the job,' said Lloyd Schwalb, a Port Authority spokesman. 'We have no control over who they may have associated with or have on their payroll. And not one of these people that you have mentioned did anything other than a superlative job.' The repair contracts, many of which were not competitively bid, are expected to cost millions of dollars." Kevin Flynn and Michael Weber. "Blast Firms' Tangled Mob Ties." New York *Newsday*, April 9, 1993.

[39] "The integrated firm buys out as many of its competitors as it can and integrates backward and forward to control as much as it can of the 'throughput' from raw material to final consumer. It absorbs the sources of uncertainty in its environment and in the process reduces the number of autonomous

from their decisions, they were free to keep making those same decisions, and never to be the wiser, or the smarter, for them.[42]

In sum, cooperation and coordination among agencies were complicated operational and political tasks for which the agencies were particularly ill-prepared, ill-suited, and poorly positioned. Indeed, the task of managing a public construction enterprise was a difficult one of coordination by itself. So, too, was the task of investigating and prosecuting racketeers. Optimizing to build to competitive standards of price and performance *and*, simultaneously, to control for racketeering and corruption was daunting, and perhaps impossible if it meant coordinating operations across agency boundaries.[43]

Little Public Demand Or Agency Accountability For Progress On Racketeering

The fact was that no single agency or entity had responsibility -- let alone the necessary authority, skills, or resources -- to take on the "big picture" problem and to reduce racketeering in public construction.

Neither did the public compel a solution Ultimately, the public demand on individual agencies made little mention of "racketeering." It held prosecutors responsible for prosecuting dangerous criminals; builders for building quickly and cheaply;

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[42] The problem of insulation from real-world, downstream impacts of decisions is one that organizations in the public and private sectors share. An illuminating tale of its appearance on the factory floor, for example, was reported by one researcher trying to uncover the sources of scheduling problems in a complex production line. "In all my plant visits, I arranged to spend most of my time with the man in the organization responsible for the detailed sequencing of production orders. This seemed sensible to me since this was the man who every day somehow dealt with the vast complexity of the job shop problem... Upon meeting this gentleman, therefore, it was with considerable anticipation that I would say that I had come to discuss with him his very complicated job shop scheduling problem. Without exception he would look somewhat perplexed and ask, 'What job shop scheduling problem?' Despite my explanations...he never could see my definition of his problem. He showed me records which indicated in great detail that he met virtually all his promised deliveries...[M]y inability to elicit any recognition of a scheduling problem...discouraged me. But I can now report that I have found the explanation. The job shop problem is not recognized by most factory schedulers because *for them*, in most cases, no scheduling problem exists...[T]here is no scheduling problem for them because the organization which surrounds the schedulers reacts to protect them from strongly interdependent sequencing problems." William F. Pounds, *The Scheduling Problem*. in John F. Muth and Gerald Thompson, (eds), *Industrial Scheduling*. Englewood Cliffs, NJ: Prentice Hall. 1963. Cited in Jay Galbraith, *Designing Complex Organizations*. Reading, MA: Addision-Wesley. 1973.

[43] For a discussion, generally, of the issues and challenges involved in structuring cooperative arrangements between organizations, see David Nadler, et al. *Organizational Architecture: Designs for Changing Organizations*. San Francisco: Jossey-Bass. 1992. See, also Chris Argyris and Donald Schon, *Organizational Learning: A Theory of Action Perspective*. Reading, MA: Addison-Wesley. 1978.

By contrast, however, public agencies adapted to the uncertainty concerning their own vendors' records of integrity and competence, not by shopping competitively on the basis of their past conduct and performance, but by acting as if many of these "uncertainties" were irrelevant to the decision they faced. They structured their procurement and contract award process to strip away information about a contractor's past performance on the job, and its business ethics and practices.[40]

There is little doubt that the failure of procurement staffs to take vendor's past performance into account inevitably led to downstream performance problems, as vendors with clearly visible past performance defects bid low again, were awarded new contracts, and created problems anew. Still, even as new, and by all accounts, predictable performance problems might soon arise on the job, procurement staffs, having long since finished their task to determine the responsible low bidder, were unaffected. They rarely, if ever, knew about or faced the full force of downstream performance problems caused by firms they had approved. Typically, they felt little pressure to alter their selection practices or criteria.

Indeed, where in the private sector quality control inspectors might provide information about manufacturing defects to production engineers to change product specifications; where marketing managers, seeing sales fall below expectations, might seek information and devise new strategies to bring sales back on track; where personnel managers might seek to learn the sources of worker dissatisfaction leading to high employee turnover and workforce instability; nothing of the sort often troubled these bureaucracies or caused them to alter course.[41] As the organizations arrayed around the construction marketplace were effectively held harmless against any downstream impacts

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organization. In order to control transaction costs and throughput coordination it prefers to make rather than to buy..." Charles Perrow, "Small-Firm Networks." In, Nitin Nohria and Robert G. Eccles (eds), *Networks and Organizations*. Boston, MA: Harvard Business School Press. 1992. It is interesting to note that *within* the law enforcement enterprise, the history of prosecution is one of invasion and retreat, back and forth, into the domains of police with respect to case screening and charging, on the one hand, and courts with respect to sentencing on the other, in an attempt to control the input and add value to the output of the office. "The historical evolution of the office of public prosecutor had extended the boundaries of his domain into territories formerly held by the police, the grand jury, the petit jury, the defense bar, and the judiciary. The police and the judiciary have not allowed this to happen without protest." See, McDonald, "The Prosecutors Domain," 1979.

[40] See, generally, Kelman, *Procurement and Public Management*, 1990. Pp. 11-28

[41] For a thorough exploration of the character and process of organization learning, see Argyris and Schon, *Organizational Learning*. 1978, from which these examples are borrowed. For a discussion of these factors at play in the changing decision environments of tax, environment and police agencies, see Sparrow, *Imposing Duties*, 1994. "[There] was a growing awareness that the traditional reactive, case-by-case, process-dependent approach to work was failing to achieve important public purposes. Invariably the established processes were sophisticated, and constantly being refined. But they were hopelessly overloaded. Worse, the organizational preoccupation with handling reactive workloads had bred, within agency cultures, insular and somewhat narrow views as to what was important. The public could see the agencies were busy, but didn't think they were busy on the right things. [It] didn't care much about these agencies' levels of activity because the levels of activity seemed to have little impact on things they did care about..."

procurement officers for purchasing goods and services to specified standards at the lowest possible price. There was little mention of "racketeering." [44]

In consequence, prosecutors, for example, were less concerned to reduce racketeering in the industry, than to concentrate on street crimes that were a public priority. At the end of the day, whether an agency of prosecutors, procurement officers, contract administrators, or construction managers reduced the industry's "racketeering susceptibility and potential" was a matter of some indifference. In any event, no one agency was held to account for failing to do so.

Workload Pressures Create Agency Priorities

The difficulties inherent in getting more information, coordinating across boundaries, optimizing for competing agency values, and achieving measurable social impacts were significant. Absent a compelling view of the "big picture," or public pressure to produce more than simply low-priced contracts, quick and cheap buildings, or a string of convictions, the socially valuable outcome that optimized for all three rarely claimed anyone's attention.[45]

What was left to matter most to an agency was handling the problem it knew most about and felt most acutely every day: the fair and efficient processing of sometimes staggering workloads.[46] Whether it was an organization of prosecutors, investigators, builders, or regulators, each agency was often a long-established bureaucracy with

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[44] The public demand for law enforcement action against racketeers is highest when gangsterism leads to open street violence, an unusual event in this era. Rather, the historic and current impetus for much law enforcement concern with organized crime starts and ends with the investigators and prosecutors themselves, and their concern to control certain kinds of crime on their beat and watch. This has often been based on their knowledge of sometimes obscure events that the public might be unaware of, and their understanding of the meaning of these events for the organized crime individuals and families involved. "Traditionally, the role of the public prosecutor had been to present to the court and jury evidence of criminal activity developed by the police or brought to him by a citizen independent of the actions of his own office. Dewey found that evidence of organized criminal activity did not walk in off the street in the form of a citizen complaint, the source of the vast majority of law enforcement investigations, nor was it to be had merely for the asking. Victims of underworld terror or exploitation do not volunteer to testify." See, Blakey, Goldstock and Rogovin, *Rackets Bureaus*. 1978. pp. xii-xv.

[45] Data from the field about the broader social impacts that prosecutors could achieve, for example, was murky and messy: costly to acquire, difficult to analyze, and complicated to use subject to the constraints of equity in treating like cases and defendants alike. By contrast, there was nearly perfect information quickly available to prosecutors, at low marginal cost, concerning caseload management metrics such as the number of cases that pled out or went to trial, how long the process took, and what resources it consumed. This data was easy to acquire and use simply by consulting office management information systems.

[46] The workload processing challenge could be significant. Prosecution agencies in New York City, for example, might handle over 100, 000 criminal cases annually. The sheer weight of handling this many matters every year -- whether criminal cases, or in the case of contracting agencies, competitive bids and procurements -- required that the agencies pursue a primary strategy to process unwieldy workloads efficiently and equitably, and to limit discretion.

powerful internal systems that were well-suited to coordination and control of its own internal processing environment. Each was well-positioned to pursue its own narrow objectives and to withstand the influence and pressures of others.

The Bureaucratic Strategy: A Context-Free Decision Environment

A well-defined set of procedures, standards and structures evolved to press home and enforce this bureaucratic strategy, and to limit discretion on individual matters. Whether it was a prosecution or a procurement, the bureaucratic task was to present the matter for appropriate agency action as a succession of "discrete events rather than as part of a larger web of dealings." [47] For procurement agencies, this meant excluding almost all non-cost based information about vendors that was not contained in the bid price itself. Past performance could not be a criteria of selection. It was perversely important instead that, as one frustrated corporate executive observed, "public procurement have no history." The task of vendor selection was uniquely determined and equitably performed only by considering the lowest responsible bid. [48]

For prosecutors, this same bureaucratic strategy meant excluding from consideration most information about a crime -- such as its social impact -- that was not already contained in information concerning its heinousness, as defined by statutory penalty; the defendant's dangerousness, as defined by the defendant's criminal history; and the case's evidentiary strength. [49]

The typical construction industry fraud, in fact, often seemed to lack much value at all to prosecutors. If it did not also involve an obviously serious crime such as murder, for example, frauds ordinarily scored low on investigators and prosecutors' test of case worth -- no dangerous offender, no heinous crime, strong evidence hard to assemble. In a highly regulated industry like construction, in any event, it was often prudent and possible for prosecutors to leave the business of sorting out frauds to regulators and civil juries.[50]

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[47] Kelman, *Procurement and Public Management.* 1990.

[48] *ibid.*

[49] This conception of the elements comprising "case value" was developed with prosecutors by Mark Moore, Philip Heyman, and Mark Kleiman at the John F. Kennedy School of Government's Executive Session for State and Local Prosecutors. See, Tumin, "*Findings and Proceedings,*" 1990.

[50] "Law enforcement agencies have not placed a high priority on the identification and prosecution of construction frauds. Prosecutors with few resources are reluctant to mount investigations and prosecutions which will not be fully supported by the 'victim' agency. Their reluctance is also a product of experiences like that in the Durante Construction Corporation case, in which the dedication of scarce resources produced a conviction but no significant sanction. This paving contractor and its principal were indicted in August 1987 for defrauding three City agencies by a scheme involving phony invoices and load trip tickets. In exchange fore their guilty pleas to 82 counts of fraud, Louis Durante, Jr., was sentenced to probation and a $25,000 fine, and the corporation was fined $50,000. No provision was made for restitution. In this instance, crime paid." OCTF *Final Report,* 1990, pg. 135

The Social Cost of the Bureaucratic Strategy

The social cost of this bureaucratic strategy was high. In having little information on vendor past performance, or in deeming most of it irrelevant to the contract award decision, procurement units might well award a school construction contract to a vendor with a history of fraud and racketeering. A subsequent fraud he perpetrated could result in a school opening delay, and another year of children learning in closets and toilet areas. Yet with or without this information, prosecutors might well consider the criminal case itself trivial, and forego the opportunity to gain valuable leverage over the vendor, his assets, and his future performance on behalf of the schools. The past performance of vendors, and the real-world impacts of the fraud, grave as they might be, ordinarily had as little consequence for the next decisions of procurement officials and they did for prosecutors'.

The Onset of Organization Inertia

The sheer weight of workloads, the requirements of efficient processing, the absence of effective countervailing pressures external to the organizations, the demands of horizontal equities across cases and matters, and the fixed administrative structures to control discretion engendered substantial organizational inertia. Agency activities such as "convictions achieved" and "bids opened" became goals whose quality was measured not by *external* outcome or impact, but by *internal* standards of efficiency and equity in the processing of matters.

With attention focused inward on such throughput performance metrics, the external world receded in importance. Indeed, no matter what pressures or opportunities might arise in the external environment, the bureaucracies were often largely, and rather blissfully, unaware and unpressured by them. As a result, they kept solving for the same problem over and over again: efficiency in processing, and equity in the treatment of like matters, with little cognizance of any but the narrowest of the outcomes and impacts that flowed from their decisions.

The public organizations arrayed around the problem of racketeering were, in fact, each especially well-suited as bureaucracies to managing an internal environment that was routine and characterized by great stability, where the demands for performance were limited to the efficient and fairhanded processing of huge workloads. In reality, the external environment in which the opportunities for racketeering developed was complex and uncertain. Given the highly uncertain and diverse character of the incoming workload, the bureaucracies were required to do a fair amount of work to shape it up: to shake it free of context and nuance, and to make it, *in fact*, routine, stable and amenable for processing on their terms. [51] For as good as they were at processing hundreds of

[51] Sparrow finds that "there is a certain foolishness in traditional enforcement approaches. They wait until the damage has been done and then they react, case by case, incident by incident, failure by failure.

thousands of prosecutions, bids and contracts each year, the agencies were just as ill-suited to dealing with the complexities of the overarching social problem of corruption and racketeering in the industry. They were, in that respect, knowledge based organization organized as if they were producing cars. [52]

Enforcement agencies accept the work *in the form in which it arrives*, and therefore, have tended to organize their activities around failures rather than around opportunities for intervention." See Sparrow, *Imposing Duties*. 1994.

[52] Some organization theorists argue that the "mechanistic" structure and process of bureaucracies -- reliance on highly formalized procedures, standardized structures and centralized management hierarchies -- help organizations perform better in stable, simple and routine environments. Network, or "organic" structures, are thought to be better suited to unstable and uncertain environments. For additional discussions of the "contingent" nature of appropriate patterns of organization, see Paul R. Lawrence and Jay W. Lorsch, *Organization and Environment*. Boston: Division of Research, Harvard Business School. 1967. Also, Tom Burns and G.M. Stalker, *The Management of Innovation*. London: Tavistock Publications. 1961. Richard H. Hall, *Organizations: Structure and Process*. Englewood Cliffs, NJ: Prentice Hall, 1972. And, Charles Perrow, *Complex Organizations: A Critical Essay*. New York: Random House. 1986.

IV. TRANSLATING THEORY INTO STRUCTURE: DESIGNING A NEW ORGANIZATION

Error correction takes the form of inquiry. The learning agents must discover the sources of error -- that is, they must attribute error to strategies and assumptions in existing theory in use. They must invent new strategies, based on new assumptions, in order to correct error. They must produce those strategies And they must evaluate and generalize the results of that new action. "Error correction" is shorthand for a complex learning cycle. [53]

Introduction

As Meyer Frucher contemplated his new responsibility as an SCA Trustee, he was deeply concerned for the future of the building program. Having consulted with OCTF Director Ron Goldstock and his staff during OCTF's study of the construction industry, and having had his own significant experience as a public builder, Frucher knew full well the risks and problems facing the SCA. When then-Governor Mario Cuomo named him as an SCA Trustee, Frucher insisted that the SCA have an inspector general's office capable of ensuring that the agency would do no business with the mob, nor get caught up in the cycle of corruption that infected so many public building programs.

Picking Up the Challenge

For the SCA to succeed required that it take responsibility for its own defense -- to make its own buying and building practices less prone to criminal exploitation, to exclude high-risk vendors from its business, and to attack and root out corruption, crime and organized crime in its midst.[54] The SCA could not do this alone, but would require a sustained commitment of time and resources from law enforcement.

As a result of his own experience at the Battery Park City Authority, Frucher was convinced that the SCA's Inspector General had to be someone capable of building these institutional ties to local law enforcement authorities. If successful in these relationships,

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[53] Argyris and Schon, *Organizational Learning*, 1978.

[54] Sparrow cites a similar resolve concerning fraud and abuse at the federal Health Care Financing Administration. The HCFA's $175 billion trough of Medicare and Medicaid disbursements was a frequent target of fraud and abuse. "Administrator Bruce Vladeck," Sparrow writes, "recently created a new position at a senior level with HCFA to lead the charge against fraud, and probably takes fraud control more seriously than any previous administrator. Writing in the *Journal of the American Medical Association* in March 1995, he declared, 'For many years HCFA may have appeared ambivalent toward fraud and abuse. When other agencies, particularly the OIG, assumed primary responsibilities for program integrity in Medicare and Medicaid, HCFA often was prepared to defer to them. Those days are over.' " Sparrow, *Health Care Fraud Control*, 1995.

the SCA could gain access to information to help it determine which companies to do business with, and use its links with law enforcement to monitor firms and individuals that became suspect during their contracts. If necessary, the SCA could participate in criminal investigations of businesses that it suspected of defrauding it, and use information from those investigations to pursue civil suits for monetary recoveries, as well to reform agency operations.

In spite of its perils, the moment was also a unique and fortuitous one for both public builders and law enforcement agencies in New York. For law enforcement professionals, in particular, the opportunity comprised a chance to test out their theories and strategies in operation.

> "The issue for Frucher was simple. He said, 'Toby, this is a once-in-a-lifetime chance to rebuild the public schools in New York. It may come around once every fifty years. If we blow this, we may never get another shot at it.' Very simply, our credibility hinged on keeping the SCA building program free and clear of racketeers. Yet, even as the SCA was being formed, investigations could well have been underway that it knew nothing about. The SCA didn't want to give contracts to companies that were being investigated, or contract with consultants who were on the verge of indictment. Some investigation could well be ready to drop out of the sky on our heads, and plunge the new program into scandal before it ever got off the ground." [55]

Thomas D. Thacher II, in fact, seemed uniquely situated to develop for the SCA's Office of the Inspector General the relationships with law enforcement agencies that Frucher lacked at the Battery Park City Authority. Thacher was a former New York County District Attorney, past director of OCTF's Construction Industry Project, and, in 1989, head of the joint New York County-OCTF Construction Industry Strike Force. The trustees expected that, because of his relationships with OCTF and the New York County District Attorney's Office, Thacher would help the Office of the Inspector General gain access to critical information about firms and individuals in the construction markets, and use that information to help the SCA determine which companies to do business with. As the SCA's Inspector General, Thacher would also be able to use his links with law enforcement to conduct and participate in criminal investigations of firms that successfully

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[55] Thomas D. Thacher II, interview. Thacher later wrote of this moment. "[T]he trustees spelled out a challenge that was impossible to reject. They pointed out '[that we had] been part of an investigative initiative focused on construction industry racketeering which has been more comprehensive, intensive and sustained than any before it. . But you have nonetheless concluded in the [OCTF] Report that the industry's systemic corruption and racketeering can never be controlled by law enforcement alone. You have called for institutional reform of those structural characteristics of the industry which generate motivation, ability and opportunity to act corruptly. Here then is our challenge -- we are willing to put our money where your mouth has been. Design a strategy and mechanism to protect this Authority and to support institutional reform. If you conclude that it can't be done, then much of your writings can only be judged as academic theorizing and glib thoughts that are never likely to be implemented.' Once the challenge was framed in these words, it was impossible to reject." Thacher, "Institutional Innovation in Controlling Organized Crime," 1992.

crossed the SCA's protective moat, but which were later suspected of defrauding the SCA.

The Trustees offered the position to Thacher and he accepted, becoming, in 1990, the New York City School Construction Authority's first Inspector General.

First Steps

In a memorandum to SCA Trustee Normal Steisel dated April 17, 1989, Thacher proposed a formal organization structure and mission for the Inspector General.[56] As Frucher, Thacher, DeLuca and others understood it, the SCA Inspector General function would contrast sharply with the model of the traditional inspector general, and forego investigations of minor transgressions that did not impact on the cost or quality of school construction. [57] Rather, Thacher proposed this mission:

> ...to protect the SCA from victimization by racketeering, fraudulent schemes, wasteful practices and all manner of crimes perpetrated by those doing business with, as well as those employed by, the SCA -- e.g., billing for services or supplies not delivered; bribery and extortion in the inspectional services; bid rigging, price fixing, illegal cartelization [among contractors or suppliers]; labor racketeering [by union officials and corporate officers]; no-show employee payrolls; sham MBEs... and minority group extortions... By reducing corruption and fraud and by supporting suits for the recovery of moneys that have been lost, the Inspector General should not only save the SCA a considerable amount of money, but it should further serve the legislature's stated objective of attracting greater private sector participation in the SCA's construction programs. [58]

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[56] Memorandum, Thomas D. Thacher II to Normal Steisel. *Structure of the Office of Inspector General School Construction Authority.* April 17, 1989.

[57] Those inspectors general typically monitor everything from minor transgressions, such as an employees claiming "sick days" for personal vacations, to serious felonies, such as embezzling government funds. Kevin Ford, an attorney who would soon become the SCA's First Assistant Inspector General, recalled in an interview that as Assistant Inspector General at the New York City Department of Environmental Protection (DEP), his office been required to focus principally on misconduct among the agency's more than 7,000 employees. Ford reflected that though DEP was a major municipal construction agency, prior to his arrival the DEP inspector general had initiated not a single case that involved fraud in the contracting process. (Kevin Ford, interview, 1992.)

[58] Thacher, "Institutional Innovation in Controlling Organized Crime," 1992. This mission definition formally expanded the SCA Inspector General's purview beyond organized crime, formally considered. It included, notably, criminal enterprises, syndicates and ventures of any kind impacting the SCA, whether of the *La Cosa Nostra* variety, or of public corruption and white collar crime. This comports with the robust view of the comprehensive nature of the organized crime problem that Blakey, et. al., had alluded to years earlier in the *Rackets Bureau* guide: "[M]any of the same issues faced in an organized crime control unit will be faced in a public corruption or a white collar crime control unit. Significantly, too, the activities of organized criminal groups usually involve corruption: they frequently embrace offenses traditionally associated with white collar crime. Consequently, although the touchstone of the sophisticated organized crime group -- the systematic use of violence -- will usually be missing in most public corruption or white collar investigations and prosecutions. [*sic*]. Many of the same investigative

Operational Goals and Objectives

To achieve its mission required that the Inspector General embrace several core objectives:

- "Harden" the SCA target and reduce its vulnerability to attack by strengthening the SCA's own defenses. This required that the Inspector General survey the SCA's own practices and procedures and recommend steps to fortify the exploitable ones.

- Reduce the *likelihood of attack* by being vigilant in identifying those firms and individuals that seemed likely, given the chance, to exploit the SCA, and prevent them from doing business with it at all.

- In the event of an attack, *reduce the damage done* by taking steps to identify the breach, interdict it, and repair quickly.

- *Create an intolerable -- and well-publicized -- cost* for those caught in the act, and so deter those who would ordinarily seek to exploit the SCA. By sustaining an ongoing and credible threat of discovery and punishment, the Inspector General would achieve this effect by direct incapacitation and punishment of those caught

The Operational Priorities to Pursue

"Harden" The SCA Target

To make the SCA difficult to victimize, it would be essential to find and close any "open windows" to racketeering that left the agency vulnerable to attack and corruption. To achieve this required that the SCA, using experts in loss prevention and management analysis, as well as timely information from law enforcement about the activities of racketeers, survey its own practices, assess its susceptibility to racketeering and corruption, and remedy its deficiencies. It was important that the Inspector General provide candid assessments of failure when they occurred, and make recommendations that were sensitive to the requirements of building both cleanly, and quickly. The Inspector General would also monitor SCA efforts to remedy the deficiencies it detected, and raise a ruckus if nothing was done.

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and prosecutive techniques as well as other legal or administrative problems will be common in each of these three areas. Hard and fast lines therefore, cannot be drawn...each represents a similar effort..." Blakey, Goldstock, Rogovin, *Rackets Bureaus*, 1978. Pp. xII-xiv.

Make Past Performance Count: Prescreen Potential Contractors

Second, the SCA had to be vigilant in identifying those firms that seemed likely, given the chance, to defraud or corrupt the agency, and to keep SCA business out of their hands altogether. Prequalification would comprise a moat around the agency; the Inspector General's task was to set up the filters and screens that let high performance contractors across it, and that would keep high-risk contractors standing on the distant shore, perhaps to be snapped up by law enforcement.

To establish a viable prescreening operation -- one that could withstand the inevitable legal challenges -- required the agency to establish standards and procedures for its actions. It also required that the SCA, through Inspector General, gain access to data on the past business practices and operating performance of those firms seeking its business, and use it to determine which firms to permit even to bid on agency work.

As the Inspector General was not a law enforcement agency, this data would likely be drawn, first, from public records. Sources could include credit bureaus, newspapers and magazines, courthouse filings, lawsuits, corporate ownership documents, trial transcripts, and other public sources. Law enforcement agencies also possessed information that would likely be critical to the SCA's efforts -- information from confidential sources, electronic eavesdropping, grand jury matters, and ongoing investigations. If the Inspector General could tap and mine the large stores of valuable, publicly available data, it might find information that was directly relevant to its determinations of firms' fitness and risk. If the Inspector General could also find a legal means gain to access to law enforcement's proscribed information and confidential sources, the SCA would gain even greater advantage.

It was important, therefore, that the SCA establish a strategy to gain authorized access to, manage, and use the vast stores of public and private data already available -- and unfolding in current investigations -- that concerned firms and individuals doing business in the marketplace. In this respect, the SCA's relationships with law enforcement agencies were critical to develop

Reduce The Damage Done: Uncover and Stop Schemes Quickly

To truly protect itself, the SCA would have to acknowledge the possibility that its prequalification efforts would sometimes fail. Given the fluid nature of racketeering and the imperfection of its screens, the SCA had to assume the worst, and provide for a capability to detect schemes in its midst, to cut them short, and to minimize the cost -- in dollars, lost time, and interrupted projects -- of its failure. .

While the Inspector General might develop some of this information on its own, law enforcement could develop more, especially with the access the Inspector General could give it to SCA operations. Thacher wrote:

> Only law enforcement has the investigative tools to really determine who is doing what to whom and how (e.g., wiretaps, grand juries, informants generated through promises of immunity or lenient prosecutorial exposure, search warrants, and sting operations)...[A] means for integrating law enforcement agencies into the Inspector General operations would have to be found.[59]

Integration required the agency to form cooperative working relationships with the region's Federal, state and local law enforcement agencies. If successful in these relationships, the SCA could gain access to information to help it determine which companies to do business with. Prequalification would be advantaged. And, the SCA could use its links with law enforcement to monitor suspect firms and individuals during their contracts. If necessary, the SCA could conduct and participate in criminal investigations of businesses that it had prequalified and, having successfully crossed the SCA's protective moat, were later suspected of defrauding it.

Create An Umbrella of Deterrence: Make SCA Cases A Law Enforcement Priority

Lastly, it was essential for the SCA to create an intolerable -- and well-publicized -- cost for those caught in the act. Thacher wrote,

> [The Inspector General's] operation would have to generate a perception and a reality that wrongdoing would be detected and would result in significant punishment – prosecutions, civil law suits and/or administrative sanctions ranging from the withholding of construction progress payments to debarment from future work. [60]

Building relationships with law enforcement agencies was critical if the SCA were credibly to threaten prosecution and punishment of those firms that were intent on defrauding it. In addition to providing a firm basis to debar vendors from future work, the SCA's relationships with law enforcement might gain it access to a range of civil and criminal remedies, creating an effective umbrella of deterrence. This would include remedies such as restitution, civil penalties, and forfeiture, and well as criminal fines and prison terms.

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[59] Thacher, "Institutional Innovation in Controlling Organized Crime," 1992.
[60] *Ibid.*

Getting Organized

First Budgets and Staffing

"Blue skying" their model, Thacher worked with OCTF's Joseph DeLuca and consultant James Jacobs to propose an office of 100. It included two four-person teams to be assigned from the Construction Industry Strike Force, one team to be sent from the OCTF and the other from the New York County District Attorney. Each team would comprise an attorney, investigator, accountant and analyst.

Steisel and Frucher rejected the early plans as too expensive. Eventually, Thacher, DeLuca, Steisel and Frucher settled on an Inspector General's office numbering 50, with a budget of approximately $3 million (see attached organization chart). The two law enforcement teams remained in the final model. Thacher would fund them from his own budget at a total cost of $500,000 annually. The office has maintained approximately this level of staffing in each of its five years of operation. Today, it is approved to staff 53 positions.

Reporting Relationships

The matter of title, pay, and reporting relationship remained to be resolved. Traditionally, inspectors general have some degree of independence from their host agencies. This separation is intended to prevent the host agency from influencing or compromising investigations that the host agency finds damaging.[61]

The SCA Inspector General's Office, however, did not follow this model. Thacher believed that inspectors general, because of their independence from their host agency, often had a limited ability to influence and reform the agency's practices.

> If acting as an outside, independent agency, the traditional inspector general must often rely on the threat of embarrassment through critical published reports or leaks to the media in order to generate reform of the agency's policies and procedures. Actual use, or threatened use, of such leverage necessarily results in an adversarial relationship between the inspector general and the subject agency. Recommended reforms are rarely well received when proposed by an adversary.[62]

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[61] See, Mark H. Moore and Margaret Jane Gates. *Inspectors-General Junkyard Dogs or Man's Best Friend?* New York: Russell Sage Foundation. 1986.

[62] Thacher, "Institutional Innovation in Controlling Organized Crime," 1992.

Although the Inspector General wanted to avoid the possibility that its investigations would be compromised, Thacher and the trustees "tilted in favor of institutional integration" in establishing the Inspector General's reporting relationships. [63]

> "I told Frucher and Steisel that as trustees they must demonstrate their commitment to corruption and racketeering control by structuring and placing the Inspector General within the Authority in a way that tells the world and everybody in the Authority that this is one of the most important operations *of* the Authority. That it's as important that we do it right as that we do it at all...
>
> "My view was that the Inspector General had to be one of the SCA's senior-most officers -- a vice president. We would be unable to institute reforms unless the Inspector General sat next to, and had the trust of, the President. The trustees needed to demonstrate their commitment to the importance of the Inspector General by setting his pay at no less than the highest officer of the SCA outside of the President." [64]

Steisel and Frucher assented. An arrangement was established by which the SCA Inspector General would wear two hats. In addition to heading his own inspector general's office, the Inspector General would be a senior SCA vice president. In that role, the Inspector General would report to the SCA's president/CEO (who, in turn, reported to the Board of Trustees). To counterbalance his accountability to the SCA, the Inspector General would be able to obtain physical independence: while SCA's headquarters would be located in the borough of Queens, the Inspector General would site its office in the borough of the Bronx.

The most significant safeguard of the Inspector General's independence was a second reporting relationship for the Inspector General to the Board of Trustees, who could overrule the president. This dual reporting relationship put the Inspector General on the fulcrum between two competing interests. As Inspector General, he would be responsible for doing everything possible to block corrupt companies from doing business with the SCA; as a vice president, he would also answer to the SCA's larger mission of building quality schools expeditiously and at the lowest possible cost -- two goals that could be at odds with each other. Case by case, the Inspector General would have to weigh the demands of his two positions, as his signature would be required on every contract the agency awarded.

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[63] *ibid.*

[64] Thomas D. Thacher II, interview (1992).

OFFICE OF THE INSPECTOR GENERAL

ORGANIZATION PLAN

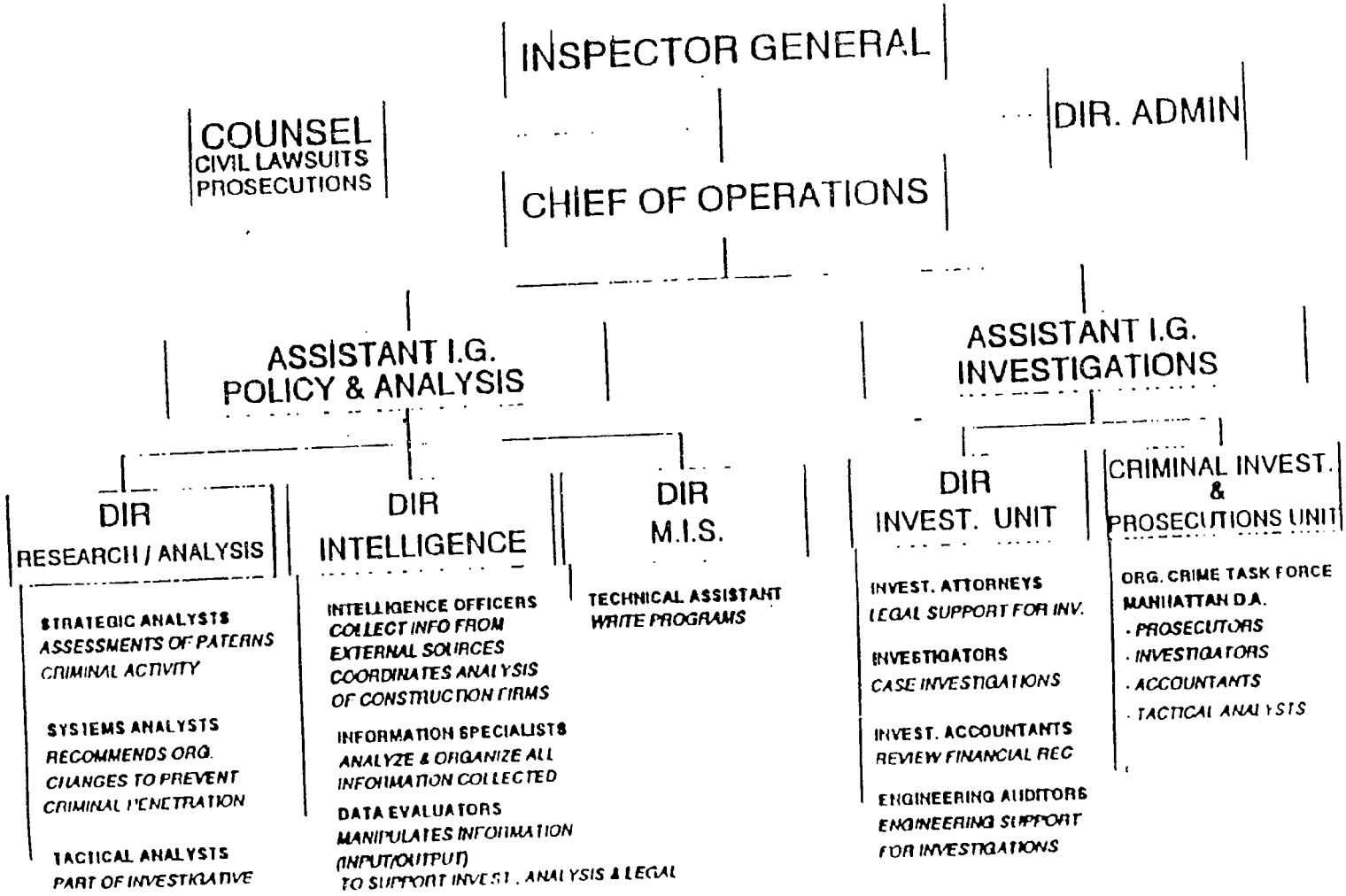

Figure 1

Office Structure

To carry out the mission, the Office of the Inspector General became organized into three units: **Operations, Administration,** and **Counsel**. Figure 1 represents the current organizational chart, and mirrors the original chart.[65]

Operations Division. The Operations Division was the largest, and comprised the ***Policy and Analysis Bureau,*** and the ***Investigations Bureau.*** Each bureau was directed by an Assistant Inspector General. [66]

- The ***Policy and Analysis Bureau*** comprised three units: *Intelligence*; *Research and Analysis*; and *Management Information Systems (MIS)*.

  - The *Intelligence Unit* obtained information about companies and individuals doing business with, or seeking to do business with, the SCA. Operationally, this meant conducting *electronic due diligence* -- consulting databases in reviewing all applicants for prequalification and subcontractor approval. In addition, it reviewed all SCA contracts, conducted final reviews of contractor integrity, integrity of the selection process, and assessed potential areas of racketeering susceptibility. Further, it provided intelligence support to Inspector General investigators and others.

    The *Intelligence Unit* was staffed by employees in three different titles:

    - INTELLIGENCE OFFICERS, who collected information from external sources and coordinated analyses of construction firms;

    - INFORMATION COLLATORS, who analyzed and organized collected data

    - DATA INPUT CLERKS, who manipulated data to support investigations, analyses, and legal work

  - The *Research and Analysis Unit* prepared analytic reports that assessed patterns of criminal activity and identified SCA rules that permitted or encouraged corruption. It worked with other divisions within SCA on developing institutional reform through changes in procedure and contract boilerplates. The Unit reviewed and commented on all proposed SCA policies and procedures. It received information from the *Intelligence Unit* and from the units that comprise the ***Investigations Bureau*** (see Figure 1).

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[65] SCA Office of the Inspector General, *Procedure No. IG-1*

[66] See, position descriptions, *New York City School Construction Authority, Office of the Inspector General. Title Codes SC 616, 600, 615, 641, 614, and 613.*

V. THE WORK OF THE OFFICE: PREQUALIFICATION, INVESTIGATIONS AND PROCEDURAL REFORM

The basic work of the office is divided into three areas: ***prequalification, investigations and prosecutions, both civil and criminal,*** and ***loss prevention through reform of SCA procedures.***

Prequalification

One of the Inspector General's most important contributions to the SCA's efforts to build free of racketeering and corruption, and to build to competitive standards of price and performance, was its work in developing the SCA's prequalification process.

The SCA's Special Commitment To Buy And Build Clean

In contrast to many New York City agencies, the SCA's trustees were at the outset concerned to protect the Authority from organized crime and corruption, and from any loss of public support that might result from the appearance of racketeer influence or control of its building program. To do so required designing a process to screen out high-risk contractors from the SCA's vendor pool.

A Flawed New York City Tradition of Vendor Review

City agencies had long had some authority, even the legal responsibility, to award contracts only to "responsible" vendors whom they found had "the capability in all respects to perform fully the contract requirements and the business integrity to justify the award of public tax dollars." [67] The permissible basis of a finding of "nonresponsibility" included criminal convictions, indictments, pending grand jury investigations, incompetence and lack of integrity. [68] Yet despite these broad legal powers, most City agencies rarely used them.

Under established procedures, agencies made responsibility determinations only *after* having opened the bids for a contract and identified the lowest-bidding firm. Once the agency opened bids, each vendor was required to hold to its bid for 45 days. During

[67] City Of New York, Office of the Comptroller. *No More Business As Usual: Keeping City Contracts Out Of The Hands Of Dishonest Contractors.* September 1992, P. 15. This wording became effective September 1, 1990.
[68] OCTF *Final Report,* 1991.

- Pursued criminal prosecutions in conjunction with law enforcement agencies, including five district attorneys, the New York State Organized Crime Task Force, and the United States Attorneys for the Southern and Eastern Districts.

- Pursued civil enforcement actions to seize targets' assets and impose other civil sanctions on wrongdoers. Worked with outside counsel retained for these purposes.

Administrative Support Division. Administrative Support provided for the agency's administration, and its internal security. Administrative duties included finances, purchasing, budgeting, support staff supervision, and office procedures. Security duties included plant security, motor pool, background checks, internal investigations of the Inspector General office itself, subpoena control, safekeeping of evidence, and maintenance of technical equipment.

prequalification reviews and investigations, and assistance in settling civil claims where the SCA had been victimized.

The *Field Investigations Unit* was overseen by the Assistant Inspector General, Investigations, and directed day-to-day by the Director, Field Investigations. It was staffed by employees in three titles:

- INVESTIGATORS, who conducted investigations

- ENGINEERING AUDITORS, who provided engineering support for investigations.

- INVESTIGATIVE ACCOUNTANTS, who conducted forensic analysis of books and records of suspect firms and individuals, lifestyle and network investigations, and who traced money flows to aide in the search for targets' assets.

- The *Criminal Investigations and Prosecutions Unit* conducted criminal investigations in conjunction with the Inspector General in matters the unit developed or the Inspector General referred. This unit was staffed by investigators, attorneys, analysts and accountants detailed to the Office of the Inspector General from the New York State Organized Crime Task Force, and the New York County District Attorney's office.

Counsel's Office. The Counsel's office included the First Assistant Inspector General, the Assistant Inspector General for Special Operations, and two Deputy Counsels. The role of counsel was to advise the Inspector General about the plethora of civil, criminal, and regulatory legal issues confronting the office. In addition, counsel functioned as the chief civil enforcement officer, determining whether in each investigation the agency should pursue civil or administrative remedies involving antitrust, forfeiture and injunctive actions, and other functions:

- Conducted administrative proceedings as part of Inspector General recommendations for disqualification, suspensions and terminations of contractors resulting for Inspector General investigations.

- Conducted negotiations related to, and prepared and executed legal documents involving contractual agreements with SCA contractors, vendors and consultants.

- Managed special monitoring relationships such as certifications and independent auditing firms, (see below, Section ---), pursuant to initiated agreements with the Office of the Inspector General.

The *Research and Analysis Unit* was led by a Director and staffed by employees in three titles:

- STRATEGIC ANALYSTS, who assessed patterns of criminal activity

- SYSTEMS ANALYSTS, who recommended organization changes to prevent criminal penetration

- TACTICAL ANALYSTS, who were part of investigative teams.

- The *Management Information Systems Unit* provided "automation support" for the Inspector General's staff. This included supporting computer and telecommunications access for units within the office, , particularly to the intelligence database développed by the *Intelligence Unit*. The MIS Unit was led by a Director.

- The ***Investigations Bureau*** was directed by an Assistant Inspector General. It included two sub-units:

  - The *Field Investigations Unit* was established to investigate complaints and allegations about potential illegalities either from within the SCA or from external sources. Complaints ranged from petty theft to labor racketeering involving bid rigging and organized crime. In addition, it might initiate its own audits and investigations, using data provided by the *Intelligence Unit*, or based upon reports from the *Research and Analysis Unit*.

  The *Field Investigations Unit* was responsible for conducting investigations of entire projects, specific contracts, and categories of construction activities believed to be corruption-prone. Where criminal prosecutions might result from an investigation, the *Field Investigations Unit* worked with and supported the *Criminal Investigations and Prosecution Unit* (see below).

  The *Field Investigations Unit* was also deeply involved in civil actions. These included but were not limited to RICO prosecutions, forfeiture and contract claims aimed at returning fruits of fraudulent activities to the SCA. It also assisted in seeking restitution on criminal cases, and claims for damages that often included the costs of investigations.

  Lastly, the *Field Investigations Unit* was deeply involved in administrative actions, including non-criminal initiatives involving support to

this period, the agency subjected the low-bidding vendor to the responsibility review. At the end of the period, all bidders would be released from their bids, and the lowest bid either accepted or rejected, or the whole matter rebid.

For an agency that was determined to build quickly or to acquire much needed equipment, rejecting the low bidder, and possibly starting from scratch, was not a pretty sight to contemplate. Having weathered a contracting process that might have taken months or even, perhaps, years, agencies were eager to get on with their business, not investigate their low bidder, let alone to find it non-responsible or to begin disbarment proceedings against it. There was, in addition, a dead-on certainty that the low-bidding vendor would sue if a higher-bidding vendor were awarded the contract, and force the entire process to begin anew.[69] To do so would amount to a sentence of slow death for a project.

The responsibility review was, nonetheless, an especially important matter in construction. Firms with poor reputations or past problems that sought new business could easily vanish one day, reconstitute themselves the next under a new "alter ego" name, slip back into the vendor pool, and qualify for new business. Only a thorough background check that went below the surface appearance of a firm would reveal its true corporate ownership.

Unfortunately, although New York City maintained an automated database system to help agencies conduct background investigations -- the Vendex system -- it comprised information that contractors *self-disclosed,* but that agencies rarely checked for veracity.[70] It also contained information that agencies reported concerning actions they had taken against firms. But since agencies rarely took such actions or made such findings, many nonperforming firms escaped Vendex mention.[71] With the 45- day clock ticking loudly in

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[69] "Once the bids are in, the low bidder has a right to be awarded the contract, subject to being found responsible. At that point, declaring the low bidder non-responsible has been regarded, perhaps incorrectly, as tantamount to taking the contract away from the contractor." OCTF, *Final Report,* 1990.

[70] "Under the [Vendex] system...companies that compete for city contracts have to fill out a form, listing the company's principals and detailing whether they or the company have ever been indicted. But some city officials acknowledge that the agencies planning to award the contracts do little to verify the answers or to investigate further." Alan Finder, "Dangerous Parking: New York's Biggest Scandal of 1980's Bubbles Up to Embarrass Inspectors." New York *Times*, April 11, 1993. Recently, the Miami *Herald* reported a story of Medicare fraud with a similar theme: "Cheating Medicare is as easy as filling out a four-page form that asks for basic information -- name, address, phone number and a statement saying the operators have never been in trouble with Medicare... Most of the time, the information isn't verified, allowing anybody with a $15-a-month rented mailbox and a beeper to go into the Medicare supply business." Cited in Malcolm K. Sparrow, *Health Care Fraud Control: The State of the Art.* NIJ Grant #94-IJ-CX-K004. Draft, August 1995.

71 Even if a company did perform poorly, it could still play the game effectively: it was not uncommon for companies to threaten to delay or pull out of jobs on which they had substantially completed work, if poorly, should agencies rattle their sabers and threaten to tarnish the company record with a poor performance rating. Indeed, when agencies did uncover information that would support debarment of a firm, few agencies were willing to invest the energy and resources to actually plead for its full debarment before the Office of Administrative Trials and Hearings. In the rare event that action was taken at all, the

its Commissioner's ear, and lacking the requisite investigative resources, skills or authorities, few agencies ever took the time to probe into a contractor's background in any meaningful way.[72]

Law enforcement agencies had information about some individuals and firms, but as Frucher experienced, they were ordinarily unauthorized and unwilling to divulge much to builders. Privacy laws, the requirements of confidentiality, and the burden of sorting public from confidential information in their files made it rare for such data to make it past one enforcement agency's front gate to another's, let alone onto the desks of civilian commissioners.

In the entire vendor review process, only the City's Department of Investigation (DOI), in its background checks on firms, provided an independent source of information to agencies. DOI checks too, however, often revealed little.[73] Even the City Comptroller, with the authority to block a contract even after an agency approved a winning vendor, had difficulty executing its task. For in practice, the Comptroller had few resources at its disposal to determine, at a level that would withstand court challenge, whether the proposed contractor had been involved in "corrupt activity."

In sum, as the SCA Inspector General came onto the scene the City vendor review process was saddled with cumbersome machinery and positioned much too far down the procurement road to be useful. The cost to agencies that pursued responsibility reviews thoroughly was much higher than if they merely did a perfunctory job and got on with their core missions.

The failure of many civil agencies to exploit the potential of responsibility reviews represented an important, missed opportunity to clean up public construction in New York. For one, the agency that bought without care or knowledge risked doing business with firms that had clearly discernible past performance and integrity problems. Those firms could now again engage in some form of corruption or racketeering, again raising costs, degrading construction quality, engendering corruption, or likely all three. Further, having failed to disqualify low-performance firms who maintained their competitive edge

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City might declare the firm non-responsible for a particular contract. As a result, a firm might be found non-responsible by one agency on a particular contract, yet still be in position to receive millions of dollar in contracts from another. (Thomas D. Thacher II, interview, 1995)

[72] A Department of Transportation spokesperson, when asked about objections concerning his department's plans to award a contract to a firm that had been linked to organized crime, was candid in his views: "We're a construction agency, not the FBI," he said. (New York *Newsday*. July 15, 1992.) For a detailed discussion of Vendex, see James B. Jacobs and Frank Anechiarico, *Blacklisting Public Contractors as an Anti-Corruption and Racketeering Strategy*. Journal of Criminal Justice Ethics, Summer/Fall 1992.

73 "Even though the Department of Investigation performs a routine check of a company before the award of a contract, it maintains that its role is minimal. Its investigators take the name of a company and its principals, listed on the Vendex form, and run them through the department's files, checking by computer whether the names have appeared over the previous five years in what investigators call 'closing memos,' the final reports on their inquiries. 'Our part in this is small,' said an Investigation Department spokesman. 'It's not an investigation. It's just a file check.' " Alan Finder, *op cit.*

The Enabling Statute: Authorization

Under the SCA's enabling statute, the Authority acquired the legal right to restrict competition on SCA contracts to firms that had been prequalified, and to eliminate firms with histories of poor performance from even bidding on SCA projects. All contracts over $10,000, and all applications of prequalification, required the Inspector General's review and approval.

The Inspector General's aim in prequalification was to identify those relatively few firms from among the many seeking to do business with the SCA whose past performance or relationships with organized crime seemed to constitute a significant future risk to the SCA; to exclude the highest risk firms from doing business with the SCA altogether; and to monitor or control by means short of full debarment those firms that seemed to constitute a risk, but whose debarment was either impracticable, impossible, or unnecessary. In this respect prequalification was the SCA's first line of defense against crime, corruption, and racketeering.

Moreover, prequalification would allow the SCA to act more like a private builder in its contract-award decisions, looking both to lowest possible price, and to past performance on the job as selection criteria. In this respect, prequalification was a critical element of SCA efforts to deny high-risk firms their competitive advantage in the marketplace. It was a centerpiece of the Inspector General's efforts to leverage the SCA's market muscle to level the playing field and restore price and performance as marketplace virtues.

The Development Of Prequalification[75]

Though the SCA was perhaps willing to risk some inconvenience to achieve this, a well-managed prequalification program might, also, actually speed up the contracting process, and permit the SCA to fortify its program *and* meet its construction timetables. After all, investigating every contractor *before* it could even bid meant that, once it opened bids, the SCA could promptly award contracts to the lowest responsible bidders *and* be confident that each had been prescreened and found clean.

To achieve the objective of buying and building clean, the SCA, spurred on by the Inspector General, gradually transformed the standard vendor review process into a far more stringent and demanding prequalification process. Specifically, it:

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[75] See, in general, *Chapter LXXIV, Part 9600, Guidelines for Qualifications and Evaluation of Contractors, Subcontractors, Consultants, Vendors and Suppliers Of Contracts On All Phases Of Construction, Reconstruction, Improvement Or Rehabilitation Of New York City Schools.* Pursuant to section 1734 of the New York City School Construction Authority Act, the legislature established these guidelines governing the qualifications and evaluation of firms.

by cheating, defrauding and corrupting the government, city agencies lost an important opportunity to give high-performance firms a competitive advantage in the marketplace.

The Inspector General's Approach to Vendor Screening

Thacher reflected on the failure of responsibility reviews, and the steps government could take to better protect its interests:

> "What are we going to do about this? The Government's view has always been, 'I've got to give it to the low bidder, and if I manage it well, they won't screw me.' Even if they've the just finished screwing the Port Authority, the Housing Authority, the Transit Authority. The result is often this: government lets the fox in, and then tries to keep him honest. Often without any means, by the way , to do that.
>
> "What's the answer? Keep the fox out altogether. Don't try to chase him after he's in, trying to catch him cheating you. Stop him at the door with a fair program that creates a penalty for bad performance on previous projects. Don't even let the fox come to the bidding table, much less onto the construction site.
>
> "We've analyzed responsibility reviews and we know they don't work. In public construction, the bid opening is always at the very end of the procurement process and is invariably late, sometimes years later than planners had thought. Once you have the low bidder identified, every incentive is to award the contract as quickly as possible to get the project going.
>
> "The last thing a commissioner whose job depends on on-time delivery of his projects wants to hear is his Inspector General saying, "I've got concerns about the integrity of the low bidder. It may take some time to prove, but I believe there are unacceptable organized crime connections." That commissioner doesn't have any extra time on his hands. Furthermore, anything that delays a contract award beyond 45 days after the bid opening -- when other bidders will be released from their bids -- means the whole bidding process has to start over. A challenge to the low bidder on ethical grounds almost always results in disputes and law suits -- and more delays.
>
> "You must, rather, start your analysis of prospective contractors well before the bidding even takes place. Prequalification is the answer. Why is it better? Because the time problems disappear: a contractor can't even bid until after it is issued its clearance, so there is no contract on the table waiting while we review the firm. And if we disqualify that company, there is no project that it can hold hostage in a lawsuit -- the problem disappears because we've bounced the company before it could even bid."[74]

[74] Thomas D. Thacher II, interview (1995).

- Established strict standards for qualifying firms to bid on SCA jobs

- Developed a new prequalification form that went well beyond the standard vendor review form

- Learned how to prioritize its investigative efforts

- After a prequalified firm had been identified as the lowest bidder, conducted a second integrity check prior to going to contract

- Invented new investigative means for uncovering corrupt firms that hid their true identity behind "alter egos"

- Established standards of evidence to be used in prequalification procedures (including the tricky question of how it would use information gained from its law enforcement sources in its debarment procedures)

- Used its powers to require "certifications" (the requisite to conditional approvals) from firms that were suspect but could not reasonably be debarred

- Found ways to impose "preconditions" on firms that sought to qualify for SCA business but seemed suspect

Establishing The Basis For Denying Prequalification

The SCA's prequalification procedures included the Inspector General's integrity test. This comprised five possible grounds for debarment from SCA work:

- For a criminal conviction within the past five years of the applicant, or its current or past officers or principals, indicating unfair or unethical business practices or moral turpitude, the applicant may be barred from doing work for the SCA for a period of up to five years from the date of conviction.

- In case of a pending criminal investigation of an applicant or its officers or principals or its affiliated companies, the applicant will be precluded from doing work for the SCA during the pendency of the investigation.

- In the event that the applicant, or any of its officers or principals, or any affiliated companies, are under indictment, the applicant will be precluded from doing work for the SCA until favorable resolution of the charges.

- A material false statement or omission made in response to any question in the prequalification application will result in debarment of the applicant for a period of up to three years from the date of filing of the application.

- If the applicant's lack of integrity and ethics arises from circumstances other than the ones noted above, the SCA will evaluate the facts and circumstances on a case-by-case basis and debar an applicant for up to five years. [76]

The Prequalification Form

When the SCA first opened for business, the Inspector General faced a significant task. Hundreds of school builders and subcontractors who had, overnight, become *former* vendors to the Board of Education sought to do business with the SCA. It was the Inspector General's task to prequalify each.

Initially, the Inspector General used the same form that all City agencies used to evaluate potential contractors, supplemented by a quickly patched together four-page questionnaire that focused specifically on integrity. Over the years this form evolved into a 30-page questionnaire related specifically to firms' financial standing, experience, performance history, and, of primary interest to the Inspector General, their "reputation for honesty and integrity."

> "What does prequalification take? A good questionnaire. Information. We must have detailed, reliable information about a company to find out whether it has a reputation for being clean, competent and financially sound. The first place to get the best information is from the applicant. So we designed a questionnaire that, if answered correctly, produces the information we need. Many questionnaires we reviewed missed the integrity piece altogether. No government agency should do business with a briber or someone who has stolen public contracts or who has falsified its business records. But look at all the forms in the country and you will not find a single form that exposes that." [77]

Today, the SCA prequalification application requires, first, that firms identify their principals or "key people," including partners, directors, officers; shareholders of more than 5% of firm stock; managers or individuals participating in policy-making or financial decisions; and "any person in a position to control and direct the firm's overall operations." It then asks of these "key people," among other questions, whether any of them -- past or present -- has ever been the subject of an investigation; been arrested or convicted; pleaded *nolo contendre*, entered into a consent decree, been granted immunity,

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[76] SCA Contract Administration Prequalification document, *Attachment 3: Procedure, Section 1.d., Integrity and Ethics*

[77] See, also, *A Guide to Best Practices for Past Performance.* Interim Edition, Office of Federal Procurement Policy, Office of Management and Budget, Executive Office of the President. May 1995. This is a comprehensive guide to rating Federal contractors based on past performance.

or taken the Fifth Amendment in testimony regarding a business-related crime, and if so, to explain. It asks, further, whether any past or present "key people" have ever knowingly filed a false statement with a government agency, falsified a business record, bribed a labor official or government employee, rigged bids with other firms, or entered into cartel-like agreements "not to submit competitive bids in another's territory."[78]

> "How is the SCA form different from other government screening questionnaires? While there are many differences, the most critical one is the way we determine who controls the firm fiscally and operationally, and the way in which we demand that applicants describe prior problems.
>
> We're experienced about criminality in the construction industry. We know that the most commonly committed crimes in this business are falsifying business records, filing false instruments with government agencies, bribery of public officials, bribery of labor officials, commercial bribery, and bid rigging.
>
> Most agencies limit their questions to prior *convictions* for these crimes. We go much further. *We ask them if they've ever committed one.* People say, 'Gee, what a stupid question. Who'd ever answer "Yes" to that?' Well, a false 'No' answer can result in debarment, prosecution, and (what is to many the most significant consequence), a finding of fraudulent inducement to enter into a contract.[79] This finding requires the contractor to give back to the SCA every penny it received from the SCA even if the SCA got value for the money it paid out."[80]

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[78] See, *New York City School Construction Authority Prequalification Application.* SCA Form 050 Oct 93

[79] Under New York State law, the SCA could recover the full cost of a contract, even if the services had been completed satisfactorily, in the event it could establish that the contract was entered into as a result of "fraudulent inducement." The last page of the form that all key persons sign includes the following certification by the signatories: "A material false statement or omission made in connection with this application is sufficient cause for denial of the application or revocation of a prior approval...*I recognize that all the information submitted is for the express purpose of inducing the Authority to award a contract...*" See, SCA Form 050 of October 1993.

[80] Thomas D. Thacher II, interview (1995). New York City agencies, like contracting jurisdictions elsewhere, occasionally face the following problem: what to do when a contractor at work on a city project is found to have engaged in fraud, bribery or other shoddy business practices somewhere else? For example, a contractor that might have just been awarded a lucrative city contract is subsequently indicted for participating in a conspiracy to rig contracts in New Jersey. The city clearly can deny further work to the contractor of the basis of the indictment, but its efforts to terminate the *existing* contract often lead to lengthy litigation. The SCA approach to this problem requires contractors -- as a matter of their contract with the SCA -- to agree to abide by a set of well-defined "fair and ethical business practices." If, during the course of a contract, the SCA learns that a contractor has, for example, bribed a public official, whether in New York, New Jersey, or anywhere, that act can constitute a breach of a material condition of the vendor's SCA contract. The SCA then has the right to terminate the contract for cause, and to seek to recover damages.

Prioritizing Firms For Investigation

The SCA's Contract Administration Unit initiates the Authority's prequalification review, logging in all questionnaires. It screens them for completeness, for indications of poor performance on past SCA and other public jobs, and to determine whether the applicant has the requisite financial ability to perform SCA work. Once finished, the Contract Administration Unit refers the application to the Inspector General's Intelligence Unit.

The Inspector General's Intelligence Unit comprises three data input clerks, three collators, two intelligence officers and one research assistant. It is responsible for verifying all integrity-related information on the application. In addition to the self-reported information contained on the questionnaire, the Intelligence Unit seeks independent sources of data, and queries and examines numerous commercial, public, and confidential databases. In some instances the Unit enhances its reviews by traditional and nontraditional investigative means.[81]

The unit's clerks enter the prequalification applications into the Inspector General's prequalification database. Collators next perform an "electronic due diligence check" for each application. [82] They search the Unit's numerous data bases for links there pointing to past performance or integrity issues for persons, firms, or addresses named in the application. Among the commercially-available news, judicial, regulatory, corporate, and other data bases it searches are Dun & Bradstreet; Equifax; Phone Disk; Nexus Lexis; Datatimes; Superior OnLine; Oshadata; Brown's Letters; Best's

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[81] See, Alice LaPlante. *Networked PCs Become a Crime Fighting Tool in New York.* Infoworld, May 25, 1992. In a letter describing the prequalification operation, Thacher wrote: "The whole operation is supported by, and in turn supports, a comprehensive electronic database that is used to help make criminal cases, identify assets of potential civil defendants, and analyze the structure and ownership of business entities (i.e., identify the real players who operationally and fiscally control corporate activities.) This intelligence base is fed by numerous and easily obtainable electronic data bases as well as by the activities of the criminal, administrative and civil units within the SCA Office of the Inspector General." Correspondence, Thacher to Kevin Ford. *Re:Fulton Fish Market.* May 12, 1995.

[82] In characterizing its prequalification investigations as "doing due diligence," the SCA Inspector General borrows purposefully from analogous private sector efforts to protect the buyers of publicly-traded securities. In its original usage, "due diligence" referred to those investigative activities undertaken by the underwriters of publicly-offered securities to assure the validity of the claims made for the security prior to offering it for public sale. Congress required such due diligence in the Securities Act of 1933 (15 U.S.C. S.77a-bbbb) in order to protect the buyer of securities against the widespread manipulations and frauds that contributed to the 1929 market crash. Section 11 of the Act established conditional liabilities for the underwriter of securities unless it conducted, as part of its own independent review, a "reasonable investigation" of "all of the information deemed material to an investor's decision to purchase." This would involve "leaving no question unasked that experienced, sophisticated persons should ask, and leaving no answer intellectually unchallenged. Every answer must be tested to ascertain whether it, in turn, raises a pertinent question." This requirement became known as the "due diligence" provision of the Act. See, Joseph Auerbach and Samuel L. Hayes, II. *Investment Banking and Diligence: What Price Deregulation?* Boston, MA: Harvard Business School Press. 1986. Pp.32-83.

Guide; Autotrac+; Prentice Hall OnLine, Fed Debar, Principal's Failed Business database, and the internet generally.[83].

Often times, however, the most significant piece of information about a prospective contractor may come from within the extensive in-office data bases amassed by the Intelligence Unit. Working with local prosecutors, for example, the Inspector General has assembled a valuable, and large, electronic data base of sworn, public testimony from trial transcripts of organized crime cases and others. In addition, unless proscribed by the requirements of active investigations or privacy statutes, virtually all Inspector General internal memoranda -- including those of investigators and intelligence officers -- are stored and searchable on an office-wide data base, whether for prequalification or other purposes. Thus, firms or individuals who may have been implicated in prior or current investigations *anywhere* in the region can be identified -- even when no other public record of their corrupt activities exists.

An intelligence officer reviews the collators findings. The officer may make further inquiries, including contacting other contracting agencies, law enforcement units, or contacts within the SCA. The Director of Intelligence makes the final review and recommendation for approval, recorded in the prequalification database and forwarded, as a notice, to SCA headquarters.

The Inspector General ordinarily expects a prequalification review to take ten days. A single full, routine prequalification workup, including input and collation, usually requires 5-6 hours of the Intelligence Unit's time.[84] Prequalification status, once granted, extends for a period of two years from the date of prequalification, at which time a requalification application is required.[85]

Contract Review (The Second Integrity Check)

Once the SCA prequalifies a firm, it can bid on SCA prime contracts. However, the Inspector General monitors intelligence on even prequalified firms throughout their relationship to the SCA. Should new information become available the Inspector General may review and revoke a firm's prequalification status. In any event, the Inspector General, which must approve each SCA contract over $10,000, subjects any firm that has been declared the low-bidder to a second, though more cursory review just prior to going to contract.

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[83] Memorandum, Susan Petraglia to Rod Leith. *Commercial Data Bases.* New York City School Construction Authority, Office of the Inspector General. August 30, 1995.

[84] *The Prequalification Process: Frequently Asked Questions and Answers.* New York City School Construction Authority

[85] Discussion draft (unapproved), *Internal Office of the Inspector General Procedures Related to the Processing and Approval of Prequalification Applications, Contracts and Subcontracts.* April 3, 1995.

The Inspector General's "contract review" works much like prequalification, including inputting the contract into a data base and conducting electronic due diligence checks on it. An internal review process follows which is expected, rapidly, to update the initial prequalification inquiries. Should staff classify the contract as "recommended Non-Approval," it is forwarded to the Pending Review committee for action. A similar process may be followed for subcontractors.

The Inspector General reports that it rarely "kills" a contract at this point. However, as months or years may have elapsed since a firm's prequalification, new information about principals and firms may well have developed in the interim. "Contract review" provides the office with a last and especially valuable opportunity, prior to going to contract, to use or uncover additional information about highly suspect firms, and so lead ultimately to disqualification or some interim control measure (see discussion of certification, below).

But contract review also provides the Inspector General with useful information about the workings of the SCA itself. In a recent example, the Inspector General discerned a pattern of irregularity in the award of relatively small-dollar contracts for rapid work in time-sensitive matters:

> "Contract review highlights problem with programs, and problems with SCA process. In one program, we saw all these small contracts coming in from individual schools and principals which showed a crazy, poorly executed bid practice, like $75,000 contracts to fix lightbulbs. All the bidders had been prequalified – it was the award process that was suspect. We found out this information seeing the contracts, and also because Toby's participating in meetings concerning these apparently routine matters. It gives us a chance to see what the solicitation process was, and to raise questions about the bid process itself before the contract is awarded. Plus, it basically tips us off to watch these contracts as they progress. SCA is used to the multimillion dollar process, not to the $75,000 process." [86]

Contract review also provides the Inspector General with tracking data on SCA workloads. This provides a window on the operations of the SCA, highlights the changing risks of fraud, waste and corruption, and helps the Inspector General focus its own investigative efforts:

> "The contract review process shows us where SCA resources are being dedicated. If we see they're doing tens of millions of dollars of electrical work, for example, then from a strategic point of view you want to gather a lot of intelligence about the electrical contracting industry. From a policy analysis view you want to take a good hard look at electric contracts to see if anything is going on.

[86] Interview, David Eichenthal (1995).

"For example, we have a requirement on SCA contracts that when it is over $1 million the contractor has to be a participant in an approved apprentice program. It turns out that half the electric contractors were not, and could not, become members of an apprentice program because of a court ruling that deregistered these programs as shams. This, then, tells us a whole lot about the limited competition that's going to result on electric contracts." [87]

This second review raised more objections from the SCA than any other aspect of the Inspector General's prequalification process. The primary objection was that it appeared to slow the process of awarding contracts. As SCA procedures required the Inspector General to approve all contracts, none could go forward until the Inspector General completed its second review. "I didn't think that that step was necessary. It did slow things down and I was interested in expediting them [contract awards]," an SCA official said in an interview. "I thought if someone had been declared to be clean six months ago that that clean bill of health ought to extend six months later." The Inspector General counters that except in unusual circumstances it conducts no additional investigation beyond the electronic due diligence checks. As such, it reviews and turns around most contracts in a day. Where new information has been made available during the months or years between a firm's initial prequalification and its bidding, either the Inspector General has this information on hand and is ready to use it, or, for the most part, easily and quickly acquires it. In any event, material circumstances affecting a firms' status easily change overnight, let alone over six months.

The George Campbell Painting Corporation Matter

Campbell Painting, founded in 1930, is a painting and general contracting firm located in the borough of Queens. At the founder's death in 1964 his son, George W. Campbell, assumed control of the firm, and today owns it jointly with his wife.

On June 7, 1995, in a memorandum to the SCA President, the Inspector General recommended that the SCA revoke Campbell Painting's prequalification status and reject it is as the apparent low bidder on an exterior modernization project. Reviewing recently-available criminal trial transcripts in which George Campbell had testified under oath, and reviewing, further, Campbell's and his attorney's explanations of that testimony to the Inspector General, the Inspector General concluded that Campbell Painting had lied on its prequalification application, and lied again in its explanations. It was apparent to the Inspector General that the firm had attempted to disguise a 30-year history of unethical business practices, including bid rigging and illegal payments to labor officials.

Campbell Painting had been debarred once before, during 1960's. The firm was then a member of a "bidder's club" that controlled the award of New York City Housing Authority painting contracts. In 1968, George Campbell was convicted in state court of bribery and conspiracy to prevent competitive bidding. As Campbell had refused to testify

[87] *Ibid.*

to a grand jury investigating the bidder's club, the Housing Authority defaulted the firm on its current contracts, and then debarred it.

Campbell downplayed his conviction to the Inspector General's investigators, saying he had "taken the rap" for his father. Yet Campbell's sworn testimony revealed that he had continued to participate in the club even after assuming control of the firm from his deceased father.

A similar bidder's club developed at the New York City Transit Authority in the late 1970s. Campbell, concerned about a second bid rigging conviction, declined to participate. The Inspector General concluded that Campbell declined not "because it is criminal and unethical to rig bids, but simply out of fear of getting caught again." During the criminal trial of painters union officials involved in this scheme, Campbell testified under a grant of immunity. In reviewing the trial transcripts, the Inspector General learned quite a bit about Campbell Painting:

> "From 1974 through 1990, Campbell routinely paid 2% kickbacks on all Suffolk County contracts to union local 1486 official Edward Capaldo. Campbell testified that he made these payments 'basically to buy labor peace.'
>
> "In 1989, Campbell paid Capaldo $10,000 to solve 'some labor problems' on a TA [Transit Authority] contract. According to Campbell, the reason he was experiencing these problems was because he had won a contract that was supposed to go to the bidders club. (Union head Jim Bishop mistakenly gave him the impression that it would be permissible to bid this contract because the "club" was not interested in it.) Frank Arnold and Capaldo initially ordered him to turn the contract down, which he refused to do because it would affect his bid bond. He told them if they could arrange to have the TA find him not responsible, he would not contest that decision. Arnold and Capaldo then countered with a demand that he kick back 10% of the contract value, but he could not afford to pay that much because of the way he had structured his bid. Campbell then implored Bishop to mediate, and Arnold and Capaldo stopped making demands upon him. However, as the contract progressed, DC9 began to raise jurisdictional issues and Campbell paid Capaldo $10,000 to solve these problems.
>
> "From 1974 through 1990, Campbell routinely made annual cash payments to various union officials, in some cases $1000 each. Campbell characterizes these payments as 'just a normal Christmas gratuity.'
>
> "From 1985 through 1990, Campbell paid District Council 9 business Agent Salvatore Savarese $500 to $1000 a year to ensure that 'friendly' or 'compliant' shop stewards were assigned to Campbell Painting.
>
> "In 1989, Campbell paid Savarese $1000 to be allowed to violate the terms of Campbell Painting's collective bargaining agreement and employ an apprentice on a job at Shea Stadium.

"In 1986, Campbell paid $1000 to another DC9 Business Agent, Ed Filancia, in order to get a difficult shop steward removed from one of his projects.

"From 1975 through 1990, Campbell Painting routinely paid its workers off the books."

Numerous questions on the prequalification application would have required full disclosure of these activities. Campbell Painting's failure to do so prompted a meeting with the Inspector General on June 5, 1995. Campbell's explanations and his attorney's further prevarications little satisfied the Inspector General. The firm and Campbell himself, it asserted, "have demonstrated a consistent pattern of illegal and unethical behavior that strongly suggests they lack the character to met our minimum standards for prequalification with respect to integrity and ethical business behavior." The prequalification application itself contained numerous misstatements which "were an attempt to distance himself [Campbell] from this unethical behavior." The Inspector General recommended that the SCA revoke Campbell's prequalification for three years.[88]

"Pending Review"

During its consideration of an application, the Intelligence Unit may discover information about a firm or principal that it considers suspicious, and that prompts it to further investigate. Its search of newsclippings data bases, for example, might reveal that a name on the prequalification application matches a name in a Chicago newspaper story identifying the individual as an organized crime associate.

If the Unit's information could disqualify or debar the applicant, the Director of Intelligence may classify the matter as "Pending Review." At that point, additional investigative efforts are made to determine the status of the information and the subject. The office may request or require meetings with the applicant to clarify the report. In some instances it may conduct physical surveillances of individuals or locations, use confidential informants to gain more intelligence, analyze telephone tolls, and review court documents, real property records, and regulatory files that are not easily accessed electronically.

Special Problems and Solutions

Uncovering An "Alter Ego"

A key aspect of prequalification was watching for companies who, because they had been debarred or were controlled by organized crime, tried to hide their true identity

[88] Memorandum, Thomas D. Thacher II to Barry E. Light, "*George Campbell Painting Corporation.*" New York City School Construction Authority, Office of the Inspector General. June 7, 1995.

and pass muster. It was easy, for example, for a company with obvious problems to go out of business and reconstitute itself as a new corporate entity, known as an "alter ego" firm. It was equally important, and often difficult, to catch them. Over time, determining who really was behind a company became one of the most important aspects of prequalification.

Construction businesses in the New York City market had reason to suspect, as the SCA initiated operations, that the "alter ego" ruse would succeed. City agencies often lacked the will or the means to uncover the hidden ownership of firms seeking. The SCA Inspector General, by contrast, was from the outset poised to deal with alter-egos, and gained early advantage from the prequalification questionnaire. But that alone was not the key to its strategy or success.[89]

> "Contractor screening requires so much more than simply pushing a computer button to get a print-out on a company. You have to do what nobody does: you have to *read the application*. And because it's not going to be complete -- the negative information won't be there -- it has to be fact-checked. Are they telling the truth? We check .... these are clever people. These people have had lawyers construct their answers.
>
> "If you really want to catch the corrupt or tainted firm, you've got to do analysis that is comprehensive. You have to scrutinize all information in the contractor questionnaire and determine the accuracy of the information given. This requires checking the contractor's answers against a databank containing information on financial histories, court cases, newspaper accounts, government reports, criminal histories, investigations, administrative actions... And it isn't all going to be electronic data bases... You may have to get up *and... go look... and call people...*
>
> "Even if you do all that you may not be able to establish conclusively what you suspect, but can't prove. Many times this analysis generates additional questions that require having the contractor come in and explain certain answers or apparent omissions. In the end, there may still be questions that no amount of investigations seems able to resolve within reasonable constrains. Then we simply ask the contractor to execute a document swearing under penalties of perjury that there is no basis for our concerns.

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[89] "The opening moves in the fraud control game consist...of the defending institution implementing transaction level filters based upon some kind of profiling; followed by the fraudsters adapting all their subsequent strategies to circumvent those controls. These moves could be regarded as a 'standard opening' in a game which, like chess, is complex, dynamic, and rich in strategy... Unfortunately, many of the institutions most vulnerable to fraud have not progressed past these standard opening moves. They enjoy a false sense of security based upon the operation of their transaction-level filters, and that sense of security is reinforced through the observation that the process-based filters reject claims from time to time...But such controls generally detect only the casual, careless and opportunistic fraud attempts; not the dedicated criminal rings who quickly progress to a higher level of sophistication." Malcolm K. Sparrow, in "Fraud Control in an Electronic Environment." Proposal submitted to the National Institute of Justice. May 27, 1993.

"In these meetings we point out to the contractor that should it lie, or seek to mislead us in that document, down the road we can get back every penny we later pay to it -- even while keeping its work -- under a theory that, by lying to us, the contractor fraudulently induced the SCA to enter into the contract. In this way, we have engineered some enormous recoveries which are tantamount to having a dishonest contractor "endow" a school project by providing what ends up being free construction services.

"Sometimes, at that point the contractor may get up from the table. 'Guys, I changed my mind, I don't want to work for the Authority,' and walk out the door. We may still debar the firm. In fact, most of our debarments are of people who have lied. We have debarred people who concealed things for which we probably wouldn't have debarred them if they had been honest in their disclosures. These aren't the kind of people we want working here. We need people we can rely on who tell the truth. This is a great place to find out who is, and who's not, of that character. A test of materiality is, 'Did he try to cover up?' indicating that he is not reliable. If that's the case, he should not get public dollars." [90]

The Marte Construction, Inc. Matter

Marte Construction is a roofing/general contracting firm incorporated in 1993, with offices at 172 Ninth Street in Brooklyn. In March, 1995, the Inspector General reviewed Marte's prequalification application and determined that it was a "successor in interest" to Iason Building Construction. The SCA had previously defaulted Iason on a roofing contract at Tottenville High School on Staten Island, making it ineligible to bid on SCA contracts until August, 1999.

Based on its investigations, the Inspector General concluded that Marte was Iason's "alter ego":

- On its prequalification application, Marte misrepresented its office address as 174 Ninth Street, Brooklyn. The Inspector General determined the true address to be *172* Ninth Street, the same office space as Iason.
- Marte's principal had been the corporate Secretary and Treasurer of Iason. In 1990 and 1992, she submitted two sworn applications to the SCA attesting to that.
- Marte's principal was the wife of the owner of Iason. The only other "key person" listed on Marte's application had been previously employed by Iason.
- Marte was incorporated just before Iason filed for bankruptcy.

When challenged to explain omissions on its application pertaining to these facts, the firm's principal either made further misstatements or failed to respond altogether. In

[90] Thomas D. Thacher II, interview (1995).

March, 1995, the Inspector General recommended Marte's disbarment for five years from the date of the SCA's default of Iason.[91]

The JAL Services Matter

JAL Services Inc. is a replacement window installation firm located at 269 Brehant Street on Staten Island. Based on its investigation, the Inspector General concluded that JAL was a successor firm to National Windows. National had previously been permanently disqualified from SCA work for submitting fraudulent prequalification documents. The falsified records sought to disguise the fact that National was controlled by Robert Carnivale, a "known associate of organized crime," who was then under federal indictment for bribery and loan sharking.

The Inspector General concluded from its interview with firm employees that Canivale controlled JAL:

- The purported owner of record, Smith [name changed], was described by JAL workers as a "druggie," rarely seen at job locations except impaired, and then only to scour construction sites for salvageable scrap metal.
- All substantive job-related issues were decided by Carnivale or his son.
- Wage rates were set by Carnivale, and on several occasions he personally handed workers their weekly paychecks.
- On various credit applications, Smith listed his place of employment as National Windows or a pizza restaurant owned by Carnivale.

When challenged by the Inspector General, Smith either made further misstatements or failed to respond altogether. The Inspector General concluded that "JAL Services Inc. is yet another attempt on the part of Robert Carnivale to circumvent the SCA's prequalification process and infiltrate our replacement window program." On June 20, 1995, it recommended permanently disbarring JAL Services from further SCA work.[92]

Standards Of Evidence

From a practical perspective, it was important for the Inspector General to protect the SCA from the inevitable legal challenges to its authority to prequalify and disbar firms on the basis of the five-point integrity standard. As the Inspector General expected that these matters would be determined at some point by the courts, it embraced a policy on

[91] Memorandum, Thomas D. Thacher II to Barry E. Light. *"Marte Construction Inc."* New York City School Construction Authority, Office of the Inspector General. March 29, 1995.
[92] Memorandum, Thomas D. Thacher II to Barry E. Light. *"JAL Services Inc.."* New York City School Construction Authority, Office of the Inspector General. June 20, 1995.

the use of evidence in its debarment recommendations that looked directly to the courtroom where the debarments would be challenged. In all cases, the Inspector General policy was to recommend a firms' debarment to the SCA only if, in the event of a court challenge, the Inspector General could produce the evidence, in open court, that provided the basis for its recommendation and sustain the SCA decision in the face of challenge.

On occasion, this turned out to be either impossible or impracticable. For example, the Inspector General might have gained access to the transcripts of wiretapped conversations involving a firm's employees and principals. The conversations incriminated them, and would have sufficed for the Inspector General to recommend debarment. Yet the Inspector General, concerned for the confidentiality of its investigations or the safety of its informants, might decide against introducing such "smoking gun" evidence in open court.

Without such evidence, however, and in the face of a legal challenge, the SCA position would be weak. Few courts would support the SCA decision to debar without it. On occasion, therefore, the Inspector General has foregone a recommendation of debarment where it could have required the office to reveal its confidential sources and means. But by observing this standard, the Inspector General has withstood several court challenges to its authority and procedures.

Where the evidence it amassed could not, ultimately, be used in open court, the Inspector General might work around the problem of exposing confidential wiretap information in evidentiary hearings by developing information from independent sources. If, nonetheless, it appeared as though the SCA might have to forego debarment, the Inspector General aggressively sought alternative means of control over suspect firms, even as it let high risk firms pass into the pool of prequalified vendors.

Certification

The Inspector General occasionally prequalified firms about whom it had serious reservations, either because it lacked sufficient or court-worthy evidence to debar a firm, or was unable to reach any certain judgment as to the risk posed by a firm.

Such instances required the Inspector General to develop a technology to control firms that passed into its vendor pool through the gray zone between outright debarment and outright prequalification. One of the Inspector General's important innovations in this area was its use of contract "certifications."

A certification is an additional, material representation which is incorporated into the construction contract. In it, the contractor agrees to abide by certain rules laid down by the Inspector General while working for the SCA. For example, the Inspector General might be concerned about a contractor's apparent but still difficult-to-prove mob connection, or its history of association with a poor performer. In the

certification, the firm would agree, as a condition of the contract, to bar certain individuals from being associated with the firm during the contract period. If the firm broke those rules during the contract period -- if the firm, for example, continued to employ the mobster it had promised to fire -- the SCA could default the firm on the contract, seek monetary recoveries, and permanently debar the firm from SCA work.

The Lefkas Matter

In 1992, the Inspector General recommended that the SCA revoke the Lefkas Contracting Corporation's prequalification status and disqualify its low bids on two pending construction contracts. For in the two years between the time the company had been prequalified and the time it bid on the contracts, the Inspector General had learned that the company had fallen under the control of Dimitrios Karidis. Karidis was a convicted criminal whom the Board of Education had debarred; the SCA had disqualified his company, Adanis Renovations.

Based on information linking Karidis and Lefkas Contracting, the Inspector General concluded in a memo that Lefkas' "business affairs are now so inexorably intertwined with ... Karidis that it should be considered an alter ego of [Adanis] and as such should be precluded from receiving SCA work until April 1995." The SCA president agreed with the Inspector General and had the company's prequalification revoked, though only for nine months, after which time the company was free to reapply.

Karidis brought suit, and the SCA settled with Lefkas Corporation. It granted the company the two school contracts for which it was the low bidder *on the condition that Karidis sever his ties with Lefkas Corp.* Such a precondition was entered into and signed by Lefkas as a matter of contract.

Using Certifications As Investigative Aids

The Inspector General also used certifications for another purpose: to trip and trap suspect firms that it believed, but could not prove, engaged in conduct that would ordinarily subject it to disqualification or debarment.

The Inspector General might believe, for example, that a firm's principal had important business dealings with another debarred contractor. It might have reasons to suspect this -- but be unable to prove it. After meeting with the firm to learn more about its business relationships, the Inspector General might require the principals to sign certifications in which they formally denied the assertions that concerned the Inspector General, and which the Inspector General believed to be, in fact, true.

Having prequalified the suspect firm on the basis of the principals' signed certifications, the Inspector General might intensify its scrutiny of the firm in

operations, hoping and expecting to catch it violating its contract. For if during the contract period the firm revealed the business relationships that, in its certifications, it had denied existed, the SCA could take immediate action to default the firm on the basis of a false filing, and debar it from future SCA work. The firm's principals would be subject to criminal charges for having filed the false instruments. Under New York State law, the SCA could both seize the work already performed, and seek to recover the sums it had already paid for it.

Certifications therefore gave the Inspector General important additional leverage over suspect firms even after they were prequalified. The certification process usually required interviews and negotiations with firm principals and counsel. These provided further opportunities for the Inspector General to observe the firm closely and to gather important background information on it.

The BQE Matter

Prior to the SCA being established, a firm known as Kappa Renovations, owned by Anthony Kappa, acquired a track record of poor performance in roofing repairs for the Board of Education. After years of work on its projects, the Board finally defaulted the firm.

In the same year as Kappa Renovations debarment, a new company -- BQE Contracting -- had emerged and won eleven contracts from the Board. At the time, BQE represented that it was owned by Rosemarie Marra. When the SCA took over the Board's building program, BQE applied for SCA prequalification. The Inspector General determined that Marra was Anthony Kappa's wife, a fact that BQE acknowledged. The Inspector General suspected more: that BQE's true ownership was obscured, that BQE was a Kappa Renovations alter ego, and that Kappa ran BQE.

At the time, the Inspector General lacked sufficient evidence to debar, and had no basis to visit the sins of the husband upon the wife without proof of true ownership. Faced with the likely requirement that it prequalify BQE, the Inspector General took special steps to protect the SCA from what it suspected was a firm that Kappa, in fact, operated and controlled.

The Inspector General summoned BQE Contracting to an interview. It informed BQE that though the firm was not obliged to prove that its ownership differed from Kappa's, the Inspector General would require BQE to certify in an affidavit that Anthony Kappa had nothing to do with BQE. The certification made clear that the firm made its declaration *as an inducement to the SCA to award BQE roofing contracts.* BQE signed

the certification, and the SCA awarded it a $5.1 million contract to repair Clara Barton High School's roof in Brooklyn. [93]

Early on in BQE's performance, problems arose, not unlike those associated with the prior work of Kappa Renovations. The Inspector General initiated an investigation that revealed that Anthony Kappa had been intimately involved in BQE's contract to repair Clara Barton High School's roof. The office brought in the Queens District Attorney and obtained a search warrant for BQE's offices. The materials seized during the search substantiated the fraud. And with the firm showing its hand in operations, the Inspector General was able to determine that Anthony Kappa was, in fact, running BQE.

> "Unless you can demonstrate that he controls or runs it, you can't debar the guy. He wasn't on the bank account. The normal indicia of his controlling it were not in place. They had done a good job of separating it... But once the job starts you can see the firm in operation, every day. Just walk up to someone and ask, who's running the job. 'Oh, its Tony Kappa.' Then having the certification in place you can do all the good things that we ultimately did." [94]

"Contrary to the representations contained in the SCA certification," Thacher said at the time, "the investigation revealed that Kappa not only played a significant role in the operations of BQE, but that he also personally received nearly $400,000 of the moneys that the firm had been paid by the SCA." [95]

Based on the certification that the Inspector General had obtained during the prequalification interview, and the facts revealed subsequently by investigative means, the SCA stopped payment on the BQE contract to repair Clara Barton High School's roof. At the time, BQE had already completed $2.2 million worth of work but had only been paid $1.2 million. The SCA argued that, having relied on BQE's false certification, BQE had fraudulently induced it into the contract with the firm. In the aftermath, Kappa pleaded guilty to labor law violations and to filing false documents with the SCA, including falsely certified payrolls. BQE agreed to forfeit the $1 million it claimed it was owed for work already performed. It paid $100,000 to the SCA as further restitution of the cost of the investigation, and $87,000 to 11 construction workers whom the Inspector General proved BQE had underpaid under New York State prevailing wage law.

The SCA seized the roof repairs, valued at $2.2 million but for which it had paid $1.2 million, without further compensation to BQE. (Thacher refers to such instances as work that disreputable contractors have "endowed" to the SCA.) Both BQE and Kappa were permanently barred from working for the SCA. And perhaps even more importantly, the Inspector General, in developing the case, had persuaded the Queens DA to prosecute what might otherwise have been viewed as too insignificant a matter for its Rackets

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[93] *New York City School Construction Authority Contractor Qualification Procedure, Certification.* Certification of BQE Contracting Corporation. February 27, 1991.
[94] Interview, David Eichenthal (1995).
[95] "Queens Firm Pleads Guilty to Defrauding the SCA". *New York Construction*, January 31, 1994

Bureau. Indeed, Queens DA Richard Brown characterized the investigation as having "been a long and difficult prosecution that has been marked by outstanding cooperation between the SCA and the Queens DA's office." Brown concluded that the case represented "the beginning of a new era...that involves the implementation of simultaneous criminal, civil and administrative sanctions against those who defraud public agencies and construction workers." [96]

Other Preconditions For Contracts

In some situations, the Inspector General might determine that the public interest required that the SCA award a contract to a low bidder who might otherwise be disqualified, or, as in the Herbert matter (below), that it continue to do business with a suspect firm that might otherwise be debarred.

The reasons might vary -- a firm might recently have changed ownership from individuals convicted of crimes to new, apparently clean owners; competition in a particular sub-industry may be so limited that the debarment of one firm would create a monopoly; or, in the case of firms with ongoing contracts, removal of the firms actively engaged in SCA construction projects would interrupt critical construction timetables.

In these circumstances, the Inspector General established certain "preconditions" for such firms to qualify for or continue in SCA work. Like certification, these measures were designed to give the Inspector General additional control over suspect firms even as the SCA awarded them the agency's business.

Independent Auditing Firms

One of the most significant such measures pioneered in use by both at OCTF and at the SCA Inspector General was the establishment of an *Independent Auditing Firm*, or IAF program. The equivalent of an ankle bracelet monitor for white-collar crimes, the IAF initiative required a suspect contractor to pay for and retain an auditing firm that the Inspector General approved to monitor the contractor's day-to-day business dealings with the SCA. The IAF would report regularly to the client -- the Inspector General -- on the suspect firm's activities. In this way, the Inspector General could monitor the contractor's conduct without actually having to commit many resources to the search for information and control.

The Herbert Matter

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[96] *Ibid*

The Herbert Construction Company is one of the largest construction contractors in New York City, and had done over $86 million in work of the SCA. In February, 1995, the New York County DA's office executed search warrants against Herbert in a bid rigging and bribery investigation. At the time, Herbert was handling two school building projects with contracts over $27 million. In order to continue working for the SCA, the Inspector General required Herbert to sign a certification that it had violated no laws. It further required Herbert to separately fund an IAF [see below] to monitor the two SCA contracts still under its control, and agreed not to bid on further SCA work.[97] Six months later, in July, 1995 the New York County DA indicted Herbert's chief executive on extortion charges stemming from a kickback scheme involving subcontractors.[98] During this period, Herbert's SCA work had continued under close monitoring, just as the investigation continued unimpeded.

The Hercules Matter

In a recent case, for example, the Inspector General entered into pioneering IAF agreements with one of the SCA's largest contractors, the Hercules Construction Corporation. In January, 1995, the Inspector General's investigators participated in the execution of a search warrants at Hercules' corporate headquarters. At the time, Hercules had been awarded over $100 million in contracts, $40 million of which remained to be completed. The SCA had grounds to terminate these contracts, but to do so would have jeopardized the SCA's ability to deliver 4,000 school seats and created the risk of extensive cost overruns and schedule delays.

To get construction of new and modernized school space done on budget and on time -- while still protecting the SCA from being victimized -- the Inspector General negotiated an IAF agreement in which Hercules agreed to undertake the following:

- Forfeit all profits on all change orders and increase retainage on contracts;

- At its own expense, fund an IAF, at a cost of up to $300,000, to be selected by the SCA. The IAF would monitor Hercules' performance on SCA contracts, ethical conduct, and compliance with federal, state, and local laws and regulations;

[97] See, *Agreement Between the New York City School Construction Authority and Herbert Construction Company, Inc., and Ted Kohl*. March 24, 1995
[98] NY *Newsday*, July 11, 1995

- Adopt a code of business ethics acceptable to the SCA (see attached), which became part of its contract.[99]

The Howell Matter

In 1990, the SCA awarded the E.W. Howell Company Inc., a firm the Inspector General had previously prequalified, a $26 million contract to construct a Manhattan school. (Howell's bid was 9 percent lower than the next lowest bidder.) The next year Howell was the low bidder on another SCA school construction project. This project, in Queens, was worth more than $32 million. (The next lowest bid was $2.5 million more than Howell's bid.)

After the contract was awarded, however, the Inspector General discovered that Howell was under criminal investigation in connection with previous public construction projects. The investigation concerned allegations of labor racketeering, illegal billing, and embezzlement. According to the Inspector General's guidelines, a company under criminal investigation is precluded from doing work for the SCA as long as the investigation is pending.

There were, however, both competing interests and mitigating circumstances in this case. Debarring Howell would have entailed awarding the Queens construction project to the next lowest bidder. However, since that bidder would likely have been disqualified as well, the award would have gone to the third lowest bidder, adding more than $2.5 million to the construction price of the school. Debarring Howell would also raise the question of whether the SCA should allow the company to continue to perform its first SCA contract.

The other factor the Inspector General had to consider was that another company, the Obayashi Corporation of Tokyo, had acquired ownership of Howell in 1989. According to Howell and Obayashi, the criminal investigation concerned activities that had occurred prior to the acquisition. The two companies maintained, moreover, that Obayashi had no knowledge of the alleged criminal conduct when it acquired Howell and that the conduct under investigation involved employees who had not been employed at Howell since at least 1989.

As a means of keeping Howell on the job at the Manhattan construction site, and not giving the Queens contract to a company that had submitted a higher bid, the Inspector General fashioned a compromise. According to an agreement worked out between the Inspector General and Howell, the company would hire, at its own expense, an investigative auditing firm. The primary purpose of the auditing firm was to protect the SCA from criminal activity on Howell's part. But the auditing firm's responsibilities were

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[99] *Discussion Notes, Meeting of the Board of Trustees, March 2, 1995* Office of the Inspector General. Also, *Agreement Between The New York City School Construction Authority And Hercules Construction Corporation*. February 13, 1995.

considerably more extensive. The auditing firm was also to reform Howell's own internal operating procedures in a way that would reduce opportunities within the company for corruption.

There would be little chance that any independent auditing firm could reform a company that was not receptive to change. But the auditing firm Howell hired (with the Inspector General's approval) concluded at the outset that Howell's Japanese owner was willing to adopt, for its own protection, an effective anti-corruption program for Howell. Without such an openness to the possibility of rehabilitation, the head of the auditing firm did not believe he would have been able to work within the culture of the organization to develop internal protections against corruption.

The auditing firm's mission was to examine all of the company's internal procedures. Among these was the company's procedure for hiring and supervising subcontractors. The auditing firm sought to assure that Howell's procedures protected the company from subcontractors. They might try to bribe Howell buyers to secure favorable treatment, including contracts, or to authorize payments to subcontractors for work only partly performed.

The task of the auditing firm was to examine the possible ways in which a subcontractor could defraud Howell, as well as all the other ways the company might be susceptible to corruption, and to write a set of internal controls that would be likely to discourage such schemes. Typically these controls attempted to change the company's operations in such a way that a large number of people within the firm would have to conspire if a fraudulent scheme were to succeed. The auditing firm also tried to devise procedures that had an independent management purpose, other than preventing corruption. Thus, if a manager was required to review a subcontractor requisition and the purpose of this review was solely to prevent the company from being defrauded by the subcontractor, the manager would not be likely to give the requisition a thorough review. If, however, the manager had to review the same requisition for budgetary purposes, he or she would be more likely to exercise caution in granting approval.

Howell adopted the auditing firm's reforms, as their agreement with the SCA required, but also took pride in them, according to the auditor. Howell's management, including those who had been hostile to the auditing firm's presence, began to think of these new procedures as making good business sense and as protecting the company from corruption. Indeed, in trying to win other building contracts, Howell would use the reforms of the auditing firm as a selling point for the company. This was an indication, to the auditor, that Howell's organizational culture was internalizing the new procedures that had been devised to protect Howell from corruption.

When a public contracting agency such as the SCA learns that one of its contractors is under investigation, having a range of feasible options makes it easier to strike a balance between competing interests -- the need to assure that critical work is performed in a timely manner, the requirement to protect taxpayer dollars, and the

desire to avoid enriching individuals or entities which may have engaged (or may continue to engage) in criminal conduct. The Inspector General's IAF agreements, like in Hercules and Howell, appeared to allow the contractors to complete ongoing projects -- sparing the expense and delay related to replacement of a contractor -- while creating additional protections against ongoing fraud.

Internal SCA Views of Prequalification

The Inspector General's most important tool for protecting the SCA from corruption -- a rigorous prequalification process -- had to overcome substantial SCA opposition. SCA's senior operating officers saw the prequalification process as a "monster," according to a former senior SCA officer who, in supporting the Inspector General, encountered opposition from the Authority's Operations Unit, its Contract Administration Office, and the Office of Counsel.

SCA officers opposed prequalification because they believed it would disrupt and distract from their primary mission -- building quality schools quickly and at a good price. The specifics of their complaints against prequalification depended, however, on their areas of expertise. To those who offered legal counsel, denying a company the ability to bid on SCA contracts seemed like an invitation to companies to sue the Authority, which they would rather have avoided by permitting only a cursory review of potential bidders. From the point of view of operations, prequalification threatened to eliminate some of the best contractors in the city, who, despite their links to organized crime, could be counted on to do quality work in a timely fashion. Others believed that prequalification would create an albatross of burdensome financial investigations, paperwork, and regulations. To the SCA's accountants, the prospect of checking bank records, tax payments, disclosures of net worth, assets listed in a spouse's name, and other financial records represented a nightmarish avalanche of fact checking. And others believed that a thorough prequalification review, with its potential to expose ties to organized crime and other incriminating information, would discourage large segments of the construction industry from bidding on school construction contracts.

Some SCA officials maintained the same attitude toward the Authority's mission -- and, by extension, the Inspector General's mission -- as did those City agency officials who were traditionally reluctant to bar a company from receiving a contract. "People [at the SCA] just felt that we are supposed to be building schools for kids, and [not] running an FBI operation," a former senior Authority official stated. By this standard, the prequalification requirement that potential bidders provide the Authority with a list of three projects it completed in the last year, including each project's initial estimated cost and its final cost -- a question intended to determine if the company had consistently and significantly overrun its bid price -- was inappropriate: companies routinely padded the cost of construction and it was not the SCA's business to weed out that practice.

As the prequalification process has evolved and become institutionalized, it has come to be received at SCA headquarters with what might be called "a grudging acceptance." Prequalification, in other words, is no longer generally viewed as detrimental to the Authority's mission. "I don't see that there's anything wrong with prequalification," one senior officer stated when asked how the process contributes to the SCA's goals.

The reason, apparently, that prequalification has received some degree of acceptance is that the process has not lived up to the worst fears of those who opposed it. In their opinion, it has not discouraged a significant number of companies, if any, from bidding on SCA contracts, though the poor local economy at the outset of the decade undoubtedly made a decision to pass up the SCA's business more difficult. Many SCA officials also contend that prequalification, in general, has not slowed the process of building and renovating schools. Only the Inspector General's second integrity check, made after the low bidder has been selected, is viewed as slowing the process of awarding contracts, though even in this case the Inspector General has not added an appreciable delay. Moreover, the Inspector General has been responsive to requests to expedite this process in particular cases, according to these observers. "In the final analysis they did...prequalify, they did approve the contracts, they did all of that stuff in enough time to make the contract awards," says an SCA official who has also been critical of some aspects of the Inspector General's operation.

Investigations

> *"When I went to Frucher and Steisel I told them: 'I need wiretapping; search warrants; informants, which means the power to give someone immunity; and grand juries' Steisel looked at me like I was insane: 'I'm not going back to the legislature to get you those powers!' I said: 'You don't have to. We'll get them to join us.' Having previously run investigations and prosecutions in the construction industry, I knew how much the SCA had to offer law enforcement..."* [100]

To advance the SCA's mission to build clean and to build to competitive standards of price and performance required that the Inspector General establish good working relations with the region's law enforcement agencies. For though the SCA, through the efforts of the Inspector General, might have some wherewithal to guard itself against corrupt employees and racketeer-influenced firms; and some ability to root out cheaters, punish them, and confer a new competitive advantage to high performance firms; without the benefit of law enforcement's *powers* by its side, the Inspector General's efforts would be listless. It could neither fully investigate firms, nor easily detect ongoing schemes, nor credibly deter crime and corruption with the threat of discovery and sanctions.

Nor could the SCA, without good law enforcement *relations*, gain access to law enforcement's assistance, or have a prayer that, in using its powers at the SCA's behest, law enforcement would care nearly as much about putting up school buildings as taking down corrupt builders. Thacher observed:

> "On the one hand, endemic and systemic corruption and racketeering could only be effectively controlled by institutional reforms -- initiatives which are totally outside of the power of law enforcement agencies, and which only an insider -- an industry or operational agency -- can achieve. On the other hand, only law enforcement, through the use of wiretaps, informants, the conferring of immunity, and grand juries, has the detailed knowledge of how a particular industry or public agency has been victimized, and of where institutional reforms are necessary." [101]

Good relations with law enforcement were therefore essential for the SCA, through the offices of the Inspector General, to develop.

Aid in prequalification and procedural reform. The SCA was responsible for prequalifying its vendors and for finding and reforming weaknesses in its procedures. But the difficult task of determining true corporate ownership, which was especially important for a public builder like the SCA, would be vastly enhanced by law enforcement's information and sources. This included access to archival data from deep within investigators' files and personal memories, and enhanced real time information concerning

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[100] Thomas D. Thacher II, interview (1992).
[101] Thomas D. Thacher II, personal communication.

the individuals and firms that were bidding on SCA contracts. Access to both would enhance the SCA's grasp of true corporate ownership and past conduct.

Aid in uncovering ongoing schemes. The SCA, through the Inspector General, was responsible for uncovering criminal schemes that employees and firms launched against it. Good relationships with law enforcement would help open law enforcement's doors to the Inspector General, and perhaps make it privy to investigative means and findings. While this would help the Inspector General to prequalify firms, it would also help it find and close SCA loopholes that had left the Authority open to criminal attack.

The task of uncovering criminal schemes by SCA employees and vendors -- in its scale, in scope, in complexity -- was almost preposterous to consider unaided by the enhanced powers and skills that law enforcement agencies uniquely possessed. Without them, the Inspector General simply lacked the means and control over investigations necessary to achieve success for the SCA.

To foster good relations, and gain access to law enforcement's investigative means and findings, the Inspector General could promise law enforcement unique access to the SCA's own operations and data. This would make law enforcement's investigative task easier, and its rewards more enticing. It would also permit the Inspector General to guide law enforcement into position to interdict crimes early on and to minimize their impact on SCA operations. This would advantage the SCA's goal to prevent crime from doing devastating damage to building programs and, ultimately, to the SCA's credibility.

Aid in creating an umbrella of deterrence. The SCA strategy relied on making good the threat of detection, and the promise of punishment for criminal employees and contractors caught in the act. Good relationships with law enforcement would enhance the aura of deterrence and retribution necessary to provide the SCA with this protective shield.

The incapacitation of wrongdoers was essential to the SCA's near term goal of protecting the schools building program from crime and corruption. But by directing law enforcement's attention to dirty contractors who were operating in the markets more broadly, the SCA might reap much broader marketplace dividends. Legitimate, high-performance firms might be encouraged to sell goods and services under the SCA's "umbrella of deterrence," and begin to return to the SCA vendor pool and to the public construction markets more broadly. Under the "umbrella," the SCA could use its market power to reward price and performance, punish cheaters, and level the playing field for honest firms. This was one of the principal goals of the Inspector General strategy.

Aid in attacking organized crime. Lastly, close relationships with the region's investigators and prosecutors could help the Inspector General achieve its objective to attack organized crime. The Inspector General would accomplish this indirectly if the SCA, working with law enforcement, used its market muscle to reform aspects of the public construction marketplace, and denied organized crime a lucrative source of money

and power. The Inspector General could also directly aide investigators and prosecutors by helping them to target illegal firms for investigation and prosecution, and by actually helping them carry out investigations.

For all these reasons, then, establishing and maintaining good working relationships with the region's state and Federal law enforcement agencies was key to the SCA's strategy, and to the Inspector General's success at SCA. Accomplishing this, however, was no trivial task.

Building Close Working Relationships

Public builders and law enforcement agencies ordinarily have little in common other than the signature some may share on their paychecks. Except when building a prison or police station, they have few opportunities to work together, other than during the quasi-adversarial circumstances of an investigation. In neither event is cooperation or shared interest the cornerstone of their relationship. Thacher summed up the barriers that existed between builders, investigators and prosecutors:

> "Law enforcement agencies -- such as the U.S. Attorney or Federal Bureau of Investigation -- and public contracting agencies -- like the Housing Authority or School Construction Authority -- are all, in theory, members of the same government. Yet, there are tremendous obstacles to the type of communication necessary to break corruption and racketeering by bridging the knowledge and power of law enforcement with the public operating agencies' power to reform.
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> "For law enforcement, it is often unclear whether a public agency and its executives are the victims or perpetrators or facilitators of whatever fraud may be under investigation.... Investigators and prosecutors are unwilling to assist or seek the assistance of agency officials who may in the future become investigative targets. Even where an agency's officials may not be targets of the investigation, law enforcement officials often fear that by tipping off officials to the existence of an ongoing investigation, leaks from these officials may find their way to the targets, thus less directly compromise an ongoing investigation. Finally, by communicating with agency officials, law enforcement officials fear that agency officials might raise concerns or issues of great import to the agency -- but of little or no interest to law enforcement -- that would only complicate an investigation.
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> "For officials of a public agency, an investigation is often the beginning of an organizational nightmare. Law enforcement demands for information are often extensive and require labor-intensive efforts to be met. When key employees or contractors are the targets of the investigation, the investigation can place these individuals or entities into a limbo that curtails the agency's overall effectiveness. Agency officials may also not want to know certain information which they either cannot act on -- because of an ongoing

investigation – or would have to act on – and would cause significant disruptions. All of this is heightened by the normal tendency of a bureaucracy to want to hide its vulnerabilities and problems from outside scrutiny." [102]

Despite these difficulties, the Inspector General was able to create close working relationships and harvest some of their potential yield. The Office of the Inspector General recruited staff with vast prior networks in law enforcement; vigorously maintained these relationships and developed new ones; articulated and embraced a shared vision of the importance of the SCA mission, the Inspector General strategy, and the law enforcement opportunity; and effectively worked the "two-way street" of reciprocity of access and horse trading in information.

Personal Relationships

As Inspector General, Thomas D. Thacher II enjoyed a significant and unique advantage in seeking close ties with the region's law enforcement agencies. Having been an Assistant District Attorney in Manhattan before joining OCTF, and then head of the joint New York County DA/OCTF Construction Industry Strike Force, Thacher was well-known to the region's law enforcement leadership. Upon his appointment to the Inspector General's position, he was able to recruit staff from among this network.

Many of the Inspector General's senior staff were former investigators, analysts or prosecutors with agencies with whom the Inspector General expected to partner. Joseph DeLuca, for example, the Assistant Inspector General for Policy and Analysis, had been OCTF's chief analyst on the Construction Industry Project. The Inspector General's current counsel, Peter B. Pope, was previously deputy chief of the New York County DA's Labor Racketeering Unit, and also clerked for federal Judge Robert Sweet, a past United States Attorney for the Southern District of New York. Pope's predecessor and the Inspector General's first Counsel, Kevin Ford, had been Inspector General for the New York City Department of Environmental Conservation, and a Special Assistant United States Attorney in the Southern District of New York. (In 1994, Mayor Rudolph Guiliani appointed Ford Deputy Commissioner of the Department of Investigation, another partner of the Inspector General's office.) The Assistant Inspector General for Investigations, Edmund Baccaglini, was a former New York Police Department Deputy Inspector who had served as commanding officer of the New York County District Attorney's squad under DA Robert M. Morganthau, and of the Bronx DA's Squad under DA Burton Roberts and DA Mario Merola. (Prior to joining the Inspector General's office, Baccaglini directed investigations for Pinkerton's under Robert Maguire, also a past Assistant United States Attorney for the Southern District of New York, then New York Police Commissioner, and now a managing director of Kroll Associates, an investigative firm in New York.) The

[102] *Ibid.*

Inspector General's Director of Field Investigations, John Loughran, had 28 years on the New York Police Department and was a past head of the NYPD/FBI joint terrorism task force. Nicholas Nagourny, the Inspector General's director of management information systems, had worked at the FBI's New York operations center.

With its wealth of experience and professional contacts, the Inspector General's investigative team acquired the look and feel of an important new law enforcement agency. Two sets of relationships became especially important in its efforts to build bridges to the region's investigators and prosecutors.

Thacher And The Office Of The New York County District Attorney

During the period 1976-80, Thacher and Michael Cherkasky, then both young Assistant District Attorneys in New York County (Manhattan), developed a relationship that provided the later foundation for cooperation between the Inspector General's office and the District Attorney's.

Though Thacher left the Morganthau office in 1980 for a brief stint in the private sector, he and Cherkasky again crossed paths when, on Thacher's return to law enforcement in the late 1980's, OCTF Director Ron Goldstock appointed him head of OCTF's Construction Industry Project. Cherkasky, too, had risen in the New York County DA's office, becoming its Chief of Investigations, including supervision of its Rackets Bureau. (Goldstock and Cherkasky are colleagues today at Kroll Associates in New York City.) In 1988, anticipating the release of OCTF's report on racketeering in construction, Governor Mario Cuomo allocated OCTF and the New York County District Attorney each $2 million to seed a joint Construction Industry Strike Force (CISF). Cherkasky, Goldstock, and Thacher organized it, and Thacher was designated to direct it.

In Manhattan, DA Morganthau used his funds, in addition, to establish a labor racketeering unit. He appointed Robert Mass head of that new unit, reporting to Cherkasky. Mass, who had previously been detailed to Goldstock's office in White Plains on a construction case, also became Deputy Director of CISF under Thacher.

By late 1989, when Thacher left OCTF and the CISF to organize the SCA's Office of the Inspector General, he had already had discussions with his colleagues about how they might continue to work cooperatively. All supported the mission of the new Inspector General and agreed that the district attorneys' law enforcement powers would provide a powerful lever for the new office.

Kevin Ford And The Southern District Of New York

A second, and perhaps as important a set of relationships were those established by the first Counsel at the Inspector General's office, Kevin Ford.

Prior to coming to the SCA Inspector General's office, Ford had been Inspector General at New York City's Department of Environmental Conservation (DEC). Although DEC was a major city construction agency, the Inspector General's office was a regulatory backwater. With few law enforcement powers of its own, it was principally concerned with employee misconduct. However, during the 1980's, Ford became involved in an extraordinary case in the jurisdiction of the United States Attorney for the Southern District of New York (SDNY). The matter involved organized crime infiltration of the waste disposal industry, and specifically the illicit use and control of the City-owned Fresh Kills landfill on Staten Island. In that matter, Ford developed a reputation and a working relationship with Federal prosecutors and investigators that proved valuable, later, at the SCA.[103]

At the time of the Fresh Kills investigation, the United States Attorney for the Southern District of New York was future-New York City mayor Rudolph Guiliani. To work more closely with Ford, the SDNY cross-designated him as a Special Assistant United States Attorney. This involved Ford in confidential law enforcement information, including electronic surveillance and grand jury matters, and broadened the relationship. (Cross-designation was an established practice in the law enforcement community of New York, which one agency might use to confer its powers and authorities, in a limited capacity, upon a member of another.) So authorized, Ford worked closely with David Lawrence, Chief of the SDNY's Public Corruption Unit, and the Federal Bureau of Investigation, among others, on the Fresh Kills case. The prosecutions that resulted counted as among the most significant and earliest environmental crimes cases to be prosecuted in the nation.

Ford's favorable relationship with senior investigators and prosecutors from the Southern District, which is arguably the single most visible and powerful law enforcement office in the United States, proved extremely helpful to the SCA Inspector General in its earliest days. Ford brought with him the goodwill of that office at its highest levels. Perhaps more importantly, Ford quickly attracted a number of active Southern District cases to the Inspector General to help investigate and prosecute. Two cases in particular -

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[103] "Under halogen lamps that lit the site like a stadium in the middle of the night, trucks from 50 different hauling companies would queue up and dump beside pits dug 35 feet into the red clay. After each truck emptied its load, earth movers would push the trash into a pit. And every morning, when the night's dumping was done, a layer of dirt would be shoved on top, making the operation look, in daylight hours, as if it was a land-grading operation using clean fill... The day after the raid, investigators returned to National Carting in Bensonhurst, Brooklyn. Parked outside was a truck marked 'Rosendale Haulage.' Federal agents were drawn to it for a gruesome reason: blood was running out of the back and down the read mud mats. Investigators peered inside and found it packed with infectious medical waste." Alison Carper, "Wasting a Neighborhood," New York *Newsday*, June 13, 1990.

- referred to below as *Operation Tightrope*, and the *Sandaq* matter -- propelled the Office of the SCA Inspector General onto the law enforcement map with significant, early wins. Each drew attention to the office, gained it credibility, and attracted more cases still.

Working The "Two-Way Street"

Thacher's, Ford's and other's long-standing relationships had created a valuable cache of initial good will between the Inspector General's office and the region's investigators and prosecutors, and favorably disposed them towards the Inspector General's mission. But no law enforcement agency was under any special obligation to assist the Inspector General. At the end of the day, the SCA Inspector General would have to compete for law enforcement's attention, at the very least with other public builders such as the Metropolitan Transportation Authority or the Port Authority of New York and New Jersey. There was plenty of criminal conduct going on in construction matters there, though much of it was opaque to investigators, and difficult to prosecute.

The Inspector General could not risk law enforcement's indifference. To capture its attention required that the Inspector General help prosecutors target major organized crime figures and enterprises for investigation and trial. As attacking organized crime directly was one of the Inspector General's primary objectives, helping law enforcement to achieve its goals would advance the SCA's, too, and help create an "umbrella of deterrence" in the marketplace.

> "We recognized that if we were to succeed in putting in place a program that would effectively protect the SCA, it would have to forge a partnership between the SCA, as an operational agency, and law enforcement, that overcame all of these substantial barriers to communication. It couldn't be done unless it was clear that it was in the self interest of both parties to the partnership to communicate with each other. The Office of the Inspector General would have to demonstrate that the partnership would not impede either parties' ability to attain their goals -- efficient and effective operations on the one hand and strong criminal investigations on the other -- and instead would advance them." [104]

The Inspector General pursued numerous joint investigations of corrupt employees and contractors. Mindful of the two-way street, also, the office occasionally helped investigative prosecutors make cases in matters that had less direct benefit to the SCA. In either event, to someone of Thacher's standing and experience in the business, it was obvious that the Inspector General had considerable assets which it could use to induce law enforcement to attend to SCA priorities.

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[104] Thomas D. Thacher II, interview (1992).

Criminal Investigations

Investigators who worked on SCA cases could gain easy access to records of firms and individuals that would ordinarily be unavailable except from the target or the SCA generally, and then only by subpoena or search warrant. The Inspector General's prequalification and intelligence data bases, for example, contained SCA prequalification applications, bidding materials, memoranda-in-support of bids and other information-rich documents. The data files included names of firm principals, prior work, addresses, telephone numbers, bonding information, and bank accounts, all of it laid out in a single document and located in a single place, in electronic form. This was an investigative treasure trove which competent investigators, eager for every shred of relevant information on their subject and targets, could exploit.

Stored in electronic form, it was easy to query and find data on informants, witnesses, and potential targets. Moreover, by working through the Inspector General's office, and using its legitimate access to SCA books and records as cover, investigators could pursue their research *without exposing the fact of their interest or investigation.* This was a considerable advantage to investigators, as it saved them time and reduced their risk.

The ease of access to vital data substantially lowered the cost of investigators' case making on cases that mattered to the SCA. It made every hour of time that an investigator spent working SCA cases, in this respect, significantly more valuable, all things equal, than an hour spent working other agencies' cases where she might struggle for confidential access to critical data. Not only could investigators slog through SCA files and records without all the worries of compromising an investigation, the channel was open, and high quality data could flow at the push of a button.

Undercover Operations

At every stage of case development, the Inspector General could reduce the burdens that law enforcement agents ordinarily encountered in making cases. The difference between the IG-assisted approach and law enforcement's customary efforts could be significant.

Early on in complex conspiracy cases, for example, law enforcement's principal focus is to find the "probable cause" that the court will require to authorize full-blown electronic surveillance -- wiretaps, eavesdropping, and the like. To establish probable cause, investigators and prosecutors often must rely on hard-to-find-and-control confidential informants.

IG-assisted investigations might have more ready access to confidential informants who could facilitate the arduous process of securing probable cause. With its own informant network, for example, the Inspector General has, on occasion, quickly advanced the pace of preliminary investigations. "Agencies come to us asking, 'Do you have a firm that meets such-and-such a profile: interacts with the Port Authority, has prevailing wage problems, etc.?' We've been able to go into our group of informants and produce somebody who has been able provide historical information to other law enforcement agencies, and also then go out for them proactively."[105]

Where no informants have existed, the Inspector General has also helped develop new ones. For example, the Inspector General might use its leverage over firms that face the threat of debarment to generate new informants from within the firm. It is not difficult to extract agreements to cooperate from firms under such a dire threat. And the Inspector General's staff has frequently helped to identify "players" in criminal conspiracies, during surveillances or on tape and video. Its experts have helped clarify the meaning of obscure events and transactions where investigators might otherwise be baffled by the nuances of construction fraud.

With its good knowledge of SCA procedures and access to SCA field operations, the Inspector General has also helped law enforcement target its undercover operations more valuably. In some investigations, Inspector General staff knew in great detail the practices, procedures and contractual relationships that governed SCA operations that were at the investigation's core. It provided detailed information on the schedule and machinery of upcoming bids, for example, or pointed fingers at suspect employees and firms, or manipulated procedures to advantage investigative efforts.

With its knowledge and position, the Inspector General has, on occasion, gracefully inserted undercover officers into suspect areas. And on several occasions, the Inspector Generals staff, during the course of its meetings with suspect firms, has "tickled" bugs -- entered into secretly recorded conversations with investigative targets after which the targets, as a result, inculpated themselves on tape.

In one recent case involving the New York County District Attorney, for example, the DA requested that the Inspector General conduct its prequalification interview with the firm's principals at the firm's headquarters rather than the Inspector General's office. The DA's investigators accompanied the Inspector General's Intelligence staff to the meeting. This offered the investigators the opportunity to see the inside of the firm's headquarters --- providing crucial information, used later, to properly place bugs to monitor conversations, and to identify the location of materials as it executed search warrants.

Later, having received its eavesdropping authority, the DA's office arranged with the Inspector General to meet with the targets in the firm's office. In that meeting,

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[105] David Eichenthal, interview (1995)

investigators asked a series of carefully selected questions intended to "tickle the bug." They were successful, for when the meeting ended and the investigators had gone, the targets discussed among themselves what they had said and, on tape, the lies they had told to the investigators.

Investigations Proceed Without Damaging SCA Interests

Law enforcement agencies may face criticism that they allow investigations to continue, and criminal activity -- including looting of the public treasury -- to go unchecked solely to advance their investigative interests. They lose sight of the collateral damage that the criminal activity they are investigating is doing to other public interests.

The Inspector General, however, was able to take steps to protect the SCA even while facilitating the expansion of ongoing investigations.

In the *Monopoly* matter, below, for example, the Inspector General became aware of a bid rigging scheme involving corrupt SCA officials and contractors. The information was developed as a result of discussions with a confidential informant, and later confirmed by other investigative means, including electronic surveillance.

Prosecutors would no doubt have felt justified letting the bid-rigging scheme run its course so as to flush out all the wrongdoers, no matter what the cost to the SCA. The SCA, however, would surely have wanted to close down the bid rigging scheme immediately to avoid any further damage to its program or credibility, whether all the wrongdoers were found or not.

The Inspector General was able to chart a middle ground. The bid rigging, it found, was made possible because of a basic flaw in the bid opening process that was being conducted by two SCA officials, one corrupt and the other inept.

The first official, who was corrupt, opened and read out loud bid numbers that contractors had submitted in writing. His favored contractor had submitted a bid that might be lowest by half; so as to minimize that contractor's actual loss when he was awarded the contract, the corrupt official would read out loud his co-conspirator's bid figure, raising it to an amount just under the next -- and legitimately lowest -- bid. The difference between the corrupt contractor's *submitted* bid and the bid as *announced* by the corrupt official could be hundreds of thousands of dollars.

The second official, who did not independently review the written submission, simply entered the number that the corrupt official had read out loud. There was thus no check on the corrupt official, and nothing to prevent him from reading out loud

numbers different from what was actually contained in the bid documents, which he would later change to reflect the number he had made up.

In this matter, the dilemma that confronted the investigative team was typical for cases involving conspiracies: whether to end the investigation outright to prevent further damage, in this case the hemorrhaging of public dollars, or to let it continue in the same damaging mode so as to discover the full extent of the conspiracy. The Inspector General did both. It purported to undertake a "systems audit" of the bidding process which "exposed" the deficiency in the bid opening procedure. (This camouflaged the real means by which the Inspector General had learned of the scheme). The Inspector General then insisted that the SCA immediately reform the process and add a third person to the bid-opening. A visible video camera was also installed in the bid -opening area.

As a result, the corrupt conduct ended, even while the investigation continued, proving quite fruitful as the wrongdoers discussed, on tape, the impact of the procedural change on their schemes. In this way the Inspector General balanced both the interests of the SCA, and of law enforcement, and helped both to achieve satisfactory results.

New Access To Old, Unreachable Targets

For many reasons discussed above, investigators and prosecutors have often found it difficult to make strong cases against even significant targets in the construction industry. Working with the Inspector General, however, provided fresh opportunities, improved leverage, new investigative strategy, and favorable angles of attack. The results could be dramatic:

> "[The *Monopoly*] case has a significance that goes far beyond the arrest and prosecution of several corrupt public officials and contractors...[I]t eliminates several notorious school contractors, notably Gatzonis, Batex (and its related affiliates) and GTS, from bidding on any further school construction work. These three contractors have a long history of doing substandard work for the Board of Education, as contractors and subcontractors. They have been the targets of a number of criminal and administrative investigations over the last decade but, until now, have always emerged unscathed if not untarnished...
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> "[I]n fact, the federal prosecutor was visibly surprised when, in our initial meeting and *prior* to the moment when he first identified the source of his information, he learned that we had brought along an extensive file concerning the same targets, based upon our monitoring of bid trends and other intelligence. Sooner or later, these defendants were going down." [106]

[106] Kevin J. Ford, memorandum to Thomas D. Thacher II, *Operation Monopoly: United States v. John Dransfied, et. al. (93-M.-0744, EDNY)*. New York City School Construction Authority. April 9, 1993

Operation Monopoly

In 1992, in the course of investigating a matter involving tax fraud and money laundering, the target contractor informed Internal Revenue Service investigators and Federal prosecutors in the Eastern District of New York that he had heard of a bid rigging scheme in place at a new public agency called the SCA. The investigators contacted former IRS investigators on the Inspector General's staff. The Inspector General was able to determine that the contractor probably had access to the matters he claimed to know of, and judged him to be credible and probably useful in an undercover operation.

Based on the review, an undercover operation was undertaken. Investigators wired the contractor and directed him to engage in conversations with other contractors whom the Inspector General identified as possible participants in the scheme. Eventually, the informant had a conversation with an SCA employee that established that there was, in fact, a conspiracy at play among several SCA employees and contractors to rig the award of SCA contracts, to manipulate contract payments and change orders, and to provide confidential SCA information to contractors seeking to secure SCA business. Subsequently, it was determined that at least eight SCA contract awards had been rigged between February and October of 1992, totaling $7.1 million.[107]

The scheme, it turned out, was made possible by two corrupt SCA employees, one of whom manipulated bids as they were submitted. Their goal was to generate $2 million in bribes within the year, and then to retire.

One of the ways the bids were rigged was called the "delta derby." In this scheme, the corrupt SCA employee would take the bid of a favored contractor, which had been dramatically and purposefully lowered to insure that it was the lowest of all submitted bids, and as the bids were opened and announced out loud, verbally inflate it to an amount just below that of the next lowest bidder. This gave the bid to the favored contractor, as planned, but now on terms much more favorable to the contractor than its original bid required.

The winning contractor and its corrupt SCA conspirators then split the "delta," or difference, between the firm's original bid, which had been lowered "off the page" in order to win, but which the corrupt SCA employee had then raised to an amount just under the true and next-lowest bid. During this scheme, the contractors paid more than $140,000 in bribes to inflate bids in this manner.

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[107] *Ibid.*

"In February of 1992, only three bids were submitted for a particular contract award. The bids were arranged so that a particular bid would be opened last. The first two bids were in excess of $640,000 but the last bid was only $341,000. The contract specialist inflated that bid and announced it as $631,000. Shortly thereafter, a representative of the contractor came in carrying a brown envelop containing a new bid sheet (page 5 of the bid package) showing a bid of $631,000 plus a new bid bond sheet reflecting the higher bid amount. In return the contract specialist gave him an envelop containing the original page 5 bid sheet and bid bond.

"After the bid opening, the contract specialist met on several occasions with the firm's representative...They discussed how much he was owed for rigging the award. The president protested that 50% of the delta, or $290,000 (the difference between the original bid of $341,000 and the awarded amount of $631,000) was too much to pay. He told the contract specialist that the 'usual' bribe or kickback was only 2-3% of a contract, not 50%. Finally, they agreed on the sum of $30,000 for this particular bribe."

Early on in the investigation, prosecutors faced a characteristic dilemma -- whether to arrest the SCA employees so as to avert the loss of untold millions of dollars diverted through the ongoing scheme. To do so might, however, leave other members of the conspiracy in place and prosecutors not knowing its full scope.

The Inspector General was able to strike a middle ground balancing both the SCA's interest to stop the hemorrhaging of moneys, and investigators' interests to let the investigation proceed to its fullest conclusion. As SCA vice president the Inspector General invoked its internal authority to conduct an audit of bid room procedures and, among other measures, recommend that two separate individuals open and read bids submitted. This effectively eliminated the "delta derby's" window of opportunity and ended the practice. Still, the investigation continued. The last rigged bid was in October 1992. The investigation continued until April 1993, giving prosecutors crucial time to locate and secure target's assets, without the continued loss of dollars to the SCA.

"...[P]rior to putting this criminal conspiracy out of commission, the Office of the Inspector General carefully monitored the activities of the two SCA employees until we sere satisfied that we had identified all or nearly of their co-conspirators and developed sufficient evidence to convict them. During this covert stage of our investigation, the defendants demonstrated considerable boldness, some might even say recklessness, in carrying forward their ambitious plans.

"In this period, corrupt conversations were conducted between the two SCA employees, and with over a dozen contractors and other SCA employees, in their offices at the SCA, over their office telephones in the hallways, the men's rooms, the cafeteria and on the streets surrounding the SCA. Envelopes

contained altered bid documents and cash were exchanged openly at the SCA or in diners and restaurants near the SCA...

"They seemed to have no fear that they would be detected and carried out their schemes in a shockingly brazen manner. In one sense, their lack of concern was well-founded. Despite the fact that they carried on their schemes for almost a year, no one at the SCA called the Office of the Inspector General to report any suspicions... On the contrary, several SCA employees passed along warnings and cautions about the Office of the Inspector General and one employee even went to the length of jotting down the license numbers of vehicles he suspected of being connected to the Inspector General." [108]

Because of the Inspector General's involvement, the investigation was probably able to go further and deeper into the conspiracy than might otherwise have been possible. During the course of the investigation, a corrupt SCA employee was found out and "flipped," going to work for the government against the targets. As a result, federal investigators had the extraordinary opportunity of having the Inspector General, as a vice president of the SCA, targeting and directing an SCA employee in the development of criminal cases for the external law enforcement agencies.

The investigation concluded with the arrest of 11 contractors, three SCA employees, and with charges against seven firms. The SCA was able to withhold $2.5 million in payments to the defendants. Several million dollars were recovered, and the offending companies debarred. The federal government forfeited over $1 million dollars from defendant bank accounts and companies identified by the Inspector General's Intelligence Unit.

Working Out the Mechanics of Cooperation

The strong, continuing relationships between the Inspector General and the region's law enforcement agencies created a favorable context for the achievement of distinct and shared operational objectives. To realize the potential of these relationships, however, the Inspector General and the local law enforcement community had to work out the mechanics of how they would operate. On a case-by-case basis, the Inspector General sought ways to:

- Gain access to investigative authorities and tools it could not otherwise tap;
- Leverage additional resources far greater than its own;

[108] *Ibid.*

- Acquire information about criminal investigations and prosecutions (both past and ongoing) concerning firms and individuals who were active in the public construction markets of New York City; and

- Credibly threaten with detection and punishment those SCA employees and contractors who were involved in crime, corruption, or racketeering.

Borrowing Law Enforcement Tools and Authority

The Inspector General was not a law enforcement agency. Its agents lacked the authority to effect arrests; conduct searches and seizures; share in the workload or workproduct of electronic surveillances; or confer immunity and develop informants.

Nonetheless, the Inspector General staffs acquired many such powers for its staff by two means: *cross-designation*, and the use of investigative staffs *under contract to the Inspector General*.

First, the Inspector General's investigators acquired limited law enforcement powers on a case-by-case basis through a process known as *cross-designation*. Cross-designation was an established means by which one law enforcement agency deputized another's agents and conferred upon them the powers and authorities they required to operate in the host jurisdiction. Typically, for example, Federal prosecutors might cross-designate state prosecutors into their jurisdictions when working on a case that originally developed under state law but which, for a variety of procedural and substantive reasons, Federal prosecutors "adopted" into the Federal district.

The Inspector General acquired cross-designated powers for its agents in several jurisdictions. By being cross-designated by the Manhattan and Queens District Attorneys, for example, the Inspector General gained jurisdiction, on a case-by-case basis, on state crimes occurring in those boroughs. The Inspector General gained jurisdiction on state crimes *outside* New York City by being cross-designated to the New York State Organized Crime Task Force, which had jurisdictions there. It acquired operating powers and authorities concerning Federal crimes by being cross-designated into the two Federal districts comprising New York City.

Having been cross-designated into these jurisdictions, the Inspector General's staff gained the full powers and protections of the partnering agency. This included access to confidential information that was otherwise restricted by law or practice, such as the authority to monitor live wiretapped conversations or review their transcripts. In return, the Inspector General's staff might contribute its time and resources to the investigation, or its unique technical and substantive expertise in a specialized area. Typically, cross-designations were good for limited periods of time, and conferred wide-ranging law enforcement powers on individuals.

Second, the Inspector General established within its Investigations Bureau the Criminal Investigations and Prosecutions Unit. The Inspector General staffed this unit by formally contracting for the services of law enforcement teams from OCTF, and the New York County District Attorney's Office. Under this arrangement, the Inspector General supported, via an annual budget transfer of $250,000 to each office, a five-person team that included an attorney, an investigator, an accountant and an analyst. The OCTF team was typically on site at the Inspector General's office in the Bronx several days each week. The Manhattan team remained sited at the DA's offices in lower Manhattan, although its staff worked out of the Inspector General's offices for extended periods. [109]

These two methods provided the formal structure and legal means by which the Inspector General gained access to wide-ranging law enforcement powers and authorities on a case-by-case basis. As cases might last for months or years, and evolve into further investigations and cases, the cross-designations, in effect, bestowed law enforcement powers upon the Inspector Generals staff on a continuous basis. It provided the office with invaluable access to the workproduct of confidential investigations, including information gathered from electronic surveillance, grand jury proceedings, search warrants, and informants. It gave the staff access to the investigators, and the investigations, and became critical to the operating capability of the office. [110]

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[109] Originally, Governor Cuomo had approved Thacher's plan to include a detachment of New York State Police troopers in the Inspector General's investigative unit. However, in managing investigations at OCTF Thacher had seen OCTF prosecutors, analysts and State Police investigators sometimes struggle to meld their different priorities and styles. He was wary of reliving that experience. Thacher was also concerned that in the off-and-on pace of investigations, in which prolonged periods of idleness could be followed by intense periods of activity, State Police commanders might pressure Thacher to free up troopers to other State Police priorities; it might be a constant battle to hold onto them. In any event, Thacher had commitments of investigative resources -- and, through cross-designations, had already derived the necessary state and county authorities -- from both OCTF and the Queens and New York County District Attorneys. While on numerous occasions State Police teams had worked well with other investigators and prosecutors in and around New York City, the fact was that by including the State Police, Thacher stood to gain little that he did not already have , and risked much. Rather than risk future conflict and jeopardize his then-cordial relations with the State Police organization, Thacher elected to back off from his own proposal, and let it pass without acting on it. See, Blakey, et.al., *Rackets Bureaus*, 1978 for a discussion of the always conflict-prone relationships on police-prosecutor teams: "The conflict emerges, not so much in determining objectives and priorities, but in the tactical movement toward achieving those objectives. Put another way, police do not resent being told what to do, but they do resent being told how to do it. Police supervisory personnel, too, must retain control over the allocation of their resources: they feel, quite understandably, that they cannot afford to delegate this responsibility outside their command structure." For a comprehensive treatment of cultural issues involved in the integration of organizations, see, Edgar H. Schein, *Organizational Culture and Leadership*. San Francisco: Jossey-Bass. 1992. "[M]ost companies today are trying to speed up the process of designing, manufacturing, and delivering new products to customers. They are increasingly discovering that the coordination of the marketing, engineering, manufacturing, distribution and sales groups will require more than goodwill, good intentions, and a few management incentives. To achieve the necessary integration requires understanding the subcultures of each of these functions and the design of intergroup processes that tallow communication and collaboration across sometimes strong subcultural boundaries."

[110] For a still trenchant analysis of the issues involved in the organization and management of police-prosecution teams, see Blakey, et. al, *Rackets Bureaus*, 1978, pp. 3-19. In the establishment of organized crime control units, "the functional relationship between a rackets unit, police departments within its

Leveraging Additional Resources

Cross-designation was not a "freebie" to the agency that acquired the new powers. In conferring these valuable authorities on another agency's staffs, the granting jurisdiction also licensed them to do work in the confidential arenas reserved for those who were sworn in the jurisdiction. The Inspector General's staff would be expected to share in the new investigative burdens as well as rewards. This included the arduous tasks of "sitting wires," transcribing recorded conversations, and assisting in surveillance and other staff-intensive activities.

Cross-designation therefore opened the door to a potentially debilitating drain on the Inspector General's staffs. Thacher recognized from the outset that a 50-person office could quickly become absorbed by a handful of cases. The risk of losing his staff to the new investigative burdens that might deplete the small office staff quickly did not pass unnoticed:

> "The teams could easily be overwhelmed by a single case. Too often inspectors general have allowed their offices simply to become adjuncts of prosecutors' offices, to develop a great case in-house and then get cross-designated to prosecute it. However much glory this might bring to the investigator or prosecutor handling the case, it works a disservice to his agency, which loses at least as much as it gains through cross-designation.
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> "We couldn't afford to let that happen, and proceeded differently. As cases were developed and got bigger, we sought more and more resources from the prosecutors' office. After all, the case was a potentially good one for them, not just us. Why not have the prosecutor assign whatever was needed to make the case as big and successful as possible?"[111]

Thacher came to the view that the primary trade for cross-designation could not, and would not be, "the body back" -- not an exchange of authority from the granting law enforcement agency in return for the use of the Inspector General's staff as personnel authorized to do work in highly technical arenas. Rather, the trade would be in three

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jurisdiction, and even other prosecutive agencies is as varied as the personalities and experience of the unit's director. Such units, however, can be roughly divided between variations of those that are essentially self-sufficient for investigative and prosecutive purposes; those that work with an external, but closely related police organization; those that work with multiple police agencies within a single prosecutive district or state; and those that lack prosecution authority, but attempt to perform a coordinating role with local prosecutors and police departments." In some respects, the SCA Inspector General borrowed from each of these models, but distinguished itself principally as being attached to the "host" agency -- the likely victim of racketeering. The Inspector General bridged the host to the outside world of enforcement agencies through the presence of onsite professionals representing some capability familiar and valuable to each outside agency, and through the machinery and access of cross-designation.

[111] Thomas D. Thacher II, interview (1995).

important assets which the Inspector General possessed and controlled, and which would add value to the granting agency's investigations.

First, the Inspector General would provide its partnering agencies with access to its stores of easily retrievable and up-to-date information on cases and individuals in its data systems. These systems were constantly refreshed with each new case, matter, or wiretap *originating in many different jurisdictions* around the region, not just a particular partnering agency. Agencies could reliably expect to get back much more than they put in: investigators from one agency gained unusually free access to intelligence gleaned from other cases or matters nearby, and the Inspector General's staff helped make sense of it all.

> "Prequalification is a critical part of the synergism. Information comes from all over the world that we're involved with. Why do investigators give it to us? Because we add to that information by marrying it to data in our files and theirs. It gives back to them what they' need, and more than they put in. Investigators typically don't share their informants with Intelligence or the people who put it in the computer for *other* people to have access to unless, giving it to Intelligence, they get more back. Where does it all find its most immediate, tangible impact? Prequal. Having done that, it generates information. Every time we do a certification we do an interview with the contractor and I say, "Tell me about your life." Ultimately I'm going to have to find out who controls that company. When they tell me, its invaluable. Not because of the issue today, per se, but because of its future value. And its marriable value -- married to other information. Standing alone, something would have no meaning. But married to something already there -- 'Geez, they're one and the same!' "[112]

Second, the Inspector General offered partnering agencies unique *access to its window on SCA operations*, and onto the construction industry. The Inspector General could create opportunities to aide investigations, whether to influence events, to see them unfold, or to cause things to happen. This was a boon to agencies looking for a better view of the industry, access to informants, and leverage over the freeform flow of events that was typical of prolonged undercover investigations. In the matter presented earlier, for example, we recounted the instance in which the Inspector General's staff, working with the New York County District Attorney, engineered a series of prequalification meetings that worked to the Government's advantage in numerous ways -- scoping out the physical site for the placement of eavesdropping equipment, helping to establish probable cause to secure the necessary authorizations, and "tickling the wire" to induce inculpatory statements from the targets.

Third, work with the Inspector General featured, prominently, access to other professionals who were at work on different regulatory, civil and enforcement aspects of the same cases. *Synergies with other civil and criminal enforcement units* promised to

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[112] Thomas D. Thacher II, interview (1992).

enhance the value of a partnering agency's own participation, sharing information, developing comprehensive strategies, and leveraging one's own resource commitments into a powerful, combined punch against a target.

As Thacher conceived it, therefore, the Inspector General's office would be "an information and access shop," not a "body" shop:

> "You sit and look at the problem of the victim from the eyes of the victim, as an officer of the Corporation. You step outside the Corporation to develop strategies to deal with those problems, as an Inspector General. You tap into a network of other professions to effectuate those strategies, some of which are back into the SCA. As you pursue each of these strategies with these other agencies or professions, there is generated information. This allows you to design and implement yet other strategies."
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> "We contract and develop networks in each of the areas we operate. It may be, for example, that we contract with a management consulting firm, or an accounting firm, an IAF, or a law firm to bring a civil case. In bringing together specialists in for each case from a variety of offices such as the Comptroller, the District Attorney, civil attorneys, accountants -- the potential of anyone of these people is itself leveraged enormously, so that *they themselves* start working together."[113]

Paying For The Privilege

The Inspector General frequently undertook several strategies simultaneously in a particular case, and across multiple cases. There might be underway in numerous cases at once criminal investigations, civil prosecutions, administrative sanctions, and loss systems analysis. To undertake such a wide range of activities with a relatively limited staff, Inspector General was forced to find ways to draw additional, and sometimes substantial investigative resources from the region's agencies.

At one point in time, as many as ten different law enforcement agencies might have been working with the Inspector General staffs on cases and investigations. Their commitment to the Inspector General came not as favor, but as a self-interested trade. Each agency got something significant of value in return -- a victory in their own area of responsibility, information, cooperating witnesses, informants, or undercovers, for example. The New York City Department of Investigations, for example, might jointly

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[113] *Ibid.* Thacher's assertion that in seeking cross-designation from the region's prosecutors he would retain his staff, but trade his information and access, and prosecutors' demonstrated interest in gaining lower cost access to potentially high value construction cases, is a rich illustration of the strategic value and role of information in law enforcement relationships. The posture helped Thacher maintain an equal footing with his powerful partners. For a classic description of the conditions under which organizations can maintain their independence in situations of potential dependence, see, Peter M. Blau, *Exchange and Power in Social Life.* New York: John Wiley & Sons. 1964. Pp. 118 ff.

initiate background investigations of SCA contractors in order to gain information to support finding more city contractors nonresponsible.

> "The trick is to figure how to take work in each specialist's area just far enough in-house that it can attract and support an outside specialist in that field. We do just enough to pay for the involvement of that specialist so that the specialist picks it up and does it for its own purposes. I.e., law enforcement adds resources to the extent it will get a mega case. The Comptroller's office will add resources to the extent its going to get a prevailing wage case. Corp Counsel will add attorneys to the extent it will get a major civil recovery."[114]

Even where public resources were scarce, the Inspector General used innovative means to create additional investigative capacity and to gain enhanced control over criminal firms, at a reduced cost to the public. It developed policies and practices for the SCA that put the burden of financing reform onto the backs of those whom the Inspector General caught cheating the SCA.

For example, one of the classic ways to defraud government in public construction is to cheat on the prevailing wage rates that state law mandates. By law, contractors on all public works projects in New York State, including SCA jobs, had to pay their employees the "prevailing rate of wage," which in the SCA's case was set by the New York City Comptroller. The SCA incorporates the prevailing wage requirement into it contracts.

Like other frauds that involve the substitution of a less expensive commodity, contractors can increase their profits by using cheaper labor than the law requires. Contractors who plan to violate prevailing wage requirements will have cheaper labor costs than those that live by the law. In a competitive bidding system, unscrupulous contractors who plan to cheat can gain an unfair advantage, bid lower, and win.

The problem has been that prevailing wage violations are difficult and costly to find and prove. In New York City, the Office of the Comptroller is charged with enforcing Labor Law §220 violations, yet it has long faced a substantial backlog of cases. While the SCA has a small Labor Law Complaint Unit -- a staff of two -- it cannot investigate every prevailing wage complaint. As a rule, city construction agencies -- including the SCA -- have generally viewed responsibility for enforcement of Labor Law §220 as the Comptroller's.

Given the importance of the problem, its magnitude, and the failure of traditional remedies to deal with it adequately, the Inspector General developed an alternative approach. It used the traditional tool of the construction contract to increase compliance, first enhancing the traditional contract in order to address the peculiar demands of the situation.

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[114] Thomas D. Thacher II, interview (1995).

Every SCA contract now requires that if a contractor, having been accused of violating prevailing wage requirements, is found to have done so, it must pay the cost of the investigation. "To hire an investigative auditing firm to look into a contractor may be $50,000 in fees -- prohibitively expensive for a public agency whose job it is to build schools," Thacher said. "The solution, then, is to put into the contract a requirement that the contractor pay the expenses of the investigation, but only if the investigation proved that the contractor had violated the contract." The investigative auditors' fee is levied onto the violating contractor rather than picked up as part of the public's tab. If a contractor refuses to pay for the cost, it can simply be deducted from the retainage on the contract.[115]

In 1994, the SCA selected five private firms to conduct Labor Law §220 investigations. Under the program, the SCA identifies firm that are subjects of prevailing wage complaints and assigns one of the private firms to investigate. Three firms have been assigned and as of late 1995, all investigations were pending.[116]

Using Law Enforcement Information To Advantage The SCA

The cross-designation of Inspector General personnel into partnering law enforcement agencies allowed the Inspector General to investigate more fully the backgrounds of companies applying to be prequalified for SCA work. It also allowed it to gather evidence for prosecutors to use in bringing criminal charges against companies that either filed false prequalification applications or violated the law while working on an SCA project. And it opened the door to important transactions around critical information that built trust between agencies.

The information flow was extremely valuable to the Inspector General. Thacher summed up the benefits to the SCA:

> "The Inspector General/law enforcement/SCA partnership provides an extraordinary quantity of current information that explains in the most graphic way possible who is doing what to whom -- and how -- in the SCA's program -- what contractors are cheaters, what employees are ineffective or worse, what processes are dysfunctional, and what departments are failing.
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> "Who better to advise the SCA on how easy it is to rip off the agency than a contractor who is doing business with the agency? Who better to detail the ease of bribing inspectors and engineering auditors than the informant who did so yesterday? Who better to describe what companies an agency shouldn't be doing business with than the informant who enabled those companies to cheat the agency?

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[115] *Ibid.*

[116] Memorandum, Thomas D. Thacher II to Barry E. Light. *Privatization of Labor Law 220 Investigations.* New York City School Construction Authority. May 5, 1993.

"Armed with this information, the SCA can move in ways that no other agency could — procedures can be reformed, companies debarred, millions of dollars recovered in civil actions, departments restructured – all as a result of Inspector General's ability to unlock doors to the treasure trove of information developed during the course of criminal investigations. By entering into this partnership with law enforcement, the SCA reaps the benefit of an unprecedented message of deterrence to corrupt forces within and without – the risk of detection and punishment at the SCA is extremely high." [117]

Prosecuting Cases

The region's investigators and prosecutors, in a departure from their normal practice, regularly shared information about their ongoing investigations with the Inspector General, strategized with its staff about how to proceed, and worked jointly on investigations. They knew and trusted the Inspector General's staff. Its extensive law enforcement backgrounds and long-standing professional relationships gave enforcement agencies confidence that information that they shared with the Inspector General would not leak, a fear that could not be put to rest sufficiently when these same investigators and prosecutors contemplated sharing information with most other inspectors general in the city.

Over the long run, however, state and Federal prosecutors were willing to work with the Inspector General not simply because the staffs might know each other or wanted the Inspector General to succeed. They worked with the office because they were hopeful that the Inspector General would gain them more powerful entree to the New York construction world and lower the cost of case-making there. They believed that the promise of this office was in their own interest in making cases, and making them relatively easily.

The current cost of doing business in construction markets was high for law enforcement. No agency had a clear view of the players and transactions, or steady access to informants on job sites. Securing probable cause for electronic surveillance was often time consuming, expensive and a difficult investigative prospect. It could depend as much or more on luck than anything. And in the construction industry, it was an expensive and sometimes nightmarish task for prosecutors to gather the evidence they required to establish, beyond a reasonable doubt, the frauds, extortions and bid rigging that were so common to the business. Proving such crimes depended on having detailed records about the construction project, and the testimony of victims, both of which were often beyond prosecutors' reach.

The current price of investigative entree to this realm was high, and it reduced law enforcement's investment to a very few cases that happened to come its way, though not

[117] Thomas D. Thacher II, personal communication.

through any intensified scrutiny, *per se*, of the construction industry, and that involved star mobsters. By engaging the Inspector General's Office, prosecutors hoped that it would be possible to monitor SCA construction projects closely enough to provide leverage and evidence in abundance.

Several cases stand out in this regard, including Operation *Tightrope*.

Operation Tightrope

On May 20, 1994 the New York Times reported on the genesis of what became Operation *Tightrope*:

> "Mayor Edward I. Koch in 1985 ordered the Department of Investigation to look into complaints about cost overruns and design flaws at La Guardia High School. The department was later joined by the FBI, the SCA, and OCTF in trying to unravel the overrun mysteries at La Guardia. Investigators...said they were largely stymied until 1990, when they uncovered evidence that [Martin Singer, the president of Mars-Normel, a construction company and major school builder] had submitted inflated bills, totaling $4.5 million." [118]

Thacher recalled the early stage of his involvement with the case:

> "We had just opened for business [spring of 1990] and were barely in operation. The Southern District U.S. Attorney called us down with a proposal. 'We have an informant who's prepared to work an undercover operation. He's agreed to cooperate and give up mobsters.' It turns out the Southern District and DOI had been investigating Marty Singer and flipped him. They wanted the SCA to put him and his firm to work.
>
> "We said, 'Wait a second.' The company they wanted us to give work was the worst. Mars-Normel was exactly the reason the Inspector General was created. There was no way this company would get SCA contracts no matter how valuable the investigative potential.
>
> " 'What we'll do instead is this,' we said. 'We'll select a contract for the informant to bid on; we'll rig it so that he wins.' At that point, under the rules, for 45 days everybody would have to hold their bid -- no one can walk away from their bids before the 45 days are up. Singer was promising that the mob would come the first day he got a contract to talk with them about. We said, 'This will give him 40 days to get all the Title 3 you want [induce incriminating conversations with targets to establish probable cause and secure court authorization for full-blown electronic surveillance of cars, offices, and homes.] Let him run loose and talk to everybody he can find. Then we'll pull the contract.'

[118] "*Contractor Known for Work on Schools,*" New York *Times*, May 20, 1994

"Meanwhile, we had an opportunity to go deeper into Marty Singer's background and noticed that years before he'd been debriefed and admitted to paying hundreds of thousands of dollars in bribes to a very significant attorney at the Board of Education who was responsible for resolving disputes with the Board's construction contractors.

"At that point, the investigation took a different course. Initially, we thought, 'That's really focused on the Board of Education: what are we going to be doing investigating Board of Education officials rather than players at the SCA?'

"But we realized that that Board attorney was probably dealing with all the contractors with whom the SCA would be dealing and wanted to weed out. If we could 'flip' this attorney, gain his cooperation, get him wired up, he could give us an extraordinary line into other firms that had been bribing Board of Education officials.

"There was also the possibility that the Board of Education employees who might come over to SCA [with the transfer of the Board's building responsibilities to the SCA] had broken bread with this guy, and we could get valuable information on these individuals. Lastly, if the SCA has one client in life, the Board of Education, and that client is corrupt, and the Board develops a capital plan and decides what, where and when and how to build, then that corruption would clearly infect the capital plan. What chance would the SCA's whole program have then? We viewed corruption at the Board as a direct threat to the capital plan the SCA was charged to execute.

"So we decided to go after the attorney and the contractors who [like Marty Singer] had tried to bribe their way out of problems with their Board of Education contracts. We wrote an investigative plan with the Federal government that became the basis of Operation *Tightrope*. It developed into one of the biggest corruption/racketeering cases involving public construction. Marty Singer was wired up, talking to Shelly Rosenblum [the Board attorney]. Shelly was arrested, flipped, and wired... set up to do business in an office in Queens. The construction community was coming in to pay him off -- lawyers, contractors, architects. This case was just a phenomenal case." [119]

Over time, the investigation, conducted by the Inspector General and the United States Attorney, the FBI, OCTF, and the New York City Department of Investigation -- a task force of forty people -- was run out of the Inspector General's Bronx offices. The Inspector General's Counsel Kevin Ford coordinated the matter.

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[119] Thomas D. Thacher II, interview (1995). Ultimately, Thacher's offer to rig a bid to Marty Singer passed without action. In any event, Thacher doubted whether Singer would ever have delivered the mob, as he was promising. Singer had made similar promises in previous encounters with federal agents, but then backed away. "In general, contractors will give up anyone, but never the mob," Thacher said. "Marty Singer was not scared of Shelly Rosenblum. He was terribly scared of Sammy Gravano." Thacher has on several occasions since, and in different matters, repeated the offer to stage rigged bids for investigative purposes, but reports that he never has.

On May 19, 1994, Mary Jo White, United States Attorney for the Southern District, announced Federal charges of bribery, fraud and racketeering against 18 Board of Education employees and contractors working for the Board. Some of the criminal conduct that was alleged dated back to 1981.

During the course of the investigation Martin Singer died, but not before he paid restitution of over $5 million to the school system. Sheldon Rosenblum, Deputy Counsel to the New York City Schools Chancellor, was charged with receiving bribes from Singer, who had worn a wire and recorded conversations with Rosenblum during 1990 and 1991 in which Rosenblum inculpated himself. Others were charged similarly, including the owners of four companies that had done $500 million in construction business with the Board of Education over 15 years. "Measured by the number of those charged and their influential positions," the New York *Times* reported, "it was one of the largest corruption scandals uncovered at the Board of Education."[120]

Making Small Cases

Not every case was a "mega" case. Some cases, developed initially by the Inspector General, were relatively small. Though they might not have a big impact on the construction industry, they might send important signals and, in advancing the SCA's objective to buy and build clean, be essential to make.

Jim O'Brien was an SCA investigator who was assigned to one such case early on. He recalled bringing that matter, involving a $100 bribe, to the Queens DA's Public Corruption Unit. "I had an open door to Queens," he stated. Though it was small by any standard, the case had been carefully prepared and was ready to go. "We brought a Grand Jury-ready package," O'Brien remembered. "The case pleaded, and everyone was happy."[121]

> "The president of a Manhattan construction company was accused yesterday of passing a $100 bribe to an employee of the city's SCA to persuade him to speed up some paperwork. John Contreras, whose company has two contracts for roofing and exterior work with the SCA worth $500,000, was trying to persuade a mid-level manager in the SCA to expedite the paperwork or a payment due his company..[T]he employee promptly reported the incident to his supervisors. Contreras surrendered at the offices of Queens District Attorney John Santucci. Kevin Ford said accepting gratuities from contractors [had been]

[120] New York *Times*, May 20, 1994. It is interesting to note that this case was made very much on terms favorable to the SCA's priorities and long term interests. In an interview, Ford remarked that the customary FBI priorities for investigative targets, in descending order of importance, were (1) organized crime figures, (2) corrupt elected officials, (3) corrupt non-elected officials, (4) labor racketeering schemes, and (5) collusive bidding among contractors. It was the Inspector General's hope to reverse these as priorities, as in general bid rigging and labor racketeering were viewed as the criminal activities most impacting the SCA and driving up costs in the construction industry.

[121] James O'Brien, interview (1992)

common at the Board of Education... 'We want to make sure contractors don't even attempt to develop the same relationship with our personnel."[122]

Since then, the SCA has conducted numerous investigations with the Queens DA, leading to prosecutions in six different matters.

A Conduit For Cases

During the first years of operation, the dynamics of competition and rivalry among New York's law enforcement agencies had an impact on the cases that the Inspector General made.

Although both OCTF and the New York County DA's office had, in 1987, received enviable $2 million seed grants to get into the construction business; and each had later set up teams to work with the Inspector General; and each had received *additional* financial support for those teams from the Inspector General, the majority of the Inspector General's first cases developed in the Federal venues of the Southern and Eastern Districts of New York. Indeed, in reviewing the arrest log of the Office of the Inspector General , it was not until 1994 that an Inspector General's case resulted in an arrest and prosecution by the New York County DA.[123] Rather, cases from the Southern District, the Eastern District, and the office of the Queens District Attorney dominated the workload. Why? Several factors may account for this.

First, given the choice, prosecutors almost always prefer to make cases in the Federal venue. The rules of procedure are much more favorable to the government, and the penalties upon conviction are much stiffer.

Second, Kevin Ford's relationship with the Southern District brought cases and activity early on in that venue. "Kevin would spend two or three days a week for us down at the Southern District [in lower Manhattan]," Thacher recalled. "The reality is that the operation had to be built on people and the strength of their relationships. The reality was that Kevin's relationships with the Southern District were strong, and he brought a number of cases from the Federal government right in the door."

Third, the physical separation of the New York County DA's team, sited at the DA's offices in lower Manhattan, from the Inspector General and his staffs in the Bronx meant there was an absence of constant physical proximity and synergism. When the Eastern and Southern districts were working cases with the Inspector General, FBI agents became frequent visitors to the Bronx offices of the Inspector General, and even had their own desks assigned. So, too, did the staffs detailed from the New York State Organized Crime Task Force, a few miles up the Major Deegan Expressway in Westchester County.

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[122] New York *Newsday*, December 20, 1990

[123] Office of the Inspector General, *Arrest Log 12/10/90 - 5/15/95.*

But the New York County DA's unit never physically resited itself to the Bronx. Thacher believes this eroded some of the potential synergy and delayed casemaking. "There was a certain amount of waiting for us to deliver to them," Thacher recalled.

As late as 1993, the Manhattan staff noted the lack of spectacular cases coming out of its efforts with the Inspector General, although investigations were in progress that they hoped would reverse this trend. "Our relationship with them was not as successful as it probably will be in the future and it certainly wasn't as successful as I had hoped it would be," Robert Mass stated. Michael Cherkasky commented that he had "great hopes" that current investigations being conducted in conjunction with the Inspector General would result in major cases; since this type of case typically might take years to conclude, Cherkasky believed that the relationship had not yet had time to bear fruit.[124] Still, the New York County prosecutors took a dim view of the value of other Inspector General cases such as the Eastern District of New York's *Sandaq Engineering, Inc.* matter which, they said, "didn't do anything." In that matter, federal prosecutors, in 1992, indicted the principals of an asbestos abatement firm, charging them with conducting phony asbestos tests and defrauding the SCA of $500,000. [125]

Starting in 1994, and into 1995, however, the long-expected cases with Manhattan began to develop, and the relationship was restored to course. On September 27, 1995, for example, DA Morganthau and Inspector General Thacher announced a 62-count indictment capping a six-month investigation of Khemsafe Environmental, an asbestos abatement firm charged with defrauding the SCA by falsifying its credentials and tests. In his statement to the press, District Attorney Morganthau said this:

"[T]oday's indictment is just the latest example of the benefits of the cooperation that has long existed between the District Attorney's office and the SCA's Inspector General. Our experience in investigating corruption in the construction industry indicates that what may at first blush appear to be a simple mistake or an isolated act of incompetence on the part of a contractor sometimes masks a far more extensive problem. Here, it might have been easy to dismiss Khemsafe's conduct at [Intermediate School] 125 as simple incompetence. However, because of our unique relationship with the SCA, and with the extensive help of DOI, we were able to demonstrate that Khemsafe's conduct was an example of incompetence crossing the line into criminal conduct with extremely serious consequences. We will continue to be vigilant to insure that others who work on public jobs will be fully accountable if they engage in criminal conduct." [126]

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[124] Interviews, Michael Cherkasy and Robert Mass, Office of the New York County District Attorney (1993).

[125] Sandaq's owners had misrepresented themselves as owning a licensed and certified asbestos testing and analysis laboratory; falsified their employees' experience to gain them asbestos handling licenses; failed to accurately identify asbestos; falsified laboratory results; and fraudulently billed the SCA by submitting false and inflated invoices.

[126] Statement of the District Attorney, New York County. *News Release*, September 27, 1995.

Procedural Reform: Reducing Opportunities For Fraud

The Inspector General's program focused principally on three aspects of SCA operations: to develop an exacting prequalifying procedure designed to keep corrupt firms from doing business with the SCA; to help other agencies make civil and criminal cases on its behalf against corrupt employees and criminal firms, so as to create a credible threat of detection and deterrence; and to find flaws in SCA practices and procedures that left the Authority vulnerable to crime and corruption, and to recommend fixes..

Indeed, some of the Inspector General's most important contributions to the SCA's immediate mission of buying quickly, inexpensively, and cleanly have focused on reforming SCA procedures and reducing the opportunities for fraud on SCA construction projects. The Inspector General also searched for methods to increase competition among bidders, thereby reducing the cost of building and renovating schools. It is these measures, and the impact that all of the initiatives together have had on the working relationships within and performance of the SCA, that are the focus of this section.

Doing The Work

The task of helping to reform SCA procedures fell to the Inspector General's *Research and Analysis Unit*. Its primary mission was to recommend policies and procedural reforms to reduce the incentives and opportunities for crime and corruption targeted against the SCA.

There were numerous ways in which Research and Analysis might learn of problems to be addressed. Complaints and allegations that came into the SCA from disgruntled employees and contractors, for example, were useful sources of information. Investigators might identify procedural problems during the course of investigations. Prequalification might stimulate additional insights on policies and procedures. Systematic reviews of SCA's procedures manual and SCA reports could be useful sources for identifying internal weaknesses. And analysts might undertake self-initiated projects, based on their knowledge of the industry or the SCA, to further strengthen the Inspector General's understanding and the SCA's capabilities. Below are several examples of this work.

Bonding

One of the Inspector General's earliest recommendations concerned SCA's bonding requirements. By law, companies bidding on SCA contracts were required to guarantee the SCA that if they could not, or did not, perform their job, the SCA would be reimbursed for its damages. This guarantee, a common requirement in New York City, is supplied in the form of a surety bond that the contractor arranges for with an insurance or surety company. [127] Since any company that could not receive bonding, because insurance and surety companies judged that the risk was too high, would be out of business, there was a flourishing market for fraudulent bonds. Such high-risk companies were able to receive bonds from fraudulent or unauthorized bonding companies, sometimes knowing that the issuers were illegitimate and sometimes not.

To protect the SCA from this risk, the Inspector General's Office conducted an analysis of the bonding industry and proposed a set of procedures intended to aid the Authority in discovering when companies submitted fraudulent bonds. The Inspector General developed a checklist for the Contract Administration Office to follow to allow it to verify each bond it received. "Effective authentication of the bonds will require a complete review of all information included on documents submitted by contractors and sureties," a document describing the new procedures stated. In addition to the checklist, a Bond Authenticity Inquiry Form was developed. Contract Administration was to forward this form to the surety company that issued the bond. Contract Administration was carefully instructed in the proper use of this form: "To ensure a prompt response from sureties, the Bond Authenticity Inquiry Forms are to be mailed as soon as bonds are submitted to the Contracts Department. A photocopy of the bond in question should be attached to each form. If necessary, a telephone call to the surety should follow within one week of the initial inquiry." [128]

Asbestos Abatement

The Inspector General made recommendations for procedural fixes based, also, on its analysis of fraudulent schemes that it discovered and investigated.

One of the earliest instances of such a reform resulted from the investigation of Sandaq Engineering, Inc., an asbestos abatement firm. In 1992, as a result of a joint investigation by the United States Attorney for the Southern District of New York and the Inspector General's office, Sandaq's principals pled guilty to defrauding the Authority of $500,000. The Inspector General also sought and obtained $2 million in settlement of a civil racketeering lawsuit brought by the SCA against the firm. In a prepared statement, the SCA Trustees said, "More important than the indictment itself is the process which produced it and the responses which shall follow -- criminal prosecutions of the

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[127] The cost of the bond is between 1 and 4 percent of the contract price. The premiums on the bonds are passed along to the Authority as part of the contract price.

[128] "*Bonding Inquiry -- Overview*," an attachment to SCA bond authentication guidelines and authenticity review form.

defendants, a civil racketeering suit to recover stolen tax dollars, and institutional reforms to prevent recurrence of the fraudulent activities." [129]

In reviewing the SCA procedures that left the Authority exposed to Sandaq's corrupt practices, the Inspector General determined that the SCA had been unprepared to manage asbestos abatement on the significant scale required by the New York City public schools:

> "The SCA initially created the Health and Safety Units to work as an adjunct to project management, providing industrial hygiene consulting when requested. Only three people were assigned to staff both Units. The Authority did not anticipate the rapid expansion of its asbestos abatement workload and concomitant increase in the responsibility that the Health and Safety Units would be required to undertake, including the assumption of several tasks previously performed by the Board of Education. Additionally, the project office management system did not encompass the specialized area of asbestos abatement. As a result, the Health and Safety Unit's two industrial hygienists were forced to assume various management tasks, such as project and contract management, inspections, budgeting and financing, with no training in these areas and little time to perform the work required at multiple sites throughout the city." [130]

Sandaq's owners obtained state licenses and certifications for asbestos abatement, and ultimately SCA contracts, by making false and fraudulent representations regarding the qualifications of the firm and its employees. Based on the Inspector General's assessment, the SCA undertook to modify its portion of the prequalification application to require firms to provide information on current licenses and certification necessary for work. It reorganized its Health and Safety units to provide additional personnel to conduct technical reviews of consultants' qualifications and past performance.

Having secured the licenses and contracts, Sandaq used unqualified employees in the field and laboratory to sample, test, analyze and monitor abatement work. As a result, the Inspector General determined, Sandaq failed to identify asbestos accurately or to provide timely samples, falsified lab results by extrapolating analysis reports to untested samples, failed to provide independent estimates of change order work, as required, failed to maintain adequate records and logs, and other deficiencies. To address this, the Inspector General recommended that the SCA reorganize and establish a new inspection unit to provide direct supervision of consultants' work in asbestos abatement and testing. The SCA, in addition, developed a standard checklist of tasks consultants were to perform as part of their monitoring duties, and required these be filled out and submitted as log of tasks performed.

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[129] Statement, New York City School Construction Authority. *PR Newswire*, June 25, 1992.
[130] Judith Anne Stevens, memorandum to Thomas D. Thacher II, *The Sandaq Investigation: SCA's Response to Fraudulent Activities in Asbestos Air Monitoring Contracts*. New York City School Construction Authority, May 18, 1992.

To get paid, Sandaq defrauded the SCA by submitting false and inflated invoices for payment, billing for work never performed, inflating labor costs, billing for laboratory work performed by its uncertified laboratory and other practices. To address this, SCA instituted systematic checks of consultant work prior to final payment approvals, and introduced a new inspections unit to function independently from project management to review work performed by air monitoring consultants.

Bid Rigging

The *Monopoly* matter referred to earlier revealed a number of extraordinary flaws in SCA policies and procedures.

The *Monopoly* matter was made possible, in part, by the SCA being lax in its screening of its new employees. Two years prior to being hired at the SCA, the individual who became the brains behind the Monopoly bid-rigging scheme had been convicted of burglary elsewhere in New York and sentenced to five years probation. When asked on his SCA employment application whether he had a criminal history, the job-seeker left this question blank and unanswered.

The SCA overlooked this omission, and lacking a separate means to check its applicants' criminal histories, failed to learn that he was a convicted felon. Ultimately, the SCA hired the job seeker. He became responsible for engineering the scheme to defraud the Authority in the *Monopoly* case.

The *Monopoly* matter, in fact, was replete with lax practice and procedural failure. In a memorandum to the Inspector General, Kevin Ford identified numerous such failings leading to the corruption and criminal conduct in the *Monopoly* matter:

> "Although the SCA's official procedures require that three SCA officials be present to monitor each bid opening, in the general rush to get the contracts out, this rule was often not observed. Instead, only two SCA representatives were usually present at bid openings, with one individual opening and announcing the bid prices while the second person merely recorded the amounts on the bid sheet. Since the other employees who assisted in the bid openings seemed to be unaware of either the policy or the purpose underlying it, they seldom paid any attention to what the contract specialist did." [131]

The Ford memorandum detailing the sources and causes of the failure was wide ranging and filled with frustration at SCA failures:

> "Unfortunately, this investigation has also revealed much about the SCA that is cause for grave concern and much that is far from flattering about operations at the SCA. These defendants demonstrated that, with little difficulty,

[131] Kevin J. Ford, Memorandum to Thomas D. Thacher II, 1993.

they could pervert the SCA's bidding process, payment process, change order process, and inspections process... They did so with relative impunity, employing very simple and unsophisticated ploys that nevertheless failed to raise any discernible concern on the part of SCA management. In fact, but for the vigilance of the Inspector General and a fortuitous break in a criminal investigation, these defendants would still be successfully defrauding the SCA today, resulting in the direct loss of many millions of dollars and causing collateral damage of far greater proportions."

The highlights of SCA weaknesses were cited to include:

- "Extremely weak and ineffective" supervision of project officers and contract specialists.

- A failure, for three years, of the SCA to embrace the Inspector General recommendation that a sophisticated system for evaluating and monitoring bids, change orders, and payment requests be introduced.

- A "depressing" tolerance of "brazenly" unethical and criminal conduct by fellow employees who failed to report the corruption, attributed to "morale among the rank and file in project management and contract administration" that Ford characterized as "abysmal." He wrote that "there are widespread perceptions that...favoritism and connections" abound in promotion and raise decisions, and that "a double standard of ethical conduct exists between management and the ranks..."

- A prevalent disparity between SCA official policy and procedures, and practice, that the Inspector General "has repeatedly noted." This was due, in part, to the "the widespread perception that the polices are routinely ignored or circumvented by senior management, not necessarily for corrupt purposes, but simply for the sake of expedience. ... This establishes a rationale, if not actual precedent, for others to do so..."

- A failure to establish "the requisite checks and balances needed to reduce corruption vulnerability...at the SCA. The combination of almost unfettered discretion in the hands of a few people, routine deviations from established policy, nonexistent or very lax ethical norms, low morale and ineffective supervision will inevitably produce corruption as this case demonstrates."

The Inspector General recommended ten measures that might address the weaknesses exposed by *Monopoly*. These included requiring three SCA representatives to

attend all bid openings, as per established policy; revising the bid document and bid bond form to reduce the possibility of someone substituting a different price; establishing and enforcing standards for rejecting bids, and, notably, adopting legislation to authorize the SCA to fingerprint prospective employees. It was recommended that the SCA president establish a process to review these issues and recommendations with "all of the affected SCA officials... since, as this case illustrates, the best designed policies and procedures are useless if they are not understood and followed by those charged with performing the duties they address." The Inspector General's role, over and above suggesting specific reforms, "will be to define and describe the problems...and to monitor the review process to insure that each problem is appropriately addressed..."

Increasing Competition: Artificial Turf

The Inspector General's efforts to help the SCA achieve its primary mission also focused on methods for improving competition within the construction industry. In September 1990, for example, the Inspector General recommended that the SCA modify the criteria that it was using for a very common material -- the artificial turf used to cover athletic fields. These specifications determined which companies were eligible to supply this material -- only a company that made turf that met these specifications could supply it for the New York City schools. In fact, just one supplier made turf that met the SCA's specifications, which had been written at the Board of Education years before.

The purpose of the Inspector General's suggestion that the SCA revise its specifications was to allow the Authority to be the beneficiary of competition among turf suppliers. The Inspector General offered its recommendations after reviewing bid documents for all the athletic field contracts let since 1985 by both the Board of Education and the SCA. This review showed that in each case the artificial surface, which was the major cost in athletic field renovations, had been obtained from a single supplier. The Inspector General also concluded that there was evidence to suspect that the company that had supplied the turf had helped write the specifications for the product, and had done so in such a way that only their product fit the bill for New York City schools. The SCA adopted the Inspector General's recommendations that it modify its specifications to create competition among suppliers and subsequently found a turf supplier that offered a lower price.[132]

The Inspector General's recommendation that the SCA review its specifications for artificial turf, and the savings that resulted, illustrates how the Inspector General has been able to find a larger institutional role for itself within the Authority. The artificial turf investigation required the type of analytical resources the Inspector General was staffed and resourced to provide. And in reducing the cost of a major material used in school

[132] The original set of specifications had been written so many years earlier that it was not possible to determine whether there had been collusion between Board of Education employees and the manufacturer.

construction and renovation, the Inspector General aided in the SCA's overall goal of reducing the cost of school construction.

This type of reform, in which the Inspector General's recommendations do not cause the rest of the SCA organization extra work and might lower its costs, was well accepted. In purchasing artificial turf, SCA officers had to refer to a set of specifications, and whether it was an old set of specifications or a new set did not affect how they performed their job. They were also happy to increase competition, though at least one SCA officer suggested that the change in specifications had not, in practice, resulted in a new supplier winning SCA's turf contracts.

The Inspector General and the SCA president both believed that more examples of one supplier winning all the SCA's contracts could be uncovered, and competition could be enhanced as a result, if there was a systematic bid-monitoring system to review the Authority's contracts. But this proposal received a lukewarm reception from a key SCA official who would have to make the system a part of his operation. Although he "resolved some day to get around to it," it was not a high priority, as all his operation's efforts were consumed with the more immediate business of processing contracts. Moreover, he viewed a bid-monitoring system as aiding the Inspector General's operation more than his own.

VI. SUMMING UP: ASSESSING THE DIFFERENCE MIDSTREAM

> *We begin to suspect that there is no stable state awaiting us over the horizon. On the contrary, our very power to solve problems seems to multiply problems. As a result, our organizations live in economic, political, and technological environments which are unpredictably unstable. The requirement for organizational learning is not an occasional, sporadic phenomenon, but is continuous and endemic to our society.*[133]

The SCA Inspector General was established to secure the SCA's building program from crime, including corruption and organized racketeering. The strategy implicit in its creation was to establish an entity attached to, and part of, the host "victim," expecting that from that position it could most effectively help to organize and effectuate the host's defense.

As its primary *tactical* concern was with criminal threat which, by its nature, might originate from outside the host organization, the entity had a prominently turned outward face. This gave it a view of its terrain, and opened it to relationship-building with external agencies who were involved in organized crime control in the field.

As its overarching *strategic* responsibility was to the host agency and to its core mission of building public schools, it maintained a prominent view inward as well. From this vantage it gained a sharper image of the workings of SCA operations and builders, and held open this "window on the industry" to outside agencies. It used its knowledge of the SCA and its access to builders, also, to temper and direct the activities of the law enforcement agencies on behalf of the SCA's goal to build schools quickly, effectively, and at low cost.

To accomplish its objectives, it was necessary to harness the authorities, resources and skills of local law enforcement and other professions on the SCA's behalf, and to do so in a manner consistent with the SCA's core mission of building safe, low-cost schools on time and on budget. Achieving this, the SCA and the Inspector General sought to gain access to much-needed information concerning corrupt or criminal contractors, so as to screen them out in the first instance; create a credible threat of discovery and penalty, so as to deter them in the future; interdict criminal schemes early on so as to minimize the damage done; and repair broken SCA procedures so as to strengthen the Authority's defenses and block opportunities for future criminal attacks upon it.

In so doing, the Inspector General would not only protect the SCA building program from crime and scandal. It would help establish at least one major buyer in the public construction marketplace that bought clean, an important step itself on the road to

[133] Argyris and Schon, *Organizational Learning*, 1978.

reform in that marketplace, and in the broader construction industry. It would strengthen law enforcement's hand in attacking organized crime in public construction and the construction industry more broadly, helping to deprive organized crime of the power and wealth it might draw from that formidable trough, including the SCA's own multi-billion dollar construction program.

Each of these measures would strengthen the SCA's near-term position and help it to build "clean." In the long run, the measures would weaken organized crime's hold on public building programs and construction markets in New York City, creating improved competition and performance, benefiting the SCA and all public buyers of construction goods and services.

Prequalification, Investigations, and Procedural Reform

The observations preceding in this report testify to the complex operational innovations made to achieve these goals and purposes. At this stage, we can offer a preliminary assessment of these initiatives, including observations about the theoretical limits of the effectiveness of prequalification in particular. We share, also, quantitative information about how often firms have been debarred; observations regarding the success or failure of the Inspector General in facilitating the prosecution or immobilization of criminal firms; and observations concerning whether and how the Inspector General might have been effective in reforming SCA procedures to block opportunities for corruption and racketeering.

Important further questions remain. Have these efforts been effective in allowing the SCA to buy and build not just "clean," but quickly, with good quality, and inexpensively? Was the innovation of the Inspector General such that it had a broader impact on restructuring public construction in New York City? Has law enforcement achieved its broader purposes in dealing with organized crime in the New York City construction industry? Empirical information about the impact on the SCA's own construction program, the impacts on public construction more broadly, and the consequence for law enforcement in attacking organized crime, per se, in the construction industry and the public construction submarkets must await a later evaluation.

Theoretical Limits

Underpinning the Inspector General's prequalification process was the notion that a prescreening process could detect and weed out the kinds of threat to which the SCA was subject. This assumed that three conditions pertained.

First, it assumed that companies that had engaged in past unethical conduct or been caught in wrongdoing would engage in future misconduct. This first condition is

important since prequalification could be effective only if some or all of the crime, corruption, and racketeering in the construction industry were done by "repeat offenders." This seemed likely given the evidence on the industry, but it was at least conceivable that some portion of the crime and corruption came from one-time offenders. To the extent this was true, prequalification efforts would be more difficult, and less effective.

Second, it assumed that not every company -- not even the vast majority of companies -- had been guilty of corruption or racketeering. This second condition is important because it suggests that stringent prequalification would not eliminate all competition for SCA business. Even after stringent prequalification, enough honest firms would remain to ensure robust competition, or at least to get the work done. This, too, seemed likely, especially over the long run. In the worst case, even if only a few firms in a specialty trade could, in the short run, survive a rigorous prequalification process, over the longer run the competitive market would facilitate the emergence of firms that met the standard. Indeed, that was part of the Inspector General's hopes for restructuring public construction in New York City.

Third, it assumed that corrupt companies would sooner or later show their hand, or could be found out by aggressive investigation. This third assumption is a necessary condition for prequalification to work. It is possible that corrupt companies which sought prequalification had committed crimes in the past without producing any outward signs. Indeed, most companies that engage in corruption and racketeering are able to do so precisely because they are good at getting away with their crimes. The better a firm had been at covering its tracks, the more difficult prequalification would be, and the less often prequalification would succeed at screening out corrupt or racketeer-influenced and controlled firms.

Outputs

What was impressive about the Inspector General's efforts was how they expanded the opportunities to find corruption-prone firms. The empirical data makes plain that fewer firms can escape detection now than in the past.

- During the period January, 1990 through December, 1995, the Inspector General had reviewed 3,844 firms' applications for prequalification.

- Of the 3,844 applications it reviewed, the Inspector General approved 2,977. This included 77 companies that were approved, but under certifications. 6 have been approved and are doing work under IAF monitoring agreements. [134]

[134] These include the following firms: Hercules, Herbert, Ebasco, Manshul, Graham, and E.W.Howell.

- 224 companies have been debarred or otherwise declared ineligible to receive SCA contracts. 19 have since received requalification. 143 companies are currently debarred.

- 60 applications are under current review. 125 are counted as being inactive or incomplete.

- 147 companies are in the status "pending review," and receiving special scrutiny. As of January, 1996, 39 of these are in the process of being disqualified.[135]

While numbers are important, they tell an incomplete tale. The core activity of prequalification, investigation and procedural reform harvested tangible benefits for the SCA:

- It clearly excluded numerous firms whose poor record of integrity made them corruption risks. *In doing so it greatly reduced one of the huge uncertainties facing the SCA, namely the unknown risk that a contractor might engage in future criminal or corrupt activities impacting SCA contracts and programs.*

- It provided for interim means of control such as certifications, so that the SCA might reign in other suspect firms. *In doing so the Inspector General gained leverage over the activities of suspect firms whose full debarment was either impossible or impracticable. The interim control measures devised by the Inspector General permitted vital construction projects to continue that otherwise might have stalled, or that would have proceeded without adequate controls on the suspect contractor. They permitted investigations to continue while minimizing the damage done by the ongoing criminal activities of suspects and targets.*

- It set the stage for subsequent investigations and prosecutions of individuals and firms that were intent on victimizing the SCA. *In doing so it created a risky landscape for contractors that it knew or suspected of lying to it; induced law enforcement agencies into continued and deepening involvements into the probe and prosecutions of such contractors; and created the investigative predicate for civil actions leading to substantial monetary recoveries and "charitable" endowments of work already done.*

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[135] Some firms have been debarred even though they never applied to the SCA for prequalification. For example, if the Inspector General learns that a firm is subcontracting on an SCA project as a non-Wicks subcontractor (which need not be prequalified) – it may, based on negative information that it has learned, undertake an integrity review of that contractor, and debar it. The firm, however, may never have applied for prequalification.

- It created a critical mass of data over which the Inspector General sat astride and gave it, in large measure, the currency it needed for effective "horse trading" with other agencies. *The requirements of prequalification led to the bold use of public and private data sources and banks for investigative purposes in a manner perhaps unparalleled by a civilian agency. It induced its frequent use by its investigative partners; and established the Inspector General as a major and central source of vital information on the activities of the industry, its contractors, and the SCA itself.*

- It lowered the cost of information gathering for law enforcement agencies and others, and provided unique access to the industry and SCA. *In so doing, it reduced the risk and increased the value of law enforcement's own investments in making construction industry cases, and induced the active participation of law enforcement agencies and others on behalf of SCA purposes. In the exchange, the SCA acquired unique access to information about crime and corruption in its midst, leading to an important series of procedural reforms, and to the rapid interdiction and containment of costly criminal activity impacting the SCA.*

- It created an increased likelihood of detection for the corrupt or criminal activities of employees and contractors, and created significant penalties for those caught plundering the SCA. *In so doing, it raised the price of crime for employees and contractors who sought to plunder the SCA's building program; in establishing a credible risk of discovery and prosecution, it added to the deterrent force of the SCA's efforts. Monetary recoveries, prison terms, fines, debarments, and seizures of work performed without further payment or compensation were among the instruments of punishment devised or used by the Inspector General and its enforcement partners.*

The Keys to Success

One might not have predicted such results merely from looking at the organization structure of the Inspector General's office.

The staff was small -- 50 attorneys, investigators, civilian professionals, clerical and administrative staff policing a $4.3 billion building program, and operating in each of the five boroughs of New York City. The organization itself was structured in a typical command-and-control manner, much like larger law enforcement bureaucracies. Like these bureaucracies, the office structure was bifurcated between civilian and sworn personnel, with the Intelligence and Research Analysis units on one side to undertake vendor prescreening and procedural reform/review; and the investigative units on the other side to pursue civil and criminal inquiries. The structure also took pains to address the legal issues in sharing information across civil and criminal units in the same office. In this

As a practical matter, the Inspector General argues that such conflicts are really only theoretical, and that in the long run, its objectives and the SCA's are identical to meeting the objectives of the SCA to build quickly, inexpensively, and cleanly. The reason is that many of the apparent benefits of going along with corruption, or failing to install appropriate safeguards, will really end up not being worth the gains. In the loopholes created, poor-quality construction will creep in and more than offset the apparent gains in speed and economy. The only way to ensure high-quality, low-cost construction over the long run is to wring crime, corruption, and racketeering out of the industry.

Still, to deal with these potential tensions, the SCA and the Inspector General worked hard to ensure that they operated as a single entity with a common purpose in the short and long run. The Board of Trustees and the president/CEO, as overseers of the entire organization, explicitly assumed the responsibility of balancing and merging the interests of the Inspector General in the context of the SCA. In addition, however, the office of the Inspector General itself was organizationally positioned so that it would also have to weigh these competing demands. The Inspector General wore two hats, one for his responsibilities as Inspector General and another for his position as a senior vice president. The Inspector General's second hat -- his SCA hat -- was intended not only to give him the power and opportunity to obtain internal SCA information and implement internal reforms, but also to give him a sense of obligation to the SCA's objectives of building quality schools quickly and inexpensively. The assumption was that if the Inspector General wore those two hats, the office would not act to block corruption without also weighing whether its actions were undermining, or causing undo harm to, the wider SCA objectives.

Indeed, the SCA was careful to structure the Inspector General's reporting relationships so that the Inspector General was at once both reasonably independent from the SCA's hierarchy and yet subordinate to its purposes. One of the unique features of the SCA's Inspector General's Office is, in fact, its *lack* of independence from the SCA. As discussed earlier, this arrangement overturns the traditional view that inspectors general should be organizationally separate from the operations they inspect in order to assure that the Inspector General's investigations are not compromised by the very people who might be the subject of, or disadvantaged by, those investigations. Frucher, Steisel and Thacher were persuaded that making the Inspector General a senior corporate officer *in* the organization, reporting to the president/CEO, would give that office influence over the Authority's policies and procedures, assuring that the reforms it proposed, such as the examples cited above, would be incorporated into the Authority's operating procedures.

This reporting relationship precluded SCA officers who believed the Authority should be driven solely by construction-related concerns, rather than ethical concerns, from thwarting the Inspector General's initiatives. When the Inspector General obtained

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$700 million the first year, a little less the second. If this, and the recession, hadn't occurred, maybe the construction industry would have balked at us. But we were the biggest game in town, and the only game for some." Thomas D. Thacher II, interview (1992).

incriminating information about a company after the firm had been awarded a contract, for example, SCA's Contract Administration Office might maintain that the company, having passed the prequalification test, should be allowed to carry out the job. The Inspector General's office, however, concluded that incriminating information should not be overlooked even if it developed after prequalification was complete. With the president supporting the Inspector General's position in these cases, the Inspector General prevailed.

The SCA structure also included a safeguard against the rule of a president who might choose to make ethical issues a secondary concern. This safety valve was the Inspector General's direct reporting relationship to the Board of Trustees, which appointed the president. And though it was effective in securing the formal independence of the Inspector General even within the SCA context, the Inspector General's direct report to the Board sometimes undercut the Inspector General's relationship with the SCA's senior officers, and sowed seeds of distrust among them. On the one hand, the Inspector General was privy to the most sensitive information pertaining to the counsel's office, contract administration, operations, and other units, which was shared when the vice presidents met as a group with the president. On the other hand, the Inspector General, unlike the SCA's other vice presidents, was also meeting with the trustees.

This unique arrangement gave rise to the perception among the SCA's senior officers that the Inspector General, if he chose to, could easily undermine them when he met with the trustees, and that he could not, therefore, be completely trusted. "This guy [the Inspector General] can grab his sandwich and run over to the trustees and have lunch -- and eat with us as well," a former senior SCA official remarked. the Inspector General thus developed a reputation, in some quarters within the SCA, as an internal spy. Also feeding this perception was the view that the Inspector General's Office was constantly on the search for wrongdoing within the SCA. "I'm sure he knows everything that I do, because that's what Inspectors General do," a senior SCA officer remarked.[141]

The Inspector General's dual reporting relationship also had the potential to undermine the authority of the SCA president/CEO. In the event of an irreconcilable disagreement between the Inspector General and the president, the Inspector General, who was otherwise subordinate to the president, could circumvent the president by dealing directly with the Board of Trustees. Although the Inspector General's reporting

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[141] Thacher recalled that originally he had sought vice president status because "the Inspector General needs muscle." Some years into the job, Thacher viewed the rationale differently. "With hindsight, the reason for being vice president is to take on the broader view - to build cheaper, faster, better, with criminal enforcement powers as one of the many tools." As vice president the Inspector General is "sensitized and exposed to broader issues, and strengthened as an SCA operator on behalf of his shop." The Inspector General's title also gives the Inspector General opportunities for authoritative exchanges with his colleagues. "We can share information we have with other vice presidents as to the potential problems of their operation, including the benefits from fixing it." The Inspector General's office "often knows of hidden problems on their projects. Project managers are constantly whispering in our ear -- 'Know what the construction manager is doing?' Not crimes, but the beginnings of crimes. This information is extremely valuable to authorities." Thomas D. Thacher II, interview (1992).

relationship to the trustees was intended for situations such as this, it became apparent, in practice, that the trustees might not be able to overrule the president without undercutting his authority, if not destroying his effectiveness in the job. Moreover, the Inspector General, even without a direct line to the trustees, would have the option to appeal a decision of the president to the Board.

These were all devices designed to ensure that the Inspector General's goal of helping the SCA buy and build clean would be given substantial weight inside the SCA, and thus make it a particular kind of buyer among the public construction agencies of New York City, and within the broader industry. But the reporting relationships were also designed to ensure that the Inspector General would weigh his immediate objective of keeping SCA construction corruption-free against the SCA's operational objectives to build quickly, effectively, and at lowest possible cost. They sought to ensure, over time, that the Inspector General did not stray too far from the path of ensuring the success of the SCA's program, and relying on that success as a principal means to get leverage on the broader objective of reforming the public construction enterprise in New York, and weakening organized crime.

The E.W. Howell matter, referred to above, illustrates the Inspector General's management of this dual obligation. In 1990, the E.W. Howell Company Inc. was awarded an SCA contract to construct a public school in Manhattan. Sometime thereafter Howell submitted the low bid on another SCA school construction project in Queens. During the course of its review of Howell in connection with the second contract, the Inspector General discovered that Howell was under criminal investigation for labor racketeering, illegal billing, and embezzlement.

the Inspector General could have used SCA guidelines to reject the second bid, suspend Howell's prequalifications, and terminate Howell's first contract. Had the Inspector General opted to stop Howell from completing the construction work it was doing, and doing very competently, in Manhattan -- as its guidelines indicated it should -- that project would have been delayed considerably while another contractor, perhaps one that did poorer quality work, was found to substitute. Moreover, debarring Howell -- which the Inspector General's guidelines also called for -- would have entailed awarding the Queens construction project to another bidder, adding more than $2.5 million to the construction price of the school.

Rather than blindly invoke its integrity option, the Inspector General used one of the interim control strategies in its tool kit to balance the integrity requirements and opportunities of the moment against the interests of building schools quickly, effectively, and inexpensively. Rather than debarring Howell outright, the Inspector General reached an accommodation with Howell that compelled the company to hire an Investigative Auditing Firm. This permitted Howell's work to continue on the Manhattan school, while protecting the SCA from any future criminal activity on the firm's part.

Working With Enforcement Agencies

Given that the Inspector General itself had limited authorities and few resources compared to its charge and scope of operations, how could it induce other entities and agencies to mobilize their authorities and commit their resources on behalf of SCA interests? The Inspector General's office itself had no law enforcement authority. To accomplish its purposes it would nonetheless need to reap the investigative and information benefits of those authorities *as if it did*. What steps could it take to access and influence law enforcement agencies towards this end? How could it overcome law enforcement's traditional mistrust of non-law enforcement personnel; its reluctance to share confidential information across its own desks let along across agencies; its interest in making "big" cases, though smaller cases and other matters might be of great concern to the SCA; and its own concern to husband and make valuable use of scarce investigative resources among specialized units?

There were, it turned out, five keys to the Inspector General's success with external agencies:

- Relationships
- Cross-designation
- Rapid, prestigious case-making
- Financial support
- Lowering the cost of making cases and the value of the return

Relationships

It is apparent that the network of relationships that the Inspector General's staff brought to the office early on achieved the intended effect of establishing their law enforcement bonifides on behalf of the SCA. No one in the law enforcement community could or did question their pedigrees. Among key enforcement agencies, the relationships the Inspector General's staff imported and soon enhanced conferred upon the office an initial outlay of good will, trust, and cooperative spirit on which the office was able to capitalize effectively.

Cross-Designation

The first benefit of the relationship network they imported and enriched was the willingness of agencies to cross-designate Inspector General investigators into their own agencies. This immediately gave these investigators the authority to share in the agencies' legally restricted work product and confidential investigations. It is our view that absent the authority of cross-designation, no information interchange could have occurred of the kind that did, whether for the purpose of prequalification or for investigating target

companies; and no relationships would have been further forged, as in fact they were, in the pressured work of "sitting wires" and the other shared sacrifices and victories of making cases.

Early Successful Case-Making

The second benefit of the relationship network was apparent in the Inspector General's standing with the United States Attorney for the Southern District of New York, and the relative comfort the Southern District apparently felt in placing cases with the Inspector General. It was fortuitous that this case-making began in earnest so early on in the "game," as it quickly gave the Inspector General's office status on a high rung of the law enforcement ladder in New York. In producing a rapid succession of good cases, it validated the extension of the Federal cross-designation authorities to the Inspector General's staff, and drew further cases and personnel to the Inspector General's office. "Nothing succeeds like success," Thacher observed of these early case victories.

Financial Support

At the same time, another investment The Inspector General made in a structural innovation was reaping fewer dividends. While the OCTF team that the office funded was frequently active in cases, the New York County District Attorney's team produced fewer results during its startup years of operations. Both teams were expensive: $250,000 per year each.

Nonetheless, it is our view that as a strategic investment, the sums that the Inspector General transferred to OCTF and to the New York County District Attorney to underwrite teams provided the Inspector General's office, and the SCA, with concrete benefits. It conveyed a positive image of the Inspector General to law enforcement: clearly the SCA trustees had amply bankrolled his operation and it was here to stay. And by drawing OCTF and New York County District Attorney teams to his office, it sent a tangible message back to the SCA trustees and president: the law enforcement community had faith in the Inspector General and its mission, and was willing to speculate on its success.

In assigning its teams, it was evident that OCTF and the New York County District Attorney assessed the risks of investing in the Inspector General in its favor. There was nothing charitable, however, in their participation. The Inspector General eliminated the need for startup capital by providing its own. The District Attorney retained command-and-control over its team and could assign it to other office matters as might be required. Lastly, there was the promise of the anticipated successful investigation and prosecution of racketeers and racketeering in the construction industry.

In achieving this prestigious venture backing from law enforcement early on, the Inspector General enhanced its credibility and standing in the SCA organization. In these early steps Thacher delivered the relationships that he had been expected to establish. [142]

Lowering the Cost of Making Cases and Increasing the Value of the Return

Ultimately, relationships must deliver on the promise of improved performance. For investigators and prosecutors, this meant facilitating their mission to make cases, and to impact organized crime. [143]

Against the backdrop of city crime pressing on investigators and prosecutors, construction cases are unattractive to prosecute. They are technically difficult, requiring sophisticated expertise not readily found in law enforcement agencies. They are time consuming, and so costly of resources and long on showing results. They typically involve a corporate victim, and rarely a "heinous" violent crime. They appear, altogether, to be costly to undertake, and to promise little worthwhile. As they occur in a highly regulated market, it is possible for grievants, in any event, to seek redress in civil courts and to leave it to private attorneys and civil juries to deal with the rampant frauds.

In spite of law enforcement's low interest in construction cases generally, with their high cost of buy-in and the low-level of valued return, The Inspector General induced the early and active participation of these agencies in SCA-related matters. It was able to provide investigators and prosecutors with insight into SCA operations, into the business practices of the construction industry more broadly, and into the structure and process of the frauds, corruption and racketeering that plagued them; with access to informants, meetings and conspiracies; with access to technical experts in construction and forensic engineering; with access to increasingly rich data bases on individuals and firms doing business in the public markets; with access to allied professionals involved in both civil and criminal aspects of identical and related cases; with access to crimes and criminals themselves; and with the ability to influence SCA operations on behalf of investigative purposes.

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[142] It is typically a critical feature of new businesses and industries forming in competitive markets that credit be available, through which entrepreneurs can acquire the assets of established firms and industries for their own use. In market transactions, banks perform this role. The analogy to Thacher's situation is intriguing. See, Bruce Kogut, Weijian Shan and Gordon Walker, *The Make-or-Cooperate Decision in the Context of An Industry Network*. In Nohria and Eccles, *Networks and Organizations*, 1992: "The ability to issue public equity is an indicator of a firm's legitimacy...[O]rganizations vary in the extent to which they are granted institutional legitimacy...only firms with strong product-development portfolios can attract investors to purchase the equity."

[143] See, for example, Stephen R. Barley, John Freeman and Ralph C. Hybels, *Strategic Alliances in Commercial Biotechnology*, in Nohria and Eccles, *Networks and Organizations*, 1992: "Organizations must engage in exchange if they are to survive. An organization may turn to some organizations for financing, to others for personnel, and to still others for information, raw materials, or political support."

These were potentially invaluable gains. Compared to law enforcement's investment in other construction agencies' cases, or in other investigative cases more broadly, these attributes of case-making with the Inspector General lowered law enforcement's initial costs and risks, and improved its results. Knowledge, information and context could be had relatively inexpensively, including at a greatly reduced likelihood of exposure. The key was that, on a day-to-day basis, the institution of the SCA Inspector General provided a place on the map, which had never existed before, that provided investigators with a swift and certain means to assess the value of information they gathered in construction matters. The Inspector General's office was a place where IRS investigators with a frayed tip about bid rigging in school construction *which would very likely have fallen by the wayside* might, instead, see it develop into one of the most significant public construction prosecutions in the city's history. Investigators who might otherwise be stymied or who would toss off criminal information as worthless could, as these investigators did, instead harvest more of its full value.

As a result, law enforcement and other agencies working with the Inspector General could expect that even a low level of investment could garner impressive results. Indeed, the more agencies threw at an SCA case, the higher might grow the per unit return to their investment. For the synergies engineered by the Inspector General's office were such that, for example, small increments in the commitments by external agencies of legal or investigative resources could leverage enormous additional returns on the civil side of monetary recovery. When the Inspector General's Counsel knew the case requirements for successful civil monetary recovery and helped guide investigations towards establishing the necessary predicates, it could make it *easier* for civil attorneys at the City's Corporation Counsel to prosecute these cases successfully.

It is probably true that for some prosecutors who were concerned to make "big" organized crime cases in the construction industry, some initially prosecuted minor cases as a cost of doing business with the Inspector General, which promised bigger and better things. It was probably also true that, in some matters, their work with the Inspector General involved cases that they could otherwise have brought to court, even without the Inspector General. Indeed, in 1991 New York County's Cherkasky said, of his cases to date, "I don't think there's any case that I would say couldn't be made otherwise." [144]

Ultimately, the test of value of the Inspector General's contribution to law enforcement's case making ability (and to the work of other agencies involved in Inspector General matters) was not whether law enforcement *could* or could not otherwise make a case. As is said, "everything is within walking distance... depending on whether one has the time." The test, rather, is whether given the cost of making cases without the benefit of the Inspector General, the prosecutors' offices *would* have -- and in the debate over appropriate use of scarce resources, *should* have -- made those cases.

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[144] Michael Cherkasky, Office of the New York County District Attorney, interview (1993)

As not every murder case is the next "Son of Sam," construction cases, too, run the gamut of seriousness. Though prosecutors might have been drawn to the SCA in anticipation of making the "mega case," it is rare that prosecuting individual contractors that colluded with others to inflate bid prices rose to that level. *It is also true that to police the construction industry effectively requires establishing a credible threat of detection and deterrence at all levels of crime and corruption affecting it.* It was to the SCA's great advantage, therefore, and to the Inspector General's credit, that it induced law enforcement to prosecute all manner of crime occurring in the SCA's midst.

Why The Inspector General Was Valuable To The SCA

The Inspector General helped make it possible for law enforcement to add value to information already in hand at little or no cost. Moreover, because the Inspector General lowered the costs of getting it and increased its value in use, the office provided a natural inducement to gather more. In so doing law enforcement was clearly able to make more cases, more efficiently for its own purposes than it otherwise might have; and its activities helped the SCA, through the agency of the Inspector General, fix the SCA's procedures, disqualify unscrupulous contractors, and secure SCA operations. As a public investment, the institution of the SCA Inspector General, in our view, added value to the public dollar spent both on law enforcement, and on building schools

Had the Inspector General been unable to broker this complex role between the civilian side of building and the sworn side of enforcement, it is doubtful, in our view, that law enforcement agencies would have continued to work with the Inspector General. Rather, they would have pursued matters, in their customary opportunistic hunt-and-kill fashion, on their own, with predictable and disastrous results for the SCA.

Without the Inspector General, the SCA would have been hostage to the unilateral case-making decisions of law enforcement as opportunities arose. At the very least, Thacher would have risked being perpetually behind the wave, reading about SCA criminal cases over morning coffee along with the SCA trustees. At worst, the SCA would have been hostage to a predictably lower level of overall case-making, with prospectively much greater collateral damage to the SCA's building interests and public stature, and to much enhanced overall crime and activity levels of racketeers at the SCA trough.[145]

With the Inspector General, and as a result of the inducements it was able to provide, the SCA stayed in the game. The Inspector General's ability to horsetrade its access and information enhanced its ability, on behalf of the SCA, to gain access to law enforcement information, and to use it to fix SCA procedures during and after investigations. With this information, the Inspector General prevented needless monetary

[145] "Many IG's will duck behind the prosecution," Thacher recalled, "and not protect the host agency. Or, they are even precluded from telling the agency so it won't get victimized, even as we are, in principle, at least *able* to tell the SCA." Thomas D. Thacher II, interview.

hemorrhaging and damaging construction debacles, minimized Monday-morning embarrassments, and influenced law enforcement investigations to enhance SCA purposes of building quickly, cheaply, and well.

Having now five years of cases in the Federal and state courts, it is safe to say that the risk of making cases with the Inspector General is consistently low enough, and the benefits on traditional prosecutorial scales of value high enough, that there is interest and enthusiasm in the region's enforcement agencies for continued involvements with the Inspector General. In that respect, the Inspector General appears to have succeeded in bringing to bear on behalf of SCA priorities and operation the capabilities of the region's key enforcement agencies, creating an environment in which the inducements to participation, and its benefits, are now a matter of record.

Lowering The Cost Of Buy-In To Construction Industry Cases Generally

We suspect, also, that the Office of the Inspector General reduced the barriers to entry for law enforcement in other, non-SCA construction industry cases. The law enforcement investment in the Inspector General, and the strengthening of its databases, substantially lowered the information-gathering and analysis cost of case-making in the construction area broadly. Names, firms, players were already well-documented. The cost of buy-in for any new case, in this respect was relatively low, requiring little large "capital" outlay by any individual agency. The community outlay for data gathering and analysis had already been made, in essence, at the Inspector General's co-operative in the Bronx. The community sense of construction industry cases as feasible to make, and as appropriate objects of law enforcement concern, had also been established. This further reduced the burden on investigators and prosecutors having to pitch their superiors for commitments of resources on construction industry cases.

In the language of economists, the Inspector General's operation therefore reduced the law enforcement's barriers to entry to other, non-SCA construction industry cases in at least two ways. By absorbing the significant capital costs of investment itself, the Inspector General reduced the capital requirements for buy-in -- and the risk posed for that capital -- for any law enforcement agency wanting to make cases in construction. By 1995, the cost of buy-in on the data gathering and analysis side of case-making was almost entirely limited to horsetrading information on a case-by-case basis. Second, Thacher's office impacted the scale economies of case-making in the construction industry as a whole: having established the data bases for SCA matters, there resulted a decline in the per unit cost of the next case made. Whether and how law enforcement took advantage of this "market condition" remains for a future evaluation to determine.

Six Significant Gains

The innovation of the Office of the Inspector General was more broadly important in six significant respects:

- It advanced the model of the inspector general as we customarily regard it.
- It demonstrated a functional model of a network organization for law enforcement which has significant implications for multiagency work across organization boundaries.
- It confirmed the value of multijurisdictional approaches to dealing with complex problems of crime and racketeering impacting key public institutions.
- It stimulated important innovations in racketeering control tactics and technologies.
- It demonstrated the means by which past performance could valuably enter into substantive contract award decisions without, apparently, adversely affecting procurement metrics.
- It broadened our understanding of organized crime control measures and added to that inventory a class of *victim-oriented strategies*. It highlighted, also, the broad strategic and high social value of the defense of key public institutions as the cornerstone of crime-fighting strategies.

Advancing The Inspector General Model

Strategically, three aspects of the invention of the SCA Office of the Inspector General were striking.

First, unlike the traditional model of "inspectors general," the SCA Inspector General was primarily concerned with the threat of crimes such as corruption and racketeering, whether from within or without, whether opportunistic or enterprise. The office was decidedly *unconcerned* with the relatively trivial matters of employee malfeasance that was a customary concern of such offices. The SCA Inspector General was thus concerned to establish interfaces both *outwardly* toward non-SCA agencies with whom it would partner, and *inwardly* toward SCA units such as Contract Administration where critical procedures shaped up the day-to-day business of the Authority. In this way the Inspector General could, from its unique vantage, both peer behind the agency ramparts to see who, secretly or negligently, was opening the door from inside the Authority; peer over the ramparts to see who was coming from the field, and if necessary

raise the drawbridge; and forge alliances with other agencies in the field to disable would-be racketeers some distance from the SCA, and dissuade others from attacking it.[146]

Second, it *did* borrow from the traditional model of the inspector general the primary attachment to the host organization, the SCA, which was the likely and expected victim. But the Office of the Inspector General carried this attachment beyond the traditional model. While maintaining an external, semi-autonomous posture, the Inspector General also served as a senior corporate officer of the SCA -- one of its five vice presidents.

Third, it's role was clearly defined as being both to advance the overarching purposes of the SCA to build quickly, inexpensively, and well, and to make sure that it bought and built cleanly. Frucher, Steisel, Thacher and DeLuca carried out their own trade-off analysis and concluded that the risk of creating such a visible entity was worth the responsibilities it entailed; and that the risk, even, of burdening a construction program with racketeering and corruption controls far outweighed the risk of building schools without them.

They thus created a single entity with unique responsibilities of its own: to prevent the Authority from falling victim to corruption and racketeering -- even while it shared overlapping interests with the SCA, on the one hand, to build quickly, inexpensively, and well, and with law enforcement on the other to make cases. *In this sense, the Inspector General had the unique responsibility to optimize across building and enforcement purposes where neither of its principal partners -- neither its host, the SCA, nor the plethora of law enforcement agencies it dealt with -- ordinarily could have, or would have done so on their own. Where before the requirements of public builders and enforcement agencies seemed incompatible and in potential conflict, the Inspector General captured and held a solution to the conflict, achieving its own purposes while advancing the unique and peculiar interests of its partners.*

In these respects, the innovation of the SCA Inspector General was striking and advanced the models of both "inspectors general" as well as strategies for organized crime control in important and interesting ways.

Innovative Architecture: The Extended Network Organization

From this volatile mix of sometimes complimentary and often competing interests arose an extraordinary joint venture, organized as an extended network organization, and run, *de facto*, by Thacher from the Inspector General's office.

What might be said about this organization?

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[146] For a comprehensive discussion of competing models of inspectors general organization and strategy, see, Moore and Gates, *Inspectors General*, 1986.

Many Players, Some At A Time

At the outset, it should be noted that the extended network organization involved numerous agencies, some more active than others at different times, depending on the issue that the Inspector General faced or felt pressured by. It included the host agency itself, the SCA, and its numerous operating departments; the Office of the Inspector General; and numerous Federal, state and local law enforcement agencies, among others.

Not all partners played the same role in every matter. Indeed, as cases ebbed and flowed, or as new responses were required to address emerging problems and opportunities, some partners played a lead role and others a supporting one or none at all. The flow of information and work products was typically quite dynamic, established by the needs of the moment, based on cases and information that were developing, rather than on an overriding plan. Unlike the bureaucracies from which each partnering agency's units were drawn, the extended network organization tended to mold itself to each problem anew rather than to process all problems with a fixed set of approaches. [147]

Optimizing For The Public Good

As the extended network organization evolved, it straddled civilian and law enforcement worlds, with their different authorities, resources and skills. It housed numerous professions, each with a unique view of the terrain and contribution to make. It bridged the worlds of public building and prosecution, with their quite different priorities for building, on the one hand, and case making on the other.

The Inspector General's office established itself as the network organization's hub. Whether by force of statute or the realities of complex case-making, at some point in their process many SCA procurement, contract administration, and project management staffs, and many of the region's investigators and prosecutors, passed through the Inspector General's office in order to do their business. Once there, working with the Inspector General, each partner's objectives (or values) acquired a certain standing that they could not have easily acquired others. The partners' objectives and purposes gained notice, and exerted influence over the others. As the extended network organization acquired

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[147] See, Wayne E. Baker, *The Network Organization in Theory and Practice*. in Nohria and Eccles, *Networks and Organizations*, 1992. "The chief structural characteristic of a network organization is the high degree of integration across formal boundaries... A network organization can result naturally from integration-producing forces such as the task and environmental characteristics... or from the intentional use of integrating mechanisms -- formal liaison positions, multifunctional task forces, ... and so on -- that tend to offset disintegrating forces." See, for a discussion of the relationship between external ties and internal management of private firms, Robert G. Eccles and Dwight B. Crane. *Doing Deals: Investment Banks At Work*. Boston, MA: Harvard Business School Press. 1988. Pp. 36-52.

increasing purview over matters, *it commanded attention among all the partners to each individual partner's standards and priorities.*

As a result, and by a variety of means, the network organization gained influence over the conduct of partners who used it. It tempered their pursuit of narrow agency interests on behalf of a larger set of network organization purposes. These purposes incorporated the shared and divergent objectives of the venture's partners.

In moderating the conduct of its venture partners, the network organization corrected for the past excesses of both builders and prosecutors. Formally, for example, the Inspector General imported to the SCA's vendor selection procedure an unheard of prosecution-grade standard of "clean." Informally, the Inspector General's office moderated the myopic pursuit of investigations that, in being blind to or indifferent to SCA's core mission, could have damaged SCA's credibility and school-building capability.

Over time, the Inspector General's mission emerged as authoritative in mediating among the potentially conflicting goals of public construction and enforcement, insisting on their convergence where possible. The office came to stand for that broader set of public purposes for which no single agency stood. Although it changed their operating procedures minimally, work in the network organization moderated individual agency activities there to a *de facto* higher standard: not simply to build, but to build cleanly; not simply to make cases, but to address structural and system weaknesses that gave rise to racketeering susceptibility and potential in the industry.

It must be said that managing such a complex position put the Inspector General astride a herd of wild horses, each used to going it alone, each possessed of strong, single-minded purposes. It required strong leadership and diplomacy at all levels of the Inspector General's operation. There is little love lost between builders and law enforcement in New York City, and less trust. Yet armed with statutory compulsion and situated high in the formal SCA organization, on the one hand, and effectively leveraging enforcement wherewithal and borrowed authority on the other, the Inspector General established itself as credible and effective with both law enforcement and the SCA alike.

Making SCA Cases Easier And Desirable To Pursue

The Inspector General used its position at the network organization hub to make SCA cases attractive to law enforcement, and to induce its participation. The Inspector General did this by lowering law enforcement's risk and its capital costs of buy-in to SCA cases, and by providing synergies in making cases that increased the return on law enforcement's investment.

To be sure, the Inspector General's rapid success helped make its office attractive to work with early on. In its first cases with the Southern District the Inspector General proved itself to be no mere regulatory backwater. It was unlike other inspectors general

offices. Rather, it was a new and active *law enforcement environment* where cases were being made, and where relationships, futures and connections might be established, too.

Yet the Inspector General's priorities were focused on its client: to strengthen, protect, and reform the SCA program. The office recognized that while many law enforcement cases might be valuable for it to pursue, prosecutors' would not share its own priorities. The Inspector General expected prosecutors to focus on making big cases against long-time mob figures. Indeed, left to law enforcement's customary standards, few of the Inspector General's targets would ordinarily pass law enforcement's "sniff test" of seriousness, or lead to significant commitments of time and resources.

Initially, luck, good timing, and the Inspector General's access to the SCA and its window to the industry worked in the unit's favor. They drew law enforcement to the unit early on in major cases of interest to both parties, such as Operation *Tightrope*. Since then, the Inspector General has also, from time to time, helped investigators and prosecutors make cases that have had little direct impact on the SCA. And soon after its start up, cases began to develop that focused exclusively on the Inspector General's priorities. [148]

Over time, as contacts and work products increased, the Inspector General's organization was able to add value to diverse construction cases, proffering a growing network organization of professionals it could tap, and a burgeoning information cache it controlled. The Inspector General, in organizing the defense of the SCA, used its limited assets to induce growing law enforcement participation, which further strengthened the Inspector General's position and bolstered the network organization, which helped the Inspector General lower law enforcement's case-making risks and costs further. It was part of horsetrading.

Inducing law enforcement to prosecute major cases was never an issue: there was already plenty of law enforcement interest for that. For SCA purposes, rather, the problem was how to capture law enforcement's attention to *its* complex conspiracies, as well as to the little cases that, though not serious on the traditional law enforcement scale, nonetheless had real consequences to the SCA if left unattended. So it was especially important for the SCA that the Inspector General's office lowered the cost and increased the return to case making for law enforcement *across the board*, since it made prosecuting everything from the SCA's complex conspiracies to its run-of-the-mill chaff cases relatively feasible.

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[148] The Queens' DA's prosecution of the prevailing wage violations in the BQE matter was such an instance. In that case, Thacher was concerned to send a message to the contracting community, making it clear that the SCA would prosecute *any* bribery, even if the case involved an amount as low as $100. Few major law enforcement agencies have much interest in such a message; this was a case that prosecutors would ordinarily shun, and Thacher recognized that. But the case mattered to the SCA. Thacher's investigators had done the legwork, packaged the case, and lowered the cost of casemaking to the DA. As a result, the Inspector General was able to induce a higher level and quality of law enforcement assistance than it would have received otherwise.

The net value to the SCA was clear. The Inspector General, in effect, established SCA construction cases as matters of greater value to law enforcement compared (a) to other cases in law enforcement's portfolio that required similarly low investment -- but which could not promise the same return; or (b) which promised as high a return, but could never be gotten for the same low investment. The definition of a serious case for law enforcement did not shift; but by creating inducements for law enforcement that lowered its buy-in costs and improved its return, the Inspector General created many valuable opportunities for law enforcement at a discount to its usual costs

The effect was to permit the SCA's standard of case seriousness to co-exist with law enforcement's traditional standard. The *de facto* standard was driven, in large measure, by the institutional needs of the Inspector General's client, the SCA host organization. The SCA, through the Inspector General, drew law enforcement away from an exclusive and narrow focus on dangerous offenders charged with heinous crimes, *towards the SCA's own definition of seriousness, one that derived from the impact of crimes on the institution's vitality and its continued ability to operate.*

Multijurisdictional Approaches: Marshaling Combinations Of Powers To Match Problems

The Inspector General's resources were not only those of its own 50-person unit, but those of its network partners', too. The extended network organization gave it access to a tool array that was as complex and varied as were the legal and operating issues facing the SCA in the field. Through cross-designation, for example, the Inspector General "borrowed" law enforcement powers from the partnering agencies, and had no need to acquire more. Whether in civil litigation, loss prevention, operations analysis, forensic accounting and engineering, or other matters, the extended network organization similarly permitted the Inspector General to leverage the SCA's and other agencies' and firms' talent bases, authorities and staffs from around the region.

The *architecture* of the extended network organization permitted their effective use. Though highly distributed, the tool base was not distributed entirely outward; nor was it concentrated in the center at Inspector General headquarters in the Bronx. Rather, the extended network organization appeared to have achieved "scale without mass." Its diverse powers and resources could rapidly be called upon and deployed; be used for limited duration and purposes without incurring overhead costs; rotated or adjusted to suit a changing need; mobilized by telephone, or brought in for hands-on work and meetings.[149] With the Inspector General directing, or rather orchestrating, the office capitalized on the assets available to it throughout the network to create favorable returns

[149] For a discussion of the factors giving rise to network organizational architectures and sustaining joint ventures, see generally, David Nadler, *Organizational Architecture*, 1992, especially the chapter by Charles S. Raben, "Building Strategic Partnerships: Creating and Managing Effective Joint Ventures."

for its investors/partners, *by their own standards of value*, whether these assets were drawn from within the SCA itself, or the worlds of civil litigation or criminal law enforcement, or elsewhere.

It would be interesting, but beyond the scope of this evaluation, to determine the value of the non-SCA resources leveraged by the Authority through its investment in the Inspector General's office. It is in all likelihood substantial.

Collapsing Organization Boundaries

The extended network organization lowered boundaries among the organizations doing work within the network. People traded information, access, expertise, and resources. They discovered mutual interests in cases that were being approached from entirely different perspectives. In the press of making cases, whether civil or criminal, they came to depend on their access to expertise and resources found in the network organization.

Where units shared physical organization space at the Inspector General's office, those boundaries were further reduced. Where units remained physically distinct, as the New York County District Attorney's team more often did, it was more difficult to engage in the regular exchange of information that built relationships of collaboration and trust. Physical proximity, frequent exchanges of information, and successful joint case-making appeared to lower boundaries, and helped venture partners overcome the natural issues of ownership, turfism and suspicion that made the boundaries separating their parent units so difficult to breach.

Two information channels were especially critical in collapsing organization boundaries. First, on any given case, *cross-designation* effectively collapsed the boundary between the Inspector General and law enforcement agencies. Cross-designation permitted information exchange on confidential and otherwise legally-proscribed matters; it facilitated a shared investigative work product; it conferred formal law enforcement standing and status on Inspector General staffs. Over time, the cumulative effect of numerous cross-designations repeatedly collapsing boundaries gave the Inspector General's operation the look and feel of a law enforcement agency. In the language of Kipling, cross designation was how the leopard got its spots.

Second, the fact remained that the Inspector General's office was structurally and procedurally attached to and part of the SCA host. The Inspector General and SCA had numerous points of tangency, interface, and active relationships with the SCA host. Foremost among these relationships was Thacher's own with the President and the trustees, buttressed by his dual reporting relationship and his status as Vice President. Information and impact flowed to and from Thacher, and from him, to and from the Inspector General's office and external law enforcement agencies.

The boundary lowering included, by implication, that between the SCA and law enforcement. With the Inspector General brokering, law enforcement information effectively reshaped SCA policies and procedures. SCA actions propelled discussions of investigative strategies and opened doors to investigative opportunities that probably would never have been available to law enforcement otherwise.

Had only one of these channels been open -- had there been, for example, cross-designation into law enforcement but no access and impact on SCA policies and procedures, or SCA impact but no cross-designation -- the value of the Inspector General's office would have been substantially diminished. With both channels open, the information flow and the access backwards and forwards between law enforcement and the SCA was enhanced. The Inspector General's office was positioned to further reduce the resilience of the boundaries separating inside from outside, builder from prosecutor, to each institution's great advantage.

Increasing Integration

In the real world of enforcement, there is ordinarily high fragmentation between investigative and prospective functions; between civil, regulatory and enforcement efforts; and sometimes strident cultural and professional differences among professional legal and investigative staffs. As a result of the flow of work and information across organization boundaries throughout the Inspector General's network organization, the enforcement response itself became more integrated across its own units.

The Inspector General provided a means where, as network "coordinator," it might referee and consolidate the activities of each network partner on behalf of the Inspector General and the SCA. There was value to be gained in achieving greater integration, and the Inspector General held this out as an inducement to partners seeking ways to lower their costs, or to create more value from their current efforts. Working through the Inspector General's network, every partner would find its own work strengthened -- and its interests addressed -- by virtue of the close proximity to others and the information sharing that doing school construction-related work made possible and required. Whether it was prosecution, criminal investigation, civil recovery, or loss prevention and procedural reform, work that might typically be done in a vacuum, isolated from other partners, in fact drew from their strengths and skills. It is interesting that although nominally the weakest of all partners in terms of legal powers and staffs, the Inspector General became influential, even powerful, in shaping the priorities and activities of the partners.

Stimulating Innovation And Invention

The extended network organization's flow of authorities, resources and skills across organization boundaries created exposure to new problems and appeared, also, to

stimulate a wide range of innovative approaches to protecting the host from falling victim to crime. The introduction of certifications, for example, as a precondition to doing business with the SCA, represented an innovative means to reconcile the need for control over suspect vendors with the need to get buildings built and to conserve investigative energies. On the one hand, it provided the Inspector General with an extraordinary level of control (and information about the suspect firm) during the contract period. On the other, it permitted the Authority to do business with questionable firms, even as the certification lay traps no "dirty" firm could avoid for long.

The introduction of the IAF -- essentially, a "contract" Inspector General -- was another innovative means to control, at cost to the builder rather than the public, other suspect firms. It, too, let contractors do the SCA's work without interruption even while they fell under the Inspector General's suspicious eye.

These and other innovations comprised a variety interim sanctions short of full debarment. They were characteristic of the Inspector General's fluid response to the shifting demands of the problem environment.

Joint ventures by their very nature can be difficult to build and maintain. This is especially so when the organization is extended, as a network. They are difficult to plan centrally; the network must be grown, and depends on people and the nurturing of complex relationships over time. Clearly, the network organization Thacher developed for the Inspector General had its origins in the many years of relationship-building that preceded the establishing of the office. [150]

Making Past Performance Count

For government to level the playing fields in those legitimate industries that have been dominated or controlled by the mob requires that it make past performance count -- both in punishing poor performing firms, and rewarding those that rise to competitive standards of price and performance.

In public construction, government procurement practices have confounded and undermined efforts to restore the competitive vitality of these markets. Government procurement procedures, aimed at controlling discretion and corruption in bid practice, have fixated on the lowest cost bidder as the single most important criteria of contract award. Unlike private sector procurement, many public rules and regulations notoriously and proudly exclude past performance -- good or bad -- from consideration in the award

[150] For a discussion of alternative organization forms and factors leading to alterations of the bureaucratic form, see, Heckscher and Applegate, *Introduction*. "There is a generic similarity among these developments; they put increased emphasis on relations of influence rather than relations of powers. Or, to put it another way, they see to build agreement among people with diverse knowledge and interests not through reference to a higher 'level' but through direct discussion and persuasion. The common feature is the development of teamwork." In Heckscher and Donnelson, *The Post-Bureaucratic Organization*, 1994

of future contracts. Good performers have few competitive inducements to do well; poor performers have few inducements to improve.

At the municipal level, even egregious poor past performance has often eluded detection or caring. Agencies have been hampered both by poor information about firms, and by the press of getting buildings up or food distributed, as the case may be.

The impacts of such policies on public procurement are plain: it is easy to cheat to win at the low bidder game. The impact on the vendor pool is telling: legitimate firms that are unprepared to cheat cannot hope to win, and fall out of the bidding and the market. In their place, firms that cheat, steal and defraud the government, and give low quality and poor performance in return for high dollar, dominate. Public schools construction prior to the SCA was in just such a state.

Unless and until government includes poor past performance and makes it possible to detect it on the job and incorporate it into future contract award decisions, the prospects for leveling the public playing field, for restoring the competitive virtues of price and performance as dominant and determinant in the marketplace, and for inducing legitimate firms to return to the marketplace for public construction, are predictably nil.

Perhaps the most important innovation and intervention of the Inspector General was the development of prequalification as a means to make past performance count in the contract award decision. By positioning prequalification *prior* to bid-opening, and as a precondition of submitting a bid, the Inspector General took background reviews off-line: there was time to do proper checks; no contract was hanging in the balance or could be held hostage; and there would be no litigation impacting the contract, as when a low-bidder was found nonresponsible and disqualified in other procurement systems. No firm that was unqualified could bid for SCA work in the first place.

Moreover, prequalification became principally concerned, over time, with the problem of "alter ego" firms that poor performing contractors might establish to avoid detection and disqualification. In taking this responsibility seriously, the Inspector General recognized the requirement to provide a *sustained* level of review and attack, not just at the firm's initial effort to cross the moat, but subsequently over the years as it reconstituted itself and made repeated tries.

Prequalification also provided the means and opportunities to develop rich and complex data bases on the industry. The Inspector General created significant repositories of information that made it much easier to do the routine work of prequalification, the arduous work of alter-ego tracking, and the complex work of criminal investigation.

Without, it seems, adversely impacting critical procurement timetables, the Inspector General's prequalification system greatly reduced one of the major uncertainties public builders face -- identifying with whom the agency was doing business. In doing so, and in excluding high risk firms and individuals, there is every reason to believe that the

Inspector General's intervention should have caused key SCA performance metrics of price and performance to have improved. For without prequalification, we have little reason to doubt that the $4.3 billion SCA building program would have become a trough for racketeers, corrupt government officials, and ordinary criminals as so many of New York City's public construction projects have been in the past.

Protecting The At-Risk Institution: A High-Yield Law Enforcement Strategy

A Victim-Oriented Approach

The operation of the Office of the SCA Inspector General plainly buttresses the view that law enforcement measures that focus simply on case-making and "taking down" bad guys *are doomed to failure unless other reforms are made*. This is still not well-learned in many quarters. In September, 1995, the New York *Times* reported that in spite of relentless prosecutions, murders and incarcerations, New York's traditional organized crime families were back in some sectors and thriving.

The innovation of the Inspector General's office reveals that to succeed in thwarting criminal threats, including racketeers, a combination of strategies must, ordinarily, *include the victim as sponsor of its own defense*. Thacher put it this way:

> "We look to develop within the victim all the panoply of corruption control strategies that are out there. Up until now none of us had pulled them under one roof like this. Meaningful corruption control in systematically corrupt industries like construction is never going to work unless the full panoply of strategies is engaged and integrated under one roof. You have to guard the victim and track down the bad guys all at once. You must work proactively and reactively using all strategies simultaneously – civil, criminal, regulatory, loss preventative. The Inspector General itself cannot pursue all of these on its own, so you must leverage resources *other* than your own – compel contractors to hire monitors who investigate for the public, at no cost to the public; share information to generate criminal cases; contract out civil prosecutions to recover money and help pay for the investigative expense; design loss prevention reforms for others to implement. None of these strategies pursued alone has a chance. Put them all together, and with the victim in the chain, which we represent, you get a context for a complete program, and a fighting chance at success." [151]

[151] Thomas D. Thacher II, interview (1995).

The operation of the SCA Inspector General thus adds importantly to the small, but growing list of effective control measures *victim-oriented strategies* aimed at preventing the intrusions of racketeers and corrupt employees, detecting them, and deterring them. The impact on organized crime, per se, from such victim-oriented strategies may or may not be trivial. We leave that empirical question for future research. But the experience of law enforcement generally, and the experience, by way of counterexample, of the Inspector General suggests this: if the victim remains weak and vulnerable, or tolerates the intrusion as a cost of doing business, then law enforcement can make cases every day, in every way, without perceptibly reducing the racketeering susceptibility and potential of targets, the likelihood of attack, and the cost in pennies and dollars that society pays.

Although it is an empirical question to be resolved, it is unlikely that securing the host without also restraining the "threat" -- doing one without the other -- would be as effective as doing both together. Nor is it likely, as history has amply shown, that simply removing or restraining the threat without securing the host will count for much in the long run. As long as there are victims, there will be victimizers.

> "Law enforcement will not do it alone. The victim *has* to take responsibility for putting together this comprehensive, sustained antidote to corruption and racketeering. How does the victim do it? It has to put itself into a position that it is worth it, or valuable, for the other players that you need to be part of this comprehensive program." [152]

The Comprehensive Model Goal: Institution Building

The SCA Inspector General experience also demonstrates that law enforcement can make a most significant difference by being in position -- in some cases, physically -- next to an at-risk institution. In comparison to traditional case handling or investigative work by prosecutors, work with the SCA Inspector General provided both rich sources of information, pressure and opportunity to make cases, and synergies to facilitate it. With the Inspector General, in effect," leading from the side" in the extended network organization, prosecutions became *de facto* focused on *his* goal of institution building -- strengthening the agency of the SCA and its capability to deliver its core product -- even while they satisfied prosecutors with low cost efforts, and sometimes big cases. In position with the Inspector General, prosecutors and investigators were joined to a purpose larger than prosecution itself, and teamed with resources capable of implementing that institution-building strategy in which law enforcement might figure heavily. It was an experience greater than mere problem-solving: the Inspector General's office deployed problem solving on behalf of the larger goal of protecting the host agency and the institution it represented.

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[152] Thomas D. Thacher II, personal communication

Summary

The Inspector General's strategy, built upon a prequalification system, procedural reforms, and civil and criminal investigations, appears to have created an effective means, at relatively low cost, by which the host agency was able to secure itself from the threat of corruption and racketeering. The innovation of the SCA Office of the Inspector General has, in our view, clearly achieved an important measure and level of success in its primary mission to protect its host. It deserves careful consideration by similar institutions, public and private, facing similar threats.

The extended network organizational architecture that characterized the Inspector General's operation was critical to the Inspector General's achievements. It proved highly adaptable to problems, and stimulating of innovation. Its efficient use of non-host resources, authorities and skills; and the value it added in lowering organization boundaries, supported the exchange of information, and provided greater integration across boundaries. It brought surprising wherewithal and leverage to the Inspector General in dealing with the problems it faced.

The prequalification system, in particular, is an important innovation in permitting past performance -- at least, in matters of integrity -- to count in the bid and award process for public sector contracts. It greatly reduces major uncertainties that public agencies, wedded to the lowest cost bidder system, face in dealing with prospective contractors. There is no reason to doubt that without this moat, the SCA building program would have been a trough for individuals, syndicates and enterprise groups of racketeers intent on pillaging the SCA program. Many public and private construction projects today are exactly that in New York, even with contractors whom the Inspector General has disqualified or debarred.

The prequalification program appears to have added little or no time to the contracting process. Indeed, although we cannot say, it may well have reduced time, and cost, by helping to minimize the needless and exploitative use of change orders in the construction process. Certainly it is a highly valuable approach to minimizing the uncertainties and risks ever-present in the vendor pool of public construction in New York.

In addition, the innovation seems to demonstrate that providing interim controls short of full debarment (such as certifications and Independent Auditing Firms) not only permits agency business to be conducted, but anchors suspect firms and holds them to standards not otherwise possible. This combination -- protecting the host, on the one hand, and securing the machinery through which the racketeering venture would otherwise gain access to the host -- seems to us to represent an important breakthrough in our understanding of how firms, businesses and enterprises might hope to protect themselves best.

Clearly, also, significant opportunities as well as issues abound in the management of procedural reform. While we believe that the organization architecture of the Inspector General's office, and in particular its positioning between the SCA and enforcement agencies helped make it effective, there remains some question about whether and how the Inspector General was able to oversee the needed reforms it recommended and expected from the SCA. The innovation was a strategic success, in that it gave the Inspector General the "big picture view," from start to finish, that is the prerequisite for change and reform of weak or nonworking systems. In that respect, the architecture was effective in creating the knowledge and license needed to improve operations. What is less clear is whether the problems faced by the SCA internally were of a kind and scale that no mere tinkering with procedures would fix. The implication of materials we have reviewed here suggests that, at least at one important time in its recent past, the SCA organization culture did not support the spirit of reform in a way that would facilitate it absent intense scrutiny and oversight.

The investigative interchange between the Inspector General and law enforcement, including the strategic uses of cross-designation as a means of creating the authorities of one agency inside another, is a model that deserves the closest scrutiny for those public managers wishing to consider an Inspector General-like operation. Information impactedness, and the high transaction costs of gathering and using information is among the most important factors in impeding law enforcement effectiveness. Agency boundaries are among the most important impediments to information exchanges. The information strategy of the Inspector General reduced those boundaries significantly, and in so doing, opened an information bazaar with a window to the industry for law enforcement, and a window for the SCA to the goings on of crime and corruption in its midst.

What Frucher and Steisel both looked for from Thacher was what he delivered: an organization that successfully straddled the worlds of builders, regulators and law enforcement, bringing them together to protect the public's $4.3 billion investment in rebuilding New York City's public schools. In effect, the Inspector General's organization imported to the SCA the wherewithal, over time, of regulatory and law enforcement partners who wished to borrow the Inspector General's entree to the SCA and the public construction industry to make cases, just as the Inspector General borrowed from them their authority and resources to help secure the SCA from crime, corruption and racketeering. Although the SCA Inspector General added value to the public's investment in regulatory and enforcement efforts, the true beneficiary of the Inspector General's efforts was the broader enterprise of public school construction in New York City.

VII. TOWARDS A SYSTEMATIC EVALUATION

This preliminary assessment of the SCA's Inspector General sets the stage for a deeper, wider, and more systematic evaluation of this complex innovation. With this assessment done, it becomes much clearer what would be required to complete a more formal evaluation. We understand what important outcomes must be evaluated, and have a rough sense for how such an evaluation might be completed.

Outcomes To Be Evaluated

The important outcomes to be determined in any systematic evaluation of the SCA's Inspector General flow directly from the theory of the innovation set out earlier, and the particular evaluative frames that this theory establishes.

Impact On SCA Performance

The easiest evaluation to be conducted would be one that focused on the Inspector General's contribution to its most immediate objectives: to help the SCA buy and build cleanly, as well as to build to competitive standards of price and performance.

This evaluation would not focus on the broad objectives envisioned by the comprehensive organized crime control strategy such as restructuring a corrupt industry, or weakening organized crime by denying it access to the industry and prosecuting individual firms. Instead, it would focus on two narrower objectives. The first and primary objective would be ensuring that SCA's projects would not be tainted by crime, corruption, or racketeering. The second objective would be ensuring that its efforts contributed to broader band SCA efforts to build to competitive standards of price and performance by leveling the playing field for legitimate firms: to find and punish cheaters and to make poor past performance count in contract award decisions, so as to restore the value of competitive attributes of price and performance, and to induce legitimate firms to return to the SCA vendor pool to compete for its business

This preliminary assessment goes some of the way towards conducting aspects of this evaluation. It presents background information on the development of the operational theory of the Inspector General, and some data about its implementation that would be important to a process evaluation. It identifies both the general kinds of Inspector General activity that need to be measured to determine what their effect might have been on crime, corruption, and racketeering in the SCA projects (e.g., prequalification procedures, investigative activities, efforts to guard against fraud in SCA projects). It also identifies the important outcomes to be measured (e.g., the extent to which SCA projects are

marred by crime, corruption, or racketeering.) It reminds us of the potentially important side-effects of the Inspector General's efforts to help the SCA buy and build clean is its potential impact, either positive or negative, on SCA's performance in buying quickly and inexpensively.

What this preliminary assessment does not provide, however, is any attempt to estimate the quantitative magnitude of the impact of Inspector General efforts on levels of crime, corruption, and racketeering within the SCA projects. Nor does this assessment present a reliable method for attributing any effects on SCA projects to Inspector General interventions rather than other factors.

We would want to know, for example, whether and to what extent changes in overall job cost and performance resulted from the efforts of the Inspector General, alone and together with the SCA. What effects did the Inspector General's operation have on the total cost of building, the speed of building, and the quality of building? And by what means did the Inspector General's office achieve these effects: how did each of its efforts at prequalification, procedural reform, and investigation impact the various costs of doing business, and the total cost? What measures did the SCA take, either alone or with the Inspector General, and what impact did these have on performance, and by what means was the influence felt? These are quantifiable and, with some effort, discernible matters.

Impacts On Crime, Corruption, And Organized Crime

It would be more difficult, but still important, to estimate the impact of the Inspector General on organized crime in New York. Essentially, the goal of the evaluation would be to determine the extent to which the Inspector General's activities had loosened the grip of organized crime on construction firms operating in New York, and thereby denied the mob a potential source of money, power and reputation. This could be done, perhaps, by looking at a sample or census of construction firms operating in New York (above a certain size), and identifying them as "mobbed up" or not on the basis of operational definitions developed by the evaluator and data collected by the Inspector General and local law enforcement agencies. If fewer firms, handling a smaller volume of construction, seemed to have mob ties, that would be counted as a positive accomplishment. It might even be possible to estimate the amount of money that was diverted from organized crime coffers.

This outcome evaluation (where the desired outcome was "loosening the hold of organized crime on construction firms") could be tied to an output evaluation in which one sought to identify the role that the Inspector General had played in helping local law enforcement make effective, major cases against organized-crime-influenced firms.

Such an evaluation would probably underestimate the impact of the Inspector General since it would ignore the opportunity blocking and deterrent effects of the Inspector General and measure only the incapacitative effects. But it would have the

virtue of producing some solid, reliable evidence on an important part of the comprehensive organized crime control strategy -- namely, that the combination of civil and criminal enforcement efforts could result in more and better cases against organized-crime-involved firms.

Impact On The Construction Industry

The most difficult evaluation task would be to determine the impact of the SCA's Inspector General on the overall state of public construction in New York City. This is difficult for several different reasons.

First, it is difficult to decide what particular aspects of the industry would be important to measure. For example, are we interested only in the extent to which the industry seems vulnerable to crime, corruption, and organized crime; or are we also interested in its broader economic performance?

Second, it is not at all clear how one could construct reliable operational measures of the characteristics of the industry we would like to measure. The extent to which the industry was vulnerable to crime, corruption, and racketeering was measured once by the New York State Organized Crime Task Force. Presumably, it could be done again, relying on the same methods of investigation, to see whether the industry had changed much.

The difficulty, however, is that the characterization of the industry that occurred in that report was more qualitative than quantitative. Evidence was presented of kinds of things that occurred in the industry. There was no information about how often the sorts of things reported occurred, or how many projects and firms were affected by them. Without a quantitative baseline, it would be hard to know whether the industry had changed much. The best one could do would be to report whether the same kinds of things seemed to be occurring, or get qualitative testimony from industry participants about how conditions within the industry had changed.

Third, even if conditions within the industry had changed, it would be difficult to attribute observed changes to the effects of the SCA's Inspector General. Presumably, many factors affect the structure, conduct, and performance of the New York construction industry. The activities of the SCA's Inspector General would be only one such factor, and it would be difficult to figure out how much of any changes one observed should be attributed to the Inspector General.

This general problem is made more difficult by the fact that the potential effects on the public construction marketplace of the SCA's Inspector General are produced by such a complex process. There are the particular effects that the Inspector General would have on the industry by ensuring that the SCA bought clean. There are the effects on the industry produced by the extension of their standards to other buyers in the industry.

There are the effects on the industry associated with their support to law enforcement's attacks on criminal firms. In each case, to accurately identify the Inspector General's contribution, we would have to first see the impact of each intervention on the industry as a whole (e.g., the impact of SCA buying, the impact of the extension of SCA standards to others, the impact of strengthened law enforcement), and then estimate how important the Inspector General had been in stimulating these intermediate agencies to act as they did.

Recommendations For Next Steps In Evaluating The Office Of The Inspector General

Based on these observations, it is our recommendation that the best next steps to be taken in continuing the evaluation of the SCA's Inspector General are, first, to launch a more systematic effort to evaluate the impact of the Inspector General on the SCA's own efforts to build cleanly and to competitive standards of price and performance. This would include direct and indirect effects of Inspector General interventions on broader-band SCA efforts to level the playing field for legitimate firms, and induce their return to the SCA vendor pool.

Moreover, further explication of the control models advanced by the Inspector General such as IAFs is promising and worthy of endeavor.

Second, we recommend developing some methods for assessing the impact of the Inspector General on public building in New York City generally, and on industry restructuring and on its organized crime control objectives. Though we can see only with some uncertainty at this stage how the broader evaluations could be carried out, it is quite possible to do a more systematic evaluation of the Inspector General's impact on the SCA's own program.

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